



# Preferred Apartment Communities (APTS)

Updated May 23<sup>rd</sup>, 2022, by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$25	<b>5 Year CAGR Estimate:</b>	3.1%	<b>Market Cap:</b>	\$1.6 B
<b>Fair Value Price:</b>	\$23	<b>5 Year Growth Estimate:</b>	2.0%	<b>Ex-Dividend Date:</b>	6/13/2022 <sup>1</sup>
<b>% Fair Value:</b>	110%	<b>5 Year Valuation Multiple Estimate:</b>	-1.9%	<b>Dividend Payment Date:</b>	7/14/2022
<b>Dividend Yield:</b>	2.8%	<b>5 Year Price Target</b>	\$25	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	F	<b>Rating:</b>	Sell

## 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 \$1.6 billion. It currently has 97 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 (5/9/22) financial results for the first quarter of fiscal 2022. Same-store revenue grew 11.9% over the prior year's quarter but core FFO per unit decreased -24%, from \$0.29 to \$0.15, due to the divestment of some properties of student housing and offices. Moreover, its net debt stands at \$2.3 billion, which is 144% of the market cap of the stock and about 40 times its annual funds from operations.

On February 16<sup>th</sup>, 2022, Preferred Apartment Communities agreed to be acquired by Blackstone's REIT for \$25 per unit in cash. The deal, which has to be approved by shareholders at a special meeting on 6/17/22, is expected to close in the second quarter of 2022. The deal price is 39% higher than the stock price of Preferred Apartment Communities before the announcement. When the deal materializes, the stock of Preferred Apartment Communities will not be public anymore. We view the deal price as too high relative to the fundamentals of Preferred Apartment Communities and hence we believe that the shareholders of the REIT should be satisfied.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>FFO</b>	\$0.66	\$0.82	\$0.85	\$0.98	\$1.11	\$1.20	\$1.36	\$1.37	\$1.07	\$1.10	<b>\$1.10</b>	<b>\$1.21</b>
<b>DPS</b>	\$0.55	\$0.61	\$0.66	\$0.73	\$0.82	\$0.94	\$1.02	\$1.05	\$0.79	\$0.70	<b>\$0.70</b>	<b>\$0.90</b>
<b>Shares<sup>2</sup></b>	5.2	9.5	17.4	22.2	24.0	31.9	40.0	44.3	49.9	52.9	<b>56.5</b>	<b>100.0</b>

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 5.9% average annual rate. However, the REIT has stumbled in the last three 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 REIT to partially recover from the pandemic in the upcoming quarters and grow its FFO per unit at a 2.0% average annual rate over the next five years.

## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
<b>P/FFO</b>	11.7	10.4	10.0	11.0	12.0	13.9	11.6	14.3	7.4	10.0	<b>22.7</b>	<b>20.6</b>
<b>Avg. Yld.</b>	7.1%	7.0%	7.7%	6.7%	6.2%	5.6%	6.4%	7.1%	10.0%	6.4%	<b>2.8%</b>	<b>3.6%</b>

<sup>1</sup> Estimated date.

<sup>2</sup> 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 22.7, which is much higher than the historical average FFO multiple of 11.2. The extremely rich valuation has resulted from the aforementioned pending acquisition of the REIT. We have assigned a fair price-to-FFO ratio of 20.6 in order to match the deal price.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

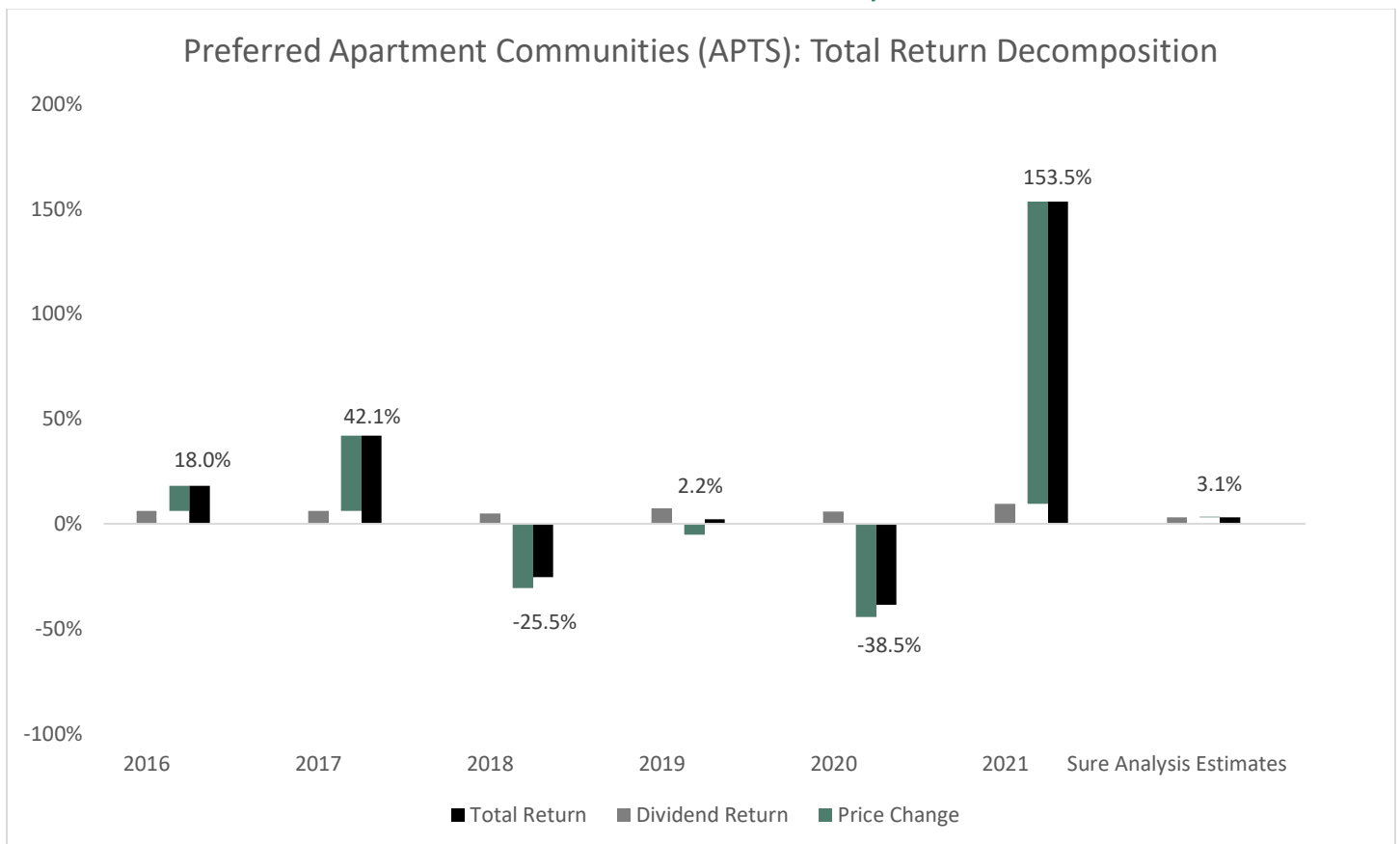
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	83%	74%	77%	74%	74%	78%	75%	77%	74%	64%	64%	74%

