April 29th, 2019
Digital Realty (NYSE:DLR)
Thomas Soussan

Sector: Real Estate
Industry: REIT - Office
Current Price: $117.26
Target Price: $159.73

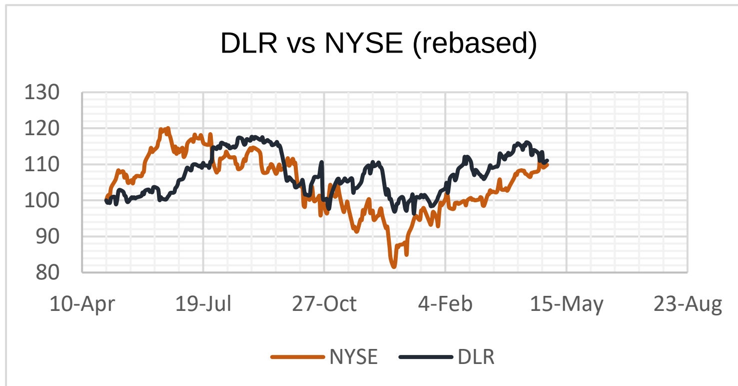
Company Description: Digital Realty supports the data centers; colocation and interconnection strategies gather more than 2,300 firms within its structures. Located throughout North America, Europe, Asia and Australia, the company's clients are ranged from cloud and information technology services and communication, manufacturing energy, healthcare and consumer products.

BUY

Current Price:	$117.26
Target Price:	$159.73
Market Cap:	3.653B
Beta:	0.68
Other key Metrics/Ratios	

P/E Ratio: 93.84 **EPS: 1.25**

NOPAT: 234.23 **ROIC: 1.10%**



Thesis: I am recommending a BUY on Digital Realty .The company provides interconnection strategies, cloud solutions to meet with the growing global demand for hyper-scale storage solution. While their whole sales segment in experiencing a slower growth, we expect an increase in other segments such as interconnectivity and collocation driving their revenues up

Catalysts: Forward looking projections

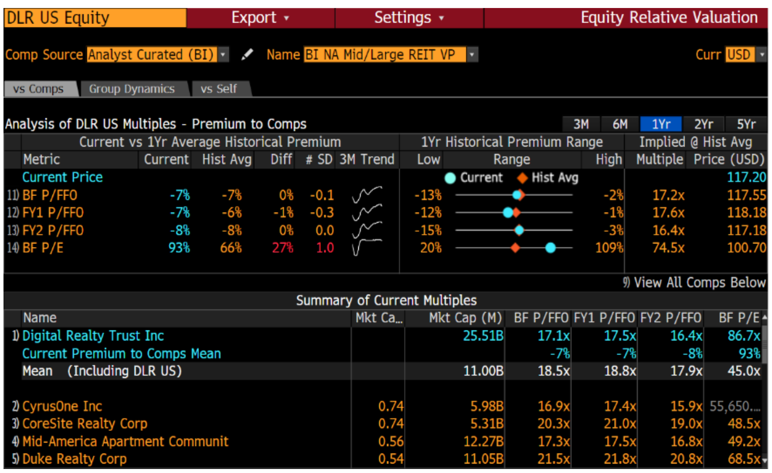
- Short Term: Slower growth in revenues from certain segments
- MidTerm(1-2years): Increase in cash inflow resulting in higher FFO payout
- Long Term(3+): Global increase of revenues, approx. 7 to 10% before reaching an organic growth of 3.25%

