

HIGHWOODS PROPERTIES INC

FORM 10-Q (Quarterly Report)

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Industry	Real Estate Operations
Sector	Services
Fiscal Year	12/31

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 quarterly period ended September 30, 1997

Commission file number: 001-13100

HIGHWOODS PROPERTIES, INC.

(Exact name of registrant as specified in its charter)

MARYLAND

(State or other jurisdiction of
incorporation or organization)

56-1871668

(I.R.S. Employer
Identification Number)

3100 SMOKETREE COURT, SUITE 600, RALEIGH, N.C.

(Address of principal executive office)

27604

(Zip Code)

Registrant's telephone number, including area code:

(919) 872-4924

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 ☒ No ☐ The Company has only one class of common stock, par value \$.01 per share, with 46,697,501 shares outstanding as of November 7, 1997.

HIGHWOODS PROPERTIES, INC.
QUARTERLY REPORT FOR THE PERIOD ENDED SEPTEMBER 30, 1997
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PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The information furnished in the accompanying balance sheets, statements of operations and statements of cash flows reflect all adjustments that are, in the opinion of management, necessary for a fair presentation of the aforementioned financial statements for the interim period. The aforementioned financial statements should be read in conjunction with the notes to consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations and the 1996 Annual Report on Form 10-K of Highwoods Properties, Inc. (the "Company").

HIGHWOODS PROPERTIES, INC.
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS EXCEPT PER SHARE AMOUNTS)

	SEPTEMBER 30, 1997 (UNAUDITED)	DECEMBER 31, 1996
ASSETS		
Real estate assets, at cost:		
Land and improvements.....	\$ 235,473	\$ 219,539
Buildings and tenant improvements.....	1,452,381	1,152,990
Development in process.....	59,071	28,858
Land held for development.....	53,290	17,551
Furniture, fixtures and equipment.....	3,010	2,096
	1,803,225	1,421,034
Less -- accumulated depreciation	(72,319)	(43,160)
Net real estate assets.....	1,730,906	1,377,874
Cash and cash equivalents.....	175,087	11,070
Restricted cash.....	9,143	8,539
Accounts receivable.....	11,831	9,039
Advances to subsidiaries.....	4,967	2,406
Accrued straight line rents receivable.....	10,024	6,185
Other assets:		
Deferred leasing costs.....	16,750	9,601
Deferred financing costs.....	21,940	21,789
Prepaid expenses and other.....	11,029	3,901
	49,719	35,291
Less -- accumulated amortization.....	(11,499)	(6,964)
	38,220	28,327
	\$1,980,178	\$ 1,443,440
LIABILITIES AND STOCKHOLDERS' EQUITY		
Mortgages and notes payable.....	\$ 649,188	\$ 555,876
Accounts payable, accrued expenses and other liabilities.....	41,565	27,600
Total liabilities.....	690,753	583,476
Minority interest.....	174,913	89,617
Stockholders' equity:		
Preferred stock \$.01 par value; 10,000,000 authorized		
8 5/8% Series A Cumulative Redeemable Preferred Shares		
(liquidation preference of \$1,000 per share), 125,000 shares issued and		
outstanding at September 30, 1997.....	125,000	--
8% Series B Cumulative Redeemable Preferred Shares		
(liquidation preference \$25 per share),		
6,900,000 shares issued and outstanding at September 30, 1997.....	172,500	--
Common stock, \$.01 par value, authorized 100,000,000 shares; issued and		
outstanding 37,948,435 at September 30, 1997 and 35,636,155 at December		
31, 1996.....	379	356
Additional paid-in capital.....	839,912	780,562
Distributions in excess of net income.....	(23,279)	(10,571)
Total stockholders' equity.....	1,114,512	770,347
	\$1,980,178	\$ 1,443,440

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

HIGHWOODS PROPERTIES, INC.
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED AND IN THOUSANDS EXCEPT PER SHARE AMOUNTS)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1996	1997	1996
REVENUE:				
Rental property.....	\$61,768	\$33,076	\$177,246	\$83,366
Interest and other income.....	1,887	3,253	5,968	4,400
	63,655	36,329	183,214	87,766
OPERATING EXPENSES:				
Rental property.....	17,407	9,015	48,995	22,210
Depreciation and amortization.....	11,151	5,459	31,051	13,357
Interest expense:				
Contractual.....	10,566	5,539	33,082	13,786
Amortization of deferred financing costs.....	567	461	1,689	1,288
	11,133	6,000	34,771	15,074
General and administrative.....	2,410	1,632	6,694	3,766
Income before minority interest and extraordinary item.....	21,554	14,223	61,703	33,359
MINORITY INTEREST.....	(3,448)	(1,881)	(9,872)	(5,205)
Income before extraordinary item.....	18,106	12,342	51,831	28,154
EXTRAORDINARY ITEM -- LOSS ON EARLY EXTINGUISHMENT OF DEBT.....	(1,328)	(2,140)	(4,665)	(2,140)
Net income.....	16,778	10,202	47,166	\$26,014
Preferred Dividends.....	(2,870)	--	(6,972)	--
Net income available for common stockholders.....	\$13,908	\$10,202	\$ 40,194	\$26,014
NET INCOME (LOSS) PER COMMON SHARE:				
Income before extraordinary item.....	\$ 0.42	\$ 0.39	\$ 1.25	\$ 1.19
Extraordinary item -- loss on early extinguishment of debt.....	\$ (0.04)	\$ (0.07)	\$ (0.13)	\$ (0.09)
Net income.....	\$ 0.38	\$ 0.32	\$ 1.12	\$ 1.10
Weighted average shares outstanding.....	36,582	31,763	35,777	23,730

