DEXUS Property Group (ASX:DXS)

ASX release

19 August 2013

2013 annual results – A year of focus and delivery

DEXUS Property Group (DXS) today announced its full-year results and strategic achievements for the year ended 30 June 2013.

RESULTS HIGHLIGHTS

Financial

- Statutory net profit of $514.5 million
- Funds From Operations (FFO)[1] of $365.4 million or 7.75 cents per security, up 1.3%
- Distribution per security grew by 12.1% for the year ended 30 June 2013
- Net tangible assets (NTA) per security of $1.05, up 5.2%
- Delivered a Return on Equity of 11.2%
- Conservative and flexible balance sheet with gearing[2] of 29.0% and credit ratings maintained
- Solid net operating income (NOI) growth of 1.6%
- On 2 July 2013, an on-market buy-back of up to 5% of DXS securities was reinstated
- FY14 FFO per security is expected to grow 5.2% and FY14 distribution per security to grow by 2.0%

Transactions

- Involved in $2.9 billion of transactions across the Group
- Sold the US and European industrial property portfolios, exiting non-core offshore markets[3]
- Reinvested $1.1 billion into office acquisitions in Sydney, Melbourne, Brisbane and Perth
- On 25 July 2013, DEXUS acquired a 14.9% interest in ASX listed entity Commonwealth Property Office Fund

Total Group portfolio

- Leased or renewed 629,209 square metres of space[4]
- Increased DXS total portfolio occupancy by area from 93.4% to 95.3%

Office portfolio

- Leased or renewed 156,024 square metres of space[4] across 130 transactions
- Occupancy by area decreased to 94.4% primarily as a result of new acquisitions and portfolio WALE improved to 5.0 years

Industrial portfolio

- Leased or renewed 327,432 square metres of space[4] across 122 transactions including leasing 87,221 square metres of development projects
- Occupancy by area improved by 4.2% to 95.9%

Development

- Completed 81,024 square metres of development projects in the $1.2 billion development pipeline
- Secured a total of $1.5 million in trading profits

Third Party Funds Management

- Achieved a 9.5% increase in funds under management
- DEXUS Wholesale Property Fund (DWPF) continued its outperformance against benchmark and secured over $820 million of new equity
- Formed the Australian Industrial Partnership with a leading global pension fund and grew the portfolio to 18 properties with a value of $487 million

DEXUS Chief Executive Officer, Darren Steinberg said: "Despite the continued uncertainty in global and local markets we had a successful year delivering a solid operational result and increasing distributions per security."

1. FFO represents net profit/loss after tax attributable to stapled security holders calculated in accordance with Australian accounting Standards and adjusted for: property revaluations, impairments, derivative and FX mark to market impacts, amortisation of certain tenant incentives, gain/loss on sale of certain assets, straight line rent adjustments, deferred tax expense/benefit, rental guarantees and coupon income.
2. Adjusted for cash.
3. Excluding Lumley Centre in New Zealand.
4. Including Heads of Agreement.

DEXUS PROPERTY GROUP

DEXUS generated a net profit attributable to stapled security holders after tax of $514.5 million for the year ended 30 June 2013, compared to $181.1 million for the prior year. The change primarily reflected higher revaluation gains in FY13 compared to FY12.

Over the 12 months to 30 June 2013, DXS achieved a total security holder return[5] of 22.1%.

Strategic progress

Darren Steinberg said: "In a tough operating environment, we delivered on all of our strategic objectives which we announced in August 2012.

"We have refocused the business, concentrating on maximising value, improving earnings and investing in our target markets. We undertook a significant number of transactions, selling non-core offshore properties well ahead of our expected timeframe and reinvesting the funds into quality Australian CBD office properties.

"We leveraged our core capabilities to drive the office portfolio performance to further our objective of being the leader in office, achieving leasing success that resulted in increased property valuations.

"We were able to reposition the business while actively and prudently managing our capital which improved the cost, duration and diversity of our debt, creating a solid foundation for further acquisition opportunities."

Transactions

DEXUS undertook a total of $2.9 billion transactions across the Group, divesting non-core properties in offshore markets and reinvesting into the Australian office market. The activity, which was completed without impacting earnings, strengthened the DEXUS platform and increased the composition of the listed DXS portfolio towards Australian office.

