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Easterly Government Properties, Inc.

Third Quarter 2020 Earnings Conference Call

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CORPORATE PARTICIPANTS

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Meghan G. Baivier, *Executive Vice President, Chief Financial Officer and Chief Operating Officer*

CONFERENCE CALL PARTICIPANTS

Manny Korchman, *Citi*

Michael Carroll, *RBC Capital Markets*

Michael Lewis, *Truist Securities*

Peter Abramowitz, *Jefferies*

Bill Crow, *Raymond James*

Merrill Ross, *Compass Point*

PRESENTATION

Operator

Greetings, and welcome to the Easterly Government Properties Third Quarter 2020 Earnings Conference Call.

At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require Operator assistance during the conference, please press star, zero on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Lindsay Winterhalter, Vice President, Investor Relations. Thank you. You may begin.

Lindsay S. Winterhalter

Good morning.

Before the call begins, please note the use of forward-looking statements by the Company on this conference call. Statements made on this call may include statements which are not historical facts and are considered forward-looking. The Company intends these forward-looking statements to be covered by the Safe Harbor provisions for forward-looking statements contained in the Private Securities Litigation Act Reform of 1995, and is making this statement for the purpose of complying with those Safe Harbor provisions.

Although the Company believes that its plans, intentions, expectations, strategies and prospects as reflected in or suggested by those forward-looking statements are reasonable, it can give no assurance that these plans, intentions, expectations or strategies will be attained or achieved. Furthermore, actual results may differ materially from those described in the forward-looking statements and will be affected by a variety of risks and factors that are beyond the Company's control, including, without limitation, those contained in Item 1A Risk Factors of its Annual Report on Form 10-K for the year ended December 31, 2019, filed with the SEC on February 25, 2020, and in its others SEC filings, and risks and uncertainties related to the adverse impact of COVID-19 on the U.S. regional and global economies, and the potential adverse impact on the financial condition and results of operation of the Company. The Company assumes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events, or otherwise.

Additionally, on this conference call, the Company may refer to certain non-GAAP financial measures, such as funds from operations, funds from operations as adjusted, and cash available for distribution. You can find a tabular reconciliation of these non-GAAP financial measures to the most comparable current GAAP numbers in the Company's earnings release and separate supplemental information package on the Investor Relations page of the Company's website at ir.easterlyreit.com.

I would now like to turn the conference call over to Darrell Crate, Chairman of Easterly Government Properties.

Darrell W. Crate

Thank you, Lindsay. Good morning everyone, and thank you for joining us on this third quarter conference call.

Today, in addition to Lindsay, I'm joined by Bill Trimble, the Company's CEO, and Meghan Baivier, the Company's CFO and COO.

During this period, we've had a significant number of calls and meetings with new investors, particularly those from the international community, so I thought I'd share a frequent question that we receive, "are we an office or are we a net lease REIT?" For those of you who are new the call, I'll share the answer.

The principles that underpin our business are clearly net lease REIT. We can develop and purchase several hundred million dollars of mission-critical buildings each year to grow earnings. However, there are two factors that make us superior to net lease: the quality of our cash flows and the value of our young buildings to track the growth and replacement cost.

First and foremost, our cash flows are based upon the full faith and credit of the U.S. government. You will not find a single U.S. REIT with a better tenant credit quality than Easterly. Our leases supporting our portfolio are, on average, 10 to 20 years in length, which provides far superior visibility to future cash flows than any traditional REIT. We have extremely high renewal rates at lease expiration to the build-to-suit, mission-critical nature of our portfolio. Today, our existing leases, each with one assumed ten year role and a ten percent rental increase, would equal $4.3 billion of future cash flow that's backed by the full faith and credit of the United States government.

Like any net lease, we build shareholder value through a robust acquisition program, coupled with non-speculative development activity. Given our attractive cost to capital, these activities translate into 2% to 3% FFO growth per year, coupled with a roughly 5% dividend yield. This delivers a 500- to 700-basis-point premium to the 10-year treasury. I would observe that the premium we deliver, relative to treasuries, is near an all-time high.

When you take a closer look at what we have built, you will see Easterly as real estate without the drama. A pandemic does not diminish our value and we are not beholding to one political party, to local rent markets or one geographic area of focus. Added to net lease attributes without volatility, our facilities are purpose-built, highly sophisticated government leased facilities, designed with SCIF space, secure networks, perimeter fencing, visitor screening, bollards, and a host of other improvements. These features add specific value to our tenants and provide an opportunity for value creation upon re-lease. Further, we've created a portfolio that delivers stability, with no single asset representing more than 2.7% of annualized lease income set to expire in the near term.

