

Dexus (ASX: DXS)

ASX release



5 May 2020

COVID-19 and March 2020 quarter portfolio update

Dexus today provides the following update on its COVID-19 response and announces its property portfolio update for the quarter ended 31 March 2020.

Darren Steinberg, Dexus Chief Executive Officer said: "The COVID-19 pandemic has had a profound impact on the economy and the real estate sector, and we acknowledge that no business, including Dexus, will be immune from the impacts of this crisis.

"Fortunately, as at 31 March 2020 our property portfolio is in strong shape and we've entered this crisis in a robust position with high portfolio occupancy, limited new supply in our key CBD office markets and a strong balance sheet.

"We know this is a challenging time for many of our valued customers (tenants) and appreciate we are in this together. We are committed to helping our customers and consistent with the government's Code of Conduct, our focus is on prioritising assistance to support the viability of our small business customers.

"In response to the current environment brought on by COVID-19, we have implemented a broad range of cost reduction measures that are prudent for our business.

"Unfortunately, a number of roles will be impacted, largely as a result of the loss of the Australian Mandate portfolio managed on behalf of the NSW State Treasury Corporation, which will result in some redundancies."

Dexus has also implemented annual leave initiatives, a freeze on recruitment and non-essential consultancy spend and temporary reductions in remuneration.

The temporary reductions in remuneration affect director and executive level roles and have been approved by the Board for an initial three month period effective 1 April 2020 which will be reviewed at the end of June 2020. These include a:

- 15% reduction in base fees for Non-Executive Directors
- 15% reduction in base salary for the CEO
- 10% reduction in base salary across all other executive level roles

On 26 March 2020, Dexus withdrew its FY20 full year guidance for distribution per security growth and the detailed assumptions associated with this guidance. At this time, Dexus continues to assess the impact of COVID-19 on its operating environment including the assistance that it may need to provide to its tenant base to ensure the portfolio is well placed to perform when this event passes.

March 2020 quarter highlights

- Leased 33,284 square metres¹ of office space across 62 transactions in the core portfolio and at development projects underway or completed, with office portfolio occupancy remaining high at 97.2%
- Leased 21,094 square metres¹ of industrial space across 22 transactions, with industrial portfolio occupancy remaining strong at 96.0%
- Post 31 March 2020, Dexus announced the settlement of GIC's additional 24% investment of \$366.1 million in the Dexus Australian Logistics Trust in addition to the establishment of a new Joint Venture with GIC that had exchanged contracts to acquire a 50% interest in Rialto Towers, 525 Collins Street, Melbourne for \$644 million²
- At 30 April 2020, Dexus had a debt duration of 7.1 years, \$1.7 billion of cash and committed undrawn bank facilities available and circa \$400 million of debt maturing in late FY21. Dexus's proforma gearing³ (look-through) is 25.4% which is below its 30-40% target range
- Post 31 March 2020, Central Place Sydney, a major commercial development underpinning the delivery of the Sydney Innovation and Technology Precinct, progressed to Stage 3 under the NSW Government's Unsolicited Proposal process
- Dexus was named on the CDP Climate A List for 2019, solidifying its position as one of Australia's leading sustainable investments of choice for real estate and was also recognised by the Workplace Gender Equality Agency being awarded an Employer of Choice for Gender Equality (EOCGE) citation for 2019-20

Dexus office portfolio

Key metrics	31 March 2020	31 December 2019
Occupancy by income	97.2%	97.4%
Occupancy by area	97.3%	97.4%
WALE by income	4.4 years	4.5 years
Average incentives ⁴	16.9%	16.2%

In April 2020, the Australian Government introduced a commercial Code of Conduct⁵ and set of principles which applies to commercial tenancies (including retail, office and industrial) for small and medium enterprise customers (SMEs) with turnover of less than \$50 million experiencing financial stress or hardship as a result of the COVID-19 pandemic.

Dexus is currently working with its customers to respond to the immediate and longer-term consequences of the COVID-19 crisis. While there is no one size fits all approach, Dexus's immediate priority is to support SMEs, including the city retailers that support the office community, who have been significantly impacted by the coronavirus pandemic, and is progressing discussions with these customers on various forms of rental relief. From those customers who have requested rental relief, Dexus estimates SMEs (office, retailers and industrial) with turnover of less than \$50 million to comprise approximately 8% of total property portfolio income and is working through if they qualify for relief. Dexus also acknowledges the significant business interruptions and impacts to its larger customers and thanks them for supporting the approach to prioritise assistance to small businesses.

In the current environment, office leasing enquiry levels have fallen and inspection rates have slowed. Lead indicators point to a period of uncertainty in the office markets across Australia, with demand across the major CBD markets likely to be patchy in the short term. In times of uncertainty, high quality and well leased assets can be expected to hold their value better than lower quality assets due to their appeal to occupants and purchasers and their relative scarcity.

