Innovative Industrial Properties (IIPR)

Updated February 24th, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	$176	**5 Year CAGR Estimate:**	24.5%	**Market Cap:**	$4.5 B
Fair Value Price:	$192	**5 Year Growth Estimate:**	20.0%	**Ex-Dividend Date:**	03/30/22
% Fair Value:	91%	**5 Year Valuation Multiple Estimate:**	1.8%	**Dividend Payment Date[1]:**	04/15/22
Dividend Yield:	3.4%	**5 Year Price Target**	$478	**Years Of Dividend Growth:**	5
Dividend Risk Score:	F	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	28.2%[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 $4.5 billion REIT owns 105 properties in 19 states. Amid the cannabis boom over the past few years, as well as its exclusivity in terms of the listing giving the the trust access to public markets, Innovate Industrial Properties remains the fastest-growing REIT in the world.

On February 23rd, 2022, Innovative Industrial announced its Q4 earnings for the period ending December 31st, 2021. For the quarter, revenues and normalized AFFO/share were $58.9 million and $1.85, an increase of 59%, and 42.3%, respectively. These rates even accelerated from Q3's 56.9% and 33.6%, respectively.

The company delivered another quarter of very high growth, with another 31 acquisitions since the beginning of October and contractual rental escalations at certain properties. As of February 23rd, 100% of IIPR's properties were leased with a weighted-average remaining lease term of approximately 16.6 years, close to the previous quarter, which is once again very impressive. With its tenants enjoying resilient marijuana demand amid growing consumption, IIPR once again collected 100% of its contractual rent due for Q4.

While no financial guidance was provided, our initial estimates assume a quite prudent FY2022 AFFO/share estimate of $8.00, below consensus estimates of $8.71. This is largely to be conservative against an already exciting investment case.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
AFFO	---	---	---	---	$(0.62)	$0.67	$1.34	$3.27	$5.00	$5.55	***$8.00***	***$19.91***
DPS	---	---	---	---	---	$0.55	$1.20	$2.83	$4.47	$5.72	***$6.00***	***$12.60***
Shares[3]	---	---	---	---	1	3.4	7.3	10.7	19.27	23.9	***23.9***	***100***

Industrial Innovating Properties has seen AFFO/share grow dramatically since the trust's IPO. Over the past four 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, IIPR acquired 37 properties in 2021 alone. With the schedule-1 drug being decriminalized in one state after the other, we expect to see the current growth rates sustained in the medium term. In line with its AFFO growth, management has consistently raised the dividend, often on a sequential basis. Payouts grew by a 28% in FY2021. We have purposely softened our AFFO/share and DPS medium-term CAGR estimates from 25% and 20%, respectively, to 20% and 16%. Again, this is largely to be prudent in the current market environment, despite the trust's results accelerating quarter-over-quarter.

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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 28.2%. Its latest QoQ growth amounts to 7%.

[3] Share count is in millions.

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As we mentioned in previous reports, and was proven in once again in Q4's results, these estimate will likely turnout to be conservative, considering the IIPR's acquisition spree. Still, IIPR has short trading history, and its acquisition-driven strategy may see availability headwinds in the future, which also supports the case for our more reserved estimates.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/FFO	---	---	---	---	---	47.8	12.2	16.6	30.2	33.0	***22.0***	***24.0***
Avg. Yld.	---	---	---	---	---	3.4%	3.3%	2.8%	2.8%	2.6%	***3.4%***	***2.6%***

IIPR's shares have plummeted since our last report due to the ongoing valuation compression high-growth equities have experienced. The stock's valuation has shifted to 22 times our already conservative FY2022 expected AFFOs. We believe that the stock is steeply undervalued at its current levels. We retain our fair valuation multiple at 24 through 2027, and that includes the potential for growth deceleration over the medium-term. Shares are currently yielding around 3.4%, which is quite substantial considering the REIT is undergoing such a rapid growth phase.

