Argosy

Market Release

26 November 2020

ARGOSY FY21 INTERIM RESULT – MANAGING THROUGH COVID-19

FOR THE 6 MONTHS TO 30 SEPTEMBER 2020

Argosy will present the 2021 interim result via a teleconference and webcast at 10am today. Please visit https://s1.c-conf.com/diamondpass/10009790-invite.html or dial 0800 122 360 and quote the conference ID 10009790. 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 2020.

Key highlights for the period include:

- Net distributable income up 21.5%;
- Net distributable income per share up 21.2%;
- Robust portfolio metrics maintained with high occupancy (99.4%) and WALT (5.7 years);
- Strong portfolio leasing and rent review outcomes, including 3.8% annualised rent growth on rents reviewed;
- An unrealised revaluation gain of $79.8 million, an increase of 4.3% on book value;
- An increase in net tangible assets per share (NTA) to $1.41 from $1.30 at 31 March 2020;
- Strong delivery on key strategy focus areas including minimising Covid-19's impact on the business, the continued focus on sustainability and green developments and executing on capital management initiatives;
- Argosy's FY21 dividend guidance increased to 6.45 cents per share, reflecting continued sound delivery of strategy.

Argosy's Chief Executive Officer, Peter Mence said, "We recognise that the FY21 year has started under challenging economic and operating conditions. Covid-19 has been tough for all New Zealanders, including our tenants and staff. During the first six months of the financial year we focused on working closely with our tenants to support them through near term uncertainty. Pleasingly, despite the challenges we both faced, Argosy has managed to deliver on many core strategic focus areas including re-commencing organic green development projects, achieving strong leasing outcomes, delivering on capital management initiatives and executing on strategic acquisition opportunities to deliver long term capital growth.

Argosy has a quality portfolio of diversified assets. The business has proved resilient and is well positioned to deliver a solid second half performance. Our third green bond issue in October was well received reflecting the continued interest in our transition towards greening the portfolio.

The $76 million acquisition of the Mt Richmond Properties announced in October will provide attractive long term capital growth and earnings sustainability for Argosy. We are confident of delivering on the remaining focus areas over FY21 including leasing up the balance of 7 Waterloo Quay in Wellington."

Chairman Jeff Morrison said, "Argosy has made a strong start to FY21 despite the challenging operating conditions and a cloudy economic outlook. New Zealand, like all other countries affected by Covid-19, continues to manage through uncertain times with the economic impact likely to continue for some time.

Argosy's current business is resilient and underpinned by a diversified portfolio of quality assets in prime locations. Its capital and portfolio position is sound as it heads into the second half of FY21.

Argosy remains focused on ensuring the sustainability of dividends to shareholders. Based on current projections for the portfolio and subject to market conditions, the Board is pleased to announce an expected dividend of 6.45 cents per share for the 2021 financial year. This increased guidance from 6.35 cents per share reflects its view that investors should share in the continuing strength of the business, whilst maintaining our momentum towards an Adjusted Funds from Operations (AFFO) based dividend policy over the medium term."

Financial Results

Statement of Comprehensive Income

For the six months to 30 September, Argosy reported net property income of $51.1 million for the period, in line with the prior comparable period. Strong like-for-like rental growth and additional income from leasing up of 7WQ and acquisitions & developments were offset by rental abatements for Covid-19 and lower insurance proceeds for rental loss at 7WQ.

Argosy provided $3.3 million in rental abatements to tenants in the interim period and $0.6m in deferrals (note that $0.3m of this will reverse in this financial year). Argosy may need to provide further support to tenants should New Zealand move back to Level 3 or Level 4 lockdowns.

Interest expense of $14.2 million is up on the prior comparable period primarily due to lower capitalised interest, as developments have completed.

Desk top valuations for the interim period to 30 September were performed by Colliers International New Zealand Limited ('Colliers'). The total unrealised revaluation gain for the six months to 30 September 2020 was $79.8 million. The portfolio is 1% under-rented excluding market rent on vacant space.

Distributable Income

Net distributable income increased by 21.5% to $36.0 million (including $4.5 million received in respect of the forfeited deposit on the Albany Lifestyle Centre) compared to $29.7 million in the prior comparable period. Net distributable income per share increased 21.2% to 4.35 cents per share from 3.59 cents per share.

