Alexander & Baldwin
Earnings Conference Call/Webcast Script
Third Quarter 2017

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Thank you, Charlotte.

Aloha, and welcome to our call today to discuss Alexander & Baldwin's third quarter 2017 earnings. With me today are our president and CEO, Chris Benjamin, and Jim Mead, CFO. Paul Ito, senior vice president, corporate finance and Lance Parker, A&B Properties president, will be joining us for the Q&A portion of the call.

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Before we commence, please note that statements in this call and presentation that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve a number of risks and uncertainties that could cause actual results to differ materially from those contemplated by the relevant forward-looking statements. These forward-looking statements include, but are not limited to, statements regarding possible or assumed future results of operations, business strategies, growth opportunities and competitive positions.

Such forward-looking statements speak only as of the date the statements were made and are not guarantees of future performance. Forward-looking statements are subject to a number of risks, uncertainties, assumptions and other factors that could cause actual results and the timing of certain events to differ materially from those expressed in or implied by the forward-looking statements. These factors include, but are not limited to, prevailing market conditions and other factors related to the Company's REIT status and the Company business generally discussed in the Company's most recent Form 10-K, Form 10-Q and other filings with the Securities and Exchange Commission. The information in this call and presentation should be evaluated in light

of these important risk factors. We do not undertake any obligation to update the Company's forward-looking statements.

Management will be referring to non-GAAP financial measures during our call today. Included in the appendix of today's presentation slides is a statement regarding our use of these non-GAAP financial measures and reconciliations. Slides from this presentation are available for download at our website, alexanderbaldwin.com. Chris will open up today's presentation with strategic and performance highlights, and then turn it over to Jim who will discuss financial performance. Chris will return for some closing remarks and then we'll open it up for your questions.

With that, let me turn it over to Chris. Chris?

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Thank you, Suzy, and good afternoon to our listeners.

I'm going to focus my remarks today on the continued strong progress we're making in the implementation of our strategic agenda, including important operational steps we've taken to grow net operating income from our commercial portfolio and monetize development assets. This is a long road we're on to transform the Company's asset mix, geographic concentration and corporate structure, but I couldn't be happier with the way things are progressing. This process started, of course, with the separation from Matson and the decision to migrate the portfolio to Hawaii. I won't go all the way back to the beginning of that migration, but I'll highlight some of the more important recent steps.

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First, there is the continued solid performance of our Hawaii commercial real estate, or CRE, portfolio, driven especially by the assets and ground leases we've acquired over the past few years. All CRE metrics reflect the strong performance of our portfolio. Same-store cash NOI was higher by 4.0% compared to the third quarter last year, same-store occupancy was up 280 basis points at 94.1%, and releasing spreads were a positive 8.4%. Year-to-date through September 30, we've renewed or released 146 space leases comprising 768,000 square feet of GLA, at releasing spreads of 15.8% on 102 comparable leases. Looking out through the remainder of the year, we expect full-year 2017 spreads to be above our previous guidance of about 13%, but below the 15.8% achieved year to date.

Ground lease renewals were positive in the quarter as well. Three were renewed at a weighted-average increase of 33%, highlighting the embedded growth potential within our portfolio. It's important to note that these increases are separate from the space lease renewal spreads I just highlighted. We look forward to additional ground lease renewals in 2018.

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On this slide, we've summarized some key commercial real estate performance metrics. Full details are included in our Supplement posted on the Investor page of our website.

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One Slide 6, underlying this strong CRE performance is continued strength in the Hawaii economy. The unemployment rate has declined to 2.5% and remains one of the lowest in the

nation. This has driven steady growth in individual income and retail spending, which are supporting not only retail tenant performance, but also the performance of our industrial tenants. People are working, income is increasing and spending is up.

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More broadly, it looks like we're headed for a sixth straight year of record visitor arrivals and expenditures based on year-to-date arrivals and expenditure figures. And other major economic indicators are positive. For example, the median price for an Oahu single family home was up 3.4% year to date to $757,000, and the value of private building permits was up 5.8% through August compared to the same period last year. So, the Hawaii economy continues to perform at a high level. Additional details about Hawaii's economy are included in the appendix to this slide presentation.

