

How Brookfield Asset Management's Offer Undervalues Brookfield Property Partners

On January 4th, 2021, Brookfield Asset Management (BAM) announced a proposal to buy the remaining 40% of Brookfield Property Partners (BPY) it does not currently own. BAM is offering public investors \$16.50 per BPY unit, or \$5.9 billion in total value.¹

Both BPY and BAM have spent the last 2 years, including the year before the pandemic, consistently arguing that BPY trades at a discount to the underlying value of its assets.² Several analysts agree that privatizing BPY would be a good deal for Brookfield Asset Management³, which had amassed \$75 billion of capital and dry powder to invest in distressed assets and other investments, as of November 12, 2020.⁴

We believe the independent directors of BPY should negotiate to ensure this offer is a good deal for BPY's public investors. We estimate a price range of \$19.50-\$21.00 per unit is more reflective of analysts' assessment of net asset value cited by BPY in September 2020 and the pre-pandemic high price in 2019.

Below we present substantiation for the following key points:

- In the third quarter of 2020, BAM reported the value of "non-controlling interests" in BPY at \$26 billion;
- BAM and BPY executives publicly stated in 2019 and 2020 that BPY's trading prices undervalued its assets;
- At Brookfield's Investor Day presentation in September 2020, management reported BPY's net asset value (NAV) at \$27.01 and stated the consensus NAV of analysts was \$19.50 per unit;
- The premium to BPY's unaffected trading price offered by BAM in this deal is 14%, lower than the premium Brookfield companies have offered in a sampling of buyouts over the last several years.

Value of BPY

BAM's 3Q20 Interim Report valued "non-controlling interests" in BPY at \$26 billion.⁵

"Non-controlling interests in our consolidated results primarily consist of third-party interests in BPY... and [its] consolidated entities, as well as co-investors and other participating interests in our consolidated investments."⁶

That quarter, BAM CEO Bruce Flatt stated that "[BPY] current trading price does not reflect anywhere near the value of the high-quality portfolio of real estate that it owns."⁷

In pre-pandemic 2019, BPY units were at high of \$21.15 in Q2. In 1Q19 BPY initiated a substantial issuer bid that resulted in the purchase of 13,981,839 units at a purchase price of \$21.00 per unit.⁸ Following the bid, BPY continued repurchasing units throughout the year, as it believed it was "acquiring our own units at a substantial discount to their intrinsic value."⁹

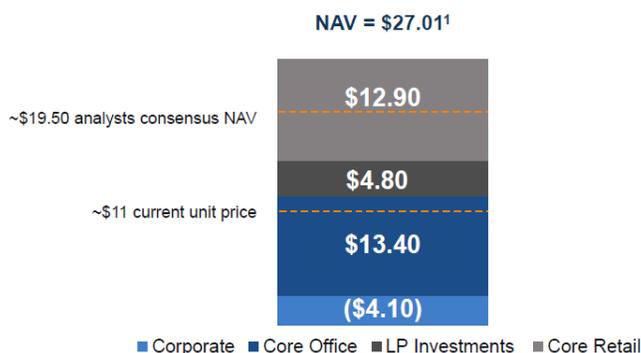
BAM is looking at pandemic-era price declines as an opportunity to buy real estate interests at distressed prices, and it has increased its investment in BPY during the pandemic.¹⁰ BAM committed up to \$1 billion of equity infusion to fund BPY's substantial issuer bid of \$12.00¹¹ and a normal course issuer bid at an average price of \$13.00, both in 3Q20¹². During 4Q20, BAM purchased an additional 22 million units of BPY for a weighted average price of \$13.50.¹³

At the last Brookfield Investor Day meeting in late September 2020, BPY reported its net asset value to be \$27.01 while the units were trading at approximately \$11. According to BPY's presentation, analysts consensus NAV at the time was \$19.50.¹⁴

Bryan Davis, BPY's Chief Financial Officer stated that day: "And that investment today can be made at a substantial discount to intrinsic value, 60% if you consider it relative to our IFRS value, or 50% if you consider it relative to consensus NAV."¹⁵

A highly compelling investment opportunity

We see tremendous value in BPY units today above the dislocated trading price



1. Includes the impact of the conversion of preferred shares.

Brookfield Investor Day, September 24, 2020, Slide 40.

