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Dexus (ASX: DXS)

ASX release

9 February 2021

2021 Half year results – Focus on growth in capital efficient funds management business

Dexus today announced its results for the half year ended 31 December 2020, confirming a distribution of 28.8 cents per security.

Highlights

- Stable, independent asset valuations supported by the continued investment demand for quality assets enabled a **Net profit after tax** of $442.9 million. Although a strong result, this was down 55.5% primarily due to net revaluation gains being lower than those recognised in the previous corresponding period
- **Adjusted Funds from Operations (AFFO)** and **Distribution** of 28.8 cents per security, up 7.1% and 6.7% respectively on the previous corresponding period, primarily driven by trading profits
- **Rent collections** were at 96.0% for the Dexus portfolio in the six months to 31 December 2020
- **Gearing** (look-through)[1] remains conservative at 24.9%
- $1.7 billion of **cash and undrawn debt facilities**
- **Continued leadership in environmental, social and governance performance** through Dexus retaining its number 1 position for the global real estate industry on the Dow Jones Sustainability Index, and maintaining a leading position in GRESB and on the CDP Climate A list
- **All funds performing** with Dexus Wholesale Property Fund (DWPF) continuing to outperform its benchmark across all time periods and Healthcare Wholesale Property Fund (HWPF) achieving an exceptional one-year return of 15.3%
- **Launched** the marketing of unlisted opportunity fund**, Dexus Real Estate Partnership 1 (DREP1)**
- Raised circa $287 million of **equity for existing unlisted funds**
- **High occupancy**[2] of 96.0% for the Dexus office portfolio and 95.5% for the Dexus industrial portfolio
- **Achieved 140 basis points of outperformance in the Dexus office portfolio** relative to the relevant MSCI/PCA benchmark[3] over the year to 30 September 2020, driven by the quality of the portfolio
- **Completed $248 million of developments**
- **Progressed planning for city-shaping projects** in the group's $11.4 billion development pipeline
- **Realised $47.1 million of trading profits** (post tax) in HY21 while contracting future trading profits

The COVID-19 pandemic continues to cloud the outlook for the operating environment as a number of clusters emerged across Australia over the holiday period. Globally however, Australia has performed very well in suppressing the transmission of the virus through various restrictions, supporting the return to a sense of normality across the general population. The imminent roll out of the vaccine, as well as the impact of both fiscal stimulus and historically low interest rates, are supporting economic activity, with both business and consumer confidence returning to pre-COVID levels.

Dexus Chief Executive Officer, Darren Steinberg said: "Despite the widespread impact of the pandemic, the first half of FY21 has been characterised by increased leasing activity, relatively strong rent collections, initiatives to grow our funds management business and the selective recycling of assets. Our high quality portfolio, the strength of investment demand for quality assets, and our platform capabilities will enable us to drive performance in this next stage of the real estate cycle."

Strategy

Darren Steinberg said: "We have been active in growing our business while maintaining a strong balance sheet. Since 2012 we have successfully grown our total funds under management to $32.1 billion, through transactions, developments and favourable asset valuations, while at the same time recycling $11.6 billion through asset sales.

"The pandemic has reinforced the importance of having a diversified business model and strategy that can deliver through the cycle, demonstrated by our strong cash flow and resilient asset values. Our agile and high performing workforce will take advantage of the changed market conditions by focusing on strategic initiatives that will help us unlock the relative value of our business and strengthen the platform for the future.

"These strategic initiatives include **increasing the resilience of portfolio income streams, expanding and diversifying the funds management business** and **progressing the group development pipeline**.

"In the year ahead, this will see us continue to implement active leasing strategies to maximise office portfolio cash flow generation, increase weightings toward sectors with strong tailwinds and expand our flexible workspace offering. We will also look to make changes to simplify the corporate structure of the group[4]."

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Financial result

Dexus's net profit after tax was $442.9 million, a decrease of $551.3 million or 55.5% from the previous corresponding period. The reduction in net profit was primarily driven by net revaluation gains of investment properties of $160.8 million, which were $563.6 million lower than the previous corresponding period.

