Research Update:

Ventas Inc. Outlook Revised To Negative From Stable On Deteriorating Operating Performance From COVID-19

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Rating Action Overview

- We expect Ventas Inc.'s operating performance to deteriorate materially over the coming months because the COVID-19 pandemic is significantly increasing costs and simultaneously weakening occupancy at senior housing properties.
- We are revising our outlook to negative from stable and affirming our 'BBB+' issuer credit rating on the company.
- The negative outlook reflects our view that the company's senior housing assets will remain under significant pressure for the duration of the pandemic, with sharp declines in same-store net operating income (NOI) within the seniors housing operating portfolio (SHOP) and material rent reductions at triple-net leased properties.

Rating Action Rationale

The COVID-19 pandemic will likely pressure Ventas' assets significantly, particularly senior housing properties. As of March 31, 2020, 55% of Ventas' NOI was generated from senior housing facilities, including 33% from SHOP assets. While SHOP assets will incur cash flow pressure immediately, thinly covered triple-net leased assets will also require significant rent reductions, in our view. We think senior housing properties are vulnerable to cash flow pressure during the COVID-19 pandemic for the following reasons:

- Seniors housing residents are commonly in their mid-80s with a heightened risk for death (globally, 10%-15% of people 80 and older who have contracted the virus have died). Increased deaths from COVID-19 could accelerate the natural rate of attrition at these communities.
- Move-ins, while still occurring in many communities, have slowed considerably, given shelter-in-place mandates and the fact most tours are virtual only. Many facilities are also restricting move-ins to ensure the health and safety of residents. We also think media reports regarding risks related to senior living communities could also slow the pace of move-ins until

there is a vaccine, given the fears of contagion.

- Across the industry, operating costs for senior housing operators are up approximately 10% nationally, with significant pressure on labor costs and personal protective equipment (e.g., gowns, masks, and gloves).
- Seniors housing operators aren't eligible for explicit health care grants under the Coronavirus Aid, Relief, and Economic Security (CARES) Act because the industry is predominantly private-pay, while other health care facility types will have better access to government relief. Moreover, we think the majority of operators are too large to qualify for the Paycheck Protection Program.

Operating performance is likely to weaken meaningfully, but Ventas maintains good asset quality and relatively good diversification across its facility types. We acknowledge a wide variety of potential outcomes related to the duration of the pandemic and whether there will be multiple waves of COVID-19 cases (that further pressure occupancy). That said, we assume senior housing assets will exhibit significant stress throughout the remainder of 2020, even without additional waves.

We assume SHOP assets (33% of NOI) will be the most affected by COVID-19. Ventas' assets are relatively well-located in high-barrier markets with other strong characteristics such as high median household incomes and household values, above-average revenue per occupied room (REVPOR), and solid occupancy relative to peers. That said, Ventas' SHOP portfolio was likely to incur significant same-store NOI declines in 2020 even before the pandemic. The company posted a same-store NOI decline of 10.4% in the first quarter. Moreover, its SHOP portfolio declined 330 basis points (bps) in April and had estimated occupancy of just 80.7% on May 1. We expect it will decline to the mid- to high-70% area by the end of the second quarter but, barring an additional wave of COVID-19 cases that prompts continued move-in restrictions, will start to stabilize there. We assume relatively flat REVPOR in 2020, combined with operating expenses rising in the high-single-digit to low double-digit percentage area to further pressure NOI.

Ventas' other assets will also face pressure to varying degrees. The triple-net seniors housing assets (22% of NOI) will face similar pressure to the SHOP portfolio, albeit on a lag. Since tenant-level rent coverage is quite thin (1.1x across the whole portfolio), a significant number of leases will likely require amendments with reduced rent. In particular, about 15% of NOI is generated from senior housing triple-net leased properties where rent coverage is below 1.2x. We think most of those leases are likely to require concessions given the pressure created by COVID-19. While the company's medical office buildings (MOBs; 20%) should generate more stable cash flows, we still expect a fair amount of rent deferrals (since the majority of elective outpatient procedures have been postponed) although we expect almost all rents to ultimately be collected. Ventas' research and innovation segment (7%) is composed of academic life sciences buildings, which we expect to continue to pay their full rental obligations throughout this pandemic. Inpatient rehabilitation facilities (IRFs), long-term acute care facilities (LTAC, 7%), and health systems (6%) should benefit from significant government grants from the CARES Act, and we expect the vast majority of rent to be collected from these facilities.

