Worried About Canadian Real Estate? Bet on the U.S. Instead

Description

While real estate prices have been booming in Canada for well over a decade, the prices south of the border are yet to recover to their pre-crisis levels. Across the United States, housing supply remains constrained, job creation has been exploding, and rental yields are up, but house prices remain suppressed.

This creates a fertile ground for savvy landlords who can deploy cash to acquire more properties and benefit from incredible rental yields in the country's most lucrative markets. For Canadian investors, **Tricon Capital Group** (TSX:TCN) offers a convenient way to add exposure to this relatively undervalued market.

Since the late 1980s, the real estate firm has been investing in the U.S. across four verticals: Tricon Housing Partners (Land and Homebuilding), Tricon American Homes (Single-Family Rental), Tricon Lifestyle Communities (Manufactured Housing Communities), and Tricon Luxury Residences.

Over the decades, the company has amassed a portfolio currently worth $5.7 billion and financed real estate transactions worth $20 billion. The rental homes segment accounts for the vast majority (nearly 87%) of the company's earnings before expenses. Most of the assets (92%) are based in the U.S.

Since the company entered the single-family rental market in 2012, it has managed to expand book value at an annualized rate of 24%. This rapid expansion in the book value coupled with the high rental yield on the company's property portfolio allows it to offer a reasonably attractive 2.8% dividend yield.

I believe a number of factors work in Tricon's favour over the next few years. Firstly, renting a property rather than buying is becoming the preferred choice for millions of people across North America. A combination of high debt burdens, elevated property values, and tighter mortgage rules have made homeownership unattainable for most.

Secondly, the U.S. market offers plenty of value and inventory that is ripe for acquisition. According to the company's investor presentation, its prime focus is on an area of the southern United States called "The Sunbelt." This belt includes cities like Austin and Tampa, where the company estimates population could grow over 20% in the near future.

Second-tier U.S. cities are also facing an influx of talent from other parts of the country and a consequent rise in median income. This means Tricon's early investments could lead to both capital appreciation and higher rental yield in the future.

This year, the company is on track to generate $116 million core funds from operations (FFO) and net fees. Meanwhile, the book value per share hovers around $11.2 at the moment. This means the share price is currently trading at 12.3 times FFO per share and at a 10.7% discount to net book value per share.

In other words, Tricon is an undervalued opportunity to add some exposure to America's relatively healthy rental property market. New tax policies implemented by the Trump administration could create a favourable environment for real estate investors and landlords. Investors looking for a steady dividend stock or for diversification away from Canada's seemingly overpriced real estate sector should take a closer look here.

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