NET LEASE forum

The On-Line Newsletter
from the Editors of
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INDUSTRY UPDATE

New Net-Lease Finance Intermediary Launches

A new intermediary for net-leased property mortgages has been launched by **Commercial Net Lease Realty Services Inc.**, a subsidiary of **Commercial Net Lease Realty Inc.**, the Orlando-based REIT. **NNN 1031 Mortgage Funding** will serve essentially as a referral service, says SVP Jay Bastian, to help connect 1031 exchange investors and others with a variety of kinds of financings for single-tenant, net-leased properties.

"We're trying to aggregate demand in the triple-net lease debt arena," Bastian tells *NET LEASE forum*. CNLR Services sells properties ideal for 1031 exchange replacement. "We've found the biggest hurdle for selling properties was the debt. Most 1031 investors are not necessarily sophisticated real estate investors."

He declined to name the specific lenders that customers may be referred to, except that the parent REIT will provide funds—typically $3 million to $30 million—under a mezzanine loan program for a combined loan-to-value of up to 89.9%.

Other financing programs available through NNN 1031 Mortgage Funding are self-amortizing credit-tenant lease loans of $1 million to $50 million; standard fixed-rate non-recourse loans of $1 million to $50 million placed with CMBS or life company sources; sale-leaseback financing of up to $100 million; a joint venture development program that will fund 100% of project costs from $2 million to $20 million; and a developer equity program that will provide all equity ($5 million or less) necessary to obtain construction financing.

The division's website, www.nnn1031funding.com, went live earlier this month. Bastian reports that within less than a week's time, a dozen visitors had already filled out its online form seeking financing of $2 million or more.

AT DEADLINE

Building materials manufacturer **USG Corp.** has agreed to a 15-year net lease worth $88 million for a new building at 550 W. Adams St. in Chicago, *GlobeSt.com* reports. The company will lease 240,000 sf of the total 470,000 sf as its headquarters. Developer **Fifield Realty Corp.** received $9.75 million of tax increment financing for the $128-million project, which will be built on what is now a parking lot.

With Eckerd Details Announced, Cap Rates Drop, Financing Emerges

After a bit of anticipation and speculation about the details, **JC Penney Co.** of Plano, TX, announced the buyers of its **Eckerd** drug store chain. With Woonsocket, RI-based **CVS Corp.** in line to take Eckerd stores and support facilities in southern states, primarily Florida and Texas, those properties are expected to become much easier to finance and to sell at lower cap rates. Listings have already begun to reflect this, even though the deal isn't expected to close until the end of the second quarter.

As Owen G. Cone, a mortgage banker with **Thomas D. Wood & Co.** in Coral Gables, FL, put it: "There are a lot of moving pieces and I don't think the dust is quite settled." But he does expect that Florida and Texas Eckerd stores will be

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NETLEASE Case Study

The recent sale of an industrial building (above) in Long Island City, NY, wasn't your typical sale-leaseback. But it was a transaction that shows how flexibility can make both buyer and seller a winner.

Scalamandré Silks is renowned for its high-end fabrics, trimmings, carpets and wallcoverings. Founded by Franco and Flora Scalamandré, the family-owned business is steeped in history. The year 1929 was an important one for Franco Scalamandré, originally from an Italian weaving district in Caserta, Italy. He received his US citizenship, married Flora, incorporated the company and made a down payment on a Queens building—today, really four connected buildings at 37-24 24th St. in Long Island City, Queens.

The business has been located there ever since, and is now run by a third

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easier to finance, and with higher LTVs and lower interest rates. Lenders have begun to look at those properties as if they were already backed by the stronger CVS credit, he says, adding that while a few are taking applications under that assumption, most are still reluctant to commit funds until the deal is actually closed. (*See page 4 for more information about ratings actions concerning CVS Corp. and CMBS transactions backed by CVS lease payments.*)

Cap rates for those properties have already dropped as well; while just a few weeks ago one could find Eckerd stores listed at cap rates in the 8% range, they came down virtually overnight and are now in the 7s, even 6.75%. "Cap rates have definitely come down," Cone observes. "I'm seeing them at 7% and even lower than that."

Assuming the deal closes as it was announced, CVS will pay $2.15 million cash for 1,260 stores, three distribution centers in Dallas, Houston and Orlando and Eckerd Health Services, which includes its mail-order and pharmacy-benefits management businesses. The acquisition will put CVS firmly in the No. 1 drug store chain position, with more than 5,000 locations in 36 states. According to **Standard & Poor's Ratings Services**, "The company plans to convert the Eckerd stores to its own brand and store format over the next 12 to 18 months, and to invest $300,000 to $350,000 in each store up front." CVS's biggest rival, **Walgreen Co.,** moves to the No. 2 spot, with 4,336 units.

