



WE SET THE NARRATIVE

# NewLake Capital Partners Inc.

OTCQX:NLCP

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## NEW LAKE CAPITAL PARTNERS

<b>New Lake Capital Partners</b>	<b>OTCQX: NLCP</b>
<b>Date</b>	<b>May 8th, 2024</b>
<b>Rating</b>	<b>Buy</b>
<b>Fair Value</b>	<b>\$27.97</b>
<b>Expected 1 Year Return Including Dividend</b>	<b>45.93%</b>
<b>Estimate 2024 FY Revenue</b>	<b>\$50.14</b>
<b>Estimate 2024 FY AFFO</b>	<b>\$43.23</b>
<b>Estimate 2024 FY Dividend</b>	<b>\$1.64</b>

### Company Description

NewLake Capital Partners, Inc. is a real estate investment trust focusing on providing real estate capital to cannabis operators licensed by states. It engages in sale-leaseback transactions, buys properties for third parties, and finances build-to-suit projects. NewLake's portfolio consists of 31 properties, with 14 for cultivation and 17 dispensaries, leased on a triple-net basis to single tenants.

### Rating Methodology

After carefully evaluating a company's financial health, operational efficiency, and growth prospects through various analyses, we culminate our assessment by assigning a rating of "Buy," "Hold," or "Sell." This rating is determined based on the company's performance in comparison to its peers, alongside an examination of its valuation. A "Buy" rating suggests the company outperforms its competitors and is undervalued or poised for growth, indicating a good investment opportunity. A "Hold" rating implies the company is performing on par with industry standards, and its current valuation accurately reflects its market position and future prospects, suggesting investors should maintain their positions without adding more. A "Sell" rating is given if the company underperforms relative to its peers or is overvalued, indicating a potential decline in value and advising investors to divest. This systematic approach helps investors make informed decisions by understanding a company's relative standing in its sector and its potential for future performance.

### NLCP Benchmark Comparable's

COMPARABLE COMPANY	TICKER	FOCUS
AFC Gamma, Inc.	US: AFCG	Cannabis Focused
Essential Properties Realty Trust, Inc	US: EPRT	Not Cannabis Focused
Four Corners Property Trust, Inc.	US: FCPT	Not Cannabis Focused
Innovative Industrial Properties, Inc.	US: IIPR	Cannabis Focused
<b>NewLake Capital Partners, Inc.</b>	<b>US: NLCP</b>	Cannabis Focused
NNN REIT, Inc.	US: NNN	Not Cannabis Focused
NETSTREIT Corp.	US: NTST	Not Cannabis Focused
Postal Realty Trust, Inc.	US: PSTL	Not Cannabis Focused
Chicago Atlantic Real Estate Finance, Inc.	US: REFI	Cannabis Focused

## Report Process

We have established a process for analyzing a REIT, which we will outline in this section before discussing specific details regarding New Lake Capital Partners (NLCP).

## Establish Comparables

We initiated our research process by developing a benchmark of companies similar to New Lake Capital Partners (NLCP). This index includes companies that share characteristics with NLCP, specifically those classified as small or mid-cap firms. Our main criterion for inclusion was engagement in the cannabis industry, which aligns with NLCP's business focus.

Due to the small number of REITs solely focused on the cannabis sector (only three in addition to NLCP), we expanded our benchmark to include five additional firms. This extension increased the total number of companies in our benchmark to nine, enhancing the breadth of our comparative analysis. The selection was based on market capitalization, cannabis focus where applicable, and a similar REIT structure, providing a diverse and relevant group for our analysis.

## Understanding the Industry and Catalysts

Next, we aim to independently validate the fundamental thesis and strategic approach of the REIT, designed to drive revenue growth for shareholders.

## Understanding NLCP

We will then review the primary thesis and strategic plan of the REIT to ensure it is designed to achieve revenue growth for shareholders.

## Establish KPIs

We have set Key Performance Indicators (KPIs) for comparing NLCP against a custom benchmark of other companies. Our analysis will include the three financial statements, as well as dividend metrics and valuations.

## KPI Results

Next, we compare and rank NLCP against its peers across each category. This comparison allows us to evaluate the REIT's effectiveness in generating value for shareholders relative to its competitors.

## Valuation Analysis

Next, we will apply traditional comparative valuation methods together with our internal calculations to determine the value of the REIT's units.

## Our Take

At the end, we will analyze all the information gathered and conclude whether we recommend the REIT as a Buy, Hold, or Sell. We will also provide our target valuation for the REIT.

# Executive Summary

NLCP is a real estate investment trust specializing in leasing properties to state-licensed, cannabis-focused operators in the U.S. Federal restrictions on cannabis create a niche opportunity for NLCP, allowing it to secure favorable lease agreements and benefit its shareholders.

The cannabis industry is rapidly growing, with an expected compound annual growth rate (CAGR) of approximately 10.5% to 11.2%, potentially reaching \$43 billion by 2027. This growth boosts demand for real estate for cultivation and dispensaries, which benefits NLCP.

NLCP focuses on tenant underwriting and risk management, preferring leases with financially stable public entities to ensure transparency and reliability. Its portfolio is diversified across various states and tenant types, which supports stability and growth.

