



## Monthly Passive Income: Is RioCan a Buy for the 4.75% Yield?

### Description

**RioCan** ([TSX:REI.UN](#)) is recovering after the heavy hit the [REIT](#) took during the pandemic. Retirees and other investors seeking monthly passive income are wondering if this is a good time to add RioCan to their Tax-Free Savings Account ([TFSA](#)) portfolios.

### RioCan overview

RioCan primarily operates shopping malls in large Canadian cities. The company sold off most of its holdings in secondary markets before the pandemic in a strategy shift that includes building mixed-used rental and residential properties in large urban areas located close to core public transit routes. At the end of the second quarter (Q2) RioCan had 202 properties that include retail, office, and residential rental space as well as 12 development properties.

As of August 8, the residential rental portfolio, branded as RioCan Living, had 2,005 completed apartment units in nine buildings located in Toronto, Montreal, Ottawa, and Calgary. An additional 214 units are targeted for completion in Q4 2022. Another 592 at the FourFifty The Well project in Toronto will be completed in phases with occupation beginning in late 2023.

On the condo and townhouse side, RioCan has 2,627 units under construction or in the process of interim closing. Another 451 units are in pre-sale phases.

The Bank of Canada is raising interest rates to fight inflation. This is driving up mortgage rates and will ultimately drive more demand for rental units, as potential home and condo buyers are squeezed out of the market.

RioCan's retail portfolio is benefitting from the end of COVID-19 lockdown. Shoppers are returning to stores, movie theatres, and gyms located in RioCan's shopping malls. Demand for prime retail space remains strong, and RioCan is typically able to replace tenants that leave with new ones at higher rental rates.

## Financial results

Funds from operations (FFO) in the first half of 2022 came in at \$262.2 million compared to \$233.6 million in the first six months of 2021. FFO per trust unit on a diluted basis rose to \$0.85 in Q1 and Q2 2022 from \$0.73 during the same period last year.

For the full year, RioCan confirmed its 2022 guidance of FFO growth of 5-7% per trust unit.

Committed occupancy improved in Q2 for the sixth straight quarter and returned to the pre-pandemic level of 97.2%. RioCan gets 85.7% of its annualized net rent from strong anchor tenants that have a national presence and sell products people need on a regular basis. These include grocery chains, pharmacies, and other essential goods retailers.

## Risks

Rising interest rates and soaring construction costs coupled with a drop in residential property valuations could squeeze margins on the for-sale developments. At the same time, rental rates on the apartment units might not increase enough to cover higher construction and debt-servicing costs on the new buildings.

REITs carry significant debt, and RioCan could see borrowing costs increase on debt renewals if interest rates remain elevated for several years. This could reduce cash available for distributions down the road if revenue growth doesn't keep pace.

## Distributions

RioCan pays a monthly distribution of \$0.085 per trust unit. That's down from the pre-pandemic payout of \$0.12 per unit. RioCan cut the distribution to \$0.08 to preserve cash during the worst part of the COVID-19 crisis and started the process of increasing the payout again earlier this year. The business is performing well, and investors could see the monthly distribution increase to \$0.09 for 2023, but a rapid return to the pre-COVID level shouldn't be expected.

The current distribution looks safe, even with economic headwinds on the way, and offers a 4.75% yield at the time of writing.

## Should you buy RioCan for monthly passive income?

RioCan trades near \$21.50 per trust unit compared to the 2022 high around \$26. It fell below \$19.50 in July, but that could prove to be the bottom for the year. Investors seeking monthly passive income might want to take a half position in RioCan at this level and look to add more trust units if the market pulls back again in the coming months.

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