



MPW – Steward’s having a fire, sale

Steward has sold operational assets purchased from IASIS at a cost effectively entirely borne by MPW. New tenant receives discounted rent.

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February 16, 2023 – On February 15, 2023, Steward Health Care Systems (“SHCS”) announced that it had entered into an agreement to sell its Utah operations to Commonspirit¹. This is an objectively bad deal for MPW, who have taken a 20% haircut on their Utah rent.

The sale by Steward is equally nonsensical. Steward and MPW management have consistently told select investors and analysts in the course of the preceding weeks that SHCS had its best EBITDA year and was FCF positive. Why has it sold its best asset at fire sale prices?

The real kick in the teeth is for MPW investors, who effectively paid for SHCS’s Utah assets and will see no money from its sale.

The Announcement & Rent Haircut

Light on details as usual: MPW’s statement announcing its new tenant of Utah properties failed to explicitly disclose a rent haircut of \$17m, which can be derived from the reported new lease base, gross asset value, and Steward’s master lease agreement.

Viceroy estimate MPW are now generating ~94m rental income from this property, substantially less than its current ~\$110m.

Cash lease base appears to have been cut to 7.8% from ~9%.

healthcare providers, will become one of MPT’s largest tenants. Cash rental payments during the 15-year initial lease term are to begin at roughly 7.8% of MPT’s gross investment and increase by 3.0% annually. The overall cash flow profile of the lease is particularly attractive given the tenant’s strong investment grade credit. The lessee will have the option to purchase the facilities at the higher of fair market value or MPT’s gross investment at 5, 10 and 15 years.

Figure 1 – MPW Press Release – February 15, 2023

MPW’s master lease agreement with Steward can be accessed here:

<https://www.sec.gov/Archives/edgar/data/1287865/000119312517065943/d295656dex1033.htm>

Commonspirit will pay substantially less rent on its Utah hospital tenancy than its predecessor, Steward.

¹ <https://www.healthcarediver.com/news/hcas-purchase-5-utah-hospitals-put-on-pause-after-judges-order/625111/>



Steward Exposure & Fire Sale

It's reported that MPW have told analysts that Steward's sale of Utah assets was commensurate with its prior deal with HCA, which fell through after the FTC challenged the transaction². This was slated at \$800-\$850m.

We thank HedgeEye for publishing Commonsprit's unaudited quarterly financials showing a purchase price of \$685m³, which is in **fire sale territory at 15% - 20% discount to SHCS's failed HCA deal**.

In February 2023, CommonSpirit entered into an asset purchase agreement to acquire a regional health system, including five hospitals, over 40 clinics, and other ambulatory services in Utah for a gross purchase price of \$685 million, plus certain working capital adjustments. The acquired facilities will support the mission and strategy to better serve the health care needs of the communities in Utah. The acquired facilities will be managed by Centura Health. The transaction is subject to customary closing terms and conditions and is scheduled to close by the end of the fiscal year.

Figure 2 – CommonSpirit unaudited quarterly financials

This is even more bizarre as Steward and MPW have similarly advised analysts that it was FCF positive, and vastly beat earnings expectations.

Results improving substantially versus Q1 2022, as restrictions on elective surgeries in Massachusetts have expired and as staffing and other cost pressures have eased.


- **Volume metrics up** across all key categories
- **Higher-quality volume** improving profitability
- **EBITDAR increased** in majority of regions
- **Contract labor expense decreased 21%**, with labor costs now < 50% of revenue
- **May and June significantly outperformed** original expectations
- **Q2 2022 +11% versus pre-COVID Q2 2019** (excluding South Florida)

LIQUIDITY UPDATE¹

Recent improvements to hospital operations noted above are expected to continue through the remainder of the year and to coincide with positive developments related to Steward's liquidity position:

- **\$350 million annual labor and non-labor cost savings initiative** is fully-implemented as of August
- **\$70 million** in Medicaid reimbursement previously delayed due to dispute between Texas and CMS is now being collected
- **\$70 million** collection in Q3 2022 of accounts receivable related to Tenet transition in Florida
- **\$125 million** in cash expected from CareMax transaction, expected to close in Q4 2022
- **\$45-50 million current monthly pace of Medicare advance and Tenet management contract repayments ends in September**

Steward expects a substantial and sustainable positive free cash flow run-rate beginning in Q4 2022



And before turning the call over to Steve, let me outline the strong operating performance that Steward is reporting to us. **Unadjusted EBITDA for the second quarter was approximately \$51 million. The third quarter is expected to be more than \$30 million. Fiscal year '22 unadjusted EBITDA is projected to be between \$50 million and \$80 million. Contract labor in Q3 fiscal year '22 has decreased 30% from Q1 FY '22 run rate and is expected to decline an incremental 20% in Q4, resulting in a 50% decline since the first quarter of this year. Steward is also forecasting unadjusted EBITDA of more than \$350 million for fiscal year '23. Steve?**

Figures 3 & 4 – MPT August 2022 Investor Update and Q3 2022 earnings call

Obviously, MPW provide none of Steward's financial statements to validate these Blue-Sky statements, however it is perplexing that Steward would sell its best assets for fire sale prices if it didn't have to.

