DEXUS Property Group (ASX:DXS)

ASX release

14 February 2013

Half-year results for the six months to 31 December 2012

DEXUS Property Group (DEXUS) today announced its half year result for the six months ended 31 December 2012. In a very active period, DEXUS made significant progress on a number of key strategic objectives and operational initiatives.

KEY HIGHLIGHTS

Financial

- Statutory net profit of $267.0 million
- Funds From Operations (FFO)[1] of $182.2 million or 3.85 cents per security
- Delivered a distribution of 2.89 cents per security
- Total valuation uplift of $120.4 million or 1.7% increase on prior book values
- Net tangible assets (NTA) per security up 3% to $1.03
- Achieved a strong total shareholder return[2] of 29.5%
- Reaffirmed FY13 distribution guidance[3] of 5.8 cents per security
- Gearing of 29.0%[4] and credit ratings maintained (BBB+ and Baa1)

Operational

- Undertook $1.7 billion of transactions
- Achieved like-for-like net operating income (NOI) growth of 2.2%[5] across the total portfolio
- In the office portfolio, leased 61,882 square metres[6] across 63 transactions
- In the industrial portfolio, leased 176,780 square metres[6] across 58 transactions
- DEXUS Wholesale Property Fund (DWPF) successfully raised $400 million in equity
- Achieved a 4.7 star NABERS Energy rating for the office portfolio exceeding the 2012 target

CONTINUED EXECUTION OF STRATEGY

DEXUS CEO, Darren Steinberg said: “The Group made solid progress on achieving its vision of being globally recognised as Australia’s leading real estate company combined with its objective of being the leading owner and manager of Australian office, through the sale of offshore properties and numerous off market acquisitions.

“The US portfolio sale considerably improves the quality of the Group’s earnings profile as the proceeds are reallocated into the Australian market.”

During the period DEXUS acquired a number of Australian office properties contributing to rebalancing the Group’s portfolio composition towards its strategic target of 80% Australian office and 20% Australian industrial, ensuring diversification across the portfolio.

Darren Steinberg said: “Our team has remained focused on forward leasing and proactive negotiations with tenants, which resulted in securing tenants at some of our newly acquired properties prior to settlement and the retention of existing tenants prior to lease expiry.

1. Funds from Operations represent statutory net profit adjusted to exclude property revaluations, unrealised mark to market changes, changes in deferred tax, amortisation of tenant cash and fit-out incentives, gain/loss on sale of certain assets and rent straight-lining.
2. DXS share price appreciation plus distributions paid. Source: UBS.
3. Barring unforeseen circumstances. Assumptions include: 75% payout ratio, delivering 2% like-for-like NOI growth in the office portfolio, $2m in trading profits, cost of debt at 6.0% and excluding further on-market buy-back.
4. Pro-forma gearing including the impact of the settlement of the US portfolio sale, the acquisition of interests in three Sydney properties and the acquisition of 40 Market Street, Melbourne and Carole Park industrial estate, South Brisbane.
5. Excluding discontinued operations of US and Europe.
6. Including Heads of Agreement.

DEXUS PROPERTY GROUP

Darren Steinberg said: "Progressing our objective of having the best people and systems to strengthen our core capabilities, we enhanced our platform to provide best in class facilities management services and technology systems. This platform allows our team to focus on service excellence and high performance, improving the efficiency of our business.

"Our decision to move to Australia Square during the second quarter of 2013 will enable the creation of a new workplace that supports our culture of service excellence and high performance through the adoption of leading technologies in a destination that aligns with our revised vision and strategy.

"In our third party funds business, our total funds under management increased 6.5% during the period and the importance of DWPF as a capital partner was enhanced through its successful raising of $400 million in equity. In addition, our relationship with DWPF was strengthened through the joint acquisition with DXS of 12 Creek Street in Brisbane and 39 Martin Place in Sydney."

FINANCIAL RESULTS

FFO[7] for the period is $182.2 million or 3.85 cents per security, in line with guidance, and represents a 1.0% increase on a cents per security basis over the prior corresponding period (December 2011: 3.81 cents per security).