The sale of the US portfolio for US$617 million across three transactions achieved a 12% premium to prior book value. DXS's reinvestment of $1.1 billion into Australian office markets included:

- a 50% interest in 12 Creek Street, Brisbane
- a 100% interest in 50 Carrington Street, Sydney
- a 25% interest in Grosvenor Place, Sydney
- a 50% interest in 39 Martin Place, Sydney
- a 50% interest in 2-4 Dawn Fraser Avenue, Sydney Olympic Park
- a 100% interest in 40 Market Street, Melbourne
- a 50% interest in fund-through investments at 480 Queen Street, Brisbane and Kings Square, Perth

The major benefit of these acquisitions has been the enhancement to investor returns through the improvement in the quality of DEXUS's earnings.

On 25 July 2013, DEXUS entered into a forward contract to acquire a 14.9% interest in the ASX listed Commonwealth Property Office Fund (CPA). Consistent with other acquisitions and divestments made by the Group over the past 18 months, DEXUS will continue to demonstrate a disciplined approach to generate attractive risk adjusted returns.

FINANCIAL RESULTS

Statutory net profit:	$514.5 million (2012: $181.1 million)
FFO:	$365.4 million (2012: $367.8 million)
FFO per security:	7.75 cents (2012: 7.65 cents)
Distribution per security:	6.00 cents (2012: 5.35 cents)
Total assets:	$7.8 billion (2012: $7.4 billion)

5. DXS share price appreciation plus distributions paid.

Chief Financial Officer, Craig Mitchell said: "In a busy year of transactional activity, we delivered a solid operational result, meeting our earnings guidance of 7.75 cents per security for the 12 months ended 30 June 2013 and increasing distributions per security by 12.1%."

Net profit attributable to stapled security holders after tax for the year to 30 June 2013 was $514.5 million. FFO was $365.4 million underpinned by solid like-for-like income growth of 1.6% across the total portfolio.

Strong valuation gains were the primary driver of a 5.2 cent increase in NTA per security to $1.05. DEXUS calculates Return on Equity (ROE) by adding the change in NTA per security over the year to the income distribution paid to security holders during the year. DEXUS delivered a ROE for the 12 months to 30 June 2013 of 11.2% which is ahead of its target of 9-10% per annum through the cycle.

Distributions per security was 6.00 cents for the year, up 12.1% and the final distribution for the six months ended 30 June 2013 of 3.11 cents per security will be paid to security holders on 30 August 2013.

PORTFOLIO UPDATE

Total portfolio metrics

Portfolio value:	$7.3 billion
Total area:	1.8 million square metres
Area leased during year:	483,456 square metres[6]

	30 June 2013	30 June 2012
Occupancy by area	95.3%	93.4%
Occupancy by income	94.9%	95.8%
WALE by income	4.8 years	4.7 years
Retention rate (rolling 12 months)	71%	n/a

Valuations

Leasing success, the weight of capital seeking quality Australian office property and recent transactional evidence all contributed to a $191 million or 3.5% increase in valuations on prior book values across the office portfolio. The DXS office portfolio's weighted average capitalisation rate tightened 13 basis points from 7.30% to 7.17% at 30 June 2013.

Increasing investor demand for prime quality industrial properties is being offset by the discounting of valuations for secondary properties and those with leasing risk. This has resulted in DXS's industrial portfolio experiencing a moderate uplift in valuations of $5.8 million or 0.4% on prior book values.

Darren Steinberg said: "The weight of capital seeking quality Australian office and industrial buildings will contribute to a further tightening of capitalisation rates in buildings with strong fundamentals over the next 12 to 18 months. Recent transactional evidence supports this view. We are expecting a further 15 to 25 basis points tightening across our portfolio over the coming year."

Office portfolio

Portfolio value:	$5.7 billion
Total area:	682,207 square metres
Area leased during period:	156,024 square metres[6]

	30 June 2013	30 June 2012
Occupancy by area	94.4%	97.1%
Occupancy by income	94.6%	96.8%
WALE by income	5.0 years	4.9 years
Average incentive	12.2%	17.3%
Average rental increase/(decrease) in rent	(0.1)%	4.6%
Retention rate (rolling 12 months)	72%	66%

6. Including Heads of Agreement.

The DXS office portfolio comprises over 87% of prime grade properties located in the Sydney, Melbourne, Brisbane and Perth CBD markets.

Kevin George, Executive General Manager, Office and Industrial said: "We have achieved pleasing results in a difficult operating environment. We expect tenant demand to remain subdued in the near term as weak business confidence continues to impact office fundamentals.

"Despite the current conditions, our focus on forward leasing positioned the portfolio well, shown through the reduction in FY14 expiries to 5.6% and strong expected like-for-like office income growth."

