

Office REITs

Office REIT 4Q23 earnings preview:
lowering estimates & adjusting POs

Price Objective Change

Demand improved into year-end but challenges remain

Office demand picked up into year-end in NYC but the leasing and financing environment remains challenging for office landlords. This is driven by elevated availability of space with continued record levels of sublease space, limited US bank financing to the office sector and concern over distress in 2024 as landlords question whether or not extensions are a smart strategy. Extensions work if landlords are willing and able to spend capital on buildings to provide amenities which are demanded today.

RXR CEO positive on leasing velocity but overall cautious

Last week, we hosted our annual NYC and CRE outlook call with Scott Rechler, Chairman and CEO of RXR Realty. Rechler is positive on office leasing velocity for top quality space but is more cautious on the overall macro environment, including regional bank lending to CRE and the market pricing in 6 Fed cuts in '24. Office lending is particularly difficult with few financing options available besides from existing lenders. RXR is positioning itself to be opportunistic as distress arises over the next two years.

Lack of visibility supports our cautious view on 2024

As we wrote in our [2024 Year Ahead](#) (see report) we expect the operating environment to remain challenging for office landlords in 2024. Tenants are still taking a protectionist approach to office space needs and supply remains elevated, especially on the West Coast. We expect return to office mandates to have a limited impact from here on leasing decisions. The new norm is making leasing decisions based on a hybrid workforce. Join our expert calls on 1/16 & 1/18 for more color. Contact your salesperson to register.

Lowering our 2024 estimates ahead of 4Q23 earnings

Our key focus this earnings season will be on 2024 guidance where we see risk of initial guidance midpoints missing the Street. Consensus 2024 FFO/sh earnings revisions averaged -0.7% for Office REITs in December (see [consensus earnings revisions note](#)). We are lowering our 2024 FFO/sh estimates by -1.5% on average to reflect our continued cautious view (Exhibit 2), and we are now below the Street on average by -2%. We also lowered our SLG estimates by -2% and introduce a new asset level model for SLG (see our [deep dive note here](#)). Our 2024 FFO estimate is -1c below the Street.

Adjusting POs on BofA's updated interest rate outlook

We are adjusting our price objectives to reflect BofA's updated interest rate outlook. BofA econ team is now calling for 100bp of rate cuts in 2024 starting in March. This compares to their prior 75bp forecast starting with cuts in June. While our base case estimates for 2024 continue to reflect a soft landing, we are adjusting cap rates lower where appropriate to reflect lower rates. Please see inside a detailed explanation for each PO change by REIT with a summary in Exhibit 1.

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United States
REITs

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Exhibit 1: Summary of PO Changes

Updated POs after model reviews

Ticker	Old PO	New PO	QRQ	Rating
BXP	\$67.00	\$75.00	B-1-7	Buy
CUZ	\$23.00	\$26.00	B-1-7	Buy
ESRT	\$10.50	\$11.00	C-1-7	Buy
HIW	\$20.00	\$23.00	B-2-7	Neutral
HPP	\$4.50	\$5.25	C-3-8	U/P
KRC	\$35.00	\$41.00	B-2-7	Neutral
VNO	\$24.00	\$28.00	C-2-8	Neutral

Source: BofA Global Research

BofA GLOBAL RESEARCH

Key Terms:

CRE: commercial real estate

FFO: funds from operations

NAV: net asset value

NOI: net operating income

PO: price objective

RTO: return to office

RXR: RXR Realty

U/P: Underperform

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Refer to important disclosures on page 6 to 8. Analyst Certification on page 4. Price Objective Basis/Risk on page 3.

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Timestamp: 08 January 2024 12:42AM EST

PO and Estimate Changes

Exhibit 2: Summary of estimate changes

Updated estimates after review of models

Ticker	2023		2024		2025		2026		2027	
	Old	New	Old	New	Old	New	Old	New	Old	New
BXP	\$7.27	\$7.26	\$7.30	\$7.16	\$7.33	\$7.20	\$7.34	\$7.25	\$7.40	\$7.07
CUZ	\$2.63	\$2.63	\$2.65	\$2.59	\$2.78	\$2.71	\$2.83	\$2.76	\$2.84	\$2.77
HPP	\$0.98	\$0.99	\$1.01	\$1.01	\$1.24	\$1.20	\$1.43	\$1.36	\$1.52	\$1.42
KRC	\$4.58	\$4.57	\$4.36	\$4.24	\$4.59	\$4.50	\$5.04	\$5.03	\$5.13	\$5.14
VNO	\$2.55	\$2.55	\$2.45	\$2.45	\$2.46	\$2.46	\$2.57	\$2.56	\$2.70	\$2.69

