CHARACTERISTICS OF A-REIT PRIVATE PLACEMENTS DURING THE GLOBAL FINANCIAL CRISIS

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ABSTRACT
The study investigates a variety of characteristics surrounding Australian Real Estate Investment Trust (A-REIT) private placements with a dataset of A-REIT private placements from July 2006 to June 2011. The private placement of equity securities raised over A$10.4 billion for A-REITs during this period of which nearly A$7.3 billion was raised after the December 2007 Centro Properties liquidity problem announcements and the subsequent global financial crisis, with most of this capital raised during 2008 and 2009. The size and speed of the capital raising continues to suggest that A-REITs are regarded highly by the investment community. Additionally, while the general finance literature suggests that existing shareholders do not fare badly from private placements offered to subscribers issued at a discount, this is the first Australian REIT study to report similar findings.

Keywords: private placement, equity capital, A-REITs

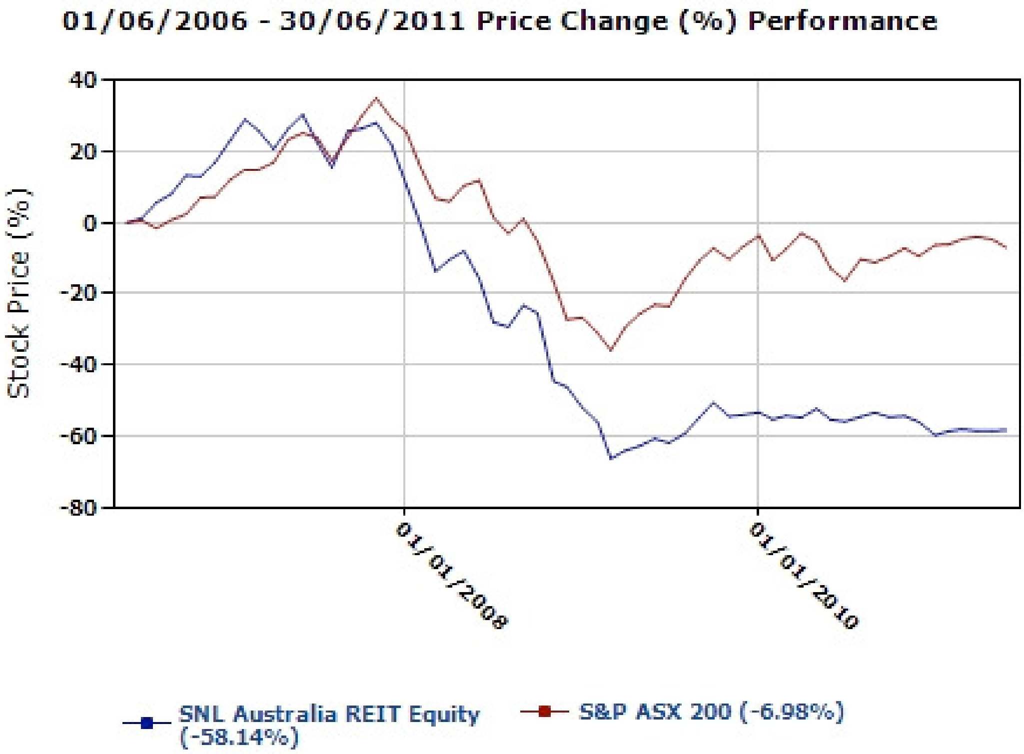
INTRODUCTION
The capital raising activities of firms is an important issue for management. A good deal has been written about the initial public offering (IPO) activities of Australian Real Estate Investment Trusts (A-REITs) (for example Dimovski and Brooks 2006 and Dimovski 2010). More recently Dimovski (2011) has documented some of the characteristics of A-REIT rights issues. Rights issues are equity issues to existing unit holders (subsequent to the IPO) in proportion to the number of units they already hold in the entity.

The main purpose of this paper is to report some of the characteristics of A-REIT private placements. Placements are generally made to larger institutional investors including insurance companies, investment banks and pension funds. Such placements are a relatively quick way (often arranged in one or two days) of raising significant sums of money from a few institutions. The issuing company does not need to provide a disclosure document or prospectus since such placements are usually to sophisticated investors. Although many placements are underwritten, they do not need to be.

