Dexus Convenience Retail REIT (ASX:DXC)

ASX release

8 August 2022

Strong result in line with upgraded guidance

Dexus Convenience Retail REIT (DXC) today announced its results for the full year ended 30 June 2022, confirming a distribution of 23.1 cents per security.

Highlights

- **Statutory net profit** of $82.6 million, up 11.9% on the prior year, primarily driven by higher rental income from acquisitions and fair value gains on interest rate derivatives
- **Funds from Operations (FFO)** up $5.6 million, or 21.5%, to $31.5 million, supported by 2.3% like-for-like net operating income growth and the impact of acquisitions
- **Distribution per security of 23.1 cents**, up 5.5%, representing an FFO payout ratio of 100%
- **Strengthened capital position** through extending weighted average debt facility maturity to 4.2 years with 58% of debt hedged across FY22
- **15 acquisitions** totaling $168 million delivering enhanced portfolio quality with a long weighted average lease expiry of 10.3 years and average annual rent reviews of 3.3%[1]
- **Four divestments** totaling $13 million reflecting **an average premium to book of 3.8%[2]**, supporting capital recycling initiatives and reinforcing the high-quality nature of the underlying portfolio
- **Net Tangible Asset (NTA) of $4.03** up 9.6%, primarily driven by **$30.8 million of property valuation gains** with rental growth accounting for 47% of valuation gains
- **Purchased 1.4 million securities** as part of the on-market securities buyback program

Jason Weate, DXC Fund Manager said: "We delivered a solid financial result for the year in line with our upgraded guidance, demonstrating the resilience of the portfolio which provides income certainty backed by some of the highest-quality tenant covenants in the market. We promptly responded to changes in the economic environment by launching an on-market securities buyback program, pursuing asset sales and strengthening our capital position to support Security holder value over the long term."

Strategy

"Today's results demonstrate that we continue to deliver on our strategy of providing investors with a defensive income stream, further supported by our disciplined approach to capital allocation.

"We executed on 15 acquisitions during supportive market conditions with an appropriate cost of capital. These assets comprised strategically-located facilities that further diversify the tenant base, and were underpinned by a long weighted average lease expiry of 10.3 years and strong average rent reviews of 3.3% providing sustainable sources of property income growth through the cycle[1].

"We also divested four assets delivering an overall premium to book of 3.8%[2], crystallising gains for Security holders. The strong pricing achieved on sales reinforces the high-quality nature of the underlying portfolio, demonstrating the investor appeal in service station and convenience retail properties as a source of defensive and growing income.

"An increased focus on asset sales going forward will allow us to further enhance the quality of the portfolio and strengthen the balance sheet, while also providing optionality for capital redeployment, including potential further buyback of securities on-market following the 1.4 million securities already purchased at an average discount of 15% to NTA per security.

"We continue to work closely with tenants to enhance the long-term viability of their sites while also providing additional value to DXC and increased lease tenure."

Financial result

DXC reported a statutory net profit of $82.6 million for the full year ended 30 June 2022, up $8.8 million, or 11.9%, on the prior year, driven by higher rental income from acquisitions and fair value gains on interest rate derivatives.

FFO increased 21.5% to $31.5 million, supported by 2.3% like-for-like net operating income growth and contributions from recently acquired assets. On a per security basis, FFO increased 5.5% to 23.1 cents, reflecting the issuance of new securities to fund acquisitions during the period.

81 of DXC's investment properties were independently valued in the 12 months to 30 June 2022, with the remainder subject to internal valuations. Property portfolio valuation gains and fair value gains on interest rate derivatives contributed to the 36 cents, or 9.6%, increase in NTA per security to $4.03 as at 30 June 2022.

DXC raised a total of $56.3 million of new equity during the year, comprising $45.0 million via an institutional placement in August 2021, $10.5 million via a Securities Purchase Plan in September 2021 and $0.8 million via the Distribution Reinvestment Plan (DRP). The DRP is not currently in operation. The proceeds have assisted in funding acquisitions and have ensured that gearing remains within the 25 – 40% target range at 34.7%[3].

DXC's weighted average debt facility maturity was 4.2 years and its weighted average cost of debt remained favourable at 2.6% with 58% of DXC's debt hedged across FY22 and a weighted average hedge maturity of 3.8 years.

