

AGREE REALTY CORP  
Form 10-Q  
May 09, 2007

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q**

**Mark One**

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended March 31, 2007**

**OR**

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 1-12928  
Agree Realty Corporation**

(Exact name of registrant as specified in its charter)

**Maryland**  
(State or other jurisdiction  
of incorporation or organization)

**38-3148187**  
(I.R.S. Employer  
Identification No.)

**31850 Northwestern Highway, Farmington Hills,  
Michigan**

**48334**

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, included area code: (248) 737-4190

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act).

Yes  No

As of May 9, 2007, the Registrant had 7,750,496 shares of common stock, \$0.0001 par value, outstanding.

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Consolidated Balance Sheets (Unaudited)**

|   | <i>March 31,<br/>2007</i> | <i>December 31,<br/>2006</i> |
|---|---------------------------|------------------------------|
| <b>Assets</b>   |                           |                              |
| <b>Real Estate Investments</b>  |                           |                              |
| Land  | <b>\$ 78,611,458</b>      | \$ 77,536,458                |
| Buildings   | <b>189,192,954</b>        | 189,117,421                  |
| Property under development  | <b>3,159,751</b>          | 1,593,828                    |
|   | <b>270,964,163</b>        | 268,247,707                  |
| Less accumulated depreciation   | <b>(49,558,930)</b>       | (48,352,753)                 |
| <b>Net real estate investments</b>  | <b>221,405,233</b>        | 219,894,954                  |
| <b>Cash and Cash Equivalents</b>  | <b>168,312</b>            | 463,730                      |
| <b>Accounts Receivable – Tenants</b> , net of allowance of \$20,000 for possible losses at March 31, 2007 and December 31, 2006 | <b>377,736</b>            | 732,141                      |
| <b>Unamortized Deferred Expenses</b>  |                           |                              |
| Financing costs, net of accumulated amortization of \$4,528,272 and \$4,482,272 at March 31, 2007 and December 31, 2006         | <b>973,905</b>            | 1,019,905                    |
| Leasing costs, net of accumulated amortization of \$678,061 and \$665,811 at March 31, 2007 and December 31, 2006               | <b>417,695</b>            | 421,229                      |
| <b>Other Assets</b>   | <b>1,252,258</b>          | 982,640                      |
|   | <b>\$ 224,595,139</b>     | \$ 223,514,599               |

*See accompanying notes to consolidated financial statements.*

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**Agree Realty Corporation**  
**Consolidated Balance Sheets (Unaudited)**

|   | <i>March 31,</i><br><b>2007</b> | <i>December 31,</i><br>2006 |
|---|---------------------------------|-----------------------------|
| <b>Liabilities and Stockholders Equity</b>  |                                 |                             |
| <b>Mortgages Payable</b>  | <b>\$ 47,720,435</b>            | \$ 48,291,247               |
| <b>Notes Payable</b>  | <b>23,075,000</b>               | 20,500,000                  |
| <b>Dividends and Distributions Payable</b>  | <b>4,107,512</b>                | 4,111,807                   |
| <b>Deferred Revenue</b>   | <b>11,931,567</b>               | 12,103,954                  |
| <b>Accrued Interest Payable</b>   | <b>301,741</b>                  | 239,318                     |
| <b>Accounts Payable</b>   |                                 |                             |
| Capital expenditures  | <b>370,310</b>                  | 766,378                     |
| Operating   | <b>691,801</b>                  | 1,140,617                   |
| <b>Tenant Deposits</b>  | <b>64,085</b>                   | 64,085                      |
| <b>Total Liabilities</b>  | <b>88,262,451</b>               | 87,217,406                  |
| <b>Minority Interest</b>  | <b>5,862,042</b>                | 5,878,593                   |
| <b>Stockholders Equity</b>  |                                 |                             |
| Common stock, \$0.0001 par value; 20,000,000 shares authorized, 7,750,496 shares issued and outstanding | <b>775</b>                      | 775                         |
| Additional paid-in capital  | <b>141,521,493</b>              | 141,276,763                 |
| Deficit   | <b>(11,051,622)</b>             | (10,858,938)                |
| <b>Total Stockholders Equity</b>  | <b>130,470,646</b>              | 130,418,600                 |
|   | <b>\$ 224,595,139</b>           | \$ 223,514,599              |