At 31 December 2020, 111 of Dexus's 122 office and industrial properties were independently valued by external valuers. Most of the valuation uplift was seen across the industrial portfolio which increased by 4.8%, with the office portfolio remaining in line with prior book values as a result of softer valuer assumptions, offset by successful leasing at some assets.

Valuation gains across the total property portfolio for the period to 31 December 2020 contributed to the 10 cent or 0.9% increase in net tangible asset (NTA) per security to $10.96 at 31 December 2020.

The total property portfolio weighted average capitalisation rate tightened 4 basis points over the period to 5.01%. The weighted average capitalisation rate of the Dexus office portfolio tightened 2 basis points from 4.97% at 30 June 2020 to 4.95% at 31 December 2020, and for the Dexus industrial portfolio tightened 30 basis points from 5.66% at 30 June 2020 to 5.36% at 31 December 2020.

Underlying Funds from Operations (FFO) per security of 30.1 cents, which excludes trading profits, reduced by 5.6% as a result of the impact of rent relief provided, divestments including the second tranche of the Dexus Australian Logistics Trust (DALT) portfolio, and a reduction in the contribution from management operations.

AFFO and distribution per security of 28.8 cents was up 7.1% and 6.7% respectively on the previous corresponding period primarily due to the amount and timing of the receipt of trading profits in the first half of FY21. The distribution payout ratio remains in line with free cash flow in accordance with Dexus's distribution policy. The distribution will be paid to Dexus Security holders on Friday, 26 February 2021.

Rent collections were at 96.0% for the Dexus portfolio in the six months to 31 December 2020.

As part of Dexus's active approach to capital management and in response to security price volatility, Dexus continued its on-market securities buy-back program to acquire up to 5% of Dexus securities on issue. In the six months to 31 December 2020, 2,147,026 Dexus securities were acquired on market as part of this buy-back. To date, in FY21, Dexus has bought back circa 5 million Dexus securities at pricing ranging from $8.65-$9.04, resulting in 1,086,065,010 securities on issue as at 9 February 2021.

Dexus continued to maintain a strong and conservative balance sheet with gearing (look-through)[1] at 24.9%, well below the target range of 30-40%, and $1.7 billion of cash and undrawn debt facilities.

Chief Financial Officer, Alison Harrop said: "The extension of the National Commercial Code of Conduct[5] in some States and the continued economic impacts of the pandemic are expected to have a moderate impact on property portfolio income over the coming months, however this has already been assumed in our full year FY21 guidance for distribution per security.

"We continued to selectively recycle assets, receiving the proceeds from the sale of 45 Clarence Street, Sydney in late December 2020. We also utilised the on-market securities buy-back and will buy back securities when we see the opportunity to enhance returns for Security holders."

Dexus has manageable debt expiries over the next 12 months and remains within all of its debt covenant limits, retaining its credit ratings of A-/A3 from S&P and Moody's respectively.

Funds Management

Dexus manages $15.6 billion of funds across its diversified funds management business, which includes eight vehicles.

All funds and partnerships have performed well despite the market conditions with DWPF continuing to outperform its benchmark over one, three, five, seven and ten years. HWPF continued to deliver strong performance, achieving an exceptional one-year return of 15.3%.

Executive General Manager, Funds Management, Deborah Coakley said: "We are making progress on growing our relationships with existing and new third party capital partners, progressing discussions with a number of investors for our new unlisted opportunity fund."

During the period, Dexus made an initial approach on behalf of DWPF to the Responsible Entity of the AMP Capital Diversified Property Fund (ADPF), in response to ADPF investor encouragement, to consider a merger of ADPF with DWPF. Discussions continue to progress with the advisers of the Responsible Entity of ADPF, on a proposal for consideration by both sets of investors.

DWPF also sold 452 Flinders Street, a 22-level A-grade tower in the Melbourne CBD, for $454 million[6] representing an 11% premium to book value at 30 June 2020 and highlighting the resilience of prime grade office values.

