Corporate Office Properties Trust (OFC)

Updated May 12th, 2022 by Felix Martinez

Key Metrics

Current Price:	$25	**5 Year CAGR Estimate:**	10.3%	**Market Cap:**	$2.93 B
Fair Value Price:	$30	**5 Year Growth Estimate:**	3.5%	**Ex-Dividend Date:**	06/29/2022[1]
% Fair Value:	84%	**5 Year Valuation Multiple Estimate:**	3.5%	**Dividend Payment Date:**	07/15/2022
Dividend Yield:	4.4%	**5 Year Price Target**	$35	**Years Of Dividend Growth:**	0
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Rating:**	Buy

Overview & Current Events

Corporate Office Properties Trust is a Real Estate Investment Trust (REIT) that invests in office and data center buildings, mainly in the suburbs of the Washington, D.C. metropolitan area. It primarily leases to the U.S. government and its contractors. As of March 31, 2022, the company derived 90% of its core portfolio annualized rental revenue from Defense/IT Locations and 10% from its Regional Office Properties. COPT's core portfolio of 186 office and data center shell properties encompassed 21.8 million square feet and was 94.1% leased. Also, the company owns one wholesale data center that is 86.7% leased. The company was founded in 1988 by Clay W. Hamlin III as Royale Investments, Inc. However, the company now trades under the ticker symbol "OFC" and has a current market capitalization of $2.93 billion.

On April 28, 2022, OFC reported first-quarter results for Fiscal Year (FY)2022. The company's total revenue was $195.5 million for the quarter versus $154.4 million for the first quarter of 2021, increasing 26.6% year-over-year. The revenue increase was driven by rent increases and an increase in leasing. Net income for the quarter was $59 million compared to a loss of $(6.7) million in 1Q2021. Diluted funds from operations per share were $0.58 for the first quarter of 2022 compared to $0.27 for 2021. This represents an increase of 114.8%.

The company's core portfolio is 92.2% Occupied and 94.1% Leased at quarter-end. During the quarter, the company placed into service 283,000 square feet of developments that were 100%.

The company's development pipeline consists of 11 properties totaling 1.7 million square feet and 96% leased. These projects have a total estimated cost of $552.7 million.

OFC management team provided the full year 2022 guidance in the quarterly report. Management expects its full-year guidance FFO to be between $2.31 and $2.37 per share. We will use $2.34 as our fair value and total return calculations.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$2.13	$1.97	$1.88	$2.01	$2.01	$2.03	$2.01	$2.03	$2.12	$2.29	***$2.34***	***$2.78***
DPS	$1.10	$1.10	$1.10	$1.10	$1.10	$1.10	$1.10	$1.10	$1.10	$1.10	***$1.10***	***$1.10***
Shares[2]	73.5	85.0	88.2	97.7	94.5	99.2	104.1	111.6	112.1	112.4	***112.4***	***112.5***

The most significant growth prospects from OFC will be the continuation of profitable acquisitions in the future and increasing rents at a modest rate. OFC had grown FFO at a Compound Annual Growth Rate (CAGR) of 0.8% over the past ten years. Over the past five years, FFO growth has improved with a CAGR of 2.9%. During the COVID-19 pandemic, most REITs had to cut their dividend, or FFO decreased for the year. However, FFO increased by 4% from 2019 to 2020. We expect OFC to continue to grow FFO at a 3.5% CAGR for the next five years. We expect the Trust to make $2.78 in FFO per share in 2027.

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[1] Ex-Dividend and Dividend Payment Dates are estimates.

[2] Share count is in millions.

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The dividend has not been increasing throughout the years. The company has been paying the same dividend rate of $1.10 per share for the past ten years. Thus, we do not foresee any dividend increase over the next five years.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	11.7	12	15.1	10.9	15.5	14.4	10.5	14.5	12.3	12.2	***10.7***	***12.7***
Avg. Yld.	4.4%	4.6%	3.9%	5.0%	3.5%	3.8%	5.2%	3.7%	4.2%	3.9%	***4.4%***	***3.1%***

OFC currently trades hands with a 10.7x FFO, which is lower than its peers. Over the ten years history of OFC, the Trust has ten-year multiple averages of 12.9x FFO. Thus, we think a multiple of 12.7x FFO is fair for OFC. This will provide a 3.5% tailwind expansion over the next five years. The current dividend yield of 4.4% is slightly higher than its five-year average. Thus, the company looks to be undervalued.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	51.6%	55.8%	58.5%	54.7%	54.7%	54.2%	54.7%	54.2%	51.9%	48.0%	***47%***	***40%***

