Transcript

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InvenTrust Properties Corp 3rd Quarter 2022 Earnings Conference Call

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Operator Thank you for standing by and welcome to InvenTrust's third quarter 2022 earnings conference call. My name is Forum and I'll be your conference call operator today. Before we begin, I would like to remind our listeners that today's presentation is being recorded and a replay will be available on the investor section of the company's website at InvenTrustProperties.com. All lines will remain muted during the presentation portion of the call, with an opportunity for questions and answers at the end. If you would like to ask a question, please press star, one on your telephone keypad. I would now like to turn the call over to Mr Dan Lombardo, Vice President of Investor Relations. Please go ahead, sir.

Dan Lombardo Good morning, everyone, and thank you for joining us. In the room with me today is DJ Busch, President and Chief Executive Officer, Mike Phillips, Chief Financial Officer, Christy David, Chief Operating Officer, and Dave Heimberger, Chief Investment Officer. Following the team's prepared remarks, we will open the lines and answer questions from the research analyst community. As a reminder, some of today's comments may contain forward looking statements about the company's views on the future of our business and financial performance, including forward looking earnings guidance and future market conditions. These are based on management's current beliefs and expectations, and are subject to various risks and uncertainties.

Any forward looking statements speak only as of today's date, and we assume no obligation to update any forward looking statements made on today's call, or that are in the quarterly financial supplemental or press release. In addition, we will also reference certain non-GAAP financial measures. The comparable GAAP financial measures are included in this quarter's earnings materials, which are posted on our investor relations website. With that, it is my pleasure to turn the call over to DJ.

DJ Busch Thanks, Dan, and good morning, everyone. A little over a year ago, InvenTrust listed on the NYSC, and at that time, we laid out a business plan and strategy that offered a unique investment opportunity in the retail REIT sector. We've continued to execute on our stated goals throughout the last 12 months, one of which is moving our portfolio concentration closer to 100% Sun Belt by sourcing attractive grocery anchored acquisitions in our target markets, while opportunistically rotating out of our non-Sun Belt assets. We also utilise our investment grade rating to diversify and fortify our capital structure. Our team's efforts across all facets of the business proved that a simple and focused strategy can deliver strong results, as shown by our solid double digit core FFO growth in 2022, as implied in our updated guidance.

What this past year also underscored is that the underlying quality of our portfolio is outstanding. Our Sun Belt markets continue to experience in migration of companies and highly skilled workers, further adding to the positive demographic trends seen over the past decade. Further, the demographic profiles of our consumers in our markets likely are able to better absorb some of the pressures from inflation and economic uncertainty. While we know we're not immune to the adverse impacts of inflation, rising interest rates, and recessionary risks, InvenTrust has, and is expected to, continue delivering consistent results. Leasing demand remains robust, resulting in record high leased occupancy and strong same property NOI growth for the first nine months of the year.

On the supply side, higher cost and inflation headwinds are limiting new development of grocery anchored centres, as the hurdles from new construction remain challenging. This scenario brings additional demand and leasing opportunities to our portfolio, and affords us the opportunity to evaluate and focus on ensuring the proper tenant mix and credit quality at our centres, all while driving rents. When you include our sector leading balance sheet, we have positioned the company not only to drive growth when times are good, but also, preserve cash flow, while looking for opportunities during times of economic uncertainty. The strength of our balance sheet and our low leverage uniquely positions us to take advantage of any value dislocation we may see in the market. That said, on the transaction front, we remain extremely disciplined in our evaluation of new acquisitions. With that, I'm going to turn the call over to Mike to discuss our financial results and guidance in more detail.

Mike Phillips Thanks, DJ, and thank you, everyone, for joining us. Yesterday, InvenTrust reported a core FFO of $82.9 million or $1.23 per share, representing an increase of 21% for the first nine months of 2022, compared to the same period last year. The increase was largely driven by pro rata same property NOI, contributing eight cents per share, an additional three cents from 2022 acquisitions. In addition, we realised G&A savings of nine cents, due to recurring and non-recurring cost reduction, as well as a positive seven cent impact from our $100 million share repurchase in Q4 of last year. These gains were offset by an increase in interest expense of seven cents. Pro rata, same property NOI year-to-date reached $110.5 million, growing 5.4% over the same period last year.

The increase was primarily driven by contractual rent increases, occupancy gains, reductions of abatements given in 2022, offset by net out of period rent collected. I did want to point out, as expected and discussed in our previous two earnings calls, our year-to-date results did decelerate in comparison to the strong start for the first half of the year. This is primarily due to significant out of period rent collected in the third quarter of 2021, as well as the timing of operating expenses that have been contemplating our guidance throughout the year. Removing this out of period rent from the comparison periods, pro rata same property NOI would have increased 0.8% for the quarter, and 6.6% year-to-date.

