Hudson Pacific Properties, Inc. (HPP) Q3 2023 Earnings Call

November 2, 2023

Corporate Participants:

Laura Campbell *Executive Vice President-Investor Relations & Marketing*

Victor Coleman *Chairman & Chief Executive Officer*

Harout Diramerian *Chief Financial Officer*

Mark Lammas *President*

Arthur Suazo *Executive Vice President-Leasing*

Jeff Stotland *Executive Vice President-Global Studios*

Other Participants:

Alexander Goldfarb *Analyst, Piper Sandler*

John P. Kim *Analyst, BMO*

Michael A. Griffin *Analyst, Citigroup*

Caitlin Burrows *Analyst, Goldman Sachs*

Blaine Heck *Analyst, Wells Fargo*

Rich Anderson *Analyst, Wedbush*

Ronald Kamdem *Analyst, Morgan Stanley*

Thomas Catherwood *Analyst, BTIG*

Dylan Robert Burzinski *Analyst, Green Street Advisors*

Operator: Good morning and welcome to the Hudson Pacific Properties Third Quarter 2023 Conference Call. All participants will be in listen-only mode. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Laura Campbell, Executive Vice President, Investor Relations and Marketing. Please go ahead.

Laura Campbell: Good morning, everyone. Thanks for joining us. With me on the call today are Victor Coleman, CEO and Chairman; Mark Lammas, President; Harout Diramerian CFO; and Art Suazo, EVP of Leasing.

Yesterday we filed our earnings release and supplemental on an 8-K with the SEC, and both are now available on our website. An audio webcast of this call will be available for replay on our website.

Some of the information we'll share on the call today is forward-looking in nature. Please reference our earnings release and supplemental for statements regarding forward-looking information, as well as the reconciliation of non-GAAP financial measures used on this call.

Today, Victor will discuss macro conditions in relation to our business. Mark will provide detail on our office and studio operations and development, and Harout will review our financial results and 2023 outlook. Thereafter, we'll be happy to take your questions.

Victor?

Victor Coleman: Thank you, Laura. Good morning, everyone, and thanks for joining our call today. As we head into year-end with our leasing activity accelerating, we're in a position to begin benefiting next year from both the ongoing sentiment improvement in office and the pending completion of the writers' and related actor strikes. Tech employers along the West Coast are finally enforcing in-office policies mostly three to four days a week and growing. Foot traffic and public transit ridership is improving, and there's a renewed public sector focus in our markets to address crime and safety and implement more pro-business policies.

Close to 90% of our office space outside of the San Francisco CBD is already utilized on either a hybrid or full-time basis and portfolio-wide, our office-related parking revenue is up 13% year-to-date. San Francisco's outlook is improving as well. In the third quarter, there were over 5 million square feet of requirements in the city, up 80% year over year and at fully 75% of pre-COVID levels. Over 40% of these requirements are tech related, and there are now 11 requirements over 100,000 square feet, with AI remaining as a key driver of this growing demand. This includes late stage deals with OpenAI for 450,000 square feet of Uber sublease space in Mission Bay and Anthropic for 230,000 square feet of Slack sublease space in the South Financial District. We're seeing similar strong tenant interest in our assets across markets in the form of increasing tours. The number of tours at our assets, which were already in line with pre-COVID levels, increased 17% sequentially, while aggregate square feet of demand grew 20%.

With the writers' strike resolved as of September, we're closely watching the progress of the SAG-AFTRA strike and discussions with AMPTP. Both sides appear motivated to get a deal done soon. We've seen a pickup in pre-production activity on our lots related to in-place leases, as well as an increase in tours, especially for production offices used by writers. Once the actors reach an agreement, we expect to experience an increase in stage bookings, positively impacting both occupancy and rental revenue as productions begin to prep. As filming resumes, we'll start to see the ramp-up of our service-related revenue as well.

With the holidays approaching, the precise timeline remains difficult to predict. However, assuming that SAG strike resolves by mid-November, we expect some level of increased activity through year-end, with the recovery picking up through the first quarter and normalized production in the second quarter next year.

We continue to build on our studio business, and in the third quarter, we closed on our joint venture with Vornado and Blackstone to develop Sunset Pier 94 as Manhattan's first purpose-built studio. New

York has been a high priority marketplace for expansion for our Sunset Studios brand due to the established talent base, production infrastructure and recently extended and expanded tax credits. This represents only a $39 million capital commitment with fee-enhanced returns of approximately 9%.

Beyond just project-level NOI, we expect our new footprint in the city to drive further demand for and revenue from our existing New York Quixote businesses, building a full service platform in a city akin to what we've done successfully in Los Angeles. Our vision is an end-to-end production solution totally vertically integrated with topnotch facilities and exceptional service.

