Real Estate Investing 101: Active and Passive Investing

Description

When it comes to real estate investing, what first comes to mind is buying a home. Surely, it is one of the biggest investments of our lives! We expect that in the decades we own our homes, they will appreciate in value.

Actively investing in real estate

Real estate investing also comes in other forms. Rental properties usually follow after people have purchased their homes and have additional cash for long-term investing. Some folks also rent out a portion of their homes (like the basement or a room) so that their principal residence also generates rental income.

In any case, rental properties require active work — looking for new tenants when your old ones leave and property management, including repairs and maintenance. Landlords who don't want a side job might hand over the work to a property manager, but in so doing will increase their operating costs. As a result, their net rental income also diminishes.

Unless you have a related real estate business, you're unlikely to go spend millions of dollars investing in other types of properties like office towers, malls, and industrial space that require other specialized management. However, you can invest in residential properties and other real estate types on the stock market passively through real estate investment trusts (REITs).

Passively investing in real estate

When investing in Canadian REITs, investors can buy shares and sit back to watch their investments grow, relying on the professional management teams behind the REITs to do all the work. However, you do need to pick quality investments that you expect will grow over time and aim to buy at cheap valuations.

You can begin your research with the following Canadian REITs that are relatively cheap and have growth potential.

Currently, **InterRent REIT** (TSX:IIP.UN) trades at a decent discount of nearly 21% from the 12-month consensus price target of $19.63. Other than a yield of 2.2% paid in the form of a monthly cash distribution, you can also expect price appreciation. Let's be more conservative and assume that InterRent stock can arrive at $19.63 per unit in two years instead of one, it'll still return total returns of approximately 14.6% per year. InterRent has raised its cash distribution every year since 2012 with a five-year dividend-growth rate of about 7%.

In late January, portfolio manager Andrew Moffs said this:

> "We've been bullish since the recent selloff of the stock. InterRent has a dynamic management team. It is in the Ottawa, Toronto and Montreal areas where there is population growth. This includes immigrants who are looking for reasonably priced housing."
> *Andrew Moffs, senior vice president and portfolio manager at Vision Capital*

Canadian Net REIT (TSXV:NET.UN) invests in commercial real estate, but it enjoys net-lease and management-free leases. Consequently, its cash flows are higher quality with lower cash outflows. Predictable cash flows combined with a juicy yield of about 4.3% makes the small-cap REIT perfect for passive income. Like InterRent, Canadian Net REIT is a Canadian Dividend Aristocrat. NET.UN's five-year dividend-growth rate is approximately 13%. Over the next few years, it's hard not to see it grow at a rate of around 10%.

Canadian REIT cash distributions are different from dividends

Notably, Canadian REITs pay out cash distributions that are taxed differently than dividends. For example, cash distributions that are returns of capital reduce the cost basis of your investment. These cash distributions are tax deferred until you sell your REIT investment in a non-registered account or your cost basis goes to $0.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:IIP.UN (InterRent Real Estate Investment Trust)
2. TSXV:NET.UN (Canadian Net Real Estate Investment Trust)

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