MPW – Steward Throws in the Towel

It'd be funny if it weren't so tragic.

PLEASE READ IMPORTANT DISCLAIMER – PAGE 4

July 30, 2024 – Well folks there it is. On July 26, 2024, Steward Health Care threw in the towel and called time on Master Lease II over 8 MPW hospitals in Massachusetts.

These hospitals were contributed by MPW into the seemed-like-a-great-idea-at-the-time joint venture with Macquarie which the company touted as validating its absurd valuations. The irony of using a deal that helped drive its tenant into bankruptcy as an example of business sustainability is not lost on us.

The key takeaways from the filing are damning for MPW.

1. No bidder was willing to assume Master Lease II under its current terms.
2. No bidder put in a bid for the entire enterprise (real estate included) that even came close to the value of the real estate implied by the lease.
3. Every bidder requested significant rent concessions or a significant discount to acquire the property.
4. No actionable bids were received for the Carney and Nashoba Valley hospitals.

> 7. With respect to the Massachusetts Hospitals, the Debtors did not receive any bids that provide for a bidder to assume Master Lease II or acquire the underlying real estate at a value that exceeds the "lease base" under Master Lease II for such hospital. Rather, the bids received contemplate a purchase price for the total hospital enterprise (*i.e.*, inclusive of real estate and operations) that are significantly less than the value of the real estate implied by the rent obligations and the lease base under Master Lease II.[6,7]
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> 8. Therefore, there is no scenario in which a buyer of the Massachusetts Hospitals will assume Master Lease II or the rent obligations thereunder. Accordingly, the Debtors have filed this Motion to reject Master Lease II, relieve themselves of the burden of continuing to
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> 5 The only exceptions are that no actionable bids have been received for Carney Hospital and Nashoba Valley Medical Center, and the Debtors are seeking court authority to close such hospitals (the "**Closing Massachusetts Hospitals**") pursuant to the Hospital Funding and Facility Closure Motion.
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> 6 Because the Master Lease II rents were negotiated and agreed to in a different market environment with different capitalization rates, and are higher than current market rates, every bidder for the Massachusetts Hospitals asked the MPT-Macquarie JV for significant rent concessions or to acquire the underlying real property at a significant discount to the MPT-Macquarie JV's lease base.
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> 7 Because MPT's and Macquarie's investment in such real estate is substantially impaired, the Debtors have asked MPT and Macquarie to agree to certain concessions to allow the Debtors to transition the Massachusetts Hospitals to new operators. The Debtors have allowed for substantial engagement with the bidders to facilitate a transition, but have been stymied by MPT and Macquarie seeking to extract concessions to facilitate a consensual transition to date.

Figure 1 – Steward Emergency Motion

This completely validates Viceroy's research, namely that MPW's deals with Steward were blatantly uneconomic and unsustainable without a constant round-tripping of funds.

As we pointed out in our previous report into the Macquarie JV, it was a thinly veiled recapitalization of the properties designed to move debt off MPW's balance sheet and book dubious revaluation gains. Instead MPW falsely asserted that the JV validated the value of these properties and by extension its entire book.

The Recap Recap

The Macquarie JV had three principal goals:

1. Repay the ~$900m July 2021 Interim Credit facility, which it had originated to purchase 5 South Florida hospitals leased to Steward
2. Move the ensuing debt off MPW's balance sheet, if only cosmetically
3. Book a dubious $600m gain on sale to inflate its earnings
4. Artificially reduce its asset concentration to Steward, through its dilution of asset ownership

MPW contributed real estate valued at $1.1b, Macquarie contributed $400m in cash and the JV secured a $919m mortgage from a consortium of Apollo, Athene and Aspen. This mortgage, MPW claimed, represented 55% of asset value.

Viceroy stated in our original report on the Macquarie JV that it appeared to be this mortgage representing 55% of asset value that MPW used to justify a $600m gain on real estate and a property value of $1.7b. MPW did not publish the agreement confirming the 55% figure.

