Corrected Transcript

03-May-2012

DCT Industrial Trust, Inc. *(DCT)*

Q1 2012 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to the DCT Industrial First Quarter 2012 Earnings Conference Call and Webcast. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] During the Q&A session, we please ask that you limit yourself to one question and a single follow-up for the interest of time. Please note, this event is being recorded.

At this time, I would like to turn the conference over to Ms. Melissa Sachs, Vice President, Corporate Communications. Ms. Sachs, the floor is yours ma'am.

Melissa Sachs
VP-Corporate Communications & Investor Relations, DCT Industrial Trust, Inc.

Thank you. Hello, everyone and thank you for joining DCT Industrial Trust first quarter 2012 earnings call. Today's call will be led by Phil Hawkins, our President and Chief Executive Officer, and Matt Murphy, our Chief Financial Officer, who'll provide more details on the quarter as well as our guidance for the balance of the year. Additionally, Mike Ruen, Managing Director of our East Region will be available to answer your questions about the markets and our specific real estate activities.

Before I turn the call over to Phil, I would like to remind everyone that management's remarks on today's call will include forward-looking statements within the meanings of Federal Securities Laws. This includes without limitation, statements regarding projections, plans or future expectations. Actual results may differ materially from those described in the forward-looking statements and will be affected by a variety of risks, including those

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set forth in our earnings release and in our Form 10-K filed with the SEC, as updated by our quarterly reports on Form 10-Q.

Additionally on this call, we may refer to certain non-GAAP financial measures. Reconciliations of these non-GAAP financial measures are available in our supplemental, which can be found in the Investor Relations section of our website, dctindustrial.com.

And now, I will turn the call over to Phil.

Philip L. Hawkins

President & Chief Executive Officer, DCT Industrial Trust, Inc.

Thanks, Melissa, and welcome, everyone. We had a great quarter and an excellent start to 2012 and are making strong progress towards our strategic and operational goals. Our market teams continue to execute exceptionally well leasing space and sourcing attractive acquisition and development opportunities.

I'm very pleased with our operating results in the first quarter. Highlights include, leasing of 3.3 million square feet in the quarter, a 13% increase over the first quarter of last year. Leasing has continued strong in April with 1.4 million square feet of leases signed, including the pre-leasing of our two building, 179,000 square foot Dallas Center project to a well known Fortune 500 company. We also signed 435,000 square feet of new and expansion leases in our operating portfolio, and our pipeline of leases under negotiation remains quite active as well.

I was especially pleased with same-store NOI, which increased 9% on a cash basis and 3.8% on a GAAP basis, driven by both higher occupancy and higher net effective rents. It's nice to see this in strong positive territory.

Rents declined 3.7% on a cash basis and increased 3.1% on a GAAP basis, continuing a trend of gradual improvement over the past several quarters. Based on these trends, we've increased the mid-point of our FFO guidance by $0.015 per share to $0.40, a 4% increase.

I continue to be optimistic about our business and the outlook for 2012. Tenant demand, in particular, is quite encouraging. Larger bulk requirements remain the hottest sector, but smaller and medium sized users are becoming more active as well. This is a continuing trend that we have observed over the last two quarters.

A survey of small and mid-sized business owners recently conducted by PNC Bank caught my attention and reinforces the trends we're seeing on the ground. PNC observed significant improvement in business expectations and optimism compared to last fall and a return to positive levels not seen since 2007. They further state that this improvement in small business cinema is across all industries with manufacturing firms, not surprisingly, continuing to lead the way. Even the outlook of the previously downtrodden construction companies is sharply improved over the last survey.

Across the board, we're seeing good leasing activity in each of our markets. We are definitely more conscious today about pushing rents than just six months ago, given the improving market environment. An old saying goes that it takes two deals to make one good one. In fact, we had a number of situations recently where two or more tenants actively competed for the same space. This is a great sign and I'm happy to deal with the high-class problem of upset users calling me to complain about losing out on a space. It makes my market leaders nervous when I get those calls, but I view it as one of the best perks of my job and a strong indication that the market is indeed moving our way.

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In terms of capital deployment activity, we acquired three buildings totaling $26 million, since the first of the year. We have a good pipeline of potential acquisitions, with about $75 million under agreement or active negotiation. Despite a very competitive investment market, I'm optimistic that we can continue finding opportunities in our focused markets at prices below replacement costs and with attractive returns. These will continue to be mostly, if not entirely, smaller one or two building acquisitions, many of which will be sourced off-market.

Over the past year, our average acquisition size was $10 million and 60% of those transactions were sourced off-market. This speaks to both our approach as well as the strength of our local market teams.

We will continue to take on leasing and redevelopment risk in our acquisition program, where were believe the return premiums warrant the additional risk and effort. We have been able to acquire a number of such deals and, more importantly, remain ahead of leasing expectations with each value add acquisition.

At this early stage in the recovery, I'm happy taking on the leasing challenge in order to own a quality building at a lower all-in basis that generates a higher return. While small in size, our recent $1.8 million Phoenix acquisition is a good example. It's an outstanding and well-located 76,000 square foot Class A asset offering a secured truck court and single tenant control.

We've been talking with the users' seller for quite some time about various transaction structures as they have simply outgrown the building. They're leasing it back for three months, giving us some lead time for making cosmetic renovations, as well as marketing the space. Once stabilized, we will own the building for less than $36 per square foot and generate an anticipated yield in excess of 10% in a market where stabilized assets of similar size and quality are trading at cap rates around 7%. The market is active for this sized user and we have several high quality well-known prospects for this space, giving me optimism that we won't just meet our pro forma, but exceed it.