Over the quarter to 31 March 2020, a total of 33,284 square metres¹ of office space was leased across 62 transactions in the core portfolio and at development projects underway or completed. Notable activity during the quarter included:

- Signing Heads of Agreement for a new customer at 180 Lonsdale Street, Melbourne across 3,574 square metres
- State of NSW has exercised the option to extend their lease across 2,952 square metres at 130 George Street, Parramatta
- Renewing customers at King Square, Perth and Waterfront Place, Brisbane across 3,657 square metres and 3,736 square metres respectively

Dexus industrial portfolio

Key metrics	31 March 2020	31 December 2019
Occupancy by income	96.0%	96.0%
Occupancy by area	95.5%	95.7%
WALE by income	4.4 years	4.6 years
Average incentives	13.0%	13.3%

In the current environment, industrial leasing enquiry levels have slowed, with a divergence in demand depending on the extent to which individual companies' product lines fall into non-discretionary and discretionary categories. Some categories remain relatively active such as food, pharmaceuticals and online goods. Enquiry has been positive for supermarket overflow space across the eastern seaboard. Within Sydney and Melbourne, we are seeing strong demand from the healthcare and construction plant and equipment sectors.

Industrial property markets are expected to be relatively resilient given market vacancy is relatively low and the risk of over-supply will be mitigated by the responsiveness of supply to the adjusting levels of demand. The long-term growth drivers for the Australian industrial market remain intact with continued expansion in ecommerce and infrastructure investment.

Over the quarter to 31 March 2020, 21,094 square metres¹ of industrial space was leased across 22 transactions, with notable activity including:

- Securing new customer, Probiotic at 52 Holbeche Road, Arndell Park across 9,795 square metres for a 10-year term, incurring minimal downtime of only two months

- Renewing a customer across 4,356 square metres at 145-151 Arthur Street, Flemington
- Securing leasing across 3,616 square metres at Axxess Corporate Park through 12 transactions
- Renewing three customers and securing two new customers across a total 2,642 square metres at Lakes Business Park, Botany

Development

Dexus's group development and concept pipeline stands at a cost of circa \$11.2 billion post completions and additions. Committed project spend until the end of 2022 is forecast at \$289 million for Dexus.

As a consequence of the current environment, development projects have not been materially impacted at this stage, with impacts primarily centred around heads of agreement not converting to binding leases or customers seeking to delay lease start dates.

During the quarter, Dexus progressed its office developments at 180 Flinders Street and 80 Collins Street in Melbourne which are 76% and 98% committed respectively. Dexus also completed The Annex at 12 Creek Street, Brisbane (24% committed) providing 12 levels of boutique office space, and completed the retail component of 175 Pitt Street, Sydney (80% committed). Development approval was also received for 35,730 square metres of gross floor area at 60 Collins Street, Melbourne.

Dexus continued to progress the activation and conversion of the uncommitted development pipeline including progressing Central Place Sydney to move to Stage 3 under the NSW Government's Unsolicited Proposal process.

Capital management

From a balance sheet perspective, Dexus's proforma gearing³ (look-through) is 25.4%. Debt is well diversified and comprises 38% from bank debt and 62% from debt capital markets, with a debt duration of 7.1 years at 30 April 2020.

Over the past 12 months Dexus has accessed both equity and debt capital markets to provide additional funding capacity and flexibility.

Post issuance of the \$500 million of 12-year Medium Term Notes and since the HY20 results, Dexus has secured additional bank debt facilities totalling \$550 million with a weighted average tenor of 5.0 years providing it with further funding flexibility in the current environment. At 30 April 2020, Dexus had \$1.7 billion of cash and committed undrawn bank facilities available and circa \$400 million of debt maturing in late FY21.

Dexus remains within all of its debt covenant limits, including gearing and interest cover, and is below its target gearing range of 30-40%.

Dexus continues to retain its strong credit ratings of A-/A3 from S&P and Moody's respectively.

Environmental, Social and Governance (ESG)

Dexus's focus on ESG factors continues to contribute to long-term value, and during the quarter Dexus was recognised by a number of external groups, including:

- Dexus being named on the CDP Climate A List for 2019, solidifying its position as one of Australia's leading sustainable investments of choice for real estate. Dexus was one of six companies in Australia and one of four Australian property companies to be included on the CDP Climate A List for 2019
- Dexus being recognised by the Workplace Gender Equality Agency (WGEA) for its active commitment to and progress towards gender equality across its workplace – being awarded an Employer of Choice for Gender Equality (EOCGE) citation for 2019-20

Funds management

During the quarter, Dexus confirmed that on 30 June 2020 it would cease management of the Australian Mandate which comprises a \$2.2 billion⁶ property portfolio.