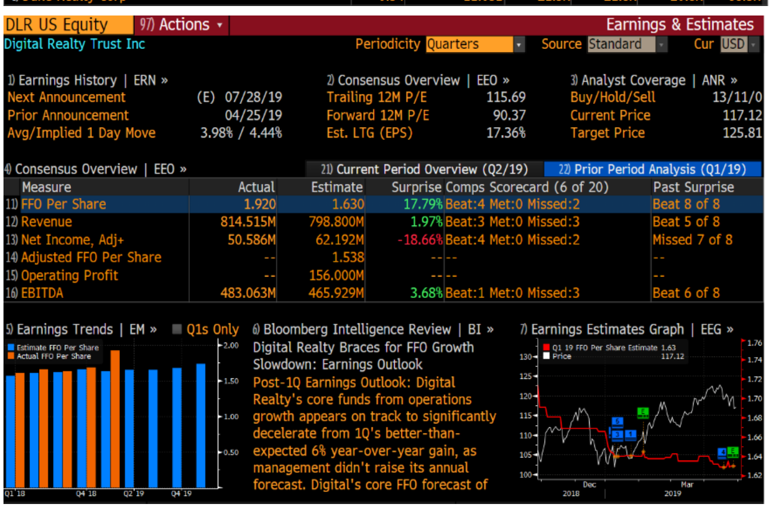
Macro-economy outlook

The macroeconomic context is a significant variable to take into account for an internationally exposed company like Digital Realty. In fact, their operations could be harmed by any political decision taken in a country they operates in. The latest release from both the IMF and WEO (World Economic Outlook) have shown a potential weakening economy for the upcoming quarters and for the year 2020. In fact, the revised global economy projections from October 2018 announced a decrease of 0.2 and 0.1percentage point from the initial 3.5% growth for 2019 and China, the S&P 500 that has rallied by 22.7% from a 15.74% drop from December 2018, and has reached its all-time high and keep increasing as of today at 2,947.22. The bullish trend of the market offer the S&P a possible window of increase due to a possible rally during the second half of the year. With a systematic risk of 78% the variance associated with market movements on DLR historical performance, the company is therefore highly impacted by the market fluctuations and is dependent to the global economy like Brexit vote that may change the regulation and affect the company revenues. However, a beta of 0.68 help them to offset significant market fluctuations and make this company a defensive stock due to its statute of REIT. The company geographic concentration are mainly on the US land (52.4%) in the following locations: Northern Virginia, Chicago, and Silicon Valley & New York. Ultimately, their main source of revenues come from their lease and properties.

Multiples Analysis & Earnings Performance

The multiples analysis slightly differ from the traditional public companies since DLR has a statue of REIT. Being a REIT affects the traditional accounting tools since we cannot judge whether the company is operating well based on its net income. Instead, we use other metric such as Fund From Operations also known as FFO and FFO per share as synonym of EPS. . Furthermore, the metrics shows that the company is fairly priced compared to its main competitors as equivalent market capitalization like Mid-America Apartment Communit or Duke Realty Corp, while company with lower market capitalization would tend to be overvalued. The company has no other choice that to its dividend and beat estimates to maximise the shareholders profits. The Q1 results were significantly higher than the expectation, the company has beaten all the Wall Street estimates showing a better than expected grow in FFC/Share mainly reaching 1.92 vs the 1.63 estimated or a delta of 17.79%. and so did the revenues by an increase of 1.97%. Despite these good results, it becomes hard for the company to keep up with the Wall Street estimation since their last acquisition has taken more time than expected, driving the flat return of 1.5% Yoy.