The Australian Stock Exchange (ASX) listing rules 7.1 and 7.2 broadly restrict listed entities making placements of more than 15% of the amount of capital that an entity can issue privately in any one year without the approval of shareholders. Even though listed entities can do this, existing shareholders often do not like private placements because they reduce the proportional ownership of the existing shareholders, as well as their voting power. In addition, existing shareholders may not like the private placement price to be at a price below the current market price since this may encourage a reduction in the value of that current market price to the placement price. On the other hand, private placements often need to be made at a discount to encourage institutional investors to invest. Because the announcement of a placement may affect the market price, listed entities often seek ASX approval to suspend trading in the shares or units until the placement is finalized (generally only a day or two).

In addition, this paper explores whether the broad finding in the finance literature that suggests that private placements show a positive wealth effect to existing shareholders applies to A-REIT private placements (see for example Wruck 1989, Hertzel and Smith 1993, Krishnamurthy, Spindt, Subramanium and Woidtke 2005 and Wruck and Wu 2009). That is, that while new shareholders are sold shares at a discount to the market price, the market price recovers and perhaps advances on the previous closing price to record short term profits for the existing shareholders at a point of time (as well as for the subscribers). While this paper does not find significant positive wealth effects for the existing shareholders, it does report that the existing owners are not on average significantly worse off in terms of wealth (and share price) in the short term. This is an important finding for existing A-REIT shareholders, A-REITs and investment banks associated with these placements.

The use of private placements during the global financial crisis (GFC) was significant. Westfield, Stockland, Mirvac, DEXUS and Charter Hall, amongst others, all raised large sums of capital this way during the GFC. It allowed companies to raise equity capital quickly to shore up debt to equity positions.

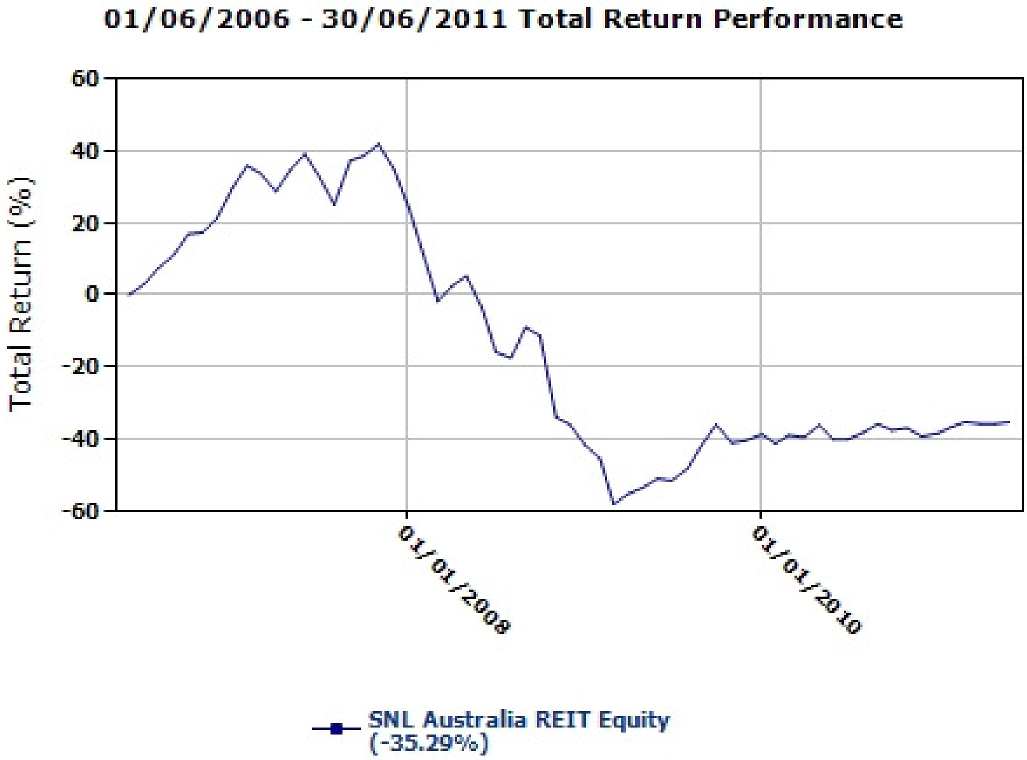


SNL Real Estate ASX200 vs SNL A-REIT Equity Share Price Performance
Source: SNL Data
Figure 1

