What the Westfield sale means for property trust investors

On Tuesday, Unibail-Rodamco (Unibail) announced it had entered into an agreement to acquire all of the outstanding shares in Westfield Corporation (ASX:WFD). This is Australia's biggest ever acquisition, worth $32bn, and has naturally received widespread commentary.

What hasn't been covered in much detail is what this means for Westfield shareholders and investors in property trusts more generally.

Westfield shareholders' three big questions

1. Is Unibail paying a fair price?

On the face of it, yes. At the announcement, the price was equivalent to A$10.01per share, a premium of almost 18% to Westfield's last close. That price consists of US$2.67 per share in cash (35%) with the balance in Unibail-Rodamco scrip and a holding in Westfield's property tech company, OneMarket. The price has since fallen in line with Unibail's share price fall.

Even before the offer, Westfield traded at one of the largest premiums to net tangible assets compared to its global peers, plus a low yield with hard to predict growth prospects. That's why APN's AREIT Fund has been underweight the stock, despite it having an attractive portfolio of assets (albeit with a long tail of lesser quality assets). The premium paid only pushes the valuation metrics higher. Shareholders have done well.

2. Will the deal proceed?

Probably, although it's impossible to say with certainty. US-based REITs will be combing through the paperwork but may not have the financial firepower to match Unibail's offer. There's also the small matter of a US$150m break fee, paid by Westfield to Unilbail if it withdraws from the agreement (and vice versa if Unibail withdraws), plus Frank Lowy's comment that he's "100% comfortable with the decision". The Lowy family owns 9.5% of Westfield and Unibail 4.9%.

Nothing is ever certain in these situations but this deal looks more likely to go through as proposed than not, especially as other potential bidders do not have the capacity to match it.

3. Should I hang on to my new Unibail shares?

Accessed via an Australian-listed CHESS depositary interest (CDI) (also issued by the likes of Janus/Henderson, Newscorp, Resmed and James Hardie), the new entity certainly looks attractive. The Unibail/Westfield CDI will offer investors access to greater asset diversity than the Westfield portfolio and will have less riding on risky assets like World Trade Centre in New York and problematic developments like Milan. We expect the yield from the portfolio to be higher, too.

The value creation component of the deal also makes sense. Unibail's forecast of additional earnings per share is based on significant operational cost savings. In the last financial year alone, for example, Westfield's joint CEOs earned around US$20m a year between them. The total savings are easy to see while the value of the new Unibail portfolio is heavily weighted to flagship shopping destinations, which is another attractive feature.

Whether Westfield shareholders hang on or sell out is a matter of personal preference but on the face of it there could be much to like about the new CDI.

AREIT investors' three big questions

1. Is the deal good for investors in other REITs?

We think so, yes. REIT investors have had a tough time of it lately, what with Amazon's arrival, slow wages growth and a number of retail chain collapses. This has created a sense of malaise in the sector, depressing AREIT share prices. This deal offers a fillip to the negative sentiment, an example of a global property giant not only seeing beyond it but using it as an opportunity to create value.

As the implications of the deal sink in we'd expect to see the oversold retail sector rebound. This could be the change in sentiment property trust investors have been waiting for.

Also worth noting is that the deal is likely to increase sector transparency. One of the issues (alongside those listed above) that has restricted APN's investment in Westfield was the lack of detail regarding individual properties in the company's portfolio. If Unibail's purchase triggered a new era of transparency that would be a good thing for everyone.

2. Does the deal reduce investment choice?

Not really. Initially, the market capitalisations of the old Westfield will fall by the cash component of the bid (ie. around 35%). This means that the stock's market weight will fall from around 14% (today) to around 9%. It will be smaller but retain its place as the third largest AREIT listed on the ASX.

In return, investors will get the potential benefit of being able to invest in a more diversified portfolio of retail property at a lower risk and (probably) higher yield. In that sense, the deal increases investor choice.

3. Is the spin-off of Westfield's retail technology platform an opportunity?

The OneMarket spin-off is a side issue but an interesting one. Prior to the sale to Unibail, Westfield intends to float the retail tech company on the ASX. Once the transactions close, Unibail will retain a 10% stake in OneMarket.

Westfield's much-hyped tech business is supposed to lead the world to a new kind of retail experience, integrated with web-based technology. It's been a massive cash drag in recent years and Unibail appears to see little value in it. New potential investors will be invited to participate in the float while existing Westfield shareholders will be allocated their portion.

The details around this aspect of the arrangement confirm the headline. This is all about a global property giant opportunistically adding more flagship centres to its portfolio. In our view, it's a $32bn vote of confidence in the future of the world's best shopping malls, not a Westfield pet tech project.

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