Key performance indicators include:

- Revenue Growth: NLCP has a three-year CAGR of 59.5%.
- Gross Margin Yield: Consistently high at 99%, indicating efficient operations.
- SG&A Margin Yield: Maintained at 16%, showing effective management.
- Debt to Tangible Equity: Low debt levels enhance financial stability, with an Altman Z-score of 11.4.
- AFFO Growth and Payout Ratio: AFFO growth stands at 11%, with a sustainable payout ratio of 77%.
- Dividend Yield and Growth: Offers a yield of 8.66% and a growth rate of 5.13% year-over-year.
- Valuation: NLCP trades at a price-to-book value of 0.98 times, suggesting an exceptional value at its current price.

Considering these factors and utilizing a Dividend Discount Model with mean reversion principles, we project NLCP's potential annual return of 45.93% and a target price of \$27.97. This and a strong dividend and conservative debt profile make NLCP a buy recommendation.



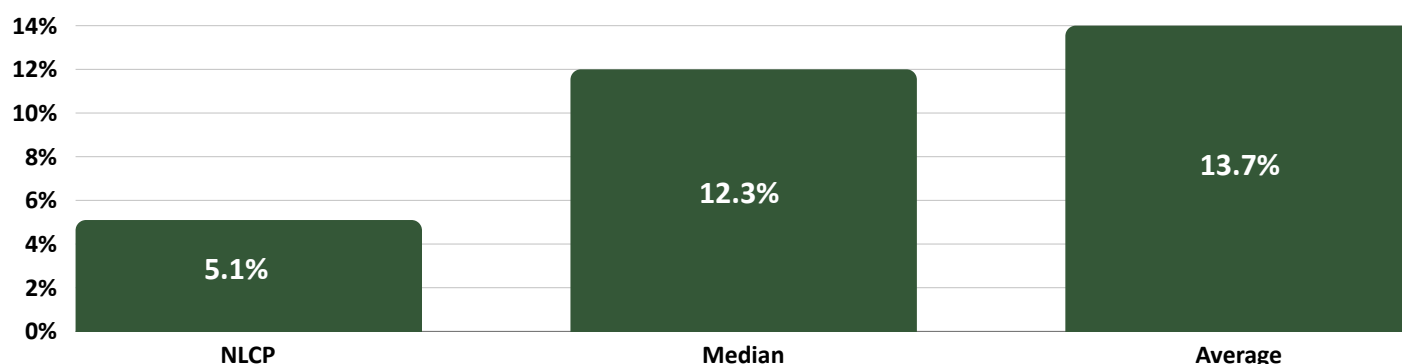
NLCP is one of four public REITS that provide real estate capital to US State-Licensed Cannabis Operators (SLCO). In the US, SLCO faces difficulties in finding willing landlords. This difficulty presents an opportunity for NLCP shareholders. NLCP can secure highly favorable terms for their shareholders for these real estate transactions.

<b>Macro Industry Outlook – Cannabis Trends</b>	<p>Cannabis is expanding at a rate significantly higher than the overall economic growth in the US. The increase in state-level licensing is converting the illegal market into a regulated one. Furthermore, cannabis is reaching new consumers who had not used it prior to its legalization in their states. The introduction of different cannabis products, such as edibles and beverages, also attracts individuals who are opposed to smoking.</p> <p>The above are the perceived drivers of the growth in Cannabis. A number of groups attempt to estimate the growth of the industry. MJBIZ Research predicts a growth rate of 11.19% from 2023 to 2028. BDSA forecasts a compound annual growth rate (CAGR) at 10.5% from 2022 to 2027, resulting in a \$43 billion legal U.S. cannabis market in 2027.</p> <p>This growth necessitates a significant footprint for both cultivation and dispensaries for vertically integrated cannabis operators. This situation helps NLCP increase its revenue by meeting the additional real estate capital needs of the SLCO.</p>
<b>Macro Industry Outlook – Improving Catalyst</b>	<p>The financial condition of tenants is crucial for REITs and landlords. Cannabis companies had inherent challenge with cannabis being a federally scheduled class 1 narcotic. With news of the DEA is planning to accept HHS recommendation to res Schedule 1 to Schedule 3, cannabis companies would be eligible for standard business tax deductions, significantly reducing their expenses. This would enhance their financial stability, providing additional cash flow and security for landlords of cannabis-related properties.</p>
<b>Real Estate Story – Portfolio Overview</b>	<p>NLCP is diversified across regions, types of real estate, and tenants. As of the December 31st, 2023 financial report, NLCP serves 13 State-Licensed Operators (SLCOs) across 12 US states, covering 1.6 million square feet of property. Seventy-one percent of the SLCO tenants are public companies, which enhances transparency regarding their financial status. Eighty-two percent of the SLCOs operate in multiple states, adding regulatory diversification. Additionally, 93% are vertically integrated in their operations. Despite these tenants having market capitalizations above \$3 billion, they still require a specialized partner like NLCP.</p>

