Transcript of
JLL Income Property Trust
3Q16 Public Earnings Call
November 22, 2016

Participants

Allan Swaringen – President and CEO
Gregg Falk – CFO and Treasurer
Sam Podwika

OPERATOR
On behalf of JLL Income Property Trust, I'd like to welcome you to their third quarter 2016 earnings conference call. This call is being recorded and our audience lines are currently in a listen-only mode. [Other operator instructions.] At this time, I would like to turn the conference over to Sam Podwika, from JLL Income Property Trust. Sam, please go ahead.

Sam Podwika
Thanks, and welcome, everyone, to today's call.

Any statements made about future results and performance or about plans, expectations or objectives are forward-looking statements. Actual results and performance may differ from those included in the forward looking statements as a result of factors discussed in the Company's annual report on Form 10-K for the year ended December 31, 2015, and in our other reports filed with the SEC. The Company disclaims any undertaking to update or revise any forward-looking statements.

In addition, all non-GAAP financial measures discussed during this call are reconciled to their most directly comparable GAAP financial measures in accordance with the SEC rules in our Form 10-Q for the quarter ended September 30, 2016.

Links to a transcript and audio replay of this call will be posted and available on our website, JLLIPT.com. For further information on the Company's performance, we invite you to review our Quarterly Report on Form 10-Q filed on November 14, 2016 and other filings which are available on the Company's website, as well as the SEC's website, sec.gov.

Now I would like to turn over the call to Allan Swaringen, President and Chief Executive Officer and Gregg Falk, Chief Financial Officer. At the conclusion of their comments, we will open the call for your questions.

Allan, if you'd like to begin?

Allan Swaringen
Thanks, Sam. Hello, everyone, and thank you for joining us for our third quarter earnings call. JLL Income Property Trust had an exceptional third quarter. We closed on seven new acquisitions investing in excess of $350 million, all in keeping with our investment strategy to acquire and manage income-producing core commercial real estate properties. We also had another strong quarter attracting new capital with over $170 million raised in Q3.

We successfully increased our working capital line of credit to $150 million and extended its term for another year. This expanded credit facility provides us with increased capacity and greater flexibility to pursue our strategic objectives in what continues to be a highly competitive capital markets environment.

Moving to the broader real estate market environment, capital market conditions have improved over the third quarter after a bumpy start earlier this year. According to RCA, transaction volumes are down about 8% from 2015 levels; however, we view this as more a function of an extremely robust 2015 than a market disruption in 2016. Most assets in the market are trading and while bidding pools are slightly diminished, there are still enough active buyers and sellers to create an efficient market. In August, year over year monthly transaction volume was down 5.3% against August 2015. Real estate prices resumed their uptick after plateauing in early 2016, and Moody's/RCA CPPI is up 8% year over year through August. Listed REIT shares fell in Q3, but only after soaring in Q2.

The third quarter saw signs of strength in terms of GDP, ticking up from recent disappointing results in the second quarter, US GDP grew at a 2.9% annualized rate, up from 1.4% in Q2. Private expenditures continue to grow, albeit at a slower rate in Q3. The biggest increase came from a one-off 10.0% growth in exports; though unsustainable, the result nevertheless represented the largest growth rate in almost three years. Despite the recent good news, the outlook for 2016 is largely unchanged and the presidential election result has widened the range among economic forecasts. Inflation currently remains below the Fed's 2% target, though it has ticked up in recent months.

The Fed did not move interest rates at its September meeting but a rate hike is still on the table for its December meeting. Normalization of interest rates is expected to be gradual, and currently there is a gap between what the Fed board members believe rates will be and what markets are expecting. The rate on the 10 Year Treasury note increased 13 basis points during Q3 and ended the quarter at 1.59%; however, since the election resulted in surprising president elect Trump, the rate on the 10 year has ballooned out to 2.35%, a twelve month high. While investors had been seeking safety in the face of global political and economic instability, the outlook for growth given president elect Trump's expansionary rhetoric has certainly altered bond investors views on inflation.

