

Highwoods Properties (HIW)

\$37.51 (As of 08/18/20)

Price Target (6-12 Months): **\$40.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/07/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: C

Growth: C

Momentum: A

Summary

Highwoods has collected 99% of its second-quarter and July contractually-required rents amid the coronavirus crisis. Notably, its portfolio in higher-growth markets of the Sun Belt-region is benefiting from decent demand and rent growth. Furthermore, the company reported better-than-expected second-quarter results on growth in occupancy and same-property cash NOI. Moreover, a strong balance-sheet position enables Highwoods to pursue its growth endeavors. However, speculative new leasing is likely to be slow, while uncertainties with rent collections might prevail amid the pandemic. Furthermore, asset dispositions are expected to affect revenues in the near term, while an extensive development pipeline exposes it to operational risks. Moreover, shares of the company have underperformed the industry it belongs to over the past year.

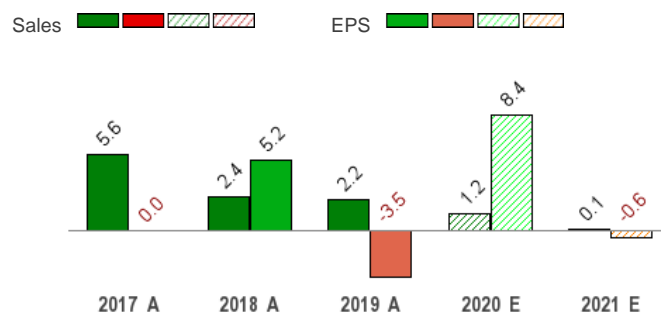
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$52.76 - \$25.10
20 Day Average Volume (sh)	656,088
Market Cap	\$3.9 B
YTD Price Change	-23.3%
Beta	0.98
Dividend / Div Yld	\$1.92 / 5.1%
Industry	<u>REIT and Equity Trust - Other</u>
Zacks Industry Rank	Bottom 15% (214 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.5%
Last Sales Surprise	-1.0%
EPS F1 Est- 4 week change	0.7%
Expected Report Date	10/27/2020
Earnings ESP	-0.4%
P/E TTM	10.3
P/E F1	10.4
PEG F1	2.6
P/S TTM	5.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	190 E	192 E	194 E	198 E	746 E
2020	193 A	183 A	184 E	183 E	745 E
2019	172 A	184 A	187 A	192 A	736 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.88 E	\$0.90 E	\$0.89 E	\$0.91 E	\$3.59 E
2020	\$0.93 A	\$0.93 A	\$0.88 E	\$0.89 E	\$3.61 E
2019	\$0.72 A	\$0.87 A	\$0.88 A	\$0.91 A	\$3.33 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 08/18/2020. The reports text is as of 08/19/2020.

Overview

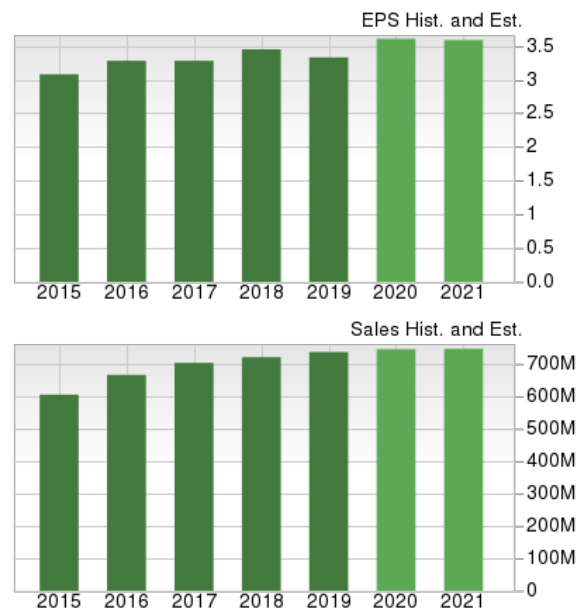
Raleigh, NC-based Highwoods Properties, Inc. is an office real estate investment trust (REIT) that owns, develops, acquires, leases and manages office properties. Its core portfolio consists of properties in the best business districts (BBDs) of Atlanta, Charlotte, Nashville, Orlando, Pittsburgh, Raleigh, Richmond and Tampa.