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As pleased as I am with the financial performance of the portfolio, I’m even more excited about the strategic opportunities we have in our growing Hawaii portfolio. With high-performing retail locations on all major islands, A&B is well positioned to be the landlord of choice for new-to-Hawaii retailers that want to establish a presence here and capitalize on the strong consumer demographics of the market. Things like high household incomes, high levels of discretionary spending, and low retail square footage per capita characterize the market. New leases with ULTA Beauty and Dry Bar reflect that positioning. We're very excited that ULTA, the nation’s largest beauty retailer, chose to open its first stores in Hawaii at two of our centers--Pearl

Highlands and Kailua Town. The stores will occupy a total of 23,800 square feet and undoubtedly will create excitement and draw shoppers to our centers. We're also excited to welcome Hawaii's first Dry Bar, a hair salon franchise specializing in blow outs, to our retail space at The Collection. We continue to build relationships with other retailers looking to expand their footprint to Hawaii and hope to announce more of these new-to-Hawaii leases in future quarters.

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On the topic of CRE growth, we continue to focus on how we can expand our portfolio, both through acquisitions and through development or redevelopment opportunities. We continue to pursue a number of opportunities and remain hopeful that we will be in a position to advance our mainland-to-Hawaii migration over the next year as we identify attractive acquisition opportunities. Since the pace of Hawai`i acquisitions is always hard to forecast, we continue to advance our redevelopment and development-for-hold projects, which also can provide superior returns. At Pearl Highlands, we recently turned over space to food court tenants who are now building out their improvements to be open by yearend. Likewise, Regal Cinemas' renovation is underway and is expected to be completed in time for the showing of holiday releases. Upon stabilization, these two projects are expected to add $600,000 to annual cash NOI, representing a 10% stabilized return on cost. Construction continues at Lau Hala Shops in Kailua and planning work is advancing at Ho'okele Shopping Center on Maui.

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We’ve also had good success recently in accelerating monetization of some of our development assets. Much of that success is in the form of binding sale contracts that have not yet closed, but during the quarter we did sell the Brydeswood development on Kauai for $8.1 million, a vacant land parcel on Maui for $7.9 million and a commercial lot at Maui Business Park for $1 million. At our joint ventures, two units at The Collection, three units at Kukui'ula and four Ka Milo units were closed during the quarter, contributing to the $2.9 million in equity of earnings that we reported.

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On Slide 11, here’s a little more detail on a few of our projects:

At Kamalani, we're seeing significant increases in sales interest and activity. I’m very pleased to say that, through today, 10 units have closed already, 51 are under binding contract and 18 are under contract but not yet bound. Based on the current construction schedule and the number of bound contracts, we expect 38 additional closings in the fourth quarter. These proceeds from these sales will be recycled and will allow us to continue development of the first increment without additional cash contributions, while we evaluate potential partnerships for future increments. As expected, these affordable homes in increment 1 will not generate income, but will fulfill the affordable requirements for the market-priced portion of the project and provide an additional 55 affordable credits for other Maui development projects.

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Keala o Wailea, the 70-unit multi-family joint venture with Armstrong Builders, continues to make steady progress in sales and construction. There are 62 binding contracts, and while 20 units had been expected to close this December, 15 of those are likely to slip into January as we've had some minor construction delays and we want to ensure the quality of the homes rather than rushing their delivery. This will not, however, affect cash flow to A&B as these first unit proceeds will go to pay down the construction loan. We expect an additional 25 closings by the end of the first quarter and expect to sell out the entire project by the end of 2018.

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We also look forward to closings at The Collection joint venture, where we have binding contracts for three townhomes; closings on Kahala Avenue, where we have one binding contract and some additional interest that I'll reference in a moment; and at Maui Business Park, where we have one binding contract; and finally at Kukui`ula, where we have four binding contracts, all of these we hope to close this year. As I said, we do have additional strong sales interest at Kahala Avenue, as well as Maui Business Park and Wailea. So as you can see, we're making good on our pledge to accelerate development unit and parcel sales, and this is helping generate cash flow to support other Company priorities.

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The next element of our strategy that is advancing is our effort to repurpose our agricultural lands. You'll recall it has been less than a year since we ceased our sugar operation on Maui, but

we're making notable progress in transitioning our former plantation lands to diversified agriculture. Since the sugar shutdown, A&B has worked with local farmers and ranchers, energy companies and the County of Maui in pursuit of what we hope will be a patchwork of farms covering a wide range of agricultural uses on our former sugar lands. To date, we have converted 4,500 of the 36,000 acres of former sugar cane lands into these uses. Additionally, we've been engaging with the County of Maui to expand its ag park by 900 acres, and are in active negotiations for leases to other ag users that could take our total repurposing of our land to more than half of the old sugar lands in a relatively short time. The largest of these potential users is intending to grow energy crops. We're simultaneously focused on completing these potential leases and adding to the pipeline. We originally had assumed a very long time frame for repurposing of these lands, so the pace at which we're identifying uses and tenants is quite encouraging. I should point out, however, that signing a lease is only the first step and it could still take some time before crops are planted and lease rents ramp up.

