

Zacks Small-Cap Research

Sponsored – Impartial - Comprehensive

M. Marin
312-265-9211
mmarin@zacks.com

scr.zacks.com

10 S. Riverside Plaza, Chicago, IL 60606

Tejon Ranch (TRC-NYSE)

TRC: Believe Expanded JV Validates Development Strategy & Enhances Value of TRC's Real Estate Assets

Tejon Ranch Company is a real estate-development company that targets maximizing shareholder value by monetizing its land-based assets located near Los Angeles and Bakersfield, CA, where housing demand is high and availability of Class A properties is limited.

OUTLOOK

TRC announced yesterday it has started construction of an industrial building at the TRCC that is planned to be roughly 630,000-square-feet. The company is developing this building with joint venture partner Los Angeles-headquartered Majestic Realty. According to *National Real Estate Investor* magazine, Majestic is one of the country's largest privately-held industrial developers. We view it as a positive that this project represents an expansion of an existing relationship between TRC and Majestic, which would seem to underscore Majestic's positive view of the TRCC's development prospects.

Current Price (7/8/21) \$14.89
Valuation \$25.00

SUMMARY DATA

52-Week High \$17.90
52-Week Low \$13.44
One-Year Return (%) 7.98
Beta 0.56
Average Daily Volume (sh) 134,023

Shares Outstanding (mil) 26
Market Capitalization (\$mil) \$392
Short Interest Ratio (days) N/A
Institutional Ownership (%) 69
Insider Ownership (%) 21

Annual Cash Dividend \$0.00
Dividend Yield (%) 0.00

5-Yr. Historical Growth Rates
Sales (%) 0.7
Earnings Per Share (%) 48.0
Dividend (%) N/A

P/E using TTM EPS N/A
P/S using 2021 Estimate N/A
P/S using 2022 Estimate N/A

Zacks Rank N/A

Risk Level Low,
Type of Stock Small-Value
Industry Real Estate Ops

ZACKS ESTIMATES

Revenue

(in millions of \$)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2018	\$13.5A	\$5.1A	\$15.4A	\$11.6A	\$45.6A
2019	\$10.7A	\$8.9A	\$9.7A	\$20.3A	\$49.5A
2020	\$10.3A	\$4.8A	\$13.5A	\$9.2A	\$37.8A
2021	\$11.1A	\$4.8E	\$13.7E	\$9.4E	\$40.0E

EPS / Loss Per share

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2018	\$0.06A	-\$0.04A	\$0.13A	\$0.01A	\$0.16A
2019	\$0.00A	\$0.03A	\$0.00A	\$0.37A	\$0.40A
2020	-\$0.03A	-\$0.01A	\$0.02A	-\$0.00A	-\$0.03A
2021	-\$0.04A	-\$0.03E	\$0.02E	-\$0.01E	-\$0.06E

Quarters might not add to annual reflecting rounding

Disclosures on page 10.

WHAT'S NEW? KEY POINTS

- TRC announced yesterday it has started construction of an industrial building at the TRCC that is planned to be roughly 630,000-square-feet. The company is developing this building with a joint venture partner, Los Angeles-headquartered Majestic Realty, which is one of the country's largest privately-held industrial developers, according to *National Real Estate Investor* magazine.
- We view it as a positive that this project represents an expansion of an existing relationship between TRC and Majestic, which would seem to underscore Majestic's positive view of the TRCC's development prospects. The project represents the third new building and fourth JV partnership agreement TRC has entered into with Majestic over the past five years.
- Proximity to nearby cities makes the TRCC an attractive location. The site of the planned new building is roughly 39-acres fronting the I-5 (interstate 5) highway, one of the busiest land-based transportation routes for passengers and cargo.
- We view the latest planned development as another positive that is not fully reflected in the TRC share price.
- With cash and equivalents and marketable securities of \$52.3 million at the end of 1Q21 and a commitment to conserving capital if the pandemic continues to constrain revenue, the company remains well-capitalized. The company also reduced long-term debt to \$51.5 million at the end of March 2021, from \$57.5 million at year-end 2019.

