HILLIARD LYONS

Healthcare Real Estate Investment Trusts
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COMPANY UPDATE

Key Metrics

OHI - NYSE - as of 5/3/17		$32.45
1 Year Price Target		$ 38.00
52-Week Range	$28.11 -	$38.09
Shares Outstanding (mm)		198.8
Market Cap. ($mm)		$6,451.1
1-Mo. Average Daily Volume		1,062,000
Institutional Ownership		85.0%
Debt/Total Capital	Mar-17	38.8%
Est 3-year FFO Growth Rate		6.0%
Est 3-year Dividend Growth Rate		6.0%
Book Value		$ 21.40
Dividend		$ 2.52
Dividend Yield		7.77%
Est. Fixed Charge Coverage		3.7 X

FFO Per share

	2016	Prior 2017E	Current 2017E		Prior 2018E	Current 2018E
1Q	$0.83	--	$0.86	A	--	$0.89
2Q	$0.87	--	$0.87		--	$0.91
3Q	$0.83	--	$0.87		--	$0.91
4Q	$0.88	--	$0.91		--	$0.94
Year	$3.41		$3.52	*		$3.65
P/E	9.5x		9.2x			8.9x

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

Revenue ($mm)

	2016	Prior 2017E	Current 2017E		Prior 2018E	Current 2018E
1Q	$212.9	--	$231.7	A	--	$253.3
2Q	$228.8	--	$239.9		--	$259.4
3Q	$224.6	--	$242.5		--	$260.7
4Q	$234.5	--	$252.4		--	$269.2
Year	$902.8		$970.7			$1,042.6

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.*

Omega Healthcare Investors, Inc.

OHI -- NYSE – Buy-2

Q1 Earnings Update

Investment Highlights

- OHI reported Q1 normalized FFO of $0.86 a share, compared to $0.83 a share normalized in the year earlier period, equal to our number and the consensus. The company retained its recently issued guidance.
- Despite continued strong operating performance, OHI shares persist in their discount valuation in comparison to the peer group. Fundamentals remain solid, and cash flow performance has generally bettered the group. Further, in our view, it is obvious that the company's cash flow is deliverable to shareholders with nineteen consecutive dividend increases, with the most recent one bringing the dividend to $2.52 a share annually. At this point, our rating remains Buy reflecting these positive fundamentals. The shares continue to trade under our $38 a share 1 year price target, which is based on a multiple of 10.5 times our current year FFO, a solid discount to the peer group and even historic trading multiples. We will wait until after the company's 10AM conference call and a discussion with management before making any changes to our forward estimates, price target or rating.
- OHI has now increased its dividend nineteen consecutive quarters and 26 times in the last seven and a half years. The company's 7.8% yield is still a solid premium to the peer group, an attraction for income-oriented investors and we remain of the opinion that investors willing to take on some risk and searching for dividend income and long-term price appreciation could consider OHI shares to meet these goals in a group with strong demographic trends. With forward Fed rate increases likely to be measured, income-oriented securities, should be pressured, but OHI should escape most of the pressure as its yield remains solidly above potential rates and the increasing dividend should mitigate the risk even further.

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

First Quarter Review

Total revenue was $231.7 million versus $212.9 million, an 8.9% increase. Rental income of $192.5 million was up 9.0% (please see income statement on page 3). Mortgage interest income was down 3.9% at $16.0 million, while the company added $15.6 million from direct financing leases, up 1.3% from the year earlier period.

General and administrative expense rose 14.4% to $8.8 million from $7.7 million, a little above our expectations. Total interest-related expense rose 19.8% to $47.5 million, due to a higher level of debt and management refinancing into longer term, higher cost debt. Depreciation expense rose 12.1% to $70.0 million. The company recognized a number of charges this year, including a $7.6 million impairment on real estate assets held for sale, a $2.4 million provision for uncollectables and a $7.4 million gain on a sale of an asset. The company also recognized $3.8 million in acquisition costs last year and none in this year's first quarter. First quarter net income available to common shareholders was $104.4 million versus $55.6 million. The per share net income this quarter was $0.51 versus $0.28 a share on 3.9% more common shares outstanding in this year's Q1.

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 $176.7 million compared to $165.4 million in last year's first quarter, a 6.8% increase. Normalized FFO per diluted share were $0.86 versus $0.83 in the year earlier period.

OHI reduced its debt since the end of the year, having approximately $4,300.9 million in total debt (please see balance sheet on page 4) at quarter end, down from $4,366.9 million at the end of 2016. The company's debt to capital ratio was 38.8% at quarter end, down from the end of 2016 due to lower debt. OHI has no debt coming due until its line of credit ($500 million in total) matures in 2019 including the one year company extension option. We expect no liquidity issues for OHI, as it has been very pro-active in taking care of its maturities.

