Columbia Property Trust (NYSE:CXP)
Second Quarter 2018 Earnings Call and Webcast
July 26, 2018

These prepared remarks are provided for the convenience of investors only. For a recording of the full call, including the question and answer portion that followed these remarks below, please review the Q2 2018 Earnings Call webcast (link will be active for approximately 12 months after the call).

Matt Stover, Director – Finance & Investor Relations

Thank you and good afternoon everyone. Welcome to the second quarter 2018 Columbia Property Trust investor conference call. On the call with me today are Nelson Mills, President and Chief Executive Officer; Jim Fleming, Executive Vice President and Chief Financial Officer; and other members of our senior management team.

Our results were released this afternoon in our quarterly supplemental package which can be found on the Investor Relations section of our website and on file with the SEC on Form 8-K. We also filed our 10-Q with the SEC this afternoon. Additionally, we'll be providing a copy of today's prepared remarks on our website shortly after the call, and an audio replay will be available by this time tomorrow.

Statements made on today's call regarding expected operating results and other future events are forward-looking statements that involve risks and uncertainties. A number of factors could cause actual results to differ materially from those anticipated, including those discussed in the Risk Factors section of our 2017 Form 10-K. Forward-looking statements are made based on current expectations, assumptions and beliefs, as well as information available to us at this time. Columbia undertakes no obligation to update any information discussed on this conference call. During this call, we will also discuss certain non-GAAP financial measures. Reconciliations to comparable GAAP financial measures can be found in our supplemental financial data.

With that, I'll turn the call over to Nelson Mills.

Nelson Mills, President and Chief Executive Officer

Thank you, Matt, and thank you everyone for joining us today. It's an exciting time here at Columbia Property Trust, as the success of our portfolio transformation and leasing efforts continue to yield solid financial results. Best of all, we're in a strong position to capitalize on future opportunities ahead to create additional shareholder value.

The real estate we've assembled over the last several years is now one of the best-positioned portfolios in the entire office sector. Approximately 80% of our assets are located in the three high-barrier, coastal gateway markets of New York City, San Francisco, and Washington D.C. We've focused specifically on attractive sub markets within these cities, such as Midtown South in Manhattan, and the SOMA and Financial Districts in San Francisco.

As tenant demand for these exciting neighborhoods continues to grow, we have a targeted approach to offer tenants just what they want -- that is well-located and newly renovated boutique space with efficient floor plates. We've built a competitive position by meeting the market's demand for flexible, creative space coupled with attractive amenities and attentive services. This has translated to a strong leasing pace, at attractive rates and terms, across our portfolio.

The competitiveness of our portfolio is evident in our quarterly performance. As Jim will share in a moment, we're again raising our full-year guidance. The leased rate for our portfolio has now reached 97%, up from 95% a year ago. We generated normalized FFO of $0.39 per share, up sharply from $0.26 a year earlier. Our same-store NOI growth accelerated to 11.7%, up from 5.5% in the first quarter. We also leased 150,000 square feet in the second quarter, including Inspire Brand's headquarters at Glenlake, replacing the majority of Newell Rubbermaid's commitment which expires in 2020.

We have very few expirations in the next couple of years, but we're highly focused on proactively addressing longer-term expirations across the portfolio. We're making great progress on that front and look forward to reporting our success in the coming quarters.

We continued to reshape our portfolio during the quarter with the sale of 222 East 41st Street in Midtown Manhattan. This is a building acquired in 2007, which was occupied primarily by a single tenant. When we learned that the tenant would not renew, we launched a proactive leasing campaign that resulted in an innovative, full-building, 30-year lease to NYU Langone Medical Center with almost no downtime in occupancy. This enabled us to achieve an exit cap rate in the low 4s, with a gross sales price of $332.5 million.

The proceeds from this sale further strengthened our capacity to capture opportunities ahead. Our strong balance sheet remains a hallmark of Columbia, and we finished the quarter with leverage below 30%.

On top of that, we have strong NOI growth, with very little in the way of near-term lease expirations, and a significant number of signed leases starting to commence. The gap between our economic occupancy and our leased percentage will further narrow, driving even more growth in earnings.

We do have some current leasing opportunities, with 220,000 square feet of vacancy and 225,000 square feet scheduled to expire this year and next. We expect to achieve substantial rent increases for the vast majority of that space. In fact, we estimate that our in-place net rents today are, on average, 10% below current market rental rates.

