S&P Global
Market Intelligence

InvenTrust Properties Corp. NYSE:IVT

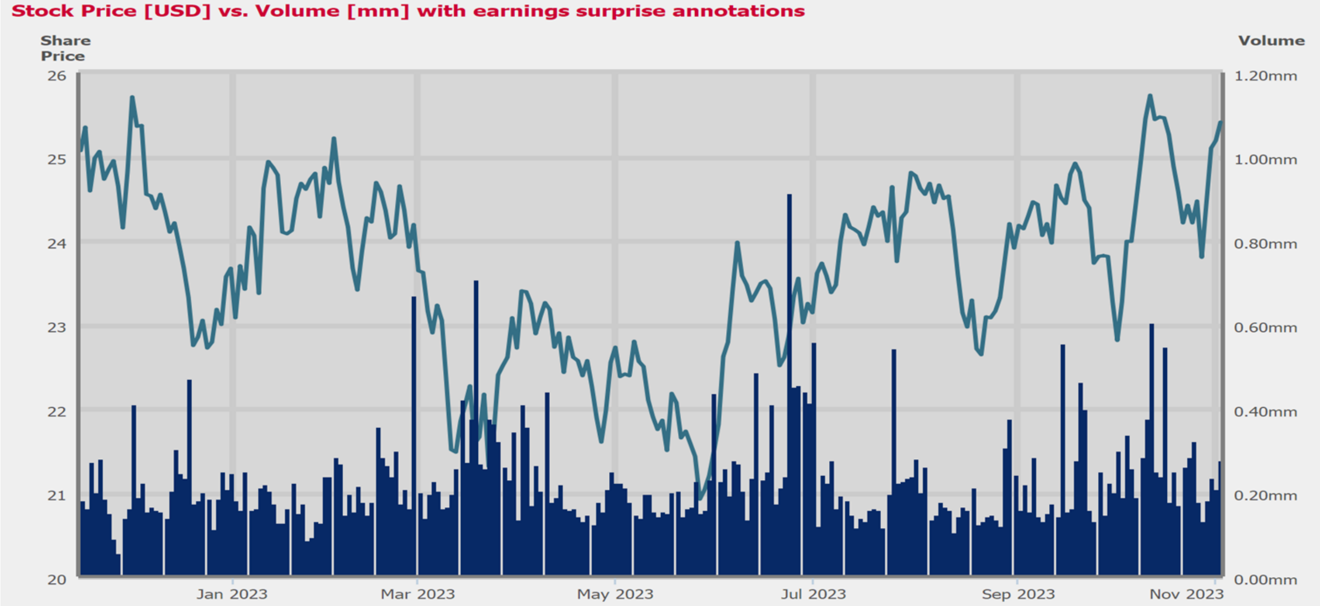
FQ3 2023 Earnings Call Transcripts

Thursday, November 2, 2023 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2023-			-FQ4 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.00	(0.06)	NM	(0.02)	(0.02)	NA
Revenue (mm)	63.59	64.06	▲0.74	63.99	257.43	NA

Currency: USD
Consensus as of Sep-20-2023 10:09 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2022	0.00	(0.05)	NM
FQ1 2023	NA	NA	NA
FQ2 2023	0.02	(0.01)	NM
FQ3 2023	0.00	(0.06)	NM

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Call Participants

EXECUTIVES

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

Dan Lombardo
Vice President of Investor Relations

Daniel Joseph Busch
CEO, President & Director

Michael Douglas Phillips
Executive VP, CFO & Treasurer

ANALYSTS

Cesar Bracho

Elizabeth Yang Doykan
BofA Securities, Research Division

Paulina Alejandra Rojas-Schmidt
Green Street Advisors, LLC, Research Division

Presentation

Operator

Hello and thank you for standing by, and welcome to InvenTrust Third Quarter 2023 Earnings Conference Call. My name is Bailey, 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 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

Thank you, operator. Good morning, everyone, and thank you for attending our call today. Joining me from the InvenTrust team 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 for 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, I will turn the call over to DJ.

Daniel Joseph Busch
CEO, President & Director

Thank you, Dan, and good morning, everyone. I'll begin the call with some brief remarks regarding the quarter, Mike will provide you with an overview of our financial results, and Christy will touch on some of our operational accomplishments.

