

Real Estate Investment Trusts (REITs)

Presented by “6_The Hard Way”



2 February 2008



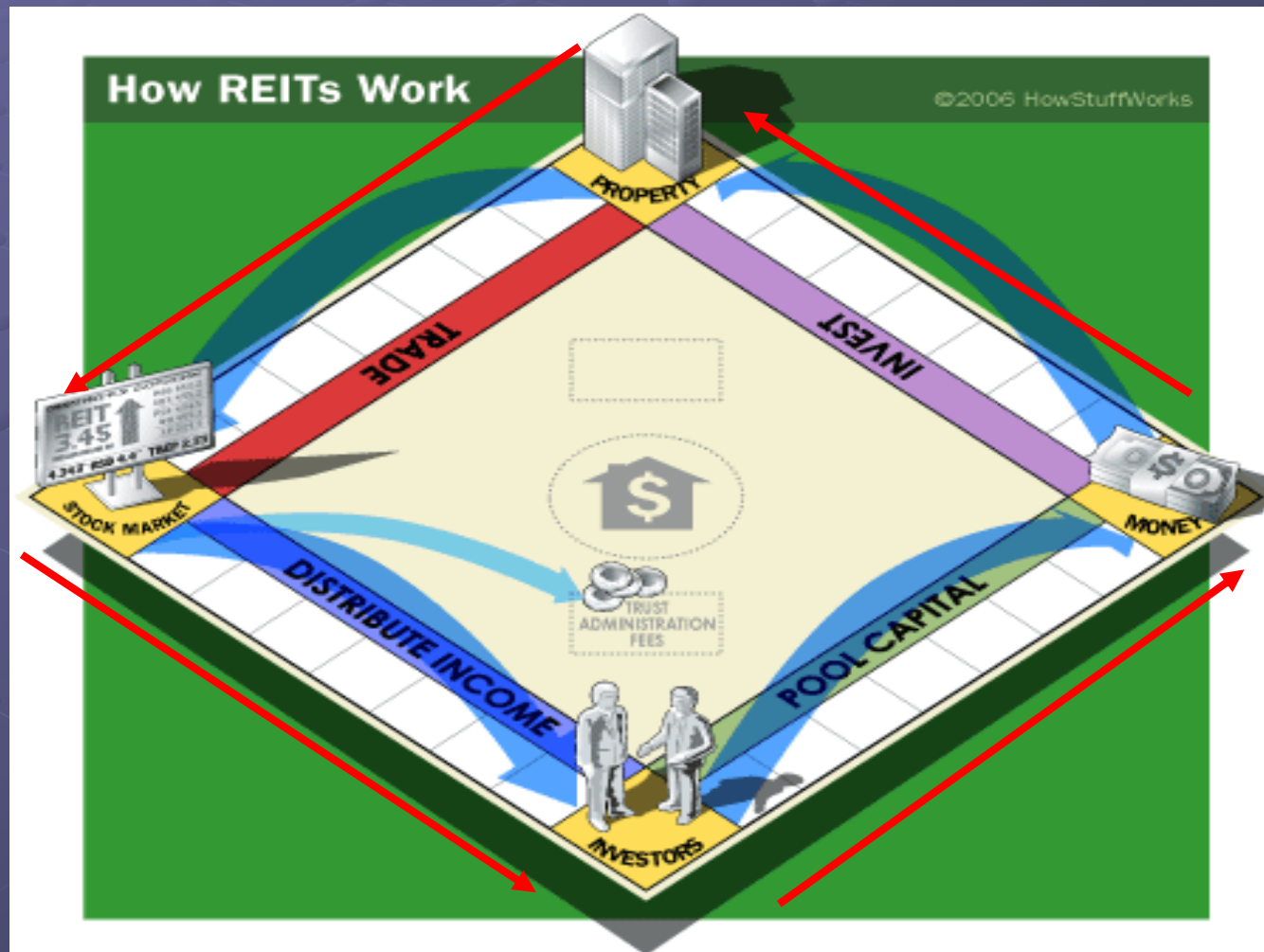
Presentation Goals

- What is a REIT
- REIT Industry
- HRPT Properties Trust
- Economic Environment
- Macro Economic Impact



What are Real Estate Investment Trusts?

▲ Is a tax designation for a company that invests in real estate that reduces or eliminates corporate income tax





Regulatory Framework

The Four Requirements You Must Know!

- ▶ A REIT must distribute 90% of its annual income as dividends to its shareholders
- ▶ A REIT must have at least 75% of its assets invested in real estate, mortgage loans, other REITs, cash, or government securities
- ▶ A REIT must derive at least 75% of its gross income from rents, interest, and gains from sale
- ▶ A REIT must have at least 100 shareholders and must have less than 50% of the outstanding shares concentrated in the hands of five or fewer shareholders



Critical Dates in REIT History

1880

Origins – double taxation avoided if income was distributed to beneficiaries

1930

Tax advantage reversed, taxed at corporate Level, and as individual incomes

1960

Demand grew, 2x taxation reversed

1993

Barrier to pension funds removed



Types of REITs

Equity REITs: (96.1%) – Invest & own properties. Revenues are generated from their properties rents

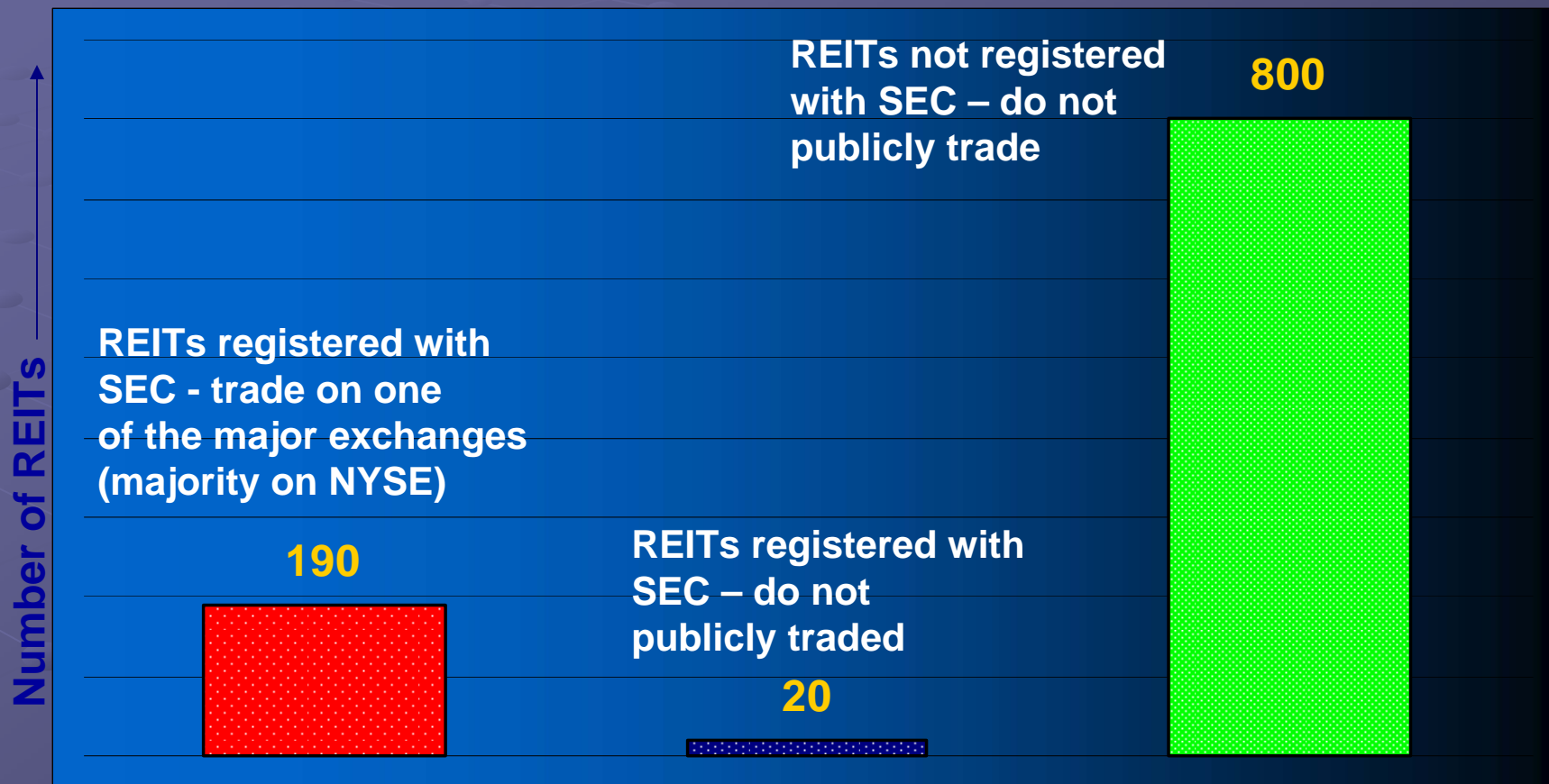
Mortgage REITs: (1.6%) – Deal in investment & ownership of property mortgages. They loan REITs money for mortgages to owners of real estate, or invest in existing mortgages of mortgage backed securities. Revenues are generated primarily by the interest that they earn on the mortgage loans.

