EASTGROUP PROPERTIES INC
Form 10-Q
July 21, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTER ENDED JUNE 30, 2014 COMMISSION FILE NUMBER 1-07094

EASTGROUP PROPERTIES, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

MARYLAND	13-2711135
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

190 EAST CAPITOL STREET SUITE 400 JACKSON, MISSISSIPPI	39201
(Address of principal executive offices)	(Zip code)

Registrant's telephone number: (601) 354-3555

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES (x) NO ( )

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES (x) NO ( )

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer (x) Accelerated Filer ( ) Non-accelerated Filer ( ) Smaller Reporting Company ( )

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ( ) NO (x)

The number of shares of common stock, $.0001 par value, outstanding as of July 18, 2014 was 31,620,960.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES

FORM 10-Q

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FOR THE QUARTER ENDED JUNE 30, 2014

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

	June 30, 2014 (Unaudited)	December 31, 2013
ASSETS		
Real estate properties	$1,840,488	1,778,559
Development	184,618	148,767
	2,025,106	1,927,326
Less accumulated depreciation	(576,182)	(550,113)
	1,448,924	1,377,213
Real estate assets held for sale	425	—
Unconsolidated investment	2,832	2,764
Cash	19	8
Other assets	96,408	93,427
TOTAL ASSETS	$1,548,608	1,473,412
LIABILITIES AND EQUITY		
LIABILITIES		
Secured debt	$488,632	499,793
Unsecured debt	305,000	305,000
Unsecured bank credit facilities	142,392	88,952
Accounts payable and accrued expenses	45,017	37,104
Other liabilities	26,796	23,858
Total Liabilities	1,007,837	954,707
EQUITY		
Stockholders' Equity:		
Common shares; $.0001 par value; 70,000,000 shares authorized; 31,620,960 shares issued and outstanding at June 30, 2014 and 30,937,225 at December 31, 2013	3	3
Excess shares; $.0001 par value; 30,000,000 shares authorized; no shares issued	—	—
Additional paid-in capital on common shares	832,061	790,535
Distributions in excess of earnings	(294,741)	(278,169)
Accumulated other comprehensive income (loss)	(1,148)	1,629
Total Stockholders' Equity	536,175	513,998
Noncontrolling interest in joint ventures	4,596	4,707
Total Equity	540,771	518,705
TOTAL LIABILITIES AND EQUITY	$1,548,608	1,473,412

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
REVENUES				
Income from real estate operations	$53,801	48,957	106,578	97,110
Other income	18	139	53	186
	53,819	49,096	106,631	97,296
EXPENSES				
Expenses from real estate operations	15,625	13,663	30,637	27,204
Depreciation and amortization	17,154	16,301	34,322	31,863
General and administrative	2,958	2,777	6,406	6,141
Acquisition costs	160	138	160	167
	35,897	32,879	71,525	65,375
OPERATING INCOME	17,922	16,217	35,106	31,921
OTHER INCOME (EXPENSE)				
Interest expense	(8,898)	(8,717)	(17,884)	(17,338)
Other	218	255	534	479
INCOME FROM CONTINUING OPERATIONS	9,242	7,755	17,756	15,062
DISCONTINUED OPERATIONS				
Income from real estate operations	—	35	—	36
INCOME FROM DISCONTINUED OPERATIONS	—	35	—	36
NET INCOME	9,242	7,790	17,756	15,098
Net income attributable to noncontrolling interest in joint ventures	(124)	(147)	(266)	(301)
NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS	9,118	7,643	17,490	14,797
Other comprehensive income (loss) - cash flow hedges	(1,740)	2,118	(2,777)	2,340
TOTAL COMPREHENSIVE INCOME	$7,378	9,761	14,713	17,137
BASIC PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Income from continuing operations	$0.29	0.25	0.56	0.49
Income from discontinued operations	0.00	0.00	0.00	0.00
Net income attributable to common stockholders	$0.29	0.25	0.56	0.49
Weighted average shares outstanding	31,137	29,991	30,972	29,900
DILUTED PER COMMON SHARE DATA FOR NET INCOME ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				
Income from continuing operations	$0.29	0.25	0.56	0.49
Income from discontinued operations	0.00	0.00	0.00	0.00
Net income attributable to common stockholders	$0.29	0.25	0.56	0.49
Weighted average shares outstanding	31,244	30,096	31,063	29,990
AMOUNTS ATTRIBUTABLE TO EASTGROUP PROPERTIES, INC. COMMON STOCKHOLDERS				

