Safehold Inc. *(Holding)*

Date of Report: Nov. 18, 2020 P/E Ratio for SAFE: 59.30

Stock: Safehold Inc. (SAFE) EPS for SAFE: 1.13

Sector: Real Estate Current Price: $66.82 | Price Target: $70.26

Recommendation: **HOLD**

Company Summary:

Safehold Inc. is focused on ground leases, so the company owns the land and then a tenant signs a lease so they can build on this land. They specialize in making this process more efficient. This has created a capital advantage for their customers and gives the ability to gain larger returns for both parties. Their business model has added in risk aversion to account for tougher economic times. Ground leases face less defaults on payments and the lease terms are much longer than typical leases (50-100 years). Their focus is on high quality multifamily (duplexes and apartments), office, industrial, hospitality, and mixed-use properties. However, a ground lease can work with any property type, so they have a lot of options and potential growth. The company's typical transaction ranges from $15-$500 million and their cap rate range is as low as 3.25%-4.25%. Safehold handles properties across the united states in big cities and has entered 9 new markets in 2019. There has been a strong amount of insider buying and it has outperformed the S&P 500 by 52% over the past 12 months. They have received 100% of their ground rent in quarter 3 of 2020 and have grown revenue by 81% and total shareholder return by 64%.

Industry Outlook Summary:

With some extensive research through IBISWorld, we gathered that the four major external drivers in the REIT industry are *revenue*, *rental vacancy rates*, *per capita disposable income* and *corporate profit*. Beginning with rental vacancy rates, these rates reflect the percentage of US rental properties that are without tenants. The vacancy rate is indicative of rental demand, as higher vacancy rates generally indicate that demand for rentals is low, while demand for housing is high. Rental vacancy rates are anticipated to increase in 2020, posing a potential threat to the industry. Secondly, per capita disposable income is defined as personal income minus current personal taxes. Consumer confidence and disposable income levels largely determine retail spending trends. As disposable income declines, consumers cut back on retail spending. A decline in retail spending decreases demand for retail space as companies cut costs or exit their respective industries. Per capita disposable income is expected to decrease in 2020. Lastly, another major factor contributing to the industries outlook for REIT's is corporate profit. Corporate profit influences businesses' demand for rental space. Contracts for office rental space and other commercial purposes normally span many years and depend on the performance of the businesses seeking to rent space. As corporate profit increases, demand for rental space rises. Corporate profit is expected to decline in 2020. *(source: IBISWorld)*

Industry Outlook COVID – 19 Summary:

The sharp decline in consumer activity among retail, lodging and other properties due to the COVID-19 (coronavirus) pandemic has caused severe rent shortfalls for REITs. According to the National Association of REITS (NAREIT), retail REITs surveyed in April 2020 noted only collecting 70.0% of rents due. Moreover, the continuing severity of the crisis threatens to worsen commercial rent collection throughout 2020. Conversely, the industry mostly performed well prior to 2020. Rising capital markets, low interest rates and robust property values have been major contributors to the industry's growth during the period. Nevertheless, the shock of the coronavirus pandemic is expected to drag down the industry's growth. As a result, industry revenue has declined at an annualized rate of 2.7% to $181.8 billion over the five years to 2020, including a decline of 15.1% in 2020 alone as REITs struggle to collect rent amongst struggling businesses. Moreover, the industry average profit margin, measured as earnings before interest and taxes, has declined during the period, accounting for 20.8% of revenue in 2020. *(source: IBISWorld)*

Cash Flow History and Forecasts:

