HILLIARD LYONS

Healthcare Real Estate Investment Trusts
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COMPANY UPDATE

Omega Healthcare Investors, Inc.

OHI -- NYSE – Buy-2

Q4 Earnings Update

Investment Highlights

- OHI reported Q4 normalized FFO of $0.88 a share, compared to $0.81 a share normalized in the year earlier period, to our estimate of $0.86 a share, and the consensus estimate of $0.85. Non-recurring items pushed as reported FFO down to $0.65 a share, but we exclude these items for our normalized estimate. Results continued to be very strong despite the level of investments below our expectation, with the AVIV purchase continuing to exceed the expectations management offered at the time of purchase.
- An expected rise in interest rates has driven REIT prices down recently. OHI has not escaped that decline, and that decline has made the shares even more attractive, in our opinion. Our expectation that rates will not rise as much as investors may be anticipating, results in the decline offering an attractive opportunity to pick up OHI shares at a relatively attractive price. Our $40 per share one year price target is based on a multiple of 11 times our estimate for 2017 FFO, slightly below historical multiples. We may adjust this target after the conference call based on any changes to our estimates for recently announced acquisitions and the recent decline in group values.
- In light of the current interest rate environment, OHI's 7.6% yield on its just increased dividend looks very attractive, sitting well over two percentage points above the peer group. We expect the payment to continue to be increased on a quarterly basis going forward, something that may very well be necessary, with the Q4 earnings number actually exceeding the dividend payment. At this point we remain of the opinion that investors willing to take on some risk and searching for dividend income and price appreciation should consider OHI shares, although we will be waiting until after the 10AM conference call before making any adjustments to our rating, estimates and/or price target.

Key Metrics

OHI - NYSE - as of 2/8/17		$32.57
1 Year Price Target		$ 40.00
52-Week Range	$26.96 -	$38.09
Shares Outstanding (mm)		198.8
Market Cap. ($mm)		$6,474.9
1-Mo. Average Daily Volume		1,062,000
Institutional Ownership		85.0%
Debt/Total Capital Dec-16		41.6%
Est 3-year FFO Growth Rate		6.0%
Est 3-year Dividend Growth Rate		6.0%
Book Value		$ 21.40
Dividend		$ 2.48
Dividend Yield		7.61%
Est. Fixed Charge Coverage		3.7 X

FFO Per share

	2015		2016		Prior 2017E	Current 2017E
1Q	$0.71	--	$0.83		$0.88	$0.88
2Q	$0.77	--	$0.87		$0.91	$0.91
3Q	$0.79	--	$0.83		$0.90	$0.90
4Q	$0.81	--	$0.88		$0.92	$0.92
Year	$3.08		$3.41	*	$3.62	$3.62
P/E	10.6x		9.6x			9.0x

*-May not add up due to rounding, not restated.

Revenue ($mm)

	2015		2016	Prior 2017E	Current 2017E
1Q	$133.4	--	$212.9	$245.2	$245.2
2Q	$197.7	--	$228.8	$253.6	$253.6
3Q	$202.0	--	$224.6	$253.7	$253.7
4Q	$210.5	--	$234.5	$262.6	$262.6
Year	$743.6		$902.8	$1,015.0	$1,015.0

Company Description: *Omega Healthcare Investors, headquartered in Hunt Valley, MD, is a real estate investment trust (REIT) that has investments in healthcare facilities, specifically long term care facilities, located throughout the country, mainly skilled nursing facilities, although the company also owns a small number of assisted living facilities and specialty hospitals.*

Note Important Disclosures on Pages 6-7.
Note Analyst Certification on Page 6.

Fourth Quarter Review

Total revenue was $234.5 million versus $210.5 million, an 11.4% increase as a result of recent investments and normal rental bumps. Rental income of $194.9 million was up 11.2% (please see income statement on page 3), again due to acquisitions and rental bumps. Mortgage interest income fell 9.9% to $15.8 million from $17.6 million due to mortgage roll offs and write downs. The company also saw a 2.4% increase in revenue from direct financing leases to $15.7 million this year.

