STAG Industrial (STAG)

Updated August 13th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	$28	**5 Year CAGR Estimate:**	9.7%	**Volatility Percentile:**	56.0%
Fair Value Price:	$26	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	43.4%
% Fair Value:	107%	**5 Year Valuation Multiple Estimate:**	-1.4%	**Valuation Percentile:**	47.3%
Dividend Yield:	5.1%	**5 Year Price Target**	$35	**Total Return Percentile:**	64.7%

Overview & Current Events

STAG Industrial is an owner and operator of industrial real estate. It is focused on single-tenant industrial properties and has 370 buildings across 37 states in the United States. Stag Industrial went public in 2011.

The focus of the REIT on single-tenant properties might create higher volatility in cash flows compared to multi-tenant properties, as the former are either fully occupied or completely vacant. However, STAG Industrial executes a deep quantitative and qualitative analysis on its tenants. As a result, it has incurred credit losses that are less than 0.1% of its revenues since its IPO. As per the latest data, 55% of the tenants are publicly rated and 28.4% of the tenants are rated "investment grade".

Like most REITs, STAG Industrial has markedly underperformed the market in the last 12 months, as it has lost 0.5% whereas S&P has advanced 15%. The main reason behind this underperformance is the environment of rising interest rates, which negatively affect REITs in two ways. As interest rates rise, the yields of REITs become less attractive and hence their valuation is pressured. Moreover, rising interest rates force REITs to refinance their debt at higher rates when it comes due. REITs, utilities and MLPs are the most vulnerable stocks to rising interest rates.

On the other hand, the rising interest rates indicate that the economy is strong and STAG Industrial greatly benefits from a strong economy. At the end of July, the REIT reported (7/31/18) its financial results for Q2-2018. The REIT grew its core FFO per share 10% over last year, from $0.41 to $0.45, thus exceeding the analysts' estimates ($0.44). Its same-store net operating income rose 2.6% while its occupancy rate climbed from 94.0% in Q2-2017 to 95.6% in Q2-2018.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
FFO	----	----	----	$1.03	$1.25	$1.44	$1.33	$1.42	$1.43	$1.67	***$1.75***	***$2.34***
DPS	----	----	----	$0.73	$1.07	$1.20	$1.29	$1.36	$1.39	$1.41	***$1.42***	***$1.50***

As the Q2 results of STAG Industrial positively surprised the market, we slightly raised our estimate for the FFO per share of this year from $1.72 to $1.75. Moreover, STAG Industrial has grown its FFO at a 6.0% average annual rate in the last five years. It still has a market share that is less than 1% in its target market. Therefore, it has ample room to continue to grow for years and hence it is can be reasonably expected to keep growing at its recent pace in the upcoming years. If this happens, the REIT will grow its FFO per share from $1.75 this year to approximately $2.34 in 2023.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg P/FFO	----	----	----	11.1	14.4	14.2	18.4	13.0	16.7	16.4	***16.0***	***14.9***
Avg. Yld.	----	----	----	6.4%	7.2%	5.7%	5.6%	6.4%	6.4%	5.3%	***5.1%***	***4.4%***

STAG Industrial is currently trading at a P/FFO ratio of 16.0, which is higher than its historical average of 14.9. As it is reasonable to expect the REIT to revert towards its average valuation level in the next five years, the REIT is likely to incur a 1.4% annualized drag due to P/FFO contraction.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	----	----	----	10.0%	7.1%	8.7%	8.6%	9.3%	9.2%	9.1%	***9.0%***	***9.0%***
Debt/A	----	----	----	50.4%	51.3%	46.9%	45.3%	54.9%	51.2%	47.4%	***47.4%***	***50.0%***
Int. Cov.	----	----	----	1.1	0.5	1.0	0.8	0.2	1.8	1.8	***1.6***	***1.5***
Payout	----	----	----	70.9%	85.6%	83.3%	97.0%	95.8%	97.2%	84.4%	***81.1%***	***64.1%***
Std. Dev.	----	----	----	28.0%	15.4%	22.5%	21.8%	23.9%	27.2%	12.1%	***17.1%***	***20.0%***

STAG Industrial has a well-laddered lease maturity schedule, with a weighted average lease term of 4.8 years and about half of the leases maturing between 2022 and 2027. Thus the cash flows of the REIT can be considered fairly reliable. Thanks to these reliable cash flows, STAG Industrial is one of the few REITs that pay dividends on a monthly (instead of a quarterly) basis – a valuable characteristic for income investors. Income investors should also note that STAG Industrial currently offers a generous 5.1% yield and has never cut its dividend throughout its short history so far. Moreover, while its payout ratio rose to markedly high levels during 2014-2016, it has fallen to healthy levels in the last two years.