Property portfolio and asset management

DXC's property portfolio includes 112 assets valued at $850 million. The portfolio is diversified by geography, tenant and site type.

The portfolio is 83% 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 weighted average capitalisation rate for the portfolio is 5.74%, tightening 28 basis points over the past 12 months. During the year, the valuations of metropolitan assets increased 4.6% on prior book values, while highway assets remained flat and regional assets increased 4.8%.

Following significant transactional activity including 15 acquisitions and four recent divestments[2], DXC's income exposure to non-fuel tenants increased from 6% to 11%, with recent acquisitions focused on new-build assets reflecting an average age of 3.8 years. The portfolio has a weighted average lease expiry of 10.8 years with limited lease expiry risk prior to FY30, providing strong income visibility.

The portfolio generates strong organic rental growth with average rent reviews of 3.1% per annum[1]. 77% of rental income is subject to fixed increases, while 23% is linked to CPI escalations with half of these subject to caps of 3 - 4%.

The portfolio remains 99.7% occupied by income and is underpinned by reliable and experienced national and global tenants, with 89% of rental income derived from major tenants.

During the year, three new long-term lease deals were completed, including the introduction of a car wash operator on a 15-year lease at Redbank Plains, as well as extending the lease expiry for 7-Eleven at Redbank Plains from FY30 to FY37. Additionally, DXC also secured Liberty, who are wholly-owned by Viva Energy Australia, on a 15-year lease at the Lawnton site, extending the lease expiry at this site from FY22 to FY37.

Developments

During the year, DXC completed two fund-through development projects at Hillcrest, South Australia, and the Dubbo Service Centre (Stage 1), New South Wales which includes a strong retail offering in a Carl's Jr restaurant.

DXC also acquired Glasshouse Mountains Dual Service Centre in March 2022, which includes the potential for a fund-through development project to reposition the existing service stations and expand the retail offerings.

Environmental, Social and Governance (ESG)

DXC's portfolio is well positioned to ensure it remains resilient over the long term. Approximately 11% of the portfolio's income is derived from non-fuel tenants, while three sites across the portfolio offer electric vehicle charging stations.

DXC is progressing carbon neutral certification across its managed properties for the 12 months to 30 June 2022. Final certification is expected to be achieved post-reporting period as Dexus is in the final stages of quantifying DXC's greenhouse gas emissions over the financial year following the procurement of required renewable electricity and carbon offsets.

DXC supports its tenants' ESG aspirations and their continued investment in sustainability initiatives across the portfolio. During the year, DXC facilitated an agreement to rollout onsite solar at 29 Chevron sites in DXC's portfolio with works expected to begin in FY23.

DXC will continue to leverage and align with Dexus's Sustainability Approach to support long-term value creation, including through increased environmental auditing of all sites to better track sustainability performance.

Overview and outlook

While the macroeconomic environment is uncertain, DXC is well placed to continue to deliver strong relative performance. The portfolio comprises high-quality assets that offer sustainable sources of income growth, underpinned by long-term leases to major tenants with 3.1% average annual rental increases[1]. We expect strong investment appeal for real estate assets providing certainty of income.

Solid momentum has been achieved into FY23 and DXC will continue to actively pursue capital recycling initiatives to optimise the portfolio, repay debt and provide value-accretive redeployment optionality including potential further securities buyback activity.

DXC provides FY23 guidance of FFO and distributions ranging between 21.2 – 22.0 cents per security, based on property income growth supported by contracted rental increases, current interest rate expectations and barring unforeseen circumstances (assumes average floating interest rates of 2.75% - 3.75% (90-day BBSW) 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 2022, the fund's portfolio is valued at approximately $850 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 estate 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] Assuming long-term average CPI of 3.0%.
[2] Includes the sale of 656 Bruce Highway, Woree which exchanged on 19 July 2022 (settlement expected July 2024), as well as the sale of 2215 David Low Way, Peregian Beach which exchanged on 3 August 2022.
[3] Adjusted for cash. Reflects pro forma gearing for the sale of 2215 David Low Way, Peregian Beach which exchanged on 3 August 2022. Gearing as at 30 June 2022 was 35.0%.