



ISTAR FINANCIAL INC.

HOLD

Stock Data

Price (52 weeks)	\$33.43 - \$44.91
Symbol/Exchange	SFI/NYSE
Beta	0.5
Dividend yield	2.79 %
Fully diluted shares	111.38M
Average daily volume	277,286
Current market cap	4.92B
Book Value/Share	\$22.36

Valuation (per share)

DDM (Beta 0.5, Growth 2.5%)	\$53.20
DDM (Beta 0.3, Growth 3%)	\$82.70



Business Overview

iStar Financial Inc., founded in 1993, is the leading publicly traded finance company focusing on the commercial real estate industry and is taxed as a Real Estate Investment Trust (REIT). The REIT industry is a \$150 billion niche in the \$2 trillion real estate industry.

The trust provides structured finance to private and corporate owners of real estate nationwide, including senior and junior level mortgage debt, mezzanine and subordinated capital, and net lease financing through its origination, acquisition and servicing platform. iStar works mostly with businesses with portfolios composed of office buildings, multifamily real estate, hotels, malls, warehouses, distribution facilities, and other properties.

Business Divisions

iStar has 5 main business divisions. Combined, these divisions create a portfolio worth \$7.2 billion as of September 30th, 2004.

Corporate Tenant Leasing (45% of Portfolio): Corporate tenant transactions range from \$20 to \$200 MM and provide capital to corporations, as well as to borrowers who control properties leased to single creditworthy tenants. iStar's net leased facilities are typically subject to long-term leases with rated corporate credit tenants, and provide for all expenses at the property to be paid by the tenant on a triple net lease basis.

Structured Finance (24% of portfolio): Structured finance provides loans ranging from \$20 to \$100 MM to borrowers controlling institutional quality real estate. It is possible for these loans to be fixed or floating rate and are structured to meet specific financing needs of the borrowers, including acquisitions, financing, repositioning or construction of large, high quality real estate. A wide range of structured finance options including first mortgages, second mortgages, partnership loans, participation debt and interim/bridge facilities are offered to the borrowers.

Portfolio Finance (14% of portfolio): Portfolio finance provides loans ranging from \$25 to \$150 MM to borrowers that own multiple properties. Loans are cross collateralized to give borrowers the benefits of all available collateral and underwritten to recognize inherent portfolio diversification. Property types can include multifamily, suburban office, all-suite, extended stay, and full service hotels and other property types where individual property values are less than \$20 MM on average.

Corporate Finance (10% of portfolio): Corporate finance transactions range from \$20 to \$150 MM and provide senior and subordinated capital to corporations engaged in real estate or real estate related businesses. Financing may be either secured or unsecured. Transactions include privatization and other acquisition financings, recapitalizations, and private investments in public companies.

Loan Acquisitions (7% of portfolio): Acquired loans range from \$5 to \$100 MM. iStar acquires loans and loan participations that present attractive risk-reward opportunities. These loans are collateralized by real estate and are generally acquired at a discount to the principal balance outstanding.

Insider Trading

There have been no insider transactions in the last six months. The last insider transaction took place in April 2004 when Matthew Lustig, a director for iStar, acquired 546,000 shares at \$34.35.

Comparables Analysis

The principle advantage to investment in REITs is the dividend income. In order to give a broader picture of the variety of REITs on the market and the different dividend yields offered, included below is a description of three competitors of iStar and their relevant comparative stats.

American Mortgage Acceptance Company (AMC): American Mortgage Acceptance Company is a real estate investment trust whose business plan focuses on originating and acquiring mortgages secured by multi-family properties which may take the form of government insured first mortgages, insured mortgage pass-through certificates or insured mortgage backed securities and uninsured mezzanine loans, construction loans and bridge loans. In addition, the Company has indirectly invested in subordinate commercial mortgage-backed securities and may invest in other real estate assets including non-multifamily mortgages. It also issues guarantees of construction and permanent financing and makes standby loan commitments.

Annaly Mortgage Management, Inc. (NLY): Annaly Mortgage Management, Inc. is a real estate investment trust that owns and manages a portfolio of mortgage-backed securities and agency debentures. The Company is primarily engaged in the business of investing, on a leveraged basis, in mortgage pass-through certificates, collateralized mortgage obligations (CMOs) and other securities representing interests in or obligations backed by pools of mortgage loans. It also invests in agency debentures. The Company principally aims to generate net income for distribution to its stockholders from the spread between the interest income on its investment securities and the costs of borrowing to finance its acquisition of investment securities. In June 2004, the Company acquired Fixed Income Discount Advisory Company, a registered investment advisor.

