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Pennsylvania Real Estate Investment Trust (PEI)

Q2 2020 Earnings Call

CORPORATE PARTICIPANTS

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Christy McElroy
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Michael W. Mueller
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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the PREIT Second Quarter Earnings Call. At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions]

I would now like to hand the conference over to one of your speakers today, Heather Crowell. Thank you. Please go ahead, madam.

Heather Crowell

Executive Vice President-Strategy & Communications, Pennsylvania Real Estate Investment Trust

Thank you. Good morning, and thank you everyone for joining us for PREIT's second quarter 2020 earnings call. We hope everyone is staying well. During this call, we will make certain forward-looking statements within the meaning of federal securities laws. These statements relate to expectations, beliefs, projections, trends, and other matters that are not historical facts and are subject to risks and uncertainties that might affect future events or results. Descriptions of these risks are set forth in the company's SEC filings. Statements that PREIT makes today might be accurate only as of today, August 11, 2020; and PREIT makes no undertaking to update any such statements.

Also, certain non-GAAP measures will be discussed. PREIT has included reconciliations of such measures to the comparable GAAP measures in its earnings release and other documents filed with the SEC. Members of management on the call today are Joe Coradino, PREIT's Chairman and CEO; and Mario Ventresca, our CFO.

We will limit today's call to 30 minutes. Our prepared remarks will last approximately 15 minutes and then we will take questions. To allow a chance for everyone, we will allow one question and one follow up per caller. Thank you in advance for respecting our time constraints. Joe?

Joseph F. Coradino

Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

Thank you, Heather, and thank you all for joining us. We actually miss you guys and hopefully we'll see you soon, and we also hope that you continue to stay safe. The past few months have been intense and challenging as a world, as a country and certainly as a sector, our resolve continues to be tested. It's important to note that our results reflect the closure of our malls for an average of 86 days, nearly the entire quarter. As we entered the third month of the quarter we had only five properties open. Nonpayment of rent of course impacted our results and our liquidity position.

As Thomas Paine said these are times that try men's souls. So we're going to focus this call on the recovery of our sector and the steps we're taking to get stronger. As of today all of our properties are open. This is a modified open, it includes capacity restrictions, used prohibitions in a more challenging shopping experience. We're getting close to our goal line probably in the red zone and while we share details on our quarter and you may be tempted to compare them across the sector. But broadly speaking, we really didn't have a quarter. We were not open for business. That said, upon reopening we've been pleased with traffic and shopping patterns occurring across the portfolio. We've seen a purposeful shopper carrying multiple bags, we've seen our market dominance properties recover quickly, comparatively improving your market position upon reopening.

Some examples, Capital City Mall, which is essentially the only mall in Harrisburg-York market where there were once three malls is generating traffic in the 70% to 85% range of prior traffic and is 98.6% occupied, which is great under stabilized circumstances. We've got [indiscernible] (03:51) customer there and many tenants report beating their July sales goals. At Patrick Henry Mall, that's pretty amazing. We continue to see traffic at an impressive 105% of average. Patrick Henry is the only mall on the Hampton Roads Peninsula boasting seven military bases. And we're reaping these benefits of addition by subtracting – by subtraction boasting the only remaining Macy's on the peninsula.

Throughout the portfolio, areas in strengths include athletic shoes, self-care, jewelry and athleisure. Back-to-school spending is expected to break records this year as parents prepare for combinations of in-class and at-home learning. We believe the diverse tenancy we have in place positions us well to capitalize on these shifting trends. We do note that properties that rely more heavily on dining and entertainment that remain restricted by partial opening of restaurants and non-operating movie theaters have been slow to recover traffic, which indicates that these are popular venues that we expect will regain traction if they become fully operational. We're also excited to see new tenants in our portfolio. Yes, there are tenants opening in our portfolio.

