InvenTrust Properties Corp. **NYSE: IVT**

FQ1 2024 Earnings Call Transcripts

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EXECUTIVES

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COO, Executive VP, General Counsel & Corporate Secretary

Dan Lombardo
Vice President of Investor Relations

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David Heimberger
Senior VP & Chief Investment Officer

Michael Douglas Phillips
Executive VP, CFO & Treasurer

ANALYSTS

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BofA Securities, Research Division

Dori Lynn Kesten
Wells Fargo Securities, LLC, Research Division

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

Presentation

Operator

Thank you for standing by, and welcome to InvenTrust First Quarter 2024 Earnings Conference Call. My name is Harry, 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 would 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 your attendance on today's call. 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

Thanks, Dan, and thank you to everyone joining us this morning. Today, I'll start with some brief commentary on our first quarter results, the overall operating environment and how InvenTrust continues to be positioned to grow sustainable cash flow long term. Mike will discuss our financial results and provide color around our updated 2024 guidance, and Christy will conclude with additional commentary regarding the leasing and operating landscape. 2024 is off to a solid start following an excellent 2023, where operating fundamentals in the open-air retail sector continue to benefit from supply and demand dynamics, not seen in several real estate cycles in our property type.

We have discussed on previous updates, the tenant demand continues to remain very robust for all of our properties. Some of that demand is due to the nature of the necessity-based property type that has not only withstood but validated the importance of our offerings to the communities in which we serve. The balance of the demand we at InvenTrust are specifically experiencing is due to the markets in which we operate. As we have said since becoming a public company, we expect the concentration we've aggregated within the portfolio, that is major cities in some markets should outpace the national average from a market rent growth perspective. And we believe that our past performance, but equally as important, our future expectations will continue to prove out that thesis.

Our simple and focused strategy to own and operate essential open-air retail centers exclusively in the Sun Belt region of the U.S. is playing out. And our straightforward and low levered capital structure will allow us to continue to deploy capital in an appropriate manner, if and when, we can do so in an accretive way for our shareholders. Leasing activity continues to meet or exceed expectations. Our Leased Occupancy rate finished the quarter at 96.3%, both up slightly sequentially and on a year-over-year basis, all while delivering double-digit blended leasing spreads.

Importantly, we are retaining high-quality tenants across the portfolio, negotiating rates that are favorable for our tenants' continued success, but with better annual escalations, specifically for Small Shop tenants with minimal cash outlay. [Certainly], we are retaining the proven tenants that are integral to the merchandise mix of our centers, while preserving capital, which will drive higher free cash flow for the portfolio into the future. Small Shop leasing continues to be strong. And while we saw more normal first quarter [arbitration], lease Small Shop occupancy remained above 92%. We continue to replace underperforming tenants and bring in higher credit and quality operators that will better serve their community constituents.

Christy will provide a little more detail in our leasing activity in a few minutes. But to finish on the operating environment, I felt it's important to highlight how underappreciated the lack of new institutional quality supply exists in open-air retail. Cannot be understated how few development starts are materializing. What this means is that given the lead time from start to stabilization in retail real estate is that landlord should benefit for the next few years before supply, if ever begins to emerge in a material way in our sector. Coupled out with the demand drivers in the Sun Belt, InvenTrust feels uniquely positioned to appropriately take advantage of this imbalance.

On the capital allocation front, the opportunity set of new deals has improved, but we remain selective in deploying capital, [heating] to our cost of capital, ensuring that we are growing in an appropriately accretive manner. Obviously, the capital market environment has been frustratingly volatile. As much as we would like to accelerate our external growth to complement our internal operations, we will continue to be prudent in our approach. Our balance sheet remains one of the lowest levered in the sector, which allows us to be patient, yet opportunistic and we keep a robust pipeline to be at the ready when the markets open up to our favor.

As discussed on last quarter's call, we secured our first acquisition in the Phoenix market in the first quarter of 2024. And we also had another property subsequent to the quarter in the Upper West Side of Atlanta. Moores Mill is a neighborhood Publix-anchored center that boasts powerful grocery sales, growth-oriented supporting tenants and is situated on a generational piece of infill real estate.