Income from continuing operations	$9,118	7,608	17,490	14,761
Income from discontinued operations	—	35	—	36
Net income attributable to common stockholders	$9,118	7,643	17,490	14,797

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

	Common Stock	Additional Paid-In Capital	Distributions in Excess of Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest in Joint Ventures	Total
BALANCE, DECEMBER 31, 2013	$3	790,535	(278,169)	1,629	4,707	518,705
Net income	—	—	17,490	—	266	17,756
Net unrealized change in fair value of interest rate swaps	—	—	—	(2,777)	—	(2,777)
Common dividends declared – $1.08 per share	—	—	(34,062)	—	—	(34,062)
Stock-based compensation, net of forfeitures	—	3,908	—	—	—	3,908
Issuance of 634,138 shares of common stock, common stock offering, net of expenses	—	39,359	—	—	—	39,359
Issuance of 1,630 shares of common stock, dividend reinvestment plan	—	103	—	—	—	103
Withheld 31,417 shares of common stock to satisfy tax withholding obligations in connection with the vesting of restricted stock	—	(1,844)	—	—	—	(1,844)
Distributions to noncontrolling interest	—	—	—	—	(377)	(377)
BALANCE, JUNE 30, 2014	$3	832,061	(294,741)	(1,148)	4,596	540,771

See accompanying Notes to Consolidated Financial Statements (unaudited).

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Six Months Ended June 30,	
	2014	2013
OPERATING ACTIVITIES		
Net income	$17,756	15,098
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization from continuing operations	34,322	31,863
Depreciation and amortization from discontinued operations	—	80
Stock-based compensation expense	2,824	2,327
Gain on sales of land and real estate investments	(95)	—
Changes in operating assets and liabilities:		
Accrued income and other assets	2,128	2,765
Accounts payable, accrued expenses and prepaid rent	(3,123)	743
Other	(80)	(62)
NET CASH PROVIDED BY OPERATING ACTIVITIES	53,732	52,814
INVESTING ACTIVITIES		
Real estate development	(56,125)	(40,165)
Purchases of real estate	(41,751)	(69,952)
Real estate improvements	(9,912)	(9,501)
Proceeds from sales of real estate investments	3,471	—
Repayments on mortgage loans receivable	78	52
Changes in receivable for development infrastructure cost reimbursements	—	(1,351)
Changes in accrued development costs	12,076	2,970
Changes in other assets and other liabilities	(4,536)	(4,446)
NET CASH USED IN INVESTING ACTIVITIES	(96,699)	(122,393)
FINANCING ACTIVITIES		
Proceeds from unsecured bank credit facilities	165,969	194,775
Repayments on unsecured bank credit facilities	(112,529)	(94,002)
Repayments on secured debt	(11,152)	(12,296)

Debt issuance costs	(42)	(1,459)
Distributions paid to stockholders (not including dividends accrued on unvested restricted stock)	(34,183)	(31,874)
Proceeds from common stock offerings	37,033	13,877
Proceeds from exercise of stock options	—	120
Proceeds from dividend reinvestment plan	103	105
Other	(2,221)	(915)
NET CASH PROVIDED BY FINANCING ACTIVITIES	42,978	68,331
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11	(1,248)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	8	1,258
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$19	10
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for interest, net of amount capitalized of $2,336 and $2,560 for 2014 and 2013, respectively	$17,350	16,657

See accompanying Notes to Consolidated Financial Statements (unaudited).

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EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(1) BASIS OF PRESENTATION

The accompanying unaudited financial statements of EastGroup Properties, Inc. ("EastGroup" or "the Company") have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In management's opinion, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The financial statements should be read in conjunction with the financial statements contained in the 2013 annual report on Form 10-K and the notes thereto. Certain reclassifications have been made in the 2013 consolidated financial statements to conform to the 2014 presentation.

(2) PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of EastGroup Properties, Inc., its wholly owned subsidiaries and its investment in any joint ventures in which the Company has a controlling interest. At June 30, 2014 and December 31, 2013, the Company had a controlling interest in two joint ventures: the 80% owned University Business Center and the 80% owned Castilian Research Center. The Company records 100% of the joint ventures' assets, liabilities, revenues and expenses with noncontrolling interests provided for in accordance with the joint venture agreements. The equity method of accounting is used for the Company's 50% undivided tenant-in-common interest in Industry Distribution Center II. All significant intercompany transactions and accounts have been eliminated in consolidation.

