Buy This Cheap REIT for Safe Income and More

Description

Retail real estate investment trusts (REITs) have dipped due to the changing retail landscape. As a result, the retail REITs are relatively cheap for current income.

The retail REITs in Canada should experience weaker headwinds than the U.S., because in Canada, there's less retail space per capita than the U.S. And it costs more to ship and deliver in Canada. Some value retailers, including Winners, Marshalls, and **Dollarama**, have even continued to grow.

The retail REITs collect rent from their portfolios of retail properties. The REITs distribute a big portion of their cash flow to their unitholders such that the unitholders can conveniently get juicy monthly income.

RioCan Real Estate Investment Trust (TSX:REI.UN) is the behemoth with a leading position. It has ~75% of its assets in Canada's six-largest markets and plans to increase that percentage to 80%. The REIT also has an investment-grade balance sheet and has been awarded an S&P credit rating of BBB.

RioCan has 299 properties across roughly 6,400 tenants, and it generates about 85% of its rental revenue from national or anchor tenants. As well, it generates about 66% of its rental revenue from Ontario and a relatively small percentage of approximately 15% from Alberta.

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shopping mall

Top 10 tenants

RioCan's top 10 tenants contribute about one-third of its rental revenue with weighted average remaining lease terms of six to eight years, if not longer.

These tenants are all publicly traded companies, including **Loblaw**, **Canadian Tire**, **Cineplex**, **Wal-Mart**, Winners/HomeSense (a part of **TJX**), **Metro**, **Cara**, **Lowe's**, Sobeys/Safeway (a part of **Empire**), and Dollarama.

Improving fundamentals

Management seems to be doing the right thing. Since 2015, RioCan's committed occupancy has improved from 94% to nearly 97%. Further, since 1996, the REIT has maintained its committed occupancy at 95% or higher, except for in 2015.

To counter the changing retail space, RioCan has been executing a core strategy of developing urban, retail-focused mixed-use assets and having "experiential" retail tenants, the fastest-growing tenant categories (including fitness, food and beverage, and entertainment tenants) in its tenant mix. As well, the company has shifted its focus towards online-resistant tenants.

RioCan's payout ratio for the first half of the year was 80%. Its payout ratio has been improving since 2009. If the trend continues, we could see a distribution hike from RioCan soon.

Investor takeaway

At ~$24.20 per unit, RioCan offers a safe yield of 5.8%. According to the analyst at **Bank of Nova Scotia** and the stock's historical normal multiple, RioCan can trade at $27 per unit within the next 12 months. So, an investment today also has upside potential of more than 11%.

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