



Paramount Group Inc (PGRE)

Updated November 2nd, 2023 by Quinn Mohammed

Key Metrics

Current Price:	\$4.6	5 Year CAGR Estimate:	4.4%	Market Cap:	\$1.0 B
Fair Value Price:	\$6.5	5 Year Growth Estimate:	-5.0%	Ex-Dividend Date¹:	12/29/2023
% Fair Value:	71%	5 Year Valuation Multiple Estimate:	7.0%	Dividend Payment Date¹:	01/13/2024
Dividend Yield:	3.0%	5 Year Price Target:	\$5	Years of Dividend Growth:	0
Dividend Risk Score:	C	Retirement Suitability Score:	D	Rating:	Hold

Overview & Current Events

Paramount Group Inc is a real estate investment trust which acquires, manages, and redevelops office properties in the central business district submarkets of New York City, Washington DC, and San Francisco. Paramount's primary customers are financial services firms, legal services firms, and technology and media industries. The trust was established in 1978, and the current president and CEO, Albert Behler, has been at the helm since 1991. Paramount owns or has an interest in 13.8 million square feet of high quality office building investments, retail property, and debt and equity investments. Paramount Group trades on the NYSE under the ticker symbol PGRE and is one of the largest publicly owned real estate companies headquartered in New York, NY. PGRE has a market capitalization of \$1.0 billion. On June 15th, 2023, Paramount announced a 55% decrease to the dividend, from \$0.0775 quarterly prior to \$0.035. Albert Behler, the CEO of PGRE, said that this will enable the company to focus on paying down some debt and improving liquidity.

Paramount Group reported third quarter 2023 results on November 1st, 2023. The trust announced core funds from operations (FFO) of \$47.8 million, or \$0.22 per diluted share. Results compared unfavorably to the prior year's \$54.2 million, or \$0.24 per diluted share. Paramount also reported a 7.1% decrease in same store cash net operating income (NOI) and a 10.3% decrease in same store NOI compared to the prior year.

The trust leased a total of 298.3K square feet during the quarter. The occupancy rate stood at 88.1% at Q3 2023 end. Leadership narrowed its guidance for the 2023 fiscal year and estimates core FFO to come in between \$0.85 to \$0.87, for a mid-point of \$0.86.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Core FFO			\$0.81	\$0.89	\$0.87	\$0.94	\$0.90	\$0.96	\$0.92	\$0.98	\$0.86	\$0.67
DPS			\$0.42	\$0.38	\$0.38	\$0.40	\$0.40	\$0.37	\$0.28	\$0.30	\$0.14	\$0.15
Shares²			212.1	218.1	236.4	239.6	231.5	222.4	218.7	218.6	218.5	250.0

While Paramount Group is a trust with a long history, being established in 1978, it has only been publicly traded for a short period of time. Thus, we can only use historical data back to 2015 to form an opinion and estimate forward growth. Since 2015, PGRE has grown adjusted FFO at a rate of 2.8% annually. The trust managed to grow year-over-year into the pandemic year, but it slashed its dividend and its valuation plummeted. We forecast that, in the intermediate term, core FFO per share may decline by 5% per year due to the effect of rising interest rates on PGRE's interest expense, upcoming lease expirations, and the continuing work from home trend.

The trust led in same store cash NOI growth from 2017 to 2020 among its peers. Paramount has embedded rent growth within the portfolio due to strong historical and projected future rental rate growth in their submarkets, and contractual fixed rental rate increases in leases and rent from the lease-up of vacant and expiring leases. The trust targets acquisitions opportunities with a value-add component where PGRE can leverage their operating expertise, tenant

¹ Estimate

² In millions

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relationships, and asset and property management approach. The trust will also incrementally add to AFFO with value-add renovations and redevelopments of office properties.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/AFFO			22.4	18.3	18.6	15.7	15.4	9.4	10.4	8.2	5.3	7.5
Avg. Yld.			2.3%	2.3%	2.4%	2.6%	2.9%	4.7%	3.4%	3.6%	3.0%	2.9%

The current P/AFFO of 5.3 is heavily discounted in comparison to its average nine- and five-year valuations of 14.8 and 11.8. This discount is largely due to the persistence of the work-from-home model, which has rendered office properties unattractive. This, in addition to lower occupancy, causes us to discount our valuation estimate, to peg fair value at 7.5 times core FFO. Following the latest dividend cut, PGRE only yields 3.0%, which is below its average yield of ~3.2%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

