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Jan 15, 2020

AvalonBay Communities (AVB)

$209.51 (As of 01/14/20)

Price Target (6-12 Months): **$222.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 01/16/19) Prior Recommendation: Outperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:F
	Value: F | Growth: D | Momentum: D	

Summary

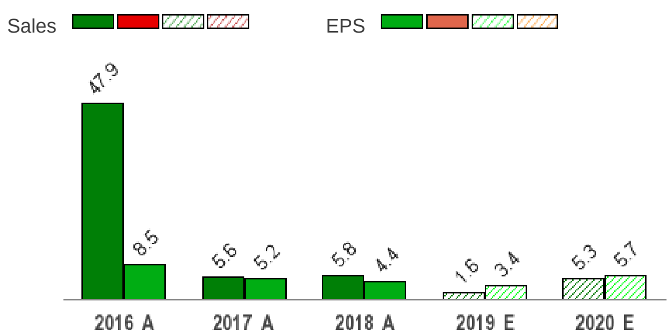
AvalonBay is anticipated to benefit from its high-quality assets in premium locations, favorable demographics, household formation and job-market growth. The company has a healthy balance sheet to support its growth endeavors. Following a robust prime leasing season in 2019, the U.S. apartment rental market put up a decent show in October and November, despite demand for apartments generally slowing down during the colder months, as renters usually prefer less to move in this season. However, new apartment deliveries are likely to remain elevated in its markets in the near-to-mid term, curtailing robust growth in rent and occupancy level. Also, shares of AvalonBay have underperformed its industry so far in the year, while the trend in estimate revisions of 2019 funds from operations (FFO) per share does not indicate an upbeat outlook.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$222.87 - $178.28**
20 Day Average Volume (sh)	**575,252**
Market Cap	**$29.3 B**
YTD Price Change	**-0.1%**
Beta	**0.45**
Dividend / Div Yld	**$6.08 / 2.9%**
Industry	**REIT and Equity Trust - Residential**
Zacks Industry Rank	**Top 46% (116 out of 254)**
Last EPS Surprise	**-0.4%**
Last Sales Surprise	**0.3%**
EPS F1 Est- 4 week change	**0.0%**
Expected Report Date	**02/05/2020**
Earnings ESP	**0.0%**
P/E TTM	**22.7**
P/E F1	**21.3**
PEG F1	**3.8**
P/S TTM	**13.3**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2020	596 E	603 E	608 E	614 E	2,445 E
2019	460 A	577 A	588 A	594 E	2,322 E
2018	561 A	569 A	576 A	579 A	2,285 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	$2.41 E	$2.41 E	$2.46 E	$2.53 E	$9.84 E
2019	$2.30 A	$2.27 A	$2.34 A	$2.39 E	$9.31 E
2018	$2.18 A	$2.21 A	$2.28 A	$2.31 A	$9.00 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 01/14/2020. The reports text is as of 01/15/2020.

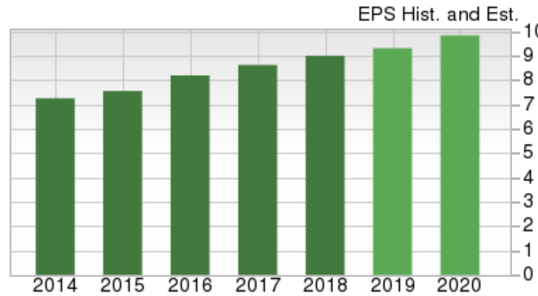
Overview

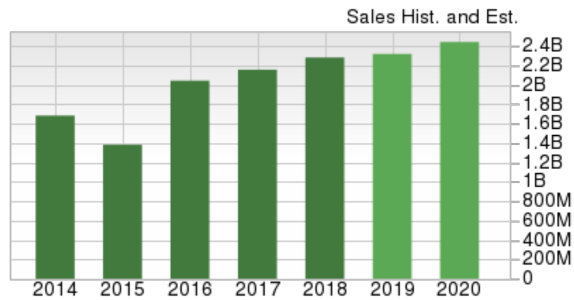
AvalonBay Communities, Inc. is a real estate investment trust (REIT) primarily focusing on developing multifamily apartment communities for higher-income clients in high barrier-to-entry regions of the U.S.

