The Deal

Ventas pays C$2.1B for Sunrise

by David Elman

Only two months after acquiring 64 properties from Canada's Reichmann family, **Ventas Inc.** is making another big deal.

The Louisville, Ky.-based healthcare REIT and **Sunrise Senior Living REIT** announced in separate statements Monday, Jan. 15, that Ventas will pay C$15 per unit for the Toronto-based owner of 74 assisted living communities. Including the assumption of C$1 billion in debt, the deal is valued at C$2.14 billion ($1.83 billion).

Analysts said the 6.2% net operating income yield on the deal and the 35.7% premium to the stock price of Sunrise REIT appeared expensive but in line with the valuation of recent deals.

"I think the price is aggressive, though not as aggressive as a couple of other big deals," **KeyBanc Capital Markets** analyst Karin Ford said.

She pointed to **Fortress Investment Group LLC**'s December announcement that it would pay an undisclosed price — rumored to be $6.5 billion — for 299 senior living communities of **Holiday Retirement Corp.** New York-based Fortress probably received a capitalization rate 50 basis points below that of the Sunrise deal, Ford said.

The deal marks Ventas' entry into Canada, with the acquisition of 11 properties plus an additional community in development.

All told, Ventas said it plans to acquire five Sunrise communities in the U.S. and Canada under development, and it retains a right of first offer to acquire new properties.

Sunrise affiliate Sunrise Senior Living Inc., which developed the properties and has a 15% to 25% minority interest in 56 of the assets, will continue to manage the assisted living communities. McLean, Va.-based Sunrise does not have a stake in Sunrise REIT, president and CEO Douglas J. MacLatchy said.

Ventas will add a Sunrise portfolio of roughly 6,000 suites in 17 states, British Columbia and Ontario to its existing collection of 454 independent and assisted living facilities, hospitals, skilled nursing facilities and medical office buildings in 43 states. As a result, Ventas said, its portfolio will become more diversified by tenant and asset class.

Cap rates are declining in senior housing assets because of fairly high occupancies, low levels of new supply, improved demographics and a stable regulatory environment, KeyBanc's Ford said.

Although the Fortress and Ventas deals have been the only large transactions lately involving senior housing, she believes there will be continued capital interest in the space because healthcare has typically been valued at a 30% discount to the rest of the real estate sector.

UBS Securities LLC analyst Omotayo Okusanya II said that smaller, pure-play healthcare real estate companies, especially in the assisted living, skilled nursing, or medical office building segments, were likely targets in future deals. He cited **Senior Housing Properties Trust** and financing **REIT Omega Healthcare Investors Inc.**

Okusanya left his Buy 2 rating and $50 price target unchanged. He noted that the Sunrise REIT purchase had very minimal tax consequences and that a potential change in REIT legislation would make it even easier for Ventas to boost revenue.

The analyst said he liked the right of first refusal Ventas obtained, as well as that Sunrise assets tended to be best in class with occupancy rates higher than the industry average. In addition, the average resident at a Sunrise property pays $5,400 per month, versus a $3,000 national average, he said.

Ford reiterated her buy rating on Ventas.

"The main takeaway on the deal is that Ventas is going to double its internal rate of growth," she said, through the creation of a taxable REIT subsidiary that will own the Sunrise REIT assets and pay Sunrise a management fee. The growth will offset estimated dilution of 2007 funds from operations per share of 5

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cents to 7 cents, according to the analyst.

Okusanya pointed in a research note to an improved development pipeline and platform, increased exposure to private pay revenue sources and a lower exposure to Ventas' largest tenant, **Kindred Healthcare Inc.** The Louisville, Ky.-based healthcare services company will provide an estimated 30% of revenue, down from 46%.

"This transaction will add 74 exceptional private pay assets to our diverse high-quality portfolio and is expected to increase our revenue from private pay assets to approximately two-thirds of our total revenue. The acquired assets are all new assisted living communities located in large metropolitan areas, with high barriers to entry, and extraordinary growth prospects," Ventas chairman, president and CEO Debra A. Cafaro said in a statement.

"There are very, very strong fundamentals in the senior housing business right now," Cafaro said in an interview.

Private pay assets — where residents are not reimbursed by Medicare or Medicaid — are considered desirable because of fundamentals and the supply-demand dynamic, she said.

Ventas will fund the deal with interim financing from **Merrill Lynch & Co.**

Cafaro said that, despite having to focus on integrating the Sunrise assets and closing the transaction, Ventas is developing prospects for long-term financing.

"Over the past year, the [Sunrise REIT board of trustees], together with its financial advisors, reached the conclusion that our units were undervalued in the market and that there was an opportunity to unlock significant value for unitholders," said Michael Warren, chairman of the board of Sunrise REIT, in a release. "We initiated a process to achieve value maximization for our unitholders. We have clearly achieved that."

The deal comes at a 35.7% premium to the C$11.05 closing price of Sunrise REIT units Jan. 12 on the Toronto Stock Exchange.

MacLatchy would not comment on the sales process beyond the statement. He did, however, say that Sunrise REIT reasonably canvassed the market and that Ventas was one of the companies Sunrise approached.

"It was a standard seller process," Cafaro said.

Sunrise REIT shares rose 34.8% Monday on the Toronto Stock Exchange to C$14.90.

Sunrise shares were up $2.12 Tuesday afternoon to $34.92, while Ventas shares were up 54 cents to $43.15.

Sunrise REIT unit holders will vote on the deal at a meeting set to occur by March 31. Ventas and Sunrise expect the deal to close shortly afterward.

Sunrise REIT cannot solicit other bids, but Ventas has the right to amend its offer if Sunrise declares another bid superior. If the REIT did not pursue a transaction with Ventas, it would receive a breakup fee of C$39.8 million under certain circumstances.

Alan Hartman, Anthony Streich, Chris Kolenaty, Christine Bergmann and James Forbes of Merrill Lynch were financial adviser to Ventas.

Adam O. Emmerich, Trevor S. Norwitz, Joseph D. Larson, Robin Panovka, Philip Mindlin and David M. Einhorn led a **Wachtell, Lipton, Rosen & Katz** team that provided legal counsel with **Osler, Hoskin & Harcourt LLP** to Ventas.

TD Securities Inc. supplied a fairness opinion to a special committee of independent Sunrise trustees.

Stikeman Elliott LLP was legal counsel to Sunrise REIT. ■

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