

# SimCities

**Ira Sohn Conference**  
**May 8, 2017**



Pershing Square Capital Management, L.P.

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# Land Development is Typically a High-Risk Business

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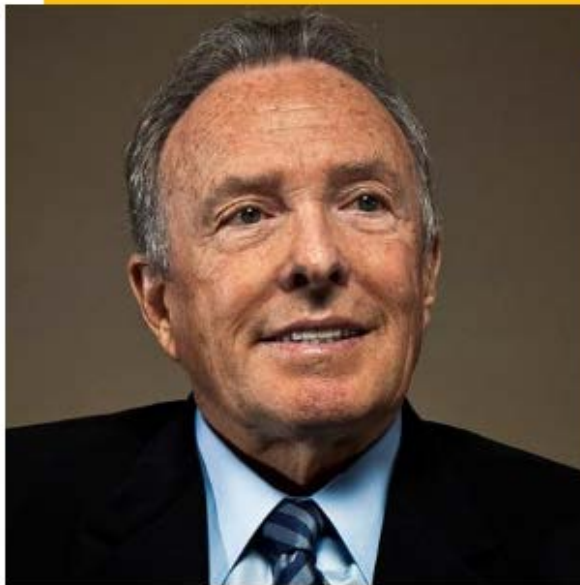
**History is replete with boom and bust cycles and bankruptcies in the land development business. Why?**

- ▶ Land developers typically use large amounts of recourse leverage
- ▶ Substantial capital must be spent long before the first lot is sold
- ▶ There is substantial risk and time required to obtain zoning and building permits
- ▶ There is pressure to build immediately without regard to market conditions due to large upfront investments and leverage
- ▶ The vast majority of profits are not realized until the last few lots are sold

***As a result, many investors are reluctant to invest in land development, and therefore use extremely high discount rates to value these investments***

Donald Bren, the Largest Land Developer in the U.S., is the 27<sup>th</sup> Wealthiest Man in the U.S.

## Forbes ranks Bren as wealthiest real-estate developer in the U.S.



#27

< PREV

### Donald Bren

Chairman, Irvine Company

REAL TIME NET WORTH — as of 5/5/17

**\$15.2 B**

2016 FORBES 400 NET WORTH — as of 4/3/17

**\$15.2 B**

- Bren is the country's richest real-estate developer.
- His Irvine Co. owns over 115 million square feet of real estate, mostly in Southern California.
- His empire includes 500 office buildings, 40-plus shopping centers and nearly 60,000 apartments.
- Bren attended the University of Washington on a skiing scholarship and spent 3 years in the Marines.

***Bren built his fortune developing The Irvine Ranch MPC over the last 40 years successfully navigating boom and bust real estate cycles***

# Bren Owns The Irvine Ranch Master Planned Community (MPC)

Donald Bren turned a minority investment in 1977 in a land development project in Southern California into a \$15B+ personal fortune



***At the time of Bren's investment, The Irvine Ranch was already an established MPC. One of the keys to investing in MPCs is avoiding the high-risk start up phase. In other words, you don't want to be the first owner.***

# An MPC is a Real World SimCity

**An MPC is a large-scale (typically 10,000+ acres) privately owned development, where the owner has substantial control over planning, zoning, the release of property for sale, and development**

- ▶ **MPC land values tend to increase at a more rapid rate and have less volatility than standalone properties because successful MPC owners control the supply of land to the market and take a longer-term approach to planning, conservation, design, and community building**
- ▶ **This long-term approach increases residential and commercial appeal and long-term value**
- ▶ **Carefully designed amenities, appropriate community services, high quality schools and hospitals, places of worship – all make well designed MPCs a very appealing place to live, work, and invest**

***As a result of its controlled ownership, MPC property development is much less exposed to the boom / bust cyclicity of stand-alone, smaller-scale real estate development***

# The Irvine Ranch

**The Irvine Ranch is a 93,000-acre property that includes nine miles of coastline along the Pacific and accounts for 20% of Orange County**

