Love Passive Income? Here’s How to Make Plenty of It as a Real Estate Investor

Description

Everyone knows that investing in a rental property is one of the most lucrative ways of earning passive income. However, the red-hot Canadian housing market has priced out many investors. Fear not, there is still an alternative investment for those desiring real estate exposure and passive income.

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Buying shares in a real estate investment trust, or REIT, can be a great way of diversifying a stock portfolio. As a fund of real estate assets trading on a stock exchange, REITs offer real estate exposure at a low cost, along with high monthly dividends.

However, picking the right REIT to invest in can be difficult. While you get caught up reading the recommendations from the other Foolish writers, my suggestion is an exchange-traded fund (ETF) that holds a diversified portfolio of REITs. Here’s why.

Why REITs? Why REIT ETFs?

Being a landlord is harder than people imagine. It’s not as simple as collecting a juicy rent paycheque every month. As a landlord, you’re liable for collecting rents, making repairs, paying property taxes, and dealing with tenant issues. It can quickly balloon into a full-time job as opposed to a passive income stream.

With a REIT, all you need to do is sit back and collect the monthly distributions. Unlike rent income, income from REITs can potentially be tax-free if you hold them in a TFSA. Unlike with real property, you can invest as much as you like without needing to take out a mortgage.

My favorite REIT ETFs

The Canadian ETF industry has a variety of ETFs available, so it’s important to shop around and compare your options. A great beginner pick is the **Vanguard FTSE Canadian Capped REIT Index ETF** (TSX:VRE), which holds 19 REITs and real estate service companies.

VRE is the lowest cost option with a management expense ratio of 0.38%. Right now, it has a 12-month trailing yield of 3.78%. Still, some investors might not like how it doesn't offer pure-play REIT exposure given that it also holds real estate service companies.

An alternative here is the **iShares S&P/TSX Capped REIT Index ETF** (TSX:XRE), which only holds 18 REITs and no real estate service companies. XRE currently has a higher 12-month trailing yield of 3.93%, but costs a higher MER of 0.61%.

Some investors might not like how XRE and VRE are highly concentrated in their top five holdings. This is a result of both ETFs being market-cap weighted. An alternative for those seeking higher diversification is the **BMO Equal Weight REITs Index ETF** (TSX:ZRE), which holds 24 different REITs in equal allocations.

The Foolish Takeaway

Regardless of your ultimate choice, any of the three REIT ETFs could be a great way of adding real estate exposure to your passive income stream. The ultimate choice should boil down to your investment objectives. Personally, I think VRE is best for those desiring the lowest fees, XRE for those seeking pure REIT exposure, and ZRE for those who want greater balance and diversification.

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3. TSX:ZRE (BMO Equal Weight REITs Index ETF)

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