Management's Prepared Remarks
Second Quarter 2018 Conference Call
July 25, 2018

Brendan Maiorana
Senior Vice President, Finance and Investor Relations
If any of you have not received yesterday's earnings release or supplemental, they're both available on the investors section of our website at highwoods.com. On today's call, our review will include non-GAAP measures, such as FFO, NOI and EBITDA*re*. The release and supplemental include a reconciliation of these non-GAAP measures to the most directly comparable GAAP financial measures.

Forward-looking statements made during today's call are subject to risks and uncertainties, which are discussed at length in our press releases as well as our SEC filings. As you know, actual events and results can differ materially from these forward-looking statements. The Company does not undertake a duty to update any forward-looking statements.

Ed Fritsch
President, Chief Executive Officer
Macro-economic conditions remain healthy nationally and across our southeastern footprint. Employment gains, including office-using jobs, have been strong across the country and generally even better in our markets. GDP growth has accelerated of late, and many economists expect 2Q'18 to be a break-out quarter from the steady, yet somewhat modest growth experienced most of this cycle.

We continue to see healthy demand for our well-located BBD office product from current customers and prospects. During the past few years we've often been asked our opinion on "*what inning are we in?*" or *"how long will this cycle last?"* As we've stated before, we'll leave these predictions on the length of the cycle to others, but for now, the steady cadence of positive economic activity supports business growth from our customers and prospects.

The main drivers supporting our upbeat outlook include:

- Southeast population and job growth, which are significantly outpacing the national average supported by business friendly environments, high quality of life and affordability.
- Our markets continue to experience positive net absorption.
- On average, new supply remains modest.
- And finally, rents continue to rise.

This healthy macro-economic outlook and strong demographic drivers across our footprint helped drive strong leasing during the quarter and support a positive outlook for our operations.

In addition to delivering 87 cents of FFO per share, we leased over 1.1 million square feet of second generation office space, including 189,000 square feet of re-lets and approximately 100,000 square feet of expansions. In addition to this solid volume, our leasing metrics were strong. We posted GAAP rent growth of 18.2%, while cash rent spreads have remained healthy, including this quarter's positive 2.3% growth. Further, we were successful generating longer term leases, at a weighted average of 6.8 years, and we posted healthy net effective rents averaging $15.24 per square foot. Our strong leasing performance of late, with help from portfolio recycling, has resulted in cash rents that are 4.1% higher per square foot compared to a year ago.

As expected, portfolio occupancy dropped in the quarter compared to the end of 1Q, ending 2Q at 91.8%. As we've discussed previously, we expect occupancy to bottom in 3Q and rebound by year-end.

The robust leasing volume in the second quarter largely addressed future lease expirations. In our latest At-A-Glance, we listed our five 2019 expirations for leases greater than 100,000 square feet. We've made excellent progress on four of the five.

- We sold Highwoods Tower Two where INC is located in Raleigh,
- We renewed UMA for their 150,000 square feet in Tampa,
- Subsequent to quarter-end, we renewed AT&T's lease for 105,000 square feet in Raleigh, and
- We continue to expect a renewal with the FAA in Atlanta, supported by the building originally being a build-to-suit for them and its proximity to Hartsfield International Airport.

Furthermore, we're seeing strong interest in our portfolio in Buckhead, including backfilling 55% of the former Towers Watson space at One Alliance and strong showings at Monarch. And, in Richmond, where we have already backfilled 77% of SCI's 163,000 square feet, we have a lease out for signature for the remainder of the space.

We continue to have success with our development pipeline. Our 2.0 million square foot, $725 million pipeline is a stout 92% pre-leased on a dollar weighted basis.

On Monday of this week, we announced we have a fully executed agreement with Asurion for a 551,000 square foot, $285 million headquarters building that is 98.3% pre-leased. The project size grew from our soft announcement earlier this year of 479,000 square feet and $252 million. As you'll recall, this development will be on a parcel we acquired early this year, and we own a neighboring development parcel where we can develop another 700,000 square feet. We're pleased to put this significant land investment into production so soon after acquisition. This project is a big win. I congratulate our entire team on their vision and hard work, I thank our new customer and we are thrilled to welcome Asurion to our stable of large corporate clients and look forward to a long-term, mutually beneficial relationship.