*See accompanying notes to consolidated financial statements.*

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**Agree Realty Corporation**  
**Consolidated Statements of Income (Unaudited)**

|   | <i>Three Months<br/>Ended<br/>March 31, 2007</i> | <i>Three Months<br/>Ended<br/>March 31, 2006</i> |
|---|--|--|
| <b>Revenues</b>   |  |  |
| Minimum rents   | \$ 7,687,360                                     | \$ 7,532,443                                     |
| Percentage rents  | 13,679   | 14,071   |
| Operating cost reimbursements                                     | 756,350  | 711,625  |
| Other income  | 6,103  | 14,359   |
| <b>Total Revenues</b>   | <b>8,463,492</b>                                 | <b>8,272,498</b>                                 |
| <b>Operating Expenses</b>   |  |  |
| Real estate taxes   | 457,361  | 440,276  |
| Property operating expenses                                       | 510,447  | 547,128  |
| Land lease payments   | 170,050  | 195,465  |
| General and administrative  | 996,263  | 1,050,957  |
| Depreciation and amortization                                     | 1,234,186  | 1,202,313  |
| <b>Total Operating Expenses</b>                                   | <b>3,368,307</b>                                 | <b>3,436,139</b>                                 |
| <b>Income From Continuing Operations</b>                          | <b>5,095,185</b>                                 | <b>4,836,359</b>                                 |
| <b>Other (Expense)</b>  |  |  |
| Interest expense, net   | (1,176,639)                                      | (1,153,567)                                      |
| <b>Income Before Minority Interest</b>                            | <b>3,918,546</b>                                 | <b>3,682,792</b>                                 |
| <b>Minority Interest</b>  | <b>(313,487)</b>                                 | <b>(296,098)</b>                                 |
| <b>Net Income</b>   | <b>\$ 3,605,059</b>                              | <b>\$ 3,386,694</b>                              |
| <b>Earnings per Share Basic</b>                                   | <b>\$ 0.47</b>                                   | <b>\$ 0.45</b>                                   |
| <b>Earnings Per Share Dilutive</b>                                | <b>\$ 0.47</b>                                   | <b>\$ 0.45</b>                                   |
| <b>Weighted Average Number of Common Shares Outstanding Basic</b> | <b>7,643,026</b>                                 | <b>7,605,496</b>                                 |

**Weighted Average Number of Common Shares Outstanding**  
**Dilutive**

**7,685,616**

**7,652,469**

*See accompanying notes to consolidated financial statements.*

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**Agree Realty Corporation**  
**Consolidated Statement of Stockholders Equity (Unaudited)**

|   | <i>Common Stock</i> |               | <i>Additional</i> |                 |
|---|---------------------|---------------|-------------------|-----------------|
|   | <i>Shares</i>       | <i>Amount</i> | <i>Paid-In</i>    | <i>Deficit</i>  |
|   |                     |               | <i>Capital</i>    |                 |
| <b>Balance, January 1, 2007</b>                                     | 7,750,496           | \$ 775        | \$ 141,276,763    | \$ (10,858,938) |
| Vesting of restricted stock   |                     |               | 244,730           |                 |
| Dividends declared for the period January 1, 2007 to March 31, 2007 |                     |               |                   | (3,797,743)     |
| Net income for the period January 1, 2007 to March 31, 2007         |                     |               |                   | 3,605,059       |
| <b>Balance, March 31, 2007</b>                                      | 7,750,496           | \$ 775        | \$ 141,521,493    | \$ (11,051,622) |