Hybrid REITs: (2.3%) – Combine the investment strategies of Equity REITs & Mortgage REITs by investing in both properties and mortgages.

Source: www.reitnet.com



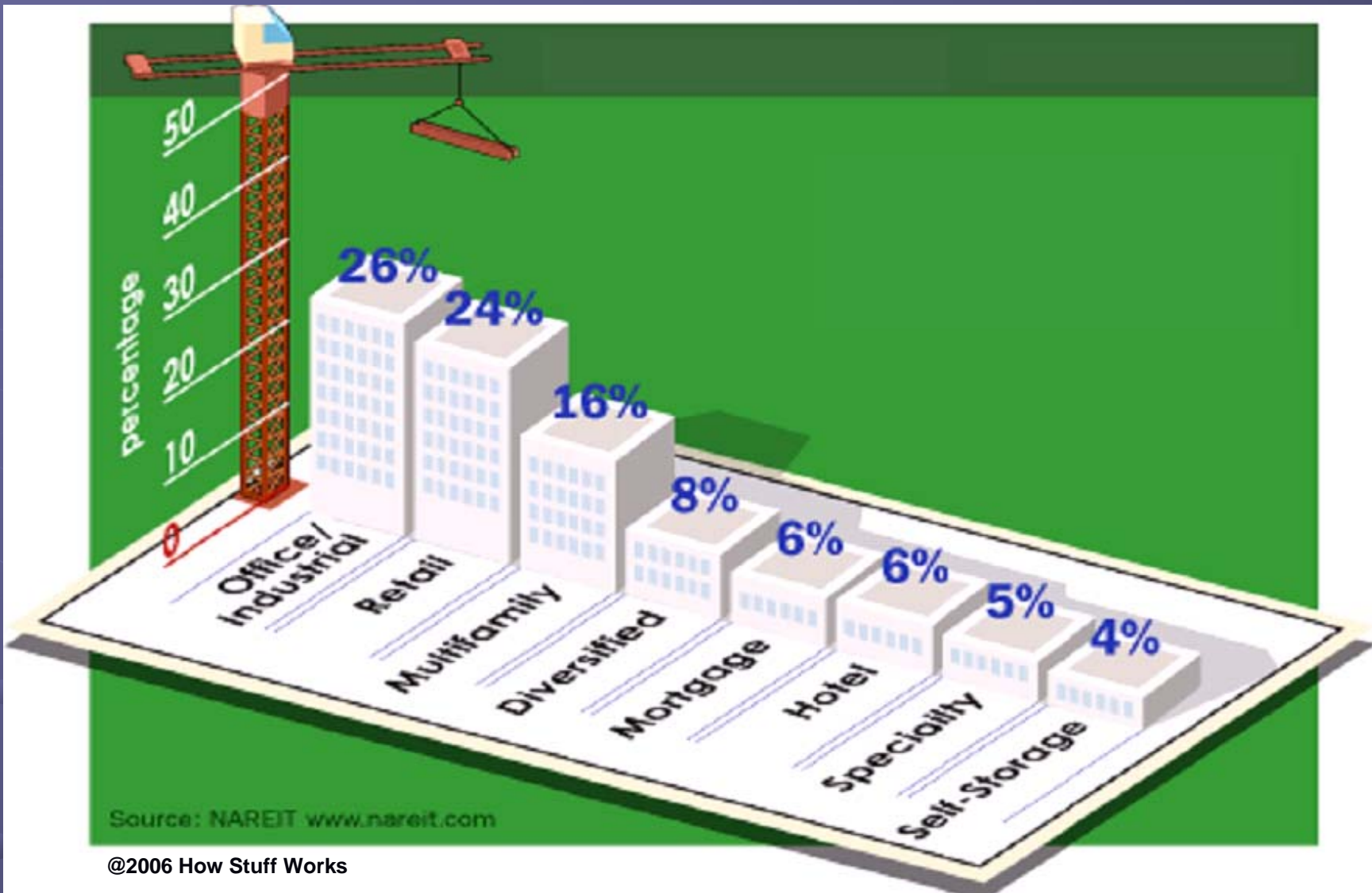
Number of REITs in the Industry



Source: [NAREIT](#)

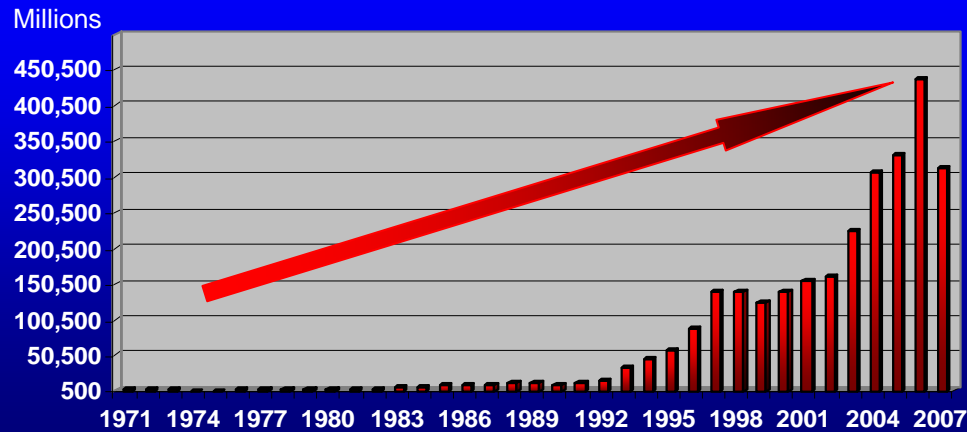


Publicly Traded REITs Property Types



The REIT Industry

REIT Market Cap



Market Cap

1971 – \$1.5 B

2007 – \$312 B

~2,000%
Growth

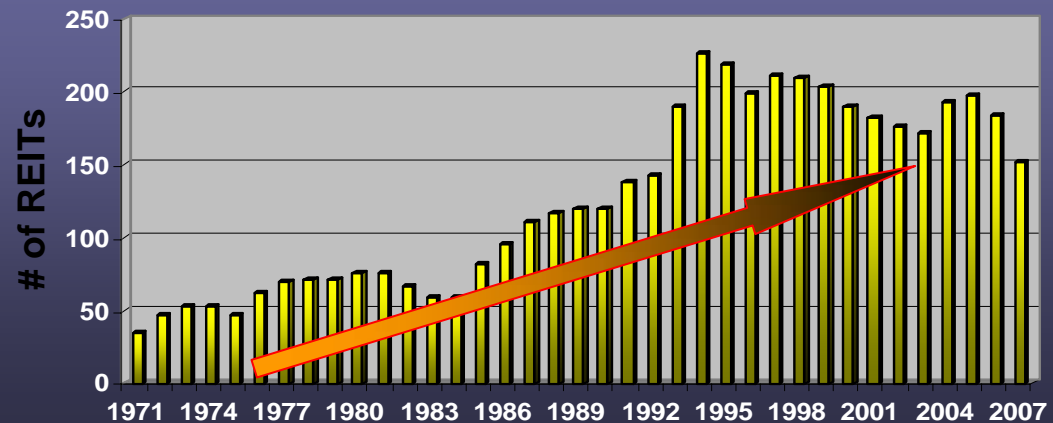
~450%
Growth

of REITs

1971 – 34

2007 – 190

REIT Growth



Source: [NAREIT](#)



