MPW – Under-Waterland

MPW engages in **marked-up uncommercial sale-leaseback deals** with European tenants, **paying up to 4.3x fair value**, **in order to finance tenants' loss-making operations**.

PLEASE READ IMPORTANT DISCLAIMER – PAGE 8

October 22, 2024 – In Q2 2023, MPW engaged in significant uncommercial round-trip transactions with its European tenants, Median and Priory Group, via sale-leaseback transactions[1]. Both **tenants are owned by Waterland Private Equity**, with minority interests from MPW.

MPW's assertions about the solvency of its tenants are fairytales told to shareholders and analysts. MPW's rent roll is almost exclusively distressed, and management continues to portray these tenants as not only a going concern, but a sound investment.

Priory Group

MPW consistently claims Priory Group, its third-largest tenant, is a well-capitalized and profitable machine. This is a lie. **Priory Group has been operationally loss-making for years** and relies on the proceeds of sale-leaseback transactions to remain solvent. Priory is MPW's third largest tenant by asset exposure, and largest unencumbered credit.

Priory Group operational losses widened to £73m in 2023.

Priory Group UK 1 Limited

Consolidated income statement for the year ended 31 December 2023

£'000	Note	Year ended 31 December 2023	Year ended 31 December 2022 (restated*)
Continuing operations			
Revenue	3	**767,552**	712,182
Operating costs	4	**(711,963)**	(671,352)
Exceptional items	7	**(57,024)**	11,143
Other operating income		**277**	277
Operating (loss)/profit		**(1,158)**	52,250
Analysed as:			
Adjusted EBITDA		**115,665**	102,384
Depreciation	11,12	**(59,799)**	(61,277)
Exceptional items	7	**(57,024)**	11,143
Operating (loss)/profit		**(1,158)**	52,250
Finance costs	8	**(72,002)**	(69,297)
Finance income	8	**765**	171
Loss before tax		**(72,395)**	(16,876)
Income tax	9	**28,439**	9,253
Loss for the year		**(43,956)**	(7,623)

Figure 1 – Priory 2023 Financial Accounts – P&L [2]

We note that Priory's rent is recorded as "finance costs". Why this is not included as operational expenses or in Priory's non-GAAP operational measurements (EBITDA) baffles us.

8. Finance income and finance costs

£'000	2023	2022
Finance costs		
Interest payable on intercompany loans	**20,049**	20,083
Interest on lease liabilities	**51,721**	49,196
Net cost on post-employment benefit	**112**	18
Net foreign exchange gain on intercompany loans	**(3)**	-
Other interest costs	**123**	-
	72,002	69,297

Figure 2 – Priory 2023 Financial Accounts – Note 8

[1] https://www.medicalpropertiestrust.com/press-release?page=https://medicalpropertiestrust.gcs-web.com/news-releases/news-release-details/medical-properties-trust-inc-reports-first-quarter-results-5
[2] https://find-and-update.company-information.service.gov.uk/company/09057543

Priory's EBITDA is further bumped by the exclusion of recurring "one time" costs.

7. Exceptional items

£'000	2023	2022 (restated*)
Reorganisation and rationalisation costs	86	1,802
Professional costs and other fees	348	5,472
Insurance proceeds	(4,399)	(2,000)
Impairment of property plant and equipment and right of use assets	67,067	29,143
Reversal of prior year impairments	(1,927)	(22,170)
Profit on disposal of property, plant and equipment, right of use assets and lease liabilities	(4,151)	(23,390)
	57,024	(11,143)

Figure 3 – Priory 2023 Financial Accounts – Note 7

Priory bleeds cash when accounting for recurring (and likely unrecoverable) working capital loans to related parties, reinvestment in PPE (maintenance capex), and rent (recorded as a "financing cash flow").

