LaSalle Investment Management (Securities)

Recently, ***Geoffrey Dobrmann****, publisher and editor-in-chief of* The Institutional Real Estate Letter – North America, *spoke with* ***Stanley Kraska Jr., Keith Pauley, George Noon, Ernst-Jan de Leeuw*** *and* ***Todd Canter,*** *of LaSalle Investment Management (Securities). The following is an excerpt of that conversation.*

GLOBAL REAL ESTATE SECURITIES TEAM

Stanley Kraska Jr. is a managing director of LaSalle Investment Management (Securities) with more than 20 years real estate experience. His responsibilities include portfolio management and overall group management. He is a member of the the Global Securities Advisory Committee, is the co-chair of the Portfolio Management Oversight Committee, and a member of LaSalle Investment Management Global Management Committee.

Keith Pauley is a managing director and chief investment officer of LaSalle Investment Management (Securities) with more than 20 years of investment experience. His responsibilities include portfolio management and oversight of securities research and trading activities in North America. He is a member of the Global Securities Advisory Committee and is co-chair of the Portfolio Management Oversight Committee.

George Noon is a managing director of LaSalle Investment Management (Securities) with more than 20 years of investment experience. His responsibilities include portfolio management and oversight of research and trading activities in Asia / Pacific. He is a member of the the Global Securities Advisory Committee and the Portfolio Management Oversight Committee.

Ernst-Jan de Leeuw is a managing director with LaSalle Investment Management Securities B.V. with over 13 years of investment experience. He is a member of the Global Securities Advisory Committee and Portfolio Management Oversight Committee. His responsibilities include portfolio management and oversight of research and trading activities in Europe.

Todd A. Canter is the global strategist and CEO of Asia Pacific for LaSalle Investment Management (Securities) with over 14 years of investment experience. He is a member of the Global Securities Advisory Committee. His primary responsibilities global product management and strategy, and oversight of the Asia Pacific securities operation.

CORPORATE OVERVIEW

LaSalle Investment Management is a leading global real estate investment manager, with approximately $37.5 billion of assets under management. LaSalle is a member of the Jones Lang LaSalle group (NYSE: JLL).

CORPORATE CONTACT

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How have public Global Real Estate Securities (GRES) fared during the credit crisis and economic downturn?

Kraska: At first glance, publicly traded GRES, like all equities and corporate bonds, fared poorly. They posted returns of –55 to –60 percent from Sept. 30, 2008, to the bottom on March 9, 2009. Even after a 100 percent rebound up until today [9/30/09], GRES are still down 33 percent from May 2008 levels, and 45 to 50 percent from their 2007 highs. However, just looking at returns can be misleading. By considering other factors, we can see that GRES actually fared very well during the worse credit crisis in any of our lifetimes.

What factors are those?

Kraska: Even after a steep correction in real estate values, public companies still have equity value — unlike many of the more highly leveraged private operators. The relatively low leverage maintained by the vast majority of companies served them well, and there have been very few bankruptcies. During the crisis, management teams were securing balance sheets, managing assets, and cutting costs when necessary. In addition, GRES provided liquidity even at the depth of the crisis. Investors could exit (albeit at much reduced prices) or enter the sector on a daily basis. For all intents and purposes, GRES were the only working equity markets in the real estate sector. Public real estate companies raised more than $40 billion in over 100 separate new equity offerings in 2009. Public buyers saw an opportunity and acted.

Have there been significant differences in performance by market or property type? Public vs. Private?

Kraska: Generally, there was nowhere to hide during the crisis. Stocks in all countries and all property types were hit hard. Public returns were much worse than stated private returns, particularly in the United States. Of course, the private returns are based on appraisals, which in the best of times, lead to a lagging indication of value. In times when there are few to no "comparable sales" for appraisers to rely on, the private returns are even more difficult to determine. We have recently seen private returns turn sharply negative, and they are starting to catch up with public markets.

What role will public real estate securities play in the real estate industry going forward?

Pauley: We think public real estate securities are positioned to play a major role, similar to that which occurred in the United States in the mid 1990s, when many private owners were forced to turn to the public markets to access capital and the public market cap increased by more than $125 billion. We expect today's ongoing deleveraging process to create compelling investment opportunities for investors with access to capital. These conditions should work to the advantage of the public owners of real estate. The public markets are greedy and they don't hold a grudge. There was panic and gridlock in the financial and capital markets in the final months of 2008, but since the first of the year, there have been more than 100 equity offerings, by over 90 public real estate companies around the world. More than $40 billion has been raised. We expect the better managed, better capitalized public companies to aggressively take advantage of buying opportunities arising from the turmoil.

Will we continue to see high levels of equity issuance?

Pauley: We expect the existing public real estate companies to increasingly rely on equity to finance their growth. While public real estate companies are in a strong capital position relative to other investors, the credit market crisis is likely to have an enduring impact on investor and management perceptions of prudent leverage levels, and it is likely that the better-managed companies will want to continue to lower their leverage over time. We think investors will continue to have a healthy appetite, given the investment opportunities these companies are likely to have over the next few years.

