InvenTrust Properties Corp. NYSE:IVT

Earnings Call

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Call Participants

EXECUTIVES

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COO, Executive VP, General Counsel & Corporate Secretary

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Daniel Joseph Busch
CEO, President & Director

David Heimberger
Senior VP & Chief Investment Officer

Michael Douglas Phillips
Executive VP, CFO & Treasurer

ANALYSTS

Floris Gerbrand Hendrik Van Dijkum
Compass Point Research & Trading, LLC, Research Division

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Presentation

Operator

Thank you for standing by, and welcome to InvenTrust Fourth Quarter 2022 Earnings Conference Call. My name is Emily, and I will 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 Investors section of the company's website at inventrustproperties.com. [Operator Instructions]

I'd now like to turn the call over to Mr. Dan Lombardo, Vice President of Investor Relations. Please go ahead, sir.

Dan Lombardo
Vice President of Investor Relations

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 up the lines and answer questions. 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.

Daniel Joseph Busch
CEO, President & Director

Thanks, Dan. Good morning, everyone, and thank you for joining us. The InvenTrust team had a productive 2022, our first full year as a publicly traded company. The simple and focused Sun Belt portfolio and investment strategy is proving out in all aspects of our business. The operations team continues to capitalize on solid leasing demand while also carefully managing expenses and build out costs associated with a robust leasing pipeline.

By year-end, we successfully rotated capital out of Colorado, selling all three properties in the state, leading to further investment in our Sun Belt markets.

Lastly, we maintained our displayed approach to balance sheet management while diversifying our capital sources through the execution of our inaugural private placement. As discussed on previous calls, InvenTrust continues to benefit from structural and macroeconomic trends creating positive tailwinds for the retail sector and specifically our portfolio. These include the continued migration of people and jobs to the Sun Belt, bringing higher household income consumers to our markets, the continued investment by retailers in brick-and-mortar locations to support evolving omnichannel business strategies and the limited to no new supply of institutional quality grocery-anchored centers.

For these reasons, InvenTrust high-quality properties remain extremely desirable to new and existing retailers. We finished 2022 at an all-time high leased occupancy rate of 96.1% grew same-property net operating income by 4.6% for the full year and delivered double-digit core FFO growth compared to the previous year. All of these results were ahead of our initial forecast.

We remain diligent in our search for opportunities for external growth. In the fourth quarter, we acquired two assets, a grocery-anchored center outside of Charlotte and one of our joint venture assets in San Antonio, which is shadow anchored by the dominant regional grocer HEB.

We also started 2023 by acquiring the remaining stake in our company's joint venture. It is well documented that this portfolio was a component of our acquisition strategy. We are pleased with the execution of this transaction. PGGM has been an outstanding partner over the past 10 years and a supporter of our Sun Belt grocery-anchored strategy and ESG initiatives.

With this transaction, the InvenTrust portfolio is now 100% wholly owned and further simplifies our investment story. Including this JV transaction, InvenTrust net investment activity totals over $200 million since our listing in line with our expectations. While we continue to actively look for acquisition opportunities, we recognize the pricing uncertainty in the current environment and are being prudent as we see borrowing cost increase in cap rates expand. Growing the portfolio is important to our long-term strategic plan, but we will remain disciplined when deploying our capital.

Looking ahead into 2023, a degree of uncertainty exists in the economy. Inflationary impacts on the consumer, combined with higher interest rates and potential tenant store closures could dampen some of the positive trends at the retail sector has benefited from over the past few years.

However, we continue to be optimistic about our business. This confidence comes from the positive performance of our Sun Belt portfolio during the pandemic, the resilient nature of our grocery-anchored and necessity-based tenants and our investment-grade balance sheet. Our initial 2023 guidance, which builds upon strong 2022 results continues to show the strength of our simple and focused strategy.

With that, I'm going to turn it over to Mike Phillips to provide more color on our financials and guidance.

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Thanks, DJ, and thank you, everyone, for joining us. I'll start with a recap of 2022. InvenTrust finished the year on a strong note. Yesterday, we reported full year core FFO of $105.9 million or $1.57 per share. This represents 12% growth over 2021. The increase was largely driven by $0.09 per share from pro rata same-property NOI and $0.04 from 2022 acquisitions.

Additionally, we realized G&A savings of $0.07 and a positive $0.08 impact from our $100 million share repurchase in Q4 of 2021. These gains were offset by $0.11 due to higher net interest expense from the private placement that was funded in Q3 of 2022 and increased borrowing costs.