*See accompanying notes to consolidated financial statements.*

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**Agree Realty Corporation**  
**Consolidated Statement of Cash Flows (Unaudited)**

|   | <i>Three Months<br/>Ended<br/>March 31, 2007</i> | <i>Three Months<br/>Ended<br/>March 31, 2006</i> |
|---|--|--|
| <b>Cash Flows From Operating Activities</b>   |  |  |
| Net income  | \$ 3,605,059                                     | \$ 3,386,694                                     |
| Adjustments to reconcile net income to net cash provided by operating activities                                  |  |  |
| Depreciation  | 1,220,048  | 1,190,712  |
| Amortization  | 60,138   | 42,601   |
| Stock-based compensation  | 244,730  | 202,000  |
| Minority interests  | 313,487  | 296,098  |
| Decrease in accounts receivable   | 354,405  | 281,457  |
| (Decrease) increase in other assets   | (285,377)  | 35,159   |
| Decrease in accounts payable  | (448,816)  | (573,253)  |
| Decrease in deferred revenue  | (172,387)  | (172,387)  |
| Increase (decrease) in accrued interest   | 62,423   | (12,020)   |
| Decrease in tenant deposits   |  | (905)  |
| <b>Net Cash Provided By Operating Activities</b>  | <b>4,953,710</b>                                 | <b>4,676,156</b>                                 |
| <b>Cash Flows From Investing Activities</b>   |  |  |
| Acquisition of real estate investments (including capitalized interest of \$105,000 in 2007 and \$23,000 in 2006) | (2,346,146)                                      | (34,093)   |
| <b>Net Cash Used In Investing Activities</b>  | <b>(2,346,146)</b>                               | <b>(34,093)</b>                                  |
| <b>Cash Flows From Financing Activities</b>   |  |  |
| Payments of mortgages payable   | (570,812)  | (592,728)  |
| Dividends and limited partners' distributions paid  | (4,132,076)                                      | (4,102,505)                                      |
| Line-of-credit net borrowings (payments)  | 2,575,000  | (5,300,000)                                      |
| Repayments of capital expenditure payables  | (766,378)  | (112,687)  |
| Payment of leasing costs  | (8,716)  | (10,283)   |
| <b>Net Cash Used In Financing Activities</b>  | <b>(2,902,982)</b>                               | <b>(10,118,203)</b>                              |
| <b>Net Decrease In Cash and Cash Equivalents</b>  | <b>(295,418)</b>                                 | <b>(5,476,140)</b>                               |
| <b>Cash and Cash Equivalents, beginning of period</b>   | <b>463,730</b>                                   | <b>5,714,540</b>                                 |

|  |    |                |    |                |
|--|----|----------------|----|----------------|
| <b>Cash and Cash Equivalents</b> , end of period | \$ | <b>168,312</b> | \$ | <b>238,400</b> |
|--|----|----------------|----|----------------|

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**Agree Realty Corporation**  
**Consolidated Statement of Cash Flows (Unaudited)**

|  | <i>Three Months<br/>Ended<br/>March 31, 2007</i> | <i>Three Months<br/>Ended<br/>March 31, 2006</i> |
|--|--|--|
| <b>Supplemental Disclosure of Cash flow Information</b>          |  |  |
| Cash paid for interest (net of amounts capitalized)              | \$ 1,068,216                                     | \$ 1,134,682                                     |
| <b>Supplemental Disclosure of Non-Cash Transactions</b>          |  |  |
| Dividends and limited partners distributions declared and unpaid | \$ 4,107,512                                     | \$ 4,093,131                                     |
| Real estate investments financed with accounts payable           | \$ 370,310                                       | \$ 120,187                                       |

*See accompanying notes to consolidated financial statements.*

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**Agree Realty Corporation**  
**Notes to Consolidated Financial Statements**

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements for the three months ended March 31, 2007 and 2006 have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for audited financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The consolidated balance sheet at December 31, 2006 has been derived from the audited consolidated financial statements at that date. Operating results for the three months ended March 31, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007, or for any other interim period. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2006.

**2. Stock Based Compensation**

On January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (R), Share-Based Payments (SFAS 123R), under the modified prospective method. Under the modified prospective method, compensation cost is recognized for all awards granted after the adoption of this standard and for the unvested portion of previously granted awards that are outstanding as of that date. In accordance with SFAS 123R, we estimate the fair value of restricted stock and stock option grants at the date of grant and amortize those amounts into expense on a straight line basis or amount vested, if greater, over the appropriate vesting period. As of March 31, 2007, there was \$3,023,315 of total unrecognized compensation costs related to the outstanding restricted shares, which is expected to be recognized over a weighted average period of 3.84 years. We used a 0% discount factor and forfeiture rate for determining the fair value of restricted stock. The forfeiture rate was based on historical results and trends and we do not consider discount rates to be material. The holder of a restricted share award is generally entitled at all times on and after the date of issuance of the restricted shares to exercise the rights of a shareholder of the Company, including the right to vote the shares and the right to receive dividends on the shares.

