id: 0
question:
Hui Lin, CFA is an investment manager looking to diversify his portfolio by adding equity real estate investments. Lin and his investment analyst, Maria Nowak, are discussing whether they should invest in publicly traded real estate investment trusts (REITs) or public real estate operating companies (REOCs). Nowak expresses a strong preference for investing in public REITs in taxable accounts. Lin schedules a meeting to discuss this matter, and for the meeting, Lin asks Nowak to gather data on three specific REITs and come prepared to explain her preference for public REITs over public REOCs. At the meeting, Lin asks Nowak: “Why do you prefer to invest in public REITs over public REOCs for taxable accounts?” Nowak provides Lin with an explanation for her preference of public REITs and provides Lin with data on the three REITs shown in Exhibits 1 and 2.The meeting concludes with Lin directing Nowak to identify the key investment characteristics along with the principal risks of each REIT and to investigate the valuation of the three REITs. Specifically, Lin asks Nowak to value each REIT using four different methodologies: Method 1Net asset value Method 2Discounted cash flow valuation using a two-step dividend model Method 3Relative valuation using property subsector average P/FFO multiple Method 4Relative valuation using property subsector average P/AFFO multiple
| Exhibit 1. Select REIT Financial Information |
| RE IT A | RE IT B | RE ITC |
| Health |
| Property subsector | Office | Storage | Care |
| Estimated 12 months cash net operating income | \$350， 000 | \$267， 000 | \$425， 000 |
| (NOI) |
Funds from operations(FFO)	\$316， 965	\$290， 612	\$368， 007
Cash and equivalents	\$308， 700	\$230， 850	\$341， 000
Accounts receivable	\$205， 800	\$282， 150	\$279， 000
Debt and other liabilities	\$2， 014， 000	\$2， 013， 500	\$2， 010， 000
Non-cash rents	\$25， 991	\$24， 702	\$29， 808
Rec un ng maintenance-type capital expenditures	\$63， 769	\$60， 852	\$80， 961
Shares outstanding	56， 100	67， 900	72， 300

| Exhibit 2.REIT Dividend Forecasts and Average Price Multiples |

Nowak’s most likely response to Lin’s question is that the type of real estate security she prefers:
A: offers a high degree of operating flexibility.
B: provides dividend income that is exempt from double taxation.
C: has below-average correlations with overall stock market returns.
D:
answer: B
explanation:
REITs are tax-advantaged entities whereas REOC securities are not typically tax-advantaged entities. More specifically, REITs are typically exempted from the double taxation of income that comes from taxes being due at the corporate level and again when dividends or distributions are made to shareholders in some jurisdictions such at the United States.