CHAPTER 5

REITs by Property Type

As discussed in the first chapter, one of the primary ways to classify REITs is by the type of property in which they invest. This chapter provides a basic overview of the major property types owned by equity REITs, as well as detail on mortgage REITs. This chapter also provides sublists of the 181 equity REITs and 42 mortgage REITs that compose the FTSE NAREIT All REITs Index, sorted according to NAREIT's property sector and subsector classifications. (Appendix C presents additional information on each company, including website addresses.)

Each type of real estate is associated with distinct supply-and-demand fundamentals that in turn assign certain risks and rewards to the landlords' expected income. Although these risks and rewards become most apparent during times of economic boom or bust, they constantly govern the profitability of different property types and by extension affect stock-price performance. This chapter also highlights economic factors that influence demand for each property type; Chapter 7 provides a more in-depth discussion of the links between current economic news such as changes in interest rates or employment trends, and their effects on the stock prices of different types of REITs.

Diversified and Specialized REITs

Diversified REITs are equity REITs that invest in two or more types of commercial property (see Table 5.1). On the opposite end of the property spectrum are specialty REITs (Table 5.2), which own

The Intelligent REIT Investor: How to Build Wealth with Real Estate Investment Trusts,
Stephanie Krewson-Kelly and R. Brad Thomas

Table 5.1 Diversified REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Vornado Realty Trust	VNO	$21,143	www.vno.com
VEREIT, Inc.[a,b]	VER	17,406	www.vereit.com
NorthStar Realty Finance Corp.	NRF	15,403	www.nrfc.com
W. P. Carey Inc.[a]	WPC	8,755	www.wpcarey.com
Lexington Realty Trust[a]	LXP	3,830	www.lxp.com
Global Net Lease[a]	GNL	2,548	www.globalnetlease.com
Washington Real Estate Investment Trust[†]	WRE	2,191	www.washreit.com
Investors Real Estate Trust	IRET	1,998	www.iret.com
American Assets Trust, Inc.	AAT	1,978	www.americanassetstrust.com
Alexander's, Inc.	ALX	1,448	www.alx-inc.com
BRT Realty Trust	BRT	836	www.brtrealty.com
Gladstone Commercial Corporation	GOOD	833	www.GladstoneCommercial.com
Whitestone REIT	WSR	784	www.whitestonereit.com
Winthrop Realty Trust	FUR	746	www.winthropreit.com
Armada Hoffler Properties, Inc.	AHH	690	www.armadahoffler.com
One Liberty Properties, Inc.	OLP	650	www.onelibertyproperties.com
HMG/Courtland Properties, Inc.	HMG	32	www.hmgcourtland.com
Total for 17 REITs:		$81,271	

*As of December 31, 2015, in millions of dollars.
[a]Indicates that the associated REIT generally uses long-term triple-net leases.
[b]Former name: American Realty Capital Properties (formerly NYSE: ARCP).
[†]This REIT is in the process of being acquired and will not remain publicly traded.
Source: NAREIT, S&P Global Market Intelligence.

only one type of highly specialized real estate, such as billboards, correctional facilities, or farmland. Many of the specialty REITs are new to the industry, though other specialized property types are more established and now have their own NAREIT classification. Data center REITs (Table 5.3) own, develop, and manage wholesale data center properties and data center shells. Infrastructure REITs (Table 5.4) invest in communications, energy and transportation projects. Timber REITs (Table 5.5) own acres of forest, the trees on which are harvested for paper and wood products production. In 2015, there were 44 REITs in these combined categories with total assets of $214.1 billion.

REITs that use Triple-Net-Leases

Recall from Chapter 4 that a triple-net lease is one in which the landlord collects a base rent that excludes—meaning it is net of—taxes, insurance, and maintenance expenses associated with

Table 5.2 Specialty REITs

Company Name	Ticker Symbol	Total Assets*	NAREIT Sub-Property Type	Website Address
Iron Mountain Incorporated	IRM	$6,351	Data Center	www.ironmountain.com
EPR Properties	EPR	4,217	Cineplex Theater	www.eprkc.com
Outfront Media	OUT	3,845	Billboards	www.outfrontmedia.com
GEO Group, Inc.	GEO	3,503	Prison	www.geogroup.com
Lamar Advertising	LAMR	3,392	Billboards	www.lamar.com
Corrections Corporation of America	CXW	3,356	Prison	www.cca.com
Gaming and Leisure Properties, Inc.	GLPI	2,448	Casino	www.glpropinc.com
Farmland Partners Inc.	FPI	345	Land	www.farmlandpartners.com
Gladstone Land Corporation	LAND	230	Land	www.gladstoneland.com
American Farmland Company	AFCO	190	Land	www.americanfarmlandcompany.com
Total for 10 REITs:		$27,877		

*As of December 31, 2015, in millions of dollars.
These REITs generally use long-term triple-net leases and/or ground leases.
Source: NAREIT, S&P Global Market Intelligence.

Table 5.3 Data Center REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Digital Realty Trust, Inc.	DLR	$11,451	www.digitalrealty.com
Equinix	EQIX	10,357	www.equinix.com
DuPont Fabros Technology, Inc.	DFT	2,815	www.dft.com
CyrusOne Inc.	CONE	2,196	www.cyrusone.com
QTS Realty Trust, Inc.	QTS	1,758	www.qtsdatacenters.com
CoreSite Realty Corporation	COR	1,163	www.CoreSite.com
Total for 6 REITs:		$29,739	

*As of December 31, 2015, in millions of dollars.
These REITs may use long-term triple-net leases at some or all of their properties.
Source: NAREIT, S&P Global Market Intelligence.

Table 5.4 Infrastructure REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
American Tower Corp	AMT	$26,904	www.americantower.com
Crown Castle International Corp	CCI	22,036	www.crowncastle.com
Communications Sales & Leasing	CSAL	2,543	www.cslreit.com
InfraREIT, Inc.	HIFR	1,664	www.infrareitinc.com
CorEnergy Infrastructure Trust	CORR	678	www.corenergy.corridortrust.com
Power REIT	PW	22	www.pwreit.com
Total for 6 REITs:		$53,847	

*As of December 31, 2015, in millions of dollars.
These REITs generally use long-term triple-net leases and/or ground leases.
Source: NAREIT, S&P Global Market Intelligence.

Table 5.5 Timber REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Weyerhaeuser Company†	WY	$12,486	www.weyerhaeuser.com
Plum Creek Timber Company, Inc.†	PCL	4,990	www.plumcreek.com
Rayonier Inc.	RYN	2,319	www.rayonier.com
Potlatch Corporation	PCH	1,017	www.potlatchcorp.com
CatchMark Timber Trust, Inc.	CTT	599	www.catchmark.com
Total for 5 REITs:		$21,411	

*As of December 31, 2015, in millions of dollars.
These REITs generally use long-term triple-net leases and/or ground leases.
†These two timber REITs are merging; the transaction is expected to be complete in the first half of 2016.
Source: NAREIT, S&P Global Market Intelligence.

occupying the property. These and other operating expenses are paid directly by the tenant to the various service providers. REITs that use triple-net leases typically lease their properties to a single tenant for 10 or more years. NAREIT no longer includes a *triple-net* property category. However, companies categorized by NAREIT as specialty, data center, infrastructure, and timber REITs generally use triple-net leases (including ground leases), as do some of the diversified REITs.

