CUSHMAN & WAKEFIELD
Waterloo Region

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Nick's Notes

Sale - Leaseback Transactions

Special Topic Edition

Sale–Leaseback Transactions: A Financing Alternative for Middle Market Companies

During the height of the recession, most capital markets were "locked up" making it difficult and in some cases impossible for middle market companies to attract bank financing to run and grow their businesses. Once the economy began to improve and the recession subsided, bank credit and other sources of capital became more available. As the economic recovery continues to build momentum, access to capital is generally improving.

A company's investment in real estate and buildings are often overlooked as possible value in financing transactions. Many times the corporate real estate is underutilized as a financing source and is financed with a simple mortgage. An alternative to a mortgage financing that better utilizes a company's real estate is the sale-leaseback.

WHAT IS A SALE-LEASEBACK?

A sale-leaseback enables a company to reduce its investment in these non-core business assets (the land & building) and liberate the cash in exchange for executing a lease and paying rent. A real estate sale-leaseback is a transaction in which the owner-occupant sells the land and building used in its business operations to a special purpose investor and then simultaneously leases the property back from the investor on lease terms agreed to concurrent with the real estate sale transaction. Typically, this will be a long-term investment for the special purpose investor so the seller is able to negotiate directly with the investor a mutually agreeable and clear set of lease terms. Sale-leasebacks have become more popular in recent years as an alternative to mezzanine financing so companies can avoid the high mezzanine interest rates.

BENEFITS:

In the right set of circumstances, a sale-leaseback transaction can have a number of benefits to the middle market company that is the real estate seller…

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Featured Investment Opportunity

Exclusive Investment Offering Region of Waterloo

Multi-tenanted industrial building with 100% Occupancy

- 122,000 SF
- Additional 7 acres for future development
- Strong covenants with all major tenants

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Set Your Own Lease Terms

Because the seller is also the lessee, the seller has significant bargaining power in structuring the property lease. In addition to realizing their investment in the real estate, the lessee has the opportunity to negotiate an acceptable lease agreement with the investor acquiring the property. Typical leases run 10 to 15 years. The seller, now the tenant, can also negotiate extension options after the lease expiration, and can also include terms for early lease termination if the tenant sees a need for more flexibility.

Retain Control of Real Estate

Most sale-leasebacks are structured as triple-net leases, so the tenant will be responsible for the taxes, insurance, and common area maintenance. A long-term, 'hands-off' lease from the investor provides the tenant similar control over the property as was the case when the tenant owned the property. The tenant can work with the special purpose investor and include options that will provide for future expansion and sublease of the property.

Tax Savings

Generally, lessees that are engaged in a lease are able to write off their total lease payment as an expense for tax purposes. As property owners, the interest expense and depreciation were the only tax deductions available. As a result, a sale-leaseback may have a greater tax advantage.

Greater Value to the Real Estate

Unlike a mortgage, a sale-leaseback can often be structured to finance up to 100% of the appraised value of the company's land and building. As a result, a sale-leaseback more efficiently uses the company's investment in the real estate asset as a financing tool.

No Financial Covenants

Because a sale-leaseback is not technically a financing instrument it does not have any covenants on the company. Fewer covenants provide a company with greater control over its own business and operations

Attractive Implied Financing Rates

Although the sale-leaseback cap rates are frequently slightly more than similar mortgage rates, a sale-leaseback provides cash proceeds for up to 100% of the appraised value of the property versus the 70% to 80% of appraised value under a typical mortgage. A sale-leaseback investor has only the real estate as collateral and a relationship with the seller through the lease agreement.

As a result, the sale-leaseback is slightly more expensive than senior financing and less expensive than mezzanine financing

Capital for Growth

A sale-leaseback can be used to free up cash to grow a business through acquisition or acquire additional facilities, technology, and equipment. With the tightening of the credit markets, many businesses do not have access to as much credit as they need to achieve their growth objectives; many are too close to their borrowing limit to consider expansion or make an acquisition of a competitor. Sale-leasebacks can be used as an off balance sheet financing structure that gives the seller the opportunity to turn a non-earning asset into growth capital. The company can then save the available bank financing for acquisitions and growth opportunities in the future. The sale-leaseback proceeds could also be used for other corporate purchases like the buyout of a shareholder or a special cash distribution to all the shareholders. The absence of covenants in sale-leasebacks provides business owners with significant discretion on what is the best use of their company's cash.

Corporate Restructuring/Exit Financing

Depending on the value of the company's real estate, a sale-leaseback can supply a considerable amount of liquidity and be a quick initial step to begin a reorganization process, as well as providing an exit strategy for owners and partners considering retirement.

