



## COMPANY UPDATE / ESTIMATE CHANGES / PRICE TARGET CHANGE

SPG - NYSE (as of 10/26/2017)	\$163.76
Price Target	\$189.00
52-Week Range	\$150.15 - \$189.25
Shares & Units Outstanding (mm)	358
Market Cap. (\$mm)	\$58,626
3-Mo. Average Daily Volume (000)	1,516
Institutional Ownership	100%
Debt/Total Market Capital (9/17)	34%
Annual Dividend	\$7.40
Dividend Yield	4.5%
Fixed Charge Coverage (9/17)	5.1x

### FFO Per Share FY 12/31

	2016	Prior 2017E	Curr. 2017E	Prior 2018E	Curr. 2018E
1Q	\$2.63		\$2.74 A	\$2.84	\$2.85
2Q	\$2.63		\$2.47 A	\$2.97	\$2.97
3Q	\$2.70		\$2.89 A	\$3.09	\$3.07
4Q	\$2.53	\$3.12	\$3.10	\$3.33	\$3.33
Year	\$10.49	\$11.22	\$11.20	\$12.23	\$12.22
P/FFO	15.6x		14.6x		13.4x

Quarterly FFO amounts may not add up to annual amounts due to rounding.

### NOI (Net Operating Income) (\$mm)

	2016	Prior 2017E	Curr. 2017E	Prior 2018E	Curr. 2018E
1Q	\$942		\$976 A	\$1,023	\$1,021
2Q	\$947		\$980 A	\$1,032	\$1,031
3Q	\$971		\$999 A	\$1,099	\$1,096
4Q	\$1,033	\$1,077	\$1,077	\$1,150	\$1,148
Year	\$3,894	\$4,062	\$4,024	\$4,304	\$4,297

*Company Description:* Simon Property Group, Inc., headquartered in Indianapolis, Indiana, owns or has an interest in retail properties in North America, Europe, and Asia.

## REITs

Analyst: Carol L. Kemple  
502.588.1839 / [CKemple@hilliard.com](mailto:CKemple@hilliard.com)  
Institutional Sales Desk: George Moorin  
502.588.9141 / [GMoorin@hilliard.com](mailto:GMoorin@hilliard.com)  
J.J.B. Hilliard, W.L. Lyons, LLC  
October 27, 2017

## Simon Property Group, Inc.

SPG - NYSE – Buy - 2

### Third Quarter Results

- **Simon reported third quarter FFO of \$2.89 per share versus \$2.70 per share in the year ago period.** Results were slightly below our estimate but above the consensus, and were positively impacted by strong releasing spreads.
- **Occupancy was down 100 basis points year-over-year at 95.3%.** We note Simon combines occupancy and rental rates for the regional malls and premium outlets, instead of reporting them separately. Releasing spreads for the trailing twelve months were up 11.2%.
- **Development Activity.** Simon has redevelopment and expansion plans underway at 31 properties in the U.S. and Canada. Simon's total cost of all development and redevelopment projects under construction at quarter end was \$1.0 billion.
- **Dividend Increase.** In the 3Q17 earnings release, SPG announced a quarterly dividend increase of \$0.05 per share to a new quarterly rate of \$1.85 per share.
- **Management provided 2017 FFO per share guidance of \$11.17 to \$11.22.** Our revised FFO per share estimate is \$11.20, down from \$11.22 previously.
- **We are maintaining our Buy rating.** Our one year price target is lowered to \$189.00.

**Note Important Disclosures on Pages 6 and 7.**  
**Note Analyst Certification on Page 6.**

## **Additional Discussion**

Total revenue for the third quarter was \$1.4 billion, up 3.4% from the year ago period (please see page 3). Minimum (base) rent, which made up 61.4% of total revenue, was up 2.2%. Tenant reimbursements, the next largest revenue item, were \$386.7 million versus \$378.2 million and represented an estimated 131.1% versus 130.4% of total real estate expenses, including property operating expenses, real estate taxes, maintenance, advertising and a credit loss provision.

Combined occupancy (both regional malls and premium outlets) was down 100 basis points from 3Q16 at 95.3%. Releasing spreads for the 12 months ended September 30, 2017 rose 11.2%. Comparable NOI (net operating income) increased 2.5% for the three months ended September 30, 2017.

Net income available to common shareholders was \$513.8 million compared to \$504.7 million in the year ago period. Funds from operations were \$2.89 per share, up from \$2.70 per share a year ago.