Safehold Inc. (SAFE)								
Current Position: Holding	Historical				Forecast			
	2016	2017	2018	2019	2020	2021	2022	2023
Total Revenue	$ 21,743	$ 23,234	$ 48,200	$ 93,396	$ 154,278	$ 228,297	$ 337,830	$ 499,913
Cost of Revenue	$ 861	$ 1,471	$ 1,600	$ 2,673	$ 4,010	$ 5,455	$ 7,420	$ 10,093
Gross Profit	$ 20,882	$ 21,763	$ 46,600	$ 90,723	$ 150,268	$ 222,843	$ 330,410	$ 489,820
SGA	$ 2,883	$ 6,237	$ 10,662	$ 14,435	$ 20,807	$ 30,895	$ 45,873	$ 68,113
Operating Income/Loss	$ 14,857	$ 7,967	$ 28,320	$ 66,909	$ 114,800	$ 172,800	$ 260,103	$ 391,515
EBIT	$ 14,857	$ 7,967	$ 28,320	$ 66,909	$ 114,800	$ 172,800	$ 260,103	$ 391,515
Interest Expense	$ (8,242)	$ (9,917)	$ (15,389)	$ (29,868)	$ (60,004)	$ (89,250)	$ (132,751)	$ (197,455)
Net Income	$ 6,615	$ (1,950)	$ 11,936	$ 33,728	$ 55,143	$ 84,272	$ 128,788	$ 196,819
Dividends per Share	$ 0.60	$ 0.60	$ 0.60	$ 0.62	$ 0.65	$ 0.66	$ 0.68	$ 0.69
FFO	9.8	5.4	11.4	14.0	11.5	9.4	7.8	6.4
					PV DPS	$ 0.61	$ 0.57	$ 0.54
FCFE	**$ 6,298**	**$ 136,910**	**$ 247,733**	**$ 843,442**	**$ 850,268**	**$ 580,273**	**$ 714,379**	**$ 869,632**
Net Income	6,615	(1,950)	11,936	33,728	55,143	84,272	128,788	196,819
CapEx	-	-	-	-	-	-	-	-
Change in WC	(317)	-	(2,056)	(21,167)	(595)	(4,827)	(5,729)	(6,875)
Net New Debt	-	138,860	237,853	830,881	795,720	500,829	591,321	679,688
				PV of CF	$ 922,541	$ 683,112	$ 912,469	$ 1,205,187
Recommendation: HOLD	Revenue Growth	6.86%	107.45%	93.77%	65.19%	47.98%	47.98%	47.98%

The dividends per share forecast was based on the 4% increase from 2019 to 2020. The company had a healthy payout ratio of 62%, but this could be expected to decline in the future due to wanting to reinvest money into the company. For this reason, dividends were increased by 2% for the next three years. Capital expenditures are not expected to occur because majority of the leases signed require the tenants to take care of capital expenditures (triple net). Cash flows are assumed to decrease in 2021 due to impacts of covid-19 but are assumed to remain back to normal in 2022. The company has received 100% of their ground rent in 2020 and has 60+ year leases that will continue to cash flow for the remainder of their term. They have $200 million in letters of intent which proves the demand for their acquisitions of new land. They have signed more leases with multi-family properties which could be less risky than offices and hotels during this time. They've still been able to increase revenue by 81% and create a 64% return for their shareholders compared to 2019.

Valuation:

Growth Rate	3.50%
Discount Rate	8.50%
Sum of CF	$ 3,723,309
Equity Value	$ 3,723,323
Shares Outstanding	52,993,116
Short-term PV	$ 1.73
Terminal Value	14.27855

Target Price	**$ 70.26**
Current Stock Price	**$ 66.82**
Under Valued	**$ 3.44**

Analyst Target Price	
Low	$ 67.00
Avg	$ 72.50
High	$ 79.00

The discount rate used for safehold is 8.50% (average) and a growth rate of 3.50 % which is believed to be the standard for the real estate sector. The FCFE per share is $10.95 which is lower than market price.

Sensitivity Analysis:

Sensitivity Analysis	Discount Rate					
		7.50%	8.00%	8.50%	9.00%	9.50%
Net Income Growth Rate	32.82%	65.88	66.68	67.49	68.30	69.13
	42.82%	67.15	67.97	68.80	69.63	70.48
	52.82%	68.56	69.41	70.26	71.12	71.99
	62.82%	70.13	71.00	71.88	72.77	73.66
	72.82%	71.86	72.76	73.67	74.58	75.51

This analysis is based on the discount rate and the net income growth rate.