



Whitestone REIT (WSR)

Updated November 8th, 2022 by Kay Ng

Key Metrics

Current Price:	\$9	5 Year CAGR Estimate:	11.4%	Market Cap:	\$460M
Fair Value Price:	\$11	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	12/01/22
% Fair Value:	83%	5 Year Valuation Multiple Estimate:	3.8%	Dividend Payment Date:	12/14/22
Dividend Yield:	5.2%	5 Year Price Target	\$13	Years Of Dividend Growth:	1
Dividend Risk Score:	D	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

Whitestone is a retail REIT that owns about 60 properties with about 5.2 million square feet of gross leasable area primarily in top U.S. markets in Texas and Arizona. Its tenant base is very diversified with about 1,592 tenants. The top 5 industries are roughly as follows: restaurant & food service (23% of annual base rent (ABR)), salons (9%), grocery (9%), financial services (8%), and medical & dental (8%). Whitestone was founded in 1998 and headquartered in Houston, Texas.

Whitestone reported its third-quarter 2022 results on 11/1/22 for which it witnessed an all-time high occupancy rate. For the quarter, revenue growth was 9.2% to \$35.4 million versus Q3 2021. Funds from operations per share ("FFOPS") growth was 9.1% to \$0.24. Same-store net operating income ("SSNOI") rose 4.5% to \$21.6 million. Occupancy for wholly owned properties improved to 92.5% versus 89.9% a year ago. As well, rental rate growth was 19.2%, up from 13.1% a year ago, driven by a strong rebound in rental rate growth in renewal leases (to 16.5% vs. 5.4% a year ago) and new leases (to 20.0% vs. 14.1% a year ago).

Whitestone improved its 2022 guidance, including same-store NOI growth of about 6.0% and also expects 2022 FFO per share to increase to \$1.00-\$1.02. It forecasts the same ending occupancy of about 92.5%. We improve marginally our 2022 FFOPS estimate to the midpoint of \$1.01.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
FFOPS	N/A	\$0.79	\$0.96	\$1.04	\$0.93	\$0.95	\$0.97	\$0.90	\$0.83	\$0.86	\$1.01	\$1.17
DPS	\$1.14	\$1.14	\$1.14	\$1.14	\$1.14	\$1.14	\$1.14	\$1.14	\$0.42	\$0.43	\$0.48	\$0.67
Shares¹	16.8	21.9	22.8	27.0	29.2	38.5	39.8	40.6	43.3	50.0	50.0	67.0

Since Whitestone began reporting FFO, it has seen minimal growth in its FFOPS. This is not a result of decreased FFO but an increase in shares outstanding. The REIT has been issuing shares to fund acquisitions. Between 2016 and 2021, Whitestone issued more than 20 million shares. As a result, there was no dividend growth from 2016 to 2019 and a dividend cut occurred during the pandemic. In February 2022, the company raised its dividend by 11.6% which equates to an annualized payout of \$0.48 per share. This follows the February 2021 dividend, which could be the start of a dividend growth trend if WSR can continue growing its FFOPS and healthily increase the dividend. For now, we use an estimated dividend growth rate of 7% through 2027, which would lead to a sustainable payout ratio of ~60% for a REIT.

Management believes, post-pandemic, investments in acquisitions, re-development, and development projects can drive returns of at least 10%. The continuation of SSNOI growth since Q1 2021 is a good sign. We would like to see it stay that way, hopefully supported by a positive macro environment as we get used to having COVID-19 around. For now, we estimate a FFOPS growth rate of 3% through 2027 on a steady recovery. We would improve our estimates if/when we see the REITs' investments paying off.

¹ Shares 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
P/FFO	--	16.6	15.8	11.5	15.5	15.2	12.9	14.6	9.2	9.6	9.1	11.0
Avg. Yld.	--	--	7.5%	9.5%	7.9%	7.9%	9.3%	8.7%	5.5%	4.5%	5.2%	5.2%

From 2017 to 2021, Whitestone traded at a price to funds from operations multiple (P/FFO) of 12.3. In a rising interest rate environment, REIT valuations have been pressured. So, we now target a fair P/FFO of 11.0.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	--	144%	119%	110%	123%	120%	118%	127%	51%	50%	48%	57%

