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# CAPITAL 1031 EXCHANGE COMPANY, LLC

Tax Deferred Exchange Company

EMAIL NEWSLETTER

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## The drop in the market over 2006 and 2007 has created some uncertainty for investors.

- Sub-prime lenders are closing their doors in the midst of regulatory "cease and desist" orders, and there are a rising number of loan defaults;
- Foreclosures are on the rise;
- Homeowners are calling on Congress for aid in making loan payments;
- National Builders are reporting huge reductions in revenues. D.R. Horton reported revenues down 50% in the last quarter of 2006. Toll Brothers and Lennar are experiencing similar declines;
- The local and national press is simply overrun with news of falling home prices, construction declines and defaulting loans.

Most real estate investors knew that this was coming. Prices could not continue to rise, and builders could not sustain the frenzied pace of development. Investors spent the last three years hearing nothing but the debate on whether there was a "bubble" in the real estate sector. Of course, some areas have suffered more than others. Florida, the Carolinas, and the New Jersey shore are currently experiencing significant "inventory", and a recent ULI report stated that there are over 2,000 new condominium units available in the city of Philadelphia.

### *Yet all is not bleak for investors.*

Mortgage rates remain largely unchanged despite news of a shake-out in the sub-prime industry. Money Magazine reports: "The 30-year fixed rate averaged 6.14 percent...A year ago, the 30-year stood at 6.34 percent." Property values have fallen significantly. And the new real estate catch phrase is "inventory." Some areas are better situated than others. Ed Fitzgerald, an investor and realtor in Atlantic City, N.J. reports that although prices have adjusted down the shore, there is growing activity in AC. Another investor, Ronald Gold, of Miami, Florida remarks that the real estate market is driven by market psychology. "Many buyers love to buy during the upswing, but get cold feet in a down market. It is difficult for most investors to act contrary to the overall market."



*What does this mean to investors who need to do a 1031 exchange in order to avoid a large tax hit? It means several things:*

1. **Selling:** It has been harder to sell properties in the last year. Sellers have to get realistic about pricing and realize that we are no longer in an escalating market. In 2006 we saw a record number of reverse exchanges (ie. the replacement property is purchased before the sale of the relinquished property.) Why did this happen? Our clients had found good deals on replacement properties, but had not sold their relinquished property. The number of reverse exchanges performed in 2006 by our company was double that of 2005. Many of those investors were able to complete the reverse

exchanges, because they dropped the prices on their properties and got them sold within the 180 exchange period. Our attorneys worked tirelessly last year to service our clients with the more labor intensive reverse exchanges. We expect to see more of them in 2007, as we remain in a buyer's market.

- 2. Location:** During the rising market there were frequent complaints by our investors about finding a replacement property that was not overpriced. Our mantra has always been to look for the right location to buy the replacement property and be a value investor. While this is no easy task, a similar concept holds true in a market that is adjusting downward. We have had over a decade of year over year appreciation. Even if your investment property has decreased in value recently, you probably still have significant capital gains if you held it long enough. So the question for any investor contemplating an exchange is whether there are replacement properties that might have the potential to appreciate faster than the property they currently hold. One of our contacts, Joseph Marley, of Visionary Real Estate, is investing in Panama City, Florida. He feels that the area has huge potential for appreciation in the next decade. He has shifted inventory from the New Jersey shore to the Florida panhandle. We have other investors that have found more solid income producing properties. A down market can be a great time to upgrade your investment property.
- 3. Patience:** Since we are in a buyer's market, waiting until your property is under contract might be prudent before you enter into a replacement property contract. Or buying with a sale contingency would also be prudent. The bottom line is there are many more good values than a year ago.

*Once again, thank you for your continued business and support.*

The Capital 1031 Team

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