Preferred Apartment Communities had grown its FFO per share every year between its IPO in 2011 and 2019. 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% in 2020. 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 exert a great financial burden on the REIT. In the last 12 months, Preferred Apartment Communities has paid only \$37 million on common dividends but \$148 million on preferred dividends.

## 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, the REIT is on track to be acquired with an excessive premium in June. As the stock has jumped to the announced deal price, it has essentially exhausted its upside potential. We thus rate the stock as a sell.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Revenue</b>	12	32	57	109	200	294	397	470	502	451
<b>Gross Profit</b>	9	23	44	80	142	211	282	333	342	306
<b>Gross Margin</b>	71.7%	73.1%	77.5%	72.8%	71.0%	71.8%	70.9%	70.7%	68.2%	67.8%
<b>SG&amp;A Exp.</b>	3	5	8	13	25	35	38	45	215	33
<b>D&amp;A Exp.</b>	4	15	16	38	78	113	165	179	202	169
<b>Operating Profit</b>	2	3	20	28	39	59	70	100	(80)	103
<b>Operating Margin</b>	18.9%	10.6%	34.6%	25.7%	19.3%	20.2%	17.6%	21.3%	-15.9%	22.7%
<b>Net Profit</b>	(0)	(4)	2	(2)	(10)	28	43	(7)	(178)	20
<b>Net Margin</b>	-1.2%	-12.4%	3.7%	-2.2%	-4.8%	9.4%	10.9%	-1.5%	-35.4%	4.5%
<b>Free Cash Flow</b>	4	9	15	35	62	86	145	146	48	152

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Total Assets</b>	123	342	691	1,296	2,421	3,252	4,411	4,771	4,281	3,563
<b>Cash &amp; Equivalents</b>	3	9	3	2	12	21	39	94	29	30
<b>Accounts Receivable</b>	1	1	4	11	15	38	42	65	101	67
<b>Goodwill &amp; Int. Ass.</b>	---	1	13	19	79	103	136	155	127	60
<b>Total Liabilities</b>	73	176	400	770	1,536	1,972	2,802	2,836	2,843	2,541
<b>Accounts Payable</b>	1	2	5	13	21	31	39	42	42	37
<b>Long-Term Debt</b>	70	170	382	709	1,465	1,843	2,362	2,637	2,631	2,343
<b>Shareholder's Equity</b>	50	165	289	523	884	1,276	1,608	1,931	1,440	1,024
<b>D/E Ratio</b>	1.41	1.03	1.32	1.36	1.66	1.44	1.47	1.37	1.83	2.29

## Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Return on Assets</b>	-0.1%	-1.7%	0.4%	-0.2%	-0.5%	1.0%	1.1%	-0.2%	-3.9%	0.5%
<b>Return on Equity</b>	-0.3%	-3.7%	0.9%	-0.6%	-1.4%	2.6%	3.0%	-0.4%	-10.5%	1.7%
<b>ROIC</b>	-0.1%	-1.7%	0.4%	-0.3%	-0.5%	1.0%	1.2%	-0.2%	-4.1%	0.6%
<b>Shares Out.</b>	5.2	9.5	17.4	22.2	24.0	31.9	40.0	44.3	49.9	52.9
<b>Revenue/Share</b>	2.42	3.40	3.25	4.93	8.35	9.21	9.92	10.63	10.30	8.76
<b>FCF/Share</b>	0.81	0.92	0.89	1.59	2.57	2.70	3.63	3.29	0.98	2.95

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

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