**Table of Contents****Agree Realty Corporation  
Notes to Financial Statements****2. Stock Based Compensation (continued)**

|   | Shares<br>Outstanding | Weighted<br>Average<br>Grant Date<br>Fair Value |
|---|-----------------------|---|
| Unvested restricted shares at December 31, 2006 | 131,120               | \$29.42   |
| Restricted shares granted                       |                       |   |
| Restricted shares vested                        | (23,650)              | 24.51   |
| Restricted shares forfeited                     |                       |   |
| Unvested restricted shares at March 31, 2007    | 107,470               | 30.50   |

**3. Earnings Per Share**

Earnings per share has been computed by dividing the net income by the weighted average number of common shares outstanding. The per share amounts reflected in the consolidated statements of income are presented in accordance with SFAS No. 128 Earnings per Share .

The following is a reconciliation of the denominator of the basic net earnings per common share computation to the denominator of the diluted net earnings per common share computation for each of the periods presented:

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2007</b>                         | <b>2006</b> |
| Weighted average number of common shares outstanding                                    | 7,750,496                           | 7,706,846   |
| Unvested restricted stock   | (107,470)                           | (101,350)   |
| Weighted average number of common shares outstanding used in basic earnings per share   | 7,643,026                           | 7,605,496   |
| Weighted average number of common shares outstanding used in basic earnings per share   | 7,643,026                           | 7,605,496   |
| Effect of dilutive securities:  |                                     |             |
| Restricted stock  | 42,590                              | 45,178      |
| Common stock options  |                                     | 1,795       |
| Weighted average number of common shares outstanding used in diluted earnings per share | 7,685,616                           | 7,652,469   |

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**Agree Realty Corporation  
Part I**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

***Forward-Looking Statements***

Management has included herein certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended. These forward-looking statements represent our expectations, plans and beliefs concerning future events and may be identified by terminology such as anticipate, estimate, should, expect, believe, intend and similar expressions. Although the forward-looking statements made in this report are based on good faith beliefs, reasonable assumptions and our best judgment reflecting current information, certain factors could cause actual results to differ materially from such forward looking statements, including but not limited to; the effect of economic and market conditions; risks that our acquisition and development projects will fail to perform as expected; financing risks, such as the inability to obtain debt or equity financing on favorable terms; the level and volatility of interest rates; loss or bankruptcy of one or more of our major retail tenants; a failure of our properties to generate additional income to offset increases in operating expenses; and other factors discussed elsewhere in this report and our other filings with the Securities and Exchange Commission, including our Form 10-K for the fiscal year ended December 31, 2006. Given these uncertainties, you should not place undue reliance on our forward-looking statements. Except as required by law, we assume no obligation to update these forward looking statements, even if new information becomes available in the future.

***Overview***

We were established to continue to operate and expand the retail property business of our predecessor. We commenced operations in April 1994. Our assets are held by, and all operations are conducted through, Agree Limited Partnership (the Operating Partnership), of which Agree Realty Corporation is the sole general partner and held a 92% interest as of March 31, 2007. We are operating so as to qualify as a real estate investment trust (REIT) for federal income tax purposes.

The following should be read in conjunction with the Consolidated Financial Statements of Agree Realty Corporation, including the respective notes thereto, which are included in this Form 10-Q.

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Part I*****Recent Accounting Pronouncements***

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48),

Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, Accounting for Income Taxes. This interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company adopted this statement in the first quarter of 2007. The impact of adopting FIN 48 did not have any impact on our financial position or results of operations.