- ▶ **In 1977, Donald Bren (along with four other investors) bought The Irvine Ranch for \$337 million. Over time, he bought out his partners to obtain full control**
- ▶ **Bren resisted persistent pressure to sell the land piece-by-piece to the highest bidders**
  - Instead, with thoughtful development and careful design of the Irvine Ranch, Bren created some of the most valuable real estate in the country and built a personal fortune
- ▶ **Irvine (population 250,000) is now home to residential villages, shopping centers, parks, top-ranked schools, and headquarters for many Fortune 500 companies**
  - The City of Irvine is America's safest big city with public schools which rank No. 1 in California

# What Were the Keys to Bren's Success?

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- 1. He invested in well-located real estate with favorable long-term demographics**
- 2. He bought into an existing MPC where a significant upfront investment had already been made and the community was already established**
- 3. He used the growing value of land to minimize the need for outside equity partners over time**
- 4. He used debt and municipally funded bonds<sup>(1)</sup> to pay for infrastructure and improvements, minimizing the need for equity**
- 5. He limited the use of recourse loans and maintained a conservatively funded balance sheet**
- 6. He carefully controlled the supply of land sold to homebuilders**
- 7. He carefully controlled the development of apartment buildings and commercial property so that he was never too far ahead of demand**
- 8. He took a very long-term view**

(1) These are often called municipal utility districts (MUDs) or tax increment financings (TIFs) and are funded by incremental future tax revenues from the residents of an MPC



# What Was His Approach to Land Development?

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**The Irvine Ranch has followed these guiding principles for more than 50 years, beginning more than 10 years before Bren acquired the land**

- 1. Maintain land under a single owner (Bren bought out his partners so he had total control)**
- 2. Establish a master plan to guide land use and infrastructure decisions**
- 3. Create a planning group to guide the evolution and implementation of the master plan**
- 4. Continually reinvest in the land**
- 5. Continue the tradition of land stewardship, with an eye on the long-term view**
- 6. Contribute to the quality of the cities on The Irvine Ranch**
- 7. Make sound, realistic economic and political decisions**

# How Can One Invest with Donald Bren?

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Donald Bren Comments Regarding The Irvine Ranch:

*“Developing this property in the best possible way is the most important thing in my life. I expect to be working on this into my 90s”*

*“There is no price that is acceptable”*

***The Irvine Ranch is a private company and Bren will never sell***

How Can a Public Market Investor  
Participate in Donald Bren's Approach to  
Land Development and Long-Term Value  
Creation?

*Howard Hughes*®

(Ticker: HHC)

# HHC Owns a Geographically Diversified Collection of Some of the Best MPCs in the Country

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## HHC's MPCs Share Many Characteristics with The Irvine Ranch

**HHC's MPCs are superbly located large-scale communities, acquired by HHC decades after hundreds of millions of dollars of capital was invested to establish the communities**

<b>MPC</b>	<b>Date Founded</b>	<b>Total Gross</b>	<b>MPC</b>	<b>Location</b>
		<b>Acres</b>	<b>Population</b>	
Maryland	1967	16,450	112,000	Columbia, MD
The Woodlands <sup>(1)</sup>	1974	30,530	115,000	Houston, TX
Summerlin	1990	22,500	107,000	Las Vegas, NV
Bridgeland	2003	11,400	8,300	Houston, TX
Total		80,880	342,300	

### High Density Urban MPCs

South Street Seaport	400,000 SF + 65K SF rooftop	New York City
Ward Village	9 million SF of entitlements	Honolulu, HI

(1) Includes acreage from The Woodland Hills MPC, a new MPC in close proximity to The Woodlands which was acquired by HHC in 2014

## Like Donald Bren, HHC was not the First Owner of its MPCs

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### **HHC is the third or fourth owner of many of its MPCs**