Moving to the balance sheet. As of September 30th, our net leverage ratio was 25% and net debt to adjusted EBITDA was five times, which makes our leverage profile one of the lowest in the sector. Our pro rata weighted average interest rate is 3.8%, and our weighted average maturity is 4.9 years. Approximately 87% of our debt is fixed rate. At the end of the third quarter, we had approximately $575 million of total liquidity, including $350 million of borrowing capacity available on our credit facility. With our cash on hand, cash flow generated by our portfolio and the significant capacity available on our revolver, we can address our near term maturities, as well as continue to evaluate strategic opportunities in our capital allocation plan without needing to source new debt.

Moving on to our guidance. We are raising our core FFO range to $1.57 to $1.60. Reduced G&A and an increase in interest income are the main drivers of the upward revision. We are maintaining our pro rata same property NOI growth guidance at 4% to 5%. Our full guidance assumptions are provided in our supplemental disclosure filed yesterday. With that, I'm going to turn the call to Christy to discuss our portfolio activity.

Christy David Good morning, everyone. As Mike and DJ have mentioned, InvenTrust continues to experience strong operational and leasing performance. For the quarter, we signed 83 leases representing 478,000 sq ft from various retail categories. Our leased occupancy ended the first nine months of the year at 95.6%, 210 basis points above the same time period last year. Our anchor lease percentage for the third quarter remained at 98.2%, and our small shop increased to 91%, both at all-time highs. The solid leasing volume was bolstered by lease spreads at 8% for comparable new and renewal leases for the quarter. These results continue to validate the strength of our markets, are irreplaceable locations, and showcase our portfolio's ability to attract and retain tenants.

Our annual base rent, as of September 30th, for the pro rata same property portfolio was $18.91, an increase of 2.5%, compared to September 30th, 2021. Anchor tenant ABR was $12.39, with small shot ABR hitting $31.91. Both increases over Q2 of 2022 and Q3 of 2021. Our retention rate through the year is above 89%. We expect lease renewals to continue to make up a significant percentage of our leasing deals. In an environment of rising build out costs, a robust retention rate that eliminates downtime will remain a focal point in our overall leasing strategy. In our discussions with retailers, there is a common theme, to make long-term real estate decisions to secure the best brick and mortar locations with landlords that are committed to meeting store opening expectations.

Our team continues to be proficient in effectively turning signed leases into rent paying tenants. In a period where supply chain issues remain prevalent, we are thrilled with our team's ability to deliver spaces on time. For the third quarter and year-to-date, InvenTrust opened up 120,000 sq ft and 225,000 sq ft of space respectively. Finally, I wanted to address the impact of Hurricane Ian as it relates to our portfolio. InvenTrust owns 11 properties in Florida and seven in North Carolina, all near the path of the storm. I applaud the hard work and dedication of the InvenTrust team, who helped prepare our properties and tenants for this historic weather event. Their efforts were crucial in limiting the damage to our centres.

After evaluating the centres immediately after the storm, some property did sustain some wind and water damage. However, we are pleased to report the clean-up has been swift and our tenants are back open, operating and servicing their communities. The recovery for impacted areas remains an ongoing process, and we continue to work closely with our tenants to provide the support and assistance needed. Our thoughts continue to be with our partners and their families that were impacted by the hurricane. Now I will turn the call over to DJ for some final remarks.

DJ Busch Thanks Christy. I would like to conclude by officially welcoming Smita Shah InvenTrust's Board of Directors. Last month, InvenTrust announced the expansion of our board, and the appointment of Smita. I know she will be a dynamic add to our board and will bring a new perspective, as well as an impressive array of leadership and understanding of complex global infrastructure and environmental solutions. Smita's appointment furthers InvenTrust's commitment to finding high calibre professionals across all levels of the company, while enhancing our governance and management oversight efforts. We look forward to working with her and the rest of the board in our goal to maximise shareholder value. Operator, this concludes our prepared remarks. Please open the line for any questions.

Operator Absolutely. If you would like to ask a question, please press star, followed by one, on your telephone keypad. If, for any reason, you would like to remove that question, please press star, followed by two. Again, to ask a question, press star, one. As a reminder, if you are using a speakerphone, please remember to pick up your handset before asking your question. Our first question comes from the line of Floris van Dijkum with Compass Point. Floris, your line is now open.

Floris van Dijkum Thanks for taking my questions, guys. DJ, I'd love to get your comments… The real estate industry, and the retail industry, in particular, are being impacted by two trends, retail, in particular. One positive and maybe one quite negative. The positive is that most of your peers have been talking about continued leasing demand from retailers. And I wanted to get your perspective on that, what you're seeing and what you expect to see going forward. And then the negative trend is, obviously, rising interest rates are going to put upward pressure on cap rates, and maybe if you can provide a little commentary on that as well.

DJ Busch Good morning, Floris. Thanks for the question. To address the positive first, you hit the nail on the head. The underlying fundamentals of the business are quite strong, as many of our peers have alluded to or mentioned in their calls as well. We're seeing much of the same. Obviously, the markets that we're in have continued to experience tremendous in migration, positive demographic trends, all in the face of higher inflation, higher housing costs, and the like. But what we're seeing on the ground is continued leasing demand. One thing that I would mention is, obviously, the big piece that's really in our favour is the lack of supply, lack of institutional supply. With occupancy levels across the board at all-time highs, that gives us a lot more leverage than we've had in the past. You add to that the construction costs being elevated, the mobility of the tenants is probably not as easy as it used to be.

