



Federal Realty Investment Trust
Second Quarter 2024 Earnings Call
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CORPORATE PARTICIPANTS

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Jeffrey Berkes, *President and Chief Operating Officer*

CONFERENCE CALL PARTICIPANTS

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Dori Kesten, *Wells Fargo*

Michael Goldsmith, *UBS Securities, LLC*

Steve Sakwa, *Evercore*

Greg McGinniss, *Scotiabank*

Alexander Goldfarb, *Piper Sandler*

Jeffrey Spector, *Bank of America*

Michael Mueller, *J.P. Morgan*

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PRESENTATION

Operator

Good day, and welcome to the Federal Realty Investment Trust Second Quarter 2024 Earnings Call.

All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's remarks, there will be an opportunity to ask questions. To ask a question, you may press star then one on your touchtone phone. To withdraw your question, please press star then two.

Please note, this event is being recorded.

I would now like to turn the conference over Brenda Pomar, Senior Director of Corporate Communications. Please go ahead.

Brenda Pomar

Good evening. Thank you for joining us today for Federal Realty's second quarter 2024 earnings conference call.

Joining me on the call are Don Wood, Federal Chief Executive Officer; Jeff Berkes, President and Chief Operating Officer; Dan G., Executive Vice President, Chief Financial Officer, and Treasurer; Jan Sweetnam, Executive Vice President, Chief Investment Officer; and Wendy Seher, Executive Vice President, Eastern Region President, as well as other members of our executive team that are available to take your questions at the conclusion of our prepared remarks.

A reminder that certain matters discussed on this call may be deemed to be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include any annualized or projected information as well as statements referring to expected or anticipated events or results, including guidance. Although Federal Realty believes the expectations reflected in such forward-looking statements are based on reasonable assumptions, Federal Realty's future operations and its actual performance may differ materially from the information in our forward-looking statements and we can give no assurance that these expectations can be attained.

The earnings release and supplemental reporting package that we issued tonight, our annual report files on Form 10-K, and our other financial disclosure documents provide a more in-depth discussion of risk factors that may affect our financial conditions and results of operations.

Given the number of participants on the call, we kindly ask that you limit yourselves to one question during the Q&A portion of our call. If you have additional questions, please re-queue.

With that, I will turn the call over to Don Wood to begin our discussion of our second quarter results. Don?

Donald Wood

Thanks, Brenda, and good afternoon, everyone.

Here are the highlights. All-time record quarterly FFO per share at \$1.69, exceeding internal expectations, analyst consensus, and a very tough comp one year ago. All-time record second quarter comparable leasing volume at 594,000 square feet, within 4,000 square feet of the most comparable leasing volume ever in any quarter. Strong occupancy gains on both a leased and an occupied basis, the 95.3 and 93.1 respectively, up 100 and 110 basis points respectively from the last quarter, levels not seen since the 2017/2019 time period.

Quarterly residential operating income on our stabilized resi properties up 6.7% versus last year, 9.5% when including the new Darien Connecticut products. By the way, the apartments at Darien Commons are 99% leased with a waiting list to get in. Strong transactional activity in the quarter with the \$215 million acquisition of Virginia Gateway and the \$12 million buyout of the minority interest at CocoWalk, not to mention the sale of our remaining assets on Third Street Promenade in Santa Monica for \$103 million. The momentum continued in July with our \$60 million acquisition of Pinole Vista Crossing in Pinole, California.

Yes, this was a very strong quarter, top to bottom, and based on what we see with our deal pipeline, this leasing environment is expected to continue for at least the balance of the year. Let me give you a little more color on leasing and its impact on occupancy. One hundred and twenty-two comparable deals at an average starting rent of \$37.72 per foot compared with the final year of the previous lease of \$34.29. Ten percent more rent to start, and that's great. By the way, those numbers include 98% of our deals, so they are truly representative of the entire Company's results.

But what makes that particularly impressive is that the rent on many of the previous leases has likely been growing at 3% or so over the last five or 10 years, and there's still room to increase the new rent to start the next five to 10-year cycle. It's actually 23% more on a straight-line basis because of those very important contractual bumps. Contractual rent bumps on all of our commercial deals done this quarter averaged 2.4% and sit at roughly 2.25% portfolio-wide, very likely the best portfolio-wide in the business. This isn't new for us. It's why in the last 20 years, this Company has grown its bottom-line earnings, 18 of them, with only the great financial crisis and the global pandemic momentary setbacks.

In this second quarter, 2Q year-over-year growth is muted, largely due to the Bed Bath stores that were all still open in the second quarter of last year. Yet we still expect the whole-year growth over 2023 to be right at the top of the sector. Compare FFO for share growth over the past one, three-year, five-year, 10-year, 20-year periods against any other large retail portfolio that has a long history, and you'll see why we're so committed to our way of doing things.

