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THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Four Corners Property Trust LLC (NYSE:FCPT)

BILL LENEHAN was named Chief Executive Officer of Four Corners Property Trust LLC in connection with Darden Restaurant's real estate spinoff transaction. Prior to assuming the CEO role, he was an active member of Darden Restaurants' board of directors, Chair of its real estate and finance committee and member of its corporate governance committee. He has a strong track record of success in real estate and has been active in assembling portfolios of triple-net retail properties. Mr. Lenehan recently served as Interim CEO of MI Developments, Inc., now named Granite REIT, an owner of net-leased industrial and manufacturing real estate, where he was a member of their strategic review committee and was a Director; and spent approximately 10 years as an investment professional in the real estate group of Farallon Capital Management, LLC. Mr. Lenehan also previously served on the board of directors for Gramercy Property Trust Inc., a publicly traded net-lease REIT, where he was Chairman of the investment committee, and currently serves on the board of directors of Macy's, Inc. He is a graduate of Claremont McKenna College.

SECTOR — FINANCIAL SERVICES

TWST: Let's start by talking about the origins of Four Corners Property Trust: a spinoff by Darden of its real estate. When, why and how did that come about?

Mr. Lenehan: Darden was itself a subsidiary originally. Many of these assets came from a subsidiary of General Mills back in the day. General Mills was a very well-capitalized company, and there are two big implications to that. One, General Mills got the best land sites. If you were opening a mall, the General Mills concepts were very attractive because they had high volumes, they drew a lot of traffic, you knew that they had the money to actually build the store, and so they got great sites that performed really well. The other implication was that General Mills had a lot of asset value. They didn't necessarily want to be an asset-light company, and culturally they wanted to hold on to their real estate.

So fast-forward many years, Darden had very high average unit volumes, very appealing concepts and went through the Great Recession with strong performance, and ultimately their expense structure became a little bit out of whack. But they had the advantage that they weren't paying rent on hundreds of their properties, and so what should have been industry leading margins turned into margins that were the same as many of their competitors, and so didn't look horrible, but they certainly didn't want to aggravate the problem by doing sale/leasebacks on their properties and incurring more rental expense.

An activist fund named Starboard went through a process of assembling a new board of directors; they asked me to join along with some other really fantastic people, and we replaced the incumbent board of Darden a few years ago. I was sort of the real estate person. They asked me to take a look at the real estate and see what could be done to create shareholder value.

At the same time, and this is extremely important, the individual who was the Interim CEO, Gene Lee, was working on a lot of this stuff before the new board came, but he continued to drive incredible cost reduction, revenue performance, growth, brand solidification, etc. at Darden. So he had already started, but hopefully he thinks that we helped as a board continue the process, of making the business of Olive Garden, LongHorn and the specialty brands run a lot better. If you look at Darden's stock price, it has done fantastically well, even excluding the idea that their shareholders received a couple-billion-dollar company called Four Corners as part of the process. But Gene really architected, with a lot of leadership at the brand level, a tremendous improvement in Darden's business.

As that was happening, that gave us the luxury to burden Darden with some rent, because Gene was finding cost saves in other places of the business, frankly larger than the rent we ended up putting on the operating company. And so we looked at the real estate of Darden. We had great advisers in J.P. Morgan and Moelis. We spent a year working really, really hard to understand what should be done with the real estate, and ultimately we did not one transaction — oftentimes we're asked the question, what's the one transaction you can do to maximize shareholder value, but that's a false choice because you're not limited to one transaction.

We looked at many different structures, transactions, etc., and we came up with the following. We did a sale/leaseback on the corporate headquarter building to an institutional buyer. We didn't want the public REIT, Four Corners, to have 418 individual properties that were worth a few to several million dollars apiece and then one huge specialty-purpose suburban office building. That would have been highly awkward for the public company. We also sold 64 individual properties one by one, raising roughly $250 million, and then we spun 418 properties in a tax-free spinoff transaction creating this new public company.

Because we had raised this cash, Darden was cash-flow generative, it had cash on its balance sheet, we raised this cash through the spin but also through selling individual assets and the corporate headquarter building. The one really interesting thing about the Darden spinoff transaction was that it was deleveraging, and that Four Corners started life with very low leverage itself. Darden's debt level went from about $1.5 billion down to about $500 million, and we spun with the lowest leverage in the industry, which gave us a great trajectory to grow the portfolio without having to access the capital markets.