These markets include the New England, the New York/New Jersey Metro area, the Mid-Atlantic, the Pacific Northwest, and the Northern and Southern California regions of the United States typically characterized by dense population, low supply of zoned apartment land, and lengthy, contentious entitlement processes. 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 292 apartment communities as of Sep 30, 2019. These communities included 85,647 apartment homes in 11 states and the District of Columbia. Of the total communities, 20 were under construction and five were under re-development as of that date.

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 Buy:

Amid favorable demographics and healthy demand in its markets, AvalonBay is well poised to grow given its portfolio of high-quality assets in premium locations. It also has a healthy balance sheet.

▲ AvalonBay has high quality assets located in some of the premium markets of the country, which enable the company to generate steady rental revenues. Moreover, a stable economic growth is likely to support the industry. High consumer confidence on the back of a healthy labor market is expected to spur demand for the company's properties. Amid these, lease ups are performing well and are likely to contribute considerably to core FFO per share growth. Moreover, AvalonBay's current development activity is expected to contribute significantly to its NOI growth.

▲ Demographic growth continues to be strong in the young-adult age cohort, which has a higher propensity to rent. In fact, 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. This age cohort has also experienced a considerable part of the net job growth and is helping to grow primary renter demand. Household formation is also picking up pace, which is encouraging.

▲ AvalonBay is also leveraging technology, scale and organizational capabilities to drive innovation and margin expansion in its portfolio. In addition, easy availability of capital and comparatively lower levels of interest rates keep the momentum upbeat. Moreover, following a robust prime leasing season in 2019, the U.S. apartment rental market put up a decent show in October and November, despite demand for apartments generally slowing down during the colder months, as renters usually prefer less to move in winters.

▲ AvalonBay has a healthy balance sheet and ample liquidity to support its growth needs. As of Sep 30, 2019, AvalonBay did not have any borrowings outstanding under its $1.75-billion unsecured credit facility. The company had around $334.75 million in unrestricted cash and cash in escrow as of the same date. In addition, the company's annualized net debt-to-core EBITDA for the July-September quarter was 4.7 times. Further, it generates 93% unencumbered NOI, which is encouraging.

▲ Moreover, 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 2018 earnings release, AvalonBay announced a 3.4% 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.

Reasons To Sell:

- New apartment deliveries are anticipated to remain elevated in a number of the company's markets in the near-to-mid term. This high supply is likely to put pressure on rental rates. Hence, growth in its stabilized portfolio is likely to remain modest in the upcoming period. Furthermore, there is high concession activity amid higher supply, which remains a concern.

- Although interest-rate levels are low, presently, any hike in future will likely be a challenge for the company. Essentially, rising rates imply higher borrowing cost for the company, which would affect its ability to purchase or develop real estate and lower dividend payouts as well. In addition, the dividend payout itself might become less attractive than the yields on fixed income and money market accounts.

Apartment deliveries are likely to remain high in a number of its markets in the near future. Aggressive rental concessions and moderate pricing power amid high supply are concerns.

- 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 edged down 0.7%, as against the industry's rise of 0.2%. Also, the trend in estimate revisions of 2019 FFO per share does not indicate a favorable outlook for the company. In fact, the Zacks Consensus Estimate for 2019 FFO per share witnessed marginal downward revision over the past two months. Therefore, given the above-mentioned concerns and downward estimate revisions, the stock has limited upside potential.

