Sun Communities (SUI)

Updated November 11th, 2024 by Aristofanis Papadatos

Key Metrics

Current Price:	$125	**5 Year CAGR Estimate:**	8.2%	**Market Cap:**	$16 B
Fair Value Price:	$129	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**[1]	12/27/2024
% Fair Value:	97%	**5 Year Valuation Multiple Estimate:**	0.7%	**Dividend Payment Date:**	1/14/2025
Dividend Yield:	3.0%	**5 Year Price Target**	$165	**Years Of Dividend Growth:**	8
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Hold

Overview & Current Events

Sun Communities (SUI) is a real estate investment trust (REIT) that was founded in 1975 and became public in 1993. It is a leading owner and operator of manufactured housing (50% of total rental revenue), recreational vehicle communities (29% of rental revenue) and marinas (21% of rental revenue), with a market capitalization of $16 billion. Sun Communities is the largest publicly traded owner of manufactured housing in the U.S. and the second-largest owner in the U.K., with a total of nearly 180,000 manufacturing housing and recreational vehicle sites.

In early November, Sun Communities reported (11/6/24) financial results for the third quarter of fiscal 2024. Occupancy at manufactured houses and recreational vehicle sites improved from 97.2% in the prior year's quarter to 98.8%, a markedly high level. Same-property net operating income grew 0.5% thanks to rent hikes. Nevertheless, core funds from operations (FFO) per share dipped -9%, from $2.57 to $2.34, due to a steep increase in interest expense, which was caused by the nearly 23-year high interest rates that have been prevailing in recent months.

Sun Communities lowered its already cautious guidance for 2024 due to asset sales and the double impact of high interest rates on its business. High mortgage rates reduce the demand for housing while high interest rates increase the interest expense of the REIT. As a result, Sun Communities lowered its guidance for growth of same-property net operating income from 4.7%-5.7% to 3.5%-3.9% and its guidance for FFO per share from $7.06-$7.22 to $6.76-$6.84. Accordingly, we have lowered our forecast for FFO per share in 2024 from $7.15 to $6.80. Notably the REIT has raised its dividend by just 1% this year, marking the lowest raise in the last 8 years.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
FFO	$3.06	$3.31	$3.22	$3.95	$4.48	$4.75	$5.09	$6.51	$7.35	$7.10	***$6.80***	***$8.68***
DPS	$2.60	$2.60	$2.60	$2.68	$2.84	$3.00	$3.16	$3.32	$3.52	$3.72	***$3.76***	***$4.28***
Shares[2]	41.8	53.7	66.3	76.7	82.0	88.9	97.5	115.1	122.9	123.5	***125.0***	***180.0***

Sun Communities benefits from highly favorable fundamentals, as there is steadily increasing demand for manufactured houses and recreational vehicle sites while there is very low supply of new units. The REIT has taken advantage of the strong supply-demand characteristics. It has raised the rental rates of manufactured houses and recreational vehicle sites by 4% and 5% per year on average, respectively, over the last decade. Thanks to its strong pricing power, the trust has raised rental rates by 5% at manufactured houses and 6% at recreational vehicle sites this year.

Sun Communities has grown its core FFO per share by 9.8% per year on average over the last decade and by 9.6% per year on average over the last five years. The REIT has stagnated in the last two years due to 23-year high interest rates, which have caused interest expense to double since 2021. However, we view this headwind as temporary, as we expect interest rates to moderate in the upcoming years. We thus expect Sun Communities to grow its FFO per share by 5.0% per year on average beyond this year. If the Fed keeps reducing interest rates until 2026, the REIT may exceed our growth assumptions but we prefer to be on the safe side given the uncertainty over the time of interest rate reductions.

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[1] Estimated date.

[2] 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
Avg P/FFO	16.5	20.0	22.6	21.9	21.5	28.1	28.1	27.1	22.0	18.6	***18.4***	***19.0***
Avg. Yld.	5.1%	3.9%	3.6%	3.1%	3.0%	2.2%	2.2%	1.9%	2.2%	2.8%	***3.0%***	***2.6%***

Thanks to its reliable growth trajectory, Sun Communities has traded at price-to-FFO ratios above 20 for most of the past decade. The REIT is currently trading at a FFO multiple of 18.4, which is lower than the historical 10-year average of 22.6. As interest rates were almost zero for most of the past decade, the historical valuation is probably higher than the fair valuation of the REIT. We assume a fair price-to-FFO ratio of 19.0 for Sun Communities. If the stock trades at its fair valuation level in five years, it will enjoy a 0.7% annualized valuation gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

