

# The Gaming REITs



**Sector Primer 2019**

*This is not a Green Street Advisors Research Report*



Green Street Advisors  
— ADVISORY & CONSULTING GROUP —



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**Section I.**

# **Executive Summary**



# Executive Summary

<b>Gaming REITs</b>	<ul style="list-style-type: none"><li>• There are three net lease REITs that specialize in the ownership of gaming assets<ul style="list-style-type: none"><li>◦ Gaming and Leisure Properties (GLPI); came public in 2013</li><li>◦ MGM Growth Properties (MGP); came public in 2016</li><li>◦ VICI Properties (VICI); came public in 2018</li></ul></li></ul>
<b>Net Lease Structure</b>	<ul style="list-style-type: none"><li>• Under a net lease, the tenant pays the property expenses, insurance, taxes, and capital expenditures</li><li>• This structure is known as a “triple-net lease” or “NNN lease”</li><li>• Most publicly-traded NNN REITs primarily own properties leased to retailers</li><li>• Many health care REITs also own properties that are leased to operators through NNN leases</li></ul>
<b>Net Lease Attributes</b>	<ul style="list-style-type: none"><li>• The consistency of the cash flows generated by long-term, NNN leases is appealing to REIT investors</li><li>• Having the tenant – not the property owner – foot the cap-ex bill is another attractive attribute</li><li>• The NNN and health care sectors have consistently traded at valuation premiums</li></ul>
<b>Gaming Sector</b>	<ul style="list-style-type: none"><li>• The gaming REIT sector is relatively new; investors are still assessing how the companies should be valued</li><li>• The purpose of this industry primer is to help investors better understand the sector</li></ul>
<b>Gaming Industry</b>	<ul style="list-style-type: none"><li>• Gaming is a mature industry in the U.S. that is comprised of nearly 1,000 properties</li><li>• Gaming demonstrated less volatility during the GFC than other real estate sectors</li><li>• Gaming is an operationally complex business where scale provides a huge advantage</li><li>• Consequently, there is a small group of publicly traded operators who dominate the business</li><li>• The public filings of these gaming REIT tenants provide significant transparency</li><li>• The reporting requirements of the gaming regulators adds further insight into the industry’s health</li></ul>
<b>Private Market Valuation</b>	<ul style="list-style-type: none"><li>• Gaming properties trade infrequently, and when they do, cap rates are usually higher than other REIT sectors</li><li>• The perception that gaming is volatile is one reason...</li><li>• ...and onerous regulations keep most traditional RE investors out of the gaming auction tents</li></ul>
<b>Public Market Valuation</b>	<ul style="list-style-type: none"><li>• Gaming REITs trade at lower valuation multiples and higher implied cap rates vs the NNN REITs</li><li>• As the market learns more about the “actual” risks of the gaming sector vs the “perceived” risks, that valuation gap could narrow</li></ul>



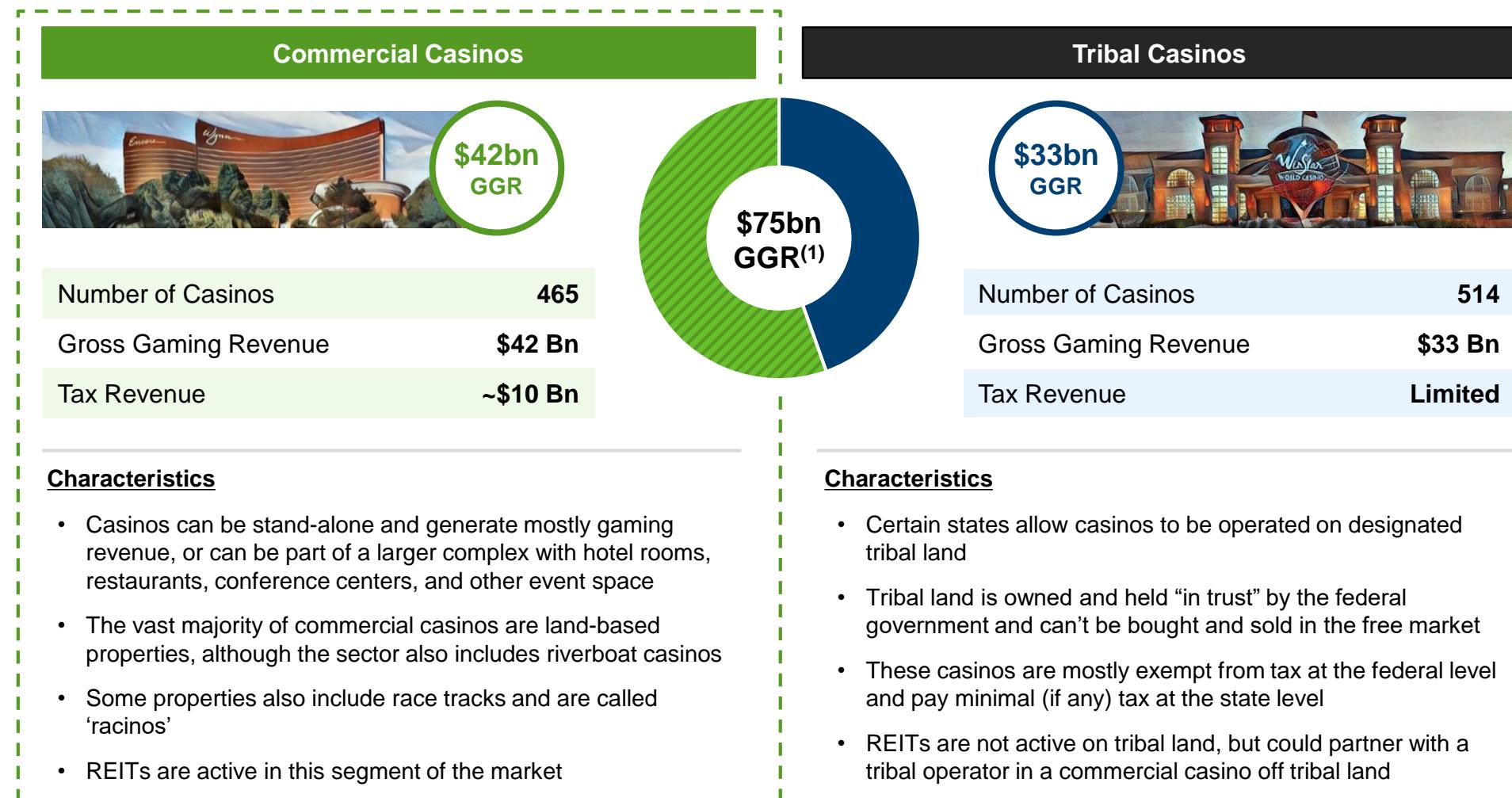
**Section II.**

## Gaming Industry Overview



# U.S. Gaming Industry: Overview

There are nearly 1,000 casinos operating across the U.S., generating ~\$75 billion in Gross Gaming Revenue (GGR). Over half of the industry's revenue is produced by "commercial" casinos, while the balance is from "tribal" casinos that are located on Native American-controlled land.



(1) U.S. Gross Gaming Revenue (GGR). GGR is the earnings of an operation (amount wagered minus winnings returned to players) before paying taxes, wages and other expenses.

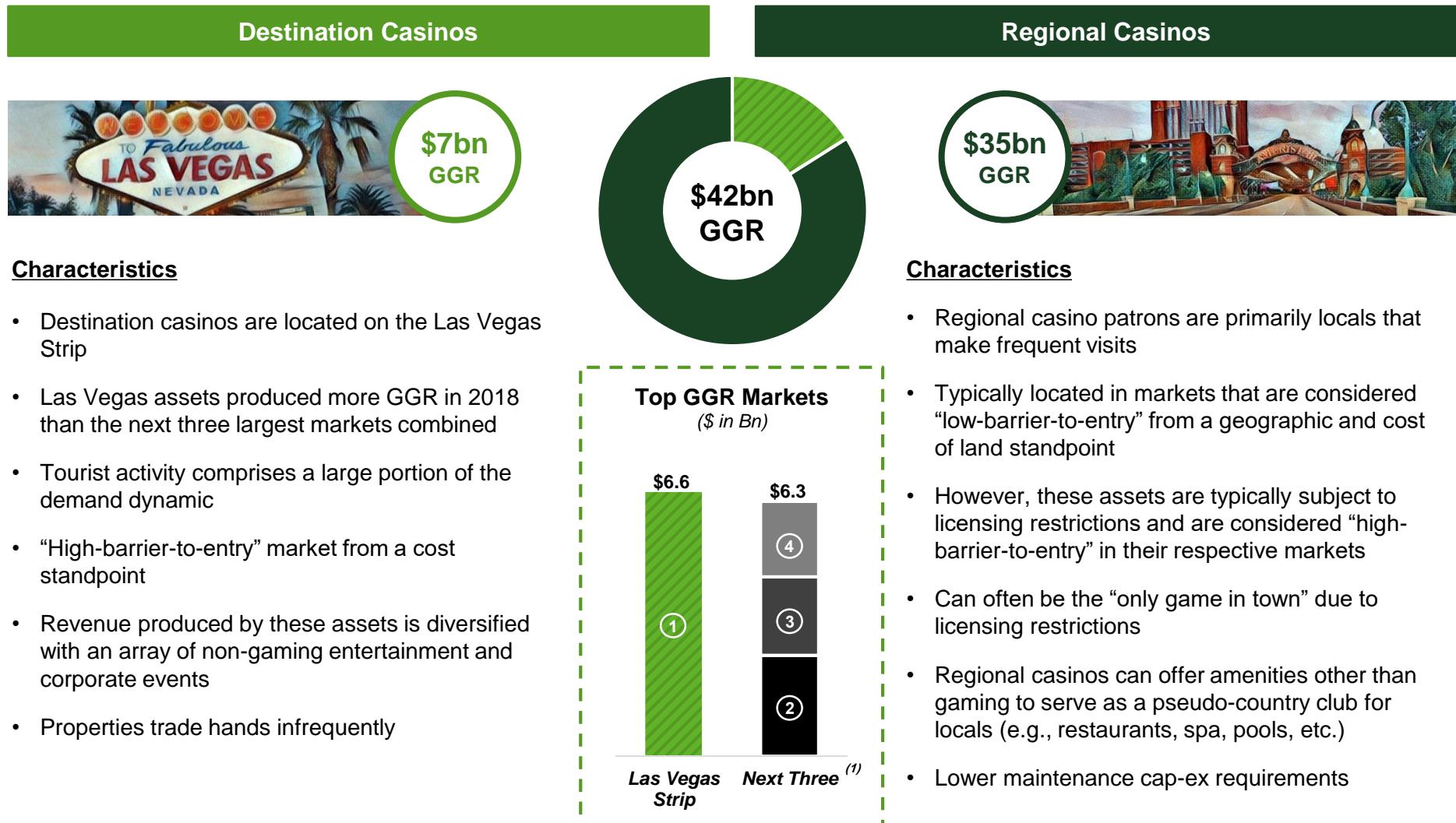
(2) Commercial GGR reflects 2018 results, while tribal GGR reflects 2017 results.

Source: Green Street Advisors, American Gaming Association: "State of the States 2019"



# U.S. Gaming Industry: Commercial Casinos

The “commercial” casino segment is comprised of two broad categories: 1) Destination Casinos that are located on the Las Vegas Strip, by far the industry’s largest market, and 2) Regional Casinos that cater primarily to local residents.



(1) Atlantic City, Chicagoland, and Baltimore/Washington D.C.

Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research



# U.S. Gaming Industry: Scale of Gaming Assets

To put the industry in perspective, it is noteworthy that some of the largest U.S. casinos realize cash flows that are 3-4x that of some of the largest properties familiar to REIT investors including the Ala Moana mall in Hawaii and the General Motors building in New York.



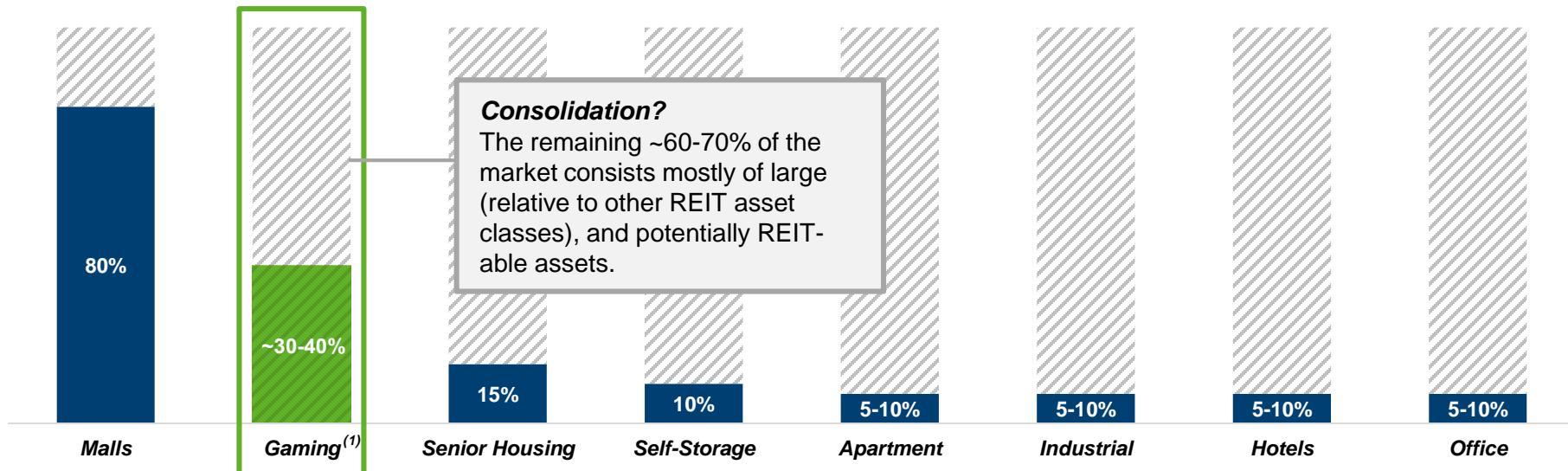
Source: Green Street Advisors, RCA, company public filings



# U.S. Gaming Industry: REIT Ownership

The REIT industry has grown significantly over the past 25 years. Yet, in most property sectors, REITs own <15% of the total supply of buildings. The noteworthy exception is the mall sector. The gaming REIT sector is relatively new, but the three publicly-traded companies already own a sizeable portion of the “commercial” gaming facilities.

REIT Market Share by Sector (as % of Value Except for Gaming)



Asset Quality Spectrum



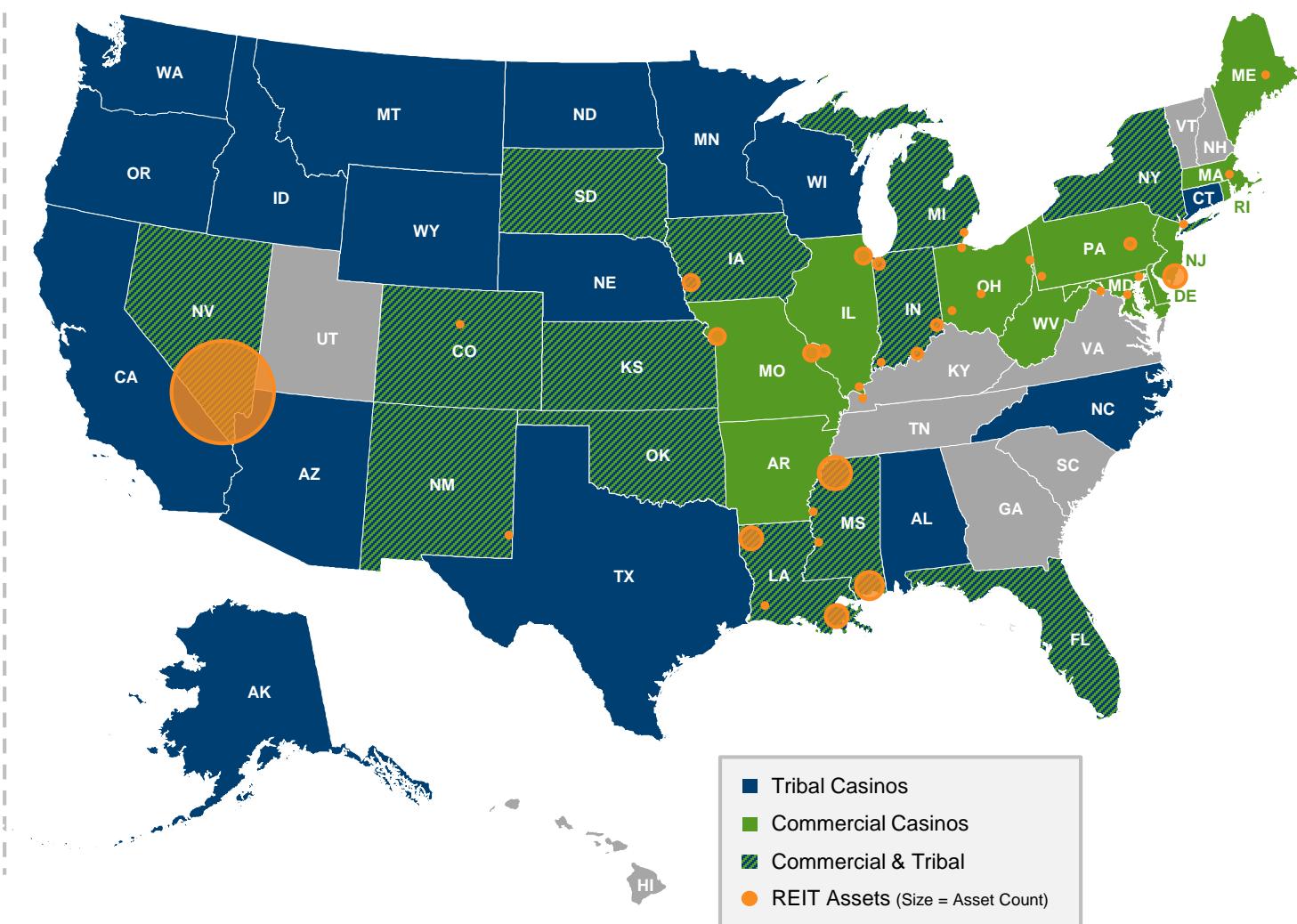
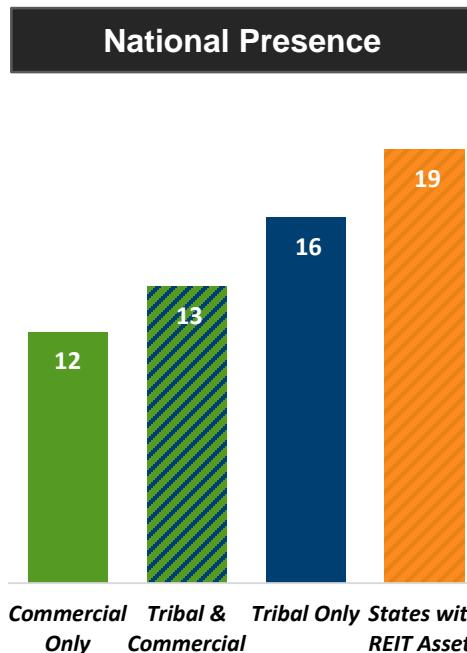
REIT-owned gaming assets tend to be of higher quality than the average gaming asset and are often among the ‘trophy assets’ in their respective markets.

(1) Green Street estimate based on GGR only, which excludes different sources of non-gaming revenue that may be part of a larger addressable market  
Source: Green Street Advisors



# U.S. Gaming Industry: Geographic Distribution

Commercial casinos are subject to licensing (to allow for a gambling business) and regulations (taxation of gaming revenue). Licensing and regulation is governed by state regulators and tend to differ meaningfully from one jurisdiction to another. About half of U.S. states allow for the operation of commercial casinos.



About half of U.S. states allow commercial casinos, with a good chunk of states allowing only tribal casinos. There are a handful that don't allow either.

Note: References only full-offering commercial casinos; limited forms of gaming legislation in-place in WA, KY, and VA.

