



STORE Capital

First Quarter 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Christopher Volk – *President and Chief Executive Officer*

Mary Fedewa – *Chief Operating Officer*

Catherine Long – *Chief Financial Officer*

Moira Conlon – *Investor Relations*

PRESENTATION

Operator

Hello and welcome to STORE Capital's First Quarter 2018 Earnings Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star (*) key followed by zero (0). After today's presentation there will be an opportunity to ask questions. To ask a question you may press star (*) then one (1) on your telephone keypad. To withdraw your question please press star (*) then two (2). Please note this event is being recorded. I would now like to turn the conference over to Moira Conlon, Investor Relations. Please go ahead, ma'am.

Moira Conlon

Thank you, Pete, and thank you all for joining us today to discuss STORE Capital's first quarter 2018 financial results. This morning we issued our earnings release and quarterly investor presentation, which includes supplemental information for today's call. These documents are available in the Investor Relations section of our website at ir.storecapital.com under News & Results, Quarterly Results. I am here today with Chris Volk, President and Chief Executive Officer of STORE; Mary Fedewa, Chief Operating Officer; and Cathy Long, Chief Financial Officer. On today's call, management will provide prepared remarks and we will then open the call up for your questions. In order to maximize participation while keeping our call to one hour, we will be observing a two-question limit during the Q&A portion of the call. Participants can then reenter the queue if they have follow-up questions.

Before we begin, I would like to remind you that comments on today's call will include forward-looking statements under the federal securities laws. Forward-looking statements are identified by words such as will be, intend, believe, expect, anticipate, or other comparable words and phrases. Statements that are not historical facts such as statements about our expected acquisitions or our AFFO and AFFO per share guidance for 2018 and 2019 are also forward-looking statements. Our actual financial conditions and results of operations may vary materially from those contemplated by such forward-looking statements. Discussion of the factors that could cause our results to differ materially from these forward-looking statements are contained in our SEC filings, including our reports on Form 10-K and 10-Q.

With that, I would now like to turn the call over to Chris Volk. Chris, please go ahead.

Christopher Volk

Thank you, Moira, and good morning everyone and welcome to STORE Capital's first quarter 2018 earnings call. With me today are Mary Fedewa, our Chief Operating Officer and Cathy Long, our Chief Financial Officer. We continue to be active on the acquisition front. Our investment activity for the quarter totaled just over \$320 million, and we profitably divested approximately \$45.5 million in real estate investments. Our investments and property sales reflect our ability to consistently invest in and divest of assets in ways that are accretive to our shareholders. At the same time, our portfolio remained healthy, with an occupancy rate of 99.6% and about 71% of the net lease contracts rated investment-grade in quality based on our STORE Score methodology. You'll hear more about our property investment and sales activity and portfolio health from Mary.

Our dividend payout ratio for the quarter approximated 70% of our adjusted funds from operations, serving to provide our shareholders with a well-protected dividend and a company that's well-positioned for long-term internal growth based on anticipated tenant rent increases and the reinvestment of our surplus cash flows.

During the first quarter, we closed on our inaugural issuance of public unsecured term debt, a \$350 million offering of investment grade-rated 4.50% ten-year senior notes. The notes were rated Baa2 by Moody's and BBB by Fitch and S&P, respectively. It has always been part of our financing strategy to enter the public debt markets. Our ability to publicly issue corporate investment-grade term debt expands our borrowing capacity and flexibility. Incorporating this newly issued debt with gradual new equity issued through our ATM program, and our funded debt/EBITDA on a run rate basis continued to approximate 5.7 times for the quarter. Moreover, substantially all of our investments during the quarter added to our pool of unencumbered assets, which stood at \$3.5 billion, or about 55% of our gross investments, providing us with flexibility in our financing options.

