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# A Winning Strategy

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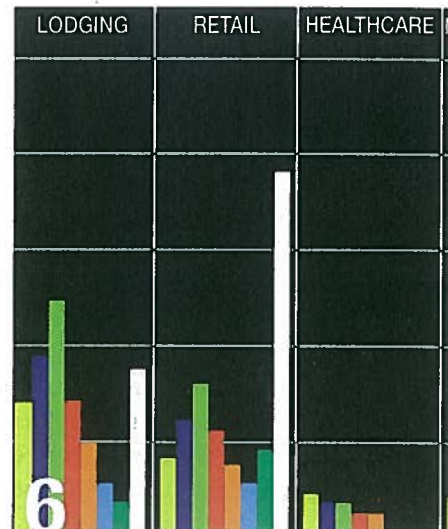
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AMB's Hamid Moghadam is positioning his company for both the short and long term, making cutbacks but retaining the flexibility to access the resources he needs when the time is right to pursue opportunities again.

### Visionary: Top Honors

In October, the Commercial Real Estate (CREW) Network honored 20 Under 40 achieving women during its annual Convention & Marketplace. This diverse array of women offer their insights, drawing on their challenges and successes.

### Financial Report: Net Benefits

As the commercial property investment market cratered over the last year and a half, the sale-leaseback sector was among the hardest-hit areas of the industry. But a recent spate of big deals may be signaling a comeback for these single-tenant transactions.

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[Feature]



# A Winning Strategy

By Brad Berton

AMB's Hamid Moghadam Maintains a Solid Defense and a Potent Offense

You might think a severe pullback in user demand would leave a lot of real estate owner-operator executives with plenty of idle time on their hands to contemplate better days ahead. But don't tell Hamid Moghadam.

**S**ure, the affable chairman & CEO of globally active industrial REIT AMB Property Corp. is always—always—thinking about positioning his highly regarded company for optimal profitability in future years. But amid the slackest space demand he has seen in his long and productive career, Moghadam in recent quarters has been about as busy as ever responding to the stock market crash, capital markets disruption and general economic malaise.

In other words, as the 53-year-old executive likes to say, “A winning strategy requires a solid defense as well as a potent offense.”

Indeed, when trade-centric AMB's share price tanked, debt markets turned skittish and tenant activity disintegrated, Moghadam's team responded decisively with multiple strategies aimed at deleveraging the balance sheet, reducing cost structure and retaining tenants.

Even those decisions portrayed Moghadam's emphasis on positioning the company for brighter times: For instance, while the AMB brain trust ultimately opted to lay off a third of the global workforce, they were determined to retain key development specialists who would serve in other capacities for the next year or two or three. They also declined to shut down regional operations that are likely to become important to the company's growth down the road. Nor is the company bowing to tenant's-market temptations to compete through long-term leases at today's depressed effective rental rates.

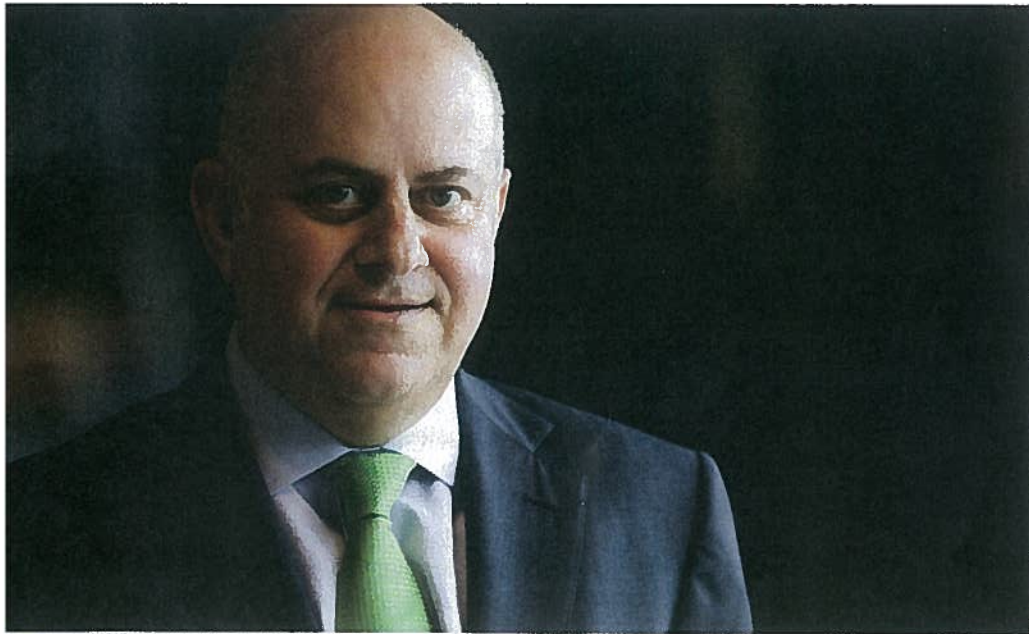
And predictably, Moghadam is also busy talking with AMB's institutional-fund investors about excellent investment opportunities likely to arise amid the property distress seen around the globe.

