This 1 REIT Yields a Massive 9.78% Dividend

Description

There are many reasons why you might consider adding a few REITs to your investment portfolio. They allow you access to the lucrative real estate market, without all the risks and difficulties of becoming a property owner. They allow you to enter a market (in a way) that has such a high cost of entry. And REITs offer excellent dividend yields.

The high dividend yield is one of the inherent characteristics of REITs. But even though they are high compared to other industries, under normal circumstances, they rarely offer yields as high as the one **RioCan REIT** (TSX:REI) is currently offering.

A massive dividend yield

RioCan is currently offering a robust yield of 9.78%, which comes with a hefty price of an unsustainable payout ratio (533%). The company hasn't slashed its monthly dividends yet and is still paying $0.12 per share per month to its investors. The reasoning behind this extremely generous yield is the same as it is throughout the sector: A significant dip in valuation.

The RioCan stock is trading at a price that's 46.6% below its pre-pandemic valuation. And in half a year since the crash, the stock has only managed to grow its share price by 18.6%. One of the reasons behind its failure to recover from the March crash (though it's not uncommon in the real estate sector right now) is its retail-based portfolio. Retail businesses have been some of the worst financial victims of the pandemic.

According to the second-quarter results, the company's revenues didn't take that solid a hit during the pandemic. The difference in revenue from the second quarter was about $57 million from the second quarter last year. This isn't enough to account for the $350 million loss the company reported, most of that came from the fair-value losses.

The company

RioCan is one of the largest REITs in the country. It has an enterprise value of $8.58 billion, and as of the second quarter, the company had total assets of $15 billion and a debt of about $6.7 billion. The company owns 176 commercial assets that are currently functional, and a few more are under development. They are distributed among six major Canadian markets, and the bulk of its 89 assets are in Toronto.

Nearly half of the assets RioCan owns are grocery-anchored centers. About 27.4% of the portfolio comprises open-air centres, with the rest divided between mixed-use (15.9%) and enclosed centres (7.8%). This heavy emphasis on retail (even if a sizeable portion of it is made up of grocery and pharmacy) is one of the reasons why this REIT is currently in such a slump.

While the situation is expected to improve once the pandemic is under control, the company might have to make some significant changes in its asset-class distribution, since the future of retail is bleak at best.

Foolish takeaway

Even though RioCan isn't a Dividend Aristocrat, we can be reasonably sure that the company might not slash its dividends. It would alienate investors, and it's something that the company can't risk in the current economy. If you're worried about the sustainability of dividends, try to determine whether the payout ratio is driven this high by rental income losses or fair value adjustment.

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