The financial results for the six months to 31 December 2012 are underpinned by like-for-like NOI growth of 2.2%[8] across the total portfolio. Net profit attributable to stapled security holders after tax is $267.0 million for the six months ended 31 December 2012 (2011: $145.7 million).

Strong valuation gains of $120.4 million, including a $92.8 million uplift from the office portfolio, primarily drove a 3 cent increase in NTA per security to $1.03 (June 2012: $1.00). As a consequence of these operational and valuation movements, DEXUS delivered a six-month return on equity (ROE) of 5.9% which, on an annualised basis, is ahead of the Group's target through-the-cycle ROE of 9-10% per annum.

DEXUS delivered a distribution of 2.89 cents per security for the six months ended 31 December 2012, to be paid on 28 February 2013. This distribution is up 8.2% on the prior corresponding period.

TRANSACTIONS

The Group undertook $1.7 billion of transactions involving 54 properties during the period, including the sale of the majority of the remainder of the US industrial portfolio for US$561.0 million at a 13% premium to prior book value.

Subsequent to the announcement of the US portfolio sale, DEXUS announced the reinvestment of proceeds into the acquisition of interests in three Sydney properties for $503.7 million[9], including a 25% interest in Grosvenor Place at 225 George Street in Sydney. This transaction is expected to settle on 28 February 2013 and will be accretive to earnings from FY14 onwards.

Darren Steinberg said: "Our latest acquisition enhances the quality and diversification of the office portfolio and deepens the Group's knowledge and relationships in Sydney, Australia's largest office market. The transactions conducted over the past six months demonstrate our team's capabilities, in particular the ability to acquire the majority of properties on an off-market basis."

7. Funds from Operations represent statutory net profit adjusted to exclude property revaluations, unrealised mark to market changes, changes in deferred tax, amortisation of tenant cash and fit-out incentives, gain/loss on sale of certain assets and rent straight-lining.
8. Excluding discontinued operations (US and Europe).
9. Total transaction value including DWPF's 50% interest in 39 Martin Place, Sydney.

PORTFOLIO UPDATE

Total portfolio metrics[10]

Portfolio value:	$7.1 billion
Total area:	1.7 million square metres
Area leased during period:	238,662 square metres[11]

	31 December 2012	30 June 2012
Occupancy by area	94.7%	93.4%
Occupancy by income	95.0%	95.8%
WALE by income	4.7 years	4.7 years
Retention rate (year to date)	74%	61%
Retention rate (rolling 12 months)	62%	61%

Office

Portfolio value:	$5.5 billion[12]
Total area:	612,071 square metres
Area leased during period:	61,882 square metres[13]

	31 December 2012	30 June 2012
Occupancy by area	95.2%	97.1%
Occupancy by income	95.3%	96.8%
WALE by income	4.9 years	4.9 years
Average incentive	9.6%	17.3%
Average rental (decrease)/increase in rent	(2.7%)	4.6%
Retention rate (year to date)	69%	66%
Retention rate (rolling 12 months)	62%	66%

Kevin George, DEXUS Executive General Manager, Office and Industrial said: "While office market demand remains tempered, we are seeing some positive signs in core markets and solid interest in high quality buildings. The tough business conditions are resulting in a number of firms seeking to modernise and gain workplace efficiencies which has flowed on to increased enquiry within our portfolio. We have also seen suburban based tenants looking to move to CBD locations due to competitive conditions and a reduced price differential."

The office portfolio performed well during the period delivering a total return of 10.3%. NOI increased by $10.5 million to $151.8 million (December 2011: $141.3 million) underpinned by like-for-like NOI growth of 2.6%, and the acquisition of 12 Creek Street, Brisbane and 50 Carrington Street, Sydney.

Significant leasing activity was undertaken with 63 new leases signed covering 61,882 square metres[13]. New rents were on average 2.7% lower than prior rents, with average incentives across all leases of 9.6%. On a comparable basis, excluding the two leases where no incentives were given, new commencing face rents were 4.9% higher than prior rents with average incentives of 16.1%.

