Dexus Convenience Retail REIT (ASX:DXC)

ASX release

7 August 2023

Result underpinned by resilient portfolio and active capital management

Dexus Convenience Retail REIT (DXC) today announced its result for the year ended 30 June 2023, confirming a distribution of 21.6 cents per security.

Summary

- **Delivered FY23 guidance** with Funds From Operations (FFO) and distributions per security of 21.6 cents[1]
- **Statutory net loss after tax of $8.4 million**, impacted by $41.3 million of asset devaluations reflecting a 5.0% decline on prior book values
- **Achieved solid property income growth with an average rent review of 3.7% for the period** and like-for-like net operating income growth of 2.7%
- **Strengthened capital position** with pro forma gearing of 31.8%[2], and FY24 average hedging expected to be above 70% following contracted asset sales and incremental hedging[3]
- **Maintained a long weighted average debt maturity of 4.2 years** with no debt maturities until FY26[4]
- **Expanded divestment program delivering $52.3 million of proceeds[5]**, reflecting 7% of the portfolio at an average 2.5% discount to prior book values**,** while enhancing overall portfolio quality and operating performance metrics

Jason Weate, DXC Fund Manager said: "We are pleased to have delivered guidance for Security holders while continuing to deliver resilient top line growth, underpinned by some of the highest-quality tenant covenants in the market. We continued to pursue asset divestments to further strengthen our balance sheet and enhance the strategic positioning of the portfolio."

Strategy

"Today's result demonstrates the positioning of our portfolio, to provide investors with defensive income with embedded growth.

"We have delivered on our strategic objective to further strengthen DXC's capital position via an expanded divestment program, executing on $52.3 million[5] of disposals at attractive pricing for our investors.

"This reflects a strong outcome in a subdued market, reducing pro forma gearing to below the midpoint of our target 25 to 40% target range[2] and lowering exposure to floating rate debt, as well as improving overall portfolio quality with 42% of asset sales in regional locations.

"We will continue to actively manage the portfolio and balance sheet to position the vehicle for long-term growth opportunities for Security holders."

Financial result

DXC delivered on FY23 guidance with FFO of $29.8 million, or 21.6 cents per security[1]. The result represents a 5.3% decline on the prior year, reflecting like-for-like net operating income growth of 2.7% and a full period contribution from acquisitions undertaken in HY22 being more than offset by higher floating interest rates.

The statutory result reflected a net loss after tax of $8.4 million, compared to the prior year's net profit after tax of $82.6 million, primarily driven by $41.3 million of investment property valuation declines, compared to valuation gains of $30.8 million in the prior year.

DXC had 82 of its 105 investment properties independently valued during the year, with the remainder subject to internal valuations. The external and internal valuations resulted in a 5.0% decrease on prior book values, contributing to NTA per security decreasing by 28 cents, or 6.9%, to $3.75.

Divestments have reduced gearing from 35.0% to 31.8% on a pro forma basis[2], below the mid-point of the target range of 25 – 40%. Average FY23 interest rate hedging of 64% is expected to increase to over 70% in FY24 following contracted asset sales and incremental hedging[3], while the weighted average hedge book maturity remains strong at 4.1 years. Active extension of debt facilities has preserved a long weighted average debt maturity of 4.2 years[4], with no debt expiries until FY26.

Property portfolio and asset management

DXC's property portfolio includes 105 assets valued at $781 million. The portfolio is diversified by geography, tenant and site type.

The portfolio is 85% weighted (by value) to metropolitan and highway assets, with regional properties comprising the remainder. Metropolitan and highway assets benefit from higher levels of traffic flow and offer greater flexibility to explore alternate land usage to support the consumer trend towards greater convenience retail spend per visit.

The portfolio weighted average capitalisation rate has expanded by 36 basis points over the past 12 months to 6.10% reflecting the broader increase in interest rates.

Portfolio occupancy of 99.4% is underpinned by experienced national and global tenants, with 88% of rental income derived from 10 major tenants. The portfolio has a weighted average lease expiry of 9.7 years with 89% of income expiring in FY30 or beyond, providing strong income security and visibility.

The portfolio consistently generates organic rental growth with average rent reviews of 3.7% achieved for the year. The portfolio generates 75% of income from fixed rental increases, while 25% is from CPI escalations with approximately half of these subject to caps of 3 to 4%.

Environmental, Social and Governance (ESG)

DXC remains focused on driving long-term portfolio resilience. Approximately 12% of the portfolio's income is derived from non-fuel tenants.