Source: BofA Global Research estimates

BofA GLOBAL RESEARCH

BXP (B-1-7): Following a review of interest rates and operating conditions in BXP's markets we are increasing our price objective to \$75.00 from \$67.00. Our \$75 price objective for BXP represents a -5.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 6.9% (previously 7.1%) cap rate to our forward NOI estimate of \$2.033B (previously \$2.039B). We reiterate our Buy rating.

CUZ (B-1-7): Following a review of interest rates and operating conditions in CUZ's markets we are increasing our price objective to \$26.00 from \$23.00. Our \$26 price objective for CUZ represents a -10.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 7.4% (previously 7.8%) cap rate to our forward NOI estimate of \$534M (unchanged). We reiterate our Buy rating.

ESRT (C-1-7): Following a review of interest rates and operating conditions in ESRT's markets we are increasing our price objective to \$11.00 from \$10.50. Our \$11.00 price objective for ESRT represents a -10.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 8.2% (previously 8.3%) cap rate to our forward NOI estimate of \$398M (unchanged). We reiterate our Buy rating.

HIW (B-2-7): Following a review of interest rates and operating conditions in HIW's markets we are increasing our price objective to \$23.00 from \$20.00 but reiterate our Neutral rating as leasing and financing challenges remain. Our \$23 price objective for HIW represents a -25.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 8.0% (previously 8.2%) cap rate to our forward NOI estimate of \$524M (unchanged).

HPP (C-3-8): After updating our model for HPP's recent dispositions we are increasing our price objective to \$5.25 from \$4.50 but lowering our estimates. We reiterate our Underperform rating as leasing and financing challenges remain. Our \$5.25 price objective for HPP represents a -30.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 8.9% (unchanged) cap rate to our forward NOI estimate of \$472M (previously \$515M).

KRC (B-2-7): Following a review of interest rates and operating conditions in KRC's markets we are increasing our price objective to \$41.00 from \$35.00 but reiterate our Neutral rating as leasing and financing challenges remain. Our \$41 price objective for KRC represents a -15.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 7.9% (previously 8.0%) cap rate to our forward NOI estimate of \$715M (previously \$718M).

VNO (C-2-8): Following a review of interest rates and operating conditions in VNO's markets we are increasing our price objective to \$28.00 from \$24.00 but reiterate our Neutral rating as leasing and financing challenges remain. Our \$28 price objective for VNO represents a -20.0% discount (unchanged) to our forward NAV estimate. We derive our NAV estimate by applying a 7.5% (previously 7.9%) cap rate to our forward NOI estimate of \$1.027B (unchanged).

Exhibit 3: Stocks mentioned

Rating and price summary

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BXP	BXP US	Boston Properties	US\$ 70.36	B-1-7
CUZ	CUZ US	Cousins Prop Inc.	US\$ 24.39	B-1-7
ESRT	ESRT US	Empire State Realty	US\$ 9.81	C-1-7
HIW	HIW US	Highwoods	US\$ 23.04	B-2-7
HPP	HPP US	Hudson Pacific	US\$ 9.67	C-3-8
KRC	KRC US	Kilroy Realty	US\$ 40.26	B-2-7
VNO	VNO US	Vornado	US\$ 27.94	C-2-8

Source: BofA Global Research

BofA GLOBAL RESEARCH

Price objective basis & risk**Boston Properties (BXP)**

Our price objective for BXP of \$75 is -5% discount to our forward 12-month NAV estimate. We apply a 6.9% cap rate to our forward 12-month NOI estimate of \$2.03B to calculate our NAV. We apply this cap rate based on our view of private market transaction comps in BXP's markets. Risks to our price objective are development leasing, operating conditions in BXP's office markets and development yields below our expectations. Further, a prolonged period of tight credit market conditions could weigh on access to capital, borrowing costs, and direct real estate values.