InvenTrust delivered another solid quarter of operating results driven by our simple and focused strategy. That is to own and operate essential open air retail centers exclusively in the Sun Belt region of the U.S., maintain a simple and low levered capital structure and employ straightforward capital allocation plan. The better-than-expected performance has allowed us to once again adjust our 2023 full-year guidance higher for FFO per share, which Mike will touch on in a bit. The performance in the quarter is even more impressive given the recent liquidation of a top tenant, which drove nearly the entirety of our sequential lease occupancy decline. But like the commentary by many of our peers, the activity around these spaces has been unprecedented with opportunities to grow the rent, upgrade the merchandise mix and ultimately make our centers more valuable. Christy will provide more color on this in a bit.

On the supply side, new retail construction remains materially lower than historical averages and shopping center vacancy is at its lowest level since the global financial crisis. Our leasing results reflect this landlord, favorable supply and demand dynamic, which is amplified in the markets where we operate. Demographic trends in the Sun Belt continue to give us the confidence that market rent growth in our communities should outpace the national average for the foreseeable future. Continued tenant demand, coupled with the activity in our leasing pipeline, bodes well for our ability to organically grow cash flow while waiting for the broader capital markets to be more competitive for external growth opportunities.

Regarding our balance sheet, after exercising an extension option subsequent to the quarter, which Mike will touch on, we have no meaningful maturities until late '24, which provides us some flexibility and allows us to be patient until the debt capital markets stabilize, whatever level that may be. Given the uncertainty regarding the capital markets, our external growth criteria has and will remain very selective. Our liquidity and low leverage affords us the ability to be opportunistic when appropriate, but at the end of the day, our primary focus is sustainable cash flow growth year in and year out, which should in turn translate into superior total returns for our shareholders.

And with that, I'm going to turn the call over to Mike to discuss some of our financial results. Mike?

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Thank you, DJ, and good morning, everyone. Same-property NOI grew 5.3% over the third quarter of last year. Year-to-date same-property NOI was $106.3 million, growing 4.4% over the first 9 months of 2022. Year-over-year growth continues to be driven by higher occupancy, contractual rent bumps and solid leasing spreads. In addition, we have a tailwind of 110 basis points due to lower operating costs in 2023 compared to 2022. And as anticipated, these gains were offset by 70 basis points for out-of-period rents collected in 2022.

InvenTrust reported NAREIT FFO of $27.6 million or $0.41 per diluted share for the 3 months ended September 30, 2023, an increase of 5.1% for the same period in 2022. Our year-to-date NAREIT FFO was $84.7 million or $1.25 per diluted share, a decrease of $0.06 per share driven by our private placement debt funding in the third quarter of last year and GAAP adjustments related to our PGGM acquisition completed earlier in 2023. Our core FFO for the quarter was $27.6 million or $0.41 per diluted share, up 11% from last year, and our 9-month core FFO increased 1% compared to 2022. Components of core FFO growth include the increase in same-property NOI, the acquisition of 45% of our joint venture that was not owned and higher interest income, offset by an increase in interest expense.

From a balance sheet perspective, we ended the quarter with $457 million of total liquidity, including a full $350 million of borrowing capacity available on our revolving line of credit. Our net leverage ratio was 27%, and our net debt to adjusted EBITDA is 5.2x on a trailing 12-month basis. Our weighted average interest rate is 3.9% with a weighted average maturity of 4.1 years. In October, we executed a 1-year extension option for the cross-collateralized pool loan we assumed when we acquired the remaining interest in our joint venture, which was set to mature this year. With this subsequent activity, our debt metrics moved to a weighted average interest rate of 4.3% with a weighted average maturity of 4.2 years and a variable rate debt of approximately 10%. In the third quarter, we declared a dividend payment of $0.215 per share, which is a 5% increase over last year. And in August, Fitch Ratings affirmed our long-term issuer rating at BBB- with a rating outlook of stable.

Turning to our guidance. We are raising our 2023 core FFO midpoint to $1.64 with a range of $1.63 to $1.65 per share. We also raised our 2023 NAREIT FFO midpoint to $1.68 with a range of $1.66 to $1.69. Finally, our same-property NOI growth guidance midpoint increased to 4.63% with a range of 4.25% to 5%. Our full-year guidance assumptions are provided in our supplemental disclosure filed yesterday.

And 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

Thanks, Mike. The InvenTrust portfolio continues to deliver solid operating results, highlighted by strong leasing activity, leasing spreads and occupancy levels. Our outstanding performance is indicative of our strategy of owning and operating premier necessity-based shopping centers and growing Sunbelt markets. Tenant demand for our portfolio remains broad-based and includes tenant categories such as grocers, off-price retailers, medical, fitness concepts and restaurants. For the quarter, we leased 273,000 square feet with additional leases in our pipeline at various stages of negotiation, including our Bed Bath & Beyond spaces, which we will discuss in detail shortly.