Kate Spade, Industrious, francesca's opened at Fashion District Sephora, Tempur-Pedic and Jamba opened at Woodland, Talbot's Outlet, Restore Cryotherapy and Plymouth Performing Arts Center opened at Plymouth Meeting. And we also have a number of key tenants under construction still open, Planet Fitness at Moorestown, Solar and Shake Shack ay Plymouth Meeting, White House Black Market at Woodland, Pete's and Arden at Willow Grove, [indiscernible] (05:57) at Capital City and Miller Ale House (sic) [Miller's Ale House] (05:59) and Mall at Prince George's. So we are beginning to regain some level of normalcy and continue to open stores in our properties. Fashion District, which opened on July 3 is 69% reopened. Now that number is affected by Round One, AMC and City Winery continuing to be closed. When they open, the number increases to nearly 80%. When you include executed leases for stores that will open this year, we expect to exceed 90% occupancy at Fashion District by year-end. We're pretty excited about that by the way that's been a long road to [indiscernible] (06:49) and one where we think we'll continue to generate positive trends.

We believe we've installed among the best safety precautions in the industry and are mindful of the changing nature of restrictions and requirements. As of August 7, 83.1% of our core portfolio has reopened which is impacted of course by theaters remaining closed. Across the portfolio, traffic is registering 68% of pre-COVID averages and grew at nearly every property for the past two weeks. It's noteworthy that 12% of our tenants report outperforming pre-COVID sales.

Openings and their strength are an important precursor to improving collections. We were among the last to be able to open a majority of our portfolio. Cash collections are improving but not yet meeting occupancy levels. From April through July, our cash collections were 53%. As more of our properties opened and we execute deferrals with key national tenants these figures are improving. We expect to ultimately collect 85% of COVID period rents that would be April, May, June and July. Since the beginning of 2020, we've seen bankruptcy filings that impacted 101 stores in our portfolio operating at of 2.4 million square feet. If we exclude J.C. Penney, these stores occupy about 388,000 square feet and pay gross rents of $12.5 million.

Regarding J.C. Penney, we believe we fared well with only 2 of 14 stores on the closing list. We expect to minimize our capital outlay on these locations by taking advantage of their placement within the respective properties and not replacing them with an anchor, but with in-line retail and decommissioning the rear portion of the store or simply moving the non-retail usage in one case residential. The impact of the pandemic and resulting closure of our properties for an extended period of time has had an impact on our liquidity.

As you saw in our release, we did get temporary covenant relief and we're pleased today to report that we've also signed documents for $30 million bridge loan that is expected to close before the end of today and run for a period of time during which we hope to finalize a long-term transaction. As we had we had previously reported, we continue to work with our bank group to structure a long term modification to our credit facility.

When you look at the future of our business, it's natural at a time like this to focus on the worst case. However, taking a more constructive approach, we're seeing occupancy and traffic exceed our expectations as evidenced by both construction in progress and recent openings. So there is cause for optimism regarding our core business. Having said that, we're also experiencing bankruptcies and store closings, which are giving rise to interest from a variety of alternative uses. As of this call, we're negotiating agreements with a healthcare provider, a food market are in discussions with several fulfillment and logistics operators and are exploring opportunities to incorporate research and lab facilities at our properties. This of course is in addition to multi-family and hotel users that are already underway.

This interest and this is an important point [indiscernible] (11:01) in the quality of the locations and the underlying demographics associated with the portfolio with a concentration in high barrier entry markets like Philadelphia and D.C. In the final analysis, we own quality real estate that is suitable for a vast array of alternative uses. And one thing that isn't changing is that our holdings are vital contributors to the communities they call home. Thousands of jobs and hundreds of community events depend on our properties. In fact, since the pandemic began we've hosted three dozen community and charitable events at our properties.

This summer, we're hosting another two dozen community events branded Park and Play, an outdoor event series that spans a variety of activities ranging from drive in movies to virtual concepts to unique crab and seafood festival and more. As people grapple with uncertainty, they crave normalcy, people in places they're familiar with and bring them comfort. That's what our properties offer.

Now I'll turn it over to Mario.

Mario C. Ventresca

Executive Vice President & Chief Financial Officer, Pennsylvania Real Estate Investment Trust

Thank you, Joe. As Joe noted the results that are being communicated today are reflective of a portfolio that was essentially closed for the entire second quarter. During the quarter, we came together as a team working from our homes to mobilize and combat the impacts of COVID on our company. In that regard, we have made tremendous strides although we've recognized there is much more that we need to accomplish. For the second quarter, we've reported an FFO loss of $0.06 per share and an FFO loss of adjusted of $0.06 per share. For the six months of the year we reported FFO of $0.08 per share and FFO as adjusted of $0.09 per share.

