Forget About Buying a House; Buy These 2 REITs Instead and End Up Richer

Description

Even after one of Canada's greatest real estate bull markets, there's scant evidence that buying a house and living in it qualifies as a good investment.

Homeowners who have a house that's increased by 150-200% over the last 20 years may disagree with me, but they're missing some important facts.

These folks constantly understate the amount of money they've had to pour into their property over the years. Appliances need to be replaced when they break. Furnaces and hot water tanks wear out too. A roof can easily cost $10,000 or more. Yards require expensive equipment to maintain. And we haven't even begun to talk about unnecessary cosmetic changes.

Then there are the additional costs like mortgage interest, property taxes, home insurance, and utilities. Sure, you'd have to pay some of those things even if you rent, but the point is those costs exist and they add up.

By the time we factor in those expenses, the massive gains many homeowners have experienced start to evaporate.

For real estate to be a good investment, it needs to spin off income. Rental real estate generates enough revenue to pay the expenses plus have enough for a decent profit margin.

The difference is stark. Say you buy a building yielding 8%. 25% of the rent goes toward expenses, meaning that the investment returns 6% a year before taxes. If you live in the same building, you get zero income and still have to pay the expenses.

I'm not saying that folks shouldn't own homes. There are plenty of advantages to owning, including stability, cost certainty, and being able to customize the place to your personal taste. But it's not generally a great investment.

Owning rental real estate is the better way to get ahead. Here are two great REITs to get you started.

H&R

H&R Real Estate Investment Trust (TSX:HR.UN) is one of Canada's largest real estate owners. It owns some 38 million square feet of real estate split between retail, office, industrial, and residential space. It has property across Canada and has recently been focusing on its United States expansion, including a large residential complex near **Amazon.com's** upcoming Long Island City headquarters.

H&R has delivered great returns over the past decade. When you include reinvested dividends, shares are up 409.75% over the last 10 years, which translates into a 17.69% annual return. That's enough to turn an original $10,000 investment into once worth more than $50,000 today.

Investors might not be able to replicate those returns over the next decade, since 10 years ago we were in the depths of the Great Recession. But H&R looks poised to deliver solid returns going forward. The company continues to expand by making smart acquisitions. It has proven it can develop property profitably, too.

H&R shares currently yield 6.7%, with a solid payout ratio under 80% of funds from operations.

Northview

Northview Apartment Real Estate Investment Trust (TSX:NVU.UN) owns apartment buildings mostly located in more remote areas. Many of its peers focus on the Greater Toronto market, while Northview owns the majority of its property in the Northern and Atlantic regions. These properties can be purchased for a better cap rate than ones in larger centers, which leads to better returns.

The bad news with this strategy is the trust has a relatively high concentration of properties in markets heavily dependent on oil. This should impact results going forward, although it shouldn't be a major deal. Retail and industrial space always get hit much harder than residential during tough times.

Like H&R, Northview has delivered terrific returns over the last decade; $10,000 invested during the last week of 2008 would be worth nearly $25,000 today with dividends reinvested. That's a total annual return of 10.38%.

Northview pays a generous 6.7% dividend, which is much higher than its peers. The distribution is sound too, with a payout ratio just over 75% of funds from operations.

The bottom line

The difference between owning real estate to live in and owning it as an investment is stark. One generates income. The other costs money. If you're really looking to make a nice return owning real estate, ditch your primary residence and invest in some of Canada's best REITs.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

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

PARTNER-FEEDS

1. Msn
2. Newscred
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