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133 Castlereagh Street  
Sydney NSW 2000  
www.stockland.com

T 02 9035 2000  
F 02 8988 2552

## STOCKLAND 1H19 RESULT – DEVELOPMENT INCOME SKEWED TO SECOND HALF

### Financial results for the half year ended 31 December 2018

- Funds from operations (FFO) of \$407 million, down 6.7% on 1H18 reflecting residential profit skew to 2H19
- FFO per security of 16.8 cents, down 6.7% on 1H18
- Adjusted funds from operations (AFFO) of \$352 million, down 6.9% on 1H18
- AFFO per security of 14.6 cents, down 6.4% on 1H18
- Statutory profit of \$300 million, down 56.2% on 1H18, reflecting losses on financial instruments, reduced commercial property valuation increases relative to 1H18, retirement living fair value changes and a tax expense (1H18 included a tax benefit)
- Return on equity (ROE) of 10.6%, down 60 basis points on FY18, excluding workout projects
- Net tangible assets (NTA) per security of \$4.19, up 0.2% on FY18
- Distribution per security (DPS) of 13.5 cents, up 3.8% from 1H18

### Capital Management

- Gearing: 26.4%, and Covenant limit now 50%, from 45%
- Weighted average debt maturity: 5.3 years, compared to 6.2 years at FY18
- Weighted average cost of debt: 4.4%, compared to 5.2% in FY18
- Credit rating: A-/stable (S&P), A3 (Moody's)

### Commercial Property

- FFO: \$314 million up 3.8%; comparable growth of 1.7%
- Retail FFO: \$218 million up 4.3%, comparable growth down 1.1%
- Comparable specialty sales per square metre growth of 4.8%, total foot traffic up 4%
- Logistics FFO: \$81 million, comparable growth of 4.5%
- Workplace FFO: \$24 million, comparable growth of 10.5%

### Communities

- Residential: Operating profit: \$142 million, down 21.8%, operating profit margin: 21.6% compared with 20.9% for 1H18
- Retirement Living: Operating profit: \$20 million, up 8.3%

### Outlook for FY19

- FFO per security growth for FY19 is expected to be around 5 per cent, at the lower end of our 5-7 per cent guidance range, reflecting weaker market conditions. This assumes no material deterioration in current market conditions.
- Reaffirming an estimated full year DPS of 27.6 cents, a 4% increase on FY18, assuming no material deterioration in the current market conditions.

#### For media enquiries

**Larissa Webster**  
Senior Manager  
Media & Communications  
M +61 (0)418 254 959

#### Amy Menere

General Manager  
Stakeholder Relations  
T +61 (0)2 9035 2551  
M +61 (0)422 449 310

#### For investor enquiries

**Antoinette Plater**  
National Manager  
Investor Relations  
T +61 (0)2 9035 3148  
M +61 (0)429 621 742

#### Stockland

Stockland (ASX: SGP) was founded in 1952 and has grown to become Australia's largest diversified property group – owning, developing and managing a large portfolio of shopping centres, residential communities, workplace and logistic assets and retirement living villages. Stockland is rated as the most sustainable real estate company in the world in 2018 by the Dow Jones Sustainability World Index (DJSI). Stockland is also an Employer of Choice for Gender Equality, as recognised by the Workplace Gender Equality Agency.

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Stockland Managing Director and CEO Mark Steinert said: "Our results for the half were generally in line with our expectations, with lower first half profit primarily due to a second half residential profit skew in FY19 versus an atypical first half skew in FY18, and the impact of retail remixing. Weak housing markets and ongoing headwinds in the retail sector will likely see our full year results at the lower end of our guidance range for FFO per security growth of 5-7 per cent.

"We have been highly proactive in our approach to these market challenges, and focused on positioning our business to mitigate downside risk.

"Our residential settlements were in line with expectations, as the strength of our brand, community offering and focus on owner occupiers provided resilience in a challenging market.

"In spite of reduced credit availability and investor tax policy uncertainty, factors such as growth in underlying owner occupier demand, government policy support for first home buyers, generally balanced supply and resilient economic conditions support confidence in the master planned community market which is 85 per cent of our business. In the first half, owner occupiers represented around 87 per cent of our buyers, our profit margins are stable and cancellation rates remain below the long term average.

"The retail market continued to experience a number of challenges including ongoing administrations, reduced credit availability to franchisees and increased statutory and operating costs. Our retail portfolio results were impacted by these factors as we continue to undertake proactive remixing. Our workplace and logistics portfolio performed very well, with strong leasing and development activity setting the portfolio up to deliver good returns this financial year and into the future.

