The 2 Best Canadian REITs to Buy for Reliable Passive Income

Description

Commercial real estate has been a good passive-income-producing asset to hold when inflation is soaring. Economic growth pushes rents higher, which likewise pushes property values up.

As a result, putting cash into real estate can offset the de-valuing effects of inflation. That is why many real estate investment trusts (REITs) on the **TSX** are performing well in 2022.

There is one caveat, however. Increasing interest rates is the most formidable tool to slow down out-of-control inflation. Most real estate is purchased with some element of debt. Consequently, rising interest rates can lower the prospective earnings potential of a REIT. This is a risk to monitor.

Keep your passive income safe: Only buy the highest-quality REITs

When looking to buy REITs that pay safe and reliable passive income, it is crucial to ensure a few things. Firstly, buy REITs with high-quality, well-located properties. A REIT with these elements will consistently outperform peers with secondary market exposure. Top-quality assets tend to maximize rental and cash flow growth.

Secondly, only buy REITs with manageable, low levels of debt (also called leverage). Low leverage affords an organization flexibility both in good times and bad. It is crucial that a REIT can faithfully service and reduce its debt over time.

Lastly, a REIT must have a sustainable distribution. REITs that have a high distribution payout ratio are at higher risk of cutting their dividend. This occurred with several diversified Canadian REITs in March 2020. It was not a pretty time for investors.

A REIT that can support and grow its distribution is likely growing its cash flow per unit as well. Distribution growth is a key characteristic in finding a high-quality REIT that reliably produces passive income.

Two REITs that meet this criteria are **Granite REIT** (TSX:GRT.UN) and **Minto Apartment REIT** (TSX:MI.UN).

Granite REIT: A solid long-term stock for passive income

With a market capitalization of $6.4 billion, Granite REIT is Canada's largest industrial REIT. Its largest tenant is **Magna International**, but it has a large group of high-quality e-commerce and consumer staple tenants as well. Its properties are well located across Canada, the United States, and Europe.

It has over 99% occupancy, and its average lease term is 5.8 years. Many of these leases are inflation-indexed or have annual contracted rent increases. The REIT has a best-in-class balance sheet, which is helping it fund a very active development and acquisition pipeline.

This should support high single-digit cash flow-per-share growth for the next few years. The REIT has grown its monthly distribution every year for the past 11 years. It only pays a 3.2% distribution yield, but further distribution increases are likely.

Minto Apartment REIT: An undervalued dividend grower

Another great Canadian REIT for passive income is **Minto Apartment REIT** (TSX:MI.UN). It owns nearly 8,000 apartment units in some of Canada's fastest-growing cities (Ottawa, Toronto, and Montreal).

Its properties are amenity rich and extremely well located to business, transportation, and/or education hubs. Consequently, it is in a strong position to enjoy consistent rental rate growth. Like Granite, Minto also has several development opportunities that will fuel long-term cash flow-per-share growth.

Minto has an excellent balance sheet with leverage below most Canadian peers. While it only pays a 2.33% distribution yield, it has grown its distribution every year since its inception in 2018. This REIT is down 8.5% this year. It presents excellent long-term value at today's price.

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TICKERS GLOBAL

1. NYSE:MGA (Magna International Inc.)
2. TSX:GRT.UN (Granite Real Estate Investment Trust)
3. TSX:MG (Magna International Inc.)
4. TSX:MI.UN (Minto Apartment Real Estate Investment Trust)

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