Now, as I do each quarter, here are some statistics relevant to our first quarter investment activity:

- The weighted average primary lease term for our new investments continues to be long, at approximately 17 years.
- The median new tenant Moody's RiskCalc credit rating profile was Ba2.
- The medium post overhead unit level fixed charge coverage ratio for assets purchased during the quarter was 2.4:1.
- The median new investment grade contract rating (or STORE Score) for investments was favorable at Baa2.
- Our average new investment was made at approximately 80% of replacement cost.
- 98.5% of the multi-unit net lease investments made during the quarter were subject to master leases.
- And, all of the 103 new assets we acquired during the quarter are required to deliver unit-level financial statements, giving us required unit-level financial reporting from 97% of the properties within our portfolio.
- Our investment activity continued to be highly granular, with 33 separate transactions completed and an average transaction size of under \$10 million.
- At the end of the quarter, the proportion of revenues realized from our top 10 customers was 18.8% of annualized rents and interest, up slightly from 18.5% at the end of 2017. Further, our top 10 customers continued to be highly diverse and the largest single customer represented just 3.5% of our annualized rents and interest, with a long term target of having no tenant exceed 3% of our annual revenues.
- During the quarter we sold 22 properties, which represented an original acquisition cost of approximately \$45.5 million, and we netted a gain over our original cost of \$4.3 million. Mary will dive deeper into this number for you, but our ability to generate profits from asset sales owes itself to our direct origination strategy. And, as I have long stated, portfolio management activities like this, which produce real economic gains, serve to offset sporadic vacancies or asset underperformance, which is a customary part of the net lease business.
- Last of all, and normally this would be the first thing I would address, I will talk about our lease economics: our weighted average lease rate was approximately 7.84%, which is near where we were last quarter.
- The average annual contractual lease escalation for investments made during the quarter approximated 1.7%, providing us with a gross rate of return (which you get by adding the lease escalations to the initial lease rate) of almost 9.6%.
- As to what these impressive economics mean for our stockholders, our 7.84% lease rate this quarter was roughly 335 basis points above the 4.5% interest rate on our inaugural 10-year public debt offering, which is a great starting spread. At leverage averaging about 42% of cost, that makes the levered current cash yield about 10.2%. Add in the

leveraged impact of the annual 1.7% rent increases (which you get by taking our 1.7% annual increases divided by our approximate 58% of equity at cost) and you arrive at a gross leveraged return before costs of over 13%. Net investor rates of return will also be impacted by operating costs, property performance, and the accretion from asset sales gains and external growth. However, the majority of our outperforming investor returns that we have delivered from STORE and our two predecessor companies have always been driven by having favorable leveraged gross total property-level rates of return from the outset, which is why we take the time to disclose major return components.

And with that, I will turn the call over to Mary.

Mary Fedewa

Thank you, Chris. Good morning everyone. 2018 is off to a good start with acquisitions of about \$320 million at a cap rate of over 7.8% for the first quarter. We invested in 33 separate transactions and added seven new customers with a granular transaction size of under \$10 million.

We continued to actively manage our portfolio and take advantage of opportunities to sell properties. During the quarter we sold 22 properties which had an acquisition cost of \$45.5 million, generating net gains over the original cost of approximately \$4.3 million. Twelve, or about 55% of the properties sold were opportunistic sales and delivered the bulk of the gains, which averaged 17% profit over cost. Three properties were sold for strategic reasons to reposition the portfolio at a 4.2% gain over cost. These gains were slightly offset by the losses on seven remaining properties that were sold as part of our ongoing property management activities. We recovered an impressive 94% of our original cost from these sales.

Now turning to our portfolio performance highlights. As of March 31, 2018:

- The service sector accounted for about 67% of our portfolio;
- 18% was in experiential retail;
- And about 15% was in manufacturing.
- Customer ranking within our top ten remains extremely diverse by design, with our largest tenant, Art Van Furniture, representing 3.5% of rent and interest. Customers new to our top 10 are Zips Holdings, Camping World, and National Veterinary Associates. Zips and National Veterinary Associates moved into the top ten as a result of incremental business with these longstanding customers. Camping World is back in our top ten as a result of the new leases we signed for eight Gander Mountain properties, now Gander Outdoors. These eight are among the 70 new store locations being opened by Camping World in 2018. Camping World is classified as a retailer, but also provides a heavy service component as the only national parts and service provider for recreational vehicles. National Veterinary Associates is one of the largest operators of veterinary hospitals in the U.S., with over 400 locations. Zips operates the second largest carwash business in the U.S.
- Delinquencies and vacancies remained very low due to our active portfolio management and strong tenant partnerships, with only seven out of our 2,000 properties currently vacant.
- Our portfolio health has remained stable and consistently strong.

Now, turning to the overall market, our pipeline, and our origination platform. Cap rates remain stable. This enables us to continue our pattern of strong spreads over our cost of long-term borrowings. Our pipeline remains robust and diverse, with 84% of our pipeline representing

customer-facing industries.