Risks and Rewards of REITs That Use Triple-Net Leases

During times of economic expansion, landlords that use long-term, triple-net leases do not profit as much as other landlords that use shorter-term, gross, or full-service leases because they cannot capture rising market rents. However, triple-net landlords do benefit from steady, bond-like cash flows generated by their leases. As a result, triple-net REITs are viewed as the most defensive, least volatile REITs and tend to outperform other REITs during times of economic uncertainty.

One source of risk in the triple-net REIT model relates to how these companies grow. Few if any of the triple-net REITs grow through development, and their internal growth is embedded in the long-term nature of their leases (often indexed to inflation). This leaves acquisitions as the only source of external growth for these REITs. As such, it is imperative that these companies attain and then maintain a low cost of capital. (See Chapters 7 and 8 for a discussion of REITs' cost of capital.) By way of a simple example, if the investment yield on a property leased pursuant to a long-term triple-net lease is 7 percent, then the triple-net REIT needs to have a cost of capital that is less than 7 percent in order for the acquisition to be additive to its future cash flow.

In the last decade, the number of income-oriented investors competing to buy buildings that are triple-net leased to creditworthy tenants has increased dramatically. The near-decade of super-low interest rates in the United States that followed in the wake of the Great Recession of 2008–2009 was a primary cause of the increase in demand for many high-yield investments, including triple-net properties that generate yields of 5 percent or more. Although higher interest rates in the future may cause a marginal decline in property values, implying higher yields from real estate than today, management teams of triple-net REITs—or any REIT that relies on acquisitions to grow—need to remain vigilant about their costs of capital.

Health-Care REITs

NAREIT lists 17 health-care REITs with combined assets of $114.3 billion (Table 5.6). Health-care REITs receive their income primarily from leasing facilities to health-care providers, usually on a triple-net

Table 5.6 Health-Care REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Welltower Inc.	HCN	$29,024	www.welltower.com
Ventas, Inc.	VTR	22,262	www.ventasreit.com
HCP, Inc.	HCP	21,450	www.hcpi.com
Omega Healthcare Investors, Inc.	OHI	8,019	www.omegahealthcare.com
Senior Housing Properties Trust	SNH	7,184	www.snhreit.com
Medical Properties Trust, Inc.	MPW	5,609	www.medicalpropertiestrust.com
Healthcare Trust of America, Inc.	HTA	3,172	www.htareit.com
New Senior Investment Group	SNR	3,017	www.newseniorinv.com
Care Capital Properties, Inc.	CCP	2,955	www.carecapitalproperties.com
Healthcare Realty Trust	HR	2,817	www.healthcarerealty.com
Sabra Health Care REIT, Inc.	SBRA	2,486	www.sabrahealth.com
National Health Investors, Inc.	NHI	2,146	www.nhireit.com
Physicians Realty Trust	DOC	1,645	www.docreit.com
LTC Properties, Inc.	LTC	1,275	www.ltcreit.com
CareTrust REIT, Inc.	CTRE	673	www.caretrustreit.com
Universal Health Realty Inc Tr	UHT	459	www.uhrit.com
Community Healthcare Trust Incorporated	CHCT	143	www.communityhealthcaretrust.com
Total for 17 REITs:		$114,337	

*As of December 31, 2015, in millions of dollars.
These REITs generally use long-term triple-net leases and/or ground leases.
Source: NAREIT, S&P Global Market Intelligence.

or modified-gross basis. (Please refer to Chapter 4 for detail on lease structures.) Property types include senior and assisted-living/rehabilitation facilities, medical clinics, medical office buildings (also referred to as *MOBs*), health-care laboratories, and hospitals.

Population growth, aging demographics, and shifts in consumer preference have all fueled the growth in nonhospital health-care locations and in turn health-care REITs. In their January 2013 report, *U.S. Healthcare Industry and Medical Office Market Overview*, the Rosen Consulting Group ("RCG") wrote:

> The healthcare industry has been growing at a strong pace for decades. Looking forward, this trend is expected to accelerate as baby boomers reach retirement age and echo boomers begin to establish their own facilities. As demand for medical services increases, this will further increase the need for physicians, lab technicians, and other medical support staff, driving demand for the high-quality . . . MOBs that house them.

The *Patient Protection and Affordable Care Act*, which is commonly referred to as the *Affordable Care Act* (ACA or "Obama Care") was signed into law in March 2010. By increasing the number of Americans who have access to health insurance, the ACA is viewed as an additional source of demand in the health-care real estate industry, as a greater number of cost-efficient facilities will be required to administer health services.

Growth in MOBs and other specialty health-care real estate has also expanded dramatically in the past few decades. As RCG observes in the same 2013 report previously stated:

> Evolution in the healthcare industry is also contributing to opportunities in the medical office space. Driven by shifting consumer preferences, limited space in hospitals, and lower costs, procedures that have traditionally been performed in hospitals, such as surgery, have been moving to outpatient facilities. Additionally, increased specialization in the medical field has been driving demand for medical office facilities suited to the needs of the particular profession.

Risks and Rewards of Health-care REITs

Health-care REITs should continue to benefit from robust demand for an increased number of health-care facilities required to support the expanding U.S. population, in as cost-efficient a manner possible. Where there is growth in demand, there is also the possibility for too much new supply being built at once. Investors should be aware of this potential risk when evaluating where different health-care REITs are building and buying facilities.

Health-care REITs' tenants are doctors and health-care service providers, who in turn have varying degrees of exposure to government policy vis-à-vis reimbursement levels for Medicare and Medicaid. Most REITs have minimized their exposure to potential changes in Medicare and Medicaid reimbursement levels by leasing to tenants that emphasize private-pay care. Even so, health-care REITs' total returns remain subject to risk associated with potential reductions to government Medicare and Medicaid reimbursement rates. Even if no changes are made, if investors believe reimbursement rate cuts are possible, all health-care REITs are likely to underperform other property types.

The final risk to consider when reviewing health-care REITs is their use of long-term triple-net leases with the tenants who operate (no pun intended) out of their facilities. In a rising interest rate environment, REITs that use triple-net leases tend to be valued like long-term bonds, in that their stock prices typically underperform other types of REITs that use shorter-term leases. (See Chapter 7 for more information about the factors that influence REIT share price performance.)

Industrial REITs

There are 11 industrial property REITs in the FTSE NAREIT All REIT Index, with combined assets of $60.2 billion (Table 5.7). Industrial properties are leased to businesses for a variety of purposes, including distribution warehousing, light manufacturing, and research and development (R&D).

