

#### IN THIS CHAPTER

- » Discovering what REITs are and what they do
- » Recognizing the sheer size of the publicly traded U.S. REIT sector
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- » Finding out why REITs are easy to love

## Chapter **1**

# Who Wants to Be a Virtual Landlord?

**B**eing a landlord can make you rich. That's what you want to hear, I know. And fortunately, it's true. Owning buildings and renting them out can be extremely rewarding as you collect income from the property you own. All the same, I wouldn't call being a landlord an easy road to wealth.

There's a lot involved in renting out property on a legal level and perhaps even more so on an ethical one. So many issues can (and do) come up, from structural considerations regarding the actual buildings and properties they sit on to weather-related hazards that can literally hit your holdings, to general nuisances and differences of opinion with tenants. For those who manage entire apartment buildings, those differences can present themselves on a daily basis.

But suppose you could bypass all that by being a virtual owner instead. Suppose you could be almost entirely oblivious of the day-to-day details of dealing with rentals and renters — yet still receive steady income from them every month or every quarter. Suppose you could go online, click a few buttons, and put a few hundred dollars down (or more, if you so choose) to become an almost instant virtual owner of commercial real estate.

Would you be interested? If so, this book about real estate investment trusts, or REITs, is for you.

## Commercial Real Estate for the Masses

For centuries and even millennia, owning property was a wealthy person's venture. In fact, land was one of the biggest signifiers of wealth, with kings and lords fighting wars over who was entitled to what. Peasants and even noblemen stayed on land at the will of their superiors. And while that arrangement wasn't always the brutal, one-sided affair Hollywood likes to portray, it obviously was a far cry from an easy road toward wealth independence.

Even as global societies advanced and individuals started owning their own homes, commercial real estate and its benefits (potential pitfalls as well) remained firmly a resource for the rich. It wasn't until the mid-20th century that REITs (pronounced "reets") were introduced and we "little people" had a solid chance of benefiting from sizable property ownership, too. This game-changing category gives the average investor the same access to property-based money-making potential as the rich. I'd even go so far as to say that REITs exist to even out the playing field. (For more detail on when and where and how they were created, turn to Chapter 3.)



REMEMBER

REITs are companies that own, manage, and/or finance real estate holdings. These holdings can be in the form of apartment buildings, hotels, shopping centers, self-storage facilities, warehouses, and even billboards, data centers, and woodlands. And that's the short list — a list that keeps growing every decade. In Chapters 6 and 7, I go through each REIT sector in detail, discussing their pros and cons, because there are definite positives and negatives to know about.



TIP

As I continuously stress throughout this book, there is no such thing as a perfect investment. So the more you know about REITs — or any other asset you want to put money into — the better off you'll be.

## REITs Do the Work for You

You probably don't have the finances, time, or desire to start your own real estate investment trust. Which is perfectly fine. Even reasonable. But if you're reading this book, you probably do have the finances, time, and desire to buy into REITs that someone else started, developed, and continues to successfully run.

As I previously state, it takes very little money, comparatively speaking, to buy a few shares. And when it comes to publicly traded REITs — the ones you see listed on the stock market — it takes just a call to your broker or a series of clicks on your keyboard to get the deal done. That's all you need to become a landlord.

And not just any landlord, but a no-muss, no-fuss one. Because, again, you're a shareholder owner, not a hands-on owner. That means you don't have to deal with collecting rent, fixing roof leaks, paying insurance, or evicting problematic tenants and finding better ones.

Take it from me. I have more than three decades of experience in building and brokering over \$1 billion of income-producing real estate transactions. I've been a landlord to drugstores, auto parts stores, casual-dining restaurants, fast-food restaurants, tire centers, grocery stores, movie theaters, bookstores, discount stores, warehouses, billboards, cell towers, office buildings, and fitness centers. So trust me when I say there's a lot involved.

Regular landlords have to deal with things like high leverage, partnership disputes, recessions, tenant bankruptcies, and even tornadoes. (My neck of the woods in South Carolina isn't part of Tornado Alley by most definitions, but we still get these forces of nature more often than I'd like.) In Chapter 3, I explain the three Ts most landlords wish they didn't have to deal with: toilets, trash, and taxes. By this, I mean all the parts and pieces they're responsible for — the physical structures complete with pipes, electrical wiring, windows, and doors — as well as services and those pesky obligations to Uncle Sam.

This all adds up, taking significant chunks out of the money landlords make.



REMEMBER

Of course in a capitalistic society, they're not supposed to add up more than your profits. If you do it right (with perhaps a little bit of luck added in), you can make a really decent living. There are specific advantages to owning direct real estate, such as depreciation and lower volatility, as I explain in Chapter 2. But doing it right entails a lot of time, effort, and financing.

There's also the fact that even if you were making a seven-figure salary, it would still be difficult to personally buy up such properties as

- » Caesars Palace in Las Vegas
- » The Empire State Building in New York City
- » The Hilton Waikoloa in Hawaii

The same goes for 195,000 acres of farmland, 226,000 cellphone towers, or over 12,000 free-standing properties worldwide — each set with a single purchase. And that's to say nothing about strings of properties in more than 40 countries and regions around the globe.

Yet REITs allow you to do exactly that. You don't get to own the entirety of those portfolios, of course. You're just one of hundreds, thousands, or even tens of thousands of other investors. But as I note in Chapter 3, fractional ownership still matters. Plus, you still get a piece of the rental profits, not just through share price appreciation but also through dividend payments multiple times per year.

This is because REITs, by law, have to pay out at least 90 percent of their taxable income to their shareholders in the form of dividends. As Chapter 3 details, this allows them to avoid taxes themselves. Shareholders still have to pay taxes on any gains you make, mind you. But they get higher dividends as a result of this corporate-level deal.

