Argosy

20 November 2018

MARKET RELEASE

ARGOSY 2019 INTERIM RESULT – BUILDING MOMENTUM

FOR THE 6 MONTHS TO 30 SEPTEMBER 2018

Argosy will present the 2019 interim results via a teleconference and webcast at 10am today. Please visit https://services.choruscall.com.au/diamondpass/argosy-880125-invite.html or dial **0800 122 360** and quote the conference **ID 880125**. It is recommended that you dial in or log in a few minutes before the start time. A copy of the webcast will be available on Argosy's website later in the day.

Argosy Property Limited ("Argosy" or the "Company") has reported its results for the 6 months to 30 September 2018.

Highlights

- **Net property income up 4.7%**
- **Net distributable income up 9.2%**
- **Net distributable income per share up 8.8%**
- **Revaluation gain of $34.6 million, an increase of 2.2% on book value**
- **Continued divestment of non Core assets significantly above book value**
- **Strong progress at 7 Waterloo Quay with very good enquiry from the Government sector for space in the building**
- **Acquisition of 11 Coliseum Drive, Albany and 133 Roscommon Road, Wiri**
- **Balance sheet is in good shape and we are considering longer term debt funding options**
- **Full year dividend of 6.25 cents per share expected in line with previous guidance**
- **Lift in NTA to $1.17 from $1.12 at the end of March.**

Peter Mence, Argosy's Argosy Chief Executive Officer said "With a strong FY18 platform as our base, we have started the first six months of the FY19 year very well. In the first six months of the financial year, Argosy has continued to improve the quality of the portfolio through acquisitions, tenant-led developments and the divestment of non Core assets. We are pleased to report that the metrics of the portfolio remain strong with occupancy at 98.4% and a weighted average lease term of 5.6 years.

We can also announce further progress at New Zealand Post House at 7 Waterloo Quay, Wellington. The reinstatement works for levels 1-4 and 7 are largely complete (apart from some further seismic work), with the balance of the damaged floors expected to be completed this financial year (except for level 12). Further details on this building are provided below."

Chairman Mike Smith said "We have commenced the 2019 year well. The management team has continued to reposition the portfolio and work hard on the operational elements of the business including resolution of lease expiries and addressing key vacancies. Strategic acquisition and divestment opportunities for Argosy have materialised and we have also continued to focus on organic growth opportunities. As signalled in May, we expect the full year dividend to be 6.25 cents per share for this financial year."

Financial Results

Statement of Comprehensive Income

Argosy reported net property income of $50.8 million for the period, which includes rental loss recoveries from insurers, and is 4.7% higher than the previous interim period. Lost revenue from divestments in the period has been more than compensated for by strong rental growth and leasing up of vacant space, notably at 82 Wyndham Street, Auckland.

Administration expenses were up $0.4 million on the previous interim period primarily due to restructuring costs and additional resourcing costs across the business.

Profit before interest, other gains/losses and taxes was $45.6 million, up 4.2% on the previous interim period.

Interest expense of $12.2 million was down $0.4 million on the previous interim period as the interest on higher average debt was offset by higher capitalised interest on developments.

An interim revaluation was undertaken by Argosy following evidence of improved market conditions since the last valuation date of 31 March 2018, and desktop valuations performed by Colliers International during the period. A revaluation gain of $34.6 million or 2.2% on previous book value, has subsequently been recorded.

The sale of Wagener Place, St Lukes, resulted in a significant gain of $2.9 million over book value.

Net profit after tax was $66.8 million for the period, compared to $23.1 million in the previous interim period.

Distributable Income

For the period ending 30 September gross distributable income[1] was $33.4 million which was 7.1% higher than the previous interim period. Gross distributable income per share for the period was 4.04 cents per share, compared to 3.79 cents per share in the previous interim period (up 6.6%).