The impact on occupancy on both a leased and fiscal basis has been steady and impressive over the last three years, but never more so than this quarter. Both small shop and anchor occupancy growth stood out. In the 2024 second quarter, we picked up 100 basis points in overall lease percentage, bringing it to 95.3%. Great result, thanks to record-setting leasing volumes, the acquisition of a well-leased Virginia Gateway, the sale of a less well-leased Third Street Promenade, and by the planned redevelopment of places like Andorra Shopping Center. Our anchor lease percentage gained 90 basis points alone since last quarter and sits at 96.7%. There's another 100-plus basis points to come here.

Let me talk for a moment or two about the transactions this quarter, starting with the sale of Third Street Promenade in Santa Monica. First of all, what a great investment this has been for the Trust over the past 25 years. A 13% unlevered IRR over that period and a springboard for this Company into relationships with a type of tenant that benefited every mixed-use and lifestyle-oriented project we did. Over the past few years, we lost confidence in the future income growth there for a host of reasons and sold to a local developer for \$103 million, on in \$20 million when including a one-off sale there late last year.

Reinvesting those proceeds in a dynamic asset like Virginia Gateway with far more future growth possibilities seemed like a no-brainer. We've spoken about Virginia Gateway at various events and meetings over the past couple of months, so I won't use this time to repeat them. Suffice it to say, our Virginia Management and Development Team is all over it and excited to have the new raw material to create significant value over the next few years through releasing and selective placemaking and redevelopment.

Earlier this week, we closed on the acquisition of Pinole Vista Shopping Center in Northern California for \$60 million, which will generate an initial cash-on-cash return in the low sevens and will grow from there. This dominant 216,000 square foot grocery-anchored regional shopping center sits on 19 acres and was purchased at \$277 a foot. Not bad. The center fits in nicely with our West Coast portfolio complementing Crow Canyon Commons and East Bay Bridge in the East Bay and will be managed from our West Coast headquarters at Santana Row. We're not done on the acquisition front either.

Lease-up at Santana West continues with a newly signed deal with an AI-powered cloud database provider for 24,000 square feet on the first floor of the state-of-the-art building. Active negotiations with other prospective tenants for much of the remainder of the building should enable us to continue to report on new deals.

In Lower Merion Township outside Philadelphia, the longstanding Old Lord & Taylor building at our Bala Cynwyd Shopping Center has been fully demolished and construction is underway on our \$95 million residential development of 217 apartments with ground floor retail that will be integrated with and complementary to one of Federal's most successful shopping centers. We expect a 7% stabilized yield here. It's nice to see that development economics can still work in the right locations.

You might be interested to know that in addition to Bala Cynwyd, we have over 3,700 residential units with active design or entitlements in process at a dozen of our existing assets. As construction costs continue to stabilize, as they've been doing, and rents continue to rise with inflation, as they've been doing, these projects are getting closer and closer to penciling. Stay tuned.

By the way, for those New Yorkers listening who may have reason to be out on Long Island around Huntington, please stop by our completely redeveloped and reimagined Huntington Shopping Center, where the brand-new Whole Foods opened just last week and joined a new cadre of tenants, including REI, Ulta, new dining alternatives, and others. Set in a beautifully landscaped, comfortable setting, it really represents the best of Federal Realty thinking and execution. The \$85 million comprehensive redevelopment brought in on time and on budget. The before and after effect is pretty striking. Huntington Shopping Center is now a worthy, grocery-anchored, open-air complement to Simon's powerful Walt Whitman Mall next door.

As I was finishing up these prepared remarks earlier in the week, I was reading them to the senior team in preparation for this call. Our President, Jeff Berkes, sat back reflectively and commented as to how significant the results of our capital allocation decisions have been over the past 90 days to 120 days, given the relative size of this Company. He's right. Collectively, they're meaningful and they move the needle in a 102-property portfolio.

Between Virginia Gateway and Pinole, we've made nearly 900,000 square feet of acquisitions, deploying \$275 million of capital at a seven-plus percent yield. We've completed a comprehensive and transformational \$85 million redevelopment in Huntington, New York, began a new \$95 million mixed-use development in Bala, and freed up \$103 million of underperforming capital with the Third Street Promenade sale, all while executing 124 total leases for over 600,000 square feet of commercial space, cementing future growth. I'd say the future looks bright.

That's all I wanted to cover in my prepared remarks this afternoon. I'll turn it over to Dan to provide more granularity before opening it up to your questions.

Daniel Guglielmone

Thank you, Don, and hello, everyone.