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

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

	NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1996
OPERATING ACTIVITIES:		
Net income.....	\$ 47,166	\$ 26,014
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization.....	32,520	14,645
Minority interest in income.....	8,979	4,858
Loss on early extinguishment of debt.....	5,534	2,432
Changes in operating assets and liabilities.....	2,338	(59)
Net cash provided by operating activities.....	96,537	47,890
INVESTING ACTIVITIES:		
Additions to real estate assets.....	(149,458)	(113,250)
Proceeds from disposition of real estate assets.....	--	900
Cash from contributed net assets.....	--	20,711
Cash paid in exchange for partnership net assets.....	(5,314)	(322,276)
Other.....	(15,005)	(2,755)
Net cash used in investing activities.....	(169,777)	(416,670)
FINANCING ACTIVITIES:		
Distributions paid.....	(57,770)	(37,938)
Payment of preferred dividends.....	(5,959)	--
Repayment of mortgages and notes payable.....	(223,388)	(184,858)
Payment of prepayment penalties.....	(5,534)	(1,184)
Borrowings on mortgages and notes payable.....	183,000	307,500
Net proceeds from the sale of common stock.....	58,463	298,804
Net proceeds from sale of 8 5/8% Series A Cumulative Redeemable Preferred Shares.....	121,804	--
Net proceeds from sale of 8% Series B Cumulative Redeemable Preferred Shares...	167,066	--
Payment of deferred financing costs.....	(425)	(1,077)
Net cash provided by financing activities.....	237,257	381,247
Net increase in cash and cash equivalents.....	164,017	12,467
Cash and cash equivalents at beginning of the period.....	11,070	6,838
Cash and cash equivalents at end of the period.....	\$ 175,087	\$ 19,305
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest.....	\$ 7,763	\$ 12,816

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

HIGHWOODS PROPERTIES, INC.
CONSOLIDATED STATEMENT OF CASH FLOWS
(UNAUDITED AND IN THOUSANDS)

SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES

The following summarizes the net assets contributed by the unit holders of the Highwoods/Forsyth Limited Partnership (the "Operating Partnership") or acquired subject to mortgage notes payable:

	NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1996
ASSETS:		
Rental property and equipment, net.....	\$226,051	\$614,329
Restricted cash.....	--	11,476
Deferred financing costs, net.....	--	3,871
Accounts receivable and other.....	--	1,653
Total assets.....	\$226,051	\$631,329
LIABILITIES:		
Mortgages and notes payable assumed.....	\$133,736	\$292,356
Accounts payable, accrued expenses and other liabilities.....	--	19,142
Total liabilities.....	\$133,736	\$311,498
Net assets.....	\$ 92,315	\$319,831

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

HIGHWOODS PROPERTIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 1997

(UNAUDITED)

1. BASIS OF PRESENTATION The consolidated financial statements include the accounts of Highwoods Properties, Inc. (the "Company"), Highwoods/Forsyth Limited Partnership (the "Operating Partnership") and the following subsidiaries:

Highwoods/Florida GP Corp.

Highwoods Realty GP Corp.

Highwoods/Tennessee Properties, Inc.

Highwoods/Florida Holdings GP, L.P.

AP-GP Southeast Portfolio Partners, L.P. Highwoods/Tennessee Holdings GP, L.P.

Highwoods/Tennessee Holdings, L.P.

AP Southeast Portfolio Partners, L.P.

Highwoods/Florida Holdings, L.P.

Highwoods Services, Inc.

Southeast Realty Options Corp.

The Company's investment in Highwoods Services, Inc. (the "Service Company") is accounted for using the equity method of accounting. All significant intercompany balances and transactions have been eliminated in the consolidated financial statements.

The extraordinary loss represents the write-off of loan origination fees and prepayment penalties paid on the early extinguishment of debt.

The Company has elected and expects to continue to qualify as a real estate investment trust ("REIT") under Section 856 through 860 of the Internal Revenue Code of 1986, as amended.

In February 1997, the Financial Accounting Standards Board issued Statement No. 128, EARNINGS PER SHARE, which is required to be adopted on December 31, 1997. At that time, the Company will be required to change the method currently used to compute earnings per share and to restate all prior periods. Under the new requirements for calculating primary earnings per share, the dilutive effect of stock options will be excluded. The impact of Statement 128 on the calculation of primary and fully diluted earnings per share for these quarters is not material. Minority interest in the Company represents the limited partnership interests ("Common Units") owned by various individuals and entities and not the Company in the Operating Partnership, the entity that owns substantially all of the Company's properties and through which the Company, as the sole general partner, conducts substantially all of its operations. Per share information is calculated using the weighted average number of shares outstanding (including common share equivalents).

The accompanying financial information has not been audited, but in the opinion of management, all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of the financial position, results of operations and cash flows of the Company have been made. For further information, refer to the financial statements and notes thereto included in the Company's 1996 Annual Report on Form 10-K.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with all of the financial statements appearing elsewhere in the report. The following discussion is based primarily on the consolidated financial statements of Highwoods Properties, Inc.

RESULTS OF OPERATIONS

THREE MONTHS ENDED SEPTEMBER 30, 1997

Revenues from rental operations increased \$28.7 million, or 87%, from \$33.1 million for the three months ended September 30, 1996 to \$61.8 million for the comparable period in 1997. The increase is primarily a result of the acquisition of 6.4 million square feet of office and industrial properties and the completion of 763,000 square feet of development activity during latter part of the third quarter and the fourth quarter of 1996 and the addition of 3.2 million square feet in the first quarter of 1997 from the acquisition of the Anderson Properties and Century Center portfolios. The Company's portfolio increased from 16.7 million square feet at September 30, 1996 to 21.9 million square feet at September 30, 1997. Same property revenues, which are the revenues of the 204 in-service properties owned on July 1, 1996, increased 3% for the three months ended September 30, 1997, compared to the same three months of 1996.