The labor market continues to be healthy, although growth has been inconsistent. The unemployment rate is 5.0%, down 70 basis points from the end of 2014 but up slightly from last quarter. The labor market added a monthly average of 156,000 jobs in Q3, below median forecast estimates. The increase in unemployment was largely driven by an increase in the number of workers entering the workforce instead of by slowing job creation. The US job growth outlook is solid with Moody's Economy.com forecasting average monthly job growth of about 170,000 for the next two years.

Gregg will now give you a recap of our financial performance and then I will discuss our Q3 activities in greater detail. Gregg?

Gregg Falk
Thanks, Allan. Our operating performance continues to be strong, and we are confident that we can continue to add value to our portfolio as national property market fundamentals remain healthy. As I highlight our financial results I will discuss the key underlying drivers of our performance.

We reported total revenues of $94 million for the first nine months of the year, an increase of approximately $28 million or 42% over the prior year. The Company had a net loss of $0.5 million for the nine months ended on September 30th, a decrease of $20.3 million from the prior year as our disposition of four of our student housing properties in the first quarter 2015 resulted in an accounting gain recorded last year. In the third quarter of 2016 we took a non-cash accounting impairment charge of $6.4 million on Railway Street Corporate Centre our office property in Calgary, Canada as the extended bear market in oil has continued to weaken the Calgary office market. The accounting charge had no impact on NAV as we had previously written the property down to its fair value.

Funds from Operations, or FFO, is a supplemental measure of operating performance used by the real estate industry which most closely resembles GAAP net income. For the nine months ended September 30th, we reported FFO of $32.6 million, an increase of approximately $13 million or 66% from the prior year, primarily due to the increasing FFO contributions from our new acquisitions. Our per share FFO was $0.33, a slight decrease from the prior year, but in-line with expectations as the number of shares outstanding increased by 79% from the prior year due to the ongoing success of our continuous public offering.

We closely monitor AFFO as a supplemental measure of operating performance. AFFO is calculated as FFO adjusted for non-cash items and non-operating expenses. AFFO was $32.4 million for the nine months ended 2016 compared to $20.8 million for the same period in 2015, a 56% increase. The increase is principally attributable to contributions from our new acquisitions and increased revenues from our office segment. Our per share AFFO for the nine months ended September 30th was $0.32.

We had exceptional growth in total assets within our portfolio over the last 12 months reaching $2 billion, an increase of approximately 69% over the prior year. We've added 34 new properties to our portfolio in the last twelve months – demonstrating LaSalle's broad execution capabilities and our targeted investment strategies.

Real estate market fundamentals remain strong as high occupancy continues to support positive rent growth across all four major property types. Vacancy rates remain below long-term averages, and we expect that on a national level new supply will mirror positive demand. Vacancy rates may rise over the coming quarters, although in a few markets the influx of new supply has been somewhat less than expected as banks have become more disciplined lenders.

Our stabilized apartment portfolio maintained its strong occupancy rate of 94% for the quarter; however, with the acquisition of Dylan Point Loma, located in San Diego, California, our aggregate occupancy decreased this quarter by 9% to 88% compared to the prior quarter. We acquired Dylan Point Loma in August during its initial lease-up, with an occupancy of 40%. We committed to this investment over a year ago and will complete the property's lease up in keeping with our "lease to core" apartment strategy. This property's in-fill coastal location, extraordinary community amenities, designer architecture and barriers to new competition make it an excellent addition to our growing portfolio.

The occupancy of our industrial segment decreased this quarter by 3% to 97% compared to the prior quarter due to the anticipated move-out at lease expiration of an existing tenant in one of our Chicago market warehouse properties. The overall Chicago warehouse market fundamentals remain quite strong and we are optimistic about the future releasing prospects for the 260,000 square foot vacancy.

Our office occupancy is 91% and our retail occupancy is 97% for the quarter, both unchanged from the previous quarter.

Despite the slight decrease in our portfolio occupancy we remain positive about the occupancy of the portfolio at 95% at the end of the quarter. Our weighted average lease duration at September 30th was 6.6 years, in-line with the prior quarter.

Touching on our returns and distributions, it is one of our primary investment objectives to offer an attractive level of current income to our stockholders. As discussed during Q2, our Board of Directors approved an increase in our quarterly distribution to $0.125 per share for the third quarter, a 4.2% increase from the second quarter's $0.12 per share. The dividend represents an annualized rate of $0.50 per share and marks the fourth dividend increase since the first quarter of 2012. We were pleased to enhance our current return to our stockholders through that increased dividend and demonstrate our ongoing commitment to providing attractive, risk-adjusted returns.

