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# REITs Revealed

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## Introduction

REITs Revealed is a practical guide to investing in publicly traded real estate investment trusts and real estate ETFs with discipline, clarity, and purpose. Real estate touches nearly every part of daily life—where we live, shop, store, heal, work, and connect—and listed REITs offer a transparent, liquid way to participate in that essential economy. Yet the public markets can turn durable, cash-generating properties into volatile tickers. Bridging that gap—between stable cash flows and shifting investor sentiment—is the core aim of this book.

We begin with fundamentals: how REITs earn money, why their accounting differs from traditional corporates, and which metrics actually matter. You will learn to read the income statement and cash flow statement through the lens of real estate, focusing on measures like net operating income, funds from operations, and adjusted funds from operations. From there, we move to the balance sheet—the foundation of every REIT—so you can judge leverage, liquidity, and the timing of debt maturities with a lender’s caution and an owner’s eye.

Dividends are the heartbeat of many REIT strategies, but not all payouts are created equal. This book shows you how to evaluate dividend coverage, capital allocation, and the trade-offs between growth and current income. We unpack lease structures—triple-net, gross, percentage rent, and escalators—because the fine print in a lease often explains why two seemingly similar REITs deliver very different results. By understanding the cash-flow engine room, you can distinguish between yield that is vulnerable and income that is built to endure.

Sector rotation is the second pillar of our approach. Property types respond differently to macro forces such as interest rates, employment, e-commerce penetration, demographics, and technological change. Industrial and data centers may thrive when logistics and connectivity lead demand; lodging may be more cyclical; healthcare and residential each have their own drivers and risks. We translate these patterns into a systematic rotation framework so you can tilt toward strength and away from deteriorating fundamentals, rather than reacting to headlines after the fact.

Tools matter, so we provide them. You’ll find screening templates that surface quality balance sheets, resilient cash flows, and attractive valuations across the REIT universe. We also cover real estate ETFs as flexible building blocks—useful for quick exposure, factor tilts, or implementing a sector view with less single-name risk. Whether your objective is steady income, long-term total return, or a blend of both, you will learn how to assemble portfolios, set guardrails, and calibrate position sizes to your goals and risk tolerance.

Finally, this is a book about behavior as much as it is about balance sheets. Real estate returns compound quietly; markets, however, can test conviction loudly. By anchoring decisions in fundamentals—lease terms, tenant quality, capital structure, and sustainable dividends—and by rotating thoughtfully across sectors, you can navigate cycles with more confidence and fewer surprises. REITs Revealed equips you to move from browsing tickers to owning businesses, from chasing yield to underwriting it, and from reacting to prices to anticipating cash flows.

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## CHAPTER ONE: Foundations: What REITs and Real Estate ETFs Are

Real estate is everywhere. It is the apartment you live in, the warehouse that stores the online order that arrives tomorrow, the hospital that treats your grandparents, the tower that beams your favorite podcast to your phone, and the shopping center where you buy dog food. It is also the invisible scaffolding behind the economy, providing the space that commerce needs to function and shelter that people require to thrive. For investors, accessing this sector used to mean scraping together a down payment, signing a mountain of mortgage paperwork, and dealing with leaky faucets at inconvenient hours. The public markets changed that.

Real estate investment trusts, or REITs, were created to let anyone own a slice of income-producing property through a brokerage account. They are companies that own, operate, or finance real estate, and they come with special tax rules that encourage them to pass most of their taxable income to shareholders as dividends. In exchange for that pass-through treatment, REITs must meet specific requirements set by regulators, including how they derive their income and how they distribute it. The result is an investment that behaves somewhere between a stock and a bond, with characteristics that are unique enough to warrant their own analysis toolkit.

A REIT's business model is straightforward on paper, though sometimes intricate in practice. It buys or builds properties that generate rent, it borrows money to amplify returns, and it collects the net cash to pay dividends and reinvest. Because most REITs are externally managed by a sponsor or internally managed by a team of real estate professionals, investors often talk about the "sponsor" or "management" as an important factor in capital allocation decisions. What distinguishes REITs from regular corporations is the distribution requirement and the nature of their income. You cannot simply sell widgets; you have to own or finance qualifying real estate and behave like a real estate company.

There are several flavors of REITs, and the differences are not just cosmetic. Equity REITs are the most common; they own and operate physical properties, from apartments to data centers. Mortgage REITs, or mREITs, lend against real estate or invest in mortgage-backed securities, generating income from interest rather than rent. Hybrid REITs do both. Within equity REITs, there is a distinction between "net lease" REITs, which often sign long-term triple-net leases where tenants pay taxes, insurance, and maintenance, and traditional operating REITs that handle more of the expenses themselves. The lease structure matters because it changes who bears the operational risks and how resilient the cash flows are.

REITs must also be structured as corporations, typically as a real estate investment trust under the relevant tax code, and they must meet several ongoing tests. They must derive at least three-quarters of their gross income from real estate-related sources, and they must pay out at least ninety percent of their taxable income to shareholders in the form of dividends. If they fail these tests, they risk losing their special tax status, which would be a very expensive mistake. In practice, you will often see REITs talk about “REIT taxable income,” which is a starting point for calculating distributions, and “FFO,” which we will explore in the next chapter as a better operational gauge than earnings per share.