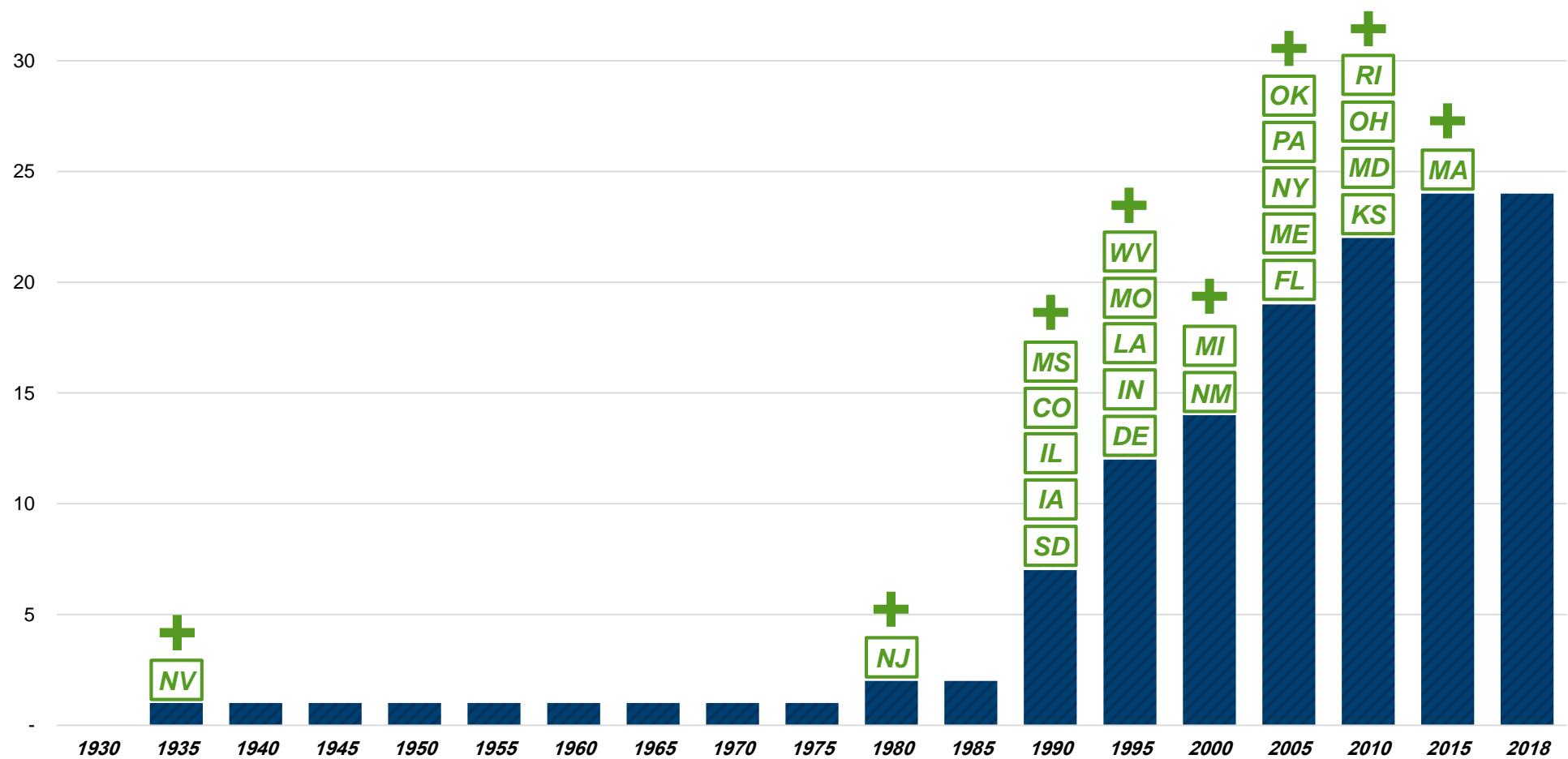
Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research, VICI/MGP/GLPI Investor Materials



# U.S. Gaming Industry: Evolution of Legislation

For a period of 50 years after the 1930's, commercial casinos were only allowed in Nevada. The 1990's sparked the beginning of the rapid adoption of commercial casino legislation and the subsequent growth of the asset type as well as gaming as a recreational pursuit.

States that Permit Commercial Casinos



Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research



# U.S. Gaming Industry: Licensing

In the states that allow gambling within a commercial casino, there are two types of licensing commonly granted. Some states issue a finite number of licenses, which puts a cap on the number of casino properties in that state, while others do not restrict the number of licenses within their jurisdiction. In either case, the significant regulatory processes involved in obtaining a license characterize the gaming sector as relatively high barrier-to-entry.

## Limited-License States



### Characteristics

Limited-license states auction off a fixed number of licenses to qualified operators, dictating suitable location selection based on proximity to existing casinos and zoning regulation.

#### Pros

- Strict supply constraints and protection from the State limit competition...

#### Partnership with State



#### Cons

- ...but this benefit has a price which comes in the form of higher taxes on gaming revenue

## Unlimited-License States



Significant geographic barriers-to-entry

Significant regulatory and competitive barriers-to-entry

### Characteristics

Unlimited-license states do not regulate the number of licenses within their jurisdiction. However, there may be limitations in the number of gaming properties that can be built due to significant geographic, competitive, and regulatory constraints within each jurisdiction.

#### Pros

- Lower taxes on gaming revenue can provide greater flexibility and higher margins...

#### Free Market



#### Cons

- ...but these properties can face enhanced competition, greater cash flow volatility, and higher cap-ex requirements

(1) While Missouri is classified as an unlimited-license state by the American Gaming Association, in-place legislation points to attributes akin to a limited-license state  
Source: Green Street Advisors, American Gaming Association, States Gaming Commissions



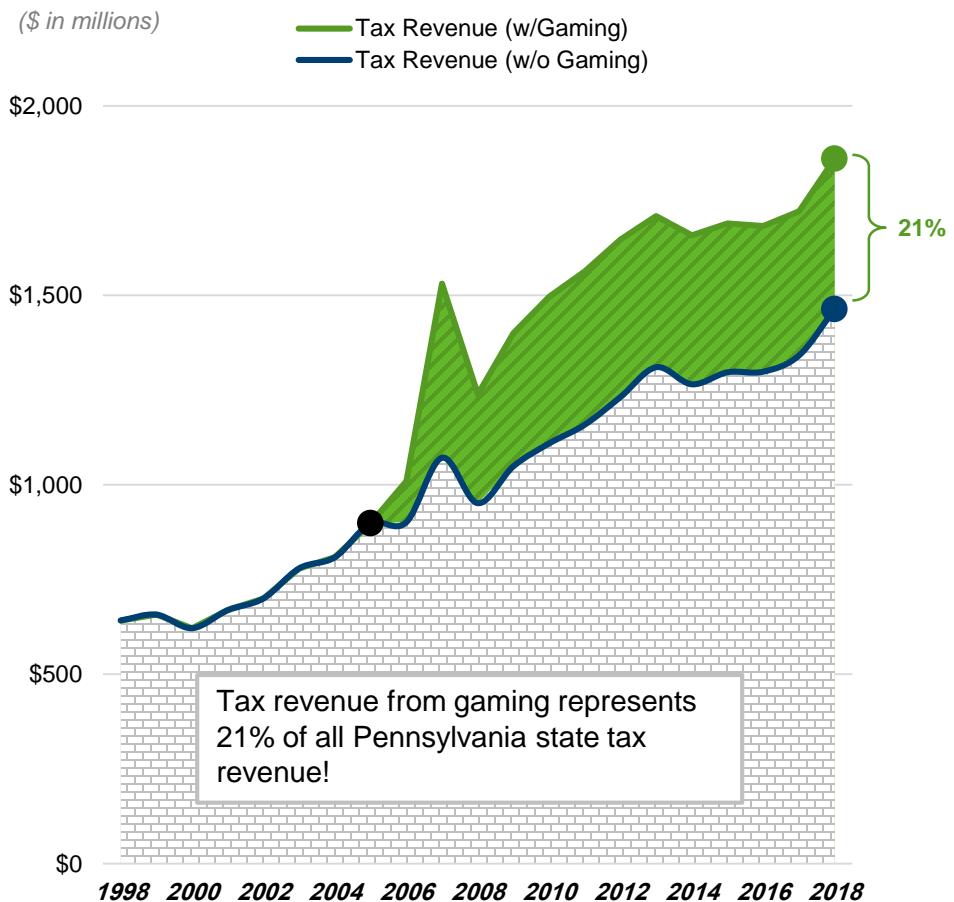
# U.S. Gaming Industry: Regulation

In limited-license states, local authorities have “skin in the game” alongside casino owners and operators in the form of significant tax revenue and jobs emanating from these properties.

## Mission Critical Gaming Properties

- Across the U.S., gaming supports 1.8 million jobs nationwide and commercial casinos contribute ~\$10 billion of gaming tax revenue
- Governments are incentivized to support casino operations to maintain jobs and tax revenue in their local markets
- The importance of gaming from a tax revenue standpoint provides additional protection for property owners
- This is especially true in higher-tax, limited-license states where the government effectively partners with gaming operators
- Due to the importance of gaming tax revenue to the state, threat of repurposing for alternative use of gaming assets is low, relative to other sectors

## Case Study: Pennsylvania Tax Revenue

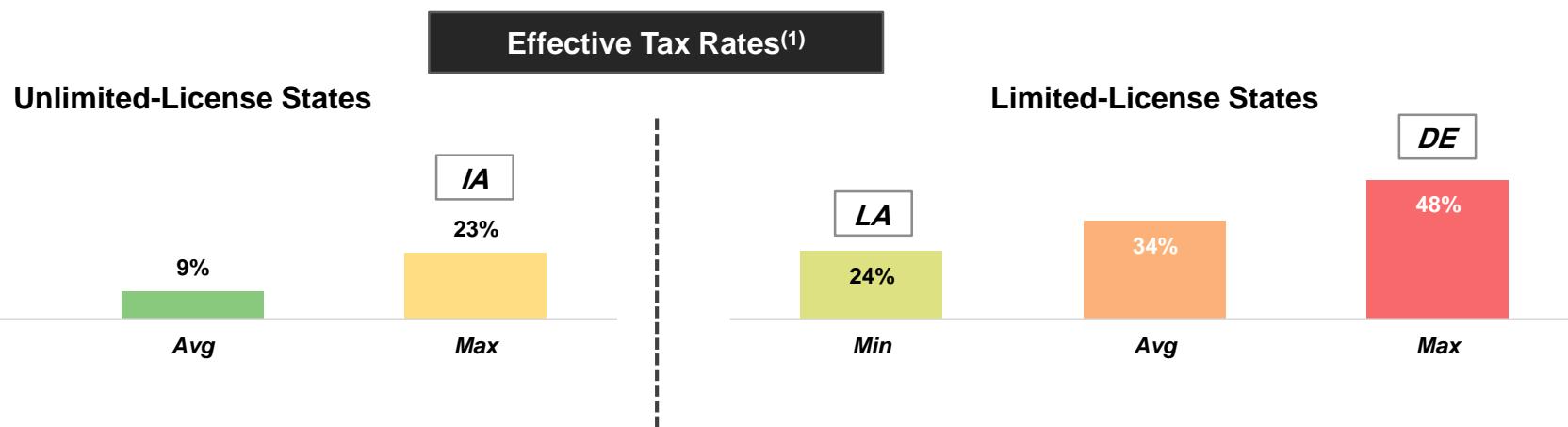
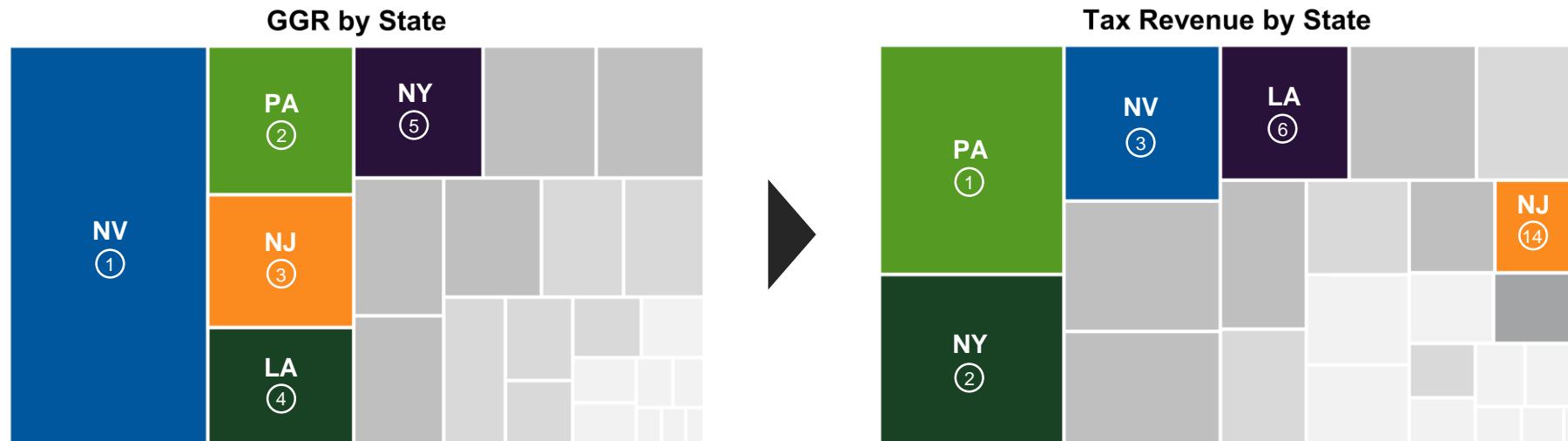


Source: American Gaming Association, Green Street Advisors



# U.S. Gaming Industry: Tax Implications

Each state has the ability to restrict or limit the number of gaming licenses allowed at a time. By doing so, the state can leverage operating exclusivity when negotiating with gaming operators to optimize tax revenue. As a result, states that produce the most gaming revenue do not necessarily produce the most tax revenue.

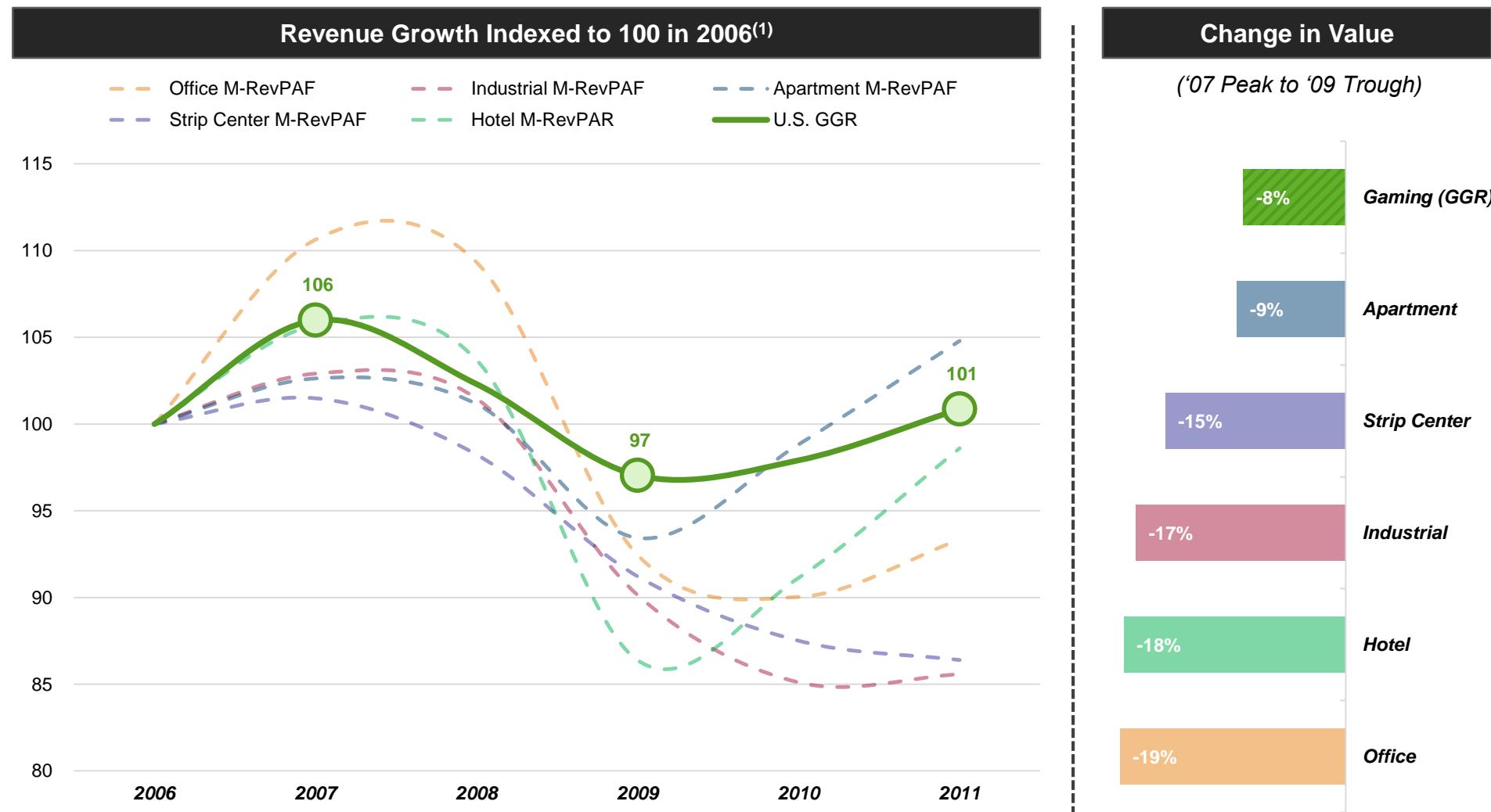


(1) Effective tax rates calculated as total direct state gaming tax revenue as a percentage of total state gaming revenue.  
Source: American Gaming Association: "State of the States 2019", Green Street Advisors



# U.S. Gaming Industry: Revenue Volatility

Gaming is perceived to be a volatile, cyclical sector that is highly correlated with overall health of the economy. Interestingly, gaming revenue during the Great Financial Crisis of '08-'09 demonstrated less volatility by some measures than most other major real estate sectors.