The REIT Industry - Cost Structure

Equity Residential (EQR)	Year Ended December 31,	
	2003	2002
REVENUES		
Rental income	\$1,808,925	\$1,799,581
Fee and asset management	14,373	9,582
Total revenues	1,823,298	1,809,163
EXPENSES		
Property and maintenance	498,608	464,981
Real estate taxes and insurance	196,987	181,890
Property management	68,058	72,416
Fee and asset management	7,819	7,885
Depreciation	444,339	419,039
General and administrative	38,810	46,492
Impairments	1,162	18,284
Total expenses	1,255,783	1,210,987
Operating income	567,515	598,176
Net income	543,847	421,313

Depreciation is a large part of expenses, but in the case of real estate it may not apply!

NAREIT defines FFO as net income (computed in accordance with GAAP) excluding gains or losses from sales of most property and depreciation of real estate

Slide 10

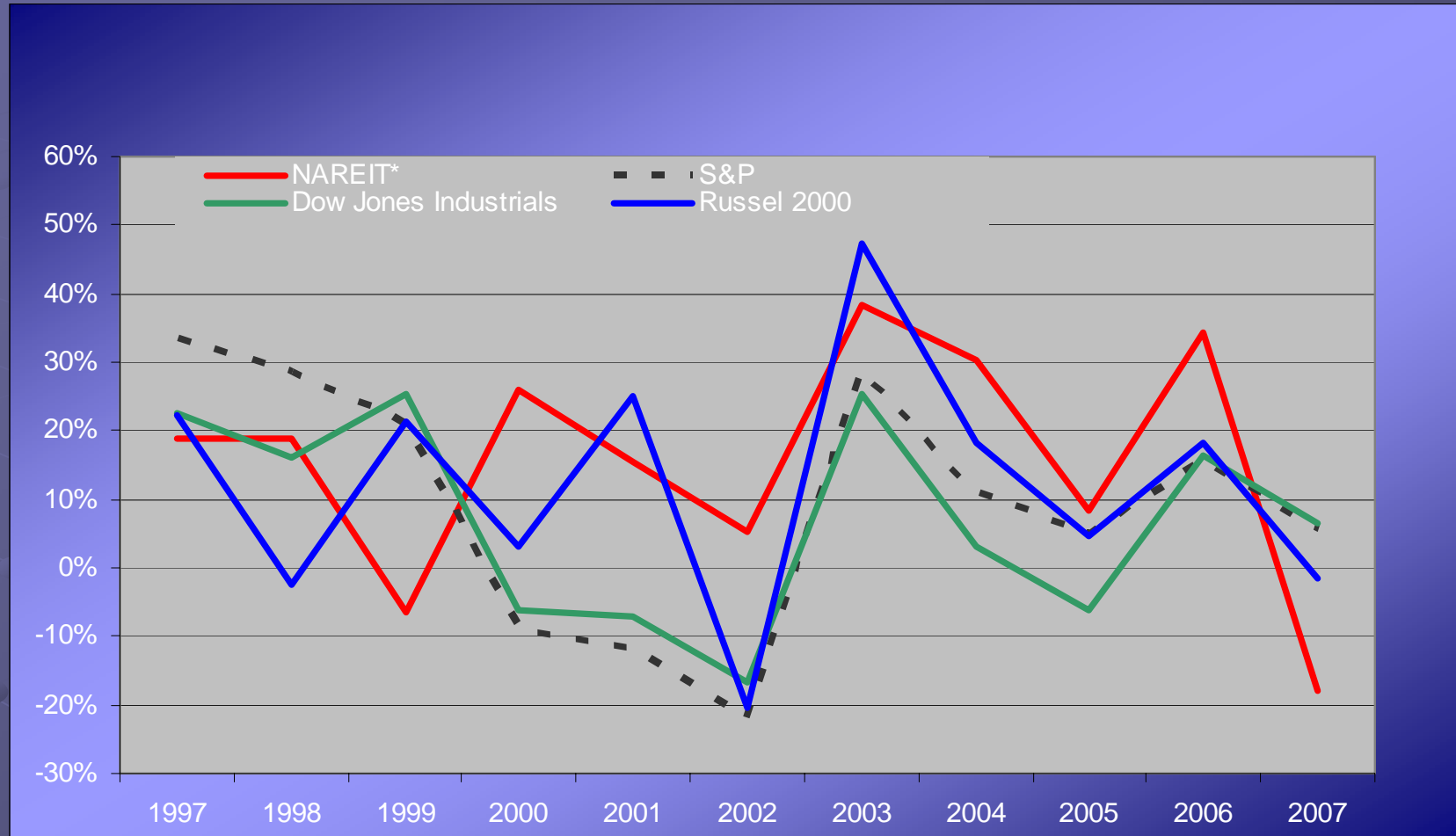
A2 Slides 2 & 3 could be used to show GAAP used by REIT companies.

www.investopedia.com/articles/04/112204.asp (reference)

AZEIGLER, 1/29/2008



The REIT Industry versus The Street



* Includes all REITs that trade on the New York Stock Exchange, American Stock Exchange and NASDAQ Global Market List.

Source: [NAREIT](http://www.nareit.com)



HRPT Properties Trust

HQ: Newton, MA

Assets: \$6B in office & industrial properties

Type: 351 office, 153 industrial properties

Area: Approximately 64 million square feet

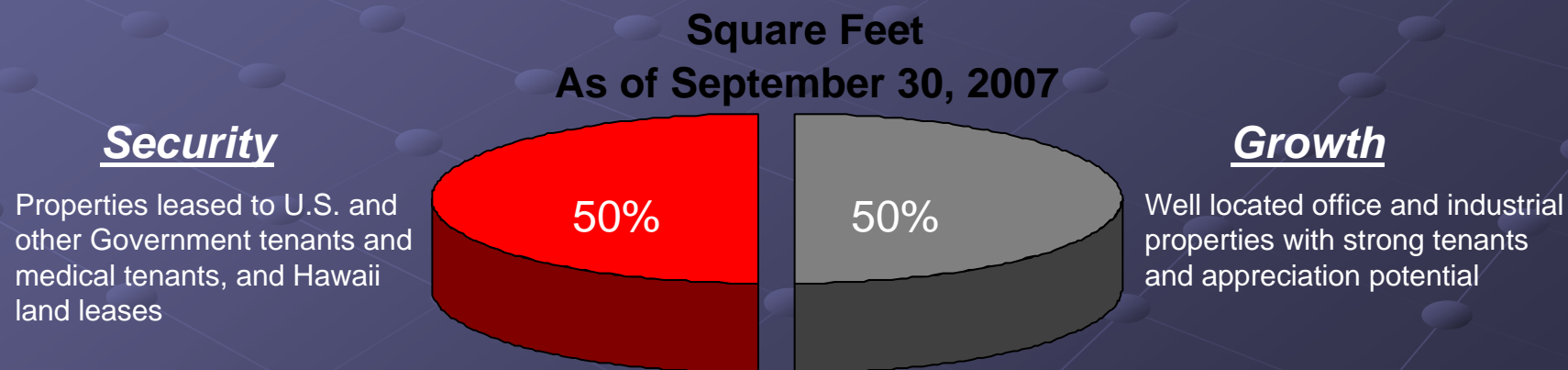
Where: 38 states (including Hawaii), and DC

