

REAL-ESTATE FINANCE

Why Investors Trust Vornado

Missing Out on Equity Office Opens Up Other Opportunities; Expect a Measured Approach

By JENNIFER S. FORSYTH

Twice over the past six months, **Vornado Realty Trust** pursued the acquisition of a rival real-estate investment trust and came up empty-handed. But don't look for the New York company to try another flashy deal just to prove it can.

Investors and analysts say they believe Vornado will settle back into the role in which it feels most comfortable: looking for unique opportunities for real-estate investment with reliable returns without taking on much debt.

The options aren't obvious, at least if Vornado is looking to acquire more office property. Prices for office buildings in the markets where Vornado concentrates—New York and Washington, D.C.—are at record levels, making bargains almost impossible to find. "I don't really know where they are going to go with their capital," says Matthew Ostrower, a REIT analyst with Morgan Stanley.

Vornado is just as likely to turn its attention to other types of investments. Vornado joined two private-equity partners to take Toys "R" Us private in July 2005 and, the same year, invested heavily in **McDonald's Corp.**—two companies with decidedly different business models from Vornado's. A similar deal, such as buying another retailer or some other company with valuable real-estate holdings, is within the realm of possibility for Vornado, analysts say.

Whatever Vornado's next move, investors and analysts expect the same opportunistic but measured approach that has characterized Chief Executive Steven Roth in the past.

"I don't think they would do something in a knee-jerk reaction," says Ross Smotrich, senior REIT analyst for Bear Stearns. "On the other hand, the way they go about business is by looking out for these kinds of opportunities and they are not afraid to pursue them."

Indeed, Vornado chased a big fish—and a whale—simultaneously last year.

In July, Vornado bid for **Reckson Associates Realty Corp.** of Uniondale, N.Y., but eventually lost out to another REIT. At the same time, Vornado was discussing a possible merger with Equity Office Properties Trust, the nation's largest office landlord founded by real-estate legend Sam Zell. But eventually discussions fell apart and Equity Office announced in November it was being acquired by private-equity giant **Blackstone Group** for \$48.50 a share.

In January, Vornado made another run at Eq-

uity Office with a higher bid. A bidding war ensued and Vornado went as high as \$56 a share in cash and stock before bowing out. Blackstone won the support of Equity Office's board with an all-cash offer of \$55.50 and closed the \$39 billion deal, including debt, Friday.

Yet, the market wasn't disappointed. Vornado stock jumped 7% the day the company gave up. Vornado shares rose \$2.93, or 2.2% to \$134.32 in 4 p.m. composite trading on the New York Stock Exchange yesterday.

After coming within a breath of winning Equity Office, most any deal Mr. Roth and President Michael Fascitelli conceive of is presumably within reach. Christopher Haley, a REIT analyst with Wachovia Capital Markets, estimates Vornado's available cash and liquidity at more than \$3 billion. Vornado executives declined to comment.

Vornado's recent purchase of 350 Park Avenue in Manhattan at about \$931 per square foot (or a first-year yield below 4%) shows that the company is more comfortable with current market prices than some analysts might have guessed. Still, prices keep getting steeper. As part of its closing on the Equity Office deal, Blackstone arranged for the New York portfolio (save for 1095 Avenue of the Americas) to be sold simultaneously to Macklowe Properties for \$7 billion or \$1,100 a square foot—a price that Mr. Haley described as "unbelievable."

Vornado doesn't have to make big moves to keep shareholders happy. Simply completing the varied and significant development projects it has planned should pay off handsomely. Perhaps the most important of these are Vornado's plans—with its partner, **Related Cos.**—to remake the Madison Square Garden arena and the Penn Station commuter hub, opening up the possibility to build millions of square feet of retail and office space. David Greenbaum, a Vornado executive vice president, recently told a shareholder group that he expected the public approval process on these plans to begin in the next 12 months.

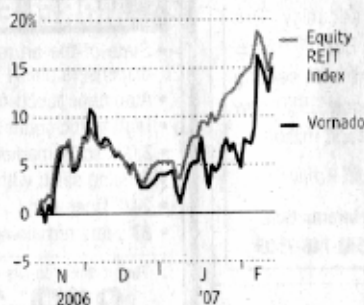
Also, real-estate services firm **Grubb & Ellis Co.** recently reported that Vornado plans to replace the nearby Hotel Pennsylvania with a 2.5 million square-foot office tower that will include five trading floors.

To be sure, Mr. Roth isn't King Midas. The company's investment in **GMH Communities Trust**, a student and military housing company, while initially successful, hit what Mr. Roth called a "speed bump" in the public markets—making it a less attractive investment than other alternatives.

Yet, investors are willing to overlook missteps from a company that has delivered average total returns of 30% over the past five years. Says Dean Frankel, domestic portfolio manager of Urdang Securities Management, a Vornado shareholder: "I, as an investor, expect them to do what they've always done, which is go make good deals."

Rapid Recovery

Three-month share performance of Vornado Realty Trust vs. the Dow Jones Equity All REIT Index



Sources: WSJ Market Data Group; Dow Jones Indexes