Desk Top Valuations

The desk top valuations performed by Colliers resulted in an interim revaluation gain of $79.8 million, or a 4.3% increase on book values immediately prior to the revaluation.

By location, Auckland was the largest contributor to the revaluation gain with $54.0 million or 68% of the total portfolio gain. By sector, Industrial was a strong driver of the overall gain at $44.1 million, up 5.7%. The Office portfolio increased $21.4 million, or 2.7% and Large Format Retail also increased by $14.3 million or 5.3%.

As a result of the revaluation gain, Argosy's NTA has increased to $1.41, an 8.5% increase from $1.30 at 31 March 2020. Following the revaluation, Argosy's portfolio shows a contract yield on values of 6.04% and a yield on fully let market rentals of 6.14%.

Portfolio Activity

Portfolio Metrics, Rent Reviews and Leasing

Argosy's WALT as at 30 September was 5.7 years and portfolio occupancy was 99.4%.

"We are pleased to have reported strong portfolio metrics for the interim reporting period. Argosy's quality portfolio coupled with the strong metrics has allowed Argosy to deliver excellent operational outcomes in a challenging environment. Argosy's business is underpinned by a diversified portfolio that delivers resilient and defensive cashflows." said Peter Mence.

For the six months to 30 September, Argosy completed rent reviews achieving annualised rental growth of 3.8%. These reviews were achieved on rents totalling $36.1 million. On rents subject to review by sector, Argosy achieved annualised rental growth of 2.9% for Industrial rent reviews, 5.3% for Office rent reviews and 2.5% for Large Format Retail rent reviews.

For the first half of FY21, 49% of rents reviewed were subject to fixed reviews, 34% were market reviews and 17% were CPI based. Market reviews accounted for 55% of the total annualised rental uplift with Auckland and Wellington each accounting for 50% of the total annualised rental uplift.

Despite the impact from Covid-19, there was still plenty of activity across the business. The management team have remained very focused on delivering on Argosy's FY21 strategy focus areas.

Argosy completed 25 leasing transactions across 55,997m^2 of NLA over the first six months. Leases were mixed between extensions (7), renewals (10) and new leases (8).

Key leasing transaction successes over the period include;

- Parliamentary Services, 147 Lambton Quay, 8,139m^2 on a new 3 year lease;
- Citibank, 23 Customs Street, 545m^2 on a 5 year renewal;
- CNZ (Auckland) at 23 Customs Street, 657m^2 on a 3 year renewal;
- Fergs Beds at Albany Lifestyle Centre; 608m^2 of space on a 2 year extension from 2024;
- Peter Baker Transport, 18,703m^2 of space extended for a further 1 year.

Overall, the leasing outlook compared to six months ago is still challenging, albeit some subsectors and locations are performing better than others.

Acquisitions and Value Add Developments

Argosy made no strategic acquisitions during the first six months of the financial year. However, it did complete the acquisition of two contiguous industrial properties in Mt Richmond, Auckland, in October.

Peter Mence said, "Our focus has very much been on working closely with our tenants and recommencing work on existing development projects affected by the Covid-19 lockdowns. However, this did not mean we weren't seeing opportunities in the market. We have identified and acted upon opportunities which meet our investment criteria, in particular the $76 million acquisition of two Mt Richmond Properties, announced subsequent to the interim period end.

We were pleased to secure these strategic sites within a prime industrial precinct with historically very low supply levels. The acquisition of the Mt Richmond Properties fits squarely with our green development strategy and affords us flexibility to support the growth of existing tenants' needs and potential new tenants.

The acquisition provides Argosy with an attractive initial holding yield and positive cashflow. The sites are close to the Auckland CBD with strong arterial network connections. The redevelopment potential of the large sites provides Argosy with the opportunity to create long term value and drive earnings and capital growth."

Value Add developments

8-14 Willis Street and 360 Lambton Quay, Wellington

Following recommencement of works post the Covid-19 lockdown, Argosy's green development at 8-14 Willis Street/360 Lambton Quay continues to progress. The project will now include an 11th floor to the 8-14 Willis Street building at an additional cost of $6.8 million. The tenant, Statistics New Zealand, will pay gross rent of $539 per m^2 for the additional space of 1,175m^2. The yield on incremental cost is 7.2%. The development was forecast to complete in August 2021. However, supply chain delays arising from Covid-19, design changes and the additional floor have resulted in a new expected programme completion date of February 2022. The company has discontinued negotiations with a major international retailer for the space at 360 Lambton Quay. However, Argosy is currently working with a number of interested parties for the available space.

