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May 19, 2020

# Duke Realty Corp. (DRE)

**$32.45** (As of 05/18/20)

Price Target (6-12 Months): **$35.00**

| Long Term: 6-12 Months | **Zacks Recommendation:** | **Neutral** |
|---|---|---|
| | (Since: 02/03/19) | |
| | Prior Recommendation: Underperform | |
| Short Term: 1-3 Months | **Zacks Rank:** (1-5) | **3-Hold** |
| | Zacks Style Scores: | VGM:D |
| | Value: F \| Growth: D | Momentum: B |

## Summary

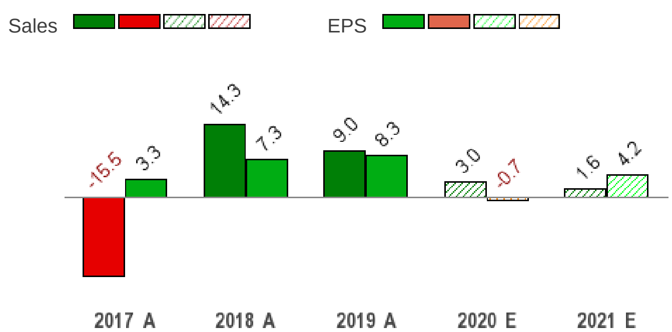
Duke Realty's lower-than-expected first-quarter results reflected a decline at its in-service portfolio leasing. Nonetheless, higher rents drove revenues during the quarter. Notably, the supply-chain disruption caused by the coronavirus pandemic is likely to increase demand for incremental inventory storage over the long term. Given Duke Realty's solid capacity to offer bulk distribution properties, the company is well poised to capitalize on this demand. Moreover, solid balance-sheet strength and ample liquidity enable it to pursue future growth endeavors. Shares of Duke Realty have outperformed its industry over the past year. However, demand for logistic properties and rent growth are expected to be affected amid a slowdown in the economy. The company has also suspended new speculative development starts.

## Price, Consensus & Surprise


## Data Overview

| | |
|---|---|
| 52 Week High-Low | **$38.88 - $25.19** |
| 20 Day Average Volume (sh) | **2,771,882** |
| Market Cap | **$12.0 B** |
| YTD Price Change | **-6.4%** |
| Beta | **0.66** |
| Dividend / Div Yld | **$0.94 / 2.9%** |
| Industry | [REIT and Equity Trust - Other] |
| Zacks Industry Rank | **Top 31% (78 out of 254)** |
| Last EPS Surprise | **-5.7%** |
| Last Sales Surprise | **0.2%** |
| EPS F1 Est- 4 week change | **-1.1%** |
| Expected Report Date | **07/29/2020** |
| Earnings ESP | **-1.1%** |
| P/E TTM | **22.5** |
| P/E F1 | **22.7** |
| PEG F1 | **5.1** |
| P/S TTM | **12.8** |

## Sales and EPS Growth Rates (Y/Y %)




## Sales Estimates (millions of $)

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|---|---|---|---|---|---|
| 2021 | 217 E | 218 E | 218 E | 219 E | 896 E |
| 2020 | 219 A | 220 E | 221 E | 222 E | 882 E |
| 2019 | 210 A | 213 A | 215 A | 217 A | 856 A |

## EPS Estimates

| | Q1 | Q2 | Q3 | Q4 | Annual* |
|---|---|---|---|---|---|
| 2021 | $0.35 E | $0.37 E | $0.38 E | $0.38 E | $1.49 E |
| 2020 | $0.33 A | $0.36 E | $0.37 E | $0.38 E | $1.43 E |
| 2019 | $0.33 A | $0.36 A | $0.37 A | $0.38 A | $1.44 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 05/18/2020. The reports text is as of 05/19/2020.