The office portfolio delivered a strong total return for the 12 months to 30 June 2013 of 10.6% driven by underlying rental growth and improved property values. NOI increased by $27.5 million to $317.4 million underpinned by like-for-like income growth of 1.8%.

DEXUS's proactive leasing approach resulted in the leasing of 156,024 square metres during the year representing 16% of the office portfolio. Occupancy across the office portfolio was 94.4%, impacted primarily by the acquisitions made during the year and the Government vacating 14 Moore Street, Canberra. The weighted average lease duration improved marginally to 5.0 years and tenant retention increased by 6% from 30 June 2012 to 72% at 30 June 2013.

New rents were down 0.1% on average compared with prior rents, with average incentives across all leases of 12.2% (2012: 17.3%). On a comparable basis, excluding leases where no incentives were given, new commencing face rents were 4.3% higher than prior rents with average incentives of 21.1%.

Key leasing successes included:

- Over 23,000 square metres leased at Australia Square, Sydney including key lease renewals with Ninemsn and Origin Energy for six year lease terms and HWL Ebsworth for 13 years
- Lend Lease extended its lease to March 2019 over 17,547 square metres at 30 The Bond in Sydney
- The Victorian State Government renewed 23,528 square metres for a further five years at 8 Nicholson Street, Melbourne
- Early leasing progress at newly acquired properties including
  - 50 Carrington Street, Sydney, 82% of total space has now been committed up from 61% on acquisition in November 2012
  - 39 Martin Place, Sydney, 82% of total space has now been committed up from 75% on acquisition in February 2013

Industrial portfolio

Portfolio value:	$1.6 billion
Total area:	1,093,267 square metres
Area leased during period:	327,432 square metres[7]

	30 June 2013	30 June 2012
Occupancy by area	95.9%	91.7%
Occupancy by income	96.1%	92.8%
WALE by income	4.1 years	4.4 years
Average incentive	7.9%	5.6%
Average rental (decrease)/increase in rent	(2.4)%	(5.0)%
Retention rate (rolling 12 months)	70%	59%

DEXUS has a strong track record in using its industrial capabilities to deliver high quality industrial product to the market, targeting the key metropolitan markets of Sydney, Melbourne and Brisbane and ensuring its properties are located close to multi-modal infrastructure and employment hubs.

7. Including Heads of Agreement.

Kevin George said: "Strong tenant relationships and a well-located quality portfolio of industrial facilities have driven increased retention and significantly improved occupancy levels. Through proactively pursuing all operational targets, strong investor returns were secured for the period including a 1.1% increase in like-for-like income and a portfolio total return of 8.8%."

Occupancy increased by 4.2% to 95.9% and the weighted average lease expiry decreased slightly to 4.1 years. During the year 327,432 square metres of industrial space was leased across 122 lease deals, including 87,221 square metres of development leasing.

Key leasing successes included a number of long-term vacancies at:

- 1 Garigal Road, Belrose for a 10 year lease over 10,605 square metres
- Pound Road West, Dandenong for a seven year lease over 7,607 square metres
- Silverwater industrial estate – a total of 6,349 square metres leased on average terms of 5.5 years, improving occupancy from 66% to 100%

Developments

The Group has a $2.9 billion pipeline across its DXS listed portfolio and third party funds management business. DEXUS grew and diversified its $1.2 billion DXS development pipeline in FY13 to include high quality industrial and office developments, trading and repositioning opportunities and development fund-through investments.

Kevin George said: "We made significant progress on our development pipeline, utilising our development expertise to complete six prime industrial properties in New South Wales, Queensland and Victoria across 81,024 square metres and valued at $106.9 million.

"Industrial tenants continue to seek new, modern facilities with higher specifications located close to major road networks and we successfully leased over 80,000 square metres of industrial development space, including achieving 100% occupancy on completed developments at The Quarry at Greystanes.

"We delivered $1.5 million in trading profits against our $4 million target, driven by a management decision to defer the sale of trading properties in order to maximise returns. Our trading profit target for FY14 is $4-5 million."

Corporate Responsibility & Sustainability (CR&S)

DEXUS creates values for all of its stakeholders by integrating CR&S objectives into every aspect of business operations.

Kevin George said: "Our commitment to energy efficiency delivered positive results in energy consumption in our office and industrial portfolio, achieving real cost savings and assisting in reduced let-up times, tenant retention and property valuations."