On November 18th, our Board of Directors also approved a gross distribution for the fourth quarter of 2016 at $0.125 per share to stockholders of record as of December 29th, payable on or around February 1st. This was the

twentieth consecutive quarterly dividend dating back to the first quarter of 2012. These gross dividends will be paid out to stockholders, but will be reduced for share-class specific fees.

Since we launched our initial public offering in October 2012 we have provided net of fees annualized total returns for our Class A and M shares of common stock of 6.4% and 7.1%, respectively. Our third quarter total net return for Class A and M shares was 1.2% and 1.4% respectively. We reported total net returns over the trailing four quarters for Class A and M shares of 4.8% and 5.5%, respectively.

For the third quarter, there was an increase in our NAV per share for our Class A and M shares of 0.3% and 0.4% respectively, as a result of a net increase in the value of the portfolio.

Now, I'll hand the call back over to Allan to discuss in detail our significant accomplishments for the quarter.

Allan Swaringen
Thanks Gregg.

As I mentioned earlier, we had another strong quarter closing over $350 million of new acquisitions bringing our total to almost $700 million for the year. Success in attracting new capital along with effectively investing that capital has provided our investors with a more diversified portfolio – diversified by property types, geographic regions and underlying tenant industries.

We expanded our portfolio holdings across three of the four primary property sectors during the quarter, adding two new apartment communities, two additional bulk distribution industrial properties and three new grocery-anchored retail properties. The two Apartment properties we acquired were Dylan Point Loma and The Penfield adding 434 additional rental units to this property segment. As Gregg mentioned, Dylan Point Loma is our ultra-luxury 180 unit coastal apartment community in San Diego. LaSalle ranks the San Diego downtown and coastal close-in apartment market as one of the top five target markets for core apartment investing in the U.S. The Penfield is a 254 unit, award-winning, transit-oriented, apartment complex that includes a ground-floor commercial space that is leased to Lunds & Byerlys, a premier local grocer, on a long-term basis. The Class-A property is located in the heart of downtown Saint Paul, Minnesota, the Midwest's strongest apartment market. The area is home to sixteen Fortune 500 companies including 3M, Ecolab and St. Jude Medical, and ranks as the fourth most educated and fourth highest median income in the nation. Both investments represent a continuation of our core Apartment investment strategy to acquire properties in strong urban in-fill locations that appeal to millennial renters. So far this year we have acquired three multi-family properties bringing our apartment allocation to 20% of our overall portfolio and nearly $415 million in gross assets.

Acquiring high quality, state-of-the-art warehouses in select, primary transportation hubs continues to be a core component of our Industrial investment strategy. During the quarter we closed on Pinole Point Distribution Center, which includes two Class-A, state-of-the-art warehouses in the Bay Area suburb of Richmond, California. The two warehouses are 100% leased to two national tenants Amazon.com and Williams-Sonoma. The San Francisco Bay Area is supported by a sophisticated trade infrastructure with three international airports and the nation's fifth busiest container port. This is our ninth industrial acquisition this year and the 27th industrial investment we've made overall in the warehouse sector bringing our aggregate industrial portfolio to over 6 million square feet.

Increasing our portfolio's allocation to high-quality, grocery-anchored centers in the top nationally ranked retail markets has been the focus for our Retail investment strategy. In Q3 we acquired Silverstone Marketplace and Kierland Village Center- both first-class grocery-anchored neighborhood shopping centers in the Phoenix suburb of Scottsdale, Arizona. The city of Scottsdale is a thriving community that has seen a nearly 10% increase in population since 2000, and is projected to grow at twice the national rate through 2020. With median household incomes among the highest in the nation, the city also boasts a highly-educated population. Scottsdale's targeted retail location is rated in the top-quartile of LaSalle's proprietary ranking of more than 40,000 grocery-anchored shopping centers. Additionally, at the end of September we closed on Timberland Town Center, a newly

constructed shopping center located in the affluent Portland suburb of Beaverton, Oregon. The property is 98% leased to a mix of grocery, retail, restaurant, personal and professional service tenants. Beaverton boasts favorable income and education demographics, and an unemployment rate of less than 4%. All three acquisitions demonstrate our preference for necessity and experiential-driven shopping formats with complementary and synergistic tenant rosters, bringing our aggregate retail portfolio investment to more than $660 million.