A brief comment about the Chicago acquisition we completed in April. While 50% occupied at the time of purchase, this building is now 100% leased with the new tenant expected to take occupancy by September after the tenant improvements are completed.

With the improvement in leasing markets, combined with a strong investment market, where buildings are often trading at prices above replacement cost, we are ramping up development in those markets where rents and demand make sense. We're now under construction on three projects in Washington D.C., Houston and Miami, totaling 600,000 square feet with projected total cost of $44 million and a projected cash yield after stabilization of 8.7%. We recently pre-leased our entire Dallas Center project and a strong leasing activity on our Miami and Houston developments as well.

We expect to start construction on an additional $80 million to $120 million this year, including a second quarter start on DCT 55, a 600,000 square foot cross-dock building located in the I-55 Corridor of Chicago. We also have projected an early third quarter start on Slover Commerce Center, a 650,000 square foot cross-dock building in the Inland Empire West submarket of Southern California. We have strong pre-leasing activity on these buildings, which are well timed and well suited for their respective markets. We are working on several other development opportunities all in costal markets that we were optimistic will someday become reality.

Our development focus remains on $1 billion or $2 billion projects in the in-fill locations where we can minimize land carry. With respect to dispositions, we have several modest sized portfolio sales in the works and are optimistic that we will successfully close them while there is nothing specific to report at this time. The

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environment for selling assets is quite favorable and the sale of lower growth non-strategic asset is an important priority for us in 2012.

In my view 2012 is all about execution, execution on our long-term strategic goals and on our 2012 business plan, execution in the markets, leasing space and pushing rents wherever possible and execution of a prudent capital deployment and recycling plan, focus on acquiring and developing quality assets in attractive markets and continuing to prune lower growth assets from our existing portfolio. We are off to a strong start in 2012 and I'm confident that the momentum will continue.

With that, let me now turn the call over to Matt Murphy for additional color on the quarter and our guidance for the remainder of the year.

Matthew T. Murphy

Chief Financial Officer, DCT Industrial Trust, Inc.

Thank you and good morning, everyone. 2012 is off to a tremendous start at DCT and we're very excited about our prospects for this year and beyond. Funds from operations was $29 million for the first quarter, or $0.11 per diluted share. Both of these numbers represent more than a 20% increase from the first quarter of 2011.

Total consolidated occupancy decreased approximately 40 basis points during the quarter to 90.1%, reflecting the normal seasonality of the industrial business. Relative to expectations our occupancy decline was remarkably modest, given that approximately 40% of our 2012 scheduled leased expirations occurred during the first quarter. Average occupancy for the quarter and ending occupancy at March 31 were both well ahead of plan. Further, we have an additional 1.3% of our portfolio leased, but not yet occupied.

Notwithstanding the slight decline in occupancy, our leasing results continue to be strong. We completed leases on 3.3 million square feet of space during the first quarter, or 13% ahead of 2011. Given the fact that the first quarter is typically the slowest leasing quarter in our business and the given the positive sentiments expressed by our customers, we believe this bodes very well for the future. We retained over 70% of our expiring leases in the quarter and this contributed to our occupancy staying at a higher level than expected and continues a very strong trend over multiple quarters.

Same-store net operating income was also a bright spot in the quarter as improving fundamentals, which began several quarters ago, continued to accelerate. Net operating income on assets owned throughout both periods increased 3.8% on a GAAP basis and 9% on a cash basis. Over 93% of this increase was driven by revenue as first quarter 2012 average occupancy in the same-store pool increased 200 basis points over the first quarter of last year. Free or reduced rent periods on existing leases continue to burn off and concessions on new leases are declining in virtually all markets with concessions on renewals declining the most of all. It is also encouraging that the improvement we have experienced is very broad based with 17 of our markets experiencing positive cash same-store growth in the first quarter and 16 markets improving on a GAAP basis.

Turning to the remainder of 2012, we are increasing and narrowing our funds from operation guidance to $0.38 to $0.42 per diluted share up from the previous $0.36 to $0.41. This improvement is predominantly due to property operating results, where we are more optimistic today about projected occupancy and rental rates. We are raising our estimate of average occupancy for the year to 91% to 93% and ending occupancy to 93% to 94%.

More importantly in my view, we are increasing our estimates with regard to same-store net operating income growth to 1.5% to 3% on a GAAP basis and 3% to 5% on a cash basis. These estimates of occupancy in same-store growth do not take into consideration the potential effects of any anticipated acquisitions or dispositions.

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On the capital deployment front, while the markets remain highly competitive, we continue to find opportunities to create value through selective acquisitions and disciplined development activities, while at the same time executing on strategic opportunities to upgrade our portfolio and fund investment through our capital recycling efforts. We anticipate closing on $100 million to $150 million of acquisitions in 2012, comprised of a combination of stabilized assets and value-add opportunities.

We have also made significant progress on building an excellent pipeline of attractive development opportunities and are therefore increasing our estimate of additional 2012 development starts to $80 million to $120 million.

Our current plan remains to fund capital deployment with proceeds from disposition of non-strategic assets. We have been pleased with the liquidity and pricing in the investment sales market and feel very confident that we will be able to execute on transactions that are both accretive from an NAV and cash flow growth perspective, as well as impactful from strategic perspective. While this will likely have a dilutive impact on earnings in the short term, we believe it will be beneficial on the intermediate long-term as we continue to upgrade the portfolio and further enhance our cash flow growth profile.