## **Overview**

**Retail & Leasing Environment** - Total sales per square foot at Simon's malls and premium outlets were up 3.0% on a rolling twelve month basis. Base minimum rent per square foot was up 3.3% y/y and releasing spreads were up 11.2%. We believe many retailers with expansion plans would rather open up shop in quality class A malls like many of Simon's, instead of class B and C malls.

A lot of media focus lately has been given to store closings. We believe the measured re-tenanting and redevelopment of underperforming anchor space could be a good opportunity for mall REITs to grow revenue in the long term and bring different uses to the malls. Management mentioned on the call that they are seeing strong demand for space. SPG is seeing interest from fitness/wellness, food, cosmetic and mixed-use retailers wanting space. The percentage of new leases signed with apparel retailers is lower than in the past.

**Development & Renovation Activity** - Simon opened one open-air luxury shopping center and completed one outlet center expansion in the quarter. Simon has two new outlet centers under development. In addition to these projects, Simon has renovation and expansion plans underway for 31 properties in the U.S. and Canada. We expect management will most likely concentrate its new development efforts on outlet centers in the near future.

**Share Repurchase** - The company did not repurchase any shares during the quarter.

**Financials** - In our opinion, Simon's balance sheet is well positioned. The company has \$1.3 billion of debt maturities in 2017 and \$0.9 billion in 2018, including its share of joint venture debt. Debt (including JV debt) to total market capitalization was 34.3% at September 30, 2017. At September 30, 2017 SPG had more than \$6.5 billion of liquidity.

**Guidance and Estimates** - Management raised the lower end of 2017 FFO per share guidance from a range of \$11.14 to \$11.22 to a range of \$11.17 to \$11.22. Our 2017 FFO per share estimate is \$11.20.

**Quarterly Income Statement**

(in thousands, except per share amounts)	3Q17	3Q16	% Change
Minimum (Base) Rent	\$861,184	\$842,801	2.2%
Overage Rent	36,634	40,089	-8.6%
Tenant Reimbursements	386,713	378,187	2.3%
Management Fees and Other Revenue	28,946	41,721	-30.6%
Other Income	90,161	54,370	65.8%
<b>Total Revenue</b>	<b>1,403,638</b>	<b>1,357,168</b>	<b>3.4%</b>
Property Operating Expenses	118,807	120,099	-1.1%
Real Estate Taxes	111,953	111,727	0.2%
Repairs and Maintenance	25,352	23,178	9.4%
Advertising and Promotion	36,006	35,695	0.9%
Provision (Reversal) for Credit Losses	2,895	(747)	
Home and Regional Office Costs	31,451	41,606	-24.4%
General and Administrative Expenses	13,014	15,154	-14.1%
Impairment Charge			
Transaction Expenses			
Marketable and Non-Marketable Securities Charges and Realized Gains, net			
Other Expenses	57,055	22,508	153.5%
Depreciation and Amortization Expense	317,037	311,757	1.7%
<b>Total Operating Expenses</b>	<b>713,570</b>	<b>680,977</b>	<b>4.8%</b>
<b>Operating Income</b>	<b>690,068</b>	<b>676,191</b>	<b>2.1%</b>
Interest Expense	(199,032)	(214,861)	
Loss on Extinguishment of Debt			
Income Tax Benefit (Expense) on Taxable REIT Subsidiaries	(14,511)	(6,325)	
Income from Unconsolidated Entities	116,110	83,374	39.3%
Impairment Charge from Investments in Unconsolidated Entities			
Gain Upon Acquisition of Controlling Interest, and on Sale or Disposal of Assets, etc.		49,561	
Discontinued Operations			
Discontinued Operations Transaction Expenses			
<b>Consolidated Net Income</b>	<b>592,635</b>	<b>587,940</b>	<b>0.8%</b>
Net Income Attributable to Noncontrolling Interest	78,018	82,362	-5.3%
Preferred Dividends	834	834	0.0%
<b>Net Income</b>	<b>\$513,783</b>	<b>\$504,744</b>	<b>1.8%</b>
<b>Earnings Per Share</b>	<b>\$1.65</b>	<b>\$1.61</b>	<b>2.5%</b>
<b>Avg. Shares Outstanding</b>	<b>310,853</b>	<b>314,234</b>	<b>-1.1%</b>

