



# Realty Income (O)

Updated November 9<sup>th</sup>, 2019 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$76	<b>5 Year CAGR Estimate:</b>	2.9%	<b>Volatility Percentile:</b>	16.3%
<b>Fair Value Price:</b>	\$56	<b>5 Year Growth Estimate:</b>	5.0%	<b>Momentum Percentile:</b>	79.2%
<b>% Fair Value:</b>	135%	<b>5 Year Valuation Multiple Estimate:</b>	-5.8%	<b>Growth Percentile:</b>	41.0%
<b>Dividend Yield:</b>	3.6%	<b>5 Year Price Target</b>	\$72	<b>Valuation Percentile:</b>	17.1%
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	D	<b>Total Return Percentile:</b>	19.8%

## Overview & Current Events

Realty Income is a retail real estate focused REIT that has become famous for its successful dividend growth history and monthly dividend payments. Today, the trust owns more than 4,000 properties and is valued at \$24 billion. Realty Income owns retail properties that are not part of a wider retail development (such as a mall), but instead are standalone properties. This means that the properties are viable for many different tenants, including government services, healthcare services, and entertainment. Realty Income was founded in 1969 and is headquartered in San Diego.

Realty Income announced its third quarter earnings results on November 5. The trust reported that it generated revenues of \$374 million during the quarter, which was 10.7% more than the revenues that Realty Income generated during the previous year's quarter. Realty Income's rents at existing properties were responsible for some of the growth in the trust's top line, but investments into new properties were an even larger factor for increased rent generation. Revenues were higher than what the analyst community had forecast, beating the estimate by \$4 million.

Realty Income's funds-from-operations rose substantially versus the prior year's quarter, but since Realty Income also issued new shares to finance some of the acquisitions the trust made, its funds-from-operations-per-share only rose by 2.5% during the third quarter compared to the previous year. Realty Income's funds-from-operations-per-share of \$0.83 were in line with what the analyst community had expected. Realty Income's management increased its guidance for 2019; the REIT now forecasts funds-from-operations of \$3.29 to \$3.34 on a per-share basis.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>AFFOPS</b>	\$1.86	\$1.86	\$2.01	\$2.06	\$2.41	\$2.57	\$2.74	\$2.88	\$3.05	\$3.19	<b>\$3.32</b>	<b>\$4.24</b>
<b>DPS</b>	\$1.71	\$1.72	\$1.74	\$1.77	\$2.15	\$2.19	\$2.27	\$2.39	\$2.53	\$2.64	<b>\$2.72</b>	<b>\$3.39</b>
<b>Shares<sup>1</sup></b>	104	118	133	133	207	225	250	260	284	299	<b>310</b>	<b>345</b>

Realty Income does not generate overly high funds-from-operations growth rates on a per-share basis, but the growth that the REIT is experiencing has been very steady. Adjusted FFO-per-share grew by 6.2% annually between 2009 and 2018, although the growth rate has declined to a lower level of 5% over the last three years.

Realty Income generates its growth through growing rents at existing locations, via contracted rent increases or by leasing properties to new tenants at higher rates, as well as by acquiring new properties. Management invested about \$1.8 billion in new properties during 2018. Realty Income expects to increase its investments in international markets during the next couple of years. It made a deal in the UK during Q1, as part of a \$3 billion spending spree during the first three quarters of 2019. These acquisitions will help drive profits in the future, although they may not pay off immediately. Realty Income's properties are relatively Amazon-proof, as the REIT owns standalone properties that can be used as cinemas, fitness centers, pharmacies, etc. This is in stark contrast to mall REITs, which in some cases have trouble finding tenants for their properties. Realty Income's properties are in demand and will likely remain so. The occupancy rate across Realty Income's portfolio is very high at more than 98%, and the REIT has been growing its same-property rents continuously. Due to the fact that tenants pay a fixed rent, Realty Income's business is not cyclical.

<sup>1</sup> In Millions

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## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
P/AFFO	14.0	18.3	17.4	19.4	15.4	18.7	19.0	19.8	18.7	19.7	22.9	17.0
Avg. Yld.	7.6%	5.4%	5.1%	4.5%	5.0%	5.0%	4.6%	3.9%	4.4%	4.3%	3.6%	4.7%

Realty Income has been a higher-quality retail REIT for many years. The trust's strong track record of dividend growth, as well as its solid operational performance, even during the last financial crisis, are reasons for its above-average valuation. Shares currently look quite expensive, though, even compared to the already relatively high median funds-from-operations multiple. We therefore believe that shares are overvalued at current prices.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	91.9%	92.5%	86.6%	85.9%	89.2%	85.2%	82.8%	83.0%	82.9%	82.8%	81.9%	80.0%