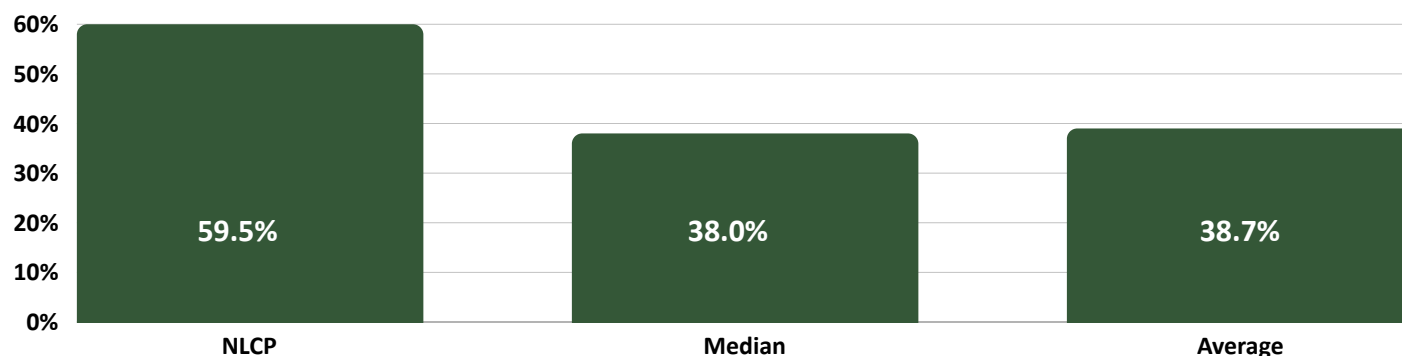
<p><b>Real Estate Story - Underwriting</b></p>	<p>NLCP's underwriting is based on six principles:</p> <ol style="list-style-type: none"> <li>1. Tenants are required to have strong financial profiles, with a preference for public companies that must adhere to financial reporting requirements. Private companies may also be considered if management is confident in their transparency.</li> <li>2. While ideas are the easy part of running a business, execution is the most challenging. NLCP evaluates the tenant's management team to ensure they can effectively operate in their highly regulated marketplace.</li> <li>3. The cannabis industry is very capital intensive for SLCO's, hence it is important that the companies have access to additional funding if necessary which provides the cashflow necessary to pay their rents on time.</li> <li>4. NLCP focuses on states with limited licensing to ensure more stability for tenants. For example, Florida and Illinois issue 20 and 22 operating licenses respectively, compared to Oregon and Washington, which have 1275 and 1021 licenses. Targeting states with fewer licensees reduces competitive pressures on SLCO tenants which allows improving margins and cash flows which increases their ability to pay rents.</li> <li>5. NLCP prioritizes strong property-level cash flows. One key metric is <math>\text{EBITDA} + \text{Rent} / \text{Rent}</math>. This calculation provides NLCP a quick measure of the strength of the cash flows of an individual property.</li> <li>6. Ideally, properties should also be close to an urban center in case they ever need to be repurposed.</li> </ol> <p>This approach ensures a thorough evaluation of potential risks and benefits associated with each tenant and property, aligning with NLCP's strategic objectives.</p>
<p><b>Real Estate Story - Risk Management</b></p>	<p>NLCP reduces risk through two main risk-mitigating principles:</p> <ol style="list-style-type: none"> <li>1. The structure of deals with tenants is fundamental. Leases are structured as triple net (NNN) leases, where the tenant is responsible for all real estate taxes, building insurance, and maintenance costs in addition to rent. This minimizes the landlord's financial risks and responsibilities. These leases are long, typically spanning 15 – 20 years, which benefits NLCP shareholders. Additional annual rent increases are pre-negotiated, and agreements include security deposits and cross-collateralization in security. While cross-collateralization is not typical, it can be demanded due to the favorable power dynamic for NLCP shareholders.</li> <li>2. As previously mentioned, most tenants are public companies, making their financials publicly accessible. However, NLCP management also insists on facility-level reporting to provide detailed insights into the security of each lease agreement. Additionally, NLCP arranges calls with tenants to receive regular updates. These calls not only provide updated financial information but also give NLCP management additional competitive information regarding the cannabis marketplace and their tenants' competitors.</li> </ol> <p>These principles ensure that NLCP strategically manages risk while maintaining strong oversight and control over its investments, aligning with the long-term interests of its shareholders.</p>

KPI	Income Statement – Revenue Growth
Why it is important?	Revenue growth is crucial, as it is highly correlated with long-term unit price performance over time.
Factual information	We analyze NLCP's revenue growth using two key metrics: the Last Twelve Months (LTM) growth rate of 5.1% and the more significant three-year Compound Annual Growth Rate (CAGR) for revenue, which is 59.5%.
Peer Comparison	First, for the comparison benchmark, the median revenue growth over the last 12 months is 12.3%, with an average growth of 13.7%. Looking at the 3-year Compound Annual Growth Rate (CAGR), the benchmark shows a median growth of 38% and an average growth of 39%.
Take Away / Conclusion	NLCP has significantly outperformed its benchmark over a three-year period. However, it has lagged behind its benchmark in the past year. Given the challenging regulatory environment in the cannabis industry in 2023, the LTM growth rate of 5.1% is considered reasonable. Analyzing revenue over a three-year period offers a more accurate reflection of revenue trends by mitigating the impact of short-term volatility in revenue reporting.

