



AvalonBay Communities Inc. (AVB)

Updated February 15th, 2024 by Samuel Smith

Key Metrics

Current Price:	\$177	5 Year CAGR Estimate:	10.8%	Market Cap:	\$25.2B
Fair Value Price:	\$196	5 Year Growth Estimate:	5.5%	Ex-Dividend Date:	3/27/24
% Fair Value:	90%	5 Year Valuation Multiple Estimate:	2.1%	Dividend Payment Date:	4/15/24
Dividend Yield:	3.8%	5 Year Price Target	\$257	Years Of Dividend Growth:	2
Dividend Risk Score:	F	Retirement Suitability Score:	D	Rating:	Buy

Overview & Current Events

AvalonBay Communities (AVB) is a \$25.2 billion multifamily REIT that owns a portfolio of several hundred apartment communities and is also an active developer of apartment communities. The trust's strategy consists of owning top-tier properties in the major metropolitan areas of New England, New York/New Jersey, Washington D.C., California, and the Pacific Northwest. It was formed by the 1998 merger of Avalon Properties with Bay Apartment Communities.

AvalonBay Communities, Inc. (AVB) reported its Q4 2023 earnings on February 1, 2024, showcasing strong financial and operational performance. The company reported a core funds from operations (FFO) per share of \$2.74, which represented a 5.8% increase from the previous year's quarter. This performance was supported by a year-over-year rise in same-store residential rental revenues, despite a slight decline in occupancy. Total revenues for the quarter amounted to \$704.7 million, marking a 5.2% increase from the same period last year. For the full year of 2023, AvalonBay's core FFO per share reached \$10.63, outperforming the previous year's total of \$9.79. This annual performance was underpinned by a 6.7% increase in total revenues to \$2.77 billion. AvalonBay's portfolio activities in the fourth quarter included the acquisition of two wholly-owned communities and the sale of Avalon Mamaroneck, resulting in a GAAP gain of \$77.9 million. As of December 31, 2023, the company had 17 consolidated development communities under construction, with an estimated total capital cost at completion of \$2.49 billion. Looking ahead to 2024, AvalonBay has set its core FFO per share expectations in the range of \$10.53 to \$11.03, indicating modest growth at the midpoint. The company anticipates same-store residential revenue growth of 1.6-3.6% and projects same-store residential NOI to expand between 0.0-2.5%. Additionally, AvalonBay announced an increase in its first-quarter 2024 dividend to \$1.70 per share, up from \$1.65 paid in the previous quarter.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
FFO/S	\$6.78	\$7.55	\$8.19	\$8.62	\$9.00	\$9.34	\$8.69	\$8.26	\$9.79	\$10.63	\$10.90	\$14.25
DPS	\$4.64	\$5.00	\$5.40	\$5.68	\$5.88	\$6.08	\$6.36	\$6.36	\$6.36	\$6.60	\$6.80	\$8.55
Shares¹	132.0	137.0	137.0	137.7	138.1	140.3	139.2	139.5	139.7	141.9	141.9	140

Over the past decade, AvalonBay generated very impressive annualized Core FFO/share growth thanks to its growing scale and strong rental rate growth. However, this growth rate has slowed dramatically in recent years, coming in at 5.5% in 2017, 4.4% in 2018, and just 3.8% in 2019 before declining in 2020 and 2021 due to COVID-19. In 2022 FFO per share resumed growth as COVID-19 headwinds dissipated and 2023 is expected to see continued growth. Additional potential headwinds for AvalonBay are the threat of future rent control legislation in its West Coast markets (this has already been on the ballot in recent elections) as well as the uncertain economic climate in AvalonBay's target markets as a result of the fallout from COVID-19, including the growing work from home trend. Overall, we are projecting a 5.5% annualized growth rate 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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
P/FFO	19	24.2	21.8	20.7	19.2	23.3	19.0	29.2	17.2	16.8	16.2	18.0
Avg. Yld.	3.6%	2.7%	3.0%	3.2%	3.4%	2.8%	3.9%	2.6%	3.8%	3.7%	3.8%	3.3%

The P/FFO valuation multiple has varied between the high teens and the low 20s over the past decade, and the dividend yield has ranged between 2.6% and 3.9%. However, the abundant new supply reaching markets combined with increasing inflationary and rising interest rate pressures on margins - not to mention a challenging acquisition climate due to compressed cap rates – will lead to continued slowing growth relative to pre-COVID-19 levels. Therefore, the stock will warrant a lower valuation multiple and a higher dividend yield. Nevertheless, we still think the stock is undervalued at present.