The other buyer in the deal is the **Jean Coutu Group Inc.**, a retailer based in Longueuil, Quebec that in 1994 bought 221 Brooks drug stores and, in 1995, 30 stores under the Rite Aid banner. Coutu is paying nearly $2.38 million for 1,539 Eckerd stores and support facilities in the Northeast and mid-Atlantic, as well as the Eckerd headquarters in Clearwater, FL. The acquisition pushes the company to the No. 4 spot among US pharmacy retailers, with 2,196 stores. According to the company, the stores it acquires will continue to operate as Eckerds.

Busy First Quarter For 1031 Exchange Options

The first quarter was a strong one for **1031 Exchange Options**, a real estate investment consultancy active in placing investors in tenant-in-common deals. According to the company, which just moved to new and bigger offices in Walnut Creek, CA, to accommodate a staff that has tripled in eight months' time, its first-quarter production grew by 77% over the same quarter in 2003.

During the first quarter of this year, 1031 Exchange Options helped clients buy $78 million of real estate in 63 transactions. It expects to increase its full-year results over those of 2003, anticipating client investments in excess of $750 mil-

▸▸▸ Continued on page 3

RECENT TRANSACTIONS

▸ **Express Scripts Inc.** sold its 233,000-sf office building in East Hanover, NJ and leased back 44,000 sf. The company was represented by **NAI James E. Hanson**; **Preferred Real Estate Investments Inc.** was the buyer.

▸ Five restaurant properties in California and Missouri were purchased by **CRIC Capital LLC** and leased back to **El Torito Restaurants Inc.** and **Acapulco Restaurants Inc.** The companies, which operate Acapulco, El Torito and Casa Gallardo eateries, are subsidiaries of **Real Mex Restaurants Inc.**

▸ **American Financial Realty Trust** purchased six branch properties in Florida and Georgia under its formulated price contract with **Wachovia Bank NA**. A total of $4.84 million was paid for the properties, five of which are vacant, the sixth occupied by **BB&T Corp.** AFRT is in contract to sell one vacant property; the others are being marketed for lease.

▸ A 35,300-sf auto dealership in Knoxville, TN was purchased by **One Liberty Properties Inc.** for $11.4 million. The property is net-leased to CarMax Auto Superstores Inc., a subsidiary of **CarMax Inc.,** which is an obligor under the lease.

▸ **Nationwide Health Properties Inc.** completed the first stage of a sale-leaseback of health-care facilities with **Emeritus Corp.** The closing involved 17 properties for $136 million. Emeritus will operate the facilities under a triple-net master lease.

▸ A 6,050-sf retail property in Buford, GA was leased by **Something Unique Enterprises LLC** under a 10-year triple net with an aggregate value of almost $1.8 million. **Sperry Van Ness** represented owner **Southfund Partners**.

▸ Three megaplex theaters, in Phoenix, Mesa, AZ and Hamilton, NJ, were the subject of a sale-leaseback. **Entertainment Properties Trust** paid $64.2 million for the properties, while seller **American Multi-Cinema Inc.**, subsidiary of **AMC Entertainment Inc.,** continues to operate them under long-term net leases.

▸ **LA-Z-BOY Furniture Galleries** triple-net-leased a 16,119-sf freestanding building in Mission Viejo, CA. **Lee & Associates** represented the tenant, which signed a 15-year lease with an aggregate value of $3.39 million; **Resource Commercial Real Estate** sat in for landlord **Adobe/Avery Parkway LLC**.

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lion. Last year, the company placed clients in more than $300 million of tenant-in-common properties, including the Puente Hills Mall deal, the largest TIC acquisition ever recorded.

"In addition to our significant business growth in production over the company's first quarter last year, we saw a 54% transactional growth rate," founder and president Cary Losson said in a statement. "The average size of our transactions continues to increase, and we are on track for a very productive year."

Non-Traded Inland REIT Sets Date for NYSE Listing

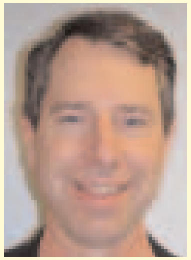
The New York Stock Exchange's listing and compliance committee has green-lighted Oak Brook-IL-based **Inland Real Estate Corp.**'s listing application. The REIT expects to begin trading on the Big Board on June 9. Formed in 1994, it is the first of three publicly registered, non-traded REITs launched under the **Inland Real Estate Group of Cos.** umbrella and the first to seek an exchange listing.