This embedded growth will be evident in our industry-leading same-store NOI and FFO growth this year. But as I indicated earlier, we never stop seeking ways to create value, and 222 East 41st Street in Manhattan is just one example. 650 California Street in San Francisco's Financial District is another. We purchased this iconic office tower in 2014 and quickly revitalized it, enhancing its appeal to a broad range of tenants. We have re-leased a majority of the building to high-quality small- to mid-sized tenants – all with good credit – at triple-digit rent roll ups. The building is now 96% leased with an average remaining term of over six years.

Another example is 315 Park Avenue South in Manhattan's Midtown South district, a building we've re-positioned to drive leasing success. This quarter we signed another full-floor lease, leaving just one floor available. When we acquired the building in 2015, we knew we would get 17 of the 20 floors back through lease expirations in the first three years. We've now leased 16 of those 17 floors at substantial roll-ups in rent.

Looking ahead, our track record and balance sheet will enable us to continue our momentum and success. We're focused on: identifying and capturing compelling acquisition targets; enhancing our properties to attract demand; and proactive and innovative leasing – all geared toward continuing to grow cash flows.

I want to thank our team for their ongoing commitment, hard work and creativity in delivering these results. We have a terrific team and we're committed to improving it even further. To that end, I'm very pleased to welcome the newest member of our senior leadership, Dave Cheikin. As Senior Vice President of Strategic Real Estate Initiatives, he will bring further leadership and innovation to the operation of our real estate platform.

Dave spent the past 16 years with Brookfield Properties, most recently as head of the New York and Boston regions where he oversaw the company's 25 million-square-foot commercial office portfolio. Dave will be based out of our New York office and will provide operational leadership for our portfolio nationwide. He'll also provide direct oversight for our properties in New York, Washington D.C., and Boston, alongside our proven teams in those markets. We're very excited to have Dave on board.

As you can tell, we're excited about what we've accomplished, the results we're now generating, and the many opportunities ahead. We'll keep working hard to create value and to establish Columbia as the best operator in our markets.

And with that, I'll turn the call over to Jim.

James A. Fleming, Chief Financial Officer

Thank you, Nelson. We had another strong quarter and we're raising our guidance ranges today for our year-end leased percentage, our same-store NOI growth, and our FFO. These measures reflect the strength of our portfolio and the capabilities of our local leasing teams, and position us as one of the leaders in the office sector from a growth perspective.

We're now 97% leased across our portfolio, up another 30 basis points during the quarter, with limited roll over the next few years, and as Nelson mentioned we've re-loaded our balance sheet. These two factors provide an excellent foundation for further growth ahead.

We have a shrinking but still meaningful gap between our economic occupancy and our leased percentage. Currently at an eight percentage point spread, this is down from 13 percentage points a quarter earlier. Our year-end forecast for economic occupancy is 92 to 93%, and this should drive another $17 million of annualized revenue over today's level.

Second, at 97% leased, most of the heavy lifting with our current portfolio has been accomplished, but we have another 220,000 square feet of available space to lease, much of which is in our most attractive and desirable buildings. We also have 225,000 square feet of leases expiring the second half of this year and in 2019, which creates more opportunity for our leasing teams to capitalize on lease roll-ups.

Our balance sheet has continued to improve, with most of the proceeds from the sale of 222 East 41st Street used to pay down debt. We ended the quarter with more than $4 billion of unencumbered properties, and our net debt is now less than 30% of gross assets. We recently gave notice to pre-pay our Glenlake mortgage in October, which will leave us with only one mortgage loan in our entire portfolio. Our debt to EBITDA ratio is down to 6.2x and as we've previously said, we expect it to be around 6x for the full year 2018. Now that we’ve re-loaded our balance sheet, we will continue to seek attractive opportunities to invest in growth assets so we can build on our recent success.

Based on the strong second quarter results and our outlook for the rest of the year, we're again raising our normalized FFO guidance to a new range of $1.46 to $1.51. This range reflects very robust growth of 28 to 32% over 2017 levels, and we see AFFO rising even more. We’re also raising our outlook for full-year, same-store NOI growth to a range of 11% to 13%, and we now expect a year-end leased percentage of 95% to 97%.

With this quarter's share repurchases, we’ve now repurchased $42 million of stock year to date, reducing our share count to 118 million shares. That level could fall further as we remain opportunistic buyers of our stock given our strong balance sheet, with $153 million still available under our current share repurchase authorization.

After a lot of hard work and good execution over the past several years, we’re now in a very good position: we have strong growth in earnings and cash flows, very little near-term leasing risk, a solid balance sheet, and a high quality portfolio. We believe our stock also provides great value today.

We look forward to updating you again on our progress at the end of October, and with that, Nelson and I will be happy to take your questions. Operator, if you could please open the lines.

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