Newell (2006) and Newell and Peng (2006) reported that the A-REIT sector provided an outstanding period of outperformance for stock market investors and Newell (2007) identified the importance of A-REITs to industry based superannuation funds. However in late 2007, the Centro Properties Group issued an announcement that they were about to experience increased financing costs, that they were continuing to renegotiate a $1.3 billion loan (which was overdue) and that they did not believe it prudent to pay a distribution to unit holders for the second half of the year ended 31 December 2007. Dimovski (2009) identified that this information changed the risk profile of A-

REITs enormously and as a consequence had major implications for the cost of capital to the sector. Additionally, Chikolwa (2008a and 2008b) points out that the Commercial Mortgage-Backed Securities (CMBS) market was an important debt funding option for A-REITs, but the sub-prime mortgage market events in the US resulted in a significant credit crunch to the global financial system and a perception of a significantly increased risk in lending to REITs, including A-REITs.

Figure 1, with data from the SNL Real Estate database, shows the relative share price performance for the S&P ASX 200 to the SNL A-REIT Equity index (which includes the top 25 or so) A-REITs for the period of this study 1 June 2006 to 30 June 2011. The A-REIT performance has tracked considerably lower. Indeed while the S&P ASX 200 index has decreased around 6.98% during the period of the study, the SNL A-REIT Equity index has decreased 58.14%. Figure 2 includes the dividend/distribution returns to the capital (price change returns) from A-REITs to show the sector is down 35.29% at the end of the 2011 financial year from where it was in June 2006. This data shows the A-REIT sector has been under considerable strain since December 2007.



SNL Real Estate Australian REIT Total Performance
Source: SNL Data
Figure 2

The structure of this paper is as follows. The next section briefly summarises some previous rights issue capital raising research. The third section identifies the data and reports the results. The last section contains some concluding comments.

LITERATURE REVIEW

Chan and Brown (2004) have offered a comprehensive study around the legal rules of when, how and how often placements can be made (including some discussion of the history of placements) in the US, UK and Australia. Briefly, in the US they point to the New York Stock Exchange (NYSE) listing rule 312.03 requiring shareholders to approve private placements sold at a discount to the market price if the issue is greater than 20% of the issued shares; and in the UK, they note the Companies Act 1985 and the London Stock Exchange (LSE) both limit the operation of placements. These guidelines effectively limit placements in any one year to 5% of the ordinary capital on issue and to 7.5% over any three-year period. The discount on the market price is also limited to 5%. In Australia listed entities were restricted to issuing no more than 10% of the issued capital in any twelve month period but this has been increased to 15% for all listed companies since 1998. Shareholder approval is required if more than 15% is sought to be raised by private placement.

In early IPO finance literature, Rock (1986) and Beatty and Ritter (1986) suggest that there is lower underpricing if there is lower information asymmetry. This means that the more that companies reveal about themselves and the more that is known about them, the less they need to discount the equity securities they offer to new subscribers.

Wruck (1989) and later Hertzel and Smith (1993) using US data both suggest that private placements are used to mitigate the information asymmetry regarding the issuing firm and hence signal/certify the quality of the issuing firm. Wruck (1989) contends that private placements allow for an increased ownership concentration to improve the monitoring of management. Hertzel and Smith (1993) argue that the intensive effort in convincing informed investors of the quality of the issuing firm and the subsequent investment by those investors certifies firm quality. Slovin, Sushka and Lai (2000) using UK data provide similar findings. They suggest a private placement enhances the firm's ability to signal their quality.

There is a substantial body of literature that provides evidence that while the new investors in private placements may be offered shares at a discount, the existing investors generally don't lose in the short or long term. Indeed the following studies provide evidence that private placements are typically quite favourable to existing shareholders: Varma and Szewcyzk (1993) found this in the banking sector; Deng, Li and Wu (2011) found this with Chinese stocks; and Krishnamurthy, Spindt, Subramanium and Woidtke (2005) and Wruck and Wu (2009) found this with US stocks.

