Simon Property Group (SPG)

Updated March 22nd, 2020 by Samuel Smith

Key Metrics

Current Price:	$59	**5 Year CAGR Estimate:**	25.8%	**Market Cap:**	$21B
Fair Value Price:	$100	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	5/14/20[1]
% Fair Value:	59%	**5 Year Valuation Multiple Estimate:**	11.1%	**Dividend Payment Date:**	5/29/20[2]
Dividend Yield:	13.9%	**5 Year Price Target**	$140	**Years of Dividend Growth:**	10
Dividend Risk Score:	D	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	2.4%

Overview & Current Events

Simon Property Group is a real estate investment trust (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 $5.8 billion in annual revenue and has a market capitalization of $21 billion.

Simon reported Q4 earnings on 2/4/20. FFO per share came in at $3.29, up from $3.20 in the year-ago quarter. Revenue also increased to $1.49B from $1.46B in the year-ago quarter. U.S. malls and premium outlets reported retailer sales per square foot of $693, which increased by 4.8% year-over-year. Leasing spreads were also very strong, increasing by 14.4%. Comparable property NOI increased by 1.7%. Looking ahead, management expects FFO per share of $12.33 at the midpoint, down from $12.37 in 2019. That being said, due to closures from the coronavirus pandemic and additional pressures on already stressed tenants, we expect FFO per share to come well short of that guidance.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
FFO/Shr	$5.01	$6.89	$7.98	$8.85	$8.90	$9.86	$10.49	$11.21	$12.13	$12.37	***$10.00***	***$14.00***
DPS	$2.60	$3.50	$4.10	$4.65	$5.15	$6.05	$6.50	$7.15	$7.90	$8.20	***$8.20***	***$9.79***
Shares[3]	293	294	310	310	311	309	313	311	309	306	***306***	***295***

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 steady performance continuing. Recent years have seen a growth rate of ~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 high, hovering around 96% in recent quarters. It also charges more than $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 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 should rise in line with FFO, and we see it hitting $9.79 by 2025. Another tailwind to the per-share growth thesis is that Simon is one of the few REITs with the balance sheet and free cash flow generation capacity to repurchase shares. Given the current discount to NAV in the shares, doing this will unlock significant value for shareholders while also growing FFO-per-share at a more rapid pace, and thereby helping to offset the drag on growth from the rise of e-commerce.

[1] Estimate
[2] Estimate
[3] In millions

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/FFO	17.6	16.5	18.7	18.4	19.0	19.1	19.2	15.1	13.9	11.9	***5.9***	***10.0***
Avg. Yld.	3.0%	3.1%	2.7%	2.9%	3.0%	3.2%	3.2%	4.2%	4.7%	5.6%	***13.9%***	***6.8%***

Simon's valuation has been remarkably steady for much of the past decade and today, at just 5.9 times this year's FFO estimate, the stock is extremely cheap. We see fair value at 10.0 times FFO, implying a massive annual tailwind to total returns in the years to come. We've moved our estimate of fair value down since the last report, reflecting concerns raised by management over retail tenants, as well as overall slowing growth due to the coronavirus uncertainty.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	52%	51%	51%	53%	58%	61%	62%	64%	65%	66%	***82.0%***	***68.4%***

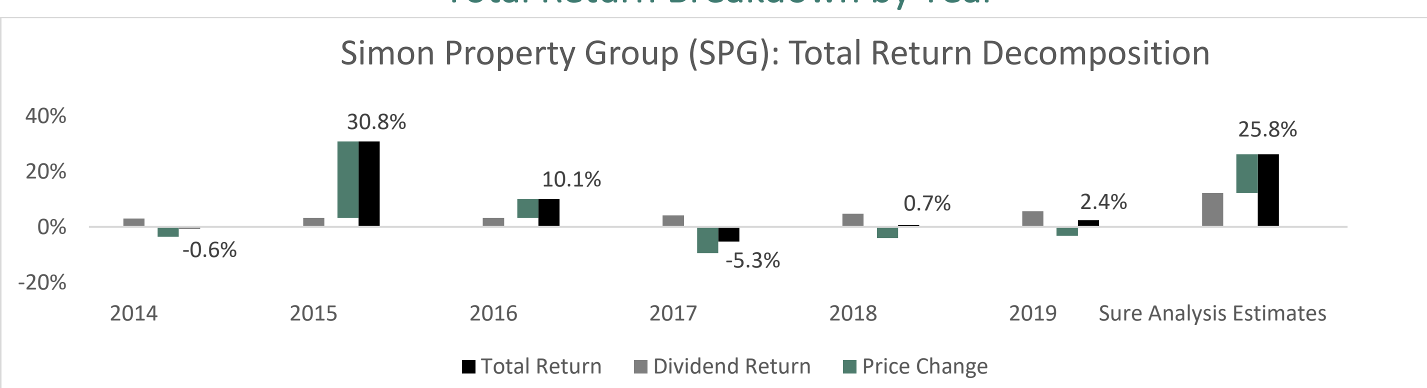
Simon's quality metrics have been very stable in the past decade as the trust has kept operating metrics such as balance sheet leverage and interest coverage, in a fairly narrow range. Profitability has improved over time as the trust's strength has afforded it the ability to raise prices, but we believe 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 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. Another advantage is its low cost of capital that comes from its A-rated balance sheet, enabling it to invest in ways that competitors cannot afford to. That being said, it is not immune to recession as it did cut its dividend during the last downturn. However, despite the cut, its overall business held up fairly well during that period should be able to again. It is also one of the best positioned retail REITs to weather the impact of e-commerce on bricks-and-mortar retail stores.

