EDITED TRANSCRIPT

Agree Realty Corporation's
Third Quarter 2022 Earnings Conference Call
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PRESENTATION

Operator

Good morning, and welcome to the Agree Realty Corporation's Third Quarter 2022 Conference Call. (Operator Instructions). After today's presentation, there will be an opportunity to ask questions. (Operator Instructions). Please note, this event is being recorded.

I would now like to turn the call over to Reuben Treatman, Director of Corporate Finance. Please go ahead, Reuben.

Reuben Treatman | Agree Realty Corporation **|** Director, Corporate Finance

Thank you. Good morning everyone and thank you for joining us for Agree Realty's Third Quarter 2022 Earnings Call. Before turning the call over to Joey and Peter to discuss our results for the quarter, let me first run through the cautionary language.

Please note that during this call, we will make certain statements that may be considered forward-looking under federal securities law. Our actual results may differ significantly from the matters discussed in any forward-looking statements for a number of reasons. Please see yesterday's earnings release and our SEC filings, including our latest Annual Report on Form 10-K, for a discussion of various risks and uncertainties underlying our forward-looking statements.

In addition, we discuss non-GAAP financial measures, including core funds from operations or core FFO, adjusted funds from operations or AFFO, and net debt to recurring EBITDA. Reconciliations of these non-GAAP financial measures to the most directly comparable GAAP measures can be found in our earnings release, website and SEC filings.

I'll now turn the call over to Joey.

Joey Agree | Agree Realty Corporation | President & CEO
Thank you, Reuben. Good morning everyone and thank you for joining us.

Before running through our standard update, I'd like to take a step back to provide some observations on the current state of the market as well as the steps that we've taken to further strengthen our positioning in a challenging macro environment.

Our recent capital markets transactions have bolstered our balance sheet with attractively priced capital. At quarter end our fortress balance sheet stood at approximately 3.1 times pro forma net debt to EBITDA, providing tremendous flexibility and enabling us to opportunistically execute as buyers and sellers continue to adjust to the market.

Cap rates are creeping higher, most significantly in the merchant builder space, and provided us opportunities to take advantage of distressed situations. We have seen the levered buyer and a number of institutionally capitalized investors exit the market altogether or move significantly up the risk curve to drive incremental yield.

As the bid/ask spread continues to narrow and more sellers capitulate, our focus will remain on the strongest retailers in the country with the balance sheets to execute their omni-channel strategy in a challenging retail environment. We will not go up the risk curve in terms of tenant credit profile, single purpose assets, or private equity sponsored sale-leasebacks.

Our working assumption is that attractively priced long-term debt does not return to the market for the foreseeable future. Hence, we are focused on unlevered returns on equity. We are very fortunate to have the balance sheet and cost of capital to still drive incremental spreads without leverage. Our focus continues to remain on per share AFFO growth while preserving the dry powder to execute on distress.

I remind all investors, that our company has thrived in times of economic uncertainty. We launched our acquisition platform after the great financial crisis and nearly doubled the size of our company during Covid. Candidly, I think the market has been ready for a reset for a while now, and I am confident that our team is ready to once again seize on the opportunities that will be forthcoming.

Moving on to our third quarter activities…we selectively invested approximately $372 million in 121 properties across our three external growth platforms. 98 of these properties originated through our acquisition platform, representing volume of more than $360 million. The properties acquired during the quarter are leased to 39 tenants, including best in class operators in the dollar store, auto parts, farm and rural supply, grocery, home improvement, consumer electronics, and off-price sectors.

The acquired properties had a weighted-average cap rate of 6.2% and a year-to-date record weighted-average lease term of 11.1 years. Nearly 73% of the acquired properties were leased to investment grade operators.

Throughout the first nine months of the year, we've invested a record $1.2 billion in 328 retail net lease properties spanning 42 states. Over two thirds of the annualized base rent acquired is derived from leading investment grade retailers. These metrics demonstrate our continued focus on leveraging all three external growth platforms to execute on opportunities with best-in-class operators.

Given the increased visibility into our high-quality pipeline, we are increasing the bottom end of our acquisition guidance to $1.6 billion while maintaining the high end of our guidance at $1.7 billion. That said, we will remain prudent and disciplined in how we deploy capital.

Our investment activities were supported by almost $815 million of equity and debt raised during the quarter that fortified our balance sheet. At 9/30, we had over $630 million of forward equity and cash on the balance sheet, with no outstanding balance on our revolving credit facility.

Moving on to our development and Partner Capital Solutions platforms, our team continues to uncover compelling opportunities, helping to build the company's largest ever development pipeline. Our platform is uniquely situated to provide struggling merchant developers with the ability to lock in funding, while providing us with additional opportunities to drive superior risk-adjusted returns. We continue to have dialogue with many of our retail partners to find solutions that fit their store growth strategies.

During the quarter, we commenced two new development and PCS projects including one Gerber Collision location in Murrieta, California as well as a Sunbelt Rentals in Wentzville, Missouri.

We also completed the development of the two Gerber Collision locations as well as a Burlington. Construction continued on 18 additional projects. In total, we had a record 25 projects either completed or under construction during the first nine months of the year, representing approximately $82 million of committed capital.

Moving on to dispositions, we sold our Gardner White Furniture store in Canton, Michigan for approximately $20 million during the quarter.

