Income Investors: Which One of These 6.8% Yielding REITs Is Worth Your Consideration Today?

Description

They both offer a similar distribution yield of 6.8% annually, they both pay monthly every month, but investors wishing to open a new position in REITs as positive sentiment returns to the real estate sector after a false alarm may have a tough time choosing between an **H&R Real Estate Investment Trust** (TSX:HR.UN) and a **Crombie Real Estate Investment Trust** (TSX:CRR.UN) investment.

Let's take a better look into the two offerings.

H&R REIT

H&R Real Estate Investment Trust is a diversified REIT that holds 235 income producing properties across the United States and Canada, with higher exposure to office (50%) and retail (31%) segments. The REIT also owns a 33.6% interest in ECHO Realty LP that consists of 228 properties.

H&R REIT's sale of 63 slow growth U.S. retail properties during the second quarter could further reduce operating cash flow from its portfolio, but management's decision to carry out a significant unit's buy-back program, new acquisitions, and ongoing developments of higher growth properties could stabilize and probably grow portfolio income and cash flow per unit over the coming quarters.

During the six months ended June 30, 2018, the trust purchased and cancelled 6,609,420 units for a total amount of $136.3 million and may have bought back many more units this quarter.

The REIT's funds from operations (FFO) payout rate at 79.1% for the second quarter is still reasonable, but it was higher than that achieved in a comparable quarter last year, as cash flows per unit declined and portfolio occupancy levels dipped to 93.9% last quarter.

H&R REIT is favorably levered. Its total debt ratio at 43.8% of assets is the envy of many Canadian REITs today, as several competitors are struggling to reduce leverage during a generally rising interest rate regime. The REIT is relatively more liquid and operationally more flexible after repaying significant debts after the recent asset sales.

The strong U.S. same property net operating income growth (NOI) of 1.8% during the last quarter is very encouraging.

Most noteworthy, H&R REIT's equity units are currently trading at a near 20% discount to net asset value, offering new investors a welcome margin of safety, allowing them to enjoy a 6.8% annualized distribution yield while waiting for the new capital rationing plan to deliver potential valuation growth.

Crombie REIT

Following a short-lived price dip in May this year, Crombie Real Estate Investment Trust equity units are on a sustained valuation rebound, threatening to further shrink the currently lucrative $0.074 per unit monthly distribution’s 6.74% annual yield.

Crombie invests in income-producing retail, office, and commercial mixed use properties in Canada, with a growth strategy focused primarily on the acquisition of grocery and drug store-anchored retail properties in the country’s top markets.

The REIT owns 290 income producing properties today, up from 286 at December 31, 2017, with a total committed occupancy rate of 96.1% as at June 30, 2018, up from 95.2% exit 2017.

Investors in Crombie REIT will share a common interest with Empire Company Limited, which, through a subsidiary, held a 41.5% economic and voting interest in the REIT at December 31, 2017.

Although Crombie’s total debt ratio slightly declined to 49.9% by the end of the second quarter from 50.3% flat though 2016 and 2017, leverage may still be higher than what some investors would prefer during a generally rising interest rate environment. That said, the REIT’s strong operating profit growth has kept interest coverage and debt coverage ratios well in check over the most recent quarters.

Crombie reported same-property net operating income (NOI) growth of 2.9% last quarter, higher than the 2.1% compound same property NOI growth rate achieved over the past five years.

The REIT’s distributions are well covered today, with funds from operations (FFO) payout rate of 72.7% for last quarter, and 73% for the first six months of 2018, which is an improvement from the 76% payout for the comparable period in 2017.

I like Crombie’s strong development pipeline. The REIT had 22 major development opportunities exit 2017, which represented $3 -4.5 billion of potential mixed use development that could be completed over a 10- to 15-year period.

The strong expected growth in net asset value could produce a welcome capital appreciation for investors, especially given Crombie’s current price to net asset value valuation multiple of 2.245 times today (which compares better to H&R REIT’s 0.8.)

Crombie has a running distribution reinvestment program (DRIP) that allows investors to easily convert monthly distributions into more equity units, further growing their investment holding.

Investor takeaway

Both REITs offer investors dependable monthly income.

H&R’s units trade at a discount for tangible reasons, but offer investors a margin of safety, while Crombie units trade at higher multiples, offering higher capital growth potential but higher equity risk should anything go wrong.

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2. TSX:HR.UN (H&R Real Estate Investment Trust)

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Author
brianparadza