We also remain focused on deleveraging and further fortifying our balance sheet. We have no material maturities until year-end 2024 when our loan secured by One Westside matures. And in the third quarter, we raised $72 million of proceeds from the sales of two California office assets, which reflect excellent execution by our team in an obvious tough transaction environment. Our dividend reductions have thus far this year yielded $54 million of savings. In terms of dispositions, we currently have two assets under contract to sell with a possibility of adding a third, all with the potential to close by year-end. And additionally, I'll note that we once again earned top rankings in the GRESB Real Estate Assessment. This is the third consecutive year we've been named a regional sector leader in the Office of Americas, and our fifth consecutive year earning Five Star and Green Star ratings. We are very proud of our team for continuing to innovate and make our business more sustainable in ways that create values for our tenants and shareholders.

With that, I'm going to turn it over to Mark.

Mark Lammas: Thanks, Victor. Our gross leasing activity accelerated again in the third quarter. We signed nearly 520,000 square feet of leases, including the renewal of our 140,000-square foot tenant at Met Park North in Seattle. Our cash rents increased nearly 9%, largely due to the strength of leases signed in the Seattle and Vancouver markets. These are positive results, thanks to the hard work of our team, but it's still taking considerably longer to get leases signed versus pre-COVID.

This is especially true for new deals, and as a result approximately 80% of the leases we signed in the third quarter were renewals. Even with this relatively healthy level of activity, our lease percentage, as expected, dropped 390 basis points to 83%, with 330 basis points of that decline attributable to one tenant, Block's move out at 1455 Market, which we've discussed for more than a year. The sales of 3401 Exposition and 604 Arizona also contributed.

Occupancy within our portfolio has been impacted over the last 12 months by similar large tenant move outs. As we look to 2024, we only have one lease over 100,000 square feet expiring, specifically Nutanix for 117,000 square feet. This expiration is the result of a 216,000-square foot renewal and extension through 2030 we completed with that tenant in 2022. Thus, with our leasing pipeline steady at 2.1 million square feet, including 400,000 square feet of deals in leases or late stage LOI, we're optimistic we'll begin to see occupancy in our portfolio stabilize and start to recover in the coming quarters. We currently have 62% coverage, including deals in discussion on our remaining 2023 expirations, which are approximately 5% below market, with about 37% coverage on our 2024 expirations over 50,000 square feet.

Turning to the studios, the trailing 12-month lease percentage for stages at our in-service studios ended the quarter down 580 basis points at approximately 90% leased due to a single tenant opting not to

renew on six stages at Sunset Las Palmas because of the strike. Underscoring the uniqueness of this situation, this is the lowest lease percentage we've had at that facility during our ownership since 2017.

Having acquired Quixote in the third quarter of last year, this is the first quarter we're disclosing the trailing 12- month results for those assets. Quixote stages were 41% leased on a trailing 12-month basis in the third quarter, which obviously includes the strikes' impact and is therefore not indicative of the asset's long-term potential. That said, historically, several of Quixote's stages have been leased on a short-term, less than one year basis. So going forward, we could expect to see lower trended occupancy for those assets versus our predominantly long-term leased in-service portfolio, but also comparatively higher per square foot ABR. You'll note ABR per square foot for the Quixote studios was $64 as opposed to $46 for our in-service studios. So there is a trade-off between occupancy and rate which we would expect to benefit from as production activity ramps up post-strike.

Our team has continued to do an exceptional job of leveraging our Quixote stages and services to maximize revenue derived from non-strike-impacted productions, including short-form content like print ads, reality TV and large-scale events. However, similar to occupancy, I'll underscore our third quarter revenue from Quixote, as well as our same-store studio assets, is far from indicative of long-term potential performance. Year-to-date, the combined studio businesses have generated approximately $10 million of cash NOI due to the impact of the strikes. By contrast, our same-store studios generated approximately $34 million of cash NOI in 2022, and we estimate that our Quixote stages and services have the potential to generate $80 million to $85 million of annual cash NOI once normalized production activity resumes. In short, our same-store studio historical performance and initial estimates for Quixote support the potential for as much as $120 million of annual cash NOI, compared to just $13 million based on annualized year-to-date results.

Moving to development, we're staying disciplined in our approach. Our in-process projects reflect highly differentiated product within our respective markets, and our remaining capital commitments are minimal. Nearly half of this in-process pipeline is studio-related. Sunset Glenoaks Studios in Los Angeles is expected to deliver at the end of this year, and as Victor noted, we've started construction on Sunset Pier 94 studios in New York, with delivery anticipated by end of 2025. Despite the strike, we've continued to tour potential tenants who recognize the exceptional quality and uniqueness of these properties and who have interest in both long-term and show-by-show leases. Clearly, the strikes' resolution will accelerate leasing activity for these assets.

