



Dream Office REIT (DRETF)

Updated March 26th, 2020 by Samuel Smith

Key Metrics

Current Price:	\$13	5 Year CAGR Estimate:	10.4%	Market Cap:	\$793M
Fair Value Price:	\$13.5	5 Year Growth Estimate:	3.1%	Ex-Dividend Date:	3/30/20
% Fair Value:	96%	5 Year Valuation Multiple Estimate:	0.7%	Dividend Payment Date:	4/15/20
Dividend Yield:	8.0%	5 Year Price Target	\$16	Years Of Dividend Growth:	0
Dividend Risk Score:	D	Retirement Suitability Score:	D	Last Dividend Increase:	NA

Overview & Current Events

Dream Office REIT is an open-ended Investment Trust which acquires and manages predominantly office and industrial properties in major urban areas throughout Canada with a focus on downtown Toronto. The trust's portfolio is made of: 68% of operations in Toronto, 14% in Montreal/Ottawa, 8% in Mississauga/North York, 4% in Calgary and 6% in other markets. As of the end of 2018, Dream Office ownership interests included 7.3 million square feet of gross leasable area from 37 properties, which include 34 office properties, two properties under development and one property held for future redevelopment. Dream Office has leases with 641 tenants across Canada, a few of its larger tenants include: Government of Canada (11% of revenue), Government of Ontario (9.3%) and State Street Trust (4.2%). This \$793 billion market capitalization trust is listed on the over-the-counter market in the U.S. under the trading symbol DRETF.

On February 20th, 2020 Dream Office released Q4 results. Diluted FFO per unit came in at \$0.40 for the quarter (up from \$0.39 in the year-ago quarter) and \$1.70 for the year (up from \$1.59 in the year-ago period). This growth was largely due to increases in same-store NOI, improved operational efficiency, and property and construction management fees earned. The strong same-store performance was largely driven by higher occupancy and rental rates in downtown Toronto. The company's asset sales and lease termination fees did serve as a tailwind, however.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
FFO/S	\$2.43	\$2.69	\$2.86	\$2.88	\$2.88	\$1.69	\$2.54	\$2.03	\$1.66	\$1.73	\$1.50	\$1.75
DPS	\$2.20	\$2.20	\$2.20	\$2.23	\$2.24	\$2.24	\$1.56	\$1.25	\$1.00	\$1.03	\$1.04	\$1.16
Shares¹	45.9	66.2	97.6	103.4	107.9	107.9	104.8	73.7	59.4	57.8	57.8	51.8

Instead of EPS, we used funds from operations per share (FFO/S) as Dream Office's primary growth metric. We used FFO/S, because it more accurately communicates a REIT's true performance, as EPS depreciates investment properties over time, however many investment properties actually increase in value over time. Dream Office's FFO/S has been very volatile over the last decade from inconsistent funds-from-operations, and also a rapidly increasing share count to 2014-2015, and then decreasing by almost 50% from years 2016-2018. Since 2016, the trust has been engaged in heavy buybacks, dramatically reducing the shares outstanding.

Going forward we expect disruption from the coronavirus to result in a global recession that will weigh heavily on results this year and next before fundamentals rebound in the years following. Given the company's considerable exposure to high quality assets in Toronto and fairly low payout ratio, it should be able to weather the storm better than some peers.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
P/FFO	12.4	12.1	13.1	10.0	8.8	10.3	7.7	10.9	13.4	12.8	8.7	9.0
Avg. Yld.	7.3%	6.7%	5.9%	7.8%	8.9%	12.9%	7.7%	4.5%	4.5%	4.7%	8.0%	7.4%

¹ In millions

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Dream Office's average price to funds from operations ratio (P/FFO) has deviated significantly around its historic average of 10.6. Comparing current average P/FFO ratios to its historic average, Dream Office is undervalued at current prices. However, given the uncertainty facing the global economy right now, we are lowering our fair value estimate to 9 times FFO. We therefore expect valuation multiple compression to pose a small tailwind to total returns moving forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	91%	82%	77%	77%	78%	133%	61%	62%	60%	60%	69%	66%