Last Earnings Report

AvalonBay's Q3 FFO Misses, Revenues Beat Estimates

Quarter Ending	09/2019
Report Date	Oct 28, 2019
Sales Surprise	0.30%
EPS Surprise	-0.43%
Quarterly EPS	2.34
Annual EPS (TTM)	9.22

AvalonBay Communities' third-quarter 2019 core FFO per share of $2.34 increased 2.6% year over year. However, the figure missed the Zacks Consensus Estimate by a penny.

This year-over-year growth indicates increase in average rental rates, while economic occupancy registered a decline.

Total revenues of $587.6 million were up 2% year over year. The revenue figure also surpassed the Zacks Consensus Estimate of $585.9 million.

Quarter in Detail

In the reported quarter, revenues from established communities improved 2.7% year over year to $461.2 million. Results reflect a 2.9% increase in average rental rates, while economic occupancy edged down 0.2%.

Operating expenses for established communities flared up 4.2% on a year-over-year basis. Consequently, NOI from established communities increased 2.1% year on year to around $327 million.

During the third quarter, the company acquired two communities — Portico at Silver Spring Metro, in Silver Spring, MD, comprising 151 apartment homes for $43.45 million and Avalon Bonterra, in Hialeah, FL, containing 314 apartment homes for $90 million.

The company sold four wholly-owned operating communities for $259.6 million, leading to a gain of $130.4 million in accordance with GAAP. These included AVA Stamford, in Stamford, CT; Archstone Lexington, in Flower Mound, TX; Memorial Heights Villages, in Houston, TX; and Avalon Orchards, in Marlborough, MA. With the sale of Archstone Lexington and Memorial Heights Villages, the company completed its exit from the Texas market.

Further, during the quarter, the company completed the development of AVA Esterra Park, in Redmond, WA, comprising 323 apartment homes, for a total capital cost of $91 million.

As of Sep 30, 2019, AvalonBay had 20 communities under construction (expected to contain in total 6,700 apartment homes and 94,000 square feet of retail space), which will likely be accomplished for a projected total capital cost of $2.5 billion.

Balance-Sheet Position

As of Sep 30, 2019, AvalonBay did not have any borrowings outstanding under its $1.75-billion unsecured credit facility. The company had around $334.75 million in unrestricted cash and cash in escrow as of the same date. In addition, the company's annualized net debt-to-core EBITDA for the July-September quarter was 4.7 times.

Recent News

Dividend Update

On Nov 20, AvalonBay's board of directors announced fourth-quarter 2019 dividend of $1.52 per share. This dividend is scheduled to be paid on Jan 15, to common stockholders of record as of Dec 31, 2019.

Valuation

AvalonBay's shares are up 15% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are up 17.4% and 12.9% over the past year.

The S&P 500 Index is up 24.7% over the past year.

The stock is currently trading at 21.26X forward 12-month FFO, which compares to 20.67X for the Zacks sub-industry, 14.95X for the Zacks sector and 19X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 24.19X and as low as 17.02X, with a 5-year median of 20.94X. Our neutral recommendation indicates that the stock will perform in line with the market. Our $222 price target reflects 22.53X 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	21.26	20.67	14.95	19
	5-Year High	24.19	21.89	16.21	19.34
	5-Year Low	17.02	16.2	12.01	15.17
	5-Year Median	20.94	18.54	13.98	17.44
P/S F12M	Current	11.94	10.28	6.53	3.52
	5-Year High	13.18	10.76	6.61	3.52
	5-Year Low	9.37	7.42	5.2	2.54
	5-Year Median	11.71	8.86	6.04	3
P/B TTM	Current	2.71	2.86	2.84	4.49
	5-Year High	2.87	3.09	2.89	4.49
	5-Year Low	2.05	2.06	1.83	2.85
	5-Year Median	2.47	2.38	2.5	3.61

As of 01/14/2020

Industry Analysis **Zacks Industry Rank:** Top 46% (116 out of 254)