(3) USE OF ESTIMATES

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenues and expenses during the reporting period and to disclose material contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

(4) REAL ESTATE PROPERTIES

EastGroup has one reportable segment – industrial properties. These properties are concentrated in major Sunbelt markets of the United States, primarily in the states of Florida, Texas, Arizona, California and North Carolina, have similar economic characteristics and also meet the other criteria permitting the properties to be aggregated into one reportable segment.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows (including estimated future expenditures necessary to substantially complete the asset) expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset. As of June 30, 2014 and December 31, 2013, the Company determined that no impairment charges on the Company's real estate properties were necessary.

Depreciation of buildings and other improvements is computed using the straight-line method over estimated useful lives of generally 40 years for buildings and 3 to 15 years for improvements. Building improvements are capitalized, while maintenance and repair expenses are charged to expense as incurred. Significant renovations and improvements that improve or extend the useful life of the assets are capitalized. Depreciation expense for continuing and discontinued operations was $14,094,000 and $28,067,000 for the three and six months ended June 30, 2014, respectively, and $13,494,000 and $26,551,000 for the same periods in 2013.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The Company's real estate properties and development at June 30, 2014 and December 31, 2013 were as follows:

	June 30, 2014	December 31, 2013
	(In thousands)	
Real estate properties:		
Land	$274,860	265,871
Buildings and building improvements	1,249,926	1,210,318
Tenant and other improvements	315,702	302,370
Development	184,618	148,767
	2,025,106	1,927,326
Less accumulated depreciation	(576,182)	(550,113)
	$1,448,924	1,377,213

(5) DEVELOPMENT

During the period in which a property is under development, costs associated with development (i.e., land, construction costs, interest expense, property taxes and other direct and indirect costs associated with development) are aggregated into the total capitalized costs of the property. Included in these costs are management's estimates for the portions of internal costs (primarily personnel costs) deemed directly or indirectly related to such development activities. The internal costs are allocated to specific development properties based on construction activity. As the property becomes occupied, depreciation commences on the occupied portion of the building, and costs are capitalized only for the portion of the building that remains vacant. When the property becomes 80% occupied or one year after completion of the shell construction (whichever comes first), capitalization of development costs ceases. The properties are then transferred to real estate properties, and depreciation commences on the entire property (excluding the land).

(6) BUSINESS COMBINATIONS AND ACQUIRED INTANGIBLES

Upon acquisition of real estate properties, the Company applies the principles of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, Business Combinations, which requires that acquisition-related costs be recognized as expenses in the periods in which the costs are incurred and the services are received. The Codification also provides guidance on how to properly determine the allocation of the purchase price among the individual components of both the tangible and intangible assets based on their respective fair values. Goodwill is recorded when the purchase price exceeds the fair value of the assets and liabilities acquired. Factors considered by management in allocating the cost of the properties acquired include an estimate of carrying costs during the expected lease-up periods considering current market conditions and costs to execute similar leases. The allocation to tangible assets (land, building and improvements) is based upon management's determination of the value of the property as if it were vacant using discounted cash flow models. The Company determines whether any financing assumed is above or below market based upon comparison to similar financing terms for similar properties. The cost of the properties acquired may be adjusted based on indebtedness assumed from the seller that is determined to be above or below market rates.

The purchase price is also allocated among the following categories of intangible assets: the above or below market component of in-place leases, the value of in-place leases, and the value of customer relationships. The value allocable to the above or below market component of an acquired in-place lease is determined based upon the present value (using a discount rate reflecting the risks associated with the acquired leases) of the difference between (i) the contractual amounts to be paid pursuant to the lease over its remaining term, and (ii) management's estimate of the amounts that would be paid using fair market rates over the remaining term of the lease. The amounts allocated to above and below market leases are included in Other Assets and Other Liabilities, respectively, on the Consolidated Balance Sheets and are amortized to rental income over the remaining terms of the respective leases. The total amount of intangible assets is further allocated to in-place lease values and customer relationship values based upon management's assessment of their respective values. These intangible assets are included in Other Assets on the Consolidated Balance Sheets and are amortized over the remaining term of the existing lease, or the anticipated life of the customer relationship, as applicable.