With respect to our only other in-process development, Washington 1000 will deliver in the first quarter of next year. There are currently 2 million square feet of tenant requirements for downtown Seattle. This will be the best product in that market with no other product delivering in South Lake Union Denny Triangle through year-end 2024. The surrounding neighborhood is vibrant due to the combination of return-to-office mandates and the recently completed convention center, which added hotel, residential and retail amenities. Our basis is only $640 per square foot, representing a 30% to 40% discount to comparable trades in recent years.

And now, I'll turn the call over to Harout.

Harout Diramerian: Thanks, Mark. Our third quarter 2023 revenue was $231.4 million compared to $260.4 million in third quarter of last year, primarily due to the sales of 6922 Hollywood, Skyway Landing

and Northview Center. Previously communicated tenant move outs at Skyport Plaza and 10900 to 10950 Washington, as well as a reduction in studio services and other revenue due to the related union strikes.

Our third quarter FFO excluding specified items was $26.1 million or $0.18 per diluted share, compared to $74.1 million or $0.52 per diluted share in the third quarter last year. There are no specified items for this quarter. Prior-year specified items totaled $0.07 per diluted share. The year-over-year change in FFO is attributable to the previously mentioned asset sale and tenant move outs, higher operating expenses associated with Quixote acquisition, and higher interest expense. Our third quarter AFFO was $28.1 million or $0.20 per diluted share compared to $55.8 million or $0.39 per diluted share, with the change largely attributable to the previously mentioned items affecting FFO. Our same-store cash NOI grew $126.7 million, up slightly year over year, with the same-store office cash NOI up 3.5%, largely driven once again by significant lease commencements at One West Side and Harlow. The 40.9% decline in same-store studio cash NOI reflects, as Mark mentioned, a single tenant decision not to renew on six stages at Sunset Las Palmas due to the strike.

During the third quarter, we repaid our $50 million Series E private placement notes, with funds from our unsecured revolving credit facility. At the end of the quarter, we had $555 million total liquidity, comprised of $75 million of unrestricted cash and cash equivalents, and $480 million of undrawn capacity on our unsecured revolving credit facility. There is additional capacity of $295 million under our One Westside Sunset Glenoaks and Sunset Pier 94 construction loans.

At the end of the quarter, our company share of net debt to company share of undepreciated book value was 38.6% and 77.1% of our debt was fixed or capped. The reduced percentage of fixed or capped debt reflects the expiration of the hedge associated with our Bentall Centre loan until the refinancing is complete and a new hedge is put in place. On a pro forma basis, for the new hedge, our percentage of fixed and capped debt would be 79.7%.

Regarding our upcoming maturities, as noted, we're in the process of completing our refinancing on our Bentall Centre asset, of which our 20% ratable share is $98.4 million. Thereafter, our only remaining expiration through 2024 is our loan secured by One Westside and Westside Two, which matures in December 2024, and of which our 75% ratable share is $243.5 million.

Specific to our covenants, our percentage of unsecured indebtedness to unencumbered asset value increased in the third quarter to 57.7%, up from 53.7% in the second quarter. This increase was anticipated per our projections and we expect to remain compliant.

Turning to our outlook, while we remain positive about the strikes' near-term resolution, we still don't have sufficient visibility around the nature and timing of the post-strike ramp-up and production. Thus, we continue to maintain our approach on our 2023 FFO outlook and studio-related assumptions, again providing certain assumptions related to our office outlook. We're reaffirming our office same-store cash NOI growth projection ranging from 1% to 2%. As always, this outlook excludes the impact of any potential dispositions, acquisitions, financings and/or capital markets activity. Should the strike resolve by year-end, we would anticipate reinstating our full year FFO outlook for 2024 when we report our fourth quarter 2023 results next year.

Now, we'll be happy to take your questions. Operator?

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question today comes from Alexander Goldfarb from Piper Sandler. Please go ahead.

Alexander Goldfarb: Hey, good morning. Morning out there. So two questions. Maybe first, just sticking with the Bentall asset. Your partner has been busy exiting a number of other office assets that they've owned. I assume that Blackstone is, likes studios, too, given that they just upped with the Hudson Studio here in New York. But can you just give a sense of Bentall if this is an asset that they're committed to and you guys will stay in or should we look for you guys to exit Vancouver?

Victor Coleman: Hey, Alex. Thank you for the question. Yes, currently, we've had countless conversations with Blackstone on this asset, and I don't want to speak for them as to how their portfolio has performed, but it's our understanding that this could be their best office asset in their entire portfolio. And to-date, they are fully engaged and prepared to continue the ownership and the plan to remain in Vancouver with this asset and look to extend this relationship on this asset and in Vancouver with us.

