

AvalonBay Communities (AVB)

\$151.74 (As of 08/11/20)

Price Target (6-12 Months): **\$129.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 07/07/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: D

Summary

AvalonBay's lower-than-expected second-quarter results reflect uncollectible lease revenues as well as a decline in economic occupancy. The company has high quality assets in some of the premium markets of the United States, a healthy balance sheet, and is leveraging technology, scale and organizational capabilities to drive growth. However, its performance in the near term is likely to continue to bear the brunt of the pandemic with economy and job markets being widely affected. Particularly, rental housing demand in higher cost and urban/infill markets is being adversely impacted by the work-from-home flexibility, low mortgage rates and reduced demand from corporates and students. As such, its occupancy and pricing power are likely to continue to feel the heat. Also, its shares have underperformed the industry over the past year.

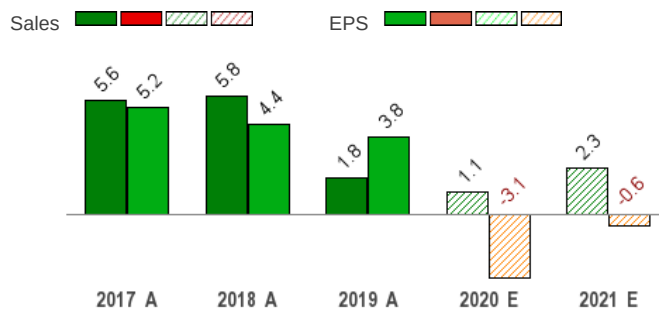
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$229.09 - \$118.17
20 Day Average Volume (sh)	967,714
Market Cap	\$21.4 B
YTD Price Change	-27.6%
Beta	0.79
Dividend / Div Yld	\$6.36 / 4.2%
Industry	REIT and Equity Trust - Residential
Zacks Industry Rank	Bottom 10% (228 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-0.9%
Last Sales Surprise	-1.9%
EPS F1 Est- 4 week change	-0.2%
Expected Report Date	10/26/2020
Earnings ESP	-2.8%
P/E TTM	16.2
P/E F1	16.8
PEG F1	3.0
P/S TTM	9.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	591 E	596 E	599 E	602 E	2,403 E
2020	602 A	576 A	577 E	581 E	2,350 E
2019	460 A	577 A	588 A	594 A	2,325 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.16 E	\$2.20 E	\$2.23 E	\$2.29 E	\$9.00 E
2020	\$2.39 A	\$2.23 A	\$2.18 E	\$2.22 E	\$9.05 E
2019	\$2.30 A	\$2.27 A	\$2.34 A	\$2.43 A	\$9.34 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/11/2020. The reports text is as of 08/12/2020.

Overview

AvalonBay Communities, Inc. is a real estate investment trust (REIT) primarily focusing on developing, redeveloping, acquisition, ownership and operations of multi-family apartment communities for higher-income clients in high barrier-to-entry regions of the United States, which generally command the highest rents in the markets.

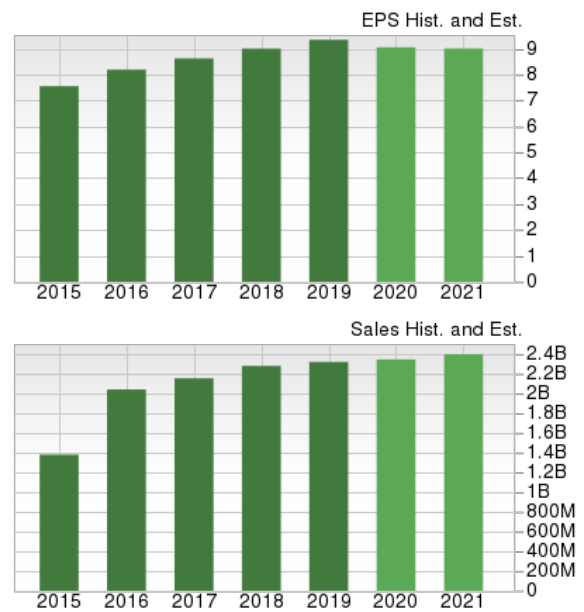
These markets include New England, the New York/New Jersey metro area, the Mid-Atlantic, the Pacific Northwest, and Northern and Southern California. The company is also targeting expansion in Southeast Florida and Denver, CO.

The company focuses on metropolitan areas historically experiencing rising employment in high wage sectors of the economy, along with high home ownership cost and vibrant quality of life. The company has a principal executive office in Arlington, VA, and a number of regional offices, administrative offices or specialty offices in its markets.

AvalonBay owned or held direct or indirect ownership stake in 295 apartment communities as of Jun 30, 2020. These communities included 86,380 apartment homes in 11 states and the District of Columbia.