In conclusion, we continue to be very excited and optimistic about the prospects for our business and for DCT. We believe that the current economic environment have slow – reasonably steady growth is very conducive to strengthening of market fundamentals and we anticipate this will continue or even accelerate in certain markets over the near and intermediate term. While development has increasing in some markets and frankly the right markets, it is still very moderate in terms of its scale versus the size of the existing asset pool and the size of tenant demand.

Consequently at this point of cycle we consider development and other value add activates to be an opportunity for us rather than a risk associated with any of our building, which we still believe is quite muted today.

In summary, we feel very good about our results for the first quarter and frankly for the last several quarters and feel confident that this momentum will continue through 2012 and beyond.

With that, I'll now turn the call back over to Mike for questions. Thank you.

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QUESTION AND ANSWER SECTION

Operator: Thank you sir. We will now begin the question-and-answer session. [Operator Instructions] As a reminder, we ask that you limit yourself to one question and a single follow up. Please note that you may re-enter queue if you have additional questions. [Operator Instructions] At this time, we'll pause momentarily to assemble our roster. And the first question we have comes from Craig Mailman of KeyBanc Capital Markets. Please go ahead.

Craig Mailman
Analyst, KeyBanc Capital Markets
Q

Good morning, guys. It sounds like the acquisition pipeline is pretty good here. I'm just curious what kind of spread between stabilize and value add you guys are seeing from either a price per pound basis or cap rate basis, kind of how that's trended over the last six months just given the improvement in the sales market?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.
A

I'd say that – this is Phil, a typical spread is probably 50 basis points for relatively lower risk deals to 100 basis points or more. We've been able to find some deals, which have much higher spreads than that. The Phoenix example, while small, and I wish I could duplicate that many times, is certainly on the much higher end than that. I would say that over the last several quarters, there's been more capital flowing into value add than we would have seen a year ago, but still scarce relative to all the capital chasing stabilized. So, spreads, if anything, have narrowed, but still are significant enough, at least, the deals we look at or get excited about are still there. Now, I'll also say we look at a lot of deals, maybe hundreds of deals, and we say no, a heck of a lot. One of the most common reasons for saying no to a value add opportunity, beside strength of the quality of the real state or the quality of the location, is the lack of what we think is risk adjusted return. We want to get paid for our efforts and paid for the risk.

Craig Mailman
Analyst, KeyBanc Capital Markets
Q

Okay, that's helpful. And then, just kind of switching gears to leasing, things seem pretty good here and you guys are, again, seeing small, medium tenant mix. Could you maybe just give a breakdown of the leasing activity amongst sort of bulk versus small, medium, maybe just like a percentage breakdown, if it's handy? And then maybe talk about which segment you guys think you're going to have more success on raising rents in the near term?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.
A

Craig it's Phil again. Let me take a whack at that and Matt or Mike may want to add some additional color. Clearly, the most – the dominant amount of square footage remains bulk for two reasons. One, it's the most active sector; and two, it's where square footage is. I'd say that the smaller and medium sized tenant, it's a trend, but it's still early. So, they're more active than they were, but still from a square footage perspective, smaller, but we've got a number of yields we've done. I don't know if we've got a breakdown on leasing. Actually, I'm looking at Matt. We don't have breakdown large versus small available. Maybe call Matt at some point off line and we can give it to you.

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Craig Mailman
Analyst, KeyBanc Capital Markets

Q

Great. And then, on the rent piece of it?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Craig – I'm sorry, what?

Craig Mailman
Analyst, KeyBanc Capital Markets

Q

On the rent side of it or where you guys seeing it easier to push – the large bulk tenants or the small medium-sized guys?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

I think it's a function of both size, yes, quality bulk space in strong markets is the easiest example, but then the are other spaces in other markets where – in-fill location well suited for – well suited space that we're doing the same on. The example I used – was thinking about when I was preparing my remarks, the first call I got was, I think, in January, might have been even December, in Mike's region. It was in Baltimore. But we've had a – Mike's region, five different situations, where we've had multiple tenants competing for the same space.

Craig Mailman
Analyst, KeyBanc Capital Markets

Q

Great. Thanks.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Thanks.

Operator: The next question we have comes from George Auerbach of ISI Group. Please go ahead.

George D. Auerbach
Analyst, International Strategy & Investment Group, Inc.

Q

Great. Thanks. Good morning, everyone. Phil, could you talk about your targeted returns on development either on an absolute basis or on a spread to where disposition cap rates are today?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Actually, let me – I'll talk about development, as well as value add. For each market, we've identified threshold targeted returns for stabilized assets that are based on our view of our cost of capital and our desired returns to achieve, and somewhat consistent with our strategic plan, which has a priorities of markets, as well as the risk of markets. Then from there, depending on the amount of risk – additional risk we take in the asset, i.e. leasing risk, redevelopment risk and ultimately, development and leasing risk, we expect a premium. And that ranges from, say, 50 basis points for fairly straightforward value add acquisitions to 100 to 150 basis points for more significant risk. And obviously, we'd like to get more if possible. But typically – and that's all IRR driven and I know IRRs have its flaw – their flaw. We're well aware of those flaws. So internally, we create controls, such as limiting

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residual values to some function of replacement costs, and that's some mathematical carrying out of a hypothetical cap rate five and 10 years out. So we try to be mindful of that, but we do think about, on our IRR basis, we expect to get spreads over our threshold for risk and if we don't, we say no.

