

TENANT CREDIT 101



BIG PICTURE

- What is Tenant Credit?
- Why Should We Care About It?
- In Today's Heated Capital Markets Does Tenant Credit Really Matter?
- STAG Perspective



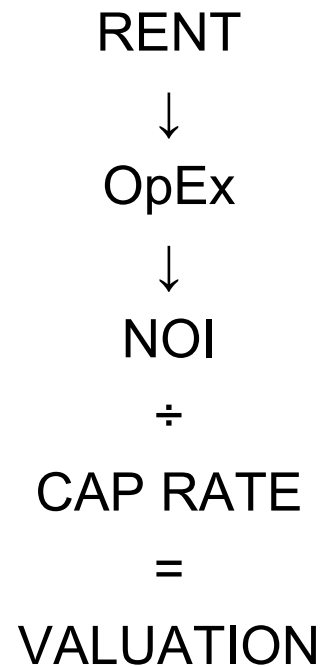
What is Tenant Credit?

The ability of a company to meet its financial obligations. These financial obligations can include many things such as.....

- ✓ Secured Debt
- ✓ Unsecured Debt
- ✓ Real Estate Leases



Why Tenant Credit Matters



RENT: Impacted by tenant credit, which ultimately flows through to valuation



In Today's Heated Capital Markets Does It Still Matter?

- Yes and No.
- Still relevant but marketplace seems to “discount” it more today than in the past.
- Why?
 - ✓ Excess liquidity
 - ✓ Relaxed underwriting standards
 - ✓ Lower yield requirements
 - ✓ Most likely: recent low default rates



STAG PERSPECTIVE?

Prudent, diligent credit analysis will provide better risk adjusted returns over the long-haul



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THE TOOLS

PUBLIC COMPANIES: Available information; transparency.
Levels the playing field.

Many Tools Available:

1. Rating agencies
2. Publicly traded equity – financial statements
3. Government websites (SEC)
4. Bloomberg
5. Credit websites (credit risk monitor, Credit Watch)
6. The internet



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THE TOOLS

PRIVATE COMPANIES: Harder to gather information, lack of obligation to provide information.

Tools Available:

1. Company website
2. Hoovers and other private company information services
3. Company management
4. Good, old fashioned credit due diligence



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THE STEPS

1. Industry Analysis

- Mature: Beverages
- Growth: Medical
- Decline: Textiles
- Volatile: Auto for example

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THE STEPS

2. Competitive Set

- Competitive Landscape - highly fragmented or monopolistic?
- Barriers to Entry
- Pricing power

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THE STEPS

3. Product

- Niche
- Pedestrian
- Outsourced
- Overseas

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THE STEPS

4. Management Team

- Experience
- Depth
- How do they interact w/ the financial community
- You need to be comfortable with the people running the show and their ability to be successful



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THE STEPS

5. Capital Structure

- Leverage (types)
- Equity Backing (family, VC, etc)
- Liquidity
- Types and Age of Assets

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THE STEPS

6. Ratio Analysis

- YOY (provides perspective and helps indicate trends, direction of business)
- Relative to Industry Benchmarks
- Profitability
- Leverage

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THE EXAMPLES

Plastics Tenant

- ✓ Private Credit
- ✓ Injection Molding Plastic Components
- ✓ One Significant Customer
- ✓ STAG “C” Credit Rating
- ✓ Real Estate: Fully leased warehouse/office building in Minnesota. 17 Years of remaining lease term.

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THE EXAMPLES

Pepsi Co.

- ✓ World leader in snack and beverage industry
- ✓ Global brand awareness
- ✓ Over \$30 billion annual sales
- ✓ Strong Management
- ✓ Public Rating: “A+”
- ✓ Real Estate: Fully leased manufacturing/warehouse building in Kansas. 4.5 years of remaining lease term.

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THE FINANCIALS

Financials are for year end 12/31/05	Pepsi Co.	Plastics Company
in (\$000s)		
Net Sales	\$32,562,000	\$24,541
EBITDA	7,762,000	1,702
Net Income	4,078,000	(113)
Long Term Debt	2,313,000	3,702
Net Worth	14,251,000	2,829
Pre-Tax ROE	28.6%	-3.9%
EBIT to Interest	23.1x	1.2x
Operating Cash Flow to Total Debt	112.0%	-13.1%
Debt to Capital	16.4%	38.2%
Altman Z-Score	3.1	2.1

Altman Z-Score

- Another tool available to credit analysts
- Uses statistical techniques to predict a company's probability of failure
- Uses 5 ratios at various weightings
- EBIT/TA : 3.3 weight
- Net Sales/TA: 0.99 weight
- MV of Equity/TL: 0.6 weight
- Working Capital/TA: 1.2 weight
- Retained Earnings/TA: 1.4 weight
- >3.0 = safe
- $2.7-2.99$ = alert
- $1.8-2.7$ =high probability of default w/in 2 yrs
- <1.80 = imminent default

Standard & Poor's

- Current rating activity for securities issues valued at over US\$30 trillion
- About 1,000 ratings analysts
- Ratings Analysis Methodology
 - Business Risk Profile
 - Financial Risk Profile
- Corporate Credit Rating (CCR)
 - 'AAA' (strongest) to 'D' (weakest)

S&P Matrix

Business/ Financial	Minimal (AAA/AA)	Modest (A)	Typical (BBB)	Aggressive (BB)	Highly Leveraged (B)
Excellent (AAA/AA)	AAA	AA	A	BBB	BB
Predictable (A)	AA	A	A-	BBB-	BB-
Solid (BBB)	A	BBB+	BBB	BB+	B+
Fair (BB)	BBB	BBB-	BB+	BB-	B
Vulnerable (B)	BB	B+	B+	B	B-