The company's long-term strategic plan entails acquisition of high-quality, trophy office buildings in the BBDs of markets that enjoy favorable economic and demographic trends. In August 2019, Highwoods announced a market-rotation plan, per which it aims to fortify its BBD office focus, and exit Greensboro and Memphis, through a two-phased planned departure.

In November 2019, the company entered the Charlotte market through the acquisition of Bank of America Tower. Further, in December, it announced \$89.6 million of office properties sale in Memphis and in January 2020, the company announced \$233.4 million worth of asset sales in Greensboro. Moreover, in March, the company announced sale of four office buildings comprising 599,000 square feet in the Poplar corridor submarket of Memphis. The move marked the closing of the first phase of its market-rotation plan and it finally included selling a select portfolio of assets in Greensboro and Memphis, for a total price of \$428 million since its initial announcement of this two-pronged strategy last August. The rest of the assets will be sold in the second phase, which has no pre-planned schedule.

As of Jun 30, 2020, Highwoods had ownership or interest in 28.1 million rentable square feet of in-service assets as well as 1.2 million rentable square feet of office properties under development. The company also owned 225 acres of development land as of the same date.

Note: All EPS numbers presented in this report represent 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:

- ▲ Highwoods provides comprehensive real estate services to customers and third parties through a fully-integrated platform. The company has a well-diversified tenant base that includes several bellwethers. Its average in-place rent witnessed a CAGR of 3.8% over the past seven years. This trend continued in the first half of 2020 as well. Further, a large part of its portfolio is concentrated in high-growth Sun Belt markets, which have long-term favorable demographic trends and are expected to continue experiencing above-average job growth. This bodes well for Highwoods' long-term growth. Also, despite the coronavirus crisis, the company has collected 99% of its contractually required rents for the second quarter and July.
- ▲ Much of the leasing proportion has shifted from new to renewal oriented deals due to the pandemic. Going forward, the next cycle of office-space demand will likely be driven by de-densification to allow higher square footage per office worker and the need for better-amenitized office properties to focus on health & wellness amid social-distancing requirements. Moreover, tenant downsizing is less likely and this will improve tenant retention. Hence, Highwoods is well-positioned to benefit from the emerging trend, given the demand for office space in the Sunbelt region that is benefiting from favorable demographic trends. In fact, the company enjoyed solid renewal activity, with favorable economics during the second quarter.
- ▲ Highwoods has been making concerted efforts to expand its footprint in high-growth markets and improve portfolio quality. In addition, the company is following a disciplined capital-recycling strategy that entails disposing of non-core assets and investing the proceeds in premium asset acquisitions and for undertaking accretive development projects. In sync with this strategy, in August 2019, Highwoods announced a market-rotation plan, per which it aims to fortify its BBD office focus, and exit Greensboro and Memphis markets, through a two-phased planned departure. In fact, in November, it entered the Charlotte market through the acquisition of Bank of America Tower. Moreover, after announcing asset sales in Memphis and Greensboro in December and January, the company announced sale of four office buildings comprising 599,000 square feet in the Poplar corridor submarket of Memphis in March. The move marked the closing of the first phase of its market-rotation plan. The rest of the assets in Greensboro and Memphis will be sold in the second phase, which has no schedule as of now. The company is also focused on development efforts in key markets. Management projects these developments to generate more than \$40 million of annual net operating income (NOI) upon completion and stabilization, and nearly \$5 million of NOI in 2020.
- ▲ Highwoods has adequate liquidity from cash in hand, cash flows from operating activities and other financing sources to meet short-term liquidity needs. In fact, as of Jul 21, the company had \$6 million of existing cash and full availability under its \$600-million revolving credit facility. Further, it is trying to lower its leverage that stood at 36.8% as of the second-quarter end. The company has no debt maturities to address until June 2021. Moreover, it generates 96.8% unencumbered NOI, providing scope for tapping additional secured debt capital if required. Highwoods maintains investment-grade ratings of BBB/Baa2, with stable outlook from S&P and Moody's. Hence, a robust balance sheet, declining debt-to-capital ratio and strategic capital raises position Highwoods to adequately fund its development pipeline and capitalize on growth opportunities.
- ▲ In addition, dividend payouts are arguably the biggest enticement for REIT investors and Highwoods has consistently increased its dividend rate. In February 2020, the company increased its quarterly cash dividend to 48 cents per share, resulting in an annualized dividend of \$1.92 per share. This marked a 1.1% increase over the prior quarter's dividend. Notably, the company's dividend has increased at a CAGR of 3% over the past five years. Given its lower dividend payout (as compared to its industry), the company's dividend distribution is expected to be sustainable.
- ▲ Shares of Highwoods have underperformed the industry it belongs to over the past year. However, the trend in estimate revisions of 2020 FFO per share indicate a favorable outlook for the company as the Zacks Consensus Estimate moved marginally upward over the past week. Therefore, given the progress in fundamentals and upward estimate revisions, the stock has decent upside potential in the near term.