Alexander Goldfarb: Okay. And then the second question is, I think I'm not sure if this was just about Quixote or Quixote, I always have trouble pronouncing it, or studios overall. But you guys mentioned that you're only $13 million now versus $120 million potentially. So just want to get better understanding, especially as we think about hopefully the strikes resolving and how the NOI build-up comes back. Simply put, where is NOI now? And where could it go? And I'm asking the question again, based on you mentioned that you're sort of $13 million now, potential of $120 million with the studios.

Victor Coleman: Sure. So let me just start top level and then Mark and Jeff can jump in. So, as you know, this strike is now six months in and we can talk about the status of it, if that's what you wanted. But just in terms of the numbers, I mean, we are looking at somewhere around loss of EBITDA for the company for the year at around $100 million, okay? And so if we were to look to be stabilized and the strike is moving forward, it would be more like the $120 million that was broken out in the comments that Mark in his prepared remarks, which is a combination of Quixote, our Sound Stage businesses and our ancillary revenues and cost savings that we've implemented throughout the last nine months of this year.

Mark Lammas: Yeah, Alex. I mean, you can obviously see it's broken out by segment, so you can see precisely where we are year-to-date in terms of NOI on the studio business itself. I mean, so that's sort of what's underpinning the annualized number that we shared in our prepared remarks. I think maybe more importantly, Alex, is what we're trying to do is give you and others an idea of what the potential is, right. And so 2022, for our same-store assets, it's a normal operating type year. We had normal occupancy at the stages we had up until about the last month of that year, we had normalized production activity until it started to curtail in anticipation of the strike. So that's a pretty good benchmark, right.

And we've shared along the way as we've done the acquisition, Zio, Star Waggons and eventually Quixote itself, we've shared what we view as the potential EBITDA on a normalized basis. Jeff and his team have implemented somewhere, we believe, on synergy-type savings and top line improvements that we think will result in somewhere in the neighborhood of $15 million, you combine that with the $70 million of prior pre-synergy run rate NOI, that's how you get to that $80 million to $85 million of normalized annualized NOI. So those are the contributors, if you will, that get to that $120 million.

Alexander Goldfarb: Okay. Thank you.

Operator: Our next question comes from John Kim at BMO Capital Markets. Please go ahead.

John Kim: Thank you. Just sticking to that NOI uplift in studios, looking at your presentation in September, you go from $120 million to $159 million, including developments, and the UK Waltham Cross is not included in that NOI contribution. I was just wondering if there was an update on that project.

Victor Coleman: No, I mean, currently we're still in design phases and entitling and we have not anticipated a start date in 2024 yet for Waltham Cross. We're looking at some other alternatives around candidly sizing the deal on maybe two phases and that's going to come back in some pricing differential, but that's why it's not in the underlying cash flow going forward yet.

John Kim: Okay. And on the development yields that you're expecting on the two current developments, does that include any additional revenue from Quixote?

Mark Lammas: No.

Victor Coleman: No, no. That's just a straight development. You remember, and it's complicated and it's a very good question. We balance this out, this is a Sunset asset, so it's an asset under Sunset, both Pier 94 and Sunset Glenoaks. And then the Quixote is the operating business asset and that is a different enhanced number on top of that. For all the service revenue that will go through, will go through Quixote on those Sunset-owned assets, but they're separate ownerships so we have to keep it separate in terms of the returns.

John Kim: Okay. So that yield is just the studio rental yield? And you do expect Quixote to service both the studios?

Victor Coleman: Yeah. The 9% yield that was in the remarks was for Pier 94 and that's just the Sunset yield on the studio for Hudson.

John Kim: My final question is on your dispositions. You mentioned two to three that may close this year. Any commentary that you can provide on the dollar amount and the yield?

Victor Coleman: No. We just don't do that. I appreciate you asking. We have three assets. Two are under contract. Hopefully the third will be. And as we get closer to closing, we'll share the numbers and the assets and the size.

John Kim: Okay. Thank you.

Victor Coleman: Thank you.

Operator: Our next question comes from Michael Griffin at Citi. Please go ahead.

Michael Griffin: Great. Thanks. Maybe just a question on leasing. You called out Seattle and Vancouver in the release as being markets that you're seeing relative strength. And is there something about these markets that give you more confidence, I guess, relative to San Francisco and LA?