To keep the tax advantage, many REITs elect to be taxed as a REIT at the corporate level and then pass the income through. That means shareholders generally owe tax on the dividends they receive, and some portion may be taxed at ordinary income rates rather than qualified dividend rates, depending on the REIT’s source of income. Some investors prefer to hold REITs in tax-advantaged accounts like IRAs to defer or avoid those taxes. While we will not dive deeply into tax strategy here, it is worth understanding that the REIT structure is designed to minimize corporate-level tax by distributing earnings, which can be attractive for income-focused portfolios but creates specific tax considerations.

On the public markets, REIT shares trade like stocks, with ticker symbols, bid-ask spreads, and daily prices set by supply and demand. That liquidity is a huge advantage over private real estate, where selling a property can take months and requires hefty transaction costs. However, the market price can diverge significantly from the underlying value of the assets, especially during periods of rising interest rates or macroeconomic stress. In those moments, a high-quality portfolio of properties might trade at a steep discount to its net asset value simply because sentiment turns negative, creating potential opportunities for investors who have done their homework.

This book’s focus is on publicly traded REITs, which are listed on major exchanges such as the New York Stock Exchange and Nasdaq. There are hundreds of them, covering every conceivable property type, and they are a major component of broader market indices like the MSCI US REIT Index. Many investors gain exposure through real estate ETFs, which are exchange-traded funds that hold baskets of REITs. ETFs can be broad, covering the entire sector, or targeted, focusing on specific subsectors like data centers, industrial properties, or net lease REITs. They offer instant diversification and simplicity, which can be appealing, but they also carry their own nuances in terms of holdings, weighting methodology, and expense ratios.

Real estate ETFs are not a single homogenous group. Some are market-cap weighted, meaning larger REITs have a bigger influence on performance. Others equal-weight the holdings or apply fundamental factors such as cash flow or dividends. There are

also specialized ETFs that hold only mortgage REITs or only specialty property types, each with a distinct risk profile. Understanding how an ETF is constructed is crucial because two funds with similar names can behave very differently. For example, a “residential” ETF might include apartments, manufactured housing, and single-family rentals, each with different sensitivities to employment and interest rates.

The listing of REITs also brings a level of transparency not always present in private markets. Public REITs file quarterly financial statements, issue supplemental packages with property-level detail, and hold earnings calls. They provide guidance, discuss capital recycling plans, and disclose leverage metrics and debt maturity ladders. This public information is a gift to the diligent investor, who can build models, compare companies, and track portfolio changes over time. However, the abundance of data also creates noise, and investors need to know which numbers matter more than others, which we will address throughout the book.

One distinctive feature of REIT investing is the prominence of dividends. Many REITs distribute a large share of their cash flow, and their dividend yields are often higher than those of typical stocks. That income can be attractive, but it is not automatically “safe.” A dividend is only as sustainable as the cash flow supporting it, and REITs can and do cut dividends when fundamentals deteriorate. Evaluating dividend safety involves looking at payout ratios relative to cash flow, the stability of the underlying leases, and the balance sheet’s ability to absorb shocks. Yield without coverage is a warning sign, not a gift.

The concept of net asset value, or NAV, is central to REIT analysis. NAV estimates the market value of a REIT’s properties minus its debt and other liabilities. Because REITs own identifiable assets, investors can estimate what the portfolio is worth and compare it to the company’s market capitalization. If a REIT trades at a significant discount to NAV, it might be undervalued; if it trades at a premium, it may be overvalued or have superior growth prospects. NAV is not static, as property values and interest rates change, so it requires regular updating. Think of NAV as a north star rather than a precise odometer.

Another tool that sets REIT analysis apart is the capitalization rate, or cap rate. This is a simple ratio of a property’s net operating income to its value, expressed as a percentage. Cap rates reflect the market’s required return on an unleveraged property and are influenced by interest rates, risk appetite, and the quality of the location and tenant. REITs often disclose acquisition cap rates and disposition cap rates, which help investors understand the pricing of their portfolio and the direction of yields in the market. Changes in cap rates can have large effects on valuations, especially when interest rates move.

Investors also need to grasp the difference between accounting earnings and the cash flows that support dividends. Traditional earnings per share can understate the true

cash-generating ability of a REIT because of depreciation and amortization, which are non-cash charges that reduce reported net income but not cash flow. That is why the industry uses metrics like funds from operations, or FFO, and adjusted funds from operations, or AFFO, which we will cover in detail in Chapter Two. These measures are closer to the real cash available to pay dividends and reinvest, and ignoring them can lead to mistaken conclusions about a REIT's profitability.

REITs can be growth engines as well as income generators. Some REITs are internally managed with a pipeline of development projects or an active "value-add" program that renovates properties to increase rents. Others are externally managed with incentives tied to asset growth, which can be both a blessing and a curse. Growth-oriented REITs may reinvest cash flows into new properties, but this requires disciplined capital allocation. Investors should be wary of deals that buy earnings per share at the expense of long-term value or that pile on leverage in pursuit of scale. The history of REITs includes episodes where growth was financed unsustainably, with painful consequences.