General and administrative expense fell 2.1% to $7.5 million from $7.6 million, below our expectations as management continues to restrain such spending very well. Interest expense rose 15.8% to $46.9 million with the increase in quarter-end debt, which has risen to $4.37 billion from $3.57 billion at the end of 2015. Interest expense was in line with our expectations. Depreciation expense rose 16.5% to $70.8 million versus $60.8 million. Fourth quarter net income available to common shareholders was $124.3 million versus $60.6 million. The per share net income this quarter was $0.63 versus $0.31 on 3.7% more common shares outstanding in this year's Q4. Note that the EPS number was actually above the dividend in this quarter, indicating we could continue to see dividend increases, possibly more than the penny a share that has been typical.

Ongoing funds from operations (FFO) on a normalized basis, which exclude real estate gains as well as other non-recurring and non-cash items, were $180.4 million compared to $159.4 million in last year's fourth quarter, a 13.2% increase. Normalized FFO per diluted share were $0.88 versus $0.81. For the year, normalized FFO was $3.41 versus $3.08 a share.

The company had $93.7 million in cash on its balance sheet at quarter end. The company's debt to capital ratio was 41.6% at quarter end up from 34.2% at the end of 2015, due to the decline in share price. OHI has no debt coming due until its line of credit matures in 2019. We expect no liquidity issues for OHI, as it has been very pro-active in taking care of its maturities and has a strong balance sheet.

Other 4th Quarter Activity

Investment/Capital Markets Activity – During the fourth quarter OHI announced a $50 million joint venture investment under which a joint venture 15%-owned by OHI will be purchasing 64 facilities from Welltower (HCN-$66.03) for $1.1 billion. The JV will receive $103.9 million a year in rent with annual escalators. OHI also entered into an asset management agreement with the JV. In addition to this investment, the company undertook $50 million in capital renovation and construction projects. Also during Q4 the company issued 1 million shares of common stock under its "at the market" (ATM) and dividend reinvestment programs, raising $30 million.

Dividend – Following an elimination of the dividend for a period stretching from 2001 through the latter part of 2003, OHI has instituted consistent dividend increases. In fact, OHI has raised the dividend 12 times over the past 3 years. In 2011 alone, the quarterly rate per share was increased to $0.38 (from $0.37) in the second quarter, and then to $0.40 for the third quarter payment. OHI then increased the payment for the first quarter of 2012 by another penny to $0.41 a share and another penny with the Q2 payment to $0.42 a share and two cents more in the fourth quarter, raising the payment to $1.76 annually. Then in 2013, 2014, 2015 and 2016 the company increased the dividend in each quarter, ending with an annual payment of $2.44 a share and then made another bump up early this year for the first quarter pushing the payment to $2.48 a share.

Quarterly Income Statement

(in thousands)	4Q 2016	4Q 2015	% Change
Rental Income	$194,891	$175,292	11.2%
Other Investment Income	$7,210	$1,811	298.1%
Miscellaneous	$823	$481	0.0%
Income from Direct Financing Leases	$15,724	$15,354	2.4%
Mortgage Interest Income	15,838	17,574	-9.9%
Total Revenue	234,486	210,512	11.4%
General & Admin	7,478	7,635	-2.1%
Legal expense	0	0	0.0%
Restricted Stock Expense	3,674	4,451	-17.5%
Acquisition Costs	-2	2,018	
Provision for Uncollectables	5,878	7,579	
Impairments	0	3,040	
Nursing Home Expense for Owned and Operated	0	0	0.0%
EBITDA	217,458	185,789	17.0%
Interest Expense	46,872	40,479	15.8%
Depreciation Expense	70,808	60,794	16.5%
Income (Loss) Before Discontinued Operations and Other Items	99,778	84,516	18.1%
Discontinued Operations (including gain on sale of assets)	30,277	(58)	
Non controlling	(5,185)	(2,901)	
Investment interest and other	(611)	(439)	
Debt refinancing costs	0	(20,476)	
Net Income (Loss)	$124,259	$60,642	104.9%
Net EPS (diluted)	$0.63	$0.31	105.2%
Avg. Shares Outstanding (diluted)	204,955	197,560	3.7%

Funds From Operations	4Q 2016	4Q 2015	
Net Income	$129,883	$63,543	104.4%
Depreciation Expense	71,915	60,794	18.3%
Other (adding/substracting one-time items)	(21,377)	35,025	
Normalized Funds From Operations	**$180,421**	**$159,362**	13.2%
Normalized FFO Per Share (diluted)	**$0.88**	**$0.81**	9.1%

Source: Company reports.

