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Real estate investing for 2009: TICs, DSTs, private placement, REITs or oil & gas?

January 28, 2009 - Spotlights

The place to look for the best investment values in real estate today is in the institutional market. Some value-added and opportunistic real estate investments have tremendous potential today. Real estate with a market value over $10 million qualifies as institutional grade, and the bigger the better. This is the type of real estate sought by pension plans, state and federal governments, REITs, limited partnerships, etc. Foreign governments are big investors and consider U.S. real estate attractive because of the stability of the U.S. economy, just as foreign investors are attracted to U.S. govt. bonds. Although our economy is in a deep recession, we still are among the most secure economies in the world. Several REITs today feature properties with fixed, long term financing with investment-grade tenants. I call these Income Preferred REITS, as they provide solid dividends with a slow growth of principal. Growth is never guaranteed, but these REITS are structured to diminish principal risk while providing a secure income stream. These REITs have current dividends in the mid 6% range, and could be appripriate for seniors and other risk adverse investors.

Tenant-in-common owned real estate (TICs) are institutional quality buildings with professional management. TICs are custom made for those needing replacement property for 1031 exchanges. The investor can use a 1031 exchange to buy TIC investment property without paying taxes on the property they sold. The taxes due are tax-deferred as the basis is transferred to the replacement property. If the TIC owner dies, the heirs receive a step-up basis - paying reduced or no capital gains taxes if they sell. TICs are especially attractive when investors have enough money to purchase a diversified portfolio of TICs. But TICs usually have variable, short-term financing. In today's difficult financing world, you must inspect the financing arrangements very carefully. Make sure your TIC sponsor has publicly audited financials, and avoid those sponsors which do not reveal their finances. Obtaining 3rd party audited financials for every TIC sponsor under consideration is an important part of your due-diligence process.

I think that Delaware Statutory Trusts (DSTs) are a better alternative to TICs for 2009. DSTs also allow 1031 investors to purchase institutional quality real estate. Apartments and high credit quality, tenant, triple-net leased properties are popular DST property types. It's possible to purchase a diversified group of single-tenant, stand-alone retail buildings in a single DST. Financing options for DSTs are usually more attractive than financing options for TICs. DSTs feature fixed, long term debt which is critical in today's economy.

Wise investors "buy low & sell high" - for those interested in taking advantage of low real estate prices, this is the time to buy low. These buildings are in excellent locations, but have been mis-managed for a number of years. The partnership buys the building (usually at a bargain rate), fixes it up, with the intent to sell it within a short time at a considerable profit. Many of these real estate companies have previous offerings which have returned double digit returns to their investors.

If they can do that well in a booming real estate market where good prices were difficult to obtain - imagine what these highly skilled professionals can do now that they are in a buyer's market. These private placements are usually held for 2-5 years - and the potential can be exceptional. These buildings are not available for 1031 exchanges, however, as they are partnerships, which do not qualify for 1031 treatment.

Value added real estate is more geared to those who want income as well as growth opportunity. While opportunistic real estate involves major improvements to a building, value-add programs involve simpler fix-ups. Value-added real estate generally yields more income to investors, but with less capital gains than can be had with opportunistic real estate. Most anyone can invest in value-added properties through public securities markets, while opportunistic real estate investing is almost always limited to accredited investors through private placements.

Another real estate investment attractive today is oil & gas private placements. Either drilling programs, working interests, or royalty programs offer unique tax advantages for investors while predicting double-digit returns. Oil & gas programs have come along way within the last few years - the industry has done a fantastic job reducing risk. Oil & gas programs are available for 1031 exchanges or as direct investments.

Thus, for those looking for 1031 replacement property DSTs are the preferred choices. For those investors looking for excellent returns and don't need a 1031 exchange, real estate private placements are very appealing, as are income-preferred REITs. Oil & gas investing can offer large write-offs from adjusted gross income with outstanding income potential. Investing in real estate and oil and gas contain risk and are illiquid assets. Investors must be aware that it is possible to lose money with these investments.

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