



Choice Properties REIT (PPRQF)

Updated February 27th, 2023 by Samuel Smith

Key Metrics

| | | | | | |
|-----------------------------|--------|--|--------|----------------------------------|----------|
| Current Price: | \$10.8 | 5 Year CAGR Estimate: | -2.9% | Market Cap: | \$7.8B |
| Fair Value Price: | \$4.7 | 5 Year Growth Estimate: | 6.7% | Ex-Dividend Date: | 02/27/23 |
| % Fair Value: | 230% | 5 Year Valuation Multiple Estimate: | -15.3% | Dividend Payment Date: | 03/15/23 |
| Dividend Yield: | 5.2% | 5 Year Price Target | \$7 | Years Of Dividend Growth: | 2 |
| Dividend Risk Score: | F | Retirement Suitability Score: | D | Rating: | Sell |

Overview & Current Events

Choice Properties Real Estate Investment Trust invests in commercial real estate properties across Canada. The company has a high-quality real estate portfolio of over 700 properties which makes up over 60 million square feet of gross leasable area (GLA). Choice Properties' portfolio is made up of over 700 properties, including retail, industrial, office, multi-family, and development assets. Over 500 of Choice Properties' investments are to their largest tenant, Canada's largest retailer, Loblaw. This \$7.8 billion market capitalization company is listed on the Toronto Stock Exchange under the trading symbol 'CHP-UN', or in the United States on the over-the-counter market under the trading symbol 'PPRQF'.

Choice Properties announced its Q4 results on February 16, 2023. The net loss for the quarter was \$579.0 million, which is an increase of \$415.9 million from the net loss of \$163.1 million in Q4 2021. This increase was due to an unfavorable adjustment of \$486.8 million to the fair value of the Trust's Exchangeable Units, caused by the increase in the Trust's unit price, and an unfavorable adjustment of \$20.8 million to the fair value of the Trust's investment in real estate securities of Allied, due to the decrease in Allied's unit price. However, there was a net fair value gain of \$193.4 million on investment properties on a GAAP basis, as compared to a gain of \$96.3 million in Q4 2021, which partially offset the losses. Additionally, there was a net fair value gain of \$207.2 million on a proportionate share basis for Q4 2022, primarily attributed to leasing and cash flow growth in the industrial portfolio.

Growth on a Per-Share Basis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| AFFO/S | \$0.33 | \$0.59 | \$0.57 | \$0.62 | \$0.70 | \$0.62 | \$0.64 | \$0.63 | \$0.64 | \$0.63 | \$0.47 | \$0.65 |
| DPS | \$0.30 | \$0.54 | \$0.51 | \$0.52 | \$0.56 | \$0.57 | \$0.56 | \$0.58 | \$0.58 | \$0.56 | \$0.56 | \$0.57 |
| Shares¹ | 87.6 | 89.3 | 91.0 | 92.6 | 94.3 | 278.2 | 310.3 | 326.9 | 327.6 | 327.8 | 327.8 | 350 |

For Choice Properties' primary growth metric, we used adjusted funds from operations per share (FFO/S) instead of the typical EPS, since AFFO/S gives a much more accurate picture of a REIT's performance. Choice Properties only has reportable operations starting in the third quarter of 2013, which explains why the company's 2013 values are significantly lower.

Given the strength of its portfolio and its low expected AFFO per share this year, we are expecting a 6.7% AFFO/share CAGR moving forward as the REIT will recover its former earnings power over the next half decade.

Choice Properties has sustained or grown their dividend steadily on a same-currency basis since 2015. The company kept the dividend at an annualized \$0.65 (CAD) for their first three years of operations. The company's average annual dividend growth rate after that was respectable in the low single digits before dividend growth had to pause due to headwinds facing the retail industry and COVID-19. Going forward, we expect Choice Properties to keep their dividend steady to allow the company's cash flow generation to generate a greater coverage ratio for the payouts. We also note that the dividend can move up or down when it is converted into US dollars depending on current exchange rates.