We also made strong leasing progress on the remainder of the development pipeline since our last earnings call. We signed leases for 100,000 square feet of the pipeline, which equates to one-third of our previously available space. We've seen strong interest in our development properties in Raleigh. 5000 CentreGreen, which we started completely spec, is now 87% leased and we have solid prospects to bring this project to the mid 90s%. As a reminder, we're still more than a year from our projected stabilization date. At 751 Corporate Center, also in Raleigh and which we started 35% pre-leased, we're now 89% leased, and have strong prospects to also bring us to the mid 90's% while still 2+ years from our pro forma stabilization date. In Nashville, at Virginia Springs I, which we started 34% pre-leased, we have an LOI with a customer that will bring this project to 100% pre-leased, more than 2 years ahead of pro forma stabilization.

Finally, our in-process build-to-suit projects, namely

- Virginia Urology in Richmond will deliver next month on schedule
- MetLife III in Raleigh is on schedule for delivery in the second quarter of 2019, and
- Mars Petcare headquarters in Nashville is tracking nicely to deliver on time in the third quarter of 2019.

Some uncertainty has arisen regarding the potential impact of the widely discussed tariffs on steel and aluminum. As you would expect, we pay careful attention to construction costs and see pricing real-time from our many projects. Construction costs continue to rise at approximately ½ a percent per month, very much in line with the zip code we've been experiencing and expressing the past few years. The more dominant driver recently has been the cost of labor, both skilled and unskilled, while material prices have played a lesser role. Unfortunately, tariff chatter alone is beginning to impact the price of metal goods. Thus far the overall cost effect has been very nominal. While the potential exists for tariffs to become more impactful, we don't anticipate them to be a huge disrupter.

As you know, we are largely insulated from cost increases on our current development pipeline since most of our build-to-suit projects are open-book, and we have GMP contracts in-place for our other developments. During the past several years, demand from users has remained strong despite experiencing higher first generation rents due to escalating construction costs. This sustained interest gives us confidence that the depth of demand should remain attractive as construction costs and rents continue to increase. Of course we will continue to carefully monitor market dynamics as we evaluate future development opportunities.

We've raised the low-end of our outlook for development announcements from $100 to $285 million, which we're at today with the Asurion build-to-suit, and we have raised the high-end from $350 to $385 million to reflect another $100 million of potential announcements. Any additional development announcements this year are likely to be more typical-sized projects of around $50 million. Development continues to be a core competency for us and an ongoing engine of strengthening cash flow and earnings growth.

Turning to dispositions, as previously forecasted, we sold Highwoods Tower Two in Raleigh for $31 million, including an adjacent 2-acre parcel of land. We also sold 25 acres of non-core industrial land in the Atlanta area for $3 million. Our disposition outlook remains $61 to $136 million. We've prepared a number of non-core properties for disposition, and as usual we expect to be regular sellers of non-core properties going forward.

We've kept our acquisition outlook unchanged at $0 to $200 million, as there aren't a lot of institutional quality assets available. For the few assets that we've seen in the market, pricing for BBD located Class A office properties remains highly competitive with initial cap rates carrying a 5-handle. We continue to evaluate on and off-market opportunities with a focus on prudent investing, but at this point in the year, the low-end of our outlook range seems likely.

In summary, strong leasing activity in our operating portfolio and continued crisp execution across our development program, combined with carefully managed operating expenses and a strong balance sheet, sets the table for growth in our earnings, cash flow, and NAV over the next several years.

Ted Klinck
Executive Vice President, Chief Operating and Investment Officer
Overall, the demand we're seeing across the portfolio makes us upbeat about our leasing prospects for the next several quarters. As Ed mentioned, we've taken care of several large expirations from our 2019 list and we renewed a large 2020 expiration. Out of the five 2019 expirations greater than 100,000 square feet, we have now renewed two of them, UMA and AT&T, and in addition closed the sale of Tower Two where INC is located. Further, we feel confident about landing a renewal with the FAA, especially given the building's proximity to the Atlanta airport. At this juncture, T-Mobile is the only large 2019 expiration that we're unsure about – we expect to get a better sense about their renewal likelihood by year-end. In addition to shoring up many of our large future expirations, we also made meaningful progress elsewhere in our portfolio that we believe will materialize into signed leases in the latter half of the year.