£'000	Note	Year ended 31 December 2023	Year ended 31 December 2022 (restated*)
Operating activities			
Operating (loss)/profit		(1,158)	52,250
Profit on disposal of property, plant and equipment		(4,151)	(23,390)
Depreciation of property, plant and equipment and right of use assets		59,799	61,277
Net impairment of non-current assets		65,139	6,973
Decrease/(increase) in inventories		6	(29)
(Increase)/decrease in trade and other receivables		(4,707)	11,946
Decrease in trade and other payables		(1,533)	(1,097)
Post-employment benefits		(2,250)	(2,250)
		111,145	105,680
Taxation received		7,238	881
Net cash generated from operating activities		118,383	106,561
Investing activities			
Interest income		687	92
Proceeds from disposal of property, plant and equipment		18,154	12,262
Purchases of property, plant and equipment		(32,666)	(38,359)
Proceeds from sale and leaseback transaction		43,698	-
Loans to group companies		(82,632)	(30,541)
Net cash used in investing activities		(52,759)	(56,546)
Financing activities			
Repayment of obligations of principal under lease liabilities		(11,626)	(10,358)
Interest paid on lease liabilities		(51,721)	(49,196)
Other interest paid		(123)	-
Net cash used in financing activities		(63,470)	(59,554)

Figure 4 – Priory 2023 Financial Accounts

MPW reports Priory's EBITDARM rent coverage at 2.2x in its Q4 2023 supplemental. This figure blatantly misrepresents Priory's actual financial condition.

EBITDARM RENT COVERAGE: OPERATORS WITH PROPERTY-LEVEL REPORTING

Tenant	Net Investment (in thousands)[A]	Primary Property Type	TTM EBITDARM Rent Coverage
Steward Health Care[B]	$ 2,342,414	General Acute	N/A
Priory Group	1,227,168	Behavioral	2.2x

Figure 5 – MPW Q4 2023 Supplemental[3]

[3] https://medicalpropertiestrust.gcs-web.com/static-files/f061e036-5020-45d1-a597-6df85c4d381e

Viceroy calculates Priory's pre-rent-FCF rent coverage at 0.06x in 2023.

Priory FCF Rent Coverage ($000s)	2023	2022
Cash from operating activities	118,383	106,561
Less:		
Capex	(32,666)	(38,359)
WC Loans to off-balance sheet related parties	(82,632)	(30,541)
Free cash flow before rent	**3,085**	**37,661**
Rent	(63,347)	(59,554)
Rent coverage ratio	**0.05**	**0.63**
Free cash flow	**(60,262)**	**(21,893)**

Figure 6 – Viceroy Analysis

Priory carries £203m negative equity, having accumulated £926m of losses to 2023.

£'000	Note	31 December 2023	31 December 2022 (restated*)	1 January 2022 (restated*)
Non-current assets				
Intangible assets	10	1,619	-	-
Property, plant and equipment	11	410,523	461,090	484,454
Right of use assets	12	528,969	557,015	554,569
		941,111	1,018,105	1,039,023
Current assets				
Net investment in finance leases	12	-	-	302
Inventories	13	491	497	468
Trade and other receivables	14	146,025	69,394	81,910
Corporation tax recoverable		-	10,769	7,763
Cash	15	12,673	10,519	20,058
		159,189	91,179	110,501
Assets held for sale	16	2,221	7,944	500
		161,410	99,123	111,001
Total assets		1,102,521	1,117,228	1,150,024
Current liabilities				
Trade and other payables	17	(81,048)	(98,315)	(124,636)
Corporation tax payable		(164)	-	(7,739)
Lease liabilities	12	(54,988)	(52,761)	(54,790)
Borrowings	18	(21,396)	(20,363)	(19,295)
Provisions	19	(13,995)	(15,273)	(15,457)
		(171,591)	(186,712)	(221,917)
Net current liabilities		(10,181)	(87,589)	(110,916)
Non-current liabilities				
Lease liabilities	12	(829,440)	(773,825)	(776,980)
Borrowings	18	(299,167)	(280,151)	(261,136)
Deferred income tax	20	(2,831)	(31,489)	(35,949)
Pension liability	21	(3,371)	(3,370)	(2,147)
		(1,134,809)	(1,088,835)	(1,076,212)
Net liabilities		(203,879)	(158,319)	(148,105)
Equity attributable to the owners of the parent:				
Share capital	22	74,984	74,984	74,984
Share premium account		647,240	647,240	647,240
Accumulated losses		(926,103)	(880,543)	(870,329)
Total equity		(203,879)	(158,319)	(148,105)

Figure 7 – Priory 2023 Financial Accounts – Balance Sheet

Priory's working capital ratio is 0.9x, meaning there is currently £0.9 of current assets to every £1 of current liabilities. Of these current assets, 50% are what appear to be zero-interest working capital loans Priory make to related parties.