- 1. 1950s: Land encompassing the Summerlin MPC acquired by Mr. Howard Hughes and conducted business as The Howard Hughes Corporation**
- 2. 1996: The Rouse Company acquired control of Summerlin from the Howard Hughes estate**
- 3. 2004: General Growth Properties (GGP) acquired The Rouse Company**
  - Rouse owned Summerlin, Columbia, Bridgeland, the Seaport District and a majority interest in The Woodlands
- 4. 2010: GGP bought 100% ownership of Summerlin by buying the remaining interests from the heirs of Mr. Howard Hughes**
- 5. 2010: HHC acquired its MPC assets from GGP in a spin-off transaction**

# The Howard Hughes Corporation: A Little History

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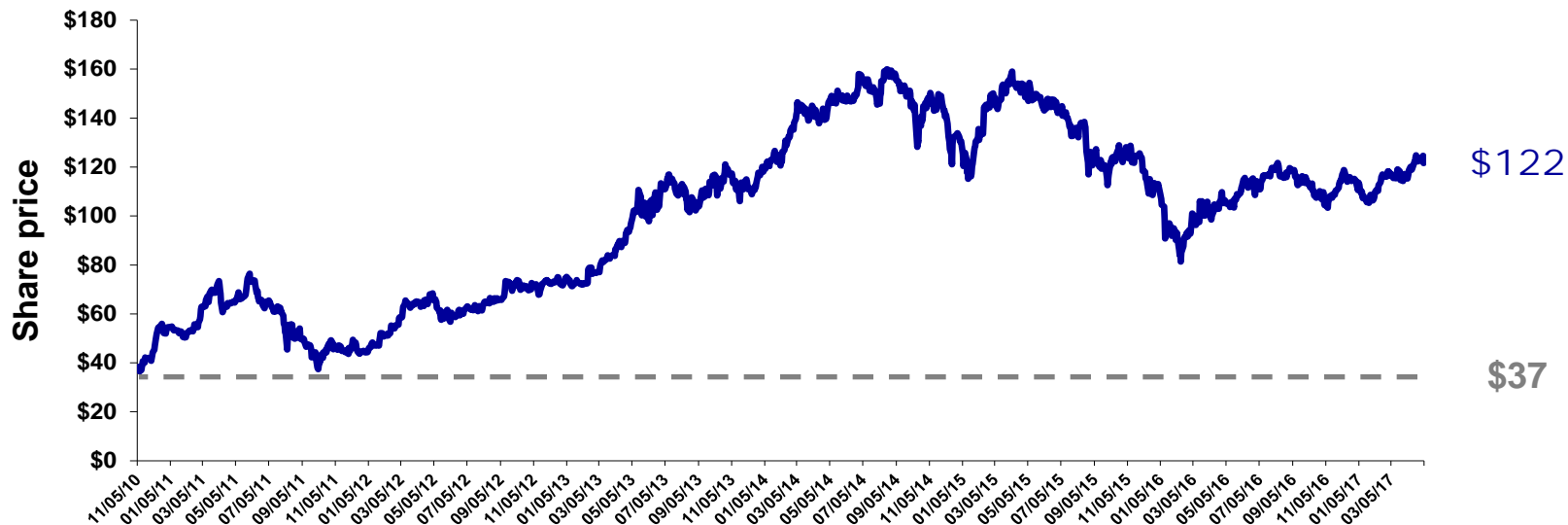
- ▶ **2008 / Early 2009: Pershing Square acquires 25% of GGP for ~\$60 million**
- ▶ **2009: GGP files for bankruptcy in April 2009**
- ▶ **2010: GGP acquires remaining interest in Summerlin from the Howard Hughes' heirs for \$230 million**
- ▶ **2010: GGP emerges from bankruptcy**
  - GGP creditors receive par plus accrued interest while shareholders have made 100X+ their investment since November 2008
- ▶ **2010: HHC is formed as a subsidiary of GGP and spun-off to shareholders with a contemporaneous \$250M investment from Blackstone, Brookfield Asset Management, Fairholme and Pershing Square**
- ▶ **2011: HHC purchases 47.5% interest in The Woodlands from Morgan Stanley Real Estate (to establish 100% ownership of The Woodlands)**
- ▶ **2012: HHC buys out Brookfield, Fairholme and Blackstone**
- ▶ **2014: Pershing Square sells remaining stake in GGP, while retaining our initial stake in HHC**