As noted on previous calls, this was the Art Van flagship we developed prior to the company's acquisition by TH Lee, which was subsequently re-leased to Loves Furniture and then most recently to Gardner White. During the time we owned the asset, we were able to re-lease this property twice, recapturing effectively 100% of rent without tenant improvement dollars. So... now three tenants and a pandemic later, we are ultimately selling the asset at an IRR of approximately 10%, which demonstrates our bottoms up approach to real estate underwriting.

Through September 30th, we've sold 6 properties for gross proceeds of nearly $45 million with a weighted-average cap rate of 6.5%. Given our year-to-date activity, we are increasing the lower end of our disposition guidance range to $45 million while maintaining the upper end of our range at $75 million.

On the leasing front, we executed new leases, extensions, or options on approximately 192,000 square feet of gross leasable area notably new leases, extensions or options included a Dick's Sporting Goods in St. Joseph, Missouri, and a Big Lots in Cedar Park, Texas. At quarter end our 2022 lease maturities stood at just .2% of annualized base rents. We are also in terrific position for the upcoming year with only 1.5% of portfolio wide leases maturing.

At quarter end, our portfolio encompassed over 1,700 retail properties across all 48 continental United States, including 201 ground leases representing 12.7% of total annualized base rents. Occupancy ticked up during the quarter to 99.7%. While our investment grade exposure stood at nearly 68%, representing a two-year stacked increase of 530 basis points. Our portfolio is the best in the country and undoubtedly positioned to withstand any economic headwinds.

With that, I'll hand the call over to Peter and then we can open it up for questions.

Peter Coughenour | Agree Realty Corporation | CFO
Thank you, Joey.

Starting with the balance sheet, as Joey mentioned, we had another very active quarter in the capital markets, raising or settling almost $1.3 billion of capital.

At quarter end, we had no floating rate exposure and approximately $252 million of cash on hand. In conjunction with no material debt maturities until 2028, we are well positioned to withstand interest rate headwinds and volatility in the capital markets.

In August, we completed a $300 million public bond offering comprised of 4.8% senior unsecured notes due in 2032. In connection with the offering, we terminated related swap agreements of $300 million, receiving approximately $28 million upon termination. Considering the effect of the terminated swap agreements, the effective all-in rate for the 2032 notes is 3.76%. The offering further staggered our maturities and extended our weighted-average debt maturity to approximately 8 years.

During the quarter we raised more than half a billion dollars of additional forward equity. We sold nearly 1.7 million shares during the quarter via our ATM program, raising net proceeds of approximately $127 million. In September, we completed a 5.8 million share forward offering for anticipated net proceeds of approximately $382 million upon settlement.

In conjunction with the September forward equity offering, we settled all 8.7 million shares of outstanding forward equity, realizing net proceeds of approximately $601 million. At quarter end, we still had 5.8 million shares anticipated to be settled from the September forward offering, representing anticipated net proceeds of approximately $382 million.

Our capital markets transactions provided us with more than $1.6 billion of liquidity at quarter end, including cash on hand, full availability on our $1 billion revolving credit facility, and our aforementioned outstanding forward equity.

As of September 30th, proforma for the settlement of the $382 million of outstanding forward equity, our net debt to recurring EBITDA was approximately 3.1 times. Excluding the impact of unsettled forward equity, our net debt to recurring EBITDA was approximately 4 times.

Total debt to enterprise value at quarter end stood at 24%, while our fixed charge coverage ratio, which includes principal amortization and the preferred dividend, remained at a very healthy level of 5 times.

Moving to earnings, Core FFO and AFFO for the quarter were $0.97 and $0.96 per share, representing 5.6% and 7.8% year-over-year increases, respectively. As mentioned on prior calls, we continue to anticipate high single-digit AFFO per share growth in 2022, implying two year stacked growth in the high teens.

As a reminder, treasury stock is included within our diluted share count prior to settlement if and when ADC stock trades above the deal price of our outstanding forward equity offerings. The aggregate dilutive impact related to these offerings was a penny in the third quarter.

During the third quarter, we declared monthly cash dividends of 23.4 cents per common share for July, August and September. On an annualized basis, the monthly dividends represent a 7.8% increase over the annualized dividend from the third quarter of last year. While meaningfully increasing the common dividend over the past year, we maintained conservative payout ratios for the third quarter of 73% of Core FFO per share and AFFO per share, respectively.

Subsequent to quarter end, we again increased our monthly cash dividend by 2.6% to 24 cents per share for October. The monthly dividend reflects an annualized dividend amount of $2.88 per share, or a 5.7% increase over the annualized dividend amount of $2.72 per share from the fourth quarter of 2021.

General and administrative expenses totaled $7 million in the third quarter. G&A expense was 6.4% of total revenue, or 5.9% excluding the non-cash amortization of above and below market lease intangibles. We now anticipate that G&A expense will decline between 40 to 50 basis points as a percentage of total adjusted revenue compared to last year, from a prior anticipated range of 20 to 50 basis points.

Total income tax expense for the third quarter was approximately $720 thousand. Our expectation for total income tax expense this year remains between $2.5 and $3.5 million.

In summary, our well-positioned balance sheet affords us tremendous flexibility with proforma net debt to EBITDA of 3.1 times and roughly $1.6 billion of liquidity to fund our robust investment pipeline.

With that, I'd like to turn the call back over to Joey.

Joey Agree | Agree Realty Corporation | President & CEO
Thank you, Peter. At this time, operator, we will open it up for questions.

QUESTIONS AND ANSWERS

Operator
[Operator Instructions] First question will be from RJ Milligan of Raymond James.