We expect Ventas' credit protection measures to weaken modestly. Despite tremendous near-term pressure facing the business, we think the impact to credit metrics will be more modest. Going into 2020, we expected Ventas to make a concerted effort to reduce leverage (adjusted debt to EBITDA was 6.5x at year-end 2019, with fixed-charge coverage [FCC] of 3.9x) by selling significantly more assets than it acquired. In the first quarter, Ventas reduced leverage by receiving $109.3 million in disposition proceeds and loan repayments, and raised an additional

$620.1 million through the joint venture formation of Ventas Life Science & Healthcare Real Estate Fund. By contrast, acquisitions were just $79.6 million in the quarter. Moreover, subsequent to the first quarter, Ventas received $34 million in cash from Holiday Retirement (one of its operators) for terminating the lease agreement on 26 independent living facilities and transitioning them to SHOP assets. Ventas will also collect $66 million in a five year note (with a blended yield of 7.0% per annum) after granting a secured loan to the prior guarantor of the Holiday lease and certain Holiday affiliates.

While transactions are more challenging to execute in this environment, we think there is a good chance Ventas can mitigate some of its cash flow deterioration by executing on additional asset sales, although they could be largely on pause in the second quarter. Moreover, we expect the company to reduce development spending and other capital expenditures (capex) by around $300 million in 2020 to further conserve capital. There could also be a dividend cut if operating performance continues to deteriorate.

As a result, we project Ventas' adjusted debt to EBITDA to rise to the high-6x to mid-7x area from the low-6x area at the end of the first quarter, with FCC declining to the low-3x area.

Environmental, social, and governance (ESG) credit factors for this rating change:

- Health and safety

Outlook

The negative outlook on Ventas reflects our view that its seniors housing assets will remain under significant pressure for the duration of the COVID-19 pandemic, with sharp declines in same-store NOI within the SHOP segment and material rent reductions likely at triple-net leased properties. While there is a high degree of uncertainty in our projections, we expect Ventas' credit protection measures will deteriorate modestly, with FCC declining to the low-3x area and adjusted debt to EBITDA rising to the high-6x to mid-7x area in 2020 before improving modestly in 2021.

Downside scenario

We could lower the rating if:

- Operating performance deteriorates beyond our expectations, without a subsequent strong recovery in 2021, somewhat impairing our view of the business.
- Credit protection measures weaken more than our forecast, with FCC declining below 3x or adjusted debt to EBITDA rising to and remaining above 7x for a sustained period.

Upside scenario

We could revise the outlook to stable if:

- Ventas successfully manages through the operating pressure stemming from its large exposure to senior housing assets, with occupancy stabilizing from increased move-ins.
- Adjusted debt to EBITDA is sustained in the mid-6x area or lower with FCC above 3x, perhaps the result of asset sales combined with steadier operating performance.

Company Description

Ventas, the second-largest health care REIT, owned 1,201 health care properties throughout the U.S., Canada, and the U.K. with undepreciated real estate investments totaling roughly $29 billion as of March 31, 2020. This diversified portfolio comprises seniors housing facilities, which accounted for 55% of the company's annualized NOI, split between investments structured through the REIT Investment Diversification and Empowerment Act (33%) and triple-net leases (22%); MOBs (20%); research and innovation (7%); IRFs and LTACs (7%); health systems (6%); and other facilities/investments (6%).