"During the half we renewed our leadership team, undertook a detailed review of our assets and refined our strategy to position our business for sustainable growth. This new team has accelerated the execution of our strategy and increased the scope of capital release from commercial property asset sales, and we are driving further improvement in the quality of our portfolio, and improving our income resilience. Progress to date includes:

- Achieved \$113 million of retail town centre divestments (Stockland Bathurst and Stockland South Caloundra). We are on track to achieve our target of \$400 million of divestments in the next 18 months and beyond this, we will look at further non-core retail divestments up to \$600 million in a disciplined way to progress our targeted re-weighting to Workplace and Logistics.
- Increased our weighting to Logistics, which now makes up around 16 per cent of our portfolio, an increase in assets of 18 per cent since 1H18, and we are on track to achieve a 25-35 per cent weighting for Workplace & Logistics in the next five years (weighting is currently 21 per cent).
- Successful sale of The Grove community in Melbourne at a 59 per cent premium to book value. This demonstrates the overall quality and value of our residential landbank and reaffirms our commitment to recycling capital released from divestments into accretive investments, including our securities buy-back.
- Made a number of improvements to our retirement living portfolio, completing development projects providing FFO growth this half and identifying a number of non-core villages for divestment as we continue to improve the overall quality of the portfolio.
- Progressing a capital partnership for the retirement living business, with advisers appointed and due diligence underway. Initial interest from investors has been good, reflecting the quality and strength of our operations and the annuity income stream.
- We are also actively progressing capital partnering opportunities across all other sectors represented in our business, with ongoing engagement with a range of potential domestic and international partners.

- Executed \$115 million of our \$350 million buy-back of Stockland securities, which delivered accretion of 0.1 cents to EPS for the half, a prudent use of capital at this point in the cycle which will help support the resilience of security holder returns into the future.

“While we will remain focused on executing our strategy to create sustainable communities, own and manage leading retail town centres and grow our workplace and logistics asset base, we have increased the rate at which a number of our priorities are being executed in order to improve the quality of our portfolio and the resilience of our income. We are also extremely active in broadening our capital base via a range of well-progressed capital partnership discussions,” said Mr Steinert.

## **FINANCIAL & CAPITAL MANAGEMENT**

Chief Financial Officer Tiernan O'Rourke highlighted the Group's focus on active capital management for this part of the cycle.

“Over the half, we've sustained disciplined capital management and made a conscious decision to raise our gearing to 26.4 per cent, reflecting the skew of pre-sold development settlement timings to the second half and the timing of asset sales. We expect gearing to be maintained around this level for the full year, which is within our 20 - 30 per cent target range, as we continue to execute on our strategic priorities over the next few years.

We have completed the renegotiation of our debt documentation including the update of terms and conditions to be consistent with the market and our peers.

“As a result, the Total Liability to Total Tangible Assets covenant definition has been replaced by Financial Indebtedness to Total Tangible Assets, and the limit increased to 50 per cent (from 45 per cent) across all markets making up our total debt portfolio.

“This shift from a total liabilities to a financial indebtedness methodology and the limit increase have combined to improve our borrowing capacity by over \$2 billion to around \$3 billion of headroom.

“We've continued to actively manage the Group's liquidity over the half, through the use of bank debt and short-term Commercial paper issuance. This has seen us improve our weighted average cost of debt (WACD) over the period to 4.4 per cent, from 5.2 per cent in FY18, while our weighted average debt maturity (WADM) reduced to 5.3 years, compared with 6.2 years as at 30 June 2018. We expect our WACD for the full year to be circa 4.5 per cent, but our WADM to increase as we issue planned long-term debt during the first half of the 2019 calendar year.

“The maintenance of our A1-stable credit rating from Standard and Poor's and A3 credit rating from Moody's demonstrates the resilience of our balance sheet and provides access to a broad range of debt markets on competitive terms and tenors, placing us in a strong position for the future,” Mr O'Rourke said.

“We've taken a prudent approach to revaluing our commercial property assets, completing independent revaluations of 86 per cent of our portfolio over the last nine months and 71 per cent of the portfolio over the last six months, resulting in an overall net valuation uplift of \$27 million at 31 December 2018. This included a strong \$200 million uplift for our workplace and logistics portfolio, and a \$173 million decline in retail town centre valuations, which reflects lower forecast rental growth, place-making and upgrading capital expenditure, rent reductions associated with re-mixing and capitalisation rate increases reflecting transactional evidence from the broader market.”

