Income Investors: 1 TSX Dividend Stock to Buy and 1 to Avoid

Description

Income investors need to be aware that not all income stocks are equal. Unfortunately, the coronavirus crisis has forced income investors to re-think the way they invest. Not all income stocks are created equal, so it is imperative to build an income portfolio with discretion.

A perfect example is **H&R REIT** (TSX:HR.UN). Last week, H&R announced a massive 50% dividend cut; previously, the REIT was yielding over 16%! While this move was certainly prudent by management, this scenario demonstrates a few things income investors must be cautious of.

Income stocks: Be cautious with +10% yields

First, overtly high-yielding income stocks (10% or more) can be dangerous. A high yield often means the markets foresee significant future business disruptions. From time to time, the market can be wrong, but more times than not, it is right.

Second, high-yielding stocks generally mean the investment thesis has changed. H&R's portfolio of office and retail properties were already challenged prior to the COVID-19 hit. The crisis will seriously challenge any hope of a turnaround.

H&R has significant office exposure to Alberta, and there are major concerns around its most expensive property: the Bow. H&R is also heavily (33%) exposed to retail. Retail is a massively challenged sector, right now. We have already seen a wave of retail bankruptcies, and this is only the beginning of some more ugly times.

Third, high-yielding stocks, like H&R, generally signal growth is detracting or stalled. In order to attract capital, it needs a substantial yield to compensate for higher business risks.

As a consequence, income investors can actually put their principle capital at risk, just for the sake of a higher monthly distribution. This is what has happened with H&R. Despite a still elevated 8% yield, I wouldn't touch this stock.

Income investors: Buy long-term growth themes

I would rather own a business that has the capacity to grow my investment capital — not just pay out income. I want income stocks that have long-term growth themes supporting their investment thesis. So, look out for best-in-class income stocks that are actually growing their cash flows, even in tough times.

That brings me to my buy suggestion: **Summit Industrial Income REIT** (TSX:SMU.UN). It has 154 light industrial properties located primarily across Ontario (52.6%), Alberta (28.7%), and Quebec (18.5%). Summit focuses particularly on mid-size (about 60,000 square feet) warehouses and logistics properties. This is an attractive dividend-paying stock for the long run.

First, this income stock has strong exposure to growing markets like Quebec and Ontario. These regions have seen strong population and economic growth for a number of years. Demand is very high, vacancy is at all-time lows, and the opportunity for rental growth is significant.

Its Alberta exposure is somewhat a concern. Yet most of Summit's Albertan properties are leased to international/national tenants, and it only has 5% overall portfolio exposure to oil and gas.

Second, the REIT will survive the COVID-19 crisis. Management believes that less than 2% of its 2020 rents are really at risk. The REIT has strong portfolio occupancy of 98.9% and has collected 87% of May's expected rents. Summit's properties are mostly distribution/warehouse space, so it could actually benefit over time from the recent acceleration towards e-commerce.

Last, Summit has a good balance sheet and growth fundamentals. It has a solid history of accreting cash flows through organic growth, developments, and acquisitions. In Q1, it achieved an impressive average 14% rental growth rate on lease renewals. Summit has $200 million of excess liquidity, which it can hold to preserve its balance sheet, or it can begin to deploy it as 2020 stabilizes.

The bottom line

Summit pays a well-covered 5.72% distribution. The stock is trading cheaply today at 85% of its price to NAV. The REIT is structurally set up for long-term growth, despite, perhaps, some temporary COVID-19 setbacks. It has the right type of properties in the right locations, and I think this income stock will go up for a long time to come.

CATEGORY

1. Coronavirus
2. Dividend Stocks
3. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. TSX:HR.UN (H&R Real Estate Investment Trust)
2. TSX:SMU.UN (Summit Industrial Income REIT)

PARTNER-FEEDS

1. Business Insider
2. Msn
3. Newscred
4. Sharewise
5. Yahoo CA

Category

1. Coronavirus
2. Dividend Stocks
3. Investing

Tags

1. Editor's Choice

Date
2025/07/19
Date Created
2020/05/18
Author
robbybrown