



# Choice Properties REIT (PPRQF)

Updated December 30<sup>th</sup>, 2019 by Samuel Smith

## Key Metrics

<b>Current Price:</b>	\$10.55	<b>5 Year CAGR Estimate:</b>	2.5%	<b>Market Cap:</b>	\$4.3B
<b>Fair Value Price:</b>	\$7.80	<b>5 Year Growth Estimate:</b>	2.7%	<b>Ex-Dividend Date:</b>	12/30/19
<b>% Fair Value:</b>	135%	<b>5 Year Valuation Multiple Estimate:</b>	-6.0%	<b>Dividend Payment Date:</b>	1/15/20
<b>Dividend Yield:</b>	5.3%	<b>5 Year Price Target</b>	\$8.90	<b>Years Of Dividend Growth:</b>	4
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	C	<b>Last Dividend Increase:</b>	2.7%

## Overview & Current Events

Choice Properties Real Estate Investment Trust invests in commercial real estate properties across Canada. The trust has a high-quality real estate portfolio of over 700 properties, which make up over 60 million square feet of gross leasable area (GLA). Throughout 2018, Choice Properties acquired 209 properties totaling 22.7 million square feet of GLA, this process included acquisition of Canadian Real Estate Investment Trust for \$3.7 billion. Choice Properties' portfolio is made up of over 700 properties, including retail, industrial, office, multi-family, and development assets. Over 500 of Choice Properties' investments are to their largest tenant, Canada's largest retailer, Loblaw. This \$4.3 billion market capitalization trust is listed on the Toronto Stock Exchange under the trading symbol 'CHP-UN', or in the United States on the over the counter market under the trading symbol 'PPRQF'.

On November 6th, 2019 Choice Properties released Q3 results for the period ending September 30th, 2019. Same-asset net operating income was up 2.6% during the quarter on a cash basis, and period end occupancy was a robust 97.8%. The trust also recently strengthened its balance sheet by selling off 30 properties. FFO per unit was flattish year-over-year during the quarter, falling slightly from \$0.19 to \$0.18. Tailwinds to FFO included positive leasing activity, growth in net operating income from completed development projects, and \$1.5 million in non-recurring items. However, higher borrowing costs and a higher total of units outstanding weighed on per-unit results. The equity offering just occurred in May, so the full impact of those proceeds has not been factored into results thus far.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>FFO/S</b>	N/A	N/A	N/A	N/A	\$0.70	\$0.67	\$0.70	\$0.74	\$0.85	\$0.76	<b>\$0.78</b>	<b>\$0.89</b>
<b>DPS</b>	N/A	N/A	N/A	N/A	\$0.51	\$0.56	\$0.47	\$0.51	\$0.58	\$0.54	<b>\$0.56</b>	<b>\$0.64</b>
<b>Shares<sup>1</sup></b>	N/A	N/A	N/A	N/A	371.7	395.3	408.1	410.6	413.4	668.2	<b>672.5</b>	<b>690.1</b>

For Choice Properties' primary growth metric, we used funds from operations per share (FFO/S) instead of the typical EPS, since FFO/S gives a much more accurate picture of a REITs performance. Choice Properties only has reportable operations starting in the third quarter of 2013, which explains why the trust's 2013 values are significantly lower. In the last six years, Choice Properties has grown their FFO/S at a rate of 3.2% annually. For our future calculations we used a growth rate of 2.7% given the headwinds to retail and expected slowing of economic growth. We are expecting a 2024 FFO/S of \$0.89, which drives a 5-year price target of \$8.90. To achieve our projected growth rate the trust will need to manage their new growth from recent acquisitions effectively and continue to grow their portfolio.

Choice Properties has been increasing its dividend steadily on a same-currency basis since 2015. The trust kept the dividend at \$0.65 (CAD) annually for their first three years of operations. The trust's average annual dividend growth rate for the last three years has been a respectable 3.9%. Going forward, we expect Choice Properties to increase their dividend with the growth of the trust, which drives a 2024 DPS value of \$0.64 (USD). Note the trust's shares outstanding increased between 2017 and 2018 due to significant acquisition activity.

<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/FFO	N/A	N/A	N/A	N/A	N/A	11.5	12.2	13.5	12.5	11.2	13.5	10.0
Avg. Yld.	N/A	N/A	N/A	N/A	6.2%	6.2%	5.5%	5.3%	5.5%	6.4%	5.3%	7.2%

Choice Properties' average price to funds from operations ratio (P/FFO) has remained around their historic average of 12.2 for much of their six reportable years. Comparing the current P/FFO ratio to their historic average, Choice Properties is significantly overvalued at current prices as we view 10 times FFO as a fair valuation, given their heavy exposure to the out-of-favor retail sector, as well as heavy tenant concentration.

