Stocks Vs. Real Estate Investing And the Winner is…

By Mark Tiefel

Here's a fun exercise: type "Superman vs. Batman" into any search engine and you will discover the kinds of answers people routinely look for. Apparently, searchers like to ask which superhero is older, which is smarter, more popular, and all-around better. It's only funny because we humans make it a habit to compare things (and evidently, superheroes). We like to weigh one thing against another to see which comes out on top.

As an investor, you may not be comparing superheroes, but you certainly can compare investment strategies. If you wonder whether stocks are a better investment than commercial real estate or if commercial real estate provides a better ROI than stocks, you're not alone.

In an attempt to take the guesswork out of which investment is a better fit for you, we have gathered the research. Here is what we found:

Stocks

Pros:

- **Historically solid returns**. On January 1, 1986 the S&P 500 Index stood at $208. Thirty years later, on January 1, 2016, the index was $1,905, representing a 7.66% compounded rate of return.
- **Captures growth in economies around the globe**. By holding both U.S. and international stocks, you can benefit by what happens in both the U.S. and globally.
- **Provides a regular stream of income**. A great advantage of stocks is that some stocks pay dividends. For dividend paying stocks, even during "down" years investors know that – based on the history of that stock – dividends are coming.
- **Opportunity to diversify**. With stocks, you can spread out the risks, investing in everything from low-risk/low-reward stocks to high-risk/high-reward stocks. If some of those stocks happen to have a bad year, you don't have to worry because the others will lessen the blow.
- **Liquidity**. Simply put, it's easier and faster to sell stocks than it is to sell a commercial property.

Cons:

- **Market volatility**. Yes, the market did well for the majority of years between 1986-2016, but the bad years were quite difficult for many people.
- **Analyzing can be tough**. Picking just the right mix of stocks can be time-consuming and frustrating. After all, you don't know the future and the factors than can impact a stock's value.

- **Not knowing when to sell**. Just as you're never going to be 100 percent sure about which stocks are the best picks, you can never know with certainty when a stock is peaking and should be sold. In addition, you have to factor in paying capital gains tax and almost immediately focus on reinvesting proceeds to continue making money.

Commercial Real Estate

Pros:

- **Provides a steady income**. Investing in real estate offers endless options for fixed income. Each type of real estate, i.e. multifamily, office, industrial, etc. offers different types of risk, as well as, different rates of return. This allows an investor to balance the types of returns they are looking for with the level of risk they are willing to accept.
- **Non correlation to stock ownership**. Due to its low correlation to stocks, real estate can also protect your portfolio when the stock market is down.
- **Real estate capitalizes on a growing economy.** A strong economy (which is historically more common than not) can cause your commercial properties to appreciate quickly. In the long run, this appreciation can balance out any losses taken during tough times.
- **Allows for creative diversification**. The fact that there are so many different types of commercial real estate means that you can diversify your portfolio, further protecting you against economic downturns. Commercial real estate options include multifamily units, industrial properties, office buildings, and retail space.
- **Commercial real estate is tangible**. You know what you're getting when you buy real estate because you can see it and touch it. You don't have to visualize your investment because it's right in front of you.
- **Offers tax benefits**. According to the certified public accountants at Zinner & Co., owning real estate offers at least six important tax benefits. Here are three of them:

1. Tax laws allow you to claim depreciation on real property.
2. When you sell a property, 1031 Exchange allows you to defer profits as long as you buy another property of equal or greater value. In certain situations you can defer capital gains upon selling stocks and other appreciated assets by purchasing a new property in a designated "Opportunity Zone."
3. You can refinance one of your properties, do a "cash out refinance" and not be taxed on the equity until the property is sold.

Cons:

- **Lack of liquidity**. While stocks can be quickly turned to cash, it takes times to sell real estate. If you need money quickly, commercial real estate can be a frustrating investment to hold. Like any real estate, you never want to be in the position of selling a property for less than it's worth simply because you need the money.

- **Diversification can be an issue**. A number factors can reduce demand by tenants for your property. Maybe a large employer in the area decides to shutter their business. Or the neighborhood experiences an increase in crime. A recession will impact most businesses in some way, thus, reducing demand for space. The single egg in your basket would appear less valuable immediately.
- **Taking on too much property debt.** Placing too much debt on a property that either matures at the wrong time or becomes too expensive during an economic downturn.
- **Property Operating Risks.** Any tenant who fails to pay rent or destroys your property poses a risk to your investment. Also, you may encounter unforeseen expenses that eat away at profits.

Obviously, no one has a crystal ball and can determine with absolute certainty the success of any investment. What you ultimately decide to invest in depends, in part, on which set of pros and cons feels most comfortable. The best part of both investment vehicles? You don’t have to be Superman or Batman to make money.

Mark G. Tiefel is President of Capital Equity Group, Inc.,
a private real estate investment firm
specializing in the ownership of apartments.