Innovative Industrial Properties (IIPR)

Updated November 10th, 2020 by Nikolaos Sismanis

Key Metrics

Current Price:	$154	**5 Year CAGR Estimate:**	20.0%	**Market Cap:**	$3.41B
Fair Value Price:	$113	**5 Year Growth Estimate:**	25.0%	**Ex-Dividend Date:**	12/30/20
% Fair Value:	137%	**5 Year Valuation Multiple Estimate:**	-6.0%	**Dividend Payment Date[1]:**	01/15/21
Dividend Yield:	2.9%	**5 Year Price Target**	$344	**Years Of Dividend Growth:**	4
Dividend Risk Score:	F	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	64%[2]

Overview & Current Events

Innovative Industrial Properties, Inc. is a single-use "specialty REIT" that exclusively focuses on owning properties used for the cultivation and production of marijuana. Because the industry is in the midst of a legal transition, there are constraints on capital available to businesses engaged in the marijuana business. IIPR went public in a "loophole" time period. No other cannabis-related REITs have been approved for listing on the NYSE or the NASDAQ. Having the fortunate status as the only publicly traded marijuana REIT in the US has led to stunning returns and portfolio growth. The $3.41 billion trust owns 63 properties in 15 states. Amid the cannabis boom over the past few years, as well as its exclusivity in terms of the listing, which gives the trust access to public markets, Innovate Industrial Properties is currently the fastest-growing REIT in the world.

On November 4th, 2020, the trust announced its Q3 2020 earnings for the period ending September 30th, 2020. For the quarter, revenues and normalized AFFO/share were to $34.3 million and $1.28, an increase of 197%, and 48.2%, respectively. The trust delivered another quarter of explosive growth due to acquiring five new properties, totaling approximately 448,000 rentable square feet located in Florida, Michigan, and New Jersey. The trust's rental collections were robust, despite COVID-19, due to its tenants facing increasing marijuana production demand, amid the stay-at-home economy. IIP collected 100% of contractual rent due for the quarter, as well as for the month of October. Management also managed to collect all deferred rents from the three tenants mentioned in our previous report, further adding to its already exceptional results. The trust raised its quarterly dividend for a third time during the year, tangibly rewarding its stockholders in line with its performance trajectory.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
AFFO	--	--	--	--	--	--	$(0.62)	$ 0.67	$ 1.34	$ 3.27	***$4.70***	***$14.34***
DPS	--	--	--	--	--	--	--	$0.55	$1.20	$2.83	***$4.40***	***$10.95***
Shares[3]	--	--	--	--	--	--	1	3.4	7.3	10.7	***21.5***	***125***

Industrial Innovating properties has been snowballing, growing AFFO/share dramatically since the trust's IPO. Over the past three years, not a single quarter has seen less AFFO/share than the one before it, fueled by non-stop acquisitions. To capitalize on the growth of the cannabis sector, IIP acquired 35 properties in 2019 alone. With the schedule-1 drug being decriminalized in one state after the other, we expect growth to be sustained in the medium term. In line with its AFFO growth, management has been raising the dividend once every two quarters consistently. Distributions grew by an astonishing 135.8% in FY2019. We retain our AFFO/share and DPS medium-term CAGR at 25% and 20%, respectively, to be prudent. As we mentioned and was indeed the case, it's highly likely that these figures will be much more attractive, considering the trust's current triple-digit growth rates. Still, the trust has a short trading history, and its acquisition-driven strategy may see availability headwinds in the future, hence our more reserved estimates.

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[1] Estimated dates based on past dividend dates.

[2] IIP grows its DPS on a quarterly basis or semi-annual basis. YoY DPS growth is 64%. Its latest QoQ growth amounts to 10.3%.

[3] Share count is in millions.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/FFO	--	--	--	--	--	--	--	47.76	12.16	16.6	***32.8***	***24.0***
Avg. Yld.	--	--	--	--	--	--	--	3.4%	3.3%	2.8%	***2.9%***	***3.2%***

Despite shares currently trading at a 52-week high, the valuation of 32.8X FY2020's expected AFFOs, is quite reasonable, considering the trust's rapid expansion. Shares are currently yielding around 2.9%, which is quite high for a trust undergoing such a rapid growth phase. To reflect IIP's acceleration of its growth rate, we are raising our future fair valuation multiple from 18 to 24. The trust's growth exceeded our slowdown expectations, and rental collection could not have been reported any better, despite its tenants' start-up nature. Future positive valuation drivers include the Federal legalization of Cannabis through The MORE Act, as well. The bill would make marijuana federally legal across all states and remove the plant's categorization as a schedule-1 drug. The recent legalization of cannabis in Montana during the quarter is another step towards such a case.