Source: [Based on HRPT Company Data of 30 September 2007](#)



HRPT – Overall Business Strategy

- Focus on medical and government tenants which are less affected by changes in the business cycle and more prone to sign long term leases
- Investments in Hawaii remain very secure with land leases in which tenants have constructed their own building
- Focus growth on well located, high quality buildings leased to strong credit tenants



Source: [Based on HRPT Company Data of 30 September 2007](#)



HRPT – Property Management Strategy

- Maintain properties to the highest of industry standards
- Continue to invest in “*attractiveness of our property*” to continually increase values
- Improve efficiency of property operations through economies of scale purchasing, energy management programs, and real estate tax leverage

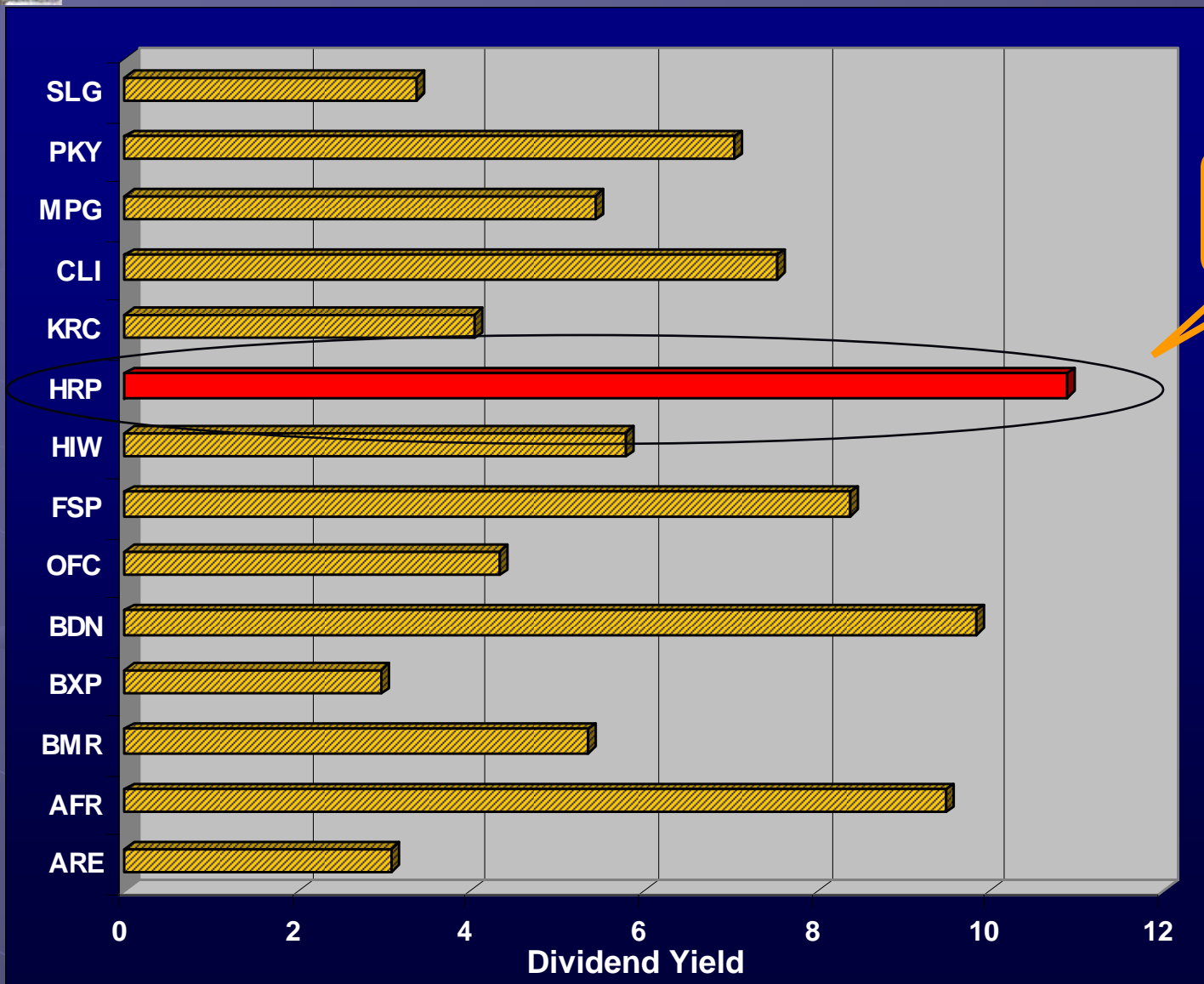


HRPT – Investment Strategy

- ▶ Purchase well leased and maintained properties
- ▶ Look for properties located near existing structures
- ▶ Attempt to identify and create synergy's between the two structures
- ▶ Grow with existing tenants by building to suit (high quality tenants only)
- ▶ Invest in properties that are seen as “long term” investments, not for short term hold and sell
- ▶ DO NOT seek to turn around properties
- ▶ DO NOT see out joint ventures
- ▶ DO NOT undertake speculative development



HRPT versus REIT Peers



Best Performance

Source: NAREIT

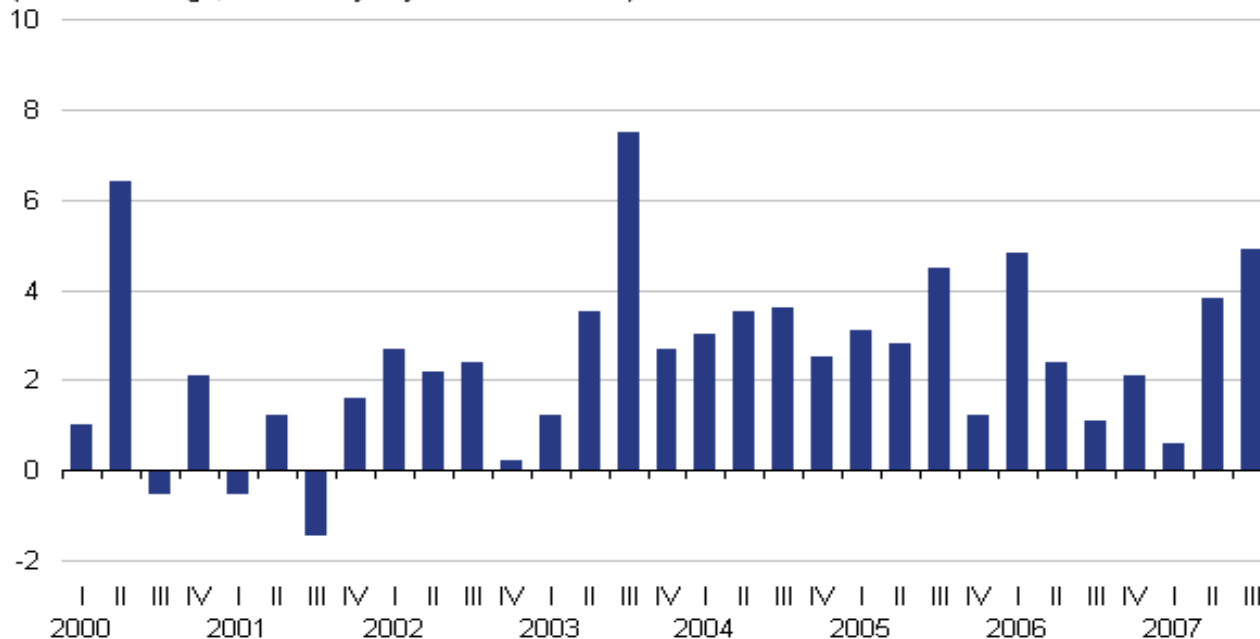
Dividend Yield: Dividends paid / market cap