Safety, Quality, Competitive Advantage, & Recession Resiliency

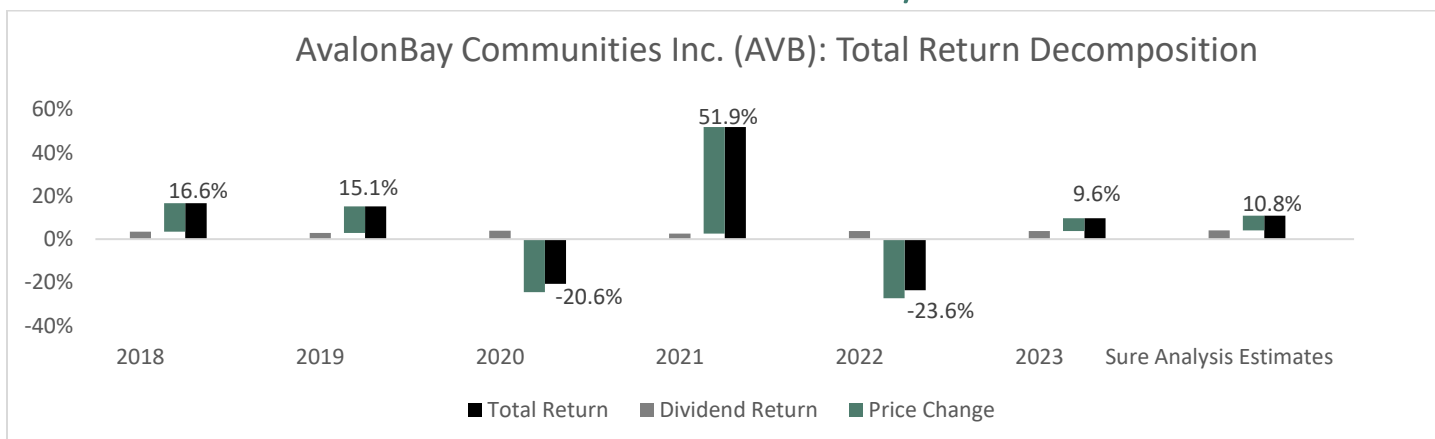
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	68%	66%	66%	66%	65%	65%	73%	77%	65%	62%	62.4%	60.0%

AvalonBay significantly outperformed the S&P 500 during the Great Recession due to the defensive nature of the multifamily sector. However, it still experienced a sizable decline in FFO/share (from \$4.61 in 2007 down to a low of \$3.89 in 2009). Additionally, multifamily apartments lack a strong competitive advantage due to the ease of creating new supply, as well as the alternative sources of affordable housing in large metropolitan areas in which AvalonBay operates. Given that fact, AvalonBay's investments are essentially a bet on the economic strength of its core markets. Furthermore, the fact that most of its assets are high-quality "A" apartment units makes it even more levered to the state of the economy, as these apartments are in high demand during strong economic conditions but are less affordable during a recession. AVB does have considerable economies of scale, low cost of capital, operational and marketing expertise, and a brand name advantage, which enable it to compete effectively against competitors. The trust's balance sheet is also very strong, as its sector-leading A- credit rating makes clear. AvalonBay has plenty of resources to invest in its development projects and sustain the dividend during a downturn, while also reacting opportunistically to opportunities that may become available.

Final Thoughts & Recommendation

AvalonBay has an excellent track record and a stellar balance sheet. AvalonBay appears slightly undervalued at the moment and likely to deliver 10.8% annualized total returns moving forward. As a result, we rate it a Buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	1,685	1,856	2,045	2,159	2,285	2,325	2,301	2,295	2,593	2,768
Gross Profit	1,096	1,214	1,362	1,436	1,518	1,557	1,478	1,441	1,674	1,780
Gross Margin	65.0%	65.4%	66.6%	66.5%	66.4%	67.0%	64.2%	62.8%	64.6%	64.3%
SG&A Exp.	41	43	46	54	60	58	60	70	74	77
D&A Exp.	443	478	531	584	631	662	707	759	815	
Operating Profit	612	693	785	798	826	837	710	613	785	886
Operating Margin	36.3%	37.3%	38.4%	37.0%	36.2%	36.0%	30.9%	26.7%	30.3%	32.0%
Net Profit	684	742	1,034	877	975	786	828	1,004	1,137	929
Net Margin	40.6%	40.0%	50.6%	40.6%	42.7%	33.8%	36.0%	43.8%	43.8%	33.6%
Free Cash Flow	834	1,019	1,087	1,182	1,214	1,181	1,083	1,050	1,247	

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	16,141	16,931	17,867	18,415	18,380	19,121	19,199	19,902	20,458	20,678
Cash & Equivalents	509	401	215	67	92	40	217	420	613	398
Total Liabilities	7,081	7,081	7,688	8,021	7,744	8,128	8,444	8,966	9,202	8,893
Accounts Payable	102	99	101	85	97	92	94	64	73	
Long-Term Debt	6,490	6,457	7,031	7,329	7,040	7,296	7,564	8,104	8,316	7,982
Shareholder's Equity	9,046	9,841	10,171	10,388	10,633	10,990	10,752	10,933	11,253	11,783
LTD/E Ratio	0.72	0.66	0.69	0.71	0.66	0.66	0.70	0.74	0.74	0.68

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	4.3%	4.5%	5.9%	4.8%	5.3%	4.2%	4.3%	5.1%	5.6%	4.5%
Return on Equity	7.7%	7.8%	10.3%	8.5%	9.3%	7.3%	7.6%	9.3%	10.2%	8.1%
ROIC	4.5%	4.7%	6.2%	5.0%	5.5%	4.4%	4.5%	5.4%	5.9%	4.7%
Shares Out.	132.0	137.0	137.0	137.7	138.1	140.3	139.2	139.5	139.7	141.9
Revenue/Share	12.84	13.79	14.88	15.63	16.52	16.66	16.39	16.42	18.53	19.54
FCF/Share	6.35	7.57	7.91	8.56	8.78	8.46	7.71	7.51	8.91	

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

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