Competitive advantage/ Growth potential

Digital Realty having a statute of REIT, we will use different metrics to show their comparative advantage. Since most of the REIT firms redistribute their income as a form of dividends, the company must be able to generate a significant amount of cash while having a FFO/share competitive relative to its peer. Over the past two years, DLR has been able to deliver tremendous cash from operations since their FFO has grown by 35% from 2017 to 2018 mainly driven by a sharp increase of net income available to common stockholders (+44.34%) while their depreciation on assets experienced a slower growth (40%).The company is set acquire data centers across the world in order to maximize their shareholders return. In fact, the recent acquisition of Ascenty - which is the leader of data center infrastructure in Latin America, in December 2018 and the acquisition of DuPont Fabros Technology Inc in 2017 highlight the company's objective to meet the global demand for hyper-scale and public cloud solution. Operating in 35 major metropolitan cities, 12 countries over five continents, the company is globally expanding its footprint (34.4 million square feet including 3.4 million under active development) which is a clear advantage compared to its peers. Additionally, providing two types of products going from Colocation to scale or hyper-scale renting is a key differentiation for Digital Realty. By being able to host different kind of data for small companies to large boxes for big conglomerate like Google, the company is able to host the biggest large-cap data thanks to its technology. The company ranks its customers in three distinct categories such as Cloud (IBM,Oracle Amercia Inc, Equinix), Digital Content Providers and Financial Companies (Facebook, Linkedin, JPMorgan Chase & Co) and Network and Mobile Services (Verizon, AT&T, Comcast Corporation). Considering each of this company expending worldwide, they will need more storage and so will expand their utilization of DLR technology. By leveraging out a lot of debt (28%) to finance its project, the company wants to maintain a high operating efficiency and maximize returns for its shareholders. The revenues are expected to keep increasing on time horizon n+3 at a 7.2% growth rate thanks to an increase in colocation and interconnection, which grew faster than expected for the past quarter while they both represent 10% of their current revenues. Alongside, their EBITDA is increasing over YoY by 26.73% despite a EBITDA Margin growing at a slower pace (2.25%) as a result of increase operating expenses.

Threats/ Downside

Being internationally represented, Digital Realty is subject to economic fluctuations. In fact, the company does not enter into forward contracts to hedge to foreign exchange rated variations. Instead, the company tends to borrow in the local currency they operate in, leaving behind huge amount of credit lines that worth $1.1B representing 9% of their total liabilities. The company has many credit line in various currencies such as British pound sterling, Euro, Canadian dollar & Singapore dollar. As a results any insatiability is the nominate countries, such as Great Britain with Brexit, may be a threats to the company since the local currency they have to back their loan with may suddenly drop or sharply increase based on the negotiations with the European Union.

More important, considering that 25% of their revenues are generated from the international market, such fluctuations may also badly affect their revenues and operations that will lead to a loss to earning for the shareholders. As a more fact, the company is driven by five leading customers representing 25% of their annualized rent or $759M. In order words, an expected shift in this concentration of significant customers will negatively affect the company annualized rent/revenues. Additionally, given the large company's acquisitions of data centers may eventually affect their rent price. As any other business, the cloud business along with data centers are subject to supply and demand; consequently, if demand and supply cannot find a fair equilibrium, the oversupply of data center lead by the drop in price until finding a price at which the company will not be profitable enough. Lastly, it is hard to a project the company shape over 8 to year period since the top 20 customers of the company such as IBM, Oracle or AT&T may find a potential and better way to store data, and so break the partnership with Digital Realty leading to a stock price drop.

Ownership

The first screen shot, which is the percentage of ownership within the company, show us what type of investors target the company. Representing more than 85% of the market shares held, investment advisors that are any person or group that conduct recommendations such as JPMorgan or Morgan Stanley, benefit the most from the dividend of the company. In other words, with a FFO payout of 60.82%, the investment investors receive roughly $700M in dividends out of the $1.3B in FFO. However, the percentage of floating share representing 64% may be a threat to the company in term of take over if hedge funds would drastically increase their positions in the company. The main holder of the floating shares remain a passive strategy group –Vanguard, which has 15.68% followed by Capital Group Cos and BlackRock Inc with respectively 12.32% and 9.69% of the floating shares. The IGPV function shows us, also, at which the volume of shares at which price the investors want the stock. There are some bullish investors That target a $120 per share, which confirms a undervalued/fairly price stock.


