7 Reasons Why Dream Office REIT Is Better Than a Rental Property

Description

Admittedly, here at Motley Fool Canada we're somewhat biased towards owning stocks.

But at the same time, we shouldn't ignore creating wealth through real estate. It has many of the same characteristics as investing in the stock market. Real estate is mostly passive (especially if you use a property manager), spins off predictable cash flow, and people will always need a place to live. And since much of our banking system is based on lending against real property, it's easy to borrow up to 95% of the property's value.

But because of low interest rates and the overall interest in the sector, I'd argue that now is a pretty poor time to be buying Canadian real estate, especially for investment purposes. Investors are willing to accept anemic cash flows that barely cover the interest on the mortgage, content to make it up when the property inevitably appreciates in value. That has the potential to end very badly, as we saw in the U.S. back in 2007.

For investors who are looking for opportunity in the real estate sector, I think a REIT like **Dream Office REIT** (TSX:D.UN) is a much smarter choice. Here are seven reasons why.

Diversification

Buying a rental property is pretty much the epitome of putting all your eggs in one basket.

Dream offers much more diversification. It owns 176 office properties scattered across the country, covering more than 24 million square feet. It also boasts some of Canada's finest companies as tenants, including the **Bank of Nova Scotia**, **Enbridge**, and various levels of government.

Who would you rather rent to—these companies, or the average person responding to a rent ad on Kijiji?

Ultra passive

Although many investors are content to sit on their investments and forget about them, I'd recommend at least reading the quarterly reports each quarter. That's about four hours of work per year.

No rental property I know of only comes with four hours of work annually. Sure, you could give all that work to a property manager, but you'd also be giving up a large percentage of your profits.

No repairs

Although I'll admit the old cliché of getting called at four in the morning to deal with clogged toilets never happens, there are still going to be repairs to a rental property. It's the nature of the business.

By buying a stock like Dream, you don't have to spend a minute of your time worrying about any plumbing issues. Sure, they'll happen, but you can just let Dream's employees take care of everything. And because it has more than $6.8 billion in property, it's much more efficient for Dream to manage its properties than it is for you to manage your own.

Built in leverage

Let's face it. Borrowing 20 times the value of a down payment to buy a single condo is pretty risky. If the value of the property declines just 5%, the owner's equity is gone.

Investors who buy Dream are getting leverage built into the company. It currently owes $3.1 billion on $6.8 billion worth of real estate, a ratio that's a little high for the REIT world, but not excessively so. It sure is safer than owing $285,000 on a condo worth $300,000.

Better returns

These days, especially in Toronto or Vancouver, amateur real estate investors are looking at returns between 3-5%, and that's even before paying down the mortgage, or giving the tax man his share.

Meanwhile, Dream Office REIT offers an eye-popping yield of 8.9% thanks to recent weakness in the share price. And at a payout ratio of approximately 80% of funds from operations, that generous dividend looks to be pretty safe.

Discounted assets

In total, Dream has $7 billion in assets and $3.2 billion in liabilities, for a total book value right around $3.8 billion. And yet the company only has a market cap of $2.7 billion. Investors who buy today are picking up assets at a 29% discount to what they're worth. It's like buying a $300,000 condo for just $213,000, while getting paid nearly 9% to own it.

Real estate is a terrific way for someone to build wealth. But today in Canada, buying a rental property just isn't the way to do it. Investors are much better off to buy a high-quality REIT like Dream.

CATEGORY

1. Dividend Stocks
2. Investing

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1. TSX:D.UN (Dream Office Real Estate Investment Trust)

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Date
2025/08/18
Date Created
2015/06/11
Author
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