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

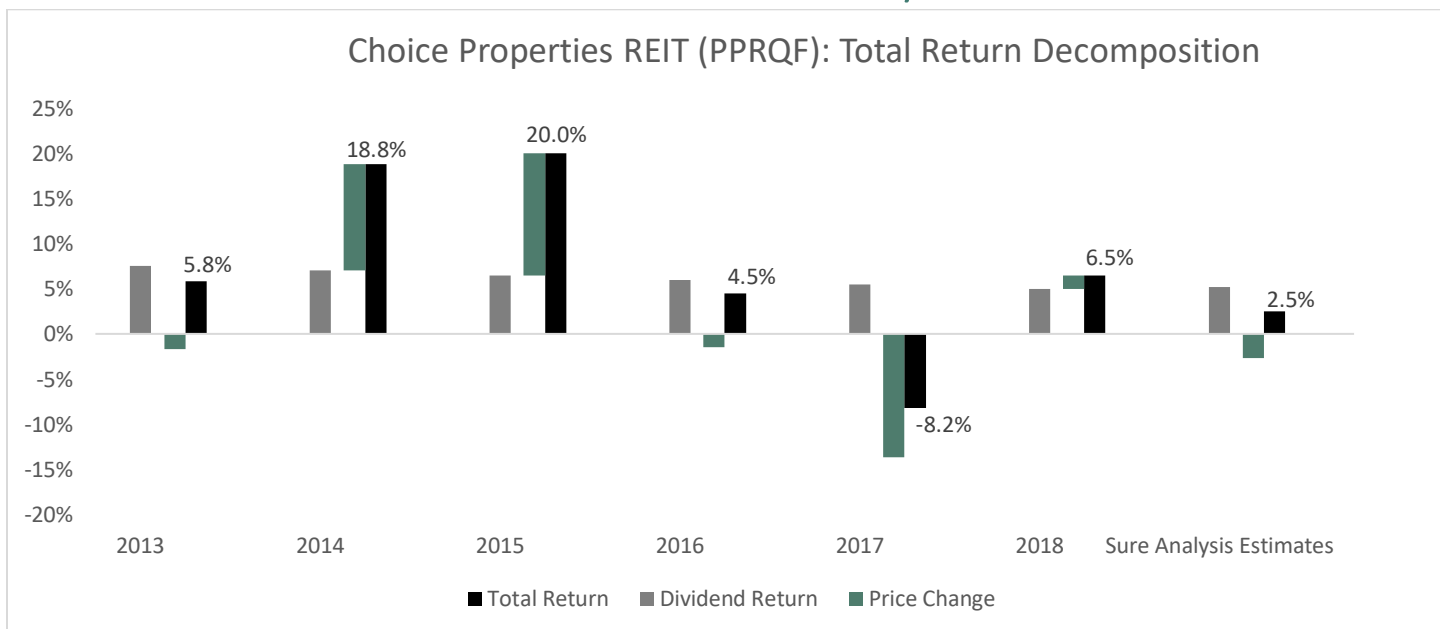
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	N/A	N/A	N/A	N/A	73%	84%	67%	69%	68%	71%	72%	72%

Choice Properties' portfolio has outsized exposure to Loblaw, making the REIT rather dependent on Loblaw's continued operations. One benefit of their strategic alliance with Loblaw is long-term leases, which gives some certainty for future earnings. Choice Properties has not been around for a recessionary period, so to predict how the trust would perform in a recession we observed similar trusts' performance in a recession. The most similar trust we found to Choice Properties is Crombie Real Estate (CRR-U), which also operates a REIT out of Canada with a portfolio designed like Choice Properties' portfolio. During the last recession, The Great Recession in 2008-2009, Crombie Real Estate's FFO/S decreased by nearly 19%, which is a relatively solid performance, all things considered. Overall, we view Choice Properties' dividend as likely safe during a recession thanks in part to its conservative payout ratio for a REIT.

## Final Thoughts & Recommendation

Overall, we expect total returns of 2.5% annually going forward, mainly driven by the 5.3% annual dividend yield and low single-digit FFO-per-share growth rate, and offset by considerable multiple compression. Given the reasonable underwhelming total return potential and the trust's large exposure to retail and a single tenant, we rate it as a sell.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue					319	683	743	784	831	1148
Gross Profit					239	510	551	583	621	834
Gross Margin					75.0%	74.7%	74.1%	74.4%	74.8%	72.6%
SG&A Exp.					12	24	6	39	35	50
D&A Exp.							1	1		
Operating Profit					226	486	520	544	588	788
Operating Margin					71.0%	71.1%	70.0%	69.5%	70.8%	68.6%
Net Profit					67	200	-155	-223	404	650
Net Margin					21.1%	29.2%	-20.9%	-28.5%	48.7%	56.6%
Free Cash Flow					261	472	528	530	504	684
Income Tax										1

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets					7448	8192	8906	9435	9924	15549
Cash & Equivalents					51	1	44	5	6	31
Accounts Receivable					9	9	6	15	21	38
Goodwill & Int. Ass.										30
Total Liabilities					6576	7154	8063	8858	8987	12049
Accounts Payable					211	389	438	473	426	373
Long-Term Debt					3376	3557	3881	4101	4198	7177
Shareholder's Equity					872	1031	835	569	928	3492

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets						2.6%	-1.8%	-2.4%	4.2%	5.1%
Return on Equity						21.0%	-16.6%	-31.8%	54.0%	29.4%
ROIC						5.8%	-4.2%	-5.6%	9.6%	11.3%
Shares Out.					371.7	395.3	408.1	410.6	413.4	668.2
Revenue/Share					0.88	38.09	32.38	34.55	43.25	4.13
FCF/Share					0.72	5.29	5.81	5.73	5.34	2.46

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

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