Same store NOI during the quarter decreased by $17.4 million. The primary drivers of the decline in our wholly owned portfolio were COVID mall closures, associated rent abatement and percentage sales revenue declines of $11.5 million and loss rent from bankruptcies of $2.2 million. Note, we elected to record the rent abatements upfront in their entirety during the second quarter. The impact of these one-time reductions in NOI and FFO is $0.14 per share. We also recorded an increase in credit losses of $3.7 million. Offsetting some of this [ph] which came in (13:44) real estate tax expense savings of just under $2 million.

Non-same-store NOI decreased by $2.7 million due to the sale of Whole Foods at Exton and the closure of several anchors in Valley View at Exton Square Malls. Interest expense was $1.6 million higher due to a higher level of borrowing than the second quarter of last year. We also focused on managing our cash expenditures in addition to previous one-time savings and G&A and operating expenses totaling $4.7 million, we made permanent overhead reductions. We laid off 31 employees and this is expected to save the company approximately $4 million annually in G&A expenses. We also have reduced plain capital spending for 2020 by $26 million.

During the quarter, nine of our tenants filed for bankruptcy protection. The store count impacted by second quarter bankruptcy was 51 in 2.1 million square feet contributing approximately $10.2 million in annual revenues. Several tenants filing for bankruptcy during and after the second quarter were significant in both the number of stores and square footage such as J.C. Penney, GNC, New York & Company and Ascena brands. We expect that most of the stores impacted by bankruptcy will remain open.

In April, we received a $4.5 million Paycheck Protection Program loan under the CARES Act for which we expect to be granted complete forgiveness of the obligation. We also during the quarter negotiated forbearance arrangements for mortgages on six wholly-owned and two joint venture properties. And on July 24, we obtained waivers through August 31, 2020 on certain covenants and approval to enter into a $30 million bridge facility that as Joe said, we expect to close today. For the duration of this agreement, which expires the early of September 30, 2020 or completion of a long-term credit facility expansion dividends will be suspended. We have been engaged in discussions with our bank group regarding this recast of the credit facility.

Looking ahead including our joint venture assets, we have over 325,000 feet at executed leases in our pipeline for future openings, most of which are scheduled to open in 2020 and will contribute $11.7 million of annualized revenues at our share. This revenue will come online and get our P&L towards the back half of this year. During June, we completed our single tenant outparcel sales initiative after closing on the remaining $14.4 million in outparcel sales with FCPT and recorded a gain on sale of $9.2 million in the second quarter for the six outparcels. The outparcel sale efforts gross proceeds totaled $27.8 million.

As we've reported in the past, we have five purchase and sale agreements with four institutional investors for the sale of our land dedicated to multi-family development. We continue to make progress toward entitlement of this land that will lead us to a closing. We have been extending due diligence in closing dates on these deals while we've been working through the zoning and anchor approval processes.

We will also continue to extend due diligence as a result of COVID-19 related financing market challenges for the sale leaseback transaction for the five properties for $154 million. This is now forecast to close in 2021.

And with that, we'll open it up for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from Christy McElroy of Citi. Your line is open.

Christy McElroy
Analyst, Citigroup Global Markets, Inc.

Q

Hi. Good morning. Thank you. Joe, you made a comment that you expect to I think ultimately collect 85% of the COVID period rents. Just if I think about the 15, would you expect the majority of that remaining 15 to be as we think about a permanent impairment here NOI going forward, as you think about as you can see loss that you suffered during the quarter that you'll continue to see and then permanent rent relief that you expect to put in place?

Joseph F. Coradino
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

A

Christy, that's when we embarked upon thinking through our COVID period rents. We decided that the retailers who were local and we define them as having less than a certain number of stores that they own that we were going to abate some of their rent. And they were both specialty retailers' carts et cetera as well as just local retailers who might operate one restaurant or something of that sort where they're kind of living out of the cash register. And for those tenants we were more willing to abate. So the bulk of those dollars come from that and are really a one-time COVID event if you will.