With that, I'm going to turn the call over to Mike to discuss our financial results. Mike?

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Thank you, DJ, and good morning, everyone. I will start with our results for the quarter, then discuss our balance sheet position and end with an update to our 2024 full year guidance. InvenTrust reported strong same property NOI of $41.5 million, an increase of 4.1% over the same time period last year. The increase was driven by growth from base rent, including 170 basis points from embedded rent bumps and net expense reimbursements of 280 basis points. NAREIT FFO for the quarter was $30.8 million or $0.45 per diluted share for the 3 months ending March 31, 2024, an increase of 9.8% over last year.

For the quarter, core FFO grew 10% to $0.44 per share compared to the same time period in 2023. Components of FFO growth for the quarter are primarily driven by same-property NOI and NOI from acquisitions. As DJ mentioned earlier, our balance sheet remains strong and provides us the ability to remain flexible as we navigate a challenging capital markets environment. We finished the first quarter with $421 million of total liquidity, including a full $350 million of borrowing capacity available on our revolving line of credit.

Our net leverage ratio was 28%. Our net debt to adjusted EBITDA is 5.1x on a trailing 12-month basis. Our weighted average interest rate ended the quarter at 4.3% with a weighted average maturity of 3.7 years. Our debt maturities are manageable, and we are comfortable with the limited amount maturing over the next 2 years. We will continue to observe markets as we evaluate our options for the $72 million [pool of] loan that matures in November. And as a reminder, we do have a 1-year extension option. Finally, we declared an annualized dividend payment of $0.91 per share, a 5% increase over last year.

I will conclude my remarks by updating InvenTrust 2024 guidance. With our strong start to 2024, we are raising our same-property NOI growth guidance by 50 basis points at the midpoint which is now expected to be in the range of 2.75% to 3.75%. We're increasing NAREIT FFO to $1.71 to $1.77 per share, and finally, we are moving core FFO guidance up to $1.67 to $1.71 per share. Our bad debt reserve will remain at 50 to 100 basis points of total revenue, and our net investment activity for the year remains unchanged at $75 million.

Finally, as we mentioned last quarter, we continue to anticipate a headwind in the second quarter due to the impact of the bankruptcies of Bed Bath & Beyond and Christmas Tree shops that took place in 2023, and NOI growth should reaccelerate after the second quarter. 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?

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

As DJ mentioned, demand continues to be strong and is coming equally from local, regional and national tenants looking to expand their footprint. On the tenant side, store openings outpaced closings in 2023 by 2:1, and that trend is continuing into 2024. Given the favorable demand dynamics in the strip center space, we are committed to adding to our organic growth profile by securing annual contractual rent bumps and converting tenants to fixed CAM, both key factors to achieving stable long-term cash flow.

Turning to our operating results. We started 2024 by signing 41 leases for over 180,000 square feet with additional leases in our pipeline at various stages of negotiation. We executed leases with tenants such as [7 Brew, Sephora and Cavender's], which backfills at Bed Bath & Beyond space. We have one remaining Bed Bath & Beyond space with the replacement tenant identified and lease negotiations underway. Our total portfolio lease occupancy ended the quarter at an all-time high of 96.3%, up 10 basis points from last quarter. Our Anchor Space Leased Occupancy finished at 98.6%, an increase of 40 basis points from last quarter and our Small Shop Leased Occupancy ended the quarter at 92.1%. As of March 31, InvenTrust total portfolio ABR is $19.61, an increase of 2.6% compared to the first quarter of 2023.

For the quarter, we posted blended comparable leasing spreads of 11.2%, and spreads for new leases were 24.3% with renewals at 9.4% for the quarter. Our retention rate remains at 90% as we continue to see tenants renew their existing leases at meaningful increases. Our signed, not open, pipeline remains at 290 basis points as of the first quarter, representing nearly $8 million of annual base rent with 75% expected to come online at some point this year.
In closing, leasing demand has never been stronger. Our portfolio has and continues to prove its resiliency and ability to drive results. Operator, that concludes our prepared remarks, and you can open the line for questions.