## **COMMERCIAL PROPERTY**

Stockland's Commercial Property business delivered stable results, with comparable FFO growth up 1.7 per cent, with continued challenges in the retail sector offset by the strength of the workplace and logistics markets.

Mr Steinert said: "There has been a structural shift in the retail sector and consumer needs. Louise Mason and her team have implemented a number of changes to re-shape our Commercial Property portfolio to improve overall quality, and are actively changing the tenant mix in our retail town centres for long term resilience of lease income, and completing non-core divestments.

"This includes taking a firm view on our core and non-core assets incorporating recent trading patterns, trade area fundamentals, forecast tenant demand and a further assessment of capital expenditure requirements. Core assets reflect leading town centres with strong and growing trade areas with limited competition, and where we have the opportunity to enhance the asset to generate sustainable income growth over time.

"We have reviewed our development pipeline, which shows an increased investment in development projects in our Workplace and Logistics pipeline at or above our hurdle rates, while the retail town centre pipeline has been reduced by around 50 per cent as our development focus shifts to smaller, curated retail town centre enhancements."

### ***Retail town centres***

Mr Steinert said: "While comparable FFO of -1.1 per cent was down on the last half due to remixing related rent adjustments and higher outgoings, we maintained high occupancy across our retail town centres in 1H19 and reported a 4.8 per cent increase in comparable specialty sales per square metre to \$9,295. Foot traffic was also up 4 per cent over the past 12 months.

"Our centres are focused on providing convenient, everyday shopping for our communities, with non-discretionary spend making up around 70 per cent of our total sales, giving us some protection from the challenging retail environment and the growth in online retail.

"Our strategy of remixing and increasing our focus on services, lifestyle, health, dining and entertainment are helping to drive foot traffic into our centres. We have a deliberate strategy to re-mix out of apparel into food and lifestyle categories, which are generally underserved in our main trade areas. We have delivered comparable specialty sales per square metre growth of 5.7 per cent in cafés/restaurants and 3 per cent in food catering for the half, reflecting the success of this re-mixing approach."

### ***Workplace and Logistics***

Stockland's workplace and logistics business continues to perform very well, delivering high occupancy, strong leasing activity and solid rental growth. We achieved comparable FFO growth of 4.5 per cent in Logistics for the half from positive leasing results.

The Logistics market continues to be supported by ongoing investment in infrastructure and the growth in online retail. Our assets are predominantly based in the strongly performing Sydney and Melbourne markets, and we continue to pursue opportunities in these markets. The value of our Logistics portfolio has grown to around \$2.5 billion, up \$0.3 billion from 30 June 2018, including two new logistics developments at Ingleburn in Sydney and Willawong in Brisbane at risk adjusted IRR's above 10 per cent and FFO yields above 7 per cent.

Mr Steinert said: "Our development program has delivered \$99 million of new projects, with a further \$56 million of projects under construction and an additional development pipeline of over \$740 million, targeting 6-7 per cent FFO yields and centred on eastern seaboard capital cities."

"Just before the end of the half, we announced that we will develop the first stage of the new Melbourne Business Park in the western suburbs, the fastest growing logistics precinct in the State, with Mount Atkinson Holdings. This land is adjacent to our Mount Atkinson residential community, in close proximity to road and rail infrastructure, and part of a growing precinct which is projected to provide 18,000 future jobs. This transaction clearly demonstrates our ability to extend our capital partnerships and the synergies created by the diversified Stockland business.

“We have achieved strong returns from our Workplace portfolio, with comparable FFO up 10.5 per cent, reflecting the quality of our assets, predominantly located in the Sydney market. We are progressing development opportunities for our Sydney office assets, including the Piccadilly Centre in the CBD and 110 Walker Street in North Sydney. These are well-located assets for workplace and mixed use development, leveraging our master planning and development expertise,” said Mr Steinert.

## **COMMUNITIES**

### ***Residential***

Mr Steinert said: “Our Residential business achieved a good performance in a challenging market, with 2,460 settlements for the half in line with expectations, with a more typical skew to the second half of the financial year. We are in a good position for the next half, with over 5,900 contracts on hand, including around 3,600 due to settle in 2H19 and the majority of the balance to settle in FY20.

“We are the leading creator of liveable, affordable and connected master planned communities in the country. This means we are uniquely positioned to leverage our scale, brand and understanding of our customers’ needs, to drive sales in a moderating environment. This has been demonstrated by the growth in our market share\* from 14.1 per cent to 15.6 per cent over the past six months.

