



PS Business Parks, Inc. (PSB)

Updated February 23rd, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	\$159	5 Year CAGR Estimate:	7.0%	Market Cap:	\$4.36 B
Fair Value Price:	\$158	5 Year Growth Estimate:	4.5%	Ex-Dividend Date:	03/16/2022
% Fair Value:	100%	5 Year Valuation Multiple Estimate:	0.0%	Dividend Payment Date:	03/31/2022
Dividend Yield:	2.6%	5 Year Price Target	\$197	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 25.1 million rentable square feet of commercial space in six states, comprising 97 parks and 666 buildings, along with two other joint ventures. PS Business Parks generates around \$440 million in annual rental revenues and is headquartered in Glendale, California.

On February 22nd, 2022, PS Business Parks reported its Q4 results for the period ending December 31st, 2021. Rental income grew 7.3% to \$100.4 million. Higher rental revenues resulted from higher NOI and improved occupancy. Specifically, same-park cash NOI was powered by cash rental income growth of 6.5%, while occupancy improved from 92.4% to 95.5% year-over-year. However, FFO/share came in at \$1.53, representing an increase of 7.8% compared to Q4-2020. FFO/share was negatively impacted by a \$6.4 million non-cash charge related to the redemption of the Series W preferred stock and a \$3.6 million charge for a state income tax provision.

During the quarter, the company's leasing activity included closing deals for 1.8 million square feet with a weighted average cash rental growth rate of 6.1%. This is higher than the previous quarter's 5.0%. However, the company's average lease term stood at 3.6 years, compared to 3.7 years in the previous quarter, suggesting marginally lower cash flow visibility. Additionally, as of Feb. 28th, PSB had collected 99.9% of revenue billed during FY2021, suggesting elevated demand in the office REIT space. This was illustrated by the elevated occupancy levels as well.

Based on the company's rental growth rates, leasing agreements, and predictable revenues due to its multi-year contracts, we estimate that FY2022 FFO/share at \$7.36.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
FFO/shr	\$4.24	\$5.15	\$4.72	\$4.76	\$5.17	\$5.83	\$6.47	\$6.47	\$6.51	\$6.67	\$7.36	\$9.17
DPS	\$1.76	\$1.76	\$2.00	\$2.20	\$3.00	\$3.40	\$3.80	\$4.20	\$4.20	\$8.80 ¹	\$4.20	\$5.62
Shares²	24.2	24.7	26.9	27.0	27.1	27.2	27.3	27.4	27.5	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 4.8% per annum. Despite concerns regarding the future demand for office spaces in a post-pandemic world, the company appears to have fully recovered from last year's hurdles. We continue to expect 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 over FY2021. The recent results pointed to solid developments in rental growth rates on new leases and overall occupancy. PSB displays a robust dividend history, with no dividend cuts taking place since 1998. Since then, the company has quadrupled its DPS 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, but consecutive annual hikes should not be expected.

¹ Includes a \$4.60 special dividend related to the sale of various assets dispositions.

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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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/FFO	15.8	15.1	17.8	17.9	20.3	22.1	19.3	24.9	20.4	24.7	21.5	21.5
Avg. Yld.	2.6%	2.3%	2.4%	2.6%	2.9%	2.6%	3.0%	2.6%	3.2%	5.3%	2.6%	2.9%

PSB's valuation has remained rather stable over the past decade, with the stock hovering at an average P/FFO of around 22.3 during this time. We believe that PSB's valuation multiple will likely be compressed modestly. We believe that the (forward) P/FFO of 21.5 based on our FY2022 estimates is rather reasonable. The stock should retain this multiple in the medium-term. We also forecast that the yield will converge towards 2.9% in the coming years, assuming dividend growth outperforms FFO/share growth.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	42%	34%	42%	46%	58%	58%	59%	65%	65%	132%	57%	61%

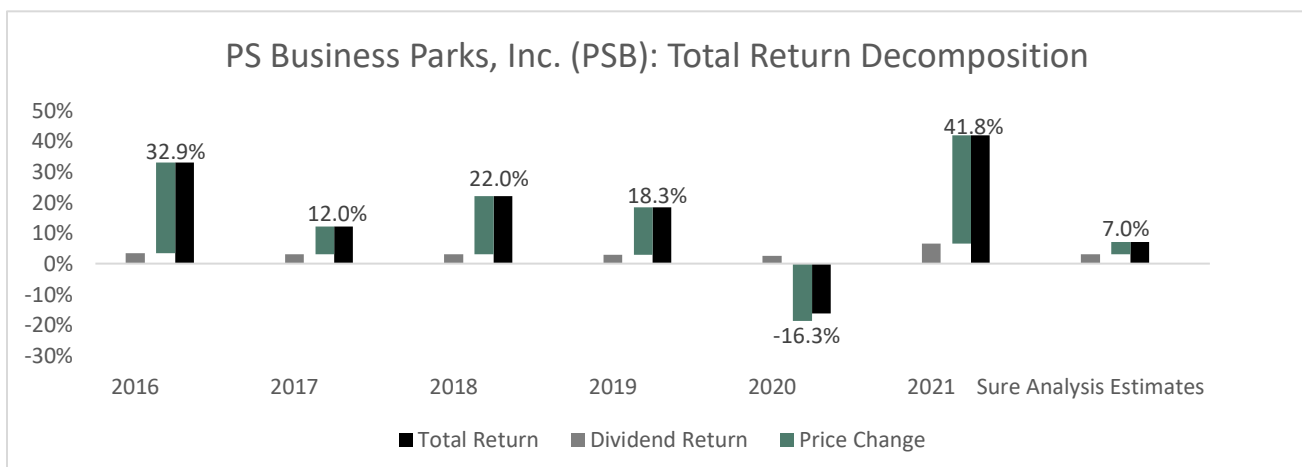
We consider PSB's current DPS as relatively safe. The company has been prudent with its dividend increases, resulting in retaining a healthy payout ratio, which currently stands at just around 57%. Hence, the dividend should remain covered even if cash flows were to come under pressure. PSB possesses several qualities, including a very diverse customer base. Its top 10 tenants account for just 10.3% 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 5.3%. These payouts are covered by around 6 times PSB'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 3.5 years.

Final Thoughts & Recommendation

PSB has delivered satisfactory returns over the past few years, posting robust FFO and DPS growth. We anticipate annualized returns of 7.0% in the medium-term, powered by PSB's current yield, our growth expectations, and stable valuation assumptions. We believe the company enjoys several noteworthy qualities, while the outlook for office space appears increasingly more optimistic as its latest results demonstrated. The stock earns a hold rating.

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
LTD/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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