

THOMSON REUTERS

# EDITED TRANSCRIPT

Q2 2019 iStar Inc Earnings Call

EVENT DATE/TIME: AUGUST 01, 2019 / 2:00PM GMT



## CORPORATE PARTICIPANTS

**Jason Fooks** *iStar Inc. - SVP of IR & Marketing*

**Jay S. Sugarman** *iStar Inc. - Chairman & CEO*

**Marcos Alvarado** *iStar Inc. - President & CIO*

## CONFERENCE CALL PARTICIPANTS

**Jade Joseph Rahmani** *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

**Stephen Albert Laws** *Raymond James & Associates, Inc., Research Division - Research Analyst*

## PRESENTATION

### Operator

Good morning, and welcome to iStar's Second Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, today's conference is being recorded. At this time, for opening remarks and instructions, I would like to turn the conference over to Jason Fooks, Senior Vice President of Investor Relations and Marketing. Please go ahead, sir.

---

### Jason Fooks *iStar Inc. - SVP of IR & Marketing*

Thank you, and good morning, everyone. Thank you for joining us today to review iStar's Second Quarter 2019 Earnings. With me today are Jay Sugarman, Chairman and Chief Executive Officer; and Marcos Alvarado, our President and Chief Investment Officer.

This morning, we published our earnings presentation highlighting our second quarter results, and our call will refer to these slides, which can be found on our website at [istar.com](http://istar.com) in the Investors section. There will be a replay of the call beginning at 12:00 p.m. Eastern Time today. The replay is accessible on our website or by dialing 1-800-475-6701 with a confirmation code of 469594.

Before I turn the call over to Jay, I'd like to remind everyone that statements in this earnings call, which are not historical facts will be forward looking. IStar's actual results may differ materially from these forward-looking statements and the risk factors that could cause these differences are detailed in SEC reports. IStar disclaims any intent or obligation to update these forward-looking statements, except as expressly required by law.

Now I'd like to turn the call over to iStar's Chairman and CEO, Jay Sugarman. Jay?

---

### Jay S. Sugarman *iStar Inc. - Chairman & CEO*

Thanks, Jason. Our second quarter was a very strong one, delivering record earnings and significantly increasing the strength of our balance sheet. When we announced our strategic shift to focus on reinventing the ground lease sector at the beginning of the year, we created a list of goals we wanted to accomplish. I'm pleased to report we've made excellent progress towards those goals in the first half of the year. So let me take you through what we've been able to do so far.

One of our key goals was to highlight the value in our portfolio that we felt was not being recognized in the share price. To that end, we successfully closed 2 large transactions in the second quarter that created approximately \$400 million in gains above our book basis. The sale of our Preferred Freezer portfolio to the largest cold storage company in the country and the expansion and extension of our Bowlero portfolio enabled us to not only demonstrate the value created in those portfolio assets over the years, but also helped fuel the record earnings this quarter and materially increase book value. We also sought other ways to highlight shareholder value in 2019. We raised our dividend by 11% earlier in the year and have continued to buy back shares in the open market.

In the first half of the year, we bought back approximately 9% of outstanding shares at a cost below \$9.50 per share, capturing additional value. But perhaps, most importantly, given our strategic focus, we wanted to help Safehold gain traction with both customers and investors and continue to build its innovative and exciting growth story in the marketplace. We believe Safehold is following a path many of the most successful companies in the country have taken, making a big industry much more efficient and delivering a decisively better customer experience. These are universal themes attractive to investors across the spectrum.

And during the second quarter, we saw Safehold reach several important milestones. Its portfolio tripling in size since the IPO, its market



penetration with customers doubling and its share price rising some 50% since its IPO. It's exciting to us as we believe we are still in the very early innings of this opportunity. Safehold recently increased its investment guidance for the year and its customer list continues to grow. We have already seen a material increase in the value of iStar's shareholdings in SAFE well above our cost. But we believe Safehold's share price still reflects only a small portion of the underlying value we believe we are creating, and we will seek to continue investing in Safehold shares at these attractive prices.

Combined, these steps have helped drive significant value at iStar, and we will continue to work to build on this momentum, while also continuing to strengthen our balance sheet and reduce legacy assets as a percentage of our portfolio.

I'll talk more about the second half of the year in a minute. Let's have Marcos take you through the numbers first. Marcos?

---

**Marcos Alvarado iStar Inc. - President & CIO**

Thanks, Jay, and good morning, everyone. My remarks will refer to the slides in the earnings presentation posted on our website this morning.