Regarding our origination platform, at our recent Investor Day, four of our Senior Managing Directors presented case studies showing how our solutions are creating alpha for our investors by helping our customers access efficient and low-cost growth capital with the highest level of operational flexibility. We continue to benefit from our strong customer relationships, with about 30% of our business coming from customers we have worked with for many years.

With that, I will turn the call to Cathy to talk about financial results.

Catherine Long

Thank you, Mary. I'll start by discussing our capital markets activity and balance sheet, followed by our financial performance for the first quarter. Then, I will review our guidance for 2018. Please note that all comparisons are year-over-year unless otherwise noted.

From a capital markets perspective, the first quarter of 2018 was a very active time for STORE. In February, we expanded our unsecured, revolving credit facility from \$500 million to \$600 million and the accordion feature from \$300 million to \$800 million. Taken together, this raises our maximum borrowing capacity under the facility to \$1.4 billion, lengthens the maturity to February 2022, and adds two six-month extension options.

In March, we closed on our first public debt offering with the issuance of \$350 million of investment-grade 10-year notes at a coupon of 4.5%. In anticipation of this debt issuance, we had entered into a treasury-rate lock agreement in January. We received \$4.3 million in settlement when the debt was issued in March, giving us an effective rate of 4.4%.

In February, we established a new \$500 million ATM program and terminated the program we launched in September 2016. During the first quarter, we sold an aggregate of 4.1 million shares under our ATM program at an average price of \$24.51 per share. We raised net proceeds of nearly \$100 million, which we put to work through our real estate investment activity. Our ATM program has been a very effective way to raise equity and makes a lot of sense for us given the flow of our business and the granular size of our transactions.

As a result of these capital markets activities, at March 31st our long-term debt stood at \$2.7 billion, with a weighted average interest rate of just under 4.4% and a weighted average maturity of 6.1 years. In an environment of raising interest rates, it's important to note that all of our long-term borrowings are fixed-rate and our debt maturities are intentionally well-laddered. Our median annual debt maturity is just under \$270 million, and we have no meaningful debt maturities until the year 2020.

Our leverage ratio at March 31st was 5.7 times net-debt-to-EBITA, on a run-rate basis. This equates to around 42% on a net-debt-to-cost basis. At the end of the quarter, we had borrowing capacity on our credit facility of over \$500 million in addition to the \$35 million of cash on our balance sheet. As I indicated earlier, the accordion feature of our expanded credit facility provides access to even more liquidity. In summary, we are well positioned with a substantial financing flexibility, conservative leverage, and access to a variety of attractive equity and debt options to fund a large pipeline of investment opportunities.

Now, turning to our financial performance. Acquisition activity during the first quarter was funded by strong cash flow from operations, cash proceeds of approximately \$50 million from asset dispositions, and the proceeds from our capital markets activities I noted earlier.

As of March 31st, our real estate portfolio stood at \$6.5 billion, representing 2,000 properties. This compares to \$5.5 billion representing 1,750 properties at March 31, 2017. The annualized base rent and interest generated by our portfolio in place at March 31st increased 16% to \$520 million, as compared to \$448 million a year ago.

Acquisition activity drives revenue growth and revenues increased 17% year-over-year to \$126 million. Our first quarter acquisition volume was weighted towards the end of the quarter; therefore, the full impact of that volume will not be realized until the second quarter of 2018. Our consistently strong revenue growth reflects the broad-based demand for our real estate capital solutions.

Total expenses increased 7% to \$85 million, compared to \$80 million a year ago; substantially, all of this increase can be attributed to higher depreciation and amortization reflecting the growth of the portfolio.

Interest expense was relatively flat compared to a year ago as higher average balances outstanding on our credit facility were offset by decreases in the weighted average interest rate on our long-term borrowings.

Property costs were \$1.3 million for the quarter as compared to \$800,000 a year ago. The increase was primarily related to property taxes, insurance, and other costs on properties that were vacant during the quarter.

G&A expenses were \$10.9 million, compared to \$10.2 million a year ago, primarily due to the growth of our portfolio and related staff additions. For the quarter, G&A expenses, as a percentage of average portfolio assets, decreased to 68 basis points from 78 basis points during the first quarter of 2017, reflecting the scale efficiencies that come with portfolio growth.

