# American Assets Trust (AAT)

*Updated April 26th, 2023 by Aristofanis Papadatos*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $17 | **5 Year CAGR Estimate:** | 25.1% | **Market Cap:** | $1.4 B |
| **Fair Value Price:** | $38 | **5 Year Growth Estimate:** | 3.0% | **Ex-Dividend Date:** | 6/7/2023 |
| **% Fair Value:** | 44% | **5 Year Valuation Multiple Estimate:** | 17.7% | **Dividend Payment Date:** | 6/22/2023 |
| **Dividend Yield:** | 7.8% | **5 Year Price Target** | $45 | **Years Of Dividend Growth:** | 3 |
| **Dividend Risk Score:** | D | **Retirement Suitability Score:** | C | **Rating:** | Buy |

## Overview & Current Events

American Assets Trust (AAT) is a real estate investment trust (REIT) that was formed in 2011 as a successor of American Assets, a privately held company founded in 1967. AAT is headquartered in San Diego, California, and has great experience in acquiring, improving and developing office, retail and residential properties throughout the U.S., primarily in Southern California, Northern California, Oregon, Washington and Hawaii. Its office portfolio and its retail portfolio comprise of approximately 4.0 million and 3.1 million square feet, respectively. AAT also owns more than 2,000 multifamily units and has a market capitalization of $1.4 billion.

In late April, AAT reported (4/25/23) financial results for the first quarter of fiscal 2023. Same-store net operating income grew 6.5% and funds from operations (FFO) per share grew 16% over the prior year's quarter. The positive performance resulted primarily from a settlement payment received but also from rent hikes and increased tourism in Hawaii, partly offset by higher operating expenses and interest expense. The REIT has decelerated in the last two quarters, as it has begun to face tough comparisons over the strong performance in 2022. It slightly improved its guidance for its FFO per share in 2023, from $2.16-$2.30 to $2.23-$2.33. We note that AAT has beaten the analysts' estimates for 9 consecutive quarters and maintain our annual forecast of $2.25. We also note that the REIT appears resilient to high inflation thanks to its ability to raise rental rates every year. AAT has raised its dividend by 3% this year.

## Growth on a Per-Share Basis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **FFO** | $1.55 | $1.63 | $1.77 | $1.85 | $1.92 | $2.09 | $2.19 | $1.89 | $2.00 | $2.34 | ***$2.25*** | ***$2.61*** |
| **DPS** | $0.85 | $0.89 | $0.95 | $1.01 | $1.05 | $1.09 | $1.14 | $1.00 | $1.16 | $1.28 | ***$1.32*** | ***$1.60*** |
| **Shares**[1] | 57.5 | 59.9 | 62.3 | 63.2 | 64.1 | 64.1 | 70.8 | 76.1 | 76.2 | 76.3 | ***76.4*** | ***100.0*** |

AAT pursues growth by acquiring properties in submarkets with favorable supply and demand characteristics, including high barriers to entry. It also redevelops several of its newly-acquired properties in order to enhance their value. In addition, it has a capital recycling strategy, which involves selling properties whose returns seem to have been maximized and buying high-return properties. Thanks to these growth drivers, AAT has grown its adjusted FFO per share at a 4.7% average annual rate over the last decade. Its FFO per share decreased for the first time in a decade in 2020 due to the pandemic but AAT has recovered from this crisis. We expect the REIT to grow its FFO per share at a 3.0% average annual rate over the next five years, below its historical growth rate due to somewhat high interest expense.

## Valuation Analysis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | Now | 2028 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **P/FFO** | 20.5 | 21.4 | 23.2 | 22.0 | 21.2 | *17.6* | 20.8 | 15.9 | 17.8 | 13.4 | ***7.6*** | ***17.1*** |
| **Avg. Yld.** | 2.7% | 2.6% | 2.3% | 2.5% | 2.6% | *3.0%* | 2.5% | 3.3% | 3.3% | 4.1% | ***7.8%*** | ***3.6%*** |

AAT is trading at a 10-year low price-to-FFO ratio of 7.6, which is much lower than the 10-year average price-to-FFO ratio of 19.4. The somewhat rich historical valuation of AAT has resulted from its consistent growth year after year, until the