(1) A proxy for GGR in other commercial real estate sectors is Market Revenue per Available Foot/Room (M-RevPAF/M-RevPAR), a single figure that combines changes in rent and occupancy  
Source: Green Street Advisors, American Gaming Association



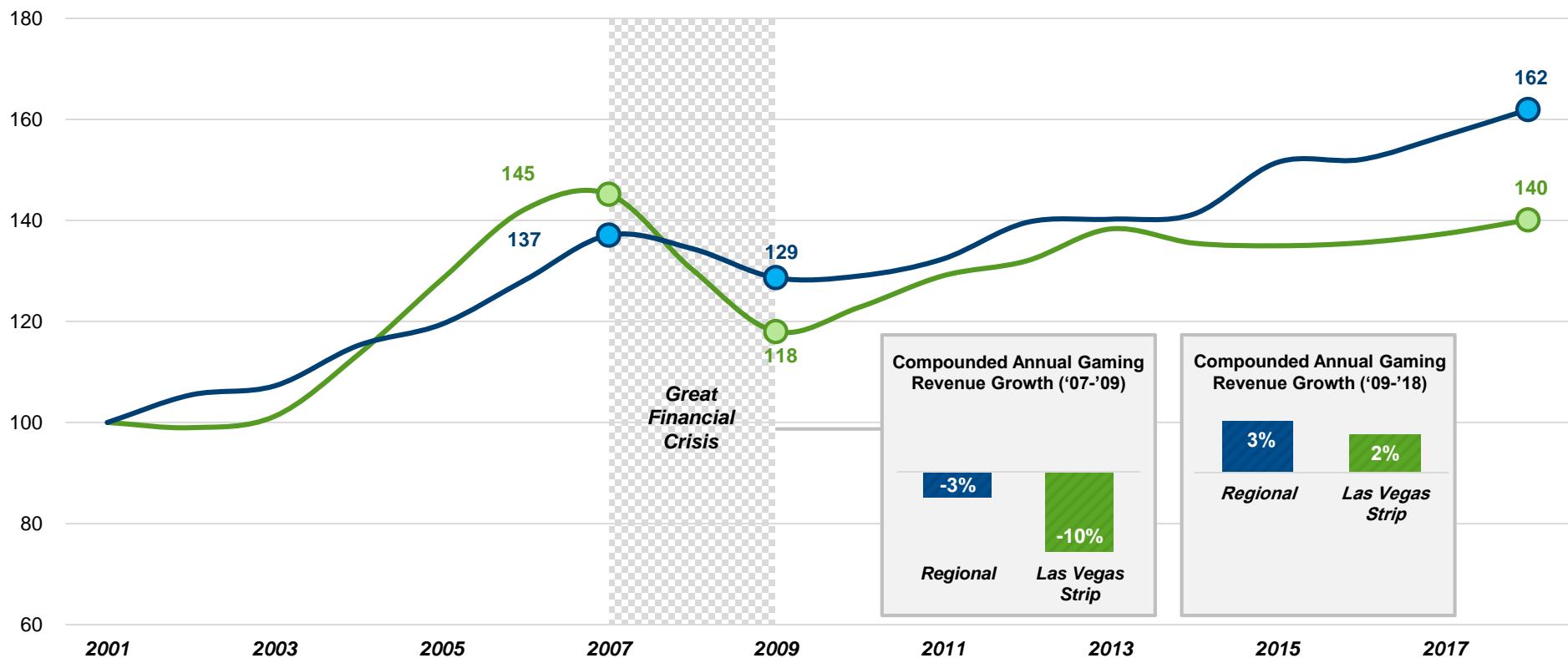
# U.S. Gaming Industry: Revenue Volatility (cont'd)

Regional assets tend to attract a more local and loyal clientele, resulting in relatively low gaming revenue volatility over full economic cycles. Destination casinos, on the other hand, rely primarily on domestic and international tourism, as well as corporate/convention spending. Leisure spending can fluctuate throughout the economic cycle, which has prompted operators in Las Vegas to diversify their sources of revenue well beyond just gaming.

Historical Gross Gaming Revenue by Type

(Revenue Growth Indexed to 100 in 2001)

— Las Vegas Strip — Regional



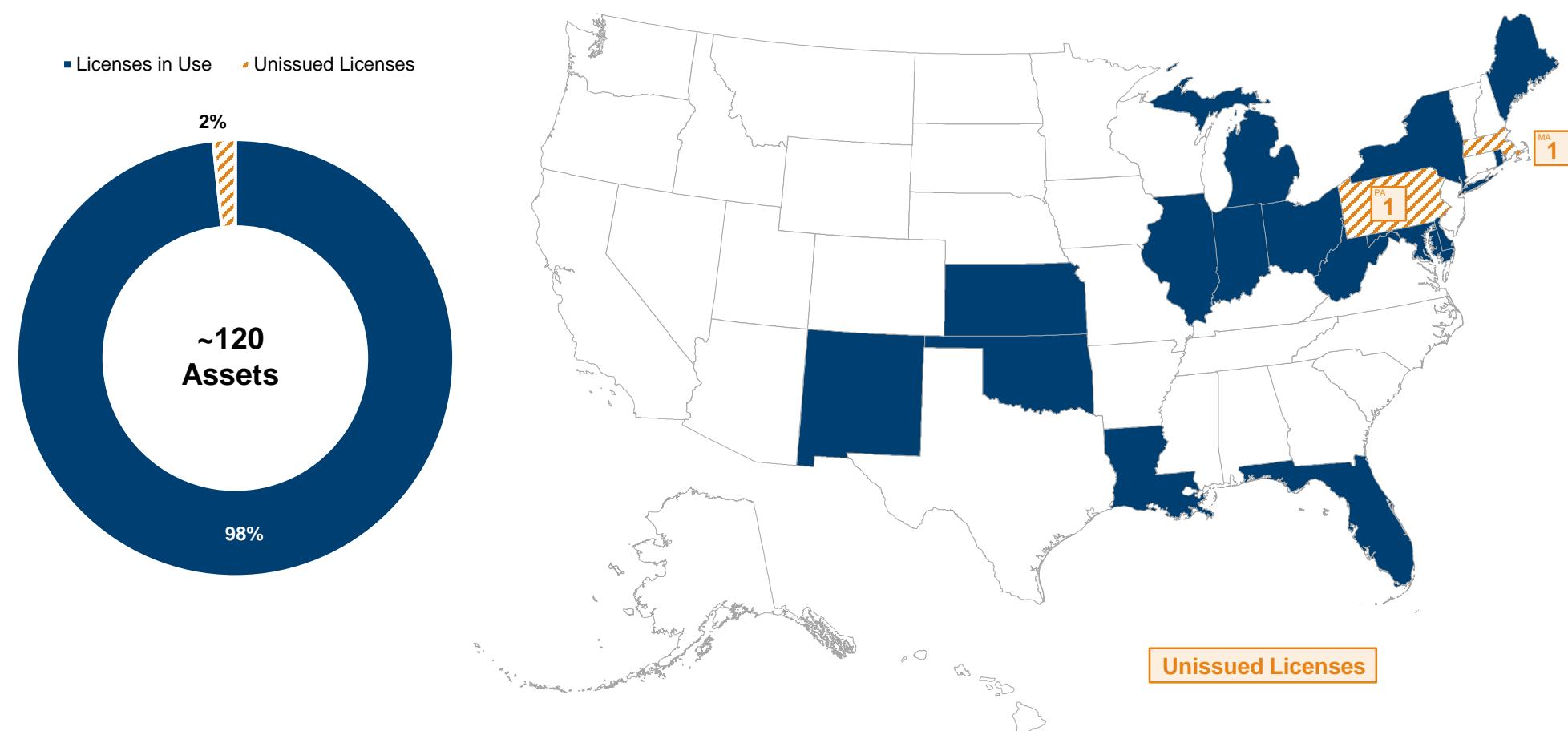
Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research



# U.S. Gaming Industry: Supply Growth

Limited-license states have issued roughly 120 full commercial casino gambling licenses (excluding satellite casinos and other limited offering venues), and two of these remain unissued. Existing licenses carry limitations and restrictions on where the new casinos can be built in relation to the current stock of properties.

## Supply Considerations in Limited-License States\*



\*State legislation is constantly evolving, and certain states are considering allowing gaming or expanding the number of available licenses  
Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research

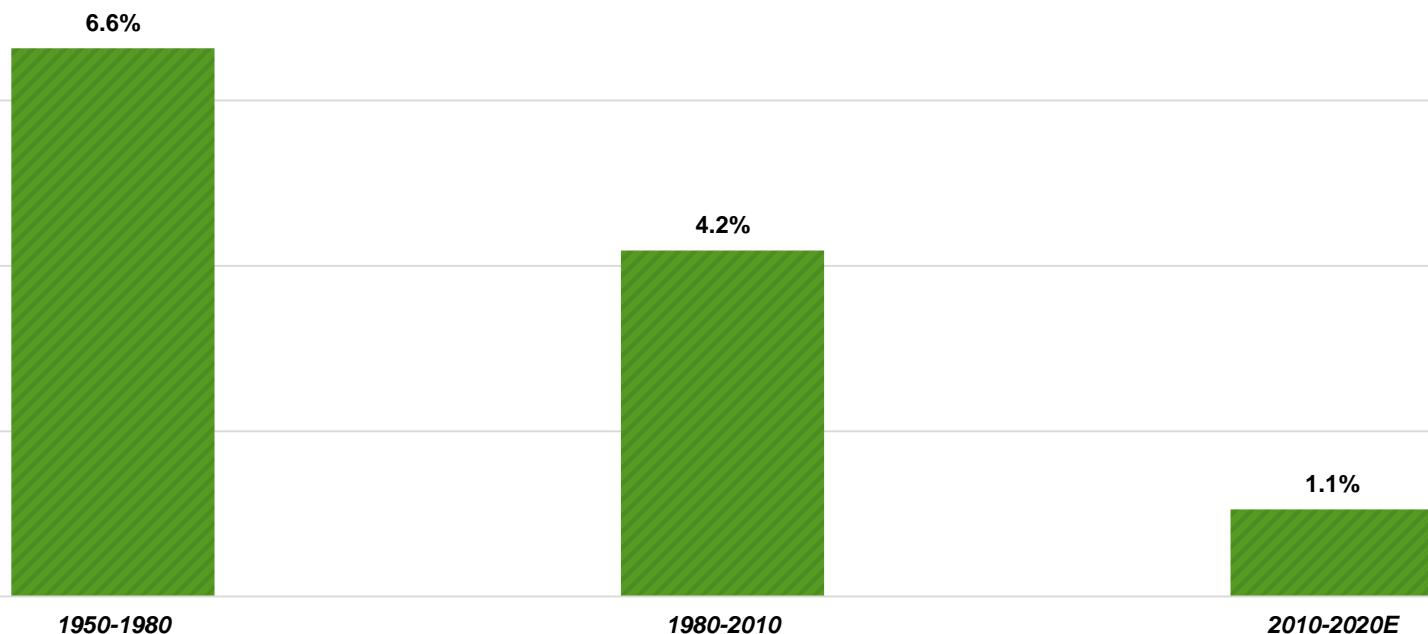


# U.S. Gaming Industry: Supply Growth (cont'd)

Unlimited-license states, such as Nevada, do not offer existing owners and operators the same regulatory protections from new supply as limited-license states. However, the pace of new construction in Las Vegas over the past decade has been just a fraction of the historical growth pace, demonstrating that capital markets discipline can be an effective governor on supply growth.

## Supply Considerations in Unlimited-License States (Las Vegas Case Study)

Annualized Las Vegas Strip Room Count Growth  
(CAGR)



Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research

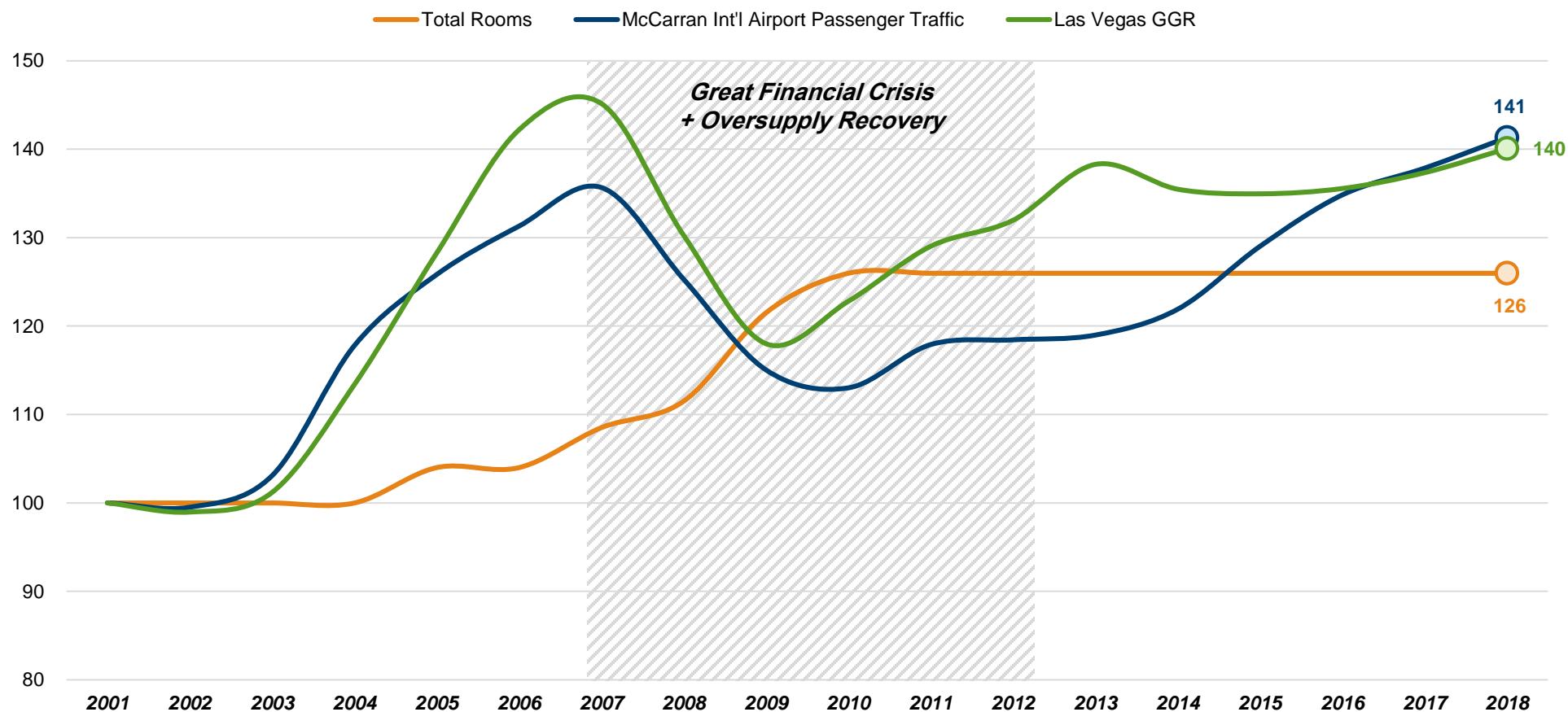


# U.S. Gaming Industry: Supply Growth (cont'd)

The supply and demand dynamics of casino properties in unlimited-license states resemble traditional commercial real estate. In periods of economic expansion, assets are able to deliver outsized revenue growth thanks to muted (and lagging) new supply. This is typically followed by periods of accelerating supply growth and slower revenue growth.

## Las Vegas Case Study (cont'd)

(Growth Indexed to 100 in 2001)

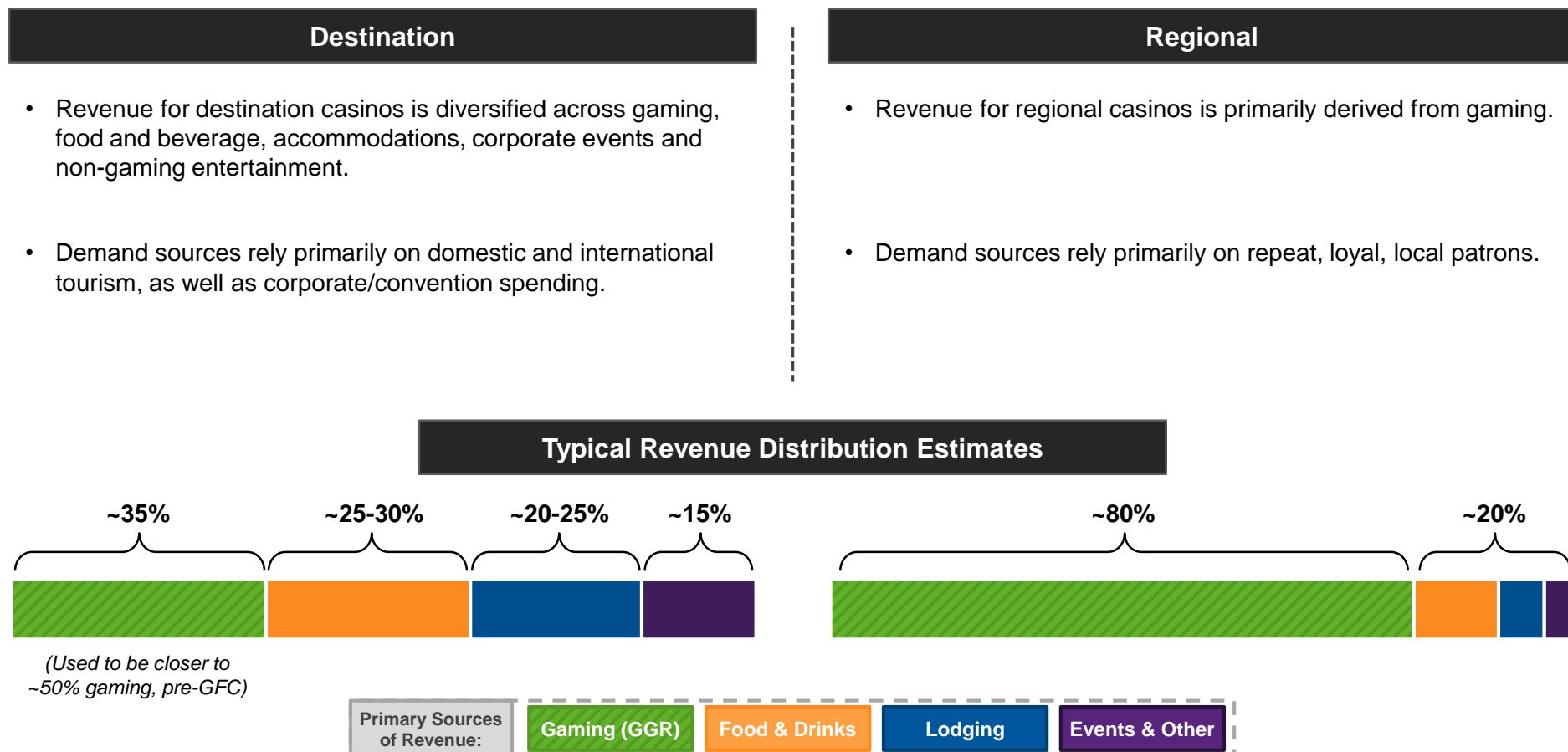


Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research, McCarran International Airport



# U.S. Gaming Industry: Revenue Diversification

The revenue composition for “Destination” properties on the Las Vegas Strip has become far more diversified. The variety of revenue sources allows operators to pull different operational levers at different points in the economic cycle. “Regional” properties rely primarily on gaming revenue generated by repeat visits from their loyal, local clientele.



Source: Green Street Advisors, American Gaming Association, UNLV Center for Gaming Research, VICI/MGP/GLPI Investor Materials



**Section III.**

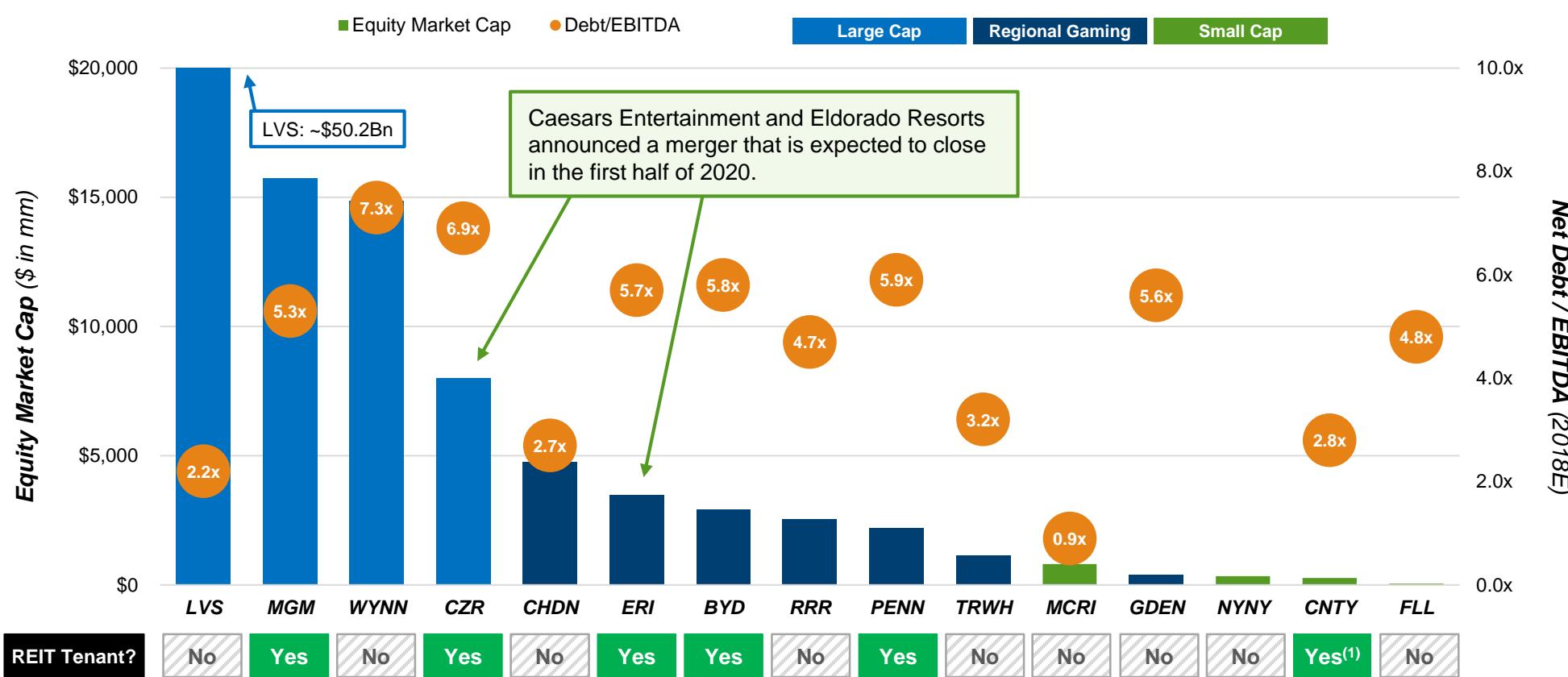
## Gaming REITs & Operators Overview



# Operators: Overview

The U.S. gaming industry is concentrated among a small number of sophisticated operators, most of which are publicly traded, though the universe of potential tenants includes a number of private operators as well. The investor disclosure provided by the public companies, plus the detailed reporting required by gaming regulators, makes the industry far more transparent than most.