Economic Factors - GDP

Real Gross Domestic Product

(Percent change, seasonally adjusted annual rate)



U.S. Bureau of Economic Analysis

Real GDP

4Q2007 - + 0.6 %

3Q2007 - + 4.9 %

2007 - 2.2 %

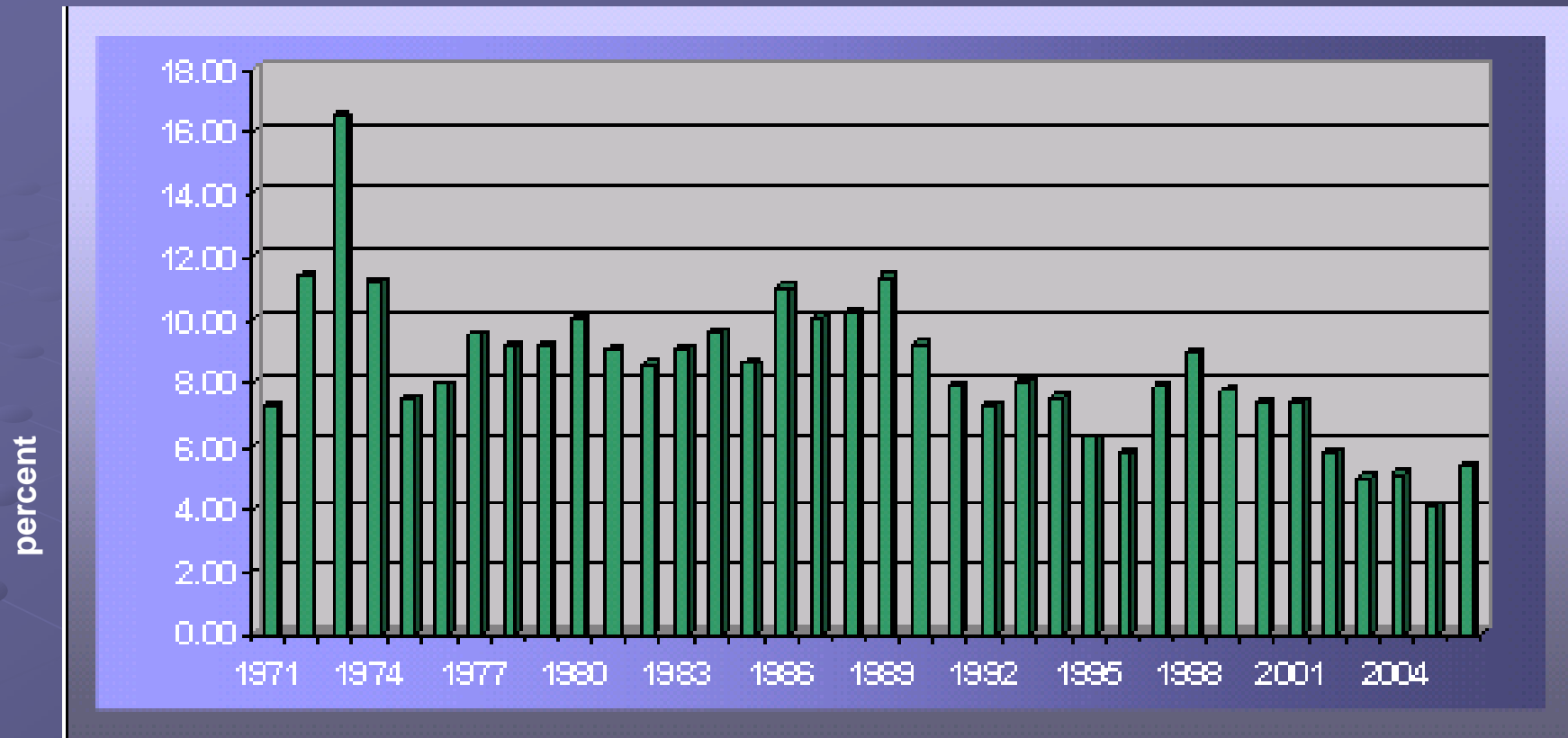
2006 - 2.9 %

1/30/2008

- As with many industries, GDP is a major economic indicator
- As GDP grows, so does the need for retail outlets, distribution centers, plants, ect.



GDP & Dividend Yields

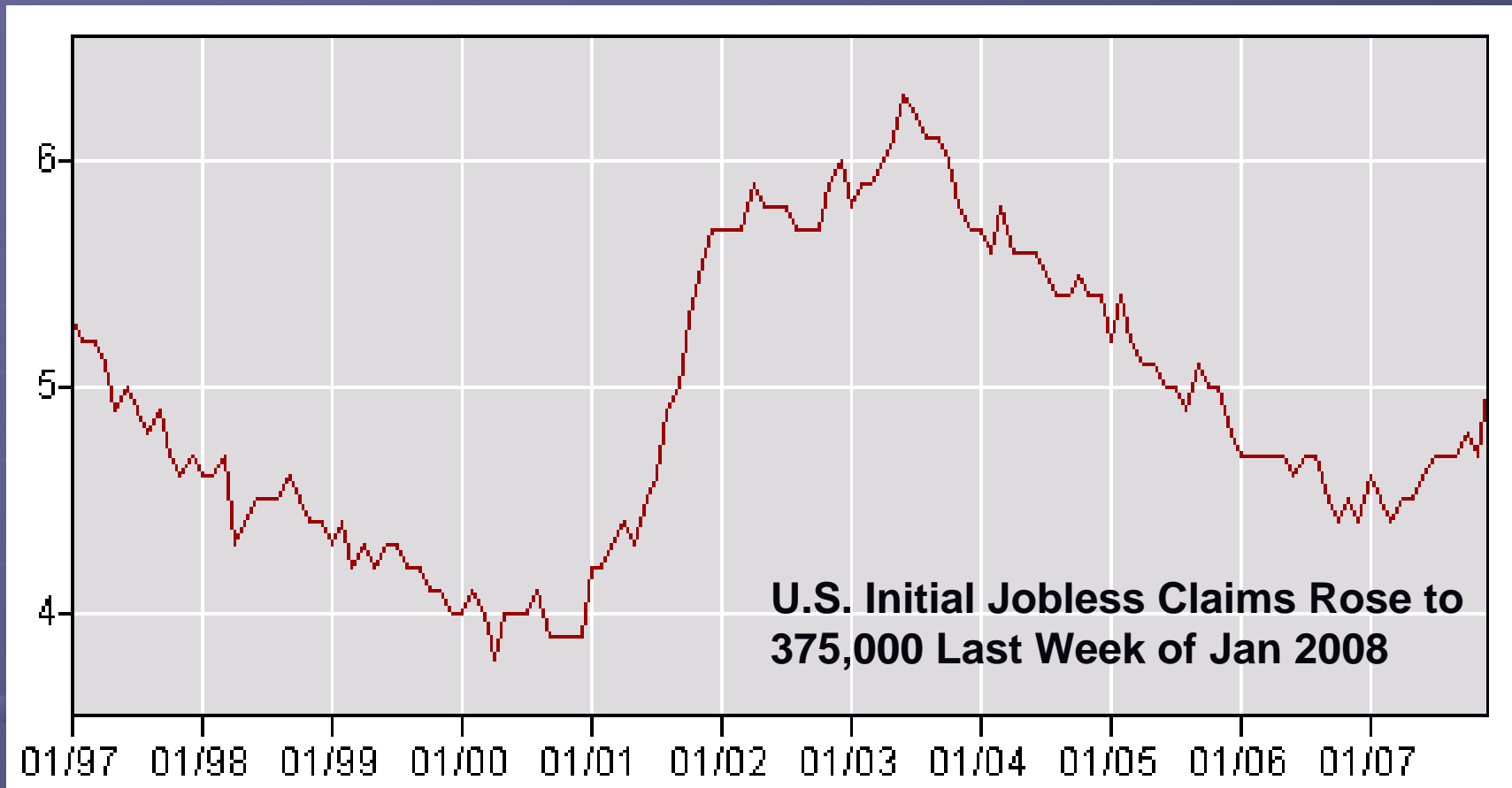


✓ Trend follows closely with GDP growth – in a lower GDP environment companies tend to curtail their real estate needs

