Gazit Globe Ltd. or First Capital Realty Inc.: Which Is the Better Buy?

Description

Does the name Dori Segal ring any bells?

It should if you've owned **First Capital Realty Inc.** (TSX:FCR) for more than five years. Segal was CEO for 15 years until February 2015 and is still the company's chairman.

Segal transitioned out of his position to spend more time growing **Gazit Globe Ltd.** (TSX:GZT)(NYSE:GZT), an Israeli-controlled real estate company, which, not coincidentally, also owns 33% of First Capital.

Both have underperformed relative to the TSX Composite Index in 2017 — Gazit Globe and First Capital are up 1% and 5.4%, respectively, versus 7.3% for the TSX — yet an argument can be made to buy either stock.

By the end of this article, you'll have my answer as to which is the better buy.

Gazit Globe's value

Over the past three years, Gazit Globe's stock's delivered a negative annual return of 2.1% at a time when both the TSX and New York Stock Exchange have handily beat it.

In those three years, Gazit Globe's net operating rental income has remained relatively flat around US$831 million, or $1.02 a share.

The company has ownership varied ownership interests in four publicly traded companies: First Capital at 33%, **Regency Centers Corp.** (NYSE:REG) at 12%, **Citycon** (trades on Helsinki Stock Exchange) at 44% and **Atrium** (trades on the Vienna and Euronext Stock Exchanges) at 60%. It also owns 100% of the three private subsidiaries operating shopping centres in Brazil, Israel and Gazit Horizons, its new U.S. subsidiary investing in mixed-use developments in urban centres.

Together, it has an ownership interest in 426 properties in 20 countries with 71 million square feet of space valued at US$22.1 billion.

A quick back-of-the-napkin calculation of its interests in the four public companies is $5.3 billion, or more than double its current market cap, and that doesn't include its three private subsidiaries.

It's a buy, right? Not so fast.

Both its Citycon and Atrium ownership interests are consolidated on its balance sheet, meaning the debt of those businesses, as well as its private subsidiaries, also have to be considered before making an assessment.

At the end of 2016, it had $5 billion in long-term debt outstanding. So, for the investment to make sense, the private subsidiaries need to be worth more than $300 million to deliver any value.

Considering it carries its investment in its Brazil subsidiary at $818 million, I'd say Gazit Globe's stock is undervalued. By how much? That's the million-dollar question.

Bottom line on both stocks

Risk-averse investors should buy First Capital's stock for two reasons. First, because it avoids the various currencies Gazit Globe uses to carry out its business. Second, it's got a dividend yield of 4.1% you can count on.

However, as value investments go, if you're a patient investor, Gazit Globe probably has the better upside.

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