Net distributable income increased by 9.2% to $28.7 million compared to the previous interim period, due primarily to improved net property income. Net distributable income per share increased 8.8% to 3.47 cents per share from 3.19 cents per share in the previous interim period.

Interim revaluations

The independent work performed and interim revaluation resulted in an uplift of $34.6 million, a 2.2% increase on book values immediately prior to the interim revaluation. As a result of the revaluation, Argosy's NTA has lifted to $1.17, up from $1.12 at the end of March.

The Company's portfolio following the revaluation shows a contract yield on values of 6.63% and a yield on fully let market rentals of 6.70%.

Portfolio Activity

Leasing and Rent Reviews

Underpinned by continued strength in Auckland and Wellington property market fundamentals, Argosy has delivered strong leasing and rent review results over the first half of the year. During the interim period, 24 lease transactions were completed on 39,500sqm of net lettable area, including 16 new leases, seven renewals and one extension.

Significant leasing transaction successes over the first half of the financial year include:

320 Ti Rakau Drive, East Tamaki, Auckland	*Bunnings Limited*	*10 years*
Albany Lifestyle Centre, Albany, Auckland	*E Road Limited*	*9 years*
Albany Lifestyle Centre, Albany, Auckland	*Peterken Enterprises Limited*	*6 years*
Albany Mega Centre, Albany, Auckland	*Outdoor Holdings Limited*	*6 years*

There has been some progress in leasing the vacant floors at 23 Customs Street, Auckland. Levels 2, 14 and part 13 are now leased and there is strong enquiry on the remaining floors (levels 6, 7 and part 13).

Argosy's weighted average lease term at 30 September decreased to 5.6 years compared to the 6.1 years at the end of March 2018. This movement reflects the adjusted arrangements with New Zealand Post at 7 Waterloo Quay which are discussed in more detail in the 7 Waterloo Quay update below.

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[1] Profit before tax and distributable income are alternative performance measures used to assist investors in assessing the Company's underlying operating performance and to determine income available for distribution to shareholders. Note 14 of the financial statements released today provides a full reconciliation between profit before tax and distributable income.

Argosy has maintained a very high occupancy level over the interim period and occupancy was 98.4% at 30 September 2018 compared to 98.8% at the end of March.

During the first six months, a total of 42 rent reviews on $15.5 million of existing rental income were completed. Rental growth of 3.4% was achieved or 3.1% on an annualised basis on all rents reviewed. Across the rental increase, the industrial portfolio accounted for 57% of the total rental uplift on 50% of the rent reviewed (9 reviews). This continued strong rental growth has been a key contributor to the improvement in net property income in the interim period.

Approximately 57% of all rents reviewed (by income) were fixed reviews, 14% were market reviews and 29% were CPI based.

Acquisitions and Value Add Developments

Ongoing tightness across the property market continued in the first half of this financial year. Despite this, opportunities have emerged during the period to make strategic acquisitions.

In September, Argosy acquired 11 Coliseum Drive in Albany (The Warehouse), for $26.4 million. This property is contiguous to the Argosy owned Albany Mega Centre and comprises 7,600sqm of warehouse, 760sqm of office, mezzanine and garden centre and 413 carparks. The lease had 6.5 years to run on the initial 12-year lease. The purchase allows us to now consider a range of organic growth options across the entire Albany Mega Centre site. Longer term, we are optimistic about the opportunity and value this acquisition can deliver for Argosy and its shareholders.

Argosy also acquired a freehold 15,838 sqm industrial yard in September on Roscommon Road, Wiri for $8.6 million. The site is leased to NZX listed Turners Automotive Group on a 15-year lease, providing a holding return of 5% with fixed reviews of 2.5% per annum, with a market review in year six.

Argosy also continued to progress its development pipeline with a $10.3 million upgrade of the Placemakers property in Hutt Road, Kaiwharawhara now underway. This project will be another green development for Argosy and the Company is targeting a 4-Star Green Built Industrial rating. Argosy will continue to pursue these value-add opportunities to improve overall portfolio quality and add value to shareholders.

