NET LEASE forum

The On-Line Newsletter
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INDUSTRY UPDATE

AFRT Set To Close On $705M Boston Buy

Said To Be Discussing Net Lease With Gross Tenant

When Florham Park, NJ-based **Gale Co.** and its partners began building the office tower at Boston's 1 Lincoln St. less than four years ago, it was a purely speculative, multi-tenant project. But its $705 million sale this month as an asset 100%-leased to one investment-grade tenant represents a doubling of its $350 million construction cost.

Sharing that tidy profit with Gale are its financial partners, **Morgan Stanley Real Estate Funds** and the **State Teachers Retirement System of Ohio**, as well as limited development and ownership partner **Columbia Plaza Associates**, a minority community organization that had been given the property's development rights by the city. Gaining the new building and credit tenant **State Street Corp.** is Jenkintown, PA-based **American Financial Realty Trust**.

The buyer typically goes after properties triple-net or bond-net leased to banks and financial institutions, though the Boston property, now known as State Street Financial Center, has a modified gross lease. AFRT is said to be in discussions with the tenant about restructuring the 20-year lease, which the REIT says has a net value of more than $1 billion. An AFRT spokesperson said executives would not be available for additional comment until after the deal's closing, which was expected around the President's Day holiday.

Investor interest in single-tenant buildings with strong credit tenants—State Street is rated AA by **Fitch Ratings** and **Standard & Poor's Ratings Services** and Aa3 by **Moody's Investors Service**—led Gale and partners to dispose of the property ahead of schedule. According to John Hynes III, Gale managing partner in Boston, the original plan was to lease up the building within two years after its summer 2003 completion, and then sell. Of course, with State Street committing to the entire building in 2001, after first expressing interest in roughly half, then two-thirds of the 1.05 million sf of the office space, lease-up was a moot point. The strategy then shifted to refinancing or putting the property on the market in summer 2004, when State Street is set to finish its occupation of the building.

AFRT's latest buy

But the strategy changed yet again. "We were getting so much unsolicited interest from brokers and buyers this summer, due

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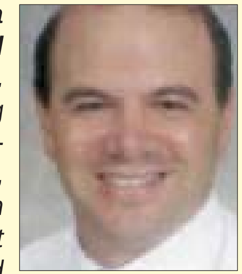
AT DEADLINE

Two Minneapolis companies, the **Upland Real Estate Group** and the **Geneva Organization**, have launched **Safe Harbor Properties Exchange.** The new endeavor will serve as a "conduit" for 1031 exchange and tenancy-in-common investments. Look for more details in our March 2 issue.

NETLEASE INSIDER



Christian S. Marabella

Marabella Commercial Finance Inc. *arranges financing exclusively for net-leased properties, like the $2.8-million first mortgage it recently completed for a CVS drug store.* ***NET LEASE forum*** *spoke to Christian S. Marabella, president and owner of the Escondido, CA-based brokerage, about the business.*

Q: How did your company get started?

A: My dad, Don Marabella, started doing sale-leasebacks with Safeway back around 1972. He would put syndications together and they would buy stores; he did quite a bit with Safeway, which at the time was a growing company. Back then you were able to finance deals 100%. The main drive at that time was taxes; you could offset your salary because the depreciation was very accelerated. So you could get 100% financing, a fully amortizing loan co-termi-

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to all the reasons we all know of only too well," Hynes tells *NET LEASE forum*. "There's a ton of capital out there and we've got a brand-new building in a great market, a great location within the market and a great credit behind the lease. When you line those stars up, investors and brokers representing investors are saying, 'your building isn't going to get much more valuable than what it is now.'"

After the partners decided to test the waters late last summer, Hynes says they offered State Street a first crack at buying the asset, the first new office building in Boston's financial district in more than a decade. State Street's offer was declined and the property went to market on Dec. 1. "We had an enormous amount of interest, international interest, notwithstanding the holidays," Hynes adds. "We had inquiries from 40 different investment groups; we had 20 investors come here to look at the building and we had 15 offers." Other interested parties included a number of REITs but mostly pension fund advisors, half of which were international advisors.

Threesome JV To Target $1B Of Distressed, Leaseback Retail

Retail properties that are distressed, underutilized or could otherwise be turned into working capital via a sale-leaseback are the kinds of assets being targeted for acquisition by a new joint venture. White Plains, NY-based shopping center REIT **Acadia Realty Trust**, **Klaff Realty LP**, a Chicago real estate investment concern that is a leader in acquiring distressed retail assets, and its long-time capital partner, Philadelphia opportunistic investor **Lubert-Adler Management Inc.**, have come together for the effort.