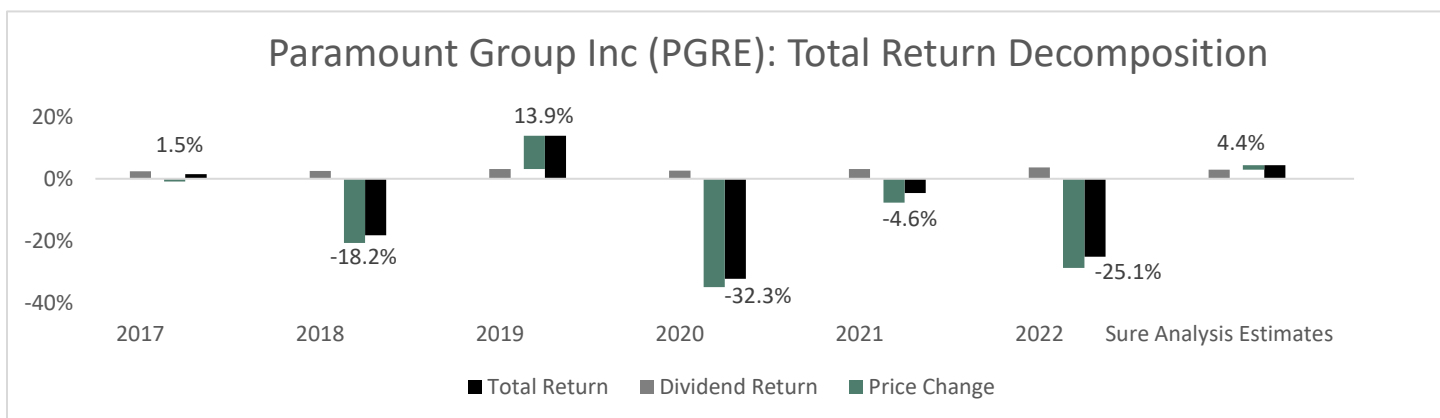
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout			52%	43%	44%	43%	44%	39%	30%	31%	16%	22%

Paramount's dividend has been choppy since it was instated in 2015, it was cut during the pandemic, and again in June 2023. At both times, the dividend appeared to be fairly covered by adjusted FFO, but the CFO of PGRE, Wilbur Paes, says they are looking forward to future plans and the upcoming lease role, so the dividend was preemptively slashed. The trust believes that its proven acquisition and operating expertise enables it to gain advantages over competitors through superior acquisition sourcing, focused leasing programs, active asset and property management and first-class tenant service. The trust was not publicly traded at the time of the Great Recession, and we believe the trust would only be somewhat recession resistant given the stickiness of office leases. However, this stickiness is being challenged now as corporations reduce their office footprint.

Final Thoughts & Recommendation

Paramount Group has a long history as a trust but only recently came to the public markets, debuting only five years prior to the pandemic. It cut the dividend during the pandemic, and again very recently, even though it was fairly covered by AFFO. The 3.0% dividend yield is low for an REIT. We also estimate a 7.0% tailwind to total returns due to valuation expansion. However, AFFO per share is likely to decrease in the coming years. Paramount Group trades at 71% of our fair value estimate, and with total expected returns of 4.4%, we rate shares as a hold, but reiterate as we have before that the dividend is not likely to be reliable.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	59		662	683	719	708	744	714	727	740
Gross Profit	42		418	433	453	453	479	447	461	463
Gross Margin	72.4%		63.1%	63.4%	63.0%	64.0%	64.4%	62.5%	63.5%	62.5%
SG&A Exp.	57		42	54	62	58	69	65	59	59
D&A Exp.	11		295	269	266	258	248	236	232	233
Operating Profit	-30		81	110	125	155	170	147	170	171
Op. Margin	-50.5%		12.2%	16.1%	17.4%	21.8%	22.9%	20.5%	23.4%	23.1%
Net Profit	17		-4	-10	86	9	-37	-25	-20	-36
Net Margin	28.2%		-0.7%	-1.5%	12.0%	1.3%	-5.0%	-3.5%	-2.8%	-4.9%
Free Cash Flow	33		-17	148	190	157	285	237	244	247
Provision for Tax	11		3	2	5	3	0	1	4	3

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	2,923	9,030	8,775	8,867	8,918	8,756	8,734	8,554	8,495	8,453
Cash & Equivalents	307	439	144	163	219	340	306	435	525	409
Accts. Receivable	10	8	11	15	17	20	19	18	16	24
Goodwill & Int.	0	669	511	412	352	270	203	154	119	90
Total Liabilities	897	3,475	3,465	3,981	3,896	3,864	4,103	4,038	40,40	4,042
Accounts Payable	11	93	103	104	118	124	117	102	116	123
Long-Term Debt	500		2,988	3,595	3,541	3,567	3,821	3,801	3,836	3,840
Total Equity	322	3,911	3,761	3,990	4,177	4,001	3,786	3,653	3,588	3,592
LTD/E Ratio	1.55		0.79	0.90	0.85	0.89	1.01	1.04	1.07	1.07

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	0.6%		-0.1%	-0.1%	1.0%	0.1%	-0.4%	-0.3%	-0.2%	-0.4%
Return on Equity	4.4%		-0.1%	-0.3%	2.1%	0.2%	-0.9%	-0.7%	-0.6%	-1.0%
ROIC	0.7%		-0.1%	-0.1%	1.0%	0.1%	-0.4%	-0.3%	-0.2%	-0.4%
Shares Out.			212.1	218.1	236.4	239.6	231.5	222.4	218.7	221.3
Revenue/Share	0.24		3.12	3.13	3.04	2.95	3.21	3.21	3.32	3.35
FCF/Share	0.14		-0.08	0.68	0.80	0.65	1.23	1.07	1.12	1.11

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

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