Major Public Gaming Operator U.S. Revenue Comparison



(1) The Century Casino portfolio acquired by VICI is expected to close Q1 2020

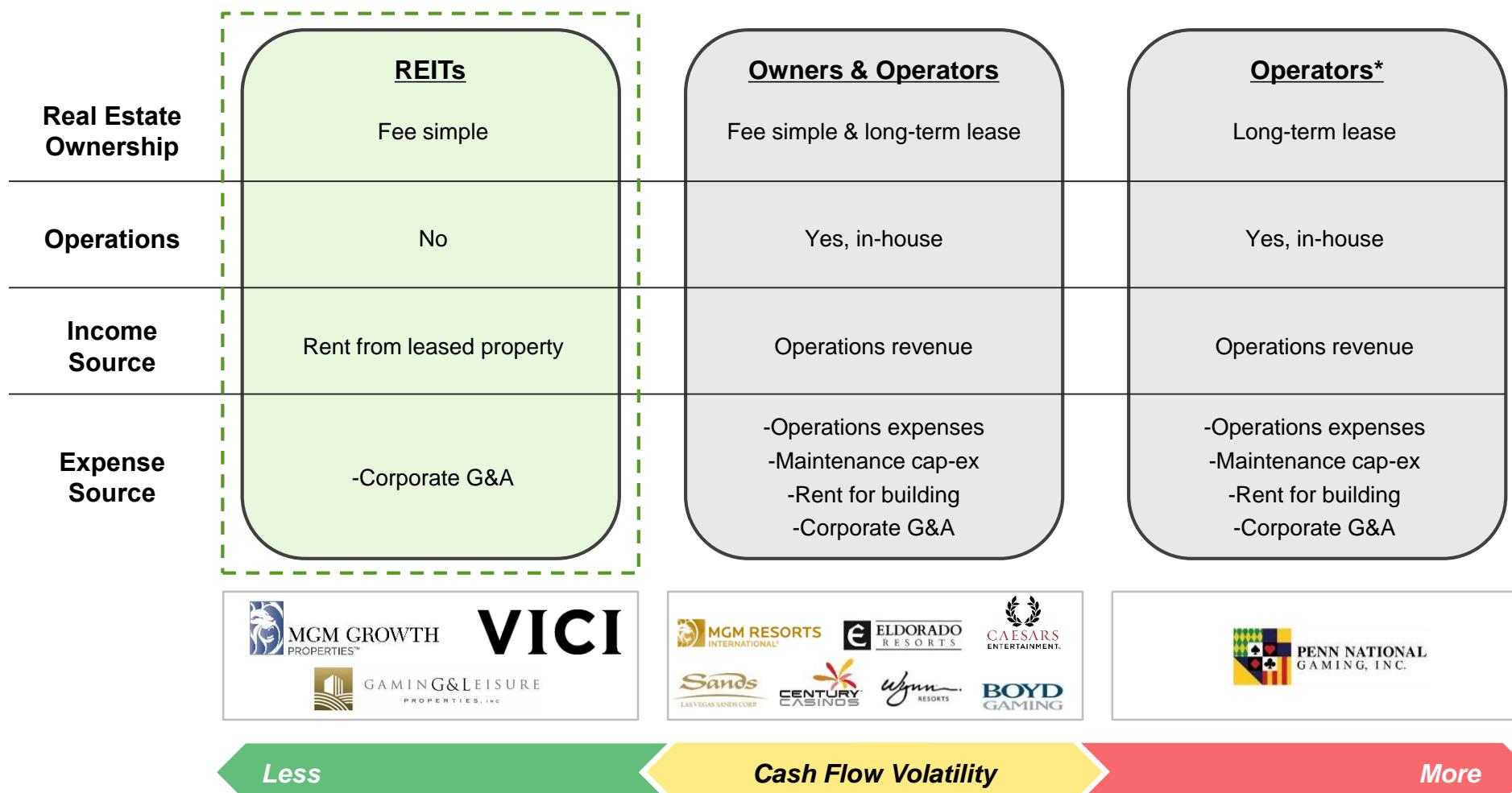
Companies: Las Vegas Sands (LVS), MGM Resorts (MGM), Wynn Resorts (WYNN), Caesars Entertainment (CZR), Churchill Downs (CHDN), Eldorado Resorts (ERI), Boyd Gaming (BYD), Red Rock (RRR), Penn National Gaming (PENN), Twin River (TRWH), Monarch Casino & Resort (MCRI), Golden Entertainment (GDEN), Empire Resorts (NYNY), Century Casinos (CNTY), Full House Resorts (FLL), Nevada Gold & Casinos (JWN)

Source: Green Street Advisors, Bloomberg, SNL, Company Investor Materials



# Gaming REITs: Ownership Considerations

The gaming industry is following the path blazed in the lodging sector with the creation of three Gaming REITs over the past five years. Gaming is a capital-intensive industry, and the emergence of the REITs provides an attractive alternative source of capital for the operators. The REITs also provide investors with a way to invest in the gaming sector, but with a far lower risk profile than offered by investments in the operators.

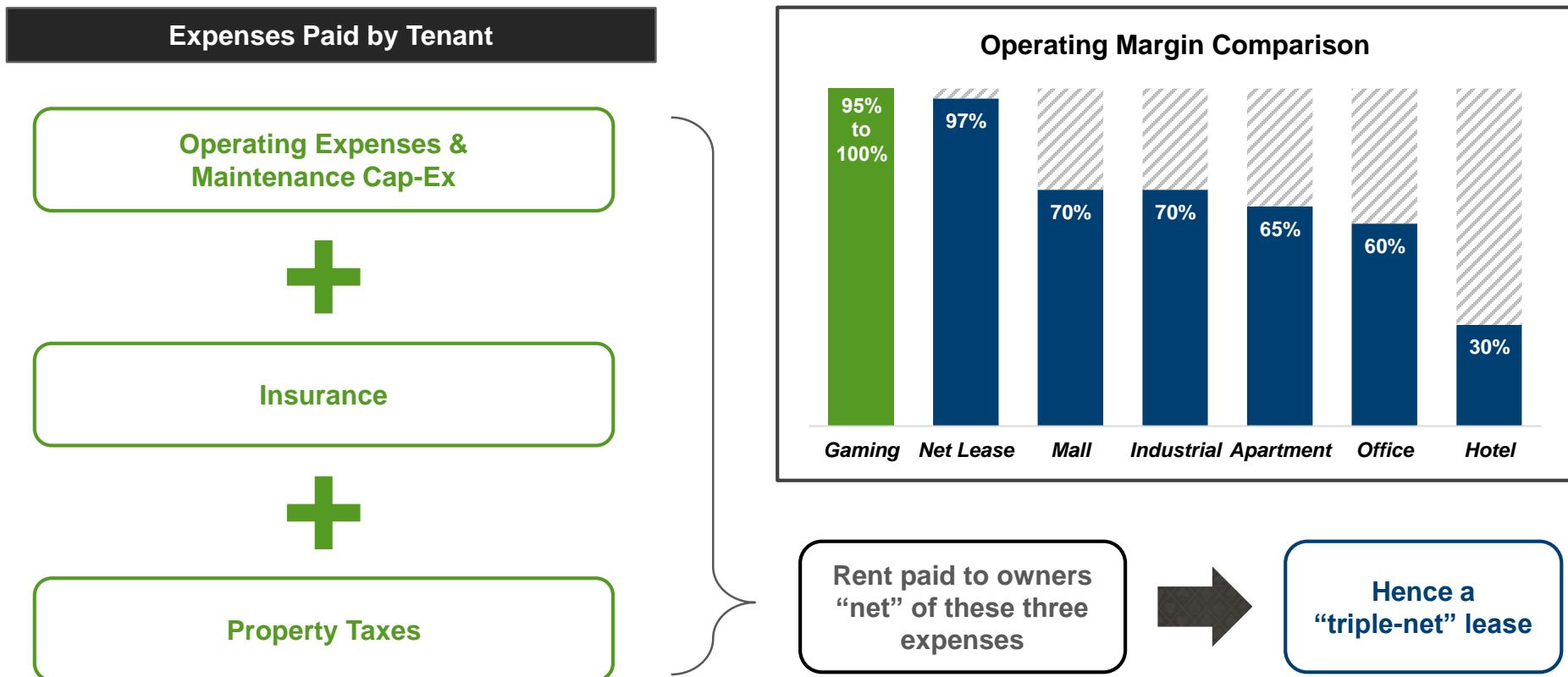


\* Penn National Gaming has <5% real estate ownership  
Source: Green Street Advisors, Company Investor Materials



# Gaming REITs: NNN Lease Structure

The Gaming REITs own properties that are leased to operators under long-term leases that require the tenant to pay all the operating expenses, insurance, and property taxes. These are known as “triple-net” or “NNN” leases, and they provide a steady and predictable stream of cash flow to the property owner.

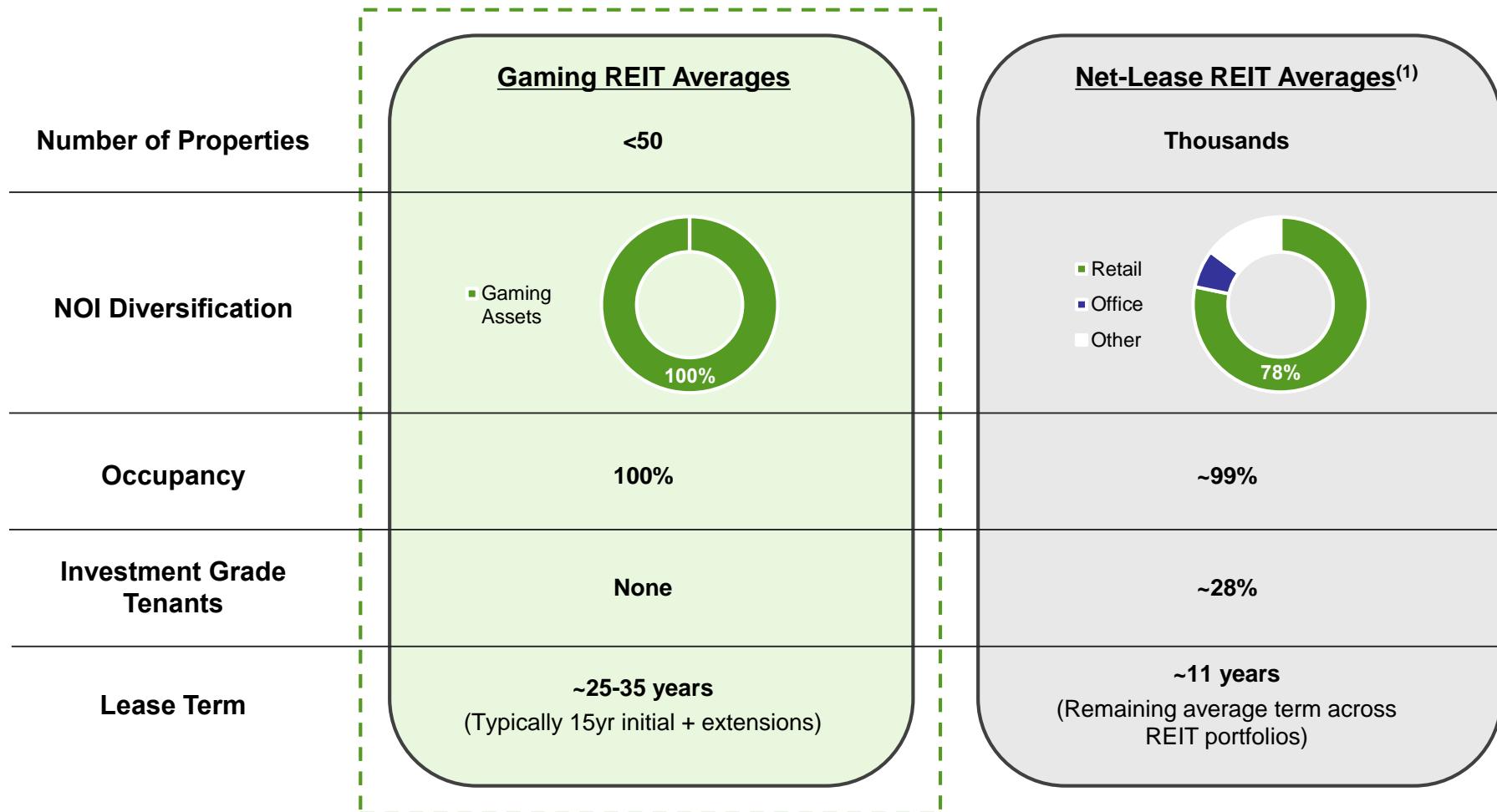


Source: Green Street Advisors



# Gaming REITs: Net-Lease Sector Similarities

The Gaming REITs are most comparable to the larger companies in the NNN-lease segment of the REIT industry because of the consistency of the cash flows generated by their leases. While the operating cash flows of the tenants may fluctuate depending on the economic cycle and their own position within their respective industries, the long-term NNN leases provide investors with an easily forecastable cash flow outlook.

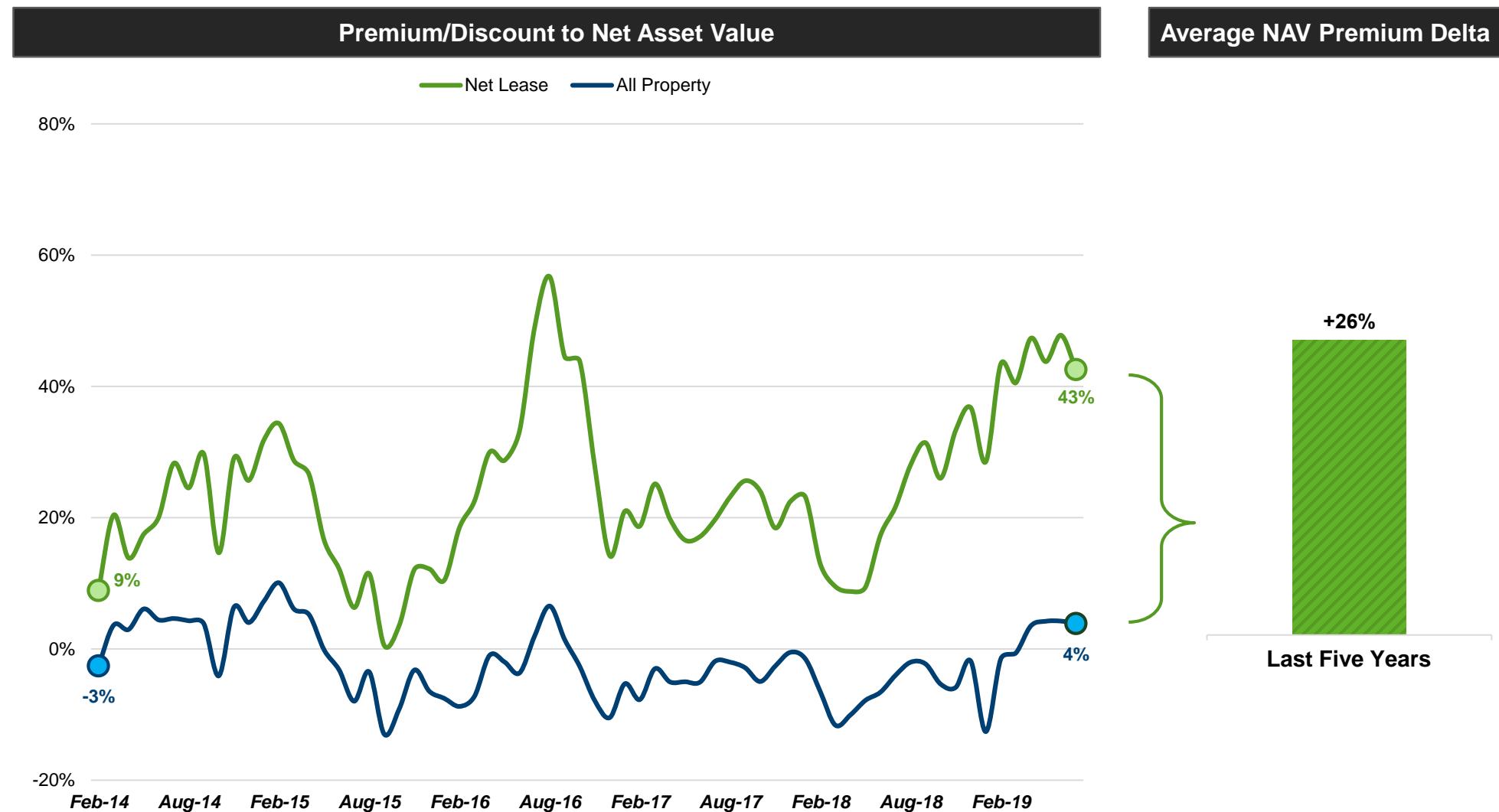


(1) Weighted-Average of National Retail Properties Inc., Realty Income Corp, Spirit Realty Capital Inc., Store Capital, and Vereit  
Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Gaming REITs: Net-Lease Sector Acceptance

The Net-Lease REITs have been embraced by investors despite their heavy investment concentration in properties leased to retailers, an industry characterized by tremendous change and uncertainty.



Source: Green Street Advisors, as of 7/1/19

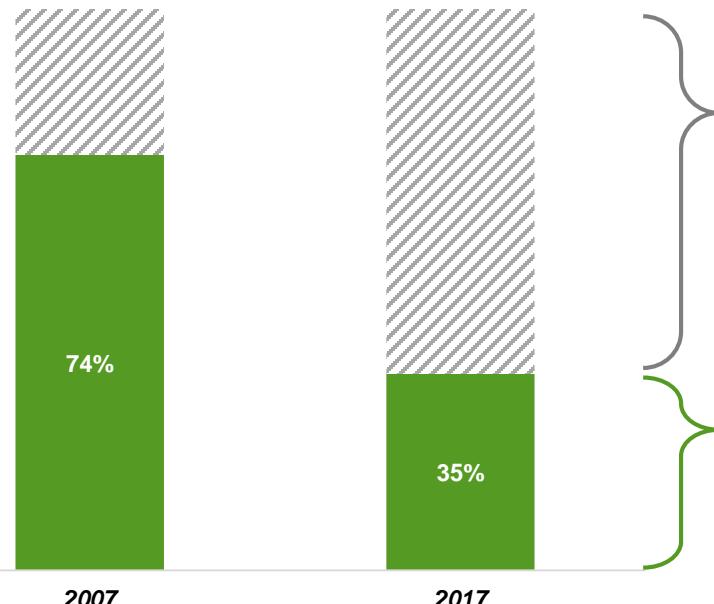


# Gaming REITs: Health Care Sector Similarities

The Gaming REITs also share a heritage with the Health Care REITs, which historically were NNN REITs that specialized in the ownership of nursing homes, senior housing, and hospitals. Changes in the REIT legislation a decade ago prompted the Health Care REITs to move away from their NNN-lease roots, yet roughly a third of the assets in that REIT sector are still in the NNN-lease structure. How these NNN Health Care properties are priced in the private and public markets provide important valuation comparables for the Gaming REITs.

