



## DISCOVERING VALUE WHITNEY TILSON JOHN HEINS

### A Tale of Two Stocks

We have positions in two real estate companies, Howard Hughes Corp. and St. Joe Company, that on the surface appear to be similar. Bill Ackman, of Pershing Square, and Bruce Berkowitz, of Fairholme Fund, both highly successful value investors, chair Hughes and St. Joe, respectively, and have enormous stakes in the companies. Both firms are

developing properties that are potentially valuable but currently generate little cash flow. But that's where the similarities end for us. Hughes (symbol HHC) is one of our largest holdings, and St. Joe (JOE) is among our biggest short positions.

**Undervalued assets.** When General Growth Properties emerged from bankruptcy last November, it did so as two companies: a new General Growth Properties (GGP), which retained all of the best malls, and Howard Hughes, a collection of 34 properties in 18 states that are not generating meaningful cash flows because they are under development or need fixing. We believe the potential for many of Hughes's properties is enormous but isn't reflected in the \$73 share price (prices are through June 3).

Take Summerlin, a 22,500 acre master-planned community in Las Vegas. It contains some 40,000 homes

occupied by about 100,000 residents; nearly 7,000 acres, zoned for both homes and commerce, remain to be sold. The Las Vegas housing market is depressed, so Summerlin was valued last September at \$460 million. But we think the true value is closer to \$1.6 billion. Hughes's market capitalization is only \$2.8 billion.

Another property of note is Ward Centers, a 60-acre site located near Waikiki Beach, in Honolulu. Hawaii officials have approved a plan for a major multi-use oceanfront development on the land. We think Ward Centers is worth \$800 million to \$1.6 billion.

Investing in Hughes at this stage is largely a bet on its top leaders. Given their superb record in real estate, that's a bet we're comfortable making. Another confidence builder: Key officials have invested \$19 million of their own money to buy long-term warrants on the stock, thereby aligning

their interests with those of shareholders.

**Overpriced.** St. Joe owns 574,000 acres of mostly raw timberland, concentrated in northwest Florida. Timberland is easy to value, so the debate over St. Joe centers on the worth of its residential and commercial properties. Led by Berkowitz, St. Joe bulls believe those developments have enormous potential value. They contend that the Northwest Florida Beaches International Airport, which opened in May 2010, will unleash much of that value.

ments on the ocean in popular areas. The company sold most of the lots in those tracts at good prices. But then St. Joe went crazy, spending well over \$1 billion on developments that are neither close to the ocean nor the airport.

Because of their less desirable locations and the housing bust, these developments today look like ghost towns, and, in our view, they are likely to remain so for years to come. They're not worth a fraction of what St. Joe spent to build them, yet the firm hasn't meaningfully marked down

**“The potential for Howard Hughes's properties is enormous but isn't reflected in the price.”**

We're skeptical. To test our thesis, we recently flew to northern Florida to see the airport and a few St. Joe properties for ourselves. What we saw reinforced our case against St. Joe's stock. The area contains pretty beaches, but the region is quite poor and not well developed. It doesn't hold a candle to other tourist destinations in Florida.

In the early years of the housing bubble, St. Joe built a small number of develop-

their values, which it will eventually have to do. We're even more skeptical of the possibility of significant industrial or commercial developments on St. Joe's land.

We think there is little value to St. Joe beyond its timberland, which is probably worth \$7 to \$10 per share. At \$20, St. Joe is clearly overvalued, and so we are short the stock. ■

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