Our Base-Case Scenario

- As the coronavirus pandemic escalates and economic activity declines amid a backdrop of volatile markets and increasing credit stress, S&P Global Ratings economists now project a 5.2% decline in U.S. real GDP this year followed by a 6.2% increase in 2021;
- We acknowledge many possible outcomes, but we project same-property NOI to decline 10%-20% in 2020, followed by a relatively sharp rebound in 2021. The variance and uncertainty is largely tied to the potential for additional waves of COVID-19 cases that exacerbate deaths and slow move-ins to seniors housing properties;
- We project acquisitions of less than $500 million in 2020, followed by $500 million-$1 billion in 2021;
- Development funding will be $300 million-$350 million in 2020 and approximately $600 million in 2021;
- Dispositions will be $1 billion-$1.5 billion in 2020 (including proceeds raised by the joint venture formation of the Ventas Life Sciences & Healthcare Real Estate Fund) and $1 billion in 2021; and
- We do not project any equity issuance in 2020, but expect modest issuance in 2021 as a source of capital to fund acquisitions.

Based on these assumptions, we arrive at the following credit metrics:

- Debt to EBITDA in the high-6x to mid-7x area over the next two years;
- FCC in the low- to mid-3x range; and
- Debt to undepreciated capital in the low-40% area.

Liquidity

Our short-term rating on Ventas is 'A-2', which reflects our long-term rating on the company and our assessment of its liquidity as strong. We expect Ventas' liquidity sources to be at least 1.5x its uses over the next 12 months and anticipate they will remain positive even if its EBITDA declines by 15% (a REIT-specific threshold for strong liquidity). We believe the company has sufficient covenant headroom for its forecast EBITDA to decline by 15% without causing it to breach any covenant tests. We also believe Ventas would likely absorb high-impact, low-probability events without refinancing, and view it as having a generally high standing in the credit markets and well-established relationships with its banks.

Principal liquidity sources:

- $2.8 billion in unrestricted cash and equivalents as of March 31, 2020;
- Approximately $110 million of availability under the $3 billion revolving credit facility that matures in April 2021 (excluding two six-month extensions at the company's option);
- Approximately $250 million availability on a secured revolving construction facility that matures in 2022;
- $500 million in unsecured notes that settled April 1, 2020;
- $34 million cash received subsequent to the first quarter from the termination of a lease agreement with Holiday retirement; and
- Annual funds from operations of approximately $1 billion-$1.3 billion over each of the next two years.

Principal liquidity uses:

- Principal mortgage amortization payments of approximately $20 million-$30 million per year;
- Maintenance capex of approximately $150 million-$180 million annually;
- Unfunded active development and redevelopment projects totaling approximately $1.02 billion as of March 31, 2020 (most projects are either in the construction loan or have committed mortgage financing); and
- Common dividends between $900 million and $1.2 billion per year.

Ratings Score Snapshot

Issuer Credit Rating	BBB+/Negative/A-2
Business risk	Satisfactory
Country risk	Very low
Industry risk	Low
Competitive position	Satisfactory
Financial risk	Modest
Cash flow/Leverage	Modest
Anchor	bbb+
Modifiers	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Neutral (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | Industrials: Key Credit Factors For The Real Estate Industry, Feb. 26, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- REITrends: COVID-19 Could Threaten Stability For North American REITs, March 17, 2020
- Waiting Is The Hardest Part: Seniors Housing-Focused REITs Await The "Silver Tsunami", Feb. 10, 2020

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Ventas Inc.		
Ventas Capital Corp.		
Nationwide Health Properties Inc.		
Issuer Credit Rating	BBB+/Negative/--	BBB+/Stable/--
Ventas Realty L.P.		
Issuer Credit Rating	BBB+/Negative/A-2	BBB+/Stable/A-2
Senior Unsecured	BBB+	
Commercial Paper	A-2	
Nationwide Health Properties Inc.		
Senior Unsecured	BBB+	
Ventas Canada Finance Ltd.		
Senior Unsecured	BBB+	

Ratings Affirmed; Outlook Action

	To	From
Ventas Capital Corp.		
Senior Unsecured	BBB+	