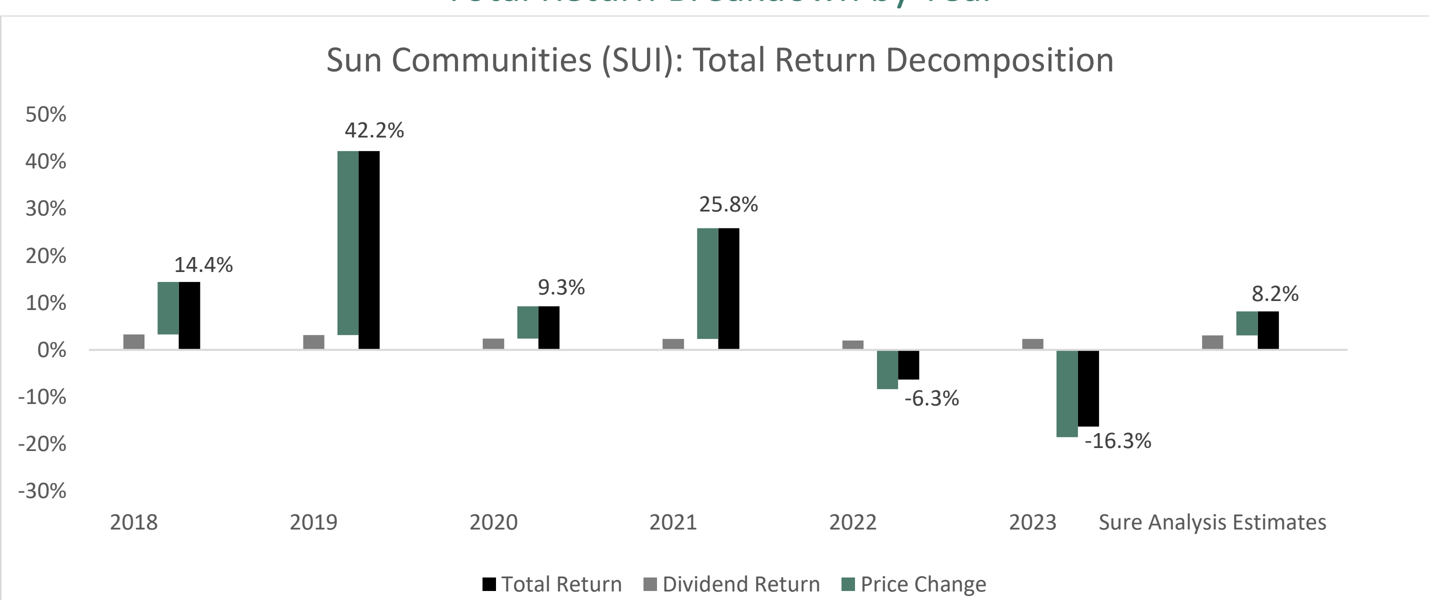
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	85%	79%	81%	68%	63%	63%	62%	51%	48%	52%	***55%***	***49%***

Sun Communities has raised its dividend for only 8 consecutive years and is offering a 3.0% yield, which is much lower than the 4.1% median dividend yield of the REIT sector. In addition, Sun Communities has a material debt load, with a leverage ratio (Net Debt to EBITDA) of 6.0, which is above our comfort maximum of 5.0. On the other hand, net debt is standing at $9.0 billion, which is only 56% of the market cap of the stock, while the REIT has investment grade ratings from S&P (BBB) and Moody's (Baa3). In addition, the REIT proved resilient to the pandemic, as it kept growing its FFO per share and its dividend. Given also its reliable long-term growth trajectory, the REIT is not likely to cut its dividend. Overall, the reliable growth trajectory of Sun Communities compensates for its low dividend yield.

Final Thoughts & Recommendation

Sun Communities passes under the radar of most investors due to its low yield (for a REIT) but it has more promising growth prospects than most REITs. It is currently facing a downturn due to nearly 23-year high interest rates but it is likely to recover strongly in the upcoming years. The stock can offer an 8.2% average annual return over the next five years thanks to 5.0% annual growth of FFO per share, its 3.0% dividend and a 0.7% valuation tailwind. It thus maintains its hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	470	659	816	961	1,106	1,246	1,388	2,260	2,935	3,179
Gross Profit	263	379	460	542	613	699	774	1,151	1,415	1,491
Gross Margin	55.9%	57.6%	56.4%	56.3%	55.4%	56.1%	55.8%	50.9%	48.2%	46.9%
SG&A Exp.	37	47	64	84	81	93	110	181	257	270
D&A Exp.	131	175	219	258	276	315	373	509	576	641
Operating Profit	92	154	174	196	244	278	288	447	557	561
Op. Margin	19.5%	23.4%	21.4%	20.4%	22.1%	22.3%	20.7%	19.8%	19.0%	17.6%
Net Profit	29	155	26	72	107	162	132	380	242	(213)
Net Margin	6.1%	23.6%	3.2%	7.5%	9.7%	13.0%	9.5%	16.8%	8.2%	-6.7%
Free Cash Flow	133	182	241	258	363	477	543	754	735	791
Provision For Tax	0	1	0	(0)	0	1	(1)	1	6	(8)

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	2,938	4,182	5,871	6,112	6,710	7,802	11,207	13,494	17,084	16,941
Inventories	83	45	8	10	62	35	77	66	73	29
Goodwill	9	15	22	30	49	62	47	51	203	206
Cash & Equivalents	30	44	100	86	59	67	734	802	1,420	1,103
Total Liabilities	2,030	2,645	3,509	3,448	3,543	3,899	5,579	6,764	9,196	9,768
Long-Term Debt	1,786	2,290	3,064	3,038	3,052	3,364	4,687	5,602	7,128	7,777
Shareholder's Equity	878	1,456	2,296	2,598	3,107	3,820	5,525	6,624	7,810	7,083
LTD/E Ratio	2.03	1.57	1.33	1.17	0.98	0.88	0.85	0.85	0.91	1.10

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	1.2%	4.4%	0.5%	1.2%	1.7%	2.2%	1.4%	3.1%	1.6%	-1.3%
Return on Equity	4.4%	12.7%	1.3%	2.9%	3.7%	4.6%	2.8%	6.2%	3.3%	-2.8%
ROIC	1.2%	4.8%	0.6%	1.3%	1.8%	2.4%	1.5%	3.4%	1.8%	-1.4%
Shares Out.	41.8	53.7	66.3	76.7	82.0	88.9	97.5	115.1	122.9	123.5
Revenue/Share	11.24	12.27	12.30	12.53	13.48	14.02	14.24	19.64	23.88	25.68
FCF/Share	3.19	3.39	3.64	3.36	4.43	5.36	5.57	6.55	5.98	6.39

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