## HHC Since IPO

**Pershing Square has owned HHC since its spin-off from GGP in November 2010 and has never sold a share**

Stock price performance of HHC from 11/5/2010 to 5/4/2017



## Since Acquiring Control of its MPCs, HHC has Followed Bren's Strategy

### HHC owns and controls irreplaceable real estate in some of the best markets

	Irvine Ranch	HHC	Most Developers
<u>Irvine Key Principals</u>			
Single Owner/Sole Control	✓	✓	✗
Thoughtful Master Plan	✓	✓	✗
Reinvest in Land	✓	✓	✗
Minimize 3 <sup>rd</sup> Party Equity	✓	✓	✗
Take Long-Term View	✓	✓	✗
Control Supply of Land and Commercial Development	✓	✓	✗
Provide Land Stewardship	✓	✓	✗

## Upon Obtaining Control, HHC Took A Long-Term Approach

### **GGP viewed its MPCs as a cash cow to be liquidated to help pay debt service**

- ▶ **HHC, as a conservatively financed public company, has permanent capital that enables it to follow Bren's long-term, value-maximizing approach**
- ▶ **Since obtaining control of its MPCs, HHC has discontinued substantially all commercial land sales, systematically acquired control of assets previously sold (or adjacent to its MPCs), and bought out its partners**
- ▶ **Once a well designed MPC reaches a certain tipping point, the commercial development opportunity becomes very large**
- ▶ **HHC controls the substantial majority of commercial and residential vacant land at its MPCs and controls the zoning. This limits supply, and reduces the likelihood of overbuilding**

# Integrated Segments Create Virtuous Cycle

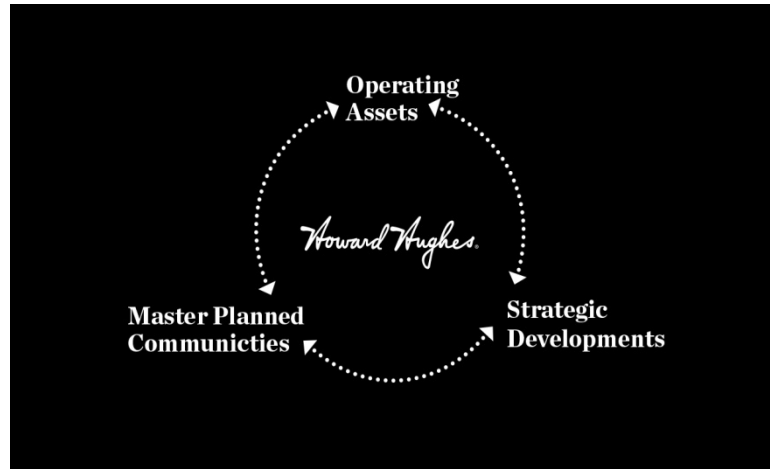
HHC's three integrated business segments allow it to self-fund the equity required for development from (i) MPC land sales, (ii) cash flow from its operating assets, and (iii) equity in the land

**Operating Assets** create a growing stream of income that provides cash for **Strategic Developments** and amenities for its MPCs, which in turn increase demand and land prices

**Lot sales to homebuilders increase demand for Operating Assets and provide equity and cash flow for future Strategic Developments**