Question and Answer

Operator

[Operator Instructions] And our first question today is from the line of Dori Kesten of Wells Fargo.

Dori Lynn Kesten
Wells Fargo Securities, LLC, Research Division

You made good headway today on your net acquisition guide. Can you talk generally about the kind of deals you're underwriting today, the amount that you're seeing versus maybe 3 months ago? And then just any shifts in pricing or competition you've seen of late. .

Daniel Joseph Busch
CEO, President & Director

Yes. Sure. I'm going to let Dave start, and then I'll add some color maybe at the end. Go ahead, Dave.

David Heimberger
Senior VP & Chief Investment Officer

Yes, sure. So I'll start with volume. It's improved. There's more options for us to underwrite. So at any point in time, we look at the pipeline, it could have $300 million or $500 million of options. It's more towards the higher end at the moment. So we've been really active underwriting, obviously, being very sensitive and observing our cost of capital, trying to make sure we're targeting appropriate IRRs. On the 2 deals that we mentioned in the press release or the earnings release, those sort of fit that mold again. One in Phoenix, we talked about last quarter, but just to recap, again, Chandler, great wedge of growth -- Phoenix Sprouts-anchored, so again, has of that specialty grocer component to it. And then Moores Mill, very unique piece of real estate in Atlanta is sort of very complementary to what we already own there, very high-performing Publix and we continue to see what we think will be significant rent growth over time.

So again, two deals added. The pipeline is full. We're very active. We're closing on that $75 million goal. Obviously, that's a marker that we want to achieve this year. There's more options but obviously sensitive to our cost of capital before exercising any more external growth levers.

Daniel Joseph Busch
CEO, President & Director

And I think, Dori -- it's DJ. The most important part is the way we think about the $75 million, it's a point in time based on where our cost of capital is, obviously, we would hope as most people in the sector that it was a little bit stronger today because there are some opportunities out there. So I wouldn't expect if the environment stays the same for us to go materially over that. What we could see is if there are opportunities out there, we could use perhaps and we've talked about it a lot. There's a couple of properties we could use as a rotation of capital and use those as a source of proceeds if we find some other interesting opportunities in our markets.

Dori Lynn Kesten
Wells Fargo Securities, LLC, Research Division

Okay. And are you able to give the cap rate for the Atlanta acquisition?

Daniel Joseph Busch
CEO, President & Director

No. So without giving the specific cap rates, I would just tell you that we're still able to get to our unlevered IRR targets, which, call it, is anywhere in the low to mid-7s. So that's kind of how we're looking at it from an underwriting perspective. Both Atlanta and Phoenix, we were able to get to that level.

Dori Lynn Kesten
Wells Fargo Securities, LLC, Research Division

Alright. And the last one is, can you just walk through what the key drivers were of the guidance range? [indiscernible]?

Michael Douglas Phillips

Executive VP, CFO & Treasurer

Yes, the guidance range for same property?

Dori Lynn Kesten
Wells Fargo Securities, LLC, Research Division

Yes, the guidance range.

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Yes. So base rent drove most of it, that's 220 basis points, and that's heavily influenced by 170 basis points of contractual rent bumps, which we still continue to be successful in getting, call it, in the 3% and sometimes up to 4%, especially in the Small Shops within -- where we're executing new deals. And then kind of as you walk down the line for quarter-to-date, we did have 280 basis points of contribution from net expense reimbursements. Our expenses were a little late this quarter compared to Q1 of 2023.

What you'll see throughout the year is that increase a little bit in the subsequent quarters and get us kind of to an operating expense comparable year-to-date last year, maybe slightly lower.

Operator

Our next question today is from the line of Jeff Spector of Bank of America.