## Evolution of Health Care Sector (Net Lease as % of NOI)

■ Net Lease □ Operating



### Operating Business Model

- Medical Office
- Life Science
- Senior Housing

### Net Lease Structure

- Senior Housing
- Hospitals
- Skilled Nursing

Investors can look at these property types for NNN valuation comparables



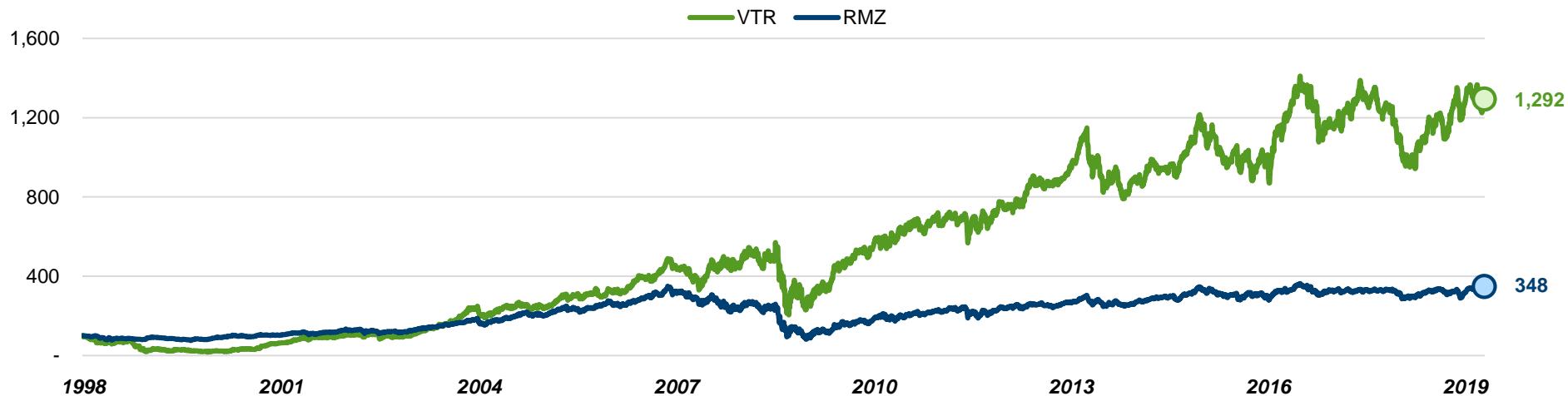
Source: Green Street Advisors



# Gaming REITs: Health Care Sector Acceptance

The three Gaming REITs were spawned by gaming operators through variations of a propco/opco transaction. This is similar to the origins of the health care REIT sector where several REITs began life as spinoffs from health care operators. Perhaps the most fascinating case study of these was Ventas. Its sole tenant went bankrupt just a year after the REIT was created in '98. Yet, through the leadership of CEO Debbie Cafaro, its initial focus on NNN-lease investments, and its diversification into other health care-related investments, Ventas blossomed into a highly regarded “blue chip” REIT.

Ventas vs. RMZ Index Total Returns Indexed to 100 at Ventas IPO



### Rough Beginnings

- Ventas is organized as a REIT whose sole tenant is Vencor via 5 master leases containing ~275 nursing homes and hospitals
- The federal government changes regulations, which drastically reduces Medicare payments to operators of nursing homes
- Vencor files for Chapter 11; **pays rent but not debt service**

### 2000's

- Deal for restructuring \$1 billion of Vencor's long-term debt announced
- New amendments to regulations return billions in Medicare reimbursements to nursing homes
- Vencor emerges from bankruptcy and Ventas begins investing again

### Today: Best-in-Class

<b>Asset Value</b>	~\$31Bn
<b>Number of Properties</b>	~1,200
<b>Hist. Premium to NAV</b>	~24% premium
<b>CEO Tenure</b>	20 Years

Source: Green Street Advisors, Bloomberg



# Gaming REITs: Side-by-Side Comparison

Investors are in the early stages of understanding the gaming REIT sector. In that process, the well-established NNN and health care sectors provide a variety of important points of comparison.

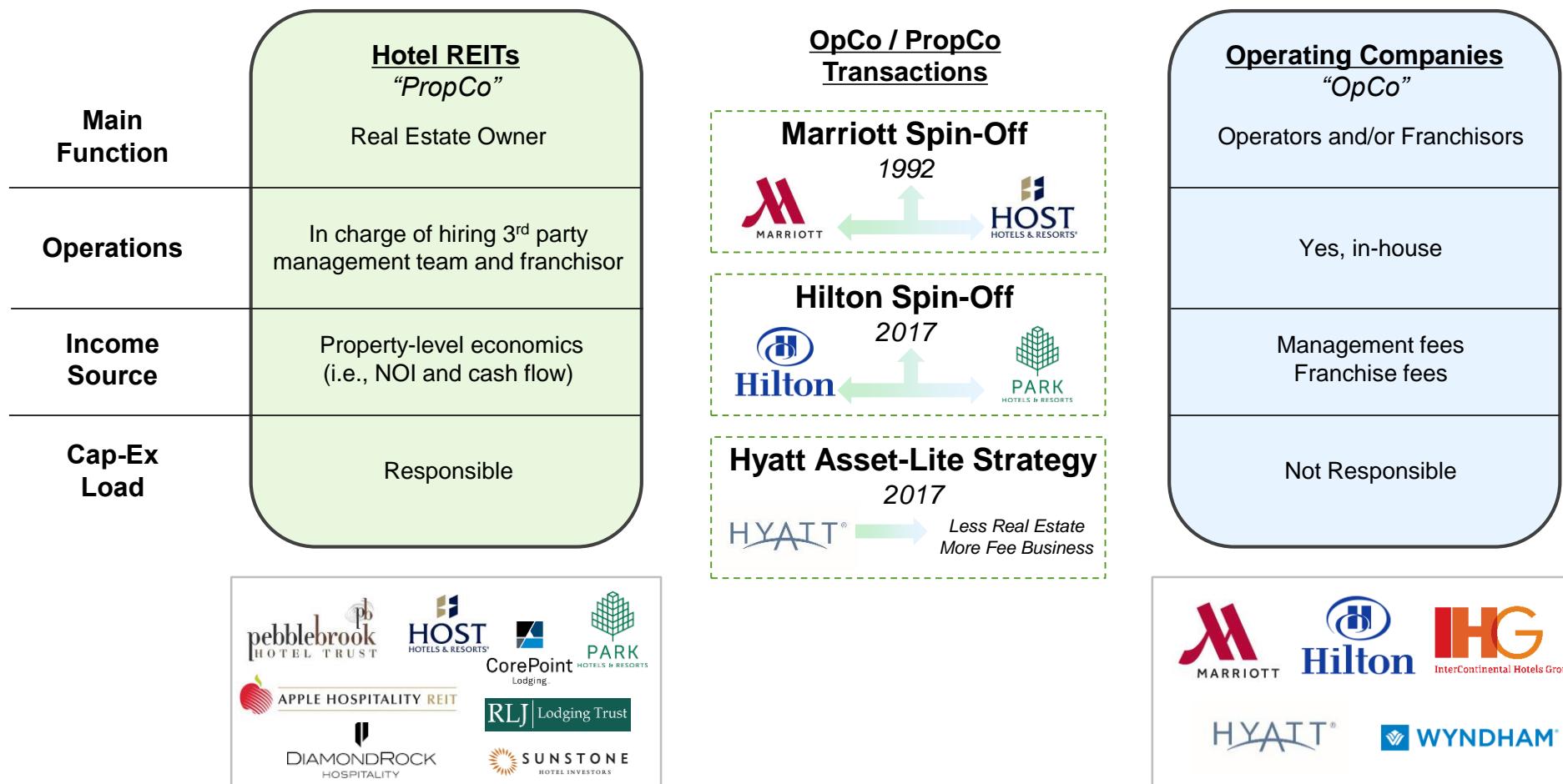
	<u>Gaming</u>	<u>Health Care</u>	<u>Net Lease</u>
<b>First REIT IPO/Spin-Off</b>	2013	1992	1991
<b>Cash Flow Source</b>	NNN Leases	NNN Leases & Operating Investments	NNN Leases
<b>EBITDA/NOI Margin</b>	~95-100%	~50%	~90-95%
<b>Underlying Business Model</b>	Operationally-Intensive & Regulated	Complex & Regulated	Simple
<b>Underlying Asset Transparency</b>	High	Medium	Low
<b>Barrier-to-Entry</b>	High	Medium	Low
<b>Cash Flow Volatility</b>	Low	Medium	Low
<b>Alternative Use Concern</b>	No	No	Yes
<b>REIT-Dedicated Shareholders</b>	~25-35%	~46%	~37%
<b>EV/EBITDA Multiples<sup>(1)</sup></b>	~14x	~18x	~18x

(1) EV/EBITDA multiples for Health Care and Net Lease companies within Green Street coverage universe, sourced from Bloomberg as of July 22, 2019  
Source: Green Street Advisors, Bloomberg, IPREO, VICI/MGP/GLPI Investor Materials



# Gaming REITs: OpCo/PropCo Precedent

Gaming is a complex, operationally-intensive business where scale provides a significant competitive advantage. In this respect, it is similar to the hotel industry. Marriott set the lodging sector on a strategic path in the early '90s when it split into two companies – an operating company now known as Marriott International (NYSE: MAR) and a real estate company now known as Host Hotels (NYSE: HST). Today, the hotel industry is largely comprised of companies that are either operators or real estate owners.



Source: Green Street Advisors



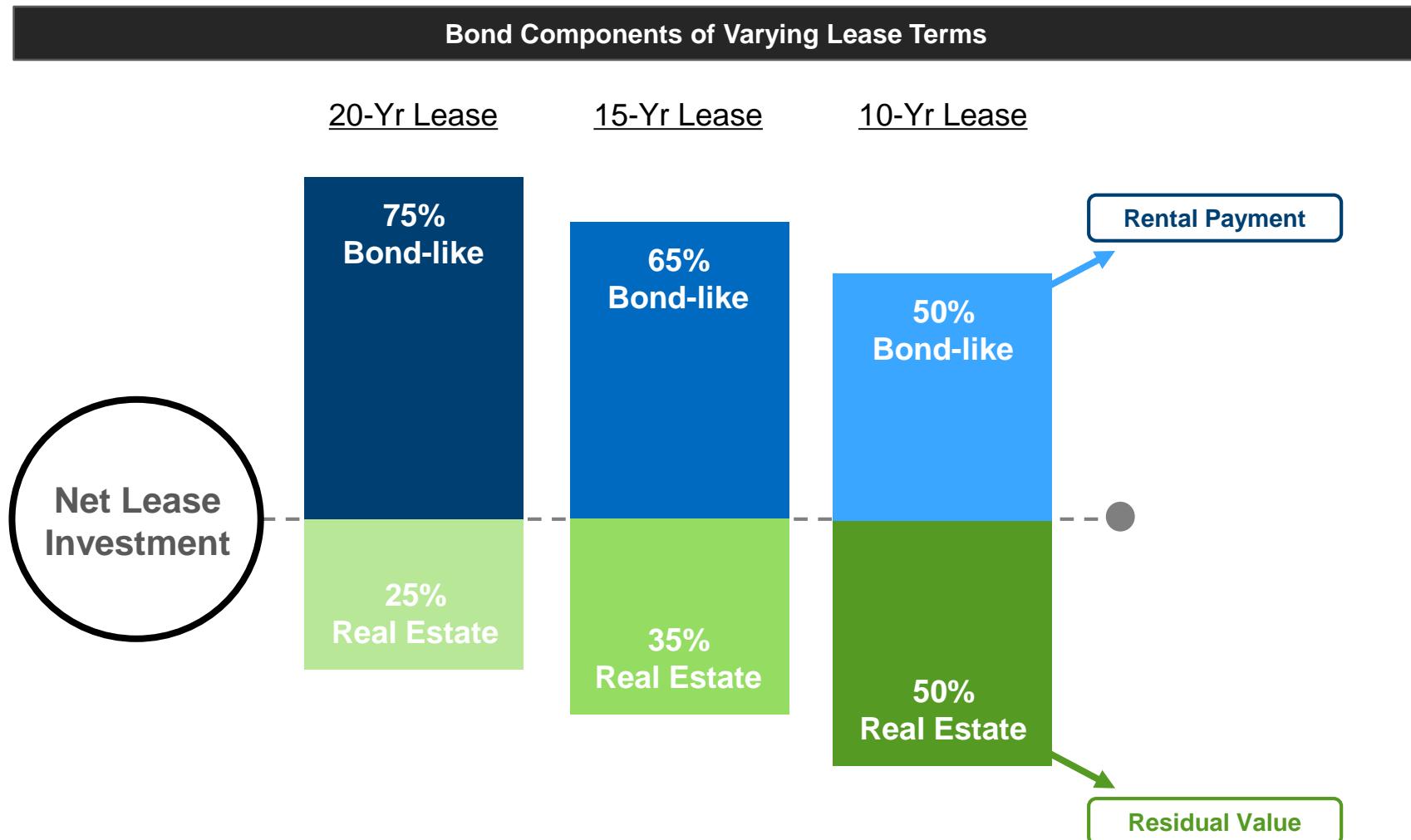
**Section IV.**

## **Valuation Considerations**



# Valuation: Part Bond, Part Real Estate

A NNN lease has the characteristics of both a bond and a real estate investment. The longer the lease, the more bond-like the investment becomes from a valuation standpoint.

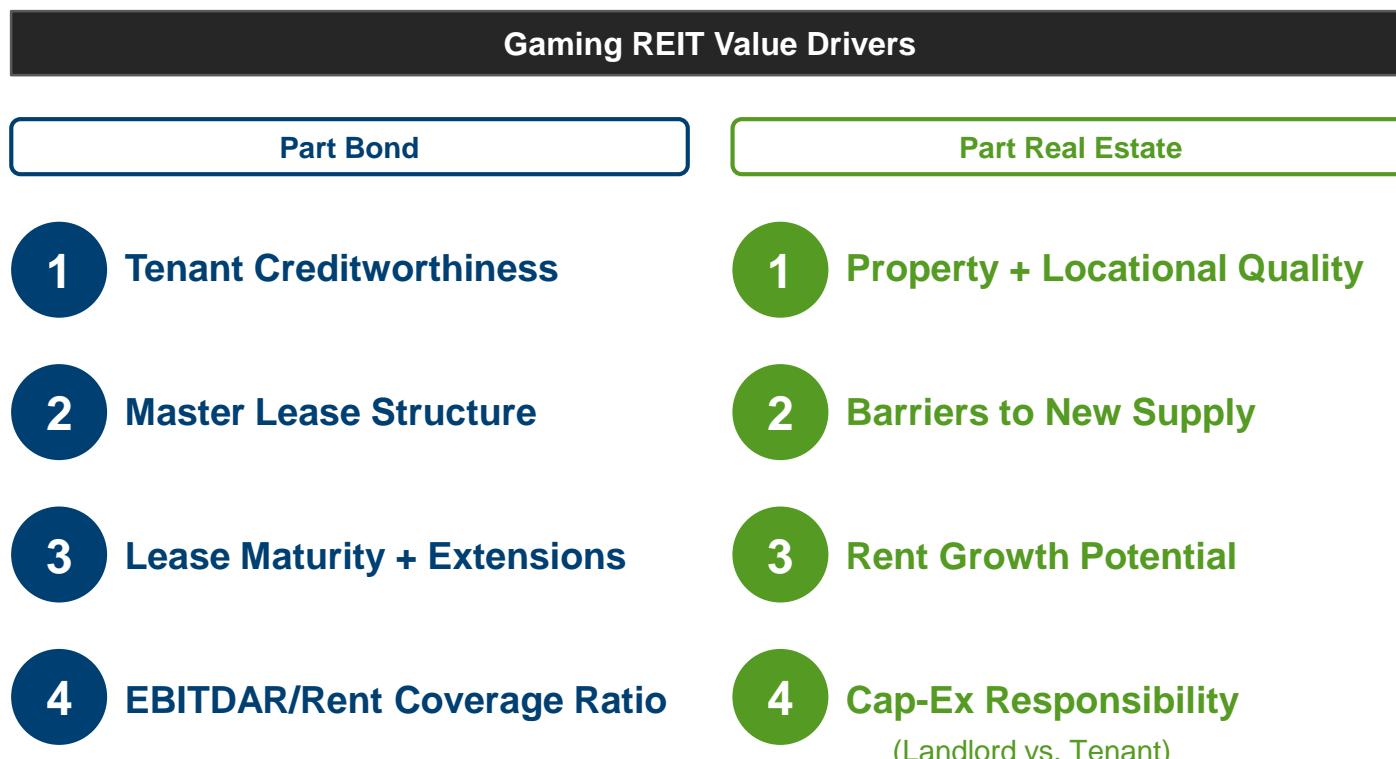


Source: Green Street Advisors



# Valuation: Gaming REIT Value Drivers

The drivers of value in the “bond” part of the NNN property valuation center primarily on the creditworthiness of the tenant. However, the structure of the lease can add substantial protections to the “lender” (i.e., the property owner). The drivers of the “real estate” part of the analysis are typical of the considerations an investor would have in other property sectors.

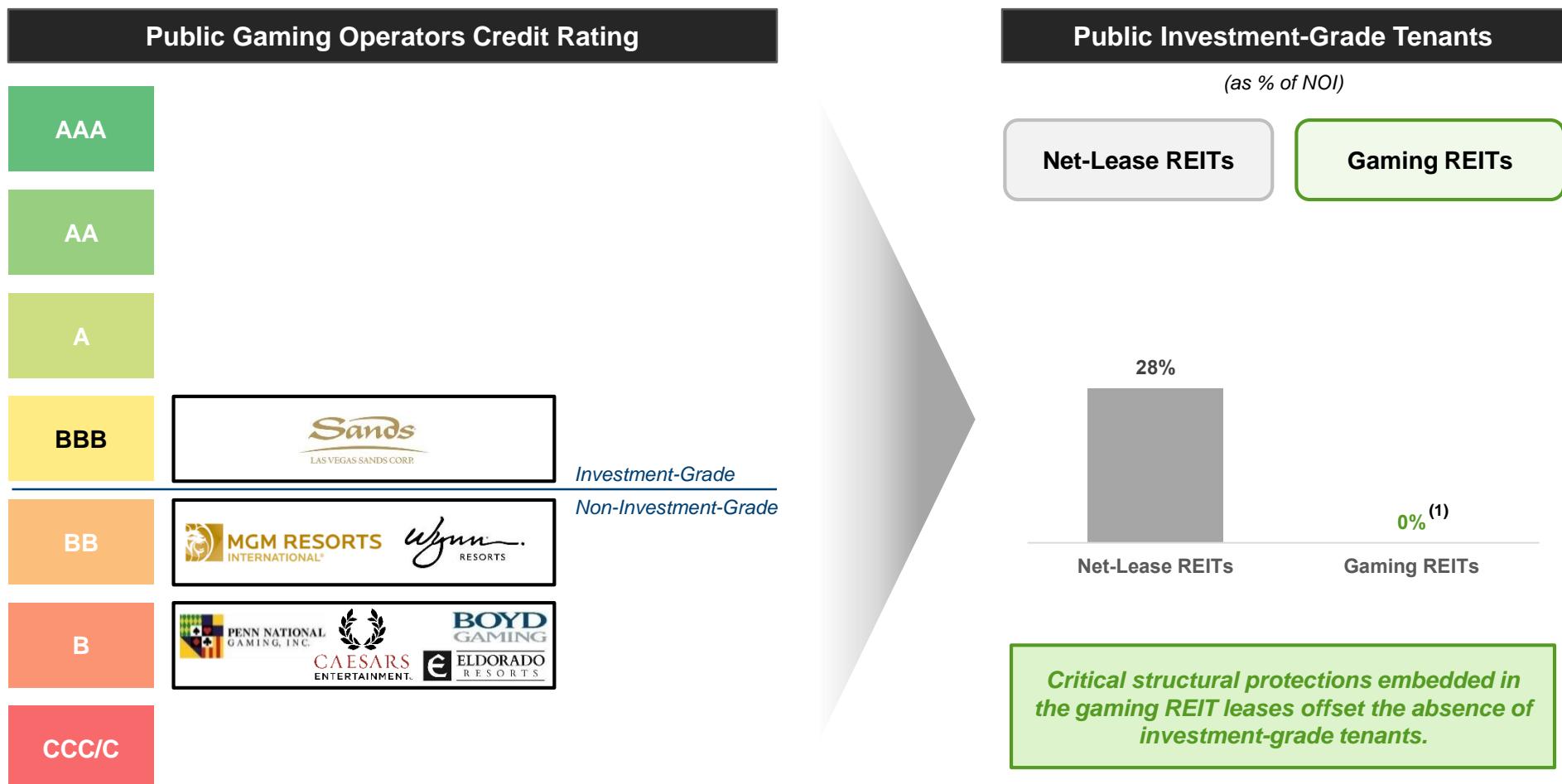


Source: Green Street Advisors



# Valuation: Tenant Creditworthiness

The Net-Lease REITs promote the tenant and industry diversification in their portfolios. The percentage of investment-grade tenants is an important metric for some. The gaming REIT sector is vastly more concentrated in terms of the number of properties and tenants. While none of the public gaming REIT tenants are investment-grade, their operating performance is highly transparent. Even more important, the landlord-favored provisions in most leases provide substantial additional credit support.