### Revenue Growth LTM vs Benchmark



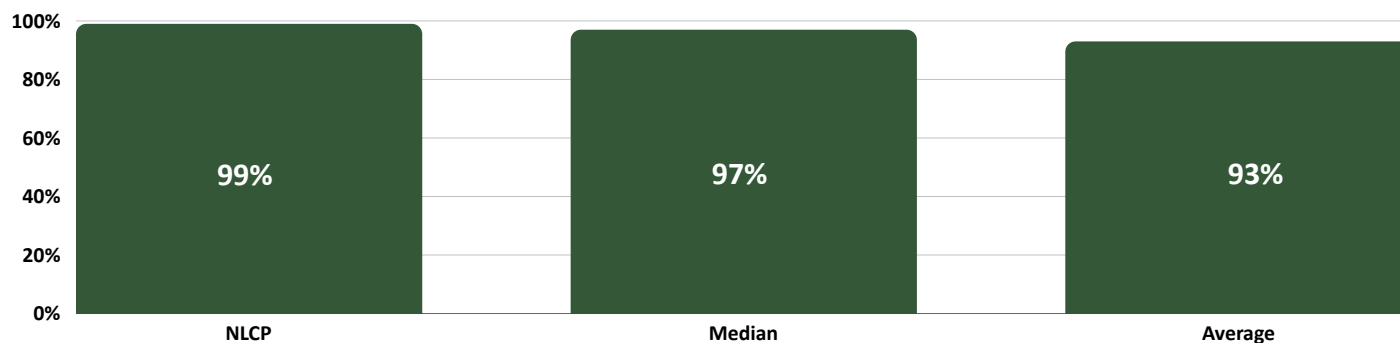
### Revenue vs Benchmark



Source: S&P Capital IQ

KPI	Income Statement – Gross Margin Yield
<b>Why it is important?</b>	Gross Margin Yield illustrates how lean and efficiently a REIT operates its business. The closer the spread between Gross Margin Yield and revenue, the better management has been at controlling direct property costs.
<b>Factual information</b>	NLCP has minimal leakage between revenue and gross margin. Over the last 12 months, the Gross Margin Yield was 99%, representing a leakage of only 1% in direct costs.
<b>Peer Comparison</b>	The median REIT in the comparison had a Gross Margin Yield of 97%, and the average was 93%, representing direct expense leakages of 3% and 7% of each dollar of revenue, respectively.
<b>Take Away / Conclusion</b>	NLCP management has shown significant efficiency by reducing the direct costs of property management to only 1% of every dollar earned from rents. This reflects the effectiveness of NLCP's management and the cost benefits of having the REIT managed internally rather than outsourcing to a third party.

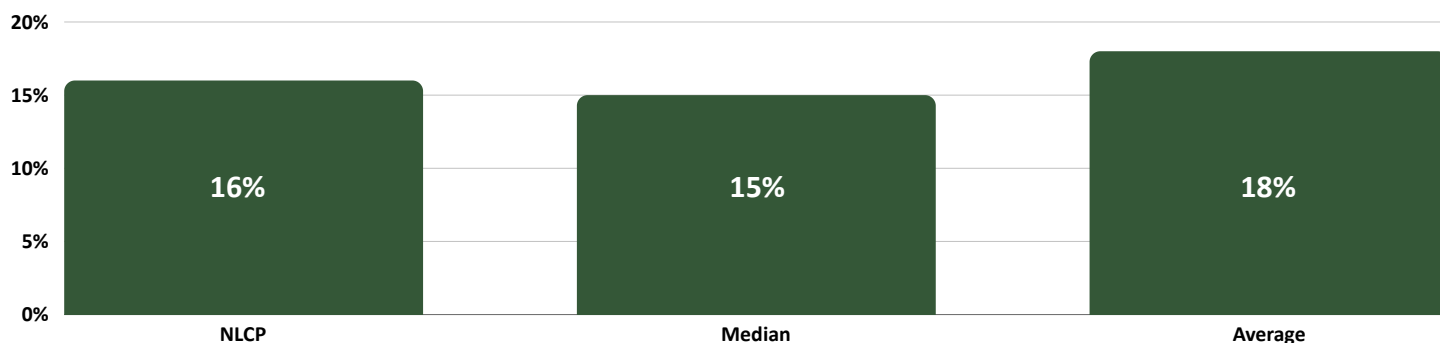
**Gross Profit Margin vs Benchmark**



Source: S&P Capital IQ

KPI	Income Statement – SG&A Margin Yield
<b>Why it is important?</b>	SG&A (Selling, General, and Administrative) Margin Yield represents the percentage of each dollar of revenue collected that is used toward operating the REIT, including expenses like office space, employee salaries, legal fees, and travel costs. The lower this metric, the more efficiently the REIT is run by management.
<b>Factual information</b>	NLCP's Last Twelve Months (LTM) SG&A Margin Yield is 16% of each dollar of revenue earned.
<b>Peer Comparison</b>	In the peer group, the average SG&A Margin Yield is 18%, and the median is 15%.
<b>Take Away / Conclusion</b>	NLCP has managed its expenses efficiently in operating the REIT, especially compared to other REITs with larger assets that report higher SG&A Margin Yields. Despite the potential for cost savings in REITs with larger Asset Under Management (AUM), NLCP's management efficiency is notable. This underscores the effectiveness of NLCP's management team in controlling operational costs and the advantages of internal management over outsourcing to a related or arm's length third party.