VIEW EXPANDED JV WITH MAJOR DEVELOPER AS A POSITIVE

Tejon Ranch Company (NYSE:TRC) announced yesterday it has started construction of an industrial building at the Tejon Ranch Commerce Center (TRCC) that is planned to be roughly 630,000-square-feet. The company is developing this building with a joint venture partner, Los Angeles-headquartered Majestic Realty. Majestic Realty is one of the country's largest privately-held industrial developers, according to *National Real Estate Investor* magazine. Originally established in 1948, Majestic has a long operating history. Moreover, as it is based in Los Angeles County, it seems likely that Majestic understands and has extensive relationships in TRCC's local real estate market.

We also view it as a positive that this project represents an expansion of an existing relationship between TRC and Majestic. Their initial partnership agreement was formed in 2016 to jointly purchase, own and manage an existing, fully leased, 651,909- square-foot building. The two JV partners then added two additional new build partnerships for speculative buildings that each generated strong pre-lease activity and which remain fully leased. This latest extension of their JV relationship would seem to underscore Majestic's positive view of TRCC's development prospects. The project represents the third new building and fourth JV partnership agreement TRC has entered into with Majestic over the past five years.

Proximity & Access to I-5 & Other Highways / Rail Make TRCC Attractive & Convenient

Proximity to nearby cities makes the TRCC an attractive location. The site of the planned new building is roughly 39-acres fronting the I-5 (interstate 5) highway, one of the busiest land-based transportation routes for passengers and cargo. The construction site will enable occupants to have easy access to the principal north-south goods movement corridor of the west coast, as well as connection to both I-15 and I-40 east-west corridors by using state highway 58.

TRC's extensive land holdings are located approximately 60 miles north of Los Angeles and 25 miles south of Bakersfield, California. Reflecting proximity to these major cities and to nearby highways –

Interstate 5, for instance – it takes about 75 minutes to travel from the TRCC to Los Angeles' Union Station. It is roughly an hour by car from Santa Clarita.



Source: <http://ir.tejonranch.com/>

Most of the ranch is bordered by Highway 138 on the south, Interstate 5 and Highway 99 on the west, and Highway 223 on the north. I5 is the major (and in places the only) conduit from the Los Angeles basin north and onto the Central Valley. The ranch is bounded by the southern San Joaquin valley, the Tehachapi Mountains and Antelope valley. Given the location and proximity to nearby cities, it is well-positioned to be an important distribution point for commercial traffic for both south bound and north bound traffic.

Moreover, the anticipated continued development of the California High-Speed [Rail](#) is also expected to facilitate commuting from TRCC to nearby cities. The California High-Speed Rail Authority has nearly 120 miles under construction, with more construction extensions anticipated. The Authority plans “a state-wide rail modernization” program that will help traverse one of the country’s largest states, mitigating automobile congestion and pollution. The Authority recently completed five high-speed rail structures throughout Madera, Fresno, and Kern counties.

Occupancy, Expected by Mid-2022, Likely Boosted by Relative Scarcity of Class A Properties

The approximately 630k-square-foot Class A industrial building is being designed for single- or multi-tenant use and will be constructed on a speculative basis. The JV partners believe the market for Class A space is highly competitive, reflecting limited inventory.

In general, prospective tenants have shown significant interest in the region’s limited inventory and in the TRCC, reflecting the location, Class-A product and economic incentives offered by Kern County, according to TRC. In fact, the company believes the TRCC represents a substantially more cost economical option compared to other properties in the L.A. basin. Moreover, management also believes

interest in TRCC has increased as a result of changing views of warehousing safety stock, as a result of disruptions to much of the general supply chain during the pandemic.