<b>Funds From Operations</b>	<b>3Q17</b>	<b>3Q16</b>	<b>% Change</b>
Consolidated Net Income	\$592,635	\$587,940	0.8%
Adjustments to Consolidated Net Income to Arrive at FFO:			
Depreciation and Amortization Expense	313,194	308,392	1.6%
Depreciation and Amortization of Unconsolidated Entities	134,998	134,795	0.2%
Impairment Charges of Depreciable Real Estate			
Gain Upon Acquisition of Controlling Interest, on Sale or Disposal of Assets, etc.		(45,162)	
Net Income Attributable to Noncontrolling Interest Holders in Properties	550	(5,361)	
Depreciation and Amortization Attributable to Noncontrolling Interest Holders	(4,605)	(3,271)	
Preferred Distributions and Dividends	(1,313)	(1,313)	
<b>Funds From Operations</b>	<b>\$1,035,459</b>	<b>\$976,020</b>	<b>6.1%</b>
<b>FFO Per Share (diluted)</b>	<b>\$2.89</b>	<b>\$2.70</b>	<b>7.0%</b>
<b>Avg. Shares and Units Outstanding for FFO Calculations</b>	<b>358,116</b>	<b>361,764</b>	<b>-1.0%</b>

Source: Company reports

**Condensed Balance Sheet**

(in thousands)	<b>12/31/2015</b>	<b>12/31/2016</b>	<b>9/30/2017</b>
Investment Properties, at cost	\$33,463,124	\$35,226,089	\$35,925,315
Less - Accumulated Depreciation	9,915,386	10,865,754	11,665,931
<b>Net Investment in Real Estate</b>	<b>\$23,547,738</b>	<b>\$24,360,335</b>	<b>\$24,259,384</b>
Cash and Cash Equivalents	701,134	560,059	508,405
Tenant Receivables and Accrued Revenue, net	624,605	664,619	686,617
Investment in Unconsolidated Entities, at Equity	2,481,574	2,367,583	2,331,538
Investment in Klepierre at Equity	1,943,363	1,797,394	1,907,632
Deferred Costs and Other Assets	1,352,259	1,353,588	1,338,834
Note Receivable from Related Parties			
<b>Total Assets</b>	<b>\$30,650,673</b>	<b>\$31,103,578</b>	<b>\$31,032,410</b>
<b>Mortgage and Other Indebtedness</b>	<b>\$22,502,173</b>	<b>\$22,977,104</b>	<b>\$23,410,357</b>
Accounts Payable and Accrued Expenses	1,323,801	1,214,022	1,290,382
Cash Distributions and Losses in Partnerships and Joint Ventures	1,368,544	1,359,738	1,388,128
Other Liabilities, Minority Interest and Accrued Dividends	214,249	455,040	514,205
<b>Total Liabilities</b>	<b>\$25,408,767</b>	<b>\$26,005,904</b>	<b>\$26,603,072</b>
Commitments and Contingencies			
Limited Partners' Interest in the Operating Partnership			
Limited Partners' Preferred Interest in the Operating Partnership	25,537	137,762	186,732
Series I Convertible Perpetual Preferred Stock			
<b>Stockholders' Equity</b>			
All Series of Preferred Stock			
Series J 8 3/8% Cumulative Redeemable Preferred Stock	43,733	43,405	43,159
Common Stock	31	32	32
Capital in Excess of Par Value	9,384,450	9,523,086	9,597,812
Accumulated Deficit	(4,266,930)	(4,459,387)	(4,776,512)
Other	(252,686)	(114,126)	(111,039)
Common Stock Held in Treasury at Cost	(437,134)	(682,562)	(1,068,310)
<b>Total Stockholders' Equity</b>	<b>\$4,471,464</b>	<b>\$4,310,448</b>	<b>\$3,685,142</b>
Noncontrolling Interest	744,905	649,464	557,464
<b>Total Equity</b>	<b>\$5,216,369</b>	<b>\$4,959,912</b>	<b>\$4,242,606</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$30,650,673</b>	<b>\$31,103,578</b>	<b>\$31,032,410</b>

<b>Balance Sheet Ratio Analysis</b>	<b>12/31/2015</b>	<b>12/31/2016</b>	<b>9/30/2017</b>
Net R/E Investments / Total Debt	104.6%	106.0%	103.6%
Debt to Equity	431.4%	463.3%	551.8%
Debt (including JV debt) to Total Market Capitalization	29.3%	31.6%	34.3%
Debt as % of Total Assets	73.4%	73.9%	75.4%
Shareholders' Equity as % of Total Assets	14.6%	13.9%	11.9%

Previous numbers have not been restated.