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Dexus and HWPF acquired (in 50/50 co-ownership) the Australian Bragg Centre in Adelaide, which is currently under development. The Australian Bragg Centre is a state-of-the-art clinical and research facility housing Australia's first proton therapy unit specialising in next generation cancer treatment. This transaction is consistent with Dexus's priority to accelerate opportunities to expand the funds management business and provides greater exposure to a growing asset class. On completion, this transaction will increase the group's exposure to healthcare assets to over $1 billion.

Environmental, Social and Governance (ESG) update

From an environmental perspective, during the period Dexus continued to manage its properties for emissions reductions supporting the group's net zero by 2030 commitment and progressed its healthy buildings initiative. This initiative is focused on adopting proven technologies to enhance the air quality in our buildings and provide a touchless experience.

Dexus also leveraged its partnership with Taronga Ventures to identify new technologies that can assist in reducing carbon emissions and became a founding member of the Australian Climate Leaders Coalition.

Dexus was again acknowledged as a global ESG leader, retaining its position on a several ESG benchmarks, including:

- Being recognised in the 2020 Principles of Responsible Investment (PRI) Leaders' Group. Dexus achieved the maximum score available, effectively demonstrating how it integrates ESG across its management platform to manage risks and create long-term value for its investors
- For the second consecutive year, retaining the number 1 position globally in the real estate industry for the Dow Jones Sustainability Index
- Retaining a position on the 2020 CDP Climate A List
- Being recognised by sustainability benchmark GRESB, with the Dexus Office Trust named as the Global Sector Leader for Listed Office, DWPF named as the Regional Sector Leader for Diversified Office/Retail (Oceania) and HWPF, which participated for the first time, named as a Global Development Sector Leader for healthcare entities

Darren Steinberg said: "This recognition is testament to our people and the way ESG is embedded and integrated across our business - it is part of our DNA."

Property portfolio

Dexus Office Portfolio

Dexus manages a high-quality $22.5 billion group office portfolio, $13.8 billion of which sits in the Dexus portfolio.

Key metrics	31 December 2020	30 June 2020
Occupancy by income	96.0%	96.5%
Weighted average lease expiry (by income)	4.2 years	4.2 years
Average incentives[7]	22.0%	17.1%
Weighted average cap rate	4.95%	4.97%

During the six months to 31 December 2020, Dexus leased 93,691 square metres[8] of office space across 135 transactions, in addition to 7,179 square metres[8] of space across 16 transactions at office developments.

Executive General Manager, Office, Kevin George said: "In an environment where global economies are still in lockdown, we are seeing activity levels increasing in Australian cities with people returning to CBDs and our buildings. The commentary on working from home versus the office continues, but the impact on both near term and longer-term leasing demand is still not clear. Increased flexibility for employees was a pre-pandemic trend that has now accelerated. We've however had a busy six-month period of leasing and our experience across those deals completed shows the office footprint is substantially unchanged.

"The portfolio has performed well in the six months with occupancy at 96.0% (up from 95.4% at 30 September 2020), following the completion of 151 deals representing 6.2% of the portfolio by area.

"The uncertainty created by COVID-19 delayed some decision making, particularly in Melbourne, where inspections of commercial premises have only until recently been prohibited under the extended lockdown. As a result, we expect that the Melbourne office market will be challenging over the short term.

"We have been working on the evolution of office for more than six years – well before the onset of COVID-19. We identified the future of office involved more flexibility and we've been evolving our platform offering to increase the relevance to our customers. We are well positioned to expand our flexible products and services to meet the needs of our customers in a post-pandemic world."

Face rents remain largely unchanged in the core CBD markets; however effective rents are under pressure as incentives continue to increase. Given the better than expected market occupancy levels and strength of key leading indicators, Dexus expects incentives to moderate in some markets over the next 12 months.

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Office portfolio like-for-like income growth was +1.5% (FY20: +4.7%), excluding the impact of rent relief measures and provisions for expected credit losses (including these impacts: HY21 -4.6% and FY20 +2.4%). The Dexus office portfolio delivered a one-year return of 3.6% at 31 December 2020 and outperformed its benchmark over the one, three and five-year time periods to 30 September 2020.

