



PS Business Parks, Inc. (PSB)

Updated July 14th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$152	5 Year CAGR Estimate:	6.0%	Market Cap:	\$5.3 B
Fair Value Price:	\$144	5 Year Growth Estimate:	4.5%	Ex-Dividend Date:	09/14/2021 ¹
% Fair Value:	106%	5 Year Valuation Multiple Estimate:	-1.2%	Dividend Payment Date:	09/30/2021
Dividend Yield:	2.76%	5 Year Price Target	\$179	Years Of Dividend Growth:	N/A
Dividend Risk Score:	C	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

PS Business Parks, Inc. is a fully integrated, self-advised, and self-managed REIT that owns, operates, and acquires primarily multi-tenant industrial, flex, and office properties. The company owns and operates 27.8 million rentable square feet of commercial space in six states, comprising 98 parks and 676 buildings, along with two other joint ventures. PS Business Parks generates around \$370 million in annual rental revenues and is headquartered in Glendale, California.

On April 27th, PS Business Parks reported its Q1 results for the quarter ended March 31st, 2021. Revenues increased by 1.72% to \$180.04 million, with operations remaining mostly stable year-over-year. FFO/share came in at \$1.67, representing a decrease of 2.5% compared to Q1-2020, which resulted from flat NOI and \$1.1 million higher general and administrative expense was driven by a \$0.7 million higher stock-compensation expense.

During the quarter, the company's leasing activity included closing deals for 2.0 million square feet in 569 transactions with a weighted average cash rental growth rate of 5.7%. However, it must be noted that the company's average lease term currently stands at 3.2 years, compared to 3.8 years in the comparable period last year. This is likely due to a part of the company's office tenants choosing to stick to working remotely in a post-pandemic world. Since the beginning of the COVID-19 pandemic, the company has granted rent relief to 398 customers (approximately 11.0% of total customers based on rental income) including \$5.9 million of rent deferral and \$1.4 million of rent abatement. Thankfully, as of Q1, PSB had collected \$3.9 million, or 98.5%, of the scheduled repayments of COVID-19 related rent deferrals. Still, occupancy has failed to recover. In fact, despite the ongoing vaccinations and overall economic recovery, occupancy during the quarter was 92.4%, compared to 92.9% for the same period in 2020.

Overall, we expect FY2021 FFO/share of around \$6.84, in line with consensus estimates, powered by the company's rental growth leasing agreements and predictable revenues due to its multi-year contracts.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
FFO/shr	\$4.69	\$4.24	\$5.15	\$4.72	\$4.76	\$5.17	\$5.83	\$6.47	\$6.47	\$6.51	\$6.84	\$8.52
DPS	\$1.76	\$1.76	\$1.76	\$2.00	\$2.20	\$3.00	\$3.40	\$3.80	\$4.20	\$4.20	\$4.20	\$5.62
Shares²	24.5	24.2	24.7	26.9	27	27.1	27.2	27.3	27.4	27.5	27.5	30.0

PS Business Parks has done a decent job over the past decade in terms of growing its revenues and underlying FFO. Over the past 5 years, FFO/share has grown by around 5.8% per annum. Future FFO/share growth is massively dependent on whether one believes demand for office properties will return to its pre-COVID levels or that a decent part of the work-from-home workforce will retain their current schedules leaving some office spaces vacant. At the moment, we are supporting the former case, expecting FFO/share growth of around 4.5% in the medium term, powered by the likelihood for the company to continue closing new leasing deals at higher rental rates, as was the case in Q1. Rental revenues and FFO have remained rather robust during the pandemic, after all. That being said, we don't consider the latter scenario

¹ Estimated dates based on past dividend dates.

² Share count is 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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unlikely since occupancy recovery remains soft. Our sentiment, therefore, could change in the short term. PSB also displays a robust dividend history, with no dividend cuts taking place since 1998. The company has quadrupled its DPS since then, with substantial, double-digit hikes, though with pauses in-between. Increases likely occur when the company feels it has reached a new profitability plateau. We estimate a DPS CAGR of 6% ahead, lower than the company's 5 and 10-year CAGRs of 7% and 10.1%, respectively, but consecutive annual hikes should not be expected.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/FFO	11.1	15.8	15.1	17.8	17.9	20.3	22.1	19.3	24.9	20.4	22.3	21.0
Avg. Yld.	3.4%	2.6%	2.3%	2.4%	2.6%	2.9%	2.6%	3.0%	2.6%	3.2%	2.8%	3.1%

PSB's valuation has remained rather stable over the past decade, with the stock hovering at an average P/FFO of around 21.4 during this time. We believe that PSB will retain a valuation multiple close to its average. The stock could be slightly overvalued at the moment but still fairly valued compared to various REITs whose valuation has unreasonably expanded these days. Investors should expect a yield between 2.7% and 3.3% in the medium term.

