Time Equities Securities LLC

How Diversified Real Estate Can Provide Value and Income to Wealth Advisers

Is the COVID-19 crisis providing opportunity in real estate?

Assumptions about how Americans will live in the future have been suddenly called into question by the coronavirus pandemic. The crisis has interrupted long-standing demographic and business trends, while altering projections about the future of urban development and travel. Some of these changes are completely new, while others represent an acceleration of long-term trends under way in response to factors like climate change or evolving technologies.

"Buying right is hugely important and cannot be stressed too much. It is hard enough to make a well-bought deal work, but when you overpay for a property, the conclusion is inevitable."

– Francis Greenburger, Time Equities CEO

Investors seeking to achieve diversification and enhance portfolio income can find opportunities in real estate as an asset class. Long-term market returns prove that opportunistic buying is a cornerstone for successful real estate investment strategies over long periods of time.

The pandemic has created the potential for allocating to real properties at attractive valuations due to market disruptions, but careful consideration of risk factors is crucial. For wealth managers, the challenge is not only determining whether this crisis represents a buying opportunity but also how best to navigate risk, going forward, in a potentially volatile market environment through an economic recovery cycle full of unknowns.

Thinking Beyond 60/40: Wealth Managers Access Real Estate

Historically, wealth managers often segregated directly held real estate from other, more liquid assets. This was due, in part, to a lack of access to reliable deal flow, which complicated allocation decisions, as well as the concentration of assets. With increased access to diversified portfolios of properties over recent decades, however, multi-family offices and private banks have increasingly mirrored the approach taken by pensions and endowments, and allocated to real estate actively based on volatility and return assumptions.

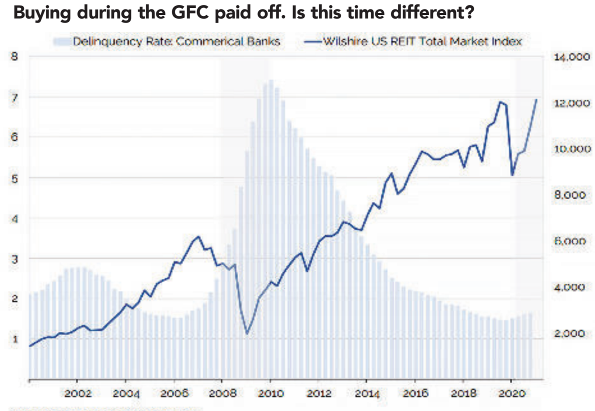
Based on long-term data analysis, direct real estate as an asset class appears attractive to investors with access. Prior to the pandemic, NEPC published 5- to 7-year return expectations of 6 percent for core real estate holdings, with anticipated volatility of 13 percent, roughly matching expectations for large-cap U.S. equities, with a substantially lower volatility profile. As of year-end 2019, NEPC identified core real estate as one of the top five asset classes on a Sharpe ratio basis, rated higher than any public U.S. equity or debt segment, including public and private REITs.

Road to Recovery or Ruin?

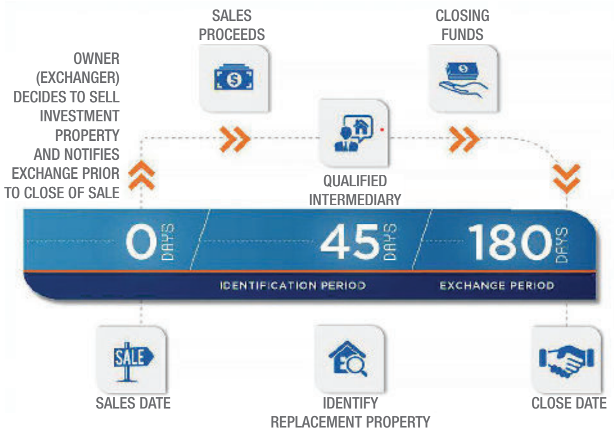
The impact of the COVID-19 virus on the global economy has been profound. Real estate markets felt the impact directly, as government-mandated lockdowns and social distancing left offices, retail stores and hotels vacant. Market intervention by the Federal Reserve and other global central banks subsequently lowered borrowing costs dramatically while increasing liquidity in credit markets.