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Another important strategic focus for us, of course, is improving the performance of our Materials & Construction segment. Financial results did improve in the quarter compared to last year, with the segment generating $9.1 million of Adjusted EBITDA, despite continued margin compression from price competition for paving jobs. We're focused on increasing paving volumes to offset margin compression, and were pleased with a 30.7% increase in paving tonnage in the quarter compared to last year. We've hired a new chief operating officer at Grace

Pacific, Pike Riegert, who is overseeing all aspects of the vertically integrated paving business, from the quarry to the roads. Pike comes to us from Zachry Construction where he was Southeast Regional Manager. Among other things, he has been charged with implementing a performance improvement plan resulting from a comprehensive study conducted in conjunction with FMI, a leading consultant to the engineering, construction and infrastructure industries.

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And on Slide 16, the final strategic agenda item I want to highlight is, of course, the REIT conversion and its related elements. I'm very proud and appreciative of our team's efforts to convert a 147-year-old C-Corp to a REIT, while simultaneously transitioning out of sugar, bringing property management in house and advancing all the other strategic priorities I just described. While Jim will shed light on several aspects of the financial steps we're taking to complete the conversion, I can report that our shareholders resoundingly approved of the steps we're taking to enhance our governance practices, facilitate the REIT conversion and ensure our continued compliance with the REIT rules. On October 27, a special meeting of shareholders was held at which 99.7% of the shares voted approved our holding company merger. The merger facilitates our compliance with REIT requirements by establishing certain standard ownership limitations and transfer restrictions on A&B common stock. As part of the holding company merger, we've also eliminated the classified structure of our board, enacted majority voting for all directors in uncontested elections, and adopted other shareholder-friendly governance changes.

While the REIT conversion has been successful and well received, it hasn't been inexpensive. Total conversion costs are expected to be between $25 million and $27 million, within our previous estimated range. This estimate does not include the shareholder distribution associated with the earnings and profits purge. In addition to the conversion costs that we're incurring, we're making important investments in technology and people to ensure that we are a fully functioning REIT and can operate cost effectively as we grow. Most conversion-related consulting expenses have or will soon ramp down, and we expect that by the end of next year we'll have completed our organizational initiatives, filled a few remaining open positions and gotten to a new steady state of corporate operations that will allow us to rely less on consultants and get our corporate expenses in line with similar organizations. We'll be in a position to shed more light on this outlook on our year-end call.

With that, let me turn it over to Jim to discuss financial matters. Jim?

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Thanks, Chris.

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Net income for continuing operations available to A&B shareholders was $7.4 million, or $0.15 per diluted share, for the third quarter, this compares with $12.1 million, or $0.24 per diluted share, for the prior year. Results included the discontinued operations of HC&S totaling $0.8 million, or $0.02 per diluted share, of after-tax losses for the third quarter and $13.6 million, or $0.27 per diluted share, of after-tax losses for the prior year.

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This next slide shows the key drivers for the quarter. Operating income improved year over year by $3.6 million and reflected improvements in all of our operating segments. However, these were offset by REIT conversion costs, and increased G&A related to some additional transition costs.

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Slide 20 shows the drivers of the G&A variances for the quarter and I'd like to use this to provide some thoughts on a run rate for the company. But before I get into run rate, while I think this analysis is indicative, it's also based on just one quarter's results, so the number may change a bit quarter to quarter.

The items that are related to:

- Our transition to a fully integrated REIT and certain consulting costs required to convert internal processes and systems, that are not in the REIT conversion cost line item, and
- Personnel transition and recruiting related costs,

altogether totaled about $3.7 million for the quarter.

In addition, certain pension costs will be removed from G&A in 2018 as a result of accounting changes, and I'll speak to pension costs in a moment, but to get a run rate I'll back those out as well.

The underlying public costs of the company, including all of the senior executives and unallocated activities of the company were approximately $4.8 million during the quarter. Add to that the commercial real estate $1.7 million run rate gives a quarterly run rate of $6.5 million or $26 million annualized. This number is most representative of the Company's G&A if it were entirely a commercial real estate operation and is about 90 basis points of our total capitalization. The remaining G&A components separately support Materials & Construction and Land Operations.

As it should be in any company, G&A is a continuing focus. As you can see in our quarterly results, the largest immediate improvements in our G&A will come with the completion of the REIT conversion, and exiting of consultants that are here as a result of our conversion. So that is our current priority, to fully staff internal functions and complete systems that have changed as a result of the REIT conversion.