Top Peers

Apartment Investment and Management Company **(AIV)**	Neutral
Camden Property Trust **(CPT)**	Neutral
Equity Residential **(EQR)**	Neutral
Essex Property Trust, Inc. **(ESS)**	Neutral
Investors Real Estate Trust **(IRET)**	Neutral
Mid-America Apartment Communities, Inc. **(MAA)**	Neutral
NexPoint Residential Trust, Inc. **(NXRT)**	Neutral
United Dominion Realty Trust, Inc. **(UDR)**	Neutral

Industry Comparison Industry: Reit And Equity Trust - Residential

Industry Peers

	AVB Neutral	X Industry	S&P 500	EQR Neutral	ESS Neutral	MAA Neutral
VGM Score	F	-	-	F	F	D
Market Cap	29.26 B	1.62 B	24.31 B	30.14 B	19.94 B	15.03 B
# of Analysts	9	4.5	13	11	10	8
Dividend Yield	2.90%	3.56%	1.76%	2.80%	2.58%	3.04%
Value Score	F	-	-	F	F	D
Cash/Price	0.01	0.03	0.04	0.00	0.00	0.00
EV/EBITDA	22.28	21.51	14.08	23.03	23.68	21.84
PEG Ratio	3.76	3.45	2.06	3.62	3.43	5.16
Price/Book (P/B)	2.71	2.44	3.33	2.91	3.11	2.41
Price/Cash Flow (P/CF)	17.70	17.58	13.62	19.93	23.46	21.16
P/E (F1)	21.29	18.84	18.86	22.41	21.47	20.11
Price/Sales (P/S)	13.28	6.91	2.65	11.29	13.87	9.27
Earnings Yield	4.70%	5.33%	5.27%	4.46%	4.66%	4.97%
Debt/Equity	0.69	0.92	0.72	0.87	0.94	0.72
Cash Flow ($/share)	11.83	2.27	6.94	4.07	12.86	6.23
Growth Score	D	-	-	D	C	C
Hist. EPS Growth (3-5 yrs)	4.40%	3.96%	10.56%	0.01%	9.23%	4.03%
Proj. EPS Growth (F1/F0)	5.64%	5.82%	7.52%	4.27%	5.33%	0.75%
Curr. Cash Flow Growth	10.46%	8.69%	14.88%	8.80%	-3.53%	-12.82%
Hist. Cash Flow Growth (3-5 yrs)	21.78%	21.31%	9.00%	17.96%	21.31%	26.71%
Current Ratio	0.89	1.04	1.23	0.13	1.59	0.08
Debt/Capital	40.95%	47.56%	42.99%	47.69%	48.69%	41.78%
Net Margin	45.56%	12.78%	11.14%	29.88%	29.78%	16.25%
Return on Equity	9.35%	4.39%	17.16%	7.73%	6.73%	3.84%
Sales/Assets	0.12	0.13	0.55	0.13	0.11	0.14
Proj. Sales Growth (F1/F0)	5.30%	6.40%	4.18%	3.34%	5.62%	3.84%
Momentum Score	D	-	-	D	D	D
Daily Price Chg	-0.72%	-0.01%	0.08%	-1.36%	-1.20%	-1.30%
1 Week Price Chg	-0.37%	0.17%	0.39%	0.57%	0.40%	0.98%
4 Week Price Chg	1.39%	2.31%	1.93%	1.31%	1.90%	2.90%
12 Week Price Chg	-5.55%	-1.57%	6.50%	-8.23%	-8.81%	-3.37%
52 Week Price Chg	16.53%	20.48%	22.56%	18.55%	19.49%	34.52%
20 Day Average Volume	575,252	400,799	1,571,506	1,475,072	363,254	457,636
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.02%	-0.02%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.00%	-0.28%	-0.02%
(F1) EPS Est 12 week change	0.29%	0.17%	-0.52%	0.63%	-0.79%	1.04%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	-0.48%	0.00%

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	F
Growth Score	D
Momentum Score	D
VGM Score	F

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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