Can These 2 REITs Survive the Death of the Shopping Mall?

Description

The shopping mall as we know it is dying.

The biggest culprit is the internet. Why brave the shopping mall when the same product is easily purchased online, usually at a discount? Others hate the crowds, the focus on consumerism, the lack of parking, and a million other things. Add in Canada's struggling retail sector–which is leading to increased vacancies, something no shopper likes to see–and it's easy to see why more people are cutting back on trips to the mall.

Some mall owners are facing this reality head on, realizing changes have to be made to ensure the concept stays profitable over the next few decades. Others are acting like an ostrich with its head in the sand, refusing to lower rents to retailers or add additional amenities shoppers want.

Shareholders of **Smart REIT** (TSX:SRU.UN) and **RioCan Real Estate Investment Trust** (TSX:REI.UN) have to be concerned about this trend. Here's how both companies are making sure their real estate remains relevant for years to come.

One main partner

Smart REIT's relationship with **Wal-Mart Stores, Inc.** (NYSE:WMT) is the gift that keeps on giving.

The company has been Wal-Mart's developer of choice for years now; the world's largest retailer acts as a anchor tenant for approximately 72% of Smart's 141 different shopping centres. Wal-Mart accounts for about 27% of Smart's total rent.

Wal-Mart attracts a lot of foot traffic, which is what every mall needs to be successful. This foot traffic is a draw for other retailers, even those who compete with the behemoth from Arkansas. This strategy, plus Smart's relatively new portfolio, has helped it achieve an occupancy rate of 98.2%–the best in the sector.

Another nice thing about Smart's Wal-Mart exposure is that it gives investors a free option on further growth in online shopping. Wal-Mart Canada already has a program where customers can order products online and pick them up in store. Delivering these products to a customer's home is the next logical step, and Wal-Mart has enough stores that it can likely do this for a pretty reasonable cost.

This is all good news for Smart's 4.8% dividend–a big reason why many investors own the stock. The company's payout ratio has recently dipped below 80% of adjusted funds from operations, even after accounting for the recent dividend increase.

A different strategy

RioCan is attempting to differentiate itself in a slightly different way, using a two-pronged approach.

The first is using diversification to solidify its tenant base. RioCan has hundreds of tenants across Canada with no one tenant exceeding 5% of total rent. If one tenant goes down–as we saw with **Target** Canada in 2015–the whole portfolio barely notices the loss.

The other big advantage RioCan has is its mature holdings. It has been around since the early 1990s, which means it has some real estate that has skyrocketed in value.

Rather than just sitting on this real estate, RioCan is taking advantage of its low initial cost to redevelop property for far less than competing projects. Most will end up with retail space in the bottom and apartments on top. By the time the total program is completed, RioCan will own up to 10,000 units.

These developments are attractive to both stores and tenants. Retailers like having many customers living an elevator ride away, while tenants like the urban location and access to amenities.

RioCan sold its U.S. operations in part to pay for this new development program. The decreased debt plus increased rents will likely push up profits to the point where the company can hike its 5.4% dividend for the first time since 2013.

The bottom line

Both RioCan and Smart REIT have different strategies to remain relevant in a changing world. Smart's developments should benefit from Wal-Mart for years to come, and it's hard to find many faults in RioCan's shift to multi-use properties.

It's pretty obvious that both of these companies are well prepared to survive the death of the traditional shopping mall.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:WMT (Wal-Mart Stores Inc.)
2. TSX:REI.UN (RioCan Real Estate Investment Trust)
3. TSX:SRU.UN (SmartCentres Real Estate Investment Trust)

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