RioCan Real Estate Investment Trust: A Smart REIT Buy?

Description

There's a reason why people love REITs. They pay quarterly (and sometimes monthly) dividends and are easy to understand. A real estate investment trust exists to hold real estate and return a vast majority of its cash flow to investors. In exchange, it gets preferential tax treatment.

RioCan Real Estate Investment Trust (TSX:REI.UN) is one of the top REITs in Canada. It is a retail operation that manages some of the largest and most profitable shopping properties in the country. In total, it has about 300 properties in its network with some of its largest tenants including **Wal-Mart**, **Canadian Tire, Loblaw**, and **Cineplex**. These are powerhouse companies that aren't going anywhere for quite some time.

The company used to own a portfolio of 49 properties in the United States, but it decided to sell it for net proceeds of $1.2 billion. As I expected, RioCan used quite a bit of the money to pay down its debt. What I didn't anticipate was how much. In December 2015 its debt-to-total-assets ratio was 46.3%. By the end of June, RioCan had reduced that to 38%, which is a historic low for the company and gives it access to $5.4 billion in case it needs to make another big acquisition.

And what's really great is that the sale only resulted in a $1 million drop in operating funds from operations year over year. The good thing is, for the portfolio that still exists, its FFO increased by 8.1% to $118 million year over year. A big reason for this increase in FFO is because its occupancy rate increased from 93.1% a year ago to the present 95.1%. The higher this is, the more money RioCan makes and, as can be seen, business is doing quite well.

When an investor buys a REIT though, their interest is in dividends, and RioCan doesn't disappoint. It currently yields 5.15%, which is a monthly distribution of 11.75 cents per share. Due to the growth in cash flow, its AFFO payout ratio was cut from 94.5% to 89.9%. The lower this number, the more room for growth there is for the dividend and the safer the yield.

So what about growth? How else is RioCan going to continue growing the company?

There are currently 15 development projects that account for 5.9 million square feet of space. One of these projects is The Well, which will have one million square feet of office space, 500,000 square feet of retail space, and 1.5 million square feet of residential space. It owns 40% of the project and expects it to come online in 2021.

Management is also expecting to invest upwards of $250 million per year over the next five years in “urban intensification projects.” A big part of this project is building residential units on top of its shopping centres. Since the company already owns the land and building, adding on top of it is not that difficult. The company hopes to get approval to build 10,000 residential units over the next decade.

All in all, RioCan continues to show that it not only has the discipline to strengthen the core business by reducing debt and increasing cash flow, but it also has a strategy to continue expanding the portfolio so revenue can grow further. All of this leads me to believe that RioCan is very much a buy.

CATEGORY

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2. Investing

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1. Editor's Choice

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jaycodon