54-56 Jamaica Drive, Wellington

This $5.6 million project for Big Chill completed in early September and new rents following completion of the development have commenced. Peter Mence said, "It's good to see this excellent Wellington industrial project complete and we'll continue to focus on the completion of our green office project at 8-14 Willis Street and 360 Lambton Quay."

Divestment of non Core Assets

Since 31 March 2020 year end, Argosy announced investment property divestments totalling $73.5 million on a weighted average premium to book value of 6.3% and include;

- 180-202 Hutt Road, Kaiwharawhara, in Wellington for $23.5 million, 11% above book value;
- 80 Springs Road, Auckland for $16.5 million, 2.3% above book value;
- 960 Great South Road, Auckland for $8.5 million, 16% above book value; and
- Corner of Wakefield and Taranaki Street, Wellington for $25.0 million, 1% above book value.

Peter Mence said "With a portfolio of Argosy's size, some properties will not continue to meet our investment criteria. After careful consideration, Argosy noted the above properties no longer met this criteria. The premiums received above book value demonstrate that the vendor market remains robust. Despite a challenging operating environment ahead, we remain focused on progressing Argosy's capital management plan. We continue to review the long term strategic ownership of all our properties, particularly around their ability to create or support long term value for shareholders."

Sale of Albany Lifestyle Centre

The Albany Lifestyle Centre is currently subject to a Sale & Purchase agreement but remains subject to purchaser due diligence.

Separate to the potential sale, the deposit of $4.5 million paid by the original purchaser, CPG Management Limited ('Cook Group') who nominated APF Nominee Limited as custodian for Augusta Property Fund, has been forfeited and has been treated as distributable income by Argosy.

Any receipt of payment for damages from Cook Group will also be treated as distributable income.

7 Waterloo Quay Wellington (7WQ) – Leasing, Façade Works and Insurance Claim Update

Reinstatement of all the office floors is now complete. Residual make-good works around the interchange are also nearing completion. The building is currently 82% leased with a WALT of 8.7 years underpinned by:

- Ground floor & Level 1; NZ Post 5.3 years, 4,430m^2
- Levels 2 & 10; Department of Internal Affairs (DIA), 9 years 4,133m^2
- Levels 3, 4 and 5: Kāinga Ora (formerly Housing New Zealand), 9 years 7,001m^2
- Levels 6, 7 and 8: Ministry of Housing and Urban Development (HUD), 9 years 3,675m^2

Argosy is in discussions with several potential tenants (including the Crown) for the remaining 3,650m^2 of space on Levels 9, 11 and 12.

The exterior façade of the building requires additional work and Argosy now expects this to cost approximately $15.5 million versus $10.0 million previously but with enhanced operational performance outcomes offsetting the additional cost (this work does not relate to the insurance claim referred to below). The timing of any works will be considered around the programmed removal of the tower scaffolding which is currently set for March 2021.

Argosy continues to work with insurers towards resolution of its insurance claim.

• The total claimed for material damage to 30 September 2020 is $50.7 million. These costs relate primarily to urgent reinstatement works required to make damaged levels of the building available for reoccupation and were not able to be agreed with insurers in advance. Further claims will be made in respect of additional reinstatement works as costs are incurred.

• Claims have been submitted to 30 September 2020 for business interruption costs (loss of rents, additional costs and claims preparation) totalling $15.1 million. The main component of this is loss of rents $14.3 million and no further claims in respect of loss of rents are expected.

• Argosy has recognised payments from insurers of $24.0 million (after a $4.9 million deductible) in relation to its interim claims. Of these, $10.9 million has been allocated to reinstatement of earthquake damage, $1.8 million to expense recoveries and $11.3 million to loss of rents.

Capital Management

At 30 September 2020, Argosy's debt-to-total-assets ratio, excluding capitalised borrowing costs, was 36.6% compared to 38.8% at 31 March 2020. The ratio reflects the net impact of development activity during the period, offset by divestments and desk top revaluation gains. The ratio also excludes the lease liability and right of use asset at 39 Market Place of $41.7 million, recorded in the period under NZ IFRS 16.

During the first six months Argosy added a new banking facility, Tranche I, for $75.0 million. This new Tranche expires in May 2024.