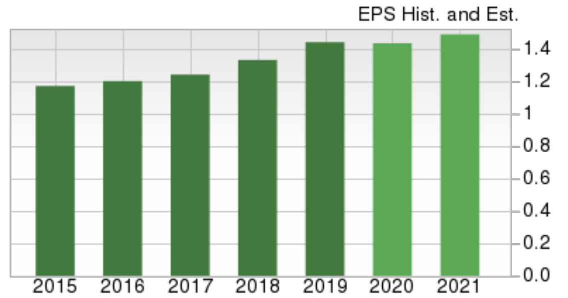
## Overview

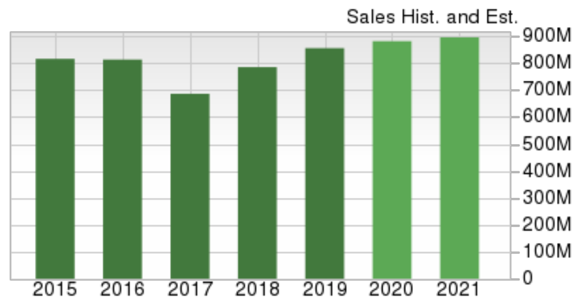
Headquartered in Indianapolis, IN, Duke Realty Corporation is a domestic pure-play industrial REIT in the United States, engaged in owning, managing and developing industrial properties across the nation. Its portfolio of industrial properties comprises about 156 million rentable square feet. These properties are located in 20 key logistic markets.

Particularly, as of Mar 31, 2020, Duke Realty enjoyed ownership of or jointly controlled 521 industrial properties. Of these, 500 properties with 146.4 million square feet were in service and 21 properties with 9.6 million square feet were under development.

Notably, Duke Realty opted for a series of asset sales in the past few years to shed medical and suburban office properties from its portfolio. These dispositions have helped the company simplify its business model and to turn into a leading domestic pure play industrial REIT. The company now focuses on building a superior portfolio of industrial properties through acquisitions and development, on a build-to-suit basis, in high-barrier markets with solid growth potential. In light of the economic uncertainty, the company has suspended new speculative development starts.

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 healthy industrial real estate market, Duke Realty's efforts to boost its ownership of strategically-located high-quality properties and decent balance-sheet position augur well for growth.

- Duke Realty has more than 45 years of experience in operation and development of industrial real estate. It focuses on having facilities in major MSA's and key trucking, rail, air cargo and shipping corridors. Such locations help generate solid demand from e-commerce and traditional distribution customers for its industrial properties. Moreover, in recent years, the company opted for a series of asset sales to complete the disposition of its medical office properties and residual suburban office properties. These dispositions have helped the company simplify its business model and turn it into a leading domestic pure-play industrial REIT.

- Amid an e-commerce boom, growth in industries and companies making efforts to improve supply chain efficiencies, demand for logistics infrastructure and efficient distribution networks has been increasing. This is helping the industrial real estate market to grow and given Duke Realty's solid capacity to offer modern, bulk distribution properties, the company remains well poised to capitalize on this trend. The company is making efforts to upgrade its portfolio on the back of development and acquisitions in high-barrier markets with solid growth potential. In fact, given the solid build-to-suit prospects, the company is focusing on these projects. Also, acquisition of properties totaled $217 million for 2019 and is expected to be up $100 million in 2020. Further, the company is making efforts to increase exposure in Tier 1 markets through disciplined capital-recycling efforts. In fact, 74% of the company's development pipeline is in coastal Tier 1 markets.

- With respect to tenants, the company has a big-box focus. This helps the company have higher credit quality tenants on its roster. Also, this leads to fewer overall tenants that the company needs to manage. Moreover, the supply-chain disruption caused by the coronavirus pandemic is likely to accelerate consumer adoption of e-commerce and increase demand for incremental inventory storage. Hence, with a decent portion of the company's tenant base being e-commerce oriented, Duke Realty is well positioned to capture growth opportunities from the e-commerce boom, even amid a slowing economy. Along with longer lease terms and lower rollover, the company has a low risk profile.

- Duke Realty enjoys a strong balance sheet, ample liquidity and easy access to capital. In a bid to manage the global uncertainties, resulting from the ongoing crisis, it borrowed $200 million on its unsecured line of credit in the first quarter. This boosted the company's cash position, providing ample liquidity to continue its operations uninterrupted, fund dividend payments and finance development pipeline. In fact, as of the first-quarter end, the company had around $1.2 billion in liquidity consisting of $188 million of cash in hand and $992 million available under its credit facility. Moreover, Duke Realty entered into a refinance transaction that enabled it to eliminate significant debt maturities until October 2022. With substantial financial flexibility, the company is well poised to capitalize on growth opportunities. Finally, the company enjoys investment-grade credit rating of BBB+ and Baa1 as well as a stable outlook from Standard & Poor's and Moody's, respectively.

