Spirit Realty Capital (SRC)

Updated May 17th, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	$47	**5 Year CAGR Estimate:**	8.4%	**Market Cap:**	$5.67 B
Fair Value Price:	$46	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	06/29/2022[1]
% Fair Value:	101%	**5 Year Valuation Multiple Estimate:**	-0.2%	**Dividend Payment Date:**	07/15/2022
Dividend Yield:	5.5%	**5 Year Price Target**	$56	**Years Of Dividend Growth:**	1
Dividend Risk Score:	F	**Retirement Suitability Score:**	C	**Rating:**	Hold

Overview & Current Events

Spirit Realty Capital is a premier net-lease REIT, mainly investing in single-tenant retail locations. The company's portfolio is well diversified, comprised of more than 2,000 properties in 48 states, leased to 334 tenants who operate in 35 different industries. Leveraging its diversified real estate assets, Spirit Realty aims to provide investors with long term stable returns. Its convenience and drug stores, home improvement stores, and various other essential properties account for around half of the trust's portfolio and have provided resilient cash flows during the pandemic. Spirit Realty is based in Dallas, Texas, and generates around $500 million in annual rental revenues.

On May 3rd, 2022, Spirit Realty reported its Q1 results for the period ending March 31st, 2022. For the quarter, rental income and FFO/share were $168.4 million and $0.95, an increase of 24.6% and 90%, respectively. Higher revenues were driven by accretive acquisitions and record occupancy levels, currently standing at a remarkable 99.8%. Occupancy remained unchanged quart-over-quarter.

Spirit Realty also collected 99.94% of its rent during Q1, which is quite noteworthy considering its extensive tenant base. The company purchased an additional 41 properties during Q1, with an average cash yield of 6.42%. The new properties increased Spirit's portfolio diversification.

Management reiterated its prior FY2022 FFO/share guidance, expecting AFFO/share between $3.52 and $3.58, the midpoint of which we have utilized in our calculations (Core FFO should land quite close to this figure as well.)

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
FFO/Share[2]	$2.85	$2.07	$3.06	$4.09	$4.20	$3.91	$3.71	$3.34	$2.73	$3.26	***$3.55***	***$4.32***
DPS	---	$1.35	$2.99	$3.06	$3.15	$3.20	$2.95	$2.50	$2.50	$2.52	***$2.55***	***$2.82***
Shares[3]	16	51	77	87	94	94	87	91	104	118	***128***	***140***

Spirit Realty's FFOs have failed to grow over the past few years, mainly caused by the challenges faced by retail REITs due to the rise of e-commerce, several acquisitions/dispositions, and, most recently, the ongoing pandemic. With the company delivering robust operational metrics during Q1 despite operating in a challenging real estate space, we believe that its performance is poised to shine as the retail economy gradually recovers.

We forecast an FFO/Share of 4% in the medium term, driven by rental collections continuing to improve, rental escalations, and attractive yields in its newly acquired properties. Regarding its DPS, it has fluctuated over the years, in line with Spirit's FFOs. Management has mentioned that it intends to maintain a payout ratio of around 75% to FFO/share. Following improving results, we retain our DPS growth estimates to 2% since FFO/share growth should sustain marginal dividend increases while retaining such a ratio. This was in line with Spirit's recent dividend hike as well. Still, investors should not rely on annual increases in the medium-term.

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[1] Estimated dates

[2] FFO/Share in 2010 and 2011 are prior to SRC's listing in 2012, hence the lack of P/FFOs as well.

[3] Share count is in millions.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
P/FFO	12.3	22.5	16.3	10.3	14	9.7	9.4	12.9	12.8	14.4	***13.1***	***13.0***
Avg. Yld.	---	1.2%	4.8%	6.0%	5.4%	8.1%	8.3%	5.4%	6.9%	5.3%	***5.5%***	***5.0%***

Due in part to the company's volatile FFO results, the stock's valuation has hovered in the high-single to low double-digits, lower than the REIT sector's average. As a result, despite the current DPS being lower than its past rates, shares are currently yielding a sizeable 5.5%, significantly higher than the sector's average of ~3.9%. The market has effectively priced the lack of meaningful growth, hence the high yield. We expect Spirit's P/FFO to remain near its current levels, at around 13x FFO, at which point the yield adequately compensates for the lack of rapid growth ahead.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	---	65%	98%	75%	75%	82%	80%	75%	92%	77%	72%	***65%***