DLR US Equity 25) Export Settings Security Ownership
DIGITAL REALTY TRUST INC CUSIP 25386810
1) Current 2) Historical 3) Matrix 4) Ownership Summary 5) Insider Transactions 6) Options 7) Debt
Compare Current Stats Against 04/28/19

Top Ownership Type (%)

51) Ownership Type	04/28/19	Curr	Change
11) Investment Advisor	85.71	85.72	+0.01
12) Pension Fund	5.08	5.09	+0.01
13) Bank	3.9	3.89	-0.01
14) Hedge Fund Manager	1.09	1.09	0.00
15) Brokerage	1.06	1.06	0.00
16) Government	0.98	0.98	0.00
17) Insurance Company	0.97	0.97	0.00
18) Sovereign Wealth Fund	0.82	0.82	0.00
19) Holding Company	0.24	0.24	0.00

Top Geographic Ownership (%)

52) Geographic	04/28/19	Curr	Change
21) UNITED STATES	86.21	86.21	0.00
22) JAPAN	3.97	3.97	0.00
23) UNITED KINGDOM	3.16	3.16	0.00
24) CANADA	2.17	2.17	0.00
25) NETHERLANDS	1.31	1.31	0.00
26) NORWAY	0.77	0.77	0.00
27) SWITZERLAND	0.58	0.57	-0.01
28) AUSTRALIA	0.45	0.45	0.00
29) SWEDEN	0.29	0.3	+0.01

Top Fund Objective Ownership (%)

53) Fund Objective	04/28/19	Curr	Change
31) Blend	22.77	22.91	+0.14
32) ETF	20.51	20.51	0.00
33) Sector Fund	19.59	19.62	+0.03
34) Asset Allocation	15.57	15.6	+0.03
35) Value	9.36	9.36	0.00
36) Growth	4.25	4.25	0.00
37) Real Estate	3.87	3.86	-0.01
38) Unclassified	2.81	2.62	-0.19
39) Country Fund	0.77	0.77	0.00

Institutional - Based on Current Filings

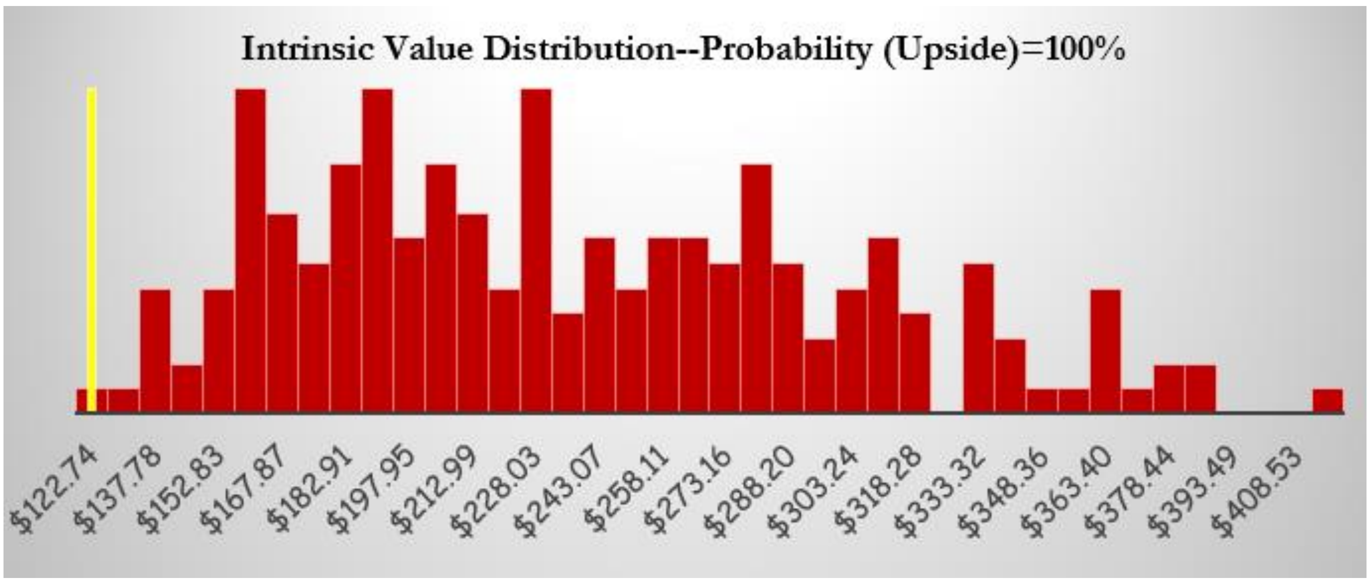
54) Institutional	04/28/19	Curr	Change
41) % of Shares Held	132.5	132.51	+0.01
42) % of Float Held	132.6	132.6	0.00
43) # of Institutions	1,050	1,047	-0.29%
44) # of Buyers	385	383	-0.52%
45) # of Sellers	352	348	-1.14%
46) # of New Buyers	118	114	-3.39%
47) # of Selloffs	142	142	0.00%
48) % Chg in Inst Positions	+41.97	+41.94	-0.03