Industrial property is among the most stable, least-volatile asset classes in the United States. National warehouse/industrial occupancy in the United States typically ranges between 88 percent and 92 percent, evidencing the steady supply-and-demand fundamentals associated with warehousing and distribution facilities. The fact that supply of newly constructed industrial property tends to track demand for new facilities is one of the primary reasons behind the sector's stability.

Demand for industrial property is correlated to consumer spending and growth in the country's gross domestic product (GDP).

Table 5.7 Industrial REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Prologis, Inc.	PLD	$31,395	www.prologis.com
Duke Realty Corporation	DRE	6,917	www.dukerealty.com
Liberty Property Trust	LPT	6,558	www.libertyproperty.com
DCT Industrial Trust Inc.	DCT	3,632	www.dctindustrial.com
First Industrial Realty Trust, Inc.	FR	2,718	www.firstindustrial.com
PS Business Parks, Inc.	PSB	2,187	www.psbusinessparks.com
STAG Industrial, Inc.	STAG	1,906	www.stagindustrial.com
EastGroup Properties, Inc.	EGP	1,666	www.eastgroup.net
Rexford Industrial Realty, Inc.	REXR	1,153	www.rexfordindustrial.com
Terreno Realty Corporation	TRNO	1,152	www.terreno.com
Monmouth Real Estate Investment Corporation	MNR	916	www.mreic.com
Total for 11 REITs:		$60,200	

*As of December 31, 2015, in millions of dollars.
Source: NAREIT, S&P Global Market Intelligence.

The more demand for consumer goods—whether they are purchased at traditional brick-and-mortar locations like malls, or online with the Internet—the greater the need for warehouses to store and distribute goods to consumers. Supply increases through new development. Industrial properties are fairly simple to build, consisting essentially of four walls tilted up on a six-inch slab of concrete, with a roof that holds it all together. As such, it typically takes only six-to-nine months to construct an industrial property after breaking ground. Due to the relatively short development cycle, industrial property markets tend not to get overbuilt.

Risks and Rewards of Industrial REITs

The trade-off for the industrial sector's stability is these REITs do not enjoy the rapid price appreciation associated with other, more volatile property sectors. Because industrial property is so essential to any economy, shares of industrial REITs tend to perform well throughout the economic cycle. Industrial REITs may not dazzle, but they also rarely disappoint.

Lease Terms

Industrial property landlords employ triple-net or modified-gross leases. As explained in Chapter 4, the tenant is responsible for all of a property's maintenance, taxes, and insurance in the former case; in the latter, the landlord/REIT typically pays basic property taxes and insurance. Lease lengths range from one-to-three years for small-space users with local distribution needs, and five, seven, or 10 years+ for larger tenants distributing goods regionally or nationally. At either end of the spectrum, tenant renewal rates tend to be high (roughly 65 percent or more), since distribution space is a critical component of a tenant's supply chain. (Tenants cannot get their goods to end users without some degree of warehousing and distribution.) Industrial leases tend to include rent escalations every one, two, or three years; these contractual rent bumps typically are indexed to increase with inflation.

Lodging/Resort REITs

In 2015 there were 20 lodging/resort (hotel) REITs in the FTSE NAREIT All REITs Index with $61.3 billion of total assets (Table 5.8). The majority of U.S. hotels are affiliated with national or international franchises or brands. REITs generally own hotels branded under the most widely recognized flags, and tend to focus on the urban markets. Popular brands (and their respective *flags*) include Marriott International (Courtyard, Residence Inn), Hilton (Hilton Garden Inn, Hampton Inn), and InterContinental Hotels Group (Intercontinental, Holiday Inn). Hotels are frequently classified by the quality-level of guest services offered, such as luxury, upper-upscale, upscale, midscale, or economy or by their location such as urban, suburban, resort, and airport.

Hotel Revenue

Location and quality levels is a key driver of a hotel's maximum revenue per available room (RevPAR), which is the product of a hotel's average daily room rate (ADR) and its occupancy rate. Close proximity to a desirable attraction, such as a beach, a central business district, a large university, or a convention center can be a competitive advantage, enabling an operator to charge higher room rates and maintain higher occupancies than hotels that operate in secondary locations. The latter tend to be roadside, limited- or economy-service hotels that compete primarily on price.

Hotel Expenses

Labor represents the most significant expense in hotel operations. As a result, hotels will have large fixed costs to operate the hotel since a minimum number of employees are required to open, run, and clean a hotel each day, regardless of occupancy levels. For this reason, hotels often reduce room rates to increase occupancy during off-seasons or in slow to declining economic times.

Technical Aspects Specific to Hotel REITs

Hotel REITs differ structurally from other equity REITs in that, according to REIT rules (see Chapter 6), hotel owners are not permitted to directly operate the properties they own. This is because earning profit from operating hotels is active and differs from the more passive business of collecting rent on hotels leased to third-party operators. As a result, hotel REITs must retain a third-party hotel manager to operate its hotels. The third-party hotel manager is in charge of all operating facets of the hotel, including hiring and managing the employees, revenue management, and maintenance. In exchange, the third-party manager receives a base

Table 5.8 Lodging/Resort REITs

Company Name	Ticker Symbol	Total Assets*	NAREIT Sub-Property Type	Website Address
Host Hotels & Resorts, Inc.	HST	$11,784	Full-service Hotel	www.hosthotels.com
Hospitality Properties Trust	HPT	6,408	Limited-service Hotel	www.hptreit.com
Ashford Hospitality Trust, Inc.	AHT	4,965	Full-service Hotel	www.ahtreit.com
LaSalle Hotel Properties	LHO	4,075	Full-service Hotel	www.lasallehotels.com
RLJ Lodging Trust	RLJ	3,980	Full-service Hotel	www.rljlodgingtrust.com
Sunstone Hotel Investors, Inc.	SHO	3,863	Full-service Hotel	www.sunstonehotels.com
Apple Hospitality REIT, Inc.	APLE	3,723	Hotel	www.applehospitalityreit.com
DiamondRock Hospitality Company	DRH	3,320	Hotel	www.drhc.com
Pebblebrook Hotel Trust	PEB	3,063	Hotel	www.pebblebrookhotels.com
Xenia Hotels & Resorts, Inc.	XHR	3,006	Hotel	www.xeniareit.com
Ryman Hospitality Properties, Inc.	RHP	2,331	Full-service Hotel	www.rymanhp.com
Chesapeake Lodging Trust	CHSP	2,094	Full-service Hotel	www.chesapeakelodgingtrust.com
Hersha Hospitality Trust	HT	1,970	Limited-service Hotel	www.hersha.com
FelCor Lodging Trust Incorporated	FCH	1,884	Full-service Hotel	www.felcor.com
Summit Hotel Properties, Inc.	INN	1,581	Limited-service Hotel	www.shpreit.com
Ashford Hospitality Prime, Inc.	AHP	1,353	Hotel	www.ahpreit.com
Chatham Lodging Trust	CLDT	1,340	Hotel	www.chathamlodgingtrust.com
SoTHERLY Hotels Inc.	SOHO	393	Full-service Hotel	www.sotherlyhotels.com
Condor Hospitality Trust, Inc.	CDOR	144	Limited-service Hotel	www.condorhospitality.com
InnSuites Hospitality Trust	IHT	27	Limited-service Hotel	www.innsuitestrust.com
Total for 20 REITs:		$61,304		

*As of December 31, 2015, in millions of dollars.
Source: NAREIT, S&P Global Market Intelligence.

management fee (typically 2 to 4 percent of hotel revenues) plus potentially an incentive fee if certain profitability thresholds are achieved. Hotel REITs generally will retain asset managers to oversee the third-party hotel manager.