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Based on BPY and BAM's own statements about the value of BPY's high quality real-estate portfolio¹⁶ and its non-controlled interests, we believe a fair offer should range somewhere between the analysts consensus NAV presented by BPY (\$19.50) in September 2020 and the 2019 pre-pandemic high unit price (\$21.00):

Quarter	Trading High	Trading Low	BAM or BPY Commentary
2019 Q1	20.74	16.15	"...We were pleased with the outcome of our Substantial Issuer Bid in February and March. Between the offers for BPY units and BPR shares, approximately \$400 million of units were tendered and settled at an average price of USD 20.83 per unit. Following completion of the offer, we have continued to repurchase units under our Normal Course Issuer Bid as we believe acquiring our own units at a substantial discount to their intrinsic value is an attractive use for excess capital." ¹⁷ - <i>Brian William Kingston, Brookfield Property Partners LP Senior Managing Partner & CEO</i>
2019 Q2	21.15	18.28	"Following closing of the offer in March, we remained active repurchasing units while they trade at a discount to their intrinsic value...We continue to believe that selling assets at premiums to carrying value and using those proceeds to repurchase our units at substantial discounts is a good use of our capital and create significant value for our unitholders." ¹⁸ - <i>Brian William Kingston</i>
2019 Q3	20.44	18.26	"Brookfield Property Partners has transformed itself over the past five years since its spin-off from BAM. In addition, NAV and cash flows have grown at a compound $\pm 10\%$ annually. For various reasons, similar to most real estate securities, this is not reflected (yet) in the stock price, enabling a buyer today to make an investment at an estimated 35% discount to the appraised IFRS value of its underlying assets and a going-in yield of over 6%." ¹⁹ - <i>Bruce Flatt, BAM CEO</i> "Despite a strong asset performance, BPY shares currently trade at a discount." ²⁰ - <i>Brian William Kingston</i>
2019 Q4	19.61	18.01	"And so I think we continue to believe where the shares trade today, it's a very attractive -- particularly when you adjust it for the risk around -- these are assets that we know very well, a very attractive place for us to put capital to work." ²¹ - <i>Brian William Kingston</i>
2020 Q1	19.99	7.25	"While the virus will have an impact on our operations over the course of the year ahead, our business remains in good shape financially due to a strong liquidity position and the high-quality nature of the assets we own. Despite this, our unit price has declined dramatically over the past 2 months and today trades at a price that is disconnected from the performance of our underlying assets." ²² - <i>Brian William Kingston</i>
2020 Q2	13.90	7.32	"We continue to believe the trading price of our units does not adequately reflect the underlying value of our assets." ²³ - <i>Brian William Kingston</i>
2020 Q3	12.16	7.25	"We also allocated approximately \$1 billion to purchases of BPY, whose current trading price does not reflect anywhere near the value of the high-quality portfolio of real estate that it owns" ²⁴ - <i>Bruce Flatt, BAM CEO</i> "And that investment today can be made at a substantial discount to intrinsic value, 60% if you consider it relative to our IFRS value, or 50% if you consider it relative to consensus NAV." ²⁵ - <i>Bryan Davis, Brookfield Property Partners LP CFO</i>
2021 1Q, as of 2/3/21 (affected by BAM's offer)	17.45	16.76	"Privatizing Brookfield's real estate subsidiary is appealing because it has consistently traded at a discount to the underlying value of its assets, Nick Goodman, Brookfield Asset Management's chief financial officer, said in an interview. "We believe that it has been consistently discounted for more than just the past year,' Goodman said. 'We believed it would be a premium offering to the market given it has a unique global portfolio and some of the highest quality real estate in the world. But it has consistently struggled to trade at its net asset value." ²⁶ - <i>Nick Goodman, BAM CFO</i>

Other Offer Premiums

BAM also offered a lower premium to BPY's trading price than Brookfield companies have when buying out their unaffiliated investors prior to the pandemic. BAM's current \$16.50 offer represents a 14% and 14.9% premium to the closing price of BPY units sold on the Nasdaq and TSX exchanges as of December 31, 2020²⁷ compared to the range of 22-35% recorded in previous Brookfield buy outs.²⁸

Date	Buyer	Buyout (remaining interest)	Premium
12/2014	BAM	30.6% of Brookfield Residential	25%
2/2016	BAM	67% of Rouse Properties	35%
3/2014	BPY	49% of BPO	22%
3/2018	BPY	66% of GGP	24%
*premium to unaffected share price			

Several analysts agree that privatizing BPY is a good deal for BAM. They point to the potential for accretion of BAM NAV and upside of increased flexibility to operate the assets.²⁹

Simultaneously, BAM spent 2020 boasting about its successful fundraising efforts and reported its highest fundraising period ever in a quarter, raising \$23 billion in the second quarter to invest in the post-pandemic economy.³⁰ BAM has the capital to offer a price that reflects its public statements of BPY's asset value in 3Q19 and 3Q20.³¹ We urge BPY's independent committee to represent the interests of its independent shareholders in negotiations with BAM.