Perhaps it's obvious, but the amount of effort that the Darden team and the board and advisers put into this process to do it thoughtfully was really remarkable. I think it's a testament to Gene Lee and Starboard that we came in as an activist board, and very quickly put that behind us. The members of the management team in Darden — Bill White, Treasurer; Rick Cardenas, now CFO; and Joe Kern and Laurie Burns from Darden's real estate group — the amount of effort that was put in on top of their day jobs of a Fortune 500 company to effectuate this transaction was just enormous, and we're forever thankful for that.

screened well over 2,000 restaurant properties to date, and we have a good sense of what are the attributes of these restaurant properties. The strategic issue might not get a full score.

For example, an Outback in Atlanta provides some diversification for us, but we already own a number of LongHorn Steakhouses in Atlanta, so it's not as diversifying as, say, a Burger King in Salt Lake, where we don't have a lot of exposure. So we first ask, is it strategic in our diversification efforts? Next, we look at credit issues, like how big is the brand? Is this a brand that if it were to have issues it would restructure, or is this a brand that would simply go away? Then we look at the financial strength of the guarantor. Is this a big public company? Is it a small franchisee?

We then look at what's the absolute amount of rent, because the first question if you ever got a property back is, how much rent is at risk? We want to make sure that we're not getting into properties that are over rented; there are quite a few in the restaurant business where they've assigned very high rents to these properties because $1 of real estate income trades at a higher multiple than $1 of franchisee profits. Then we look at real estate considerations: location, reuse potential, the length of the lease, rent to sales, is it truly triple net? We look at what is the rent growth inherent in the lease. And then we score all these criteria — and again, we've scored a couple thousand properties so far — and we try to take a balanced look at what's the credit and what's the real estate.

"We look at the businesses being half credit and half real estate. You need both. You need viable real estate that's well-located for a restaurant property, for the brand that that restaurant property is today."

TWST: Please tell us about the company's property portfolio as it stands today.

Mr. Lenehan: We spun with 418 properties. We've sold a couple, and we've bought a number. So today we are at just shy of 500 properties. It is 300 Olive Gardens, roughly 100 LongHorn Steakhouses, and then primarily quick-service restaurants that we've acquired since spin, so these are Taco Bells, KFCs, Burger Kings, etc. Our focus is entirely on net-lease restaurant real estate that is well-located, the restaurants perform well, we have net leases in place with long lease duration, and then the leases are guaranteed by either Darden in our existing portfolio, or in what we've acquired since the spin they're guaranteed by either substantive restaurant franchisee businesses or high net worth individuals, primarily substantive restaurant franchisee businesses.

We look at the businesses being half credit and half real estate. You need both. You need viable real estate that's well-located for a restaurant property, for the brand that that restaurant property is today. Is this a good location for a Burger King? Is this a good location for a KFC? But also you need the second layer of protection, which is, do you have a viable guarantor on the lease?

TWST: I was going to ask about your investment criteria. Is there anything you'd add, in terms of market locations and property characteristics, and then also both the brand and the operator?

Mr. Lenehan: We use what we call our scorecard, and that scorecard first asks the question, is this strategic? Is the restaurant property strategic in our goal to diversify what we already own? We've

We add those two ideas together and we come up with a score, and it becomes a really helpful way internally to communicate about properties. We don't get into fights where one member of our acquisition team is screaming, "It's on an outparcel of a Wal-Mart on a signalized corner, we should buy it," and another person saying, "The lease term's only seven years, we shouldn't buy it." All those concepts are encapsulated into our scorecard approach.

Then we take that score and we look at it versus what price we think we could get for the asset, and obviously there's a correlation that better scoring assets we're willing to pay more for. And then we look at that versus our cost to capital. Is it accretive to buy assets? When we spun, we had a low stock price, and there were very few assets that we could look at and buy that were accretive, so we didn't. Now we have an attractive cost of capital, and so there are more assets that both are acceptable to us as far as risk and quality, but also where we can acquire them and have it be accretive to our investors. We call that concept the "strike zone," and we have an infographic in our investment presentation that walks people through it. I think net lease is a cost-of-capital sensitive business. We take that very seriously.

TWST: What is your strategy, your goals and plans, both in terms of absolute growth of the portfolio but also diversification along the lines of tenants and brands? Obviously you started very concentrated in Darden.