Risks and Rewards of Hotel REITs

Hotels are more like an operating company than a REIT because they have no leases to guarantee future revenues for some duration of time. Instead, hotel REITs have to "lease" their properties from scratch every day. During times of strong economic growth, hotels can increase prices immediately; as a result, during certain points in the economic cycle, hotel REITs can achieve some of the highest annual total returns of any property type (see Chapter 7 for more detail). In addition, since the lease rate for hotel rooms can be reset daily, in a rising inflationary economy, hotel REITs have an advantage as they can reprice their "leases" daily. As a result, hotel REITs tend to be the least interest rate sensitive class of investment real estate. When it looks like the economy is coming out of a recession, hotel REITs tend to outperform other REIT asset classes, as investors anticipate strong revenue growth and profitability. In a declining economy, however, hotel operators often have to cut their daily rates, and a portion of their employees, to maintain profitability. Unsurprisingly, hotel REITs tend to underperform other REIT sectors when the economy is slowing or at risk of slipping into recession.

Mortgage REITs

The FTSE NAREIT All REITs index listed 41 mortgage REITs (mREITs) at the end of 2015. Early in 2016, a 42nd mREIT was added, bringing the subsector to a total of 42 mREITs with combined assets of $457.2 billion (Table 5.9). Similar to banks and other financial institutions, mREITs lend money to real estate owners directly by issuing mortgages, or indirectly by acquiring existing loans or mortgage-backed securities. In contrast with equity REITs that derive the majority of their revenues from leases, mREIT revenue equals the principal and interest payments received from real estate-based loans.

Mortgage REITs originate residential and commercial mortgages, and they also invest in securities backed by residential

Table 5.9 Mortgage REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Home Financing:			
Annaly Capital Management	NLY	$75,191	www.annaly.com
American Capital Agency Corp	AGNC	57,021	www.agnc.com
Invesco Mortgage Capital	IVR	16,773	www.invescomortgage capital.com
Hatteras Financial	HTS	16,138	www.hatfin.com
Chimera Investment	CIM	15,345	www.chimerareit.com
New Residential Investment Corp	NRZ	15,193	www.newresi.com
Two Harbors Investment	TWO	14,576	www.twoharborsinvestment .com
Capstead Mortgage	CMO	14,446	www.capstead.com
CYS Investments	CYS	14,331	www.cysinv.com
MFA Financial	MFA	13,167	www.mfafinancial.com
ARMOUR Residential REIT	ARR	13,055	www.armourreit.com
New York Mortgage Trust	NYMT	9,060	www.nymtrust.com
Anworth Mortgage Asset	ANH	6,636	www.anworth.com
Redwood Trust	RWT	6,231	www.redwoodtrust.com
PennyMac Mortgage Investment Trust	PMT	5,827	www.pennymac mortgageinvestmenttrust .com
American Capital Mortgage Investment	MTGE	5,482	www.mtge.com
Dynex Capital	DX	3,670	www.dynexcapital.com
Apollo Residential Mortgage[b]	AMTG	3,663	www.apolloresidential mortgage.com
Western Asset Mortgage Capital	WMC	3,415	www.westernassetmcc.com
AG Mortgage Investment Trust	MITT	3,164	www.agmit.com
Five Oaks Investment Corp	OAKS	2,498	www.fiveoaksinvestment.com
Altisource Residential	RESI	2,458	www.altisourceresi.com
Orchid Island Capital	ORC	2,242	www.orchidislandcapital.com
Ellington Residential Mortgage REIT	EARN	1,557	www.earnreit.com
JAVELIN Mortgage Investment[b]	JMI	874	www.javelinreit.com
ZAIS Financial Corp	ZFC	775	www.zaisfinancial.com
Cherry Hill Mortgage Investment	CHMI	$636	www.chmireit.com
Great Ajax	AJX	615	www.great-ajax.com
Subtotal for 28 Residential Mortgage REITs:		$324,039	
Commercial Financing:			
Starwood Property Trust Inc	STWD	$85,738	www.starwoodpropertytrust .com
Colony Capital	CLNY	10,039	www.colonyinc.com
Blackstone Mortgage Trust	BXMT	9,377	www.blackstonemortgage trust.com
Ladder Capital Corp[a]	LADR	5,895	www.laddercapital.com

(*continued overleaf*)

Table 5.9 (*continued*)

Company Name	Ticker Symbol	Total Assets*	Website Address
iStar Inc	STAR	$5,623	www.istar.com
RAIT Financial Trust	RAS	4,447	www.rait.com
Resource Capital	RSO	2,760	www.resourcecapitalcorp .com
Apollo Commercial Real Estate Finance[b]	ARI	2,720	www.apolloreit.com
Arbor Realty Trust	ABR	1,827	www.arborrealtytrust.com
Hannon Armstrong Sustainable Infrastructure	HASI	1,470	www.hannonarmstrong.com
Newcastle Invt Corp	NCT	1,468	www.newcastleinv.com
Ares Commercial Real Estate	ACRE	1,379	www.arescre.com
Owens Realty Mortgage Inc	ORM	273	www.owensmortgage.com
Jernigan Capital	JCAP	105	www.jernigancapital.com
Subtotal for 14 Commercial Mortgage REITs:		133,122	
Total for 42 Mortgage REITs:[a]		$457,161	

*As of December 31, 2015, in millions of dollars.
[a]LADR was not included in the FTSE NAREIT All REITs Index at 12/31/2015, but was added in 2016. At the end of 2015, there were only 41 mREITs in the FTSE NAREIT All REITs Index.
[b]In February 2016, AMTG agreed to be acquired by ARI.c.
[b]This REIT is in the process of being acquired and will not remain publicly traded.
Source: NAREIT, S&P Global Market Intelligence.