Christy McElroy
Analyst, Citigroup Global Markets, Inc.

Q

Okay. So is there any permanent rent relief as we think about whether company we feel is going through the bankruptcy process or outside of bankruptcy that you're granting at this point?

Joseph F. Coradino
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

A

At this time, no. Again, we're through about 60% of are negotiating let's call the marquee national tenants, some of which include the furlough. I might add a number of tenants upon reopening that we were negotiating with and it's more than one or two just decided, we're not going to negotiate, we're going to pay the rent. And they paid all the back rent. So, we're about 60% through with probably another 10% at – 10% or 15% at hand and that next 25% is going to involve some bank and so to speak and hopefully, we will resolve it outside of litigation. But that's a course of action we're not going to be shy to take, if necessary.

Christy McElroy
Analyst, Citigroup Global Markets, Inc.

Q

Okay. Thanks. And then just in terms of the new $30 million term loan. Can you just give a few more details like the rate, the term, any warrants, who is the lender, is there any security against the loan and it's effectively I guess giving you working capital as you bridge to get to the asset sale closing?

Joseph F. Coradino A
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

Well. Essentially, as you said it's a $30 million deal. It's a LIBOR plus about 800 bps and it's a short-term bridge. It matures September 30, and again allows us to sort of smooth over the impact of those deferments and abatements during that period of time and really gives us the ability and the time to negotiate a longer term deal with our banks.

Christy McElroy Q
Analyst, Citigroup Global Markets, Inc.

Okay. Thank you.

Operator: [Operator Instructions] Your next question comes from Mike Mueller of JPMorgan. The line is open.

Michael W. Mueller Q
Analyst, JPMorgan Securities LLC

Yeah. Yeah. Hi. Just two quick ones here. One how did rent collections trend in July compared to that whole 53% COVID period? And then can you just give us an update on the timeline for the land sales?

Joseph F. Coradino A
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

Mario, I'm going to turn that one over to you.

Mario C. Ventresca A
Executive Vice President & Chief Financial Officer, Pennsylvania Real Estate Investment Trust

Yeah, Mike. Hi. It's Mario. As it relates to July, we actually on a total cash receipt basis, meaning tenants that paid their July rent and a portion or all of their back rent, we ended up collecting 106% of our July billings during the month.

Michael W. Mueller Q
Analyst, JPMorgan Securities LLC

Got it. Okay. And then anything on the asset, the land sale timeline?

Mario C. Ventresca A
Executive Vice President & Chief Financial Officer, Pennsylvania Real Estate Investment Trust

Yeah. I'd say the asset sales – I'll turn this one to...

Joseph F. Coradino A
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

At this point, the asset sales are really being driven by entitlements and we are making progress on those, demonstrable progress at Willow Grove and Plymouth Meeting and Moorestown and our properties in D.C. both

Mall at Prince George's and Springfield Town Center and our – we did push them out a bit. But the expectation is that they will come to closing and I think the schedule now is...

Mario C. Ventresca
Executive Vice President & Chief Financial Officer, Pennsylvania Real Estate Investment Trust

A

Yeah, two will close the second quarter of next year with the balance ratably through the second quarter of 2022.

Michael W. Mueller
Analyst, JPMorgan Securities LLC

Q

Got it. Okay. Thank you.

Mario C. Ventresca
Executive Vice President & Chief Financial Officer, Pennsylvania Real Estate Investment Trust

A

You're welcome.

Operator: There are no further questions. At this time, I turn the call back over to the presenters.

Joseph F. Coradino
Chairman & Chief Executive Officer, Pennsylvania Real Estate Investment Trust

Well, thank you all for participating in the call. We'll continue to stay in touch, again look forward to, at some point seeing one another. Again we think we've created a portfolio or the impact from bankruptcies has been not nearly as devastating as we thought it was going to be to J.C. Penney's. We have a portfolio that we think is able to withstand the impact of COVID and we look forward to continuing to have the company grow stronger as we get to the other side of this. So, thank you all. Stay safe and stay strong.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.