Given that our method of value creation is differentiated from the REIT market, we've done what we can to limit our exposure to index fund price movements by limiting their ownership. I would observe, to those of you who are managing to benchmarks, we've largely performed in line or better with the Russell 1000, with cash flows far less volatile, based on the full faith and credit of the United States government.

2020 has been a dramatic year in every sense as the world navigates the pandemic, and here in the United States, we face economic, political and social unrest. It's often difficult to spot directional changes in history, but it certainly feels like one of those times. Uncertainty extends to the real estate sector, in general, and the REIT sector, in particular, as investors must make portfolio decisions based on macro and micro factors that have never been more opaque.

Ten years ago, we purchased our first FBI building for our new private equity fund, that became the first building block of what is today Easterly Government Properties. We launched into our focused first tranche of government space because we saw a clear opportunity to harness the world's best credit, while also taking advantage of long-duration leases and incredibly high renewal rates. Ten years later, that first FBI still provides a mission-critical home for the San Antonio field office and remains young in its life.

The world has gone through many gyrations since 2010, but our story, the government's mission and our strong and sustainable growth remain the same. We're looking forward 2021 and are pleased with the stability and predictability of our platform to create value for shareholders in, of course, the coming year and the decade ahead.

Thanks, everyone, and with that, I'll turn the call over to Bill.

William C. Trimble

Thanks, Darrell, and good morning. Thank you for joining us for our third quarter earnings call.

As the pandemic continues to cripple the American economy, it gives me great pride to report that Easterly is continuing to weather the storm with little to no impact on the Company's daily operations, and maintains a portfolio where tenants continue to pay 100% of their rental obligations.

While we are now eight months into the pandemic, with no end date in sight, Easterly continues to work with our government tenants to provide a safe and clean work environment. I want to highlight the incredible job our Asset Management Team has done keeping our mission-critical facilities open and ready to serve the American people. The unsolicited letters of appreciation we have received from the government makes us proud of the job our team is doing every day.

In an environment where other office landlords are questioning their long-term strategies due to the economic effects of COVID, I am pleased to report that we remain so highly focused on owning bullseye, mission-critical assets leased to the U.S. federal government. The missions, locations and design of our majority low-rise portfolio provides a safe and sustainable footprint for our enduring portfolio.

While the Easterly earnings call may be the most important event of the week to us, I would be remiss if I did not acknowledge the presidential election. As the country is on edge awaiting the election of our next President, I'm pleased to report that the impact on the Easterly portfolio should remain unchanged. Our investors have seen Easterly thrive under both democratic and republican administrations, as we remain apolitical, owning buildings whose missions transcend the parties' different philosophies.

During the last 10 years of executing our strategy in the private, and now public, markets, we have gone through government shutdowns, continuing resolutions, furloughs, debt ceiling negotiations, and are still navigating this historic pandemic. These events often cause concern, but are to be expected. When we created this strategy, it was for this very reason, that events in the short term to mid-term can cause huge swings in investors' value perceptions. We have been very deliberate in our approach to provide attractive, steady growth, with a tenant credit second to none.

Turning to our third quarter performance, our Acquisitions Team completed its fifth acquisition of the year, an approximately 76,000-square-foot Federal Bureau of Investigation field office in Mobile, Alabama. Like many of our other FBI field offices, this three-story office building sits in a large multi-acre site and is enhanced by a number of security features, including, but not limited to, perimeter fencing, controlled access, a vehicle repair annex, and future plans for the construction of a visitor screening facility, which will reside on the perimeter of the property. With this acquisition, Easterly now owns 11 of the 56 FBI field offices strategically located throughout the country and remains the single largest private owner of these highly important assets.

This was a multi-year acquisition effort and I congratulate the Easterly Team for its ability to navigate a lengthy transactional process and continue to deliver for the Company and our shareholders. This effort is reflective of the high-caliber team led by Andy Pulliam and our Vice Chair Mike Ibe, who continue to ensure a robust pipeline of actionable opportunities and an exceptional ability to execute. We continue to visit assets in person, while following protocols to help ensure the safety of our team, and work with third-party providers to complete exacting due diligence and ensure smooth closings. As we approach the end of 2020, we are confident in our ability to deliver on our stated goal of $200 million in acquisitions.