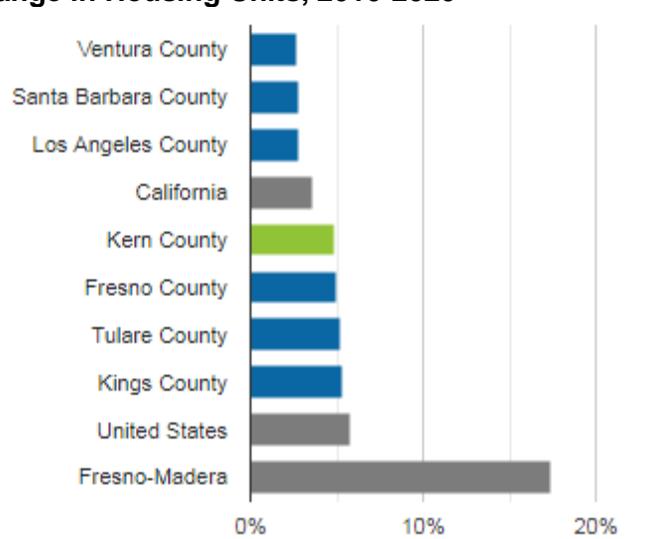
The JV partners expect the building to be ready for occupancy by mid-2022. The [TRCC](#) has a track record of delivering speedy turnaround on construction.

ADDRESSING CALIFORNIA'S HOUSING NEED

Another Project TRC Announced Recently Will Help Address Kern County Housing Shortage

The announcement of this new project follows TRC's recent [approval](#) to develop multi-family apartments within the Tejon Ranch Commerce Center (TRCC). The planned apartment development will help provide much-needed housing. Like much of the state of California, Kern County is experiencing a severe shortage of housing, including of apartment units. Construction of new units has lagged compared to many other areas within the state and the slow pace of development exacerbates the housing shortage problem. Moreover, a majority of California land is zoned for single-family or commercial use, while private home owners often oppose nearby construction of apartments. In 2019, a report from the [California Housing Partnership](#) estimated that Kern County needed an additional 26,200+ affordable rental units to meet its housing shortage.

Change in Housing Units, 2010-2020



2020 Census Bureau American Community Survey - Accessed on January 10, 2021

There is a shortage of housing in the greater Los Angeles metropolitan region overall, just as there is in the state generally. By historical measures, new and used house inventory is virtually non-existent. Reflecting the imbalance between supply (inventory) and demand, housing prices continue to increase. TRC is the only major area close to Los Angeles where infrastructure is possible and one of the few real estate development companies with scale.

The state's housing shortage is highlighted in recent proposed legislation in front of the California regulators. [Senate Bill-50](#) notes that the "lack of housing, including emergency shelters, is a critical problem that threatens the economic, environmental, and social quality of life in California." TRC is the only nearby land area with sufficient land and scale to help address the state's housing shortage in any meaningful way, as noted.

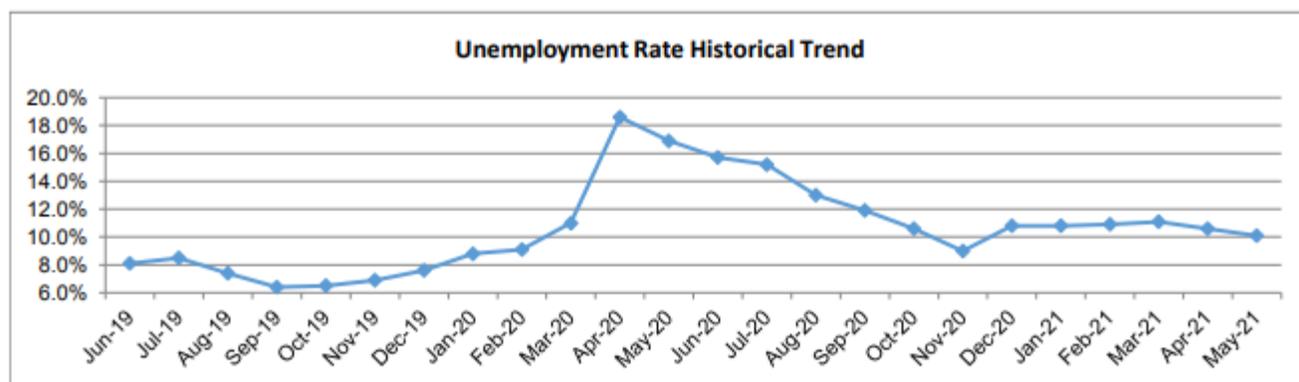
The recently granted Kern County approvals authorize TRC to develop up to a maximum of 495 multi-family residences in thirteen apartment buildings just north of the Outlets at Tejon. The development is also approved to include about 6,500 square feet of amenity space to serve the community and 8,000 square feet of revenue-generating retail space on the ground floor of some of the residential buildings.