Source: [NAREIT](#)

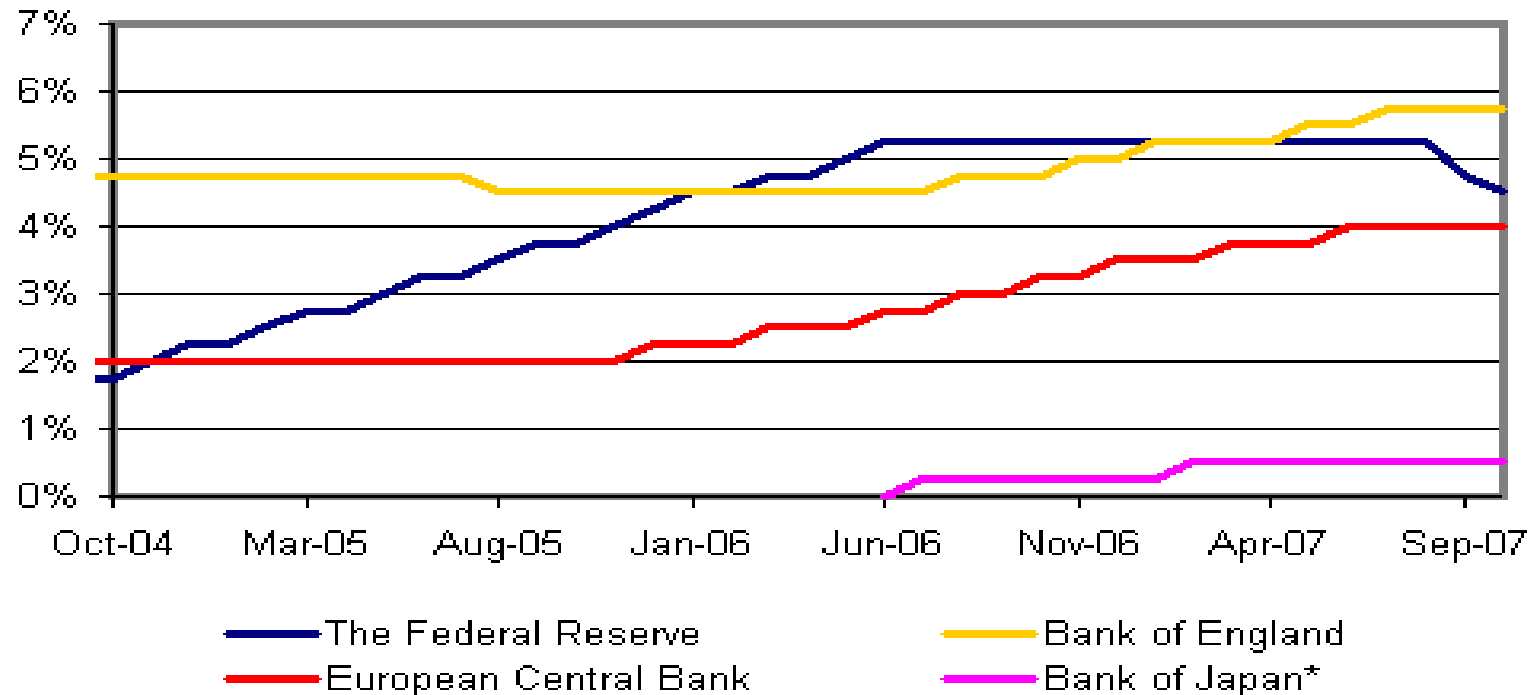


Economic Factors - Unemployment Rate



- ✓ Business closings
- ✓ Evictions
- ✓ Good time for rentals?

Economic Factors - Interest Rates



*Prior to July 2006 Japan's Target Rate was 0%

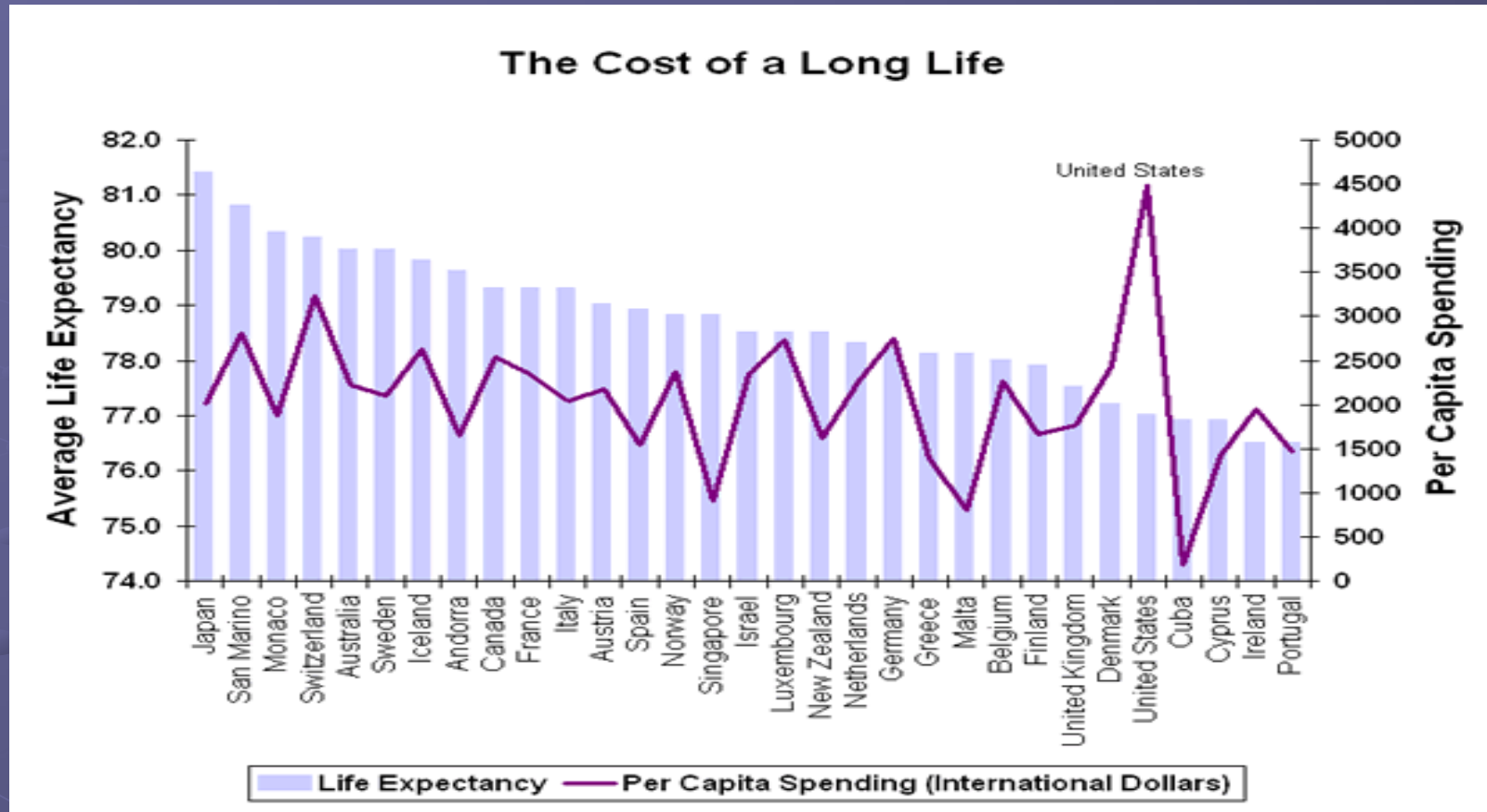
Source: Bloomberg LLP, FXstreet.com

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Posted: 11/09/2007

- ✓ REITs will invest their capital where money made available
- ✓ Recent moves by The Federal Reserve may spark industry investment

