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GGP Merger Would Make Simon A Force to Reckon With For Tenants and Lenders

Feb 17, 2010 1:33 PM, By Elaine Misonzhnik, a special to NREI from sister publication Retail Traffic

As it's becoming increasingly clear that Simon Property Group Inc. and General Growth Properties Inc. are engaging in the [early stages](#) of merger negotiations, retail real estate professionals are starting to weigh the effects a potential transaction would have on the industry landscape.

Many observers concede that a merger would be good for industry morale, as it would allow Chicago-based General Growth, the poster child for the excesses of the boom years, to emerge from bankruptcy protection in less than a year. Furthermore, it might spur other investment activity and help loosen the capital markets. But if a deal does go through, it would also make Indianapolis-based Simon Property Group a force to reckon with for tenants, vendors and lenders and might make negotiations with the mall giant difficult, industry sources say.

“Certainly, having General Growth survive in one form or another, is very important to all of us, whether we are on the landlord side or on the tenant side,” says Branson Edwards, executive vice president and managing director of retail occupier services with commercial real estate services firm Grubb & Ellis. “Any outcome that’s positive for General Growth is positive for the industry and Simon is a very well-run company. But ... the observation we are all making on the tenant side is, the larger a mall owner is, the more difficult they are to deal with and the more likely they are to try to cross-negotiate transactions and have retailers go into spaces they wouldn’t otherwise go into in order to lease the spaces they would like to lease.”

There might be positives to dealing with a landlord of that size as well, however. Edwards notes that leasing and management representatives from large REITs tend to be more professional during negotiations and make the tenants aware of their deal conditions from the get-go, speeding up the leasing process. Plus, a landlord that owns several high-quality malls in the same market might offer retailers more choices when they are looking at new locations, adds Greg Maloney, CEO and president of Jones Lang LaSalle Retail, an Atlanta-based third party property manager.

Of course, at this point, a deal between Simon and General Growth is far from certain. Many in the industry believe Monday’s offer reflects an opening price and there will likely be several rounds of offers and counter-offers from rival bidders before any kind of a resolution is reached. For example, Robert McMillan, REIT analyst with New York City-based Standard & Poor’s Equity Research, would not discuss whether the current bid reflects the fair value of General Growth, but noted that “Simon is making an offer that I think is in their best interest, that’s hopefully, accretive to their shareholders.”

Tuesday night, General Growth responded to Simon with a letter of its own. ([see response](#)) The letter explained that General Growth is still exploring its options in maximizing value from shareholders.

According to the letter, General Growth is "about to commence a process to explore several potential options for the Company's emergence from Chapter 11, including a sale of the entire Company." It plans to finalize the information memorandum and to send materials to participants in the process by the beginning of March.

Maloney declined to discuss the pricing as well, but pointed out that in most transactions of this kind, it usually takes weeks or months to get everyone to agree on the particulars.

"It looks like a pretty fair offer from our perspective, but I guess General Growth is going to try and continue with their process and see what other opportunities they have available," says Todd Lukasik, an analyst with Morningstar.

The \$10 billion offer--which works out to be \$7 billion to pay down creditors and \$3 billion for shareholders--values General Growth at about \$9 per share. That's less than where the firm's stock is trading on over-the-counter markets. Furthermore, William Ackman, founder and CEO of hedge fund Pershing Square Capital Management, controls about 25 percent of General Growth's stock and sits on the company's board. In December, Ackman argued that General Growth should be valued at between \$24 per share and \$43 per share.

Besides Simon, one obvious contender for General Growth would be Brookfield Asset Management Inc., which owns approximately \$1 billion of the REIT's unsecured debt. Canada-based Brookfield has long made known its desire to enter the U.S. mall market and might be in a stronger financial position for an acquisition of that size, according to Todd Sullivan, a Massachusetts-based investor and author of the Value Plays blog.

In fact, on Tuesday, credit agency Moody's Investors Service placed Simon's debt rating under review, as the agency worries the REIT's financial standing could suffer from the high leverage and secured debt associated with the General Growth portfolio.

Still, "General Growth has some pretty good assets, anchored by long-term leases that produce pretty stable cash flow," says McMillan. "So it's not like [acquisitions made] in the boom years."