Our reported FFO per share, \$1.69 for the second quarter, came in at the top of our quarterly guidance range of \$1.63 to \$1.69. This result was against a tough second quarter 2023 comp, which was our previous record for quarterly FFO, highlighting the overall strength and operating fundamentals across the portfolio. Primary drivers for the strong performance? Simply POI growth in our comparable portfolio, driven by strong property-level expense controls, acceleration in our occupancy levels, and continued strength in our residential portfolio.

Comparable POI growth, excluding the impact of prior period rent and term fees, was 2.9%. Now that's GAAP. It's 3.1% on a cash basis. Both numbers are above our expectation for the period, and you will see a revision upward in guidance as a result.

Comparable total property revenues were up 3.1%, with comparable min rents up 2.7% on a GAAP basis and 2.9% on a cash basis. Solid results when you keep in mind that Bed Bath & Beyond was in possession of largely paying rent throughout the second quarter in 2023.

Portfolio occupancy increased in the quarter to 95.3% leased and 93.1% occupied. Both metrics over 100 basis points increased since March 31. As a result, rent from signed leases not yet occupied in the existing portfolio stayed elevated at \$26 million, with an additional \$13 million of rent to come online from leases signed in the non-comparable pipeline.

Also note that we continue to have a robust leasing pipeline with a significant amount of new leases being negotiated for currently vacant space. With a tenant watch list that is minimal, given our lack of exposure to troubled tenants, and our proven ability to get tenants open and rent paying for a tenant coordination team that is second to none, we expect our current spread between leased and occupied to move toward our target of 125 basis points over the quarters ahead.

As we stood last quarter, we are extremely well positioned again to drive our occupancy metrics over the balance of the year and have increased our targeted year-end occupancy level to roughly 93.5%. The strength in leasing from a rollover and contractual rent-bump perspective, with 10% cash rollover and 2.4% blended increases from combined, anchor and small shop leases, resulted in a straight-line lease rollover of 23% and net effective straight-line rollover after capital of 15%, which highlights our ongoing focus on controlling tenant capital.

Now to the balance sheet and an update on our liquidity position. Given roughly \$700 million of successful refinancing activity to start 2024, we have no material maturities until 2026. We stand with about \$1.3 billion of available liquidity from our \$1.25 billion credit facility and net cash on hand. This liquidity stands against redevelopment expansion spend remaining of only \$65 million for the balance of 2024 and only \$205 million remaining to spend on our needle-moving \$850 million in-process redevelopment and expansion pipeline.

With the completion of the sale of Third Street Promenade in Santa Monica for \$103 million, access to the equity markets and the acquisition of Virginia Gateway and buyout of our partners at CocoWalk, along with meaningful growth in EBITDA this quarter, our leverage metrics at June 30 continue to show improvement. Two-Q annualized net debt-to-EBITDA has decreased to 5.8 times, that metric targeted to improve over the course of 2024 and reach the mid-5s in 2025. Fixed charge coverage increased to 3.6 times for the quarter. That metric should also improve as incremental EBITDA continues to come online.

With respect to guidance, with a solid first two quarters behind us and tenant demand continuing at a stronger pace than expected, we are raising our 2024 FFO guidance from \$6.77 per share at the midpoint to \$6.79, with the range refined upwards to \$6.70 to \$6.88. This represents 3.7% bottom-line FFO growth at the midpoint and 5% at the upper end of the range. Strong growth in the face of a higher interest rate environment that faced us in both 2022 and again here in 2023 and again here in 2024.

This upward revision implies over 5% FFO growth at the midpoint in the second half of 2024. This upward revision is driven by stronger underlying portfolio performance than expected, as occupancy metrics outperform expectations, as well as the acquisition of Virginia Gateway and Old Vista Crossing, combined with the sale in Santa Monica, which only provides modest net accretion this year but will contribute more fully in 2025. Our guidance reflects only these three transactions.

As a reminder, prospective acquisitions and dispositions will be reflected in our guidance when completed. We are also revising our comparable growth outlook, upward comparable growth, excluding prior-period rents and term fees is revised to 3% to 4%, 3.5% at the midpoint. We are leaving our comparable growth outlook as is at 2.25% to 3.5%, given term fees year-to-date have lagged.

As such, we are adjusting downward our assumption for term fees from \$4 million to \$7 million to \$4 million to \$6 million, as well as our assumption for G&A expense down to \$48 million to \$51 million. While leasing progress continues both at One Santana West and 915 Meeting Street, none of this incremental activity is expected to impact our forecast for 2024. We will see the benefit in 2025. More to come on that outlook overall as the year progresses, additional leases get signed, and clarity on delivery dates becomes more evident. We are maintaining our expected credit reserve of 70 to 90 basis points, and all other guidance assumptions can be found outlined on Page 27 of our 8-K.