Full year pro rata same-property NOI finished at $141 million, growing 4.6% over last year. The increase was primarily driven by contractual rent increases, occupancy gains, reduction of abatements in the current year and offset by net out-of-period rent collected and onetime and pre-leasing expenses designed to meet the demand we are seeing, some of which were not fully recoverable. Excluding out-of-period rent collected, our pro rata same-property NOI grew by 6% over 2021.

Moving to the balance sheet. As of December 31, our net leverage ratio was 25% and net debt to adjusted EBITDA is 4.8x. Our pro rata weighted average interest rate is 4% with a weighted average maturity of five years. At year-end, we had approximately $514 million of total liquidity, including a full $350 million of borrowing capacity available on our credit facility with no near-term maturities.

Finally, as you saw in our press release yesterday, the Board announced a 5% increase in our dividend beginning with our April 2023 payment. This brings our annualized dividend to $0.86 per share.

Moving on to 2023 full year guidance. We expect core FFO to be between $1.59 and $1.64 per share, which is an increase in the range of 1.3% to 4.5% over 2022. Our same-property NOI growth is expected to increase by 3.5% to 5% for the full year, which contemplates a bad debt reserve of 50 to 150 basis points of total revenue.

For both same-property NOI and core FFO, we anticipate a lower run rate in the first half of the year due to out-of-period rent collected in the first half of 2022 and increased interest expense from our private placement.

In the back half of the year, we expect these comparisons to ease as the sign that open pipeline begins to materialize. Our full year guidance assumptions are provided in our supplemental disclosure filed yesterday.

With that, I'm going to turn the call over to Christy to discuss our portfolio activity.

Christy L. David
COO, Executive VP, General Counsel & Corporate Secretary

Good morning, everyone. As DJ highlighted, demand for space across our portfolio continues to be strong with limited to no new supply coming online in our markets, available space in premier centers is scarce. This provides InvenTrust with significant pricing and negotiating leverage through new and renewal lease negotiations.

To that end, we leased over 461,000 square feet of space during the quarter, bringing our total leasing activity for 2022 to 1.3 million square feet. We ended 2022 at 96.1% leased occupancy, which is a 220 basis point increase from the end of last year as well as an all-time high.

Our anchor space leased occupancy increased to 98.7%, and our small shop increased to 91.3%, both all-time highs. As of December 31, InvenTrust pro rata same-property portfolio ABR, was $19.22, an increase of 3.3% compared to December 31, 2021. Anchor tenant ABR was $12.43 with small shop ABR hitting $32.12, both increases on a sequential and year-over-year basis.

Our retention rate for the quarter was above 90% and blended lease spreads for the full year were 8.4% for comparable new and renewal leases. A key benefit of our concentrated and clustered portfolio is the intelligence and market data generated by our local underground operations team. This information allows us to move quickly and take action as it pertains to distressed tenants well ahead of any store closure announcements.

With that said, none of our Bed Bath & Beyond, Party City or Regal theater locations are currently targeted for closure, which we feel validates the strength and quality of our centers. In this environment, vacant retail space is becoming scarce and is viewed at a premium. We view recapturing space now in an orderly manner as a positive opportunity embedded in our portfolio and one we are ready to capitalize on.

Finally, I wanted to conclude my remarks by adding some additional thoughts on our acquisition of the PGGM JV portfolio. These assets as well as the Stone Ridge property we acquired at the end of 2022 or all centers my team has been operating and leasing as if they were wholly owned for the past decade, allowing for a natural and seamless transition. There are several interesting leasing opportunities that we are currently working on to further drive growth at these centers.

Now I will turn the call over to DJ for some final remarks.

Daniel Joseph Busch
CEO, President & Director

Thanks, Christy. InvenTrust accomplished a lot in its first year as a publicly traded company, and we are even more excited for the future. InvenTrust thesis is simple, focused and provides a unique and specialized investment alternative for investors, an exclusive Sun Belt, predominantly grocer-anchored portfolio that is expected to deliver long-term value for our shareholders.
Operator, this concludes our prepared remarks. Please open the line for any questions.

Question and Answer

Operator

[Operator Instructions] The first question today comes from Floris Van Dijkum with Compass Point.

Floris Gerbrand Hendrik Van Dijkum
Compass Point Research & Trading, LLC, Research Division

DJ, I wanted to see if you could give us maybe a little bit more information on the PGGM transaction in terms of pricing? And also what the impact of that transaction will be on your leverage ratio going forward? Presumably, you funded your portion of the equity for that transaction with cash. And so if you can give us a little bit more detail? And is that indicative of where you think cap rates are for the market? And what do you expect is going to happen in your markets in terms of cap rates?