Our anchor space lease occupancy finished at 96.6%, a decline of 200 basis points from last quarter, primarily driven by new vacancies from recent bankruptcies. Our small shop leased occupancy increased to 92.4%. Our total portfolio lease occupancy finished at 95.1%. As of September 30, InvenTrust total portfolio ABR was $19.36, an increase of 2.4% compared to 2022. Comparable leasing spreads were at 16% and 8% for new and renewal leases, respectively. A portion of our new leasing activity did involve larger spaces with longer lease duration, which aligns with our increased leasing costs compared to last quarter. Our retention remains high at 89%, which we continue to view as a positive balance with our new deal activity given the capital commitments required for retenanting.

InvenTrust had 5 Bed Bath & Beyond spaces, one lease at The Highlands of Flower Mound property in Dallas MSA was purchased at auction by Michaels, which will lead to minimal disruption and no impact to base rent. For our other Bed Bath & Beyond spaces, we have identified replacement tenants and are in the process of finalizing lease terms. Our leasing team is also in the process of replacing a former Christmas tree shop space with a painted tree boutique, a home decor and boutique clothing store. This tenant is a fantastic addition to our Westpark Shopping Center in the Richmond MSA. We are projecting these tenants to open their stores sometime in the next 12 to 18 months with sizable rent increases.

As DJ mentioned earlier, retailer bankruptcies continue, which ultimately affords us the opportunity to remerchandise with stronger credit tenants. Rite Aid recently announced their bankruptcy and initial list of store closings. InvenTrust has one Rite Aid location in Southern California, which accounts for 0.2% of our overall ABR. This space is in a strong center and was not on the current list of stores to be closed. Our exposure is limited and we are confident in our ability to absorb and re-lease these spaces.

In closing, we acknowledge that our results reflect the strength of the current retail environment, the attractiveness of our Sun Belt assets and our operating team's hard work, we see this momentum continuing as we work through the opportunity set in our pipeline. Operator, that concludes our prepared remarks, and you can open up the line for Q&A.

Question and Answer

Operator

[Operator Instructions] Our first question today comes from the line of Lizzy Doykan from Bank of America.

Elizabeth Yang Doykan
BofA Securities, Research Division

I just wanted to dig into the comments around Bed Bath and the other anchor tenants with bankruptcies involved. Could you again confirm how many Bed Bath boxes are left [indiscernible] in addition to Christmas Tree and Michaels. And then kind of talk to the expected time line for backfilling each of these boxes? And then separately, if we could kind of get a better understanding of the economics on the returns associated with the boxes when it comes to the associated costs?

Daniel Joseph Busch
CEO, President & Director

Yes. I can provide -- I can start and I'll have Christy hopefully fill in the blanks. But we have 5 Bed Bath & Beyond boxes. One was assigned and then the other 4 are currently under some form of negotiation. We think we'll be able to have those executed in short order, hopefully by the end of the year, maybe tailing into the early next year. But we feel really good about the backfills and the opportunities that we have at all the locations.

From a timing standpoint, these things usually take once they are executed and I think it's pretty standard right around 12 months, maybe up to 15 months. So we're not expecting a whole lot of income when you think about 2024. So maybe a little bit of a headwind that we think we can certainly overcome as we look out to next year. And as it relates to the economics, it really -- obviously, with construction costs up, we're much more sensitive to using our own capital because we want to get a good return on that capital. We've been very pleased, and it sounds like many of our peers, the same as it relates to the rents that we're able to attain in some of these spaces.

And just to give you a little bit of color, when we're looking at our negotiations right now, the payback periods for these boxes are, in most cases, under 2 years, which is pretty strong for an anchor space. And we're looking at net effective rents, healthy net effective rents, call it, in the low-double digits.

Elizabeth Yang Doykan
BofA Securities, Research Division

Okay. And to confirm, is that above what's typical of repositioning or retenanting your anchor boxes in terms of [indiscernible] and economics?

Daniel Joseph Busch
CEO, President & Director

It is surprisingly so because if you think about pre-pandemic, we're talking about probably a $60 square foot buildout and now that's closer to 90%. So the rents -- and because of the performance of the open air space and the strength of the retailers and the sales up to this point, we're able to push the rents to offset those higher construction costs in almost every case.

Elizabeth Yang Doykan
BofA Securities, Research Division

Great. And then for my next question, you all spoke to this last quarter, but just curious on hearing any new thoughts on addressing the swap that's set to expire in November this year on the $75 million maturity for the mortgage loan. Would you look to reinstate the swap, let it go to variable? Could you just discuss what options you're considering when it comes to refinancing the loan given your view of where rates are headed.

