Equity Residential (EQR)

Updated March 1st, 2021 by Samuel Smith

Key Metrics

Current Price:	$65.4	**5 Year CAGR Estimate:**	3.1%	**Market Cap:**	$25.3B
Fair Value Price:	$50.0	**5 Year Growth Estimate:**	5.1%	**Ex-Dividend Date:**	03/01/21[1]
% Fair Value:	131%	**5 Year Valuation Multiple Estimate:**	-5.3%	**Dividend Payment Date:**	04/04/21[2]
Dividend Yield:	3.7%	**5 Year Price Target**	$64	**Years Of Dividend Growth:**	0
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	N/A

Overview & Current Events

Equity Residential (EQR) is a $25.3 billion multifamily REIT that owns a portfolio of 303 apartment communities with over 78,000 units, with more in development. The trust's strategy consists of owning large, high-quality properties in the urban and suburban submarkets of Southern California, San Francisco, Washington, D.C., New York, Seattle, and Boston. It was formed 50 years ago as a property management partnership between two individuals and has grown into a large multifamily equity business today.

EQR reported Q4 results on 02/04/21. Normalized FFO per share came in at $0.76, down from $0.91 in the year-ago quarter. Occupancy stood at 94.2% in Q4. Pricing trends continued improving and the company collected 97% of its expected residential revenues in Q4. To meet its obligations on its $750 million 4.625% unsecured notes, EQR used the proceeds from its sale, cash on hand and borrowings under commercial paper program by discharging them pursuant to their indenture. That said, the company strengthened its balance sheet as they paid down nearly $1 billion in the aggregate in debt in 2020. EQR also reported that they sold a 679-unit Vantage Point apartment property located in downtown San Diego for approximately $312.5 million at a 4.1% disposition yield, generating an unlevered IRR of 8.8% over the company's ten-year ownership period. Meanwhile, Q4 revenue decreased by 10.3% to $613.4 million year-over-year.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
FFO	$2.58	$2.76	$2.99	$3.17	$3.46	$3.09	$3.13	$3.25	$3.47	$3.26	***$2.93***	***$3.75***
DPS	$1.58	$1.78	$1.85	$2.00	$2.21	$2.02	$2.02	$2.16	$2.27	$2.41	***$2.43***	***$2.50***
Shares[3]	295	320	354	378	381	382	383	384	384	384	***384***	***387***

Over the past decade, EQR has generated a solid ~3.4% Core FFO/share growth rate. This is even more impressive when you consider that the trust downsized and deleveraged, which led to a decline in FFO/share between 2015 and 2016. Since the deleveraging, the growth rate has gradually accelerated until this year's COVID-19 disruption. This shows that the trust continues to deploy capital effectively while managing its costs, despite rising margin pressures from inflation and plenty of competing new supply hitting key markets.

These positive trends are due to the fact that when the trust downsized several years ago; it sold out of its inland markets that have very low barriers to entry in order to concentrate on coastal markets which possess greater development challenges due to regulatory and land restrictions. Additionally, these coastal markets have strong economic fundamentals thanks to strong jobs growth in high-paying sectors.

At the same time, the multifamily cycle is a bit long in the tooth and cap rate spreads are increasingly compressed due to property value inflation and rising interest rates. With the headwinds from the coronavirus outbreak and some

[1] Estimate

[2] Estimate

[3] In millions

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.

restrictions on evictions being enacted, we believe that EQR's FFO will drop this year. However, the dividend should be safe and we expect the REIT to bounce back pretty well in the years to come.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/FFO	20.8	17.3	22.8	23.3	21.0	20.4	20.1	24.5	24.5	18.5	***22.3***	***17.0***
Avg. Yld.	3.1%	3.2%	3.9%	3.1%	2.5%	3.1%	3.4%	2.7%	2.7%	3.9%	***3.7%***	***3.9%***

The valuation multiple has hovered at or above 20x FFO/share and the dividend yield has ranged between 2.5% and 3.9% until the recent COVID-related price decline has brought it to around 22.3x FFO and a 3.7% yield. However, due to the aforementioned flattening growth trend that we project for Equity Residential and adding in the headwinds from the coronavirus, the stock will warrant a lower valuation multiple and a higher dividend yield. Therefore, we assign a fair value multiple estimate of 17x FFO. This number is not without precedent, as it fell to ~17x FFO back in 2013 during a general period of public market weakness in the multifamily sector.