2022 Activity

Macquarie Transaction

On March 14, 2022, we completed a transaction with Macquarie Asset Management ("MAM"), an unrelated party, to form a partnership (the "Macquarie Transaction"), pursuant to which we contributed eight Massachusetts-based general acute care hospitals that are leased to Steward, and a fund managed by MAM acquired, for cash consideration, a 50% interest in the partnership. The transaction valued the portfolio at approximately $1.7 billion, and we recognized a gain on sale of real estate of approximately $600 million from this transaction, partially offset by the write-off of unbilled straight-line rent receivables. The partnership raised nonrecourse secured debt of 55% of asset value, and we received proceeds, including from the secured debt, of approximately $1.3 billion. We obtained a 50% interest in the real estate partnership valued at approximately $400 million (included in the "Investments in unconsolidated real estate joint ventures" line of our consolidated balance sheets), which is being accounted for under the equity method of accounting.

Figure 2 – MPW 2022 10-K

The terms of the Master Lease II laid out by Steward in their filing show this is likely exactly what happened. Steward's filing states base annual rent obligations of $114m at a current lease rate of 9.29%. Working backwards this results in a lease base of $1.23b.

Parties	Certain affiliates of Steward Health Care System LLC ("**Lessees**") Certain affiliates of MPT Operating Partnership, L.P. ("**Lessor**")
Lease Guaranty	Steward Health Care System LLC guarantees all of the obligations of each lessee under Master Lease II.
Commencement Date	March 14, 2022 (the "**Initial Commencement Date**").
Fixed Term	Commencing on the Initial Commencement Date and ending at midnight on October 31, 2041 (the "**Fixed Term**").
Extension Term	One (1) 5-year extension option available on the same terms and conditions set forth in Master Lease II.
Base Rent Obligations	The current annual base rent payable under Master Lease II is approximately $114 million
Lease Base	*See* Master Lease II, Schedule 3.1(a) for the lease base for each leased property as of the Initial Commencement Date.
Current Lease Rate	9.29%

Figure 3 – Steward Emergency Motion

This is substantially less than what MPW valued the property at in its books and suggests strongly to us that there is no basis for MPW's revaluation gains outside this purported 55% asset-to-loan value figure.

All this raises the question: did they conjure its $600m revaluation gain from nowhere?

They couldn't have picked a worse example

In its farcical lawsuit, MPW accused Viceroy of defamation for accusing it of purchasing hospital real estate at heavily inflated prices to support inflated lease bases and rents. In support of its position MPW leaned heavily on the Macquarie JV and its now dubious $1.7 billion valuation:

> 25. MPT's underwriting model has been tested and proved. In 2022, for example, private equity firm Macquarie Asset Management ("Macquarie") acquired as part of a 50/50 partnership with MPT a portfolio of eight Massachusetts hospitals for a total purchase price of about $1.7 billion. The transaction validated MPT's original underwriting: MPT had purchased these eight hospitals (plus a ninth) from hospital operator Steward Health Care System LLC ("Steward") in 2016 and 2018 for a combined cost of approximately $1.3 billion, and had then leased the premises to Steward as operator. The properties had performed as hoped, yielding approximately $475 million in income for MPT from 2016 to 2022, and then were sold at a healthy profit.

Figure 4 – MPW v. Viceroy Research

Steward's capitulation confirms that MPW's lawsuit against Viceroy, like its entire enterprise, is a sham built upon the lies and deceit of its corrupt and dishonest CEO and executive team. We don't think it's a coincidence that the best example MPW could find for its practices literally bankrupted the tenant.

The gig is up.

What's next

For years MPW has touted its investments as safe due to the nature of their leases, cross-default clauses and their purported ability to re-tenant hospitals at similar lease terms. Clearly this is not the case.

It's clear that MPW's entire book must be impairment tested and is grossly overvalued. We believe the only reason the company appears to be refusing to offer rent concessions or discounts is that it would trigger a disastrous revaluation.

As you can imagine we have very little faith in MPW's auditors PWC who have presided over this mess since 2008. We hope this serves as an extremely late wake-up call. Investors should ask themselves how many other skeletons are hiding in the closets in Birmingham.

Attention: Whistleblowers

Viceroy encourage any parties with information pertaining to misconduct within Medical Properties Trust, its affiliates, or any other entity to file a report with the appropriate regulatory body.

We also understand first-hand the retaliation whistleblowers sometimes face for championing these issues. Where possible, Viceroy is happy act as intermediaries in providing information to regulators and reporting information in the public interest in order to protect the identities of whistleblowers.

You can contact the Viceroy team via email on viceroy@viceroyresearch.com.

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