Daniel Joseph Busch
CEO, President & Director

No, it's a great question. We try not -- we try to be agnostic to where rates are headed. I don't think we're -- none of us are economists in this room. But we're always trying to make sure that we have full visibility as it relates to forecasting our cash flows. So obviously, fixing it is something that we're considering. And also, you have to remember, we have plenty of liquidity and a lot of cash on the balance sheet so we could chip away at that loan if we wish to, if that's the best use of our capital at that time.

Because at the end of the day, as I said in my prepared remarks, we're just -- we're trying to consistently grow cash flow and that can come in a lot of different forms. So we are looking at a lot of different opportunities, whether that be fixing it, paying a portion of it down. All those things are on the table. The good news is with that extension option, we do have some latitude as we look forward into 2024. And with an additional extension option, there's really very little that we have to address as we look forward to next year.

Operator

Our next question today comes from the line of Cesar Bracho from Wells Fargo.

Cesar Bracho

Can you comment about the bid ask spreads you're seeing in your core Sun Belt markets for properties that meet your criteria? Like do you think that gap has closed a little bit in recent trades or what do you see?

Daniel Joseph Busch
CEO, President & Director

Yes. It's a good question. I would say that there are still things that are hitting the market. The way I would characterize it, Cesar, if you think about what we sold in the quarter, the smaller asset in Atlanta, those deals in that kind of $10 million to $15 million range, I think the bid spread continues to be something that people can get comfortable transacting. So it's a little bit more narrow. As it grows and as those assets become a little bit more financing dependent, that's where you see the bid ask spread widen. And I think that's still the case. We're obviously not in the market for very large assets at this moment in time because of that reason. And it's not that you can't get financing for larger open air assets you can the pricing is just obviously much more elevated than it has been in the past. And I think that's something that we're going to have to get comfortable with and see where the pricing shakes out.

I know just from listening to some of our peers, it sounds like there has been some of those larger assets to transact some of the more high-quality blue chip shopping centers of larger size, which is good to see. But I would say, if I look back to our comments last quarter, it hasn't changed that much with the exception of in the smaller -- in the smaller assets, there's still some activity.

Cesar Bracho

And just quick following up. How would you -- what is that cap rate difference now for larger assets versus, say, the smaller assets similar to what you sold recently? And can you provide a cap rate for the asset that was sold?

Daniel Joseph Busch
CEO, President & Director

Ours was in the high-5s. And I would say that's probably -- I felt like that was a good price for both buyer and seller for an asset like the one that we sold. I can't really comment on some of the other ones, although it seems like some of the cap rates were pretty attractive for -- from a -- as those assets get larger, the cap rate tends to widen now. And I think some of those cap rates were probably very well executed, but that's just from the outside looking in.

Cesar Bracho

Got it. And then one more, if I may. Like what's the realistic time line for -- to put the excess cash to work -- like I acknowledge the comment to Lizzy's question on the optionality of using to pay down debt, depending on where rates go. But just curious, I will think the priority is to grow the property portfolio. So just curious what -- what's a realistic time line to put that to it?

Daniel Joseph Busch
CEO, President & Director

It's a good question. I think we look at it as a fluid situation. I mean, we're still active in our pipeline still has assets that we would love to transact. It's just obviously, the hurdle rate is much higher. We're looking at using our cash to pay down a portion of our debt the same way we would look at growing our business. Now obviously, our mandate is to try and grow this business, but we have to do it in an accretive manner. So the overarching goal for this company is to grow cash flow. Obviously, we want to do that while growing scale. But I don't see it -- we try to look at it under the same lens. But to your point, shrinking the company via paying down debt with maybe portions of cash is -- it's just one option that we're considering. But you're absolutely right. I mean if we can find accretive acquisitions so where we can continue to grow cash flow and expand the asset base, we'll absolutely do that. We just have to do it in a prudent manner.

Operator

The next question today comes from the line of Paulina Rojas from Green Street.

Paulina Alejandra Rojas-Schmidt
Green Street Advisors, LLC, Research Division

Your implied guidance range for 4Q for same-property NOI is relatively wide. I think that 1 month of 4Q is already behind us. And you're not the only one -- some of your peers are on the same. So my question is what leads you to keep in place this wide range? And how conservative do you think you will be with your '24 guidance? And do you think it's wise at this point to be conservative and think that perhaps next year we will see higher than average tenant fallout?

