Simon Property Group (SPG)

Updated October 29th, 2018 by Josh Arnold

Key Metrics

Current Price:	$180	**5 Year CAGR Estimate:**	9.7%	**Volatility Percentile:**	21.5%
Fair Value Price:	$201	**5 Year Growth Estimate:**	3.0%	**Momentum Percentile:**	80.7%
% Fair Value:	89%	**5 Year Valuation Multiple Estimate:**	2.3%	**Growth Percentile:**	10.6%
Dividend Yield:	4.4%	**5 Year Price Target**	$234	**Valuation Percentile:**	64.7%
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Total Return Percentile:**	49.6%

Overview & Current Events

Simon Property Group is a REIT that was formed in 1993. The trust focuses on retail properties, mainly in the US, with the goal of being the premier destination for high-end retailers and their customers. The trust has interests in about 230 different properties that amount to nearly 200 million square feet of leasable space. Simon produces about $5.5 billion in annual revenue and has a market capitalization of $64 billion.

Simon reported Q3 earnings on 10/25/18 and results were strong. Q3 FFO-per-share came in above expectations at $3.05 as revenue rose slightly. Fundamentals remain strong as occupancy was 95.5% and retailer sales per square foot were up 4.5%, so its customers are doing well. Total portfolio net operating income growth was 4.1%, leasing spread was up 14% and base minimum rent was up 2.8%. Simon also slightly narrowed its FFO-per-share guidance range, but our estimate is unchanged at $12.10.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
FFO/Shr	$6.42	$5.33	$5.01	$6.89	$7.98	$8.85	$8.90	$9.86	$10.49	$11.21	***$12.10***	***$14.00***
DPS	$3.60	$0.45	$2.60	$3.50	$4.10	$4.65	$5.15	$6.05	$6.50	$7.15	***$8.00***	***$10.50***
Shares	221	286	293	294	310	310	311	309	313	311	***309***	***310***

Simon's FFO history is quite good in that it saw only a minor dip in profitability during the Great Recession. Funds from operations have since more than doubled. Simon's focus on high-end retailing has proven an immense source of strength in recent years and we see that strength continuing. In total, we see Simon producing a 3% average annual FFO growth rate moving forward. Recent years have seen a growth rate roughly double that at 6%, but given Simon's already-dominant position in the retail sector, the unstoppable rise of e-commerce crimping demand for physical stores, and how mature the current economic cycle is, it looks like Simon and other retail REITs will have a harder time with future FFO growth.

That said, Simon is still the best retail REIT in the market by many metrics. Its occupancy rates remain extremely high, hovering around 95% in recent quarters. It also charges nearly $54 per square foot on average, which is tremendously high for retail space. Simon has built a niche with high-end retailers over the years such that it has the most desirable spaces and developments, and thus sees a virtuous combination of very high occupancy and leasing rates.

The distribution is obviously a big draw for Simon's shareholders as the trust allocates much of its excess capital in this way. The distribution has roughly kept pace with FFO growth over the long term and we see the distribution hitting $10.50 by 2023. Simon is already a strong income choice with its mid-4% yield and we see payout growth continuing.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/FFO	13.1	10.4	17.6	16.5	18.7	18.4	19.0	19.1	19.2	15.1	***14.9***	***16.7***
Avg. Yld.	4.3%	0.8%	3.0%	3.1%	2.7%	2.9%	3.0%	3.2%	3.2%	4.2%	***4.4%***	***4.5%***

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.

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Simon's valuation has been remarkably steady for much of the past decade and today, at just 14.9 times this year's FFO estimate, the stock is relatively cheap. We see fair value at 16.7 times FFO, implying a decent 2.3% tailwind to total returns in the years to come. Risks to this estimate would include a recession, but given that the economy and Simon's own operating metrics remain strong, we do not see this risk as imminent by any means. The distribution should grow slightly more quickly than FFO in the coming years, but with the stock's valuation moving higher, the yield should remain roughly where it is in the mid-4% area.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	88%	89%	78%	79%	71%	72%	82%	82%	82%	82%	***83%***	***84%***
Debt/A	87%	80%	77%	79%	79%	80%	80%	83%	84%	87%	***87%***	***83%***
Int. Cov.	1.6	1.4	1.7	2.3	2.5	2.3	2.7	3.3	3.5	3.8	***4.0***	***4.5***
Payout	56%	8%	52%	51%	51%	53%	58%	61%	62%	64%	***66%***	***75%***
Std. Dev.	51%	61%	22%	21%	14%	19%	12%	21%	19%	14%	***15%***	***18%***