In September 2006, FASB issued SFAS No. 157, Fair Value Measurements ( SFAS No. 157 ). This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands the disclosures about fair value measurements. SFAS No. 157 applies to other accounting pronouncements that require or permit fair value measurements. The changes to current practice resulting from the application of SFAS No. 157 relate to the definition of fair value, the methods used to measure fair value and the expanded disclosure about fair value measurements. The definition focuses on the price that would be received to sell the asset or paid to transfer the liability at the measurement date (an exit price) and not the price that would be paid to acquire the asset or received to assume the liability at the measurement date (an entry price). This statement also emphasizes that fair value is a market-based measurement, not an entity specific measurement, and subsequently a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. The statement also clarifies the market participant assumptions about risk and assumption about the effect of a restriction on the sale or use of an asset. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods with those fiscal years. This statement should be applied prospectively as of the beginning of the year in which this statement is initially applied. A limited form of retrospective application of SFAS No. 157 is allowed for certain financial instruments. We are currently evaluating the provisions of SFAS No. 157 to determine the potential impact, if any, the adoption of SFAS No. 157 will have on our financial position or results of operations.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities ( SFAS No. 159 ). This statement permits companies and not-for-profit organizations to make a one-time election to carry eligible types of financial assets and liabilities at fair value, even if fair value measurement is not required under GAAP. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the provisions of SFAS No. 159 to determine the potential impact, if any, the adoption of SFAS No. 159 will have on our financial position or results of operations.

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**Agree Realty Corporation  
Part I**

***Critical Accounting Policies***

In the course of developing and evaluating accounting policies and procedures, we use estimates, assumptions and judgments to determine the most appropriate methods to be applied. Such processes are used in determining revenue recognition, capitalization of costs related to real estate investments, potential impairment of real estate investments, operating cost reimbursements, and taxable income.

Minimum rental income attributable to leases is recorded when due from tenants. Certain leases provide for additional percentage rents based on tenants' sales volumes. These percentage rents are recognized when determinable by us. In addition, leases for certain tenants contain rent escalations and/or free rent during the first several months of the lease term; however such amounts are generally not material.

Real estate assets are stated at cost less accumulated depreciation. All costs related to planning, development and construction of buildings prior to the date they become operational, including interest and real estate taxes during the construction period, are capitalized for financial reporting purposes and recorded as property under development until construction has been completed. Subsequent to completion of construction, expenditures for property maintenance are charged to operations as incurred, while significant renovations are capitalized. Depreciation of the buildings is recorded on the straight-line method using an estimated useful life of forty years.

In determining the fair value of real estate investments, we consider future cash flow projections on a property by property basis, current interest rates and current market conditions of the geographical location of each property. Substantially all of our leases contain provisions requiring tenants to pay as additional rent a proportionate share of operating expenses (Operating Cost Reimbursements) such as real estate taxes, repairs and maintenance, insurance, etc. The related revenue from tenant billings is recognized in the same period the expense is recorded.

We have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the Code), commencing with our 1994 tax year. As a result, we are not subject to federal income taxes to the extent that we distribute annually at least 90% of our REIT taxable income to our stockholders and satisfy certain other requirements defined in the Code. Accordingly, no provision was made for federal income taxes in the accompanying consolidated financial statements.



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**Agree Realty Corporation  
Part I**

***Comparison of Three Months Ended March 31, 2007 to Three Months Ended March 31, 2006***

Minimum rental income increased \$155,000, or 2%, to \$7,687,000 in 2007, compared to \$7,532,000 in 2006. The increase was the result of the development of a Walgreens at our Capital Plaza Shopping Center in December 2006 and the acquisition of a Rite Aid Drug Store in Summit Township, Michigan in September 2006.

Percentage rental income remained constant at \$14,000 in 2007 and 2006.

Operating cost reimbursements increased \$44,000, or 6%, to \$756,000 in 2007, compared to \$712,000 in 2006.

Operating cost reimbursements increased due to the increase in property operating expenses as explained below.

Other income decreased \$8,000 to \$6,000 in 2007, compared to \$14,000 in 2006. The decrease was primarily the result of other income recognized of \$8,000 in 2006. There was no such income in 2007.

Real estate taxes increased \$17,000, or 4%, to \$457,000 in 2007, compared to \$440,000 in 2006. The increase was the result of general assessment adjustments.