Divestment of non-Core Assets

With the continued strength in property markets over the first half of the financial year, Argosy successfully completed the sale of Wagener Place in Auckland for $31.0 million. This transaction settled in July 2018. The Wagener Place sale was an opportunity to reduce Argosy's retail exposure in an area where there will be increasing competition.

In September, Argosy announced that it had unconditionally sold the non Core property at 626 Great South Road, Greenlane. The property was sold at a price of $10.6 million, 8% over the book value of $9.8 million. Settlement is scheduled for 30 November 2018.

Subsequent to period end, Argosy announced the sale of two non Core regional assets, 1478 Omahu Road in Hastings and 31 El Prado Drive in Palmerston North. 1478 Omahu Road has been sold for $10.2 million which represents a 12% premium over book value immediately preceding the September valuation. Settlement will take place in March 2019. The property at 31 El Prado Drive has been sold for $35.5 million, which represents a 25% premium over book value immediately preceding the September valuation. Settlement will take place in December 2018. The divestment of these regional assets means that Argosy has only 3 properties outside its core Auckland and Wellington markets.

At year end, Argosy has categorised approximately 10% or $153.4 million of the portfolio as non Core. This number includes the two assets noted above as well as the Albany Lifestyle Centre which is currently on the market. Argosy will continue its divestment programme over the next 12-18 months to take advantage of current market conditions.

7 Waterloo Quay

Earthquake Damage and Insurance Claim

Argosy's 14 level property at New Zealand Post House at 7 Waterloo Quay in Wellington sustained damage in the 7.5 magnitude Kaikoura earthquake on 14 November 2016. Independent engineers confirmed that the building is structurally sound, but it suffered damage to fit out and services. Argosy has material damage insurance and we are working with our insurers to progress a significant insurance claim. Argosy expects that, as with many earthquake insurance claims, there may be debate with insurers over the extent of damage, the appropriate method of reinstatement and the extent of cover.

Argosy commissioned a comprehensive damage survey of 7 Waterloo Quay, and detailed damage assessment reports were provided to insurers earlier in the year. We envisage that the damage reports may be updated, based on our advisors' experience that additional earthquake damage may become apparent. More recently, detailed reinstatement scope reports were completed by our expert consultants and these have been provided to our insurers. We are now engaged in an exercise to quantify the cost to repair the damage. We expect that this process will be completed in early 2019 to enable a material damage claim to be submitted to insurers.

Argosy also has business interruption insurance, which is expected to cover loss of rents and certain additional expenses until mid-November 2018, being a period of two years from the date of the earthquake.

Argosy has made six interim claims under its material damage and business interruption insurance and received progress payments from insurers (to 31 October 2018) of $14.9 million plus GST (after a $4.8 million deductible). In the interim period to 30 September 2018, $2.3 million has been allocated by Argosy to loss of rents, and $2.8 million to material damage reinstatement. Further interim claims will be presented for the remainder of the two-year business interruption indemnity period, and for material damage.

Reinstatement and Leasing

Demand for space from late calendar 2019 has dictated a desired delivery in this timeframe. With recent changes in the method of measurement for seismic resilience, some upgrade to the building is considered desirable to maximise the potential from the current strong leasing environment. It is expected that these works will cost between $15-20 million and be complete in September 2019.

Argosy has proceeded with its interim works programme to make damaged levels in the building available for occupation (including levels 10-12). The reinstatement project is on program to be completed (apart from level 12) by March 2019.

Damaged levels 1-4 and 7 were leased to New Zealand Post (Post) to December 2025. As part of a lease termination agreement, Post has agreed to pay a termination fee of $2.9 million to Argosy effective 30 November 2018 and relinquish these floors. This amount, although calculated based on the previous rent from levels 2-4 and 7 through to 31 August 2019, is required by accounting standards to be fully recognised in the second half of this financial year. Post will remain on the ground floor (part) and levels 5, 6, 8 and 9. Management is working with Post on longer term accommodation options.

