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SIZING UP SMALL-CAPS

This Manufactured-Home Stock Could Ride the Housing Shortage Higher

It's a good time to be in the business of building and renting affordable homes, and UMH Properties' shares are cheap, relative to its peers

By Carleton English

Illustration by Iker Ayestaran

Good luck finding a deal on a home these days—but there are still some to be had in housing stocks. Shares of UMH Properties, an owner and operator of manufactured-home communities, looks like one of them.

Prices have soared 19.5% from a year ago, according to the S&P CoreLogic Case-Shiller Home Price Indices, while the U.S. faces an estimated shortage of five million homes, according to recent research from Realtor.com. For many Americans, even saving up for a down payment can be daunting.

That's where UMH Properties (ticker: UMH) comes in. The New Jersey–based company is a real estate investment trust that owns 127 manufactured-home communities in 10 states, primarily in the Northeast and Southeast. It makes money from selling and renting manufactured homes—essentially, factory-built houses—with units selling for roughly twice the local annual income in areas where houses can cost more than seven times a year's pay. That comes to about $60,000 to buy, or $800 a month to rent.

It's a good time to be in the business of selling affordable homes. The Biden administration has made tackling sky-high housing costs a priority. In September, the White House said that it would like to increase the supply of manufactured housing by expanding financing through Freddie Mac, while also calling on state and local governments to ease zoning restrictions on manufactured housing.

It's also an issue that both Democrats and Republicans agree is worth addressing. There are currently two bills in Congress that would provide assistance to first-time home buyers. One promises $25,000 in direct payments to buyers, and the second offers a $15,000 tax credit. While the bills have yet to pass, UMH is hopeful.

"It would be huge for us," UMH CEO Sam Landy told Barron's. "The biggest hurdle is the down payment, and you have just made a huge group of people eligible."

UMH isn't the only REIT playing

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in the manufactured-housing space. Equity LifeStyle Properties (ELS), Cavco Industries (CVCO), and Sun Communities (SUI) should also benefit as such housing becomes more accepted. But UMH, with a market cap that just crossed $1 billion, is the smallest, and its stock just might have the most upside, despite having already gained 58% this year.

First, its shares are cheap, at least relative to its peers. It currently trades at 23 times forward funds from operations—REITs' preferred measure of operating earnings—of $1.01 per share, while Equity LifeStyle and Sun trade at 31 times and 27 times, respectively. At the same time, UMH pays a dividend of 76 cents, while yielding 3.2%, roughly double that of peers. (REITs are required to pay out at least 90% of their profits to shareholders as dividends.)

The lower valuation can be blamed on UMH's occupancy rate. Just 86% of its properties have tenants, lagging behind peers, which have occupancy rates of about 94%. The difference can be ascribed to UMH's business model, which involves buying under-occupied sites at steep discounts and rehabbing existing manufactured units or installing its own, and then filling them with occupants. While the process is easier than starting from scratch—and obtaining the necessary zoning approvals—it's not quite turnkey for getting occupants in immediately, meaning that, for a few years, the properties may lose money.

UMH Properties

REIT and Home Manufacturer

Headquarters: Freehold, N.J.	
Recent Price: $23.41	
YTD Change: 58%	
Market Value (bil): $1.1	
2022E Sales (mil): $206	
2022E Net Operating Income (mil): $101	
2022E FFO: $1.01	
2022E P/FFO: 23.1	
Dividend Yield: 3.2%	

E=estimate; FFO=funds from operations

Source: FactSet

But the gap in occupancy rates also shows that UMH has room for improvement that its competitors lack. "UMH has significantly lower occupancy, which means low-hanging fruit on the upside," says Robert Stevenson, managing director at Janney Montgomery Scott.

Soaring housing prices have raised concerns that the real estate market has become overheated. That's still up for debate, but even if it has, UMH should be able to weather a downturn better than other housing stocks. "It's not luxury housing," says David Schawel, chief investment officer at Family Management, a financial advisory firm in New York. "If there's an economic pullback, they are not going to be hit as much."

UMH stock could also get a boost from a little bit of financial engineering. The company has two sets of preferred shares coming due, one in 2022 and the other in 2023, and UMH plans to refinance them at a lower rate in light of its improved access to financing. In an earnings call last month, management speculated that reducing its cost of capital could improve the company's performance by $0.20 to $0.30 per share.

The company also maintains a portfolio of publicly traded REIT securities, and one of its largest holdings, Monmouth Real Estate Investment (MNR), announced in November that it would be acquired by Industrial Logistics Properties Trust (ILPT) for $4 billion. The deal is expected to close in the first half of 2022. The extra cash could be reinvested or used to fund acquisitions, says Janney's Stevenson.

Add it all up and UMH Properties seems like a good place for investors to call home.