**SG&A Margin vs Benchmark**

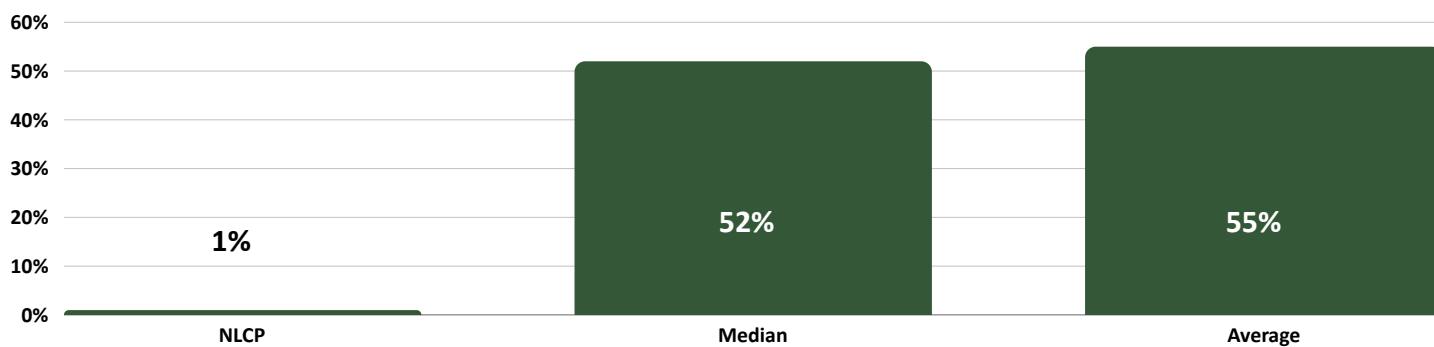


Source: S&P Capital IQ



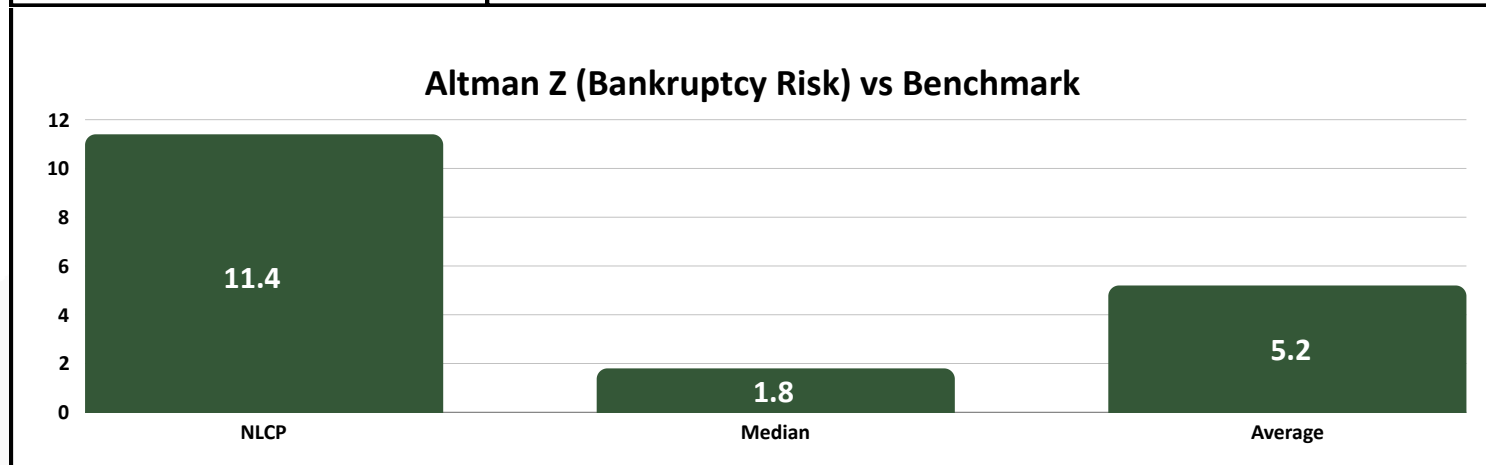
KPI	Balance Sheet - Debt / Tangible Equity
Why it is important?	REITs generally employ a business model that involves considerable leverage through bank loans secured by a first lien on their assets. Theoretically, when asset prices increase and interest rates decrease or stabilize, this leverage can enhance returns. Nevertheless, it is important to recognize that leverage can also significantly increase risk.
Factual information	NLCP has a Debt to Tangible Equity ratio of 1%.
Peer Comparison	The benchmark average is 55%, and the median is 52%.
Take Away / Conclusion	NLCP stands out from the benchmark with its nearly zero debt level, which further lowers its risk profile, already reduced by stringent underwriting criteria. The ability of NLCP to generate substantial AFFO without relying on debt affirms the effectiveness of its management strategy. Furthermore, if NLCP management decides to utilize debt in the future, it could significantly boost the growth rate of AFFO, potentially leading to higher dividend payouts.