During the April-June period, the company did not commence or complete any development communities. As of Jun 30, 2020, AvalonBay had 19 development communities under construction (expected to contain 6,198 apartment homes and 64,000 square feet of retail space). The estimated total capital cost at completion for these development communities is \$2.34 billion at share.

Note: All EPS numbers presented in this report represent funds from operations ("FFO") per share. FFO, a widely used metric to gauge the performance of REITs, is obtained after adding depreciation and amortization and other non-cash expenses to net income.



Reasons To Sell:

- ▼ The coronavirus pandemic has been wreaking havoc and resulting in macroeconomic uncertainty and choppy job-market environment, resulting in household contraction and consolidation. Apart from these, a number of factors are affecting rental demand, including pandemic and work-from-home flexibility that is resulting in a shift of some renter demand away from higher cost and urban/infill markets. In addition, record-low mortgage rates and the desire for space is spurring homes sales. Moreover, there is a decline in demand from two categories of renters — corporate and students — since most temporary corporate assignments have been canceled, while higher education is adopting remote learning models and limiting on-campus activities for the fall. As such, there is a reduced demand in many urban submarkets.
 - ▼ Moreover, amid this situation, there is a pressure on occupancy and rent change, while rent-paying capability of tenants has been affected. In fact, the company's second-quarter 2020 same-store residential revenue decline reflects a loss of occupancy and uncollectible lease revenues or bad debt. Particularly, blended lease rent change reflects a contraction of 40 basis points (bps) in the second quarter, while effective rent change was down 3.1%. Economic occupancy shrunk 120 bps, while bad debt was 200 bps higher than normal. Given the magnitude of the downturn as well as eviction moratorium in many of its markets, higher-than-normal bad debt is likely to continue in the near term. Furthermore, amid a slowdown in demand, concession activity is likely to be high. In fact, during the second quarter, the company experienced higher concessions and lower other income with the waiving of various fees for its residents, including late payments. Given the magnitude of uncertainty in the economy and about reopening, any turnaround is unlikely in the near term.
 - ▼ The health crisis has also resulted in construction delays, particularly, at the beginning of the pandemic. This weighed on both deliveries and occupancies during the second quarter, lowering lease-up NOI from new development. Moreover, new rent-control regulations have been introduced in some of the major markets in recent times, while a number of other markets are being considered for establishing such regulations in future. This is likely to curb any significant growth in the top line.
 - ▼ The company also faces stiff competition from other housing alternatives such as rental apartments, condominiums and single-family homes. Such a competitive landscape limits the company's ability to increase rent, thereby restricting its growth momentum to some extent.
 - ▼ Shares of AvalonBay have lost 25.7% over the past year, wider than its industry's decline of 18%. Additionally, the trend in estimate revision for current-year FFO per share is not favorable for the company. The Zacks Consensus Estimate for 2020 FFO per share witnessed marginal downward revision over the past week. Therefore, given the above-mentioned concerns and downward estimate revisions, the stock is unlikely to perform well in the near-term.
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Adverse impacts of coronavirus pandemic on economy and job market will likely affect demand and hurt the rent-paying capability of tenants, leading to rental concessions and pricing-power moderation.

Risks

- AvalonBay has high-quality assets located in some of the premium markets of the country, which enable the company to generate steady rental revenues. The company's properties generally command the highest rents in its markets.
 - Demographic growth also continues to be strong in the young-adult age cohort, which has a higher propensity to rent. People in the age bracket of 20-34 are the main cohort for formation of the new households and majority of them prefer to remain renters and enjoy locational advantage as well as flexibility that rental apartments offer. Further, a significant change in lifestyle has taken place and life cycle events are getting delayed. This is leading to an extension of the average age of first-time homeownership.
 - AvalonBay is also leveraging technology, scale and organizational capabilities to drive innovation and margin expansion in its portfolio. This has become all the more essential in this social-distancing era, as the virus outbreak needed a quick shift to virtual operations for the continuity of normal business operations.
 - AvalonBay has a healthy balance sheet and ample liquidity to sail through these uncertain times. In addition, since late 2008, the company's net debt-to-EBITDA ratio has improved to 4.9x from 6.5x, while the interest coverage ratio has increased to 6.9x from 4.5x. As of Jun 30, 2020, AvalonBay did not have any borrowings outstanding under its \$1.75-billion unsecured credit facility. Further, its unencumbered NOI percentage has increased to 94% from 77%, providing scope for tapping additional secured debt capital if required. Also, it currently has credit ratings of A-, Stable Outlook from S&P and A3, Stable Outlook from Moody's. Thus, the company remains well poised to capitalize on investment opportunities which might come up because of this downturn.
 - Also, solid dividend payouts are arguably the biggest enticement for REIT investors and AvalonBay has consistently paid dividends each year since it went public in 1994. In fact, concurrent with its fourth-quarter 2019 earnings release, AvalonBay announced a 4.6% hike in its quarterly dividend rate, which continued the more than 20-year history of solid dividend growth. Since its IPO, the company has achieved annualized dividend growth of 5.2%. Along with a healthy balance sheet, such efforts boost investors' confidence in the stock.
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Last Earnings Report

AvalonBay Communities Q2 FFO & Revenues Miss Estimates

AvalonBay's second-quarter 2020 core FFO per share of \$2.23 edged down 1.8% year over year from the prior-year quarter's \$2.27. The reported figure also missed the Zacks Consensus Estimate of \$2.25.

