

Residential investment property or real estate investment trusts?

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Australian investors are generally passionate about property as an investment. Most investors have focused on residential property, but what about real estate investment trusts?

What are real estate investment trusts?

A real estate investment trust (REIT) or listed property trust (LPT) is a collective investment vehicle that owns a portfolio of property. REITs are quoted on the Australian Securities Exchange (ASX), which allows you to purchase an interest in a professionally managed portfolio of commercial real estate. Real estate investment trust managers invest in properties across a range of geographic regions, with varying lease lengths and tenant types. As at 31 December 2010 there were 43 REITs listed on the ASX, with a combined market capitalisation of over \$62 billion¹.

Advantages of real estate investment trusts

While history has shown that property has proven to be a good investment, residential property is only one way to access the property sector.

There are a number of advantages of REITs over traditional residential property investments including:

- **Diversification.** We all know the phrase 'don't put all your eggs in one basket'. The same principle applies to property investment. There is a significantly higher chance of an isolated event changing the value of a residential investment property. With an investment in REITs the risk is spread across a number of properties. Also REITs generally invest across a number of property sectors such as office, retail and hotels – not just residential property. Given that these sectors do not perform the same way at the same time, you get further diversification. Some REITs also have exposure to international property, providing yet another level of diversification.
- **Liquidity.** In the future you may need to sell your investment. While selling a residential property can take some time – finding an agent, advertising, negotiating the sale and settlement – the sale process with REITs is significantly faster. REITs are listed on the ASX, so selling an investment is as easy as placing an order with a stockbroker. Also, instead of selling your entire investment, you can choose how much you liquidate.
- **Access to new opportunities.** REITs provide investors with investment access to sectors of the property market once beyond the scope of the average investor. With the combined spending power of investors, REITs invest in hotels, office towers and shopping centres.
- **Expertise.** REITs are managed by property professionals. They are skilled at determining which properties offer the most value, both in terms of capital growth and income, negotiating on price, development, tenancing and ongoing maintenance. While the key to investing in property is buying well, further value can be added through successful management.
- **Higher yields.** The average rental yield for a median residential property in Sydney over the 12 months to September 2010¹ was 3.3% (and that's before any expenses were taken out). This compares with the income yield from REITs which was 5.7% over the same period.
- **No need to borrow.** With the Sydney moving annual median house price close to \$618,600², investing in residential property demands a significant capital investment and in most cases a large amount of debt. In comparison, the minimum capital investment required to gain exposure to the property market through REITs with Perpetual's WealthFocus platform is \$2,000 or \$1,000 with a savings plan.



¹ Source: UBS.

² Source: Real Estate Institute of Australia, September 2010.

- **No surprise bills.** With REITs there are no additional costs other than the initial investment. Water rates, council rates, strata fees, one-off special levies and property management fees are just a few of the bills that you might expect with a residential property.
- **No stamp duties.** When you buy a property, you incur a stamp duty that may run into several thousand dollars, depending on the sale price. In contrast, there is no stamp duty on buying shares in REITs. To give you an estimate, the stamp duty on a \$618,600 investment property in NSW is currently around \$23,000 (Source: Australian Property Investor).

Risks of investing in REITs

While it is not possible to identify every risk, some of the potential risks to consider include:

- loss of capital or not receiving income (investment risk)
- an event that has a negative effect on the price of all investments in the market (market risk)
- securities falling in value or not paying income (asset risk).

How to invest in REITs

One way to gain a desired level of diversification, as well as to build a portfolio of property securities, is through a property securities fund such as the **Perpetual Property Securities Fund** or the **Perpetual Property Income Fund**.

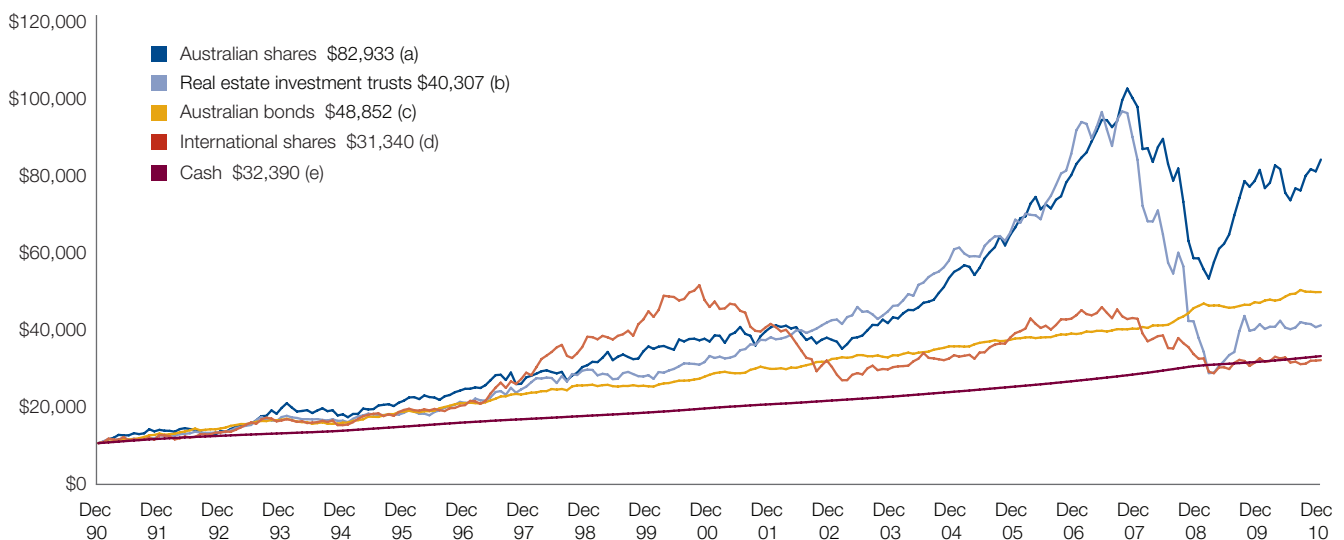
Property security funds invest in more than one REIT, providing greater diversification of assets as well as the comfort of knowing your money is being managed by professional investors.

Like investing in actively managed share funds, property security managers attempt to provide higher returns than the market, adjusted for risk and fees charged.

The Perpetual Property Securities Fund invests in property trusts (including REITs) and property-related companies that are managed by experienced property professionals with a proven ability to deliver results with their investment strategies. The Perpetual Property Income Fund invests in listed property securities and unlisted property funds.

Chart 1 – REITs are the third strongest performing asset class over the past 20 years

\$10,000 Invested on 31 December 1990



Source: Datastream. (a) As measured by the Blended All Ordinaries Index. Post 31/3/2000 S&P/ASX All Ordinaries Accumulation Index. Prior to 31/3/2000 ASX All Ordinaries Accumulation Index; (b) As measured by the Blended Property Trusts Accumulation Index. Post 30/6/2002 S&P/ASX 300 Property Trusts Accumulation Index. Between 1/4/2000 and 30/6/2002 it was the S&P/ASX 200 Property Accumulation Index. Prior to 1/4/2000 it was the ASX Property Trusts Accumulation Index; (c) UBSA Composite Bond Index; (d) MSCI World ex Australia Accumulation Index \$A; (e) UBSA Bank Bill Index. Past performance is not indicative of future performance. Total returns have been calculated assuming reinvestment of distributions. No allowance has been made for taxation.

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Further information

Adviser Services 1800 062 725

Investor Services 1800 022 033

Email investments@perpetual.com.au

www.perpetual.com.au