Safety, Quality, Competitive Advantage, & Recession Resiliency

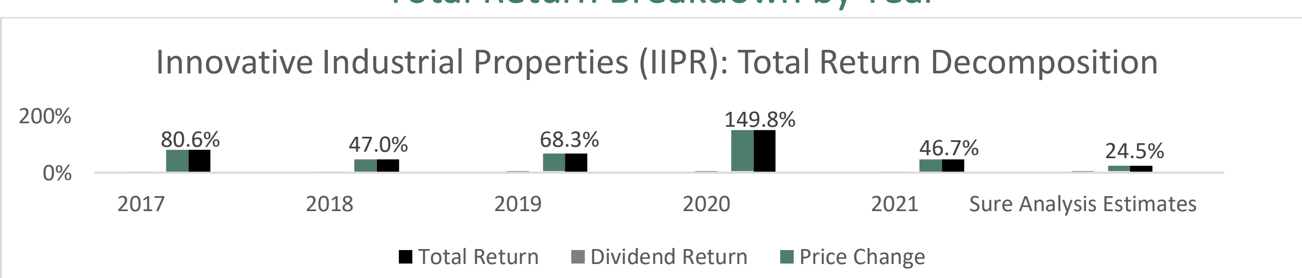
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	---	---	---	---	---	82%	90%	87%	89%	86%	75%	***63%***

The company's seemingly high payout ratio is non-meaningful as AFFOs proliferate and only reflect this year's cash flows. Being the only listed pure-cannabis REIT, the company 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. With more states legalizing weed over time, the company is subject to a fantastic medium/long-term expansion trend. Despite the headwinds COVID-19 caused in many industries, IIPR was barely affected, continuing its proven acquisition-based growth model. Because of how new the cannabis sector is, its recession resiliency is untested to the passage of time and remains to be seen. Still, its average lease duration of 16.6 years is unparalleled to the industry. Not even the highest-quality, most mature REITs in the world get to enjoy such a lengthy lease profile, which adds to the dividend's safety.

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 rental cash flows from IIPR's facilities. We have specifically assumed prudent estimates ahead, yet the stock is undervalued enough relative to our growth rates that we forecast annualized returns of around 24.5% through 2027. Shares earn a buy rating, with a considerably higher margin of safety since our previous report.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	---	---	---	---	$0.32	$6.42	$14.79	$44.67	$116.90
Gross Profit	---	---	---	---	$0.23	$6.30	$14.34	$43.35	$111.94
Gross Margin	---	---	---	---	72.9%	98.2%	97.0%	97.1%	95.7%
SG&A Exp.	---	---	---	---	$0.83	$5.50	$6.38	$9.82	$14.18
D&A Exp.	---	---	---	---	$0.03	$0.92	$2.63	$8.60	$28.02
Operating Profit	---	---	---	---	-$0.69	-$0.11	$5.34	$24.94	$69.74
Operating Margin	---	---	---	---	-213.4%	-1.7%	36.1%	55.8%	59.7%
Net Profit	---	---	---	---	-$4.39	-$0.07	$6.99	$23.48	$65.73
Net Margin	---	---	---	---	-1368.2%	-1.1%	47.2%	52.6%	56.2%
Free Cash Flow	---	---	---	---	-$28.34	$5.02	$15.69	$44.93	$110.81
Income Tax	---	---	---	---	$0.32	$6.42	$14.79	$44.67	---

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	---	---	---	---	$63.33	$80.03	$281.47	$745.86	$1,768
Cash & Equivalents	---	---	---	---	$33.00	$11.76	$13.05	$82.24	$126.01
Total Liabilities	---	---	---	---	$2.89	$6.48	$17.17	$197.85	$243.11
Accounts Payable	---	---	---	---	$0.07	$1.08	$4.40	$28.39	$41.14
Long-Term Debt	---	---	---	---	$0.00	$0.00	$0.00	$134.65	$136.69
Shareholder's Equity	---	---	---	---	$60.44	$59.54	$250.28	$534.00	$1,511
LTD/E Ratio	---	---	---	---	0.00	0.00	0.00	0.25	0.09

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	---	---	---	---	---	-0.1%	3.9%	4.6%	5.2%
Return on Equity	---	---	---	---	-14.5%	-0.1%	4.5%	6.0%	6.4%
ROIC	---	---	---	---	---	-0.1%	4.1%	5.0%	5.6%
Shares Out.	---	---	---	---	0.96	3.38	7.29	10.68	19.56
Revenue/Share	---	---	---	---	$0.33	$1.90	$2.03	$4.18	$5.98
FCF/Share	---	---	---	---	-$29.43	$1.49	$2.15	$4.21	$5.67

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

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