Andrew Reale
BofA Securities, Research Division

This is Andrew Reale on for Jeff. First, just with an insubstantial amount of uncollectible rent and recoveries reported in the quarter. Just wondering why reaffirm 50 to 100 basis points of bad debt within guidance. And then just wondering, what do you have assumed for reserves in terms of Small Shop as well as your bigger box exposure to Rite Aid at this point in the year?

Daniel Joseph Busch
CEO, President & Director

Andrew, happy to provide a little bit more color. Obviously, we're trending at the lower end of that bad debt range. And it really comes -- the way we think about, I think the way that most of our peers have explained, it is on a net basis. So you do have some unforeseen fallout that you're capturing within that bad debt, that 50 to 100 basis points. And it can be offset by some surprises as it relates to out-of-period collection of rents, mostly from tenants that are on a cash basis. So what happened in the first quarter is we had the expected fallout that we -- that was implied in our guidance, but we actually got a couple of wins as it relates to prior period collection of rents.

Now we're not expecting much more out-of-period rents throughout the balance of the year, which is why we felt comfortable maintaining that range. But to your point, obviously, we have one Rite Aid. We have one [Joint Fabric]. So those are the primary retailers that have been in the news, those consist of, call it, 25 basis points, if you will. So, so far, the news has been good as it relates to those tenants for InvenTrust specifically. But there's still a process to be run through the bankruptcy. But if those tenants were to stay in, you could expect us to probably end the year at the low end of that range.

But with that being unknown and trying to be appropriately conservative, or I would say, pragmatic as it relates to our Small Shop tenants throughout the year, we felt okay to keeping that 50 to 100 basis point range.

Andrew Reale
BofA Securities, Research Division

Okay. That's helpful. And then just on the Small Shop Leased Occupancy saw that sequential decline after I think, reaching a record high last quarter. Still healthy, and we understand it's getting harder to push occupancy with the lack of available space, but just hoping to get a little more color on what drove the decline in the quarter? And then maybe what are you hearing from your latest leasing discussions with Small Shop tenants in particular?

Daniel Joseph Busch
CEO, President & Director

Yes. Maybe I'll just -- I'll start, and I'll hand it over to Christy to talk a little bit on the discussions we've been having. But really, if you think about the quarter 1, it was a more -- and I think we mentioned in the prepared remarks, it was a more normalized kind of level of fallout for our portfolio. It was about 60,000 square feet of tenants to put. And you can see this in the changes between Economic and Leased Occupancy. We've already released 30% of that space. We have another 50% of that space already with replacements at spreads that are [healthily] in the double digits. And then we're working on a de minimis amount of the space that's left. So that's why you saw a contraction between the kind of the Economic Leased Occupancy.

But to your point, we do expect if the leasing environment holds and because we are still seeing some really nice activity on the Small Shop side, even with the minimal amount of space, we do expect to kind of climb that to surpass our high watermark by the end of the year.

Christy, do you want to talk about some categories that we're seeing some activity in?

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

Sure. I would just add that, in general, our Small Shop pipeline remains very healthy. We are actually taking opportunities where we do see some Small Shop failing or struggling be proactive in trying to release those with tenants that would add to the mix at our centers. And we're primarily seeing the demand driven by the quick [QSR] category, personal health and services, of course, the full service [indiscernible], but those are the main drivers of what's in our pipeline today.

Operator

[Operator Instructions] Our next question today is from the line of Paulina Rojas of Green Street.

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

And DJ, sector is today in a sweet spot, where supply is very limited, demand is strong and then you hear a lot of emphasis on your end. How bullish are you about the ability of landlords to push rents aggressively in the next 5 years? And in your answer, if you could somehow frame this level of enthusiasm, whether it's talking about rent growth or NOI growth trend, something to help us compare for what is ahead.

Daniel Joseph Busch
CEO, President & Director

No, Paulina, it's a great question. I think I tried to get to it anecdotally, and I think we've talked about several quarters that the lack of supply -- there's very, very minimal new construction starts in retail because the construction cost to do -- for new developments just remains much, much too high. But because of the long lead times in multi-tenant, open-air retail, the amount of time it takes to get many of these things built, two, if not three years, at least, it sets up for strong fundamentals from our perspective for the next several years.

