TFSA Income Investors: 3 REITs With the Safest Yields

Description

Dividend cuts are painful, more so if you somewhat rely on dividend income to pay the bills. It's important that you populate your income portfolio with assets that make reasonably safe regular payouts. One asset class created to pay out the majority of its income to investors is Real Estate Investment Trusts (REITs). I will touch on three Canadian REITs that currently pay the safest distribution yields right now.

The REIT's Adjusted Funds From Operations (AFFO) payout rate is a key input when evaluating the safety of a trust's current yield. AFFO adjusts an otherwise volatile net income for non-recurring gains and losses on property disposals. It removes non-cash gains and losses on fair values of assets, adjusts for rent increases, necessary capital expenditures, and routine property maintenance expenses.

The AFFO payout rate shows the proportion of recurring cash-based income that is being paid out to investors. A REIT with the lowest AFFO payout rate should normally offer the safest yield. The opposite is true. One may regard payout rates below the 80% margin as generally safe. The chances of an abrupt distribution cut are very high when the AFFO payout breaches the 100% mark.

Here are three trusts paying the safest yields right now.

H&R REIT

H&R Real Estate Investment Trust (TSX:HR.UN) owns a $13.3 billion portfolio of office, retail, residential and industrial properties located in Canada, with a number of new developments in the United States.

The trust pays out a $0.0575 monthly distribution that currently yields about 5.1%. Its AFFO payout rate during the third quarter was at 49%, one of the lowest in the industry. This makes HR's current distribution one of the safest payouts for income investors to buy today. Units have rallied over 35% in one month recently in a COVID-19 vaccine powered recovery rally. Momentum is there for capital gains.

Notably, H&R cut its distribution by 50% in May when the coronavirus ravaged it's retail property rent collections due to significant exposure to enclosed malls. However, collections have improved markedly during the third quarter to 95% by October and mall rent collections increased from 60% during the second quarter to 83% by October. Occupancy rates remain strong to support rental income in the future and new developments will generate new revenue growth going forward.

Artis REIT

Artis Real Estate Investment Trust (TSX:AX.UN) owns a diversified portfolio of office, retail, and industrial properties in Canada and the United States.

The trust recently announced a 3% distribution increase in November. Its current payout yields 5.1% annually and Artis' FFO payout rate was just 37.8%, and its AFFO payout rate stood at a safe 51.3% during the third quarter of 2020. The distribution remained well-covered during the COVID-19 pandemic as AFFO per unit grew 8% year-over-year between July and September this year.

Rent collections improved, occupancy rates remained stable at 91.6% during the past quarter. New rent income from new acquisitions and developments and lower interest expenses aided AFFO growth during the third quarter.

It's important to note that Artis is undergoing another strategic refocus that may include a spin-off or retail assets, more asset sales, and significant debt reductions that may prop up its balance sheet over the next few months.

CT REIT

If distribution safety is proven by how well a trust has managed to survive a perfect COVID-19 storm without cutting the payout, then **CT REIT** (TSX:CRT.UN) pays one of the safest 5.4% yielding distributions in Canada. The trust actually increased its distribution twice for 2020. The cumulative distribution increase for 2020 is 5.3%, and the AFFO payout rate remains safe and workable at 79.6% after a marginal 0.4% year-over-year increase in AFFO during the third quarter.

CRT is the landlord to the **Canadian Tire Corporation** (CTC). The trust was spun out of CTC's real estate portfolio. The mother company represented 91.5% of the trust's annualized base rent by September 30, this year. Occupancy remains strong at 98.8% going into the fourth quarter.

Perhaps due diligence should include an assessment of whether the major tenant will always be capable of paying its rent. The last time I checked, Canadian Tire had an investment grade rating of BBB with a stable trend. DBRS Morningstar last confirmed the rating in June 2020.

The landlord shouldn't be concerned about rent non-payment when unsecured lenders still feel secure about interest and principal debt repayment.

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TICKERS GLOBAL

1. TSX:AX.UN (Artis Real Estate Investment Trust)
2. TSX:CRT.UN (CT Real Estate Investment Trust)
3. TSX:HR.UN (H&R Real Estate Investment Trust)

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