ASX Property Stocks Down Under

> *Private property was the original source of freedom. It is still its main bulwark.*

- Walter Lippmann (1889-1974), Journalist and philosopher

GOODMAN GROUP

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Stocks Down Under rating: ★★

ASX: GMG
Market cap: A$41.5BN

52-week range: A$16.37 / A$26.96
Share price: A$22.27

Back in 2020, if you wanted to tap into the eCommerce boom without the risk of investing in a company still making losses, Goodman Group (ASX: GMG) was probably the best vehicle. It is a property stock that owns and leases industrial properties, such as logistics facilities, warehouses and office parks. While other eCommerce companies, such as Kogan (ASX: KGN), became multi baggers, only to lose ground, Goodman is still up nearly 40% in two years. But is it still worth the premium?

Share price chart

Source: Tradingview

The ASX's biggest property stock

Goodman Group listed on the ASX in 2005 at $2 per share. After shedding over half its value during the GFC and consolidating its shares in 2012, the company recovered and has gained over 200% in 5 years. With a market capitalisation of over $40 billion, it is the top Property stock on the ASX and is among the Top 15 ASX 200 companies. Goodman's portfolio has increased substantially in recent years and so has its share price. Property revaluations, new developments and most importantly, the growth in demand for eCommerce and logistics facilities have all been catalysts for the company's growth.

Goodman has $68.2 billion in total Assets Under Management (AUM) - a figure that has nearly doubled since FY18 - and has another $12.7bn in developments. It has properties globally, but the bulk of properties ($50.7bn) are in Australia, New Zealand and the Asia-Pacific region. Its top global customer by net income is Amazon is 11.4%. Amazon-operated assets owned by Goodman include fulfillment centres at Lytton in Brisbane and Oakdale West Industrial Estate in Sydney's west – the latter being the largest warehouse in Australia. Other top customers include Coles, Australia Post, FedEx, JD, DHL and Global Express.

The right place at the right time

Demand for logistics facilities had been growing before COVID-19, but the closure of brick-and-mortar stores due to the pandemic was the catalyst for demand to take off exponentially. Goodman couldn't have picked a better space to be in when the pandemic began. Many other ASX property stocks, particularly companies leasing office or discretionary retail space, were hit by COVID-19 restrictions as tenants were forced to cease or scale back operations due to lockdowns and apply for rent relief or deferrals.

But for most of Goodman's facilities, it was business as usual, not having to either close its facilities or give rent relief to tenants, so its cash flow remained steady. Goodman also benefited from uplifts in the valuation of its properties driven by record low interest rates and market demand for industrial properties.

In FY20, the company made a statutory profit of $1.5bn, operating earnings per share (EPS) of 57.5 cents and a payout of 30 cents per share. In FY21, Goodman's statutory profit was $2.3bn, its EPS was 65.6 cents and the shareholder payout was 30 cents a share. The company maintained 98.1% occupancy and like-for-like net property income growth of 3.2%. FY21 was also a positive year from an ESG standpoint. The company achieved carbon neutrality across its global operations – four years ahead of schedule – and significantly increased its reliance on renewable energy.

Caught up in the eCommerce and REIT sell off

After hitting an all-time high in December 2021, Goodman dropped 13% in January. This fall was roughly in line with the S&P/ASX 200 A-REIT Index as fears about inflation and the prospect of rising interest rates hit the market. Investors fear that rising interest rates will increase the cost of debt and slow the pace of asset valuation increases.

We also note that many eCommerce companies, such as Kogan (ASX: KGN) and Redbubble (ASX: RBL), have been under siege for several months because of slowing growth rates. It's not that these companies' growth has stopped, but the growth is lower than in 2020 when consumers flocked en-masse to these companies almost overnight. And moderating growth rates have made investors particularly concerned about companies that are not profitable or have low margins.

Goodman's half yearly results on February 17 caused a brief share price spark, but the company finished that week lower than it began. This was despite the company recording a statutory profit of ~$2bn with operating EPS 27% higher and AUM 32% higher compared to the prior corresponding period.

Is it a bargain now?

Goodman Group is different to non-profitable growth companies, being an FFO positive property trust, but we are concerned about its high valuation. Even with the recent drop in the share price, Goodman is trading at just under triple its NTA and it's trailing P/FFO is over 30x. Meanwhile, its peers Centuria Industrial REIT (ASX: CIP) and Dexus Industrial REIT (ASX: DXI) are trading at discounts to their NTAs and are at a trailing P/FFO of 21.4x and 15.7x, respectively.

We admit Goodman deserves a premium and has more income streams than just rent as it manages and develops property too and has no need to acquire further assets with $12.7bn in the pipeline. But in a rising interest rate environment it is difficult to see Goodman worth the substantial premium it trades at right now.

The last two times we covered Goodman Group, on 28 February 2020 and 3 March 2021, we awarded the company four stars and that has worked out quite well. In both instances, we thought the company had growth catalysts to keep its share price going – record low interest rates, soaring property valuations and a rapid adoption of eCommerce with a consequential need for logistics space.

We can still see the growth catalysts, but this time, we are not so sure these will be as powerful as they were in 2020. Goodman is still a good property stock with an attractive niche, but unfortunately is a bit too expensive to justify four stars again. On top of that, the stock has broken the long term share price uptrend on 17 February when the company reported its 1HY22 results. We believe this may be the start of ongoing share price weakness ahead. So, third time is not a charm. It's two stars for Goodman Group this time around.

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