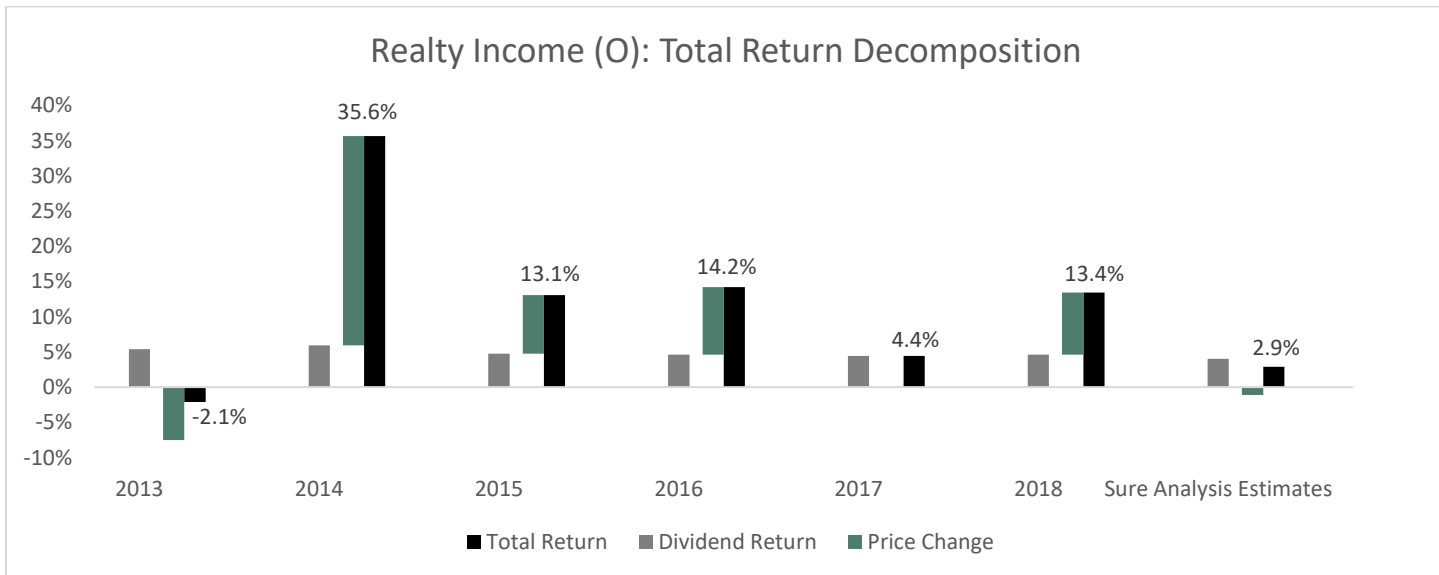
Realty Income has a high dividend payout ratio, but that has been true for all of the last decade. In fact, its current dividend payout ratio is close to the bottom of the historical range. Due to the steady growth of Realty Income's profits, even during the last financial crisis, the dividend looks sustainable, despite the fact that Realty Income pays out more than 80% of its funds-from-operations in the form of dividends.

Realty Income's most important competitive advantage is its world class management team that has successfully guided the trust in the past. Management is highly adept at finding attractive investment opportunities while also growing rents from existing properties, which has been very profitable for its shareholders. Due to the focus on standalone properties that can be used in many different ways, Realty Income should be relatively safe from the so-called retail apocalypse.

## Final Thoughts & Recommendation

Realty Income stands out from other retail REITs thanks to its very consistent dividend and earnings growth track record. The trust is well-recognized among income investors, partially due to making monthly payments. At the current price, Realty Income does not look very attractive, however, as shares trade at a huge premium to what we deem a fair valuation. Due to its high valuation, Realty Income earns a sell recommendation at current prices.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	323	333	412	485	780	934	1023	1103	1216	1328
Gross Profit	316	328	397	463	741	880	968	1040	1146	1262
Gross Margin	98.0%	98.3%	96.3%	95.6%	95.0%	94.2%	94.6%	94.3%	94.3%	95.0%
SG&A Exp.	21	25	31	38	57	51	49	52	58	84
D&A Exp.	90	92	117	148	307	375	409	450	499	540
Operating Profit	205	211	249	278	378	454	509	538	589	638
Operating Margin	63.6%	63.2%	60.5%	57.3%	48.4%	48.6%	49.8%	48.8%	48.5%	48.0%
Net Profit	131	131	157	159	246	271	284	316	319	364
Net Margin	40.7%	39.2%	38.1%	32.8%	31.5%	29.0%	27.7%	28.6%	26.2%	27.4%
Free Cash Flow	227	243	299	326	519	628	694	800	876	941
Income Tax	1	1	1	1	2	3	3	3	6	5

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	2915	3536	4419	5429	9924	11013	11845	13153	14058	15260
Cash & Equivalents	10	18	4	5	10	4	40	9	7	10
Accounts Receivable	10	11	15	22	39	64	82	105	120	145
Goodwill & Int. Ass.	17	43	171	259	951	1055	1050	1097	1210	1214
Total Liabilities	1427	1689	2165	3017	4503	5372	5292	6366	6667	7140
Long-Term Debt	1355	1600	2055	2870	4167	4931	4821	5840	6111	6500
Shareholder's Equity	1150	1509	1917	1803	4776	5218	6136	6371	7372	8089
D/E Ratio	0.91	0.87	0.91	1.19	0.77	0.88	0.74	0.86	0.83	0.80

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	4.4%	4.1%	3.9%	3.2%	3.2%	2.6%	2.5%	2.5%	2.3%	2.5%
Return on Equity	11.1%	9.8%	9.2%	8.6%	7.5%	5.4%	5.0%	5.0%	4.6%	4.7%
ROIC	4.5%	4.2%	4.0%	3.3%	3.3%	2.7%	2.6%	2.6%	2.4%	2.6%
Shares Out.	104	118	133	133	207	225	250	260	284	299
Revenue/Share	3.11	3.15	3.27	3.65	4.07	4.27	4.33	4.32	4.44	4.58
FCF/Share	2.19	2.30	2.37	2.46	2.71	2.87	2.94	3.13	3.20	3.24

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

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