National Retail Properties (NNN)

Updated May 13th, 2023 by Samuel Smith

Key Metrics

Current Price:	$44.1	**5 Year CAGR Estimate:**	9.2%	**Market Cap:**	$8.0B
Fair Value Price:	$44.7	**5 Year Growth Estimate:**	4.6%	**Ex-Dividend Date:**	07/27/23[1]
% Fair Value:	99%	**5 Year Valuation Multiple Estimate:**	0.3%	**Dividend Payment Date:**	08/15/23[1]
Dividend Yield:	5.0%	**5 Year Price Target**	$56	**Years of Dividend Growth:**	21
Dividend Risk Score:	C	**Retirement Suitability Score:**	A	**Rating:**	Hold

Overview & Current Events

National Retail Properties is a REIT that owns ~3,000 single-tenant, net-leased retail properties across the United States. It is focused on retail customers because they are much more likely to accept rent hikes in order to avoid switching locations and losing their customer base. Thanks to this strategy, National Retail has offered consistent growth with markedly low volatility. It is also characterized by very high occupancy rates; its 15-year low occupancy rate is 96% and it typically ranges between 98%-99%.

National Retail recently reported Q1 results. FFO (Funds From Operations) per share increased by 6.7% compared to the previous year, while Core FFO per share saw a 3.9% increase, and AFFO (Adjusted Funds From Operations) per share increased by 3.8% compared to the prior year. The company also maintained high occupancy levels, with a rate of 99.4% and a weighted average remaining lease term of 10.3 years as of March 31, 2023. This represents a consistent occupancy rate compared to the previous quarter and a slight improvement from the previous year. Additionally, the company made property investments totaling $156.2 million, acquiring 43 properties with a combined gross leasable area of approximately 275,000 square feet. These acquisitions were made at an initial cash cap rate of 7.0%. The company also sold six properties for $11.9 million, resulting in gains of $6.3 million, and achieved a cap rate of 6.6% on those sales. Furthermore, the company raised $16.9 million in net proceeds through the issuance of 367,569 common shares, providing additional capital for future endeavors. Lastly, the company maintained a strong financial position with a sector-leading weighted average debt maturity of 12.9 years for unsecured debt, indicating a favorable debt management strategy.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2022	2028
FFO/S	$1.93	$2.08	$2.22	$2.35	$2.52	$2.65	$2.76	$2.59	$2.86	$3.14	***$3.19***	***$4.00***
DPS	$1.60	$1.65	$1.71	$1.78	$1.86	$1.95	$2.06	$2.07	$2.10	$2.20	***$2.20***	***$2.70***
Shares[1]	122	132.2	141	147.2	153.6	161.6	171.7	175.3	175.6	181.5	***182.1***	***195***

National Retail Properties has more than doubled its FFO since 2011, but it has also significantly increased its share count in order to fund its acquisitions of properties. As a result, the REIT has grown its FFO per share at a mid-single digit rate per year on average since 2011. While the impact of dilution is noticeable, the dilution also has another, less obvious effect: it has greatly increased the financial burden of the dividend on the REIT.

We believe that growth will slow moving forward as investment spreads compress, and the law of large numbers makes it increasingly challenging to move the needle with acquisitions. The trust's high level of occupancy should afford it low-single-digit levels of revenue growth, while slightly increasing margins should continue to see it growing FFO-per-share at a mid-single digit rate despite the ever-rising share count. The bulk of National Retail's FFO-per-share growth will come from net new property acquisitions.

[1] In millions

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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/FFO	13.2	16.4	15.4	16.7	14.8	16.1	19.2	15.4	16.5	14.4	***13.8***	***14.0***
Avg. Yld.	6.30%	4.80%	5.00%	4.40%	5.00%	4.50%	3.90%	5.20%	4.50%	4.9%	***5.0%***	***4.8%***

Using expected 2023 FFO numbers, National Retail Properties is trading at a price-to-FFO ratio of 13.8. The trust's 10-year average price-to-FFO ratio is 14, and, while recent multiples have been far higher due to low interest rates and strong results, we believe that current headwinds and rising interest rates justify a lower valuation. Therefore, we are placing 14 times FFO as our fair value estimate. Accordingly, we believe that slight multiple expansion will provide a small tailwind to the trust's total returns moving forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	83%	79%	77%	76%	74%	74%	75%	80%	73%	70%	***69%***	***68%***

National Retail's payout ratio is being maintained near three-quarters of FFO, and we believe it will stay there for the foreseeable future. Given this, the dividend is fairly safe at this point with the trust's rising earnings. On the other hand, National Retail Properties is significantly impacted by recessions. In the Great Recession, its funds from operations per share plunged 34%, from $1.99 in 2008 to $1.31 in 2010. Nevertheless, given that the financial crisis was triggered by the bubble in the housing market, the performance of the REIT in that crisis was satisfactory.