14. Trade and other receivables

£'000	2023	2022
Trade receivables	46,059	39,770
Allowance for doubtful debts	(989)	(1,737)
	45,070	38,033
Amounts owed by group undertakings	73,826	2,643
Other receivables	10,932	9,417
Prepayments and accrued income	16,197	19,301
	146,025	69,394

Amounts owed by group undertakings include £2.6m (2022: £2.6m) relating to an unsecured loan with RemedcoUK Limited, interest accrues at 3.0% p.a. Remaining amounts are interest free and repayable upon demand.

Figure 8 – Priory 2023 Financial Accounts – Note 14

These WC loans to related parties were previously treated as operational outflows and were reclassified in 2023. They have almost tripled year-on-year to 2023.

2022 Cash Flows

£'000	Note	Year ended 31 December 2022	Year ended 31 December 2021 (restated*)
Operating activities			
Operating profit		41,203	74,696
Profit on disposal of property, plant and equipment		(23,390)	(44,409)
Depreciation of property, plant and equipment and right of use assets	12	61,014	71,775
Amortisation of intangible assets	4	-	-
Net impairment of non-current assets	7	18,283	39,326
Non-cash exceptional items		-	1,403
(Increase)/decrease in inventories		(29)	71
Decrease/(increase) in trade and other receivables		9,302	(16,553)
(Decrease)/increase in trade and other payables		(28,994)	25,209
Post-employment benefits		(2,250)	(1,780)
		75,139	149,738
Taxation		881	(67,425)
Net cash generated from operating activities		76,020	82,313
Investing activities			
Interest income	8	92	56
Proceeds from disposal of property, plant and equipment		12,262	13,360
Purchases of property, plant and equipment		(38,359)	(44,301)
Proceeds from sale and leaseback transaction		-	801,252
Proceeds from sale of Education division (less divested cash)		-	138,292
Net cash (used in)/generated from investing activities		(26,005)	908,659

2023 Cash Flows

£'000	Note	Year ended 31 December 2023	Year ended 31 December 2022 (restated*)
Operating activities			
Operating (loss)/profit		(1,158)	52,250
Profit on disposal of property, plant and equipment		(4,151)	(23,390)
Depreciation of property, plant and equipment and right of use assets		59,799	61,277
Net impairment of non-current assets		65,139	6,973
Decrease/(increase) in inventories		6	(29)
(Increase)/decrease in trade and other receivables		(4,707)	11,946
Decrease in trade and other payables		(1,533)	(1,097)
Post-employment benefits		(2,250)	(2,250)
		111,145	105,680
Taxation received		7,238	881
Net cash generated from operating activities		118,383	106,561
Investing activities			
Interest income		687	92
Proceeds from disposal of property, plant and equipment		18,154	12,262
Purchases of property, plant and equipment		(32,666)	(38,359)
Proceeds from sale and leaseback transaction		43,698	-
Loans to group companies		(82,632)	(30,541)
Net cash used in investing activities		(52,759)	(56,546)

X3

Figure 9 – Priory 2023 Cash Flows vs Priory 2022 Cash Flows

Priory has not disclosed why these outflows were restated or what the loans were for. Given that they have not been recouped, and carry zero interest, we believe these loans to group companies are disguised operating expenses and are uncollectable.

Median

Like Priory, MPW has consistently claimed that Median is well-capitalized and profitable. This is also untrue. This is a lie. **Median** scraped by with an operational margin of 2% in 2023 and posted €100m of losses over the last 2 years due to a commercially unsustainable capital structure.