Consolidated Balance Sheet

(in thousands)	December 31, 2016	December 31, 2015
Real Estate Assets		
Land and Buildings	$7,566,358	$6,743,958
Less: accumulated depreciation	$ (1,240,336)	$ (1,019,150)
Total Net Real Estate Investments	6,326,022	5,724,808
Cash and Cash Equivalents	93,687	5,424
Net Investment in Direct Financing Leases	601,938	587,701
Mortgage notes receivable	639,343	679,795
Accounts Receivable	240,035	203,862
Other Investments	256,846	89,299
Goodwill	643,474	645,683
Restricted Cash	13,589	14,607
Real estate held for sale	52,868	6,599
Other assets	81,458	61,231
Total Assets	**$8,949,260**	**$8,019,009**
Bank Borrowings	$190,000	$230,000
Mortgage Loan payable	54,365	236,204
Unsecured Borrowings	4,122,489	3,102,882
Real Estate Purchase Liability	0	0
Bond payable	0	0
Accounts payable and accrued expenses	360,514	333,706
Dividends payable	0	0
Other	9,906	15,352
Total Liabilities	**$4,737,274**	**$3,918,144**
Preferred stock	-	-
Common Stock	19,614	18,740
Capital in Excess of Par Value	4,861,408	4,609,474
Cumulative Net Income	1,738,937	1,372,522
Cumulative Dividends	(2,707,387)	(2,254,038)
Other	299,414	354,167
Total Shareholders' Equity	**4,211,986**	**4,100,865**
Total Liabilities and Shareholders' Equity	**$8,949,260**	**$8,019,009**

Balance Sheet Ratio Analysis	December 31, 2016	December 31, 2015
Net R/E Investments / Total Debt	69.0%	62.3%
Debt to Equity	103.7%	87.0%
Debt as % of Total Assets	48.8%	44.5%
Shareholders' Equity as % of Total Assets	47.1%	51.1%

Source: Company reports.

First Take

The fourth quarter results were excellent, not only exceeding the consensus but also our above consensus number, as the AVIV transaction continues to benefit results through economies of scale. Management initiated guidance for 2017, offering a range for normalized FFO of a very strong $3.40 to $3.44, well below our current estimate of $3.62 a share, which includes acquisitions and investments not included in OHI's guidance, and is also below the consensus estimate of $3.46 a share. Note that just annualizing the company's Q4 number gives one normalized FFO of $3.52 a share. So including normal rental bumps, continued rationalization of all of the recent investments and ongoing construction projects, we have a tough time justifying a reduction in 2017 numbers in comparison to the Q4 number. As such, we believe that the company is likely to easily exceed guidance by the end of 2017, and unless we see some rationale for a drop in the Q4 number, we are likely to continue to be above guidance, although we may adjust numbers after talking to management.

The strength of the company's results is reassuring in light of most of the larger healthcare REITs exiting the skilled nursing area. This is creating more pure play peer companies, although OHI should remain dominant with a solid cost of capital advantage, larger and more diversified portfolio and a wider network of relationships. In fact, we believe that some of these spin-off companies may eventually be acquisition targets for OHI. The acquisition activity so far in Q1 is below our expectations, although we will also be asking management about any further potential acquisitions, as well as how the acquisition market is currently looking from a competition perspective and how future development activity is likely to impact results. There appear to be absolutely no issues with the company's capital structure at this point, as management has stretched out its maturities to a point where it has no appreciable debt due for over two years and has added debt capacity. All of this activity should offer significant opportunity to use additional debt for purchases should attractive acquisition opportunities arise. We will issue a full report discussing all of these issues and any changes in estimates or price target following the 10AM conference call. Overall we view it as a solid quarter and while the forward outlook is below our expectation, we believe that is just typical management conservatism.

Risks

There are a number of risks in owning OHI shares and REITs as an investment group. REITs in general need access to debt capital to grow, if such debt capital is unavailable, the company may have difficulty in growing. The company's dividend is very attractive to shareholders and OHI, as well as REITs in general, have seen their prices rise with the decline in overall interest rates. Should rates rise, that could hurt OHI's share price. Because of their thirst for debt, changes in interest rates can also impact a REIT's cash flow and ability to make accretive acquisitions. OHI's dependence upon the long-term care sector of the health care real estate group could create issues due to government payments being the de-facto source for much of its rent. With reimbursements cut, as the Center for Medicare and Medicaid Services reduction illustrates, there will be a negative impact on its tenant base, which in turn could have a negative impact on OHI. It is always possible that the company could make a poor acquisition in the future. OHI's geographic exposure to Florida might be an issue if the state has further economic problems and is forced to cut reimbursements to providers claiming Medicaid payments. There is also integration risk with all of the deals that OHI is doing and of individual deals being completed. Changes to the Affordable Care Act could also create risk for OHI.