With our new acquisitions during the third quarter, our portfolio is now comprised of 27 industrial warehouses, 24 retail properties, 8 office buildings, 7 apartment complexes and 2 parking garages. In total, across all 68 properties, we now own interests in over 13 million rentable square feet. At the end of Q3 our portfolio diversification by property type was 20% for Apartments, 24% Industrial, 23% Office, 31% Retail and 2% Other.

At quarter end our overall company leverage ratio was 39%, a 2% increase from the prior quarter. With limited near term debt maturities, we have a portfolio-wide weighted average remaining loan term of 7.3 years. Our weighted average interest rate on outstanding borrowings is 3.8%, a decrease of 50 basis points from the prior year.

We've seen strong inflows of new capital along with favorable economic and real estate market conditions, which allows our acquisitions and asset management teams to continue to execute on our strategic priorities to grow and expand our portfolio in property types and geographic markets that we believe are positioned to outperform. Equally important is the ability to provide liquidity to stockholders in accordance with our share repurchase plan, available to stockholders after a minimum twelve month holding period. While we emphasize that investors should plan to hold our shares for five to seven years or longer, our share repurchase plan, subject to its quarterly limits, is available to stockholders who desire to reduce their investment in core real estate. During the third quarter, we redeemed $8.2 million shares pursuant to our share repurchase plan, which had a quarterly limit of $59.2 million. For the fourth quarter, share repurchases are limited to approximately $67.7 million which is 5% of the NAV of the company as of September 30th.

We remain committed to actively managing our real-estate assets to provide attractive income returns to our stockholders, our 4.2% third quarter dividend increase is indicative of that commitment. Financial Advisors and Portfolio Managers are looking for increased diversification and alternative sources of income for their client portfolios and core real estate is well positioned to provide both. We are very pleased with our accomplishments so far this year and are confident that we can continue to add value to our portfolio and generate moderate appreciation over time for our stockholders.

Thank you for your time and attention today and I hope you found our remarks informative. Operator, we would now like to open the call for any questions.

OPERATOR
At this time I will open the lines for your questions. [Instructions for asking questions.] Our first question comes from Tom Lonergan, a private investor.

Q: My question is, how do you see the results of the election impacting the commercial real estate market?

Allan Swaringen
Wow, Tom. That's a big question. Holy cow. So, our firm has spent a lot of time to the extent we've had time in the last two weeks, obviously, think more about the outlook for President Elect Trump. We tend to think about this from three perspectives and I'm going to try to put them in the context of what's important to commercial real estate and then what's important to JLL Income Property Trust. The wave of popular sentiment that Mr. Trump rode into the White House under the banner of Let's Make America Great Again, as many things Mr. Trump boasted about, in fact maybe a little bit harder to deliver on than to just make speeches about. I say that not as a criticism of President Elect Trump but more from the standpoint of that the health and outlook for the US economy is largely

driven by first, the household sector which is principally consumer spending and then secondarily private commercial businesses, not part of the Federal Government or not part of the Executive Branch.

So, to put that in context, depending upon which estimates you are looking at, government spending not including social support costs, actually is about in the range of 10% to 15% of US GDP. So, 85% to 90% of really what's going on in our economy is really not driven by the Federal Government or even other forms of government. So, in the context of materially impacting the US economy, other than sentiment and sentiment is certainly relevant, Presidents don't actually have as much power as what they tend to speak about during their campaigns. So that 10% to 15% of the overall GDP, if Mr. Trump really believes he can move US GDP from a 1.5% to a 3%, nearly doubling it, he only has a string of about 10% to 15% of the bigger picture to push on which could be a little bit more challenging.