- Solid dividend payouts remain arguably the biggest attraction for REIT investors and Duke Realty has raised its regular common dividend rate by 9.3% to 23.50 cents for its third-quarter 2019 dividend. Previously, the company raised dividend payouts by 7.5%, 5.3%, 5.6% and 5.9% fourth-quarter 2018, 2017, 2016 and 2015 respectively. Furthermore, during the fourth-quarter of 2017, the company paid 85 cents as special dividends. Given its financial strength and lower dividend payout (as compared to its industry), the company's dividend distribution is expected to be sustainable.

## Reasons To Sell:

Declining demand for logistic properties amid an economic slowdown will suppress the near-term rent growth. Moreover, near-term lease concessions and rent collections are concerns for Duke Realty.

- Recovery in the industrial market has continued for long, and hence growth in rent is expected to slow down in the days to come. Additionally, amid a slowdown in the economy, demand for logistic properties is expected to decline, further suppressing the near-term rent growth. Moreover, near-term lease concessions and rent collections are a concern. Although the company has substantially collected its March and April rents, rent relief and deferrals will likely be a concern, specifically for the company's smaller tenants that are severely impacted by the virus outbreak.

- Duke Realty has been enhancing its portfolio mix through continued divestitures. The company opted for a series of asset sales in 2017 to complete the disposition of nearly all of its medical office properties. Furthermore, the company sold almost all of its residual suburban office properties during the same year. Also, for 2019 and first-quarter 2020, property dispositions aggregated $494 million and 27 million, respectively. Further, the company anticipates dispositions of non-strategic properties of $125-$250 million for 2020. While such efforts are a strategic fit for the long term, the near-term dilutive effect cannot be bypassed. In fact, such short-term impact tends to drag the company's quarterly results and weigh on its profitability.

- Although Duke Realty's large development pipeline is encouraging for its future growth, it increases operational risks by exposing it to rising construction costs, entitlement delays and lease-up risks. Although, in recent quarters, the company enhanced the amount of speculative development in its portfolio, in light of the economic uncertainty, it has suspended new speculative development starts. Nonetheless, the company has a solid pipeline of potential build-to-suit projects. Particularly, the company's overall development pipeline at the end of first-quarter 2020 consisted of 9.7 million square feet of space under construction, at projected stabilized cost of $1.1 billion. These projects are 61% pre-leased.

- In the past year, shares of Duke Realty have gained 7.2% compared with the industry's decline of 12%. However, the trend in estimate revision of 2020 FFO per share does not indicate a favorable outlook for the company, given the marginal downward revision over the past month. Therefore, given the above-mentioned concerns and downward estimate revisions, the stock has limited upside potential.

## Last Earnings Report

**Duke Realty Q1 FFO Misses Estimates, Revenues Beat**

| Quarter Ending | 03/2020 |
|---|---|
| Report Date | Apr 29, 2020 |
| Sales Surprise | 0.15% |
| EPS Surprise | -5.71% |
| Quarterly EPS | 0.33 |
| Annual EPS (TTM) | 1.44 |

Duke Realty's first-quarter 2020 core FFO per share of 33 cents missed the Zacks Consensus Estimate of 35 cents. Nonetheless, the reported tally remained unchanged from the year-ago quarter.

In light of the coronavirus pandemic and the resultant economic disruptions, the company has revised its 2020 guidance. Further, amid the pandemic, Duke Realty had to increase collectability reserves for straight line receivables by $5 million and this impacted its core FFO per share by more than 1 cent. Nonetheless, decent leasing activities, and strong rent growth on new and renewal leases drove the company's same-property net operating income (NOI).

Rental and related revenues of $218.76 million increased 4.2% on a year-over-year basis. Also, the figure surpassed the Zacks Consensus Estimate of $218.43 million.

**Quarter in Detail**

Duke Realty leased 4 million square feet of space during the March-end quarter. Tenant retention was 68.3%. Moreover, the company registered same-property NOI growth of 6.6% year over year. In fact, Duke Realty reported overall cash and annualized net effective rent growth on new and renewal leases of 17.1% and 32.7%, respectively, in the quarter.

As of Mar 31, 2020, the company's total portfolio, including properties under development, was 94.3% leased, unchanged from the prior quarter end, and up 130 basis points (bps) from the prior-year end. In-service portfolio was 97.2% leased as of Mar 31, 2020, down from 97.8% leased on Dec 31, 2019, and from 98.4% on Mar 31, 2019.

Notably, during the first quarter, the company started two development projects, aggregating 991,000 square feet, with estimated costs of $96 million. Its building dispositions totaled $27 million in the first quarter.