Property operating expenses (shopping center maintenance, snow removal, insurance and utilities) decreased (\$37,000), or 7%, to \$510,000 in 2007 compared to \$547,000 in 2006. The net decrease was the result of decreased shopping center maintenance costs of (\$45,000); a decrease in snow removal costs of (\$15,000); an increase in utility costs of \$6,000; and an increase in insurance costs of \$17,000 in 2007 versus 2006.

Land lease payments decreased \$25,000, or 13%, to \$170,000 in 2007 compared to \$195,000 in 2006. The decrease was the result of our purchase of the fee interest in the land located at our Lawrence, Kansas property previously leased.

General and administrative expenses decreased by \$55,000, or 5%, to \$996,000 in 2007, compared to \$1,051,000 in 2006. The net decrease was the result of increased compensation related expenses as a result of salary increases and the value of employee stock awards of \$64,000; a decrease in contracted services to investigate development opportunities of (\$25,000); a decrease in legal and auditing cost of (\$80,000) and decreased property related expenses of (\$14,000). General and administrative expenses as a percentage of total rental income decreased from 13.9% for 2006 to 12.9% for 2007.

Depreciation and amortization increased \$32,000, or 3%, to \$1,234,000 in 2007, compared to \$1,202,000 in 2006. The increase was the result of the development and acquisition of the two properties in 2006.

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Part I**

Interest expense increased \$23,000, or 2%, to \$1,177,000 in 2007, from \$1,154,000 in 2006. The increase in interest expense resulted from increased borrowings to fund the development and acquisition of the two properties in 2006. Our income before minority interest and discontinued operations increased \$236,000, or 6%, to \$3,919,000 in 2007 from \$3,683,000 in 2006 as a result of the foregoing factors.

***Liquidity and Capital Resources***

Our principal demands for liquidity are distributions to our stockholders, debt repayment, development of new properties and future property acquisitions.

During the quarter ended March 31, 2007, we declared a quarterly dividend of \$0.49 per share. The dividend was paid on April 12, 2007 to holders of record on March 30, 2007.

As of March 31, 2007, we had total mortgage indebtedness of \$47,720,435 with a weighted average interest rate of 6.64%. Future scheduled annual maturities of mortgages payable for the years ending March 31, are as follows: 2008 \$2,630,803; 2009 \$2,795,481; 2010 \$2,986,064; 2011 \$3,189,677; and 2012 \$3,407,209. This mortgage debt is all fixed rate debt.

In addition, the Operating Partnership has in place a \$50 million credit facility (Credit Facility) with LaSalle Bank, as the agent, which is guaranteed by the Company. The Credit Facility matures in November 2009 and can be extended at our option, for two additional one-year periods. Advances under the Credit Facility bear interest within a range of one-month to twelve-month LIBOR plus 100 basis points to 150 basis points or the lender's prime rate, at our option, based on certain factors such as the ratio of our indebtedness to the capital value of our properties. The Credit Facility is used to fund property acquisitions and development activities. As of March 31, 2007, \$20,500,000 was outstanding under the Credit Facility bearing a weighted average interest rate of 6.32%.

We also have in place a \$5 million line of credit (Line of Credit), which matures in November 30, 2007, and which we expect to renew for an additional 12-month period. The Line of Credit bears interest at the lender's prime rate less 75 basis points or 150 basis points in excess of the one-month to twelve-month LIBOR rate, at our option. The purpose of the Line of Credit is to provide working capital and fund land options and start-up costs associated with new projects. As of March 31, 2007, \$2,575,000 was outstanding under the Line of Credit bearing a weighted average interest rate of 7.50%.