Highwoods' diversified real estate portfolio, efforts to expand in high-growth markets, non-core assets sale and investing the proceeds for further expansion bode well for long term growth.

Reasons To Sell:

- ▼ The coronavirus pandemic has led to an uncertain economic environment. In such a scenario, reduced office space utilization and rental payment collections have become uncertain, and landlords are offering tenant lease incentives and concessions. Amid this, the company will likely face headwinds like slowdown in new leasing activities and rent deferrals. In fact, temporary rent deferrals affected second-quarter same property cash NOI by \$4.5 million. Moreover, management expects the company to witness slow speculative new leasing, impacting rental revenues.
- ▼ Highwoods faces intense competition from developers, owners and operators of office properties as well as other commercial real estates, including sublease space available from its tenants. This restricts its ability to attract and retain tenants at relatively higher rents than its competitors and hinders its leasing activity. It also impacts the company's ability to acquire properties at favorable prices. Further, higher development activities across the company's markets will likely result in new supply in the upcoming periods. This will likely impact the occupancy levels of its office properties.
- ▼ The company also has an extensive development pipeline worth \$503 million, which is 77% pre-leased. Although this is encouraging in the long run, it exposes the company to various operational risks such as construction cost overruns. In addition, the company is shedding non-core assets to enhance its portfolio mix. In the first quarter, the company completed the first phase of its market-rotation plan, selling 3.6 million square feet of assets in Greensboro and Memphis for \$338.4 million. Moreover, in July, it disposed of two non-core office buildings in Memphis for \$23.3 million. While dispositions are a strategic fit for long-term growth, the near-term dilutive impact on earnings, lower revenues and NOI due to lost revenues from property sales cannot be avoided.
- ▼ The company's assets are mainly concentrated in Atlanta, Nashville, Raleigh, and Tampa. As of Jun 30, 2020, contributions from the markets to the company's annualized cash revenues were 20.1%, 19.4%, 17.6% and 13.6%, respectively. Hence, any economic or political downturn in these markets might affect Highwoods' performance.

Near-term revenue loss on account of large-scale asset dispositions is a concern for Highwoods. Further, an extensive development pipeline exposes the company to higher development costs.

Last Earnings Report

Highwoods Beats on Q2 FFO, Collects 99% July Rents

Highwoods' second-quarter 2020 FFO per share of 93 cents surpassed the Zacks Consensus Estimate of 89 cents. The figure also improved 7% from the 87 cents reported in the year-ago period.

Rental and other revenues of \$183.2 million in the quarter decreased marginally year over year. Moreover, the reported figure missed the Zacks Consensus Estimate of \$185 million.

With regard to its rental receipts for July and for the second quarter, management announced that it has collected 99% of the contractually-required rents, with rent deferrals granted to tenants, representing 1.2% of its annualized rental revenues.

Quarter in Detail

Highwoods leased 821,000 square feet of second-generation office space during the second quarter, including 91,000 square feet of new leases and 48,000 square feet of expansion leases. Rents were up 5.5% on a cash basis.

At the end of the second quarter, total in-service portfolio occupancy was 91.1%, improving 20 basis points sequentially.

Same-property cash NOI increased 2.4% year over year, excluding the impact of temporary rent deferral agreements.