At 30 September, Argosy's total bank debt facility was $660.0 million ($585.0 million at 31 March 2020). The company's weighted average debt tenor, including bonds, was 3.2 years (3.6 years at 31 March 2020) and its weighted average interest rate was 3.74% from 3.95% at 31 March 2020. Following the issue of $125.0 million in green bonds in October, Argosy cancelled $125.0 million of banking facilities. The net effect of this saw Argosy's weighed average debt tenor increase to 4.0 years.

From a capital management perspective, Argosy's target gearing band remains at 30-40%. The Board regularly reviews the various capital management options at its disposal and remains comfortable that the band provides Argosy sufficient flexibility based on current market conditions and internal development forecasts.

At interim period end, Argosy remained well within all bank covenants and currently sits just above the middle of the target gearing band.

Argosy regularly reviews its investment portfolio against its investment policy framework criteria. Where properties no longer meet the criteria, they may be reclassified as non Core. At 30 September, Argosy had approximately $116.0 million or 6% of its portfolio classified as non Core, including the Albany Lifestyle Centre.

Dividends

A second quarter dividend of 1.6375 cents per share has been declared for the September quarter with imputation credits of 0.0709 cents per share attached. The second quarter dividend will be paid to shareholders on 23rd December 2020 and the record date will be 9th December 2020. The Dividend Reinvestment Plan (DRP) will be available for shareholders to participate in.

The full economic impact of Covid-19 is yet to be felt but the domestic and global economies will not be immune to the risk of further weakening. However, Management continues to work hard to minimise the impact of Covid-19 on tenants and the business. Argosy's tenant base remains resilient and defensive, underpinned by a quality portfolio of diversified properties by type and location.

Despite the potential challenges ahead, Argosy remains very focused on delivering sustainable dividends to shareholders.

Governance

On 28th July 2020, Argosy held its first ever hybrid Annual Shareholder Meeting (ASM) at the Royal New Zealand Yacht Squadron, in Westhaven, Auckland. While New Zealand was in Alert Level 1, the hybrid functionality of the ASM allowed investors to attend 'virtually' and participate in all elements of the meeting including being able to ask questions and complete all voting.

Argosy's Chairman Mike Smith and Chief Executive Officer Peter Mence both gave addresses on Argosy's performance during the 2020 financial year.

The ASM saw Rachel Winder and Martin Stearne both elected as directors by shareholders. The meeting was however most notable as being the last for chairman Mike Smith and director Peter Brook, after 18 years of loyal and valued service to Argosy. A director since 2013, Jeff Morrison was appointed as Argosy's new chairman, taking effect from the close of the meeting.

During the period the Board established an Environmental, Social and Governance (ESG) Committee to oversee Argosy's ESG Framework. It ensures sustainability factors remain front of mind to both preserve and create value for investors. Members of the ESG Committee are Mike Pohio (Chairman) and Rachel Winder.

Outlook

Argosy's management team has worked closely with tenants to support them during the pandemic and this strong tenant focus will continue over the remainder of the 2021 financial year.

Covid-19 is expected to deliver additional challenges to the domestic economy over the next 6-12 months.

Generally, Management expect to see ongoing operating headwinds with some sectors of the economy more impacted than others. Rising unemployment levels, weaker consumer confidence and challenging business conditions will create some degree of uncertainty. Offsetting these factors is a low interest rate environment which will provide positive economic stimulus.

Outlook continued

Noting all of the above, the Board's focus and message to shareholders is unchanged. The Board remains focused on ensuring the delivery of strategy, carefully managing the near term challenges with a view to delivering on the longer term goals.

Argosy's capital and portfolio position is sound. The issue of additional green bonds has diversified and extended its overall debt tenor. The divestment of non Core properties has supported the capital management program with funds reinvested into green development projects. Argosy's portfolio of quality investment properties has a diverse tenant composition which continues to provide resilience and stability to its cashflows. Such resilience and certainty of cashflows are increasingly important to investors.

For the remainder of FY21, the focus will be on addressing residual expiries within the portfolio and leasing up remaining vacancies. The focus on green developments and transitioning Value Add properties into higher quality ones, to drive earnings and capital growth is ongoing. This emphasis will continue Argosy's momentum towards creating further incremental value and sustainable dividends for shareholders.

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ENQUIRIES

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