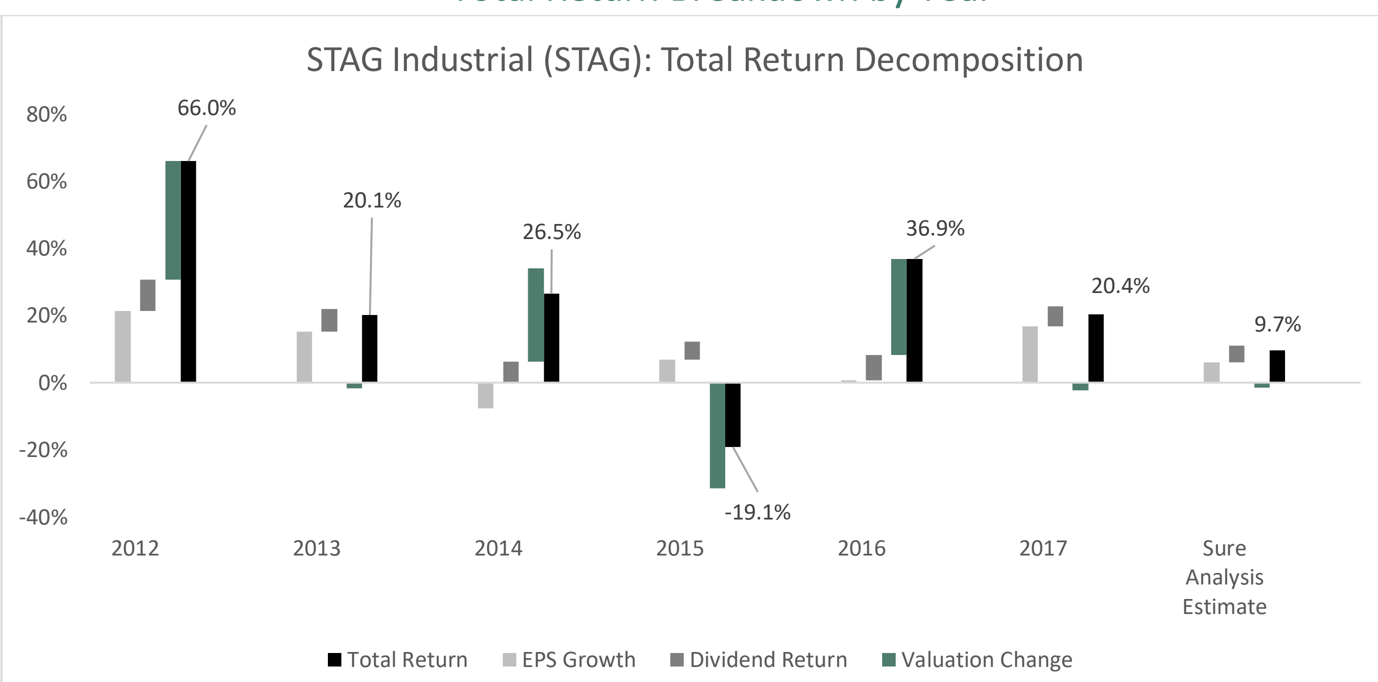
On the other hand, the REIT heavily dilutes its shareholders on a regular basis. Its share count has risen from 42 million in 2013 to 101 million now. While the dividend per share has risen only 18% since 2013, the annual amount paid has more than doubled, from $76 million in 2013 to $160 million this year. Investors should certainly keep this in mind.

Due to its focus on industrial properties, the REIT is highly vulnerable to recessions. As a recession has not occurred for 9 consecutive years and interest rates are on the rise, investors should certainly take this risk factor into account. Overall, STAG Industrial is likely to keep raising its dividend at a slow pace until a recession shows up. In such an event, the REIT will have an elevated probability of reducing its dividend due to the nature of its business model.

Final Thoughts & Recommendation

STAG Industrial continues to grow thanks to favorable economic conditions. In the absence of a recession, this REIT is likely to offer a 9.7% average annual return over the next five years thanks to 6.0% annual growth in its FFO per share and its 5.1% dividend, which will be partly offset by a 1.4% annualized P/FFO contraction. The company is a buy for income-oriented investors looking to bolster their exposure to the industrial real estate sector.

Total Return Breakdown by Year



Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.