Now turning to our quarterly stats. We beat our prior five quarter average on several fronts. We leased over 1.1 million square feet of second gen office space, a 30% beat. The average dollar weighted term was 6.8 years compared to 6.0 years. GAAP rent spreads were positive 18.2%, 230 basis points higher and net effective rents were $15.24 per square foot, or 2.2% better. Our 2Q same property cash NOI growth was negative 1.1% as same property average occupancy was down 140 basis points compared to last year. Of note, rent in our same property pool was flat even though occupancy was down, driven by solid cash rent spreads we've achieved over the past many quarters and the healthy annually compounding rent bumps we have on nearly all of our leases. Occupancy is projected to bottom in 3Q as we've now gotten back 178,000 square feet from Fidelity in Raleigh. As a reminder, we're getting full economics from Fidelity through their original November expiration date.

Now to our markets.

Atlanta's Class A asking rates have increased 4.2% year-over-year, as reported by CBRE. There is currently 1.4 million square feet of office under construction, or approximately 1% of stock, none of which is located in Buckhead, where interest has picked up substantially since our last earnings call. Our nearly 2 million square foot Buckhead portfolio was 83.3% occupied at the end of 2Q, equating to more than 300,000 square feet of occupancy upside. Already in Q3, we signed a lease for 42,000 square feet and expect to sign additional leases totaling a similar amount before our next call.

Turning to Raleigh, the market ranks 1st in the Southeast for projected population growth according to CBRE's 2018 Southeast US Economy Outlook. Population growth is expected to be 10.3% over the next 5 years, more than twice the national projection of 4.2%. The positive economic and demographic trends are translating into increasing office employment, which grew 2.2% year-over-year, 80 basis points higher than the national average. Fundamentals remain strong in Raleigh. The second quarter was the sixth consecutive quarter with positive net absorption of at least 500,000 square feet, as reported by CBRE. Class A asking rates increased 2.5% year-over-year. While there is 2.7 million square feet under construction, based on the strong net absorption, new supply is meeting market demand. Out of the total new supply, 1.6 million square feet is competitive to our BBD-located product and is approximately three quarters pre-leased. We signed 171,000 square feet of second generation leases during the second quarter, which was approximately double the prior 5 quarter average. GAAP rent spreads were strong at positive 28.1%. As I mentioned earlier, while Fidelity is paying their full economics on the lease of 11000 Weston through November, we already regained possession of the space and there is a hub of activity Highwoodtizing the building. We are optimistic about backfilling this space given the tightness in the submarket. At the end of 2Q, our 1.2 million square foot in-service Weston portfolio was 96.7% occupied and the Class A vacancy in the submarket was 7.7%.

Nashville's unemployment rate remained unchanged from 1Q at 2.6%. Office employment grew 3.1% year-over-year versus the national average of 1.4%. According to Cushman and Wakefield, the market posted positive net absorption for the fifth consecutive quarter, registering 158,000 square feet in 2Q. There is currently 1.8 million square feet under construction set to deliver over the next two years. New supply equates to 4.8% of total stock, which based on Nashville's strong demand trends, we'd expect to be absorbed with little impact on market vacancy. Our Nashville portfolio was 94.4% occupied at the end of 2Q. We signed 95,000 square feet of second gen leases with GAAP spreads of positive 20%.

Lastly, Tampa's office employment grew 1.6% year-over-year, 20 basis points above the national average. Net absorption, as reported by JLL, was negative 52,000 square feet for the quarter, but year-to-date is a positive 217,000. Class A vacancy was 9.0% and asking rents increased approximately 8% since last year. We signed 396,000 square feet of second gen leases, largely comprised of two sizable renewals. First is the renewal of UMA's 153,000 square feet. We're thrilled they renewed their long-term commitment to Tampa Bay Park. The second was a 103,000 square foot long-term blend and extend of a lease previously set to expire in 2020. Tampa's signed deals during the quarter had a weighted average term of 8.6 years and GAAP rent growth was 15.0%. Our Tampa portfolio was 92.8% occupied at the end of 2Q.