Victor Coleman: So let me start on just the general and then Art's sitting here. So, Michael, he can jump in on that. So, listen, Vancouver has been consistent throughout pre-pandemic, pandemic and currently

today, right? The vacancy is very low. The rental rates have not moved considerably in either direction. And it's been absolutely consistent and could be one of the best markets, but yet, as we've talked in the past, it's very small. What we've seen in the shift in Seattle is generally that when the workforce has gone from three days a week going to four days now in that area, some of the high quality space in both Bellevue and Seattle is getting eaten up. And there are a few deals right now that are about to be announced in both those markets. But we're seeing the quality space being eaten up in those markets a lot more efficient than I would say, and specific to Los Angeles, we don't have that kind of space available in Los Angeles for the same level and size of tenants.

Plus, I think what's the underlying tone in Los Angeles and Art's going to talk about some of the demand numbers. But because we have a strike here, and we are a media entertainment-related city in Los Angeles where we're sitting right now, things have slowed dramatically until we get back up and running. So it's not just the studio business, it's the overall industry itself for people growing in real estate.

Arthur Suazo: Right. And the groundswell, really, Michael, in Seattle, as Victor mentioned, with return to office really starting to take hold more and more with the mandates, it's really the growth of tech users coming back into the market that we've seen really grow over the last three quarters, right. Also net loss in San Francisco obviously has shown the most growth in demand, really the 80% growth in demand year over year and probably 25% quarter over quarter because of that same reason, because of tech.

In Los Angeles, we're really only talking about relative to our portfolio, West Los Angeles and the reasons Victor stated with regard to the strike, entertainment and media were really driving, they have been driving that market through the pandemic and keeping it healthy. And we'll start to see those numbers come back. But it's still very, very modest level of activity.

Michael Griffin: Great. That's helpful. And then maybe one question on occupancy, if I can. I think, Mark, in his prepared remarks kind of alluded to a stabilized expectation for occupancy heading into 2024. Should we read that as kind of flat from current levels or anything you can provide there would be helpful.

Mark Lammas: Yeah. Our forecast shows steady improvement actually into – as we head into 2024 and even into 2025. I mean, we also mentioned the sort of the shift, if you will, from the expirations that we've experienced over the past year or two, what will be a year and a half of very little large expirations, only one over 100,000 feet on that matches really, really well with the pipeline in terms of where the demand is coming from. So, yeah, we expect to see steady improvement essentially from here on out and for the foreseeable future.

Michael Griffin: Great. That's it for me. Thanks for the time.

Victor Coleman: Thank you.

Operator: Our next question comes from Caitlin Burrows of Goldman Sachs. Please go ahead.

Caitlin Burrows: Hi. Good morning there. So we've had the writers' strike and the actors' strike. I'm wondering if you have a view on whether crews will strike, if that's anything you've heard about?

Victor Coleman: Crews?

Mark Lammas: Next year.

Victor Coleman: Oh, next year, yeah, no. I mean, we haven't heard anything about that at this date. I mean, they typically have been more in line and you never know what happens, Caitlin, right. But they've typically been more in line with like the Directors' Guild and we settled like prior to. As I said, we're in a unique time line with multiple industries looking to strike. But the two biggest are obviously SAG-AFTRA and the WGA, and they've always led the way. So we're hopeful that won't happen. But so far today we've heard nothing.

Caitlin Burrows: Okay, thanks. And then also, Harout or actually, Mark, last quarter, you mentioned that you guys had stresstested your covenants through the end of 2024 and that you would remain even in the worst quarter over 300 basis points clear of the limit. So now you just have 230 basis points remaining buffer on the unsecured indebtedness to unencumbered asset value covenant. So wondering if you could go through why it might have exceeded that stress test that you mentioned last quarter and kind of your confidence in the trend going forward and ability to forecast that? Thanks.

Mark Lammas: Yeah. I mean, we are still largely in line with our own expectations, although it is – I mean, it's a fairly complicated calculation. It uses trailing numbers that get grossed up, there's onetime items that have to get excluded. And so we are materially in line, I would say. I do appreciate your point regarding the sort of 300 basis points. As we look at the number and we stress test it, we still are confident we are going to remain compliant, so I'm not sure there's much more we can add other than we're focused on it. We're looking at all of our leasing expectations. We factored in the sales that Victor mentioned earlier, they're running through all of our projections and we expect to remain compliant.

Caitlin Burrows: Okay. Thank you.

Mark Lammas: Thanks.

Operator: Our next question comes from Blaine Heck at Wells Fargo. Please go ahead.

Blaine Heck: Great. Thanks. So just following up on covenants and thinking about some of your options to bring your metric away from the limits, I understand increasing income would certainly help on some of them. But just taking the income side out of the equation, I guess, what can you do on the balance sheet side? I believe if you kind of draw down the rest of your line, that puts you in violation. But if you could confirm, that it'd be helpful. Have you looked into any additional secured debt on the media portfolio? Is that a possibility or does it just really come down to dispositions at this point?