Base/Best/Worst case

The company valuation is done on the following criterions:

- 25% EV/REVENUE
- 50% EV/EBITDA
- 25% P/E

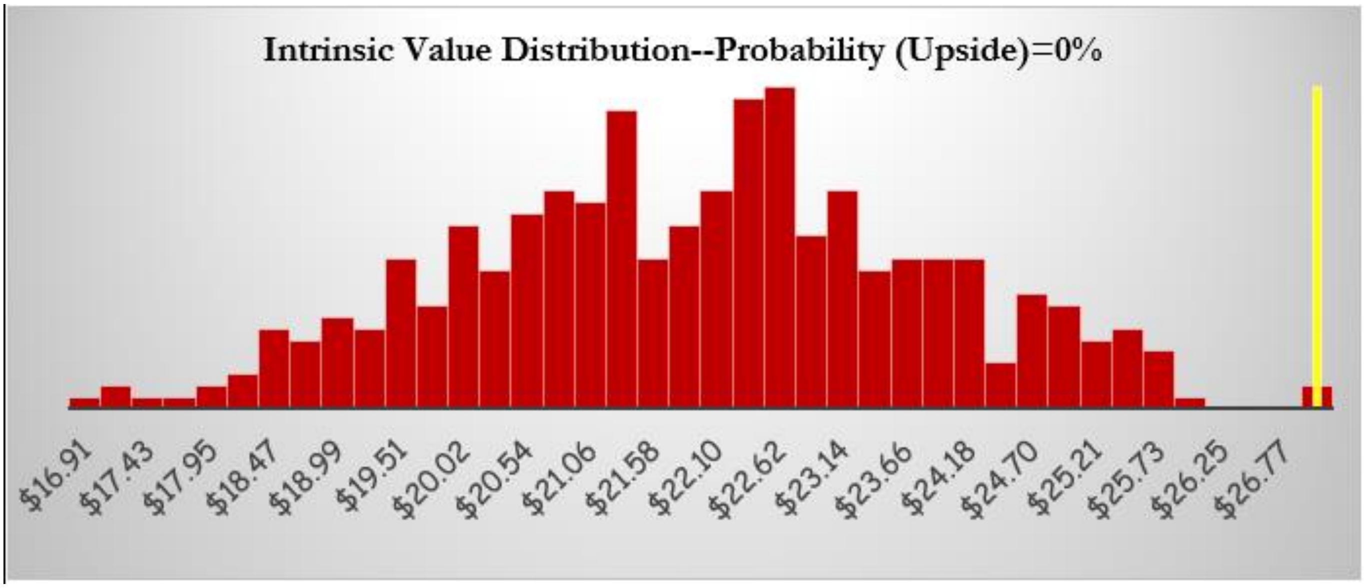
<u>Base case</u>:



