Investing in Real Estate:

More Than Just Bricks and Mortar

Astute investors understand that proper diversification involves holding a range of investments in *all* asset categories—stocks, bonds, real estate, and cash—not just those that happen to be in favor at a given moment. Yet, many people may shy away from investing in real estate due to a lack of knowledge or experience. If you haven't given much thought to how real estate can fit into your portfolio, here is a short course on some of the ways to invest in this sector:

o **Direct Ownership.** Many people already own real estate in the form of their homes, but they typically don't consider their personal residences as part of their asset allocation strategy. This is because many people buy their homes principally as places to live, rather than as investments. Nevertheless, a home typically represents one of the largest purchases most people will ever make and when they do sell, they hope they will be able to realize a profit. Consequently, although home ownership has *personal use* attributes (e.g., comfort, enjoyment) not usually associated with an investment, it also has investment attributes in that most people are careful to preserve and enhance its value.

Investing in real estate can also be accomplished by purchasing properties such as apartment buildings, rental homes, or office buildings. These investments generate rental income that can be partially sheltered through depreciation write-offs, and they also have the potential to be sold for profit. However, this type of investing can be time consuming. It requires knowledge of local residential and commercial markets, and may be more appropriate for those who desire to become landlords. One option is to turn over landlord responsibilities to a professional management company, but this transfer of responsibilities comes with a cost that will affect your bottom line.

o **Public and Private Limited Partnerships.** Commonly referred to as "passive activities," limited partnerships typically involve a number of limited partners investing in a property (or group of properties) managed by a general partner or sponsor, such as a brokerage firm. Although partnerships tend to be *illiquid* as short-term investments, under the right circumstance they may still be viable entities for investing in real estate.

o **REITs.** Real Estate Investment Trusts (REITs) pool investor money, much like a mutual fund, and use professional management to oversee a portfolio that may include properties (Equity REITs), mortgages (Mortgage REITs), or both (Hybrid REITs). REITs usually specialize in specific types of property, such as shopping centers, office buildings, and health care facilities. They may also specialize based on geographical location.

REITs offer investors a way to participate in the real estate market with greater *liquidity* than limited partnerships and with less personal involvement than direct ownership. They are easily traded on the major stock exchanges and the price generally fluctuates like a stock's, although for different reasons. Also, a large percentage of a REIT's taxable income must be paid out to shareholders. Investment return and principal value of REITs will fluctuate due to market conditions, so that shares, when redeemed, may be worth more or less than their original cost.

o Mutual Funds. Some mutual funds focus on real estate by investing in REITs and real estate-related industries, such as building supply companies and home furnishing manufacturers. Compared to REITs, which tend to be more narrowly focused by industry and region, real estate mutual funds tend to be more broadly diversified.

Expand Your Horizons

Real estate remains an important asset category, even if investors' attention is occasionally drawn elsewhere according to market swings. Perhaps it's time to reconsider the role real estate might play in *your* investment program, particularly if you are concerned about an allocation strategy that includes *all* asset classes. Bear in mind, past performance is never an indication of future results. In addition, be sure to read the prospectus before investing in any security or variable product.

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