



Essex Property Trust Inc. (ESS)

Updated February 16th, 2021 by Samuel Smith

Key Metrics

Current Price:	\$270	5 Year CAGR Estimate:	3.0%	Market Cap:	\$18.3B
Fair Value Price:	\$230	5 Year Growth Estimate:	3.3%	Ex-Dividend Date:	03/31/21 ¹
% Fair Value:	117%	5 Year Valuation Multiple Estimate:	-3.3%	Dividend Payment Date:	04/15/21 ²
Dividend Yield:	3.1%	5 Year Price Target	\$270	Years Of Dividend Growth:	26
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase:	6.5%

Overview & Current Events

Essex Property Trust Inc. (ESS) was founded in 1971 and became a publicly traded real estate investment trust (REIT) in 1994. The trust invests in west coast multifamily residential properties where it engages in development, redevelopment, management and acquisition of apartment communities and a few other select properties. Essex has ownership interests in 245 apartment communities consisting of over 60,000 apartment homes. The trust has more than 1,800 employees and produces approximately \$1.5 billion in revenue.

On February 4th, 2021 Essex reported fourth quarter results. Core FFO-per-diluted share declined by 12.5% to \$3.15 during Q4. Same-property gross revenue fell by 8.0% and same-property net operating income fell by 12.7% from Q4 2019. One apartment community was sold during the quarter for a contract price of \$60 million. The company committed \$206 million in structured finance investments. ESS also repurchased a total of \$46.3 million worth of shares of common stock in the fourth quarter.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
FFO	\$5.74	\$6.71	\$7.59	\$7.89	\$9.72	\$11.12	\$11.91	\$12.76	\$13.55	\$12.90	\$12.77	\$15.00
DPS	\$4.16	\$4.40	\$4.84	\$5.11	\$5.76	\$6.40	\$7.00	\$7.44	\$7.80	\$8.31	\$8.36	\$9.00
Shares³	33.9	36.4	37.4	63.7	65.4	65.5	66.1	65.9	66.0	65.6	66.0	66.0

Essex Property Trust has achieved impressive growth for several decades on the back of the strong west coast property market, but growth has been slowing in the past few years. Like many REITs, the trust historically has issued new shares to fund rapid growth. In 2014, the trust merged with BRE Properties, which drastically increased the trust's size and shares outstanding. Since then, the trust's rate of growth has slowed, and they have maintained a more static number of shares outstanding.

Consensus analyst expectations prior to the COVID-19 outbreak were for mid-single digit growth in FFO per share between in the coming years. We conservatively estimate mid-single-digit growth over the next five years from 2021 through 2026, following the recent trend of slowing growth and because several major west coast cities have seen a recent dip or flattening out of property values, which could put pressure on rent prices.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/FFO	22.2	22.2	20.4	23.1	23.1	19.4	20.5	18.9	22.1	19.8	21.3	18.0
Avg. Yld.	3.3%	3.0%	3.1%	2.8%	2.6%	3.0%	2.9%	3.1%	2.6%	3.3%	3.1%	3.3%

¹ Estimate

² Estimate

³ Share count is in millions.

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Essex Property Trust currently trades for 21.3x FFO, which is below its recent historical average. While it is reasonable to pay up for a trust of this level of quality, we consider the historical valuation to be rich compared to the trust’s growth rate and current headwinds. Therefore, we believe the fair value should be closer to 18 times FFO moving forward, making the trust overvalued at present.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	72%	66%	64%	65%	59%	58%	59%	58%	58%	64%	65%	60%

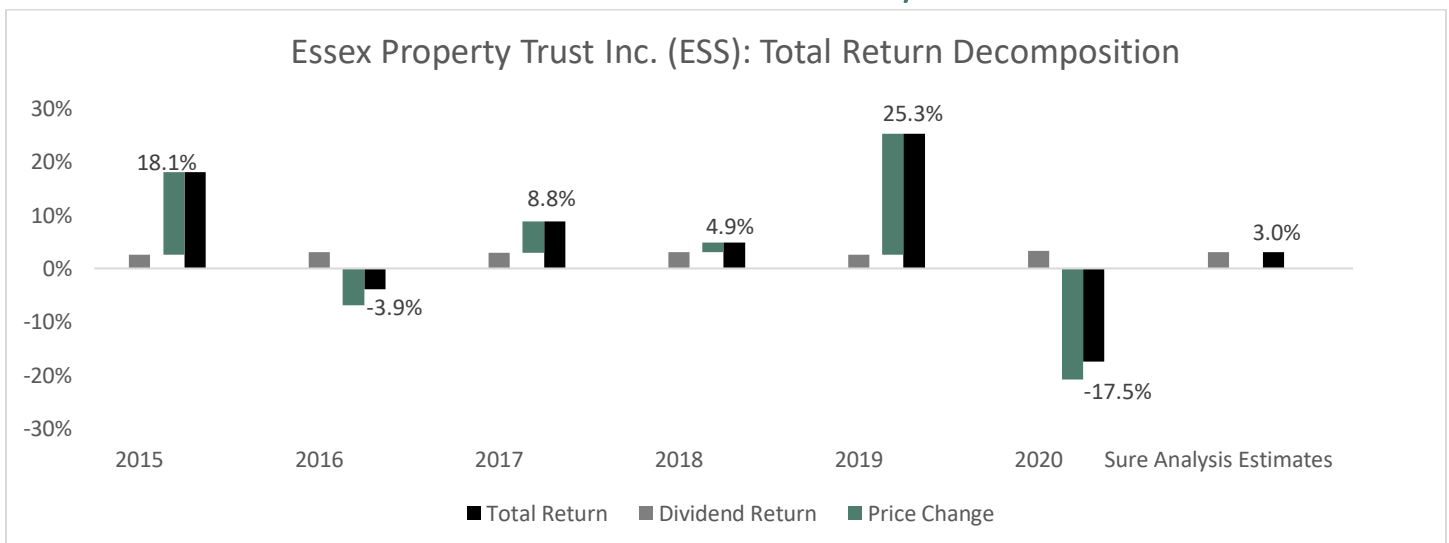
Essex Property Trust is a high-quality apartment REIT that has raised its dividend for 26 consecutive years from the time it first became a publicly traded trust. Real estate has a natural moat and Essex’s exposure to high-value cities with strong technology cultures further widens that moat. However, apartments generally have a more elastic supply than single family homes, which offsets some of that protection. This was shown during the previous recession, when the trust’s FFO fell, but not by an extreme amount, and Essex was able to continue raising its dividend.

