



Smart REIT: A Smart Way to Invest in Wal-Mart Canada

Description

Retail is a tough business.

Think about the average store. Unless it serves a very small niche, it has to compete with the titans of the industry. There are also very few ways for a retail shop to differentiate itself, so they're all left to compete on price. It becomes a race to the bottom; whoever can sell the cheapest usually gets the business.

And then there's the internet. By not having to invest in storefronts and leveraging its buying power, a site like **Amazon** can give customers lower prices while subsidizing the cost of shipping. And the scary thing about Amazon is its web-hosting service generates cash flow that gets used to subsidize the retail business. There's no indication Amazon really cares about retail making money either. It's more interested in market share.

Up here in Canada, our retailers don't just have to compete with Amazon. They also have to traverse what most consider to be a very crowded retail environment, while convincing customers who are awash in debt to keep opening their wallet. Oh, and they also have to contend with the economic fallout from oil's decline, which has hit Alberta and Saskatchewan pretty hard.

Combine all of this together, and it's easy to see why many investors have sworn off investing in retail.

Still, that doesn't mean we should avoid the sector altogether. There are better ways to get exposure.

Real estate

The ideal way to play the retail sector is pretty simple. Find the real estate that houses the dominant players and own it rather than the retailers themselves.

Smart REIT ([TSX:SRU.UN](#)) is the obvious choice for investors looking for a way to do this. Smart has been **Wal-Mart** ([NYSE:WMT](#)) Canada's developer of choice for more than a decade now and doubled down on its exposure to the company when it merged with Smart Centres back in 2015. Mitch Goldhar, the former head of Smart Centres, has stayed on with the new combined entity.

Smart has done a good thing hitching its wagon to Wal-Mart. Even though the retailer competes with just about everyone else in the sector, other retailers have quickly gobbled up the space beside Wal-Mart in Smart's developments. Occupancy is currently at 98.2%, which is the highest among all of the Canadian retail REITs.

The reason for this high occupancy is simple. Wal-Mart attracts foot traffic. Even companies that compete with Wal-Mart benefit from that traffic. **Reitmans**, a clothing retailer, has 108 locations spread out over Smart's 142 different properties, even though it overlaps significantly with Wal-Mart, which anchors some 70% of Smart's properties.

In total, Wal-Mart accounts for 26.8% of Smart's total rent.

Get a generous dividend

Some retailers pay generous dividends, but most don't. They have to invest earnings in things like technology, store revamps, and other capital expenditures.

Retail REITs can afford to pay nice dividends because all they do is collect the rent, pay the property taxes, and insure their holdings. Sure, they have to pay for capital expenditures sometimes, but these don't add up to much, especially over the life of a building.

Smart REIT pays a dividend of 4.7%, which is actually quite low versus its peers. There are a few reasons why investors are willing to take such a low yield, including Smart's relatively new assets, its high occupancy, growth rate, and, perhaps most importantly, a reasonable payout ratio. It pays out approximately 80% of its adjusted funds from operations to shareholders.

And unlike many other REITs, Smart is growing its distribution. In 2013 it paid out \$1.55 per share to shareholders. In 2016 it's on pace to pay out \$1.65 per share in distributions with that number increasing to \$1.70 per share in 2017. Even though the dividend has grown, the payout ratio has decreased from 88% to 80%.

Make the smart choice

When compared to some of its peers, Smart REIT is an expensive stock. There's a reason for that. Simply put, Smart is doing a lot of things right, and investors are willing to give it a premium multiple.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:WMT (Wal-Mart Stores Inc.)

2. TSX:SRU.UN (SmartCentres Real Estate Investment Trust)

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