10. Excluding discontinued operations (US and Europe).
11. Including Heads of Agreement.
12. Pro-forma including post balance date office acquisitions.
13. Including Heads of Agreement of 7,855sqm.

A continued focus on proactive asset management and forward leasing of future expiries delivered results during the period. Lease renewals were secured for over 50,000 square metres on average 8.5 months prior to their expiry, and 11,000 square metres of new leases were signed. Key successes during the period include the Victorian State Government renewing its lease for a further five years over 23,528 square metres at 8 Nicholson Street, Melbourne together with Woodside having exercised its five year option over 4,281 square metres at Woodside Plaza in Perth. Following this activity, the portfolio was 95.2% leased at 31 December 2012 with a WALE of 4.9 years.

While the appetite for prime assets remains strong, leasing challenges in secondary markets are contributing to a yield spread between prime and secondary properties. This resulted in a $92.8 million or 1.9% increase on prior office book values. The office portfolio weighted average capitalisation rate tightened by one basis point to 7.29%.

Industrial

Portfolio value:	$1.6 billion
Total area:	1,056,589 square metres
Area leased during period:	176,780 square metres[14]

	31 December 2012	30 June 2012
Occupancy by area	94.4%	91.7%
Occupancy by income	93.9%	92.8%
WALE by income	4.0 years	4.4 years
Average incentive	6.3%	5.6%
Average rental decrease in rent	(0.7%)	(5.0%)
Retention rate (year to date)	78%	59%
Retention rate (rolling 12 months)	63%	59%

Kevin George said: "The industrial portfolio results this period reflect the importance of strong tenant relationships in driving increased retention and significantly improving occupancy levels. Through proactively pursuing all operational targets, strong investor returns were secured for the period including an increase in like-for-like NOI and a portfolio total return of 7.8%."

Headline NOI of $57.8 million (2011: $58.4 million) was $0.6 million lower due to the formation of the $360 million Australian industrial partnership which resulted in the sale of a 50% interest in 13 industrial properties. Like-for-like NOI growth across the industrial portfolio was 1.1%.

In the six months to 31 December 2012, 58 new leases covering 176,780 square metres[14] were signed including 50,508 square metres of leases completed on new developments. Leases on existing properties were struck at an average rent of $116.00 per square metre and an average incentive of 6.3%.

The year-to-date retention rate increased to 78% while occupancy improved by 2.7% to 94.4%. Two key leasing successes during the period included: the leasing of 6,349 square metres at the Silverwater industrial estate on average terms of 5.5 years, improving occupancy from 66% at 30 June 2012 to 100% at 31 December 2012; and the leasing of 33,106 square metres at Gillman in South Australia, improving occupancy from 57% at 30 June 2012 to 89% at 31 December 2012.

The Group completed three developments, comprising a total area of 45,310 square metres, for a total cost of $54.0 million and an average target IRR of 18.1%. Six development projects are currently underway, for a total cost of $87.3 million across four sites in New South Wales, Victoria and Queensland. These developments will have a total lettable area on completion of 100,804 square metres.

The industrial portfolio weighted average capitalisation rate is 8.58%, representing a one basis point tightening and resulting in a $6.4 million (0.4%) increase on prior industrial book values.

14. Including Heads of Agreement of 31,865sqm.

CAPITAL MANAGEMENT

Key metrics	31 December 2012	30 June 2012
Gearing	29.0%[15]	27.2%
Duration of debt	4.1 years	4.2 years
Cost of debt	5.8%	6.1%
Hedged debt	70%	73%
Undrawn facilities (approximately)	$0.5bn	$0.6bn

During the period DEXUS continued its disciplined and active approach to capital and risk management, including being active in the domestic medium term note (MTN) market by refinancing short-dated bank debt with long-dated MTNs.

Craig Mitchell, DEXUS CFO said: "Our active approach helped improve the cost, duration and diversity of our debt profile and considerably improved the margins achieved for MTN debt. In the six months to 31 December 2012, we raised $205 million from the MTN market including $105 million through responding to reverse enquiry from investors.