During the three months ended September 30, 1997, 175 leases representing 737,000 square feet of office and industrial space commenced at an average rate per square foot which was 8.2% higher than the average rate per square foot on the expired leases.

Interest and other income decreased \$1.4 million from \$3.3 million for the three months ended September 30, 1996 to \$1.9 million for the comparable period in 1997. The prior year amount was abnormally high as a result of the \$299 million in cash available for investment raised from the sale of 11.8 million shares of Common Stock.

Rental operating expenses increased \$8.4 million, or 93%, from \$9.0 million for the three months ended September 30, 1996 to \$17.4 million for the comparable period in 1997. The increase is a result of the addition of 10.2 million square feet through a combination of acquisitions and developments during the latter part of the third quarter and the fourth quarter of 1996 and the first two quarters of 1997. Rental operating expenses as a percentage of related revenues increased from 27.3% for the three months ended September 30, 1996 to 28.2% for the comparable period in 1997. This increase is a result of an increase in the percentage of office properties in the portfolio, which have fewer triple net lease pass throughs.

Depreciation and amortization for the three months ended September 30, 1997 and 1996 was \$11.2 million and \$5.5 million, respectively. The increase of \$5.7 million, or 104%, is due to an increase in depreciable assets over the prior year. The \$541 million acquisition of Crocker Realty Trust, which closed at the end of the third quarter of 1996, had very little impact on the depreciation expense in the prior year. Interest expense increased \$5.1 million, or 85%, from \$6.0 million for the three months ended September 30, 1996 to \$11.1 million for the comparable period in 1997. The increase is attributable to the increase in the outstanding debt for the entire quarter. The closing of the Crocker acquisition at the end of the third quarter of 1996 had very little impact on the interest expense in the prior year. Interest expense for the three months ended September 30, 1997 and 1996 included \$567,000 and \$461,000, respectively, of amortization of non-cash deferred financing costs and the costs related to the Company's interest rate protection agreements. General and administrative expenses decreased from 4.9% of rental revenue for the three months ended September 30, 1996 to 3.9% for the comparable period in 1997. The decrease is attributable to the realization of the economies of scale related to the acquisition of the 5.7 million-square foot Crocker portfolio, which was completed in September 1996.

Net income before minority interest and extraordinary item equaled \$21.6 million and \$14.2 million for the three-month periods ended September 30, 1997 and 1996, respectively. The Company's net income allocated to minority interest totaled \$3.4 million and \$1.9 million for the three-month periods ended September 30, 1997 and 1996, respectively. The Company accrued \$2.9 million in dividends in the third quarter of 1997 for the 125,000 shares of preferred stock that the Company issued in February and September 1997 (see " -- Liquidity and Capital Resources" below).

NINE MONTHS ENDED SEPTEMBER 30, 1997

Revenue from rental operations increased \$93.8 million or 112%, from \$83.4 million for the nine months of 1996 to \$177.2 million for the nine months of 1997. The increase is a result of the Company's acquisition and development activity in 1996 and 1997. In total, 103 office and industrial properties encompassing 8.2 million square feet were added in 1996 and 77 properties encompassing 4.8 million square feet were added in the first nine months of 1997.

During the nine months ended September 30, 1997, 547 leases representing 3,253,000 square feet of office and industrial space commenced at an average rate per square foot 7.4% higher than the average rate per square foot on the expired leases.

Interest and other income increased \$1.6 million from \$4.4 million in 1996 to \$6.0 million in 1997. The increase is related to the receipt of \$1.6 million in lease termination fees and other miscellaneous property income in the first nine months of 1997 and a full nine months of third-party management fees derived from the management contracts assumed in the merger with Eakin & Smith, Inc. on April 1, 1996.

Rental operating expenses increased \$26.8 million, or 121%, from \$22.2 million in 1996 to \$49.0 million in 1997. Rental expenses as a percentage of related rental revenues increased from 26.6% in 1996 to 27.6% in 1997. The increase is a result of an increase in the percentage of office properties in the portfolio, which have fewer triple net lease pass throughs.

Depreciation and amortization for the nine months ended September 30, 1997, and 1996 was \$31.1 million and \$13.4 million, respectively. The increase of \$17.7 million, or 132%, is attributable to an increase in depreciable assets over the prior year. The \$541 million acquisition of Crocker Realty Trust, which closed at the end of the third quarter of 1996, had very little impact on the depreciation expenses in 1996. Interest expense increased \$19.7 million or 130%, from \$15.1 million in 1996 to \$34.8 million in 1997. The increase is attributable to the large increase in the outstanding debt for the entire nine-month period. The closing of the Crocker acquisition at the end of the third quarter of 1996 had very little impact on the interest expense in the prior year. Interest expense for the nine months ended September 30, 1997, and 1996 included \$1.7 million and \$1.3 million, respectively, of amortization of non-cash deferred financing costs and of the costs related to the Company's interest rate protection agreement. General and administrative expenses decreased from 4.5% of total rental revenue in 1996 to 3.8% in 1997. This decrease is attributable to the realization of the economies of scale related to the acquisition of the 5.7 million-square foot Crocker portfolio, which was completed in September 1996.

Net income before minority interest and extraordinary item equaled \$61.7 million and \$33.4 million for the nine-month periods ended September 30, 1997, and 1996, respectively. The Operating Partnership's net income allocated to the minority interest totaled \$9.9 million and \$5.2 for 1997 and 1996, respectively. The Company incurred an extraordinary loss in the first quarter of 1997 of \$4.7 million related to the early extinguishment of debt. The Company also recorded \$7.0 million in preferred dividends for the nine months ended September 30, 1997.