Amortization expense for in-place lease intangibles for continuing and discontinued operations was $1,121,000 and $2,333,000 for the three and six months ended June 30, 2014, respectively, and $999,000 and $1,777,000 for the same periods in 2013. Amortization of above and below market leases increased rental income by $89,000 and $176,000 for the three and six months ended June 30, 2014, respectively, and increased rental income by $27,000 for the three months ended June 30, 2013 and decreased rental income by $10,000 for the six months ended June 30, 2013.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

During the six months ended June 30, 2014, EastGroup acquired Ridge Creek Distribution Center III in Charlotte, North Carolina, and Colorado Crossing Distribution Center in Austin, Texas. The Company purchased these properties for a total cost of $41,751,000, of which $37,964,000 was allocated to real estate properties. The Company allocated $7,061,000 of the total purchase price to land using third party land valuations for the Charlotte and Austin markets. The market values are considered to be Level 3 inputs as defined by ASC 820, Fair Value Measurements and Disclosures (see Note 17 for additional information on ASC 820). Intangibles associated with the purchase of real estate were allocated as follows: $4,660,000 to in-place lease intangibles, $4,000 to above market leases (both included in Other Assets on the Consolidated Balance Sheets), and $877,000 to below market leases (included in Other Liabilities on the Consolidated Balance Sheets). These costs are amortized over the remaining lives of the associated leases in place at the time of acquisition.

During the year ended December 31, 2013, the Company acquired Northfield Distribution Center in Dallas, Texas, and Interchange Park II in Charlotte, North Carolina. The Company purchased these properties for a total cost of $72,397,000, of which $65,387,000 was allocated to real estate properties. The Company allocated $13,218,000 of the total purchase price to land using third party land valuations for the Dallas and Charlotte markets. Intangibles associated with the purchase of real estate were allocated as follows: $8,399,000 to in-place lease intangibles, $158,000 to above market leases, and $1,547,000 to below market leases.

EastGroup expensed acquisition-related costs of $160,000 in the three and six months ended June 30, 2014, and expensed $138,000 and $167,000 during the same periods of 2013.

The Company periodically reviews the recoverability of goodwill (at least annually) and the recoverability of other intangibles (on a quarterly basis) for possible impairment. In management’s opinion, no impairment of goodwill and other intangibles existed at June 30, 2014 and December 31, 2013.

(7) REAL ESTATE HELD FOR SALE/DISCONTINUED OPERATIONS

The Company considers a real estate property to be held for sale when it meets the criteria established under ASC 360, Property, Plant and Equipment, including when it is probable that the property will be sold within a year. Real estate properties held for sale are reported at the lower of the carrying amount or fair value less estimated costs to sell and are not depreciated while they are held for sale.

In April 2014, the FASB issued Accounting Standards Update (ASU) 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360), Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, which amends the requirements for reporting discontinued operations. Under ASU 2014-08, a disposal of a component of an entity or a group of components of an entity is required to be reported in discontinued operations if the disposal represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results when the component or group of components meets the criteria to be classified as held for sale or when the component or group of components is disposed of by sale or other than by sale. In addition, this ASU requires additional disclosures about both discontinued operations and the disposal of an individually significant component of an entity that does not qualify for discontinued operations presentation in the financial statements. The Company adopted the provisions of ASU 2014-08 beginning with the period ended March 31, 2014, and has applied the provisions prospectively.

Prior to the adoption of ASU 2014-08, the results of operations for the operating properties sold or held for sale during the reported periods were shown under Discontinued Operations on the Consolidated Statements of Income and Comprehensive Income. Interest expense was not generally allocated to the properties held for sale or whose operations were included under Discontinued Operations unless the mortgage was required to be paid in full upon the sale of the property.

During the first quarter of 2014, EastGroup sold one operating property (58,000 square feet) for $3,600,000 and recognized a gain of $95,000. The results of operations and gain on sale for the property sold during the period are reported under Income from Continuing Operations on the Consolidated Statements of Income and Comprehensive Income. The gain on sale is included in Other.

As of June 30, 2014, the Company owned one operating property, Tampa West Distribution Center VI, that was classified as held for sale on the June 30, 2014 Consolidated Balance Sheet. The 9,000 square foot property was sold in July 2014 for $743,000, generating a gain that will be recognized by the Company in its third fiscal quarter of 2014.

During 2013, the Company sold three operating properties (49,000 square feet) for $3,198,000 and recognized gains of $798,000. The results of operations for the properties sold during 2013 are reported under Discontinued Operations on the Consolidated Statements of Income and Comprehensive Income.

EASTGROUP PROPERTIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The following table presents the components of revenue and expense for the properties sold during 2013.

DISCONTINUED OPERATIONS	Three Months Ended June 30, 2014	2013	Six Months Ended June 30, 2014	2013
	(In thousands)			
Income from real estate operations	$—	83	—	157
Expenses from real estate operations	—	(21)	—	(41)
Property net operating income from discontinued operations	—	62	—	116
Depreciation and amortization	—	(27)		