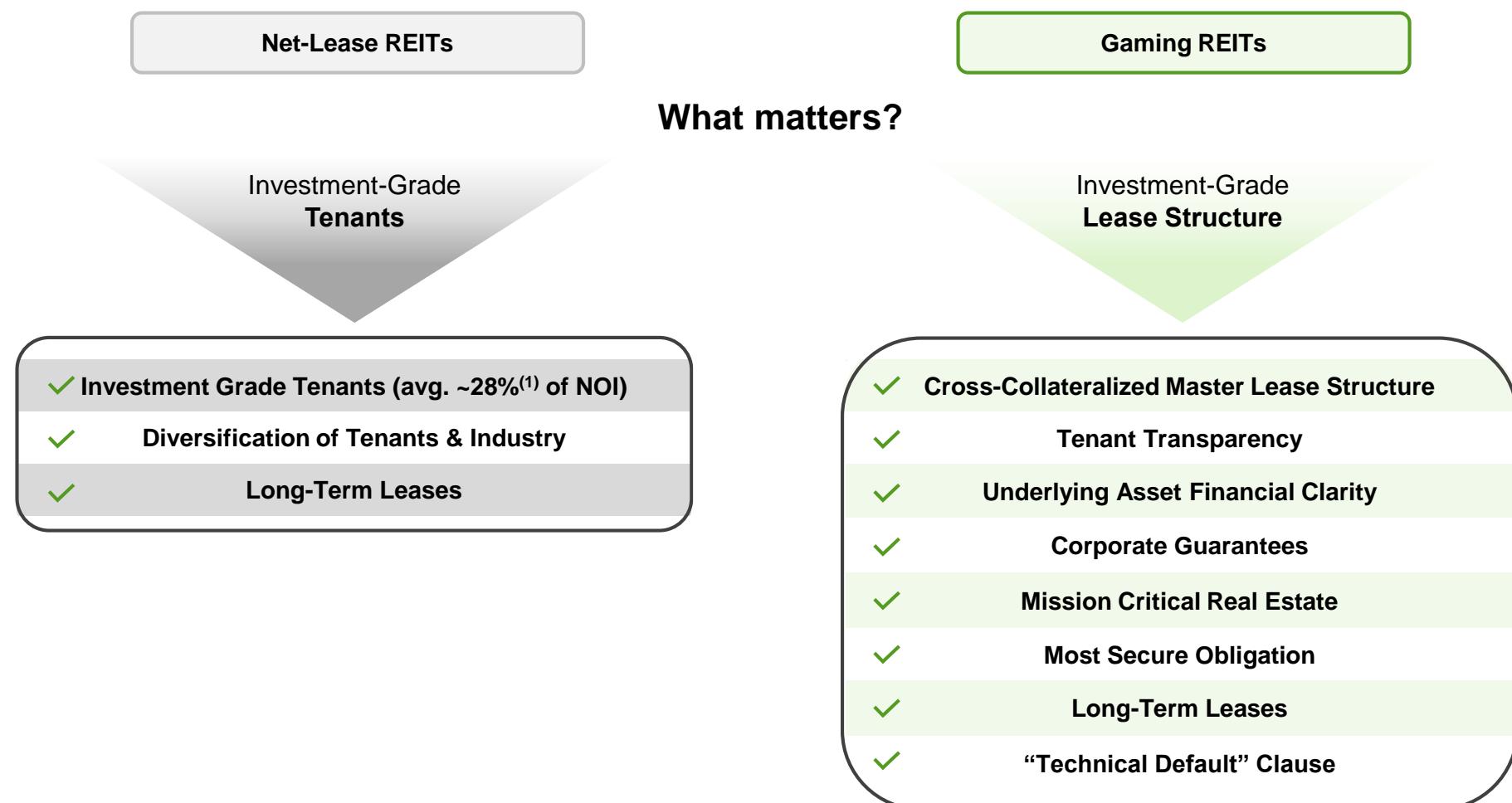
(1) Seminole Hard Rock, a private operator, is an investment grade tenant of VICI  
Source: Green Street Advisors, Bloomberg



# Valuation: Tenant Creditworthiness (cont'd)

What the Gaming REITs lack in terms of investment-grade protection, they make up for in sophisticated lease structures, favorable lease covenants, and additional tenant transparency. In a distressed situation, the rent payment to the owner should take precedence over almost any other financial obligation as it sustains the operator's core business operations.

## Investment-Grade Tenants vs. Investment-Grade Lease Structure

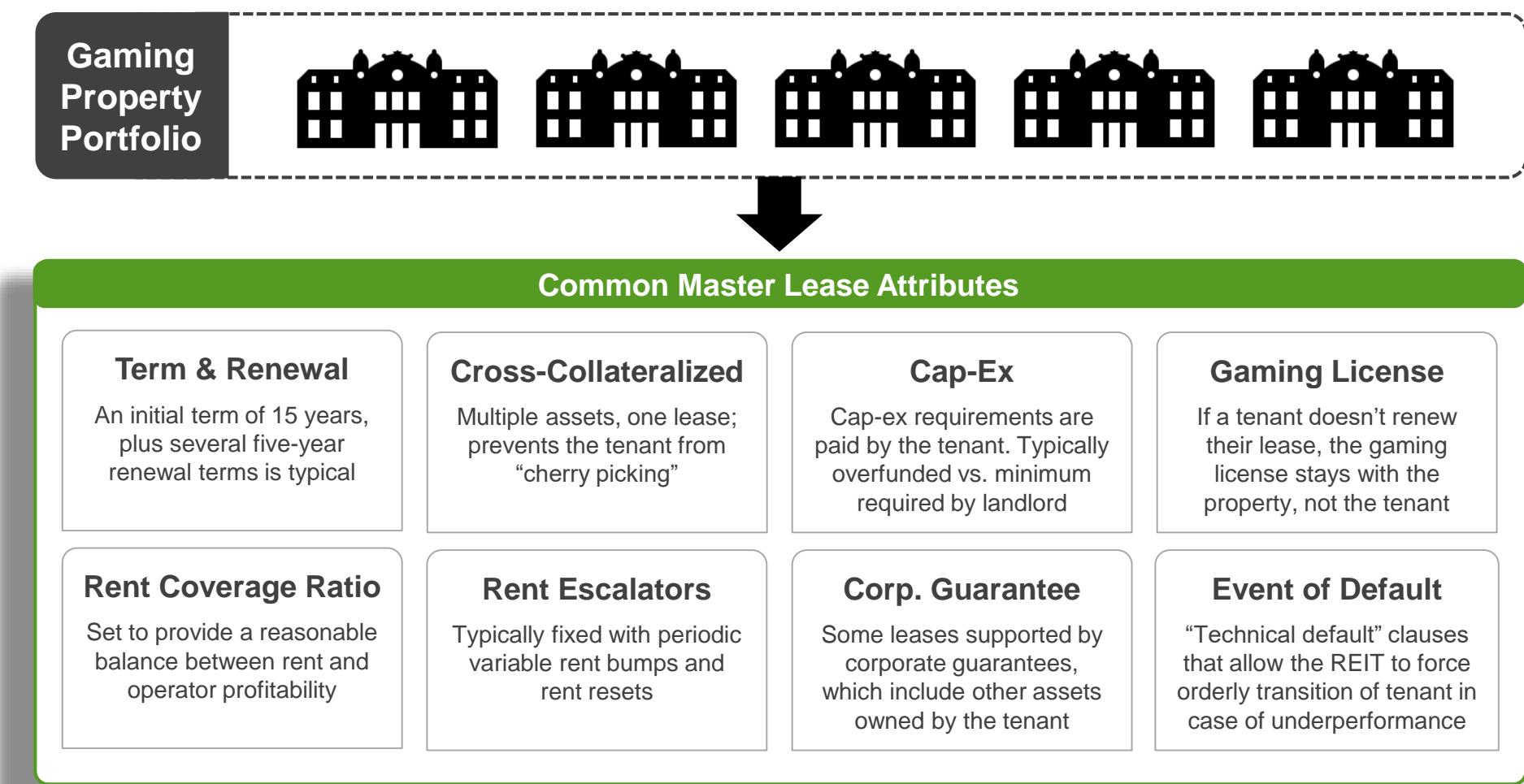


(1) Only actual investment grade-rated tenants; not all have a parent guarantor  
Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Valuation: Master Lease Structure

Many gaming REIT properties are subject to master leases where several assets are pooled into a single lease between the REIT and the operator. The lease typically provides for a single rent payment plus subsequent lease escalations and maturity dates. The master lease structure provides a variety of benefits to both the tenant and the landlord, and it bolsters the credit quality of the “bond” part of the NNN lease.



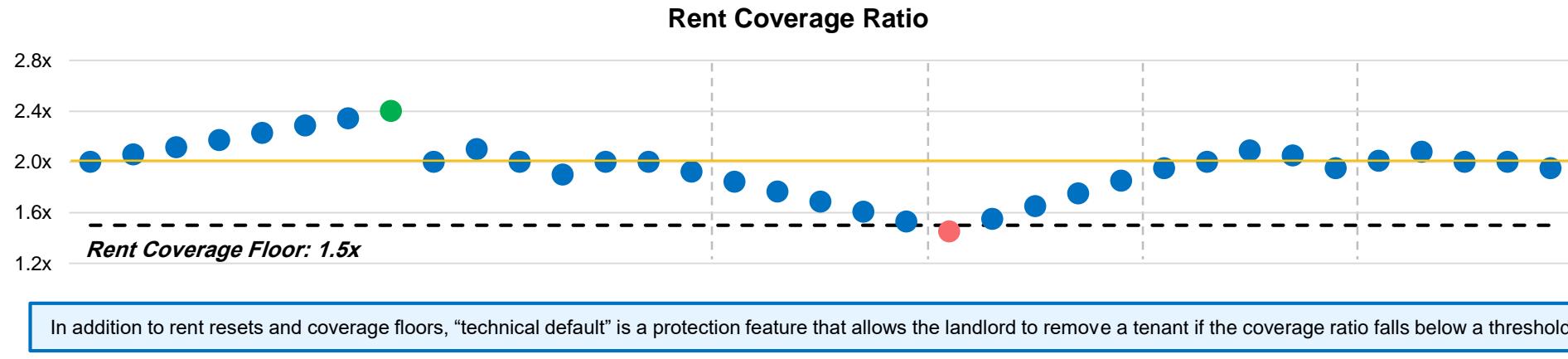
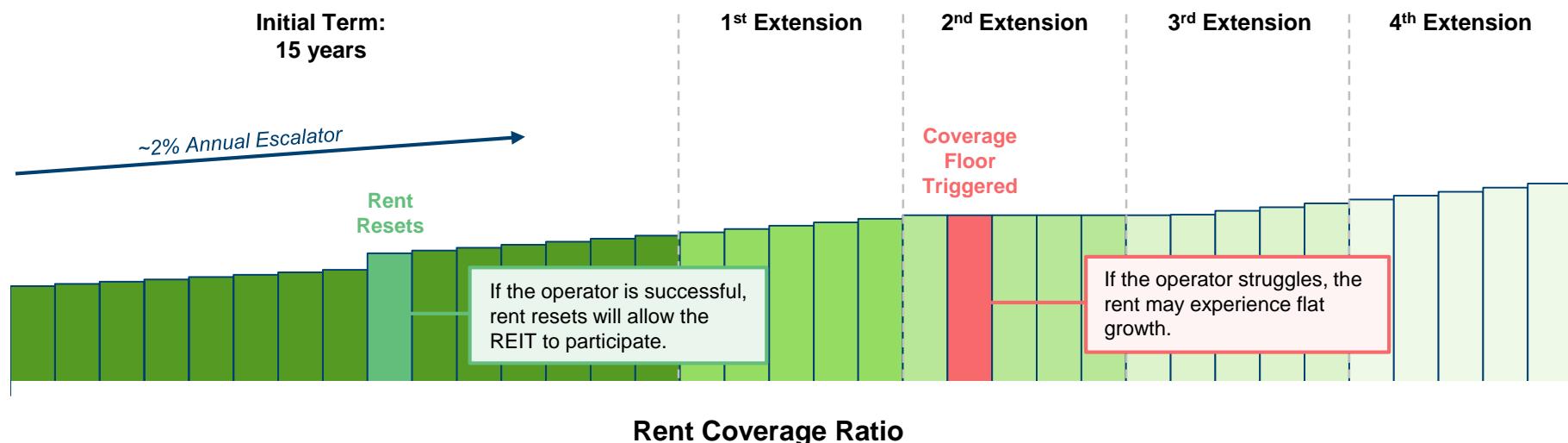
Note: Not all of these attributes are available across the three gaming REITs  
Source: Green Street Advisors



# Valuation: Master Lease Structure (cont'd)

In the later years of the typical gaming REIT master lease, the rent will reset based on the performance of the operator. Under most scenarios, the rent will increase and allow the REIT to participate in the operator's success. However, in distressed situations, where the rent coverage ratio falls below a specified threshold, the variable rent could reset lower, which may lead to flat rent growth until operations have recovered.

Typical Master Lease Structure (*Hypothetical*)



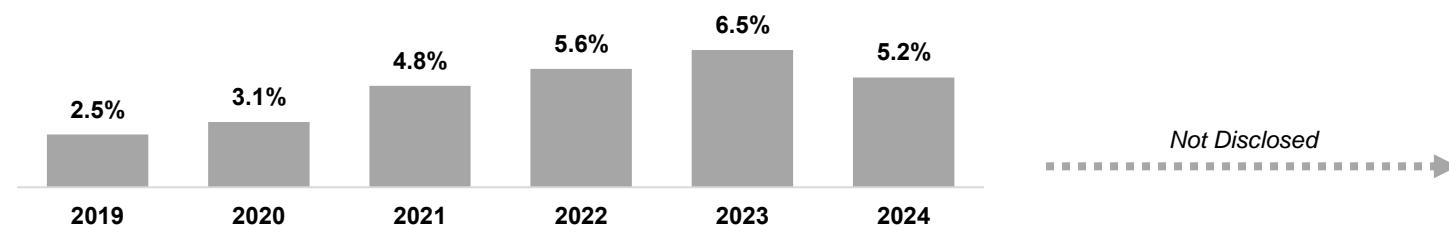
Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Valuation: Lease Duration

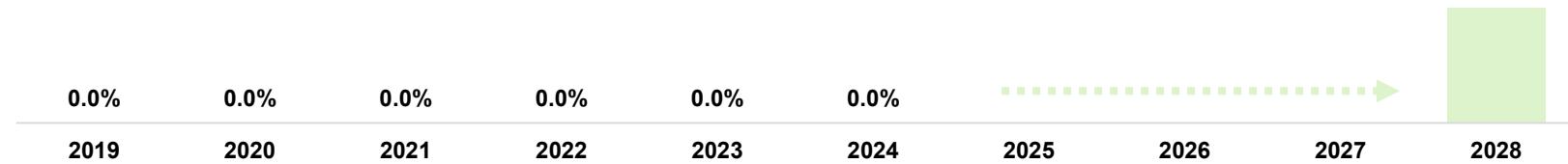
Dealing with maturing leases is both a challenge and an opportunity for most REITs, including the NNN REITs. For the Gaming REITs, lease maturities are a non-issue as the sector is relatively new, and the companies' recently crafted leases have initial terms of 10-15 years. This differentiation provides more clarity and certainty to the future cash flows and dividend-paying ability of the gaming REITs.

Lease Expiration Per Year (as % of NOI)



Net-Lease REITs

~28% of lease expirations on aggregate over the next six years



Gaming REITs

No lease expiration until 2028

Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Valuation: Rent Coverage Considerations

A common metric used to assess the rent-paying ability of a NNN tenant is the “rent coverage ratio.” The figure provides a rough gauge as to how far the EBITDAR of a property or portfolio could fall before the tenant would be unable to pay its rent. In general, the higher the ratio, the lower the risk of default. There are a variety of ways that rent coverage is calculated, which can make direct comparisons difficult across Gaming REITs and other NNN and Healthcare REITs.