George D. Auerbach
Analyst, International Strategy & Investment Group, Inc.
Q

Could you maybe just quantify maybe in the five or seven best markets in the states, kind of where that spread is for development?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.
A

Well, it's hard to quantify because the land – we're buying land six months ago, in some cases, or a year ago. I'd say for development cash yields, because I'd rather talk in that – even though we think about both yield and IRR. IRRs are so different between the operator – whoever's got the Excel spreadsheet is going to have, or the [indiscernible] (22:19) run will have their definition. But I would say 100 basis points or more of spread right now. And I'll use an example, Southern California, we think we can develop in the low 7s with a favorable land basis, but you can probably – high 6s to low 7s for – if you can find right land in a market, where stabilized deals are selling from the low 5s and even sub-5 for certain assets.

George D. Auerbach
Analyst, International Strategy & Investment Group, Inc.
Q

Great. And then just last question, Matt, you're taking up the guidance range for development. I guess, given the size of the organization today, what should we think of as kind of a good long-term volume of development you can do, given the size of the organization?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.
A

Yeah, I would say, obviously, it depends on macroeconomic conditions as well as market conditions. But I think, given the size of our company, our organization and our sort of appetite, I would say, having an active pipeline of $200 million to $300 million at any given point in time at all points of the development cycle is sort of a reasonable expectation.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.
A

George, we think about it – this is Phil, we think about it in terms of risk management and we would like to keep development – really value add, including development – no higher than 15% of our total assets and that's the risk portion of it. So pre-leasing will certainly come off of that, as Matt said, in any phase of the development. So, we are mindful of no matter how good we feel about the market and our ability to develop in it, being mindful of risk management.

George D. Auerbach
Analyst, International Strategy & Investment Group, Inc.
Q

That's helpful. Thank you.

Operator: The next question we have comes from Brendan Maiorana of Wells Fargo.

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Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

Thanks. Good morning. Matt, I have a question for you just with respect to the guidance a little bit, the year-end target on occupancy, 93% to 94%. It sounds like there's going to be more dispositions that are going to occur this year because you have more development starts and you've got more – and acquisitions are probably trending towards the high-end if I take the $26 million that's been done and the $75 million that you got in the pipeline. How much of the improved occupancy number at the end of the year is driven by sales of assets that may be below – occupancy that's below your average, if at all?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, Brendan, as I mentioned in the comments, when I'm projecting occupancy, it's based on the portfolio we own today. I'm not taking into consideration the potential impact of either acquisitions or dispositions, because you never know what you're going to sell or what you're going to buy. So those numbers are based on the portfolio as it is today.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

And do you guys think the sales that you do – because the sales in the quarter were largely – it seem like largely vacant assets, or certainly under leased assets. Is the outlook for sales what you think is likely to fund your investment activity more in line with the average occupancy across the portfolio, or do you think that those cap rate on dispositions are likely to be artificially low because occupancy is low?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, I think, Brendan, obviously sales of vacant buildings to users are a great execution from the ability to source capital that way. I think given that the amount of transactions that we expect to do during the course of the year, we're clearly going to sell better leased assets on average than they are today. So, clearly I would expect the occupancy of the buildings we sell will be higher than what we have done so far certainly this year and even when you sort of factor in the assets that we did at the end of 2011.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

Okay. And then just last question. The straight line rent adjustment dropped down and it was a nice benefit to the same store growth numbers in this quarter. You guys talked about it last year that you had a lot of embedded cash rent growth in the portfolio, given some of the leases that were signed with a lot of free rent upfront. Is most of that – are those leases, are they cash flowing now such that we're not likely to get that benefit on a go-forward basis?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Well, I think clearly the benefit will not be as great as it was as we moved towards the end of 2011. But at the same time, I mean, we still have $5 million of annualized base rent in the free rent period. We have about $2.5 million of what I've referred to as teaser rates, where we've had sort of introductory rates that are sort of below market and below the sort of extrapolatable rate that you'll get kind of once they stabilize. Honestly, I think that $2.5 million is a little on the conservative side, because what constitutes the teaser rate is somewhat in the eye of the holder.

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But I think ultimately there is a lot of embedded cash flow growth still in the portfolio today. I think if you look at – from our supplemental, if you look at the property tables, which kind of gives you a snapshot of annualized base rent today, it's just literally a moment in time at March 31. And then kind of compare that to what is in the leasing tables on the next couple pages after that, which basically shows you the expiration of leases over time, giving credit for contractual rent bumps. There's still a big – there's is a big bump in those numbers. So, clearly, the free rent is burning off. It is without question a significant contributor to the cash rent – the cash same-store growth we had in the first quarter, but it isn't done.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

Okay, very helpful. Thanks.

Operator: The next question we have comes from John Stewart of Green Street Advisors.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Thank you. Matt, can we get the breakdown or allocation of the – specifically, Atlanta and Phoenix acquisitions?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

When you say the breakdown --

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Well, I mean we've got [indiscernible] (28:32) but not the purchase price allocation to those deals?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

John, it's Phil. For tax – realty tax reasons and other reasons in some cases, maybe all cases confidentially reasons, we're not able to disclose individual purchase prices. You may be able to get them other ways, but we can't be party to that.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Okay. Well, how about the yields on the Atlanta deal, Phil? So given if that's ones 100% leased, I wouldn't have thought that 6, 5 was necessarily a market in Atlanta. Are cap rates lower than we thought?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Well, I actually – let me answer that question two ways. First, it's every bit of market or lower, which Mike can comment on in a second. Cap rates in Dallas and Atlanta have moved down into the low 6s and 6 in many cases. It's on the low end of what we've wanted to do, honestly. So, the question is why did we do it? And the reason we did it is, first, it starts with the real estate, great real estate in an infill location, in our mind, probably one of the best locations in Atlanta and one of the best parks. And then, second, it was a project where we already had a significant presence and therefore synergies, if you will. And then, lastly, the tenant is very entrenched from an

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improvements perspective as well as customers that are nearby. And so we felt very strongly about the long-term prospects. But it was – honestly, it's one of the closer calls we've had. It's a call we made in favor of buying it. But that said – Mike, you maybe – color you want to make on market, cap rates in Atlanta for Class A stabilized?