Safety, Quality, Competitive Advantage, & Recession Resiliency

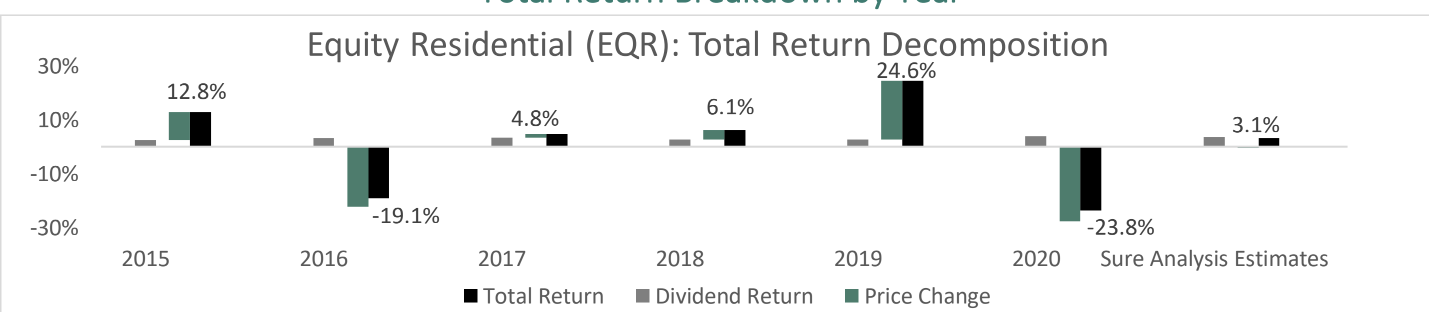
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	61.2%	64.5%	61.9%	63.1%	63.9%	65.4%	64.5%	66.5%	65.4%	73.0%	***82.9%***	***66.7%***

Equity Residential experienced a lot of market volatility during the stock market crash, but rebounded quickly from the Great Recession due to the defensive nature of the multifamily sector. However, it still experienced a sizable decline in FFO/share and a dividend cut during the recession. While multifamily apartments lack a strong competitive advantage due to the ease of creating new supply, as well as the alternative sources of affordable housing in the large metropolitan areas in which Equity Residential operates, the REIT does have the advantage of scale, low cost of capital, operational and marketing expertise, and a brand name advantage in markets that benefit from higher than average barriers to entry. A risk during a recession will be that the trust's properties are mostly "A" quality, which tend to outperform during economic expansions but underperform during contractions. The trust's balance sheet is also very strong, as its sector-leading A- credit rating makes clear. After issuing $400 million of 10-year unsecured notes at a coupon of 4.15%, executing an accretive capital recycling program, and carrying a mid-70% payout ratio, EQR has plenty of resources to invest in its growth projects and sustain the dividend during a downturn while also reacting opportunistically to opportunities that may become available.

Final Thoughts & Recommendation

Equity Residential has a strong track record and a stellar balance sheet. However, without a strong moat protecting its earnings power and the economy facing uncertainty from ongoing COVID-19 disruption and uncertainty, the stock appears overvalued at this time and likely to deliver mediocre annualized total returns (3.1%) over the next several years. We therefore rate it a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	1525	1748	2388	2615	2745	2426	2471	2578	2701	2572
Gross Profit	956	1122	1553	1731	1840	1620	1645	1698	1792	1655
Gross Margin	62.7%	64.2%	65.1%	66.2%	67.0%	66.8%	66.6%	65.9%	66.4%	64.4%
SG&A Exp.	44	47	62	51	65	58	52	54	53	48
D&A Exp.	664	685	1013	759	766	706	744	786	843	833
Operating Profit	407	514	512	922	1009	856	849	859	909	786
Operating Margin	26.7%	29.4%	21.5%	35.2%	36.8%	35.3%	34.4%	33.3%	33.6%	30.6%
Net Profit	894	842	1831	631	870	4292	603	658	970	914
Net Margin	58.6%	48.2%	76.7%	24.1%	31.7%	177%	24.4%	25.5%	35.9%	35.5%
Free Cash Flow	793	885	729	1133	1171	1036	1062	1163	1274	1109
Income Tax	1	1	1	1	1	2	0	1	(2)	1

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	16659	17201	22835	22951	23110	20704	20571	20394	21173	20287
Cash & Equivalents	384	613	54	40	42	77	51	47	46	43
Total Liabilities	10796	9674	11989	12243	12414	10243	10097	9995	10628	9523
Accounts Payable	35	38	119	154	187	147	115	102	94	107
Long-Term Debt	9721	8529	10766	10845	10921	8987	8957	8818	9037	8044
Total Equity	5469	7240	10457	10318	10433	10192	10205	10136	10278	10488
D/E Ratio	1.71	1.17	1.02	1.05	1.04	0.88	0.87	0.87	0.88	0.76

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	5.4%	5.0%	9.1%	2.8%	3.8%	19.6%	2.9%	3.2%	4.7%	4.4%
Return on Equity	17.3%	13.2%	20.7%	6.1%	8.4%	41.6%	5.9%	6.5%	9.5%	8.8%
ROIC	5.7%	5.3%	9.7%	2.9%	4.0%	20.9%	3.1%	3.4%	5.0%	4.8%
Shares Out.	295	320	354	378	381	382	383	384	384	384
Revenue/Share	5.17	5.46	6.74	6.92	7.21	6.35	6.46	6.72	6.99	6.66
FCF/Share	2.69	2.77	2.06	3.00	3.08	2.71	2.77	3.03	3.30	2.88

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