For the 12 months to 30 June 2013, DEXUS achieved notable reductions in comparable energy and water consumption and greenhouse gas emissions across the Group's total portfolio. There was a 7.7% reduction in greenhouse gas emissions per square metre, and energy and water consumption were down by 7.5% and 0.7% respectively.

DEXUS exceeded environmental performance objectives across the DXS office portfolio, achieving an average 4.7 star NABERS Energy rating against its 4.5 star target and an average NABERS Water rating of 3.5 stars as at 31 December 2012 in line with its target. Energy improvements achieved in the office portfolio resulted in savings of $5.3 million per annum and reductions in tenant outgoings.

DEXUS achieved carbon neutrality at its Melbourne office and for the third consecutive year at its head office in Sydney as a result of sustainability initiatives and credit offsets purchased from Australian forest projects.

CAPITAL MANAGEMENT

Key metrics	30 June 2013	30 June 2012
Gearing	29.0%	27.2%
Duration of debt	5.4 years	4.2 years
Cost of debt	5.9%	6.1%
Hedged debt	64%	73%
Undrawn facilities (approximately)	$0.3bn	$0.6bn

As part of the Group's continued strategic and active approach to capital management, over $1 billion of new funding was secured, through the Australian Medium Term Note (MTN) market and the US Private Placement (USPP) market, improving the cost and diversity of funding and increasing the duration of debt to over 5 years.

Craig Mitchell said: "In what is a very pleasing endorsement of our active capital and risk management approach, our USPP offering was five times oversubscribed resulting in the pricing of a long-dated USPP for US$300 million."

DEXUS was active in the MTN market, refinancing short-dated debt with long-dated notes, raising $235 million including $135 million in taps through responding to reverse enquiry from investors.

Following the sale of the US portfolio, DEXUS further restructured its debt book retaining long dated 144A bonds and ensuring it had no debt maturities until July 2014.

DEXUS chose not to extend its on-market securities buy-back which commenced in April 2012, following the successful redeployment of US sale proceeds into new office acquisitions and improved share market performance, resulting in 64% of the targeted $200 million buy-back being completed. Post balance date on 2 July 2013, a buy-back of up to 5% of DXS securities was reinstated as a result of share market volatility, providing the flexibility for DEXUS to acquire DXS securities on-market with a focus on enhancing value and returns to investors.

Craig Mitchell said: "Our balance sheet remains strong with gearing at 29% and limited short term refinancing requirements. Upon completion of 480 Queen Street, Brisbane and Kings Square, Perth, pro-forma gearing increases by approximately 4%, comfortably within our target range of 30-40%. Our residual gearing capacity positions us well for potential acquisitions should suitable opportunities arise."

As at 30 June 2013, the weighted average cost of debt is 5.9%, average duration of debt is 5.4 years and headroom is approximately $0.3 billion. DEXUS is comfortably inside all covenant limits and its credit ratings of BBB+ and Baa1, both with stable outlooks, were reaffirmed during the year.

THIRD PARTY FUNDS MANAGEMENT

Over the year, DEXUS advanced its objective of being the wholesale partner of choice, growing funds under management by 9.5% to $6.1 billion. Further diversifying its capital sources, DEXUS established and grew a new capital partnership, the $0.5 billion Australian Industrial Partnership, and jointly acquired four core office properties with DWPF.

DWPF outperformed its benchmark over one, three and five years and secured over $820 million of equity over the year, including $348 million from a pro-rata offer.

Craig Mitchell said: "DWPF's successful equity raising, undertaken in a competitive market, builds on the Fund's track record of attracting capital and adds to the more than $2 billion secured since 2010 from domestic and offshore investors."

SUMMARY AND OUTLOOK

Darren Steinberg said: "We have worked hard to position the Group for continued growth in the year ahead. We have shown our ability to reduce our exposure to leasing risks and grown earnings by acquiring quality properties across the investment spectrum.

"Looking ahead, despite uncertain market conditions, we are confident our team's strong corporate and leasing backgrounds will enable us to continue to drive high performance.

"Barring unforeseen changes to operating conditions, our guidance[8] for earnings or FFO for the 12 months ending 30 June 2014 is 8.15 cents per security, a 5.2% increase from FY13.

"We are targeting an FY14 distribution payout ratio of 75% of FFO in line with free cash flow, delivering an expected distribution of 6.12 cents per security."

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8. Assumptions include: 75% payout ratio, delivering circa 4% like-for-like income growth in the office portfolio, $4-5m in trading profits, cost of debt at 6.0% and excluding further on-market buy-back.