Now, before we go to Q&A, let me highlight that yet again, Federal Realty's Board of Directors has declared an increase in its quarterly common dividend per share to \$1.10 or \$4.40 per share on an annualized basis, which represents the fifty-seventh consecutive year we've increased the dividend. In REIT industry records, we stand as the only REIT with the status as a Dividend King, which signifies 50 or more consecutive years of annual dividend increases. A 57-year record serves as a testament to our commitment to delivering a stable, growing cash flow stream for our common shareholders.

With that, Operator, I'm going to open up the line for questions.

Operator

Thank you. We will now begin the question-and-answer session. To ask a question, you may press star then one on your touchtone phone. If you're using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star then two. We kindly ask that you please limit yourself to one question and may requeue for additional questions.

Our first question today will come from Juan Sanabria with BMO. Please go ahead.

Juan Sanabria

Hi, thank you for the time. Just hoping, Don, you could talk a little bit more about the acquisition environment. Has the touch of assets you're looking for changed? I think before you're focused on larger assets with less competition. Just general pricing expectations, great success year-to-date, but have cap rates come in at all or that low 7% is still the bogey that we should have in the back of our minds?

Donald Wood

Yes. No, Juan, it's a very fair question. We talked earlier in the year about a window and being able to jump through the window when the arbitrage makes sense. I can tell you that if we signed up Virginia Gateway today, it would be more expensive than what we bought at, crystal clear, so that they have come in a little bit. As you would expect with assumptions of interest rates overall coming down. There's nothing more sensitive than that. Yet still, we've got some things working in the hopper that look like they can make some sense again, whether we close them or not, I don't know.

But yes, you should absolutely, you should assume that there's a direct correlation between the product that's available out there and what the cost of money is. Frankly, the ones that we've made so far, where we hit that window right on, I'm feeling great about those two. In terms of the others that we're looking at now, still assume around the same places, maybe inside it a little bit. But let's see what happens with interest rates in the rest of the year with respect to how much product is available.

Juan Sanabria

Great. Then just you mentioned incremental leasing at Santana. Just curious where that is leased today. If there's been any update from Splunk and Cisco and how we should think about capitalized interest in 2025 with the leasing progress you've made to date for that specific asset?

Donald Wood

Jan, you want to take that?

Jan Sweetnam

Yes, sure. Juan, the leasing at Santana West with this new AI-based tech company is going to bring us well above 50%. We have letters of intent. We're working back and forth, actually pretty rapidly right now, with about another 70,000 square feet of demand there. We may not be able to sign all of them. We'll see. But I would think that we'll start to get pretty well leased up by the end of the year, beginning of the first quarter of next year. Seeing pretty good activity. Smaller tenants, we're breaking floors. That's where we're seeing really, really strong demand. No update whatsoever on Cisco or Splunk or what their plans are, that lease is still a ways off. We'll have to see what comes with that.

Daniel Guglielmone

With regards to capitalized interest, with regards to 2025, we have no change in terms of the outlook. We're getting better clarity. But we still need more things to pull in place before we'll provide any guidance on that front.

Operator

Our next question will come from Dori Kesten with Wells Fargo. Please go ahead.

Dori Kesten

Thanks for taking my question. You previously talked about adding about 100 basis points of small shop occupancy this year and I believe 200 on anchor. I think you're already there on small shop and pretty close on anchor. Can you give us an update on your perspective about where you may end the year on occupancy?

Donald Wood

Yes. I expected this question, Dori, because, yes, we blew through our assumptions with respect to what we assumed. As I said, I still think there's another 100 basis points or so to go more on anchor. I don't think it's this year. I think it's between—it's by the end of 2025, effectively there. On small shop, man, there might be a little bit more to go there too, which I was not expecting to be able to say, but the pipeline really looks very strong. That's all good news. I don't know if I have a number for you.

Daniel Guglielmone

No. In my prepared remarks, I highlighted that we've revised upward our targeted year in occupancy level to roughly 93.5%. That's a ballpark estimate and obviously dependent upon how quickly we can get folks open in terms of what deals we've got already executed.

Operator

Our next question will come from Michael Goldsmith with UBS. Please go ahead.

Michael Goldsmith

Good afternoon. Thanks a lot for taking my question. Same property NOI slowed sequentially in the quarter, though presumably that reflects the more difficult comparison, just given the guidance that implies a return same property NOI growth back to that mid-to-high 3% range. But can you just talk a little bit about the assumptions of how you get there? Is that right that we're getting back to that mid-to-high 3% range and just outline some of the expectations on how you get there through the back half of the year? Thanks.

Daniel Guglielmone

Sure. It's really going to be driven by occupancy. I've got largely—it was a little back end of the quarter weighted in terms of the move ins. We didn't see fully the strength in occupancy growth during the quarter. We'll see that more fully in the third quarter. We expect to be in the mid-to-upper threes in the second half of the year. It's not a big stretch just assuming occupancy rates are elevated in the second half of the year.