On 1 April 2020 Dexus settled on the second tranche rights exercised for GIC to acquire an additional 24% interest in the Dexus Australian Logistics Trust core portfolio for \$366.1 million.

In addition, on 6 April 2020, Dexus announced the establishment of a new Joint Venture ("JV") with GIC that had exchanged contracts to acquire a 50% interest in Rialto Towers, 525 Collins Street, Melbourne, for \$644 million². The establishment of the JV and acquisition of Rialto Towers is consistent with Dexus's strategic objective of being a wholesale partner of choice, providing the group with a breadth of capital sources through economic cycles. Dexus has invested in this opportunity to leverage the long-term fundamentals of the Melbourne office market including the recent strong population growth trend (circa 1.8% per annum) and have been able to access this quality product off-market. The asset is multi-let to circa 80 customers and is an asset that will involve leveraging Dexus's leasing capabilities and extensive customer relationships to drive asset performance.

Trading

Dexus has received proceeds from the initial 25% interest sale of 201 Elizabeth Street, Sydney and has a put and call option to sell its remaining 25% interest in late 2020 for a total of \$315 million. The sale has contributed circa \$34 million to pre-tax trading profits in FY20 and is expected to contribute a further circa \$34 million in pre-tax trading profits in FY21 in the event either option is exercised.

The sale of the North Shore Health Hub on a fund-through basis to HWPF is expected to generate trading profits across FY20 and FY21, with the amount for each financial year dependent on the progress of the development and leasing.

Summary

Darren Steinberg said: "Dexus is in a strong position. We have entered this period of uncertainty owning and managing a quality property portfolio with high occupancy and a strong balance sheet.

"There are a lot of moving parts both domestically and globally and it is reassuring to see that Australia is well placed in managing the spread of COVID-19 compared to the rest of the world. We are starting to see restrictions being progressively eased by state governments across the markets that we operate in.

"The eventual recovery will be helped by sizable government fiscal stimulus, a lower for longer interest rate environment, and the ongoing infrastructure pipeline underway in key capital cities."

Authorised by Brett Cameron, General Counsel and Company Secretary of Dexus Funds Management Limited

For further information please contact:

Investors

Jessica Johns
Senior Manager, Investor Relations
+61 2 9017 1368
+61 427 706 994
jessica.johns@dexus.com

Media

Louise Murray
Senior Manager, Corporate Communications
+61 2 9017 1446
+61 403 260 754
louise.murray@dexus.com

Disclaimer

This update was prepared against the backdrop of the unfolding disruption caused by the outbreak of COVID-19 and the resultant deterioration in business conditions. It is apparent that there are potential implications from the outbreak for the global and domestic economy, volatility in equity markets, liquidity in credit markets and impact on the appetite for and pricing of real estate assets which are uncertain and unquantifiable at this time. This update should be read and considered in light of that uncertainty.

About Dexus

Dexus is one of Australia's leading real estate groups, proudly managing a high-quality Australian property portfolio valued at \$33.8 billion. We believe that the strength and quality of our relationships is central to our success and are deeply committed to working with our customers to provide spaces that engage and inspire. We invest only in Australia and directly own \$16.8 billion of properties, with a further \$17.0 billion of properties managed on behalf of third-party clients. The group's \$11.2 billion development pipeline provides the opportunity to grow both portfolios and enhance future returns. With 1.8 million square metres of office workspace across 55 properties, we are Australia's preferred office partner. Dexus is a Top 50 entity by market capitalisation listed on the Australian Securities Exchange (trading code: DXS) and is supported by 27,000 investors from 20 countries. With 35 years of expertise in property investment, development and asset management, we have a proven track record in capital and risk management, providing service excellence to customers and delivering superior risk-adjusted returns for investors. www.dexus.com

Dexus Funds Management Ltd ABN 24 060 920 783, AFSL 238163, as Responsible Entity for Dexus (ASX: DXS)
Level 25, 264 George Street, Sydney NSW 2000

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- 1 Including Heads of Agreement.
 - 2 Reflecting the net acquisition price for the 50% interest in Rialto Towers (of which GIC will hold a 90% share and Dexus a 10% share) and excludes acquisition costs, incentives and other costs.
 - 3 Proforma 31 March 2020 look-through gearing including the settlement of GIC's additional interest in the Dexus Australian Logistics Trust core portfolio and acquisition of Rialto Towers (before transaction costs) previously announced on 1 April 2020 and 6 April 2020, respectively.
 - 4 Excluding development leasing.
 - 5 The code of conduct is available at <https://www.pm.gov.au/sites/default/files/files/national-cabinet-mandatory-code-of-conduct-sme-commercial-leasing-principles.pdf>.
 - 6 Following the ASX release on 4 March 2020, Dexus has been informed that the Investment Management of the Australian Mandate's 50% interest in Westfield Knox will be transferred to the new manager.