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REIT turn? What is the future for these investment opportunities?

When asked about the best time to buy real estate, property mogul Donald Trump once said, “Real estate is always good as far as I’m concerned.” And, at least until recently, he’s been right.



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But following years of strong performance, the real estate market now is in tatters, which raises an interesting question — should equity investors be buying real estate investment trusts (REITs), in anticipation of a recovery?

REITs are companies that buy, develop, manage and sell real estate. Some focus on particular property types, such as apartments, shopping malls or office buildings, while others own diversified portfolios. In exchange for preferential tax treatment, REITs distribute at least 90 percent of their taxable income to shareholders. As a result, they tend to blur the line between stocks and bonds, combining high-dividend yields with consistent capital appreciation.

During most of this decade, REITs were an outstanding investment. Indeed, spurred higher by declining interest rates, the collapse of the technology bubble and

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growing demand for higher-yielding investments, REITs — as measured by the Standard & Poor’s REIT Composite index — rose more than 314 percent from 2000 until 2007, for an average annual return of 22.52 percent.

But the good times ended in 2007 as concerns about residential housing and other issues snowballed into a full-blown debt-market crisis. As a result, the Standard & Poor’s REIT Composite index dropped nearly 17 percent last year. Moreover, many sub-sectors of the REIT market — including, not surprisingly, almost every housing-related REIT — collapsed.

But interestingly, through August, the average domestic REIT is up 0.82 percent as measured by the Standard & Poor’s REIT Composite index, which makes REITs one

of the best performing areas of the U.S. stock market through August. That's an impressive showing, considering the Standard & Poor's 500 index fell more than 11 percent through August.

Unfortunately for international investors, the same can't be said of foreign REITs. Many of these once high-flying REITs are still in decline. Indeed, REITs have plummeted more than 15 percent in the last 12 months in Singapore, and are down more than 45 percent in Australia. In Japan, J-REITs have tanked almost 30 percent in the last 12 months.

So, should cagey investors be looking to step back into REITs at this point? That's a difficult question, but consider that commercial real estate fundamentals are still in pretty good shape by historic standards, despite the current economic mess.

Further, at least through the first half of the year, occupancy rates remained in the low-to-mid-90-percent range across most property types, and there's been consistent rental rate growth in most regions of the country.

Moreover, many REITs are still cheap, with several trading at a discount to their net asset value of around 20 percent. Many of these same REITs were trading at a premium just two years ago.

Investors interested in REITs have a variety of options. Perhaps the easiest way to access REITs is through one of the many

specialized mutual funds focusing on the sector. Examples include the CGM Realty Fund (CGMRX), Cohen & Steers Realty Shares Fund (CSRSX), Third Avenue Real Estate Value Fund (TAREX) and T. Rowe Price Real Estate Fund (TRREX).

Alternatively, investors can purchase shares directly in one of the myriad publicly traded REITs, including Simon Properties Group (SPG), ProLogis (PLD), Vornado Realty Trust (VNO) and Boston Properties (BXP).

Finally, there are also a variety of exchange-traded and closed-end funds that offer exposure to REITs, both domestic and international. These include the Vanguard REIT ETF (VNQ), ING Clarion Global Real Estate Fund (IGR), iShares Dow Jones U.S. Real Estate Index Fund (IYR) and — for investors willing to walk on the wild side — the recently released Claymore/AlphaShares China Real Estate ETF (TAO).

REITs have been market stars since 2000, but nothing lasts forever. While opinions differ on whether REITs are still headed lower or simply experiencing a breather before resuming their upward march, for most investors they'll likely continue to be an important part of a diversified allocation strategy.

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