Duke Realty exited first-quarter 2020 with $187.6 million of cash and cash equivalents, up from $110.9 million as of Dec 31, 2019.

**2020 Guidance**

Duke Realty revised its 2020 core FFO per share outlook to $1.41-$1.51 from the prior mentioned $1.48-$1.54.

The company estimates same-property NOI growth of 1.75-3.25%. The guidance for acquisitions of properties is upto $100 million. The projection for building dispositions is $125-$250 million. However, the company has ceased new speculative development starts and expects rent growth to diminish.

## Recent News

**Duke Realty Bags 800,218-Sf Leases for Logistics Building – May 14, 2020**

Duke Realty inked a long-term lease for an entire 800,218-square-foot logistics building that is currently under construction in the Inland East submarket of Southern California.

The speculative development at 4501 Patterson is situated in Perris, on the southeast corner of Patterson Avenue and Markham Street. It is being constructed on a 37.3-acre site and will be delivered in September 2020.

Per management, the growing preference of the Inland Empire East submarket for large blocks of modern distribution space is due to the region's easy access to the I-215, I-10 and other major highways and interstates.

**Dividend Update**

Concurrent with its first-quarter 2020 earnings release on Apr 29, 2020, Duke Realty announced quarterly cash dividend on common stock of 23.50 cents per share. The dividend for the first quarter will be paid out on May 29 to shareholders on record as of May 14.

## Valuation

Duke Realty's shares have been up 7.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector declined 12% and 18.9%, over the past year, respectively.

The S&P 500 Index is up 3.9% over the past year.

The stock is currently trading at 22.31X forward 12-month FFO, which compares with the 16.93X for the Zacks sub-industry, 15.4X for the Zacks sector and 21.52X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 25.45X and as low as 14.43X, with a 5-year median of 21.14X. Our neutral recommendation indicates that the stock will perform in line with the market. Our $35 price target reflects 23.95X FFO.

The table below shows summary valuation data for DRE.

**Valuation Multiples - DRE**

| | | Stock | Sub-Industry | Sector | S&P 500 |
|---|---|---|---|---|---|
| P/E F12M | Current | 22.31 | 16.93 | 15.40 | 21.52 |
| | 5-Year High | 25.45 | 18.10 | 16.18 | 21.52 |
| | 5-Year Low | 14.43 | 14.32 | 11.58 | 15.23 |
| | 5-Year Median | 21.14 | 16.08 | 13.94 | 17.49 |
| P/S F12M | Current | 13.48 | 7.39 | 5.81 | 3.34 |
| | 5-Year High | 15.83 | 8.14 | 6.70 | 3.44 |
| | 5-Year Low | 7.03 | 5.91 | 4.99 | 2.53 |
| | 5-Year Median | 12.18 | 6.88 | 6.05 | 3.01 |
| P/B TTM | Current | 2.38 | 2.11 | 2.36 | 4.03 |
| | 5-Year High | 2.98 | 3.01 | 2.90 | 4.56 |
| | 5-Year Low | 1.85 | 1.80 | 1.71 | 2.83 |
| | 5-Year Median | 2.29 | 2.51 | 2.53 | 3.65 |

As of 05/18/2020

## Industry Analysis **Zacks Industry Rank:** Top 31% (78 out of 254)


## Top Peers

| Company (Ticker) | Rec | Rank |
|---|---|---|
| Americold Realty Trust **(COLD)** | Neutral | 3 |
| EastGroup Properties, Inc. **(EGP)** | Neutral | 3 |
| First Industrial Realty Trust, Inc. **(FR)** | Neutral | 3 |
| Prologis, Inc. **(PLD)** | Neutral | 3 |
| PS Business Parks, Inc. **(PSB)** | Neutral | 3 |
| Rexford Industrial Realty, Inc. **(REXR)** | Neutral | 3 |
| Stag Industrial, Inc. **(STAG)** | Neutral | 3 |
| Terreno Realty Corporation **(TRNO)** | Neutral | 3 |