Other 1st Quarter Activity

Investment/Capital Markets Activity – During the first quarter OHI undertook limited investment activity, amounting to only $7.6 million, plus an additional $30.0 million in capital renovation projects, as it concentrated on its balance sheet. The acquisition was an assisted living facility in Virginia with a 7.5% yield with annual escalators. Also during the quarter the company sold 15 properties for $45.8 million in net cash resulting in a $7.4 million gain. At quarter end the company had nine facilities worth $23.2 million held for sale. During the quarter the company redeemed $400 million in 5 7/8% senior notes due in 2024 at a slight premium, and issued $550 million in 4 ¾% senior notes due in 2028 and $150 million in 4 ½% notes due in 2025. The company is also using the proceeds to repay a $200 million term loan facility and the remainder to pay down the credit line and for future investment. As these bonds were issued at the end of the quarter, they did not have an impact on Q1 results.

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 and just did another penny a quarter with its payment now at $2.52 a share annually.

Quarterly Income Statement

(in thousands)	1Q 2017	1Q 2016	% Change
Rental Income	$192,537	$176,703	9.0%
Other Investment Income	$6,914	$4,128	67.5%
Miscellaneous	$691	$0	
Income from Direct Financing Leases	$15,646	$15,442	1.3%
Mortgage Interest Income	15,956	16,606	-3.9%
Total Revenue	231,744	212,879	8.9%
General & Admin	8,780	7,677	14.4%
Legal expense	0	0	0.0%
Restricted Stock Expense	3,744	2,778	34.8%
Acquisition Costs	-41	3,771	-101.1%
Provision for Uncollectables	2,404	5,124	
Impairments	7,638	34,558	
Nursing Home Expense for Owned and Operated	0	0	
EBITDA	209,219	158,971	31.6%
Interest Expense	47,539	39,666	19.8%
Depreciation Expense	69,993	62,433	12.1%
Income (Loss) Before Discontinued Operations and Other Items	91,687	56,872	61.2%
Discontinued Operations (including gain on sale of assets)	7,420	1,571	
Charges	0	0	
Investment interest and other	9,373	(247)	
Non-controlling	(4,040)	(2,641)	
Net Income (Loss)	$104,440	$55,555	88.0%
Net EPS (diluted)	$0.51	$0.28	80.9%
Avg. Shares Outstanding (diluted)	206,174	198,350	3.9%

Funds From Operations	1Q 2017	1Q 2016	
Net Income	$109,112	$58,196	87.5%
Depreciation Expense	71,651	62,433	14.8%
Other (adding/substracting one-time items)	(4,087)	44,723	
Normalized Funds From Operations	**$176,676**	**$165,352**	6.8%
Normalized FFO Per Share (diluted)	**$0.86**	**$0.83**	3.6%

Source: Company reports.

Consolidated Balance Sheet

(in thousands)	March 31, 2017	December 31, 2016
Real Estate Assets		
Land and Buildings	$7,581,665	$7,566,358
Less: accumulated depreciation	$ (1,306,084)	$ (1,240,336)
Total Net Real Estate Investments	6,275,581	6,326,022
Cash and Cash Equivalents	40,349	93,687
Net Investment in Direct Financing Leases	604,777	601,938
Mortgage notes receivable	644,696	639,343
Accounts Receivable	272,506	240,035
Other Investments	255,899	256,846
Goodwill	643,692	643,474
Restricted Cash	12,198	13,589
Real estate held for sale	23,245	52,868
Other assets	69,175	81,458
Total Assets	**$8,842,118**	**$8,949,260**
Bank Borrowings	$123,000	$190,000
Mortgage Loan payable	54,052	54,365
Unsecured Borrowings	4,123,813	4,122,489
Real Estate Purchase Liability	0	0
Bond payable	0	0
Accounts payable and accrued expenses	316,985	360,514
Dividends payable	0	0
Other	9,746	9,906
Total Liabilities	**$4,627,596**	**$4,737,274**
Preferred stock	-	-
Common Stock	19,676	19,614
Capital in Excess of Par Value	4,878,637	4,861,408
Cumulative Net Income	1,843,377	1,738,937
Cumulative Dividends	(2,829,718)	(2,707,387)
Other	302,550	299,414
Total Shareholders' Equity	**4,214,522**	**4,211,986**
Total Liabilities and Shareholders' Equity	**$8,842,118**	**$8,949,260**

Balance Sheet Ratio Analysis	March 31, 2017	December 31, 2016
Net R/E Investments / Total Debt	68.5%	69.0%
Debt to Equity	102.0%	103.7%
Debt as % of Total Assets	48.6%	48.8%
Shareholders' Equity as % of Total Assets	47.7%	47.1%

Source: Company reports.

First Take

First quarter results were in line with our and the consensus expectation. Acquisition activity was sparse during the quarter, with management concentrating more on the balance sheet this quarter. As such, total investment was only $38 million, below our expectations. Management also is targeting some non-core assets, likely some of those picked up in the Aviv transaction, and we expect to see more divestitures in the second quarter. However, beyond that we anticipate a pick-up in investment as the year progresses, although we also expect management to stay disciplined, which could hold back investment should rates move up. Management retained its FFO guidance at $3.40 to $3.44 a share. Our estimate remains above this guidance range—although we note that our estimate includes some investment activity beyond that already contracted for.