As for REIT equity private placements, using 1981 to 1999 US data, Marciukaityte, Higgins, Friday and Mason (2007) found a significant negative abnormal return to existing investors in the short term (-1,+1) but positive long run abnormal returns to existing investors in the two to five year period. They suggest managers time their placements when equity prices are high but that in the long term, real estate has provided superior investment opportunities for those involved in REITs. An earlier study by Higgins, Howton and Howton (2004) examined the private placement of debt securities by US REITs. They did not find any significant short term market reaction.

DATA AND RESULTS

This study examines 55 private placements made by A-REITs from 1 July 2006 to 30 March 2011. A total of over $10 billion of equity was raised privately during this period, that on an average per year basis is quite similar to the $13 billion in rights issue raising in Australia reported in Dimovski (2011). Data is collected from three main sources. The first is the SDC capital raising database to identify the placements and the capital raised. The second and third sources were FinAnalysis and SNL Real Estate respectively, to corroborate the pricing, underwriters, date of offer and whether rights offers or other unit/share purchase issues were offered to existing unitholders, alongside the private placement to significant institutional investors.

Name	**Year of Issue**	**Amount raised**
Westfield	2009	$2.900 billion
CFS Retail	2010	$540 million
Charter Hall	2008	$500 million
Stockland	2007	$402 million
CFS Retail	2008	$325 million
DEXUS	2008	$302 million
Stockland	2008	$300 million
Mirvac	2008	$300 million
Valad	2007	$286 million
Goodman	2008	$230 million

Ten Largest Private Placements July 2006 – March 2011
Source: Authors
Table 1

Table 1 identifies the ten largest private placements during July 2006 to March 2011. Over $6 billion of secondary equity capital was raised by this "top ten". The significance of Westfield to the A-REIT sector is clear with this single entity having the ability to place nearly $3 billion of this $6 billion. What made this capital raising even more impressive was that this placement was done in 2009, during the GFC period. (Westfield had also raised $3 billion in 2007, before the GFC, through a rights issue.) Other A-REITs undertaking major placements during the period of the study include CFS Retail ($540 million in 2010 and $325 million in 2008), Charter Hall ($500 million in 2008) and Stockland ($402 million in 2007 before the GFC and $300 million in 2008 during the GFC).

Table 2 identifies the major investment banks involved in the private placements during the period of the study. The table also partitions the data into placements undertaken before the Centro Properties liquidity problem announcements in December 2007 and those after. The top ten underwriters wrote over $9 billion of underwriting business during the period of the study, with the top six writing nearly $8 billion. While JP Morgan, UBS, Citigroup, Deutsche Bank, Macquarie and Credit Suisse respectively led the league table over the whole period of the study, Goldman Sachs JB Were (GSJBW) underwrote a useful five placements totalling $436 million after the GFC. Interestingly, while UBS appeared a dominant bank for A-REITs seeking private placements in July 2006 to December 2007 (before the GFC), JP Morgan, Deutsche, Citigroup and Credit Suisse all made significant advances in their market shares from January 2008.

Name	July 2006 to Dec 2007 Issues/Capital	Jan 2008 to March 2011 Issues/Capital	Total Issues / Total capital raised
JP Morgan	4 / $189 m	9 / $1573 m	13 / $1762 million
UBS	11 / $911 m	5 / $721 m	16 / $1632 million
Citigroup	5 / $387 m	4 / $898 m	9 / $1285 million
Deutsche	2 / $122 m	5 / $1160 m	7 / $1282 million
Macquarie	6 / $420 m	7 / $624 m	13 / $1044 million
Credit Suisse	2 / $96 m	3 / $880 m	5 / $976 million
GSJBW	0 / $0 m	5 / $436 m	5 / $436 million
CBA Equities	0 / $0 m	2 / $232 m	2 / $232 million
Commsec	0 / $0 m	3 / $205 m	3 / $205 million
Morgan Stanley	1 / $40 m	1 / $150 m	2 / $190 million

Top Ten Underwriters of Private Placements July 2006 – March 2011
Source: Authors
Table 2

	Private Placements	Rights coincided	Stapled	Underwritten
PANEL A				
Total Sample	55	28	31	46
(% of total issues)	100%	51%	56%	84%
PANEL B				
Partitioned by Issue Period				
July 2006 – December 2007	28	12	14	23
(% of total issues)	51%	22%	25%	42%
January 2008 – March 2011	27	16	17	23
(% of total issues)	49%	29%	31%	42%