Michael J. Ruen
Managing Director-East Region, DCT Industrial Trust, Inc.

A

Yeah, absolutely, John. I would say, there are a number of comps that we've seen for Class A stabilized that have blown through a 7 in Atlanta. And what really tipped the scale are the things that Phil mentioned. For us to be in a position to build up our presence in that particular park to almost 1 million square feet, we believe we'll get a significant premium for that type of ownership. And again, the tenant that's in there, we've got another eight years of term growing at 2.5% a year. So, for those reasons we really thought it was a good buy for us.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Got it. And so, you guys have – you talked about the spread between core and value add, where would you peg the spread between coastal and secondary markets today?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

John, this is Phil. Let me – did I cut off prior to the question? I'm sorry if I did.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

No.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Okay. Cap rates right now, and John you're probably pretty familiar with some of the larger that have been done in the Southern California, South Florida, low 5s and in some high 4s for – and some of those are unique, but clearly the [indiscernible] (31:35) portfolio, clearly a 5.0 cap rate in Miami, and there have been a number of California transactions, at 5% plus or minus. We get to – there have been a few Chicago acquisitions sub-6, I'm probably getting Class A stabilized we're talking about. And then you get into, for me, Dallas and Atlanta, low to mid-6s. And then from there as you get into – and I'm probably missing some markets, but you get into secondary, but primary type markets you're probably in some cases high 6s to low 7s, all the way up to high 7s for markets that may be viewed with less favor long-term and/or market that typically not are supply constrained, but place like in the mid-7s. There is transactions that are rumor to be happening in places like Columbus, Memphis that are in the kind of high 7s, mid to high-7s in some cases depending on the asset and stabilization.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

That's very helpful. Thank you.

Operator: And the next question we have comes from Jamie Feldman, Bank of America Merrill Lynch.

Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.

Q

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Great, thank you. So, I was just thinking about your higher occupancy guidance and then the 14.6% of base rents rolling for the rest of the year. How much of that is kind of baked in with leases that are already in process? How much of that is you're feeling pretty good about and how much is still left to do?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, I think I would say of the 300 to 400 basis points of occupancy increase that are inherent in where we stand today relative to those projections, I'd say fully baked probably 20% of it, active negotiations probably another 20%, 25% and then the rest of it is – quite honestly a lot of that increase is reasonably back end weighted.

We have – the majority of our remaining role – really the large majority of our remaining role in 2012 happens in the second quarter. So, you're going to probably not see us make a lot of progress from an occupancy perspective in the second quarter, although there are some deals that are baked, as you put it. And the remainder of it is, we feel reasonably good about a lot – a meaningful number of those renewals and are in active negotiation on a number of additional leases, I think the way that I think about it is that leasing volume continues to be strong. When you juxtapose that with the idea that we really don't have many expirations in the back half of the year and you – there is no reason to consider that leasing occupancy is going to drop off the table. It has to manifest itself in absorption, I guess has to is probably too strong, but that's the way we think about it.

Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.

Q

So, as you said 20%, you think fully baked, 20% to 25% in the negotiation. That's just of the upside, that's not including renewals?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

No, that's of new leases required to get the 300 to 400 basis points of absorption.

Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.

Q

Okay. So, then where would you stay you stand on just renewals?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Renewals, we have – there's a number of large – couple of large tenants that I know of specifically that are expiring in the second quarter that are gone. We also feel very confident about a couple of other large spaces, but you never know until you sign. Those large – I mean we're talking 3,000 plus. I don't want to count chickens, but if those guys were going leave, they'd be in the process of leaving. So, we feel pretty good about that. Retention has been 70% plus for the last X number of quarters in a row and in some cases meaningfully above 70%. You know as well as I do the typical standard that I think people talk about is two-thirds. So, we know nothing that would lead us to believe that the conclusion is anything lower than that. Again, so it's based on I think reasonable expectations, but I was talking about new movements, which to me are the ones that are harder to feel good about in the abstract.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Jamie, a real quick point, which is the 1.3% of spaces leased, but not occupied, certainly, the head start.

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Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.

Q

Good point. Okay. All right. Thank you.

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, thank you.

Operator: The next question we have comes from Paul Adornato of BMO Capital. Please go ahead.

Paul E. Adornato
Analyst, BMO Capital Markets (United States)

Q

Thanks. Could you remind us how the portfolio breaks out in terms of bulk distribution versus smaller spaces and how you're feeling about that?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

So, bulk distribution, as we term it, which is somewhat market-by-market specific, is plus 92%, 93% of our total portfolio, about 90% I should say. Smaller spaces that's sort of true flexed up is more like 3% or 4%. So, that constitution has gotten better over the last several years, but hasn't moved a lot.