So, those two dynamics, I think, are working in our favour. How long and how sustainable that is remains to be seen, but for the foreseeable future, we see pretty good traction as it relates to our leasing demand. On the capital market side. Look, I think we're all dealing with the same thing. Luckily, we did a lot of our financing right before we listed the company, and then thereafter, with a private placement earlier this year, where in hindsight, the rates look quite favourable, based on where pricing is today. As it relates to cap rates, I think the thing that we're watching is cap rates is just one data point. We're trying to get to a return where we can make it accretive to our business. And because we haven't seen cap rates move as much as we've seen financing costs, that's a little bit more difficult in today's environment.

Now, if cap rates increase and unlevered returns increase, where we can make money, that's okay, too. So, as I mentioned in the prepared remarks, we're taking a little bit of a wait and see approach, to see if cap rates rise and there are some opportunities that we can take advantage of.

Floris van Dijkum In terms of cap rates, I know you just bought a smaller centre in in North Carolina, I believe, just outside of Charlotte. How long have you been looking at that? And has the cap rate on that centre moved in your favour, or was this an historical deal that was done that cap rates that you think are maybe not reflective of where they are going to?

DJ Busch It's a fair question, and obviously, it just closed subsequent to the quarter, so obviously, that's been in negotiation for a while. It was unencumbered, so those deals tend to move a little bit more quickly. We were very happy with the yield that we were getting. It's accretive to the business, accretive to the cash flow on the portfolio, which is why it made us comfortable. Also, remember that we've been recycling out of Colorado, so really, it's almost like a match funding, taking out some of our Colorado assets and moving even deeper into the Sun Belt, particularly North Carolina on an accretive basis.

Floris van Dijkum Thanks, DJ. That's it from me.

Operator Thank you for your question. Our next question comes from the line of Craig Schmidt with Bank of America. Craig, your line is now open.

Craig Schmidt Thank you. I just wanted to focus on the property operating expense. It continues to increase, and maybe you can tell us what's driving that and is the third quarter a good run rate?

DJ Busch Good morning, Craig. Thanks for the question. Third quarter wouldn't be a good run rate. I think we've alluded to it in the first and second quarters of this year that many of our property operating expenses, particularly on the non-recoverable side, were going to be a little bit backloaded. The run rate, I would say, was probably closer to what you saw at the beginning, or the first half of the year, as opposed to what you're going to see in the third and fourth quarter, where we expected some one-time items, some opportunities to get some things done at the property levels to further increase the demand at our centres. But I would look at the first half, as opposed to the second half, and that goes for the fourth quarter as well.

Craig Schmidt Great. And then how much higher can you take your anchor occupancy and your small shop occupancy? I'm just wondering where the bigger opportunity lies.

DJ Busch We're at all-time highs now. I think we can continue to push. The big bogey is we haven't seen any bankruptcies in a while, so I think withstanding no bankruptcies with some of the obvious centres that have struggled, where us, and many of our peers, have at least some exposure, everything else feels quite good. I would say, on the small shop side, we're just being mindful of the inflationary pressures on the small shop tenants. I think it hits them particularly harder than it does maybe for some of the larger national anchors. But we expect occupancy, based on our lease occupancy versus physical, to continue to increase, barring any major disruptions on the bankruptcy front.

The good news, though, Craig, is once we get to these levels of occupancy, that's where we can start to really push price. And, as Christy mentioned, with a retention rate in the high 80s and where you can push price, there's no better return than hitting renewals, where you're not putting a whole lot of capital, if any, back into the centres, but you're increasing your rents.

Craig Schmidt Thank you. Then finally, maybe talk a little bit about the consumer. Are you still seeing a good traffic to your centres through October? And when you talk to your retailers, what are their expectations for holiday 22?

DJ Busch I think holiday 2022 is still a little bit unknown. I will tell you that the consumer, at least at our centres, is still quite strong. Our traffic is down modestly from earlier in the year, but still above pre-pandemic levels, which is great. I think, obviously, the grocers, in an inflationary environment, continue to do quite well. Even if trips are down, baskets make up for that. What we're focused on is making sure that small shops, the ancillary offerings in our centres, whether it be services or smaller food options, that's where our focus has been, and we haven't seen any material changes yet, which is, not to say it won't happen, if this is more sustainable or longer lasting than we anticipate. But going into this holiday season, I would say that we feel cautious, but relatively optimistic that our centres are going to do well.

Craig Schmidt Thank you. That's it for me.

DJ Busch Thanks, Craig.

Operator Thank you for your question. This concludes our question and answer session for today's call. I will pass back to DJ Bush now for closing remarks. Thank you.

DJ Busch Thank you, everyone, for joining us this morning. If you have any follow-ups, please don't hesitate to reach out. Enjoy the rest of your day.

Operator This concludes today's conference call. Thank you for your participation. You may now disconnect your line.