About $300 million of equity is expected to be turned into $1 billion of property assets over the next 24 to 36 months. The types of assets they plan to target will vary, but will likely be similar to the acquisitions Klaff has made in the past. These include acquiring properties, leases and designation rights of bankrupt retailers, and transacting sale-leasebacks with retailers that need capital for other purposes. Stephen Smith, former managing director and global client services director for **LaSalle Investment Management,** has joined Klaff Realty as a principal in the venture.

Klaff and Lubert-Adler both have considerable experience in the distressed retail business, while Acadia brings its redevelopment, operational and leasing expertise to the mix. Klaff and Lubert-Adler have teamed on numerous bankruptcy and sale-leaseback transaction before, including with **Service Merchandise**, **Levitz**, **HomeLife**, **Montgomery Ward**, **Lechmere**, **Hechinger** and **Kmart**. Acadia has its own experience filling stores vacated by bankrupt companies like **Caldor**, **Ames** and **Grand Union** with

▸▸▸ Continued on page 3

RECENT TRANSACTIONS

▸ A 310,519-sf industrial building in Temple, TX triple-net leased to **Temperature Controlled** was purchased by a New Jersey buyer for $17.13 million. **Marcus & Millichap Real Estate Investment Brokerage Co.** repped seller **Atlantic Financial Group**. Parent company **Performance Food Group Co.** guarantees the 22-year lease.

▸ **Grand Paramus LLC** parted with two Paramus, NJ buildings leased to **Chase Manhattan** in a sale arranged by **Sonnenblick-Goldman Co.** The 25-year net lease, guaranteed by **JPMorgan Chase**, runs through August 2007. The price was not disclosed but the going-in cap rate was 5.5%. The buyer of the property, with a retail bank branch, office space, training facility and home mortgage operation, is **Jessum Co.**

▸ A 42,000-sf El Segundo, CA office building triple-net leased to **Xerox Corp.** was sold for $6.8 million to a private group of investors represented by **Coldwell Banker Commercial REP. Grubb & Ellis** sat in for seller **Layton-Belling**.

▸ **Ventas Inc.** has agreed to buy 14 independent-living and assisted-living facilities representing 2,000 units for $115 million; it has closed on four of the properties at a cost of $37 million. Affiliates of **Brookdale Living Communities Inc.** will operate the properties under a 15-year triple-net master lease.

▸ A 743,000-sf lease signed by **PepsiCo Beverages and Food** at Stellar Way Business Park in Grand Prairie, TX represents a renewal for 451,000 sf and an expansion of 292,000 sf. **Catellus Development Corp.** owns the industrial complex.

▸ **Vornado Realty Trust** used a 1031 exchange to turn part of its proceeds from the sale of a Manhattan office building into the acquisition of Forest Plaza Shopping Center, a $32.5-million, 165,000-sf **Waldbaum's**-anchored shopping center on Staten Island, NY.

▸ A $4.8-million, 102,000-sf industrial building in Irvine, CA helped **Wohl Investment Co.** complete a 1031 exchange. **Voit Commercial Brokerage** represented the buyer, while **Klabin Co.** spoke for the seller, **American Electronics.**

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new, viable tenants such as **Wal-Mart**, **Home Depot** and **Shaw's** and otherwise repositioning shopping centers.

Even as the economy improves, the JV expects plenty of opportunities. "This type of venture doesn't rely on any real estate cycle or economic cycle," says an Acadia spokesman. "It's almost countercyclical."

With IPO Proceeds In Hand, GPP Focuses On New Buys

With proceeds of $179.7 million from its IPO late last month, Omaha-based **Government Properties Trust** is ready to add more assets to its five-property portfolio. As its name implies, the company is focused on properties with the US, state and local governments as well as government-sponsored enterprises as their sole tenants under long-term leases.

Trading on the New York Stock Exchange under the symbol GPP, Government Properties Trust plans to qualify as a REIT and appears to be the only company to focus solely on government-leased properties. "We believe our singular focus and status as a public company will make us an attractive buyer for owners and developers of government-leased properties, and creates an opportunity for us to become a national consolidator of such properties," the company's latest Securities and Exchange Commission filing states. President and CEO Thomas D. Peschio did not respond to an interview request.