Packaging Business for Sale

Often a savvy business owner who is contemplating selling his company can benefit by taking the real estate out of the company sales transaction and, by doing so, maximize the value of the real estate and increase the overall gross sale proceeds. If the real estate is left in the transaction the full value is seldom realized, as the EBITDA multiple often does not value the company's real estate at its true fair market value. Sale-leaseback investors will typically make their offer price based on an appraisal, extensive real estate market study, and a review of comparable market lease rates. The seller can complete a sale-leaseback and negotiate a long-term lease and pull out the real estate sale proceeds or repay corporate debt before the sale of the business.

"Portfolio Sales of Smaller Industrial Properties Surging "...

How a Sale Leaseback Helps to Increase the Proceeds to the Seller in a Corporate Sales Transaction…

Straightforward M&A Sale				Operating Co. Value post SALE-LEASEBACK			ADD REAL ESTATE PROPERTY VALUE	
EBITDA		$ 4,000,000	------->	EBITDA	$ 4,000,000			
				Rent Payment	600,000	------->	Rent Payment	$ 600,000
				EBITDA (Net of Rent)	$ 3,400,000		CapRate paid on Rent	10%
							Equivalent Multiple paid on Rent	10.0x
EBITDA Multiple		5.0x	------->	EBITDA Multiple	5.0x		Real Estate Purchase Price	$ 6,000,000
				Operating Co. Purchase Price	$ 17,000,000	------->	+ Operating Co. Purchase Price	$ 17,000,000
Total Purchase Price		$ 20,000,000					Combined Purchase Price	$ 23,000,000
Amount allocated to Operating Co.	70%	$ 14,000,000		Amounts allocated to Operating Co. vs. Real Estate may vary widely				
Amount allocated to Real Estate	30%	$ 6,000,000						

SELLER'S ADVANTAGE	
Enhancement in Total Purchase Price	$ 3,000,000
Effective EBITDA Multiple	5.8x

Sale-Leaseback Benefits

- Greater financing value for real estate
- No equity dilution
- Relatively quick closing
- No covenants
- Friendly lease terms
- Improved balance sheet
- Favorable borrowing rates (cap rate in the lease)
- Potential tax saving

Properly structured a sale-leaseback can more efficiently use a company's assets as a financing tool. It is important to work with an experienced team of attorneys, tax professionals and investment bankers to structure a deal that meets the company's specific circumstances. It is also important to find the right special purpose investors that will provide a market price for the real estate and negotiate a market lease with the seller.

"Properly structured a sale-leaseback can more efficiently use a company's assets as a financing tool"…

Contact **Nick Holzinger** for more information on the **SALE LEASEBACK** process.

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Market News

COMMERCIAL, INDUSTRIAL AND INVESTMENT REAL ESTATE SOLUTIONS.

WHO WE ARE

- Our team of sales professionals provide custom tailored Real Estate solutions. We invest the time to understand our clients' short- and long-term business goals, allowing us to collaborate with our clients and in-house specialists, and then deliver highly customized real estate solutions. Our brokerage has the resources of a global leader and as the proven experience and success as a market leader in Waterloo Region.

WHAT WE BELIEVE

- Deep local and global knowledge creates significant value for our clients
- Relentless curiosity delivers unseen opportunities
- Every touch point is an opportunity to deliver an exceptional experience for clients
- Diverse backgrounds, cultures, and expertise inspire breakthrough innovation
- Our brand and our people will be the envy of the industry
- Alone we are good; together we are great

WHAT YOU CAN EXPECT FROM US

- A strong bias for action
- A rigorous focus on results
- Value created through insight
- The right people powered by the right platform

CORE SERVICES

Landlord Representation

- Property Analysis
- Location Analysis
- Market Analysis
- Target Market Analysis
- Property Positioning
- Marketing & Leasing Strategy
- Marketing & Sale Disposition Strategy
- Marketing Program Execution
- Negotiations

Tenant Representation

- Market Assessment
- Strategy Development
- Demographic Analysis
- Site Selection Strategy
- Occupancy Cost Analysis
- Acquisition/Disposition
- Build-to-suit Planning
- Negotiations

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Nick has over 40 years of experience as a real estate professional and has been involved in some of the most prominent real estate transactions in Southwestern Ontario.

Our team of professionals provide custom tailored industrial, commercial and investment Real Estate solutions.

If you are in the market to **BUY, SELL, LEASE OR INVEST,** contact Nick and his team.

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