After an uncertain year for office markets, an improvement in many of the key leading indicators signals a period of strengthening demand ahead. The indicators include:

- Business conditions were at their highest level since 2018 in the December 2020 NAB Business Survey
- Professional job advertisements, an indicator of corporate hiring intentions, are up 31% since June 2020
- Employment in white collar industries has grown by 2.5% over the past 12 months.

Dexus Industrial Portfolio

Dexus manages a growing, high-quality $5.5 billion group industrial portfolio, $2.4 billion of which sits in the Dexus portfolio.

Key metrics	31 December 2020	30 June 2020
Occupancy by income	95.5%	95.6%
Weighted average lease expiry (by income)	4.3 years	4.1 years
Average incentives	19.7%	13.4%
Weighted average cap rate	5.36%	5.66%

During the six months to 31 December 2020, Dexus leased 168,749 square metres[8] of industrial space across 46 transactions. Portfolio occupancy remains high at 95.5%.

Executive General Manager, Industrial, Retail and Healthcare Stewart Hutcheon said: “Tenant demand for high quality logistics facilities in precincts that are well located near major transport hubs, continues to drive leasing success across our industrial portfolio. We are working closely with our industrial customers to support their growth across Australia.”

Industrial portfolio like-for-like income growth was +1.0% (FY20: +0.1%) excluding the impact of rent relief measures and provisions for expected credit losses (including these impacts: HY21 -1.0% and FY20 +2.1%). The Dexus industrial portfolio delivered a one-year return of 12.8% to 31 December 2020 and outperformed its benchmark over the three and five-year time periods to 30 September 2020.

Developments

Dexus’s group development pipeline now stands at a cost of $11.4 billion, of which $5.8 billion sits within the Dexus portfolio and $5.6 billion within third party funds. Dexus group has circa $200 million remaining to spend on its committed development projects to FY22, including the Australian Bragg Centre.

Chief Investment Officer, Ross Du Vernet said: “During the period, $536 million of projects were added to our group committed development pipeline including the acquisition of the Australian Bragg Centre and the Ford Facility at Merrifield Business Park, and increasing the scale of existing industrial development projects underway, including the Amazon facility at the Horizon 3023 Estate at Ravenhall. We also made further progress across our city shaping developments, receiving DA approval for Waterfront Brisbane and progressing through Stage 3 of the USP at Central Place Sydney. We have the flexibility to activate these projects at the right time, subject to a level of tenant pre-commitment.”

During the period, development projects at 180 Flinders Street and the 80 Collins Street (hotel component) in Melbourne were completed, in addition to 9 Custom Place at Truganina in Victoria.

Construction continues across 227,000 square metres of industrial development projects at Ravenhall, Richlands and South Granville owned by Dexus and its third party capital partners, where 90,427 square metres of leasing was secured during the period.

In the current environment, Dexus has reduced risk relating to the uncommitted city shaping developments because the existing assets on these sites are currently income producing and the majority are owned in partnership with third party capital partners, enabling Dexus to progress planning and enhance the optionality of these projects.

Transactions and trading

Dexus had an active start to FY21, announcing $2.8 billion of contracted transactions across the group, including acquisitions and divestments in the six months to 31 December 2020.

In December 2020, Dexus settled on the sale of its 100% interest in 45 Clarence Street, Sydney realising $530 million[6], progressing the optimisation of the portfolio composition through asset recycling.

Dexus also conditionally entered into sale agreements (subject to FIRB approval) to sell a 100% interest in 60 Miller Street, North Sydney and a 50% interest in Grosvenor Place, Sydney in which Dexus holds a 37.5% interest (including Dexus’s 25% direct interest and the Dexus Office Partnership 12.5% interest).

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Dexus Chief Investment Officer, Ross Du Vernet said: ‘‘We are seeing lots of opportunities in the current market and will selectively recycle assets where we can maximise returns. The success we have had in recycling assets will further strengthen our balance sheet and enable Dexus to organically fund higher return growth initiatives in our funds management and development businesses.”