DEVELOPMENT EFFORTS CREATE MUCH NEEDED NEW JOBS

Permanent jobs and development-related employment

The company's development efforts will also create both permanent and development-related jobs. Centennial, for instance, is expected to create more than 23,000 permanent jobs on site and nearly 25,000 construction jobs.

The company's land assets are located in an area that is characterized by high unemployment, which appears to be supported by recent government employment data. For instance, the Kern County unemployment rate was 11.1% in March 2021, up from 10.9% in February 2021 and above an unadjusted unemployment rate of 8.2% for the state of California, according to the California [Labor Market Information Division](#). At 10.1%, the Kern County unemployment rate during the month of May 2021 was higher than the 5.8% U.S. national unemployment rate during the same period, according to data from the Bureau of Labor Statistics ([BLS](#)) and State of California Employment Development Department.



Source: [https://www.labormarketinfo.edd.ca.gov/file/lfmonth/bake\\$pds.pdf](https://www.labormarketinfo.edd.ca.gov/file/lfmonth/bake$pds.pdf) accessed July 2021

VALUATION

We view the latest planned development as another positive that is not fully reflected in the TRC share price. Tejon Ranch is in the early stages of its real estate development plans, which makes the use of certain traditional valuation methods such as P/E, multiple of cash flow or a dividend discount model, among other methods, inappropriate. Book value, for example, does not reflect the value of the land once development plans are further along.

We believe TRC shares should be valued on a price-to-acre basis. With the aforementioned shortage of housing in the state, we do not believe the current share price accurately reflects the potential value of the real estate once development plans are more advanced.

TRC owns 270,000 acres. At the current price of TRC shares, this equates to a valuation of about \$1,400 per acre. This is down from a valuation range of about \$2,200 to \$3,800 for TRC in recent years and significantly below nearby relative land values.

For instance, according to the Federal Housing Finance Agency, the average land value per acre for *residential* land in the state of California exceeds \$400,000. Given that TRC's asset is largely undeveloped except for TRCC and that the Federal Housing Finance Agency's metric includes expensive urban cities such as San Francisco and Los Angeles that drive the state average up, we would not expect TRC to command a similar valuation at this point. Nevertheless, we believe it points to just how under-valued TRC is, as reflected in the current share price. Measured on a price-to-acre basis, TRC even falls below California *farm* values, which command average valuations of about \$10,000 per acre, according to the USDA.

TRC initiatives discussed in this report and other recent updates increase the value of TRC's land holdings, in our view. Our \$25 per share valuation implies a valuation of just over \$2,400 per acre, which represents a substantial discount to the valuations implied by other real estate valuations noted above. Even based on *only* the land that has been approved for development and/or is currently producing revenue from agribusiness and other operations (which we think understates TRC's potential), the \$25/share expected near-term valuation implies a value of less than \$8,400 per acre, a steep discount to the above-noted average \$10,000 based on USDA data and only a fraction of the value accorded residential property within the state.

We also expect the value of land to increase significantly, and of TRC shares, as TRC continues to advance its development plans. We also expect multiple expansion on TRC shares as the company hits certain milestones in its development objectives.

Potential Funding Sources

As noted, the new project is being constructed on a speculative basis. As with the company's other planned projects, potential capital funding sources for development this industrial building and of the recently authorized apartment units include possible joint ventures with financial partners, debt financing and/or the sale of rights, among other sources. Moreover, TRC's agribusiness and commerce business units are operational and generate recurring revenue.

TRC ended 1Q21 with cash & equivalents and marketable securities of \$52.3 million. The company also has a commitment to conserving capital if the pandemic continues to constrain revenue. The company also reduced long-term debt to \$51.5 million at the end of March 2021, from \$57.5 million at year-end 2019.

RISKS

Risks to TRC achieving its objectives, and to our valuation, include the following.