Beginning with Slide 3. We had a record quarter highlighted by \$363 million or \$4.55 per share of net income and \$317 million or \$3.98 per share of adjusted income. Results were driven primarily by 2 previously announced transactions, Preferred Freezer and Bowlero, which generated \$220 million and \$180 million of gains this quarter, respectively.

We have made some large strides at Safehold. And our investment in the stock appreciated by nearly 40% in Q2 as SAFE is one of the top-performing REITs during the quarter. All the recent progress we have made has translated into significant growth in the book value per share and -- iStar stock was one of the top-performing REITs during Q2.

Flipping to Slide 4. Let me take a quick moment to walk you through this quarter's large gains in a little bit more detail. First, Preferred Freezer. During the quarter, we sold a portfolio of 7 cold storage properties net leased to Preferred Freezer for a price of \$440 million, including the assumption of \$228 million of debt by the purchaser resulting in a gain of \$220 million. As we have stated in the past, we may opportunistically sell net lease assets when market conditions are favorable.

Second, with Bowlero, we made an additional investment of \$57 million to purchase 9 bowling and entertainment centers and committed to fund an additional \$55 million towards future purchases. All of the leases will be subject to our existing master leases.

In addition, we extended the term of our 2 master leases by 15 years to 2047. As a result of the transaction, we were required to reclassify our lease from an operating lease to a sale type lease, resulting in a \$180 million gain based on the fair market value of our assets.

Our long-term relationship with Bowlero continues to be productive, and this recent transaction helps highlight the underlying value that has been created in our portfolio over the last 15 years.

Moving to Slide 5. We had a productive quarter, investing over \$250 million. This included \$154 million of fundings, primarily related to loans and net leases and an additional \$7 million of open market Safehold stock purchases. CapEx was a little over \$50 million in the second quarter, driven by our investment in Asbury Park. We are very pleased with the progress we've made in Asbury and the continued strength in pricing for the residential condominiums at Asbury Ocean Club. At the beginning of July, we opened the Asbury Ocean Club hotel and began closing on units. Since we opened the building, we've seen a nice pickup in traffic at our sales center, and more importantly an increase in volume of units under contract.

For the latter half of the year, we expect sales proceeds to exceed any remaining capital expenditures necessary at the building. And as a result, our investment balance in Asbury Park should begin to decrease. At the same time, we continue to market other legacy assets for sale.

We continue to believe STAR trades at a meaningful discount to book value. On last quarter's call, we announced that the Board reauthorized up to \$50 million of share repurchases. During the quarter, we bought back \$39 million of stock or about 6% of the shares

outstanding.

On Slide 6, we highlighted sales performance during the quarter. As we announced earlier this year, scaling the ground lease business has become the focus of iStar's go-forward strategy, and we are building momentum with both investors and customers in this endeavor.

For the second quarter, SAFE generated \$0.18 of earnings per share and signed up \$186 million of ground leases and raised its full year investment target from \$750 million to \$1 billion, reflecting the strengthening pipeline. Achieving this investment target would more than double the size of the portfolio from the beginning of the year. And we are very excited by the progress we are making, and we believe the value creation should translate over to iStar's stock performance.

Lastly, on Slide 7, we highlighted the substantial equity value growth at iStar. Our book value per share on a GAAP and adjusted basis grew to \$9.95 per share and \$14.65 per share, respectively. And when factoring in the market value of our Safehold investment, the adjusted book value sits at \$18.02 per share, representing a significant premium to the current stock price.

In summary, this quarter was marked by significant gains, continued investment activity and meaningful progress at Safehold, all culminating in value growth at iStar.

With that, let me turn it back to Jay.

---

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Thanks, Marcos. I mentioned, we've achieved many of the goals we set out at the beginning of the year. So we've begun focusing on new goals for the second half of the year. Foremost among them is to accelerate the growth of Safehold, and we've raised Safehold's investment guidance for the full year by 33%, with most of that increase taking place in the second half of the year. We'll also seek to further strengthen our balance sheet. And lastly, we're doing a thorough search for a new CFO who will be a strong addition to our team, and we'll work to try to have that process wrapped up by the end of the year.

And with that, operator, let's go ahead and open it up.

---

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) First question today is from Jade Rahmani with KBW.

---

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Regarding the second half 2019 goals, can you remind us of what you just said regarding the balance sheet? I think I heard you say strengthen the balance sheet. Curious if you could elaborate?

