RioCan Real Estate Investment Trust: Don’t Believe the Worries About Retail

Description

If you flip on the TV and listen to the financial pundits talk about the death of retail, you likely feel like it’s Armageddon for malls. “**Amazon.com, Inc.** (NASDAQ:AMZN) is gobbling up everything,” they opine, “so avoid the retail space as a whole.”

Naturally, the market freaks out and stocks give up considerable value, even though it’s unwarranted. The perfect example of this is **RioCan Real Estate Investment Trust** (TSX:REI.UN), one of my favourite REITs in all of Canada. It owns some of the highest-quality retail locations in the country. We’re talking massive malls with tenants like **Canadian Tire**, **Loblaw**, **Cineplex**, **Dollarama**, and **Wal-Mart.**

And yet, over the past year, this stock has given up over $5 per share, or over 17%. That’s despite the fact investors have earned 12 monthly distributions of $0.12.

Amazon is coming, so investors are scared. Fortunately, you get to benefit from the market’s overreaction and pick up shares in a company executing quite well.

Over the past few years, there have been a few key things that occurred to put RioCan on a strong footing.

First, **Target** exited Canada, which investors initially worried would hurt the company. It was a logical concern because a big tenant was leaving. However, RioCan was able to fill all of Target’s space and generate 40% more cash flow than it would have earned had Target stayed. And across the entire network, none of its 6,200 tenants account for more than 5% of its rental revenue.

Second, RioCan became incredibly opportunistic when the Financial Crisis hit. The company started purchasing cheap U.S. properties back in 2009. In 2016, it sold them. The entire portfolio earned $930 million for RioCan, not to mention the rents that it earned for the seven years it held those properties.

This sale has allowed RioCan to significantly pay down its debt, which is important with interest rates beginning to rise. In March 2016, its total-debt-to-total-asset ratio was 45.4%. Fast forward to March 2017, that dropped to 40.5%.

The company has no problem generating funds from operations. In Q1 2016, it earned $143 million, which included its U.S. portfolio. In Q1 2017, it earned the exact same amount, but it didn't have the U.S. portfolio.

There are a few reasons it's been able to achieve the strong FFO. Its committed occupancy increased to 96.2% from 94.8% a year prior. That means only 3.8% of its portfolio is not leased. And across the network, it has had a retention rate of 88.6% with renewal rent increases of 8.2%. Its tenants are coming back and paying more. This is unheard of in a world where "retail is dead."

Going forward, there are a couple of plans for the company to continue earning and growing.

It has a joint venture with **Hudson's Bay Co.** (TSX:HBC), where both parties contributed assets to the overall entity and is now generating rent. The plan is to take this company public at some point, which will provide dividends to RioCan. The CEO of RioCan cautioned that this will take some time, but it's on the horizon. Hudson's Bay is going to look to capitalize on its real estate, and RioCan can help.

And the other growth prospect is actually in residential properties. RioCan has these amazing retail locations, so why not build on top of them? RioCan is looking to build up to 10,000 residential units across approximately 50 of its top properties over the next 10 years. That's rent coming in, and its retail tenants will have more customers.

Like I said, you've got the opportunity to earn $0.12 per month. And at a yield of 5.83%, you're getting an incredibly strong company that is fighting back against the "retail is dead" mantra. Will some companies suffer? Absolutely. But RioCan only invests in the highest-quality assets. Now you get to play along.

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