## Rent Coverage Ratio Methodologies

### 4-Wall EBITDAR Calculation

The traditional “four-wall” rent coverage ratio includes the EBITDAR generated by the properties within the master lease

$$\text{Coverage Ratio} = \frac{\text{Portfolio EBITDAR}}{\text{Portfolio Rent}}$$

### Corporate Guarantee Calculation

Corporate guarantees add EBITDAR of other assets owned by the tenant that are not in the master lease

$$\text{Coverage Ratio} = \frac{\text{Entity EBITDAR}}{\text{Portfolio Rent}}$$

### Corp. Guarantee + Net Rent Calculation

“Net Rent” calculation subtracts landlord-to-tenant dividend payments from the portfolio rent (in cases where the tenant has ownership stake in the landlord)

$$\text{Coverage Ratio} = \frac{\text{Entity EBITDAR}}{\text{Net Rent}}$$

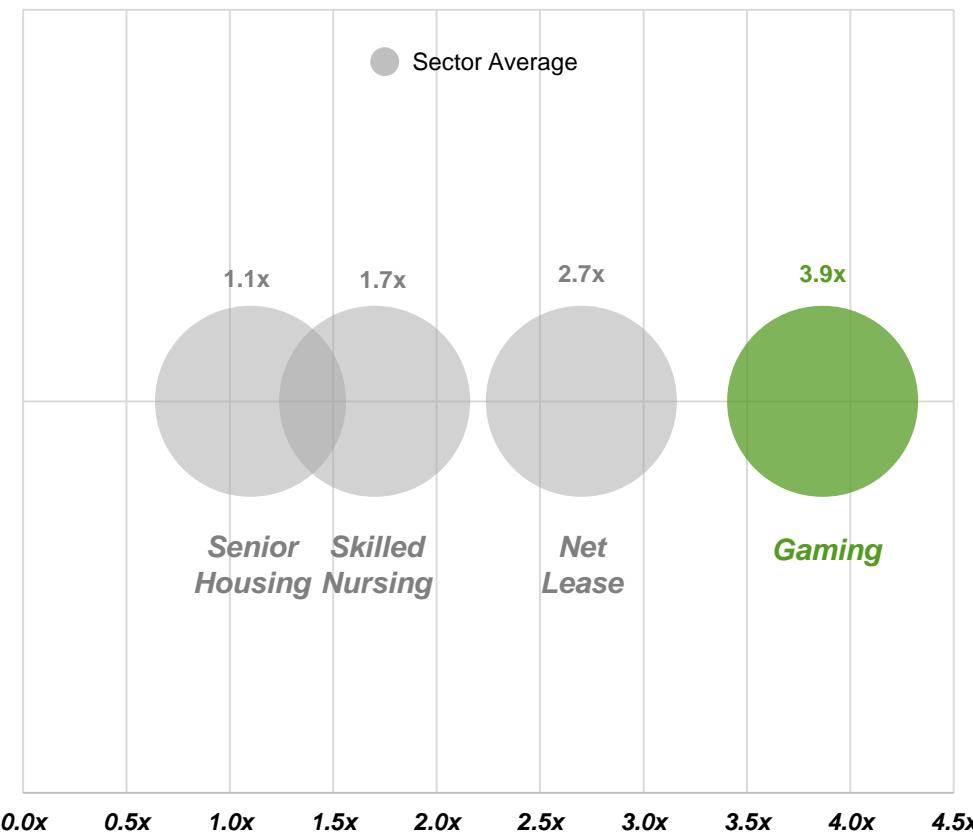


Similar to most  
Net-Lease REITs &  
some Healthcare REITs



MGM GROWTH  
PROPERTIES™  
*(due to unique  
relationship with MGM  
Resorts<sup>1</sup>)*

## Rent Coverage Ratio Averages by REIT Sector

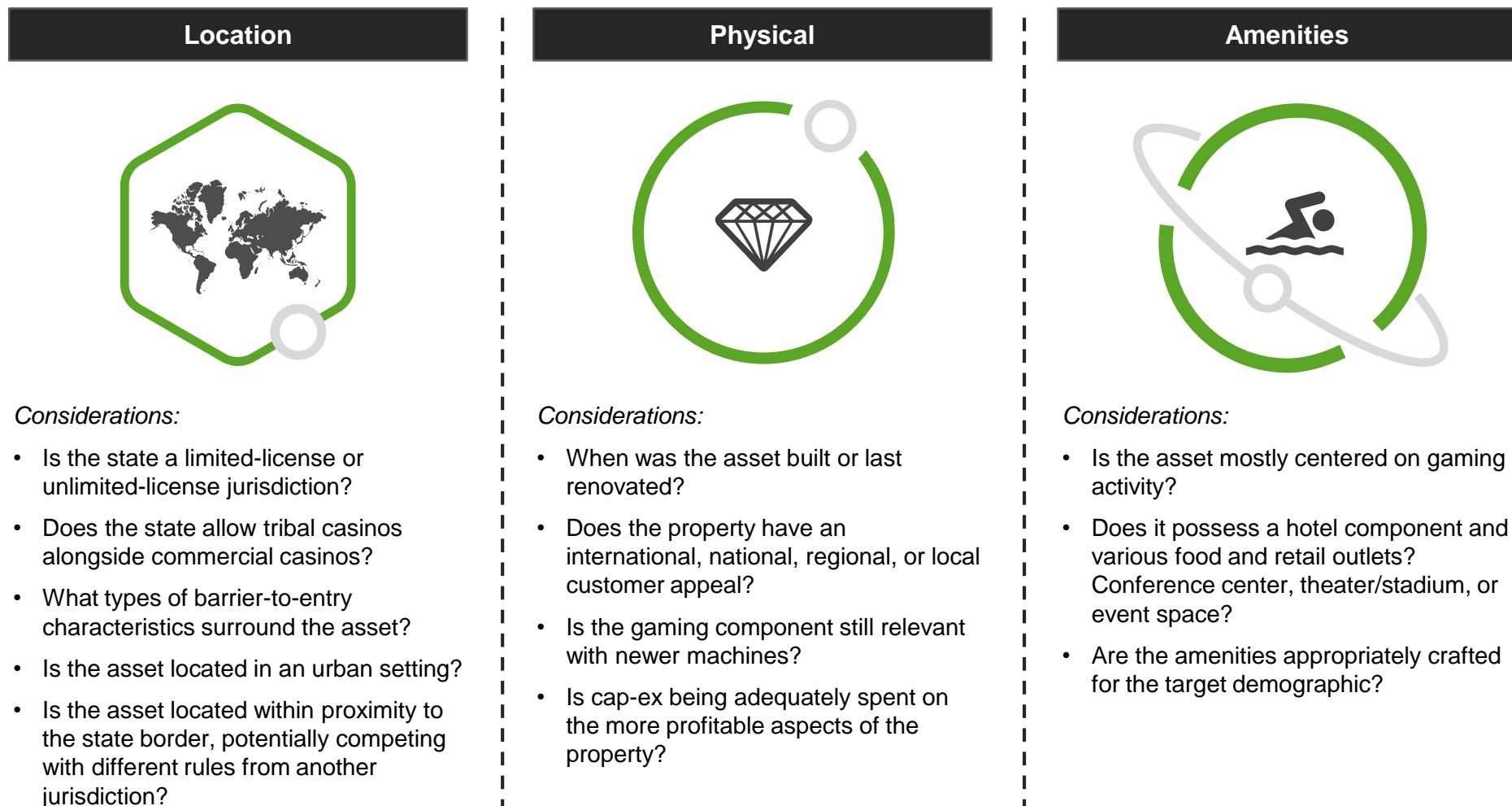


(1) MGP reports rent coverage as EBITDAR / (Rent - Dividends paid to MGM); MGM owns ~69% of MGP  
Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Valuation: Asset Quality Considerations

High values and low cap rates in most property types are typically accorded to the best buildings located in primary markets. Due to the highly regulated nature of the gaming industry, the valuation rules of thumbs used in other property sectors are not as applicable to NNN-leased gaming properties. Physical and locational quality can be trumped by barriers to entry created through license restrictions and other regulations.

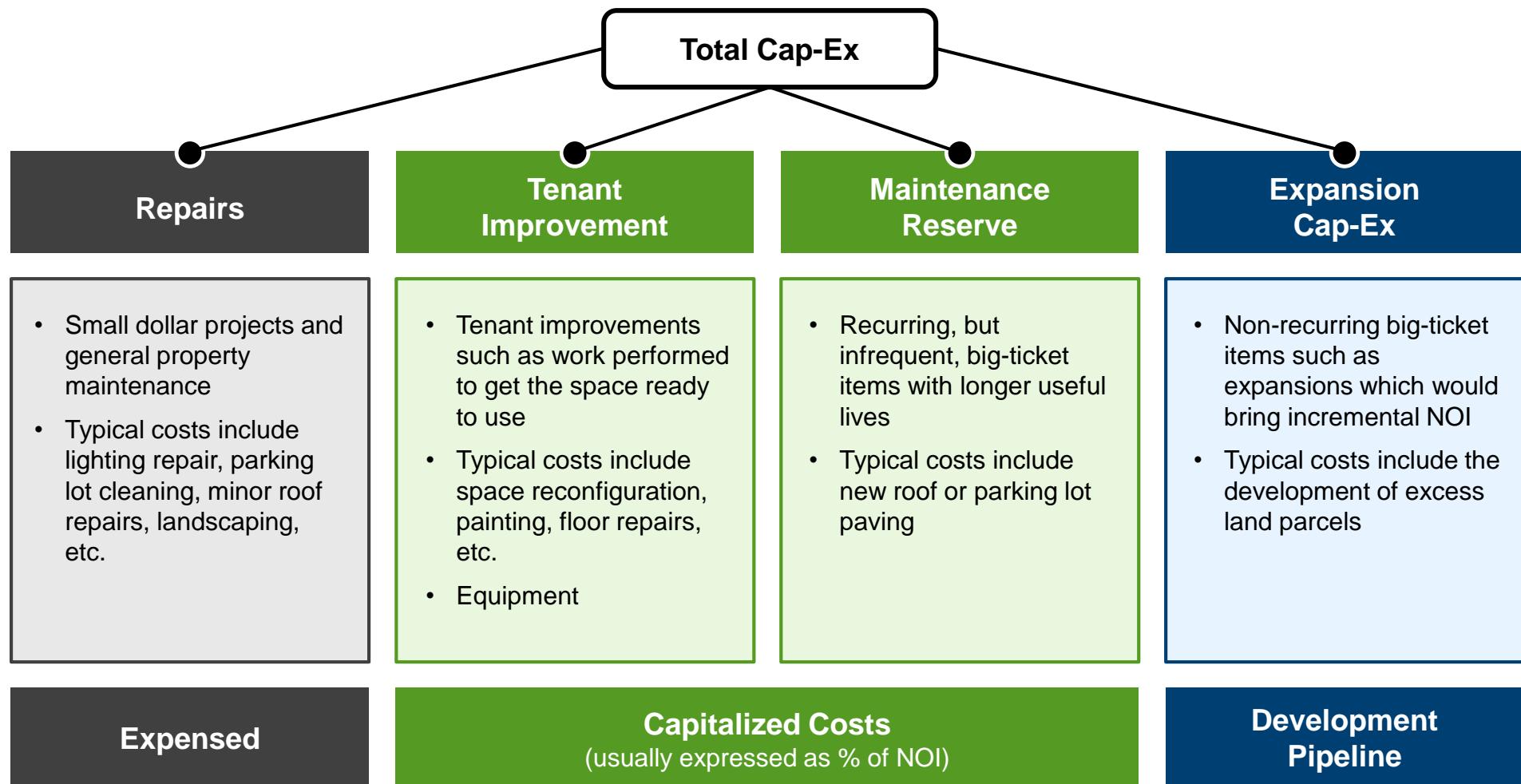


Source: Green Street Advisors



# Valuation: Cap-Ex Overview

Owners of commercial real estate need to reinvest in their properties to keep them competitive. The size of these capital expenditures is often underestimated by the market. One of the most interesting advantages of the NNN lease structure is that cap-ex responsibility is borne by the tenant rather than by the property owner.



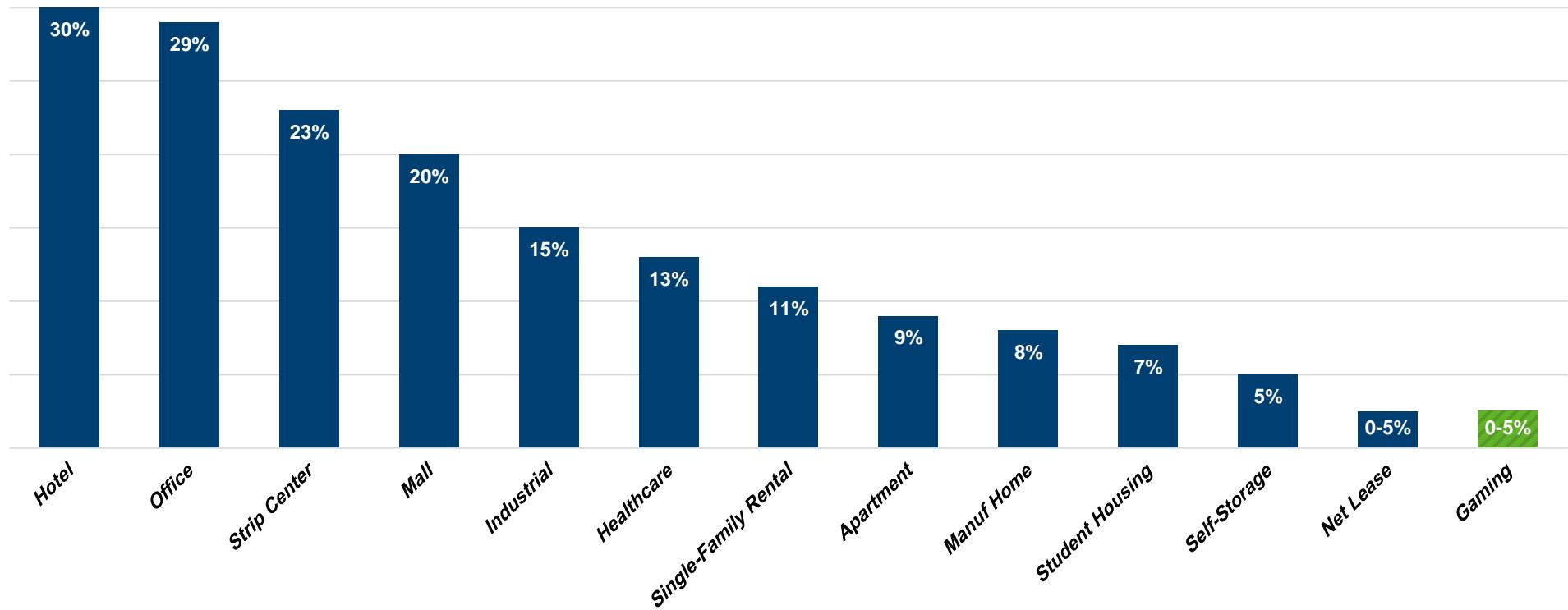
Source: Green Street Advisors



# Valuation: Cap-Ex Burden by Sector

The average cap-ex incurred by property owners over long holding periods can absorb as much as 30% of net operating income. For Net-Lease REITs, the amount is at the very low end of the range and is typically incurred to re-lease space vacated by defaulting tenants or in situations where former tenants elect not to renew their lease. Given the “mission critical” nature of the gaming locations to the operator’s business, lease renewals are likely to be far higher for the gaming REITs than in other property types such as stand-alone retail boxes.

Cap-Ex by Real Estate Sector (as % of NOI)



Note: Green Street normalizes these costs to reflect an expected average over the life of the building.  
Source: Green Street Advisors



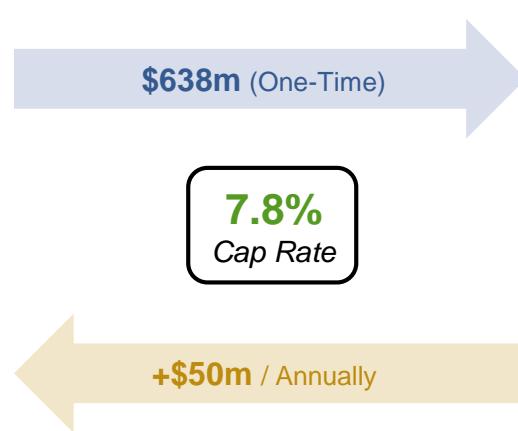
# Valuation: Cap-Ex Case Study

Gaming properties periodically require substantial renovations to remain competitive. The transformation of the former Monte Carlo in Las Vegas provides an informative case study on how the operator and gaming REIT can collaborate on a large-scale property makeover, with each achieving their corporate objectives.



## Transaction Overview

- MGM Growth Properties (REIT) owned the existing Monte Carlo and leased it to MGM Resorts (OpCo)
- MGM Resorts funded the entire \$650m renovation to reposition the asset
- The REIT ultimately acquired substantially all the renovations in exchange for an increase in rent
- MGM Resorts will capture the incremental revenue growth above and beyond the increased rent payment



Source: Green Street Advisors, MGP Investor Material



# Valuation: Internal/External Growth Avenues

Gaming REITs possess several avenues for potential growth. While the sector is relatively new, the fact that the three REITs have communicated different growth strategies is noteworthy as investors can choose the names where the strategy is most appealing.

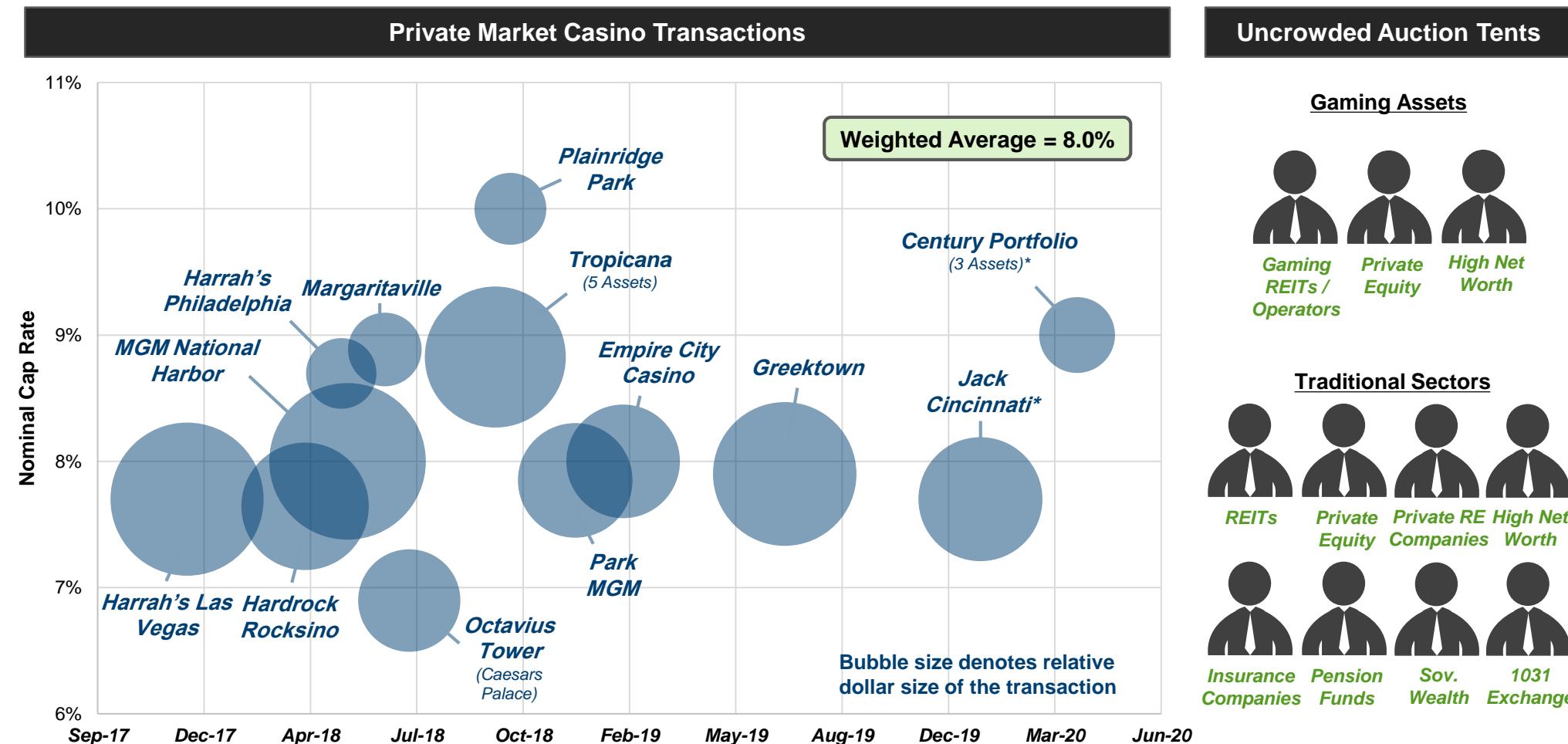
Organic	Acquisition	Development	Other Avenues
<ul style="list-style-type: none"><li>• Contractual rent bumps</li><li>• Potential rent resets</li><li>• Incremental revenue generated by capital expenditures (paid for by the tenant) deployed to certain outlets within the asset</li></ul> 	<ul style="list-style-type: none"><li>• Acquisition of existing assets with or without an existing operator</li><li>• Entering new markets may require considerable regulatory obstacles on the REIT management team / Board</li><li>• Uncrowded auction tents</li></ul> 	<ul style="list-style-type: none"><li>• Right of First Offer (RoFo) for assets under existing operating company partnership umbrella that have been developed or entirely redeveloped</li><li>• Gaming REITs have not been ground-up developers</li><li>• Large land banks</li></ul> 	<ul style="list-style-type: none"><li>• International gaming expansion</li><li>• Diversification into related or other experiential sectors - leisure, entertainment, and hospitality</li></ul> 

Source: Green Street Advisors



# Valuation: Recent Gaming Transaction Comps

Nominal cap rates are the language the real estate industry speaks. Cap rates on recent gaming property trades have been relatively high compared to other property types. A primary reason is that the auction tents for gaming assets are far less crowded than for, say, apartments or warehouses given the operating complexity and daunting regulatory responsibilities assumed by casino owners.