R.J. Milligan | Raymond James
So I was going to start with my boilerplate question of this earning season. What's your current weighted average cost of capital, and how do you calculate it?

Peter Coughenour | Agree Realty Corporation | CFO
RJ, this is Peter. I'd say first, we are always looking at to get ahead of our capital needs so that we can retain flexibility in terms of how and when we access the markets. And to that end, we raised their settled $900 million of capital during the third quarter that was used to fund our acquisitions during the quarter but also provides a significant runway moving forward. The breakdown in terms of the capital raised during the quarter includes $300 million of long-term debt issued at an all-in rate below 4%. And we also settled $600 million of forward equity with a cost in the mid- to high fives. So blending that all together, we raised $900 million during the quarter at a weighted average cost of around 5% weighted 2/3 equity and 1/3 debt.

As Joey mentioned in his prepared remarks with the debt markets effectively frozen today, our long-term cost to borrow is in the sixes assuming a new 10-year public issuance. And so absent any changes in the debt capital markets, we'll likely look to fund the business using equity only going forward while continuing

to utilize the revolver for shorter-term borrowings.

Today, we have more than $380 million of outstanding forward equity available to us that was raised at a cost in the mid- to high fives and, any incremental equity issue would be at a similar cost based on our current share price.

I think most importantly, we're going to continue to be disciplined and prudent in terms of investing incremental capital. We're not going to deploy capital if it's only marginally accretive. And at the same time, we're not going to go up the risk curve just to achieve better spreads.

R.J. Milligan | Raymond James
Got it. So I think it's fair to acknowledge, obviously, the prefunding that you guys have executed on over the past few months. There is a pretty long equity runway relative to some of your peers. And you've got a cost of equity capital that still allows for accretive growth. But if cap rates are moving higher, or the expectation is that they are going to move higher, why accelerate growth into 4Q versus waiting for the market to move?

Joey Agree | Agree Realty Corporation | President & CEO
Well I think, RJ, that's opportunistic for us. So I anticipate cap rates in Q4 to tick up for us with a similar credit profile to the third quarter and a similar term profile to this quarter as well. So I would anticipate taking advantage of the merchant builder market where there's an immediate need to recycle capital. And I think we'll see that in Q4 given the increase in the bottom end of our guidance.

Going forward, we'll take qualitative and quantitative aspects, obviously, both into consideration as we deploy capital. I think the bottom line is. This we've taken flack historically, not from you, but we've taken flack historically for running a very low levered balance sheet, introducing forward equity into the net lease space, which wasn't really overly welcomed the first time it was introduced, to maintaining a conservative approach.

So these are the times, frankly, when that pays off. And at the same time, we're going to continue to run a low levered balance sheet, stay within our historical sandbox of investing in the best retailers in the world because at some point debt will come back into the market. I don't believe it's going to be anywhere near the rates that we've seen given the supercycle. But we'll be in a position to add incremental leverage at that time.

R.J. Milligan | Raymond James
Thanks for that. And Joey, you've been pretty vocal over the past couple quarters that you expect M&A and in the broader reach space and maybe in net lease. And we did see one of your peers taking private recently. Do you think there's more M&A to come?

Joey Agree | Agree Realty Corporation | President & CEO
First off, congratulations to Mary and her team. I mean, obviously, that was a terrific outcome for them. Look, I think we are not only in the net lease space. I think there are a number of companies situated given their cost of capital and potentially their balance sheets and/or their investment strategies which aren't able to drive those spreads. And as you know, it's very difficult to come back in the REIT space once you have an impaired cost of equity especially.

And so our approach, our bent, has always been conservative in preparation for what's next. We'll

continue to follow, obviously, that historical approach here that predates my time in terms of balance sheet management. And we'll see what happens in 2023. We don't have a crystal ball here, but I wouldn't be surprised to see more M&A activity across the REIT space.

Operator

Thank you. Our next question will be from Brad Heffern, RBC Capital Markets.

Brad Heffern | RBC Capital Markets

Joey, in your prepared comments, you mentioned distressed opportunities sort of in passing. I guess, how frequent are those? And what do they look like?

Joey Agree | Agree Realty Corporation **|** President & CEO

Well, I think the most the most distressed, "distressed," we're seeing right now is those that are in the need to sell, the need to recycle capital. And so what you'll see again from us in Q4 is opportunistically working with those developers that have pipelines that are delivered that need to recycle capital, that are historic merchant builders across the space and have recognized that the 1031 buyer or the 2021 pricing, there isn't a feasible option for them to recycle capital into new projects or into other ventures. And so that is, I will tell you, the true distress that we're seeing today. Those are the first to recognize the immediate expansion in cap rates.

The second level is those with debt maturing or have a defined use for those proceeds. And we're seeing that as well. The remainder of the market continues to lag with wishful thinking for that miraculous 1031 buyer or, frankly, the person, the buyer, that thinks we're still in 2021 or an all cash buyer. That's where we really see the bid-ask spread remaining. We anticipate that hopefully to see more capitulation for that narrow as well.

Brad Heffern | RBC Capital Markets

Okay. And then you said you won't invest if it's only marginally accretive. I know historically you've solved for a spread of 150 basis points plus or minus. So if you're saying cost of equity is in the high fives, do you anticipate cap rates going above 7% for your sandbox eventually?