LIQUIDITY AND CAPITAL RESOURCES

For the nine months ended September 30, 1997, cash provided by operating activities increased by \$48.6 million, or 101%, to \$96.5 million, as compared to \$47.9 million for the same period in 1996. The increase is primarily due to the increase in net income resulting from the Company's property acquisitions in 1996 and 1997. Cash used for investing activities decreased by \$246.9 million, or 59%, to \$169.8 million for the first nine months of 1997, as compared to \$416.7 million for the same 1996 period. The decrease is attributable to the Company's \$547 million acquisition of Crocker Realty Trust in the prior year. Cash provided by financing activities decreased by \$143.9, or 38%, to \$237.3 million for the first nine months of 1997, as compared to \$381.2 million for the same period in 1996. During the first nine months of 1997, cash provided by financing activities consisted, primarily, of \$288.9 million in net proceeds from the sale of preferred stock and the sale of \$100 million of Exercisable Put Option Securities (see below), which were offset by net payments of \$118.4 million to reduce existing indebtedness and \$105 million to pay off the assumed indebtedness associated with the acquisition of the Century Center and Anderson Properties portfolios. Additionally, payments of distributions increased by \$19.9 million to \$57.8 million for the first nine

months of 1997, as compared with \$37.9 million for the same period in 1996. The increase is due to the greater number of shares outstanding and a 7% increase in the distribution rate.

On February 12, 1997, the Company issued 125,000 shares of 8 5/8% Series A Cumulative Redeemable Preferred Shares (the "Series A Preferred Shares") for net proceeds of \$121.8 million. The Series A Preferred Shares have a liquidation preference of \$1,000 per share, are not redeemable prior to February 2027, are not subject to any sinking fund or mandatory redemption and are not convertible into any other securities of the Company.

Effective May 27, 1997, the Company's syndicate of lenders lowered the interest rate to 100 basis points over LIBOR (from the previous rate of 135 basis points over LIBOR) on the Company's \$280 million revolving loan.

On June 24, 1997, a trust formed by the Operating Partnership sold \$100 million of Exercisable Put Option Securities ("X-POSSM"), which represent fractional undivided beneficial interests in the trust. The assets of the trust consist of, among other things, \$100 million of Exercisable Put Option Notes due June 15, 2011 issued by the Operating Partnership (the "Put Option Notes"). The X-POSSM bear a coupon interest rate of 7.19% and mature on June 15, 2004, representing an effective borrowing cost of 7.09%, net of a related put option and certain interest rate protection agreement costs. Under certain circumstances, the Put Option Notes could also become subject to early maturity on June 15, 2004.

On August 28, 1997, the Company entered into two

transactions with affiliates of Union Bank of Switzerland. In one transaction, the Company sold 1,800,000 shares of Common Stock to UBS Limited for net proceeds of approximately \$57 million. In the other transaction, the Company entered into a forward share purchase agreement (the "Forward Contract") with Union Bank of Switzerland, London Branch ("UBS/LB"). The Forward Contract generally provides that if the price of a share of Common Stock is above \$32.14 (the "Forward Price") on August 28, 1998, UBS/LB will return the difference (in shares of Common Stock) to the Company. Similarly, if the price of a share of Common Stock on August 28, 1998 is less than the Forward Price, the Company will pay the difference to UBS/LB in cash or shares of Common Stock, at the Company's option.

On September 25, 1997 the Company issued 6.9 million shares of 8% Series B Cumulative Redeemable Preferred Shares (the "Series B Preferred Shares") for net proceeds of \$167 million. The Series B Preferred Shares have a liquidation preference of \$25 per share, are not redeemable prior to September 2002, are not subject to any sinking fund or mandatory redemption and are not convertible into any other securities of the Company.

The Company's total indebtedness at September 30, 1997, totaled \$649.2 million and was comprised of \$258.4 million of secured indebtedness with an average rate of 8.1% and \$390.8 million of unsecured indebtedness with an average rate of 6.9%. All of the mortgage and notes payable outstanding at September 30, 1997 were either fixed rate obligations or variable rate obligations covered by interest rate protection agreements.

Based on the Company's total market capitalization of \$2.5 billion at September 30, 1997, (at the September 30, 1997 stock price of \$35.38 and assuming the redemption for shares of Common Stock of the 7,084,000 Common Units of minority interest in the Operating Partnership), the Company's debt represented approximately 26% of its total market capitalization.

To protect the Company from increases in interest expense due to changes in the variable rate, the Company: (i) purchased an interest rate collar limiting its exposure to an increase in interest rates (one-month LIBOR plus 100 basis points) to 7.25% with respect to \$80 million of the Company's \$280 million unsecured revolving loan (the "Revolving Loan"), under which the Company had \$59 million outstanding at September 30, 1997, and (ii) entered into interest rate swaps that limit its exposure to an increase in the interest rates to 7.15% in connection with the \$22 million of variable rate mortgages. The interest rate on all such variable rate debt is adjusted at monthly intervals, subject to the Company's interest rate protection program. No payments were received from the counterparties under the interest rate protection agreements for the three months ended September 30, 1997 and 1996. The Company is exposed to certain losses in the event of non-performance by the counterparties under the cap and swap arrangements. The counterparties are major financial institutions and are expected to perform fully under the agreements. However, if they

were to default on their obligations under the arrangements, the Company could be required to pay the full rate under the Revolving Loan and the variable rate mortgages, even if such rate were in excess of the rate in the cap and swap agreements. In addition, the Company may incur other variable rate indebtedness in the future. Increases in interest rates on its indebtedness could increase the Company's interest expense and could adversely affect the Company's cash flow.