Daniel Joseph Busch
CEO, President & Director

Floris, thanks for the question. So without getting into specifics on pricing, I will just tell you that the returns that we see, first of all, it was a great partnership and many of the folks or actually all the folks that are sitting here with me, we're part of this joint venture at inception.

So I joined three or so years ago, and I could not say that PGGM is a great partner and someone actually, frankly, that we wouldn't mind doing business with in the future, if it made strategic sense for our business. But we do like what we see going forward in these assets. You -- as you know, some of these are some of our larger assets.

They are in the Houston market and obviously one in San Antonio. But have predominant grocers, HEB and Kroger specifically and really fit kind of the core strategy of InvenTrust, but we are excited about the potential growth opportunities that we see in this. So without giving kind of a real cap rate, the unlevered returns that we see coming out of these properties are something that we're really excited about, and our partner was very happy with our exit execution as well.

As it relates to the balance sheet, it's a good question. Our leverage will tick up a little bit. Now we're still well within our range, as you know, finished below 5x, still have ample capacity. And as we highlighted in our release last night, this transaction is about $100 million or so pro rata of the $150 million of investment activity that we're planning to do this year.

So you can expect us to be very careful and very prudent on how we're allocating that capital, given that our cost of capital as well as many in our space is elevated, and we're still trying to find footing in the transaction market, which I think will probably be a little bit backloaded. But we still expect to look for some of those opportunities to the tune of $50 million and more if we see opportunities that are unique.

Floris Gerbrand Hendrik Van Dijkum
Compass Point Research & Trading, LLC, Research Division

Great. And if I can ask also maybe ask about your guidance. Your same-store NOI of 3.5% to 5% is probably somewhat higher than some of your peers who've made explicit reserves for bad debt around some of the troubled retailers. Maybe if you can comment a little bit on your exposure there and what sort of assumptions you've made in terms of potential reserves for the year?

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Yes. No, it's a great question. And I think there's -- many of the folks in our sector have provided really good transparency around this. I would say, one of the unique or benefits of having a smaller portfolio is we're obviously have very good insight on our select few -- or properties that have exposure to these tenants.

So as it relates to Bed Bath & Beyond, we have four Bed Bath banners, one Buy Buy Baby. But from our perspective and from our operations team's insights as well as conversation with the retailer itself. We feel confident in our ability either to negotiate if that's the strategy that we undertake or are prepared to take that back. And not unlike many of our peers, we've had many discussions with several retailers that are dying to get more space on the potential of -- or the opportunities to enter these -- enter some of our properties if that opportunity were to arise.

Daniel Joseph Busch
CEO, President & Director

To give you a little bit of the goalposts. At the low end of the 50 basis points that Mike Phillips alluded to, that's really if we really don't get much back, maybe, call it, one or two boxes and it probably comes towards the latter end of the year, plus a little bit of unforeseen fallout from, call it, small shop tenants. So that would be the low end of that $50 million to $150 million.

On the flip side, the $150 million would be -- if we were to get most of those spaces back in short order as well as maybe some other unforeseen boxes or from other smaller shop bankruptcies. That's kind of the range. What we're expecting and what -- frankly, what we're -- candidly what we're hoping is that we do get some of those spaces back because of the opportunities -- releasing opportunities that we do see at some of these assets to really upgrade the merchandise mix and bring in higher rents.

Floris Gerbrand Hendrik Van Dijkum
Compass Point Research & Trading, LLC, Research Division

Do you have an idea of what sort of rent spreads that you could achieve? I mean some of your peers have talked about up to 60% rent spreads that they've actually achieved already. Should we expect some sort of big jump in base rents if you were to release some of that?

Daniel Joseph Busch
CEO, President & Director

No. 60% is, I think, not knowing who said that. It feels to me that those are out there, but those are exceptions rather than the rule. When we look at our portfolio in a very pragmatic fashion, we like the -- our ability to replace the current rents. I would say let's take, for example, Party City and Tuesday Morning, which tend to be around 10,000 to 12,000 square feet.

We have very de minimis exposure to either one of those tenants. But if -- I think it's 4 boxes in total. If we were to get any of those spaces back, those rents could probably be pushed to the tune of, call it, 10% to 20%, and then as it relates to Bed Bath & Beyond a little larger spaces, we think anything between, call it, 5% and 15% is a reasonable spread.

