

**REAL ESTATE
ASSET ENHANCEMENT PROGRAM
*RETAIL***



*A CASE STUDY FROM
AMERICAN REALTY ADVISORSSM*



801 North Brand Boulevard, Suite 800, Glendale, CA 91203
818-545-1152 www.americanreal.com

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RETAIL

CHINO HILLS, CA

In 2001, American Realty Advisors, on behalf of one of its value-added separate account clients, originated a mezzanine loan to a group of Los Angeles based local investors with a successful track record in the re-positioning of Southern California retail properties. The investment was used to assist in the acquisition of a 325,783 square foot community shopping center, originally built in 1990, located in the bedroom community of Chino Hills, California, in San Bernardino County.

Before the Fund's investment, the project had been poorly managed with a strategy that lacked focus and direction. The original owner reportedly purchased the property in 1995 for \$35 million as part of a strategy to assemble a portfolio of West Coast retail properties, with the intent to recapitalize it through a public REIT trust offering. The strategy was unsuccessful and the original owner elected to dispose of all of the portfolio assets. The project was one of the last of the assets to be liquidated.

Investment Background

At the time of acquisition, the project lacked a grocery anchor tenant. Originally, Lucky Stores had occupied approximately 40,000 square feet, but with the merger of Lucky and Albertson's, this store's location had closed. Both Lucky/Albertson's and the original owner attempted to sub-lease the space to another grocery tenant, but were unsuccessful. A non-union grocery operator, KV Mart, then attempted to open a store at the project, but closed after only a few unsuccessful months in operation.

Unable to find a viable replacement tenant for the grocery space and under pressure to liquidate the asset, the original owner decided to sell the Project with the grocer space "dark."

American became aware of this opportunity through its extensive network of real estate investors and mortgage brokers. Immediately recognizing the upside potential of the transaction, American approached the borrower and offered to provide financing on behalf of its clients, conditioned upon the borrower re-leasing the grocery space to a union-represented food employer. The borrower, before American's involvement, was still considering both union and non-union opportunities.



With an agreement on the terms of potential financing from the client, the borrower was then able to enter into negotiations with Vons client to relocate one of their stores from an existing older location across the street. Vons is owned by Safeway and its employees are members of the United Food and Commercial Workers union.

Vons had outgrown its store, which was less than 40,000 square feet with limited parking. By moving across the street, they were able to expand their grocery space to 55,000 square feet and open a brand new store with a more modern design. In addition, by moving, Vons was able to improve its location by being on the "drive home" side of street.

Financial Structure

The borrower agreed to purchase the project for a price of \$27.7 million, or \$85 per square foot of rentable building area. The purchase price was well below replacement and nearly 21% below what the original owner paid in 1995. Additionally, based upon the existing cash flow in place, the purchase price equated to a "going in" capitalization rate of over 10.5%. Additional investment costs of nearly \$4.3 million, including Vons leasing costs as well as other capital costs, brought the

total project investment to \$32 million. The appraised value of the project was \$35.3 million with the new Vons lease in place.

American's funding included an original loan amount of \$5,750,000, with an additional funding of up to \$400,000, a commitment fee of 1% of the maximum loan amount, a rate of 9% (fixed) with contingent interest of 100% of all project cash flow, after the senior debt service and the fixed interest, was due and payable to the borrower until American's clients had earned an 18% internal rate of return. The borrower's equity was in the form of cash and provided for a 9% return on investment, which was fully subordinate to the senior debt service and the fixed interest. In other words, the transaction was structured so that the borrower would not see any significant cash flow from the project until American's client had earned a minimum 18% internal rate of return.

Value Realized

The primary goal was to get the Vons store opened, and with the momentum created, re-lease and/or re-tenant a large portion of the in-line shop space at higher economic rents. Approximately 20% of the in-line shop space had lease terms which were expiring at the end of the year, or had tenants on unfavorable month-to-month lease terms. Construction on the new Vons store began in September 2001 and the store opened in January 2002.

A pro-active leasing program resulted in the renewal of nearly 95% of the expiring or month-to-month leases, at rental rates, on average, 5% to 15% above pro-forma. Additionally, several new leases were entered into with strong local and regional retail operators. While it was initially anticipated that the re-leasing program would take between 18 and 24 months, the Project in the first quarter of 2002 was leased to a stabilized occupancy level of 95%.

Investor interest in the Project was high, and an agreement

to purchase the project at a price of over \$35 million was entered into with a large REIT headquartered in Texas. The transaction closed in August 2002.

As a result, the Fund received its fixed interest, exit fees of 2%, plus its share of the project's profit.

American Realty Advisors

American Realty Advisors, a California corporation, is an SEC-registered investment advisor under the Investment Advisers Act of 1940 and a leading provider of real estate investment management services to institutional investors. With more than \$3.4 billion in gross assets under management (excluding partners' share of equity and partners' share of debt on partnership investments) as of September 30, 2009, American has provided real estate investment management services to institutional investors for over 21 years utilizing core and value-added commingled funds and separate accounts.

The Firm's portfolios include office, industrial, multi-family, and retail properties nationwide. Additional information regarding American can be found online at www.americanreal.com.

In addition, American is a significant originator of debt financing for real estate investments utilizing various structures from senior debt to highly structured mezzanine or preferred equity formats, secured by mortgages or other interests in real estate. Our conservative cash flow underwriting, proactive investment management and ability to structure transactions has produced superior risk-adjusted returns on behalf of our clients.



**AMERICAN
REALTY ADVISORS**

Institutional Real Estate Investment Management

Stanley L. Iezman
President & CEO

Scott W. Darling, *Managing Director, Portfolio Management*

Kirk V. Helgeson, *Managing Director, Investments*

Jay Butterfield, *Managing Director, Fund/ Separate Accounts*

801 North Brand Boulevard, Suite 800
Glendale, CA 91203

P: (818) 545-1152 ♦ F: (818) 545-8460

www.americanreal.com ♦ www.qpam.com





If you would like information regarding this project, including returns, or for any other information regarding American Realty Advisors, please contact Jay Butterfield at 818-409-3243 or at butterfield@americanreal.com

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