As of Jun 30, 2020, Highwoods had \$4.7 million of cash and cash-equivalents compared with \$9.5 million reported as of Dec 31, 2019. The company exited the reported quarter with about \$586 million availability of funds under its \$600-million revolving credit facility, scheduled to mature in January 2022, and a net debt-to-adjusted EBITDA ratio of 4.90. The company has no debt maturities in the next 12 months.

Guidance

Highwoods revised the current year FFO per share guidance to \$3.59-\$3.68 from \$3.55-\$3.68 guided earlier.

The company updated the pandemic's impact on some assumptions. It expects a decline in parking and parking-related revenues to impact 2020 FFO per share by 5-9 cents. Moreover, a decline in rental revenues for the remainder of 2020 will impact full-year FFO per share by 2-4 cents. Highwoods also expects lost rental revenues from customers experiencing financial difficulties due to bankruptcies or default as well as non-cash credit losses of straight line receivables.

Same-property cash NOI is projected to be 1-2% for 2020, while year-end occupancy is projected to be 89-91%. Dispositions in 2020 (excluding the completed phase-one dispositions under the market rotation plan) are estimated to be \$95-\$150 million, while acquisitions are likely to be up to \$200 million.

Quarter Ending **06/2020**

Report Date	Jul 28, 2020
Sales Surprise	-0.99%
EPS Surprise	4.49%
Quarterly EPS	0.93
Annual EPS (TTM)	3.65

Recent News

Highwoods Properties Collects 99% of June Rental Receipts – Jul 1, 2020

Highwoods Properties announced that it has collected 99% of its June contractually required rents, maintaining the same level of collection with that of May and April.

The company has approved the temporary rent deferrals to its tenants, representing 1.2% of the annual rental revenues so far this year. This includes the rent deferrals reported by the company in the Apr 28 first-quarter earnings release and Jun 20 business update. The company also reported that all of its building and parking facilities have remained open for operations.

Additionally, Highwoods informed it has signed a long-term, full-building lease renewal agreement for 138,000 square foot of space with the Federal Bureau of Investigation (FBI) in Tampa, FL. This was the company's largest lease expiration remaining in 2020. It had developed the FBI's Tampa Field office as a build-to-suit in 2005.

Highwoods has also announced some non-core property dispositions. The company sold two office buildings, Centrum and Colonnade, in Memphis for \$23.3 million. The properties comprise 169,000 square feet of space in total and 89% occupied. The company is likely to record non-FFO gains of \$9.6 million in third-quarter 2020 from these sales.

Dividend Update

On Jul 28, Highwoods announced its second-quarter cash dividend of 48 cents per share, resulting in an annualized payout of \$1.92 per share. The quarterly dividend will be paid out on Sep 9 to its shareholders of record as of Aug 17, 2020.

Valuation

Highwoods' shares have been down 14.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector have declined 6.5% and 6.3% in the past year, respectively.

The S&P 500 Index is up 16.7% in the past year.

The stock is currently trading at 10.44X forward 12-month FFO, which compares to 19.40X for the Zacks sub-industry, 16.64X for the Zacks sector and 22.86X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 16.47X and as low as 7.70X, with a 5-year median of 13.56X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$40 price target reflects 11.13X FFO per share.

The table below shows summary valuation data for HIW.

Valuation Multiples - HIW					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.44	19.4	16.64	22.86
	5-Year High	16.47	19.4	16.64	22.86
	5-Year Low	7.70	14.32	11.6	15.25
	5-Year Median	13.56	16.11	14.26	17.58
P/S F12M	Current	5.21	8.4	6.22	3.71
	5-Year High	7.88	8.4	6.67	3.71
	5-Year Low	3.76	5.97	4.97	2.53
	5-Year Median	6.51	7	6.06	3.05
P/B TTM	Current	1.69	2.47	2.48	4.54
	5-Year High	2.87	3.03	2.91	4.56
	5-Year Low	1.36	1.81	1.72	2.83
	5-Year Median	2.3	2.51	2.53	3.75