Redwood Trust, Inc. (RWT): Redwood Trust, Inc. is a financial institution that invests in real estate loans. The Company invests in residential real estate loans in the United States. It also invests in real estate loan securities created from these loans. The Company's investments consist of residential real estate loans, securities backed by residential real estate loans and various other diverse residential and commercial real estate loan securities such as commercial real estate loans. The Company's four real estate loan investments are the residential real estate loans, the residential real estate loan credit-

enhancement securities and the commercial real estate loans and securities portfolio (consisting of diverse residential and commercial real estate securities).

	SFI	AMC	NLY	RWT
Beta:	0.5	-0.217	0.342	0.567
Market Cap:	5.01B	141.71M	2.40B	1.41B
Rev. Growth:	15.40%	48.30%	-11.00%	108.10%
Revenue:	689.60M	21.57M	464.73M	551.17M
Gross Margin:	62.04%	72.97%	53.01%	36.27%
EBITDA:	142.56M	13.62M	234.14M	178.91M
Operating Margins:	11.27%	61.43%	50.37%	46.03%
Net Income:	27.33M	13.27M	227.92M	248.15M
EPS:	0.221	1.59	2.021	11.786
PE:	203.44	10.69	9.79	5.06
Div	2.79	1.60	2.00	2.68
Div Yield	6.21%	9.41%	10.11%	4.49%

[AMC = American Mortgage Acceptance Co](#)

[NLY = Annaly Mortgage Management Inc](#)

[RWT = Redwood Trust, Inc](#)

Discounted Dividend Analysis

A discounted dividend analysis of iStar's stock assumes a constant growth rate for the dividends and a constant beta for the firm over time. Dividend growth rates within the industry vary by firm and can change over time. A chart of iStar's annualized dividend and growth rates appears below. The average growth rate from 2000 to 2004 has been 3.85%. For this analysis, stock price was calculated for several growth rates ranging from 1% to 5%. A conservative estimate of long-term projected growth is assumed to be slightly lower than the average of the four years, at either 2.5% or 3%.

The beta of the industry is generally listed at 0.21, though specific company betas vary significantly. iStar's beta as listed on many popular websites is around 0.19, and when regressed comes to about .03. For this analysis, betas ranging from 0.1 to 0.7 were used to calculate stock price. With a significant amount of uncertainty around the actual beta of iStar, a conservative estimate of between 0.3 and 0.5 was used to determine implied stock price.

According to this analysis, the implied stock price of iStar is between \$53.20 and \$82.70.

Recommendation

The current price for iStar is \$44.91. The implied price for this stock is between \$53.20 and \$82.70, suggesting that it is significantly undervalued. I recommend we **HOLD** iStar in the portfolio.

Valuation

<u>Assumptions</u>	
Risk-Free Rate	0.04375
Market Premium	0.07
Return on Debt	0.044
D/V	0.65223
E/V	0.34777
DPS	2.79

Dividend Growth

	Avg Yearly Div*	% Growth
1998	\$1.52	N/A
1999	\$1.86	22.37%
2000	\$2.40	29.03%
2001	\$2.44	1.67%
2002	\$2.52	3.28%
2003	\$2.64	4.76%
2004	\$2.79	5.68%

* This analysis excludes a special dividend received in 1999 for \$1.91

Beta-Growth Sensitivity Analysis

		Beta 0.1	Beta 0.3	Beta 0.5	Beta 0.7
Growth	1.0%	\$69.15	\$51.47	\$40.99	\$34.05
Growth	2.0%	\$92.55	\$63.59	\$48.44	\$39.12
Growth	2.5%	\$111.06	\$71.94	\$53.20	\$42.21
Growth	3.0%	\$138.49	\$82.70	\$58.95	\$45.80
Growth	3.5%	\$183.34	\$97.06	\$66.00	\$50.00
Growth	4.0%	\$269.92	\$117.24	\$74.88	\$55.01
Growth	5.0%	\$3,906.00	\$198.61	\$101.90	\$68.53

Full Range: 34.05 - 3906.00
 Conservative Range: 53.20 - 82.70