Operator

Our next question will come from Steve Sakwa with Evercore. Please go ahead.

Steve Sakwa

Thanks. Good afternoon. Dan, as you sit here August 1, you got a lot of things that are known, and in the bag, and you don't really have any debt speaking of to mature this year. Just help us think through the swing factors of getting to the low end of the FFO range and the high end of the FFO range.

Daniel Guglielmone

Yes. Look, I think that we outline on our guidance page all the different factors that can get us to the upper end and the lower end. Occupancy is a big driver to get us towards the top of the range. Other things that are on there, whether it be other revenue, whether it be parking or percentage rent, are probably more middle of the road in terms of what our expectations have been this year so far.

Term fees will lag based upon where we are this year because tenants candidly really don't want to give space back. That's going to be end up coming in probably closer to the bottom of our range, given where we sit today. I think we also—look, we have a very conservative approach to revenue recognition in terms of—and some of it's just timing. Timing of when cash basis tenants pay, and that can cause some swings between quarters and so forth. That's part of it.

It's also a big driver of getting us to the top of the range again is really how successful we can be in continuing to get tenants open on time or ahead of time and beating our rent commencement dates. It's going to be critical from that perspective. Then to a certain degree is how many—we do have some floating

rate exposure to get us further up is, do we have one, do we have two, do we have three rate cuts? I think that's probably more going to be more impactful next year. But also, that's a little bit of a swing.

Operator

Our next question will come from Greg McGinniss with Scotiabank. Please go ahead.

Greg McGinniss

Hey, good evening. Based on retailer guidance, it appears tenant sales growth is under some pressure. There's plenty of anecdotes out there about challenges facing the lower-end consumer and potentially inching up the socioeconomic ladder as well. Are you seeing any of this leak into tenant conversations or willingness to be taking new space right now? Or do retailers just seem either immune or they don't care that this is happening?

Wendy Seher

Yes, Greg, it's Wendy. We are not seeing that diminish in any way the leasing demand that we're seeing over our various different product types. I think if you look at the tenants that are in our portfolio, that lower-end tenant that's sensitive, whether it's Dollar Tree or Party City or some of those tenants that are—even McDonald's as they just came out with some varied reports on the consumer and their impact on that lower end consumer.

We are not seeing that. In fact, we were having discussions with Starbucks the other day, and they've had some mixed results that you saw come out. I was looking at all of our 40-some locations that we have with them and we're not seeing any impact on their sales because our demographic in our markets is more of that affluent upper end demographic. There is some fatigue showing in the \$6 latte, but not so much in our markets.

Operator

Our next question will come from Alexander Goldfarb with Piper Sandler. Please go ahead.

Alexander Goldfarb

Hey, I'm not sure it's up in my name today, but it's Alexander still. Don, question for you on new supply. We keep hearing the same thing which is that rents would have to be 35%, 50% higher to justify new supply and mass. I'm just curious, as you guys look at redevelopment and taking down portions of centers, rebuilding, are you looking at the same rent math needed to do basic redevelopment? If not, what explains the significant difference in rents needed to pencil between new supply and redevelopments?

Donald Wood

Yes. No, Alex, and I'm not calling you Alexander, by the way, you're Alex to me, buddy. You've got a couple of things to think about, including construction costs. Let me start with that because that is the first thing that—it's been a long time since we've seen pressure on prices—construction prices coming down, and we are starting to see that.

Now, whether that's actually the cost of things like lumber, which is under pressure, certainly, to come down, given the lack of housing starts, whether it's lack of work so that the developers profit, is they're more willing to take less profit. There are incremental changes there that are very important to the whole equation.

Then when you come to the rents and what rents are needed, it obviously not only depends on the starting rent, but it definitely depends on where you see your growth.

Particularly, when we're talking about a number of the things that we would redevelop, in particular, we got a lot of residential stuff that would be added to our existing properties like Bala. We're sitting there saying you clearly know that there's more housing needed throughout the country globally. When you're sitting, you add them to mixed use—or to shopping centers to create more of a mixed-use environment there. What we've seen is the ability to press up like I've told you on my residential rents.

The combination of where those rents are going, or are today, will be tomorrow and continue to grow coupled with construction costs are really important. As I'm talking to you, Jeff Berkes is putting up his finger. He's got something else to say, Alex, we're going to add that in. Go ahead, Jeff.

Jeffrey Berkes

Hey, Alex. If you're thinking about this from a, are we concerned about more competitive retail supply coming into our trade areas, I would definitely say that the vast majority of the places where we're located, single story retail with service parking is not the highest and best use of the land, which is what Don's getting to. Our locations lend themselves to densification, maybe a little bit of ground for retail in an apartment building or something like that. We are starting to see those economics become more viable.