“I know it's easier said than done, but you don't want to focus exclusively on trying to get through the downturn,” observed Moghadam, who works from a standard cubicle in AMB's bayfront headquarters atop San Francisco's redeveloped Pier 1.

At the same time, Moghadam and other top AMB officials felt it was important to devise a clear strategy for getting through the downturn and to inform the troops of those plans in concise terms. As global economic activity plunged amid the financial turmoil a year ago, Moghadam and other AMB brain-trusters divided their strategic responses into four primary areas of emphasis.

Along with new measures aimed at deleveraging AMB's balance sheet and paring general and administrative costs by 30 percent, the Moghadam-led team intensified ongoing efforts to lease operating and development space amid a tenant-demand vacuum. Meanwhile, senior management started exploring prospects for positioning the company to take advantage of promising investment opportunities as the world's shell-shocked economies start recovering.

A tenet underlying the strategic response to the economic turmoil was that, at least for the coming year or so, maximizing earnings would take something of a strategic back seat to optimizing the balance sheet, Moghadam explained. And as quite a few other REIT execs can attest, deleveraging strategies alone have entailed a heck of a lot of activity in recent quarters, such as extending and retiring debt, securing new credit lines, issuing new stock, adjusting dividend distributions and disposing of non-strategic assets.



**“Markets do turn around, and you need to leave yourself the ability to take advantage of opportunities [to augment revenues when market rates rise].”**

totaling approximately \$371 million during the subsequent two quarters presumably influenced the dividend strategies as well.

And starting in the first quarter, AMB pegged the quarterly payout to the minimum required to maintain AMB's REIT tax status, mirroring the company's 2009 taxable income guidance of \$1.12 a share. The company can always pay special distributions when a profitable event occurs.

The distribution cuts helped AMB retain \$53 million in cash during the fourth quarter and an expected \$98 million over the course of 2009.

The multi-tiered strategies improved AMB's liquidity and helped reduce balance-sheet leverage to about 44 percent, based on the portfolio's estimated value at mid-year. And Moghadam sees the ratio falling further as values recover; his long-term preference is in the 35 to 40 percent range.

Perhaps more important, AMB now has plenty of cash and credit available to cover scheduled debt maturities staggered over the coming three or four years and to fund construction completions for developments already well under way when tenant activity declined. “Now we don't have to worry about (meeting) maturities at least through 2013,” Moghadam related.

REIT specialty securities analyst Green Street Advisors likewise concluded that AMB's multi-tiered financial strategy “results in significant improvement to the balance sheet and a far more flexible liquidity position.”

Meanwhile, the Moghadam team's troops in the field have managed to consummate quite a few sizable lease transactions even amid depressed tenant demand. And reflecting AMB's presence in Asia and Europe in addition to North America, ranking among its biggest deals over the summer were transactions in Guadalajara, Madrid, Paris, Amsterdam, Nagoya and Hamburg.

AMB's portfolio—much of it owned jointly with the company's investment funds and other advisory clients—has grown to roughly 157 million square feet in 48 markets in 14 countries, most of it high-throughput distribution, designed for rapid inbound and outbound goods movement. It is nearly all located in relatively supply-constrained infill submarkets of trade-driven metro areas.

Accordingly, the current global recession, which has had an unusually dramatic impact on trade activity, has not exactly been a boon for AMB's trade-driven property portfolio. To wit, occupancies are in the low 90s compared to the company's historic average of around 95 percent. And reflecting lowered market rents, same-store net operating income fell more than 4 percent in the second quarter alone.