¹ In millions

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Valuation Analysis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | Now | 2028 |
|-----------|------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------------|-------------|
| P/FFO | N/A | 11.5 | 12.2 | 13.5 | 12.5 | 11.2 | 13.5 | 15.1 | 18.2 | 17.0 | 23.0 | 10.0 |
| Avg. Yld. | N/A | 7.30% | 7.50% | 5.20% | 6.50% | 8.30% | 6.30% | 5.20% | 4.90% | 5.20% | 5.2% | 8.8% |

Choice Properties' average price to funds from operations ratio (P/FFO) has remained around 12-13 for much of their reportable years. Comparing the current P/FFO ratio to their historic average, Choice Properties is overvalued. Furthermore, we view 10 times FFO as a fair valuation given the REIT's heavy exposure to the out-of-favor retail sector. As a result, we expect significant headwinds to total returns moving forward stemming from a contracting valuation multiple.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|--------|------|------|------|------|------|------|------|------|------|------|-------------|------------|
| Payout | 91% | 92% | 89% | 84% | 80% | 92% | 88% | 92% | 91% | 89% | 119% | 88% |

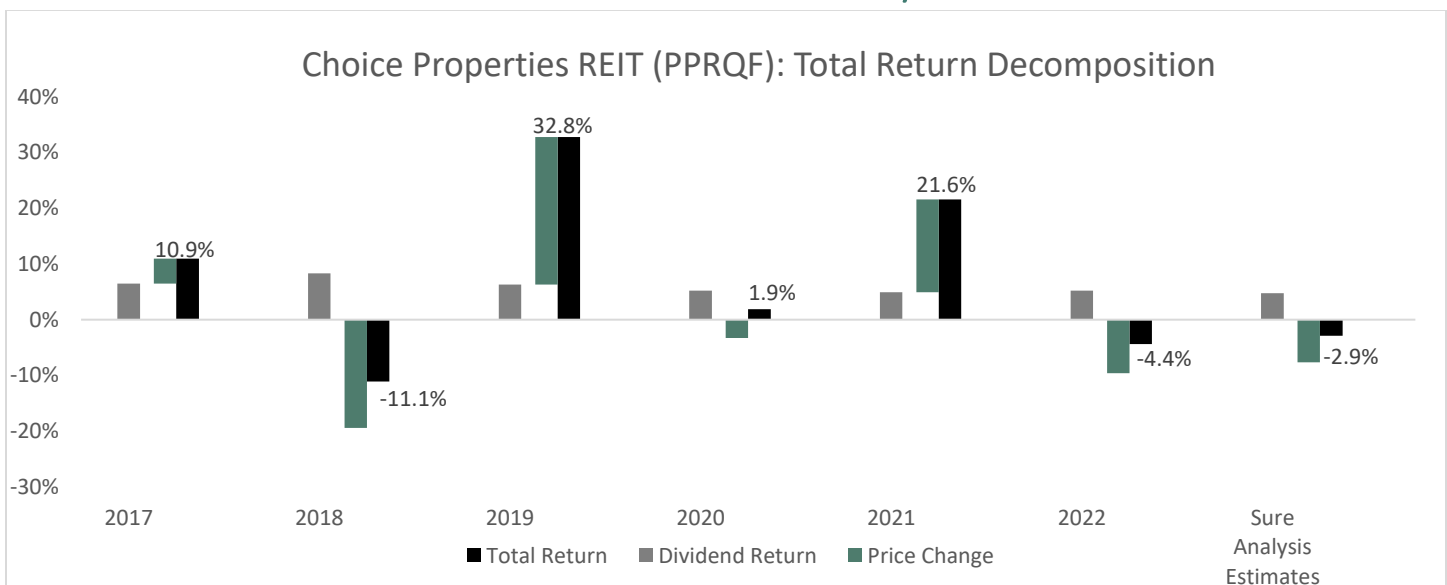
Choice Properties' portfolio has outsized exposure to Loblaw, making the REIT rather dependent on Loblaw's continued operations. One benefit of their strategic alliance with Loblaw is long-term leases, which gives some certainty for future earnings. Choice Properties has not been around for a recessionary period, so to predict how the company would perform in a recession we observed similar companies' performance in a recession.

The most similar company we found to Choice Properties is Crombie Real Estate (CRR-U), which also operates a REIT out of Canada with a portfolio designed like Choice Properties' portfolio. During the last recession, The Great Recession in 2008-2009, Crombie Real Estate's FFO/S decreased by nearly 19%, which is a relatively solid performance all things considered.

