



Paramount Group Inc (PGRE)

Updated July 27th, 2022 by Quinn Mohammed

Key Metrics

Current Price:	\$8	5 Year CAGR Estimate:	12.0%	Market Cap:	\$1.8 B
Fair Value Price:	\$11	5 Year Growth Estimate:	2.0%	Ex-Dividend Date¹:	09/29/2021
% Fair Value:	71%	5 Year Valuation Multiple Estimate:	7.0%	Dividend Payment Date¹:	10/17/2021
Dividend Yield:	4.1%	5 Year Price Target:	\$12	Years of Dividend Growth:	1
Dividend Risk Score:	D	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

Paramount Group Inc is a real estate investment trust which acquires, manages, and redevelops office properties in the central business district submarkets of New York City, Washington DC, and San Francisco. Paramount's primary customers are financial services firms, legal services firms, and technology and media industries. The trust was established in 1978, and the current president and CEO, Albert Behler, has been at the helm since 1991. Paramount owns or has an interest in 14.0 million square feet of high quality office building investments, retail property, and debt and equity investments. Paramount Group trades on the NYSE under the ticker symbol PGRE and is one of the largest publicly-owned real estate companies headquartered in New York, NY. PGRE has a market capitalization of \$1.8 billion.

On March 15th, 2022, Paramount announced a 10.7% increase to the dividend, from \$0.07 quarterly to \$0.0775.

PGRE released second quarter results on July 26th. The trust announced core funds from operations (FFO) of \$53.6 million, or \$0.24 per diluted share. Results compare favorably to the prior year's \$47.6 million, or \$0.22 per diluted share. Paramount also reported a 5.6% increase in same store cash net operating income (NOI) and a 9.0% increase in same store NOI compared to the prior year.

The trust leased a total of 250,231 square feet during the quarter. This strong leasing led to an 80 basis point increase in the occupancy rate, to 91.4% at Q2 2022 end.

Leadership slightly upgraded guidance for the 2022 fiscal year and core FFO estimates. Paramount estimates core FFO to come in between \$0.95 and \$0.99 (up from \$0.93 and \$0.97), for a mid-point of \$0.97.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Core FFO				\$0.81	\$0.89	\$0.87	\$0.94	\$0.90	\$0.96	\$0.92	\$0.97	\$1.07
DPS				\$0.42	\$0.38	\$0.38	\$0.40	\$0.40	\$0.37	\$0.28	\$0.31	\$0.33
Shares²				212.1	218.1	236.4	239.6	231.5	222.4	218.7	225.0	250.0

While Paramount Group is a trust with a long history, being established in 1978, it has only been publicly-traded for a short period of time. Thus, we can only use historical data back to 2015 to form an opinion and estimate forward growth. Since 2015, PGRE has grown adjusted FFO at a rate of 2.1% annually, which is low but positive. The trust managed to grow year-over-year into the pandemic year, but it slashed its dividend and its valuation plummeted. We believe the trust can continue growing at roughly 2.0% per year.

The trust derives almost all of annualized rent from its office properties, which limits their retail exposure which suffered greatly in 2020. The trust led in same store cash NOI growth from 2017 to 2020 among its peers. Paramount has embedded rent growth within the portfolio due to strong historical and projected future rental rate growth in their submarkets, and contractual fixed rental rate increases in leases and rent from the lease-up of vacant and expiring leases. The trust targets acquisitions opportunities with a value-add component where PGRE can leverage their

¹ Estimate

² In millions

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operating expertise, tenant relationships, and asset and property management approach. The trust will also incrementally grow AFFO with value-add renovations and redevelopments of office properties.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/AFFO				22.4	18.3	18.6	15.7	15.4	9.4	10.4	7.8	11.0
Avg. Yld.				2.3%	2.3%	2.4%	2.6%	2.9%	4.7%	3.4%	4.1%	2.8%

The current P/AFFO of 7.8 is fairly discounted in comparison to its average nine- and five-year valuations of 15.7 and 13.9. Despite the ongoing pandemic, PGRE has shielded itself from the dangers of retail properties by focusing primarily on office properties. Still, the possibility of permanent remote work taking off and the necessity of office properties diminishing is real. This, in addition to lower occupancy, causes us to discount our valuation estimate, to trade at roughly 11.0 times core FFO. The 4.1% yield is above the average yield of 3.2%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

