



Gladstone Commercial Corporation (GOOD)

Updated August 11th, 2023, by Josh Arnold

Key Metrics

| | | | | | |
|-----------------------------|------|--|-------|----------------------------------|----------|
| Current Price: | \$14 | 5 Year CAGR Estimate: | 7.6% | Market Cap: | \$560 M |
| Fair Value Price: | \$15 | 5 Year Growth Estimate: | -2.0% | Ex-Dividend Date: | 08/22/23 |
| % Fair Value: | 89% | 5 Year Valuation Multiple Estimate: | 2.4% | Dividend Payment Date: | 08/31/23 |
| Dividend Yield: | 8.6% | 5 Year Price Target | \$14 | Years Of Dividend Growth: | 0 |
| Dividend Risk Score: | F | Retirement Suitability Score: | C | Rating: | Hold |

Overview & Current Events

Gladstone Commercial Corporation is a real estate investment trust, or REIT, that specializes in single-tenant and anchored multi-tenant net leased industrial and office properties across the U.S. The trust targets primary and secondary markets that possess favorable economic growth trends, growing populations, strong employment, and robust growth trends. The trust's stated goal is to pay shareholders monthly distributions, which it has done for more than 17 consecutive years. Gladstone owns over 100 properties in 24 states that are leased to about 100 unique tenants and has a market capitalization of \$560 million.

Gladstone posted second quarter earnings on August 8th, 2023, and results were better than expected on both the top and bottom lines. FFO-per-share was 41 cents, a nickel ahead of estimates. Revenue was up 5.8% from Q1 at \$38.7 million and beat estimates by \$1.7 million. In addition, the company collected 100% of cash rents for the months of April, May, and June.

The company acquired one fully-occupied, 76k square foot property for \$5.3 million, at a cap rate of 9.71%. In addition, it sold two non-core properties for \$4.7 million.

Operating expenses were \$33.7 million, up from \$24.7 million in Q1. Gladstone repurchased \$1 million in common stock and paid 30 cents per share in dividends.

We see \$1.50 in FFO-per-share after Q2 results.

Growth on a Per-Share Basis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| FFO | \$1.49 | \$1.80 | \$1.54 | \$1.53 | \$1.54 | \$1.58 | \$1.58 | \$1.57 | \$1.54 | \$1.56 | \$1.50 | \$1.36 |
| DPS | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.50 | \$1.20 | \$1.20 |
| Shares¹ | 15.7 | 17.3 | 21.2 | 23.2 | 26.4 | 28.8 | 33.0 | 35.3 | 37.8 | 40.0 | 43.0 | 52.0 |

Gladstone reports funds-from-operations, or FFO, per share rather than earnings-per-share. This is consistent with other REITs, and we'll use FFO as the preferred proxy for underlying earnings power.

Gladstone's FFO-per-share has been between \$1.50 and \$1.60 for most of the past decade as the trust continues to issue new shares and debt to fund acquisitions, but those acquisitions fail to provide an economic gain. In other words, while the trust's new properties provide growth on a dollar basis, when the cost of those acquisitions is factored in, it is essentially no gain on a per-share basis. We don't have any reason to believe this will change moving forward as Gladstone's common shares are quite expensive to issue, yielding 7% to 9% at most times, and its preferred stock and debt are not significantly cheaper. This means that Gladstone will struggle to produce economic gains with its capital issuances given that the yields on its properties are also in the high single digits. As a result, our long-term growth estimate for Gladstone is -2%. We don't see any cause for pessimism as earnings impairment isn't likely. However, investors should note that any sort of meaningful growth is going to be difficult to generate.

¹ Share count 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.



Gladstone Commercial Corporation (GOOD)

Updated August 11th, 2023, by Josh Arnold

The distribution had been flat at \$1.50 for the past decade as the trust has struggled to grow FFO-per-share and thus, has been unable to boost the distribution. For the start of 2023, Gladstone cut its distribution by 20% to a new level of \$1.20 per year.