Because even in the next 2 or 3 years, unless we are in an environment where you can flip the development, switch back on. And there are developers that are -- that want to put shovels in the ground. They just can't. And we don't see that changing in a material way anytime soon. So the supply side, we're very bullish on. And it's really the institutional quality supply is what is most limited. And we're not seeing tenants trade down for lower quality or we call it, B quality space. So I think that's why most of the folks are almost all the folks in the institutional or public market, feel really strong about their portfolio positioning as it relates to the markets that they're operating in.

Now the one caveat to that is obviously inflation, where the economy is going and making sure that we're not pushing rents to set our tenants up for failure. I think that's why InvenTrust and many of our peers have not shifted gears but being much more careful with capital growing into the spaces, pushing rent appropriately, but then setting ourselves up for sustainable growth through better escalations, both on the base rent side and the CAM expense side. So those 2 pieces, I think, set us up very well for sustained NOI growth. And then it's just up to us. And so it's really to an extent [out] of our control to make sure we're financing our businesses appropriately.

But there are interest rate headwinds, at least on the short end of the curve, that will probably curtail cash flow growth a little bit, but I would expect same property [indiscernible] NOI growth to remain more robust than what we've seen in the past in the space. And then the better companies to be able to pass that through our free cash flow growth as well.

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

Okay. How do you think about retailer cyclicality within this discussion about demand? Because once -- yes, demand is strong, but this business is cyclical. And in a way, normal tenant failure could take care of that lack of supply.

Daniel Joseph Busch
CEO, President & Director

It's a good question. And I think that's why we're always trying to perfect the merchandise mix, but that merchandise mix is always going to change. I do think the structural change in shopping habits or 12 times and frequency of visits in the open-air community center or grocery [indiscernible] tenant space has changed almost permanently because of COVID and because of the hybrid work environment. There are services that are doing better today than -- and they will continue to do better in the years to come post-COVID than probably they ever would have done pre-COVID because of the amount of -- the frequency of visits and the changing of habit for the consumers.

And that specifically relates to QSR, full-service restaurants and the medical services and beauty. Those particular categories had a structural change in how people are visiting because they're not going to the office 5 times a week, in most cases, certainly in our markets. And it gives them more time and opportunity to spend time at our centers. So no doubt, there's a cyclical nature of our business. There's no question that there's going to be tenants that fail, whether it's because it's a failed business model or whatever it may be. And we're always monitoring those tenants. But I do think there's categories that have structurally benefit and that should continue.

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

And the last question. During the quarter, if I'm right, I saw that you had a mature benefit from net expenses. And I think we were expecting some of that because of fixed CAM but it was more than we thought. Is there any expectation of this normalizing any seasonality in these numbers that I'm seeing?

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Yes. Some of it -- this is Mike, Paulina. Some of it's timing. I would expect that throughout the year, like I said earlier, to kind of flatten out in subsequent quarters, and our expenses will end up slightly lower or about where we ended up in 2023.

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

Okay. But in terms of the full year, this should be a contribution to same-property NOI growth...

Michael Douglas Phillips
Executive VP, CFO & Treasurer

Yes, it won't be the 280 basis points that we had in Q1, but it will be closer to 150 basis points. And a lot of that too is because we are getting a little bit higher tenant recovery this year because our expenses will be down a little bit, but we also have between 40% and 45% of our portfolio on fixed CAM now. So we are getting 4% to 5% bumps on our fixed CAM when we signed them with new tenants.

Operator

[Operator Instructions] We have no further questions in the queue at this time. So I'd like to hand back to DJ Busch for any closing remarks.

Daniel Joseph Busch
CEO, President & Director

Thank you, everyone, for joining us. If you have any additional questions, feel free to reach out to Dan Lombardo. Otherwise, we look forward to seeing you guys in the coming months, either at ICSC or in New York City. Have a great rest of your day. .

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