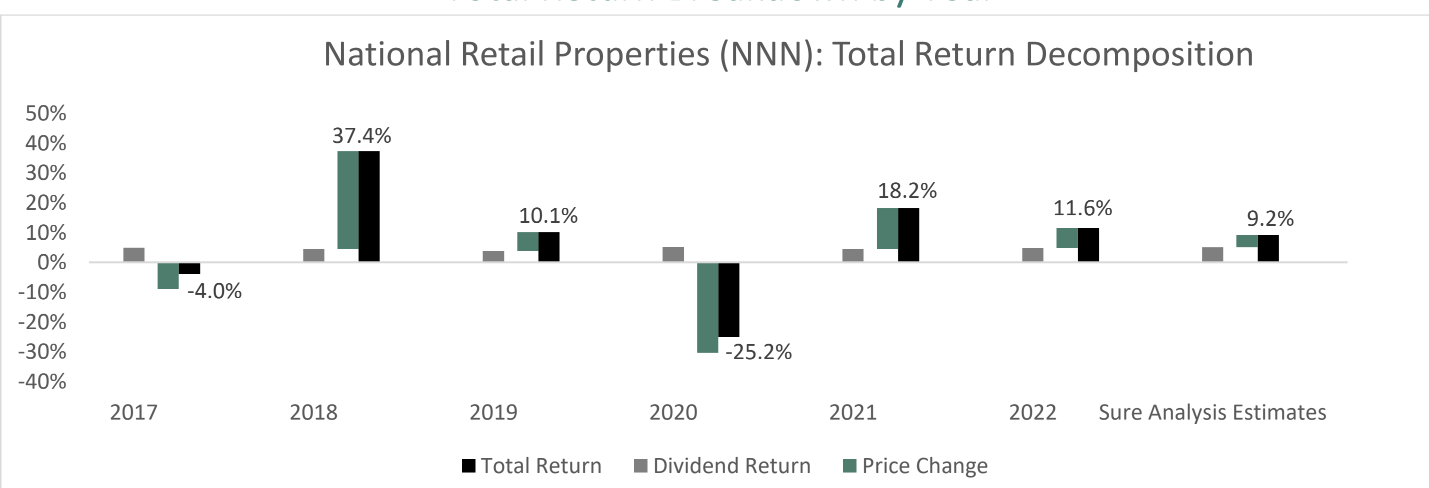
However, investors should keep in mind that its downside potential will likely be significant whenever the next recession shows up, particularly given its current valuation. The trust lacks any durable competitive advantages, though its scale and business network are gradually growing over time, which could give it increasing pricing power and economies of scale.

Final Thoughts & Recommendation

National Retail Properties is an attractive dividend growth stock given its 5% dividend yield backed by a strong balance sheet, well-diversified portfolio, impressive dividend growth streak, and lengthy growth runway.

Given that it offers estimated 9.2% annualized total returns over the next half decade due to our expectations of slowing growth in the short-term, we rate it a Hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	394	435	483	534	585	623	670	661	726	773
Gross Profit	375	416	463	513	562	598	643	632	698	747
Gross Margin	95.3%	95.6%	95.9%	96.1%	96.0%	96.0%	95.9%	95.7%	96.1%	96.6%
SG&A Exp.	31	33	35	37	34	34	38	38	45	50
D&A Exp.	100	116	135	149	174	174	189	197	205	224
Operating Profit	245	267	294	327	354	389	416	397	448	473
Operating Margin	62.2%	61.5%	60.8%	61.3%	60.6%	62.5%	62.1%	60.2%	61.7%	61.2%
Net Profit	160	191	198	240	265	292	299	229	290	335
Net Margin	40.7%	43.8%	41.0%	44.9%	45.3%	47.0%	44.6%	34.6%	39.9%	43.3%
Free Cash Flow	274	297	341	415	422	472	502	450	568	578
Income Tax	0	(0)	10							

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	4,455	4,916	5,460	6,334	6,561	7,103	7,435	7,638	7,751	8,146
Cash & Equivalents	1	11	14	295	1	114	1	267	171	3
Accounts Receivable	4	3	3	3	4	4	3	4	3	4
Goodwill & Int. Ass.	70	78	72	65	51	66	76	70	67	62
Total Liabilities	1,676	1,832	2,118	2,417	2,720	2,949	3,103	3,319	3,849	4,023
Long-Term Debt	1,570	1,730	1,976	2,312	2,580	2,851	2,988	3,221	3,746	3,916
Shareholder's Equity	2,202	2,508	2,767	2,997	3,208	3,522	3,987	3,974	3,902	4,124
LTD/E Ratio	0.57	0.56	0.59	0.59	0.67	0.69	0.69	0.75	0.96	0.95

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	3.8%	4.1%	3.8%	4.1%	4.1%	4.3%	4.1%	3.0%	3.8%	4.2%
Return on Equity	7.6%	8.1%	7.5%	8.3%	8.5%	8.7%	8.0%	5.7%	7.4%	8.3%
ROIC	3.9%	4.2%	3.9%	4.1%	4.2%	4.4%	4.2%	3.1%	3.8%	4.3%
Shares Out.	122.0	132.2	141.0	147.2	153.6	161.6	171.7	175.3	175.6	181.5
Revenue/Share	3.28	3.49	3.59	3.69	3.91	3.98	4.06	3.84	4.16	4.37
FCF/Share	2.29	2.38	2.54	2.87	2.82	3.02	3.04	2.61	3.25	3.27

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