Turning to development, another important milestone was achieved in the third quarter of 2020. Easterly has reached completion and commenced its new 20-year lease at the FDA laboratory in Lenexa, Kansas. Mike Ibe, Mark Bauer and team are truly talented in this niche market of the development world and were able to deliver this state-of-the-art laboratory a quarter ahead of schedule. The FDA Lenexa laboratory is now the newest regional laboratory for this highly important agency within the U.S. government. This also marks the second successful FDA redevelopment project in the Easterly portfolio, following the delivery of FDA Alameda in 2019, and preceding the anticipated delivery of FDA Atlanta in the first half of 2023.

Turning to leasing updates, our Asset Management Team has remained extremely busy working with GSA and the underlying tenant agencies to renew the lease of the courthouse in Charleston, South Carolina, as well as the SSA office in Dallas, Texas. A new 20-year lease commenced at the Charleston courthouse effective October 2020, and earned a highly attractive re-leasing spread, which we believe is customary for bullseye renewals. Similarly, the SSA facility in Dallas also renewed for a new 15-year term starting August of 2020. These renewals once again demonstrate the underlying value of these assets, as well as the strength of the Easterly Team as they successfully navigate a lengthy renewal process with the government. I congratulate the Asset Management Team on a job well done this quarter.

Finally, before handing the call over to Meghan, I want to thank all of our capital partners, new and old, for their commitment to the Easterly investment thesis. As I was recently talking with Andy Pulliam, our Head of our Acquisitions, we realized that just a little under two weeks ago, October 21 marked an important milestone for the Company. As Darrell previously mentioned, 10 years ago, on this date, our predecessor company purchased our very first building, the FBI field office in San Antonio, Texas. Ten years later, the following remains just as important as it did then, our focus on acquiring bullseye assets, our confidence in our re-leasing ability, our commitment to our U.S. government tenant, and our unparalleled understanding of how to effective own and operate a federally leased facility, and for those of you that have followed us and remain committed to our thesis, it should serve as no surprise that our investment approach has not changed in the last decade.

Thank you again for your time this morning, and with that, I will turn the call over to Meghan to discuss the quarterly financial results and provide guidance for 2020 and 2021.

Meghan Baivier

Thank you, Bill. Good morning, everyone.

It gives me great pleasure to post another strong quarter and continue demonstrating our ability to grow by once again raising our 2020 guidance and issuing strong earnings guidance for 2021. COVID-19 continues to have no material financial impact on our organization, as Easterly received 100% of rental income due from our tenants in the third quarter. Similarly, we still do not expect any material rent collection issues for the fourth quarter and beyond.

Turning to our quarterly results for the third quarter, net income per share on a fully diluted basis was $0.05, FFO per share on a fully diluted basis was $0.31, FFO as adjusted per share on a fully diluted basis was $0.30, and our cash available for distribution was $23 million.

As of September 30, we owned 76 operating properties comprising approximately 7 million square feet of commercial real estate, with one additional development project in design totaling approximately 162,000 square feet.

The weighted average age of our portfolio remains young at 13.3 years, while the weighted average remaining lease term grew since last quarter to 7.8 years.

Given the delivery of FDA Lenexa, the acquisition of young buildings and the renewal of several leases at our facilities, we have demonstrated the Company's ability to continue to generate cash flows with strong visibility for years to come.

Turning to the balance sheet, at quarter end the Company had total indebtedness of approximately $905.1 million, with a full $450 million available on our line of credit for future acquisitions and development-related expenses. As of September 30, Easterly's net debt to total enterprise value was 30.4% and its adjusted net debt to annualized quarterly pro forma EBITDA ratio was a low 5.6 times.

In the third quarter of 2020, the Company issued approximately 1.5 million shares of its common stock through the Company's ATM program at a net weighted average price of $22.72 per share, raising net proceeds for the Company of approximately $33.5 million. Approximately 951,000 new shares were from forward sales transactions entered into in prior quarters. Today, the Company has approximately 4.6 million shares which are subject to unsettled forward sales transactions under the Company's ATM program. Assuming these shares are physically settled in full at a weighted average initial forward sales price of $25.27 per share, the Company expects to receive net proceeds of approximately $116.2 million. With these unsettled forward sales, Easterly is very well poised to continue funding our acquisition and development pipeline, just-in-time, at a highly attractive cost to capital.