## Industry Comparison Industry: Reit And Equity Trust - Other

Industry Peers

| | DRE | X Industry | S&P 500 | EGP | FR | PLD |
|---|---|---|---|---|---|---|
| **Zacks Recommendation (Long Term)** | Neutral | - | - | Neutral | Neutral | Neutral |
| **Zacks Rank (Short Term)** | 3 | - | - | 3 | 3 | 3 |
| **VGM Score** | D | - | - | D | D | C |
| Market Cap | 11.95 B | 1.79 B | 20.09 B | 4.07 B | 4.61 B | 64.13 B |
| # of Analysts | 6 | 4 | 14 | 8 | 8 | 9 |
| Dividend Yield | 2.90% | 4.74% | 2.1% | 2.88% | 2.76% | 2.67% |
| **Value Score** | F | - | - | D | F | F |
| Cash/Price | 0.02 | 0.08 | 0.07 | 0.00 | 0.03 | 0.01 |
| EV/EBITDA | 17.25 | 13.32 | 12.13 | 20.26 | 14.87 | 25.72 |
| PEG Ratio | 5.06 | 3.48 | 2.72 | 4.90 | NA | 3.39 |
| Price/Book (P/B) | 2.38 | 1.14 | 2.75 | 3.41 | 2.57 | 1.75 |
| Price/Cash Flow (P/CF) | 15.65 | 9.46 | 10.86 | 17.92 | 12.47 | 20.85 |
| P/E (F1) | 22.71 | 13.45 | 20.10 | 20.12 | 20.38 | 24.16 |
| Price/Sales (P/S) | 12.78 | 4.21 | 2.05 | 11.93 | 10.68 | 18.13 |
| Earnings Yield | 4.41% | 7.22% | 4.77% | 4.97% | 4.91% | 4.13% |
| Debt/Equity | 0.63 | 0.92 | 0.76 | 1.05 | 0.92 | 0.43 |
| Cash Flow ($/share) | 2.07 | 2.03 | 7.01 | 5.82 | 2.91 | 4.17 |
| **Growth Score** | D | - | - | C | C | B |
| Hist. EPS Growth (3-5 yrs) | 4.84% | 2.02% | 10.87% | 7.77% | 5.83% | 10.27% |
| Proj. EPS Growth (F1/F0) | -0.47% | -2.83% | -10.31% | 3.97% | 2.22% | 8.56% |
| Curr. Cash Flow Growth | 9.22% | 3.36% | 5.51% | 25.62% | 28.05% | 3.51% |
| Hist. Cash Flow Growth (3-5 yrs) | 4.21% | 12.74% | 8.55% | 13.87% | 19.83% | 15.92% |
| Current Ratio | 1.97 | 1.74 | 1.28 | 0.01 | 1.64 | 0.91 |
| Debt/Capital | 38.50% | 48.38% | 44.46% | 51.19% | 47.87% | 29.89% |
| Net Margin | 43.19% | 12.85% | 10.59% | 35.88% | 59.20% | 48.50% |
| Return on Equity | 8.14% | 3.94% | 16.29% | 10.83% | 14.63% | 6.00% |
| Sales/Assets | 0.11 | 0.13 | 0.55 | 0.14 | 0.13 | 0.08 |
| Proj. Sales Growth (F1/F0) | 3.02% | 0.00% | -2.49% | 7.36% | 2.34% | 27.15% |
| **Momentum Score** | B | - | - | C | B | B |
| Daily Price Chg | 5.25% | 7.77% | 5.21% | 6.13% | 6.68% | 4.26% |
| 1 Week Price Chg | -9.11% | -10.78% | -4.56% | -10.69% | -7.71% | -7.44% |
| 4 Week Price Chg | -3.88% | 0.46% | 4.12% | 0.06% | 4.11% | -1.89% |
| 12 Week Price Chg | -13.97% | -31.00% | -16.39% | -25.34% | -18.34% | -9.53% |
| 52 Week Price Chg | 7.20% | -25.06% | -5.84% | -7.34% | 5.22% | 14.87% |
| 20 Day Average Volume | 2,771,882 | 813,214 | 2,651,378 | 305,087 | 1,258,240 | 3,204,665 |
| (F1) EPS Est 1 week change | -0.66% | 0.00% | 0.00% | -0.19% | 0.00% | 0.00% |
| (F1) EPS Est 4 week change | -1.15% | -1.74% | -4.48% | 0.63% | -0.54% | -0.70% |
| (F1) EPS Est 12 week change | -5.26% | -5.31% | -16.39% | -2.20% | -2.67% | -3.25% |
| (Q1) EPS Est Mthly Chg | -1.09% | -2.78% | -9.90% | -0.65% | -2.00% | -1.00% |

## 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 | B |
| 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

**This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock.The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page.** Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

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ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.