



TFSA Investor Alert: This 5.2%-Yielding Canadian REIT Was a Surprise Outperformer in 2019: Is it a Buy for 2020?

Description

The real estate investment trust (REIT) asset class has strong investment returns potential that, at times, outclasses traditional stocks and bonds, and 2019 was another good year for Canadian REITs, which saw some industry tickers generate surprise total returns above 30% during the recent past year.

Irrespective of one's income tax bracket, REIT investments are best located inside a Tax-Free Savings Account, since dividends (termed income distributions for tax purposes) are generally taxable at normal rates if received outside a registered account.

Income investors keep flocking to the asset class mainly for its regular and bond-like cash flows and monthly distributions that trusts pay out to unitholders, but there's also a potential for huge capital gains, such as has been seen on a usually dormant **Cominar Real Estate Investment Trust** (TSX:CUF.UN) over the past year.

A surprise outperformance?

A 33.89% total investment return from a largely dormant and historically underperforming ticker is a very welcome surprise. This is what investors in Cominar REIT, who'd held throughout the year, were rewarded with in 2019.

Capital gains came in at 26.43%, and distributions and their reinvestment added another 7.46% to the total return for the year.

Cominar is one of the largest diversified REITs in Canada, and it calls itself "the largest commercial property owner in the province of Québec," with a portfolio of 331 properties serving the retail, office, industrial and mixed-use needs of tenants in Montreal, Quebec City, and Ottawa areas.

Investor interest in the trust has been very low for some time, and units underperformed for years due to declining occupancy rates and unsustainable payout rates, but market attention on the trust surged

briefly in the last quarter of 2017 after a credit-rating downgrade from DBRS and [subsequent strategic restructuring efforts](#) were announced that would result in massive asset sales, dividend cuts, unit buybacks, and several internal organizational changes.

Restructuring has delivered

Progress was too slow to be seen in 2018, but results were much better, as the strategic plan entered its 24-month stretch last year.

The trust has a much better quality overall portfolio today that is delivering the desired results.

For example, management reported a 3.8% year-over-year growth in same-property net operating income during the third quarter and increased its guidance for the performance measure for the year to 2.5-3%, as occupancy rates surged by over 110 basis points to 94.4%, while the portfolio recorded a 2.4% growth in average net rent during the quarter.

There was a strong 11.5% decrease in trust administration expenses during the quarter to September last year, a benefit from restructuring efforts, and the trust managed to maintain its normalized funds from operations (FFO) per unit, even after \$210 million worth of assets were disposed earlier during the year.

Restructuring efforts have benefited the bottom line.

A buy for 2020?

Even after a rally to recovery over the past year, units still offer a respectable 5.16% yield today, and the distribution remains well covered with an adjusted funds from operations (AFFO) payout rate of under 86% for the third quarter and 93% for the first nine months of 2019.

The distribution is very well covered, and units still trade at a discount to net book value — probably due to the portfolio's exposure to retail malls, which are facing occupancy challenges and a relatively high (but declining) leverage. This discount could offer a margin of safety to value investors.

Investors should look to the growing industrial and mixed-use segment of the portfolio to continue to introduce some growth to the trust's earnings and cash flow growth.

It may still be a good idea to allocate some portion of one's \$6,000 annual TFSA contribution to the REIT sector again this year and to consider nibbling on Cominar's juicy yield.

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