> **Note**
>
> mREITs will not be included in S&P's Real Estate GICS sector; they will remain in Financials.

mortgages (RMBS) and commercial mortgages (CMBS). A mortgage-backed security (MBS) is a bond-like investment, supported by interest income generated by an underlying mortgage or collection of mortgages. The MBS issuer typically is a government agency or investment bank that purchases the loan(s) and then *securitizes* (or *packages*) them into loan-like securities that appeal to different investors. The purpose of creating these "loans from loans" is to diversify the risk of one borrower by pooling loans together or, in the case of an MBS based on one loan, to restructure the interest and principal payments so investors can buy a piece of the loan with a lower (or higher) risk profile to meet their investment objectives.

Mortgage REITs typically focus on either the residential or commercial mortgage markets. According to NAREIT:

- Most residential mREITs invest in agency RMBS, which are issued by Fannie Mae and Freddie Mac, often referred to as U.S. government–sponsored enterprises (GSEs), or Ginnie Mae. Agency RMBS constitute the bulk of assets held by mREITs today. However, residential mREITs also may invest in RMBS issued by other financial institutions (nonagency or private-label RMBS) and residential mortgage loans.
- Commercial mREITs provide financing for commercial real estate. They may invest in commercial mortgages and commercial real estate loans, as well as both rated and unrated CMBS, mezzanine loans, subordinated securities, or construction loans, and may participate in loan securitizations.

Risks and Rewards of Mortgage REITs

Because mREITs lend money at one rate and borrow it at another, their profitability is affected by changes in the interest rate environment. (Note that increases in interest rates do not directly affect equity REIT profitability. See Chapter 7, REIT Performance, for more detail.) Like banks, mREITs generally make higher profits in a higher-interest-rate environment, where the difference (or *spread*) between where they can borrow and where they lend funds may be greater. However, if interest rates rise rapidly and/or unexpectedly, mREIT profitability can get squeezed because the rate at which management now needs to borrow is higher than the rates at which they have already invested. Most mREIT management teams are

Basics of Investing in mREITs

- Rising interest rates = Margin on investments vs. cost of funds declines; profits fall → Avoid!
- Falling interest rates = Higher prepayments; profits likely to fall → Avoid!
- Stable interest rates = Steady profits → Okay to Invest

diligent about matching durations between their loans receivable and those that are payable. Although duration match-funding mitigates exposure to interest rate increases, investors won't truly know how good (or bad) a job management has done until it may be too late to avoid unexpected losses.

Mortgage REIT profitability can also be challenged in a falling interest rate environment. When rates fall, mortgages and businesses refinance debt at lower interest rates. Such prepayment activity will alter the cash flows of the MBS in which mortgage REITs may have invested and dampen the resulting yield. Because mREIT profitability can be challenged by any change in interest rates, investors are better served to invest in these REITs only when they feel confident that the interest rate environment will be stable during their investment period.

Office REITs

In 2015, NAREIT listed 28 companies as office REITs, with total assets of $145.6 billion (Table 5.10). Office REITs own everything from high-rise buildings in major metropolitan areas such as New York City, to low- and mid-rise suburban office space in secondary office markets such as Charlotte, North Carolina. Within each market, location plays a major role in determining current rental rates, future rent increases, and property occupancy. Depending on the market, properties located in a city's central business district (CBD) may garner higher rents than suburban locations due to proximity to public transportation lines, industry resources, and/or the labor force targeted by corporations doing business there. In contrast, suburban office buildings may be attractive to tenants because of their location relative to executive housing, ample parking, and worker preference to drive to work.

Office buildings are also classified based on building quality (construction and materials), conditions of their mechanical and other internal systems, in-building amenities (such a gym or restaurant), and location. Newer buildings typically are deemed to be Class-A properties. Older buildings that have less efficient mechanical and electrical systems, or that are simply less aesthetically pleasing, tend to be classified as Class-B or Class-C. Although these ratings are subjective and vary from market to market, they

Table 5.10 Office REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Boston Properties, Inc.	BXP	$18,379	www.bostonproperties.com
SL Green Realty Corp.	SLG	19,858	www.slgreen.com
Paramount Group, Inc.	PGRE	8,794	www.paramount-group.com
Alexandria Real Estate Equities	ARE	8,911	www.are.com
BioMed Realty Trust, Inc.[†]	BMR	6,461	www.biomedrealty.com
Hudson Pacific Properties, Inc.	HPP	6,254	www.hudsonpacificproperties.com
Douglas Emmett, Inc.	DEI	6,066	www.douglasemmett.com
Kilroy Realty Corporation	KRC	5,939	www.kilroyrealty.com
Gramercy Property Trust Inc.[a]	GPT	5,841	www.gptreit.com
Equity Commonwealth	EQC	5,244	www.eqcre.com
Select Income REIT	SIR	4,696	www.sirreit.com
Columbia Property Trust, Inc.	CXP	4,678	www.columbiapropertytrust.com
Brandywine Realty Trust	BDN	4,555	www.brandywinerealty.com
Highwoods Properties, Inc.	HIW	4,493	www.highwoods.com
Piedmont Office Realty Trust	PDM	4,435	www.piedmontreit.com
Mack-Cali Realty Corporation	CLI	4,063	www.mack-cali.com
Corporate Office Properties Tr	OFC	3,909	www.copt.com
Parkway Properties, Inc.[b]	PKY	3,619	www.pky.com
Empire State Realty Trust, Inc.	ESRT	3,301	www.empirestaterealtytrust.com
NorthStar Realty Europe	NRE	2,683	www.nrecorp.com
Cousins Properties Incorporated[b]	CUZ	2,598	www.cousinsproperties.com
Government Properties Inc Tr	GOV	2,175	www.govreit.com
New York REIT, Inc.	NYRT	2,072	www.nyrt.com
Franklin Street Properties	FSP	1,921	www.franklinstreetproperties.com
TIER REIT, Inc.	TIER	1,874	www.tierreit.com
First Potomac Realty Trust	FPO	1,450	www.first-potomac.com
Easterly Government Properties, Inc.	DEA	912	www.easterlyreit.com
City Office REIT, Inc.	CIO	444	www.cityofficereit.com
Total for 28 REITs:		$145,626	

*As of December 31, 2015, in millions of dollars.
[†]In January 2016, BioMed Realty Trust (former NYSE: BMR) was taken private.
[a]In December 2015, Gramercy acquired Chambers Street Properties (former NYSE: CSG).
[b]In April 2016, Parkway Properties and Cousins Properties announced they will merge; the transaction is expected to be complete before the end of the year.
Source: NAREIT, S&P Global Market Intelligence.

are useful for benchmarking rents and property values on a local, regional, or national level. It is possible, for example, to have a Class-A building in a B or C market, and, therefore, only achieve rents that are competitive with other Class-B or -C buildings.

Lease Terms

Office leases typically are full-service leases with an initial term of five to seven years, plus one or more multiple-year renewal options. In a full-service lease (see Chapter 4, Leases), the landlord is responsible for all the operating expenses of the property, including landscaping, real estate taxes, and insurance, but generally the landlord is able to pass most expenses back to the tenant in the form of the expense stops associated with the full-service lease, and common-area maintenance, or CAM, charges. Office leases commonly include annual rent escalations (also called *bumps* or *stepups*) that insulate the landlord's profit margin from costs that rise with inflation.