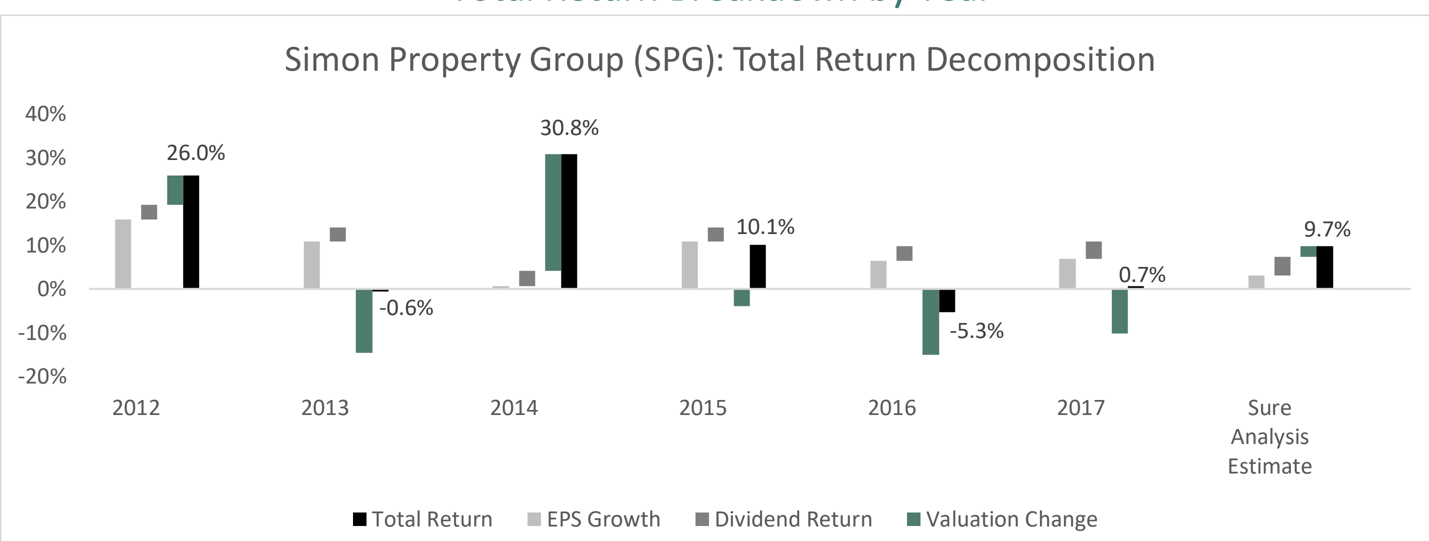
Simon's quality metrics have been very stable in the past decade as the company has kept operating metrics such as balance sheet leverage and interest coverage in a fairly narrow range. Profitability has improved over time as the company's strength has afforded it the ability to raise prices, but we believe most of the profitability gains have been made. Simon's lease pricing is already an industry-best and has stagnated in recent quarters, leading us to believe further margin gains from here will be challenging. The payout ratio should rise slightly as Simon has been boosting its distribution more quickly than FFO; given the forecast for slowing FFO growth, this should continue.

Simon's competitive advantage is in its world-class portfolio of properties that allows it to charge industry-best leasing rates. It is not immune from recession but held up very well during the last one, and that should be the case again.

Final Thoughts & Recommendation

Overall, we forecast Simon to produce robust 9.7% total returns in the coming years. We therefore rate the stock a buy as Simon offers investors a relatively cheap stock with a high yield and distribution growth prospects. The trust earns D rating for Dividend Safety, largely because of its dividend cut during the last recession.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	3783	3775	3958	4306	4256	4544	4871	5266	5435	5539
Gross Profit	3327	3350	3095	3387	3456	3706	3988	4306	4464	4559
Gross Margin	87.9%	88.7%	78.2%	78.6%	81.2%	81.6%	81.9%	81.8%	82.1%	82.3%
SG&A Exp.	371	319	228	282	291	319	355	350	366	338
D&A Exp.	957	1009	1016	1112	1301	1333	1286	1239	1328	1357
Operating Profit	1560	1604	1816	1943	2000	2189	2385	2669	2721	2802
Operating Margin	41.2%	42.5%	45.9%	45.1%	47.0%	48.2%	49.0%	50.7%	50.1%	50.6%
Net Profit	464	309	617	1025	1434	1320	1409	1828	1839	1948
Net Margin	12.3%	8.2%	15.6%	23.8%	33.7%	29.0%	28.9%	34.7%	33.8%	35.2%
Free Cash Flow	762	1344	1499	1560	1711	1860	1934	2004	2574	2862
Income Tax	4	-5	4	12	16	40	28	20	30	23

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	23423	25948	24857	26217	32587	33325	29532	30565	31104	32258
Cash & Equivalents	774	3958	797	799	1185	1691	612	701	560	1482
Acc. Receivable	415	N/A	N/A	487	521	520	580	625	665	743
Goodwill & Int.	N/A	N/A	N/A	296	507	376	312	276	285	209
Total Liabilities	20321	20765	19224	20673	25694	26502	23581	25349	26144	28019
Accounts Payable	N/A	N/A	N/A	1092	1374	1223	1260	1324	1214	1269
Long-Term Debt	18043	18630	17474	18446	23113	22670	20853	22417	22977	24632
Total Equity	2567	4412	4785	4605	5866	5805	5049	4428	4267	3643
D/E Ratio	6.90	4.18	3.62	3.97	3.91	3.88	4.09	5.01	5.33	6.68

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	2.0%	1.3%	2.4%	4.0%	4.9%	4.0%	4.5%	6.1%	6.0%	6.1%
Return on Equity	17.2%	8.9%	13.4%	21.8%	27.4%	22.6%	26.0%	38.6%	42.3%	49.3%
ROIC	2.2%	1.4%	2.6%	4.4%	5.3%	4.4%	5.0%	6.7%	6.6%	6.9%
Shares Out.	221	286	293	294	310	310	311	309	313	311
Revenue/Share	16.75	14.06	13.58	14.67	14.04	14.65	15.68	16.98	17.38	17.78
FCF/Share	3.37	5.01	5.14	5.32	5.64	5.99	6.22	6.46	8.23	9.19

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.