Safety, Quality, Competitive Advantage, & Recession Resiliency

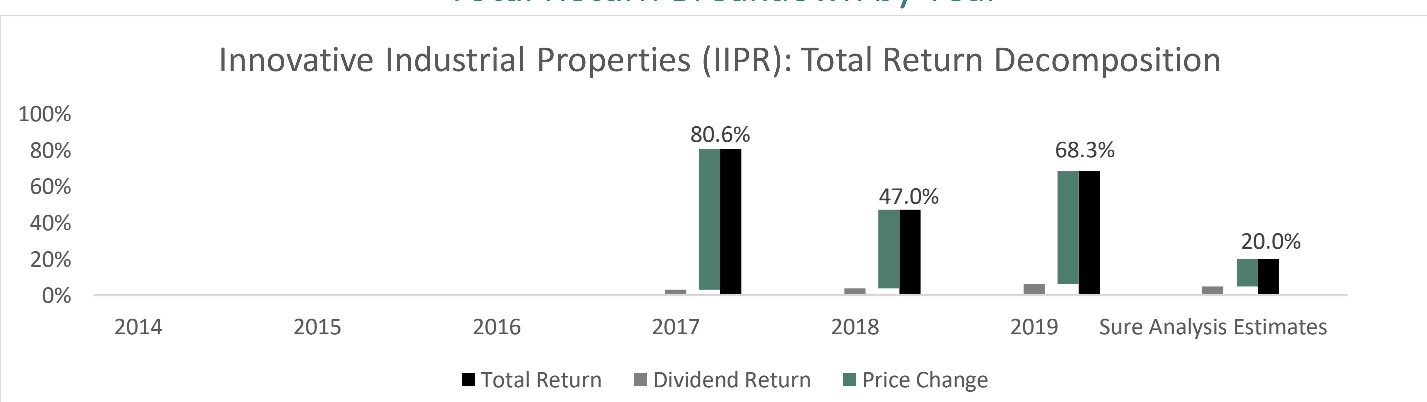
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	--	--	--	--	--	--	--	82%	90%	87%	***94%***	***76%***

The trust's seemingly high payout ratio is non-meaningful as AFFOs proliferate and only reflect this year's cash flows. Being the only listed cannabis REIT, the trust has a massive moat. With access to public markets, management can issue debt and equity much cheaper than its few private competitors. IIPR can build more durable and sustainable relationships with tenants as it possesses higher credibility and transparency. Despite the headwinds COVID-19 caused in many industries, IIPR was barely affected, continuing its proven acquisition-based growth model. However, because of how new the cannabis sector is, its recession resiliency is untested to the passage of time and remains to be seen.

Final Thoughts & Recommendation

Innovative Industrial Properties is a genuinely unique investment case. Instead of guessing which cannabis-producing stock will be a long-term winner, investors can profit off of what every producer needs, which is specialized property. This way, the sector's growth can be taken advantage of, while benefiting from the consistent cash flows from renting IIP's facilities. We believe that shares propose a special investment case that offers both the potential for substantial capital gains while stockholders get to enjoy a rapidly growing stream of distributable income. We expect the stock to deliver double-digit, market-beating returns of 20% over the next few years, despite us estimating an over-protective valuation compression ahead. Returns are likely to be higher, powered by the trust's unparalleled growth.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	---	---	---	---	---	---	$0.32	$6.42	$14.79	$44.67
Gross Profit	---	---	---	---	---	---	$0.23	$6.30	$14.34	$43.35
Gross Margin	---	---	---	---	---	---	72.9%	98.2%	97.0%	97.1%
SG&A Exp.	---	---	---	---	---	---	$0.83	$5.50	$6.38	$9.82
D&A Exp.	---	---	---	---	---	---	$0.03	$0.92	$2.63	$8.60
Operating Profit	---	---	---	---	---	---	-$0.69	-$0.11	$5.34	$24.94
Operating Margin	---	---	---	---	---	---	-213.4%	-1.7%	36.1%	55.8%
Net Profit	---	---	---	---	---	---	-$4.39	-$0.07	$6.99	$23.48
Net Margin	---	---	---	---	---	---	-1368.2%	-1.1%	47.2%	52.6%
Free Cash Flow	---	---	---	---	---	---	-$28.34	$5.02	$15.69	$44.93
Income Tax	---	---	---	---	---	---	$0.32	$6.42	$14.79	$44.67

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	---	---	---	---	---	---	$63.33	$80.03	$281.47	$745.86
Cash & Equivalents	---	---	---	---	---	---	$33.00	$11.76	$13.05	$82.24
Total Liabilities	---	---	---	---	---	---	$2.89	$6.48	$17.17	$197.85
Accounts Payable	---	---	---	---	---	---	$0.07	$1.08	$4.40	$28.39
Long-Term Debt	---	---	---	---	---	---	$0.00	$0.00	$0.00	$134.65
Shareholder’s Equity	---	---	---	---	---	---	$60.44	$59.54	$250.28	$534.00
D/E Ratio	---	---	---	---	---	---	0.00	0.00	0.00	0.25

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	---	---	---	---	---	---	---	-0.1%	3.9%	4.6%
Return on Equity	---	---	---	---	---	---	-14.5%	-0.1%	4.5%	6.0%
ROIC	---	---	---	---	---	---	---	-0.1%	4.1%	5.0%
Shares Out.	---	---	---	---	---	---	0.96	3.38	7.29	10.68
Revenue/Share	---	---	---	---	---	---	$0.33	$1.90	$2.03	$4.18
FCF/Share	---	---	---	---	---	---	-$29.43	$1.49	$2.15	$4.21

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