



Better Buy: Real Estate or REITs?

Description

[Real estate investing](#) in Canada has been widely regarded as one of the most rewarding approaches to putting your money to work for substantial long-term returns. A stellar rise in the valuation of residential real estate over the last decade or so has made many Canadians who own residential real estate much wealthier.

However, buying a house as an investment property to generate rental income in today's market has become nearly impossible. Real estate investment trusts (REITs) also offer you the chance to gain exposure to the performance of the industry without the cash outlay and many of the hassles involved with being a landlord.

Choosing between buying a rental property or investing in a REIT is a big debate for many investors today. Suppose that an investor has the capital to purchase real estate assets even at today's prices. In that case, it might seem more sensible to attempt buying a house instead of scooping up REIT units. But buying a REIT might still be a smarter investment decision.

Let's take a look at the reasons you could invest in rental property or REITs to help you determine what might be a better method to invest in real estate.

Why buying rental property makes sense

Investors buying investment properties typically do not sell soon after they make the investment. Most property investors tend to make the purchase with the assistance of a mortgage. The idea is to use leverage as a means to build equity and pay off the debt over years. The value of the property appreciates through the years.

Investors with a long investment horizon who want to rely on long-term price appreciation for substantial profits several years or decades down the line might find it more reasonable to buy a home. However, owning and managing a rental property for a long time comes with several challenges. You will have to contend with various associated costs and invest a lot of time and money in managing the property.

Why investing in a REIT makes more sense

REITs could make for an excellent investment for investors with a short investment horizon who want to enjoy more liquidity with the assets they own. When you buy a rental property, you will likely need to tie down a substantial amount of money for several years. If you purchase the house with the help of a mortgage, recovering your initial investment through rental income could take years.

Granite REIT ([TSX:GRT.UN](#)) is a trust that trades for \$89.04 per share at writing, and it boasts a 3.53% forward dividend yield that it pays out each month. Owning units of a REIT generates monthly income like you would with owning an investment property.

However, it does not come with the same massive upfront cost. You also do not need to pay property taxes, handle maintenance, or worry about finding tenants (or rent collection).

You can save even more on taxes on your income through REITs by buying and holding units in a registered account like a Tax-Free Savings Account (TFSA) or a Registered Retirement Savings Plan (RRSP). REIT investing does not offer similar capital appreciation as investment properties.

However, you could generate substantial wealth growth by using the power of compounding by reinvesting your cash distributions to purchase more units.

Foolish takeaway

REITs typically present a more viable option for investors to take advantage of the real estate industry's returns. You get the monthly income of a rental property without the hassles of managing one yourself and dealing with all the associated costs yourself. The money you invest in buying shares of a REIT goes towards helping you generate truly passive income through real estate.

A REIT like Granite, a Canadian Dividend Aristocrat, also means your passive income keeps increasing each year due to annual hikes in shareholder distributions. It might be better to put your capital to work by investing in REITs instead of buying rental properties to create a passive-income stream.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:GRT.UN (Granite Real Estate Investment Trust)

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Date

2025/08/24

Date Created

2022/05/30

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