Nevertheless, AMB's domestic occupancy rate is outperforming the national average by about 350 basis points, an advantage the company has held in previous down cycles. Indeed, Moghadam's multiple-cycle experience, stretching beyond a quarter century, can only help when markets sour so rapidly.

That experience also helps explain the focused, trade-dependent portfolio strategy Moghadam believes will continue paying major dividends over the long term. The son of an Iranian real estate developer, Moghadam earned his engineering masters degree at MIT and his MBA from Stanford before co-founding AMB in his mid-20s in the early '80s. The “A” (Doug Abbey) and “B” (Bob Burke) of AMB, Moghadam's initial partners in predecessor investment manager AMB Realty Advisors, are no longer active officers of the company (although Burke still serves on its board).

In addition to Olinger (who joined AMB from Oracle Corp.), Moghadam's senior colleagues today include industry veterans such as Europe/Asia president Guy Jaquier (formerly of CalPERS), Americas president Eugene Reilly (Cabot Properties) and AMB Capital Partners president John Roberts (Ameritech Corp.).

As the team starts thinking about new opportunities over the coming couple of years, the expertise of leasing and marketing staffers out in the decentralized company's field offices is coming to the more immediate forefront. Although AMB pulled the near-term plug on many projects in the works once demand diminished, the company and its investment partners already had a considerable pipeline under way.

In fact, as of mid-year, staffers were charged with conducting some 10 million square feet of occupancy transactions in order to bring properties under development worldwide up to 90 percent occupancy by the end of 2010.

The word from the CEO's office is to avoid *(continued on page 26)*

## Global Perspective

Amid generally awful market conditions around the planet, recovery timetables are not likely to coincide among AMB Property Corp.'s chosen markets. CFO Tom Olinger's general characterization of what to expect in most industrial property markets, at least into early 2010: negative absorption, higher vacancies, declining rents and rising concessions.

A noteworthy exception is China, where Olinger and chairman & CEO Hamid Moghadam observe that continued internal economic growth is limiting the negative effects of slowed exports. Moghadam is likewise optimistic about near-term prospects in Brazil, where an emerging middle class is enjoying the benefits of a diversifying and modernizing economy. (AMB formed a strategic alliance with regional firm Cyrela Commercial Properties to pursue Brazilian developments and investments.)

In the United States, industrial markets mostly appear to be at or near cyclical troughs, and fundamentals in AMB's chosen markets should start recovering within a couple of calendar quarters, Moghadam suggested. Continental Western Europe, which has not seen user demand dive quite as dramatically as was the case in the United States and United Kingdom, should also see better days in short order, he added.

AMB intends to eventually operate in Eastern Europe as well, but management has decided to wait for economic recovery before setting up shop, probably in Poland initially.

Like so many other international operators, AMB had targeted India as an apparently solid expansion opportunity a couple of years back. However, after coming close to closing a handful of deals there, higher-ups determined the considerable challenges of sourcing development sites outweighed profit-producing prospects, the CEO explained.

Moghadam is even optimistic about longer-term prospects in Mexico, which has certainly experienced its share of disinvestment and exchange-rate issues—not to mention high-profile narcotics-related violence. Its favorable location and cost structures should attract more activity long term as transportation costs take more precedence.

The varying regional recovery prospects notwithstanding, Moghadam and his teammates are clearly committed to casting their lots with global trade growth, which will always have its ups and downs but will almost certainly continue outpacing general economic expansion over the long haul.

While the near-term trade slump has clearly hampered AMB's financial performance, Moghadam remains confident trade growth will pick up its usual pace as the world continues to pull out of recession. And in fact trade flows and container traffic are already starting to pick up from the recessionary trough, Moghadam noted.

It also helps recovery prospects that inventories of goods generally were already at historic lows before the recession deepened, and have further diminished in recent months. As recovery prompts more production to boost depleted inventories, demand for AMB's warehousing and distribution space will follow.

As AMB's reliably stable stock price quickly fell from more than \$50 to less than \$10 at its low point, the company's balance sheet consequentially carried more leverage than Wall Street prefers. In fact before the Street's rapid retreat, AMB boasted one of the soundest balance sheets in the REIT world, with the company's debt-to-asset ratio hovering around 37 percent.

And as summer turned to fall, the global portfolio's same-store rents were actually up better than 3 percent over year-earlier levels, and overall occupancy was a solid 95 percent, Moghadam recalled. But with the decline in property values and stock prices, AMB's leverage level necessarily expanded despite the fact that its debt-coverage ratios were pretty much sterling.