BPY's Future Optimism

Additionally, BPY is optimistic about the future of its assets. In 3Q20, BPY reported its office portfolio being 91% leased on a long-term basis.³² It also predicts that the demand for office space will either remain stable and in some cases increase due to the need for social-distancing.³³ In this period, BPY has also utilized the low-interest rates brought by the pandemic to "finance, refinance, or extended mortgages on nearly \$3.5 billion of office and retail properties at interest rates below 4%."³⁴

While its mall portfolio has weighed on the company's share price, BPY reported 94% of its retail tenants being open and operational in 3Q20 and it was "beginning to see sales not only approaching normalized level but outperformance in certain markets". Specifically, luxury fashion and jewelry stores were the best performing categories with between 36% and 13% year-over-year sales growth, respectively.³⁵

BAM and BPY know the value of BPY's real estate, which public investors helped finance. BPY should demand a higher buyout price from BAM, in the range of \$19.50 - \$21.00 per unit.

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Endnotes

- 1 <https://www.sec.gov/Archives/edgar/data/1001085/000119312521001049/d33782d425.htm>
 - 2 See chart with quotes on page 3.
 - 3 Analyst Report Quotes: “we believe material long-term upside exists to the extent BAM can reinforce the \$26.80 BPY IFRS NAV over time” (Mario Saric, “BAM Bid for BPY... A Week Later,” Scotiabank, January 11, 2021, pg.4); “BPY privatization is likely to be accretive to BAM’s NAV” (Geoffrey Kwan, “Private Eyes, they’re watching you: Modeling out and sensitizing the BPY privatization,” RBC, January 11, 2021, pg.1); “the privatization of BPY makes operational sense (at least in some ways) for BAM; as long-term value-add investors, BAM will have increased flexibility to operate the assets in a manner that allows management to realize the intrinsic value of the underlying assets.” (Dean Wilkinson, “Starting the New Year with a BAM,” CIBC, January 4, 2021, pg. 1) <https://unitehere.box.com/s/0o8yraj9l5ed736er6ih95z4u4b-waoa7>
 - 4 BAM 3Q20 Earnings Call Transcript, p. 3. “Today, we have over \$75 billion of liquidity or dry powder across our private and public entities available for new investments. We see opportunities to deploy this capital beginning to pick up.” “The opportunity set we have with the verticals already is significant.”
 - 5 BAM Q3 Interim Report, pg. 25. https://bam.brookfield.com/~media/Files/B/BrookField-BAM-IR-V2/quarterly-reports/2020/Q3/BAM%202020%20%20Q3Interim_F.pdf “Non-controlling interests in our consolidated results primarily consist of third-party interests in BPY, BEP, BIP, BBU, and their consolidated entities as well as co-investors and other participating interests in our consolidated investments as follows:
AS AT SEP. 30, 2020 AND DEC. 31, 2019
(MILLIONS)
- | | 2020 | 2019 |
|--------------------------|-----------|-----------|
| Brookfield Property..... | \$ 26,247 | \$ 29,165 |
- 6 ibid
 - 7 BAM Q3 2020 Conference Call Transcript, November 12, 2020, pg. 3. <https://bam.brookfield.com/~media/Files/B/BrookField-BAM-IR-V2/events/transcripts/2020/Q3%202020%20BAM%20Transcript-F.pdf>
 - 8 <https://bpy.brookfield.com/press-releases/2019/03-28-2019-212959203>
 - 9 BPY Q1 2019 Earnings Call Transcript, May 6, 2019, pg. 4. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/quarterly-reports/2019/q1-2019-transcript.pdf>
 - 10 Bruce Flatt: “But look, what I can say is this is one of the great environments possibly to buy distressed debt that may have ever been in existence.” BAM Q1 2020, May 14, 2020, pg. 11. <https://bam.brookfield.com/~media/Files/B/BrookField-BAM-IR-V2/events/transcripts/2020/Q1%202020%20BAM%20Transcript-F.pdf>
- BAM’s ownership of BPY increased from 55% to 60% as a result of the issuer bids it funded.
- 11 <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/BPY%202020%20SIB%20Announcement%20Press%20Release%20FINAL.pdf>
 - 12 Mark Rothschild, “BAM absorbs risk, and potential upside, with proposed privatization of BPY”, Canaccord Genuity, January 4, 2021, pg. 2. <https://unitehere.box.com/s/itles3592jzpo3dltm8zrfixeqc170z7>
 - 13 Mark Rothschild, “BAM absorbs risk, and potential upside, with proposed privatization of BPY”, Canaccord Genuity, January 4, 2021, pg. 2. <https://unitehere.box.com/s/itles3592jzpo3dltm8zrfixeqc170z7>
 - 14 Brookfield Investor Day, September 24, 2020, Slide 40. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/ir-day/2020/BPY%20IR-2020.pdf>
 - 15 Brookfield Investor Day, BPY Transcript, September 24, 2020, pg.9 . <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/ir-day/2020/bpy-2020-investor-day-transcript.pdf>
 - 16 See chart- 2019 Q3 Bruce Flatt quote & 2020 Q3 Bruce Flatt quote
 - 17 BPY Q1 2019 Earnings Call Transcript, May 6, 2019, pg. 4. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/quarterly-reports/2019/q1-2019-transcript.pdf>
 - 18 BPY Q1 Earnings Call Transcript, May 6, 2019, pg. 2. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/quarterly-reports/2019/q1-2019-transcript.pdf>
 - 19 BAM Letter to Shareholders Q3 2019, November 14, 2019, pg.3. https://bam.brookfield.com/~media/Files/B/BrookField-BAM-IR-V2/letters-to-unitholders/2019/F_BAM%20Q3_2019_LtS.pdf
 - 20 BPY Q3 2019 Earnings Call Transcript, November 6, 2019, pg. 3. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/quarterly-reports/2019/bpy-usq-transcript-2019-11-06.pdf>
 - 21 BPY Q4 2019 Earnings Call Transcript. February 5, 2020, pg. 7. https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/BPY-USQ_Transcript_2020-02-05.pdf
 - 22 BPY Q1 2020 Earnings Call Transcript, May 8, 2020, pg. 3. https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/BPY-USQ_Transcript_2020-05-08.pdf
 - 23 BPY Q2 2020 Earnings Call Transcript, August 6, 2020, pg. 4. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/bpy-usq-transcript-2020-08-06.pdf>
 - 24 BAM Q3 2020 Conference Call Transcript, November 12, 2020, pg. 3. <https://bam.brookfield.com/~media/Files/B/BrookField-BAM-IR-V2/events/transcripts/2020/Q3%202020%20BAM%20Transcript-F.pdf>
 - 25 Brookfield Investor Day, BPY Transcript, September 24, 2020, pg.9 . <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/ir-day/2020/bpy-2020-investor-day-transcript.pdf>
 - 26 Bloomberg article, “Brookfield Bids to Take Brookfield Property Partners”, filed with SEC by Brookfield Asset Management, 1/5/21: <https://www.sec.gov/Archives/edgar/data/1001085/000119312521002205/d101029d425.htm>