Risks and Rewards of Office REITs

Office REIT returns are more cyclical than the average equity REIT's due to periodic overbuilding. (Also see Chapter 7, REIT Performance.) If demand for new space does not keep pace with the increase in supply, office vacancy in that market will rise and rental rates will decline. The office sector's longer building cycle is a primary contributing factor to historical overbuilding. During the two or more years it generally takes to complete an office tower, local demand for office space, which is a function of job growth and the local economy, can change materially and cause a building to sit vacant or mostly vacant until demand for office space recovers.

The way tenants use their space can also dramatically alter demand for office space, even in a growing economy. The advancement in communications over the past two decades has made working from home a viable alternative for some workers. Although not all office cultures or industries lend themselves to allowing workers to perform their duties offsite, the ability to work remotely has dampened the overall need for office space in most locations. Densification is a second trend that has dramatically reduced the need for office space in the past 15 years. In 2000, employers generally budgeted 250 square feet of space per employee. Today, the range is between 125 and 225 square feet per employee and an average of around 175 square feet per employee, representing an average decrease in demand of 30 percent. Densification, which is simply space planning more employees into the same square feet of office space, has largely run its course, to the relief of office landlords. However, the way people use—or don't use—formal office space to do their jobs is an ongoing challenge the office property sector faces.

Residential REITs

The residential REIT sector encompassed 23 REITs at the end of 2015 with total assets of $123.6 billion. There are three subcategories of residential REITs: apartments (or *multifamily*), manufactured homes, and single-family homes.

Apartment REITs

NAREIT lists 16 apartment REITs with total assets of $93.4 billion (Table 5.11). Historically, apartment REITs included only companies that owned traditional apartment buildings. More recently, however, the group expanded to include REITs that own student housing apartment complexes.

Traditional apartment buildings are classified as either garden-style or high-rise buildings. Garden-style apartments contain multiple buildings that usually are one to four stories in height and are configured around the center of the community, typically a pool or other common area(s). High-rise apartment buildings are just that: high-rise buildings that contain apartments. High-rise apartments typically are built in high-density cities or town centers where the cost of land and the monthly rental rates the landlord can charge support the additional cost per square foot associated with high-rise construction.

In both formats, apartment properties generally contain a mix of studio, one-, and two-bedroom apartment units. Properties also are classified as Class-A, B, or C. Class-A buildings include newer buildings in prime locations. Buildings in Class-B and C categories tend to be older, offer residents fewer amenities, and, perhaps, are located in less desirable locations. Rental agreements for apartment units typically are for 12 months at a time. A tenant generally may cancel a lease, however, by providing one or more months' notice, typically in writing. The landlord is responsible for the cost of

Table 5.11 Apartment REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Equity Residential	EQR	$23,157	www.equityapartments.com
AvalonBay Communities, Inc.	AVB	16,931	www.avalonbay.com
Essex Property Trust, Inc.	ESS	12,005	www.essex.com
UDR, Inc.[a]	UDR	7,664	www.udr.com
MAA[b]	MAA	6,848	www.maac.com
Apartment Investment and Management Company[c]	AIV	6,144	www.aimco.com
Camden Property Trust	CPT	6,038	www.camdenliving.com
American Campus Communities, Inc.	ACC	6,026	www.americancampus.com
Monogram Residential Trust, Inc.	MORE	3,283	www.MonogramResidentialTrust.com.
Post Properties, Inc.	PPS	2,272	www.postproperties.com
Education Realty Trust, Inc.	EDR	2,002	www.edrtrust.com
Campus Crest Communities†	CCG	1,584	www.campuscrest.com
Independence Realty Trust, Inc	IRT	1,392	www.irtreit.com
Preferred Apartment Communities, Inc.	APTS	1,296	www.pacapts.com
NexPoint Residential Trust, Inc.	NXRT	976	www.nexpointliving.com
Bluerock Residential Growth REIT, Inc.	BRG	703	www.bluerockresidential.com
Total for 16 REITs:		$98,321	

*As of December 31, 2015, in millions of dollars.
[a]UDR will be added to the S&P 500 Index in 2016.
[b]Formerly called Mid-America Apartment Communities, Inc.
[c]This REIT most commonly goes by "Aimco" but has not changed its name officially.
†This company was taken private in January 2016. Assets shown are as of September 30, 2015.
Source: NAREIT, S&P Global Market Intelligence.

maintaining the property; however, similar to a full-service lease, the tenant's rent essentially covers costs paid by the landlord. Except in properties where it is possible to meter individual utilities, a landlord also factors into the rental rate reasonable costs for water and heating, ventilation, and air conditioning (HVAC) services.

Steady Demand for Apartment Units

Similar to office space, demand for apartments is highly correlated with employment trends. As employment in an area increases, demand for apartments to house new workers who in-migrate to that area also increases. In contrast to the office sector, demand for apartments also increases when employment decreases, as some former homeowners sell their houses and go back to renting. When unemployment rises, apartment landlords tend to decrease monthly rents and/or offer concessions in the form of months of free rent and, depending on local competition, free garage parking and fitness center memberships in order to maintain occupancy levels. When the economy recovers and is expanding, apartment landlords take advantage of their shorter lease lengths to increase rents more aggressively each year and quickly stop offering concessions to attract or retain tenants.

Risks and Rewards of Apartment REITs

Because demand for apartments tends to be fairly steady, the main risk associated with this sector is the risk of oversupply. As rental rates for apartments increase, private developers and public REITs tend to develop more apartment buildings to take advantage of strong demand. As with any property type, too much supply results in lower rental rates and/or occupancy levels in a market. This in turn usually leads to a decline in the stock prices of apartment REITs with meaningful exposure to the market(s) viewed as becoming overbuilt.

Manufactured Housing REITs

There are only three manufactured housing REITs, with combined assets of $8.2 billion (Table 5.12). Commonly known as mobile homes, manufactured housing communities are a lower-cost

Table 5.12 Manufactured Housing REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Sun Communities, Inc.	SUI	$4,191	www.suncommunities.com
Equity LifeStyle Properties, Inc.	ELS	3,420	www.equitylifestyle.com
UMH Properties, Inc.	UMH	604	www.umh.com
Total for 3 REITs:		$8,215	

*As of December 31, 2015, in millions of dollars.
These REITs generally use ground leases.
Source: NAREIT, S&P Global Market Intelligence.

alternative to homeownership, which makes them popular among retirees and lower-income workers. REITs in this property niche own land that is rented to individuals pursuant to a ground lease. Tenants purchase prefabricated houses that are placed in an approved location within the community. In addition to providing sites for houses, newer manufactured home communities may also include community-focused amenities, such as lighted streets, swimming pools, and a community recreation facility or clubhouse. The landlord (REIT) receives a monthly fee from each tenant for the right to locate his home on the property. Although individuals technically could move out in any given month, the relatively high cost associated with moving the residence to a competing community tends to translate into a very high renewal rate and in turn a fairly stable income stream to the landlord.