Looking at the bottom of this slide, we are right on track with our REIT conversion cost guidance of approximately $26 million. This quarter represented an increase year over year, but we were expecting that. Looking forward to the fourth quarter, these expenses should be about $5 million.

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I spoke about the pension contribution we made at our Analyst Day last September, but let me give you a few more of the details. Our funding of $48 million was timed to permit us to offset taxes we paid a couple of years ago in addition to creating a current year taxable event. So we benefitted on a number of fronts that reduced our payment after taxes by $19 million, and enabled us to reduce the cash portion of the Special Distribution related to our REIT conversion by $6.5 million. So in total as a result of great tax planning by our team at A&B, our $48 million contribution only cost us $22.5 million in cash.

The additional benefit is that we're now 96% funded in our qualified pension obligations. That has enabled us to match fund our assets and liabilities to reduce, or we hope, almost eliminate the volatility of the plan and to also substantially reduce the costs related to administering the plan which in total should eliminate an additional $1 million from our run rate G&A.

These benefits will begin with our new plan year at the start of 2018.

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The Special Distribution is expected to be declared in mid-November and paid in January 2018. As a reminder, the majority of the dividend--about 90%--relates to the E&P purge and will be taxable for 2017 as a qualified dividend. The portion related to 2017 distributable REIT income also will be taxable for 2017, but as a nonqualified dividend. And amounts related to 2018 will also be considered nonqualified, and will be taxable for 2018. Additional details of this will be released later this month.

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Our Special Distribution will require us to fund about $159 million of cash at the midpoint of the last slide. So as we look toward that event, and in the context of continuing low interest rates and a strong lending market, we elected to increase the size of our revolving line of credit, and to take on additional term fixed rate debt.

We are fortunate to have a supportive lending group, and they enabled us to increase our line of credit to a total $450 million capacity while at the same time reducing the rate and modifying certain covenants to create more flexibility, reflective of our change in focus to commercial real estate and the REIT conversion.

We are also very fortunate to have a strong long-term relationship with Prudential that provides a highly effective private note shelf that we have used to fund long-term efficiently priced, unsecured debt. Last month, we locked rates on a forward funding of $75 million with Prudential.

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A couple of notes on the commercial portfolio activity that will affect future quarters. The first relates to the sale of Midstate 99 Distribution Center in Visalia, California. Earlier this year, we received an unsolicited offer to purchase the property and we expect to close on this sale later

this month. Since the sale was opportunistic, we have not fully solidified the other side of the 1031, but are now working on that.

The second note relates to the 139,000 square-foot Concord Commerce Center in Phoenix, Arizona, where a tenant occupying 108,000 square feet has given notice that it will vacate 64,000 square feet at yearend, and the remaining 44,000 square feet at the end of April next year. Earnings for 2017 and 18 will include lease termination fees, and the vacancy will have a negative impact on Same Store Cash NOI beginning next year.

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Let me finish up with a couple of highlights on our financial condition, and note that we've made these stats pro forma for the forward fundings that are locked in.

We will have about $358 million available on our line of credit when our new Prudential loans fund later this month and in December.

Our net debt to EBITDA at 5.2x took a little bump as a result of the pension funding, and because the tax benefits are still ahead of us.

Our debt leverage is at 22% of our total capitalization, and importantly as we move forward into an uncertain interest rate environment, we are 86% fixed rate for an average 6.2-year term.

So our balance sheet is in a very healthy condition.

Thank you and now I'll turn the call back to Chris for closing remarks.

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Thanks, Jim.

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I want to close by kind of acknowledging all of the things that we've referenced today in terms of the progress we're making as a company. Just listening to Jim talk about the pension funding strategy that was developed by the team, the refinancing steps we've taken, the leasing progress that I referenced earlier, the diversified ag progress, a lot of other things that, frankly, I can't talk about yet because we're not ready to disclose them, I'm incredibly excited about where the company is going, and I want to acknowledge our team for all the progress they're making. There are many reasons to invest in a company, and certainly our assets, our businesses and land are all spectacular, but our team is what makes us a compelling Hawaii investment opportunity. Whether it's our real estate staff, who are among the most well respected and connected in the local industry, or our diversified ag team on Maui; or our Grace Pacific estimators or our new VPs of tax and technology, we have unique skill sets that set us apart. And, as the past few years have shown, these people have a work ethic that defies any image you may have of a laid-back Hawaii. Our team knows how to create value while making our communities in Hawaii better, and they are committed to doing it. I think that shows in the results that they are producing each day.

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So I want to thank them, and I want to also thank everyone who's listening in. We look forward to seeing many of you next week at REIT World in Dallas and now we're happy to answer your questions.