Historically, rental revenue has been the principal source of funds to pay operating expenses, debt service and capital expenditures, excluding non-recurring capital expenditures. In addition, construction management, maintenance, leasing and management fees have provided sources of cash flow. The Company presently has no plans for major capital improvements to the existing properties, other than normal recurring non-revenue enhancing expenditures. The Company expects to meet its short-term liquidity requirements generally through its working capital and net cash provided by operating activities along with the Revolving Loan. The Company expects to meet certain of its financing requirements through long-term secured and unsecured borrowings and the issuance of debt securities or additional equity securities of the Company and Operating Partnership. In addition, the Company anticipates utilizing the Revolving Loan primarily to fund construction and development activities. The Company does not intend to reserve funds to retire existing mortgage indebtedness or indebtedness under the Revolving Loan upon maturity. Instead, the Company will seek to refinance such debt at maturity or retire such debt through the issuance of equity or debt securities. The Company anticipates that its available cash and cash equivalents and cash flows from operating activities, together with cash available from borrowings and other sources, will be adequate to meet the capital and liquidity needs of the Company in both the short and long-term. However, if these sources of funds are insufficient or unavailable, the Company's ability to make the expected distributions discussed below may be adversely affected.

In order to qualify as a REIT for Federal income tax purposes, the Company is required to make distributions to its stockholders of at least 95% of REIT taxable income. The Company expects to use its cash flow from operating activities for distributions to stockholders and for payment of recurring, non-incremental revenue-generating expenditures. The Company intends to invest amounts accumulated for distribution in short-term investments. The following factors will affect cash flows from operating activities and, accordingly, influence the decisions of the Board of Directors regarding distributions: (i) debt service requirements after taking into account the repayment and restructuring of certain indebtedness; (ii) scheduled increases in base rents of existing leases; (iii) changes in rents attributable to the renewal of existing leases or replacement leases; (iv) changes in occupancy rates at existing properties and procurement of leases for newly acquired or developed properties; and (v) operating expenses and capital replacement needs.

RECENT DEVELOPMENTS

OCTOBER 1997 OFFERING. On October 1, 1997, the Company sold 7,500,000 shares of Common Stock in an underwritten public offering for net proceeds of approximately \$249 million. The underwriters exercised a portion of their over-allotment option for 1,000,000 shares of Common Stock on October 6, 1997, raising additional net proceeds of \$33.2 million.

ACP TRANSACTION. On October 1 and October 7, 1997, the Company closed substantially all of its previously announced business combination with Associated Capital Properties, Inc. ("ACP") and related portfolio acquisition (the "ACP Transaction"). The ACP Transaction includes the acquisition of a portfolio of 84 office properties encompassing 6.5 million rentable square feet (the "ACP Properties") and approximately 50 acres of land for development in six markets in Florida.

The ACP Properties were 89% leased as of September 30, 1997. The ACP Properties include 82 office properties (78 of which are suburban) in Florida's four major markets, Orlando, Tampa, Jacksonville and South Florida, one 245,000-square foot suburban office property in Tallahassee and one 51,831-square foot office property in Ft. Myers. The ACP Properties include seven properties that ACP had under contract to purchase.

Under the terms of the agreements relating to the ACP Transaction, the Company merged with Associated Capital Properties, Inc. and acquired the ownership interest in the entities that own the ACP Properties for an aggregate purchase price of \$617 million. The cost of the ACP Transaction consists of the issuance of

2,955,110 Common Units (valued at \$32.50 per Common Unit), the assumption of \$481 million of mortgage debt (\$391 million of which has been paid off by the Company), the issuance of 117,265 shares of Common Stock (valued at \$32.50 per share), a capital expenditure reserve of \$11 million and a cash payment of \$25 million. Also in connection with the ACP Transaction, the Company issued to certain affiliates of ACP warrants to purchase 1,479,290 shares of the Common Stock at \$32.50 per share exercisable after October 1, 2002.

FUNDS FROM OPERATIONS AND CASH AVAILABLE FOR DISTRIBUTIONS The Company considers Funds from Operations ("FFO") to be a useful financial performance measure of its operating performance because, together with net income and cash flows, FFO provides investors with an additional basis to evaluate its ability to incur and service debt and to fund acquisitions and other capital expenditures. FFO does not represent net income or cash flows from operations as defined by GAAP, and FFO should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a measure of liquidity. FFO does not measure whether cash flow is sufficient to fund all of the Company's cash needs including principal amortization, capital improvements and distributions to stockholders. FFO does not represent cash flows from operating, investing or financing activities as defined by GAAP. Further, FFO as disclosed by other REITs may not be comparable to the Company's calculation of FFO, as described below.

FFO is defined as net income (computed in accordance with generally accepted accounting principles) excluding gains (or losses) from debt restructuring and sales of property, plus depreciation of real estate assets, and after adjustments for unconsolidated partnerships and joint ventures. In March 1995, the National Association of Real Estate Investment Trusts ("NAREIT") issued a clarification of the definition of FFO. The clarification provides that amortization of deferred financing costs and depreciation of non-real estate assets are no longer to be added back to net income in arriving at FFO. Cash available for distribution is defined as funds from operations reduced by non-revenue enhancing capital expenditures for building improvements and tenant improvements and lease commissions related to second generation space.