Single-Family-Home REITs

At the end of 2015, there were four REITs that own single-family houses for rent, which NAREIT recently carved out of specialty REITs and placed into their own subproperty type called single-family-home REITs (Table 5.13). (Note in Table 5.13 that two of these four companies are merging in 2016.) This subcategory of residential REITs grew out of the business opportunity the Great Recession of 2008–2009 presented to buy houses at deeply discounted prices and lease them back to the former owners or new occupants.

Table 5.13 Single-Family Home REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Colony Starwood Homes[a]	SFR	$7,700	www.colonystarwood.com
American Homes 4 Rent[†]	AMH	6,808	www.americanhomes4rent.com
American Residential Properties, Inc.[†]	ARPI	1,359	www.amresprop.com/Home
Silver Bay Realty Trust Corp.	SBY	1,224	www.silverbayrealtytrustcorp.com
Total for 4 REITs:		$17,091	

*As of December 31, 2015, in millions of dollars.
These REITs generally use triple-net leases.
[a]In January 2016, Starwood Waypoint Residential Trust (former NYSE: SWAY) merged with Colony American Homes. Assets shown are estimated, based on September 30, 2015 balance sheet data.
[†]In February 2016, these two REITs merged. Assets for ARPI are as of September 30, 2015.
Source: NAREIT, S&P Global Market Intelligence.

Retail REITs

In 2015, the retail REIT sector included 34 REITs with combined assets of $192.3 billion. NAREIT tracks three subcategories of retail REITs: 19 shopping center REITs with $71.7 billion of assets, eight regional mall REITs with $86.8 billion of assets, and seven freestanding retail REITs with total assets of $33.7 billion.

Initial lease terms to anchor tenants—the larger box tenants used to draw traffic to the retail center—generally are negotiated for 15 to 20 years. Inline tenants are the smaller shops in a center and generally lease their space for 5 to 10 years. Retail landlords typically employ net or modified gross leases (please refer to Chapter 4, Leases). Retail landlords also may receive percentage rents in addition to their face rents and CAM fees. Percentage rents are calculated as a portion (typically 1 to 2 percent) of revenue a tenant achieves in any given year above the base (or initial) year revenue. For example, assume Tenant A generates revenue of $100 per square foot (PSF) during the first year of its lease. If Tenant A generates $110 in revenue PSF in the following year and the landlord has negotiated to receive 1 percent of rents above the base-year revenue, then the landlord will receive an additional $0.10 PSF in percentage rents. During times of economic expansion, landlords can enhance the overall yield on their properties from percentage rents. When economic growth slows or contracts, however, the landlord may receive no percentage rents, which would represent downside risk to the retail REIT's earnings.

Shopping Center REITs

The term *shopping center* encompasses a range of formats, from grocery store–anchored neighborhood and community centers to power centers. According to the International Council of Shopping Centers (ICSC), shopping centers range in size from 30,000 to 150,000 square feet and serve the area within a three-mile radius of their locations. Table 5.14 shows the 19 shopping center REITs tracked by NAREIT.

Neighborhood and community centers are among the most defensive property types because, if they are well located, they remain well leased regardless of broader economic trends. Anchor tenants at shopping centers generally are grocery or drugstores,

Table 5.14 Shopping Center REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Kimco Realty Corporation	KIM	$11,344	www.kimcorealty.com
Brixmor Property Group Inc.	BRX	9,498	www.brixmor.com
DDR Corp.	DDR	9,097	www.ddr.com
Federal Realty Investment Trust	FRT	4,912	www.federalrealty.com
Retail Properties of America, Inc.	RPAI	4,621	www.rpai.com
Regency Centers Corporation	REG	4,191	www.regencycenters.com
Weingarten Realty Investors	WRI	3,902	www.weingarten.com
Kite Realty Group Trust	KRG	3,766	www.kiterealty.com
Equity One, Inc.	EQY	3,376	www.equityone.net
Acadia Realty Trust	AKR	3,032	www.acadiarealty.com
Tanger Factory Outlet Centers, Inc.	SKT	2,327	www.tangeroutlet.com
Retail Opportunity Investments Corp.	ROIC	2,311	www.roireit.net
Ramco-Gershenson Properties Trust	RPT	2,129	www.rgpt.com
Urban Edge Properties	UE	1,919	www.uedge.com
Inland Real Estate Corporation†	IRC	1,522	www.inlandrealestate.com
Cedar Realty Trust, Inc.	CDR	1,322	www.cedarrealtytrust.com
Saul Centers, Inc.	BFS	1,304	www.saulcenters.com
Urstadt Biddle Properties Inc.	UBA	861	www.ubproperties.com
Wheeler Real Estate Investment Trust, Inc.	WHLR	314	www.whlr.us
Total for 19 REITs:		$71,747	

*As of December 31, 2015, in millions of dollars.
†This REIT was taken private in January 2016 and is no longer public.
Source: NAREIT, S&P Global Market Intelligence.

designed to draw traffic to the center. Shopping center inline tenants tend to sell necessary consumer items and services, such as dry cleaning and shoe repair. As a result, demand for neighborhood and community shopping center space tends to be fairly stable (or *inelastic*), as evidenced by their high historical occupancy rates that typically range between 89 and 94 percent. Similar to industrial properties, new supply of shopping centers tends to track demand due to the short development time.

Power centers consist only of big-box, national retailers such as Bed Bath & Beyond, Petco, Dick's Sporting Goods, and Home Depot. According to ICSC, the average power center is between 250,000 and 600,000 square feet and has a primary trade area of 5 to 10 miles.

Although the goods sold at these stores are everyday in nature, they tend not to be true necessity items. Consumers, therefore, may substitute less-expensive brands during an economic downturn. Part of the major draw to power centers, however, is the convenience of shopping at a center that offers a series of anchor tenants clustered in one location.

Mall REITs

Malls are classified as regional or super-regional, depending on how large they are and what population base they serve. According to ICSC, regional malls are generally between 400,000 and 800,000 square feet in size and have at least two anchor tenants, such as Nordstrom (NYSE: JWN). Super-regional malls are at least 800,000 square feet in size, have at least three anchor tenants, at least one of which offers luxury and/or fashion goods, such as Neiman Marcus; and super-regional malls are the dominant shopping venue within a 25-mile radius. Malls also are classified as being Class-A or Class-B in quality, depending on location, the anchor tenants, average household income in the surrounding trade area, all of which influence a mall's sales per square foot—an essential metric for comparing productivity among different malls. Table 5.15 shows the eight regional mall REITs tracked by NAREIT.