Results reflect uncollectible lease revenues from residential and retail properties as well as decline in economic occupancy.

Total revenues of \$576.4 million slipped 0.1% year over year. The revenue figure also missed the Zacks Consensus Estimate of \$587.6 million.

The company also noted about the second-quarter residential revenue collections for established communities, through Jul 28, 2020. The collected residential revenue improved to 97.7% for April compared with the 93.9% at month end, 96.4% for May compared with the 92.8% at month end and 95.5% for June compared with the 93.6% at month end. Moreover, collected residential revenues for July was 93.3% as of Jul 28, 2020.

Quarter in Detail

In the reported quarter, revenues from established communities decreased 3% year over year to \$523.5 million. Residential and retail uncollectible lease revenues resulted in this decrease. Economic occupancy was down 120 basis points, while bad debt was 200 bps higher than normal. Operating expenses for established communities slid 1.1% on a year-over-year basis. Consequently, NOI from established communities dropped 3.7% year on year to \$368.2 million.

During the April-June period, the company did not commence or complete any development communities. As of Jun 30, 2020, AvalonBay had 19 development communities under construction (expected to contain 6,198 apartment homes and 64,000 square feet of retail space). The estimated total capital cost at completion for these development communities is \$2.34 billion at share.

As of Jun 30, 2020, the projected total capital cost of development rights increased to \$4.2 billion from the prior-quarter end's \$4.1 billion.

Balance Sheet Position

As of Jun 30, 2020, AvalonBay did not have any borrowings outstanding under its \$1.75-billion unsecured credit facility. The company had \$415.7 million in unrestricted cash and cash in escrow as of the same date. In addition, its annualized net debt-to-core EBITDA for the April-June quarter was 4.9 times and unencumbered NOI was 94%.

Stock-Repurchase Program

The company's board of directors also approved a new stock-repurchase program, under which it might acquire shares of its common stock up to an aggregate purchase price of \$500 million in open market or negotiated transactions. There is no expiration date for this stock-repurchase program.

Quarter Ending 06/2020

Report Date	Jul 29, 2020
Sales Surprise	-1.90%
EPS Surprise	-0.89%
Quarterly EPS	2.23
Annual EPS (TTM)	9.39

Recent News

Dividend Update

On May 12, AvalonBay's board of directors announced second-quarter 2020 dividend of \$1.59 per share. This dividend was paid on Jul 15, to common stockholders of record as of Jun 30, 2020.

Valuation

AvalonBay's shares are down 25.7% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector declined 18% and 6.6%, over the past year, respectively.

The S&P 500 Index has been up 14.1% over the past year.

The stock is currently trading at 16.82X forward 12-month FFO, which compares to 17.95X for the Zacks sub-industry, 16.83X for the Zacks sector and 22.80X for the S&P 500 Index.

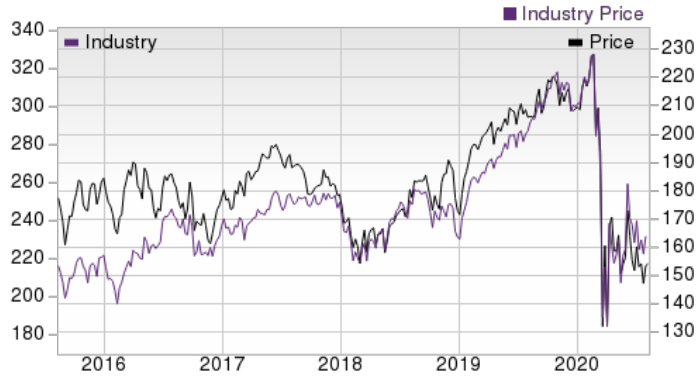
Over the past five years, the stock has traded as high as 23.09X and as low as 12.27X, with a 5-year median of 20.61X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$129 price target reflects 14.30X FFO.

The table below shows summary valuation data for AVB.

