CyrusOne (CONE)

Updated October 31st, 2020 by Nikolaos Sismanis

Key Metrics

Current Price:	$71	**5 Year CAGR Estimate:**	10.4%	**Market Cap:**	$8.6B
Fair Value Price:	$65	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date:**	12/31/20
% Fair Value:	108%	**5 Year Valuation Multiple Estimate:**	-1.6%	**Dividend Payment Date:**	01/08/21
Dividend Yield:	2.9%	**5 Year Price Target**	$105	**Years Of Dividend Growth:**	7
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	2%

Overview & Current Events

CyrusOne provides mission-critical data center facilities that protect and ensure the continued operation of firms and their IT departments. The company's strategy is focused on attracting customers that have not historically outsourced their data center needs. CyrusOne has approximately 1000 customers, including 200 of the Fortune 1000 companies. CyrusOne operates in the United States, Europe, and Asia. Its data centers provide customers the flexibility and scale to match their specific growth needs ideally. It has a market cap of $8.6 billion and generates annual revenues of around $1 billion. Boosted by the high demand for data and server storage, CyrusOne is currently the fastest-growing data center REIT in the U.S.

On October 28th, the company announced its Q3 2020 earnings for the period ending September 30th, 2020. For the quarter, revenues and normalized FFO grew to $262.8 million and $114.4 million, an increase of 5%, and 10%, respectively. FFO/share rose to $0.96, 5% higher than the year before. The mismatch in growth with the normalized FFO is due to additional share issuance. Overall, the company is set to keep growing as it ended the quarter with $82 million in annualized revenue backlog, representing about $595 million in future total contract value. Additionally, around 63% of its upcoming 345K CSF (Colocation Square Footage) is preleased, indicating strong demand for data centers, as the real estate subsector has been booming during the pandemic. To reassure investors of its strong performance, management narrowed its FY2020 guidance to FFO/share of $3.80-3.90 and total revenues of $1.020B-1.035B.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
FFO/share	--	--	--	$1.22	$1.73	$2.17	$2.66	$3.12	$3.31	$3.63	**$3.85**	**$6.20**
DPS	--	--	--	$0.64	$0.84	$1.26	$1.52	$1.68	$1.84	$1.92	**$2.03**[1]	**$2.59**
Shares[2]	--	--	--	20.9	29.2	54.3	78.3	88.9	99.8	112.1	**119.2**	**200.0**

For REITs like CyrusOne, FFO is a better measurement of profitability and cash flow than the traditional earnings-per-share metric used to value most stocks. REITs often have high rates of depreciation, and therefore EPS is not an adequate measurement of performance. Since its IPO in 2013, the company has been able to expand its FFO consistently every single year rapidly. Over the past five years, FFO/share has seen a CAGR of 12%. DPS has also been increasing annually at a swift CAGR of 20.1% since the REIT's IPO. The company's latest DPS increase of just 2% should not worry investors, as the slowdown is more than likely attributed to preserving liquidity during the current economic environment. CyrusOne should be able to leverage its cheap financing to sustain its speedy growth. Since data centers have been booming under COVID-19, creditors have meager demands, resulting in the company issuing $400 million during the quarter, at a rate as low as 2.15%. Consequently, future acquisitions such as its recent 33 acres of land in London should generate very high ROIs. Combining that 79% of its leases are contractually-locked with rental escalations, future growth prospects remain very promising. We retain our EPS & DPS growth estimates at 10% and 5%, respectively.

[1] Comprised of one $0.50 and three $0.51 distributions during FY2020

[2] Share count is in millions.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/FFO	--	--	--	18.23	15.86	14.02	16.91	18.58	17.58	17.9	**18.4**	**17.0**
Avg. Yld.	--	--	--	3.1%	3.9%	4.0%	3.4%	3.2%	3.3%	2.9%	**2.9%**	**2.5%**

Like with the rest of high-growth data center REITS, CyrusOne trades at a premium compared to traditional REITs. The stock is currently hovering at the higher-range of its historical multiples, around 18.4 times its FFOs, primarily powered by the stability of cash flows generated its properties. Data centers cannot simply shut down. Unlike, say a mall tenant, firms that rent the company's facilities cannot suspend their usage of data centers, especially now, since online traffic is hitting all-time highs. As investors are rushing to capture such secure distributable funds, we expect shares to continue trading at a premium and retain our fair valuation multiple of 17X FFOs, reflecting datacenters remaining increasingly attractive. Since our last report, the stock's yield has risen to 2.9% amid the market's recent correction, which dividend growth investors looking to initiate or double-down to their existing position are likely to appreciate.