Paul E. Adornato
Analyst, BMO Capital Markets (United States)

Q

Okay, so the comments earlier in Phil's opening remarks regarding the smaller tenants that relates only to that small 10% of your existing portfolio?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

No. Sorry for the confusion. Within our bulk portfolio, you end up with some smaller spaces and I think of smallest 50,000 and below, maybe it's 100,000 in some markets. But to me 0 to 50,000 is small, 50,000 to 100,000 is medium and 100,000 above is big, and I think 100,000 or even 200,000 above is been where the sweet spot of the market has been for demand and that sweet spot is widening a little bit and then we're seeing a little bit of more wind, no life in the small guys a year ago. I mean, none. And I remember, Mike Ruen, a year, at least, probably a year ago making a comment on our earnings call that in order to get to the next stage of recovery we needed the little guys to wake up and they are waking up. They're still not outrunning marathons, but they're awake.

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah. And, just to put some numbers to that. So, our occupancy for the 0 to 50,000 square foot spaces is about 86%. The good news is, is that's also up about 150 basis points from year end. So, to Phil's point, you are really starting to see there is room to grow in that, but you're really starting to see improvement.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

And, with square footage, you want to give him the percentage of that, I think that's what he's asking for.

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Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah. So, that's 15 million square feet, those are spaces not buildings --

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Right.

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

That's so roughly 25% of the portfolio.

Paul E. Adornato
Analyst, BMO Capital Markets (United States)

Q

Okay, great, Thanks. That's helpful. And as a follow-up, are a lot of those smaller spaces located in secondary markets or markets that over the intermediate to long-term you might want to exit, and any change in that kind of horning of markets?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Actually, the secondary markets, but we've not said which markets we'd like to exit. But the buildings we have in, say, Columbus and Memphis are really large bulk buildings with really not any small spaces. Lot of our small spaces are – where we do have flex and the two primary flex location we have are Dallas and Atlanta. Would we like to sell our flex over time? Yes. We've got – but other than that, I'd say the quote small spaces spread throughout the rest of the markets with the exception of, again, the regional – secondary regional markets. And I'm probably creating – I'm creating name with that thought, which is a mistake, but, again, Columbus and Memphis, [ph] Indi (39:42), we've got a lot of large spaces there. Chicago, we've got a lot of smaller spaces and that's done well. So...

Paul E. Adornato
Analyst, BMO Capital Markets (United States)

Q

Okay, great. Thank you.

Operator: The next question we have comes from Mitch Germain of JMP Securities.

Mitch B. Germain
Analyst, JMP Securities LLC

Q

Good morning. Any update on SCLA?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

No, I mean the update is clearly, we've done a lot of leasing there, obviously, getting 1 billion square footer, it's not news, but I'll take credit for it again. There are – there is activity from a build-to-suit perspective out there, don't know if we'll make any. So, we are very well leased. There's a document in negotiation for the majority of the remainder of the 15 A and B, which is the small space stuff. It's very well leased today like the tenancy and

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continue to entertain opportunities to do other things there again from a build-to-suit or expansion perspective, but nothing to report.

Mitch B. Germain
Analyst, JMP Securities LLC
Q

And land sales, I know that was under something that you guys are considering at one point?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.
A

There are always a conversation or two going on, nothing that I feel like is eminent today. But, clearly, you're seeing as land prices are going up in Southern California, people are looking to that as a more viable alternative.

Mitch B. Germain
Analyst, JMP Securities LLC
Q

Thank you.

Operator: The next question we have comes from Gabriel Hilmoe of UBS.

Gabriel Hilmoe
Analyst, UBS Securities LLC
Q

Good morning, guys. Just following-up on the market rents question, I was wondering if you could expand a little bit on kind of where you're starting to be able to really push rents and where you're kind of more or less still price taker?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.
A

Hey, Mike, why don't you take that one?

Michael J. Ruen
Managing Director-East Region, DCT Industrial Trust, Inc.
A

Sure. I would say, Gabriel, net effective rents are up in just about every market that we cover. But as always the increases vary a lot by market and they certainly vary by submarket. As to Phil's points earlier, I think what the major focus is, not only for us, but the markets in general, is to get the net effective rents up through a reduction in concessions. And of course, the rental rates are following suit, but more slowly.

Gabriel Hilmoe
Analyst, UBS Securities LLC
Q

Which market it's, Mike?

Michael J. Ruen
Managing Director-East Region, DCT Industrial Trust, Inc.
A

Yeah, large bulk spaces, certainly in the markets on the coast. I mean there are handful of markets on the coastal Miami, LA, Seattle, certain pockets of New Jersey, like the Meadowland's, where we're starting to see an uptick in rents where we can begin to push. And then, certainly, in the regional markets where you have control of large spaces that are 500 and larger.

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Gabriel Hilmoe
Analyst, UBS Securities LLC

Q

Okay. And then, Phil, you had mentioned and you talked about this in the past about wanting to get out of some – certain markets and you guys just exited Charlotte. I'm curious kind of near term what's maybe on the dark end in terms of exiting some of those markets?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Nothing to report. Long-term goal is to be in fewer markets, no specific timetable. And I think we're quite pleased with the progress we've made in each of the markets. And so that's been helpful. Having lost sight of our long-term strategy and therefore, thinking about it a lot of time, but really is focused on what assets can we sell at price we think are attractive and that will help our long-term growth rate. That maybe in markets honestly where we aren't exiting, we're just repositioning, that's really an asset call in addition to our – in some cases a market call, Charlotte was both. But we exited in the last quarter Minneapolis and Kansas City, so certainly made progress already.

Gabriel Hilmoe
Analyst, UBS Securities LLC

Q

Okay. Thank you.