A-REIT Private Placements by Total and Sub-Period July 2006-Mar 2011
Source: Authors
Table 3

Panel A of Table 3 reports the number of private placement issues, the number and percentage of rights issues that coincided with the placement, the number and percentage of placements that were underwritten and the number and percentage of placement issues using stapled securities. It is interesting to note that about half of the placements also coincided with rights issues to the existing shareholders and while the placements do not have to be underwritten, the vast majority were underwritten. Panel B of Table 3 dissects the data of Panel A into July 2006 to December 2007 (generally identified as before the GFC) and January 2008 to March 2011 summary statistics. There are no obvious differences in this data.

		Gross	Percentage Held by Top 20	Std deviation of Returns *	Discount
PANEL A					
Total Sample	Mean	$ 189m	71%	3.5%	-7.1%
	Median	$ 100m	75%	2.0%	-5.1%
	Minimum	$ 7m	48%	0.8%	-37.5%
	Maximum	$2900m	89%	14.8%	25 %
PANEL B					
July 2006 – December 2007	Mean	$ 112 m	69%	1.4%	-2.6%
	Median	$ 87 m	70%	1.4%	-3.3%
	Minimum	$ 7 m	48%	0.8%	-9.4%
	Maximum	$ 402 m	89%	5.3%	8.6%
January 2008 – March 2011	Mean	$ 269 m	74%	4.8%	-12.1%
	Median	$ 152 m	77%	4.8%	-7.5%
	Minimum	$ 20 m	56%	0.9%	-37.5%
	Maximum	$2900 m	86%	14.8%	25.0%

A-REIT Private Placements Summary Statistics by Total and Sub-Period July 2006-Mar 2011
Source: Authors
Table 4

Panel A of Table 4 identifies the average placement raised around $189 million of new equity while the median placement was $100 million. The largest private placement, by Westfield Group of $2.9 billion, has previously been discussed. These A-REITs are well supported by institutions and the top twenty shareholders hold slightly more than two-thirds of the available securities on average. The standard deviation of returns in the 250 days before the private placement averaged 3.5%. The mean discount offered to the new investors through the private placement was 7.1% while the median was 5.1%. The discount is determined as sum of the closing price on the day before the placement and the private placement offer price divided by the closing price on the day before. The largest discount was 37.5% but there also happened to be a premium in one instance of 25%.

		Profit to Subscribers listing day	Profit to existing	Profit to Subscribers + 10	Profit to Existing +10
PANEL A					
Total Sample	Mean	7.7%	-0.8%	7.8%	0.1%
	Median	3.3%	-2.6%	3.3%	-2.6%
	Minimum	-20.0%	-28.3%	-11.1%	-23.2%
	Maximum	57.6%	42.8 %	72.2%	58.1 %
PANEL B					
July 2006 – December 2007	Mean	1.6%	-1.1%	1.9%	0.1%
	Median	1.9%	-1.6%	1.9%	-1.8%
	Minimum	-4.4%	-10.5%	-11.1%	-12.3%
	Maximum	9.7%	13.3%	25.0%	33.3%
January 2008 – March 2011	Mean	14.4%	-0.4%	14.5%	0.3%
	Median	8.1%	-6.1%	8.0%	-7.5%
	Minimum	-20.0%	-28.3%	-9.8%	-23.1%
	Maximum	57.6%	42.8%	72.2%	58.2%

A-REIT Private Placement Profits by Total and Sub-Period July 2006-Mar 2011
Source: Authors
Table 5

Panel B of Table 4 partitions the data by the issue period. The first period was July 2006 to December 2007 - arguably the period before the GFC - and the second issue period was January

2008 to March 2011. The latter period private placements were substantially larger on average than the earlier period issues (mean of $269 million and median of $152 million compared to $112 million and $87 million). The latter period issues also had a larger percentage security holding amongst the top 20 shareholders while the standard deviation of returns for the last 250 days before the issue was nearly 3.5 times that of the earlier period. The volatility of daily returns since the GFC is quite dramatic indeed. Interestingly the average discount offered to new investors since the earlier period is over 4.5 times while even the median is over 2.25 times that of the earlier period.