Safety, Quality, Competitive Advantage, & Recession Resiliency

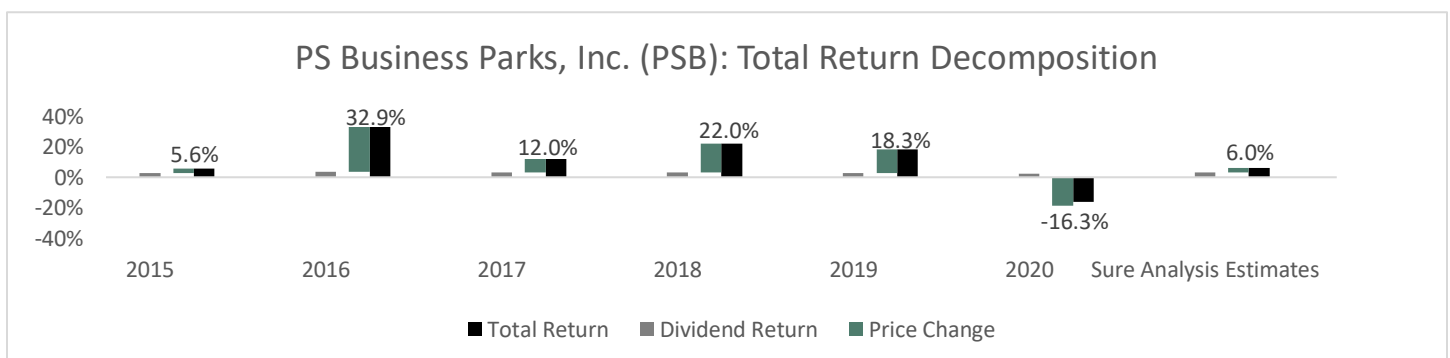
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	38%	42%	34%	42%	46%	58%	58%	59%	65%	65%	61%	66%

We consider PSB's current DPS as relatively safe. The company has been prudent with its dividend increases, resulting in retaining a healthy payout ratio, which currently stands at just over 60%. Hence, the dividend should remain covered even if cash flows were to come under pressure. PSB possesses several qualities, including a very diverse customer base. Its top 5 tenants account for only 8.1% of its annualized rental income. These tenants are also of the highest credit qualities, with its top 2 being the U.S. Government and Amazon. PSB also boasts an A- corporate credit rating by S&P, featuring a fortress balance sheet with \$0 long-term debt. The company funds its acquisition through issuing preferred stock, which currently trades with an average coupon (dividend) rate of 5.1%. These payouts are covered by 5.8 times the company's operating cash flows. We expect the company to perform relatively resilient during a recession, as was the case during the Great Financial Crisis, due to its leasing contracts having an average duration longer than 3 years.

Final Thoughts & Recommendation

PSB has delivered satisfactory returns over the past few years, posting robust FFO and DPS growth. Moving forward, we anticipate annualized returns of around 6%, powered by our modest growth estimates and multi-year contracts. We believe the company enjoys several noteworthy qualities, though still paying close attention on how the office market will play out in a post-COVID-19 world. Shares earn a Hold rating for the time being.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	298	347	360	377	373	387	402	414	430	416
Gross Profit	198	233	245	250	252	264	280	289	302	290
Gross Margin	66.5%	67.1%	68.1%	66.2%	67.5%	68.2%	69.6%	69.9%	70.1%	69.8%
SG&A Exp.	9	9	5	14	14	15	13	12	14	15
D&A Exp.	85	109	109	110	105	99	94	94	100	92
Operating Profit	105	115	131	126	133	149	173	178	183	179
Operating Margin	35.2%	33.1%	36.4%	33.3%	35.6%	38.6%	43.0%	42.9%	42.7%	43.1%
Net Profit	94	89	103	174	130	128	155	227	175	174
Net Margin	31.6%	25.7%	28.7%	46.2%	35.0%	33.1%	38.5%	54.8%	40.7%	41.8%
Free Cash Flow	132	152	163	174	192	219	220	236	246	225

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	2,139	2,152	2,239	2,227	2,187	2,119	2,100	2,069	2,046	2,058
Cash & Equivalents	5	13	31	152	189	129	115	37	63	69
Accounts Receivable	3	5	5	3	2	2	2	1	1	2
Total Liabilities	778	538	324	319	326	309	210	85	85	82
Long-Term Debt	717	468	250	250	250	-	-	-	-	-
Shareholder's Equity	581	561	723	718	740	734	734	806	801	812
D/E Ratio	0.61	0.32	0.15	0.15	0.15	-	-	-	-	-

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	5.0%	4.2%	4.7%	7.8%	5.9%	5.9%	7.3%	10.9%	8.5%	8.5%
Return on Equity	16.0%	15.6%	16.1%	24.1%	17.9%	17.4%	21.1%	29.5%	21.8%	21.5%
ROIC	5.2%	4.3%	4.9%	8.0%	6.1%	6.5%	8.4%	11.7%	8.9%	8.8%
Shares Out.	24.5	24.2	24.7	26.9	27	27.1	27.2	27.3	27.4	27.5
Revenue/Share	12.12	14.27	14.49	13.96	13.79	14.23	14.67	15.08	15.62	15.08
FCF/Share	5.38	6.26	6.58	6.45	7.11	8.04	8.02	8.62	8.94	8.15

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

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