Annual yield is calculated by dividing the distribution amount by the current market price of the security. For US income tax purposes, the Company may classify all or a portion of its distributions as dividends or other non-dividend distributions. Note that for some investors, for US income tax purposes all or a portion of the Company's 2016 dividend or distribution was treated as return of capital and not as "dividend income" as reflected on the IRS Form 1099-Div for the 2016 tax year. The Company generally makes a final determination regarding the proper tax treatment of distributions after calendar year end. We urge each shareholder to consult with his or her own tax advisor to determine the tax consequences of the distributions received, including any state, local or foreign tax considerations.

Additional information is available upon request.

Analyst Certification

I, John M. Roberts, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

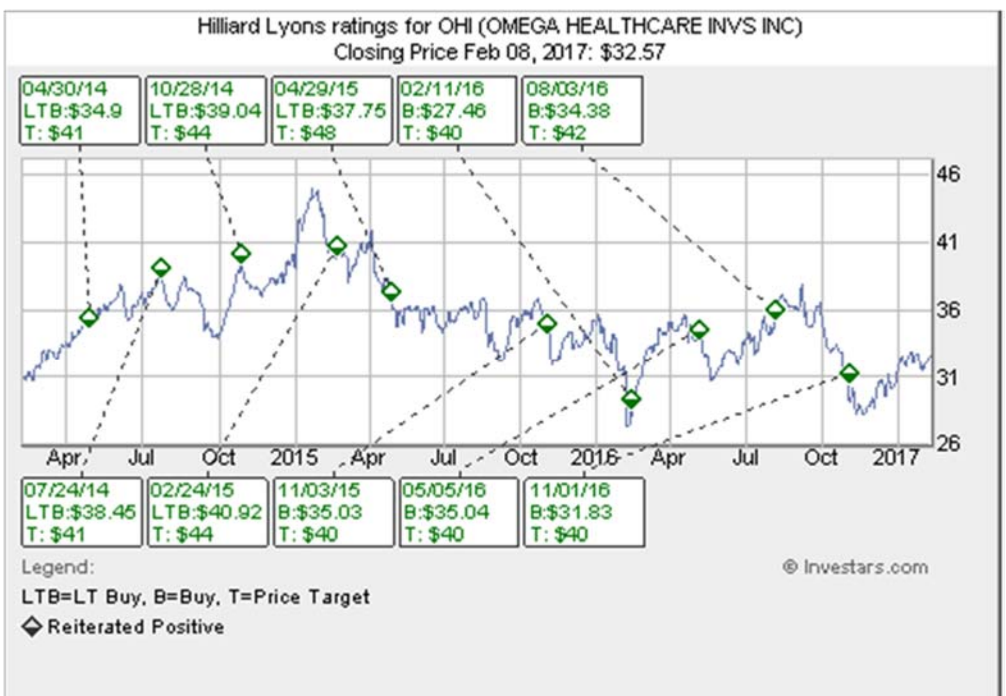
Important Disclosures

Hilliard Lyons' analysts receive bonus compensation based on Hilliard Lyons' profitability. They do not receive direct payments from investment banking activity.

The author of this report or members of his household have a long position in the common stock of OHI, but may not engage in buying or selling contrary to the recommendation.

Investment Ratings
Buy - We believe the stock has significant total return potential in the coming 12 months.
Long-term Buy - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.
Neutral - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.
Underperform - We believe the stock is vulnerable to a price set back in the next 12 months.

Suitability Ratings
1 - A large cap, core holding with a solid history
2 - A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks
3 - An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage
4 - Speculative, due to small size, inconsistent profitability, erratic revenue, volatility, low trading volume or a narrow customer or product base.



	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
Rating	**# of Stocks Covered**	**% of Stocks Covered**	**Banking**	**No Banking**
Buy	36	30%	17%	83%
Hold/Neutral	76	62%	7%	93%
Sell	10	8%	0%	100%

As of 6 February 2017

Other Disclosures

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