But in terms of us getting a lot of competitive new supply in the trade areas where we do business, we just don't see that. In fact, we see a lid on supply and maybe downward pressure on supply, which is giving us a lot of pricing power with retailers.

Operator

Our next question will come from Jeff Spector with Bank of America. Please go ahead.

Jeffrey Spector

Great. Thank you. Maybe just follow up on all the leasing that you've executed. Can you talk a little bit more about categories? I know you had a comment about lattes, but there are a lot of questions on restaurants. Can you talk a little bit more about, again, leasing demand by category, what you're trying to fill at this point, and then any other anecdotal comments you can share and what you're seeing throughout the portfolio in some of the categories like restaurants that people are concerned over? Thank you.

Wendy Seher

Yes, I think in terms of categories, it's still pretty widespread in terms of what we see, again, in our different property types. That remains strong. I was looking at sales from the first part of last year to the first part of this year, because when we're looking at what we're concerned about, our sales growing is one metric to look at, and AI is another metric to look at as to who's visiting our shopping centers. There's multiple points to check the health and the productivity of our tenants.

I was looking, for example, fast casual restaurants is booming with us. I think maybe what we're seeing is there's just more options out there. That's a big category that we've been focused on in many of our properties. Whole price apparel is doing quite well. Specialty foods are doing quite well. All those and anything health and beauty related, off the charts. Anything in those categories, they're growing like an 8% to 12% per year. When those sales are growing, we're still being able to push those rents.

That doesn't even get into with some of the retailers, sales is one metric, and that e-commerce distribution is another metric that we don't always have full eyes on that can be quite productive from a retailer perspective.

Donald Wood

Jeff, I feel like I always have to caveat whenever a question comes up about categories. I feel like I always have to qualify it by saying, you have to look at the operators and you have to look at best-in-class operators in whatever the category is. Because as we see—I was just looking at sales numbers for our restaurants, for example, at Santana Row, at Pike and Rose Assembly Row, extremely productive. Part of the reason they're extremely productive is because there's some of the best operators in the space. If you've got the best properties, you've got the ability to be a little bit more choosy on who comes into those properties. That applies whether you're talking about, apparel operators, smaller shop apparel operators, restaurant operators, gym operators, all of it. When you look at a time where the consumer is—there is worry about the consumer going forward, I can tell you, mediocre businesses go away. Strong businesses find their way through. That understanding of the strength of the operator has to be figured into the mix when you ask about categories. It's more than just categories.

Operator

Our next question will come from Mike Mueller with J.P. Morgan. Please go ahead.

Michael Mueller

Yes, hi. Going back to development, redevelopment, whenever you decide it's the right time to flex up again the program, do you think it's going to be more retail focused, or mixed use resi focused at first?

Donald Wood

I think it's going to—what we've learned on our mixed-use properties is absolutely that the integration of the uses, and this actually applies to office too, we won't be building office anytime soon. But that the integration of those units, whether you're talking about residential or whether you're talking about office or whatever you're talking about, is clearly much more impactful if it's near all the other amenities. It's the fully amenitized environment. When you look at our shopping centers, you know that our shopping centers are in pretty darn good demographic areas where the rents for residential would largely be high enough or getting to be high enough to be able to make those numbers work.

When I talk in my comments about 3,700 apartment units that are either entitled or being entitled or being designed, that's probably where we'll start as evidenced by Bala in terms of where big development happens. Now, if you go out to Huntington, that's a complete retail redevelopment of a shopping center. That opportunity came to us, frankly, before COVID, and we've worked through that. When I look now, I believe residential adding to our retail shopping centers is probably where you'll see us starting as evidenced by Bala.

Operator

Our next question will come from Craig Mailman with Citi. Please go ahead.

Craig Mailman

Hey, good evening. Just maybe a quick two parter here. One, have you guys disclosed yet the cap rate on Santa Monica? Then two, I noticed you guys did issue some equity during the quarter. I'm just curious, as

you continue to acquire assets, potentially in the back half of this year into 2025, the sources of capital, whether it be equity or would you sell more assets into the potential strength here with the 10-year coming in a bit, what's the optimal mix as you guys look to redeploy capital the most accretive methods?

Donald Wood

What was the first part of the question? You got two questions in there.

Craig Mailman

(Multiple speakers) I did. I cheated.

Donald Wood

Yes. No.

Craig Mailman

The first one was a question on cap rate on Santa Monica.

Daniel Guglielmone

The cap rate on Santa Monica is a little bit of a hard one. It's mid-to-upper sixes in place, but it quickly goes down into the fives. Next year and the year after that, low fives. The unlevered IRR that we penciled has a low six handle on it. It's a really attractive source of capital. Not as accretive this year as we would like, but very much accretive over the longer term.