[1] 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.*

onset of the pandemic. The depressed current valuation has resulted from the impact of high interest rates on interest expense. In order to be on the safe side, we assume a fair price-to-FFO ratio of 17.1, which is equal to the 5-year average of the stock. If AAT trades at that level in five years, it will enjoy a 17.7% annualized gain in its returns.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Payout** | 55% | 55% | 54% | 55% | 55% | 52% | 52% | 53% | 58% | 55% | ***59%*** | ***61%*** |

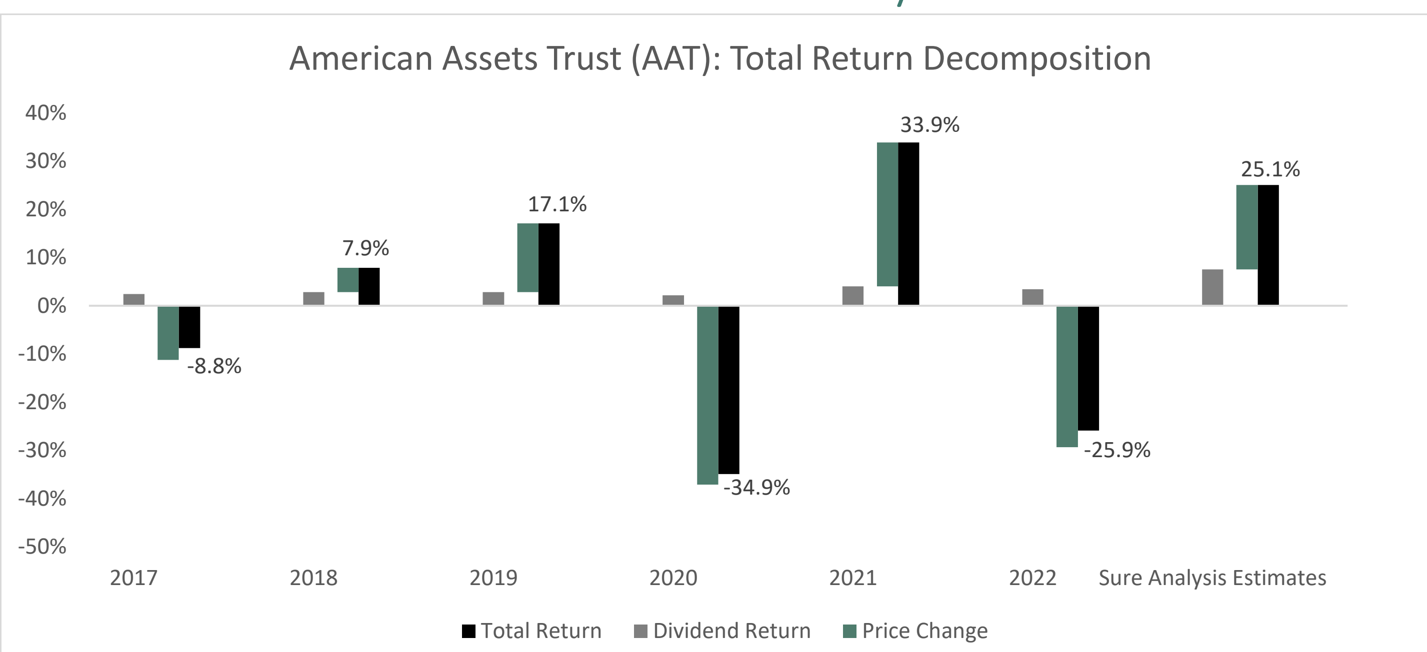
Many of the properties of AAT are located in in-fill locations, where developable land is scarce and zoning regulations significantly restrict new development. Moreover, its submarkets in Southern California, Northern California, Oregon, Washington and Hawaii are characterized by high barriers to entry, which offer the REIT a strong negotiating position with its tenants and enable it to implement material rent hikes every year.

AAT is offering a 10-year high dividend yield of 7.8%. Given the healthy payout ratio of 59% and the reliable growth trajectory of the REIT, the dividend is safe. The only caveat is the material debt load of AAT, which has an interest coverage ratio of only 1.9, much less than our comfort minimum of 3.0. On the bright side, AAT has received investment grade ratings from the major rating agencies. Given the promising growth potential of AAT, we do not expect it to face any problems servicing its debt for the foreseeable future but investors should be aware of this risk factor, which renders the REIT somewhat vulnerable to recessions. AAT was not public in the Great Recession, and hence it has not been tested in a severe recession. AAT cut its dividend by -12% in 2020 due to the pandemic.