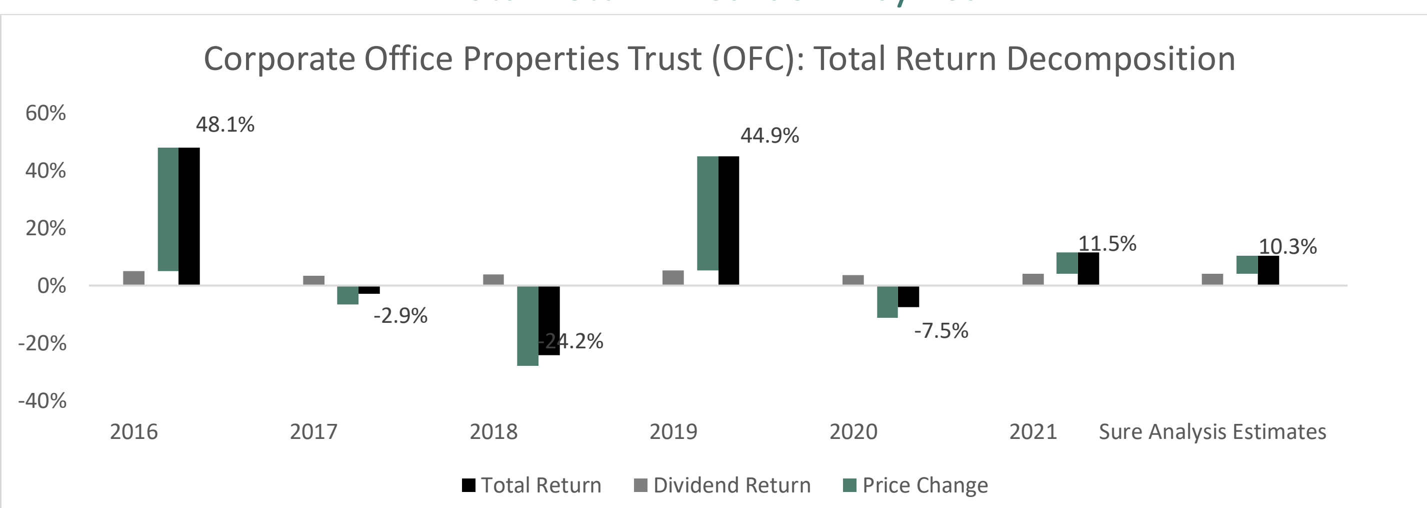
OFC's competitive advantage is that it has a strong management team. The company was very resilient during The Great Recession in 2008-2009 and droning the COVID-19 pandemic. During 2008, FFO increased by 9% to $2.44 per share. Also, in 2019, FFO increased by 2% to $2.49 per share. As mentioned above, OFC was one of the fortunate REITs that increased FFO in FY2020. This speaks volumes as most REITs struggle mightily during the pandemic. Also, OFC did not have to cut its dividend.

OFC has a good balance sheet. The Trust has an interest coverage ratio of 3.4 and a debt-to-equity ratio of 1.3. The dividend payment is meager compared to other REITs paying out 47% of its FFO. The low dividend payout ratio should help the company start a dividend growth policy in the future.

Final Thoughts & Recommendation

OFC is a well-run office REIT with a good balance sheet. The Trust went through the COVID-19 pandemic like it was not even there. The Trust looks undervalued, with an expected total return for the next five years to be 10.3%. Thus, we give OFC a Buy rating at the current price.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	508	523	586	625	574	613	578	612	582	664
Gross Profit	170	184	170	188	199	188	182	191	197	209
Gross Margin	33.5%	35.2%	29.1%	30.1%	34.6%	30.7%	31.4%	31.3%	33.9%	31.5%
SG&A Exp.	38	36	37	45	45	37	35	40	37	41
D&A Exp.	124	120	138	142	135	137	139	139	140	151
Operating Profit	133	148	133	143	154	151	147	152	160	169
Operating Margin	26.1%	28.2%	22.7%	22.9%	26.8%	24.6%	25.4%	24.8%	27.5%	25.4%
Net Profit	21	94	40	178	30	69	72	192	97	77
Net Margin	4.1%	17.9%	6.9%	28.5%	5.2%	11.2%	12.5%	31.3%	16.7%	11.5%
Free Cash Flow	172	135	165	181	208	207	156	204	206	219
Income Tax	0	2	0	0	0	1	0	0	0	0

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	3,654	3,630	3,664	3,909	3,781	3,595	3,656	3,854	4,077	4,262
Cash & Equivalents	11	54	6	60	210	12	8	15	18	13
Accounts Receivable	103	116	127	135	125	119	116	123	133	150
Goodwill & Int. Ass.	76	59	44	98	78	59	43	27	19	15
Total Liabilities	2,207	2,115	2,125	2,274	2,163	2,104	2,003	2,106	2,358	2,578
Accounts Payable	98	99	123	92	109	108	93	149	143	186
Long-Term Debt	2,019	1,928	1,914	2,078	1,904	1,828	1,824	1,831	2,087	2,272
Shareholder's Equity	1,032	1,177	1,252	1,345	1,351	1,402	1,585	1,679	1,661	1,623
LTD/E Ratio	1.48	1.35	1.32	1.35	1.25	1.30	1.15	1.09	1.26	1.40

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.6%	2.6%	1.1%	4.7%	0.8%	1.9%	2.0%	5.1%	2.5%	1.8%
Return on Equity	2.2%	8.5%	3.3%	13.7%	2.2%	5.0%	4.8%	11.7%	5.8%	4.7%
ROIC	0.6%	2.7%	1.2%	5.0%	0.8%	2.0%	2.1%	5.4%	2.6%	2.0%
Shares Out.	73.5	85.0	88.2	97.7	94.5	99.2	104.1	111.6	112.1	112.4
Revenue/Share	6.92	6.14	6.64	6.40	6.07	6.18	5.55	5.48	5.20	5.91
FCF/Share	2.34	1.58	1.87	1.85	2.20	2.09	1.50	1.83	1.84	1.95

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