**Start Here**



**Strategic Developments** grow Operating Asset cash flows and increase the value of the land in the MPCs

## A Few Examples of HHC's MPCs

*Howard Hughes*® **The Woodlands**®  
DEVELOPMENT COMPANY



## The Woodlands: Key Highlights

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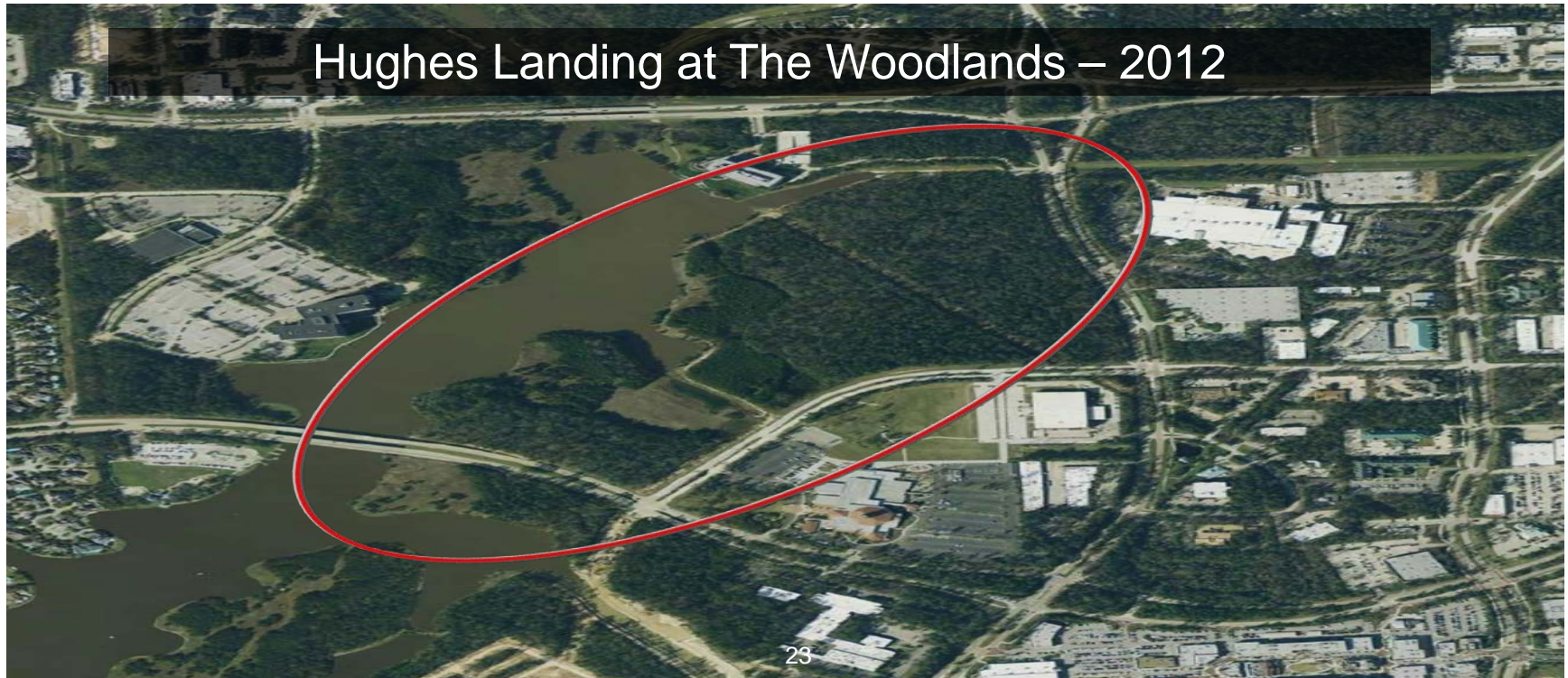
**With only 1,000 residential lots and 750+ commercial acres remaining, The Woodlands represents one of HHC's most mature and well-established MPCs. It is twice the size of Manhattan.**