Funds from operations and cash available for distribution for the three and nine months ended September 30, 1997 and 1996 are summarized in the following table (in thousands):

	THREE MONTHS ENDED SEPTEMBER 30, 1997		NINE MONTHS ENDED SEPTEMBER 30, 1996	
FUNDS FROM OPERATIONS:				
Income before minority interest and extraordinary item.....	\$21,554	\$14,223	\$61,703	\$33,359
Add (deduct):				
Dividends to preferred shareholders.....	(2,870)	--	(6,972)	--
Depreciation and amortization.....	11,151	5,459	31,051	13,357
Minority interest in Crocker's depreciation.....	--	(117)	--	(117)
Third-party service company cash flow.....	--	75	--	330
FUNDS FROM OPERATIONS BEFORE MINORITY INTEREST.....	29,835	19,640	85,782	46,929
CASH AVAILABLE FOR DISTRIBUTION:				
Add (deduct):				
Rental income from straight-line rents.....	(1,347)	(837)	(3,822)	(1,752)
Amortization of deferred financing costs.....	567	461	1,689	1,288
Non-incremental revenue generating capital expenditures (1):				
Building improvements paid.....	(933)	(818)	(2,941)	(2,018)
Second generation tenant improvements paid.....	(2,063)	(864)	(5,510)	(2,172)
Second generation lease commissions paid.....	(1,201)	(477)	(3,535)	(1,056)
CASH AVAILABLE FOR DISTRIBUTION.....	\$24,858	\$17,105	\$71,663	\$41,219
Weighted average shares/Common Units outstanding (2).....	43,550	35,895	42,686	27,748
DIVIDEND PAYOUT RATIO:				
Funds from operations.....	74.4%	87.7%	73.1%	81.6%
Cash available for distribution.....	89.3%	100.7%	87.6%	92.9%

(1) Amounts represent cash expenditures.

(2) Assumes redemption of Common Units for shares of Common Stock. Minority interest Common Unit holders and the stockholders of the Company share equally on a per share and per Common Unit basis; therefore, the resultant per share information is unaffected by the conversion. On November 4, 1997, the Company's Board of Directors declared a dividend of \$.51 per share (\$2.04 on an annualized basis) payable on November 21, 1997 to stockholders of record on November 14, 1997.

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS This Report contains forward-looking statements within the meaning of

Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These statements are identified by words such as "expect," "anticipate," "should" and words of similar import. Forward-looking statements are inherently subject to risks and uncertainties, many of which cannot be predicted with accuracy and some of which might not even be anticipated. Future events and actual results, financial and otherwise, may differ materially from the results discussed in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 1996.

PROPERTY INFORMATION

The following table sets forth certain information with respect to the Company's properties as of September 30, 1997:

	RENTABLE SQUARE FEET	NUMBER OF PROPERTIES	PERCENT LEASED/ PRE-LEASED
IN-SERVICE:			
Office.....	15,022,000	230	94%
Industrial.....	6,882,000	139	92%
Total.....	21,904,000	369	94%
UNDER DEVELOPMENT:			
Office.....	2,259,000	24	39%
Industrial.....	585,000	7	7%
Total.....	2,844,000	31	33%
TOTAL:			
Office.....	17,281,000	254	
Industrial.....	7,467,000	146	
Total.....	24,748,000	400	

The following table sets forth certain information with respect to the Company's properties under development as of September 30, 1997:

NAME	LOCATION	SQUARE FOOTAGE	BUDGETED COST	COST AT 9/30/97	PRE-LEASING PERCENTAGE*	ESTIMATED COMPLETION
OFFICE:						
Ridgefield III	Asheville	57,000	\$ 5,485	\$ 876	0%	2Q98
2400 Century Center	Atlanta	135,000	16,180	1,239	0	2Q98
10 Glenlake	Atlanta	254,000	35,135	2,589	0	4Q98
Patewood VI	Greenville	107,000	11,360	2,716	0	2Q98
Colonnade	Memphis	89,000	9,400	3,213	63	2Q98
Southwind III	Memphis	69,000	6,970	3,888	100	4Q97
Southwind C	Memphis	74,000	7,657	1,354	34	4Q98
Harpeth V	Nashville	65,000	6,900	1,712	27	1Q98
Lakeview Ridge II	Nashville	61,000	6,000	1,573	35	1Q98
Southpointe	Nashville	104,000	10,878	2,381	0	2Q98
Air Park Center One	Piedmont Triad	95,000	9,450	--	0	3Q98
R F Micro Devices	Piedmont Triad	49,000	8,420	6,658	100	4Q97
RMIC	Piedmont Triad	90,000	7,650	2,281	100	2Q98
Clintrials	Research Triangle	178,000	21,490	7,214	100	2Q98
Situs II	Research Triangle	59,000	5,857	860	0	2Q98
Highwoods Centre	Research Triangle	76,000	8,327	189	0	3Q98
Overlook	Research Triangle	97,000	10,307	522	0	4Q98
Red Oak	Research Triangle	65,000	6,394	513	0	3Q98
Rexwoods V	Research Triangle	60,000	7,444	3,281	30	4Q97
Markel-American	Richmond	106,000	10,650	1,732	48	2Q98
Highwoods V	Richmond	67,000	6,620	1,096	100	2Q98
Grove Park	Richmond	61,000	5,930	3,445	10	4Q97
Intermedia (Sabal) Phase I	Tampa	121,000	12,500	532	100	4Q98
Intermedia (Sabal) Phase II	Tampa	120,000	13,000	532	100	1Q00
TOTAL OR WEIGHTED AVERAGE		2,259,000	\$ 250,004	\$50,396	39%	
INDUSTRIAL:						
Chastain II & III	Atlanta	122,000	\$ 4,360	\$ 1,179	0%	3Q98
Newpoint	Atlanta	119,000	4,660	3,038	0	4Q97
Tradeport 1	Atlanta	87,000	3,070	785	0	1Q98
Tradeport 2	Atlanta	87,000	3,070	785	0	1Q98
Airport Center II	Richmond	70,000	3,197	997	0	4Q97
Air Park South	Piedmont Triad	100,000	2,929	273	40	1Q98
TOTAL OR WEIGHTED AVERAGE		585,00	\$ 21,286	\$ 7,057	7%	
Total or Weighted Average		2,844,000	\$ 271,290	\$57,453	33%	
TOTALS BY ESTIMATED COMPLETION DATE						
Fourth Quarter 1997		428,000	\$ 36,621	\$21,307	33%	
First Quarter 1998		400,000	21,969	5,128	20	
Second Quarter 1998		992,000	105,570	23,608	45	
Third Quarter 1998		358,000	28,531	1,881	0	
Fourth Quarter 1998		546,000	65,599	4,997	27	
First Quarter 2000		120,000	13,000	532	100	
Total or Weighted Average		2,844,000	\$ 271,290	\$57,453	33%	