- 27 <https://www.sec.gov/Archives/edgar/data/1001085/000119312521001049/d33782d425.htm>
- 28 Mark Rothschild, "BAM absorbs risk, and potential upside, with proposed privatization of BPY", Canaccord Genuity, January 4, 2021, pg. 2. <https://unitehere.box.com/s/itles3592jzpo3dlm8zrfixeqc17Oz7>
- 29 Analyst Report Quotes: "we believe material long-term upside exists to the extent BAM can reinforce the \$26.80 BPY IFRS NAV over time" (Mario Saric, "BAM Bid for BPY... A Week Later," Scotiabank, January 11, 2021, pg.4); "BPY privatization is likely to be accretive to BAM's NAV" (Geoffrey Kwan, "Private Eyes, they're watching you: Modeling out and sensitizing the BPY privatization," RBC, January 11, 2021, pg.1); "the privatization of BPY makes operational sense (at least in some ways) for BAM; as long-term value-add investors, BAM will have increased flexibility to operate the assets in a manner that allows management to realize the intrinsic value of the underlying assets." (Dean Wilkinson, "Starting the New Year with a BAM," CIBC, January 4, 2021, pg. 1) <https://unitehere.box.com/s/Oo8yraj9l5ed736er6ih95z4u4b-waoa7>
- 30 BAM Q2 2020 Conference Call Transcript, August 13, 2020, pg. 2.
- 31 See Bruce Flatt quotes in chart.
- 32 BPY Q3 2020, November 6, 2020, pg. 3. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/bpy-usq-transcript-2020-11-06-v1.pdf>
- 33 <https://www.brookfield.com/future-office-not-what-you-might-think>
- 34 BPY Q3 2020, November 6, 2020, pg. 6. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/bpy-usq-transcript-2020-11-06-v1.pdf>
- 35 BPY Q2 2020 Earnings Call Transcript, November 6, 2020, pg. 3. <https://bpy.brookfield.com/~media/Files/B/Brookfield-BPY-IR-V2/bpy-usq-transcript-2020-11-06-v1.pdf>