The RCA U.S. All-Property Commercial Real Estate Index increased by 4.9 percent year-over-year in May 2020, the lowest rate of growth since 2011, with significant weakness in office and retail properties offset by resilience in single-family and multifamily units. Transaction volumes — historically viewed as a leading indicator for commercial valuations — contracted by 79 percent year-over-year for May, while the aggregate cap-rate spread to Treasuries expanded to 87 basis points, slightly above historical averages. Critically, as commercial properties languished, residential real estate prices have begun to exhibit early signs of a strong rebound, helped by historically low mortgage rates. The NAR index of pending home sales increased 44.3 percent on a monthly basis, after falling to multidecade lows in April. Economists have debated whether this spike in home buying is sustainable or only represents a rebound driven by pent-up demand that will falter without further stimulus.

Buying during the GFC paid off. Is this time different?



1031 exchanges can defer taxes on investment properties



As elected officials and corporate leaders consider the arguments for a V-, U-, K- or L-shaped recovery path for the U.S. economy, the ongoing turmoil may present outsized opportunities and risks for real estate investors. It is important to consider that the shape of recovery from the pandemic may be different in nature from prior rebounds.

A Unique Inflection Point

During the credit crisis of 2007 and 2008, a sudden contraction of credit, combined with a global recession, depressed property values, creating buying opportunities for investors, who were richly rewarded when central-bank liquidity measures reflated prices. The market set-up facing real estate investors today sees similarly accommodative rate and liquidity policies, which are augmented by massive cash reserves held by both institutional and individual investors.

The nature of the COVID pandemic, however, suggests that this recovery will be quite different from the last and that any economic rebound will be accompanied by lasting changes in consumer behavior and consumption patterns. As such, investors who buy assets at distressed prices without considering how these changes will impact future returns run the risk of falling into a value trap by confusing permanent changes in the way people live for cyclical trends.

In a distressed environment, investors who wish to capture value must factor in the risks of ownership, rather than just buying because properties appear "cheap" when they cost less today than they did the day before.

In addition to risk management through diversification and high underwriting standards, understanding how market and business cycles will impact cash flows from ownership is critical.

Factoring Taxes

Along with investment opportunities for fresh capital, the current market shakeup may also cause wealth managers to consider the timing of asset sales, as evolving economic assumptions impact property demand. For property owners with concentrated economic risk, the opportunity to diversify with enhanced tax efficiency may also be attractive.

Section 1031 allows a taxpayer to sell a qualified property and use the sale proceeds to purchase a new qualified property while deferring payment of taxes on their profits. A 1031 transaction is sometimes referred to as a "like-kind exchange," meaning that the taxpayer has exchanged one investment property for another rather than taking their profits in cash and realizing a taxable event immediately. To receive this tax treatment, the exchange investment must be completed within a 45-day window, while the closing must occur within 180 calendar days.

With careful planning, an investor can achieve 1031 tax efficiency while exchanging the proceeds from the sale of a highly appreciated real estate asset for a property that meets its risk and income needs. In some cases, investors may be able to achieve diversified exposure to multiple geographies and property-use types.

The Time Equities Edge

With a real estate investing track record that exceeds 50 years, Time Equities has the depth of experience to manage risk across constantly changing economic cycles. With a proven decision-making process focused on long-term ownership and opportunistic buying, TEI is a singular partner for wealth managers who want to provide their clients with direct access to a diversified portfolio of high-quality real estate assets.

TIME EQUITIES INC.

Time Equities has acquired a diverse real estate portfolio with guiding principles that have remained the same for decades: a dedication to long-term ownership and opportunistic buying. TEI's keen focus is to maximize returns to investors and deliver excellent service to clients and tenants. Since 1966, TEI has expanded into multiple markets, both large and small, leveraging its portfolio into diverse asset classes both nationally and internationally. Along the way, TEI has built an equity base by co-investing with individual investors, institutions and a growing network of strategic partners, as well as offering private placement funds and custom 1031 exchange opportunities through Time Equities Securities, LLC, member FINRA, its wholly owned Broker-Dealer.

CORPORATE CONTACT

Alexander Anderson | Director, Time Equities Inc
55 Fifth Avenue | 15th Floor | New York, NY 10003
O: (212) 206-6176 | M: (717) 940-3667 | aanderson@timeequities.com | www.timeequities.com

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