The balance sheet is the backbone of any REIT, and assessing it is non-negotiable. Leverage can enhance returns in good times but amplify losses during downturns. Investors should look at debt-to-EBITDA, interest coverage, and the maturity schedule to judge resilience. A REIT with long-dated, fixed-rate debt and ample liquidity can weather a rise in rates far better than one that relies on short-term floating-rate loans and has to refinance a large portion of its debt next year. Balance sheet analysis also involves understanding the cost of capital and how it affects both acquisition yields and development returns.

The lease is the engine room of a REIT's cash flow, and its structure is critical. Triple-net leases shift most operating costs to tenants, creating predictable cash flows but less inflation upside. Gross leases put the landlord on the hook for expenses, which can be a hedge against inflation but adds operational risk. Within retail, percentage rent clauses tie base rent to tenant sales, adding variable income. Escalators, whether fixed or tied to inflation indices, determine how rents increase over time. The length of the lease, the credit quality of the tenant, and the break and renewal options all influence the durability and growth of cash flow.

REITs are not immune to macro forces, and understanding their sensitivities is part of prudent analysis. Interest rates matter for both valuation and financing costs; when rates rise, the discount rate applied to future cash flows increases, which can compress prices. Rates also shape tenant demand, as higher borrowing costs can slow business investment and consumer spending, affecting retail and office demand. For residential REITs, higher mortgage rates can push people to rent, which can be a tailwind, but affordability constraints can cap rent growth. The interplay of rates, employment, inflation, and demographics drives sector cycles.

Regulation is another factor. Public REITs follow securities laws and disclosure requirements, and their governance structures typically include independent boards and shareholder protections. However, conflicts of interest can arise in externally managed REITs where the manager also owns or sponsors properties. Investors should review related-party transactions, management fees, and incentives to ensure alignment. Many REITs publish detailed governance policies and compensation frameworks; these are not just compliance documents. They tell you how the people making decisions get paid and whether they are rewarded for growing NAV or simply gathering assets under management.

Liquidity is a double-edged sword. Public listing makes it easy to buy and sell, but it also brings volatility. REITs often move with broader equity markets, even when their underlying property cash flows are stable. During periods of stress, such as the onset of the pandemic, prices can re-rate quickly as investors reassess occupancy, rent collection, and balance sheet risk. For long-term investors, this volatility can be an opportunity, provided they have the tools to separate market noise from fundamentals. Understanding the drivers of that volatility is key to staying disciplined when headlines are loud.

Global diversification is an option for investors comfortable with additional complexity. Many countries have their own REIT regimes, from Japan to Australia, the UK, Singapore, and Canada. International REITs can offer exposure to different economic cycles, currencies, and property types, such as logistics in Europe or retail in Asia. Currency risk is a central consideration because fluctuations in exchange rates can amplify or dampen returns. Investors should also be aware of differences in tax treatment and regulatory frameworks, which can affect both dividend yields and the ability to pass through income efficiently.

It is also worth noting that not all real estate exposure in the public markets is via REITs. Some investors use real estate ETFs that include REITs and other securities, or they might invest in closed-end funds or property-heavy operating companies. However, REITs remain the purest, most transparent way to access income-producing real estate with daily liquidity. They provide a standardized framework for analysis and a rich set of public data, which is why this book emphasizes them. Real estate ETFs are the delivery mechanism for many investors, and understanding the underlying REITs is the key to using these tools effectively.

REITs Revealed is organized to build your knowledge systematically. We will start with the financial toolkit that turns property economics into numbers you can analyze, then move to balance sheet health, dividend sustainability, and valuation. From there, we will delve into lease structures and sector dynamics, so you can understand the differences between residential, industrial, retail, office, data centers, self-storage, healthcare, lodging, and specialty properties. We will also tackle mortgage REITs and

global REITs. Finally, we will provide practical tools, including screening templates and portfolio construction guidance for both income-focused and growth-focused investors, as well as ETF implementation.

Before we dig into the details, it helps to frame the mindset we will use throughout the book. Real estate investing in public markets is less about chasing headlines and more about underwriting cash flows. Ask yourself: What drives this property type? Who is the tenant, and how strong is their business? How is the REIT financed, and when is its debt due? Are the dividends supported by real cash flow, and is there room to grow without straining the balance sheet? With these questions as anchors, you can navigate the sector with clarity rather than reacting to every blip in the market.

As you begin or refine your REIT journey, remember that the sector offers a spectrum of opportunities, from conservative net lease owners to high-growth development platforms to volatile lodging and mortgage REITs. There is no single “right” REIT for everyone; there is the right REIT for your goals, your time horizon, and your tolerance for risk. The following chapters will give you the context and tools to identify that match and to build portfolios that are robust across cycles. The foundation starts here, with an appreciation for the structure of REITs and the way real estate ETFs can help you implement your strategy efficiently.

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