Further, we note that the sale decreases MPW's tenant exposure to SHCS. We anticipate this will justify MPW's withholding of Steward's financial data once more.

² <https://www.beckershospitalreview.com/hospital-transactions-and-valuation/hca-steward-make-for-2nd-called-off-hospital-deal-within-days-of-ftc-challenge.html>

³ https://app.hedgeye.com/mu/12-31-2022-unaudited-quarterly-report-final-secured?encoded_data=fqBZ!bpgjxAniZji+CUtj6FY08FaMIEk=



The Utah Background

In 2017, MPW loaned Steward \$1.4b to purchase a Salt Lake City Hospital operator IASIS and their portfolio of 19 hospitals. It also made a further \$100m minority interest equity contribution in the transaction. IASIS owned and operated 17 hospitals.

Steward Transactions

On September 29, 2017, we acquired, from IASIS Healthcare LLC (“IASIS”), a portfolio of ten acute care hospitals and one behavioral health facility, along with ancillary land and buildings that are located in Arizona, Utah, Texas, and Arkansas. The portfolio is now operated by Steward which separately completed its acquisition of the operations of IASIS on September 29, 2017. Our investment in the portfolio includes the acquisition of eight acute care hospitals and one behavioral health facility for approximately \$700 million, the making of \$700 million in mortgage loans on two acute care hospitals, and a \$100 million minority equity contribution in Steward, for a combined investment of approximately \$1.5 billion.

Figure 5 – MPW 2017 Annual Report

A \$700m portion of this loan was immediately extinguished in exchange for 9 properties.

The remaining \$700m was a mortgage loan against 2 unnamed properties: Jordan Valley Medical Center and Davis Hospital & Medical Center.

On July 8, 2020, we acquired the fee simple real estate of two general acute care hospitals located in the Salt Lake City, Utah area, Davis Hospital & Medical Center and Jordan Valley Medical Center, in exchange for the reduction of the mortgage loans made to Steward for such properties and additional cash consideration of \$200 million based on their relative fair value. The approximate \$950 million investment in these two facilities is now subject to the Steward master lease that has an initial fixed term ending in October 2031 with multiple extension options and annual escalation provisions.

Real Estate Loan Agreement and Sale of Property

At December 31, 2019, the System held mortgage agreements with MPT related to the real property of two acute care hospital campuses. On July 2, 2020, the System sold the real property of the two acute care hospital campuses to a joint venture, of which MPT is the majority owner. The System subsequently leased the property from the joint venture. Due to specified forms of continuing involvement, under the provisions of Accounting Standards Codification Topic 840-40, Leases – Sale-Leaseback Transactions, the System is required to continue to capitalize the real estate and to recognize an obligation for the sales proceeds received. The System recognized an initial obligation of \$937.2 million, which included the former mortgage obligations of \$737.2 million as well as \$200.0 million in sale proceeds. The obligation will be amortized.

Figures 6 & 7 – MPW 2020 Annual Report and Steward Health Care 2019 Annual Report

On July 8, 2020, MPW acquired the Jordan Valley Medical Center and Davis Hospital & Medical Center in exchange for a total extinguishment of the loan and an additional \$200m cash payment it labelled a fair value increase.

Jordan Valley Medical Centre and Davis Hospital & Medical Centre were certainly not the largest hospitals in this portfolio. Their combined appraised value is \$111m in 2017

| Hospital | Location | Licensed # of Beds |
|---|--------------------|--------------------|
| Davis Hospital and Medical Center | Layton, UT | 220 |
| Jordan Valley Medical Center | West Jordan, UT | 172 |
| Jordan Valley Medical Center—West | West Valley, UT | 102 |
| Mountain Point Medical Center | Lehi, UT | 40 |
| Salt Lake Regional Medical Center | Salt Lake City, UT | 158 |
| Mountain Vista Medical Center | Mesa, AZ | 178 |
| St. Luke's Medical Center | Phoenix, AZ | 200 |
| St. Luke's Behavioral Health Center | Phoenix, AZ | 124 |
| Tempe St. Luke's Hospital | Phoenix, AZ | 87 |
| Odessa Regional Medical Center | Odessa, TX | 225 |
| Southwest General Hospital | San Antonio, TX | 327 |
| St. Joseph Medical Center | Houston, TX | 790 |
| The Medical Center of Southeast Texas | Port Arthur, TX | 199 |
| The Medical Center of Southeast Texas—Victory | Beaumont, TX | 17 |
| Wadley Regional Medical Center | Tesabana, TX | 370 |
| Glenwood Regional Medical Center | West Monroe, LA | 278 |
| Wadley Regional Medical Center | Hope, AR | 79 |
| Pikes Peak Regional Hospital | Woodland Park, CO | 15 |
| | | 3,581 |