Median relies on the proceeds of sale-leaseback transactions to remain solvent. In 2023, MPW engaged in a sale-leaseback transaction with Median in which it purchased €16.1m worth of real estate for €70m (**representing a 335% mark-up**), resulting in a €53.9m gain on sale to Median[4].

Sale-and-Lease-back

In April and June 2023, the German group completed a Sale-and-Lease-back transaction whereby a freehold property was sold to corporate entities controlled by Medical Properties Trust, Birmingham, USA (MPT, who is a minority shareholder of the Median B.V. Group). The net consideration received amounted to EUR 70 million.

Fixed assets with a carrying value of EUR 16.1 million were disposed and leased back of as part of this transaction, realising a profit on disposal of EUR 53.9 million.

Figure 10 – Median 2023 Financial Accounts

Median is severely cash-flow deficient and recorded €111m of Free Cash Flow losses across 2022 and 2023.

		2023		2022	
		EUR'000	EUR'000	EUR'000	EUR'000
Operating result		**45,551**	-	**(8,602)**	-
Adjusted for:					
- Gains and losses from disposals of fixed assets	15, 17	**(56,517)**	-	(21,669)	-
- Refinancing Fees		**768**	-	2,070	-
- Depreciation/amortisation	20	**143,604**	-	116,073	-
- Expense or income, but non-cash item		**(769)**	-	(459)	-
- Change in provisions	9	**(1,777)**	-	(1,198)	-
- Changes in working capital		**(48,224)**	-	(11,610)	-
Cash flow from business operations		-	**82,636**	-	74,605
Interest received		**1,515**	-	163	-
Interest paid		**(60,204)**	-	(60,942)	-
Income tax paid	24	**(2,763)**	-	(18,278)	-
Cash flow from operating activities		-	**21,184**	-	(4,452)
Investments in:					
- Acquisition of group companies (net of cash received)		**(127,630)**	-	(60,268)	-
- Intangible fixed assets		**(5,111)**	-	(5,940)	-
- Tangible fixed assets		**(58,904)**	-	(69,168)	-
Disposals of:					
- Intangible fixed assets		**(7)**	-	13	-
- Tangible fixed assets		**143,291**	-	39,326	-
- Financial fixed assets		**356**	-	3,629	-
Cash flow from investing activities		-	**(48,005)**	-	(92,408)

Figure 11 – Median 2023 Financial Accounts – Cash Flow

Despite this, MPW reports that Median operates at a 1.7x EBITDARM coverage in 2023 (which is incredibly low).

Tenant	Net Investment (in thousands)[(A)]	Primary Property Type	TTM EBITDARM Rent Coverage
Steward Health Care	$ 2,434,365	General Acute	2.9x
Priory Group	1,179,310	Behavioral	2.2x
MEDIAN	591,196	IRF	1.7x

Figure 12 – MPW Q2 2023 Supplemental

Median cannot support MPW's rent.

[4] https://www.unternehmensregister.de/ureg/

Waterland Private Equity

We note that Priory and Median's sale-leaseback transactions in 2023 follow much larger sale-leaseback transactions in prior periods. These are covered in our preliminary report:

Annexure 8 – Priory Transaction

In December 2020 owners of Median Kliniken, Waterland Private Equity, acquired UK-based Priory Group from Acadia Healthcare for £1,078m[42]. Both Median Kliniken & Priory were MPW hospital operators, so the transaction consolidated MPW's 4th and 5th largest tenants by lease assets at the time.

Acadia purchased this business for £1.3b in 2016 and put it back on the market just 2 years later.

MPW financed Waterland's entire transaction with a £1,050m loan: £800m mortgage loan against 35 properties from Priory, and a further £250m acquisition loan secured against the same properties. The mortgage loan would be converted into ownership of those properties in June 2021. MPW received a 9.9% stake in Waterland's Priory fund for an *additional* "nominal amount".

