

Perspective in REAL ESTATE

A FEATURE EXAMINING THE ROLE OF PRIVATE EQUITY IN THE REAL ESTATE SECTOR.

M&A activity is up in the REIT sector across various segments.



The FTSE NAREIT All REIT Index is outperforming on a year-to-date basis, although it took a slight dip in April. Some REITs are faring better than others, with apartment REITs in New York City facing challenges because of both an oversupply of units and increased competition from new construction, *UrbanLand* magazine reports. Building valuations are high, and some buyers are enjoying more

profits by purchasing companies rather than their underlying real estate assets, according to *REITCafe*.

A number of M&A deals were announced in April and May. Mortgage investor Annaly Capital Management, Inc. will buy Hatteras Financial Corp. in a cash-and-stock deal valued at \$1.5 billion and expected to close by the end of Q3 2016. Both companies are structured as REITs and have nearly 90 percent of their assets in mortgage-backed securities. The deal will help Annaly diversify and expand its adjustable-rate holdings, *The Wall Street Journal* reports.

Office REIT Cousins Properties will acquire Parkway Properties in a deal valued at \$1.95 billion. The deal will create two independent office REITs with differentiated strategies as their combined Houston assets are spun off into a new publicly traded REIT, HoustonCo, according to a news release.

Earlier this month, Northstar Asset Management Group, Inc., along with its former parent company NorthStar Realty Finance Corp., and Colony Capital Inc. agreed to merge their assets into a single REIT worth about \$58 billion. The companies anticipate approximately \$115 million in annual cost savings, according to *The Wall Street Journal*.

Apple Hospitality REIT will merge with public non-listed Apple REIT Ten, Inc. to create one of the largest select-service lodging REITs in the industry in a \$1.3 billion deal. The combined portfolio will consist of 234 hotels in 33 U.S. states, including Hilton and Marriott branded select-service hotels—mid-tier hotel properties offering some services and amenities of full-service properties—according to a press release. Apple Hospitality has stayed active over the last year, according to *REIT.com*, selling 19 properties and purchasing seven hotels in 2015. Apple Hospitality CEO Justin Knight told *REIT.com* that with strong market fundamentals, urgency to merge in the hospitality REIT segment has waned and he described both the buy and sell sides as “disciplined” in their search for strategic deals.

The JBG Companies, a Maryland-based real estate firm, is reportedly in talks to acquire New York REIT, a publicly traded firm with a portfolio of Manhattan assets, after New York’s largest office landlord, SL Green Realty Corp., pulled back from a deal last fall. According to the *Real Deal*, if this goes ahead, it would be the latest in a series of deals involving privately held real estate players acquiring publicly traded REITs.

FUTURE PERSPECTIVES: WHAT TO EXPECT FROM REITS IN Q3-Q4

M&A activity in the REIT sector may prove to be robust in the second half of 2016. While the past seven years have seen a 75 percent decline in REIT deal flow compared to the seven years prior—\$14.51 billion average annual M&A volume from 2008 to 2015 versus \$27.41 billion from 1998 to 2007, according to research from Green Street Advisors—this year may see an end to the ease in deal volume. Heightened pressures from activist investors in the REIT space will increasingly cause management teams to think through operational inefficiencies and evaluate consolidation or spin-off solutions, reports *National Real Estate Investor*. Additionally, *Forbes* notes that there are currently too many REITs in the market, with more than 1,100 public and private REITs in the U.S., according to the IRS. Should market conditions remain favorable and fears around the impacts of further interest rate hikes diminish, there will likely be a steady stream, if not of growth, of real estate deals and transactions in the remainder of the year.



April also saw the year's first REIT IPO, with casino resorts investor MGM Growth Properties LLC raising \$1.05 billion. According to Dealogic, this offering was the first by a U.S.-listed company to raise more than \$1 billion since last October, when First Data raised \$2.8 billion—and could signal a thaw in the IPO market, *The Wall Street Journal* reports.

REIT segments are performing differently in the M&A market, but overall fundamentals seem strong. While no segment is in the midst of a merger frenzy, there are deals to be had in the marketplace for private equity firms with an interest in the space, if they can beat out—or partner with—a strategic investor.

Sources: Dealogic, Forbes, National Real Estate Investor, REIT.com, REITCafe, UrbanLand, The Wall Street Journal

PErspective in Real Estate is a feature examining the role of private equity in the real estate industry.

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