The trust has a solid BBB+ credit rating and currently has an interest coverage ratio of over 450%, which provides a very large margin compared to their debt covenant requirement of 150% or higher. Net debt to adjusted EBITDA is ~5.5x, which is solid. Like many real estate businesses, Essex Property Trust uses a substantial but fair amount of leverage and maintains a relatively safe balance sheet. Its weighted average interest rate is under 4.0%, which is quite low, reflecting the trust’s strong credit metrics.

Final Thoughts & Recommendation

Essex Property Trust has been a strong outperformer in terms of total returns since it went public in 1994 due to a combination of good management and a tailwind from the fast-growing west coast property market on the back of a strong technology industry in the region. However, property values in popular west coast cities are now some of the highest in the country and are showing some signs of peaking, or at least slowing growth. The growth rate of Essex Property Trust has been slowing lately, and the trust has at least moderate downside risk as the country continues to grapple with COVID-19 related headwinds. With 3% expected annualized total returns over the next half decade, we rate shares as a sell, though they remain attractive for conservative dividend growth investors given the solid yield, dividend growth track record, strong balance sheet, and sustainable payout ratio.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	467	535	611	971	1,194	1,294	1,364	1,400	1,460	1,496
Gross Profit	305	363	413	658	831	905	958	984	1,030	1,021
Gross Margin	65.3%	67.8%	67.7%	67.8%	69.6%	69.9%	70.3%	70.3%	70.5%	68.2%
SG&A Exp.	21	25	27	41	40	41	41	53	54	65
D&A Exp.	164	171	194	361	453	442	469	480	484	
Operating Profit	123	169	194	257	337	423	448	450	492	430
Operating Margin	26.3%	31.6%	31.8%	26.5%	28.2%	32.7%	32.9%	32.2%	33.7%	28.7%
Net Profit	47	125	156	122	232	415	433	390	439	569
Net Margin	10.1%	23.4%	25.6%	12.6%	19.4%	32.1%	31.8%	27.9%	30.1%	38.0%
Free Cash Flow	183	222	248	414	561	652	697	745	817	

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	4,037	4,847	5,187	11,527	12,008	12,217	12,496	12,384	12,705	12,936
Cash & Equivalents	13	19	18	26	30	65	45	134	70	84
Total Liabilities	2,479	2,963	3,184	5,391	5,671	5,925	6,099	5,990	6,302	6,753
Accounts Payable	48	65	67	135	131	138	128	127	158	
Long-Term Debt	2,361	2,819	3,034	5,081	5,319	5,563	5,689	5,606	5,809	6,252
Shareholder's Equity	1,364	1,691	1,811	5,949	6,164	6,192	6,277	6,267	6,220	6,000
D/E Ratio	1.64	1.59	1.61	0.84	0.85	0.90	0.91	0.89	0.93	1.04

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	1.2%	2.8%	3.1%	1.5%	2.0%	3.4%	3.5%	3.1%	3.5%	4.4%
Return on Equity	3.8%	8.2%	8.9%	3.1%	3.8%	6.7%	6.9%	6.2%	7.0%	9.3%
ROIC	1.2%	2.9%	3.2%	1.5%	2.0%	3.5%	3.6%	3.2%	3.6%	4.6%
Shares Out.	33.9	36.4	37.4	63.7	65.4	65.5	66.1	65.9	66.0	65.6
Revenue/Share	14.33	15.24	16.35	17.13	18.36	19.73	20.70	21.19	22.14	22.81
FCF/Share	5.60	6.32	6.64	7.31	8.62	9.94	10.57	11.27	12.40	

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

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