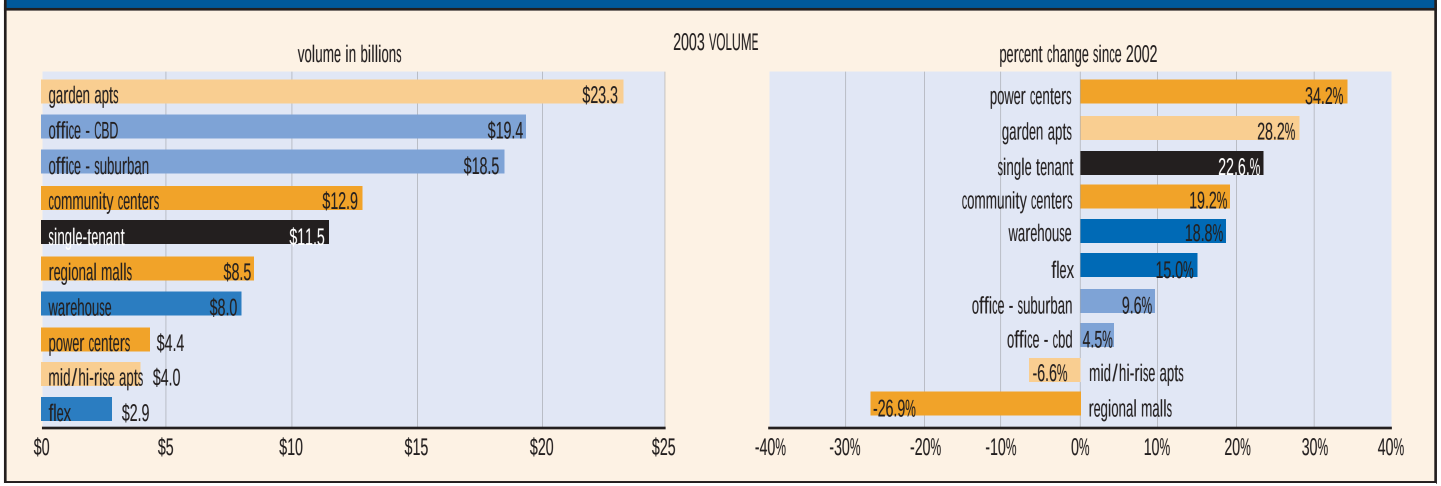
As the filing notes, the focus also poses some inherent risks. Among those is the fact that "because our largest tenant is the US government, our properties may have a higher risk of terrorist attack than similar properties that are leased to non-governmental tenants." In addition, since government leases can be gross, modified gross or net leases, "some of our leases may not provide for a full pass-through to our tenants of increases in property operating costs."

GPP owns five properties totaling 248,848 sf; four are leased to the **Drug Enforcement Administration**, **Social Security Administration**, **Department of Justice**, and **Federal Bureau of Investigation**, while the fifth is leased to **Federal Express Corp.** The company does not intend to acquire any more assets with non-governmental tenants, but it does have a pipeline of eight more properties totaling 486,540 sf. These are leased to **US Border Patrol**, **Immigration & Naturalization Service**, **Veterans Administration**, **Food and Drug Administration**, **Bureau of Public Debt**, and the FBI.

The federal government alone already leases about 23% of its 835 million sf of office space, GPP notes, and "because governments are facing significant budgetary constraints, we expect governmental entities will increasingly lease properties instead of building and owning." It expects "government demand for new office space to grow substantially, particularly in areas such as law enforcement and the judiciary, homeland security, human services and regulatory agencies," it also says. Between 2000 and 2002, it adds, commercial space owned by the US government grew by 0.2%, while leased space grew 7.8%.

2003 Single-Tenant Sales Volume

$11.5 billion of single-tenant properties traded hands in 2003, representing roughly one-tenth of all types of commercial real estate* to sell last year. Here's a look at how single-tenant assets stacked up compared to other property types, as well as how much of an increase in activity 2003 logged over the previous year.*



*Data includes properties and portfolios of $5 million or more.

Source: Real Capital Analytics

RATINGS UPDATE

▸ All ratings of **Winn-Dixie Stores Inc.** were lowered by Moody's Investors Service to B1 from Ba2. According to Moody's, the downgrade is due to its "belief that the recent deterioration in revenue, margins and debt protection measures will persist over at least the medium-term; the challenges in winning back customers and market share from efficient competitors such as Publix and the Wal-Mart supercenter format; and the likelihood that the company needs to carry out a substantial asset rationalization program." The outlook remains negative.