Economic Factors - Health Care



- ✓ Our nation's increasing need for health care will positively impact the REIT economy
- ✓ "By 2030, the number of people ages 65 & older will double to 71.5 million, or 20% of the population"

Source: www.imperialvalleynews.com



The REIT Industry – Head Winds

Through January 18, 2008, REIT stocks were down 11.1% (S&P 500 down 9.7%, Russell 2000 down 12.1%)

“....the prices of REIT shares are closely correlated with the present or prospective prices of commercial real estate..” (www.reitcafe.com/main_essential.html)”

“....with regard to REIT organizations and their business prospects, a weak economy negatively affects rents, occupancy rates, FFO/AFFO growth, and even cap rates and NAVS.” (www.reitcare.com/main_essential.htm)

“....the deflated housing bubble affects the US economy in many ways.....decline in new construction, rising delinquencies and foreclosures, and weak consumer confidence.” (www.reitcare.com/main_essential.htm)



The REIT Industry – Tail Winds

“....credit markets ease up just a bit...REIT buyouts and privatizations...arise slowly from the grave...”

(www.reitcafe.com/main_essential.html)”

“....the world’s economies are more self-reliant these days, as Europe, while slowing, is in pretty good shape, and the Asia economies are likely to remain strong.” (www.reitcafe.com/main_essential.html)”

The Federal Reserve – Rate cuts will have a positive impact on available funds and investments in general

The Long Term – REITs are typically seen as long term investments. Challenges in today’s market may provide opportunity for one to begin building such a portfolio



The REIT Industry - Demand

- Decreased interest rates
- Increased population
 - ✓ Services demand
 - ✓ Housing demand
- GDP growth
- Household growth

- Increased interest rates
- Mortgage crisis
 - ✓ Apprehensive lenders
- Weak economy
 - ✓ Delinquent tenants
 - ✓ Slow new business growth

Increase

Decrease



The REIT Industry – Forecast

- ⤴ Retail REITs remain an attractive sector for investors
- ⤴ Yields are in a range of 0.00%-14.16% for Retail REITs
- ⤴ Although Retail REITs provided a negative total return of (16%) during the fourth quarter of 2007, resulting in a decline of (15%) for 2007, valuations are still attractive
- ⤴ Retail REITs add more retail space to its portfolio through acquisition
- ⤴ If Retail REIT prices remain depressed in 2008, additional consolidation could occur