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The following table outlines our contractual obligations (in thousands) as of March 31, 2007.

|   | <b>Total</b>      | <b>Yr 1</b>      | <b>2-3 Yrs</b>   | <b>4-5 Yrs</b>   | <b>Over 5<br/>Yrs</b> |
|---|-------------------|------------------|------------------|------------------|-----------------------|
| Mortgages Payable                                   | \$ 47,720         | \$ 2,631         | \$ 5,781         | \$ 6,597         | \$ 32,711             |
| Notes Payable                                       | 23,075            | 2,575            | 20,500           |                  |                       |
| Land Lease Obligation                               | 11,610            | 674              | 1,305            | 1,387            | 8,244                 |
| Interest Payments on Mortgages And<br>Notes Payable | 26,175            | 4,375            | 7,708            | 4,817            | 9,275                 |
| Other Long-Term Liabilities                         |                   |                  |                  |                  |                       |
| <b>Total</b>  | <b>\$ 108,410</b> | <b>\$ 10,255</b> | <b>\$ 35,294</b> | <b>\$ 12,801</b> | <b>\$ 50,060</b>      |

We have two development projects under construction that will add an additional 29,311 square feet of GLA to our portfolio. The projects are expected to be completed during the second and third quarter of 2007. Additional funding required to complete the projects are estimated to be \$2,827,000, which is not reflected in the table above, and will be funded through advances under the Credit Facility.

We intend to meet our short-term liquidity requirements, including capital expenditures related to the leasing and improvement of the properties, through cash flow provided by operations and the Line of Credit and the Credit Facility. We believe that adequate cash flow will be available to fund our operations and pay dividends in accordance with REIT requirements. We may obtain additional funds for future development or acquisitions through other borrowings or the issuance of additional shares of common stock. We intend to incur additional debt in a manner consistent with our policy of maintaining a ratio of total debt (including construction and acquisition financing) to total market capitalization of 65% or less. We believe that these financing sources will enable us to generate funds sufficient to meet both our short-term and long-term capital needs.

We plan to begin construction of additional pre-leased developments and may acquire additional properties, which will initially be financed by the Credit Facility and Line of Credit. We will periodically refinance short-term construction and acquisition financing with long-term debt and / or equity.

**Off-Balance Sheet Arrangements**

We do not engage in any off-balance sheet financing arrangements with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, that have or are reasonably likely to have a material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditure or capital resources.

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Our leases generally contain provisions designed to mitigate the adverse impact of inflation on net income. These provisions include clauses enabling the us to pass through to tenants certain operating costs, including real estate taxes, common area maintenance, utilities and insurance, thereby reducing the our exposure to increases in costs and operating expenses resulting from inflation. Certain of our leases contain clauses enabling us to receive percentage rents based on tenants' gross sales, which generally increase as prices rise, and, in certain cases, escalation clauses, which generally increase rental rates during the terms of the leases. In addition, expiring tenant leases permit us to seek increased rents upon re-lease at market rates if rents are below the then existing market rates.

***Funds from Operations***

Funds from Operations (FFO) is defined by the National Association of Real Estate Investment Trusts, Inc. (NAREIT) to mean net income computed in accordance with generally accepted accounting principles (GAAP), excluding gains (or losses) from sales of property, plus real estate related depreciation and amortization and after adjustments for unconsolidated partnerships and joint ventures. Management uses FFO as a supplemental measure to conduct and evaluate our business because there are certain limitations associated with using GAAP net income by itself as the primary measure of our operating performance. Historical cost accounting for real estate assets in accordance with GAAP implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, management believes that the presentation of operating results for real estate companies that use historical cost accounting is insufficient by itself. FFO should not be considered as an alternative to net income as the primary indicator of our operating performance or as an alternative to cash flow as a measure of liquidity. Further, while we adhere to the NAREIT definition of FFO, our presentation of FFO is not necessarily comparable to similarly titled measures of other REITs due to the fact that not all REITs use the same definition.

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The following tables illustrate the calculation of FFO for the three months ended March 31, 2007 and 2006:

| <i>Three Months Ended March 31,</i>                              | <b>2007</b>         | 2006         |
|--|---------------------|--------------|
| Net income   | <b>\$ 3,605,059</b> | \$ 3,386,694 |
| Depreciation of real estate assets                               | <b>1,208,065</b>    | 1,177,360    |
| Amortization of leasing costs                                    | <b>12,250</b>       | 9,713        |
| Minority interest  | <b>313,487</b>      | 296,098      |
| <b>Funds from Operations</b>                                     | <b>\$ 5,138,861</b> | \$ 4,869,865 |
| <b>Weighted Average Shares and OP Units Outstanding Dilutive</b> | <b>8,359,163</b>    | 8,326,016    |

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We are exposed to interest rate risk primarily through borrowing activities. There is inherent roll over risk for borrowings as they mature and are renewed at current market rates. The extent of this risk is not quantifiable or predictable because of the variability of future interest rates and our future financing requirements.