Joey Agree | Agree Realty Corporation **|** President & CEO

Well, I would tell you, would I anticipate cap rates going? I mean, I'm looking into my crystal ball. I think history here is a useful guide. Between 2014 and 2018, there was approximately $55 billion of single tenant net lease, retail traded. The tenure averaged about 2.5% at those times. And the average cap rate was 6.5%. So I'm not going to sit here today and say, I believe cap rates are going to go north of 7%. That said, I have no idea what type of economic conditions we're going to be in 2023.

I think if we're investing capital, and let's call it around 75 basis points unlevered on an accretive basis and high-quality assets with a later infusion of debt, again, not with the tenure at 2% and spreads back to 100 with an all-in cost of 3%, I think we can get there.

That said, if we're unable to invest capital accretively, we're going to maintain our discipline. And so we're not going to take this balance sheet to a leverage position. We're not going to get on a hamster wheel. Halloween is over. So we're going to find the best opportunities.

What I can tell you this. I can guarantee you that this team and this company will lead the cap rate expansion in our given space. And that's without going up the risk curve. That's without moving into

private equity sponsored companies on a sale leaseback basis. That's without looking at short duration risk on assets. It's going to stay within our confines of what we're best at.

Operator
Next question comes from Josh Dennerlein of Bank of America.

Joshua Dennerlein | Bank of America Securities
Joey, I want to explore your comment on the competitive debt not returning the market anytime soon. I guess, what are you looking for when it comes to recapping the debt markets? Or how do you really describe competitive debt? What does that mean to you guys?

Joey Agree | Agree Realty Corporation | President & CEO
Well, I think, look, first off, I mean, debt today is outside our cost of equity. I mean, that's first off. So I mean, there really is no true debt market today, especially in the 10-year unsecured space. Obviously, anyone can look at where investment grade paper is trading today. We've never historically been a short-term borrower. We're not going to run a significant balance on the facility and on a variable basis. So debt obviously has to be accretive relative to our cost of equity. I think that that's the threshold.

From there, we'll see. Look, I already said I think the supercycle of lower for longer is over. That's my best guess. But at the same time, maybe it's wishful thinking. I hope in the back half of next year that we'll see a debt market that materializes and truly becomes a market again, that companies are able to obviously raise that capital in.

Joshua Dennerlein | Bank of America Securities
All right. And how are sellers -- do they understand the change in the cost of capital that buyers have today? What are the conversations like?

Joey Agree | Agree Realty Corporation | President & CEO
Josh, they are wide ranging. I will tell you there are sellers that still believe wishful thinking. Maybe that will end with the Fed today. We'll see. But we are seeing more and more sellers recognize that we're in a very distant position from 2021 or even earlier this year. I think the most important thing there isn't really sellers' recognition of the macroeconomic conditions and/or uncertainty. It is the lone hope of the loan 1031 or all-cash buyer throwing in a bid for an asset.

So in conversations with brokers, and there's been notes to a similar degree, the assets that are out there out there widely marketed, asking low cap rates sub five or five caps for high quality that lease assets are getting two bids today, maybe not 10. Activity is down to 20% of historical activity, recent historical activity.

So I think the biggest challenge there, again, is not pouring cold water. I think it's the wishful thinking and the hope for that for that 1031 buyer or all-cash buyer to return or throw in a bid. I think as we move forward in this economy as there's less to 1031 dollars here deployed, we're going to see some changes, hopefully, in terms of sellers' expectations. Hopeful expectations, I should say.

Operator
Next question comes from Ki Bin Kim of Truist.

Ki Bin Kim | Truist
Joey, sorry if I missed this, but what kind of cap rate should we expect over the next couple quarters?

Joey Agree | Agree Realty Corporation | President & CEO
Ki Bin, look, next quarter is all we have visibility into. We just began sourcing for Q1. And I would expect cap rates to pick up moderately there again, with similar profiles to the third quarter. Q2 was an aberration because of the large sale leaseback that we executed on in terms of investment grade profile. But I would expect over 70% investment grade similar to this quarter at or near 11% -- or 11 years weighted average lease term. And I would also anticipate ground lease activity kicking up there as well.

Ki Bin Kim | Truist
Okay. And I know someone asked this previously, but let me try another stab at it. How do you balance looking at -- you mentioned your WAC. Obviously it was more favorable looking backwards then going forward for everybody. But how do you balance buying this type of volume? I know you can with a great balance sheet. But how do you balance buying it versus -- with your view that cap rates need to be higher and maybe taking a little bit of a pullback?

Joey Agree | Agree Realty Corporation | President & CEO
So I think -- look, it's a great question. I think this is an art and not a science. Nobody has a crystal ball into 2023. We'll get hopefully a little bit more clarity from Mr. Powell shortly here, but nobody has clarity into 2023 yet. That's why I would refer back to Peter's comments.

We will be disciplined. We are going to make sure that transactions are accretive, both mathematically accretive, but also qualitatively accretive. We are by no means is going to put the pedal to the metal here and lever up a balance sheet with spreads that don't make sense. And we're going to be disciplined and thoughtful as we've always been.

Look, we are in very uncertain times. There are many risks on the horizon, whether they're domestic or macro international risks. We're cognizant of those risks. Again, this balance sheet, this company, was built for those risks. And so every dollar we deploy has to be thoughtful and has to do with purpose.

Ki Bin Kim | Truist
Okay. And more a bigger picture question. I'm a little surprised that more triple net REITs haven't issued convertible debt. I mean, you guys report on a AFFO basis anyway, where the GAAP interest expense non-benefit doesn't really matter. Just any broader thoughts on convertible debt and if that's a tool that makes sense for you guys, at some point?