Cousins Properties Inc. (CUZ)

Our price objective of \$26 for CUZ is a -10.0% discount to our forward NAV estimate. We apply a 7.4% cap rate to our forward nominal NOI estimate of \$534M to calculate our NAV. The cap rate is based on our view of interest rates over the next year, current private market/transaction comps, and the market exposure of CUZ. Downside risks to our PO are operating conditions below our expectations, a prolonged period of tight credit market conditions, and execution risk as CUZ works to reduce this Atlanta exposure and exit additional markets. Upside risks to our PO are operating and leasing conditions above our expectations.

Empire State Realty Trust (ESRT)

Our price objective of \$11 for ESRT is a -10% discount to our forward NAV estimate. This discount reflects uncertainty over net effective rent growth and cap rates in Manhattan, return of tourism to NYC, and NYC office asset values. We apply a blended 8.2% cap rate to our forward NOI estimate of \$398M. We use a 8.2% cap rate based on our view of interest rates over the next year, current and expected private market/transaction comps, and the market exposure of ESRT. Downside risks to our PO are NYC office market conditions and NOI from the Empire State Building Observatory below expectations. Upside risks to our PO are better-than-expected operating conditions for the Observatory and leasing progress across the office portfolio, and an even stronger market for NYC office asset trades that pushes market cap rates lower.

Highwoods Properties (HIW)

Our \$23 price objective for HIW is a -25.0% discount to our forward NAV estimate. We apply a 8.0% cap rate to our forward NOI estimate of \$524M. We use this cap rate based on our view of interest rates over the next year, current private market/transaction comps, and the market exposure of HIW. Upside risks to our HIW PO are better-than-expected operating conditions, asset pricing, and buyer demand for sales transactions in HIW's core markets. The downside risks to our HIW PO are operating conditions and acquisition and development yields below our expectations. A prolonged period of tight credit market conditions is another risk.

Hudson Pacific Properties, Inc. (HPP)

Our \$5.25 price objective for HPP is a -30.0% discount to our forward NAV estimate. We apply a 8.9% cap rate to our forward NOI estimate of \$472M. We use a 8.9% cap rate for HPP based on our view of interest rates over the next year, current private market/transaction comps, and the market exposure of HPP. The upside risk to our PO is better-than-expected operations and asset values across HPP's markets. The downside risks are operating conditions and asset values in HPP's markets below our expectations. Further, a prolonged period of tight credit market conditions could weigh on access to capital, borrowing costs and direct real estate values. HPP earns more than 60% of its revenue from assets in the San Francisco Bay Area, adding regional concentration risk.

Kilroy Realty Corporation (KRC)

Our \$41 price objective for KRC is a -15.0% discount to our forward NAV estimate. This discount reflects uncertainty over office demand and development leasing in the current environment. We apply a 7.9% cap rate to our forward NOI estimate of \$715M. We use a 7.9% cap rate for KRC based on our view of interest rates over the next year, current private market/transaction comps, and the market exposure of KRC. Downside risks to our PO are operating conditions, development leasing and investment yields below our expectations. Further, should credit market conditions weaken, it could weigh on KRC's access to capital, borrowing costs, and direct real estate values.

Vornado Realty (VNO)

Our \$28 price objective for VNO is a -20% discount to our forward NAV estimate. This discount reflects below-average earnings visibility as VNO vacates space for redevelopment in the Penn District. We apply a 7.5% blended cap rate to our forward NOI estimate of \$1.027B to calculate our NAV. We use this cap rate based on our view of interest rates over the next year, current private market/transaction comps, and the market exposure of VNO. Upside / downside risks to our PO are operating conditions, investment yields, development leasing and an economic outlook above / below our expectations. Tight credit market conditions could also weigh on VNO's shares.