---

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Yes. Look, I think with the growing success of Safehold, our goal is to create a very strong runway for iStar to continue to help accelerate that growth. We don't have any near-term maturities. But as the balance sheet was strengthened in the first half of the year, it's going to give us some opportunities to continue to work on lengthening maturities, et cetera, on this -- in the second half of the year.

---

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Okay. And I assume in addition from iStar's perspective, you would not contemplate equity issuance?

---

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Until we see the valuation gap close a little more, Jade, it's -- right now, we're still a buyer of the stock.

---



**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Okay. Turning to the mark-to-market book value calculations. Do you think the loan portfolio as well as the legacy assets in current terms are both worth carrying value, inclusive of any accumulated depreciation?

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

I do. And when you say inclusive of depreciation, you mean gross book value, not net, correct?

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Yes, relative to gross book value.

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Yes. I do.

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Would you contemplate any bulk portfolio sales of -- for example, the real estate finance portfolio or certain aspects of the net lease portfolio in order to streamline the organization's focus on the ground lease business?

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Yes. Jade, I think, as we've said in the past, those are part of the long-term strategic goals. We're looking for the best place to deploy capital. And right now, we can tell you that the ground lease sector is a big focus for us, but we can't been able -- and won't be able to deploy all of the capital that iStar has if we were to exit other businesses, and right now those other businesses are actually helping to continue the ecosystem that we're trying to build. So right now, net lease is still a core part of our business and finance is still one of our core capabilities. But if we were to find an opportunity to redeploy capital, those are certainly places we could access a significant amount of capital.

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

Okay. In terms of the SAFE float and stated goal for it to grow its equity base, what's the rationale behind iStar's continual regular purchases of SAFE stock?

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

Yes. That is part of the 10b5 plan. So it's not something we're doing on a discretionary basis. We set that up earlier in the year when we thought the value was significantly undervalued, and we still think it represents an extraordinary investment for iStar's shareholders. We represent only about 5%, maybe on a slow day 10% of the actual volume in the marketplace. So we're not driving the stock higher. We're just being quiet in the background and continue to accumulate shares that we think do not represent anywhere close to the value we think we're creating. We continue to believe it's one of the best investments we can make with capital at iStar, and we will continue to look for ways to increase that position.

**Jade Joseph Rahmani Keefe, Bruyette, & Woods, Inc., Research Division - Director**

And on the net -- on the real estate finance portfolio, are there any loans in the portfolio on a watch list? Or that you're reviewing in terms of potential risk of impairment or loss?

**Jay S. Sugarman iStar Inc. - Chairman & CEO**

There are none. I will tell you, we're continuing to watch this macro environment just to make sure that we don't get surprised from somewhere. We have seen some of these markets get very frothy on the finance side. So we have not been participating. But what we're most focused on right now is continuing to build a strong balance sheet and really accelerating Safehold. And right now, the loan book shouldn't be a problem.

**Operator**

We have a question from Stephen Laws of Raymond James.

**Stephen Albert Laws *Raymond James & Associates, Inc., Research Division - Research Analyst***

A lot of moving parts this quarter and I appreciate the disclosure in your investor supplement. Can you give us a little more color on Asbury? I know you're getting at a point where the investment exposure starts to decrease and you mentioned that in your prepared remarks, Jay. But can you talk about kind of the timing of that and how we should think about the sales there? And was that a 12-month process, is it a 36-month process? How should we think about the Asbury development as it progresses from today?

**Jay S. Sugarman *iStar Inc. - Chairman & CEO***

Sure. Look, we have done a lot of work to build the profile of Asbury Park. We've seen some really strong results, and we think Asbury Ocean Club is only going to add to that storyline. Our internal projections were more like 36 months in terms of total sellout. With the hotel opening, we've got a lot of positive reaction from people who are surprised that how good it came out, the quality, the views, the environment. So we're certainly hopeful we'll see a strong reaction in sales and maybe shorten that 36-month sell-out period. But one thing, anecdotally, I can tell you that surprised us is the number of buyers who want to focus on the highest priced units. There was some question in the marketplace about, is there a ceiling in New Jersey on what people pay for high quality at the beach? And I think we feel pretty comfortable that there is a lot of interest in the highest quality units in the building. So we have no concerns about sort of the price point issue that still is a question mark. Average selling price in the building is still around \$1,100 a foot, which is new high-water mark. And I think we believe it's well deserved given what we put on the ground there.