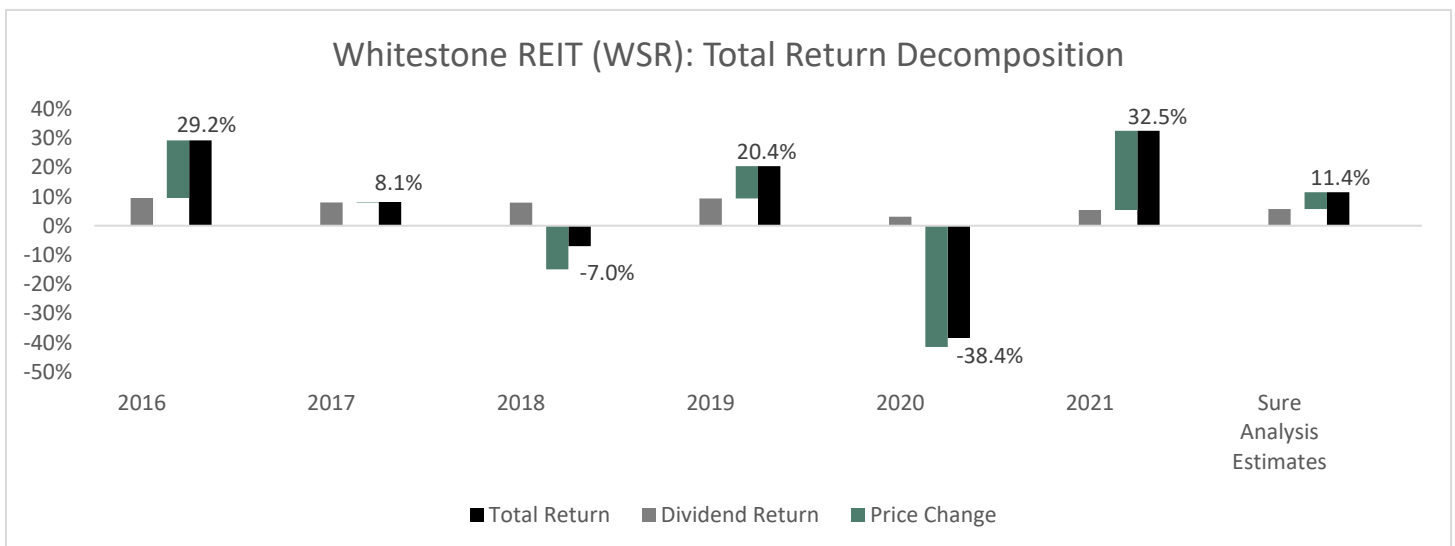
Whitestone had some financial troubles during the previous recession in 2008. From 2007 to 2008, its rental income dropped by \$5.8 million, and it took until 2012 for the rental income to return to the 2007 highs. Whitestone cut its dividend by 63% in 2020. It looked like it was ready to steadily increase its dividend to the pre-pandemic levels starting with a cautious increase of 2.4% in February 2021 followed by another dividend hike in February 2022. Currently, the payout ratio of about 50% is sustainable.

At the end of Q3 2022, Whitestone had a debt-to-equity ratio of 1.68, an improvement from Q3 2021's 1.74. At quarter end, the REIT had \$9.5 million in cash and cash equivalents. Moreover, its payout ratio is much more sustainable than pre-pandemic levels because of a lower dividend and improving FFO. Whitestone has remaining debt of about \$1.1 million due this year.

Final Thoughts & Recommendation

Whitestone has an expected annualized total return of 11.4% over the next five years, coming from a 5.2% dividend yield, 3% growth, and 3.8% valuation expansion. Concerns surrounding this REIT include rising interest rates, what is its normal growth rate in the normalized environment post-pandemic, and it's an unfavorable environment for share issuances to fund acquisitions. So, it has less levers to pull to drive growth. We rate the stock as a "buy", but better dividend ideas can be discovered in the Sure Dividend coverage universe.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	45	60	72	93	104	126	120	119	118	125
Gross Profit	28	38	47	62	70	84	82	82	79	86
Gross Margin	62.6%	62.5%	65.3%	66.5%	67.4%	66.6%	68.8%	69.1%	67.3%	68.6%
SG&A Exp.	8	11	15	20	24	24	23	22	21	23
D&A Exp.	10	13	16	20	22	27	26	27	28	29
Operating Profit	11	14	16	22	24	33	33	34	30	34
Operating Margin	23.7%	22.8%	22.4%	23.6%	22.9%	25.9%	27.9%	28.5%	25.2%	27.5%
Net Profit	0	4	8	7	8	8	21	24	6	12
Net Margin	0.1%	6.3%	10.5%	7.2%	7.6%	6.6%	17.9%	19.9%	5.1%	9.6%
Free Cash Flow	11	24	26	36	41	41	40	48	43	47
Income Tax	0	0	0	0	0	0	0	0	0	0

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	385	508	634	782	855	1070	1029	1056	1045	1102
Cash & Equivalents	7	6	4	3	4	5	14	16	26	16
Accounts Receivable	8	10	12	15	20	21	21	23	23	22
Total Liabilities	212	287	421	535	588	712	670	703	707	703
Accounts Payable	14	13	16	24	29	36	34	39	51	46
Long-Term Debt	191	261	394	498	544	659	618	645	644	643
Shareholder's Equity	166	216	210	243	256	348	350	345	332	393
LTD/E Ratio	1.15	1.21	1.88	2.05	2.13	1.90	1.76	1.87	1.94	1.64

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.0%	0.8%	1.3%	1.0%	1.0%	0.9%	2.0%	2.3%	0.6%	1.1%
Return on Equity	0.0%	2.0%	3.6%	3.0%	3.2%	2.8%	6.1%	6.8%	1.8%	3.3%
ROIC	0.0%	0.9%	1.4%	1.0%	1.0%	0.9%	2.1%	2.4%	0.6%	1.2%
Shares Out.	16.8	21.9	22.8	27.0	29.2	38.5	39.8	40.6	43.3	50.0
Revenue/Share	3.31	3.31	3.18	3.64	3.68	3.47	2.95	2.88	2.74	2.71
FCF/Share	0.82	1.31	1.13	1.41	1.43	1.14	0.97	1.15	1.00	1.02

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

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