



Valuation

Normalization of the historical discount drives our TP

MPW currently trades at wider-than-historical FFO and AFFO multiple discounts versus its smaller-cap Healthcare REIT peers. While MPW's trading risk (liquidity and daily return volatility) and financial risks are similar to or better than the peers', we view operational risks inherent in the acute care hospital space as above average. With none of MPW's peers focused on this slice of the Healthcare real estate spectrum, these risks are unique to MPW and as such we believe a discount is warranted. However, we think there are several reasons why MPW should, at a minimum, trade in line with historical relative valuations including: 1) earnings upside from accretive acquisitions with our current forward estimates embedding only about half of the average level of annual acquisitions over the past 10 years, creating upside risk to our earnings estimates; 2) VTR's entry into the hospital space, which should drive greater price transparency and awareness that may open new opportunities as more hospitals consider selling real estate; and 3) substantial improvements in the scale/diversification of MPW's business versus history.

...attractive dividend should provide a floor

On a dividend yield basis, MPW trades ~90bps wide of its peers at an elevated 6%, with an in-line AFFO payout ratio of about 78%. We view the dividend as downside protection with a basic dividend discount model suggesting \$14 per share of value using an ~8.5% cost of equity (based on a normalized 10-year rate of 2.5%) and a 1.5% long-run growth rate. This suggests 10% downside from recent levels.

Expecting a 15% total return to our \$17 target price

We are establishing a target price of \$17 per share, which equates to a 15% expected total return including the roughly 6% dividend yield. Our target price is based on a 14.3x multiple applied to our 2017 AFFO estimate of \$1.19. Our 14.3x multiple is rich by historical standards, but not relative to the historically low rate environment, and is a 3.5-turn discount to peers, roughly in line with the 5-year average. We are comfortable in applying a well-above-historical-average multiple given the current historically low interest rate environment and our house view calling for a sustained low interest rate environment through 2017. Future upside could stem from greater acceptance of the hospital property type by institutional investors, which we believe would warrant a narrowing of the historical discount to MPW's peers and, via earnings upside as we are forecasting only a modest level of acquisitions in our forward estimates despite MPW's historical success in acquiring assets at attractive spreads to its cost of capital.

While NAV is typically the basis for our target prices, with fewer private market comps than in the senior housing sector and the spread-investment nature of the hospital space, we believe an earnings multiple based approach is more appropriate. However, on an NAV basis, our \$17 target price equates to roughly a 16% premium to our NAV estimate, which itself is based on an 8% cap rate on our 2-year forward NOI estimate. This premium to NAV is in line with historical levels.