Our interest rate risk is monitored using a variety of techniques. The table below presents the principal payments (in thousands) and the weighted average interest rates on remaining debt, by year of expected maturity, to evaluate the expected cash flows and sensitivity to interest rate changes.

March 31,

|                       | 2007    | 2008    | 2009     | 2010    | 2011    | Thereafter | Total    |
|-----------------------|---------|---------|----------|---------|---------|------------|----------|
| Fixed rate debt       | \$2,631 | \$2,795 | \$ 2,986 | \$3,190 | \$3,407 | \$32,711   | \$47,720 |
| Average interest rate | 6.64%   | 6.64%   | 6.64%    | 6.64%   | 6.64%   | 6.64%      |          |
| Variable rate debt    | 2,575   |         | \$20,500 |         |         |            | \$23,075 |
| Average interest rate | 7.50%   |         | 6.32%    |         |         |            |          |

The fair value (in thousands) is estimated at \$47,720 and \$23,075 for fixed rate debt and variable rate debt, respectively.

The table above incorporates those exposures that exist as of March 31, 2007; it does not consider those exposures or positions, which could arise after that date. As a result, our ultimate realized gain or loss with respect to interest rate fluctuations will depend on the exposures that arise during the period and interest rates.

We do not enter into financial instruments transactions for trading or other speculative purposes or to manage interest rate exposure.

A 10% adverse change in interest rates on the portion of our debt bearing interest at variable rates would result in an increase in interest expense of approximately \$148,000.

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**ITEM 4. CONTROLS AND PROCEDURES**

At December 31, 2006, management identified the following material weakness in our internal controls:

We lack segregation of duties in the period-end financial reporting process. Our Chief Financial Officer (CFO) is the only employee with any significant knowledge of generally accepted accounting principles. The CFO is also the sole employee in charge of the general ledger (including the preparation of routine and non-routine journal entries and journal entries involving accounting estimates), the preparation of accounting reconciliations, the selection of accounting principles, and the preparation of interim and annual financial statements (including report combinations, consolidation entries and footnote disclosures) in accordance with generally accepted accounting principles.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange Act), as of the end of the period covered by this report.

Based on this evaluation as of March 31, 2007, and due to the material weaknesses in our internal control over financial reporting as described above, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were not effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC. There was no change in our internal control over financial reporting during the most recently completed fiscal quarter that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

Our audit committee has engaged independent third party consultants to perform periodic reviews of our financial reporting closing process.

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**Other Information**

Item 1. Legal Proceedings

We are not presently involved in any litigation nor, to our knowledge, is any other litigation threatened against us, except for routine litigation arising in the ordinary course of business which is expected to be covered by our liability insurance.

Item 1A. Risk Factors

There were no material changes in our risk factors set forth under Item 1A of Part I of our most recently filed Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

None



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Item 6. Exhibits

- 3.1 Articles of Incorporation and Articles of Amendment of the Company (incorporated by reference to Exhibit 3.1 to the Company's Registration Statement on Form S-11 (Registration Statement No. 33-73858, as amended ( Agree S-11 )))
- 3.2 Bylaws of the Company (incorporated by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2006)
- 31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Richard Agree, President and Chief Executive Officer
- 31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, Kenneth R. Howe, Vice President and Chief Financial Officer
- 32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Richard Agree, President and Chief Executive Officer
- 32.2 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Kenneth R. Howe, Vice President and Chief Financial Officer

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Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**Agree Realty Corporation**

/s/ RICHARD AGREE

Richard Agree  
President and Chief Executive Officer  
(Principal Executive Officer)

/s/ KENNETH R. HOWE

Kenneth R. Howe  
Vice-President Finance and Secretary  
(Principal Financial and Accounting Officer)

Date: May 9, 2007