*Includes letters of intent

The following tables set forth certain information about the Company's leasing activities for the three and nine months ended September 30, 1997.

	OFFICE		INDUSTRIAL	
	THREE MONTHS ENDED SEPTEMBER 30, 1997	NINE MONTHS ENDED SEPTEMBER 30, 1997	THREE MONTHS ENDED SEPTEMBER 30, 1997	NINE MONTHS ENDED SEPTEMBER 30, 1997
NET EFFECTIVE RENTS RELATED TO RE-LEASED SPACE:				
Number of lease transactions (signed leases)	111	362	64	185
Rentable square footage leased	374,084	1,759,244	363,408	1,493,806
Average per rentable square foot over the lease term:				
Base rent	\$ 16.20	\$ 16.10	\$ 7.13	\$ 5.69
Tenant improvements	(1.21)	(1.02)	(0.35)	(0.24)
Leasing commissions	(0.35)	(0.43)	(0.17)	(0.15)
Rent concessions	(0.01)	(0.01)	(0.02)	(0.01)
EFFECTIVE RENT	\$ 14.63	\$ 14.64	\$ 6.59	\$ 5.29
Expense stop	(3.87)	(3.88)	(0.25)	(0.25)
EQUIVALENT EFFECTIVE NET RENT	\$ 10.76	\$ 10.76	\$ 6.34	\$ 5.04
Average term in years	4	4	4	4
CAPITAL EXPENDITURES RELATED TO RE-LEASED SPACE:				
TENANT IMPROVEMENTS:				
Total dollars committed under signed leases	\$ 1,779,700	\$ 7,656,511	\$ 454,630	\$ 1,297,867
Rentable square feet	374,084	1,759,244	363,408	1,493,806
Per rentable square foot	\$ 4.76	\$ 4.35	\$ 1.25	\$ 0.87
LEASING COMMISSIONS:				
Total dollars committed under signed leases	\$ 514,998	\$ 3,207,468	\$ 218,614	\$ 799,637
Rentable square feet	374,084	1,759,244	363,408	1,493,806
Per rentable square foot	\$ 1.38	\$ 1.82	\$ 0.60	\$ 0.54
TOTAL:				
Total dollars committed under signed leases	\$ 2,294,698	\$10,863,979	\$ 673,244	\$ 2,097,504
Rentable square feet	374,084	1,759,244	363,408	1,493,806
Per rentable square foot	\$ 6.13	\$ 6.18	\$ 1.85	\$ 1.40
RENTAL RATE TRENDS:				
Average final rate with expense pass throughs	\$ 14.59	\$ 14.02	\$ 6.40	\$ 5.32
Average first year cash rental rate	\$ 15.60	\$ 15.08	\$ 7.12	\$ 5.70
Percentage increase	6.92%	7.56%	11.25%	7.14%

The following tables set forth scheduled lease expirations for executed leases as of September 30, 1997 assuming no tenant exercises renewal options.

OFFICE PROPERTIES:

YEAR OF LEASE EXPIRATION	NUMBER OF LEASES	TOTAL RENTABLE SQUARE FEET EXPIRING	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE FOR EXPIRATIONS (1)	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
Remainder of 1997	186	708,310	5.1%	\$ 10,500,474	\$ 14.82	5.0%
1998	394	2,305,849	16.5	33,293,265	14.44	15.9
1999	349	1,797,217	12.9	26,288,671	14.63	12.5
2000	390	2,386,722	17.1	35,864,233	15.03	17.1
2001	249	1,979,914	14.2	32,126,909	16.23	15.3
2002	231	1,950,155	14.0	29,435,111	15.09	14.1
2003	50	865,786	6.2	13,133,524	15.17	6.3
2004	29	427,591	3.1	7,060,436	16.51	3.4
2005	15	443,083	3.2	4,919,220	11.10	2.3
2006	13	550,512	3.9	7,523,576	13.67	3.6
2007+	21	527,438	3.8	9,341,217	17.71	4.5
Total or average	1,927	13,942,577	100.0%	\$209,486,636	\$ 15.02	100.0%

INDUSTRIAL PROPERTIES:

YEAR OF LEASE EXPIRATION	NUMBER OF LEASES	TOTAL RENTABLE SQUARE FEET EXPIRING	PERCENTAGE OF LEASED SQUARE FOOTAGE REPRESENTED BY EXPIRING LEASES	ANNUAL RENTS UNDER EXPIRING LEASES (1)	AVERAGE ANNUAL RENTAL RATE FOR EXPIRATIONS (1)	PERCENTAGE OF LEASED RENTS REPRESENTED BY EXPIRING LEASES
Remainder of 1997	98	769,178	12.2%	\$ 4,011,513	\$5.22	11.9%
1998	159	1,109,965	17.6	6,514,773	5.87	19.3
1999	139	1,370,792	21.6	7,022,542	5.12	21.0
2000	112	1,130,115	17.9	6,739,991	5.96	20.0
2001	55	579,958	9.2	3,434,202	5.92	10.2
2002	37	853,426	13.5	3,587,685	4.20	10.7
2003	5	72,526	1.1	595,661	8.21	1.8
2004	5	104,369	1.7	520,335	4.99	1.5
2005	5	38,532	0.6	319,660	8.30	0.9
2006	2	196,600	3.1	882,636	4.49	2.6
2007+	1	95,545	1.5	44,428	0.00	0.1
Total or average	618	6,321,006	100.0%	\$ 33,673,426	\$5.33	100.0%

(1) Includes operating expense pass throughs and excludes the effect of future contractual rent increases.