**Stephen Albert Laws *Raymond James & Associates, Inc., Research Division - Research Analyst***

Great. Well, Jay, someone who is landlocked high end at the beach sounds awfully nice. Thinking about the other legacy or noncore assets, although Asbury certainly kind of seems core at this point. But as we think about the noncore and the legacy or the development portfolio, how much more CapEx do you think is remaining for you to get the assets where you would like them to be in their business plan and then can monetize those? And kind of what's the time frame over those expenditures?

**Jay S. Sugarman *iStar Inc. - Chairman & CEO***

Yes, I think we give ourselves plus or minus 10% cushion on what we have to invest and what decisions are the best for shareholders. As we said at the beginning of the year, we are definitely not going to be allocating a lot of capital unless there's a significant return associated with that. So I still expect, as we grind down that legacy portfolio, particularly in the next 12 months that you'll see less and less capital go into that. But we still have some outstanding capital for Asbury and have some outstanding capital sort of in a bunch of smaller chunks. But overall, the trend is definitely less and less and less. And I think once Asbury is fully built and all that capital is out, you're not going to really need to pay attention to that number much more.

**Stephen Albert Laws *Raymond James & Associates, Inc., Research Division - Research Analyst***

Great. And you touched on this in some of your responses to Jade's question and you did mention that the SAFE purchases are under 10b5. But I didn't run the math, but I'm very confident you guys were the best-performing mortgage REIT since the last conference call. You're still active with your repurchase. Can you talk about how you view repurchasing iStar shares here versus other opportunities for your capital, whether it's increasing the investment in SAFE or whether it's new investments in CRE debt or other things you can do? But how do you think about the trade-offs between stock repurchases at iStar given the appreciation versus other opportunities?

**Jay S. Sugarman *iStar Inc. - Chairman & CEO***

Yes, good question. I think we have historically said we're always looking and evaluating real time about where is the best place to deploy capital to build overall value and that incorporates not only the asset value per share but also the franchise value and the enterprise value. We think Safehold right now not only has an opportunity to create very attractive assets on a risk-adjusted basis, but also to create real franchise value that will reflect back into iStar shares.

So our first and foremost target right now is to build that business, build that enterprise, capture value for iStar through its ownership position and management position there. But if we have excess liquidity, if we have excess capital, we're constantly looking at the ability to buy in iStar shares at a discount as also very attractive. And as I said, we think the finance market is pretty frothy right now. So that's not really getting a lot of our attention. We think we can create much better risk-adjusted returns inside our own balance sheet and inside of Safehold. So it continues to be a focus. We've already gone back for a second authorization from our Board. We still have some availability under that one, and we'll take a new look at things once that's exhausted.

**Stephen Albert Laws *Raymond James & Associates, Inc., Research Division - Research Analyst***

Yes. And I sort of mentioned in the last question, but I guess, the other option would be to increase the dividend other than buying back stock, which you've already done once since you've reinstated the dividend. So are there any thoughts around that? I don't think you guys are tied to any distribution requirements, just given the NOL tax loss carryforwards probably, but any thoughts around again the dividend versus repurchase?

**Jay S. Sugarman *iStar Inc. - Chairman & CEO***

Yes. I think our construct is really to review that annually, not quarterly. We made the 11% increase really to demonstrate the confidence we had in the rest of the year. I think again it's a constant dialogue depending on where places we can put capital, what they look like at any moment in time. So I don't think that's front and center right now, but certainly part of our annual plan is to continue to deliver dividends back to shareholders and increase value.

**Operator**

And Mr. Fooks, we have no further questions.

**Jason Fooks *iStar Inc. - SVP of IR & Marketing***

Okay. Great. Thank you, and if anyone else should have additional questions on today's earnings release, please feel free to contact me directly. Paul, would you please give the conference call replay instructions once again? Thanks.

**Operator**

Ladies and gentlemen, this conference will be available for replay afternoon Eastern Time today through midnight Eastern Time on August 15. You may access the AT&T Teleconference replay system at any time by dialing 1-800-475-6701, entering the access code 469594. International participants dial 320-365-3844. And that does conclude our conference for today. Thank you for your participation and for using AT&T Executive Teleconference. You may now disconnect.

**DISCLAIMER**

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Briefs are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT BRIEFS REFLECTS THOMSON REUTERS'S SUBJECTIVE CONDENSED PARAPHRASE OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT BRIEF. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2019 Thomson Reuters. All Rights Reserved.