- ▶ **Created in 1974, The Woodlands has grown into one of the country's most recognized MPCs with more than 115,000 residents**
- ▶ **Recently ranked as the premier place to live in Texas and sixth in the country**
- ▶ **The Woodlands is home to several Fortune 500 Companies**
- ▶ **ExxonMobil recently relocated its 5M square feet (SF) corporate headquarters just south of The Woodlands**



## Hughes Landing at The Woodlands

**HHC's 66-acre lakefront Hughes Landing project highlights how a well-planned commercial downtown development within an MPC can create meaningful value**





- Hughes Landing now: 1.4M SF of office, 126K SF of retail, a hotel and apartments
- Completed in just 2.5 years
- Projected to generate nearly \$50M of net operating income



# SUMMERLIN®



## Summerlin: Key Highlights

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### **Located nine miles from downtown Las Vegas, Summerlin is the premier place to live in Las Vegas**

- ▶ **Summerlin is a mature 25-year old community with 42K homes and over 100K residents, which is expected to grow to 200K+ by end of build-out**
  - With 22,500 total acres in Summerlin and 4,600 highly desirable owned remaining saleable and developable acres, HHC is the largest private land holder in Las Vegas
- ▶ **Strong overall market dynamics in Las Vegas, with \$18B of commercial real estate development in the pipeline (including the new Raiders stadium), will continue to drive demand at Summerlin**
- ▶ **In 2015, HHC entered into a joint venture with Discovery Land Company to develop a 555-acre luxury community (The Summit), which has contracted to sell 77 lots for \$247 million with more than 180 lots remaining to be sold**



## Summerlin – Vertical Development Opportunity

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**Similar to Hughes Landing, HHC retained the highly valuable commercial downtown acreage at Summerlin, and has started a large-scale vertical development with 5.5 million SF of entitlements**

- ▶ **HHC recently completed a retail, office and apartment development in Downtown Summerlin, which is estimated to generate over \$32 million of stabilized NOI**
- ▶ **Entered into a 20-year ground lease in Downtown Summerlin for a state-of-the-art practice facility for the newly awarded NHL hockey team**
- ▶ **Finalized a 15-year build-to-suit lease with Aristocrat Technologies for a two-building office campus that is estimated to generate over \$4 million of NOI**
- ▶ **Purchased the Las Vegas 51s minor league baseball team with the goal of building a new stadium for the team in Downtown Summerlin**

***Summerlin is a good example of the virtuous cycle of value creation from a meticulously controlled and planned development process***



# Downtown Summerlin & Controlled Commercial Land

Downtown Summerlin

HHC-owned land planned for 5.5M SF of future development





## Downtown Summerlin – 2010





## Downtown Summerlin - Now



## HHC's Approach to Value Creation

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- ✓ **Continue controlled residential land sale program at steadily increasing market prices**
- ✓ **Achieve stabilization of existing Operating Asset portfolio over the next 2 to 3 years**
- ✓ **Continue controlled development of new operating assets (office, retail, apartments, hotels and storage properties) to meet market demand**
  - ❖ **HHC has commercial vertical entitlements for 50 million total SF, of which 37 million SF are at its core MPCs**
- ✓ **Complete construction and leasing at the Seaport District**
- ✓ **Deliver condo towers and create revitalized retail environment at Ward Village**



What is HHC Worth?

## Valuation

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**Like The Irvine Ranch, in light of the complexity and long-term nature of HHC's assets, HHC is difficult to value**

- ▶ **GAAP accounting does not explain the true economics of the business**
- ▶ **Short-term cash flows do not reflect the long-term economics of the business**
- ▶ **Book values of assets do not reflect fair values**

***How then can one value HHC?***

***A back-of-the-envelope approach is illustrative***

## Back of the Envelope: Operating Assets

**We use projected stabilized net operating income (“NOI”), an appropriate capitalization rate, and discount this value to the present and subtract the remaining cost to complete**

