



Preferred Apartment Communities (APTS)

Updated May 24th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	\$9.80	5 Year CAGR Estimate:	11.1%	Market Cap:	\$510 M
Fair Value Price:	\$9.80	5 Year Growth Estimate:	5.0%	Ex-Dividend Date:	6/14/2021
% Fair Value:	100%	5 Year Valuation Multiple Estimate:	0.0%	Dividend Payment Date:	7/15/2021
Dividend Yield:	7.1%	5 Year Price Target	\$12.50	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

Preferred Apartment Communities (APTS) is a real estate investment trust (REIT) engaged primarily in the ownership and operation of Class A multifamily properties, grocery-anchored shopping centers, office buildings and student housing properties. It was founded in 2011 and has a market capitalization of \$510 million. It currently has 117 properties in 13 states, primarily in the Southeast region of the U.S. Preferred Apartment Communities has very young properties, with an average age around 6 years old, in high-quality suburban markets in the Sun Belt area.

In early May, Preferred Apartment Communities reported (5/10/21) financial results for the first quarter of fiscal 2021. Revenue decreased -12% over last year's quarter, primarily due to the sale of eight student housing properties. As a result, core FFO per unit declined -14%, from \$0.29 to \$0.25. Due to the pandemic, Preferred Apartment Communities cut its dividend by -33% in the second quarter of 2020, from \$0.2625 to \$0.175. While the results of the REIT are decent, we note that the pandemic caught the REIT with a huge debt load. Its net debt stands at \$2.7 billion, which is about 5 times the market cap of the stock and about 50 times its annual funds from operations. Due to its debt pile, the REIT was forced to sell 9 properties in the fourth quarter. Moreover, in the running quarter, it agreed to sell some properties of its office portfolio. As a result, it will post lower FFO this year. Due to the sale of properties, management lowered its guidance for annual core FFO per unit from \$0.81-\$0.89 to \$0.73-\$0.83. We have thus lowered our forecast from \$0.87 to \$0.83. On the bright side, the REIT will use the proceeds from sales to redeem preferred shares and hence it will reduce its preferred dividend payments.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
FFO	\$0.49	\$0.66	\$0.82	\$0.85	\$0.98	\$1.11	\$1.20	\$1.36	\$1.37	\$1.07	\$0.83	\$1.06
DPS	\$0.38	\$0.55	\$0.61	\$0.66	\$0.73	\$0.82	\$0.94	\$1.02	\$1.05	\$0.79	\$0.70	\$0.90
Shares¹	3.8	5.2	9.5	17.4	22.2	24.0	31.9	40.0	44.3	49.9	52.0	100.0

Preferred Apartment Communities has consistently grown its revenues and its earnings by adding high-quality assets in areas with promising economic prospects. During the last decade, the REIT has grown its FFO per unit at a 9.1% average annual rate. However, the REIT has stumbled in the last two years. In 2019, it incurred hefty expenses due to a restructuring of its asset portfolio, which resulted from a somewhat aggressive growth strategy in the preceding years. Moreover, the REIT has been hurt by the pandemic, which has greatly increased selling & administrative expenses. Nevertheless, we expect the pandemic to subside in the second half of this year and the REIT to grow its FFO per unit at a 5.0% average annual rate over the next five years off this year's low comparison base.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
P/FFO	15.4	11.7	10.4	10.0	11.0	12.0	13.9	11.6	14.3	7.4	11.8	11.8
Avg. Yld.	5.0%	7.1%	7.0%	7.7%	6.7%	6.2%	5.6%	6.4%	7.1%	10.0%	7.1%	7.2%

¹ 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.



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Preferred Apartment Communities is currently trading at a price-to-FFO ratio of 11.8, which is equal to the historical average FFO multiple of 11.8. As a result, we do not expect valuation to play a significant role in the 5-year return of the stock.