Table 5 examines the mean, median, minimum and maximum profits earned by the subscribers to the A-REIT placements during the study period. The profits are defined as the difference between the sum of the closing price of the units on the first day of trading less the issue price to subscribers, divided by the closing price. Many of the studies (Wruck 1989, Hertzel and Smith 1993, Deng et al 2011, Krishnamurthy et al 2005) however, calculate the profits based on the closing price of the units some ten days after the announcement to better control for market over-reactions. This plus ten day profit to subscribers is also calculated.

As for the existing shareholders, their profits are calculated as the sum of the closing price of the units the day before the announcement less the closing price of the units on the first day of trading of the new subscriber units divided by the closing price of the units the day before the announcement. Similarly, the plus ten day profit calculation uses the closing price of the units ten days after the announcement date.

Panel A reports the mean profit to the subscribers using the first day and ten day closing prices as 7.7% and 7.8% respectively – so subscribers appear to do quite well, on average, from the private placements by A-REITs. The existing shareholders, consistent with the general finance literature using the ten days closing price, show an average 0.1% profit. While this is not statistically significantly different to zero, it is still not a bad result for existing shareholders in the short term.

Panel B partitions the profit data into July 2006 to December 2007 and January 2008 to March 2011. While the average profits to the subscribers is much higher in the latter period compared to the earlier period (at 14.5% compared to 1.9%) using the ten days closing price, the average profits to the existing shareholders remains about the same (at 0.3% compared to 0.1%) using the ten days closing price.

Since the existing shareholders appear not to fare too badly in terms of profit as a result of the private placements, we might expect such placements to occur relatively regularly. Table 6 identifies those A-REITs that were involved in multiple private placements. It can be seen from this table that three entities placed privately four times during our data period (CFS Retail, Valad and Abacus – with CFS Retail raising over $1 billion by placement during this period); five A-REITs placed privately three times (including Stockland who raised nearly $1 billion by this method) during the data period and two A-REITs that placed twice.

CONCLUSION AND IMPLICATIONS FOR A-REITS

This study investigated 55 A-REITs in Australia during July 2006 to March 2011 that offered their equity by private placement to selected investors. The magnitude of the capital raising (over $10 billion during this period) and the speed (in the vast majority of cases, only a day or two) at which the capital was raised by the A-REITs, even during the GFC period, was impressive. Around $6.2 billion was raised by private placement in 2008 and 2009 alone. This continues to suggest that A-REITs are regarded highly by the investment community.

Name	July 2006 to Dec 2007 Issues/Capital	Jan 2008 to March 2011 Issues/Capital	Total Issues / Total capital raised
CFS Retail	2 / $216 m	2 / $865 m	4 / $1081 million
Valad	3 / $524 m	1 / $24 m	4 / $548 million
Abacus	2 / $160 m	2 / $111 m	4 / $271 million
Stockland	1 / $403 m	2 / $503 m	3 / $906 million
Mirvac	0 / $0 m	3 / $525 m	3 / $525 million
Comm Property	0 / $0 m	3 / $450 m	3 / $450 million
ING Office	1 / $70 m	2 / $225 m	3 / $295 million
Charter Hall	1 / $133 m	2 / $26 m	3 / $159 million
Goodman	0 / $0 m	2 / $397 m	2 / $397 million
DEXUS	0 / $0 m	2 / $391 m	2 / $391 million

A-REIT Private Placement Multiple Issuers by Total and Sub-Period July 2006-Mar 2011
Source: Authors
Table 6

While the general finance literature suggests that existing shareholders do not fare badly from private placements offered to subscribers issued at a discount, this is the first Australian REIT study to also report similar findings. This study is also important since all of the studies reported previously have drawn on data before the GFC. This study utilizes and includes data during the GFC. The mean average returns are slightly positive for existing owners after the private placement (but the median was around 7% negative in these more recent volatile times). Interestingly the mean average short-term profit to subscribers is a substantial 14% in these more recent volatile times.

The results concur with the certification and monitoring explanations of Hertzel and Smith (1993) and Wruck (1989). It appears A-REIT investors are quite accepting of concentrated groups of knowledgeable (generally institutional) investors being offered equity through private placement even given the substantial existing ownership concentration.

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