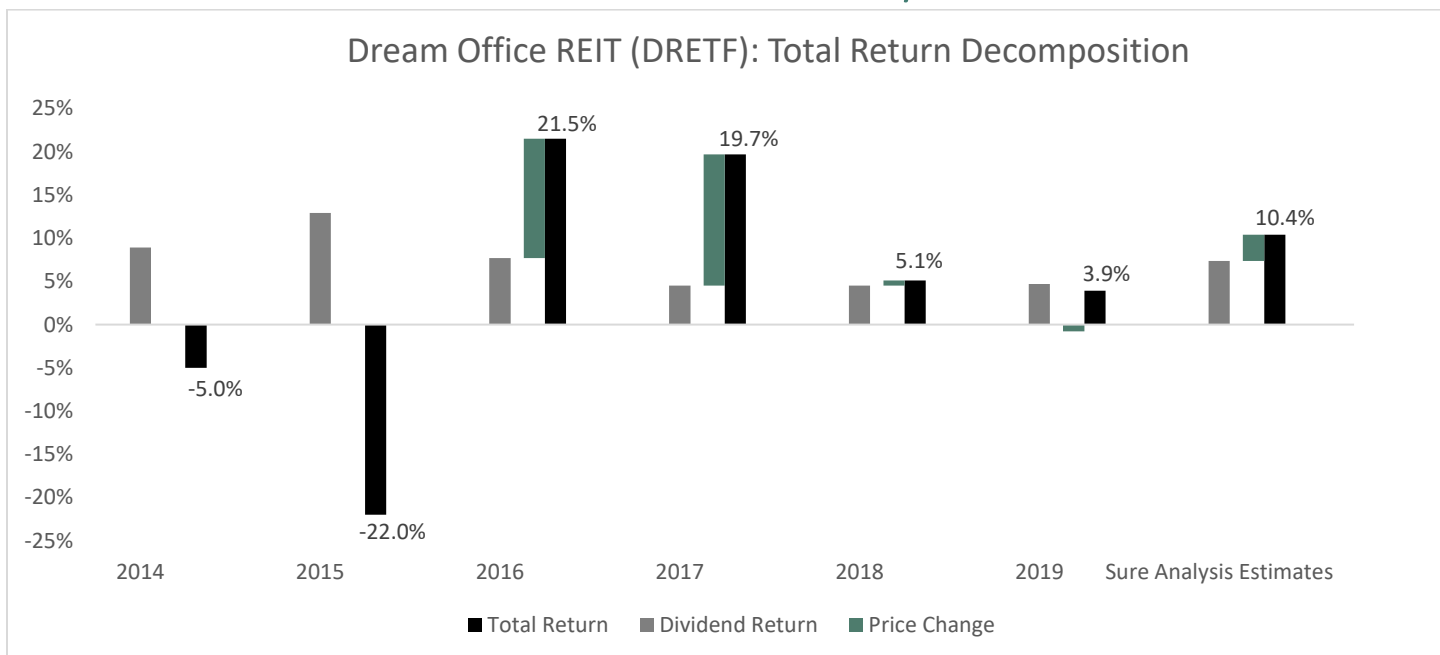
Dream Office has integrated best practices into its environmental platform since 2011. The trust has been proactively trying to reduce its environmental footprint by decreasing its resource consumption and greenhouse gas emissions. The trust also has a goal to use less energy and water to decrease waste to the environment. One way the trust cuts down on resources is by proactively developing and maintaining high-quality, energy-efficient buildings. All of Dream Office's buildings over 100,000 square feet are BOMA BEST Sustainable Buildings certified, which means the buildings are recognized in excellence in energy and environmental management and performance in commercial real estate.

Dream Office has not been around for a recession, but historically companies who operate predominantly office properties do not fare well in recessions. While local businesses are deteriorating, companies would be more likely to close offices rather than start new leases, so in a recession in the Canadian economy Dream Global should be adversely affected from potential losses of current and future tenants.

Final Thoughts & Recommendation

Overall, we expect total returns of 10.4% annually, mainly driven by its 8% dividend yield, followed by a 3.1% FFO-per-share growth rate, and a very slight boost from multiple expansion. We believe the REIT's quality diversified portfolio will enable it to weather the current storm. As a result, we rate Dream Office REIT as a buy at current prices, though more conservative investors may want to look elsewhere given that the business model is not ideally suited to recessions.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	239	375	608	687	705	691	664	474	285	229
Gross Profit	144	216	349	392	402	388	369	262	155	128
Gross Margin	60.0%	57.6%	57.3%	57.0%	56.9%	56.1%	55.5%	55.3%	54.3%	55.7%
SG&A Exp.	11	14	21	24	24	12	12	45	16	13
D&A Exp.	1	1	2	5	11	15	21	22	17	17
Operating Profit	133	202	325	365	374	372	353	206	133	113
Operating Margin	55.6%	53.8%	53.5%	53.1%	53.0%	53.9%	53.2%	43.5%	46.7%	49.2%
Net Profit	216	401	291	445	159	-55	-880	135	158	117
Net Margin	90.2%	107%	47.9%	64.8%	22.6%	-8.0%	-132%	28.4%	55.3%	51.2%
Free Cash Flow	-683	82	115	163	171	146	97	51	28	46
Income Tax		0	2	0	1	2	2	-4	0	0

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	2583	4466	6353	7125	7030	6763	5487	3322	3123	2,912
Cash & Equivalents	109	112	24	31	11	2	8	97	9	95
Accounts Receivable	3	8	11	8	6	3	2	6	8	4
Goodwill & Int. Ass.		0	64	63	61	8	7	2	1	1
Total Liabilities	1368	2349	3057	3402	3252	3281	3115	1586	1626	1,433
Accounts Payable	30	6	7	10	3	3	1	4	4	9
Long-Term Debt	1202	2125	2778	3149	3097	3011	2650	1368	1406	1,150
Shareholder's Equity	1215	2117	3296	3723	3778	3482	2372	1736	1497	1,478
D/E Ratio	0.99	1.00	0.84	0.85	0.82	0.86	1.12	0.79	0.94	0.78

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	11.0%	11.4%	5.4%	6.6%	2.3%	-0.8%	-14.4%	3.1%	4.9%	3.9%
Return on Equity	26.8%	24.1%	10.8%	12.7%	4.2%	-1.5%	-30.1%	6.6%	9.8%	7.9%
ROIC	11.8%	12.0%	5.6%	6.9%	2.3%	-0.8%	-15.3%	3.3%	5.3%	4.2%
Shares Out.	45.9	66.2	97.6	103.4	107.9	107.9	104.8	73.7	59.4	57.8
Revenue/Share	4.85	5.66	6.23	6.64	6.53	6.41	6.34	6.43	4.80	4.07
FCF/Share	-13.83	1.24	1.18	1.58	1.58	1.36	0.93	0.69	0.48	0.82

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

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