

WHY REITs ARE ATTRACTING INVESTORS AGAIN

In a dismal real estate market, some see a prime opportunity.

Presented by Glazer Financial Network

This may be a great time to get into an REIT. If you're trying to sell commercial or residential real estate today, you face quite a challenge. On the other hand, buyers are seeing all kinds of opportunities to pick up properties at depressed prices.

You may want to seize these opportunities, but you may not want to manage property. Is there a way you can invest in real estate without turning into a landlord?

There is. REITs (Real Estate Investment Trusts) allow you to get into the commercial real estate sector without the hassles of property management.

You may assume that REITs have taken a pounding recently. You would be wrong. REITs have outperformed stocks in the last couple of years. The total return for the FTSE NAREIT All-Equity REIT Index was +27.95% last year. The total return of the FTSE NAREIT All-REITs Index was +27.58%. Compare that to a total return of +15.05% for the S&P 500.¹

With reduced real estate valuations and stricter credit terms, the present commercial real estate market has many distressed owners and properties, so now may be a prime time to get into a REIT in pursuit of dividends and long-term appreciation.

According to data from Real Capital quoted by Bloomberg, the average capitalization rate on commercial properties (excluding hotels) was 7.2% as of 4Q 2010. Stack that up against the yield from a CD, a corporate bond or a 10-year Treasury.²

What do you own when you invest in a REIT? An equity REIT offers investors an opportunity for fractional ownership of a real estate portfolio. The portfolio commonly includes high-quality commercial properties - shopping malls, apartment buildings, office complexes, sometimes even things like golf courses or resorts.

REITs have no investment minimums, so they allow the small investor an easy entry into the "major leagues" of commercial real estate.

While investors own common shares in the REIT, there is a wrinkle that distinguishes a REIT from a corporation. A REIT doesn't get to decide what to do with its after-tax profits. It must pay out 90% of its taxable profits as dividends. This exempts a REIT from having to pay corporate income tax.³

There are three different classes of REITs.

- **Equity REITs** invest in hard assets (real property). The vast majority of REITs are equity REITs and most of them specialize in an income property type. There are apartment REITs, retail REITs, industrial REITs and so forth.
- **Mortgage REITs** do not invest in hard assets. Instead, they take out short-term loans to buy mortgage-linked securities. Their profits stem from the difference between the long-term interest rates of the bonds and the short-term interest rates paid on the loans.
- **Hybrid REITs** invest in commercial properties and mortgage-linked securities.

In addition, there are traded and non-traded REITs.

- **Public REITs** trade on an exchange, and therefore offer more liquidity to an investor. The downside, naturally, is that they also expose an investor to market volatility.
- **Private REITs** are not (yet) publicly traded and reduce the degree of volatility for the investor. Liquidity can be an issue as you have to sell shares through the REIT company, unless another investor in the REIT steps up to buy them.⁴

What kind of investment income does a REIT provide? The monthly dividend income from a REIT is often around 7-8% - not bad in a dire real estate market, and better than many bonds and CDs.

REITs offer another way to diversify. If you own a bunch of stocks and funds, they give you a chance to broaden your portfolio. If you own real property already, they still offer you a nice avenue for diversification.

If you are a sole owner of an income property, you are positioned to receive 100% (or nearly 100%) of the profits when you sell it. However, you must shoulder the burden of property management yourself or screen for a competent, attentive third-party manager, and you are also poised to personally absorb any loss or unforeseen costs. Sole ownership includes sizable risks.

In contrast, an equity REIT might own dozens, hundreds or even thousands of income properties - and all of them are professionally managed, often by a single firm owned by the REIT. So investing in real estate through the REIT gives you a quality of diversification you couldn't possibly attain as a small investor, a quality of property management that the small investor seldom sees, and the leadership of veteran commercial real estate investors making the buy and sell decisions ... along with the potential for a nice dividend.

Registered Representatives offering securities through Kovack Securities, Inc. Tel (954)752-4771. Member FINRA/SIPC. Investment advice offered through GFN Capital Management a Registered Investment Advisor. GFN Capital Management is not affiliated with Kovack Securities, Inc. or Kovack Advisors, Inc. ©2008 Glazer Financial Network. All Rights Reserved.

This material was prepared by Peter Montoya Inc., and does not necessarily represent the views of the presenting party, nor their affiliates. This information should not be construed as investment, tax or legal advice. The publisher is not engaged in rendering legal, accounting or other professional services. All information is believed to be from reliable sources; however, we make no representation as to its completeness or accuracy. If assistance or further information is needed, the reader is advised to engage the services of a competent professional.

Citations.

- 1 - advisorone.com/article/us-reits-rose-nearly-28-10-almost-double-sp-500 [1/5/11]
- 2 - bloomberg.com/news/2011-03-10/wealthy-u-s-individuals-invest-in-commercial-property-in-quest-for-yield.html [3/9/11]
- 3 - investopedia.com/articles/04/030304.asp [3/3/04]
- 4 - ccim.com/cire-magazine/articles/non-traded-reits-offer-stability-and-portfolio-diversification [3/22/11]