Operator: [Operator Instructions] And the next question we have is a follow-up from John Stewart of Green Street Advisors.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Thank you. Matt just wanted to touch on guidance briefly. And specifically, if you add really what you did the run rate in the first quarter looking at the same-store pool. If you just hold that pace for the balance of the year, let alone picking up another couple of 100 basis points in average occupancy, won't you be well above the high-end of the range for your same-store guidance for the year?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, I think a couple of points, John, it's a good question. I think the first quarter there is – G&A was – had some onetime benefits in the neighborhood of plus or minus $500,000, which are not sort of extrapolatable for the remainder of the year. I think the other thing to keep in mind is that – we talked about when we [indiscernible] (44:55) guidance and talked about a little bit in the first quarter as well as the disposition program that we've talked about will have some short-term dilution associated with it. So, I think the range of guidance we have allows for that to manifest itself, because as we've talked about honestly the dispositions that we've done thus far really haven't been as dilutive. So if you look at sort of the solid $0.10 we did on a sort of a run rate basis in the first quarter and then allow for a little bit of dilution, which we believe is possible and maybe likely from the disposition program as sort of how you get to the mid – upper end of the range as opposed to blowing through the top.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

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Sure. And I'm sorry, maybe I wasn't clear, but I was focused specifically on same-store guidance, and neither of those points would address the same-store pool.

Matthew T. Murphy A
Chief Financial Officer, DCT Industrial Trust, Inc.

Well, so the same-store – and I think the way – I guess, I wasn't clear the way to think about it is the increase in the – so if you look at $0.10 on a run rate basis and you assume that the dilution associated with dispositions will in the short-term take away some of the increase of the same-store increase, you end up with 40%, which is – excuse me, $0.40, which is the midpoint guidance. Obviously, we think there's room above that as NOI will sort of overwhelm, if you will, the effect of the dispositions. So, if that helps.

John J. Stewart Q
Analyst, Green Street Advisors, Inc.

A bit. On disposition; so just to confirm a couple of things. Number one, did I understand you to say that there you don't have anything specifically baked into the guidance in terms of dispositions?

Matthew T. Murphy A
Chief Financial Officer, DCT Industrial Trust, Inc.

No, that's just with regard to same-store projections and occupancy projections. There is no impact of – potential impact of those. Obviously, the FFO guidance contemplates dispositions.

John J. Stewart Q
Analyst, Green Street Advisors, Inc.

And how much?

Matthew T. Murphy A
Chief Financial Officer, DCT Industrial Trust, Inc.

So, we said $0.01 to $0.02, still feel that makes sense given what we're seeing in pricing and the expectation for volume.

John J. Stewart Q
Analyst, Green Street Advisors, Inc.

Okay. And you referenced some portfolio sales earlier, can you kind of help us think about – and sort of divorcing from the concept of guidance for a moment and just focusing on really the appetite for, let's call it, regional markets that represent low single-digits in terms of NOI for the company with the process and the appetite?

Philip L. Hawkins A
President & Chief Executive Officer, DCT Industrial Trust, Inc.

Our appetite or [indiscernible] (47:35)

John J. Stewart Q
Analyst, Green Street Advisors, Inc.

No, sorry, the market appetite, the ability to actually move --

---

Philip L. Hawkins A
President & Chief Executive Officer, DCT Industrial Trust, Inc.

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There is clear appetite increasingly so in established secondary, but well recognized regional distribution hubs. I'll use Indianapolis, I'll use Memphis as an example, where there transactions, let's say, not closed, they are in the process of closing, a fair amount of capital that is encouraging. Liquidity in those markets has improved significantly, so very much improving. As you would expect at this stage in the cycle not everybody is getting their first choice of a Class A asset in – next to Ontario Airport in the Inland Empire. Capital is moving to other location, as people are more comfortable with recovery. And frankly, they're more comfortable with the recovery in the middle of the country. I think that's been one of the positives and maybe one of the surprises is how well the non-coastal markets have recovered in terms of occupancy and net absorption and even rental rates.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Yeah. That makes perfect sense. And so, again, not – and I'm not focused on guidance here and more just kind of trying to get a sense for kind put brackets around really the ability to move products. So if everything goes to plan, how much do you think you could move in the next 12 months?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

I think we can move as much as we can deploy. And just to remind you what we said is we'll essentially balance sources and uses of capital, including though the fact we were ahead in the fourth quarter of dispositions, so we think about the fourth quarter disposition as part of our score card, if you will, but the intent not necessarily by minute by minute or even month by month, but certainly over time and over a fairly short period of time balancing and matching sources with uses. And I don't think our limit is on dispositions, it's really on what can we acquire that makes sense long-term from a product, a market and a return perspective. And that's been tougher part of it.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

If you really think it's a sellers market, why wouldn't you just move what you can and suffer dilution until you're able to redeploy?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

Well, I'm not sure, it's a point in time opportunity, number one. Number two, I think that the impact on coverage ratios, dividend, I mean a lot of the things, where you're just going to cash is not my view of where we should be in the market. I'm not afraid of those markets at all. We're doing quite well in them. Many of our same-store wins were in those types of markets. And I don't view this as a three week or even a three month or even six month window. That maybe where we could debate, but to me it's something we should be mindful over time. We're quite active in the acquisition markets. We're simply mindful of the opportunity to redeploy capital and the ability to sell assets at what we think are reasonably attractive prices, but also mindful of [indiscernible] (50:50) dilution for multiple reasons.

John J. Stewart
Analyst, Green Street Advisors, Inc.

Q

Thank you.

Operator: The next question we have comes from Jamie Feldman, Bank of America Merrill Lynch.