With so many lenders sticking to ultra-conservative terms, reducing near-term debt maturities logically became a top deleveraging priority. And during a busy first half of this year alone, Moghadam, CFO Tom Olinger and teammates forged debt repayment, repurchase and extension arrangements totaling more than \$1 billion.

The company further firmed the balance sheet with \$553 million in net new equity via a 47.4 million-share common stock offering. While of course management and existing shareholders prefer to sell additional equity at peak pricing, AMB found it necessary to price the new shares at a historically low \$12.15 each. The REIT's only other public offering since its 1997 IPO was when business was still brisk in early 2007—hence the \$59 share price.

AMB also brought in capital by selling assets primarily considered non-strategic, amounting to nearly \$600 million as of July 31 (about evenly divided between the United States and offshore) and including the \$125 million sale of the Park One property adjacent to Los Angeles International Airport.

A key consideration entailed identifying assets that would command attractive prices even amid generally declining values but that also had minimal strategic ties to AMB's portfolios. For instance, the gain on the sale of the LAX property—which the buyer had eyed strategically for years—came to more than \$48 million.

That's the Moghadam team's long-term approach coming into play amid its near-term strategies. "We didn't want to undo hard work from our platforms around the world" by selling key pieces of strategically developed local portfolios. AMB indeed managed to "preserve every important global platform," he continued. "We didn't shut down any divisions; we didn't exit any strategic markets."

Management in fact decided over the summer that given AMB's capital-raising and other balance-sheet-boosting successes—not to mention generally deflated prices—it made more sense to hold rather than sell additional properties that had been listed, Moghadam explained.

Some relatively simple adjustments to AMB's dividend distributions likewise improved liquidity amid lowered earnings by preserving cash.

As dividends paid during last year's first three quarters were sufficient to maintain the company's REIT tax status for the entire year, management opted to suspend distributions for the fourth quarter. Fairly hefty non-cash impairment charges (mostly reflecting asset devaluations)

# Feature

## A Winning Strategy

filling vacancies by encumbering properties with current market rents on a long-term basis. Instead Moghadam's general near-term strategy for leasing available space amid the demand void (and still-falling rents) is to remain aggressive on short-term rates only.

AMB has the financial heft to continue attracting tenants without giving away the long-term store, the CEO suggested. "You're shooting yourself in the foot if you do that, and we don't have to," Moghadam stressed. "Markets do turn around, and you need to leave yourself the ability to take advantage of opportunities" to augment revenues when market rates rise.

Moghadam's view is that a good chunk of today's demand decline represents deals delayed for a few years, until economic activity recovers. He believes demand (and in turn effective rental rates) will recover sharply—although it probably won't match the latest peak period.

Accordingly, AMB meanwhile will match bargain near-term rates only if long-term deals include decent bumps after two, three or possibly four years at the most, Moghadam elaborated. And with tenants so scarce these days, AMB is logically willing to make more aggressive offers with renewals than for newly developed facilities.

Value-adding prospects should also offer the REIT and its investment partners opportunities for profitable growth over the next few years. Moghadam, for his part, anticipates a decent flow of opportunities to pick up properties in AMB's markets at below replacement cost, allowing for longer-term value creation through superior management and enlightened capital improvements.

But the product and market focus will not change as AMB's investment partners pursue new deals. The team intends to continue expanding by acquiring and developing strategically located industrial assets in supply-restricted, trade-driven markets expected to grow over the long term.

In contrast to some observers, Moghadam also remains skeptical that vulture types will be able to generate high returns purchasing and resolving bulk packages of distressed debt and related assets this time around, especially in the relatively stable industrial sector.

Particularly in AMB's product category, much of today's financial distress reflects debt maturing in a crunched credit environment, rather than inability to meet mortgage obligations via rental revenues, he elaborated, adding that heavy competition driven by the huge amount of "organized" capital poised to jump on distress-related opportunities should keep yields in check.

The CEO believes the AMB team oversees, and will continue sponsoring, some of the industry's most promising vehicles for capitalizing on industrial real estate investment opportunities ahead, with access to attractively priced capital and a reputation for treating investors fairly and honestly.

Indeed, anyone seeking global investment expertise in the industrial sector seems bound to at least take a look at what AMB has to offer. "If you want to deploy capital on a global scale in our sector, you have few choices," Moghadam concluded. "And probably fewer going forward." **CPE**

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