Will we see a pick-up in public real estate securities IPOs?

Pauley: With the rebound in their stock prices, public real estate company valuation levels are very attractive relative to private market clearing prices. Additionally, we believe the advantages of the public real estate securities vehicle in terms of liquidity, financial flexibility, alignment of interests and transparency will be better appreciated by both operators and investors in the wake of the problems they are experiencing in their private investments and private investment vehicles. We are starting to see and hear about new public real estate companies, and we expect that there will be a number of public real estate company IPOs over the next couple of years.

Public real estate securities have had unusually high volatility and high correlations with financials over the past year and particularly during the acute periods of the market downturn. Do you expect these trends to persist?

Canter: Public real estate securities have been positioned to offer high current yields and diversification relative to other asset classes. Yet over the past 18 months, we have seen dividend reductions, significant share price declines and high correlations with broader equity markets. Investors have rightfully wondered whether or not the broader public real estate securities story is intact. We believe that much of this is due to the unprecedented severity of the credit collapse and economic downturn. The high market correlation, dividend cuts and volatility are inconsistent with the long-term history of public real estate securities. As the credit crisis abates, we believe that the sector will again trade on its fundamentals: supply, demand and, ultimately, cash flow growth. We also believe that dividend yields (while still relatively high at 5 percent) will remain stable and payouts will grow along with revenue. Over the longer term, we expect that correlations will trend in line with historical levels, and that the diversification story will once again be realized.

What will the successful GRES company look like in the future?

Noon: It will be important for the successful companies to recognize that they are operating in a globally competitive capital market environment, where cost of capital is a major determinant of success. Those with the lowest cost of capital, in a business with significant capital requirements, will be amongst the ultimate winners. After what we saw in global capital markets in 2008 and early in 2009, it would be nearly impossible for the successful company to overstate the importance of having financial flexibility and access to capital. Thus, we would expect to see almost every company trying to position themselves to have the broadest access to capital from a variety of sources.

de Leeuw: The successful global real estate companies will own high-quality assets that provide durable cash flows. They will have financial flexibility with access to capital and, very importantly, they will have management teams that can add value to the firm in excess of their cost. These companies will also be liquid, transparent, tax efficient and have strong shareholder-friendly corporate governance structures.

Noon: With the recent capital market crisis fresh in market participants' minds, we expect companies with above-average leverage ratios to continue to take advantage of every opportunity to meaningfully cut borrowing to ensure their corporate survival through any future market conditions. Additionally, we would expect that as attractive acquisition opportunities begin to become available to the more modestly leveraged companies, more companies will try to position themselves similarly in order to benefit as well.

de Leeuw: The most successful real estate companies will also have value-creating management teams. Management will need to have a level of core competencies that enables them to add enough value to the company to, at the minimum, offset the amount of corporate overhead that they incur. This can be accomplished through their ability to add value to the properties, through either asset or property management well in excess of their peers, or through their ability to add value to the corporation as a whole through some other competency such as development, redevelopment, or successful capital allocation strategies. This way the entity can truly be valued in excess of the NAV of the assets alone. Without some value creation capabilities the entity will likely trade at a discount to its NAV, making the entity less compelling as a going concern and much less likely to have the access to capital that was mentioned earlier.

What special skills does LaSalle Investment Management (Securities) bring to investing in GRES?

Kraska: Since 1985, we have made a significant commitment to being a leader in investment management of real estate securities on behalf of investors around the globe. We believe we have developed certain competitive advantages that enable us to provide solid performance for our clients. These advantages include a global platform, an experienced team and a time-tested methodology.

Pauley: As part of LaSalle Investment Management and Jones Lang LaSalle, we have unmatched insights into real estate markets, trends and cycles around the globe. We use the proprietary market forecasts done by the LaSalle Investment Management research group. In addition, we have access to real-time, local market knowledge from over 21,000 real estate professionals across the firm in over 180 markets in 60 countries. The firm is active in all facets of real estate in all markets where public real estate companies are present.

Canter: Within our offices in Baltimore, Amsterdam and Hong Kong, we have a strong and experienced team of highly skilled real estate securities investment professionals. Our portfolio managers typically have 20 years' experience in the industry, and our team of senior securities analysts has an average industry experience of nine years. We work together on a coordinated and comprehensive portfolio construction process. Our team has followed the vast majority of the public real estate companies since their IPOs and in some cases since they were private entities.

Kraska: Finally, we have developed a globally consistent approach to company and region selection that identifies value. Our methodology combines top-down market research with bottom-up company analysis and serves as a single, unified valuation metric across all regions and sectors. We first developed our valuation model — a dividend discount model customized for valuing real estate securities — over 20 years ago. It has served us and our investors well.❖