Daniel Joseph Busch
CEO, President & Director

It's a good question, Paulina. When we think about our implied guidance for the fourth quarter, you have to think about the size of our company, we're talking about $600,000 or $500,000 on both sides of the midpoint. So really, it's just -- if there's any unforeseen fallout really that we can't -- that we don't see today for the last couple of months of the quarter. And it can move the needle a little bit. But I think we're very comfortable with the range that we've provided. But it is just a box here and there, not even a box, really came full of small shops here or there that as we think about bad debt in the fourth quarter.

Looking forward to next year, look, I don't think Argo or anybody in the space is [goals] to be conservative. But I think it's just to be pragmatic on the current environment. It's been very resilient up to this point. I think with a lot of the opportunities that were created by Bed Bath & Beyond and maybe some of the other bankruptcies, timing is going to play a big factor next year as it relates to getting some meaningful rent back online, not only for InvenTrust but for many of our peers. And that timing will dictate how and the ability to kind of get those back online will dictate how successful next year will be.

I do think when we look forward to next year, we're going to overcome many of those headwinds because of the -- our ability -- our ability to push rents and the strength of -- the strength of our ability to push in-place escalators, everything that we've been discussing, that's going to obviously translate into or translate and transfer into 2024 as well.

Paulina Alejandra Rojas-Schmidt
Green Street Advisors, LLC, Research Division

And in terms of additional tenant fallout, I know we can't predict the future, but because of that uncertainty and everything we're seeing from a macro perspective, is it reasonable to assume higher than average -- higher than historical average for [debt]?

Daniel Joseph Busch
CEO, President & Director

Look, I think it's -- what's been fascinating to me this year, most shopping center REITs have stayed within their bad debt range even with a material bankruptcy or that for many was a top 20 tenant. And then you had a handful of other bankruptcies as well. I think that's a testament to the strength, the overarching strength of the fundamentals in the business. As we look forward to next year, without getting too much into 2024, I don't see it being that much different. When we think about anchor risk, I feel like that's been -- that's been minimized because of -- we had some of that this year. The resiliency to small shop continues to be very impressive. I would expect that to be more normalized next year as well. But it is something that we're looking at.

Look, the financing costs for many of our small shop retailers has obviously gone up, but the credit quality of our small shop retailers has also improved. So the strength of their balance sheets have improved as well, even though they're facing some of the inflationary and other headwinds that are out there. So when we look forward to next year, I don't see it being too dissimilar as we think about tenant fallout or bad debt.

Paulina Alejandra Rojas-Schmidt
Green Street Advisors, LLC, Research Division

If I may, one last one. I saw you moved the project for [indiscernible] to the product development. And here, you are transforming a single tenant building to multiple tenant -- multiple tenant buildings. You don't show the G&A, but I'm curious what's the cost per square foot to do a project like this? And I think you mentioned in your prepared remarks, the cost and I couldn't catch the details. So if you could repeat it, please, but I think you said just replacing a tenant with a senior use. And so yes, overall, you could provide an update on the cost of retenanting different types of assets.

Daniel Joseph Busch
CEO, President & Director

Yes. So I kind of missed the first part of your question -- or the second part of the question, Paulina, but I answer the first part and then maybe you can repeat the second part. But the Sarasota Pavilion is obviously a remerchandising opportunity for us. We -- the costs obviously are higher than what a single-tenant uses, and that's not -- that's certainly not unique to us. So if you think about -- and I'm just going to use very broad-based numbers, and it all depends on what you're working with and what the initial build-out looks like. But we're -- for a single tenant use, I mentioned earlier that for many of our Bed Bath & Beyond opportunities, it's somewhere close to, call it, $90 a square foot for something where you're cutting it this space in half.

And like I said, it depends on the size, it could be upwards to $150 to $170 -- $175 a foot. We're still working through that math and making sure the economics and returns make sense for InvenTrust, but it's certainly an exciting opportunity for that center. It's a really strong center in Florida. And obviously, we're doing it because we can get to that -- to those returns that are acceptable and value accretive for us. And then if you can just repeat that second part.

Paulina Alejandra Rojas-Schmidt
Green Street Advisors, LLC, Research Division

Yes, No need. I think you have articulated well and we got it.

Operator

[Operator Instructions] There are currently no additional questions waiting at this time. So I'd like to pass the call back over to the management team for any closing remarks.

Daniel Joseph Busch
CEO, President & Director

No, thank you, everyone, for joining us today, and we look forward to seeing many of you this -- later this month at NAREIT in Los Angeles. Enjoy the rest of the day.

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