Second factor we tend to think about in the commercial real estate sector as a result of an election is real estate and I've said this many times to those that hold our shares and the advisors that recommend our stockholders, commercial real estate's a lagging indicator. We tend to follow, it's an asset class that tends to follow the broader economy and health of the economy, definitely is impacted by the job market and the outlook for jobs and obviously, trade, US and global trade. So Mr. Trump certainly has spoken a lot about his perspectives on trade but if, in fact, he's quite successful in jumpstarting the US economy and putting a lot of people back to work, historically, that is a very good and very position trend for commercial real estate.

The impact his policies may have as it relates to immigration could be helpful or hurtful to the economy, could impact some sectors of the real estate market, certain geographies, but not broadly and nationally. Certainly the trade deals he's thinking about re-cutting, it'll be interesting to see because in many ways, the US economy following the GFC has been very strong benefactor of increased global trade even though the populous rhetoric about exporting jobs may have given the American people a different viewpoint.

Third thing I just make a comment about is specifically JLL Income Property Trust and our strategy of core real estate. Overall, our portfolio today is well leased, well occupied, 95% leased and occupied, we have about six and a half years of lease duration. Everything about our strategy has been trying to deliver to investors a lower volatility, more resilient investment theme and I believe the portfolio we have today nearly $2.3 billion of assets, is very well positioned, really, no matter what the outlook for the US economy is. Not that the broader US economy doesn't influence commercial real estate but our strategy specifically in core real estate and our bias towards income and our bias towards long duration leases, I think, really positions us well and more defensive. Then if we go into a growth mode, there's opportunities for us to capture that growth and if we go into a slowdown, I also believe our portfolio should be more resilient in a down turn.

So, anyway, that's our two-week view, after the Trump election and we'll see how things manifest itself. It's about 60 days out that he takes office. It will be an interesting time to watch what goes on for the first hundred days after that. But thanks for your question, Tom.

OPERATOR
Our next question comes from Gabe Youel.

Q: There have been a lot of news articles written about the apartment market overheating. What's your view on the real estate apartment market being at the top?

Allan Swaringen
So, the apartment market has been a very strong performing property sector since the GFC, one of the strongest, and I'd say it definitely has driven development, especially at the high end sector and then especially in some of the larger US metropolitan areas like New York City and San Francisco. You've definitely seen and this really came through in the second quarter earnings calls of the publically listed REITs, especially the apartment REITs, when they clearly started to see an increase in concessions that they needed to grant to continue to attract renters. They

definitely saw softening of rent and definitely in those two markets you saw renters kind of reach a price point where increasing rents, they were no longer willing to occupy the units and wherever they were choosing to live they were choosing to live less costly. So you've seen definitely a pullback in the listed apartment REITs.

And there's certainly other pockets of overdevelopment that we, through JLL and through our LaSalle Investment Management Research and Strategy Team, we tracked those apartment markets and were, in fact, avoiding those apartment markets from new investing. That said, we have been adding apartments to our portfolio and we've been doing that with a clearly defined strategy of not trying to compete in these ultra-competitive, highest price point markets but I'd say more middle market apartments and we've had kind of a two-tiered strategy there, either buying very high quality, suburban location apartments in really, really strong school districts where we feel like there's a number of demand drivers for our renters, not only from individuals but also from families and we see a lot of pretty strong barriers to entry in a lot of those more residential bedroom community areas to new development of apartments. There's still very much a NIMBY, Not in My Back Yard, resistance to new apartment development especially in certain suburban and a little more rural markets.

So, we feel like we're still finding good value in the apartment sector and have been focused on markets like San Diego, where we recently bought some apartments actually in the third quarter. We bought a really nice apartment complex in downtown St. Paul, Minnesota, many, many demand drivers for our apartments there from students, from retirees in fact, and from lots of strong job growth in downtown St. Paul. It has very strong apartment fundamentals.

And recently, we were visiting apartments that we also purchased recently in a suburb of Birmingham, Alabama in Mountain Brook, which is one of the wealthiest zip codes in the country with very strong household income, very strong housing values and lots of barriers to entry to new apartments but in an extraordinary, high-end suburban community, very wealthy suburban community of Birmingham and that really high quality apartments that, again, are attracting renters across the spectrum from retirees, empty-nesters, starter families and just individual one-bedroom apartments where people want to rent versus own.