Turning to our earnings guidance, once again, the Company is increasing its guidance for 2020 FFO per share on a fully diluted basis to a range of $1.24 to $1.26. The midpoint of this guidance is based on the Company completing $200 million of acquisitions and $35 million to $45 million of growth development-related investment in the year, and at the midpoint represents an over 4% growth rate year-over-year. This growth, coupled with a roughly 5% dividend, we believe provides a highly attractive return to our valued investors, especially when considering the Easterly platform is built on the credit of the U.S. federal government.

The Company is also issuing 2021 FFO per share on a fully diluted basis guidance in a range of $1.28 to $1.30. The midpoint of this guidance is predicated upon completing $200 million in acquisitions and $25 million in growth development-related investment in 2021.

Easterly remains on track to deliver to 2% to 3% FFO growth per share year-over-year regardless of macro economics, global health or political uncertainty. It is our goal to remain dependable and provide a constant source of growth for our shareholders. Our strategy and the strength that is provided in today's market stands alone in the public REIT space.

We thank you for your commitment to our thesis and appreciate your partnership as we continue to deliver for you. Stay safe, everyone.

With that, I will turn the call back to Rob.

Operator

Thank you. At this time, we'll be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment while we poll for questions.

Our first question comes from Manny Korchman with Citi. Please proceed with your question.

Manny Korchman

Hey, good morning, everyone. Meghan, just as we think about next year, especially where the stock price is today, how do you think about funding, and with that, is there an opportunity to expand the existing forwards even more as you did in 3Q?

Meghan Baivier

Yes, good morning, Manny. The ATM with the forward capability really is a very strong tool for us, it works well for the just-in-time funding and the nature of our pipeline, so you can expect us to continue to use that into next year.

I'm sorry, I didn't catch the second half about—can you say that again?

Manny Korchman

In 3Q, you made those programs bigger, as you had more available proceeds on them than you had the previous quarter. Is that something that you can continue to do, or maybe I misunderstood what was happening there?

Meghan Baivier

Oh, sure, just in terms of where we sit with what we could take down. That's right, we've been—as the stock moves throughout the year, it had some strong performance relative to our sort of pandemic here. The backdrop, we obviously were very efficient raising capital north of $25, and so really like what we've got in the hopper there, but we'll continue to say probably two to three quarters ahead of ourselves. I think that's a prudent course of action.

Manny Korchman

Great, and then just down in Atlanta, could you maybe elaborate on what's causing that delay of a couple quarters in the development and completion there?

William C. Trimble

Sure, Manny. Hey, good morning, it's Bill. I hope you're well. I'll tell you one thing, with the federal government—and I've always said the federal government is a temperamental partner—we have found in every one of our other projects that the reason that things move back is because the federal government wants to put more bells and whistles in a building, which of course we're only too happy to provide, and I think you can imagine and FDA laboratory, especially with what we're seeing today, is one of the most important mission-critical assets we can possibly develop. So, we're happy if people want to do some change orders and make that an even more relevant facility. It's up to the federal government, as you know, they basically run the process, and we're only too eager to do whatever they want to do.

Manny Korchman

Great, thanks very much.

Operator

Our next question is from Michael Carroll with RBC Capital Markets. Please proceed with your question.

Michael Carroll

Yes, thanks. Bill, can you give us some color on the investment pipeline today, maybe versus six to 12 months ago? Do you expect activity will kind of pick up given the amount of equity in the forward contracts you have outstanding, or it was really those four contracts that you did just a way to be more opportunistic?

William C. Trimble

I will tell you that we have never seen more opportunities than we're seeing right now, Michael, that's an absolute certainty, and we're very pleased, and that falls across a number of different agencies, a number of different owners, a lot mined by our own team, not on market, so I think we have the prudent amount of equity that we're raising on a forward basis. It's not speculative, it's based on what we're going to accomplish. Even in this environment, I'm incredibly proud of our team to be able to get this stuff done. But, no, on track and in good shape from a pipeline standpoint.

Michael Carroll

And why is that activity stronger than it has been in years past? Is it just the uncertainty caused by the pandemic, that people are looking to monetize their assets, that they might not have been able to do that before or wanted to do that before? I guess, what's driving that activity higher?

William C. Trimble

Yes, I certainly think that would be one of the many reasons that we see. I think it's a source of funds for folks that might have a hotel under development, or other areas of real estate, that are certainly not as certain as ours, and so we're actually seeing some reach-out there. I think you're also seeing that massive VA pipeline that was created during the Obama administration, and then into the Trump administration, and will continue, a $63 billion program. There's a lot of brand new 15- and 20-year mission-critical facilities that are being developed, and I think that's going to be out there for quite some time, as well. So, I think there's a combination, but I think the wind seems to be at our back right now.