- ▶ **The vast majority of HHC’s income-producing Operating Assets are within its MPCs, providing HHC with control over zoning and new supply, thereby limiting risk**
  - HHC projects total stabilized NOI of \$241M, with 1Q17 annualized cash NOI of \$169M
  - HHC estimates it will take approximately two years for the remaining assets to stabilize
  - HHC estimates that it will take ~\$300M to complete these assets

***Given the recently constructed Operating Asset portfolio, located in mature controlled MPCs, Pershing Square believes that capitalization and discount rates should be much lower than for typical real estate assets***

## Back of the Envelope: Residential Acreage at MPCs

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**Because of the substantially lower risk of predicting lots sales in mature MPCs (it is effectively inevitable, although subject to macro factors in the short term), we believe one should use very low discount rates to discount future cash flows from lot sales in HHC's mature MPCs**

- ▶ **We believe the long-term appreciation rate of HHC's residential land is approximately equal to the discount rate one would use to present value the cash flows from these assets**
- ▶ **As a result, recent land sales are a reasonable proxy for valuing the remaining residential land held by HHC's mature MPCs**

## Back of the Envelope: Other Assets

**HHC owns a collection of other assets that it inherited as part of its spin-off from GGP, which can be valued using comparable transactions**

► **Some of these assets include:**

- 110 North Wacker, arguably the best development site in Downtown Chicago, where HHC just signed a 500K SF lease with Bank of America and will develop a 51-story, 1.35M SF Class A+ Office Tower
- The Elk Grove Collection in California, a future outlet / hybrid lifestyle development (HHC recently sold 36 of the 100 acres it owns for \$36M)
- Landmark Mall in Alexandria, VA, an open-air mixed-use development with retail, residential and entertainment components
- Circle T Ranch in Dallas, a large mixed-use development in partnership with Hillwood
- Air rights above the Fashion Show Mall in Las Vegas suitable to construct a large-scale hotel and casino directly across from the Wynn

## Back of the Envelope: Our Approach

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**Pershing Square believes that the sum of the Operating Assets, residential MPC land acreage, and Other Assets approximate the current enterprise value of HHC**

***What else do you get for \$122.12 per share?***

# Seaport District Upon Completion in 2018



## Seaport District: Key Highlights

**HHC's redeveloped and revitalized Seaport District will serve as a premier destination for New Yorkers and as an anchor for the growing Lower Manhattan community**

- ▶ **400K+ SF of retail, entertainment, and restaurant space consisting of:**
  - A newly built and architecturally significant 170K SF pier 17 building on the East River
  - 180K SF historic district
  - 50K+ SF redeveloped Tin Building to become Jean George Marketplace
- ▶ **Additional 65K SF rooftop venue with iconic views of the Brooklyn Bridge and East River that can host events for up to 4,000 people standing or 2,600 seated**
- ▶ **HHC's vision is to create a carefully curated lifestyle destination, which can endure, grow and thrive in the changing retail environment**
  - Leases have a significant component of percentage rent or partnership interest for HHC, allowing for meaningful upside participation



# WARD VILLAGE

2010/2011



## Ward Village: Key Highlights

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### **HHC owns and controls an enormously valuable 60-acre coastal vertical MPC in Honolulu**

- ▶ **Ward Village is currently comprised of 1.3M SF of retail, industrial and office space, but will be redeveloped as part of a comprehensive MPC**
  - At full build-out, HHC will deliver 4,000 condos and more than one million SF of retail
- ▶ **Located less than a mile from the Ala Moana mall, one of the world's most productive and valuable malls (owned by GGP)**
- ▶ **HHC has already contracted to sell over 1,100 condo units in four condo towers, which will cost nearly \$1.5 billion when fully completed**
  - HHC has delivered and closed on the sale of 86% of the units on its first condo tower and it expects to complete one additional tower per year from 2017 - 2019



