Business Headlines

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Investors Can Seek Shelter in Real Estate

By Rachel Cohen

NEW YORK (Reuters) - Real estate was a great place to hide from the Internet technology bust this year, and money managers say it should also offer protection from an economic downturn in 2001.

Gains in real estate investment trusts, companies that own a portfolio of real estate and pay most of their earnings out in dividends, have helped send the Morgan Stanley REIT index (^RMS - news) up 27.3 percent for the year as of Wednesday's market close.

In contrast, the Standard & Poor's 500 index (^SPX - news) is down 9.6 percent for the year, while the technology-dominated Nasdaq composite index (^IXIC - news) is down 37.6 percent and on track for its worst performance ever.

Entities such as AMB Property Inc. (NYSE:AMB - news) and Vornado Realty Trust (NYSE:VNO - news) are appealing because they offer high dividend yields and the average rental income they receive is almost certain to rise, barring a recession of breathtaking ferocity. They also should benefit from expected cuts in interest rates.

``In a moderate recession, people move away from growth toward income,'' said Douglas Poutasse, chief strategist at AEW Capital Management, which manages about $5.9 billion invested in real estate assets and portfolios. ``REITs give very good income.''

Real estate securities have benefited partly from the slowing economy and partly from the expectation of lower interest rates, said Eugene Profit, a senior portfolio manager at Profit Investment Management, which has $82 million in assets.

Investors are expecting the Federal Reserve, the U.S. central bank, to cut benchmark interest rates in the new year, he said, and market interest rates are declining in anticipation of that.

``REITs are an attractive hedge,'' Profit added.

Profit owns hotel REIT Host Marriott (NYSE:HMT - news), which is trading near its 52-week high of 12-7/8.

Dividends Offer Protection

AEW Capital Management's Poutasse said REIT stocks aren't risk-free, but the dividends they pay provide some protection from a decline in their share prices.

The year-to-date dividend yield for the National Association of Real Estate Investment Trusts' composite REIT index is 8.03 percent, compared with a 52-week range of 1.1 percent to 1.26 percent for the S&P 500.

Among Poutasse's picks are industrial property owners AMB Property, which is trading near its 52-week high of $25-1/2, and First Industrial Realty Trust Inc. (NYSE:FR - news), which is hovering near its year high of $34-3/4.

``When times get shaky,'' Poutasse said, ``three-to-five-year leases with people who can pay the rent'' are more attractive.

Investors who are worried that there might be a recession or at least a sharp downturn should diversify and put money into real estate securities, said Sam Lieber, senior portfolio manager at Alpine Real Estate, which manages $100 million in assets.

Lieber said he likes office real estate investment trusts as a sector play.

``Real estate does well in a downturn: unless a company goes belly up, it still has to pay rent,'' he said. ``Even if rents come down from current levels, there is still opportunity to increase your cash flow, assuming you can find tenants for the space.''

Indeed, that churning of tenants can work in favor of the REIT as the new occupants of a building often have to pay higher rents than their predecessors who negotiated a deal when the market rate was much lower.

Lieber said a company like Vornado Realty Trust, which owns a large portfolio of New York real estate, is getting rents 30 percent below market value, allowing plenty of room for increases and, consequently, earnings growth.

He expects Vornado's earnings to grow 10 percent over the next year or two. Shares of Vornado are close to their 52-week high of $40-1/2.

Outlet Space Offers Promise

Alexandria Real Estate Equities Inc. (NYSE:ARE - news), which owns property used by the pharmaceutical and biotechnology industries, is another stock Lieber likes. It is trading near its 52-week high of $38-1/2.

``It's a good period for the pharmaceutical industry,'' which is recession-proof because slowing consumer spending hardly affects demand, he said. All companies have to invest in developing new drugs, he added. Alexandria's properties are "fancier than normal industrial space," for which there is strong demand.

To be sure, money managers don't see all real estate trusts as good bets.

As retailers have struggled under slower sales and a weak holiday buying season, money managers say retail real estate has lost some of its luster.

The exception could be outlet stores. These shops, which sell overstocked or out-of-season items at discount prices, tend to do well in a slowing economy as consumers search out bargains, Lieber said.

Chelsea GCA Realty Inc. (NYSE:CCG - news), which owns outlet mall properties focusing on high-end retailers, will have 10 to 12 percent earnings growth next year, Lieber said. It is trading near its 52-week high of $38-3/16.

Money managers agree that real estate stocks will not have explosive growth in 2001, but they will continue to post double-digit percentage gains, making them a good choice for jittery investors who don't want to take a roller-coaster ride with their money.

``There is some safety there,'' AEW's Poutasse said. ``The safety may be that it gives us a 10 percent return in 2001.''