Final Thoughts & Recommendation

Overall, we expect annualized total returns of -2.9% over the next half decade, mainly driven by the 5.2% dividend yield and mid-single-digit FFO-per-share growth rate, but fully offset by considerable expected multiple compression. Given the weak total return potential and the company's large exposure to retail, we rate it as a Sell.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|------------------|-------|-------|--------|--------|-------|-------|--------|-------|-------|-------|
| Revenue | 309 | 619 | 582 | 592 | 641 | 886 | 971 | 948 | 1,031 | 972 |
| Gross Profit | 232 | 462 | 432 | 440 | 479 | 643 | 693 | 662 | 727 | 692 |
| Gross Margin | 75.0% | 74.7% | 74.1% | 74.4% | 74.8% | 72.6% | 71.4% | 69.8% | 70.6% | 71.2% |
| SG&A Exp. | 12 | 21 | (1) | 22 | 19 | 27 | 30 | 27 | 32 | 36 |
| Operating Profit | 220 | 441 | 414 | 418 | 461 | 616 | 662 | 628 | 695 | 655 |
| Operating Margin | 71.0% | 71.3% | 71.1% | 70.6% | 71.9% | 69.6% | 68.1% | 66.2% | 67.4% | 67.4% |
| Net Profit | 65 | 181 | (122) | (168) | 312 | 501 | (438) | 336 | 18 | 572 |
| Net Margin | 21.1% | 29.2% | -20.9% | -28.5% | 48.7% | 56.6% | -45.1% | 35.5% | 1.8% | 58.9% |
| Free Cash Flow | 254 | 428 | 414 | 400 | 389 | 313 | 437 | 464 | 534 | 487 |
| Income Tax | | | | | - | 0 | (1) | (1) | (1) | (0) |

Balance Sheet Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|----------------------|------|------|------|------|------|-------|-------|-------|-------|-------|
| Total Assets | 6995 | 7057 | 6418 | 6998 | 7891 | 11416 | 11924 | 12271 | 12684 | 12393 |
| Cash & Equivalents | 48 | 1 | 32 | 4 | 5 | 23 | 32 | 163 | 66 | 48 |
| Accounts Receivable | 8 | 8 | 4 | 11 | 17 | 29 | 46 | 61 | 57 | 59 |
| Goodwill & Int. Ass. | | | | | - | 22 | 23 | 23 | 22 | 237 |
| Total Liabilities | 6176 | 6163 | 5810 | 6570 | 7146 | 8847 | 9553 | 9508 | 10088 | 16 |
| Accounts Payable | 198 | 335 | 316 | 351 | 339 | | 383 | 373 | 469 | 9575 |
| Long-Term Debt | 3171 | 3064 | 2797 | 3041 | 3418 | 5270 | 5007 | 5086 | 4886 | 426 |
| Shareholder's Equity | 819 | 888 | 602 | 422 | 738 | 2564 | 2366 | 2756 | 2596 | 4827 |

Profitability & Per Share Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|------------------|------|-------|--------|--------|-------|-------|--------|-------|-------|-------|
| Return on Assets | | 2.6% | -1.8% | -2.5% | 4.2% | 5.2% | -3.8% | 2.8% | 0.1% | 4.6% |
| Return on Equity | | 21.2% | -16.3% | -32.9% | 53.8% | 30.4% | -17.8% | 13.1% | 0.7% | 21.1% |
| ROIC | | 5.8% | -4.1% | -5.8% | 9.6% | 11.5% | -8.5% | 6.7% | 0.4% | 7.6% |
| Shares Out. | 87.6 | 89.3 | 91.0 | 92.6 | 94.3 | 278.2 | 310.3 | 326.9 | 327.6 | 327.8 |
| Revenue/Share | 0.85 | 6.93 | 6.40 | 6.39 | 6.80 | 3.19 | 3.13 | 2.90 | 3.15 | 1.34 |
| FCF/Share | 0.70 | 4.79 | 4.55 | 4.33 | 4.12 | 1.12 | 1.41 | 1.42 | 1.63 | 0.67 |

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

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