Michael Carroll

Okay, great, and then just last question. On the FDA Atlanta property, is there any updates on the expected lump sum, and when will those flow in through numbers, or are we still waiting for the GSA to kind of finalize those plans?

Meghan Baivier

Yes, we're still waiting for the GSA to complete design for us to be able to give a stronger estimate of what that total cost would be, but we are looking for that lump sum budget in around $100 million.

Michael Carroll

Okay, great. Thank you.

Operator

Our next question is from Michael Lewis with Truist Securities. Please proceed with your question.

Michael Lewis

Great, thank you. I apologize if you already touched on this, but the G&A was the lowest you had, I think, since 1Q '19, almost about $1 million lower than it had been running over the past four quarters. Was there anything specific to this quarter, and could you speak to kind of the run rate going forward?

Meghan Baivier

Hey, Michael, good morning. You're right. You're picking up on just some seasonality with a very nice professional services expense decline this quarter. So, nothing out of the norm, just the combination of those two coming through.

Michael Lewis

Okay. So, probably a run rate a little higher, more like what we've seen in the last few quarters, if we're going to estimate for next year?

Meghan Baivier

Yes, that's right.

Michael Lewis

Okay, and then—somebody had to ask about the election, I guess. I won't ask you who's going to win, but I'll ask you—I see the DEA has about five years of average lese term left. That's 10% of annual rent. I said about five years left. Average term, that's about 30%. I mean, do you have any concern at all that these, or any other agencies, could be downsized, or anything else, particularly in the event of a democratic sweep, where they've talked about some of these agencies?

William C. Trimble

No, I think DEA is something that both parties are pretty much in agreement with. You know, what's going on with the opioid crisis. I don't know who's going to jump to prosecute people quicker in that area. So, I think that that's a new world that we've been in, sadly, for quite some time and I think both parties are pretty aligned and very eager to make sure we lessen the drug problem. We have other facilities in almost every agency, but we went through every mission and hierarchy of mission in all the agencies, and we're very pleased, very pleased with our portfolio and how it's positioned. But, it shouldn't be a surprise. That's where our mantra was to begin with, to stay out of politics. Don't forget, we've lived eight years with one of the candidates as Vice President and we've just lived four years with the other one as President, and we've thrived under both scenarios.

Michael Lewis

That's great, and then last one for me, kind of a bigger picture question. I think it was on your 2Q '18 call, Darrell said he expected the dividend to be at least $0.30 a share by the end of 2020, so I made a note of it in model, and now that we're here, I'll ask about it. I think it's been obvious for a while that you weren't going to hit that mark, but maybe just give us a little sense of what happened, why you haven't been able to raise the dividend at all since then, and kind of what your expectations for the dividend are going forward over whatever period you're comfortable talking about?

Darrell W. Crate

Hey, Michael, it's Darrell, I'll speak to it. Our development pipeline, while it continues to grow and is robust, has probably taken a little bit longer to harvest than we imagined, but as we look forward, if you look at the run rate that underlies those buildings in our portfolio, we feel very confident about our cash flows and our cash flow growth. We've also done a very good job of de-levering our balance sheet and, again, positioning the business so that we have some extra pennies stored away, with some extra leverage that we could put on the business to get back to normal rates as we transition over the next year or two. So, again, we feel very good about the consistent growth. As we've laid out, we look to this FFO growth being kind of 2% steady, and as we move to our renewals and get existing buildings online, over time, we could imagine seeing those dividend increases.

Michael Lewis

Great, and then maybe I'll just ask one more about the attractiveness, the development versus acquisitions. The development, you get a nice feel, but adds a little lumpiness to the story, which you just kind of described. Now that Lenexa is done, you've got your Atlanta one, which is a bigger project, how do you think about backfilling the development pipeline versus spending that money elsewhere, mainly on acquisitions?

Darrell W. Crate

I would say that development continues to be a very accretive place for us to put our capital. As we've said all along, we're not trying to be the biggest REIT in the world, we're not trying to devour every jack-in-the-box that we can find. We're picking—if anything, as we look over these last couple of years, and as we were talking before the call, the quality of the buildings that we are bringing into the portfolio has never been stronger, and the quality of the cash flow, the stability it can deliver, is what we're trying to bring to shareholders. It's our most differentiating characteristic, is the full faith and credit of the U.S. government. As I said, with low volatility cash flows and outperforming the Russell 1000, we think that this is an anchor to windward for both equity managers and folks who are also managing REIT securities. So, as we look forward, you know, husbanding our dollars, putting them to work in development in these very high-quality new buildings, we'll serve our shareholders incredibly well.

