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BTN Research

Jeff Middleswart
jmiddleswart@btnresearch.com

Bill Whiteside, CFA
bwhiteside@btnresearch.com

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Welltower (WELL) 6/18 Quarter Update

We are still waiting on WELL's 10-Q to see some of the details about the many recent moves the company has made. In the past, they divested troubled properties into off-balance sheet investments that Welltower owns so we would like to review if that is happening again along with how they positioned other troubled assets they just purchased and sold. The last conference call had some great attempts to spin troubled transactions into positives, so we will share some of those today. While the company did announce that supply continues to exceed demand and blamed the flu for some of the weakness in operating results, they painted an upbeat picture of dumping underperforming properties from the triple-net lease portfolio will retire some debt and make the remaining portfolio appear healthier. Apparently, the flu has never happened until 2017-18, so we should keep that in mind. Maybe someday there will be a vaccine that allows people to get a shot to lower the impact of the flu and WELL will be able to produce stronger results going forward.

We have seen several transactions of late where WELL cut lease payments on properties as well as converted them from triple-net lease to variable accounts, so it was good to see the company tout that it still has automatic rent increases and very few properties are up for lease renewal in the near future. Even when a sizeable part of what is coming due has just been changed:

> Shanka Mitra – *"I also want to point out that we have significantly derisked that cash flow stream (in Triple-Nets) as we have only $28 million of triple net, senior housing, and post acute combined leases rolling before 2024. However, $22 million of that is a well-covered Brookdale lease, and we have effectively taken care of that."*

And, as new supply comes online and continues to exceed demand, Welltower has a very unique plan of turning around older properties formerly with Brookdale (a seasoned operator) that have been underperforming in Triple-Net and some RIDEA structures – it plans to raise prices and boost occupancy:

> Shanka Mitra – *"For the 60 assets that we are transitioning away from Brookdale, we see significant opportunity for growth as occupancy recovers from around 82% and rent levels are enhanced through the implementation of the new operating plans."*

Of course, Welltower still has great assets and its trophy properties are incredible – they just can't service their debt:

> Shanka Mitra – "*I'm also delighted to report that we have converted Brandywine Living from a triple net to a RIDEA structure. This portfolio of 27 communities centered around New York MSA is amongst the highest-quality real estate in our portfolio. Brandywine's portfolio has an average of 13 years with a REVPAR $7,500-plus. And through above-average margins, generates an annual NOI per unit of approximately $29,000, placing them at the top of our portfolio. Despite great operating metrics, the portfolio was over-leased and over-leveraged from day one and essentially was covering at 1.0x. We executed a classic debt-to-equity swap in the PropCo, OpCo, and management company. After this transaction, we owned 99.3% of the PropCo and OpCo and 34.9% of the management and development company. Brandywine will operate these buildings under a next-generation management contract, but we'll share the upside and downside together. We believe this structure significantly improves the alignment of interests."*

Readers know that we believe a RIDEA structure does not happen with strong performing assets. The operator of a fully leased facility would gladly pay the fixed rent and pocket the incremental profits with a triple-net lease. Only stuff with inherent problems would take a reduced rent scenario of RIDEA in exchange for splitting any potential upside if operations improve.

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