Valuation Multiples - AVB					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	16.82	17.95	16.83	22.80
	5-Year High	23.09	22.36	16.83	22.80
	5-Year Low	12.27	15.54	11.59	15.25
	5-Year Median	20.61	18.47	14.26	17.58
P/S F12M	Current	8.96	9.52	6.22	3.67
	5-Year High	12.97	12.16	6.66	3.67
	5-Year Low	6.87	7.58	4.96	2.53
	5-Year Median	11.51	9.28	6.06	3.05
P/B TTM	Current	1.96	2.31	2.47	4.68
	5-Year High	2.9	3.30	2.91	4.68
	5-Year Low	1.54	1.82	1.72	2.83
	5-Year Median	2.46	2.42	2.53	3.74

As of 08/11/2020

Industry Analysis Zacks Industry Rank: Bottom 10% (228 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Equity Residential (EQR)	Neutral	4
Essex Property Trust, Inc. (ESS)	Neutral	4
Investors Real Estate Trust (IRET)	Neutral	3
MidAmerica Apartment Communities, Inc. (MAA)	Neutral	3
NexPoint Residential Trust, Inc. (NXRT)	Neutral	3
United Dominion Realty Trust, Inc. (UDR)	Neutral	4
Apartment Investment and Management Company (AIV)	Underperform	4
Camden Property Trust (CPT)	Underperform	4

Industry Comparison Industry: Reit And Equity Trust - Residential				Industry Peers		
	AVB	X Industry	S&P 500	EQR	ESS	MAA
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	4	4	3
VGM Score	D	-	-	C	D	C
Market Cap	21.36 B	1.22 B	23.61 B	20.38 B	14.32 B	13.35 B
# of Analysts	7	5	14	11	9	6
Dividend Yield	4.19%	4.02%	1.69%	4.40%	3.79%	3.43%
Value Score	D	-	-	C	D	D
Cash/Price	0.02	0.03	0.07	0.01	0.02	0.00
EV/EBITDA	19.23	16.90	13.32	12.86	17.83	16.90
PEG Ratio	2.96	4.38	2.95	4.27	7.28	NA
Price/Book (P/B)	1.96	1.87	3.22	1.89	2.26	2.16
Price/Cash Flow (P/CF)	14.30	13.76	12.79	10.94	16.11	15.53
P/E (F1)	16.73	16.68	22.02	16.34	16.60	18.79
Price/Sales (P/S)	9.05	6.14	2.57	7.53	9.51	8.02
Earnings Yield	5.96%	6.00%	4.29%	6.12%	6.03%	5.32%
Debt/Equity	0.72	0.99	0.77	0.78	0.99	0.72
Cash Flow (\$/share)	10.61	2.46	6.94	5.00	13.62	7.52
Growth Score	D	-	-	D	D	C
Hist. EPS Growth (3-5 yrs)	3.84%	2.81%	10.41%	1.29%	7.36%	3.03%
Proj. EPS Growth (F1/F0)	-3.09%	-2.58%	-6.51%	-3.99%	-1.15%	-5.16%
Curr. Cash Flow Growth	-9.39%	7.20%	5.22%	23.84%	5.93%	20.94%
Hist. Cash Flow Growth (3-5 yrs)	6.67%	15.38%	8.55%	5.74%	12.62%	15.27%
Current Ratio	1.40	1.41	1.34	1.06	1.83	0.08
Debt/Capital	41.83%	47.18%	44.59%	44.70%	50.00%	42.02%
Net Margin	33.32%	14.71%	10.13%	41.64%	41.70%	20.38%
Return on Equity	7.21%	4.71%	14.59%	10.62%	9.81%	5.57%
Sales/Assets	0.12	0.12	0.51	0.13	0.12	0.15
Proj. Sales Growth (F1/F0)	5.93%	2.32%	-1.45%	-2.83%	4.24%	0.44%
Momentum Score	D	-	-	A	C	B
Daily Price Chg	-1.34%	-0.93%	-0.17%	-1.10%	-1.77%	-0.29%
1 Week Price Chg	0.48%	1.27%	2.30%	2.91%	1.11%	-2.27%
4 Week Price Chg	-1.72%	3.37%	6.41%	-3.98%	-3.84%	3.34%
12 Week Price Chg	-1.88%	14.47%	15.42%	-5.15%	-4.96%	5.03%
52 Week Price Chg	-25.69%	-23.13%	2.88%	-32.32%	-29.93%	-6.08%
20 Day Average Volume	967,714	437,842	2,007,486	2,588,881	437,842	541,477
(F1) EPS Est 1 week change	-0.24%	0.00%	0.00%	0.11%	-0.21%	1.11%
(F1) EPS Est 4 week change	-0.23%	0.00%	1.84%	0.11%	-0.21%	1.33%
(F1) EPS Est 12 week change	-4.05%	-2.78%	2.40%	-3.86%	-1.87%	-0.77%
(Q1) EPS Est Mthly Chg	-0.67%	0.00%	0.72%	1.48%	-0.25%	2.08%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	D
Momentum Score	D
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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