I'll just highlight one other point, which is, as we look at our existing leases and as they roll, we have $4.3 billion of cash that's ahead of us, all guaranteed by the federal government. That is true. I mean, I remember when we first met that number was just over $1 billion, and we've continued to find higher quality buildings that continue to compound, and, again, can forecast the consistency of those curves well into the future.

Michael Lewis

Great, thanks a lot.

Operator

Our next question is from Peter Abramowitz with Jefferies. Please proceed with your question.

Peter Abramowitz

Hi, thank you. I just wanted to ask about the acquisition market. Are you seeing any kind of change in terms of any more or less competition for the bullseye assets you're looking at really recently versus the last six or 12 months, and is there any impact from that on pricing either way?

William C. Trimble

Good morning. We really haven't seen any new competitors come into the market, it's the same usual players, and it's certainly gratifying to have the lowest cost of capital in that competition. Really, no public competitors at all that we're dealing with, and that's sort of been the same thing since we were in our private equity days. So, no, we really haven't seen anybody, especially in those bullseye properties.

Peter Abramowitz

Okay, got it. Then, just looking at the guidance, I think If you look at sort of the implied guidance, $0.31 to $0.33 in the fourth quarter, so either at the midpoint or the high end would be 3% to 6.5% over what you had this quarter. So, anything underlying that, that we should be aware of, that kind of would have you reaching sort of going up a penny or the high end of two pennies?

Meghan Baivier

Sure. Yes, when you think about what's changing in the fourth quarter relative to the third quarter, you've got Lenexa coming online earlier than we anticipated, by about a month, and performance there is really looking quite strong, and then, obviously, we've got a $200 million target in acquisitions through the year, and that leaves $50 million for completion. That's a pretty strong number to hit all in one quarter, relative to where we were run rating this quarter. So, both of those hitting fourth quarter will be the driver of that.

Peter Abramowitz

Got it. That's it for me. Thank you.

Operator

Our next question is from Bill Crow with Raymond James. Please proceed with your question.

Bill Crow

Yes, thanks. Good morning, folks. I have two questions. On the acquisition front, again, you talked about no new competition. I'm just wondering why that might be. Because, it seems like success kind of brings more competition, and you've delivered on the success part of it, so why aren't we seeing more capital earmarked to your sector?

William C. Trimble

Well, I think, you know, with the public markets, obviously, there's only so much room out there and we'd be well—we'd all know that was coming, if somebody went public, and we don't anticipate anybody doing that. On the private sector, I think several reasons. Our cost of capital is only becoming more attractive every day, and I think that our ability not only to harness our partners in the debt and the equity markets is a tough competitor for some of these private equity funds. I'd also say that our knowledge of the space, all the work we've done since 2009, puts us well ahead of anybody that wants to get into this space. I think it's easier, if somebody wants to invest—we've seen a lot of international interest of recent—just to go ahead and buy DEA, than to go out and start a new private equity fund. So, I think that's the reason.

Finally, I mean, I don't need to tell you, the government is an interesting—a wonderful partner, but very interesting to deal with, and, obviously, we have set up an organization that has an incredible team, whether it's Ron Kendall in our Government Affairs or Nick Nimerala in our Asset Management Group, and keep going down the list, but these people are really dedicated and experienced within this particular sector and it would be very hard for somebody to get that kind of talent at a dead standstill.

Bill Crow

Yes, fair enough, thank you. The other question—again, I've covered you for a long time, so I think I know the story, but within other parts of office, we're certainly seeing a lot of pain related to work-from-home and the economic downturn, and job losses, and things like that. I don't anticipate, obviously, any impact on your tenant base from that, but as market rents around the country come under pressure, does that take any ability of yours to push rents and renewals off the table, or it's just you're in such unique markets that it's just not relevant?

William C. Trimble

I'll start and I'll let Meghan finish. I think, yes—and, Bill, you certainly do understand our story, it has been a long time. I'm aging myself. But, in any case, certainly, with the bullseye properties—the first thing I'd say is I don't know how we all got shoved into office to begin with, we really are our own asset class, and

I think Darrell explained that beautifully in his intro. You can't go out and do IRS work from your home, you can't take the records out, you can't prosecute, the FBI can't do that from their living room, so there's a whole bunch of reasons that this footprint is completely necessary, including the laboratories, and everything else.