"We maintained our commitment to US debt capital markets through the retention of our long dated 144A bonds as part of the most recent US portfolio divestment, providing diversification of debt sources.

"Our balance sheet remains strong with pro-forma gearing at 29.0%[15], at the lower end of our target gearing range of 30-40%, and we have limited short term refinancing requirements. Our residual gearing capacity positions us well for potential acquisitions should suitable opportunities become available."

For the period to 31 December 2012, the weighted average cost of debt was 5.8%. The average duration of debt was 4.1 years and headroom was $0.5 billion. The Group is comfortably inside all covenant limits and DEXUS's credit ratings of BBB+ and Baa1[16], both with stable outlooks, were reaffirmed during the period.

THIRD PARTY FUNDS MANAGEMENT

DEXUS's third party funds management business of $5.9 billion comprises DWPF, an Australian mandate and an Australian industrial partnership.

Craig Mitchell said: "DWPF had a successful six-month period, continuing to outperform its benchmark and attracting ongoing investor support, with $400 million of equity raised including $290 million from a new major investor.

"The DWPF team remained focused on driving performance and had an active period, delivering on its investment plan and improving portfolio quality through the acquisition of $203.9 million[17] of properties and the activation of its development pipeline.

"The Australian industrial partnership acquired two industrial properties since its inception in October 2012, increasing its total number of properties to 15 and demonstrating DEXUS's commitment to being a wholesale partner of choice."

15. Pro-forma gearing including the impact of the settlement of the US portfolio sale, the acquisition of interests in three Sydney properties and the acquisitions of 40 Market Street, Melbourne and Carole Park industrial estate, South Brisbane.
16. S&P rating BBB+ and Moody's rating Baa1.
17. Excluding acquisition costs and including the acquisition of a 50% interest in 39 Martin Place, Sydney.

CORPORATE RESPONSIBILITY & SUSTAINABILITY

DEXUS's commitment to integrating leading sustainable practice into all aspects of its business practice was demonstrated by the delivery of improvements in resource consumption. For the 12 months to 31 December 2012, greenhouse gas emissions per square metre for the Group's total portfolio were down by 9.1%, energy consumption was down by 7.1% and water consumption was down by 8.6%.

The DXS office portfolio achieved an average 4.7 star NABERS Energy rating, exceeding its 4.5 star target to 31 December 2012. The portfolio also achieved an average NABERS Water target of 3.5 stars, in line with its target.

Kevin George said: "Our commitment to energy efficiency has shown positive results in energy consumption with a 35.0% reduction[18] in our office portfolio and a 28.4% decrease[18] in our industrial portfolio, delivering real cost savings for our tenants and assisting in tenant retention and driving valuations.

"We will continue to invest in strategies to improve the sustainability credentials of our assets as demonstrated through the acquisition of 50 Carrington and 40 Market Streets which, through refurbishment and building upgrades, have the potential to improve sustainability ratings and add value to our office portfolio."

Globally, 1 Bligh Street was awarded the prestigious International High-Rise Award 2012. The €50,000 prize money was donated towards the formation of the "1 Bligh Master of Architecture Final Year Prize for Sustainable Commercial Architecture", a scholarship with the University of New South Wales that will promote future sustainable design in Australia.

SUMMARY AND OUTLOOK

Darren Steinberg said: "Today we have reported solid operational results, demonstrating our ability to achieve in a challenging market. We have made significant progress executing our revised strategy over the past six months through fast-tracking our exit from offshore markets and allowing us to focus on driving value back here in Australia.

"We are well positioned for growth with a strong and conservative balance sheet, and confident that we can continue to deliver superior risk-adjusted returns for our investors from our quality Australian real estate portfolio."

DEXUS's guidance[19] for the year ending 30 June 2013 is reaffirmed with FFO or earnings of 7.75 cents per security and distributions of 5.8 cents per security.

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18. Calculated on an intensity basis and since our base year of FY08.
19. Barring unforeseen circumstances. Assumptions include: 75% payout ratio, delivering 2% like-for-like NOI growth in the office portfolio, $2m in trading profits, cost of debt at 6.0% and excluding further on-market buy-back.