- With COVID-19 cases rising in several places, we believe TRC and many companies face the risk of another economic shut down.
- The real estate development industry is highly capital intensive. TRC might not find funding sources at the rates it expects or as soon as it expects.
- The company is subject to regulatory risk. Real estate development is subject to various land use regulations that require governmental approvals and permits and potential regulatory changes could impact TRC.

- The value of the land could fluctuate depending on several factors, including the regional economy and other competing development plans by other developers.
- The I-5 is a critical part of the TRC infrastructure and traffic / roadway congestion could impact the value of the company's land.
- The area outside of the Tejon Ranch lacks infrastructure to support homeowners.
- TRC could be vulnerable to litigation risk that could impede growth.
- Water rights are often an issue in California and can impact land values. TRC has complex water agreements and both buys and sells water.
- The company's agribusiness operation is cyclical and affected by commodity cycles, especially those involving almond, pistachio, walnut, and wine grape production. The business is also highly seasonal, with the second half of the calendar year usually generating more revenue than the first due to weather and harvest conditions.
- Timing of development in the coming years will be dependent on the strength of both the economy and the residential real estate market.

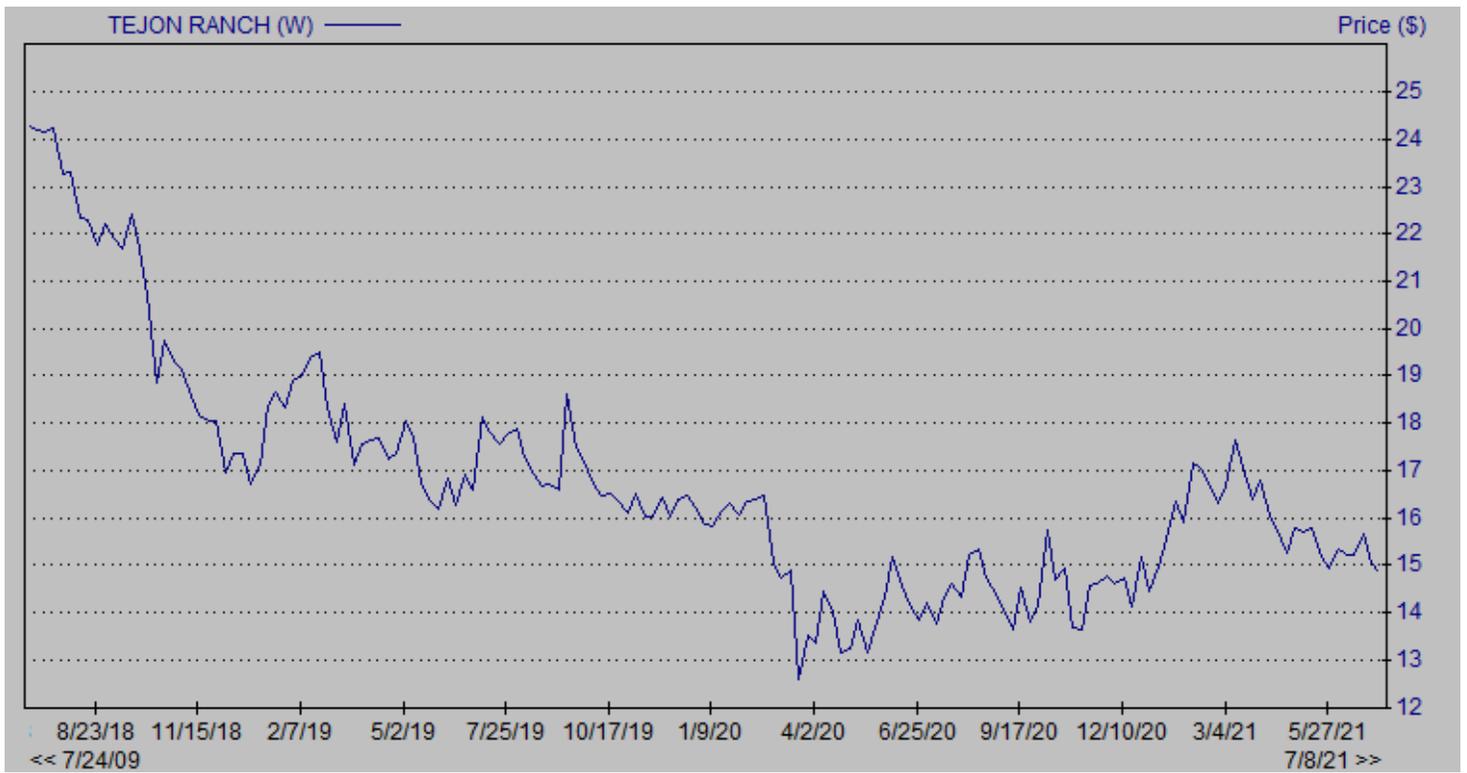
PROJECTED INCOME STATEMENT

Tejon Ranch Income Statement & Projections (\$000)

	2017	2018	1Q19	2Q19	3Q19	4Q19	2019	1Q20	2Q20	3Q20A	4Q20A	2020A	1Q21A	2Q21	3Q21	4Q21	2021E
Real estate - commercial/industrial	\$9,001	\$8,970	\$2,826	\$6,595	\$2,620	\$4,751	\$16,792	\$2,320	\$2,114	\$2,710	\$2,392	\$9,536	\$2,228	\$2,135	\$2,737	\$2,397	\$9,497
Mineral resources	5,983	14,395	6,132	660	1,559	1,440	9,791	6,178	1,776	1,322	1,460	10,736	7,176	1,794	1,401	1,562	11,933
Farming	16,434	18,563	815	886	4,602	13,028	19,331	952	209	8,537	4,168	13,866	607	211	8,622	4,210	13,650
Ranch operations	3,837	3,691	889	805	876	1,039	3,609	863	676	944	1,209	3,692	1,043	683	953	1,221	3,900
Total revenues	35,255	45,619	10,662	8,946	9,657	20,258	49,523	10,313	4,775	13,513	9,229	37,830	11,054	4,823	13,714	9,390	38,981