As of March 11, the REIT had 18,032 common stockholders. At the end of last year, it held total assets of $1.28 billion, including 29 single-tenant retail properties totaling 1.3 million leaseable sf, plus 23 community shopping centers totaling 4.7 million sf and 85 neighborhood retail centers totaling 5.6 million sf. Its properties are concentrated primarily in the Midwest.

According to information contained in a filing with the Securities and Exchange Commission, Inland Real Estate Corp. shareholders may have received another mini-tender offer from **Madison Liquidity Investors**, an Overland Park, KS-based company that buys illiquid financial assets. In a letter to shareholders this month, Robert D. Parks, chairman, president and CEO of the Inland REIT, said his company believes the $10 per share offer "is inadequate and [we] urge you to not tender your shares."

"We believe that our shares will trade at a higher price than the price offered by Madison," the letter also states.

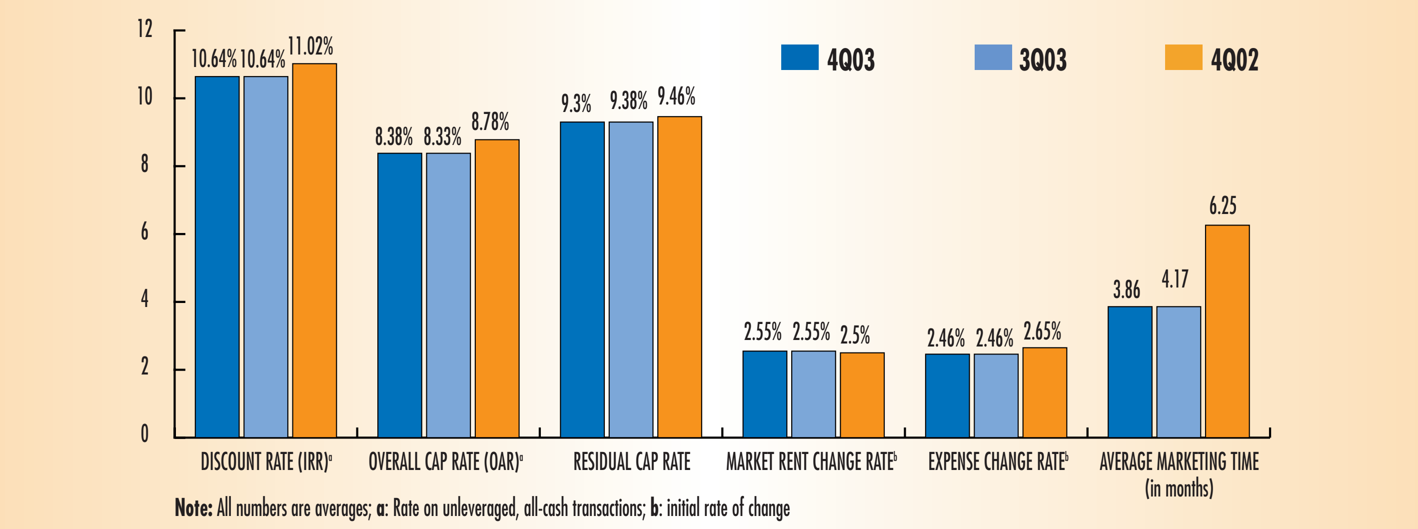
EXECUTIVE MOVES



Brian H. Scott has joined **CB Richard Ellis**' global corporate services group as a senior managing director. An 18-year real estate industry veteran with a specialty in corporate finance, Scott will focus on structuring and executing sale-leasebacks for corporate clients through its newly formed sale-leaseback group. He was most recently a managing director with **Silvermine Finance LLC** and also served in **Jones Lang LaSalle**'s capital markets group.

NATIONAL NET-LEASE MARKET RATE TRENDS 4Q03

Average marketing time for net-leased properties continued to get shorter for yet another quarter, according to results from the fourth quarter 2003 Korpacz Real Estate Investor Survey®.



Note: All numbers are averages; **a:** Rate on unleveraged, all-cash transactions; **b:** initial rate of change

Source: Korpacz Real Estate Investor Survey®

RATINGS UPDATE

▸ **Kohl's Corp.**'s senior notes were affirmed at A by **Fitch Ratings**; the outlook is negative. "The affirmation reflects Kohl's productive store format and solid financial profile weighed against an aggressive expansion program and risks inherent in entering new markets," says Fitch. "The negative outlook reflects Kohl's weaker sales trends beginning in 2003, uncertainty as to the company's ability to return to its historically strong sales growth pace and heightened competitive pressures."

