Piedmont Office Realty Trust (PDM)

Updated July 28th, 2022 by Quinn Mohammed

Key Metrics

Current Price:	$14	**5 Year CAGR Estimate:**	13.5%	**Market Cap:**	$1.7 B
Fair Value Price:	$19	**5 Year Growth Estimate:**	2.0%	**Ex-Dividend Date:**	08/26/22
% Fair Value:	71%	**5 Year Valuation Multiple Estimate:**	7.2%	**Dividend Payment Date:**	09/16/22
Dividend Yield:	6.2%	**5 Year Price Target**	$21	**Years Of Dividend Growth:**	0
Dividend Risk Score:	D	**Retirement Suitability Score:**	B	**Rating:**	Buy

Overview & Current Events

Piedmont Office Realty Trust, Inc. owns, manages, develops, redevelops, and operates high-quality office properties located primarily in sub-markets within seven major Eastern U.S. office markets. The company derives most of its revenues from U.S. government entities, business services companies, and financial institutions in the Sunbelt region. PDM is fully-integrated and self-managed. The company has local management offices in each of their markets. Piedmont trades on the NYSE under the ticker symbol PDM and is headquartered in Atlanta, Georgia. The office REIT has a market capitalization of $1.7 billion.

On July 27th, Piedmont released second quarter 2022 results. The company reported core funds from operations (FFO) of $0.50 per share for the quarter, up 4.2% from $0.48 in the same prior year period.

PDM saw a roughly 1.8% increase in same store net operating income on a cash basis and a 2.8% increase on an accrual basis year-over-year for the quarter ended June 30th, 2022. The company leased 724,000 square feet in the quarter, including 233,000 of new tenant leasing. The weighted average lease term for leases executed during the second quarter was 6.5 years, excluding one large renewal for US Bank.

As of June 30th, 2022, PDM had no secured debt, and increased the capacity on their line of credit to $600 million. Piedmont's net debt-to-Core EBITDA was 5.5x for the second quarter on an annualized basis, and the debt-to-gross assets ratio was 34.6%. The company entered into a contract to purchase 1180 Peachtree Street, a 41-story office building in the epicenter of Midtown Atlanta, GA, for $465 million. The transaction is expected to close in the third quarter of 2022.

Leadership has downgraded financial estimations for 2022 core funds from operations to be in the range of $1.99 to $2.05 (down from 1.99 to $2.07) per share. As a result, we have downgraded our 2022 core FFO per share estimate by a penny to $2.02.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
CFFO/S	$1.43	$1.46	$1.49	$1.60	$1.67	$1.75	$1.73	$1.79	$1.89	$1.97	***$2.02***	***$2.25***
DPS	$0.80	$0.80	$0.81	$0.84	$0.84	$1.34	$0.84	$0.84	$0.84	$0.84	***$0.84***	***$0.88***
Shares[1]	170.4	165.1	154.6	150.9	145.6	145.4	130.6	126.2	126.1	123.9	***123.0***	***120.0***

Piedmont measures performance using core funds from operations (CFFO) per share, as it provides a more accurate representation of the REIT's cash flow rather earnings per share (EPS), which can include a large amount of depreciation, or the gain on sale of real estate. In the last nine and five years, PDM has managed to grow core FFO by 3.6% and 2.9% annually, on average. While results have been relatively choppy, there exists a long term track record of positive growth. Given the ongoing struggles of the office real estate space due to the COVID pandemic, we estimate PDM will grow core FFO a bit below this range, at roughly 2.0% annually.

[1] In millions

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PDM will focus on growing its real estate concentration in their seven identified growth sub-markets of Atlanta, Boston, Dallas, Minneapolis, New York, Orlando, and Washington, D.C. The Trust believes that working from home should diminish as the pandemic subsides in the U.S. and they are well-positioned to adapt to the updated workforce preferences. The Trust will recycle capital into assets within their targeted submarkets that should benefit from the migration trends that COVID has accelerated. Piedmont has sold more than $1 billion of assets since early 2019 and redeployed into higher yielding assets. Currently there are approximately 1.2 million square feet in leases under an abatement period or yet to commence. Among its peers, PDM has a strong estimated same store cumulative NOI growth from 2018 through 2022 of 4.1% and is priced among the lowest in terms of valuation. PDM's share count, unlike most other REITs, has decreased over the long term, and this is a positive since core FFO is concentrated over a lower number of units, effectively increasing the core FFO per share.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/FFO	12.2	12.7	12.3	11.5	12.1	11.9	10.8	11.5	9.0	9.1	***6.7***	***9.5***
Avg. Yld.	6.0%	4.4%	4.4%	4.5%	4.2%	4.0%	4.5%	4.1%	5.1%	4.7%	***6.2%***	***4.2%***

Piedmont's valuation has trended lower in recent years, with a nine and five year average price-to-core FFO of 11.3 and 10.5. Presently PDM trades at 6.7 times estimated core FFO, and we believe the discount to be a little steep, thus we estimate the Trust can benefit from a 7.2% tailwind to the valuation to reach 9.5 times core FFO.