							\$3,831										
Real estate - commercial/industrial	6,529	6,246	1,792	4,593	1,968	4,608	12,961	1,931	1,747	2,026	1,418	7,122	1,552	1,764	2,046	1,432	6,795
Real estate - resort/residential	1,955	1,530	648	642	582	375	2,247	626	326	273	387	1,612	553	329	276	391	1,549
Mineral resources	2,964	6,223	3,832	598	576	812	5,818	3,878	714	648	1,174	6,414	5,047	721	654	1,186	7,608
Farming	16,201	16,028	1,598	825	5,979	6,849	15,251	1,702	1,099	8,108	4,194	15,103	1,478	1,110	8,189	4,236	15,013
Ranch operations	5,411	5,451	1,350	1,393	1,260	1,313	5,316	1,406	1,178	1,164	1,148	4,896	1,187	1,190	1,176	1,159	4,712
Corporate expenses	9,713	9,705	2,474	2,290	1,760	2,837	9,361	2,533	2,494	2,121	2,282	9,430	2,291	2,519	2,142	2,305	9,257
Total expenses	42,773	45,183	11,694	10,341	12,125	16,794	50,954	12,076	7,558	14,340	10,603	44,577	12,108	7,634	14,483	10,709	44,934
Operating loss	(7,518)	436	(1,032)	(1,395)	(2,468)	3,464	(1,431)	(1,763)	(2,783)	(827)	(1,374)	(6,747)	(1,054)	(2,811)	(769)	(1,320)	(5,954)
Investment income	462	1,344	349	329	294	267	1,239	228	151	455	50	884	7	153	460	51	670
Gain (loss) real estate sales				-	-				1,333	(2)	-	1,331	-	-	-	-	-
Other (loss) income	(275)	(59)	26	22	19	(1,891)	(1,824)	8	(12)	68	46	110	64	(12)	69	46	167
Total other income	187	1,285	375	351	313	(1,624)	(585)	236	1,472	521	96	2,325	71	140	528	97	837
Operating income/(loss)	(7,331)	1,721	(657)	(1,044)	(2,155)	1,840	(2,016)	(1,527)	(1,311)	(306)	(1,278)	(4,422)	(983)	(2,670)	(241)	(1,223)	(5,117)
Equity pickup	4,227	3,834	876	1,971	2,199	11,529	16,575	1,355	1,181	1,093	875	4,504	(59)	1,193	1,104	963	3,200
Pretax income	(3,104)	5,555	219	927	44	13,369	14,559	(172)	(130)	787	(403)	82	(1,042)	(1,478)	863	(260)	(1,917)
Taxes	(1,283)	1,320	95	218	7	3,660	3,980	512	196	403	(282)	829	21	(399)	233	(70)	(215)
Net income (loss)	(1,821)	4,235	124	709	37	9,709	10,579	(684)	(326)	384	(121)	(747)	(1,063)	(1,079)	630	(190)	(1,702)
Minority interest	(24)	(20)	5	2	(10)	2	(1)	(2)	7	(14)	2	(7)	(8)	(1)	(1)	(1)	(11)
Net income	(1,797)	4,255	119	707	47	9,707	10,580	(682)	(333)	398	(123)	(740)	(1,055)	(1,078)	631	(189)	(1,691)
Loss/share - EPS (FD)	(\$0.08)	\$0.16	\$0.00	\$0.03	\$0.00	\$0.37	\$0.40	(\$0.03)	(\$0.01)	\$0.02	(\$0.00)	(\$0.03)	(\$0.04)	(\$0.03)	\$0.02	(\$0.01)	(\$0.06)
Average shares out (Mns)	21.7	26.0	26.0	26.0	26.2	26.2	26.1	26.3	26.2	26.3	26.4	26.3	26.4	26.5	26.5	26.6	26.5