Analyst Certification

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Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Agree Realty Corp	ADC	ADC US	Joshua Dennerlein
	Alexandria Real Estate Equities	ARE	ARE US	Joshua Dennerlein
	American Homes 4 Rent	AMH	AMH US	Jeffrey Spector
	Americold Realty Trust	COLD	COLD US	Joshua Dennerlein
	AvalonBay Communities Inc	AVB	AVB US	Joshua Dennerlein
	Boston Properties	BXP	BXP US	Jeffrey Spector
	Brixmor Property Group	BRX	BRX US	Jeffrey Spector
	COPT Defense Properties	CDP	CDP US	Camille Bonnel
	Cousins Properties Inc.	CUZ	CUZ US	Camille Bonnel
	EastGroup Properties	EGP	EGP US	Jeffrey Spector
	Empire State Realty Trust	ESRT	ESRT US	Camille Bonnel
	Equity Residential	EQR	EQR US	Jeffrey Spector
	Essential Properties	EPRT	EPRT US	Joshua Dennerlein
	Federal Realty	FRT	FRT US	Jeffrey Spector
	Invitation Homes Inc	INVH	INVH US	Joshua Dennerlein
	Kimco Realty	KIM	KIM US	Jeffrey Spector
	Kite Realty Group	KRG	KRG US	Jeffrey Spector
	OMEGA Healthcare	OHI	OHI US	Joshua Dennerlein
	Phillips Edison & Company	PECO	PECO US	Jeffrey Spector
	Prologis, Inc.	PLD	PLD US	Camille Bonnel
	Public Storage, Inc.	PSA	PSA US	Jeffrey Spector
	Regency	REG	REG US	Jeffrey Spector
	Rexford Industrial Realty	REXR	REXR US	Camille Bonnel
	Sabra Health Care	SBRA	SBRA US	Joshua Dennerlein
	Simon Property	SPG	SPG US	Jeffrey Spector
	Welltower	WELL	WELL US	Joshua Dennerlein
NEUTRAL				
	Acadia Realty Trust	AKR	AKR US	Jeffrey Spector
	CubeSmart	CUBE	CUBE US	Jeffrey Spector
	EPR Properties	EPR	EPR US	Joshua Dennerlein
	Equity LifeStyle Properties	ELS	ELS US	Jeffrey Spector
	Essex Property Trust, Inc.	ESS	ESS US	Joshua Dennerlein
	Extra Space Storage, Inc.	EXR	EXR US	Jeffrey Spector
	Getty Realty Corp.	GTY	GTY US	Joshua Dennerlein
	Highwoods Properties	HIW	HIW US	Camille Bonnel
	InvenTrust Properties	IVT	IVT US	Jeffrey Spector
	Kilroy Realty Corporation	KRC	KRC US	Camille Bonnel
	Macerich	MAC	MAC US	Jeffrey Spector
	Realty Income	O	O US	Jeffrey Spector
	Retail Opportunity Investments Corp.	ROIC	ROIC US	Jeffrey Spector
	SL Green Realty	SLG	SLG US	Camille Bonnel
	Sun Communities	SUI	SUI US	Joshua Dennerlein
	UDR, Inc.	UDR	UDR US	Joshua Dennerlein
	Ventas, Inc.	VTR	VTR US	Jeffrey Spector
	Veris Residential Inc	VRE	VRE US	Joshua Dennerlein
	Vornado Realty	VNO	VNO US	Camille Bonnel
UNDERPERFORM				
	American Assets Trust	AAT	AAT US	Camille Bonnel
	Armada Hoffer Properties	AHH	AHH US	Camille Bonnel
	Camden Property Trust	CPT	CPT US	Joshua Dennerlein
	Douglas Emmett	DEI	DEI US	Camille Bonnel
	Healthpeak Properties, Inc.	PEAK	PEAK US	Joshua Dennerlein
	Hudson Pacific Properties, Inc.	HPP	HPP US	Camille Bonnel
	Kennedy Wilson	KW	KW US	Joshua Dennerlein
	LXP Industrial Trust	LXP	LXP US	Camille Bonnel
	Medical Properties Trust, Inc.	MPW	MPW US	Joshua Dennerlein
	Mid-America Apartment Communities, Inc.	MAA	MAA US	Joshua Dennerlein
	National Storage Affiliates Trust	NSA	NSA US	Jeffrey Spector
	NetSTREIT	NTST	NTST US	Joshua Dennerlein
	NNN REIT Inc	NNN	NNN US	Joshua Dennerlein
	Paramount Group	PGRE	PGRE US	Camille Bonnel
	Peakstone Realty Trust	PKST	PKST US	Joshua Dennerlein
	STAG Industrial	STAG	STAG US	Camille Bonnel



US - REITs Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Tanger Factory	SKT	SKT US	Jeffrey Spector
	WP Carey	WPC	WPC US	Joshua Dennerlein
RSTR				
	Spirit Realty Capital	SRC	SRC US	Joshua Dennerlein

Disclosures

Important Disclosures

Equity Investment Rating Distribution: REITs (Real Estate Investment Trusts) Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	40	46.51%	Buy	33	82.50%
Hold	27	31.40%	Hold	21	77.78%
Sell	19	22.09%	Sell	16	84.21%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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