**Debt / Tangible Equity vs Benchmark**



Source: S&P Capital IQ

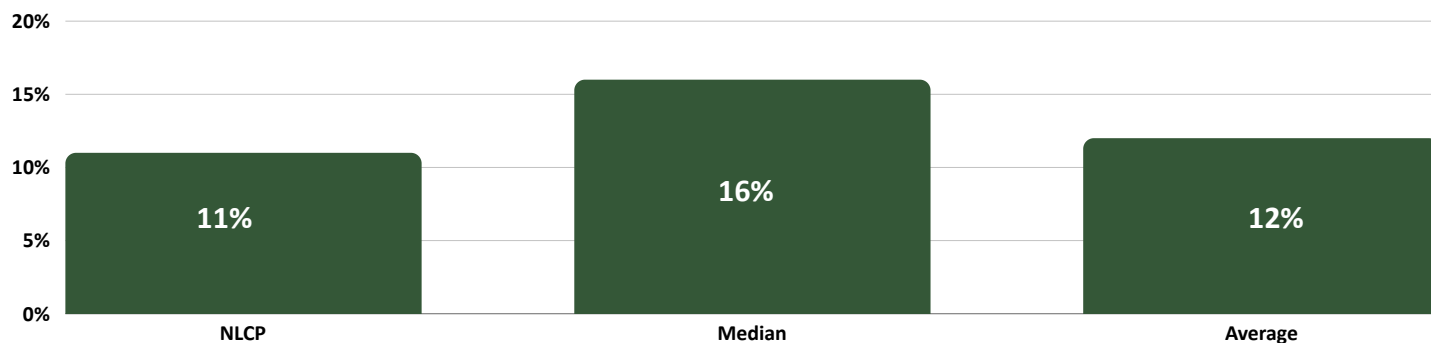
KPI	Balance Sheet – Altman Z (Bankruptcy Risk)
Why it is important?	The Altman Z-Score predicts the likelihood of a business going bankrupt within two years by combining five financial ratios into a single score; scores above 2.99 suggest low bankruptcy risk, scores between 1.81 and 2.99 indicate moderate risk, and scores below 1.81 signal high risk. This can be thought of as being similar to a credit check for a consumer.
Factual information	NLCP has an Altman Z score of 11.4
Peer Comparison	The median score for the benchmark is 1.8, while the average in the benchmark is 5.2.
Take Away / Conclusion	This illustrates the significant advantages of being debt-free. The median company in the benchmark faces a high risk of bankruptcy within the next two years. The average is skewed due to companies like NLCP, which have low debt levels. This highlights the robustness of NLCP's balance sheet and its distance from financial concerns of bankruptcy.



Source: S&P Capital IQ

KPI	Cash Flow - AFFO Growth LTM
Why it is important?	AFFO is a financial metric utilized by Real Estate Investment Trusts (REITs) to evaluate their operational cash flow after deducting maintenance costs and capital expenditures. It offers a more transparent perspective on a REIT's capacity to produce cash and maintain dividends for shareholders. Ideally, this metric should increase alongside revenue over time, as growth in AFFO closely correlates with future unit prices.
Factual information	In the last twelve months, NLCP increased its AFFO by 11%.
Peer Comparison	The benchmark median was 16%, with an average increase in AFFO of 12% over the last 12 months.
Take Away / Conclusion	NLCP is expected to lag in this category due to its no-debt structure. However, keeping close to the median is impressive without debt. An unleveraged 11% increase is noteworthy. NLCP management has the ability if it desired to add debt to its structure which would potentially increase the rate of AFFO growth.

**AFFO Growth LTM vs Benchmark**

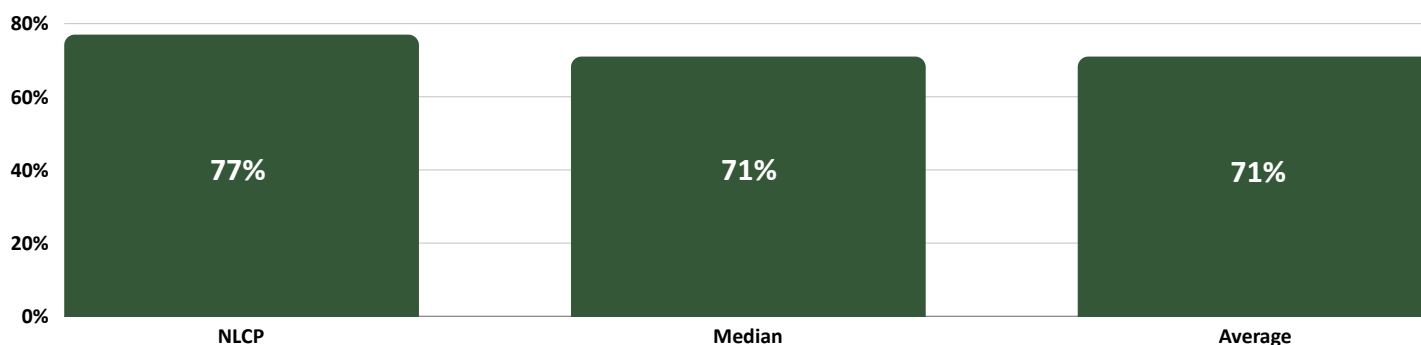


Source: S&P Capital IQ

AFC Gamma and Chicago Atlantic Real Estate Finance were not included in the benchmark calculation due to not reporting AFFO.