From a trading profit perspective, Dexus realised $47.1 million (post tax) of trading profits in the six-month period through:

- Exercising the option to sell its remaining 25% interest in 201 Elizabeth Street, Sydney which settled in August 2020
- Entering into agreements to sell a portfolio of six trading assets (Truganina VIC and Lakes Business Park South, Botany NSW) to the Dexus Australian Logistics Trust (DALT) across two tranches, with the first tranche settling in October and December 2020 respectively
- Continuing to progress the North Shore Health Hub development with project completion expected in the third quarter of FY21

In addition, Dexus entered into put and call agreements to sell 436-484 Victoria Road, Gladesville which can be exercised in FY21 or FY22.

These trading profit related transactions (including the North Shore Health Hub) are expected to contribute circa $95 million to trading profits (pre-tax) across FY21 and FY22.

Summary and outlook

Darren Steinberg said: “We expect the impacts of the COVID-led recession will continue to flow through the Australian economy in 2021 and despite the imminent vaccine roll out, governments will need to learn to live with COVID-19 being part of the community. Business owners and operators require consistent rules and regulations to ensure that the domestic economy returns to sustainable levels of growth and minimising border restrictions will further assist in Australia’s COVID-19 recovery.

“In this lower for longer interest rate environment, we believe that the desire for secure income streams will fundamentally benefit direct asset classes and in particular quality real estate assets.

“Fortunately, we have a fully integrated real estate platform with direct exposure to high quality real estate in diverse and key performing markets that has a track record of delivering solid returns over the long term.

“Our funds management business provides a capital efficient way to increase our presence in high growth sectors and the activation of our city-shaping development pipeline has embedded long-term value and provides the opportunity to organically grow at the appropriate time.”

“Questions remain on the impacts of working from home on the office sector, however we are confident that the office will remain a core part of our customers’ needs and have been preparing for increased flexibility for many years.”

Dexus expects an FY21 full year distribution per security amount that is consistent with FY20 but is subject to there being no reinstatement of any major lockdowns or unforeseen circumstances. The FY20 full year distribution per security amount was 50.3 cents.

HY21 Results

This *ASX announcement* should be read in conjunction with the *HY21 Results presentation* and *HY21 Financial Statements* released to the Australian Securities Exchange today and available at www.dexus.com

Investor conference call

Dexus will hold an investor conference call at 9.30am (AEDT) today, Tuesday 9 February 2021, which will be webcast via the Dexus website (www.dexus.com) and available for download later today.

Authorised by the Board of Dexus Funds Management Limited

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1 Adjusted for cash and debt in equity accounted investments, excluding the impact of the contracted divestments of 60 Miller Street, North Sydney and Grosvenor Place, Sydney.
2 By income.
3 Period to 30 September 2020 which reflects the latest available PCA/MSCI Australian Quarterly Digest for Office Property benchmark.
4 Subject to Dexus Security holder approval.
5 The Code of Conduct is available at https://www.pm.gov.au/sites/default/files/files/national-cabinet-mandatory-code-ofconduct-sme-commercial-leasing-principles.pdf
6 Excluding transaction costs and settlement adjustments.
7 Excluding development leasing.
8 Including Heads of Agreement.

About Dexus

Dexus is one of Australia's leading real estate groups, proudly managing a high-quality Australian property portfolio valued at $32.1 billion. We believe that the strength and quality of our relationships will always be central to our success and are deeply committed to working with our customers to provide spaces that engage and inspire. We invest only in Australia, and directly own $16.5 billion of office and industrial properties. We manage a further $15.6 billion of office, retail, industrial and healthcare properties for third party clients. The group's $11.4 billion development pipeline provides the opportunity to grow both portfolios and enhance future returns. With 1.6 million square metres of office workspace across 51 properties, we are Australia's preferred office partner. Dexus is a Top 50 entity by market capitalisation listed on the Australian Securities Exchange (trading code: DXS) and is supported by more than 29,000 investors from 24 countries. With 36 years of expertise in property investment, development and asset management, we have a proven track record in capital and risk management, providing service excellence to tenants and delivering superior risk-adjusted returns for investors. www.dexus.com

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