Mark Lammas: No, there's more than – I mean, dispositions can are a good contributor. And we expect the dispositions that we've mentioned already to be accretive to the unsecured metrics.

Victor Coleman: We also have other assets in the portfolio that we've mentioned, Blaine, in the past that are not part of the facility or credit facility.

Mark Lammas: Yeah.

Victor Coleman: That we are looking at options around that which enhances a fair amount of liquidity as well.

Mark Lammas: Yeah. Yeah. And just maybe just to reify that point, there are other levers, Blaine, beyond just dispositions. So there's unencumbered assets that we could put, I mean – sorry, there's

assets that we could put debt on that don't run through the unencumbered metrics that would be accretive. There are other assets we own that are not real estate assets, they're notes. We have the ability to sell those. Those would be accretive to the metrics. So there are a number of levers, if you will, that we can pull beyond asset sales that all would improve those metrics.

Blaine Heck: Okay. That's helpful. We noticed the term on leases signed during the quarter was significantly shorter than normal, I think, right around three years. Can you just talk about that, whether there was anything specific that might have skewed that statistic downward and whether those shorter terms are prevalent in kind of the leases that you have in the pipeline as well?

Arthur Suazo: Hey, Blaine, it's Art. Yeah, no, they're not prevalent. Listen, the sequential decrease was primarily due to really two transactions. The first was a six-month, 35,000-square-foot non-office use transaction in Pioneer Square, which we did as an accommodation to try to keep the tenant long term. And the second was a 24-month extension on 140,000-square-foot expiration in Denny Triangle. Again, with the intent further extend the lease downstream. With the combined effect of these two deals, our weighted average lease term was right in line with the prior two quarters' average weighted average lease term of about 45.5 months. So, yes, there was a couple of outliers and that was the explanation.

Blaine Heck: All right. Thanks, Art. And then last one. Given that you lost the tenant at Sunset Las Palmas, is that now the focus on the leasing side within your studio segment? And how does that affect your ability to lease up Glenoaks, I guess. Are they kind of competitive properties at this point, or you're kind of going for the same tenants or separate?

Victor Coleman: So Blaine, I mean, listen, we lost the tenant that's been there because they stopped production and they had a right to get out. And so that show was canceled based on the strike. That's the first time we've ever had a vacancy in the history of ownership of that asset. And quite frankly, in Gower and Bronson is the same. It's not competitive to Glenoaks. I mean, the activity at Glenoaks has been very surprisingly high and the interest is, it's the first of its kind of a purpose-built facility and the interest is very high. As I mentioned in my prepared remarks, I mean we're already seeing writers' rooms and activity around that up and running. When the actor strike is over, purpose-built facilities will have the highest demand. And I think we're very comfortable that this is not a trend, this is a moment in time. And my guess is the parent company that left us will be the first company that's going to call us and want to put a show in there going forward and we'll have options at Las Palmas, just like we have options at Glenoaks and all of our Quixote facilities.

Blaine Heck: Got it. Thank you all.

Victor Coleman: Thanks, Blaine.

Operator: Our next question is from Rich Anderson at Wedbush. Please go ahead

Rich Anderson: Thanks. Good morning. So you guys have done really good work converting your studio business into longer-term leases. I know this topic has come up a couple of times now, but as an exit out of the actors' strike situation, do you think the market or the business could step back in and want to continue this theme of more short-term leases at the outset and that you'll have to absorb more of that as you kind of get back to work? Or do you think that won't be a sort of something you have to give away to get rolling again?

Victor Coleman: I don't know what we're going to give away, Rich. But the fact of the matter is, I think what we've said in the past consistently is we think when the strikes are over, we will see a tremendous upswing in activity in all forms and functions. And we'll decide whether short term or long term is the most equitable decision tree for us to move forward on. I think we're going have lots of options.

We already are having – and I can have Jeff jump in and talk a little bit about the sales team and what they're seeing. But he's getting a lot of inflows on the sales side for various different options. We started this industry with show to show and we were extremely successful on that. We flipped over and did long-term leases and we've been extremely successful on that. And I think we're prepared to look at what's the best economic term. We're not afraid of either one, candidly, which we've mentioned and you've been a part of this for a long time, so you should know this. We've mentioned that show to show is much higher revenue stream than long-term leases. And so I think we are prepared and comfortable with either direction. And I think the numbers are going to bear out because there's going to be, as I said, a tremendous upswing in activity as soon as the strikes are over and we get back to stabilized revenue, which hopefully will be soon.

Jeff, you want to jump in on the sales side?