Safety, Quality, Competitive Advantage, & Recession Resiliency

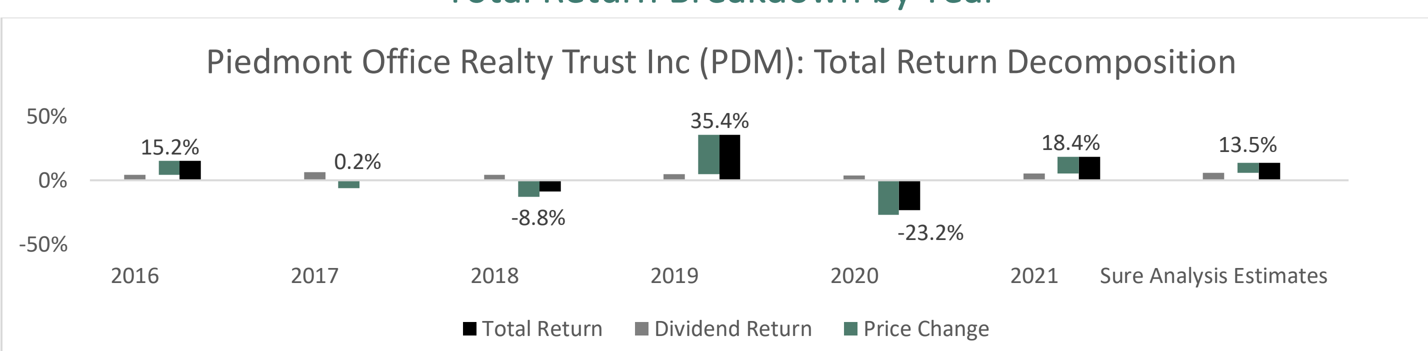
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	56%	55%	54%	53%	50%	77%	49%	47%	44%	43%	***42%***	***40%***

Piedmont Office Realty Trust has a fair payout ratio based on its core FFO, and we believe the distribution is safe. The company has not made a habit of raising the dividend, so as core FFO grows over the long term, the payout ratio decreases. The Trust had not been around during the start of the Great Recession, but we can assume that such a recession would be a risk. While office leases tend to be fairly stable, the pandemic and resulting remote work could result in a permanent paradigm shift, which would result in less office space being required. PDM does not possess any strong competitive advantage, but it's focus on its identified growth submarkets is a strength.

Final Thoughts & Recommendation

Overall, we expect total returns of 13.5% annually, primarily driven by the 6.2% dividend yield as well as a strong valuation tailwind and some earnings growth. The company is trading at a fair discount, and hovers around 71% of our estimated fair value. As a result, we rate Piedmont Office Realty Trust a Buy.

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	521	550	566	585	556	574	526	533	535	529
Gross Profit	315	329	327	343	335	352	317	322	320	318
Gross Margin	60.4%	59.8%	57.7%	58.6%	60.3%	61.3%	60.2%	60.4%	59.8%	60.1%
SG&A Exp.	21	22	24	30	27	29	30	38	27	30
D&A Exp.	161	168	195	196	202	193	166	178	195	
Operating Profit	135	141	108	117	105	128	116	101	89	81
Operating Margin	26.0%	25.6%	19.0%	20.0%	18.8%	22.3%	22.0%	19.0%	16.6%	15.3%
Net Profit	93	99	42	131	100	134	130	229	233	-1
Net Margin	17.9%	18.0%	7.4%	22.5%	17.9%	23.3%	24.8%	43.0%	43.5%	-0.2%
Free Cash Flow	117	39	48	105	122	163	131	105	81	

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4,255	4,666	4,788	4,362	4,368	4,000	3,592	3,517	3,740	3,931
Cash & Equivalents	13	7	12	5	7	7	5	14	7	7
Accounts Receivable	147	169	175	174	163	157	148	141	160	166
Goodwill & Int. Ass.	235	254	250	189	199	177	177	173	190	193
Total Liabilities	1,614	2,205	2,476	2,238	2,270	2,013	1,880	1,698	1,842	2,143
Accounts Payable	127	129	134	128	165	115	94	117	112	114
Long-Term Debt	1,417	2,002	2,270	2,030	2,020	1,727	1,685	1,481	1,622	1,878
Shareholder's Equity	2,639	2,460	2,310	2,122	2,096	1,985	1,710	1,817	1,896	1,786
LTD/E Ratio	0.54	0.81	0.98	0.96	0.96	0.87	0.99	0.82	0.86	1.05

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	2.1%	2.2%	0.9%	2.9%	2.3%	3.2%	3.4%	6.4%	6.4%	0.0%
Return on Equity	3.4%	3.9%	1.8%	5.9%	4.7%	6.5%	7.1%	13.0%	12.5%	-0.1%
ROIC	2.2%	2.3%	0.9%	3.0%	2.4%	3.4%	3.7%	6.8%	6.8%	0.0%
Shares Out.	170.4	165.1	154.6	150.9	145.6	145.4	130.6	126.2	126.1	123.9
Revenue/Share	3.06	3.33	3.66	3.88	3.82	3.95	4.03	4.23	4.24	4.26
FCF/Share	0.68	0.24	0.31	0.70	0.84	1.12	1.00	0.83	0.64	

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