Real Estate Investing: Less Is More

Description

Real estate investing is a great long-term wealth-building tool. Many investors think of owning one's home as real estate investing, or maybe an investment property. In this article, I am going to dive into the Real Estate Investment Trust (REIT) sector. Specifically, I will discuss why, in today's context, less diversification is better for real estate investments.

Secular trends strong and unlikely to change

The secular trends driving various real estate sub-sectors will not suddenly do a 180. We are not heading back to the glory days of the 1950s or 1960s. How people use property has fundamentally changed. These are tectonic shifts, not short-term "fads" that will revert to the past mean.

I'm going to discuss why avoiding exchange-traded funds (ETFs) tracking the broad REIT sector is a bad idea. Again, less is more when it comes to the diversification of your real estate holdings.

Certain REIT sub-sectors will perform better than others

The long-term shifts I just mentioned in specific real estate types are more pronounced than in others. For example, office and retail real estate are likely to remain in a secular decline for the long-term.

The coronavirus pandemic has only accelerated this shift, and it appears the market has taken this shift as a signal (finally) that times really *are* changing.

More and more companies are now recognizing the benefits of allowing their employees to work from home. For most companies, the costs of maintaining an office space just may not make sense long term. This is particularly true as, contrary to popular belief, most employees are likely to raise their productivity at home.

Similarly, retail real estate will be fundamentally different 10 or 20 years from now. Increasingly, businesses are shifting a higher portion of their business online. During the coronavirus outbreak, we saw the value of having a well-managed e-commerce presence.

The stock market has accordingly rewarded the companies with e-commerce foresight. In turn, the stock market has punished those who stuck with their bricks-and-mortar roots. An increasing number of companies are realizing that we don't need a physical presence.

At the very least, these companies need less of a physical presence. These companies will see how e-commerce can actually improve profitability long-term due to lower fixed costs.

The problem with ETFs

Most ETFs tracking the REIT sector diversify across all real estate types, which means most ETFs will have an allocation of office and retail real estate.

I suggest avoiding such ETFs and focus instead on either individual REITs with exposure to industrial or residential real estate or ETFs that hold REITs with exposure to only these two sectors. One such example is **Dream Industrial REIT.**

I see too much in the way of long-term risk for investors looking to hold any stocks with exposure to office or retail real estate right now. For the long term, conservative income-focused investor (the typical REIT investor), I would caution about too much diversification in the real estate sector.

Stay Foolish, my friends.

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