# WARD VILLAGE

2016



# WARD VILLAGE

Waiea





# WARD VILLAGE

9M SF of Condo and Retail Development

Ke Kilohana

Waiea

Ae'o

Anaha



## Back of the Envelope: 37M SF Future Development

**The value of HHC's future commercial development opportunity can be estimated by comparing the value created with the 3.9M SF of development since formation and using it to estimate the value creation potential of the remaining 37M SF.**

- ▶ **Since 2011, HHC completed 3.9M SF of commercial operating properties with \$1.6 billion of development cost (not including condominium development)**
  - These projects are projected to generate stabilized NOI of \$144 million
  - This implies a greater than 9% yield on cost, which creates meaningful value assuming cap rates of approximately 5% - 7% for these assets
- ▶ **HHC has nearly 37M of remaining vertical development entitlements at its Summerlin, Columbia, Woodlands and Bridgeland MPCs alone**
  - ~10x the amount of development that HHC has executed since 2011, and an enormous value creation opportunity over time

***HHC's future developments will likely create substantially more value than recent developments because they will occur in more mature, higher density MPCs with higher rents.***

# What About Taxes?

**HHC is structured as a C-Corp and has historically benefited from NOLs, but will likely become a limited tax payer in the next 1 to 2 years. HHC's business strategy is highly tax efficient.**

- ▶ **Operating Asset NOI is shielded by depreciation and interest expense**
  - HHC has \$4B of existing tax basis in its assets
- ▶ **MPC condo sales are taxable**
  - HHC may consider the development and retention of rental apartment buildings at Ward Village
- ▶ **Land development generally involves deferred taxation**
  - HHC's intent is to build and hold commercial development which is the most tax efficient approach
- ▶ **HHC has used NOLs to shield taxable income to date. These NOLs will likely be consumed by 2018; however, the sale of its non-core, high-basis Other Assets can create substantial new NOLs**
- ▶ **HHC is a U.S. tax payer and would be a beneficiary of tax reform**
  - Depending on the outcome of tax reform, HHC could consider a REIT for its Operating Assets

## And HHC's Balance Sheet?

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### **HHC maintains a conservatively funded balance sheet with mostly non-recourse debt**

- ▶ **Since its IPO, HHC has invested billions of dollars without having to issue equity**
  - HHC has enough cash and liquidity on hand to meet all existing development funding commitments
- ▶ **2/3rd of HHC's outstanding debt balance is non-recourse**
  - HHC can be thought of as a portfolio of separate equity investments, given the non-recourse nature of the substantial majority of its debt
- ▶ **HHC recently executed an opportunistic refinancing of its 6.875% unsecured bonds with a newly issued \$800M bond at a 5.375% rate**



# Talented & Aligned Management Team

**HHC's management is aligned and incentivized to deliver long-term value to shareholders with a significant economic stake in the company**

- ▶ **At IPO, management purchased non-tradable six-year warrants**
  - CEO David Weinreb owns warrants to purchase 2.4M shares and has recently committed to purchase \$50M of new warrants when he exercises/sells these warrants which expire in November 2017
- ▶ **Management is extremely experienced in executing complicated development projects**
  - Established platform with deep experience across asset classes and in development and construction
- ▶ **Management has significant runway for continued development of the existing assets, but can also be opportunistic with acquisition opportunities**
  - 80 South Street Seaport assemblage / purchase (\$250M cost) and subsequent sale for a \$140M profit in 15-month period highlights the ability of the team

## How Can I Learn More?

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**HHC started conducting quarterly calls this year and plans to host its first Investor Day on May 17th**

- ▶ **HHC provided a comprehensive Supplemental Information package and hosted a conference call for the first time as part of its Q4 2016 earnings report**
- ▶ **May 17<sup>th</sup>, 2017 Investor Day at the Seaport**
  - Will include tour of the Seaport, presentations from the HHC Leadership Team and Q&A with management and guest speakers
  - Interested investors can still register for event by contacting Tracey Wynn at HHC ([tracey.wynn@howardhughes.com](mailto:tracey.wynn@howardhughes.com))