“The housing market has moderated overall and we expect this to continue in the year ahead. Conditions in our sub markets are varied, we have seen declines in south-west and north-west Sydney land markets, and land markets in Melbourne. Despite this, we are still experiencing solid demand for our well-located projects, including the recently launched Minta Farm community in Melbourne’s south-east and our Aura community on the Sunshine Coast.

“The vast majority of our communities are in key growth corridors within close proximity to rail and transport links, in markets that continue to be driven by structural undersupply. Around 50 per cent of our residential customers are first home buyers and around 87 per cent are owner-occupiers, which places us in a good position in the current residential lending and policy environment,” said Mr Steinert.

Stockland expects operating profit margins of above 18 per cent in FY19, and around 17 per cent for the medium term before normalising to around 14 per cent over the long term, as we undertake more built form and a number of very high margin projects complete. These margins are subject to market conditions.

### ***Retirement Living***

Mr Steinert said: “We have made a number of changes across our retirement living portfolio to drive increased returns from this part of our business.

“We have enhanced our product offering and relative pricing in our development villages, which delivered 140 sales for the half, a 57 per cent improvement on the prior corresponding period. These results demonstrate our ability to leverage our brand, sales capability and development expertise to improve overall performance.

“Established village settlements are down 10.3 per cent for the half, reflecting the correlation of this business to the broader housing market, but the reduction is substantially less, demonstrating the lower volatility in the retirement living sector.

“As part of our focus on improving returns, we have undertaken a detailed review of our portfolio to determine core and non-core assets. We have appointed agents to begin the process of selling non-core villages where there is limited scope to deliver our customer value proposition to drive demand.

“We remain committed to meeting customer needs in this market, by providing clarity and transparency about our offering. We’ve maintained strong customer satisfaction levels of over 85 per cent and we are driving sales from referrals,” said Mr Steinert.

## SUSTAINABILITY & INNOVATION

Mr Steinert said: "We are proud of our leadership and commitment to excellence in sustainability. In 2018, we signed on to the World Green Building Council's Net Zero Carbon Buildings Commitment, which includes a net zero emissions target for our logistics centres, retirement living operations, and corporate head offices.

"We were recognised as the most sustainable real estate company in the world by the Dow Jones Sustainability Index, we received Global Sector Leader status for Listed Diversified Office/Retail respondents from the Global Real Estate Sustainability Benchmark, and we were the only Australian real estate company included in the 2018 Climate Disclosure Panel Climate A-List.

"We have continued to focus on innovation and technology to position our business for the future. This includes launching LAB-52, an internal innovation space which has facilitated the rollout of digital customer initiatives like map tables in our sales centres, and artificial intelligence initiatives are driving our customer journey assessment. We also launched Stockland 'proptech' Accelerator, powered by Blue Chilli which is being used to identify solutions to emerging customer needs. On the technology front, we continue to expand our data analytics and cyber security capability."

## OUTLOOK

Mr Steinert said: "Current market conditions are mixed, with sound economic fundamentals including continued employment growth, low interest rates and a bi-partisan commitment to infrastructure investment being offset by the deterioration in the housing market, reduced credit availability, investor tax policy uncertainty and weak consumer sentiment.

"We expect further price declines in residential land of around 5 per cent over this calendar year, concentrated in Sydney and Melbourne.

"In line with guidance, over 6,000 residential settlements are expected for FY19. The profit from the sale of The Grove community will be released over FY19-21 in line with the settlement timing of the various parcels sold. FY19 profit will be unaffected by this transaction, as the profit recognised equals the previously forecast FFO from land settlements on this project during the second half of the year.

"We expect our Commercial Property business to maintain moderate growth in returns, with comparable FFO growth of 2 – 3 per cent reflecting continued challenges in the retail market and strength in the workplace and logistics market.

"Assuming no material deterioration in the current market conditions, we remain on track to achieve FFO per security growth of around 5 per cent, at the lower end of our 5-7 per cent guidance range, reflecting weaker market conditions, and a full year distribution of 27.6 cents per security, representing growth of 4 per cent.

"A disciplined approach to the execution of our strategy will continue to be our key focus as we enter into a different phase of the property cycle, with our new leadership team committed to improving the overall quality of our portfolio and delivering security holder value into the future."

**Stockland's 1H19 results presentation will be webcast via [www.stockland.com.au](http://www.stockland.com.au) on Wednesday 20 February at 11:30am (AEDT). Toll free dial in 1800 059 809 or +61 2 9009 0729**

*\* National Land Survey, December 2018 – June 2018 market share data rebased*