Mr. Lenehan: We started off concentrated, but with a portfolio that was extraordinarily strong. Our average lease coverage was far and away industry leading, and if you were to backtest our coverage to the recession, our worst assets in the recession in 2009 were about the same coverage as our peers' average assets are today. So very strong performance and a high-quality initial portfolio, also, by the way, backed by Darden, an investment-grade company that's doing very well. So we started with an extraordinarily strong base, but as you mentioned it was not diversified by guarantor. Diversified by geography, we were in 44 states; diversified by properties, we had 418 properties at spin, and none made up a meaningful portion of the portfolio etc. — but one guarantor.

So we entered into this strategy to buy other assets to diversify. But it's really important — and this gets back to my cost-of-capital commentary — we don't provide acquisition guidance and/or earnings guidance, which for a company as simple as ours is basically the same thing, because it would pressure us to acquire assets, perhaps when we didn't have an attractive cost of capital. One of the things that I think our investors have given us credit for is that we are not financially incented, the management team or the acquisition team, to simply buy regardless of our cost of capital. We do not issue copious amounts of stock and dilute our shareholders in order to accomplish some predetermined acquisition goal. We buy when it's accretive to our shareholders, it's accretive to our strategy to diversify, and when it's not, we don't buy.

TWST: I know it's too early for second quarter numbers, but what would you say were the highlights of the first quarter?

Mr. Lenehan: On a quarterly basis, our business is not terribly dramatic. We have a policy of announcing every acquisition essentially the day it closes, or near to that. We do that probably because of my background working in an investment firm. I've always felt the less volatility a company has in its quarterly outcome versus expectation, the better. So it's pretty easy to model our quarterly numbers with a very high degree of specificity. We announce literally the day our rent ceases when we sell a property, or the day we pick up a new stream of rent when we buy, and it's in the press release with details on the property. So quarterly conference calls are not terribly dramatic, and I think again that's one of the reasons our stock trades at a nice multiple, because we don't surprise our investors.

TWST: If a prospective investor were to ask you what are the strengths and weaknesses, or pros and cons, of focusing just on restaurant properties, how would you respond?

Mr. Lenehan: I would say one pro is, because we focus on this exclusively, we've gathered quite a bit of domain expertise in this space. From the perspective of sellers of assets, they know that this is what we focus on, and we provide less surprises and more certainty of close because this is what we focus on. It makes it simple. Our investors know what we're going to buy.

Thus far, in 2017 especially, there's been significant impact of what I'll call "the Amazon effect" on other retailers. I'm on the board of Macy's, the department store company, so this is something I think about. If you look at the research — Goldman puts out some good research on this subject — food service has historically been the least impacted by online pressures. I think our investors look at our focus as we're predictable, they know what kind of things we're going to buy, and the view is that restaurants are less vulnerable to online pressures.

TWST: What will you and the rest of the management team be most focused on for the next year or two?

Mr. Lenehan: Since spin, we've established the way we finance our business. We received an investment-grade debt rating. We did our inaugural bond deal. We have issued equity under an ATM program, which is very efficient. So I think our investors can see how we intend to capitalize the growth of the business. I think they can see, because we provide really granular disclosure on what we've purchased, what our strategy is and how consistent it is in the way that we conduct ourselves. So I do not think there's a broad-brush change in strategy on the horizon. I think it's a continuation of what we've evidenced to be an effective way to grow the business and diversify, to grow AFFO per share, to grow per share asset value, etc.

I would also say I think the other components of being a public company — executive compensation, corporate governance, risk management — we've done a very thoughtful job in establishing best-in-class practices on those three categories. Again, I was an investor for 10 years at a hedge fund, and have some pretty strong views on how companies and management teams should conduct themselves as far as aligned compensation, as far as not just saying you have good corporate governance but having corporate governance that would actually stand up to third-party scrutiny, and having risk management that's well-documented and thought through. I think we've done a good job on those, and kept our overhead at a modest level even as we've grown.

TWST: Is there anything else you'd like to add?

Mr. Lenehan: I certainly would encourage prospective shareholders to reach out to us. We have done an enormous amount of investor outreach. We want investors and research analysts to understand our business. We'd love to spend time with investors to make sure they understand and are comfortable with our business model.

TWST: Thank you. (MN)

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