\*Jack Cincinnati and the Century Casino portfolio are expected to close Q4 2019 and Q1 2020, respectively

Note: The combined cap rate for the purchase of Harrah's Philadelphia and Octavius Tower was 9.5% based on an adjusted net purchase price

Source: Green Street Advisors, VICI/MGP/GLPI Investor Materials



# Valuation (Private): Nominal/Economic Cap Rates

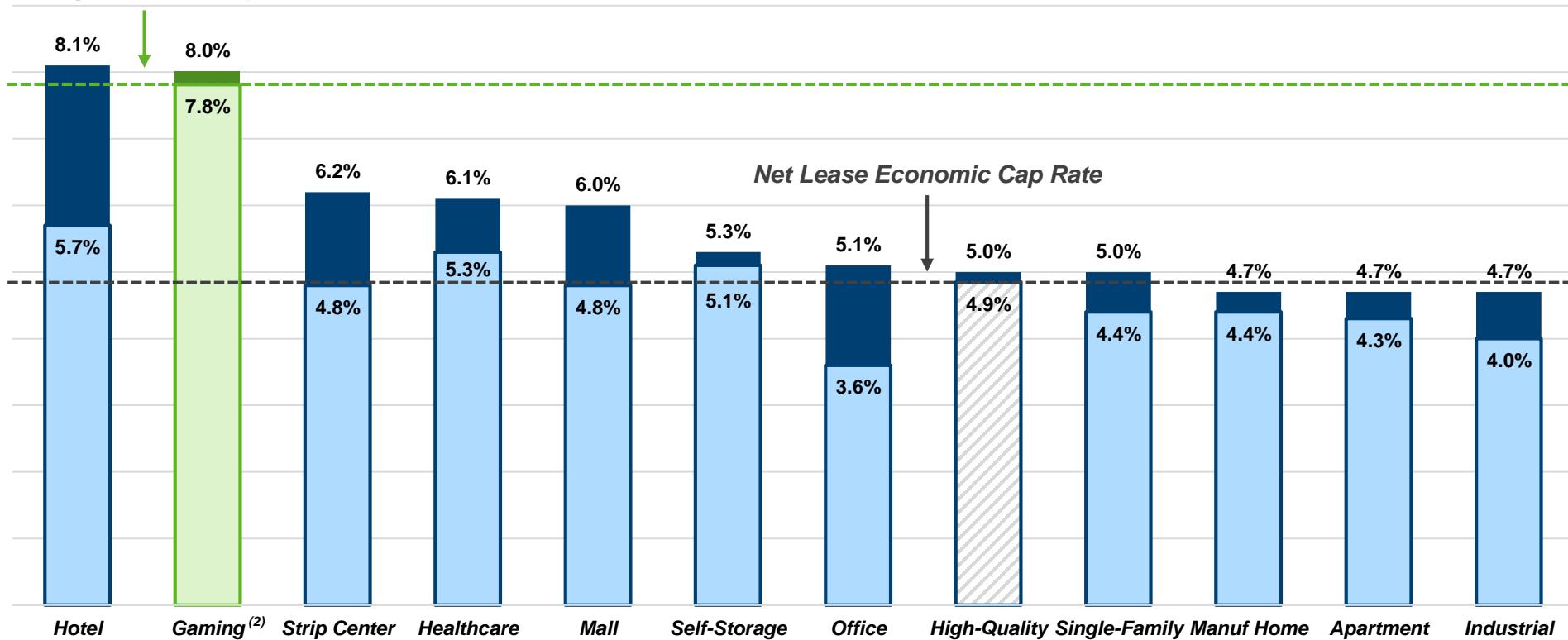
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“Nominal” cap rates are a starting point for assessing how investors are pricing the growth and risk characteristics of cash flows for different property types in their net asset valuation (NAV) of the companies. However, “economic” cap rates provide a more accurate gauge of the investment yield an investor will receive after considering cap-ex. The relative yields generated by the NNN REITs – including the gaming companies – look even better by this measure.

Nominal & Economic Cap Rates by REIT Sector<sup>(1)</sup>

■ Nominal Cap Rates ■ Economic Cap Rates

## Gaming Economic Cap Rate



(1) Based on the REITs in Green Street Coverage Universe as of July 22, 2019, except Gaming

(2) Gaming nominal cap rate is a weighted-average of recent private market transactions

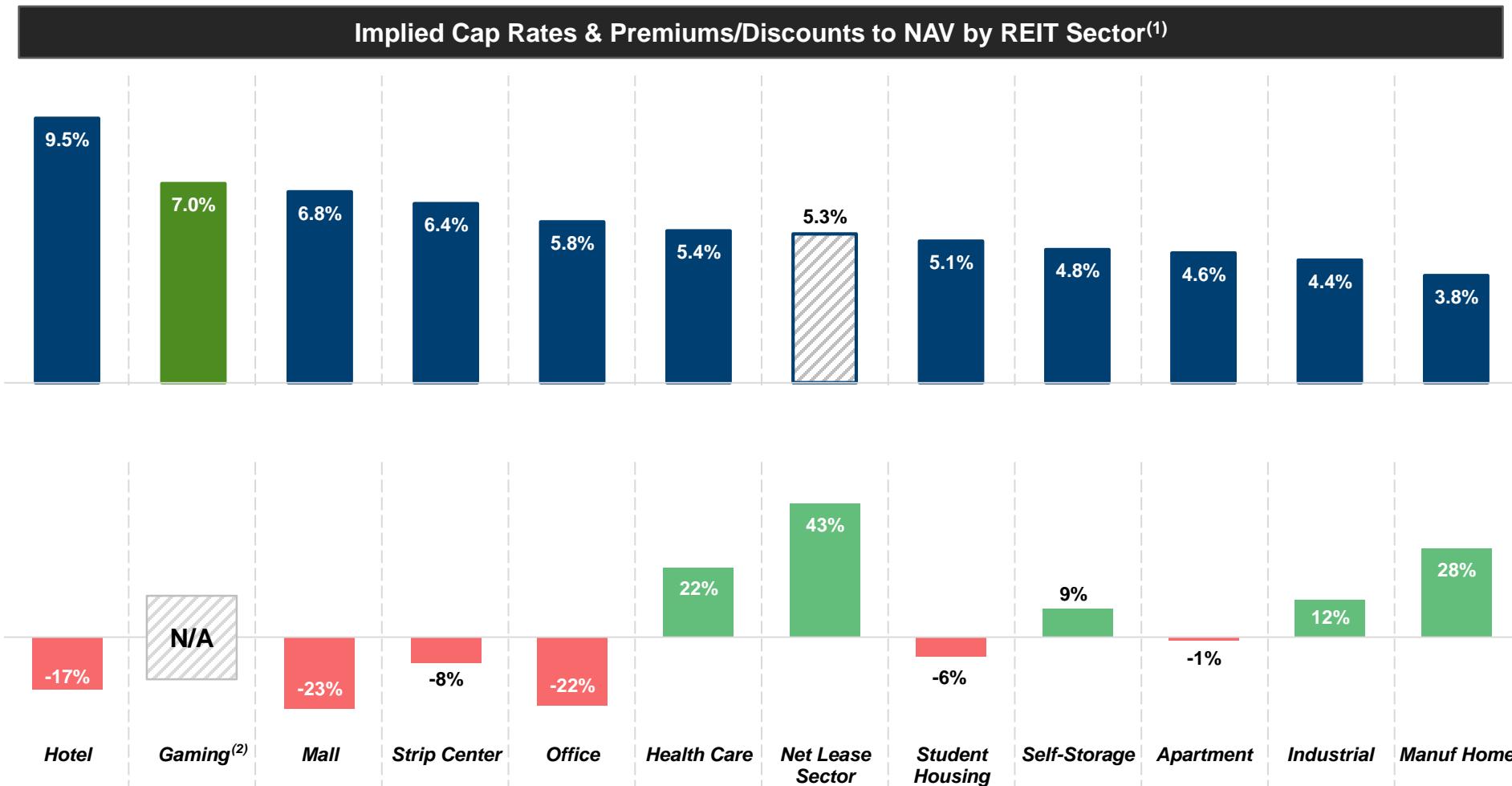
(3) Estimate of cap rate for high-quality net-lease assets based on recent private market transactions

Source: Green Street Advisors, Real Capital Analytics, VICI/MGP/GLPI Investor Materials



# Valuation (Public): Implied Cap Rates

“Implied” cap rates reflect the yield at which the NAV per share equals the current share price of the companies. The measure is used to describe the property yield embedded in a REIT’s current stock price. Implied cap rates are useful for comparing valuations across property sectors.



(1) Based on the REITs in Green Street Coverage Universe as of July 22, 2019, except Gaming

(2) Green Street does not cover the gaming REIT sector

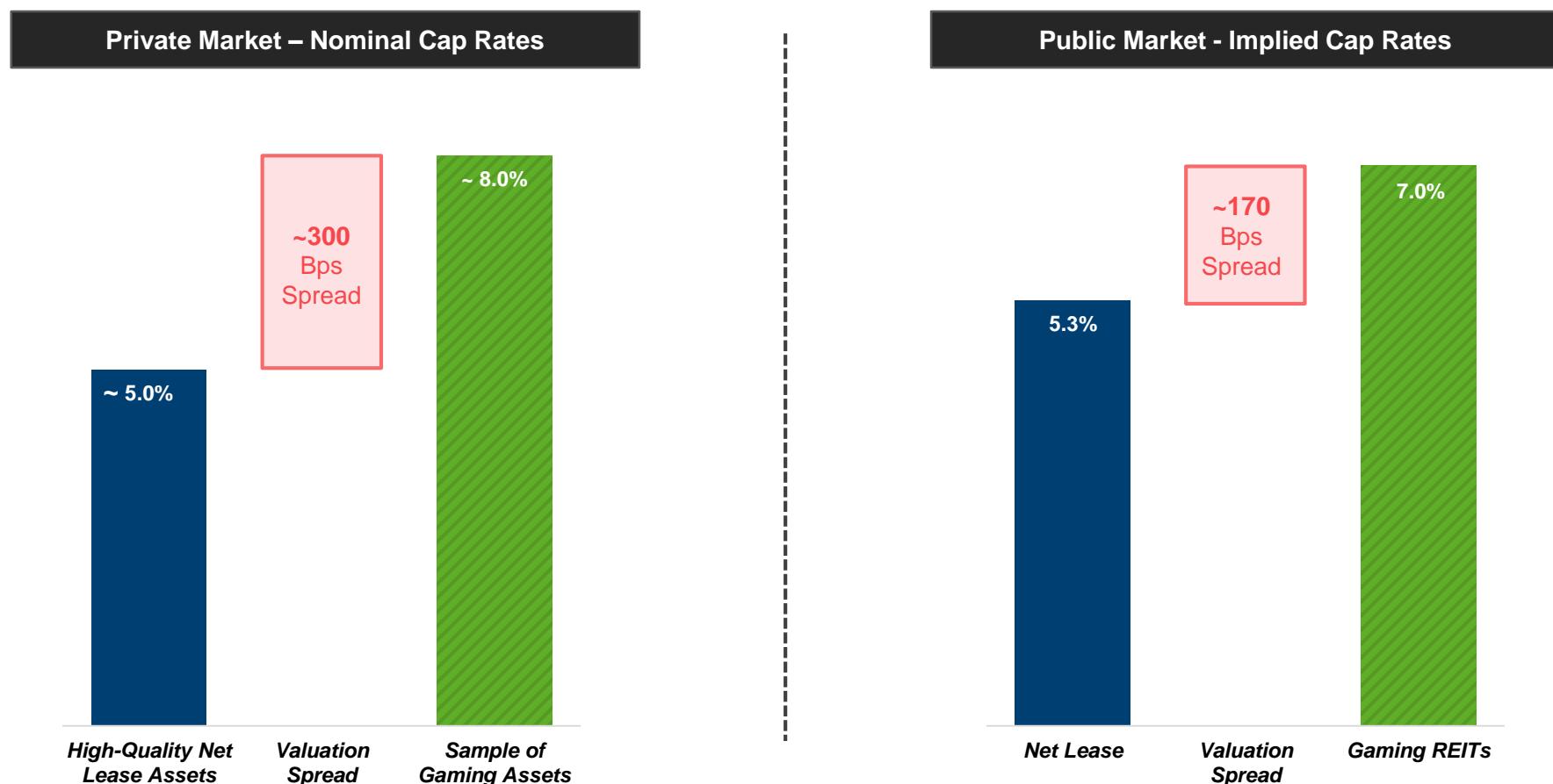
Source: Green Street Advisors, Bloomberg, SNL



# Valuation: Relative Pricing Spread Considerations

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The NNN REIT sector is well-established and better understood by REIT-dedicated investors than the Gaming REIT sector. Nevertheless, the merits of investing in the Gaming REIT sector begs the question of whether a ~300bps cap rate spread in the private market and a ~170bps spread in the public market represent excessive discounting of the “perceived” risk embedded in gaming versus the “real” risk (e.g., regulatory processes) investors are being asked to accept relative to other property sectors.



(1) Net Lease Implied Cap Rate as based on the REITs in Green Street Coverage Universe as of July 22, 2019; Gaming implied cap rate is sourced from Bloomberg as of July 22, 2019  
Source: Green Street Advisors, Bloomberg, Real Capital Analytics, VICI/MGP/GLPI Investor Materials



# Risk Considerations

As investors learn more about the Gaming REIT sector, it will be important to consider the key risk factors that may affect the sector. Some of the most pertinent questions investors are encouraged to explore with the REIT management teams include:

## Gaming REIT Risk Questions to Consider

**1**

Las Vegas experienced a significant, debt-fueled over-building supply challenge during the GFC. What's different now and what were the important lessons learned during that period?



**2**

"Stroke of the pen" risk is a concern. How could changes in gaming legislation and/or the specific tax revenue needs of a particular state potentially impact the pace of new supply growth and the performance of existing gaming properties in that state or in neighboring states?



**3**

The Gaming REIT sector is relatively new, yet the three companies already own ~35-40% of the industry based just on GGR (this percentage excludes other sources of non-gaming revenue). Are the Gaming REITs going to need to diversify into non-gaming properties in order to fulfill external portfolio growth expectations?



**4**

Most NNN REITs tout tenant diversification as a virtue. The Gaming REITs have much more tenant concentration. How should an investor think about tenant and state diversification given jurisdictional relevance, and the impact on warranted share price?



**5**

Rising interest rates are a headwind for bond values. Given that the long-term, NNN leases are quite "bond like", how should an investor think about interest rate changes and their impact on Gaming REIT share values?



**6**

Corporate guarantees add the support of other assets owned by the tenant that are held outside of the master lease. What control, if any, do the REITs have over the potential disposition or financing of these supporting assets?





**Section V.**

# **Appendix**



# Gaming REITs: Financial Metrics

	GAMING & LEISURE PROPERTIES, INC	MGM GROWTH PROPERTIES™	VICI
IPO/Spin-Off Date	2013	2016	2018
Ticker (NYSE)	GLPI	MGP	VICI
Headquarters	Wyomissing, PA	Las Vegas, NV	New York, NY
2018 Total Revenue	\$1,055M	\$1,002M	\$898M <sup>(1)</sup>
Equity Market Cap	\$8.1B	\$8.7B	\$9.9B
Debt / EBITDA	5.6x	5.6x	4.3x
Dividend Yield	6.7%	5.5%	5.2%
EV/EBITDA Multiple	~13x	~15x	~15x
Implied Cap Rate	~7.5%	~6.9%	~6.6%

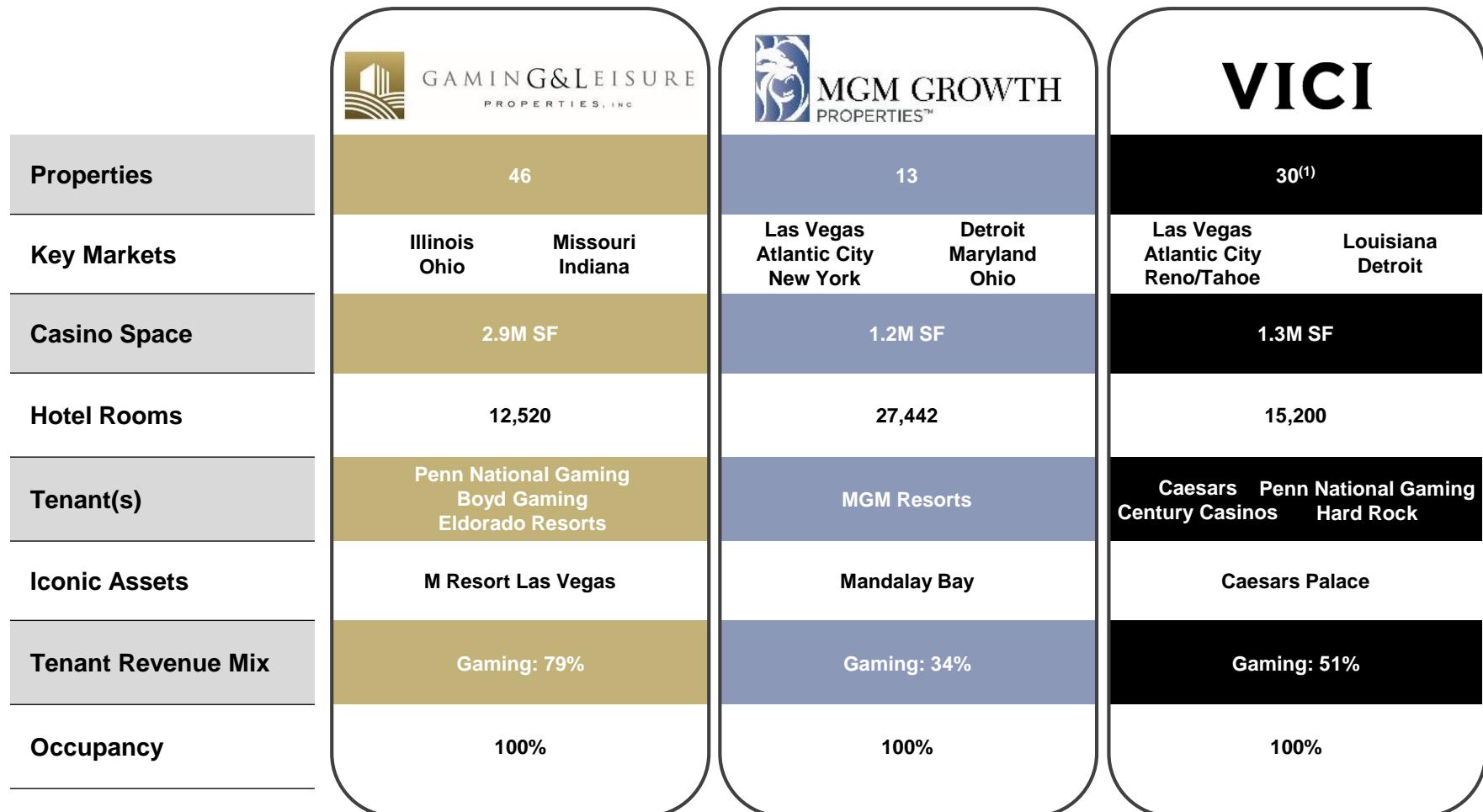
(1) Does not include two acquisitions that closed in 2019 (combined \$78.8m of rent) or acquisitions announced in 2019 to-date which will add an additional \$320.3m when closed

Note: Data as of 7/22/19, unless otherwise noted

Source: Green Street Advisors, SNL, Bloomberg, Company Estimates



# Gaming REITs: Portfolio Metrics



(1) Includes seven pending acquisitions

Note: Data as of 7/22/19, unless otherwise noted

Source: Green Street Advisors, SNL, Bloomberg, Company Estimates



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