3 Reasons Why REITs Are Better Investments Than Rental Properties

Description

Direct property ownership as an investment to create passive income and long-term wealth has long been an attractive option for many investors. While owning “brick-and-mortar” property generates income and capital appreciation, it also comes with many pitfalls that can delay or even erode wealth creation. A superior means of building wealth and a sustainable regularly growing income stream while still owning a heard asset such as real estate is to invest in publicly listed real estate investment trusts (REITs).

Let me explain why.

Greater liquidity

One of the greatest disadvantages associated with owning direct property is the lack of liquidity. It can be a lengthy and costly process to sell a property, whereas an investor can sell units in a REIT at the click of a button at a far lower transaction cost.

Importantly, during a cash crunch, where you may need to access a portion of your capital, you can sell a portion of the stocks, yet you can’t sell an investment property brick by brick or square meter by square meter. That means REIT investors can access their capital in a timely and cost-effective manner.

Improved diversification

Now that the average Canadian house price is over $500,000, it is extremely difficult for direct property investors to diversify into other investment properties or assets because the large amount of capital required means many can only afford one or two investment properties.

That creates significant risks with investor funds being highly concentrated in a small portfolio of assets. It only takes a mild property correction to wipe thousands off the capital value of the investment, or worse, a bad tenant or long-term vacancy to wipe out a significant portion of rental income.

Whereas with as little as $1,000, you can purchase units in a REIT that invests in a diversified portfolio of properties and even access classes of property not normally available to regular investors because of the high purchase prices such as light industrial, office, and retail properties. This significantly reduces risk while enhancing income and the opportunity for capital appreciation.

Lower cost and less risk

Rental properties can be time consuming, stressful, and costly to manage, especially if you intend to manage them yourself. There are considerable risks involved, which can interrupt your income stream, magnifying stress and expenses. These include vacancies; despite having no income due to vacancies, you are still liable to pay all expenses associated with the property and meeting mortgage repayments.

Bad tenants also pose a significant risk. They can withhold rent, damage the property, and refuse to leave, leading to the expenditure of substantial amounts of time and money to rectify the situation.

Whereas once you have purchased your portfolio of REITs, you can sit back and wait worry free for the distributions to start rolling in, without having to expend any further, energy, time, or money.

Putting it together for investors

One diversified REIT that possesses all the advantages discussed is **Brookfield Property Partners** (TSX:BPY.UN)(NASDAQ:BPY). It owns a US$85 billion globally diversified portfolio of flagship office and retail properties, including Brookfield Place in New York and Toronto as well London's Canary Wharf.

Brookfield Property's earnings and cash flow has grown at a healthy clip since 2014. Since then, funds from operations (FFO) have expanded at a compound annual growth rate (CAGR) of 8%, while the trust's distribution has grown by 6%. With a US$6.7 billion portfolio of projects under development, Brookfield Property's earnings and FFO will continue to grow at a steady rate.

Brookfield Property has hiked its distribution for the last six years straight to now yield a very juicy 7%, which is significantly higher than the average gross rental yield on Canadian residential rental properties. What makes it a particularly compelling buy is that Brookfield Property is trading at around a 38% discount to its net asset value (NAV) of US$27, indicating there is considerable capital appreciation available. It is rare that such a high-quality REIT would be trading at a deep discount to its NAV, making now the time to buy.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:BPY.UN (Brookfield Property Partners)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Sharewise
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