◘ Expected constant growth by year 15

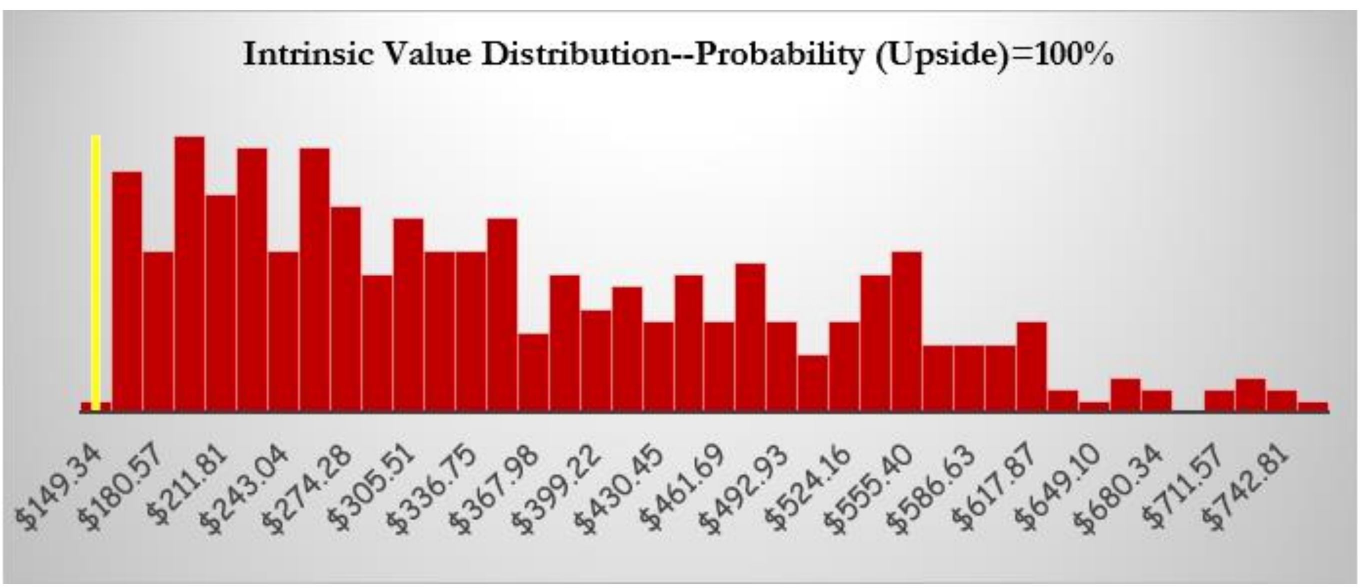
◘ Based on revenue expectations, by year 5, the growth in revenue will reach 10% and will decrease thereafter at to reach

Worst Case:



- Expected constant growth from year 3
- Valuation 100% DCF

Best case:



- Expected Constant growth from year 5
- 100% Price/Book Value valuation

Conclusion

Digital Realty is a Buy. Various component in this analysis has shown the benefits of holding this stock. Being a REIT, the company thrive in its business by opening and acquire new data centers. By giving out more than 50% of its FFO, the company is favoring its shareholders by paying them huge dividends. Although DLR could be harm by its international exposure, its footprint across the world while delivering several products to big conglomerate is an advantage for them considering the increasing amount of data storage needed to continue operations. In the future, DLR may be also hosting new giant of telecommunications, which will drive their revenues up.

SIENAcollege   BJORKLUND FUND

Digital Realty Trust, Inc.	Symbol: DLR
Analyst	TS
Buy below	$136.48
Sell above	$175.81
Probability of Price Increase	100%
Last Price	$117.25
Intrinsic Value	$150.73
Target Dividends	$4.23
Target Price	$159.54

Quarterly Earning Surprises (Actual Vs. Median Estimates)

Revenue	
3/31/2018	1.17%
6/30/2018	0.31%
9/30/2018	0.36%
12/31/2018	-0.35%
3/31/2019	3.22%
Mean (Standard Error)	0.94% (1.01%)

EBITDA	
3/31/2018	-12.44%
6/30/2018	-12.78%
9/30/2018	-17.70%
12/31/2018	-20.49%
3/31/2019	-100.00%
Mean (Standard Error)	#DIV/0!