The second piece in terms of, look, we acquired and put to work in the quarter \$287 million of capital in CocoWalk buyout at Virginia Gateway, at Pinal Vista Crossing. Raising capital, which we always do in a balanced approach that we fund the business. We have a multiple premium and an attractive multiple that even though it's not where we'd like it to be from an NAB perspective, it's still accretive capital where we deployed it, that \$287 million, and it was in modest amount, about a quarter the capital needed there was to fund it. I think it was very prudent in terms of how we approached it.

With regards to going forward and future acquisitions, we'll be opportunistic. We have a big, full pipeline of assets under consideration for sale. That will be a component of it. I don't think it necessarily means we will sell. Then we'll look to opportunistically tap the equity market as we see it's an accretive, if we can accretively deploy that capital and grow FFO from. That's how we look at that.

Operator

Our next question will come from Floris van Dijkum with Compass Point. Please go ahead.

Floris van Dijkum

Guys, how are you? Good evening. Quick question...

Donald Wood

Hey, just one thing, Floris. One question, not a three-parter.

Floris van Dijkum

No, I'm not going to cheat. I'm not. But I just—you guys have historically always focused on the softer aspects around leases in terms of rent bumps and etcetera. A lot of your peers are touting the fact that they're now driving 3% rent bumps annually, etcetera, as well as less renewal options. Maybe if you could talk about what are the improvements that you're seeing in your lease terms? Are you able to drive what percentage of your leases that you're signing, for example, on your shop tenants are having rent bumps of 4% and maybe some more detail behind that? Also maybe talk about some of the other—the terms for anchors. Are you able to shorten the lease terms there or is there at market upside at certain levels?

Daniel Guglielmone

Yes, Floris, we announced blended anchor and small shop that was 2.4%. Really, really strong. Nobody else I think is even close. That's driven by significant percentage of our leases at 3% or better on the small shop side, and we get better rent bumps on our anchors. Probably in the mid to upper ones. I think that was about where we were this last quarter.

That blended gets us there. We continue to push that. It's an important component, but we also look to push other components. The starting rent is an important part of it as well. The more qualitative aspects, I'll hand over to Wendy in terms of what are the things are we getting from tenants in this environment where we're getting better negotiating leverage.

The other thing I'd like to highlight to you is it's just also, we had a good quarter and we got a good couple quarters in terms of TI's. We're starting to—I mentioned that in my prior remarks, we're focused on controlling those TI dollars and limiting that. That's why I highlighted the net effective straight-line rents in the mid-teens is an impressive number and something I'd like to highlight.

Wendy Seher

I think the only thing that I would add to that would be the different components of that contract, whether it be options, whether it be increases, whether it be control rights, exclusivity. There's so many components that really hasn't changed with this high demand that we're going after them any differently than we've always treated them, which is every component is separate and every component needs to make sense on that particular aspect.

I would say we are having some success in getting some more flexibility on options, for example, which we don't like options. We just don't and we rarely give them. If there's a—if we have to and if there's a capital allocation that's heavy from the tenant, we have to, we'll try to see if we can do it at a fair market value with a base and try—maybe we've done several, many actually, where you tie it to a sales volume that they can't exercise it unless they're reaching a certain level of production within the center.

Yes, we are diving deep into all those like we always do and having more success. It's a balanced approach. We're doing a lot of business with these national and regional tenants. We want to make sure that we have a balanced approach.

Donald Wood

Yes. The only thing I'm going to add to that, Floris, is I've always touted that I felt that our contracts were among the strongest, if not the strongest in the industry. When I say contracts, you know what I'm talking about, not only lease bumps, which we can quantify, but certainly the qualitative things like redevelopment rights, like lack of sales kick outs, like lack of co-tenancy. All of that, I think our contracts are stronger today than they were a few years ago even. A few years ago, I think they were best in the sector. Hard to prove it. Better locations give us more leverage. That's where I think we are.

Operator

Our next question will come from Haendel St. Juste with Mizuho. Please go ahead.

Ravi Vaidya

Hi, there. This is Ravi Vaidya on the line for Haendel. I hope you guys are doing well. I've got a quick follow-up to the guide here. Why maintain the 70 to 90 bps for bad debt at this point? The portfolio seems to have minimal tenant credit issues. What's on your watch list right now for the back half of the year?

Daniel Guglielmone

Hey, look, I think 70 to 90 is still operative. I think we were at the lower end of that range in the first half of the year, the way we look at it. I think that it's proven to keep that same leverage. I'm hoping we'll end up towards the bottom end. Certainly, if we can end up towards the end, obviously that enhances our ability to outperform and get towards the upper end of our range of guidance. But I'm fine given where we were. I think the first half of the year, we ended up at the lower end of that range, and I don't think it's—we don't see a reason at this point to change that out.

Operator

Our next question will come from Linda Tsai with Jefferies. Please go ahead.