DXC sources 100% renewable electricity for its managed portfolio assets and continues to work with tenants on their emission-reduction strategies, including progressing the rollout of onsite solar across 22 properties leased to Chevron.

Throughout the year, DXC progressed planning for the uncommitted Glass House Mountains fund-through development and has been focused on ensuring that sustainability initiatives are embedded into the project design including electric vehicle charging stations, rooftop solar and rainwater harvesting.

DXC will continue to leverage and align with Dexus's Sustainability Strategy to support long-term value creation.

Overview and outlook

DXC is well placed and will retain its focus on generating defensive income with embedded growth for its investors through:

- preserving portfolio attributes that deliver certainty of income
- maintaining a prudent capital structure (including enhancing balance sheet strength through exploring additional asset sales)
- an active approach to portfolio optimisation (including a disciplined approach to capital allocation and growth opportunities), and
- benefiting from Dexus's capabilities across transactions, development and asset management.

In addition, DXC expects continued relative valuation resilience for service station and convenience retail assets due to their predictable cash flows, strong tenant covenants and a weighted average cap rate that provides a positive spread against the marginal cost of debt.

DXC provides FY24 guidance for FFO and distributions of 20.7 – 21.1 cents per security, reflecting an attractive distribution yield of over 8%[6]. Guidance has been provided based on property income growth supported by contracted rental increases, current interest rate expectations and barring unforeseen circumstances (average floating interest rate (90-day BBSW) range of 4.25% – 4.75% and no further transactional activity).

Authorised by the Board of Dexus Asset Management Limited

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About Dexus Convenience Retail REIT

Dexus Convenience Retail REIT (ASX code: DXC) (formerly APN Convenience Retail REIT (ASX code: AQR)) is a listed Australian real estate investment trust which owns high quality Australian service stations and convenience retail assets. At 30 June 2023, the fund's portfolio is valued at approximately $781 million, is predominantly located on Australia's eastern seaboard and leased to leading Australian and international convenience retail tenants. The portfolio has a long lease expiry profile and contracted annual rent increases, delivering the fund a sustainable and strong level of income security. The fund has a conservative approach to capital management with a target gearing range of 25 – 40%. Dexus Convenience Retail REIT is governed by a majority Independent Board and managed by Dexus (ASX code: DXS), one of Australia's leading fully integrated real asset groups, with over 35 years of expertise in property investment, funds management, asset management and development. www.dexus.com

Dexus Asset Management Limited (ACN 080 674 479, AFSL No. 237500) (the "Responsible Entity") is the responsible entity and issuer of the financial products in respect of Convenience Retail REIT No. 1 (ARSN 101 227 614), Convenience Retail REIT No. 2 (ARSN 619 527 829) and Convenience Retail REIT No. 3 (ARSN 619 527 856) collectively the Dexus Convenience Retail REIT (ASX code: DXC) stapled group. The Responsible Entity is a wholly owned subsidiary of Dexus (ASX code: DXS).

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[1] The Directors consider the Property Council of Australia's (PCA) definition of FFO to be a measure that reflects the underlying performance of the Group. FFO comprises net profit/loss after tax attributable to stapled security holders, calculated in accordance with Australian Accounting Standards and adjusted for: property revaluations, derivative mark-to-market impacts, fair value movements of interest bearing liabilities, amortisation of tenant incentives, gain/loss on sale of certain assets, straight line rent adjustments, non-FFO tax expenses, certain transaction costs, one-off significant, movements in right-of-use assets and lease liabilities, rental guarantees and coupon income.
[2] Pro forma for the sale of 656 Bruce Highway, Woree, QLD, 1182 Chapman Road, Glenfield WA, 264 Browns Plains Road, Browns Plains, QLD and 323 North East Road, Hampstead Gardens, SA which are expected to settle post 30 June 2023. At 30 June 2023, gearing was 33.4%.
[3] Based on existing hedges in place as at 30 June 2023 and assuming no further transactional activity.
[4] Pro forma for $30 million facility extension that occurred on 31 July 2023.
[5] Includes the sale of 656 Bruce Highway, Woree, QLD, 1182 Chapman Road, Glenfield WA, 264 Browns Plains Road, Browns Plains, QLD and 323 North East Road, Hampstead Gardens, SA for combined proceeds of $18.6 million to be received post 30 June 2023.
[6] Based on closing security price as at 4 August 2023.