We like apartments, we like them for their ability to allow us to grow rents if we're in a period of inflation which a lot of people think there's potential for the US economy to heat up after the election is pretty strong and so having some short duration leases in our portfolio is pretty important. Definitely some markets that we're going to have to avoid and definitely an overall sector that we have to track and keep our eye on it but we're still seeing pockets of good value and following on the themes of our Research and Strategy Team focused on areas of millennial job growth and areas with great transportation infrastructure and great walk scores. We still think all those can be really interesting and important drivers for still owning apartments and adding them to our portfolio.

OPERATOR
Our next question comes from Bert Olson.

Q: With the ten-year jumping north of 2% in the last few weeks, are you still finding acquisitions to invest capital accretively?

Allan Swaringen
Great, Bert, good question. It's certainly a timely question and we often get a question about interest rates with our strategy and certainly real estate and performance of real estate and interest rates are often linked together and in fact the ten-year has not only moved up from 2.2%, it's now, I think I looked before I came in there, it's about 2.3% as of this morning. And while that increase is a pretty big jump from the pre-election range of about 1.7%, I do think it's important to put that 2.2% or 2.3% ten-year treasury rate in context and, as a matter of fact, at the beginning of 2015, I looked this up, so almost two years ago now, the ten-year treasury ended at about 2.2% and then bounced around like crazy. Then, at the beginning of this year, 2016, it began the year at about 2.2% and then since then it's bounced around like crazy and it looks like this year it's going to end up at about 2.2%.

So while it's a significant move up from kind of the 1.6%, 1.7% range pre-election, and there's been a lot more volatility over the last 24 months or so in the ten-year treasury, it has still kind of been hovering in this range between 1.5% and 2.5% for the last two years. And that range still creates a situation where there's a pretty good spread to cap rates and that's what we spend a lot of time thinking about, more from the standpoint of is core real estate, is high quality income producing real estate, is it fairly valued in comparison to the risk free rate?

And even with a ten-year treasure at 2.5%, we're still at the wider side of, for 15 years there's been an average spread of about 300 basis points between cap rates and the ten-year treasury and even if the ten-year moves up to 2.5% or even a little bit beyond that, we're still on the wider side of that spread than on the narrower side. So, we very much watch the movement of interest rates but we also very much watch the movement of cap rates. To get to your question with a ten-year treasury at 2.5%, our ability to still borrow long term fixed rate money and match it with ten-year financing with life companies and when we're buying properties and even 4.5% to 5.5% cap rates, we can still do that on an accretive basis to our portfolio, grow our AFFO and FFO over time and cover the current dividend and hopefully over time still aspire to grow that dividend.

So, we watch them but we also really watch cap rates and this year, especially 2016, we've not seen the continual decline of cap rates like we saw in 2015. There's definitely been a leveling out of cap rates and so we have to watch both factors. That's a very important metric that we keep an eye on. And as I mentioned just in the prior question about apartments, we have, in fact, oriented our portfolio to have more leases, more of our income stream generated form shorter duration leases.

Our movement include in the portfolio both parking garages and apartments which, today, is about across those two property sectors, it's not quite 25% of our portfolio but it's getting close to that so we like to think about in a range of about 75% of our portfolio is longer duration leases with fixed steps in the ability to grow and then approximately 25%, not quite there yet, we still have to grow it to get there, about 25% of our portfolio has growth and uplift potential in rent growth. Given the current economic environment and, to be honest, some of the uncertainty, we like that mix of long duration, stable income, lots of longer dated lease with rent bumps adjusting up over time. But we are going to continue to grow the shorter end of the curve there and add more shorter duration leases and apartments and one of the deals we have teed up to close before the end of the year is another high quality urban apartment complex that we'll be talking about next year if we get it all closed.

So, very thoughtful about interest rates and their bouncing around but they're still in a range where we can make accretive acquisitions and grow our portfolio and its overall investment performance over time.

OPERATOR
There are no other questions and this concludes today's call. I will hand the call back to Allan Swaringen for closing remarks. Allan?

Allan Swaringen
Thank you and thank you, everyone, for joining us here for our third quarter update. We'll look forward to speaking with you in the New Year as we recap the fourth quarter and our final 2016 performance. Thanks for your time today.