Linda Tsai

Hi. Dan, you mentioned earlier you're doing a better job of controlling TI dollars. What does that process look like and what are those conversations? How do those go?

Wendy Seher

I will start with the anchors. Many of these anchors we have longstanding relationships with and they're eager to figure out how to make more deals. We're getting into the details of the space and really digging deep and they're getting creative on how they'll take that space and what condition that space needs to be in. That speaks to the demand and the quality of the real estate.

On the smaller shops, we have probably the most ability to influence that conversation. Yes, we are using that to maximum. We also want to understand how much capital they're putting into the space as well. Many discussions and having some good progress.

Donald Wood

Yes, Linda, just to make that really clear, I think the biggest thing there is what a tenant and what we as a landlord are willing to do to be able to get that tenant in the space and operating. Whether that means hanging on to an HVAC unit that you would have wanted replaced ideally. No, let's give that five years and let's see how that goes. Whether it looks at—whether it works on a storefront that a tenant particularly wants that we'll put a limit on and so they'll pick up the incremental cost of a particular storefront they get in. Things like that. What it is a willingness to work together because of the heavy supply demand where we are in demand supply of the space to accept space differently than they were before.

Operator

Our next question will come from Paulina Rojas with Green Street. Please go ahead.

Paulina Rojas

Good evening. The retail environment is clearly very solid. What do you think this environment will translate in terms of market rent growth in your markets for the next 12 months to 14 months? It seems to me that investors are generally very hesitant to forecast market rent growth above, let's say, 3%, 4%. I wonder if you agree or disagree with this view.

Donald Wood

What I would say first, Paulina, about that is take it back to the tenant. That tenant is pushing through—is doing two things in order to be profitable in their business. One is they're trying to push through the inflationary costs that are obviously 35% higher than they were pre-COVID. They're trying to push that through. The more successful they are, the more willing they are to be able to pay more rent. Kind of an obvious thing there. What's a little less obvious is the work that they're doing on their margins to try to make their businesses more efficient so that even to the extent they're unable to push all the cost increases through, they're trying to increase their profitability. That goes into what they're willing to do for space.

If you take a tenant that is having success with the consumer and you take a lack of choices that that tenant has as to where they're able to move, that's where you can get some pretty good-sized rent increases. Importantly in that absolutely is the contractual bump, and I know you hear us say it every single day, but we have to say it every single day because it's an important part of the economics.

I don't know that I have a percentage for you. When you see us able to move overall tenant increases to 10% from the new stuff versus the last year of what was in there, on top of those bumps, let me tell you, that's really strong. That's worth 23% on a straight-line basis. I don't see that changing over the next 12 months to 14 months. That's where I think you should expect us.

Operator

Our next question will come from Tayo Okusanya with Deutsche Bank. Please go ahead.

Omotayo Okusanya

Yes. Good evening, everyone. Congrats on the great quarter and the outlook. Don, curious, and I'm not sure if this is a fair question, but curious what your thoughts are on this news out there of Blackstone potentially buying ROIC and specifically just what you think the implications are for the broader shopping center group and maybe FRT in particular, if any.

Donald Wood

No, of course, Tayo, it's a very fair question. What you're going to hear is an opinion because I have no inside knowledge of it. But when you sit and you think about, looking forward at the demand for retail space over the next five years, I think you should feel pretty good about that. I think Blackstone feels pretty good about that or there wouldn't be negotiations that way. I think that is all about not only the supply demand characteristics that we've all been talking about here, but also the valuations and the choices in other sectors, which are not as robust as maybe they were over the last couple of years.

When you put all that together, it doesn't surprise me. You know that there are, whatever we've got, 17 companies in the shopping center index or something like that. Many of them are smaller cap companies. I think you should always expect companies like that to be under pressure of sale. Now, whether those

deals happen or not, we'll have to see. But I've never thought of Blackstone as being a company that really stretched. I suspect they see a lot of value there.

Operator

Our next question will come from Greg McGinniss with Scotiabank. Please go ahead.

Greg McGinniss

Thanks for taking another question. Dan, I apologize if you addressed this in the opening remarks. I just couldn't remember. But what's the expectation on bad debt embedded in same store and has that changed at all?

Daniel Guglielmono

That's still the same 70 basis points to 90 basis points we had originally. That's outlined in our guidance and in the prepared remarks. I don't think we're shifting it around. We ended up in the first half of the year in the lower end of that range. Hopefully we can remain in that lower end of that range. That's reflected in the same store outlook.

Operator

This will conclude our question-and-answer session. I'd like to turn the conference back over to Brenda Pomar for any closing remarks.

Brenda Pomar

We look forward to seeing many of you in the next few weeks. Thanks for joining us today.

Operator

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect your lines at this time.