Jeff Stotland: Yeah. I would just add that when – Rich, when we go to a show by show model, I think it separates us as a differentiator in the industry because we have a really good team capable with all of our relationships with the studios and understanding how shows get greenlit and booked and that whole process. It really enables a company like ours to succeed, whereas anybody who's got sort of a one-off studio development who doesn't have those relationships who's just hoping a long-term lease was going to save them is going to have more trouble. So I actually think we're in a competitive advantage situation when the industry goes back to predominantly show by show and that's how we're really building the business to capitalize on that.

Rich Anderson: Okay. Second question, Douglas Emmett has Warner Brothers known vacant for next year, not related to you, but, perhaps a systemic observation about the industry. Does that give you pause at any level about just the longer term sort of view on content and the studio business overall? Or did you see that as completely unrelated?

Victor Coleman: Totally unrelated, I think it's like, as I said, we're seeing a feverish activity of interest around studio occupancy and content and growth. I can't comment on Warner Brothers and I can't comment on their write-off of $500 million last quarter either and whatever else decisions they're making candidly. But they're not the only animal in the room. We've got Apple and Amazon and Netflix and HBO and Showtime and Cinemax and Disney and ABC and NBC and CBS and Paramount and everybody else who is looking for space and content in our markets that we're in and other markets around the world. And I think that's just part and parcel of the growth story.

Rich Anderson: Okay. And then last for me is New York City. Very interesting expansion there. But I imagine that's a sort of a starting point for you, at least in the metropolitan area, that there's a Netflix development going on very close to where I live in Fort Monmouth in New Jersey. I'm just curious how much you see the New York City Metropolitan area as a growth story for you going forward? What kind of opportunity set do you see longer term?

Victor Coleman: I think New York is, as I mentioned in my prepared remarks, a marketplace that we've been very eager to get into. I give the team high marks for being disciplined to not buy into the marketplace on the upswing. This is a purposebuilt facility that will be the first of its kind in the city of Manhattan. And I think as a result of that, it will give an entree for us to look at some other opportunities in our venture with Blackstone, which is their interest level there and other markets as well. As I said, discipline has been something that we've been very focused on. This is a three-year deal in the making and at the end of the day, our team, which is already doing business through our OpCos with Quixote and Zio and Star Waggons and the likes of that in the surrounding areas of New York and all the other studios in the outside areas and in Queens, in Brooklyn, in the Bronx, etcetera, we'll see where that ends up going forward. But right now, we're in a position to continue to evaluate and be disciplined.

Rich Anderson: Yeah. Okay. Thanks very much.

Operator: Our next question is from Ron Kamdem of Morgan Stanley. Please go ahead.

Ron Kamdem: Hey, two quick ones. Just going back to the covenants question, taking a different take at it, what are some of the hurdles to actually adding Quixote to the calculation, right? Because presumably that would help. But just trying to figure out what are some of the hurdles for that to get into the calculation? Or is that even realistic?

Mark Lammas: Well, it's realistic. I wouldn't describe it as a hurdle. It is running through our TAV at the time that we reset the facility in 2021, we had line of sight to what at that time was two relatively small operating businesses. The lenders were amenable to flowing through TAV. And we did not anticipate the growth of that part of our business and so we did not anticipate for the unencumbered metrics the potential impact that those could have. We're in constant contact with our lenders. We have amazing relationships with them. They are very aware that those businesses grew and that had we anticipated that type of growth, they would have been factored into those unencumbered metrics. And I do think that we're watching our calculations, our metrics and so forth. And there may be a time and an opportunity to pull those into the unencumbered metrics, and they're amenable to that.

Ron Kamdem: Helpful. Thanks. And then just switching gears, I want to follow up on your comments on Washington 100, that's delivering on 1Q obviously, no pre-leasing done. Just curious, what kind of activity, is there any more sort of color there or tenants looking, LOIs, just any sort of sense or pulse on the activity there? And what would be a reasonable expectation for getting those first leases signed?

Mark Lammas: Yeah. First of all, yeah, it's not really pre-lease market, but we're very well situated right now. It's the newest, best-in-class building in the market. In addition to that, there are no other deliveries to the end of 2024. So again, we're very well situated. As Victor mentioned, on one of the other questions, we're starting to see an uptick in large deals in the CBD and across Bellevue, there's a lot of quality sublease space. It's going to get leased up here, rebound in the following quarters, which makes us even more desirable again, and in turn it's ticked up our early interest in tours

Ron Kamdem: Great. That's it for me. Thanks so much.

Operator: Our next question is from Tom Catherwood from BTIG. Please go ahead.

Tom Catherwood: Thanks. Sticking back with the studios, Victor, appreciate your commentary on the pickup in preproduction activity. Can you provide some more color, though, on how far in advance the production planning process has to start to lock in studio space? And is that driving any early discussions with users beyond just the preproduction activity you mentioned?

