



Office Properties Income Trust (OPI)

Updated April 28th, 2023 by Aristofanis Papadatos

Key Metrics

Current Price:	\$6.50	5 Year CAGR Estimate:	27.4%	Market Cap:	\$318 M
Fair Value Price:	\$17	5 Year Growth Estimate:	0.0%	Ex-Dividend Date:	4/21/2023
% Fair Value:	39%	5 Year Valuation Multiple Estimate:	20.9%	Dividend Payment Date:	5/18/2023
Dividend Yield:	15.4%	5 Year Price Target	\$17	Years Of Dividend Growth:	0
Dividend Risk Score:	C	Retirement Suitability Score:	A	Rating:	Hold

Overview & Current Events

Office Properties Income Trust (OPI) is a REIT that currently owns 157 buildings, which are primarily leased to single tenants with high credit quality. The REIT's portfolio currently has a 90.5% occupancy rate and an average building age of 18 years. OPI has a market capitalization of \$318 million.

On 12/31/2018, the predecessor company - Government Properties Income Trust - merged with Select Income REIT (SIR) and the combined company was renamed Office Properties Income Trust. The aggregate transaction value was \$2.4 billion, including the assumption of \$1.7 billion of debt from SIR. The combined company has enhanced geographic diversification and one of the highest percentages of rent paid by investment-grade rated tenants in the REIT universe. The U.S. Government is the largest tenant of OPI, as it represents 20% of the annual rental income of the REIT.

After acquiring First Potomac Realty Trust (FPO) in 2017 and merging with SIR, OPI is now selling assets to reduce its debt. It sold nearly \$1.0 billion of assets in 2019, \$110 million in 2020, \$260 million in 2021 and \$210 million of assets in 2022.

On April 11th, 2023, OPI announced that it agreed to acquire Diversified Healthcare Trust (DHC) in an all-stock deal of nearly \$400 million. OPI pursued this acquisition to enhance its diversification and benefit from synergies. However, it cut its dividend by 55% and its stock plunged -24% on the news. Due to the several mergers in the history of OPI, its daunting long-term performance and its high debt load, we do not view this merger as positive for the stock.

In late April, OPI reported (4/26/2023) financial results for the first quarter of fiscal 2023. The occupancy rate edged down sequentially from 90.6% to 90.5% and normalized funds from operations (FFO) per share fell -16% over the prior year's quarter, from \$1.30 to \$1.09. More than 90% of the debt of OPI is at fixed rates but we expect interest expense to increase this year due to high interest rates. Given also the disappointing results and the above merger, we have lowered our forecast for annual FFO per share from \$4.45 to \$4.20.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
FFO	\$2.12	\$2.29	\$2.39	\$2.36	\$2.02	\$1.99	\$6.01	\$5.39	\$4.87	\$4.76	\$4.20	\$4.20
DPS	\$1.72	\$1.72	\$1.72	\$1.72	\$1.72	\$1.72	\$2.20	\$2.20	\$2.20	\$2.20	\$1.00	\$1.00
Shares¹	13.7	15.4	17.7	17.8	21.2	24.8	48.1	48.2	48.3	48.3	50.0	60.0

OPI has completed a major acquisition and a reverse split and it just announced a major acquisition. It has also sold several of its assets in recent years in order to reduce its leverage and hence it is difficult to forecast future funds from operations. Furthermore, the pandemic may lead many companies to adopt a "work from home" model for the long run in order to reduce their operating costs. Such a shift would hurt OPI in the long run, but it is too early to evaluate the effect of the pandemic on this trend. Due to the disappointing business performance of OPI over the last five years and the uncertainty from the imminent merger, we now assume flat FFO per share (instead of 2.0% growth) over the next five years.

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.



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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/FFO	11.8	10.5	8.0	8.2	9.7	6.8	4.8	4.8	5.0	4.2	1.5	4.0
Avg. Yld.	6.9%	7.1%	9.0%	8.9%	8.8%	12.8%	7.6%	8.6%	9.1%	11.0%	15.4%	6.0%

OPI has traded at an average price-to-FFO ratio of 7.4 during the last decade. The REIT is currently trading at a depressed FFO multiple of 1.5. However, as its mega merger was recently completed, it is hard to determine the fair valuation level. Moreover, given the high leverage of OPI, we prefer to be conservative and thus assume a fair price-to-FFO ratio of 4.0. If OPI reaches our fair valuation level in five years, it will enjoy a 20.9% 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	81%	75%	72%	73%	85%	86%	37%	41%	45%	46%	24%	24%