Floris Gerbrand Hendrik Van Dijkum
Compass Point Research & Trading, LLC, Research Division

Maybe last question for me. In terms of your shop occupancy, which obviously -- your anchor occupancy, you're almost full because you're 98.7% leased, if I'm not correct. But your shop occupancy of 91.3%. What is the least -- sorry, what's the physical occupancy there? And where -- I mean is that the segment of your portfolio that's going to provide a big chunk of your growth going forward in your view?

Daniel Joseph Busch
CEO, President & Director

Yes. No, it's a great question. And I think -- so just to give you the number, our small shop economic occupancy is 88.8%. So the spread there is actually a tad bit wider than what it is on the anchor side, which, as you mentioned, 98% leased, 96.8% economic occupancy. When I think about the small shop, that's where the next leg of growth is going to come from, right?

As you mentioned, we have three vacancies, anchor vacancies in the portfolio right now. So not a whole lot of real opportunity there unless we were to get some of the spaces back like we just discussed. So the small shop is really where we're pushing it.

And if you think about comments that I made last quarter and what you saw in the fourth quarter as well as it relates to some of our operating expenses being elevated, it's really some of our pre-leasing efforts, getting spaces that haven't been leased in a long time, making our assets as good as possible given the demand that we see today, knowing -- and I think David Luke said it well on his call that the demand is as strong as it's been, but it's not -- it may not last forever.

So what can we do to position ourselves to be ready to take advantage of those opportunities. And many of those opportunities will be coming on the small shop side, where if you think about your ability to close that spread, you get a lot more juice for lack of a better word because of the types of rents that you can put in those spaces.

Operator

The next question comes from Craig Schmidt with Bank of America.

Unknown Analyst

This is [Lily Dory] again on for Craig. Thanks for taking my question. I was wondering if you could provide a bit more detail on the Colorado assets that sold during the quarter? And kind of remind us again of how this fits into your strategy of rotating capital out of Colorado and then increasing your concentration in the Sun Belt and how that might fit in -- just within the planned $150 million of net investments within guidance?

Daniel Joseph Busch
CEO, President & Director

No, thanks for the question. And maybe I'll start and I'll pass it over to Dave Heimberger. But really, I think we've been pretty transparent as it relates to opportunities to recycle capital if we can find uses for that capital in our current markets. And that Colorado is a great example of that, exiting out of the three properties that we did own in that state. And frankly, it's a great market. It's a core market for most REITs or portfolios. It just didn't fit our focused and concentrated strategy on being in the Sun Belt. It is a great use of capital because it's such a strong market in itself, and it gives us an ability to move capital further south.

On an accretive basis. The other market that would fit that similar strategy would be the assets that we own kind of in the Virginia, Maryland corridor, call it, DC, greater DC, if you will. The fantastic properties, not being marketed today, but when we think long term, those are certainly a potential source of capital if we find further opportunities beyond the $50 million already earmarked that we're planning to deploy this year if we find the right assets and the right opportunities.

I don't know, Dave, if you had anything you want to add.

David Heimberger
Senior VP & Chief Investment Officer

Nothing really to add other than we like the idea of the sort of match funding, the PGGM strategy that we had in place, getting closer to our operational presence in our offices in the Sun Belt is obviously important to us, and Colorado just was a market that was difficult to grow in. And again, just trying to make it more simple and focused.

Unknown Analyst

And could you provide any color on just the cap rates around those sales?

David Heimberger
Senior VP & Chief Investment Officer

Yes. So we don't typically disclose cap rates on dispositions mainly to protect the buyers. I would say these are a little box on a couple of them. So probably skewed towards a higher end of the cap rate range of things you're seeing out there. So hopefully, that's enough color.

Unknown Analyst

All right. I have a second question. I guess, on the 220 bps lease-to-economic spread, what is the timing of delivery look like now? And is that on track in line with your expectations? Has there been any change in discussions with tenants just if you could provide an update on that.

Daniel Joseph Busch
CEO, President & Director

Yes. So good question. So almost all of that spread, I think all of it, we're expecting to come online at some point this year. So there's 4.8% -- I think the 220 basis points represents $4.8 million of potential ABR on an annualized basis. It tends to be back half weighted, but we would expect to probably call it, just to give you a round number, get to get half of that this year, if we stay on time and on schedule, which, as of now, we feel really, really good about.

Operator

This concludes the session on today's call. And I will now hand back to DJ for concluding remarks.

Daniel Joseph Busch
CEO, President & Director

Thank you, everyone, for joining us today. If you have any follow-up questions, please feel free to reach out to Dan Lombardo. Otherwise, enjoy the rest of your day.

Operator
Thank you, everyone, for joining us today. This concludes our call, and you may now disconnect your lines.