In conclusion, we had a strong quarter of leasing and prospect activity, and based on what we're seeing we expect this to continue.

Mark Mulhern
Executive Vice President, Chief Financial Officer
We delivered net income of $50.7 million, or 49 cents per share, and FFO of $92.2 million, or 87 cents per share. The quarter included half a penny of land sale gains, which were essentially offset by dead-deal costs related to development projects we are no longer pursuing. There were no meaningful term fees in the quarter, but as I mentioned last quarter, we did recognize the final $1.9 million portion of the Fidelity restoration fee. Compared to the first quarter, the sequential drivers of the nearly $1.5 million FFO increase were:

- Lower G&A by a little over $2 million. As you'll recall, this is the normal annual pattern for us as we have increased expense in 1Q from long-term equity grants each year; and
- Modestly lower interest expense due to repayment of a $200 million bond with an interest rate of 7.5%.

These were partially offset by:

- Lower NOI by $1.9 million, driven by lower average occupancy, lower term fees and modestly higher operating expenses.

With net debt-to-EBITDAre of 4.65 turns and leverage of 35.3%, our balance sheet remains in excellent shape. Our strong leverage metrics put us towards the lower end of our stated comfort range of 4.5 to 5.5x net debt-to-EBITDAre and we have significant liquidity to fund our growth initiatives. With the addition of the Asurion Headquarters build-to-suit to our development pipeline, we now have $368 million left to fund on our $725 million pipeline. We continue our plan to fund our business on a leverage neutral basis. However, even if we were to fund the remainder of the development pipeline without any ATM issuance or non-core dispositions, we estimate upon stabilization of the development pipeline our net-debt to EBITDAre would rise only half a turn from current levels.

During the quarter, we obtained $150 million of forward starting swaps that lock the underlying 10-year treasury at 2.905% in advance of a potential financing before July 2019. While we don't have any meaningful debt maturities before June 2020, the LIBOR hedge on our $225 million term loan expires in early 2019.

We tightened our 2018 FFO outlook to $3.39 to $3.45 per share, keeping the midpoint at $3.42 per share. As you know, we don't include the impact of any future acquisitions or dispositions in our FFO outlook, however, as Ed mentioned we kept our outlook unchanged for acquisitions and dispositions.

We kept our same property NOI growth outlook for the full year at +1.0% to +2.0%. For the first half of the year we're at +0.8%, inclusive of this quarter's negative 1.1%. While it's still early and there are several moving pieces in our outlook range, we're trending towards the low-end. This is primarily due to several 2019 renewals signed even earlier than we hoped that have a free rent component which burns off this year and obviously was not included in our original 2018 outlook, plus modestly higher property taxes.

Before we take your questions, a few other items to note:

- First, as you know, our third quarter tends to be our lowest margin quarter of the year due to the seasonality of operating expenses.
- Second, as forecasted we expect occupancy will bottom out in the third quarter due to the impact of known vacancies, and then trend upward by year-end.
- Third, for modeling purposes, at the mid-point of our outlook, we expect FFO to also bottom in the third quarter before anticipated improvement in the fourth quarter. Of note, we recognized the final $1.9 million of the Fidelity restoration fee in 2Q. In 3Q, we will recognize two extra months of rent from Fidelity, which includes its payment of the originally scheduled rent under

its lease that would otherwise run through November. These unusual items relating to Fidelity's departure end after the third quarter, creating a "clean" run-rate from the Fidelity building (aka 11000 Weston) in 4Q.

- Finally, as we have signaled for the past few years, our free cash flow continues to strengthen with the delivery of our well pre-leased development pipeline and consistent performance of our same store portfolio. While timing will impact our cash flow in any given quarter or year, we feel very good about the long-term cash flow trajectory for the company.