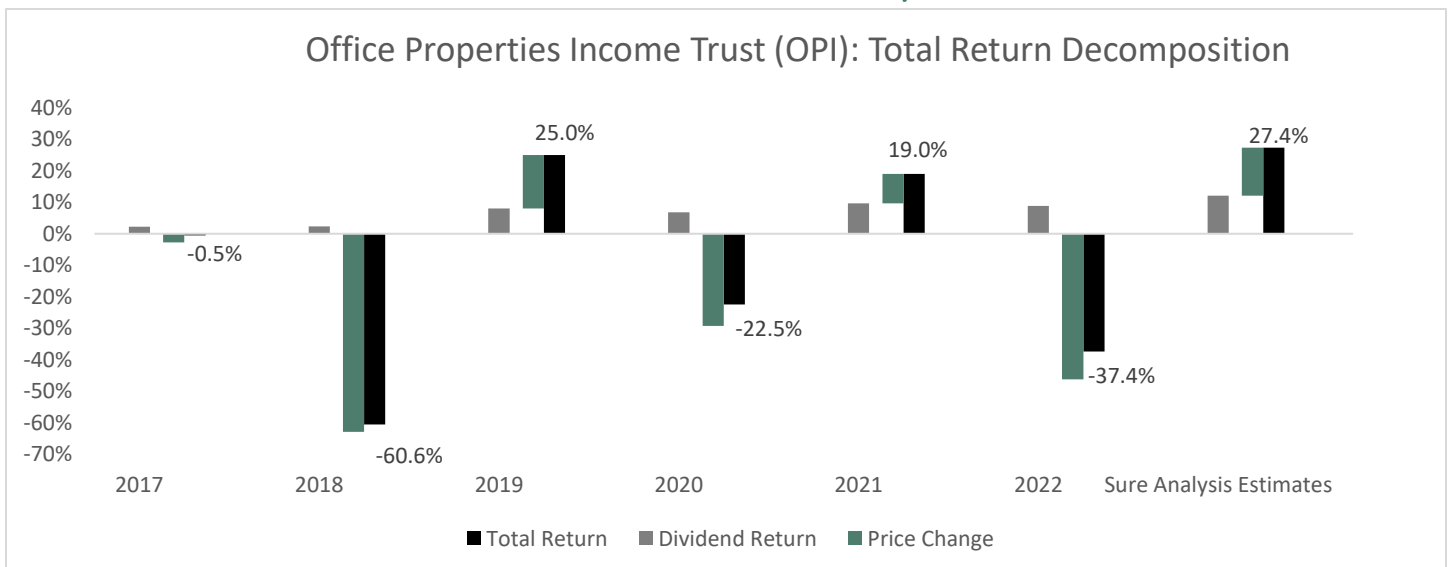
OPI generates 63% of its annual rental income from investment-grade tenants. This is one of the highest percentages of rent paid by investment-grade tenants in the REIT sector. Moreover, U.S. Government tenants generate about 20% of total rental income. This exceptional credit profile constitutes a competitive advantage.

On the other hand, OPI has greatly increased its debt load after its latest acquisition. Its net debt is excessive, as it stands at \$2.5 billion, which is about 12 times the annual funds from operations and nearly 8 times the current market cap of the REIT. OPI is in the process of selling assets but it has a very poor record of enhancing shareholder value. As it is also vulnerable to recessions, it is unsuitable for income-oriented investors.

Final Thoughts & Recommendation

Office Properties has plunged -55% this year, mostly due to its recently announced merger. Due to the brutal sell-off, the stock could offer a 27.4% average annual return over the next five years thanks to its 15.4% dividend and a 20.9% valuation tailwind. However, OPI has a very poor record of returns to its shareholders, it has a high debt load and it is vulnerable to recessions. We believe that OPI will rebound from its depressed current level but, due to all the above issues, it is suitable only for traders, not for long-term investors. OPI earns a hold rating for risk-tolerant investors.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	227	251	249	258	317	427	678	588	576	554
Gross Profit	201	223	219	227	279	377	605	523	505	496
Gross Margin	88.7%	88.7%	88.0%	88.1%	88.0%	88.3%	89.1%	88.9%	87.5%	89.5%
SG&A Exp.	30	35	33	32	40	51	67	54	52	52
D&A Exp.	56	65	68	71	109	161	287	251	237	217
Operating Profit	75	75	67	68	64	73	127	112	105	111
Operating Margin	32.9%	29.8%	26.9%	26.3%	20.2%	17.2%	18.7%	19.0%	18.2%	20.0%
Net Profit	55	57	(210)	58	12	(22)	30	7	(8)	(6)
Net Margin	24.1%	22.5%	-84.5%	22.4%	3.8%	-5.1%	4.5%	1.1%	-1.4%	-1.1%
Free Cash Flow	108	131	115	127	138	145	215	234	221	193
Income Tax	0	0	0	0	0	0	1	0	0	0

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,632	2,428	2,169	2,385	3,704	5,239	4,193	3,946	4,242	3,980
Cash & Equivalents	8	14	9	30	17	35	94	42	83	12
Accounts Receivable	33	36	45	48	61	72	84	102	113	106
Total Liabilities	643	1,130	1,212	1,450	2,353	3,460	2,487	2,337	2,745	2,594
Accounts Payable	23	26	51	54	89	146	125	116	143	140
Long-Term Debt	598	1,085	1,146	1,382	2,245	3,255	2,327	2,203	2,578	2,433
Shareholder's Equity	990	1,297	957	935	1,330	1,779	1,706	1,609	1,497	1,386
LTD/E Ratio	0.60	0.84	1.20	1.48	1.66	1.83	1.36	1.37	1.72	1.76

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	3.4%	2.8%	-9.1%	2.5%	0.4%	-0.5%	0.6%	0.2%	-0.2%	-0.1%
Return on Equity	5.4%	4.9%	-18.6%	6.1%	1.1%	-1.4%	1.7%	0.4%	-0.5%	-0.4%
ROIC	3.5%	2.8%	-9.4%	2.6%	0.4%	-0.5%	0.7%	0.2%	-0.2%	-0.2%
Shares Out.	13.7	15.4	17.7	17.8	21.2	24.8	48.1	48.2	48.3	48.3
Revenue/Share	16.60	16.35	14.06	14.53	14.96	17.18	14.12	12.22	11.96	11.48
FCF/Share	7.93	8.52	6.53	7.13	6.50	5.84	4.48	4.85	4.60	3.99

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

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