Victor Coleman: Tom, it's a great question. There is no science here on that. I can certainly tell you what we're seeing. Now, remember, while SAG and AFTRA are on strike, they can't even entertain signing facilities until that strike is done, albeit that the writers are done, the writers can sign office space and they can start working on scripts, but you can't sign soundstages in the likes of that, nor would they. So that's where we sit. Let me know, I can have Jeff jump in, but sort of if the strike were to end today, as we've sort of commented, it would be two weeks to ratify it and then it would be another six to eight weeks of activity around what shows are going first, second, third, and how they're looking at that. And so then they would come and look at opportunities at ours and everybody else's stages that have availability. And from that moment on, there would be a time line for mill space and outlining, editing and the likes of that on a pre-production side, that's why we're anticipating a full up and running three quarters next year approximately. And we could get better economics in the first quarter of next year if things happen quicker. But with the holidays, even though they've been on holidays for six months, in my opinion, they probably won't get going till January 1.

Tom Catherwood: Got it. Really helpful. Thanks, Victor. And then second question, maybe Mark, following up on the levers that you mentioned in response to Blaine's covenant question, what is your appetite to potentially monetize the retained bonds and the Hollywood media portfolio to fund either incremental investments or delevering?

Mark Lammas: I mean, I think it's an interesting potential source of liquidity and opportunity to create liquidity, improve the metrics. It's something worth exploring and I guess I'll leave it at that. We'll have to see how other things unfold.

Tom Catherwood: Got it. That's it for me. Thanks, everyone

Victor Coleman: Thank you.

Operator: The next question is from Dylan Burzinski from Green Street. Please go ahead.

Dylan Burzinski: Hey, guys. Good morning. And thanks for taking the question. I guess just going back to occupancy and the expectations over the next, call it, 18 months through 2025, are you able to share what sort of level of new leasing activity is embedded in those expectations?

Mark Lammas: Not at this time. I mean, we haven't – I mean, historically, we've been asked this question, we've tried to give people ideas of kind of where we might end up at certain points and so forth. I think it's probably caused the wrong type of understanding of our leasing, our leasing activity, the progress we make. I don't imagine that when it's time to reguide, we're going to adopt some kind of – we might consider a metric. I don't know that it'll be as granular as new versus renewal on – maybe it's worth considering something that our peers do in terms of ranges of occupancy or something like that. But I don't think it's going to quite be as pinpointed as your request for new leases.

Dylan Burzinski: That's fair. And then I guess just one more. Are you able to comment on sort of expectations for net effective rent? And obviously it's going to differ by market, but if you can just go broad strokes across your footprint, that would be helpful.

Mark Lammas: Well, I mean, I'm sure you're keeping an eye on how net effectives have trended. I mean, they've held up well. I think we're down – if you go trailing 12-month pre-pandemic, so Q1 2020 trailing 12, as of that point, we're essentially in line on a trailing 12-month basis with the latest activity, I think we're down like 4%. And they've held up almost every quarter we're at sometimes above, sometimes slightly below. But the net effective has held up. Again, we don't provide some sort of net effective, I don't think anyone provides a net effective target on a forecasting basis.

Jeff Stotland: Chiefly because the composition changes quarter to quarter, you know.

Dylan Burzinski: Great. Thanks for the detail there, guys. Appreciate it.

Victor Coleman: Thanks, Dylan.

Operator: Our last question on the call comes from Nick Yulico from Scotiabank. Please go ahead.

Nick Yulico: Hey, this is Dan Tricarico on for Nick. Just one question on leverage, how are you thinking about balancing selling assets with an expectation for improved occupancy and leasing? You're pretty well set up on the maturity ladder over the next few years and back of the envelope math, if you had the $100 million of lost EBITDA from the studios business, you'd be close to that 7 times net debt longer term target. So any thoughts there would be great. Thank you

Mark Lammas: I mean, your lead-off in the question is precisely what we're doing. I'd say we're constantly balancing that. We're looking at assets that have – and it's tenant composition, maybe the remaining term on the lease, how we view the prospects for the backfill if that's a relatively early lease expiration. And Drew and his team are looking at every element of every potential asset sale and taking into account exactly that, namely what our expectations would be, what it looks like if it does expire, what the downtime looks like, what the cost of retaining is, and it's just a constant balancing act. And I think thus far, his team has done an amazing job of like striking the balance just right every time.

Victor Coleman: Great. I think that's it. Appreciate everybody's participation in this quarter and we look forward to updating you, if not before, next quarter. Thanks very much, operator.

Operator: Thank you. This conference has now concluded. You may now disconnect.