

Dexus (ASX: DXS)

ASX release



23 October 2019

September 2019 quarter portfolio update

Dexus today announced its property portfolio operational update for the quarter ended 30 September 2019.

Darren Steinberg, Dexus Chief Executive Officer said: "This office market cycle is certainly not over, with our office portfolio effectively full and the Sydney and Melbourne office market vacancy rates at very low levels. In this environment we remain confident of being able to continue to drive rental growth in our quality office properties in these markets, particularly in those leases coming up for expiry over the next few years."

Highlights

- Leased 27,267 square metres¹ of office space and 4,660 square metres of office development space across 77 transactions with office portfolio occupancy remaining high at 98.1%
- Leased 22,691 square metres¹ of industrial space across 30 transactions, with industrial portfolio occupancy increasing slightly to 97.4%
- Launched our next stage of office as a service through the acquisition of the Australian operations of Six Ideas, a strategic workplace and change management consultancy, enabling our customers to align workplace with organisational goals and strategy
- Sold the North Shore Health Hub, Stage 1 currently under development at 12 Frederick Street, St Leonards on a fund-through basis to Healthcare Wholesale Property Fund
- Dexus was named the Global Industry Leader for the Real Estate Sector by the Dow Jones Sustainability Index (DJSI) and achieved Global Sector Leader status for listed office in the Global Real Estate Sustainability Benchmark (GRESB)

Dexus office portfolio

Key metrics	30 September 2019	30 June 2019
Occupancy by income	98.1%	98.0%
Occupancy by area	97.8%	97.8%
WALE by income	4.5 years	4.4 years
Average incentives ²	14.0%	13.4%

Executive General Manager, Office, Kevin George said: "Our portfolio occupancy remains very high. In a period of limited contiguous space options and limited new supply, we have the opportunity to reset rental levels across 147,900 square metres of vacant or expiring space across our Sydney portfolio, which is currently 8% under-rented, up to the end of FY22. This represents approximately 17% of our total office income.

"We continue to generate good enquiry volumes in line with our experience of the last 18 months and are very encouraged by the growth in SMEs and the technology sector, including cloud computing, social media and cyber security. The services industry generally is still benefiting from significant infrastructure investment in our key markets and this has helped underpin our high occupancy level.

"During the quarter we launched our next stage of office as a service through the acquisition of the Australian operations of Six Ideas, a strategic workplace and change management consultancy, enabling our customers to align their workplace with organisational goals and strategy. We also opened Dexus Place in Perth, which enables us to offer our Perth based and visiting customers the benefits of a state-of-the-art workspace with the flexibility of access from one hour to one month."

Over the quarter to 30 September 2019, a total of 31,927 square metres¹ of office space was leased across 77 transactions in the core portfolio and the development projects that are underway or recently completed. Notable activity during the quarter included:

- Securing 10 tenants across 2,983 square metres at Australia Square, Sydney

- Renewing 2,106 square metres with a tenant at 309 Kent Street, Sydney
- Securing two new tenants over 1,492 square metres at 100 Mount Street, North Sydney, taking committed space to 99.8% and WALE to 7.5 years only four months post completion.

Post 30 September 2019, Dexus and DWPF agreed terms with Herbert Smith Freehills for a long-term lease across 10,300 square metres at the 80 Collins Street precinct South Tower, increasing leased space at the South Tower from 63% to 89%.

Dexus industrial portfolio

Key metrics	30 September 2019	30 June 2019
Occupancy by income	97.4%	97.0%
Occupancy by area	98.9%	98.8%
WALE by income	4.7 years	4.7 years
Average incentives	3.8%	11.7%

Over the quarter to 30 September 2019, 22,691 square metres¹ of industrial space was leased across 30 transactions, with notable activity including:

- Securing 8,704 square metres at Axxess Corporate Park across 19 transactions, including Kaufland expanding across 2,099 square metres
- Renewing UPS across 5,465 square metres at Quarry, 5 Basalt Road, Greystanes
- Securing two new tenants and two renewals across 4,440 square metres at Lakes Business Park South, Botany

Occupancy (by income) increased slightly to 97.4%, while WALE (by income) was maintained at 4.7 years. Average incentives on leasing undertaken during the quarter reduced compared to FY19, with a higher proportion of deals during the quarter being represented by effective deals. Incentives on face deals were down slightly compared to FY19.

Development

During the quarter, Dexus completed its office development at 240 St Georges Terrace in Perth (now 95% committed³ with 7.1 year WALE) in addition to the following projects:

- City retail projects, providing enhanced amenity at 44 Market Street and 321 Kent Street in Sydney
- A 9,100 square metre distribution and office facility for Dunlop Flooring at 380 Doherty's Road, Truganina
- Healthcare Wholesale Property Fund's (HWPF's) Calvary Adelaide Hospital, a 12 storey, 343 bed hospital offering clinical services, consulting suites and a 24-hour emergency department

Dexus's group development and concept pipeline now stands at a cost of circa \$8.7 billion post completions during the quarter, including 240 St Georges Terrace and Calvary Adelaide Hospital.

