



2 Income REITs That Are Too Cheap to Ignore

Description

I have not made any secret of the fact that I am not overly enthused about the state of the global real estate market. Housing bubbles have historically been caused by the availability of cheap credit. Well, there has not been a much cheaper time to borrow than there is today, leading to a potential collapse in real estate sometime in the future.

The irony is not lost on me, then, that I am going to be extolling the virtues of buying REITs at a time of extremely elevated real estate prices. At first, I was going to stay away from these companies, but after some thought, I have begun to take a deeper look at REITs. I am becoming more intrigued with their undervalued assets.

People need places to live

The most secure REIT on the list is by far **Canadian Apartment REIT** ([TSX:CAR.UN](https://www.scribd.com/document/444444444/TSX-CAR-UN)). The REIT has a number of [investments in residential](#) properties both in Canada and in Europe. The security in this name comes from the fact that most individuals need somewhere to live. Even though there might be some near-term pressure on earnings due to potential rent deferrals, people will probably start paying their rents once their incomes come back.

CAR also has a strong balance sheet with enough cash on hand to pay down all of its short-term debt. It also has a long track record of generating free cash flow, which it has translated into distribution growth. Its yield is one of the smallest in the REIT sector at 2.95%, but it has consistently grown that yield for years. It also has a very low payout ratio of 20% of earnings. Even if earnings fall by half, this company should have no issue supporting its dividend.

The only downside is the fact that this REIT trades at one of the highest multiples in the space at the moment, although even its price-to-book (P/B) ratio is quite low. Currently, CAR trades at a below-book value ratio of 0.95 times book.

Retail is under pressure

The next choice on the list fits into the medium-risk bucket. Until very recently, it was also one about which I was less than enthused. **RioCan REIT** ([TSX:REI.UN](#)) is one of the largest REITs in the country. It is focused primarily on the Toronto real estate market, with about 50% of its properties in the region. Buying the REIT, therefore, does largely depend on your view of this city's real estate future.

RioCan has another knock against it in terms of its clientele. Although it does have residential investments, the majority of its properties are shopping centres and office buildings. In the current economic climate, this is a short-term knock against it.

Even though I still believe property prices are elevated in Toronto, there is no denying that this city is a popular destination for people and industries looking to invest in Canada. Now that the REIT is trading at about 50% of its book value, much of the potential downside is probably already priced in. This is where the majority of the risk comes from this name.

At the moment, the distribution yield sits at about 10%. RioCan's CEO has publicly stated that the distribution will be safe going forward. A [reasonably safe 10% yield](#) and a unit price that could appreciate significantly are great incentives for would-be investors.

The bottom line

REITs have not been an appealing asset class for years. Much of the risk in these names comes from the inflated real estate prices that have bubbled up on the backs of very low interest rates. Right now, though, much of the risk has been priced into the unit prices. As a result, REITs are far more attractive than they have been for quite some time.

These REITs are attractive investments at the moment. Depending on your risk profile, they would each be a great addition for adding income. Of the two, CAR is definitely the lower-risk option. It has a smaller yield but a much more stable business model. RioCan is a far-higher risk bet, in my opinion, but it also has the opportunity for greater short-term rewards.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:CAR.UN (Canadian Apartment Properties Real Estate Investment Trust)
2. TSX:REI.UN (RioCan Real Estate Investment Trust)

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