Young Investors Should Be Buying This ETF

Description

Anyone who lives in Toronto or Vancouver is painfully aware of the high cost of housing; the average price of a house in many neighbourhoods approaches a million dollars or more.

That, unfortunately, trickles down to the rental market, where the demand increases as less people are able to buy a home, forcing bidding wars to occur just as they do with the sale of houses.

That's just insane.

Rather than worry about how you're going to be able to afford to buy a home in either city, young investors should take advantage of the upside-down economic situation that exists in Toronto and Vancouver by investing in some of the residential REITs that trade on the TSX.

The Toronto Real Estate Board (TREB) brought out its fourth-quarter GTA rental market statistics January 26, and they were an eye-opener.

According to TREB, the monthly rent for an average two-bedroom apartment was $2,415 — 8% higher than in the same quarter a year earlier. A two-bedroom townhouse was slightly more affordable at $1,981 and experienced a smaller 3.2% increase year over year. Meanwhile, the number of listings decreased by 14.2% and 6.7%, respectively, over the same period.

So, not only is a house out of reach, but an apartment seems to be getting that way as well. Not to worry. Find a place with a few friends and accept the fact you might be doing this for a while and invest the savings in a TFSA, which you can withdraw tax-free when you're ready to buy a home.

There are approximately eight publicly traded residential REITs in Canada whose job it is to invest in apartment buildings in various parts of the country, generating monthly rent from tenants and, hopefully, capital appreciation when those buildings are sold in the future.

The question for any investor, not just young ones, is, which one or two should you buy?

I say, none of them. Instead, focus on exchange-traded funds that will do it for you.

Now, here in Canada, we don’t have an ETF that’s exclusively focused on residential real estate, so we’ll have to consider something that also invests in other real estate assets such as offices, industrial buildings, hotels, retail, healthcare, etc.

First Asset Canadian REIT Income Fund (TSX:RIT) is the ETF I’d recommend for young investors because it has 28.4% of its portfolio invested in residential REITs — much higher than the other real estate–focused ETFs on the TSX. By comparison, the **iShares S&P/TSX Capped REIT Index Fund** (TSX:XRE), Canada’s biggest real estate ETF with $1.3 billion in net assets, invests just 19% in residential REITs — 940 basis points fewer.

Although RIT is 20 basis points more expensive than XRE at 0.75%, its performance over the past five years more than makes up for any problem you might have with its management fees — RIT’s annual total return over the past five years is 10.7% through December 31 compared to 5.8% for the XRE — and simultaneously makes a solid argument that active management isn’t dead.

Investing in real estate while you can’t afford a home is a great way to keep you invested in an asset class that provides good protection against inflation.

And when you are ready to own a home, it makes a good time to sell your RIT holdings tax-free to use as a part of a down payment, because once you own a home, the biggest purchase you’ll ever make, you’ve pretty much got real estate covered.

CATEGORY

1. Investing

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1. TSX:CAR.UN (Canadian Apartment Properties Real Estate Investment Trust)
2. TSX:XRE (iShares S&P/TSX Capped REIT Index ETF)

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