Valuation Analysis

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | Now | 2028 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | 12.6 | 9.8 | 10.7 | 11.1 | 13.8 | 11.9 | 13.7 | 11.4 | 13.9 | 11.9 | 9.3 | 10.5 |
| Avg. Yld. | 8.0% | 8.5% | 9.1% | 8.8% | 7.1% | 8.0% | 7.0% | 8.4% | 7.0% | 8.1% | 8.6% | 8.4% |

Today the trust trades for 9.3 times this year's FFO-per-share estimate, which is very low against historical norms. The long-term average valuation for Gladstone is just over 11 times FFO-per-share, and we've moved our fair value estimate down slightly to 10.5 times earnings. This implies a tailwind from the valuation in the coming years.

The current 8.6% yield is largely in line with historical yields. We see the yield potentially declining should the valuation rise to meet our fair value estimate.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 101% | 83% | 97% | 98% | 97% | 95% | 95% | 96% | 97% | 96% | 80% | 89% |

Gladstone doesn't necessarily have a competitive advantage given that it operates in much the same way as any other commercial REIT. However, Gladstone's selection of properties has been outstanding over time as its occupancy has remained high through a variety of economic conditions.

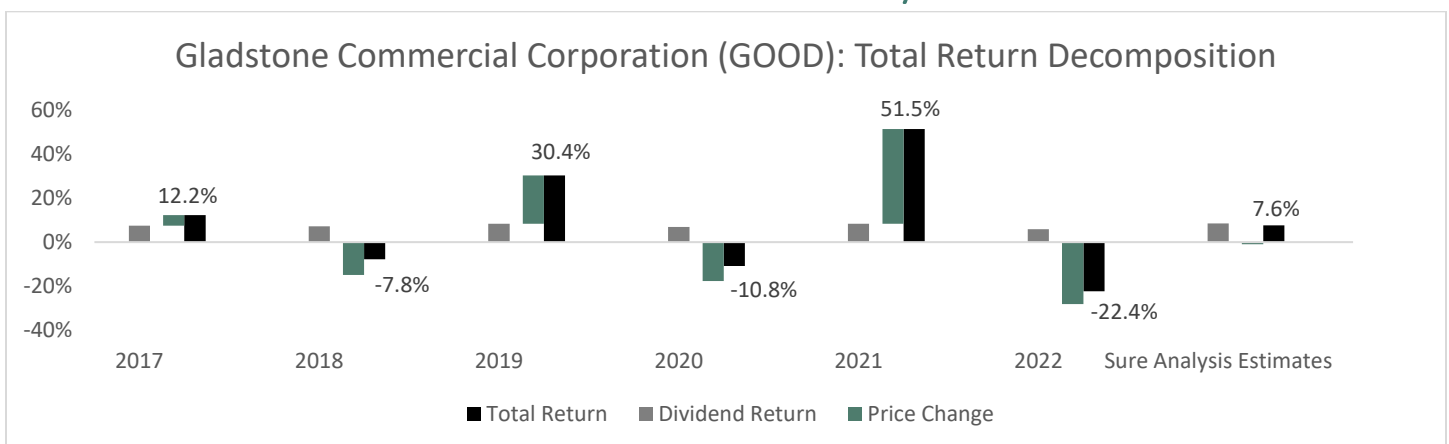
In the case of recession, Gladstone should fare quite well as it has long lease terms, so the impact on the trust's earnings should be minimal, which is consistent with how Gladstone performed during the Great Recession. Last year's challenges have shown that Gladstone can weather a tough environment.

The payout ratio is very high, but we see the trust's FFO-per-share of \$1.40+ annually as enough to maintain the lowered dividend. Investors should not expect a meaningful raise anytime soon due to the factors discussed above.

Final Thoughts & Recommendation

We forecast 7.6% total annual returns for Gladstone Commercial moving forward. We see the yield as attractive at 8.6%, and the stock is below fair value, with a resulting 2.4% tailwind. We like Gladstone's recession performance and its steady FFO-per-share, but there is a tough road ahead for growth. We're moving the stock from buy to hold.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

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.