PORTFOLIO UPDATE

During and subsequent to the first quarter, MPT continued to execute on accretive acquisitions.

MPT expects to replace the £800 million Priory real estate loan with sale-leaseback transactions involving 35 properties by the end of the second quarter, at which time the Company will begin to recognize a GAAP investment yield of 8.6%.

2021 Activity

Priory Group Transaction

On January 19, 2021, we completed the first of two phases in the Priory Group ("Priory") transaction in which we funded an £800 million interim mortgage loan on an identified portfolio of Priory real estate assets. In phase two, in a series of transactions we expect will be completed during the 2021 second quarter, we will acquire a portfolio of select real estate assets from Priory (now owned by Waterland Private Equity Fund VII C.V. ("Waterland VII")) in individual sale-and-leaseback transactions, subject to customary real estate and other closing conditions. As all conditions to closing for a particular asset are satisfied, the applicable purchase price for the asset will be paid by us by proportionally converting and reducing the principal balance of the interim mortgage loan we made to Waterland VII in phase one. The aggregate purchase price for the real estate assets we acquire from Priory is thus expected to be approximately £800 million, plus customary stamp duty, tax, and other transaction costs.

In addition, we agreed to provide Waterland VII with a 364-day £250 million acquisition loan, which we funded on January 19, 2021, in connection with the closing of Waterland VII's acquisition of Priory. The loan is secured by the same security assets securing the £800 million interim mortgage loan.

In connection with these transactions, we also acquired a 9.9% passive equity interest in the Waterland VII affiliate that indirectly owns Priory for a nominal amount.

Figures 51 & 52 – MPW Q1 2021 results and 10-Q[43]

MPW claimed that this £1,050m loan was collectively secured against a subset of Priory's properties.

However Acadia's 2020 10-K shows the Priory business consisted of "345 inpatient behavioral health facilities with approximately 8,200 beds" of which 279 were owned and 66 leased. The PPE assets for the sale were valued at $1.298m (£949m) at the lesser of carrying value and fair value less costs to sell.

40 states, the United Kingdom ("U.K.") and Puerto Rico. During the year ended December 31, 2020, we added 460 beds in the United States ("U.S."), consisting of 240 added to existing facilities and 220 added through the opening of two joint venture facilities, and we opened six comprehensive treatment centers ("CTCs"). On January 19, 2021, we completed the sale of the U.K. business, which included 345 facilities and approximately 8,200 beds.

children's services facilities and approximately 60% were adult care facilities at December 31, 2020. At December 31, 2020, we owned 279 of the properties at our U.K. Facilities and leased 66 properties.

It seems MPW believed the 35 properties were worth £800m. It is absurd to suggest that the remaining Priory business *and* a further 244 properties were worth only £250m. For MPW's financing to make any sense the entire Priory business less property would be valued close to zero.

A back-of-envelope calculation assuming homogenous property values across the portfolio suggests an overpayment of at least £600m.

Figure 13 – Viceroy Research – Medical Properties (dis)Trust[5]

[5] https://viceroyresearch.org/wp-content/uploads/2023/01/Viceroy-Research-MPW-26-Jan-2023.pdf

Upon the sale-leaseback transactions in 2023, a Priory spokesperson told The Times that they had "no concerns about our ability to meet operational costs" and had "safeguards within our leases" to protect themselves. Clearly, these are not working out.

> The deal comes after Waterland Private Equity funded its purchase of The Priority Group through the sale and leaseback of 40 of the latter's hospitals to raise £800 million in 2021. A Priory spokeswoman said sale- and-leaseback deals were a "well- established and secure method of financing, when managed correctly. We have no concerns about our ability to meet operational costs and invest in our services. There are safeguards within our leases to protect against rising costs and rent is a comparably small proportion of our overall cost structure. In fact, with rental costs below inflation, there is less financial pressure on organisations paying rent rather than those incurring higher interest rates on debt."

Figure 14 – Priory Group adds another sale and leaseback[6]

[6] https://www.thetimes.com/article/priory-group-adds-another-sale-and-leaseback-n5nhvk3t0

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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