## Get Paid While You Sleep

One of the reasons I decided to get into the real estate rental industry (so many moons ago) was because someone told me the best way to make money is while you're sleeping. It sounded like good advice, and I took it to heart along the way.

Being a landlord certainly helped me generate significant wealth by leveraging the most powerful tools of appreciation and compounding, as I discuss in Chapter 2. What I didn't know at the time though was that REITs provide all those benefits, plus the benefit of liquidity, along with transparency and diversification.

This is what makes so many REITs *sleep well at night*, or SWAN, investments. While I didn't coin the term, I use it to describe a high-quality stock that pays out dividends while you're sleeping . . . like so many of the REITs I explore in this book.

## Size Does Matter

Here's another factor to appreciate about these commercial real estate assets: their sheer size. This is a big deal for a number of reasons. For one thing, the publicly traded U.S. REIT sectors magnitude makes it liquid, allowing investors to trade in and out largely at will. Another point to consider is how the wide, wide world of real estate investment trusts provides investors with considerable diversification benefits.

For instance, tech-centered investors who want something more affordable and less volatile than Facebook can look to Digital Realty, a massive (and growing) network of data centers around the world. Or if you think that brick-and-mortar retail isn't going away, you can consider my favorite REIT, Realty Income. This means that you (the investor) can design and build your portfolio based on your individual tastes and preferences. In Chapter 10, I provide a blueprint to consider strategies I've used over the years.

There are also basic REIT categories to consider above and beyond which properties they tend to buy, which means the larger asset class provides even more opportunity to diversify. I break them all down in Chapter 4 if you want to see what I mean.

Basically, commercial real estate in general and REITs in particular are enormous investment categories that offer something for just about every investor, no matter what their interests and goals are.

## Focusing on Fundamentals

I'm sure you're familiar with the board game Monopoly, where you use play money to buy real estate, utilities, and railways. The goal is to dominate the board and have scale advantage — the point where a company has a big enough presence that it gets better banking and business deals than the competition. The issue is how to go about it. Which properties should be picked up and which ones should be passed over?

The same questions apply to income-producing real estate in the real world. When you invest in it by buying up REIT shares, you're buying (portions of) portfolios in high-quality, well-placed real estate operated by professional, ethical management teams. That's the ideal, anyway, and the ideal is very often true. But it's not a guarantee, so you do have to research and analyze what you find.

At least you really, really should.

If that sounds daunting, don't worry! That's what Chapter 8 is there for — my favorite chapter in this book. It's where I show you how to choose your REITs wisely by understanding how to calculate property values and earnings metrics, as well as balance sheet basics. The key to unlocking their value is rooted in their cost of capital: how much money they're spending in order to make money.



REMEMBER

You need to know that REITs thrive when their return on invested capital (ROIC) is greater than their opportunity cost of capital. If the former is at or below the latter, growth may not create value and can lead to a *value trap* or *sucker yield* scenario. More about those in my favorite chapter.



TIP

I also use Chapter 8 to fill you in on REIT-specific financial terms such as funds from operations (FFO) and net asset value (NAV). These can help you understand the margin of safety concept further as you start analyzing potential portfolio picks for yourself. In which case, always keep in mind that the subjects of risk and cost of capital are essential and inseparable. So while you're free to read this book in whatever order you'd like, picking and choosing topics as you see fit, I recommend that you not skip over Chapter 8. It's got way too much important information in it.

## REITs on the Street

If you've read this far, feel free to stop for a little bit. I've got some homework for you.

Get out of the house. Go for a drive. See what you can see. Or, if you're perfectly content reading on right away, at least think about your daily commute to work, the grocery store, church, the gym, or wherever else you tend to go. No matter where you're headed locally (in the United States, at least), there's a good chance you'll find yourself in close proximity to a REIT-owned property. That workplace, grocery store, church (yup, even some churches), or gym you frequent might even fall under that category.

As I reference in Chapter 4, REITs own approximately one out of every ten institutional-quality buildings in the United States. And that percentage continues to grow with investor demand.

## A Slice for All Types

While REITs were designed for the average investor, I explain in Chapter 11 that institutions, such as pensions and endowments, buy them up too. These are the big fish. The whales. And boy, but do they like to eat up shares of whatever they fix their appetite on, including REITs.



TIP

Don't be hating on these big-time players, though. They're not stealing from your pool of potential. If anything, they're helping your investments grow both in recognition and price. This category of investors is important to the growth of the sector in ways that I'm more than happy to lay out.

There are now 29 REITs included in the S&P 500 (as of May 2023). That could not have occurred without enormous firms like Vanguard, Cohen & Steers, Green Street, BlackRock, and State Street getting involved. For decades, that wasn't the case, which was to REITs' detriment. Institutional investors chose to allocate funds elsewhere, deeming REITs to be too new and risky. And I'm not saying they were wrong in displaying caution.

But REITs evolved into something worth putting big money into. I detail their historical progression in Chapter 3, including how 150 million Americans now live in households that invest in REITs through their 401(k)s, IRAs, pension plans, and other investment funds. You can also own REITs through vehicles such as exchange-traded funds (ETFs), mutual funds, and closed-end funds. These can be extremely powerful options to consider, which is why Chapter 12 gives you facts, figures, and important insights into what they are and how you can use them.

I personally prefer to buy up individual stocks instead of baskets of them. But I very well understand that everyone is different. Some of us prefer to play it as safely as possible. Some of us can afford to take greater (though not unreasonable) risks. And some of us choose a middle path between the two.

Whichever category you fall into, this book seeks to give you the kind of guidance you need to make it work for you.