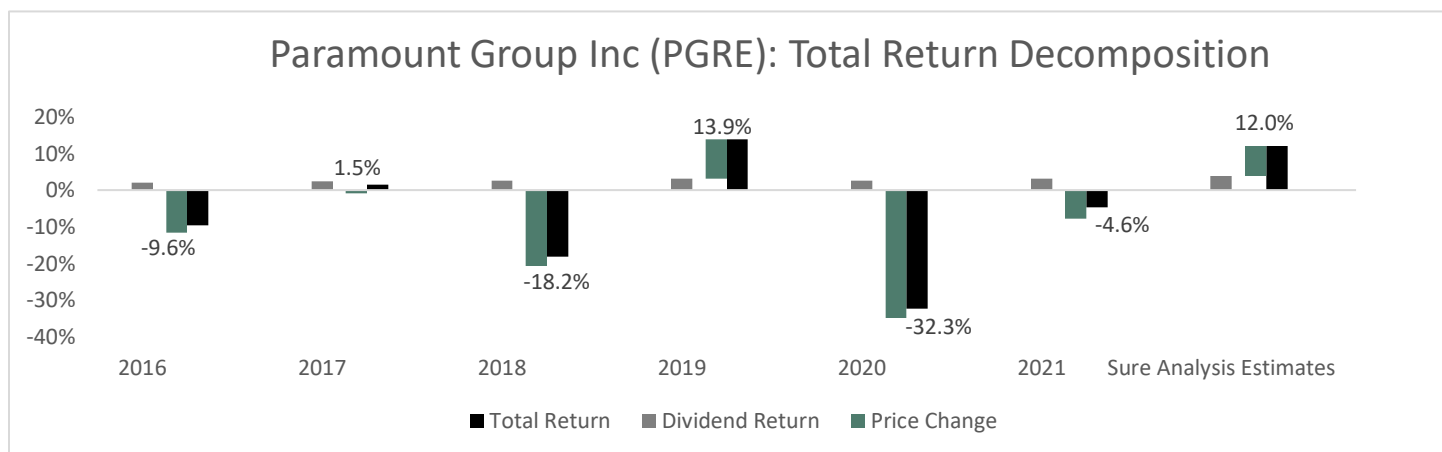
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout				52%	43%	44%	43%	44%	39%	30%	32%	30%

Paramount's dividend has been choppy since it was instated in 2015, and the pandemic brought it to its lowest rate of \$0.28 in 2021, even though the dividend appeared to be fairly covered by adjusted FFO. The trust believes that their proven acquisition and operating expertise enables them to gain advantages over competitors through superior acquisition sourcing, focused leasing programs, active asset and property management and first-class tenant service. The trust was not publicly traded at the time of the Great Recession, and we believe the trust would only be moderately recession resistant given the stickiness of office leases. We would have expected a dividend cut if the trust were trading at the time, as it has cut during the pandemic.

Final Thoughts & Recommendation

Paramount Group has a long history as a trust but only recently came to the public markets, debuting only five years prior to the pandemic. It cut the dividend during this time, even though it was fairly covered by AFFO. The 4.2% dividend yield is fair for an REIT. However, we also estimate a 7.0% tailwind due to the valuation expansion, and the trust can reasonably be expected to grow AFFO by 2.0% from here on out. Paramount Group trades at 71% of our fair value estimate, and with total expected returns of 12%, we rate shares a buy, but caution investors that the dividend may not be a reliable one.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	54	59		662	683	719	708	744	714	727
Gross Profit	39	42		418	433	453	453	479	447	461
Gross Margin	71.6%	72.4%		63.1%	63.4%	63.0%	64.0%	64.4%	62.5%	63.5%
SG&A Exp.	46	57		42	54	62	58	69	65	59
D&A Exp.	10	11		295	269	266	258	248	236	232
Operating Profit	-24	-30		81	110	125	155	170	147	170
Op. Margin	-43.7%	-50.5%		12.2%	16.1%	17.4%	21.8%	22.9%	20.5%	23.4%
Net Profit	2	17		-4	-10	86	9	-37	-25	-20
Net Margin	4.2%	28.2%		-0.7%	-1.5%	12.0%	1.3%	-5.0%	-3.5%	-2.8%
Free Cash Flow	-83	33		-17	148	190	157	285	237	244
Provision for Tax	7	11		3	2	5	3	0	1	4

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	2,612	2,923	9,030	8,775	8,867	8,918	8,756	8,734	8,554	8,495
Cash & Equivalents	305	307	439	144	163	219	340	306	435	525
Accts. Receivable	5	10	8	11	15	17	20	19	18	16
Goodwill & Int.		0	669	511	412	352	270	203	154	119
Total Liabilities	874	897	3,475	3,465	3,981	3,896	3,864	4,103	4,038	40,40
Accounts Payable	4	11	93	103	104	118	124	117	102	116
Long-Term Debt	517	500		2,988	3,595	3,541	3,567	3,821	3,801	3,836
Total Equity	420	322	3,911	3,761	3,990	4,177	4,001	3,786	3,653	3,588
LTD/E Ratio	1.23	1.55		0.79	0.90	0.85	0.89	1.01	1.04	1.07

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets		0.6%		-0.1%	-0.1%	1.0%	0.1%	-0.4%	-0.3%	-0.2%
Return on Equity		4.4%		-0.1%	-0.3%	2.1%	0.2%	-0.9%	-0.7%	-0.6%
ROIC		0.7%		-0.1%	-0.1%	1.0%	0.1%	-0.4%	-0.3%	-0.2%
Shares Out.				212.1	218.1	236.4	239.6	231.5	222.4	218.7
Revenue/Share	0.22	0.24		3.12	3.13	3.04	2.95	3.21	3.21	3.32
FCF/Share	-0.34	0.14		-0.08	0.68	0.80	0.65	1.23	1.07	1.12

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

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