Final Thoughts & Recommendation

Overall, we forecast Simon to produce robust 25.8% total annualized returns in the coming years. We continue to rate the stock a buy as Simon offers investors an attractively priced stock with a high yield and distribution growth prospects. While the balance sheet is A-rated, investors should remember that it did cut its dividend during the last recession and that it faces substantial headwinds and uncertainty at this time. That being said, its strong balance sheet, world-class management, and high-quality real estate portfolio should enable it to rebound fairly quickly once the current headwinds pass. Given, its conservative payout ratio, we merely expect a dividend freeze this year.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	3958	4306	4256	4544	4871	5266	5435	5539	5658	5,755
Gross Profit	3095	3387	3456	3706	3988	4306	4464	4559	4650	4,734
Gross Margin	78.2%	78.6%	81.2%	81.6%	81.9%	81.8%	82.1%	82.3%	82.2%	82.2%
SG&A Exp.	228	282	291	319	355	350	366	338	334	185
D&A Exp.	1016	1112	1301	1333	1286	1239	1328	1357	1350	1,394
Operating Profit	1816	1943	2000	2189	2385	2669	2721	2802	2911	2,908
Operating Margin	45.9%	45.1%	47.0%	48.2%	49.0%	50.7%	50.1%	50.6%	51.5%	50.5%
Net Profit	617	1025	1434	1320	1409	1828	1839	1948	2440	2,102
Net Margin	15.6%	23.8%	33.7%	29.0%	28.9%	34.7%	33.8%	35.2%	43.1%	36.5%
Free Cash Flow	1499	1560	1711	1860	1934	2004	2574	2862	2969	2,932
Income Tax	4	12	16	40	28	20	30	23	37	30

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	24857	26217	32587	33325	29532	30565	31104	32258	30686	31,232
Cash & Equivalents	797	799	1185	1691	612	701	560	1482	514	669
Acc. Receivable	N/A	487	521	520	580	625	665	743	764	832
Goodwill & Int.	N/A	296	507	376	312	276	285	209	151	96
Total Liabilities	19224	20673	25694	26502	23581	25349	26144	28019	26889	28,320
Accounts Payable	N/A	1092	1374	1223	1260	1324	1214	1269	1317	1,391
Long-Term Debt	17474	18446	23113	22670	20853	22417	22977	24564	23238	24,096
Total Equity	4785	4605	5866	5805	5049	4428	4267	3643	3254	2,484
D/E Ratio	3.62	3.97	3.91	3.88	4.09	5.01	5.33	6.66	7.05	9.54

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	2.4%	4.0%	4.9%	4.0%	4.5%	6.1%	6.0%	6.1%	7.8%	6.8%
Return on Equity	13.4%	21.8%	27.4%	22.6%	26.0%	38.6%	42.3%	49.3%	70.8%	73.3%
ROIC	2.6%	4.4%	5.3%	4.4%	5.0%	6.7%	6.6%	6.9%	8.7%	7.8%
Shares Out.	293	294	310	310	311	309	313	311	309	306
Revenue/Share	13.58	14.67	14.04	14.65	15.68	16.98	17.38	17.78	18.27	18.69
FCF/Share	5.14	5.32	5.64	5.99	6.22	6.46	8.23	9.19	9.59	9.52

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