Joey Agree | Agree Realty Corporation | President & CEO
It doesn't make any sense for us. Again, we're trading today on an implied or AFFO basis. And in the mid-five range, convertible doesn't make any sense for us today. In terms of an option -- a capital source for other companies, really haven't spent any time on it.

Operator

Next question will come from Nick Joseph of Citi.

Nicholas Joseph | Citi
Joey, do you have any sense of how much 1031 money is still out there looking to be deployed?

Joey Agree | Agree Realty Corporation | President & CEO
I wish I did. It's amazing that even the -- I'll tell you there's a lot of talk of it still. I think the feedback that we've gotten, that I've gotten from my team especially from recent conferences and roadshows and meetings is that there's a recognition that that money is waning. So there's a lot of talk of it.

I'll tell you that the sentiment and the hope has gone from -- in the broader community has gone to wishful thinking more from hopeful that there's 1031. And so that has been recognized. I haven't seen anybody try to quantify those dollars. But undoubtedly, those dollars are beginning to wane as the sheer number of real estate transactions in the commercial space has -- the velocity of them has decreased significantly.

Nicholas Joseph | Citi
Yes. Exactly. And then, what are you seeing in terms of the difference in stickiness for cap rates on ground leases versus a traditional net lease?

Joey Agree | Agree Realty Corporation | President & CEO
Really the same. I think ground leases have gotten -- as I mentioned probably on the last couple of calls, ground leases have gotten a lot of attention due to us, to safe hold, to the sell side covering them. I tell you that it's -- that market is very similar relative to the broader net lease market, that there's still a bid-ask spread. We're still looking for sellers to capitulate. That said, I do anticipate our ground lease pipeline in Q4 will be fairly sizable.

Operator

Next question will come from Haendel St. Juste of Mizuho.

Ravi Vaidya | Mizuho
This is Ravi Vaidya in the line for Haendel. Can you just comment in the acquisition pipeline? Are you targeting any new tenants or categories? Are you seeing any pricing differentials that you're seeing on a category basis?

Joey Agree | Agree Realty Corporation | President & CEO
So no new tenants or categories. I would tell you selectively, we will insert tenants into that sandbox, or we will remove them into that sandbox. But I don't think it's appropriate, any new tenants or categories on a holistic basis.

In terms of cap rates by sector, we're seeing velocity in those sectors in terms of cap rate dispersion. We're seeing velocity in the sectors that are driven by merchant builders. That's generally retailers that are growing at a fast clip or have leveraged the merchant build community -- builder community, excuse me, to drive new store growth from.

Ravi Vaidya | Mizuho
Got it. Just one more here. I know you're shopping in the higher-quality end of the spectrum. Cap rates tend to be stickier there. But can you comment how cap rates have shifted for investment grade tenants versus non-investment grade tenants?

Joey Agree | Agree Realty Corporation | President & CEO
I would tell you we don't spend much -- look, investment grade, we've always said, is an output of our strategy. There are significant tenants in our portfolio that don't have ratings, that are fantastic balance

sheets. Many of them are transparent for the public to see, whether that's Publix, Hobby Lobby, Chick-fil-A, Aldi. So top tier retailers in this country.

The bottom line is tenants in the non-investment grade are unrated that aren't, I would tell you probably BB or better, especially the smaller operators, and even more acutely the private equity sponsored retailers. The cap rates on those assets are blowing out, and they should. I mean, those assets today, those sponsored tenants, have balance sheets that have variable rate debt, have near-term maturities. They're generally single purpose boxes in nature. It's nearly impossible to put a residual or terminal value on the underlying real estate. They have limited access to capital, and their funding source is predominantly net lease REITs on a sale leaseback basis, who tend to be their largest unsecured creditors or amongst their largest unsecured creditors.

We have no interest in playing in that space. I think it's imprudent given the macroeconomic outlook that we see today over the potential ranges of outcome. But we've never played in that space. And so I can't give you specific instances of the cap rates because frankly, we don't spend time there.

Operator
Our next question will come from Tayo Okusanya of Credit Suisse.

Tayo Okusanaya | Credit Suisse
Congrats on a solid quarter. Joey, could you -- I mean, your earlier comment just about, again, rising cost of debt, bad balance sheets creating opportunities for you. Could you talk on the flip side with your retailers who are also going through that rising cost of capital and bad balance sheets, if any? And just talk a little bit about the watch list, where you see it is going. Any particular REIT categories you've become a little bit more concerned about with just what's going on with the overall macroeconomic backdrop in the U.S.?

Joey Agree | Agree Realty Corporation | President & CEO
Yes. Tayo, I think in terms of categories, we don't have exposure to categories where we have concern. Again, we just don't have the discretionary component, the recreational component, the luxury component in this portfolio.

We are focused specifically on those core durable, generally recession resistant tenants and the leading operators in their respective sectors. So that's really not -- now every property in our portfolio is on our website. So you want transparency, go to our website. All 1707 properties as of 9/30 are on our website.

We have three Bed Bath and Beyonds in the portfolio. We bought them all for the real estate. They are all tremendous pieces of real estate. Feel free to Google Earth them. We have one At Home in our portfolio in Provo, Utah. It is a critical piece of real estate on the main thoroughfare in Provo. We'd love to get it back one day and have had multiple offers on it.

So at the end of the day, we look at every asset and on a single or case-by-case basis. And we just -- really, outside of a couple few movie theaters that we have in the portfolio, we just don't have those challenges.