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Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.
Q

Hey, thanks. I was just hoping you could walk us through some of the total dollar amounts for some of the projects in pre-development, on page 11 of the supplemental? So like for example, DCT 55s the one you mentioned I think here it just shows the cumulative cost incurred, but what do you think the total spend will be?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.
A

Right, Jamie, this is Matt. I mean, we haven't disclosed those sort of until your – under construction, we haven't typically disclosed those. I think it's safe to say, we talk about – Phil talked about the fact that we've got the two deals that we are planning to start this year in the low end of guidance for future developments starts is $80 million. That's not a coincidence. So, that's Slover and DCT 55.

Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.
Q

Okay. And I think Slover is a bigger chunk of that or not necessarily?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.
A

Well, it's more than half, yes.

Jamie C. Feldman
Analyst, Merrill Lynch, Pierce, Fenner & Smith, Inc.
Q

Okay. All right. Thank you.

Operator: The next question we have comes from Brendan Maiorana of Wells Fargo.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC
Q

Thanks. So, Matt, I had another one for you. With respect to the TI cost, leasing commission cost, it look like the reported number was pretty low in the quarter, certainly a big drop off from Q4. When I look at the leasing that was signed during the quarter, I think the cost associated with those were higher. So should we assume that this is a little bit of a timing impact in Q1 and that that is more likely to migrate higher as we go forward throughout the year?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.
A

Yeah, I think that's a safe assumption. The other thing, if you look at CapEx, obviously, the first quarter is historically the low number on CapEx, as well as most of that stuff gets done during the summer – spring, summer and early fall months.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC
Q

On the maintenance CapEx, do you guys think that you were positive in terms of the FAD dividend coverage this quarter, at least, the way that we calculate it. Do you think that you can be positive for full year 2012 or do you think it's more likely to be a 2013 event is the thing that we're talking about last quarter?

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Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Well, obviously, those are two different questions. I think, no matter how you keep score, we're positive in the first quarter. We don't project FAD or AFFO. So I am not sure I'm going to comment on that. We've talked about previously, we still do have meaningful net absorption in 2012 projected, as I have already talked about, that comes at a cost from a timing perspective. So, it's certainly not out of the question that we will cover the dividend depending on your definition of FAD for the year, but we're not projecting that we will. I mean, we're not saying that we will. Clearly, the numbers are improving and we expect them to continue to improve.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

Okay, fair enough. And then, do you guys have a sense of when the mark-to-market on leases, the rent spreads, may turn positive? You were better than I think your negative 5 to negative 10 forecast for the year, prior initial guidance it was less negative than that in this quarter. And given the commentary that you're moving rents up in select markets and market rents are getting better in all of your markets, do you think that that's a – that you crossover in the positive territory in 2012?

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

A

This is Phil. I'm not going to go on that lame, I think it's possible. I still think – and this is not a DCT comment, because 2013 I still think because of the math it's probably early to mid-2013 when you cross. It could be earlier, if we have better rent growth than we are expecting or calculating. But I would still say the fault assumption in my view is still early 2013, maybe a little bit earlier, maybe a little bit later, but early 2013.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

And if we look at cash rents expiring over the next couple of years on – it's hard for us to do this as outsiders, but on a kind of same-store basis or same space basis, are those expiring rents going to get lower over the next couple of years, because we're going to be comping against trough market – rents that were signed at the trough in call it 2009, as we look out into 2013 and maybe into 2014? Or was it more reflective of low initial cash rents and those cash rents that are then going to expire more sort of in line with typical market rents?

Matthew T. Murphy
Chief Financial Officer, DCT Industrial Trust, Inc.

A

Yeah, I think it's a combination of all those factors. So, if you think about us as a four to five year leased term business and you think about sort of when the trough – when that the pain really started to happening from a rental rate perspective. We are now in a combination, the leases that we are singing today are being compared to a combination of pre or call it sort of 1/01/2009 rents and post 1/01/2009 rents, we have about four million square feet in 2012 that includes some of the ones that have already been done that were still pre-2009 rents.

Now having said that a number of – so you're really at that crossover point, which is part of what makes this so difficult to predict, is there are still meaningful amounts, although, diminishing amounts of leases expiring that were signed before the great recession. But at the same time, you're right, there were a number of leases shorter-term that were done in 2009, 2010 that are also expiring. And it's the confluence of those, which makes that – those rent roll downs – and you all know what a fan I'm of that calculation, those rent roll down very volatile at this point, which is why it's difficult say there will be transactions that are extremely positive that are starting now because they're comparing to against lower comps. However, there's still transactions that are comparing against

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2006 and 2007 rents, which makes that number volatile as heck. I think what you're seeing is continuous improvement. It's born itself out in our numbers. It's born itself out in the industry's numbers. And everybody feels pretty good about once you get into 2013 and beyond that you're really starting to see positive comparisons. It's that crossover point is really difficult to predict.

Brendan Maiorana
Analyst, Wells Fargo Advisors LLC

Q

Okay. Now, that's very helpful color. Thanks.

Operator: Well, that's all the time that we have for questions. We will go ahead and conclude our question-and-answer session. I would now like to turn the conference back over to management for any closing remarks.

Philip L. Hawkins
President & Chief Executive Officer, DCT Industrial Trust, Inc.

It is Phil Hawkins and thanks everyone for participating on today's call. We appreciate your interest in DCT and look forward to seeing many of you at NAREIT in June. In the meantime, feel free to call either Matt or me, if you have any questions, or even just comments. Thanks.

Operator: And we thank you, sir, and to the rest of management for your time. The conference call has now concluded. We thank you all for attending today's presentation. At this time, you may disconnect your lines. Thank you.

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