With the lack of investment activity completed through the first part of the year in comparison to our expectations, we may need to pare our estimates back a bit, although we will wait until after the conference call before making any call on that front. Management seems to be rationalizing its portfolio, and could be taking their eyes off of new investments, and rather paying more attention to monetizing underperforming assets. Certainly, given the high prices paid for properties, it is a good time to be a seller, and we would not be surprised if management pulls back a bit on investment activity to concentrate more on taking some profits. Higher interest rates in the future could make this a profitable strategy in the near term. However, management has tended to be conservative in its guidance, so we would expect them to hit their numbers even if investment activity does not meet our expectations. However, this strategy could lead us to drop our estimates back towards guidance.

The Q1 revenue line was a little under our expectations while costs were well controlled, and management continues to lower interest expense. OHI continues to hit on all cylinders, and we remain partial to the company and anticipate continued consistent dividend increases going forward. There appears to be no issues with the company's capital structure at this point, as the company has stretched out its maturities to a point where it has no appreciable debt due over the next couple of years and has a very high level of debt capacity to pay for further investments.

We anticipate that the company will be able to continue to increase the dividend at a rate that is above that of its peers going forward with the increase in cash flow we are seeing. Overall we anticipate that OHI should continue to provide solid total return for investors. We believe it is likely that our estimates for fair value for the shares should move higher on an ongoing basis with our expectations for consistent increases in earnings from recent and future investment and acquisition activity. We will be basing our thesis and any target price/rating change on what comes out of the 10AM conference call, but we continue to believe that the company's shares are attractive given the peer group valuations and interest rate environment. Overall, a solid quarter that supports our thesis on the company.

Suitability

OHI has a suitability rating of 2 on our 1-4 scale. We find the company to have a very strong balance sheet in relation to its peers, and the triple net structure of most of its leases limit its property risk. Its real estate ownership is also a positive factor, as is the company's geographic and operator diversification, with the largest portfolio of skilled nursing properties in the industry. On the other hand, the company is excessively exposed to the skilled nursing sector, with the bulk of its operator revenue paid by Medicare and Medicaid add risk due to potential political issues.

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 or not realize synergies from prior acquisitions. 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. Also, the change with patients no longer forced to take arbitration, but now able to litigate against operators includes risk for OHI's tenants.

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 family has a long common equity position in Omega Healthcare but may not trade the shares contrary to Hilliard Lyons' rating.

Investment Ratings

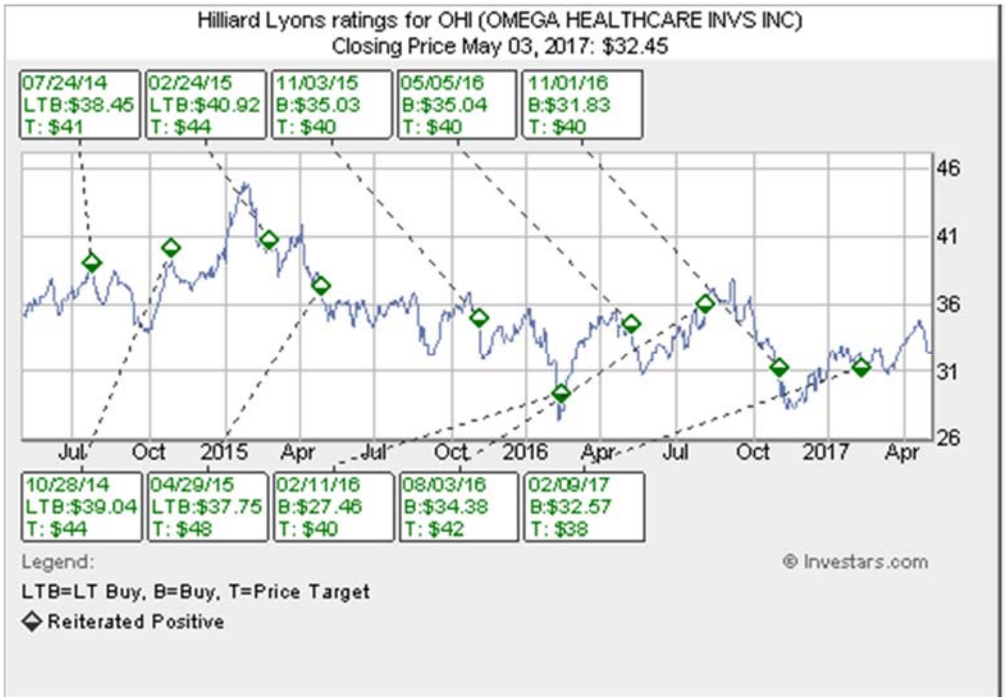
Buy - We believe the stock has significant total return potential in the coming 12 months.
Long-term Buy - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, generally 2-3 years.
Neutral - We believe 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%	14%	86%
Hold/Neutral	71	58%	6%	94%
Sell	15	12%	7%	93%

As of 5 April 2017



Other Disclosures

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