I'll say, with a small minority part of our portfolio, which we call more of the plain vanilla, which is based more on market rent, I'm very pleased to report that we've basically renewed most of those for very long-term lease terms going forward, and so I don't really see any issues there, and I think our timing was lucky, but was also good, when you consider some of those properties that'll be there for quite some time.

Meghan?

Meghan Baivier

Yes, with regards to replacement cost, obviously, the financing costs, etc., can, and likely will, on regular office rents puts some pressure on utilization, as well, but remember, when we approach a renewal of one of our assets, we're not moving right up to what we believe replacement cost is, we're able to renew with these attractive spreads, and be the best alternative to the replacement cost. So, we've got some natural built-in cushion there that we expect, and are continuing to see buffer our renewal process.

Bill Crow

All right, thank you both. Congratulations.

William C. Trimble

Thank you.

Meghan Baivier

Thanks, Bill.

Operator

Our next question is from Merrill Ross with Compass Point. Please proceed with your question.

Merrill Ross

Thank you, and good morning. I see in the renewals for 2021, there are four buildings that are 20 years old, that are clearly described as bullseye. One's a DEA lab in Dallas—actually, three are to the DEA and one is to the FBI. Do you have a preliminary view, or have you any conversations, that would allow us to estimate the renewal at replacement cost after 20 years for those buildings, or TIs that might be requested by the tenant?

William C. Trimble

Well, I'll start and Meghan can fill you in further—and good morning. When you look at our laboratory in Dallas, that probably would fall within the most sophisticated facilities that we have, and our team just constructed the most recent DEA laboratory in Pleasanton, California, in the Bay Area, which models our Dallas laboratory. I mean, they're very much the same. The price on a new one of those facilities is so astronomical—well, I'm not going to say that, if our government friends are on here, but a very expensive facility, that I think we have plenty of room, obviously, to not only get very substantial rent increases in that building, but still be a very attractive option for our government partners, compared to building something new, because, basically, if you travel to both the new one and the Dallas, as well as if you take our Vista out in California, those laboratories are almost identical.

Meghan?

Meghan Baivier

Yes, Merrill, we're always going to be careful in terms of commenting on in-practice renewals, everything that's up for renewal year or next year is in process, if it hasn't already been completed, but look forward to sharing with you the outcomes as they progress. Our target of high-teens to low-20s, we have expected that to come with, on average, about $25 a foot. That will range from zero to $50, depending upon a particular asset, but that is the zip code that we have performed within—in fact, a little bit light to that, but where we expect renewals to be next year and this year.

Merrill Ross

Thank you.

Operator

As a reminder, if you'd like to ask a question, please press star, one on your telephone keypad. One moment, please, while we poll for questions.

Our next question is from Manny Korchman with Citi. Please proceed with your question.

Michael

Hi, it's Michael filling in here with Manny. Good morning. Darrell, I wanted to come back to sort of growth and cash flow, and congratulations on the 10-year anniversary from buying that original FBI building, but I guess, if we just take a shorter time period, let's look at the last five years, 2016 to today, your core earnings and cash flow is flat, relatively flattish, your growth assets have increased 3x. Now, you've de-levered over that time, your equity base has grown 4x, but it hasn't translated yet into strong earnings per cash flow growth. I know you and I, over years, have had discussions about what's on the come. The dividend's been flat for the last three years. So, can you just sort of step back a little bit and if you're able to project forward, let's say, the next five years, how should investors think about cash flow growth, dividend growth at the expense of just total equity and asset growth?

Darrell W. Crate

Yes, Michael, I think it's a great question. As we have tried to communicate, and I really appreciate the opportunity for us to share, we're not intending to be sort of a volatile, you know, grow a lot, shrink a lot REIT. Our strategy is to be the stable table, real estate with no drama, and what that means is, again, it starts with full faith and credit of the U.S. government and, as we've said, grow our FFO 2% to 3% a year, and as we look at sort of '18 to '19, '19 to '20, we've sort of grown it a little over 3%. We are de-levering the balance sheet, which, as you guys know, adds one, two, three, four pennies of potential earnings growth into what would be capable if we wanted to run it hot, and the choice that we've made, and what we've heard, again, from investors, is if we can deliver this consistent growth of 2% to 3%, plus a dividend that's 4% to 5%, that should deliver to investors a very attractive opportunity. Again, when we look at the Russell 1000 and we look at our cash flows, and we look at what we deliver, again, our intent is to be stability in anyone's portfolio. I mean, I think that's the trajectory. You draw a line that is 2.5% out for the next five years and as we get development and bring it online, the dividend should move in line with that sort of growth.

