Should You Invest in Real Estate Stocks Right Now?

Description

Real estate stocks should make up a portion of a diversified portfolio. After all, real estate is one of the 11 sectors. Since real estate stocks have been in a substantial selloff, it could be a good idea to ease into quality holdings.

Since March, the Bank of Canada has increased the target interest rate from 0.50% to 3.25%. According to Statistics Canada, the latest data indicates inflation of 7% year over year in August. As inflation is still high, our central bank is expected to announce another interest rate hike next week on the 26th.

In today's rising interest rate environment, real estate stocks have been in a bear market. For instance, the **Vanguard FTSE Canadian Capped REIT Index ETF** is down 28% year to date. It may be smart for investors to focus on real estate stocks with growth components.

Tricon Residential

Tricon Residential (TSX:TCN) owns and operates more than 41,000 single-family rental (SFR) homes and multi-family apartments in North America. Its focus is on SFR homes, of which it has more than 33,400 in its portfolio. It targets to grow this SFR portfolio to about 50,000 by 2024.

About 95% of its balance sheet is in SFR homes and 98% is in the United States. In the latest quarter, it witnessed SFR same-home net operating income (NOI) growth of 10.5%. It also enjoys a high occupancy of north of 98%. Only 2% of its balance sheet is in residential development.

Its portfolio is primarily diversified across the high-growth U.S. Sun Belt states with more moderate home sizes and lower rent, which cater to the middle market and has, therefore, experienced lower turnover. Its blended rent growth (after mixing new and renewal rentals) is about 8.3%.

Year to date, the real estate stock is down about 38%. Across eight analysts, the stock has an average 12-month price target of $18.82, which suggests a meaningful discount of about 37%. As a bonus, investors also get a dividend yield of about 2.6% at $11.90 per share.

Summit Industrial Income REIT

Summit Industrial Income REIT (TSX:SMU.UN) is another real estate stock in a growing space. Additionally, it pays a decent cash distribution yield of approximately 3.2%.

The industrial REIT stock has declined 24% year to date. At $17.86 per unit, analysts believe the industrial real estate investment trust (REIT) is discounted by roughly 20% and can appreciate about 24% over the next 12 months.

Its occupancy is almost full at 99.1%, up from 98.8% a year ago. This represents there's a high demand for its industrial space offerings. It has an average lease term of more than five years and an average contractual rent escalation of 2.0% per year that improve the stability of its cash flow.

In the first half of the year, its funds from operations per unit increased by 16.1% and its same-property NOI growth was 4.8%. Its payout ratio improved to 76% from 85% a year ago.

The Foolish investor takeaway

Real estate stocks have experienced a substantial selloff due to rising interest rates. Investors should look into building positions in higher-growth stocks in this space, such as Tricon Residential and Summit Industrial Income REIT.

CATEGORY

1. Investing
2. Stocks for Beginners

TICKERS GLOBAL

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2. TSX:SMU.UN (Summit Industrial Income REIT)
3. TSX:TCN (Tricon Residential Inc.)

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