The office leasing environment in Wellington is very favourable at present and we are currently in negotiations for the remaining space in this building.

Capital Management

Current Leverage

At 30 September 2018, Argosy's debt-to-total-assets ratio, excluding capitalised borrowing costs, was 36.8% versus 35.9% at 31 March 2018 year end. The increase reflects the net impact of acquisitions and developments during the period largely offset by divestments and revaluation gains. Argosy's target gearing band is 30 to 40% providing flexibility depending on financial and property market conditions. Argosy currently sits in the middle of the target band and remains well within all bank covenants.

At period end, Argosy's weighted average interest rate was 4.86% versus 4.98% at 31 March 2018. In October 2018, Argosy added $25 million to its banking facilities with ANZ Bank New Zealand Limited, Bank of New Zealand Limited and The Hongkong and Shanghai Banking Corporation.

Argosy's total debt facility is now $650 million ($625 million at 30 September 2018). Argosy is reviewing its long term debt funding options with a view to diversifying its debt funding base over the next 12 months.

Dividends

Consistent with the first quarter dividend, a second quarter dividend of 1.5625 cents per share with imputation credits of 0.3890 cents per share attached has been declared for the September quarter. The dividend will be paid to shareholders on 19 December 2018 and the record date will be 5 December 2018. The dividend reinvestment plan remains suspended.

Argosy has started the 2019 financial year in a very solid financial and portfolio position. We remain focused on delivering sustainable dividends to our shareholders. Based on current projections for the portfolio, the Board expects a full year 2019 cash dividend of 6.25 cents per share, an increase of 1% on the prior year. The increase reflects our wish for shareholders to share in the continued strong results but also allows us to maintain our momentum towards an AFFO[2] based dividend policy in the medium term.

Governance – ex Annual Meeting results and appointments

At the August 2018 Annual Meeting, Jeff Morrison was re-elected as an independent Director. Chris Hunter retired as an independent director at the meeting and did not seek re-election. Subsequently Stuart McLauchlan was appointed as an independent director.

Stuart is a Senior Partner of GS McLauchlan & Co Business Advisors and Accountants, a prominent businessman and company director. Stuart is a Director of Scenic Hotels Limited, Dunedin Casinos Limited, Ngai Tahu Tourism Limited and several other companies. He is also Chairman of the NZ Sports Hall of Fame, Chairman of AD Instruments Pty Limited, Chairman of Scott Technology Limited, Chairman of UDC Finance Limited and a member of the Otago Southland Branch of the Institute of Directors. Stuart is also a past President of the New Zealand Institute of Directors.

The Board has also recently appointed Chris Gudgeon as an independent Director of the Company. Chris has been involved in property investment, development and construction in New Zealand for more than 25 years. He was previously Chief Executive of Kiwi Property Group and is a past President of Property Council New Zealand.

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[2] AFFO (Adjusted Funds From Operations) is considered by some investors to represent a measure of dividend sustainability. The interim results presentation released today provides a reconciliation between net distributable income and AFFO.

Outlook

The Company continues to operate in a low interest rate and low inflation environment, although the possibility of rising interest rates has caused some nervousness around the world's stock markets. The economy, and thus the property market, in New Zealand however remains solid with good economic growth expected to continue. Argosy remains in a strong position with a quality, resilient portfolio that is diversified by sector, location and tenant mix.

Ongoing strength in the sector should continue to provide opportunities to divest non Core assets at attractive prices and either reduce gearing or reinvest the proceeds into tenant led development opportunities.

Argosy will remain as focused as ever on addressing near term lease expiries within the portfolio and ensuring that the tenant retention rate remains high. Argosy will continue to focus on the existing portfolio of value add properties to create long term value for shareholders and increase the quality and sustainability of our earnings.

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