Safety, Quality, Competitive Advantage, & Recession Resiliency

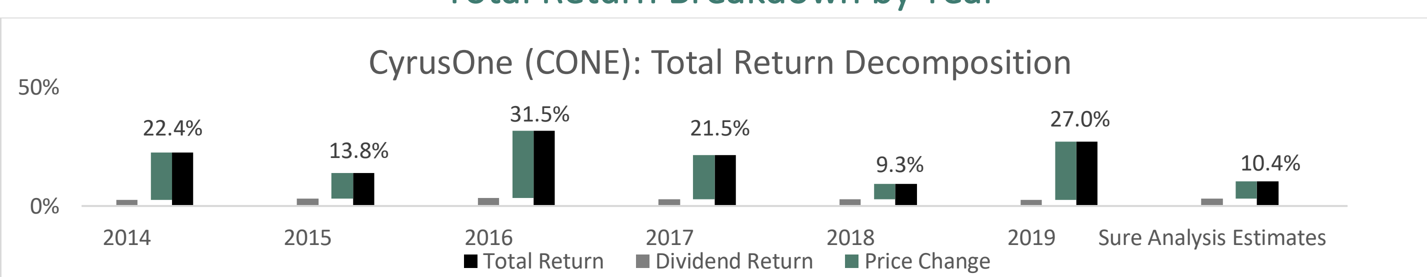
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	--	--	--	--	62.5%	73.2%	56.7%	64.7%	55.4%	46.6%	**52.7%**	***42.0%***

Being a data center REIT, CyrusOne is currently in an advantageous position, benefiting from its mission-critical tenants' secured cash flows. The company is unlikely to experience any rent deferrals, as was the case with the more traditional REITs over the past few months. Moreover, the company is prudent with its distributions, proven by its thoughtful DPS increase despite delivering satisfactory FFO/share growth during such uncertain times. The balance sheet is robust, with approximately $6.7 billion worth of real estate assets vs. $3.2 billion of long-term debt, while the previously worrying interest coverage ratio of around 1.0X its operating cash flows jumped to 1.2X, easing and short-term obligation concerns. Finally, distributions remain incredibly safe, and as already proven, they can easily withstand a potential recession going forward, facing little to no correlation with the overall economy's performance.

Final Thoughts & Recommendation

CyrusOne offers a compelling investment case. The company operates in probably the most exciting and secure sub-sector of REITs, so its premium valuation is understandable. With attractive characteristics like rapid FFO growth, a low payout ratio, and a quality pool of mission-critical tenants, the stock is a buy. Because of shares correcting over the past couple of months, the stock has climbed down from its previous, notable overvalued levels, closer to its fair price. As a result, we expect CyrusOne to deliver double-digit annualized returns over the next few years, fueled by the consistent demand for its data centers, durable pricing power with embedded rental escalations, and a significant backlog in development, soon to be contributing additional cash flows.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	---	---	---	---	$331	$399	$529	$672	$821	$981
Gross Profit	---	---	---	---	$206	$251	$342	$437	$529	$598
Gross Margin	---	---	---	---	62.4%	62.8%	64.6%	65.0%	64.4%	60.9%
SG&A Exp.	---	---	---	---	$47	$59	$78	$84	$100	$104
D&A Exp.	---	---	---	---	$118	$142	$184	$259	$334	$418
Operating Profit	---	---	---	---	$41	$50	$80	$94	$95	$77
Operating Margin	---	---	---	---	12.4%	12.6%	15.1%	14.0%	11.5%	7.8%
Net Profit	---	---	---	---	-$8	-$15	$20	-$84	$1	$41
Net Margin	---	---	---	---	-2.4%	-3.9%	3.8%	-12.4%	0.1%	4.2%
Free Cash Flow	---	---	---	---	-$173	-$94	$181	$290	$309	$366
Income Tax	---	---	---	---	$1.4	$1.8	$1.8	$3.0	$0.6	-$3.7

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	---	---	---	---	$1,571	$2,196	$2,852	$4,312	$5,593	$6,142
Cash & Equivalents	---	---	---	---	$37	$14	$15	$152	$64	$76
Accounts Receivable	---	---	---	---	$61	$76	$83	$87	$235	$292
Goodwill & Int. Ass.	---	---	---	---	$345	$624	$605	$658	$691	$651
Total Liabilities	---	---	---	---	$854	$1,374	$1,690	$2,598	$3,367	$3,707
Accounts Payable	---	---	---	---	$70	$137	$227	$98	$121	$123
Long-Term Debt	---	---	---	---	$644	$997	$1,240	$2,089	$2,625	$2,887
Shareholder's Equity	---	---	---	---	$461	$822	$1,162	$1,714	$2,226	$2,435
D/E Ratio	---	---	---	---	1.40	1.21	1.07	1.22	1.18	1.19

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	---	---	---	---	-0.6%	-0.8%	0.8%	-2.3%	0.0%	0.7%
Return on Equity	---	---	---	---	-2.0%	-2.4%	2.0%	-5.8%	0.1%	1.8%
ROIC	---	---	---	---	-0.7%	-1.0%	0.9%	-2.7%	0.0%	0.8%
Shares Out.	---	---	---	---	29.2	54.3	79.0	88.9	100.4	112.5
Revenue/Share	---	---	---	---	$11.33	$7.35	$6.70	$7.56	$8.18	$8.72
FCF/Share	---	---	---	---	-$5.93	-$1.74	$2.29	$3.26	$3.08	$3.25

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