▸ The ratings of **Tenet Healthcare Corp.** were downgraded by Fitch Ratings to B+ from BB. The outlook is negative. "The downgrade reflects continued weak operating performance primarily as it relates to cash," says Fitch. "The company's weakness in earning power is mostly attributed to the company's difficulty in achieving market-level increases in its managed care contracting efforts and continued bad debt exposure driven, in part, by the company's price structure."

▸ Among **Goodyear Tire & Rubber Co.** ratings affirmed by Moody's was its B2 senior unsecured debt. Its outlook remains stable, in light of improved liquidity that will result from an asset-backed term loan as well as "the benefits from the recent labor agreement and the positive trends in North American replacement tire volumes," according to the ratings agency.

▸ Also enjoying an affirmation of its ratings, including its AA senior notes, was **Home Depot**, though Fitch revised its outlook on the home improvement retailer to stable from negative. "The affirmation reflects Home Depot's position as the largest home improvement retailer in the world and a strong financial profile," says Fitch. "The change in the outlook to stable reflects the turnaround in Home Depot's operations over the past few quarters, supported by improvements made to the store environment, as well as the continuing strength of the US housing market."

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nus with the lease term, you had some cash flow and it sheltered your taxes. Then after '86 that all changed—they increased that depreciation to 39 years. So he got out of the game and I came in and I saw that there weren't a lot of people that knew about net-leased deals. My idea was to originate loans; I was a stockbroker and kind of stumbled into it, but there seemed to be a lot of demand for financing for landlords. So I started doing deals, and it's grown ever since.

Q: I imagine you've seen the business change a lot in the time you've been involved.

A: I have. What's changed in the US is there's a lot more retail then when my father was involved; there weren't as many corporations doing it back then. I think for sale-leasebacks the opportunity now is in Europe and elsewhere overseas; I'm talking to a couple of companies in Latin America. The cap rates are much higher, but the key is the creditworthiness, and we're trying to find out what is the creditworthiness of these companies. There's so much competition now in the US—you've got the REITs, you've got the exchange buyers, you've got everybody trying to buy these.

Q: What trends are you seeing today in the 1031 exchange and net-lease marketplace?

A: What's really been a trend out here in California is that apartments have been going up in price dramatically. With apartment units, depending on the city, at $100,000 to $150,000, a lot of people are saying, 'You know what, I want to sell, but to find other apartments in California within the 180 days is pretty tough. And I'm at the age where I want to retire and buy a net-lease deal, where the tenant maintains and pays everything and I don't have any more hassles to deal with.' That's probably the main motivation today; you can't really buy apartments in another state, because you have to maintain them, but with a net-lease property you can pretty much invest anywhere. There's also not a whole lot of supply, because corporations haven't been expanding as fast as they were, so they're not building as many new stores. There's a backlog right now.

Q: What kinds of lenders do you typically work with?

A: It's a unique beast for financing. I think my advantage is I'm doing deals with the same lenders, so I have great relationships with them, and the relationship in the lending business is everything. Which lender depends on what the borrower wants. I deal with CMBS and Wall Street lenders, with banks, with life companies. I explain to clients that first of all, you've got to find a lender who likes the use. If you're financing a Jack in the Box net-lease deal, you've got to find a lender that likes restaurants. Secondly, you've got to find a lender that wants to be in the geographic area where the store is. Thirdly, they've got to like the credit of the tenant. They've got to do net-lease deals; not all lenders do. You've simply got to find a lender that likes the size of the loan that you're dealing in. And you've got to find out what the borrower is looking for; he may be a developer who says, 'I may be selling this in a month. I don't want a prepay.' That narrows the lenders we can utilize.

Q: Any particular kinds of properties you're focused on arranging financing for?

A: I'll look at anything that's net-leased. Last year I did an outlet center in Napa with tenants like Brooks Brothers; each tenant has its own net lease. One focus I'd like to go after is movie theaters; I have a couple of lenders that would like to do some of those. The theaters for a while were out of vogue, because there was an oversupply, but I've heard some people out there say they'd like to do some now.

EXECUTIVE POSTINGS

Recently promoted at **Corporate Office Properties Trust** is **Roger A. Waesche Jr.** Waesche is now EVP and CFO of the Columbia, MD-based REIT, and formerly served as SVP and CFO.