Interest Rates Favour TSX REITs

Description

As inflation surges to the highest level in the past seven years and interest rates hold steady, Canadian REITs promise your retirement portfolio the perfect hedge against risk amid the backdrop of a dubious international trade war.

Driven by sustained low interest rates on the 10-year GoC bond, real estate investment trusts (REITs) offer an attractive combination of high dividends and elevated earnings growth on the Toronto Stock Exchange. With a population growth rate of 1.2%, low rental property vacancy rates, and impressive capitalization rates, Canadian REITs provide conservative investors with higher returns and lower risk than most industries. Capitalization rates are the rate of return on an investment property per year calculated by the net income divided by the property value.

I recommend the following two undervalued dividend stocks with market values over $1 billion and price-to-earnings ratios (P/E) below 10: **Summit Industrial Income REIT** (TSX:SMU.UN) and **InterRent Real Estate Investment Trust** (TSX:IIP.UN).

Summit Industrial Income REIT

Summit Industrial Income REIT's stock price has exploded 113% in the past five years while offering a generous dividend yield of 7.27%. In the past year alone, the price of Summit's stock increased by 30% and currently sells at a P/E ratio of 6.17, lower than the industry average of 30.40.

No savvy investor should want to miss out on the current 4.06% dividend yield priced at a steal with a 60-month beta of only .39. A stock's beta is a measure of a stock's volatility compared with the market. A beta under one indicates volatility below the market average.

Summit leases light industrial property across Canada. Managed by Sigma Asset ManagementLimited, Summit Industrial increased its portfolio size by 56.3% and increased rental prices by 11.9% in 2018. The firm demonstrates promising future earnings growth with its recent entrance into the Toronto data centre market. As the advent of big data and cloud computing disrupts every industry, investors would be foolish to pass up an undervalued early entrant into the data centre market.

InterRent Real Estate Investment Trust

InterRent REIT has offered investors a capital gain of up to 154% in the past five years in addition to an attractive average dividend yield of 2.91%. In the past year, InterRent's stock price has jumped in value by 30% and currently sells at a low P/E ratio of 8.31.

InterRent has a real estate portfolio worth over $1.5 billion and a 60-month beta of .136, a lower-than-market-average volatility. Although the stock offers a dividend yield of only 2.05%, the low beta raises the profitability of this REIT stock above its competitors through increased liquidity and reduced risk.

InterRent specializes in acquiring and renovating low-end apartment buildings in Canada. Renters have recently complained about insufficient renovations to Stoney Creek Towers, an east-end Hamilton apartment complex. Nevertheless, the company has significantly improved the condition of apartment homes across Ottawa, Gatineau, Hamilton, Toronto, and Montreal. Socially conscious investors looking to balance capital gains and high dividends in their portfolio should snap up InterRent's stock while the P/E ratio is a bargain and the company is growing.

Why REITs?

The interest rate spread between the 10-year GoC bond and the national average capitalization rate on rental properties is near 4%, up from a 2.3% spread in 2007, meaning costs are low relative to returns. Investment capital is plentiful and has far from saturated the Canadian real estate market.

While the trade war creates uncertainty in other industries, long-term investors should take advantage of low interest rates and protect their retirement savings from inflation by putting their money in high-dividend REITs with a history of offering above-average capital gains.

CATEGORY

1. Investing

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1. TSX:IIP.UN (InterRent Real Estate Investment Trust)
2. TSX:SMU.UN (Summit Industrial Income REIT)

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