Source: Company reports, Zacks estimates

HISTORICAL STOCK PRICE



DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, M. Marin, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered to be reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESTMENT BANKING AND FEES FOR SERVICES

Zacks SCR does not provide investment banking services nor has it received compensation for investment banking services from the issuers of the securities covered in this report or article.

Zacks SCR has received compensation from the issuer directly, from an investment manager, or from an investor relations consulting firm engaged by the issuer for providing non-investment banking services to this issuer and expects to receive additional compensation for such non-investment banking services provided to this issuer. The non-investment banking services provided to the issuer includes the preparation of this report, investor relations services, investment software, financial database analysis, organization of non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per-client basis and are subject to the number and types of services contracted. Fees typically range between ten thousand and fifty thousand dollars per annum. Details of fees paid by this issuer are available upon request.

POLICY DISCLOSURES

This report provides an objective valuation of the issuer today and expected valuations of the issuer at various future dates based on applying standard investment valuation methodologies to the revenue and EPS forecasts made by the SCR Analyst of the issuer's business.

SCR Analysts are restricted from holding or trading securities in the issuers that they cover. ZIR and Zacks SCR do not make a market in any security followed by SCR nor do they act as dealers in these securities. Each Zacks SCR Analyst has full discretion over the valuation of the issuer included in this report based on his or her own due diligence. SCR Analysts are paid based on the number of companies they cover. SCR Analyst compensation is not, was not, nor will be, directly or indirectly, related to the specific valuations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports and articles are based on data obtained from sources that it believes to be reliable, but are not guaranteed to be accurate nor do they purport to be complete. Because of individual financial or investment objectives and/or financial circumstances, this report or article should not be construed as advice designed to meet the particular investment needs of any investor. Investing involves risk. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports or articles or tweets are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.

CANADIAN COVERAGE

This research report is a product of Zacks SCR and prepared by a research analyst who is employed by or is a consultant to Zacks SCR. The research analyst preparing the research report is resident outside of Canada, and is not an associated person of any Canadian registered adviser and/or dealer. Therefore, the analyst is not subject to supervision by a Canadian registered adviser and/or dealer, and is not required to satisfy the regulatory licensing requirements of any Canadian provincial securities regulators, the Investment Industry Regulatory Organization of Canada and is not required to otherwise comply with Canadian rules or regulations.