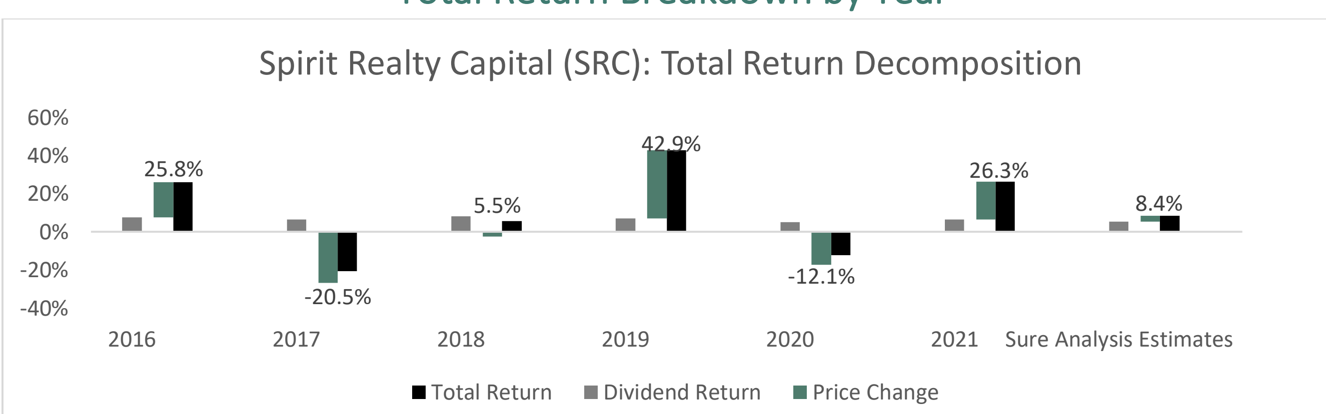
Spirit Realty's much-diversified portfolio is a double-edged sword. On the one hand, investors gain exposure in every single retail sub-sector, spread across hundreds of tenants in almost every state, enjoying a mixed stream of cash flows. On the other hand, having to manage thousands of smaller properties in what is currently the riskiest real estate sector has resulted in a lack of stability and growth in Spirit's FFOs. We believe the current dividend is safe for now, as payouts are covered adequately, while rental escalations should grow that margin further over time unless marginal DPS increases occur.

Interest coverage currently stands at 2.7 times its operating cash flows, which is significantly higher than the industry's median of 1.5. Still, considering the company's volatile performance and retail exposure, it's likely that creditors will demand higher rates upon refinancing its loans (the current cost of debt is a modest 3.58%). This seems to be changing as of recently amid Sprit's favorable refinancing, nonetheless. We see Spirit's qualities outweighing its dangers, overall.

Final Thoughts & Recommendation

Overall, Spirit Realty's Q1 results demonstrated another quarter of resilient performance. The occupancy rate was phenomenal, rental collections were robust, and management's FY2022 guidance remains quite promising. Simultaneously, shares are relatively fairly valued. Amid an attractive valuation, solid growth prospects, and its current above-average yield, we forecast annualized returns of around 8.4% in the medium-term. Accordingly, the stock earns a hold rating.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	419	603	667	435	431	445	516	484	608
Gross Profit	406	576	637	406	403	424	498	459	585
Gross Margin	96.8%	95.5%	95.4%	93.4%	93.4%	95.3%	96.4%	94.8%	96.2%
SG&A Exp.	36	56	48	49	55	53	52	48	53
D&A Exp.	168	248	261	262	256	198	175	213	245
Operating Profit	206	272	329	185	173	208	269	196	287
Op. Margin	49.1%	45.2%	49.2%	42.4%	40.0%	46.8%	52.1%	40.5%	47.2%
Net Profit	-2	-37	93	97	77	132	175	27	172
Net Margin	-0.4%	-6.1%	14.0%	22.4%	17.9%	29.7%	33.9%	5.6%	28.3%
Free Cash Flow	125	213	362	361	348	284	291	302	389
Income Tax	1	1	1	1	1	1	12	0.3	0.6

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	7231	7964	7891	7678	7264	5096	5833	6397	7331
Cash & Equivalents	67	176	22	10	9	14	14	70	18
Goodwill & Int.	910	876	791	725	532	520	611	594	653
Total Liabilities	4113	4653	4429	3996	3944	2295	2419	2796	3331
Accounts Payable	115	123	142	149	132	---	---	---	---
Long-Term Debt	3778	4323	4093	3665	1713	2055	2153	2506	3013
Total Equity	3118	3312	3462	3682	3153	2636	3247	3435	3834
LTD/E Ratio	1.21	1.31	1.18	1.00	0.52	0.73	0.63	0.70	0.75

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.0%	-0.5%	1.2%	1.3%	1.0%	2.1%	3.2%	0.4%	2.5%
Return on Equity	-0.1%	-1.1%	2.8%	2.7%	2.3%	4.6%	6.0%	0.8%	4.7%
ROIC	0.0%	-0.5%	1.2%	1.3%	1.2%	2.7%	3.4%	0.5%	2.6%
Shares Out.	51.0	77.4	86.5	93.8	93.6	86.5	90.9	104.5	118.7
Revenue/Share	8.22	7.79	7.71	4.64	4.61	5.15	5.68	4.63	5.13
FCF/Share	2.45	2.76	4.18	3.84	3.72	3.28	3.21	2.89	3.28

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