www.bloomberg.com

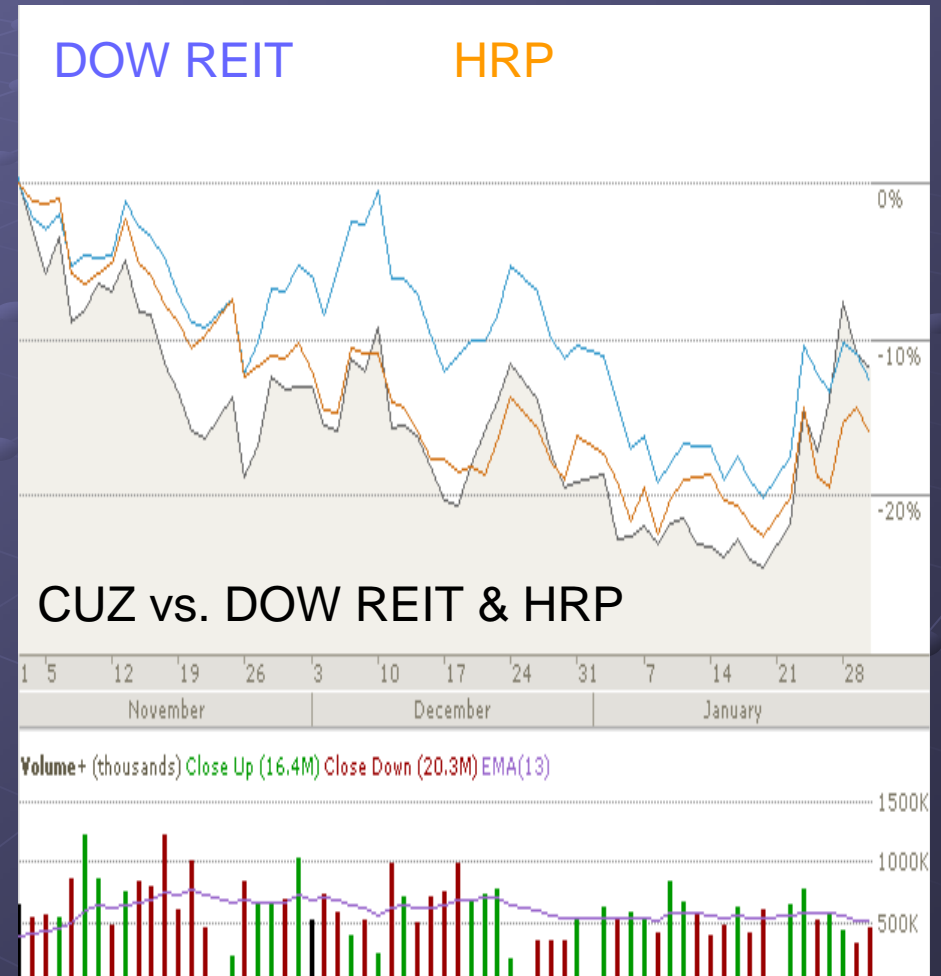


Atlanta's REIT – Cousins Prop

- Size: 1.25B Market Cap
- Employees: 488
- HQ: 191 Peachtree Street, NE



191 Peachtree street





Thank You

Question & Answer

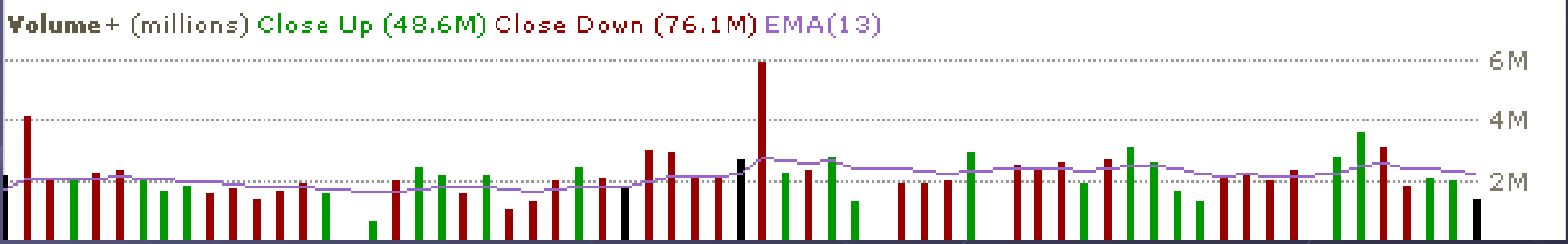
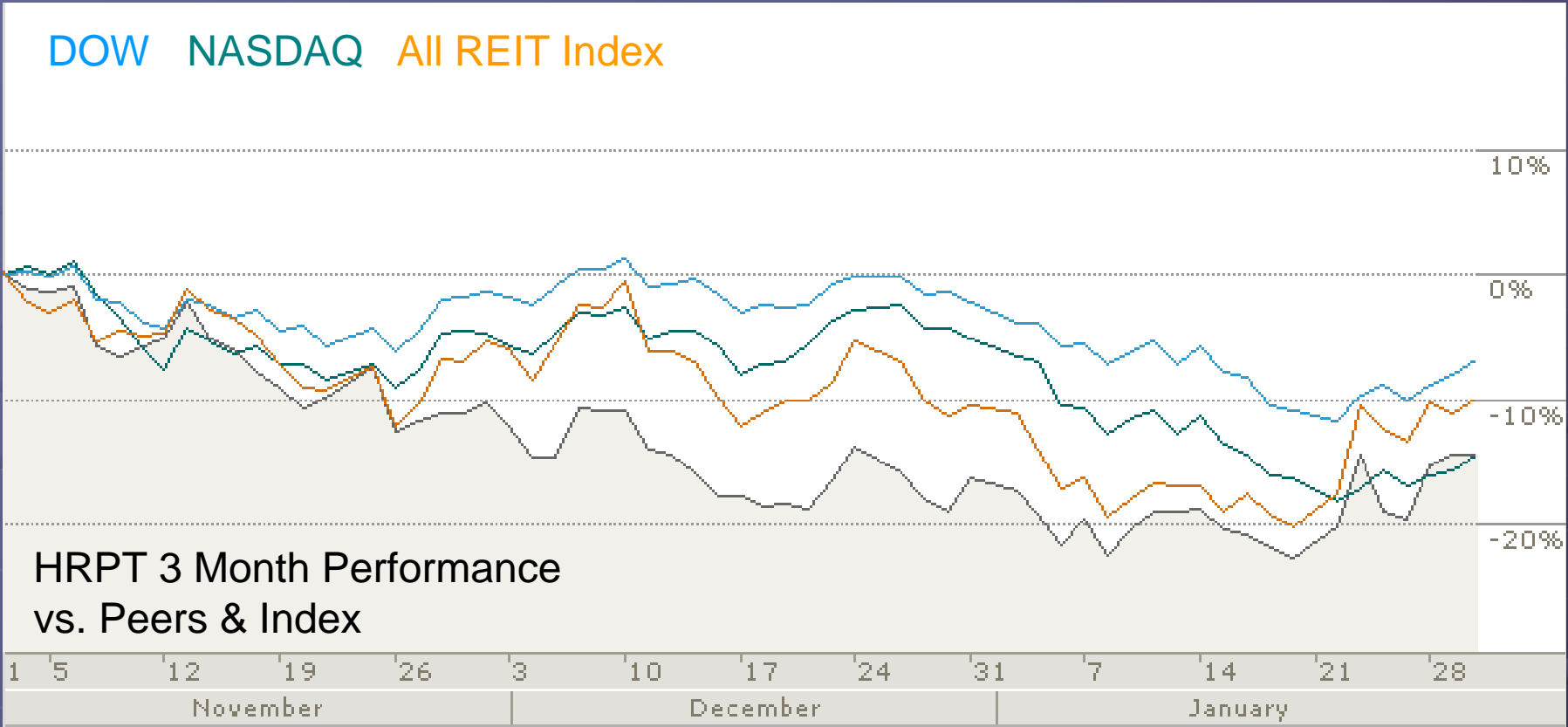


Supplemental Research





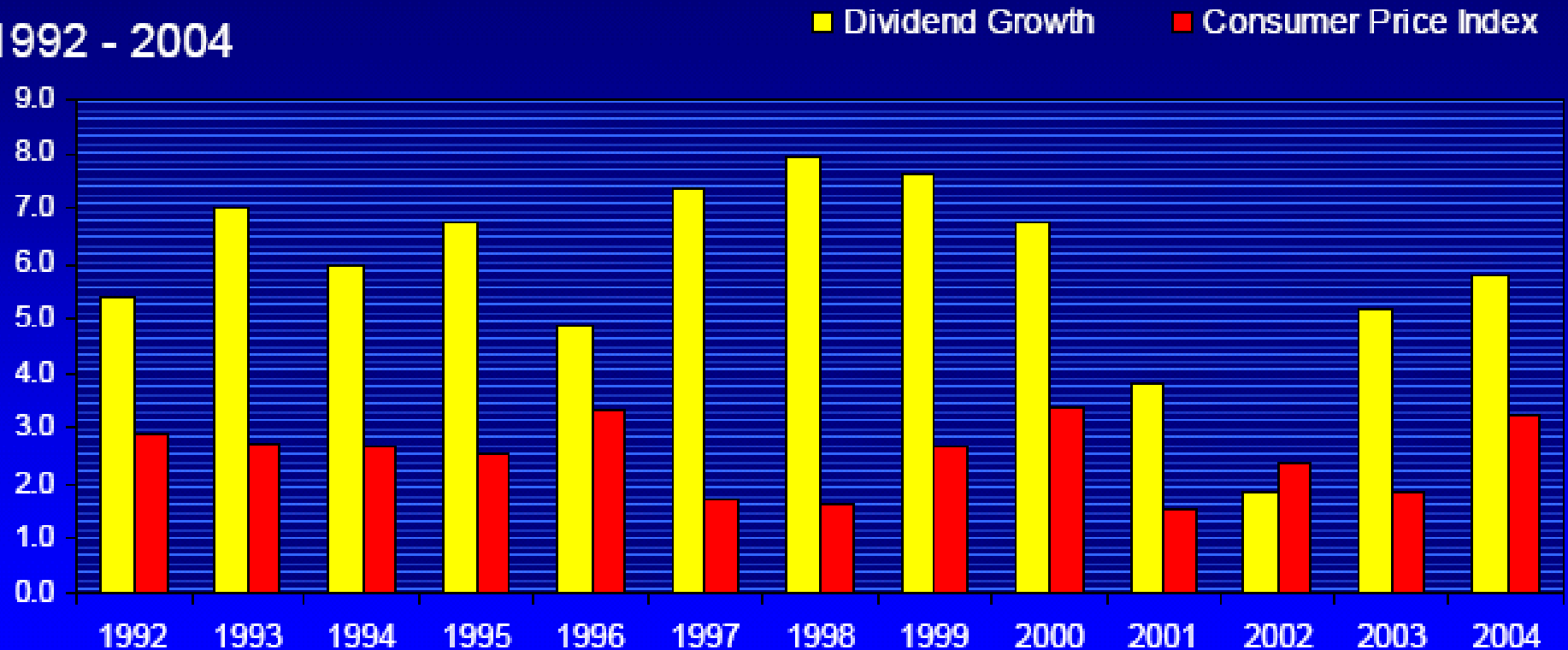
HRPT - Performance



The REIT Industry versus CPI



REIT Dividend Growth versus CPI 1992 - 2004



Remember...."CPI measures changes in the prices paid by urban consumers for a representative basket of goods and services and 42% of the basket comes from housing!"

Source: NAREIT and www.bls.gov/cpi



Economic Environment

The Role of Real Estate in the Economy

- Construction [6% of GDP]
- Service flow, “Shelter”, rent plus imputed rent [20%+ of GDP]
- Assets [55-60% of total national wealth]
- Land? Not part of GDP (we don't make land), but it is part of wealth.
- Accounting, measurement difficulties [book versus market value]



Economic Factors - Sub-prime Losses

Losses from securities linked to subprime mortgages may exceed \$265 billion as regional U.S. banks, credit unions and overseas financial institutions write down the value of their holdings, according to Standard & Poor's