INFLATION

Historically inflation has not had a significant impact on the Company's operations because of the relatively low inflation rate in the Company's geographic areas of operation. Most of the leases require the tenants to pay their pro rata share of increased incremental operating expenses, including common area maintenance, real estate taxes and insurance, thereby reducing the Company's exposure to increases in operating expenses resulting from inflation. In addition, many of the leases are for terms of less than seven years, which may enable the Company to replace existing leases with new leases at a higher base rent if rents on the existing leases are below the market rate.

PART II -- OTHER INFORMATION

- Item 1. Legal Proceedings -- None
Item 2. Changes in Securities and Use of Proceeds --

On August 17, 1997, the Company sold 1.8 million shares of Common Stock to UBS Limited for net proceeds of approximately \$57 million. A placement fee of 2% of the gross proceeds of the offering was paid to UBS-Securities. The shares were issued in reliance on exemptions from registration, including the exemption under Rule 506 of the Securities Act of 1933, as amended (the "Securities Act"). The offering was conducted privately and involved only one buyer, which was an "accredited investor" as defined under Rule 501 under the Securities Act. In addition, the Company exercised reasonable care to assure that the purchaser of the shares was not an underwriter under the Securities Act.

- Item 3. Defaults Upon Senior Securities -- None
Item 4. Submission of Matters to a Vote of Security Holders -- None
Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

EXHIBIT NO.	DESCRIPTION
2	Master Agreement of Merger and Acquisition by and among the Company, the Operating Partnership, Associated Capital Properties, Inc. and its shareholders dated August 27, 1997 (incorporated by reference to the Company's Current Report on Form 8-K dated August 27, 1997)
3	Amended and Restated Articles of Incorporation (incorporated by reference to the Company's Current Report on Form 8-K dated September 25, 1997)
27	Financial Data Schedule

(b) Reports on Form 8-K The Company filed a report on Form 8-K, dated August 27, 1997, reporting under item 5 of the Form that it had entered into an agreement to merge with Associated Capital Properties, Inc. and acquire a related property portfolio. The report included audited financial statements of Associated Capital Properties, Inc. for the year ended December 31, 1996 and of the 1997 Pending Acquisitions for the year ended December 31, 1996. The Company filed a report on Form 8-K dated September 18, 1997, reporting under item 5 of the Form that it had retained Alston & Bird LLP as its securities counsel and filing certain legal opinions in connection with its shelf registration statement on Form S-3, file no. 333-31183. The Company filed a report on Form 8-K, dated September 25, 1997, reporting under Item 5 of the Form the closing of its offering of the 8% Series B Cumulative Redeemable Preferred Shares.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.
HIGHWOODS PROPERTIES, INC.

/s/ RONALD P. GIBSON
 RONALD P. GIBSON
 PRESIDENT AND CHIEF EXECUTIVE OFFICER
/s/ CARMAN J. LIUZZO
 CARMAN J. LIUZZO
 CHIEF FINANCIAL OFFICER
 (PRINCIPAL ACCOUNTING OFFICER)

Date: November 14, 1997

EXHIBIT INDEX

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ARTICLE 5

PERIOD TYPE	3 MOS	9 MOS
FISCAL YEAR END	DEC 31 1997	DEC 31 1997
PERIOD START	JUL 01 1997	JAN 01 1997
PERIOD END	SEP 30 1997	SEP 30 1997
CASH	184,230,000	184,230,000
SECURITIES	0	0
RECEIVABLES	16,798,000	16,798,000
ALLOWANCES	0	0
INVENTORY	0	0
CURRENT ASSETS	212,057,000	212,057,000
PP&E	1,803,225,000	1,803,225,000
DEPRECIATION	72,319,000	72,319,000
TOTAL ASSETS	1,980,178,000	1,980,178,000
CURRENT LIABILITIES	41,565,000	41,565,000
BONDS	649,188,000	649,188,000
PREFERRED MANDATORY	0	0
PREFERRED	297,500,000	297,500,000
COMMON	379,000	379,000
OTHER SE	991,546,000	991,546,000
TOTAL LIABILITY AND EQUITY	1,980,178,000	1,980,178,000
SALES	61,768,000	177,246,000
TOTAL REVENUES	63,655,000	183,214,000
CGS	17,407,000	48,995,000
TOTAL COSTS	28,558,000	80,046,000
OTHER EXPENSES	2,410,000	6,694,000
LOSS PROVISION	0	0
INTEREST EXPENSE	11,133,000	34,771,000
INCOME PRETAX	0	0
INCOME TAX	0	0
INCOME CONTINUING	18,106,000	51,831,000
DISCONTINUED	0	0
EXTRAORDINARY	1,328,000	4,665,000
CHANGES	0	0
NET INCOME	13,908,000	40,194,000
EPS PRIMARY	.38	1.12
EPS DILUTED	.38	1.12

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