Michael

But shouldn't you be able to generate much—I mean, just given the amount of capital you're putting out and the spread on that capital, and then also the embedded leases that you have, you really should be able to put forth a lot better growth than a very, very low-single-digit growth platform.

Darrell W. Crate

I mean, I look at the—we have one building PTO, that if you notice, it's a long-term lease. We've got a free rent that's going to burn off here pretty soon. So, that's certainly going to lead to more cash flow generation. I mean, if you look at the spread that we're generating relative to what 10-year treasuries are yielding, I think it's very, very attractive. We're not in the super Ferrari part of real estate. We're taking the stability of government cash flows and we're delivering a healthy premium to investors. That's where we're sort of setting expectations. Again, privately, we're happy to hear any ideas on how we should be managing the business or where we should take things, or how you think that we could deliver a little more growth to shareholders.

Michael

Yes, but looking back the last three years, I don't think the intent was to have a $0.26 quarterly dividend. It just seems that there's something not connecting between all the dots, and I'm not doubting—your business is a great business, it's an attractive business. It just doesn't seem to be flowing into your results as much and I'm trying to figure out where there's a mismatch between what you're talking about and ultimately the results.

Darrell W. Crate

No, it's a great question and I really appreciate it. I mean, again, PTO has probably been the biggest cash drag. For folks who may not be familiar, that was a building that was close to Washington D.C., the Patent Trade Office, it's got some dark fiber to their headquarters, and when we originally purchased the building the commercial rates were actually in excess of what we were getting paid on our leases, and those sub-markets in Washington—sadly, it came up for release before Amazon had decided that they're going to move to Washington, and that led to us having to—there was another building that was a competitor and instead of jeopardizing and needing to stabilize the building, we ended up not having the revenue growth that we anticipated and we gave away significant free rent. I think that's driven the dividend, sort of lack of us being more conservative with how we've put the dividend forward, and as you know, these development projects that we're moving forward with the FDA lab are very lucrative, and so I think the dividend will catch up to some of this growth, but, again, where we have tried to be very clear is the ability to deliver this FFO growth based on a very stable set of cash flows.

Michael

Then, just in terms of match funding from here, just outline—do you feel that at this point you're at your sort of targeted leverage or do you feel you're a little bit below. Just to think about if you had, you know, $250 million of external growth, how investors should think about programming equity versus debt?

Darrell W. Crate

Look, I would say we'll be opportunistic in the market, and Meghan's done a terrific job of raising significant proceeds, so as we look out, we have very attractive equity that we can put to work, and I would say continuing to de-lever a little bit is a prudent thing to do. As long as we can deliver that growth—I mean, I think if we can emerge from this pandemic with investors understanding that we're going to deliver 2% to 3% FFO grow consistently, as we look out over a five-year term, and that we've taken the balance sheet to a place where we have one turn or more of additional leverage that we could put to work, so that we could do a year's worth of acquisitions, for example, without raising any equity, that's going to be very powerful as it comes in.

As an early public company, as you know, you start out with maximizing the ability, you know, maximizing your earnings and fighting your G&A, and making sure that you can continue to go from sub-scale to a scale business. We certainly accomplished that, and now, as we look at our portfolio, our ability to deliver what should be differentiated stable earnings, while also doing that at a pace that's not putting a lot of pressure on our ability to raise capital, or requiring us to have to sort of defend high levels of leverage, I think is putting us in a very good spot as we look out over the next, again, five years to deliver very consistent growth and exceed expectations for investors.

Michael

Okay, thank you.

Darrell W. Crate

Thanks so much.

Operator

Ladies and gentlemen, we've reached the end of the question-and-answer session. At this time, I'd like to turn the call back over to Darrell Crate for closing remarks.

Darrell W. Crate

Well, thank you, everyone, thanks for joining the Easterly Government Properties Third Quarter 2020 Conference Call. We look forward to continuing, again, to deliver stability and growth to shareholders, and we appreciate you joining the call today.

Operator

This concludes today's conference, you may disconnect your lines at this time, and we thank you for your participation.