Tayo Okusanaya | Credit Suisse
Great. That's helpful. And then in the transactions markets, are you seeing things look a little bit different for ground lease type transactions versus standard fee simple triple net buildings out there?

Joey Agree | Agree Realty Corporation | President & CEO
No. As I mentioned before, generally the same. Its transaction specific. Now the ground lease market is nowhere near as deep or as large as the standard debt lease market, so there are, of course, aberrations. But generally the same, nothing overly -- both markets today are in a stare down for the general -- a general stare down, I'll say, in terms of buyers and sellers and gaps there.

Operator
Next question will be coming from Linda Tsai of Jefferies.

Linda Tsai | Jefferies Group, LLC
The high single digit earnings growth in 2022 and high teens on a two-year stack, as you look at your pipeline and given the view that cap rates move higher, what type of earnings growth might be achievable next year?

Joey Agree | Agree Realty Corporation | President & CEO
Linda, it's a great question. Look, a lot of it is going to depend, obviously, on the sources and uses if and when the debt markets come back, where cap rates move to. I think the thought of net lease REITs growing in the upper single digits in terms of AFFO growth or double digits probably isn't overly prudent if there's any thought of that next year. And so we're going to see if the macroeconomic circumstances are really going to drive, obviously, the sources of capital in terms of the cost there.

And then what happens in the overall cap rate environment and pricing environment is going to be the second piece there. And I wish I had the crystal ball to be able to tell you that today. But we unfortunately don't have it.

Linda Tsai | Jefferies Group, LLC
Thanks. And then has the tone or tenor change from retailers as it relates to their store growth outlooks?

Joey Agree | Agree Realty Corporation | President & CEO
No. I will tell you that the conversations we have with retailers -- again, we're not in the luxury or discretionary space, so I can't speak to those retailers. The conversations that we're having with retailers today revolve around the inability of developers to perform on their new store strategies. Their story strategies for 2023 are generally already built out with those -- with pipelines. Now it comes down to execution.

And so I'll give you an example. We talked to a large farm and rural supply retailer recently with a developer who had 50 stores in the pipeline, then down to 30 stores. Three ended up hurtling. So generally speaking, the retailers in our portfolio have promised new store openings to the street. They are in growth mode. And now they have challenges getting constituents and stakeholders to actually execute on that new store growth due to rising costs, both labor, obviously, and materials; rising interest rates; the lack of availability of construction loans; and then most importantly now for a merchant builder, I'd tell you, the lack of clarity on what their exit cap rate will be. And so we're working with those partners to see if there's a solution that makes sense for both of us in terms of deploying all three of our platforms.

Linda Tsai | Jefferies Group, LLC
Thanks. That's really helpful. Just one last one. What's driving G&A lower?

Peter Coughenour | Agree Realty Corporation | CFO

Linda, this is Peter. In terms of decrease in G&A during the quarter, it was spread across several different areas, including accounting and tax, IT and stock-based compensation expense where there was a onetime decline due to some employee forfeitures.

I would note that our guidance for 2022 implies a 40 to 50 basis point deceleration in G&A to approximately 6.5% of total adjusted revenue. And that guidance assumes that G&A in the fourth quarter returns to a level more similar to the expense that we saw during the first and second quarters of this year.

Operator

Next question comes from Wes Golladay with Baird.

Wes Golladay | Robert W. Baird & Company

Has there ever been a time where your cost of equity has been less than your cost of debt for a prolonged period like we're seeing now? And then you did make the comment about no short-term debt. Is that to read no term loans, so always going to target tenured debt? So a little bit more clarification on that.

Joey Agree | Agree Realty Corporation | President & CEO

Yes. Not my tenure, Wes. I mean, our cost of capital is effectively inverted today. And we anticipate to remain inverted for a while here as the tenure remains elevated and spreads remain extremely elevated. When we talk about short-term debt, we're talking about carrying extended balances on the credit facility either on a variable basis or on a swap basis.

We have looked at the term loan market and executed specifically in the seven-year term loan market historically. Most recently, we've been obviously an unsecured issuer in the public bond space at the 10 and 12-year levels here. But we'll look at all available options here what makes sense in terms of our capital stack debt maturities. But we're not going to take any variable rate risk, or any tenure risk.

Wes Golladay | Robert W. Baird & Company

Okay. Got it. And then I want to look at the merchant builder situation. Do you get the sense there are retailers are willing to pay higher rent to help the merchant builders absorb a little bit higher cap rate on their exit? And when you look at your pipeline, this year was really a lot of Gerber Collisions. You made a good headway there. In the background, do you have a bunch of retailers or a handset of retailers that you're potentially going to have dropped next year where we see maybe this pipeline just swell?

Joey Agree | Agree Realty Corporation | President & CEO

So retailers are looking for all different types of solutions today. The team has been to a number of retailers' headquarters meeting with their heads of real estate in their respective departments. They're looking at increasing rent. They're looking at internalizing development. They're looking at fee-based programs to keep it on balance sheet. They're looking at more term, larger increases. I think all different types of solutions are being looked at so they can get new stores opening in the ground.

To your second question, we're always talking to retailers, and we're always looking for opportunities to grow commensurate with their pipelines. Again, it just really has to hurdle for us across all three platforms from an economic basis.

Wes Golladay | Robert W. Baird & Company
Yes, and just a follow up on that. I mean, was there something specific about Gerber where you're just going to probably maybe provide them a little bit more, I guess, platform value where they said, hey, we want to just grow with you quite a bit, and you're the one that we want to work with, where maybe others are just doing one-offs? I just wonder if there's anything special about that one because it really was a lot of Gerbers this year.