As of 08/18/2020

Industry Analysis Zacks Industry Rank: Bottom 15% (214 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Alexandria Real Estate Equities, Inc. (ARE)	Neutral	3
Cousins Properties Incorporated (CUZ)	Neutral	2
Douglas Emmett, Inc. (DEI)	Neutral	4
Kilroy Realty Corporation (KRC)	Neutral	3
Piedmont Office Realty Trust, Inc. (PDM)	Neutral	3
SL Green Realty Corporation (SLG)	Neutral	3
Boston Properties, Inc. (BXP)	Underperform	5
Hudson Pacific Properties, Inc. (HPP)	Underperform	5

Industry Comparison Industry: Reit And Equity Trust - Other				Industry Peers		
	HIW	X Industry	S&P 500	ARE	BXP	SLG
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	5	3
VGM Score	B	-	-	F	D	C
Market Cap	3.90 B	1.97 B	23.71 B	21.91 B	13.33 B	3.44 B
# of Analysts	8	4	14	3	9	8
Dividend Yield	5.12%	3.88%	1.63%	2.44%	4.58%	7.54%
Value Score	C	-	-	D	D	B
Cash/Price	0.00	0.06	0.07	0.01	0.15	0.32
EV/EBITDA	13.00	14.09	13.45	26.60	14.09	12.82
PEG Ratio	2.55	3.98	3.01	4.76	5.10	5.11
Price/Book (P/B)	1.69	1.32	3.18	1.98	1.59	0.67
Price/Cash Flow (P/CF)	9.94	10.87	12.70	24.14	11.02	6.78
P/E (F1)	10.24	15.49	21.98	23.77	12.48	6.84
Price/Sales (P/S)	5.16	4.81	2.46	13.08	4.58	2.89
Earnings Yield	9.62%	5.89%	4.33%	4.21%	8.01%	14.62%
Debt/Equity	1.01	0.92	0.76	0.68	1.56	1.17
Cash Flow (\$/share)	3.77	2.05	6.94	7.20	7.77	6.92
Growth Score	C	-	-	C	C	C
Hist. EPS Growth (3-5 yrs)	2.55%	0.73%	10.44%	7.69%	5.50%	-0.94%
Proj. EPS Growth (F1/F0)	8.33%	-2.05%	-5.97%	5.03%	-2.16%	-2.02%
Curr. Cash Flow Growth	-1.95%	3.36%	5.22%	4.79%	-2.18%	3.22%
Hist. Cash Flow Growth (3-5 yrs)	4.75%	12.74%	8.52%	23.85%	2.31%	-0.78%
Current Ratio	1.07	1.62	1.33	0.19	7.67	6.70
Debt/Capital	51.11%	48.09%	44.50%	40.53%	60.42%	52.02%
Net Margin	41.15%	10.49%	10.13%	24.09%	35.18%	19.90%
Return on Equity	13.93%	3.32%	14.59%	3.94%	12.72%	4.21%
Sales/Assets	0.15	0.13	0.51	0.09	0.13	0.09
Proj. Sales Growth (F1/F0)	1.20%	0.00%	-1.54%	15.94%	-2.16%	-17.52%
Momentum Score	A	-	-	F	C	B
Daily Price Chg	-2.04%	-0.93%	-0.41%	0.20%	-0.73%	0.09%
1 Week Price Chg	-4.54%	-0.94%	1.09%	-3.09%	-4.01%	-2.55%
4 Week Price Chg	2.85%	3.58%	3.41%	4.84%	-6.46%	-2.11%
12 Week Price Chg	0.81%	4.19%	9.80%	15.44%	1.31%	13.74%
52 Week Price Chg	-14.24%	-21.15%	3.43%	17.53%	-32.89%	-39.78%
20 Day Average Volume	656,088	625,710	1,894,669	648,971	1,338,990	1,215,394
(F1) EPS Est 1 week change	0.05%	0.00%	0.00%	0.00%	-1.94%	0.00%
(F1) EPS Est 4 week change	0.70%	0.00%	1.86%	-0.09%	-3.82%	0.82%
(F1) EPS Est 12 week change	0.80%	-0.22%	2.86%	0.14%	-5.15%	1.05%
(Q1) EPS Est Mthly Chg	1.68%	0.00%	0.80%	-0.09%	-3.99%	-1.56%

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	C
Growth Score	C
Momentum Score	A
VGM Score	B

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.

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