▸ **CVS Corp.** was put on review for a possible downgrade by both **Standard & Poor's Ratings Services** and **Moody's Investors Service**, following the announcement that it will buy part of the **Eckerd** drug store business. "Although the proposed transaction would strengthen CVS's competitive position in the South, the additional debt to fund the acquisition would weaken the company's financial profile," says S&P. "Moreover, the transaction increases the company's business risk, as the Eckerd stores have underperformed the industry for a number of years." Moody's, meanwhile, notes that while "the acquisition of these Eckerd assets is a sound strategic move … the debt financing for the acquisition will significantly increase CVS's adjusted leverage."

S&P and Moody's also placed the ratings of securities from five separate CMBS transactions on CreditWatch with negative implications. "The transactions are collateralized by credit-tenant leases loans secured by properties leased to CVS Corp.," S&P notes. "CVS guarantees the underlying lease payments."

▸ The ratings of **FleetBoston Financial Corp.** were raised and removed from CreditWatch by S&P, following the bank's acquisition by **Bank of America Corp.** "Fleet will benefit from the substantial financial and managerial resources available from BofA," which has an A+ rating and a positive outlook, says S&P. "The ratings of BofA are based on its premier consumer and commercial banking franchise that extends from coast to coast, complemented by corporate and investment banking, credit cards and asset management businesses."

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generation, brothers and co-presidents Robert and Mark Bitter, as well as their parents, still involved on a part-time basis. But a lot has changed since 1929, and the company's current leadership has struggled for years to reconcile its desire to maintain ties with their Long Island City building with the need for a modern manufacturing facility that will maintain its famed quality of product as well as financial competitiveness. A very flexible sale-leaseback, brokered by local firm **Greiner-Maltz** and purchased by Manhattan-based investor **Time Equities Inc.**, proved to be the answer.

"We've talked about it literally for over 20 years," says Robert Bitter. "We kept delaying the issue, putting it off and working hard to make things happen to be able to stay here." But it's expensive and complicated to do business in New York, and the company needed a more appropriate space to create its product, so eventually the Bitters decided something simply had to be done: Scalamandré needed to move the manufacturing side of the business to "an area where we knew it would survive for the next 15 to 20 years."

"It was very risky to stay here in an inefficient layout," Bitter continues. "We love the building, but for our kind of work, a single-level, modern, temperature-controlled facility was critical. We were not able to expand our manufacturing in our current facility without a huge cost. There's a lot of time and money that goes into maintaining the building, and not investing in the machinery we need to compete with China, India and other developing nations would be a big mistake. We are obliged to keep investing in new technologies to stay competitive."

"It's a very difficult, emotional decision," observes Greiner-Maltz senior director Decio Baio. "They're attached to the facility. Robert and Mark Bitter basically grew up in this facility as little kids. This is part of their home and their heritage."

After ultimately making the decision to sell the building, the Bitters faced another challenge: finding a buyer who would afford them the flexibility they needed to move most dying and weaving operations to a new facility in Gaffney, SC, in phases, but also to ultimately maintain a portion of the building for printing, trimming and studio functions. They turned down several purchase offers that would have required them to vacate immediately until they found Time Equities, which agreed to buy the building for $7.15 million and let Scalamandré lease back the entire 110,000 sf in the short term but vacate parts of the space in phases. Ultimately, Scalamandré expects to continue to use up to 50,000 sf for the functions it is keeping in Long Island City; portions of the building have been leased back for the next 10 years.

"Economically, it didn't pay for them to continue to carry the entire property. They're better off selling it, getting some cash out and leasing back what space they need. They're not real estate developers, so they didn't want to go into spending money on the property. Time Equities, that's their business," Baio says. "They wanted a structure where they have the option to move out as they wish, so they wound up with the best of both worlds. And so did Time Equities, because instead of buying a vacant building, they bought a building with an occupant and immediate rent."

Indeed, Bitter says they looked hard for an investor who would be respectful of the company's craft and the family's ties with the building, as well as the need for flexibility as they sift through 75 years of archives. "That was important—to find a partner that would allow us flexibility to move out in a reasonable period of time," he says. "We needed time to do that; we're approaching this in phases. And that's the beauty of this sale."

For its part, Time Equities was drawn to the Long Island City area, where it did another sale-leaseback several years ago, and the ability to renovate portions of the building over time to reposition them for light manufacturing/office users that might be attracted to the loft-like space. "Time Equities is nimble enough. We bought all cash, so we didn't have to take on financing," says acquisitions asset manager Jeff Rosenblum. "It's definitely not your typical sale-leaseback transaction, where you lock it away with a 15-year, 20-year lease."

"I sensed in the negotiations that they viewed the building as their home," Rosenblum adds. "That's why they're going to keep a portion of it. They're connected to it; it's more than bricks and mortar."