



## Was Your House Really a Good Investment?

### Description

If you ask many Canadians about their best investment, I'd guess that more than 90% would say their house.

Not only has Canada's real estate market been on fire over the last couple decades, but most Canadians also have a lifetime of precious memories associated with their principal residence. It's hard for stocks to compete with something like a child's first steps.

Those of you who have ever been involved in a real estate transaction other than your own can sympathize with this. Both sellers and buyers often fall victim to something called *subjective value*. Essentially, they're willing to value a piece of property at a premium because of something that isn't logical. A seller will associate memories with the place, while a buyer might fall in love with a unique feature of the property. This hardly ever happens with stocks.

Canadians are also sitting on record house values. Most U.S. homeowners were pretty happy with their real estate purchases in 2006. By 2009, the sentiment had obviously changed. If Canada's real estate bubble ever pops, a lot of those positive feelings will likely go away.

Besides, owning a house isn't exactly free. Everything from utilities to maintenance to taxes costs money. Let's not forget about the biggest cost of all, mortgage interest. Each of those costs takes a serious bite out of the profit of owning a home, even after it has gone up.

Although it's just a guess, let's assume the average Canadian homeowner pays an extra \$500 per month compared to a renter. I'd say it's a plausible guess because it's now cheaper to rent than to buy in many Canadian markets, and that's not even factoring in some of the various costs homeowners have to deal with. Instead of putting that money toward a house, let's assume somebody uses it to invest in real estate in another way, via a REIT.

Say our hypothetical investor chooses **RioCan Real Estate Investment Trust** ([TSX:REI.UN](#)), because it's the biggest in the sector. It owns more than 340 retail properties diversified across Canada and the United States, with the company's top 10 tenants only making up 31% of the portfolio. It's little wonder why the stock barely hiccuped when **Target** announced it was closing its doors in Canada. The stock

also has a history of consistent dividend payments, and currently yields 4.7%.

Let's assume our hypothetical investor did this exercise for 10 years, during which time the price of the average Canadian house has doubled from about \$200,000 to \$400,000. A homeowner would be sitting on a gain of \$200,000, while our renter would be sitting on approximately \$111,000 worth of RioCan stock, excluding commission and taxes.

Upon first glance, it looks as though owning the home was the better move. But remember, it's not exactly an apt comparison. Unless the homeowner paid cash for the house in the first place, his returns are decreased by taking out a mortgage.

If our renter was somehow able to use \$10,000 of his own money to borrow \$190,000 more to put into RioCan, after that same decade he'd be sitting on \$600,000. This easily beats the alternative of buying a house.

Even choosing **H&R Real Estate Investment Trust** ([TSX:HR.UN](#)) wasn't such a bad choice, and it sliced its dividend in half in 2009. H&R, which is one of Canada's largest multi-purpose REITs, still went up 8.85% annually over the last decade, assuming reinvested dividends. That not only beats the return on a typical Canadian house, but also means a \$500 monthly investment would end up being worth more than \$98,000 before trading commissions and taxes.

The point of the exercise isn't to focus on the investment. Rather, the point is to realize that home equity has value. Most people are happy to exchange it for a place to live, but is that the correct move? Over the last decade, investors in real estate have done pretty well — at least on this side of the border. But as Canada's market softens, I suspect there will be some who wish they would have kept their home equity in something a little more liquid. I'm pro-homeownership, just not from a financial perspective.

## CATEGORY

1. Investing

## TICKERS GLOBAL

1. TSX:HR.UN (H&R Real Estate Investment Trust)
2. TSX:REI.UN (RioCan Real Estate Investment Trust)

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## Date

2025/08/28

## Date Created

2015/01/27

## Author

nelsonpsmith

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