Capital management

In early October, Dexus successfully completed the issue of \$200 million of domestic Medium Term Notes with a 10-year tenor at an attractive all-in rate of 2.62%.

Sustainability

Dexus's focus on environmental, social and governance (ESG) factors continues to contribute to long-term value, and during the quarter Dexus was recognised by a number of leading global ESG benchmarks, including:

- Dexus was named the Global Industry Leader for the Real Estate sector by DJSI in the 2019 SAM Corporate Sustainability Assessment
- The group achieved Global Leadership status in GRESB, with the following rankings:
 - Dexus Office Trust was ranked the Global Sector Leader⁴ for listed office entities and was ranked the number one global listed entity across all sectors
 - Dexus Wholesale Property Fund (DWPF) was ranked the Overall Global Sector Leader⁵ for diversified office/retail entities
- Achieved an A+ rating for both the Strategy & Governance and Direct Property modules in the latest assessment by the Principles for Responsible Investment (PRI)

Funds management

During the quarter, HWPF acquired the North Shore Health Hub, Stage 1 currently under development at 12 Frederick Street, St Leonards. The state-of-the-art healthcare facility, being developed by Dexus, will support existing infrastructure in a growing healthcare precinct on Sydney's lower North Shore and is due for completion in late-2020, with 50% of the facility already pre-committed.

As mentioned in the development section, the new Calvary Adelaide Hospital development was completed during the quarter.

Trading

As mentioned above, Dexus sold the North Shore Health Hub on a fund-through basis to HWPF and will continue to manage the development for total revenue of circa \$224 million⁶.

The sale is expected to contribute circa \$18-22 million⁷ in trading profits pre-tax, which will be realised across FY20 and FY21, with the amount for each financial year dependent on the progress of the development and leasing.

Dexus also exchanged contracts to sell a 25% interest in 201 Elizabeth Street, Sydney and entered into a put and call option for the remaining 25% in late 2020 for a total of \$315 million. The sale is expected to contribute 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.

FY20 outlook and guidance

Darren Steinberg said: "We've seen a significant increase in interest from offshore investors seeking to invest into quality direct office property in our funds management business. This increased interest is partly a function of the relative pricing and rent growth for Australian office comparing favourably to global cities.

"When you combine this trend with the actual transactional evidence that has flowed through in both Sydney and Melbourne over the past few months, along with the spread to bonds which has increased further, we are confident that we will see further cap rate compression.

"Our weighted average office portfolio cap rate was 5.15% at 30 June 2019. We expect circa 25 basis points of cap rate compression to flow through for quality office properties, and at least 25 basis points of cap rate compression for quality industrial properties over the next 12 months.

"Importantly, our high-quality property portfolio with a diversified lease expiry profile and fixed rental increments of 3.5-4.0%, projects in our development and concept pipeline, and our strong balance sheet all place us in a strong position to continue to deliver for investors in a period of continued economic and geopolitical uncertainty."

Dexus reiterates its market guidance⁸ for the 12 months ending 30 June 2020 to deliver distribution per security growth of circa 5%, with the distribution payout ratio remaining in line with free cash flow.

1 Including Heads of Agreement.

2 Excluding development leasing.

3 Excluding leases which expire in December 2019, 240 St Georges Terrace is 88% committed.

4 Global Sector Leader means the entity achieved the highest score for the nature of ownership and sector combined.

5 Overall Global Sector Leader means the entity achieved the highest score for its sector, regardless of nature of ownership.

6 Land was transferred at fair value. The balance of the proceeds reflects the development spend under a development management agreement that will be paid across a number of fund-through instalments during FY20 and FY21.

7 Expected trading profit reflects a potential range of assumptions regarding leasing and incentive outcomes as well as timing of achieving key milestones.

8 Barring unforeseen circumstances, guidance is supported by the following assumptions: Impacts of announced divestments and acquisitions; FFO per security growth of circa 3%, underlying FFO per security growth of circa 3%, underpinned by Dexus office portfolio like-for-like income growth of 4.5-5.5%, Dexus industrial portfolio like-for-like income growth (excluding one-offs) of 3-4%, management operations FFO of \$55-60 million, cost of debt of mid-3%; trading profits of \$35-40 million net of tax; maintenance capex, cash incentives, leasing costs and rent free incentives of \$170-185 million; and excluding any further transactions.

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About Dexus

Dexus is one of Australia's leading real estate groups, proudly managing a high quality Australian property portfolio valued at \$31.8 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 \$15.6 billion of office and industrial properties. We manage a further \$16.2 billion of office, retail, industrial and healthcare properties for third party clients. The group's circa \$8.7 billion development and concept pipeline provides the opportunity to grow both portfolios and enhance future returns. With 1.7 million square metres of office workspace across 53 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 26,000 investors from 19 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 tenants and delivering superior risk-adjusted returns for investors. www.dexus.com

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