Gladstone Commercial Corporation (GOOD)

Updated August 11th, 2023, by Josh Arnold

Income Statement Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue | 61 | 74 | 84 | 86 | 95 | 107 | 114 | 133 | 138 | 149 |
| Gross Profit | 58 | 69 | 78 | 80 | 87 | 95 | 102 | 107 | 111 | 122 |
| Gross Margin | 94.5% | 93.6% | 93.7% | 93.2% | 91.9% | 89.3% | 89.0% | 80.5% | 80.3% | 81.9% |
| SG&A Exp. | 6 | 8 | 10 | 10 | 11 | 12 | 14 | 15 | 15 | 17 |
| D&A Exp. | 23 | 29 | 35 | 38 | 43 | 48 | 52 | 55 | 60 | 62 |
| Operating Profit | 29 | 32 | 33 | 33 | 33 | 36 | 36 | 37 | 35 | 43 |
| Operating Margin | 47.7% | 43.4% | 39.9% | 38.0% | 35.1% | 33.4% | 31.4% | 27.7% | 25.3% | 28.9% |
| Net Profit | 2 | (6) | 4 | 4 | 6 | 12 | 10 | 15 | 10 | 9 |
| Net Margin | 2.5% | -8.0% | 4.3% | 4.6% | 6.3% | 11.5% | 8.4% | 11.2% | 7.1% | 6.0% |
| Free Cash Flow | 20 | 28 | 31 | 41 | 47 | 56 | 60 | 65 | 70 | 69 |

Balance Sheet Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---------------------------------|------|------|------|------|------|------|-------|-------|-------|-------|
| Total Assets | 691 | 788 | 827 | 852 | 928 | 939 | 1,040 | 1,098 | 1,143 | 1,202 |
| Cash & Equivalents | 9 | 9 | 5 | 5 | 7 | 7 | 7 | 11 | 8 | 12 |
| Goodwill & Int. Ass. | 80 | 99 | 105 | 106 | 119 | 111 | 115 | 117 | 114 | 112 |
| Total Liabilities | 507 | 570 | 593 | 612 | 662 | 684 | 828 | 882 | 941 | 997 |
| Accounts Payable | 2 | 8 | 6 | 6 | 7 | 3 | 6 | 4 | 7 | 10 |
| Long-Term Debt | 447 | 503 | 525 | 509 | 543 | 566 | 627 | 669 | 708 | 749 |
| Shareholder's Equity | 183 | 218 | 234 | 240 | 267 | 250 | 208 | 213 | 201 | 203 |
| LTD/E Ratio | 2.44 | 2.31 | 2.25 | 2.12 | 2.03 | 2.27 | 3.01 | 3.14 | 3.51 | 3.69 |

Profitability & Per Share Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|-------------------------|------|-------|------|------|------|------|------|------|------|------|
| Return on Assets | 0.2% | -0.8% | 0.4% | 0.5% | 0.7% | 1.3% | 1.0% | 1.4% | 0.9% | 0.8% |
| Return on Equity | 1.0% | -2.9% | 1.6% | 1.7% | 2.3% | 4.8% | 4.2% | 7.1% | 4.7% | 4.6% |
| ROIC | 0.3% | -0.9% | 0.5% | 0.5% | 0.8% | 1.5% | 1.2% | 1.7% | 1.1% | 1.0% |
| Shares Out. | 15.7 | 17.3 | 21.2 | 23.2 | 26.4 | 28.8 | 33.0 | 35.3 | 37.8 | 39.0 |
| Revenue/Share | 4.56 | 4.15 | 3.79 | 3.58 | 3.60 | 3.72 | 3.73 | 3.91 | 3.77 | 3.82 |
| FCF/Share | 1.48 | 1.59 | 1.42 | 1.70 | 1.78 | 1.94 | 1.96 | 1.92 | 1.92 | 1.78 |

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

Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.