Financials

Profitability	**DLR (LTM)**	**DLR Historical**	**Peers' Median (LTM)**
Return on Capital	1.5%	1.93%	3.97%
Adjusted EBITDA Margin	49.2%	21.00%	44.99%
Return on Equity	3.4%	2.2%	5.3%
Adjusted Net margin	9.9%	9.8%	7.1%
Invested Funds	**DLR (LTM)**	**DLR Historical**	**Peers' Median (LTM)**
Cash/Capital	0.3%	0.4%	1.3%
NWC/Capital	-3.4%	-4.6%	-1.4%
Operating Assets/Capital	87.1%	101.4%	84.7%
Goodwill/Capital	16.0%	2.8%	12.9%
Capital Structure	**DLR (LTM)**	**DLR Historical**	**Peers' Median (LTM)**
Total Debt/Market Cap.	0.46	0.53	0.50
Reported Cost of Borrowing	3.4%		4.3%
Cash Interest/Total Debt			3.7%
CGFS Credit Rating	A		BBB
Credit Model Rating	bbb+		bbb-
Probability of Default	0.03%		0.01%
Cost of Capital			
	CGFS Credit Rating	**Credit Model Rating**	**Probability of Default**
Implied Cost of Borrowing (DLR)	4.1%	5.2%	4.8%
Implied Cost of Borrowing (Peers)	4.8%	5.7%	4.4%
Cost of New Debt Estimate	3.4%		
Market Risk Premium Estimate	5.2%		
Cost of Equity Estimate	8.6%		
WACC Estimate	8.6%		

Valuation

DCF Valuation

	Revenues	**EBITDA Margin**	**UFCF**	**WACC**	**ROIC**	**Price Per Share**
Base Year (Actual)	$566.34	39%	$268.20	8.12%	35.33%	$129.14
year 1	$711.74	41%	$158.32	8.93%	40.08%	$139.94
year 2	$869.28	42%	$213.29	8.92%	35.83%	$151.51
year 3	$1,049.52	42%	$265.88	8.91%	31.49%	$163.82
year 4	$1,252.44	42%	$324.88	8.91%	28.19%	$176.85
year 5	$1,477.08	42%	$390.33	8.90%	25.57%	$190.58
year 6	$1,721.34	42%	$461.80	8.89%	23.39%	$204.97
year 7	$1,981.91	42%	$538.58	8.88%	21.53%	$219.98
year 8	$2,254.19	42%	$619.72	8.88%	19.90%	$235.55
year 9	$2,532.34	41%	$703.59	8.87%	18.45%	$251.62
year 10	$2,809.38	41%	$788.22	8.87%	17.11%	$268.11
year 11	$3,077.42	41%	$871.48	8.86%	15.86%	$284.95
year 12	$3,327.98	41%	$951.04	8.86%	14.69%	$302.05
year 13	$3,552.36	41%	$1,024.59	8.86%	13.57%	$319.33
year 14	$3,742.18	41%	$1,089.59	8.86%	12.50%	$336.72
year 15	$3,889.77	41%	$1,141.58	8.86%	11.46%	$367.02
Continuing Period	$3,988.76	41%	$743.65	8.87%	8.87%	

Relative Valuation					**Asset Based Valuation**	
RELATIVE	**EV/Rev (FW)**	**EV/EBITDA (FW)**	**P/BV (TTM)**	**P/E (FW)**	**Recovery Rate**	100%
Median (Peers)	8.2x	54.0x	19.7x	98.2x	**Capital**	$7,395.45
	Revenue (NTM)	**EBITDA (NTM)**	**Book Value (LTM)**	**Net Income (NTM)**	**Intangibles**	$52.63
Base	$729.87	$297.87	$463.10	$222.24	**Claims**	$70.35
Implied EV	$6,020.88	$16,088.95				
Total Net Claims	-$90.33	-$90.33				
Implied EQ	$6,111.21	$16,179.28	$9,110.77	$21,819.43		$7,272.47

Valuation Summary

Model	**Intrinsic Value**	**Target Price**	**Weight**
DCF Valuation	$129.14	$139.94	40.00%
EV/Rev (FW)	$104.32	$112.79	0.00%
EV/EBITDA (FW)	$276.18	$298.60	30.00%
P/BV (TTM)	$155.52	$168.15	30.00%
P/E (FW)	$372.46	$402.69	0.00%
Asset Based Valuation	$124.14	$134.22	0.00%
Price per Share	$181.16	$196.00	100%