Joey Agree | Agree Realty Corporation | President & CEO
Yes. Well, we've been talking to Gerber, I would say, for upwards of six years. And we had identified Gerber specifically because they're the only public company -- traded on the Toronto Stock Exchange, owned by Boyd Group. They're the only public company in the collision space. And so as we saw, Caliber and Service King, both private equity sponsored, continue to gobble up independent operators as well as open net new stores.

We were very attracted to the collision space because of the cost of repairs, the third-party payment, cost of repairs because of the cameras and the sensors. As I mentioned before, you can't just go to your traditional bump stop. You need a technician at a computer wizard to fix everything on your car today. So we were very attracted to this space.

We identified Gerber, again, because of their low-levered balance sheet, which everybody can see online. Those conversations culminated with Gerber entering into a significant growth phase, obviously, from an organic perspective rather than an M&A perspective. And so the collision space was dominated by M&A, by the big three operators, as I mentioned, Gerber being the only public one acquiring one-off and small collision repair chains.

It then became cost prohibitive or, frankly, lack of opportunities out there. So they flipped to greenfield and brownfield development. And that's where we finally hit a chord and found a partnership there that worked for both of us.

And so we're very active, obviously, with Gerber. They have over 725 locations across the country. And we love the business, the direction of the business and, frankly, their relationships with auto insurers who direct clients to Gerber.

Operator
Next question will be from Ronald Kamdem, Morgan Stanley.

Ronald Kamdem | Morgan Stanley
Two quick ones. Just coming back to the acquisition pipeline, there's sort of two factors. There's volumes, and then there's pricing. And then you talked about that cap rate's 6.2% in the quarter. That should be going up.

As we're sort of thinking about next year, should we expect the same amount of volumes at those high cap rate levels? Because I think what your messaging is that cap rates are rising, but they're probably rising a little bit slower than cost of capital. So is this a scenario where we should be expecting higher cap rates coming through? But are the volumes -- is there a give or take there? Or is there just enough to go around? Does that make sense?

Joey Agree | Agree Realty Corporation | President & CEO
No, I think you hit it dead on. And if we don't see cap rates rise where they hurdle for us quantitatively, then you will see volume slow down. I mean, there's obviously no doubt about it. And so as cap rates move, we will be careful with -- or don't move, frankly, we'll be careful with how we put our pedal to the metal, or frankly, we lay off.

And so again, we have to be take every transaction on a discrete basis, look at the qualitative and quantitative aspects of both of them and then decide whether it makes sense relative in the broader market for us. And so we are going -- look, we are in a read-and-react mode. I think it's fair to say everybody is in a read-and-react mode. And we will not get ahead of our skis, that's for sure.

Ronald Kamdem | Morgan Stanley
Great. And then just moving on to tenant health, tenant risk. Maybe can you just remind us just what bad debt has been this year. Obviously, you guys have a super-clean portfolio, so it's pretty small. But the real question is obviously, as we're thinking about the next year, the next two or three years, are you seeing anything to suggest that there's going to be more pain coming down the retail pipeline? What are you hearing on that front?

Joey Agree | Agree Realty Corporation | President & CEO
I'll take it from a high level. Yes, I anticipate pain, not specific to this company because the portfolio is so strong. But I think a lot of balance sheets were -- retailer balance sheets were repaired during COVID. They either -- the oddity of surge sales or, frankly, the ability to access low-cost capital. And so a lot of balance sheets, ironically, were repaired during COVID. I think we're seeing the deterioration of those balance sheets today back to a more normalized pattern based upon their overall businesses.

And so over the next two or three years, I think we're going to see -- and I think maybe even a shorter period of time, we're going to see more and more distress in the broader retail environment. Again, a lot of this is dependent upon the consumer and macroeconomic conditions. But COVID was an outlier. COVID -- and I've told people consistently, COVID was not a proxy for a recession. COVID was not a proxy for retailer distress. It was a time out. And during the time out, a lot of people and a lot of retailers got to eat and, frankly, got some free things, or very cheap things.

And so now we're seeing a normalization of sales levels across most retail sectors today. And the normalized sales patterns of a lot of these retailers pre-COVID didn't make much sense to be sustainable in terms of an ongoing retail operation. And so I think we're going to see that normalization. And actually, we're seeing it today. We're seeing the tip of the iceberg today.

Peter, I'll talk to -- you could talk specifically about the bad debt.

Peter Coughenour | Agree Realty Corporation | CFO
Yes. In terms of bad debt, year-to-date, we've only recorded approximately $300,000 of bad debt expense, which is roughly 10% -- or sorry, 10 basis points of revenue on a year-to-date basis. So very minimal bad debt expense recorded year-to-date. Looking forward, we specifically identify tenants or instances of bad debt. So it's difficult to predict exactly what level of bad debt we will have moving forward. But again, as Joey referenced, we think our portfolio is in great shape today.

Operator
Next question will come from Chris Lucas, Capital One.

Chris Lucas | Janney
Just a couple of quick questions. Joey, if we take a step back and think about the buckets of transaction opportunities that you guys look at, so you've got direct-to-tenant deals, and then you've got existing lease deals that are out there that you might acquire. Are you seeing any differential in terms of the sellers in these cases, either one side or the other, adjusting to the capital market pricing today faster than the other at all?

