Is This Stock Canada's Best Office REIT?

Description

The unassuming companies are always the most interesting to me. They don't get as much press coverage, but they continue executing on their strategy, growing their business and generating strong returns for investors.

On the topic of REITs, I think **Allied Properties Real Estate Investment** (TSX:AP.UN) is Canada's top office REIT. It understands where it can execute most efficiently and it focuses all of its energy there. In short, this company is a must-own.

Let's dive in to understand why…

Allied focuses its energy on seven markets: Montreal with 4,256,906 square feet of gross leasable area (GLA); Toronto with 4,186,019 square feet with an additional 559,688 square feet in its Mission Critical project; 924,038 square feet in Calgary, 562,185 square feet in Kitchener; 286,250 square feet in Vancouver; 271,376 square feet in Edmonton; and 221,057 square feet in Ottawa.

This strategy makes perfect sense … cities are the first true social network. As more people relocate to cities, more jobs are created and even more people move there, which creates a virtuous cycle. The recent trend has been toward increased urbanization, which should create more demand for office space.

We're witnessing many other companies making similar moves. With cities becoming more of a draw, the focus is going to be on higher quality assets in cities versus assets in disparate areas. The fact that Allied has been focused on this for years gives it a leg up on its competitors.

One important distinction of high-quality real estate companies is how well it recycles capital. Ideally, you want to buy real estate low and sell it high. In 2017, Allied bought 124,549 square feet in Toronto for $123 million. However, it sold 589,760 square feet in Edmonton, Winnipeg, and Quebec City for $54 million. This ensures that the portfolio is able to operate as efficiently as possible.

But how efficient is the business?

In Toronto, the company has a leased rate of 98.6%, which is incredible. Toronto has expensive commercial rates, so the fact the company only has ~60,000 square feet of unleased property is great news. Network wide, it has a 95.8% leased rate, up from 92.1% in 2016.

The Mission Critical portion of the portfolio actually pulls the entire business down because its leased area is 83.1%. This is called out separately because it's not office space. So why would Allied invest? Because of its data centres. If we consider future economies, data centres are going to be massive parts of the commercial ecosystem. Picking these assets up now is a forward-thinking investment that should eventually pay dividends.

The company follows in the footsteps of other REITs and pays a monthly distribution. Investors can expect $0.13 per month, which is a solid 3.85% yield. Although this is lower than some of the other REITs on the market today, Allied is far more predictable. If you're looking for commercial real estate exposure, Allied is your best bet.

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