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Maximizing 1031 Exchanges: Exploring top-tier QSR brands in the franchise real estate market - by Ridder and Schonfeld

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Maximizing your 1031 Exchange: Exploring top-tier QSR brands in the franchise real estate market

Real estate investors, developers, and REITs are very familiar with the tax-deferred advantages of a 1031 Exchange. However, you may not have considered how the strategy could be beneficial in other ways including, diversifying, moving markets, and increasing income.

If you are contemplating a 1031 Exchange, or have recently transacted a deal, making the next investment step could seem daunting. After all, the real estate market is in a state of perpetual, cyclical motion, with unique opportunities arising every day. The reality is that these opportunities are created by others with similar objectives – sell to acquire.

Quick service could mean a long-lasting investment

As with most investments, the objective is to have a sustained, consistent return over time, preferably, a long time. With nearly 200,000 quick service restaurant (QSR) franchise locations in the U.S.* and increasing each year, the segment is particularly appealing. No business is completely recession proof, but quick service restaurants have a lower average check, greater convenience, and increased food choices that resonate well with financially stressed consumers.

Growing franchisees who own real estate will often find themselves in the predicament of wanting to expand locations, but not having the capital to do so. Among the possibilities to gain liquidity, they will pursue a sale/lease back. In this circumstance, the franchisee (the seller) upon sale of the property, becomes a tenant of the buyer. Clearly, the benefit to the franchisee is the immediate profit from the sale. The buyer (investor), however, acquired a 20-year cash flow stream that typically has extension options and escalations available.

Landowners are only as successful as their tenants, so how can you determine which is the best investment for you?

It goes without saying, location comes first. Ensure the real estate is well positioned in an area that promotes customer traffic and is in an area poised for development. Look for a franchise that is part of a mature brand. Choose a sizable franchise. Larger franchises are typically more appealing.

Confirm that the franchisees location has positive year-over-year results.

The value of choosing the right franchise tenant could result in as much as 20 years of perpetual lease income. With cap rates presently stable in the mid 5s to low 6s, the initial investment poses nominal risk.

Whether you are a novice or an expert dealing in franchise real estate, you can benefit from M&T Bank's more than 30 years of franchise experience. The M&T Franchise Team specializes in providing research on potential franchise tenant brands, as well as operating company and property company financing to franchisees.

*Statista, number of quick service restaurants in the U.S., www.statista.com/statistics

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