Joey Agree | Agree Realty Corporation | President & CEO
It's a great question. I think the direct-to-sellers, those conversations generally and those thoughts are moving a little bit quicker, inclusive of direct-to-retailers than either marketed opportunities and/or off market opportunities that are out there shopping. So I think those direct conversations are cutting through to today's reality a little bit quicker, generally speaking, than some of the circuitous hopeful conversations that are out there.

Chris Lucas | Janney
Okay. Thank you for that. And then Peter, I guess, maybe just taking the prior question one step further. Any sense as to what year fully swapped seven year or five year term loan all-in costs would look like today?

Peter Coughenour | Agree Realty Corporation | CFO
Yes. Chris, I guess to answer that, I would say as this year has progressed, obviously there's been a lot of volatility in the debt capital markets, specifically the public bond markets. And as a result, I think more issuers have looked to the term loan market rather than the public bond market. We had the swaps in place earlier this year, where it made sense for us to access the public bond markets at an all-in right below 4%.

In terms of accessing the term loan markets today, I think as banks have issued more term loans this year to issuers, you've seen balance sheet, bank balance sheets, grow and less of an appetite to issue term loans, particularly five and seven-year term loans. And so it's difficult to say exactly where we can price a five or seven-year term loan today. I think we're seeing banks push companies towards the shorter-term term loans, one or two years, with options to extend.

Chris Lucas | Janney
Okay. That's helpful. And last question for me, Joey. Just curious as to your thoughts about how you feel about Kroger as a credit given the Kroger-Albertsons merger announcement and how you're thinking about your portfolio there. Any risk to regulatory sales or anything like that that you're worried about?

Joey Agree | Agree Realty Corporation | President & CEO
No. Nothing there concerns me in terms of credit. There's no release provisions in any of our Kroger lease. I think the more interesting fact -- or I think the more interesting thing, frankly, is Kroger's desire to actually acquire Albertsons.

We've been talking for a long time about how we only will invest in the top-tier grocers in the country and that grocery has been thought of as a safe haven generally, both in the net lease space as well as the shopping center space in the broader retail environment. And we continue to remind people that grocery

has been a 2% business historically. When you have to pick it off of the floor, paying associates $20 an hour, some of them loaded wages even higher on the union basis, the margins quickly deteriorate.

And so what we're seeing, and I think we're seeing, with the Kroger-Albertsons is a move to increase scale even further because of margin deterioration CapEx spend in terms of Ocado and Fulfillment. And so no concern on our end. All of our Kroger deals have, again, full Kroger guarantees. No release provisions there. I would anticipate a spinoff being really consolidated in the existing Albertsons stores. I think it's going to be interesting to see what the FTC does here. We obviously tracked the Tractor-Orscheln FTC approval process, which I believe extended 18 or more months, and only -- it was in the farm and rural supply business with 180 stores that Tractor was buying. That consisted of the entire company for Orscheln. They had to divest of approximately 50%.

So as we watch the FTC here, it's going to be very interesting when it comes to something such as food, especially with the inflationary pressures we've seen on food, what that approval process is going to look like. But I think there's no doubt that we're going to continue to see grocers search for scale. And so we're going to stay at the top end of the grocery spectrum because I just truly don't believe it's actually the safe haven than investors have generally perceived.

Operator

Next will be a follow-up question from Tayo Okusanya of Credit Suisse.

Tayo Okusanaya | Credit Suisse

Yes. Just a very quick one. The cap -- the 6.2% cap rate this quarter, the gap cap rate, could you give us a sense of what the cash flows are on your most recent transactions? I'm trying to get a sense if you feel a gap in the cash yield, the spread between the investment grade and the noninvestment grade market, whether that's [about] to gap out again, because it had collapsed over a while. [Indiscernible] started to gap out again at this point.

Joey Agree | Agree Realty Corporation | President & CEO

Sorry, Tayo, you're breaking up. To the part that came through, really, the spread between investment grade and noninvestment grade or unrated for us is really close. Again, some of our favorite retailers, Aldi, Hobby Lobby, Chick-fil-A, Publix traded at very aggressive cap rates. They're are unrated. Some of them are closely held, private family owned companies, but they are -- but they trade as if they were investment grade because of the perceived credit profile, although they don't carry a third-party rating.

And so there really isn't that wide of a dispersion. I'll tell you there's probably, given term credit real estate and a number of other factors, probably about a 75 to 85-point -- 85-basis point dispersion across cap rates of where we invest capital. It's in this quarter, average of 6.2%. And again, we anticipate that ticking up in Q4 as we see more opportunities really driven by the merchant builder space.

Tayo Okusanaya | Credit Suisse

And on your cash yields, you were probably mid-5%?

Joey Agree | Agree Realty Corporation | President & CEO

Excuse me? You're breaking up again.

Tayo Okusanaya | Credit Suisse

Cash yield. I said your gap yields were 6.2%. Your cash yield for the quarter --

Joey Agree | Agree Realty Corporation | President & CEO
Oh, no. Closer -- around 6%.

Tayo Okusanaya | Credit Suisse
The cash yields are around 6%?

Joey Agree | Agree Realty Corporation | President & CEO
Yes.

Operator

That concludes our question-and-answer session. We'll turn the conference back over to Mr. Joey Agree for closing remarks.

Joey Agree | Agree Realty Corporation | President & CEO
Well, thank you, everybody for joining us today. I'm going to get the opportunity to go blow my nose. And we look forward to catching up in NAREIT in a couple of weeks. Appreciate it. Thank you.

Operator

Thank you. Conference has now concluded. Thank you for attending today's presentation. You may now disconnect.