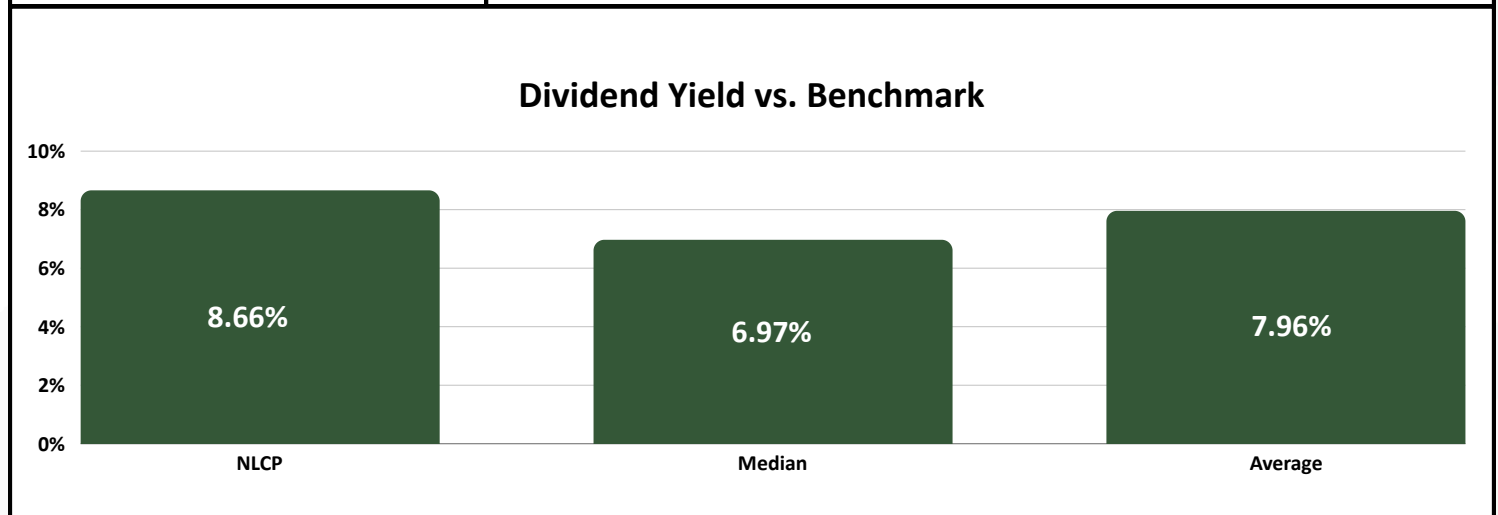
KPI	Cash Flow – AFFO Payout Ratio
Why it is important?	The payout ratio must be at a reasonable level to maintain the dividend. Rising or stable dividends support REIT values, whereas dividend cuts typically result in significant falls in unit values.
Factual information	NLCP maintained a 77% payout ratio of its AFFO.
Peer Comparison	The benchmark average and median were 71%.
Take Away / Conclusion	NLCP has a slightly higher payout ratio than the benchmark. All organizations are within a range that suggests the dividend payouts are manageable. However, the risk profile of the benchmark members with leverage is much higher. Therefore, NLCP, having no significant debt, can support a higher AFFO payout ratio. In addition, as the amount of AFFO grows, the overall payout goes down. NLCP management could then increase the dividend to match the growth of AFFO while then keeping the ratio the same.

### AFFO Payout Ratio vs Benchmark



Source: S&P Capital IQ

KPI	Dividend - Yield
Why it is important?	REIT holders focus on dividends for a significant portion of their returns. If the dividends are well covered by AFFO, a company with a higher dividend yield is generally considered better, as long as the portfolio quality is good and leverage is not excessive.
Factual information	The current target dividend yield for NLCP is 8.08%
Peer Comparison	The median benchmark yield in the index is 6.97%, and the average is 7.96%.
Take Away / Conclusion	NLCP has a higher dividend yield than its benchmark. This is noteworthy for three reasons. First, it provides yield while one waits for catalysts to happen for the Cannabis industry. Second, if the yield moves toward the median or average, the investor will benefit from an increase in unit value. Third, having a higher dividend that is well-covered by AFFO without relying on a debt structure is more conservative than dividends from REITs that use leverage. Overall, this dividend yield is highly appealing to investors searching for yield.

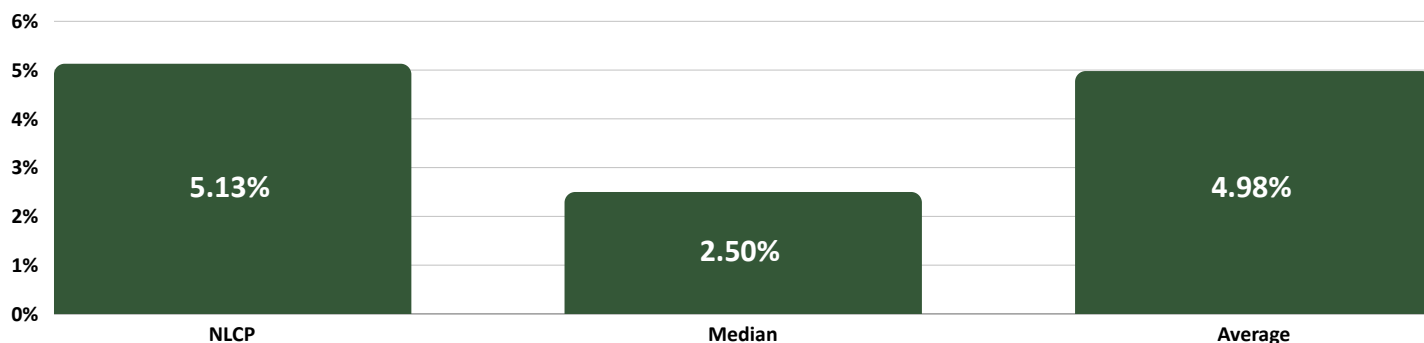


Source: S&P Capital IQ



KPI	Dividend – Growth Rate
<b>Why it is important?</b>	The dividend growth rate is highly correlated with the long-term increase in unit prices of a REIT. If investors require an 8% dividend yield and the dividend increases by 5%, the unit value must also increase by 5% to maintain the 8% yield demanded by the market. Typically, this adjustment does not occur in the short term, but over time, the rate of dividend increase is closely correlated with the increase in unit value.
<b>Factual information</b>	New Lake increased its dividend by 5.13% over the last 12 months.
<b>Peer Comparison</b>	Comparatively, the median company in the benchmark increased its dividend by 2.5%, and the average increase was 4.98%.
<b>Take Away / Conclusion</b>	NLCP outpaced its peers in increasing its dividend over the last 12 months. This is particularly noteworthy because NLCP has an unleveraged structure. Traditionally, the use of leverage should enable other companies in the benchmark to achieve higher rates of dividend growth than NLCP. In this case, the conservative approach of NLCP has proven advantageous compared to its peers.