Table 5.15 Mall REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Simon Property Group, Inc.	SPG	$30,651	www.simon.com
General Growth Properties, Inc.	GGP	24,074	www.ggp.com
Macerich Company	MAC	11,259	www.macerich.com
CBL & Associates Properties, Inc.	CBL	6,480	www.cblproperties.com
WP Glimcher Inc.	WPG	5,479	www.wpglimcher.com
Taubman Centers, Inc.	TCO	3,563	www.taubman.com
Pennsylvania REIT	PEI	2,807	www.preit.com
Rouse Properties, Inc.†	RSE	2,529	www.rouseproperties.com
Total for 8 REITs:		$86,841	

*As of December 31, 2015, in millions of dollars.
†In January 2016, a private equity firm made an unsolicited offer to take Rouse Properties private; accordingly, this REIT is not likely to remain publicly traded.
Source: NAREIT, S&P Global Market Intelligence.

Anchor tenants may lease their space, though many prefer to own their stores. Since a landlord selects an anchor tenant primarily for that tenant's ability to draw consumers to the mall itself, the choice of anchor tenants is crucial to the overall success of a project. In between anchor tenants are smaller retailers referred to as inline shops. These tenants include national retailers such as The Gap, as well as regional and local retailers. Malls typically are located in close proximity to or within major metropolitan areas and/or areas that have above-average household income levels in order to maximize sales per square foot and profitability.

Freestanding Retail REITs

Freestanding retail properties house a wide array of businesses, including fast-food and sit-down restaurants (such as Burger King and Macaroni Grill, respectively), drugstores, movie theaters, day-care services, automotive care, and gas stations. REITs that own freestanding retail properties typically use triple-net leases with their tenants (see Chapter 4, Leases). By using triple-net leases, the tenants have full control over their property operations, including staying open late or all night for business. Alternatively, if these tenants rented space in a shopping center or mall, they would be subject to that center's operating hours and other criteria. NAREIT tracks seven freestanding retail REITs, as shown in Table 5.16.

Table 5.16 Freestanding Retail REITs

Company Name	Ticker Symbol	Total Assets*	NAREIT Sub-Property Type	Website Address
Realty Income Corporation	O	$11,866	Single-Tenant	www.realtyincome.com
Spirit Realty Capital, Inc.	SRC	7,919	Diversified	www.spiritrealty.com
National Retail Properties	NNN	5,460	Single-Tenant	www.nnnreit.com
STORE Capital Corp	STOR	3,911	Diversified	www.storecapital.com
Seritage Growth Properties	SRG	2,833	Other Retail	www.seritage.com
Getty Realty Corp.	GTY	899	Single-Tenant	www.gettyrealty.com
Agree Realty Corporation	ADC	793	Single-Tenant	www.agreerealty.com
Total for 7 REITs:		$33,681		

*As of December 31, 2015, in millions of dollars.
These REITs generally use long-term triple-net leases and/or ground leases.
Source: NAREIT, S&P Global Market Intelligence.

In the past few years, three of the freestanding retail REITs listed in Table 5.16 (Seritage, Spirit, and STORE) joined the ranks of publicly traded REITs. Growth in this once sleepy subcategory of retail REITs is being fueled by increased comfort tenants have gained to lease rather than own their real estate. In a sale/leaseback transaction, an owner that occupies a property sells the building to a new owner/landlord, then leases back that same space, typically using a long-term triple-net lease. An increasing number of businesses are willing to monetize their real estate holdings through sale/leaseback transactions with REITs. By doing so, the businesses free up precious capital to deploy back into their operations while still maintaining fundamental control over their locations.

Risks and Rewards of Retail REITs

As the 2015 holiday shopping season evidenced, consumers increasingly are shopping for gifts and necessary items online rather than in retail stores. Internet sales, often referred to as e-commerce, are encroaching on the profitability of traditional brick-and-mortar stores. In January 2016, for example, in the wake of weak holiday sales, Walmart Stores (NYSE: WMT) announced it would close 269 stores worldwide in 2016, including 154 in the United States, to focus on its supercenters and e-commerce business. Similarly, Macy's (NYSE: M) announced it would close 36 stores. As e-commerce proliferates, retailers—and the REITs who act as their landlords—will need to innovate to retain market share and profitability. One effective strategy retail REITs use to mitigate the risk of losing tenants and market share to e-commerce retailers, such as Amazon.com, Inc. (NASDAQ: AMZN), is to own the most attractive locations, often measured by the average household and discretionary income levels within a one-, three-, or five-mile radius of retail centers. Such attractive locations tend to support higher sales per square foot leased for their tenants, meaning the space they rent is more productive and profitable than secondary locations. When retailers close stores, they close their least productive ones. A second strategy landlords use to maintain the revenue per square foot at their centers is to lease space to tenants that offer necessary items (such as groceries and dry cleaning) or, at the other end of the consumption spectrum, luxury goods.

Self-Storage REITs

The FTSE NAREIT All REITs Index classifies five companies as self-storage REITs with combined assets of $22.2 billion (Table 5.17). Similar to what drives the apartment sector, demand for self-storage units is driven by population growth, people moving locations for jobs or other reasons, as well as the urge many people have to archive things for future generations or the simple inability to throw anything away. Individuals who rent apartments or who live in condominiums tend to rent self-storage space. Customers select storage facilities based on price, location, security, and suitability of space to their needs. Property owners rarely depend on one customer for large portions of revenue because individual consumers (rather than businesses) represent the majority of self-storage users. The storage units themselves are simple structures located near busy roads in order to ensure visibility. They require little capital expenditures outside of roof or parking lot/pavement repairs.

Risks and Rewards of Self-Storage REITs

Self-storage units are rented on a month-to-month basis, which can create volatility in rental rates during times of weak or robust demand. Historically, oversupply had been the primary risk associated with this sector. Although the facilities take little time to construct, highly fragmented ownership historically led to less

Table 5.17 Self-Storage REITs

Company Name	Ticker Symbol	Total Assets*	Website Address
Public Storage	PSA	$9,778	www.publicstorage.com
Extra Space Storage Inc.†	EXR	6,071	www.extraspace.com
CubeSmart	CUBE	3,115	www.cubesmart.com
Sovran Self Storage, Inc.	SSS	2,122	www.unclebobs.com
National Storage Affiliates Trust	NSA	1,102	www.nationalstorageaffiliates.com
Total for 5 REITs:		$22,189	

*As of December 31, 2015, in millions of dollars.
†In 2016, Extra Space Storage will be added to the S&P 500 Index.
Source: NAREIT, S&P Global Market Intelligence.

transparent supply-and-demand information than for other commercial property types. As the REITs in this space have grown by acquiring local operators, the sector's supply issues have waned and the sector has tended to outperform other property types.

Conclusion

REIT performance varies by property sector, as each type of real estate is impacted differently by larger economic trends. Chapter 7 provides a more in-depth analysis of REIT performance, including a comparison by property sector.