Figure 8 – Steward Health Care Annual Report 2018



| Davis and Jordan Valley 2017 Value - Viceroy Research | | | | |
|---|---|--------------------|--------------------------------------|-----------------------|
| Hospital | Owner | Parcel ID | Address | 2017 Appraised value |
| Davis Hospital and Medical Center | MPT of Layton-Steward Property LLC | 90230086 | | \$ 34,979,886 |
| | | 90230013 | 1600 W Antelope Dr, Layton, UT 84041 | \$ 365,900 |
| | | 90230012 | | \$ 8,895,000 |
| Jordan Valley Medical Center | MPT of West Jordan-Steward Property LLC | 27-05-251-024-2000 | 3580 W 9000 S | \$ 10,744,200 |
| | | 27-05-251-024-2001 | 3580 W 9000 S | \$ 40,491,400 |
| | | 27-05-251-024-2002 | 3580 W 9000 S | \$ 6,049,700 |
| | | 27-05-251-026-0000 | 3590 W 9000 S | \$ 2,965,000 |
| | | 27-05-251-025-0000 | 3592 W 9000 S | \$ 5,681,600 |
| | | 27-05-251-006-0000 | 3434 W 9000 S | \$ 616,900 |
| | | 27-05-251-005-0000 | 3434 W 9000 S | \$ 1,113,700 |
| Total | | | | \$ 111,903,286 |

Figure 9 – Davis and Jordan Valley 2017 Value – Viceroy Research

The first \$700m loan was exchanged for 9 properties, and the second \$700m loan was secured against a further 2, but Iasis owned and operated 18 facilities in total at the time of acquisition. Steward basically received 7 of them for free.

Steward Transactions

On September 29, 2017, we acquired, from IASIS Healthcare LLC (“IASIS”), a portfolio of ten acute care hospitals and one behavioral health facility, along with ancillary land and buildings that are located in Arizona, Utah, Texas, and Arkansas. The portfolio is now operated by Steward which separately completed its acquisition of the operations of IASIS on September 29, 2017. Our investment in the portfolio includes the acquisition of eight acute care hospitals and one behavioral health facility for approximately \$700 million, the making of \$700 million in mortgage loans on two acute care hospitals, and a \$100 million minority equity contribution in Steward, for a combined investment of approximately \$1.5 billion.

At the time of the completion of the IASIS Merger, IASIS owned and operated seventeen hospitals, one behavioral health hospital, and several affiliated outpatient service facilities and physician clinics. The hospitals acquired include:

Figures 10 & 11 – MPW Annual Report 2017 & Steward Annual Report 2017

On a back-envelope, per-beds basis, we estimate that the purchase price of Jordan Valley Medical Centre and Davis Hospital & Medical Centre was ~\$196m⁴. Given Steward is running its hospitals business to the ground, we do not believe any fair value adjustment is warranted. We believe MPW must take a \$700m write off on this transaction alone representing the \$950 mortgage and payment less a conservative \$250m for the value of Jordan Valley and Davis.

The pattern in the Massachusetts portfolio of increasing loans continued with the Salt Lake City portfolio with Steward adding a further \$27m in Q4 2018.

2016 Mortgages. The 2017 Mortgages were secured by the real property associated with hospital campuses located in Utah acquired as part of the IASIS Merger. On November 30, 2018, Steward entered into amendments to the 2017 Mortgages increasing the principal amount of these mortgages by \$27 million. The 2017 Mortgages bear the same interest rate as the 2016 Mortgages of 7.5% for 2018. All payment terms and the maturity date of October 31, 2031 are identical to the 2016 Mortgages as a result of the Mortgage Joinder.

Figure 12 – Steward 2018 Annual Report

The FTC has blocked Steward’s sale of operations in Utah to HCA Healthcare on the grounds of maintaining competition in the area⁵.

Steward has sold assets purchased from IASIS at a cost effectively entirely borne by MPW.

It has now sold those assets. Investors have a right to be pissed off.

⁴ Iasis PPE balance of \$1.79b, portfolio beds of 3,581

⁵ <https://www.ftc.gov/news-events/news/press-releases/2022/06/ftc-sues-block-merger-between-utah-healthcare-rivals-hca-healthcare-steward-health-care-system>



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