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Deductible / Ron Stein

Harel's Goal: 10% of the portfolio — in Real Estate

The large financial institutions are looking for new investment channels that will produce a yield that is unaffected by the vagaries of the capital market—and Harel has a central role in this trend • Investment real estate already makes up more than 5% of the investment money of the insurance company — and it is only increasing the rate of the purchases

In recent years, the investment portfolios of the large financial institutions have changed considerably, and they have also begun to include alternative investment channels to the relatively standard ones in shares, Government bonds and corporate bonds, deposits and cash, etc. The alternative channel that has increased the most in recent years, at least in the large insurance groups, is direct investments in investment real estate. The largest investment real estate portfolios among the financial institutions are held by Migdal, Clal Insurance and Harel. The last of these began to enter this field a few years ago, and it even established a special investment unit for this subject approximately six years ago.

'There is a big appetite for investments in this field, as well as for infrastructure investments,' explains a senior investor in a financial institution, who stated that 'the financial institutions are turning more and more to the field of real estate, because of the understanding that it is a tool for the correct investment of money in the long term. This is in line with financial institutions around the world, which are creating a presence for themselves in real estate, inter alia as a lesson from the economic crisis of 2008 and 2009 — when it became clear how great the fluctuations are in the financial markets.'

Portfolio value of more than 5 billion sheqels

Following our exposure of Clal Insurance's real estate portfolio, Globes is now exposing the investment real estate portfolio of the Harel Group, which is managed in the Investment Division by Gadi Ben Haim. Harel's Real Estate Department currently includes ten employees, who centralize under their control the activity in the field.

As of today, the size of Harel's investment real estate portfolio stands at approximately 4.4 billion sheqels, and together with the group's real estate for personal use, this already amounts to a real estate portfolio with a combined value of 5.06 billion sheqels. This amount does not include an investment in investment funds that specialize in direct investments in real estate.

More than 3.3 billion sheqels of the current fair value is attributed to direct investments in investment real estate with funds of members and policyholders, and the balance is attributed to the group's nostro funds. As a rule, for investments in investment real estate that are not for the group's personal use, the proportion stands at approximately 75% of finance from members' and policyholders' funds, and the balance from nostro.

There are more transactions in the pipeline

At this time, Harel is in an advanced stage of several major transactions for the purchase of investment real estate, and especially a joint purchase with the Gazit company of the Ir-Yamim mall in Netanya from the Azorim company. According to publications on the subject, the value of the mall for the purpose of the transaction stands at approximately 390 million sheqels. Together with its share in this transaction, it would appear that Harel is on the way to a real estate portfolio with a total value of approximately 5.5 billion sheqels. This value includes other investments that are in the pipeline or before closing — such as the project in the Argaz compound in Tel Aviv, and the purchase of half of the Comverse compound in Raanana from Blue Square Real Estate for consideration of approximately 140 million sheqels.

In its financial statements for 2012, which were published yesterday, Harel stated that at the end of 2012, in its insurance, pension and provident fund operations, it managed assets on a total scale of approximately 90.7 billion sheqels. It follows that as of the end of last year, 5.6% of the total portfolio managed by the Harel Group (excluding short-term and medium-term savings assets managed by Harel Finance, which amount to approximately an additional 28.4 billion sheqels) was invested directly in real estate.

The goal that the company has defined for itself is a proportion of 10% between the size of the real estate direct investment portfolio and the overall portfolio. In view of the fact that the total assets of the group is growing at a significant rate, it is expected to continue significant real estate purchases for some years to come, until it comes close to the aforesaid target. In this context, we should point out that in 2012 Harel invested more than 900 million sheqels in investment real estate.

Strong tenants abroad

The logic behind these investments — which are gradually playing a more and more significant part in the public assets managed by the financial institutions — lies in a desire to vary the institutional portfolio for long-term investments, and for cash flow investment channels that constitute a kind of anchor for a relatively stable yield, which is not directly and immediately related to yields of securities traded on the capital markets. For this reason, especially if you ask Harel's staff, the real estate portfolio is not an end in itself, and the group has no aspiration to become a kind of real estate company, but it is an important and effective tool for creating yield producing income in some of the total investments managed by the group.

Over the years, according to people in the market, the average annual yield of the insurance companies on direct investments in real estate is far greater than the level of 7%.

'Over time, the financial institutions buy assets with a yield of between 7% and 8.5%. Admittedly, these transactions involve expenses that reduce the aforesaid yield, but abroad there are leveraged transactions, and the value of assets rise, so that overall until now they have reached significantly higher yields than the aforesaid lowest level,' explains someone involved in the field.

Thus, according to estimates of persons in the market, the NOI (Net Operative Income) in Harel's real estate portfolio amounts to approximately 260-270 million sheqels per annum, and the yield on the portfolio stands at approximately 8.4%. Harel chose not to respond to these figures.

Harel has been prominent in recent years for the high rate of investment real estate purchases, mainly insofar as foreign purchases are concerned. Currently, approximately 62% of the value of Harel's real estate portfolio is in Israel, 22% in England, approximately 12% in the United States and 4% in Germany and Switzerland. Harel's tenants abroad include strong tenants in long-term contracts, such as the UK Government, Unicef and the Aviva company.

To the best of our knowledge, the scope of the positive revaluations for Harel's real estate investments abroad only in the years 2009-2012 stood at approximately 440 million sheqels (partly from realizations of profits that the company had already made), something that indicates an increase in the value of the total assets that were bought by the company abroad.

Regarding Harel's exposure to investing in foreign assets, a person involved in the matter says that 'Harel's portfolio is very varied, perhaps more than others, which focus more on offices, which has been regarded over the years as more standard.' Thus, Harel's portfolio of direct real estate investments (in value rather than area terms) is composed of the following: approximately 58% in leased office real estate, approximately 31% in (retail) office real estate, approximately 8% in residential real estate and approximately 3% in logistic real estate. •

ron-s@globes.co.il

The Investment Real Estate Portfolio of the Harel Group

5,060	700	5.6%	10%	Approx. 270	Approx. 8.4%	62%
Value of Real Estate Portfolio	Of this — Real Estate for personal use	Percentage of direct investment in real estate out of portfolio	Target percentage of investment in real estate out of portfolio	Net Operating Income (NOI) in 2012 *	Yield on investments in real estate in 2012 *	Percentage of investment in assets in Israel

* Estimates on basis of assessments made by persons in the market