Source: Company reports

## Valuation

Currently at 13.4x our 2018 FFO per share estimate of \$12.22, SPG's stock is trading at a premium to its peer group (see table below) and below its five year historic and ten year historic median forward P/FFO multiples. We believe Simon warrants a premium to its peers due to its proven track record, large market capitalization, strong balance sheet, high quality properties, and excellent management team. **We rate the shares Buy with a \$189.00 target price.** We derive our target price by applying a 15.5x multiple (a discount to the company's median 10 and 5 year historic forward price/FFO multiple to account for the current challenging retail environment) to our 2018 FFO per share estimate of \$12.22. We note that the multiple we use is down from our previous multiple of 16.0x due to our view that the negative retail narrative may continue to put pressure on valuations in the near term. We believe our multiple is conservative.

Regional Mall REITs	Symbol	Price	Current	Yield	Payout Ratio	FFO Per Share			2-Year Exp. Avg. Growth	18/17E Growth	Price/FFO	
		10/26/2017	Dividend			2016	2017E	2018E			FY 2017E	FY 2018E
GGP Inc.	GGP	\$20.45	\$0.88	4.3%	55.3%	\$1.57	\$1.59	\$1.66	2.9%	4.4%	12.9x	12.3x
Macerich Company	MAC	\$57.05	\$2.96	5.2%	74.7%	\$5.08	\$3.96	\$4.11	-9.5%	3.8%	14.4x	13.9x
Taubman Centers, Inc.	TCO	\$48.60	\$2.50	5.1%	67.2%	\$2.87	\$3.72	\$3.90	17.9%	4.8%	13.1x	12.5x
CBL & Associates Properties	CBL	\$8.09	\$1.06	13.1%	46.5%	\$2.69	\$2.28	\$2.23	-8.6%	-2.2%	3.5x	3.6x
Peer Average		\$33.55	\$1.85	6.9%	60.9%	\$3.05	\$2.89	\$2.98	0.7%	2.7%	11.0x	10.6x
S&P 500	.SPX	2,560.40	\$49.45	1.9%	37.7%	\$117.75	\$131.03	\$141.07	9.9%	7.7%	19.5x	18.1x
Simon Property Group, Inc.	SPG	\$163.76	\$7.20	4.4%	64.3%	\$10.49	\$11.20	\$12.22	8.2%	8.3%	14.6x	13.4x

Note: GGP and CBL are rated Neutral and Long-term Buy, respectively, by Hilliard Lyons and the rest are not rated. SPX figures are EPS, not FFO per share.

Source: NAREIT, HL Estimates, and Thomson Eikon

## Suitability

We assign shares of Simon Property Group a suitability rating of 2 on our scale of 1 - 4 (1=most conservative, 4=most aggressive). Our rating is based on the company's large market cap and what we view as a strong balance sheet.

## Risks and Considerations

Simon Property Group's FFO may be impacted by external factors beyond the company's control or by internal factors. These risks include, but are not limited to: interest rate risk, inability to secure financing or joint venture partners, a slowing economy, general economic risk, political risk, currency risk, international economic risk, bankruptcy of tenants, store closings, inclement weather and rising materials cost related to developments and redevelopments.

*Additional information is available upon request.*

### **Analyst Certification**

I, Carol L. Kemple, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

### **Important Disclosures**

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

### **Investment Ratings**

**Buy** - We believe the stock has significant total return potential in the coming 12 months.

**Long-term Buy** - We believe the stock is an above average holding in its sector, and expect solid total returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

**Neutral** - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

**Underperform** - We believe the stock is vulnerable to a price set back in the next 12 months.

### **Suitability Ratings**

**1** - A large cap, core holding with a solid history

**2** - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks

**3** - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage

**4** - Speculative, due to small size, inconsistent profitability, erratic revenue, volatility, low trading volume or a narrow customer or product base



Rating	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	39	32%	8%	92%
Hold/Neutral	74	60%	9%	91%
Sell	8	7%	0%	100%
Restriction	2	2%	100%	0%

As of 5 October 2017

### Other Disclosures

Opinions expressed are subject to change without notice and do not take into account the particular investment objectives, financial situation or needs of individual investors. Employees of J.J.B. Hilliard, W.L. Lyons, LLC or its affiliates may, at times, release written or oral commentary, technical analysis or trading strategies that differ from the opinions expressed here.

J.J.B. Hilliard, W.L. Lyons, LLC is a multi-disciplined financial services firm that regularly seeks investment banking assignments and compensation from issuers for services including, but not limited to, acting as an underwriter in an offering or financial advisor in a merger or acquisition, or serving as placement agent in private transactions.

The information herein has been obtained from sources we believe to be reliable but is not guaranteed and does not purport to be a complete statement of all material factors. This is for informational purposes and is not a solicitation of orders to purchase or sell securities. Reproduction is forbidden unless authorized. All rights reserved.