Safety, Quality, Competitive Advantage, & Recession Resiliency

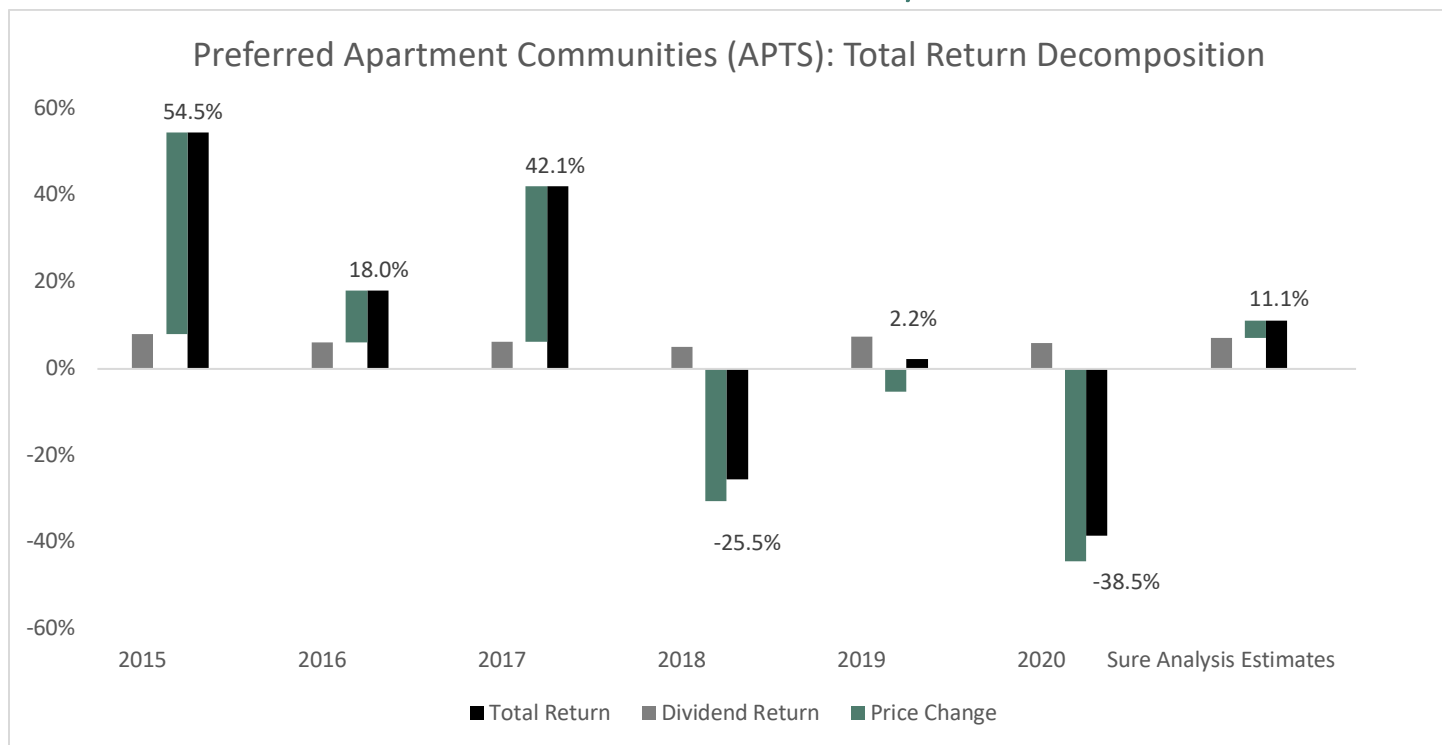
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	77%	83%	74%	77%	74%	74%	78%	75%	77%	74%	84%	85%

Preferred Apartment Communities had grown its FFO per unit every year between its IPO in 2011 and 2018. It also grew its dividend every year between 2011 and 2019. However, the coronavirus crisis caught the REIT off-guard, with an excessive debt load, and thus the REIT slashed its dividend by -33% last year. This is a stern reminder of the high risk of companies that pursue growth by adding too much debt. Due to its leveraged business model, Preferred Apartment Communities is not considered a reliable income grower. It is also important to note that the REIT pays hefty amounts on preferred dividends, which thus exert a great financial burden on the REIT. In the last 12 months, Preferred Apartment Communities has paid only \$40 million on common dividends but \$162 million on preferred dividends. Income-oriented investors should be well aware of this burden, which will continue weighing on the common dividend.

Final Thoughts & Recommendation

Preferred Apartment Communities has been caught with a huge debt load in the coronavirus crisis and thus it has sold many properties lately. However, we expect the pandemic to subside later this year. We expect the stock to offer an 11.1% average annual return over the next five years thanks to its 7.1% dividend yield and our expectations for 5% average annual growth of FFO per unit off this year's low base. We thus maintain our buy rating for the stock but only for investors who are confident that the pandemic will not extend beyond this year and can stomach the high volatility of Preferred Apartment Communities for extended periods.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	5	12	32	57	109	200	294	397	470	502
Gross Profit	4	9	23	44	80	142	211	282	333	342
Gross Margin	67.4%	71.7%	73.1%	77.5%	72.8%	71.0%	71.8%	70.9%	70.7%	68.2%
SG&A Exp.	2	3	5	8	13	25	35	38	45	215
D&A Exp.	8	4	15	16	38	78	113	165	179	202
Operating Profit	(4)	2	3	20	28	39	59	70	100	(80)
Operating Margin	-73.5%	18.9%	10.6%	34.6%	25.7%	19.3%	20.2%	17.6%	21.3%	-15.9%
Net Profit	(8)	(0)	(4)	2	(2)	(10)	28	43	(7)	(178)
Net Margin	-160%	-1.2%	-12.4%	3.7%	-2.2%	-4.8%	9.4%	10.9%	-1.5%	-35.4%
Free Cash Flow	1	4	9	15	35	62	86	145	146	48

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	92	123	342	691	1,296	2,421	3,252	4,411	4,771	4,281
Cash & Equivalents	5	3	9	3	2	12	21	39	94	29
Accounts Receivable	0	1	1	4	11	15	38	42	65	101
Goodwill & Int. Ass.	---	---	1	13	19	79	103	136	155	127
Total Liabilities	58	73	176	400	770	1,536	1,972	2,802	2,836	2,843
Accounts Payable	1	1	2	5	13	21	31	39	42	42
Long-Term Debt	56	70	170	382	709	1,465	1,843	2,362	2,637	2,631
Shareholder's Equity	35	50	165	289	523	884	1,276	1,608	1,931	1,440
D/E Ratio	1.61	1.41	1.03	1.32	1.36	1.66	1.44	1.47	1.37	1.83

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	---	-0.1%	-1.7%	0.4%	-0.2%	-0.5%	1.0%	1.1%	-0.2%	-3.9%
Return on Equity	---	-0.3%	-3.7%	0.9%	-0.6%	-1.4%	2.6%	3.0%	-0.4%	-10.5%
ROIC	---	-0.1%	-1.7%	0.4%	-0.3%	-0.5%	1.0%	1.2%	-0.2%	-4.1%
Shares Out.	3.8	5.2	9.5	17.4	22.2	24.0	31.9	40.0	44.3	49.9
Revenue/Share	1.39	2.42	3.40	3.25	4.93	8.35	9.21	9.92	10.63	10.30
FCF/Share	0.14	0.81	0.92	0.89	1.59	2.57	2.70	3.63	3.29	0.98

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

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