## Final Thoughts & Recommendation

AAT has plunged -52% over the last 12 months due to the impact of inflation on its valuation and the impact of high interest rates on its interest expense. We view these headwinds as temporary and hence we view the stock as attractive. The stock could offer a 25.1% average annual return over the next five years, thanks to 3.0% growth of FFO per share, a 7.8% dividend yield and a 17.7% annualized valuation tailwind. The security maintains its buy rating but we note that patience may be required until inflation and interest rates revert to normal levels.

## Total Return Breakdown by Year

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## Income Statement Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 255 | 260 | 276 | 295 | 315 | 331 | 367 | 345 | 376 | 423 |
| Gross Profit | 165 | 169 | 178 | 187 | 198 | 209 | 235 | 223 | 246 | 270 |
| Gross Margin | 64.7% | 64.9% | 64.4% | 63.4% | 63.0% | 63.3% | 64.0% | 64.8% | 65.5% | 63.8% |
| SG&A Exp. | 17 | 19 | 20 | 18 | 21 | 23 | 25 | 27 | 30 | 32 |
| D&A Exp. | 67 | 67 | 63 | 71 | 83 | 107 | 96 | 108 | 116 | 123 |
| Operating Profit | 81 | 84 | 94 | 98 | 94 | 80 | 114 | 89 | 100 | 115 |
| Operating Margin | 31.8% | 32.2% | 34.2% | 33.2% | 29.7% | 24.0% | 31.0% | 25.7% | 26.6% | 27.2% |
| Net Profit | 23 | 31 | 54 | 46 | 40 | 27 | 60 | 36 | 37 | 56 |
| Net Margin | 8.9% | 12.0% | 19.6% | 15.5% | 12.7% | 8.2% | 16.4% | 10.3% | 9.7% | 13.2% |
| Free Cash Flow | 37 | (39) | (24) | 61 | 98 | 82 | 65 | 63 | 64 | 65 |

## Balance Sheet Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 20222 |
|---|---|---|---|---|---|---|---|---|---|---|
| Total Assets | 1,832 | 1,942 | 1,974 | 1,987 | 2,260 | 2,198 | 2,790 | 2,817 | 3,018 | 2,988 |
| Cash & Equivalents | 49 | 59 | 40 | 45 | 83 | 48 | 99 | 137 | 140 | 50 |
| Accounts Receivable | 7 | 7 | 8 | 9 | 10 | 9 | 12 | 7 | 7 | 8 |
| Goodwill & Int. Ass. | 33 | 24 | 18 | 12 | 10 | 10 | 34 | 29 | 32 | 64 |
| Total Liabilities | 1,146 | 1,175 | 1,145 | 1,148 | 1,416 | 1,396 | 1,497 | 1,564 | 1,808 | 1,802 |
| Accounts Payable | 37 | 51 | 32 | 32 | 38 | 47 | 63 | 59 | 65 | 66 |
| Long-Term Debt | 1,045 | 1,063 | 1,056 | 1,062 | 1,325 | 1,291 | 1,358 | 1,407 | 1,649 | 1,648 |
| Shareholder's Equity | 649 | 735 | 800 | 810 | 834 | 803 | 1,314 | 1,271 | 1,239 | 1,221 |
| D/E Ratio | 1.61 | 1.45 | 1.32 | 1.31 | 1.59 | 1.61 | 1.03 | 1.11 | 1.33 | 1.35 |

## Profitability & Per Share Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|
| Return on Assets | 1.2% | 1.7% | 2.8% | 2.3% | 1.9% | 1.2% | 2.4% | 1.3% | 1.3% | 1.9% |
| Return on Equity | 3.5% | 4.5% | 7.0% | 5.7% | 4.9% | 3.3% | 5.7% | 2.8% | 2.9% | 4.5% |
| ROIC | 1.3% | 1.7% | 2.9% | 2.4% | 2.0% | 1.3% | 2.5% | 1.3% | 1.3% | 2.0% |
| Shares Out. | 57.5 | 59.9 | 62.3 | 63.2 | 64.1 | 64.1 | 70.8 | 76.1 | 76.2 | 76.23 |
| Revenue/Share | 4.43 | 4.34 | 4.42 | 4.67 | 4.91 | 5.16 | 5.18 | 4.53 | 4.93 | 5.54 |
| FCF/Share | 0.64 | (0.65) | (0.38) | 0.97 | 1.53 | 1.28 | 0.93 | 0.83 | 0.84 | 0.86 |

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