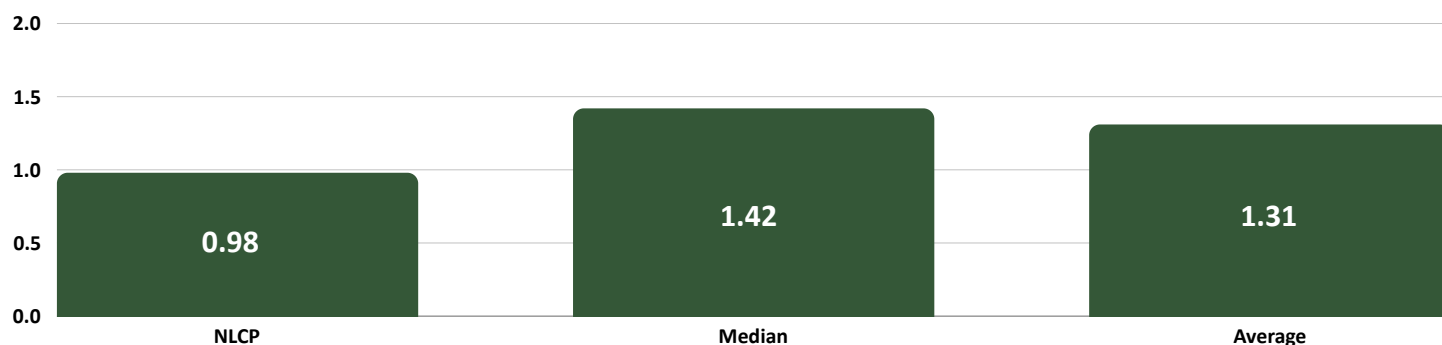
## Dividend Growth vs. Benchmark



Source: S&P Capital IQ

KPI	Valuation - Price to Book Value
Why it is important?	We use the Price to Book Value ratio to assess a REIT's potential liquidation value and to compare it to its peers. Theoretically, if all assets were sold at their fair value, this ratio indicates the amount that would be returned to shareholders. Additionally, REITs that have a lower ratio than the benchmark suggest a potential upside in unit value if they were to revert to the benchmark's mean.
Factual information	NLCP's trading multiple is 0.98 times its Book Value.
Peer Comparison	The benchmark median is 1.42 and the average is 1.31.
Take Away / Conclusion	NLCP Partners is trading at a significant discount compared to its peers based on the Price to Book ratio. This represents a lower-risk entry point for investors compared to the benchmark. Additionally, this presents an opportunity for mean reversion, where the company could adjust toward the same Price to Book value multiple as its peers in the benchmark.

**Price / Book vs Benchmark**



Source: S&P Capital IQ

# Valuation

With dividend-focused REITs, our valuation employs the principle of mean reversion via the Mean Reverting Dividend Discount Model. We begin by calculating the expected return of the benchmark by adding the dividend yield to the expected growth rate of dividends. This approach has been notably effective in predicting long-term returns for dividend-focused securities. After establishing the benchmark's expected return, we compare it to that of NLCP. For both NLCP and the Benchmark we use the previous year's dividend growth rate and the current dividend yield. For the benchmark, we utilize the median value to ensure clarity and to mitigate the influence of unusually high yields or special dividends.

## Dividend Discount Model Expected Return of the Benchmark

Current Dividend Yield	6.97%
LTM Dividend Median Growth	2.50%
Expected Annual Return	9.47%

## Dividend Discount Model Expected Return of NLCP

Current Dividend Yield	8.66%
LTM Dividend Median Growth	5.13%
Expected Annual Return	13.79%

## Stock Target Price Based on Mean Revision of the DDM

Current Stock Price	\$20.29
Mean Revision	37.85%
Target Stock Price	\$27.97

## Expected Return for NCLP

Target Dividend Yield	8.08%
Mean Revision of Stock Price	37.85%
Target Return	45.93%

# Our Take

We rate NLCP a Buy and have a valuation price of \$27.97, which provides a potential upside of 45.56%. When the dividend is included, it would represent a return of 54.22%. NLCP specialization is advantageous because the tenants are involved in the cannabis industry, enabling NLCP to negotiate favorable lease terms that benefit its shareholders. The cannabis industry's rapid growth increases demand for real estate dedicated to cultivation and dispensaries. NLCP's strategic focus on tenant selection and risk management involves leasing primarily to financially solid public entities, enhancing transparency and reliability. NLCP's diversified portfolio across multiple states and tenant types promotes stability and continued growth. For these qualitative reasons, NLCP is well-managed, positioned to increase growth, and supports a Buy recommendation.

The company's performance is strong across several key indicators: a three-year revenue growth rate of 59.5%, a gross margin consistently at 99%, and a low SG&A margin of 16%. These figures indicate effective operational management. NLCP also maintains a robust financial structure with low debt levels, evidenced by an Altman Z-score of 11.4. The trust's adjusted funds from operations (AFFO) have grown by 11%, with a healthy payout ratio of 77%, and it offers a high dividend yield of 8.66%, which has grown 5.13% year-over-year. Trading at a price-to-book value of just 0.98 times, NLCP represents excellent value. Our analysis, incorporating a Dividend Discount Model with mean reversion, suggests a target price of \$27.97 and a potential annual return of 13.79%, supporting our buy recommendation for NLCP.

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