Net income increased to \$50 million for the quarter, or \$0.26 per basic and diluted share, compared to \$31 million, or \$0.19 per basic and diluted share a year ago. Net income for the first quarter of 2018 includes an aggregate net gain of \$9.6 million from property sales versus an aggregate net gain of \$3.7 million from property sales in the first quarter of 2017. Net income for 2018 also includes an impairment charge of \$1.6 million related to a loan that was written off during the quarter. In comparison, the first quarter of 2017 included an impairment charge of \$4.3 million related to a vacant property that was sold shortly after the end of that quarter.

AFFO for the quarter increased 23% to \$86 million, or \$0.44 per basic and diluted share, from \$70 million, or \$0.43 per basic and diluted share last year.

Our dividend is an important component of our overall stockholder return and, since our IPO in 2014, we have increased our dividend per share by 24% while maintaining a low dividend payout ratio and, at the same time, reducing our leverage. For the first quarter, we declared a quarterly cash dividend of \$0.31 per common share, representing approximately 70% of our AFFO per share.

Now turning to guidance:

We are affirming our 2018 guidance first announced last November. Based on projected net acquisition volume of \$900 million for 2018, we expect AFFO per share to be in the range of \$1.78 to \$1.84. AFFO per share in any period is sensitive to the timing of acquisitions during

that period, as well as the amount and timing of dispositions and capital markets activities. In 2018 we expect acquisitions to be spread throughout the remainder of the year, though they are often weighted towards the end of each quarter. The midpoint of our AFFO guidance is based on a weighted average cap rate on new acquisitions of 7.75% and targeted leverage in the range of 5.5 times to 6 times run-rate net debt to EBITDA.

Our AFFO per share guidance for 2018 equates to anticipated net income, excluding gains or losses on property sales, of \$0.83 to \$0.87 per share, plus \$0.88 to \$0.90 per share of expected real estate depreciation and amortization, plus approximately \$0.07 per share related to items such as straight-line rents, equity compensation, and deferred financing costs.

And now, I will turn the call back to Chris.

Christopher Volk

Thank you, Cathy. As is usual for me to do, and before turning the call over to the operator for questions, I want to make a few added comments. Every quarter, we disclose STORE Scores, which are a base form of contract rating, which you get by multiplying the probability of a tenant insolvency (which we derive from Moody's RiskCalc) by our estimate of lease rejection probability (which is an option available in bankruptcy to insolvent companies). Over time, we will get more precise with this form of measurement, but I can tell you that it overlooks a number of very important contributors to our performance. Capital stacks, for one, are important. For instance, were we to adjust our top ten tenants for effective unsecured capital stacks that are effectively subordinate to us, credit ratings would be elevated by approximately two notches. Other qualitative assistance can come from guarantees, either personal or corporate, low investment prices relative to values, rent deposits, and more. And this all omits our ability to bend the risk curve through effective portfolio management.

So, since the middle of 2017, the percentage of assets we hold having base investment grade STORE Scores has declined from an average of 75% to roughly 71% this quarter. We gave a lot of thought about disclosing this transparent data, which we use ourselves, because we figured you might rightly ask about STORE Score moves. So to preempt the ask, I'll tell you that there is nothing systemic that we see; a lot of it is simply balance sheet and growth driven. No sector or industry stands out, and there is rotation. So, while the average percentage of investment grade STORE Score ratings has fallen about 4% from 75% to 71%, 5% of portfolio has experienced improvement, while almost 9% has moved in the other direction. Then, if you look behind the moves, most are technical or small moves in our estimated probability that cause individual contracts to move a notch or more. Given median unit-level coverages have been holding stable for the portfolio, little of the move pertains to unit-level performance. Very few of the contracts that have moved are on our watch list, which has actually fallen slightly since last year. And, as you know, we continue to have fewer than ten properties that are vacant (the number this quarter is seven out of 2,000).

At the center of this exceptional performance of STORE are two cornerstone principles of corporate finance. The first is simply STORE's outstanding portfolio diversity, which is the best in our decades-long history of running successful public real estate investment trusts. Diversity is what permits pools of loans and leases to non-rated entities to have a substantial majority of their cash flows become investment-grade. The second cornerstone is contract seniority. Contract seniority is what permits non-rated businesses to issue highly rated securities backed by senior cash flow claims. At STORE, we have sought to actually combine these disciplines by having a highly diversified portfolio of investments and net lease contracts that represent senior claims on the cash flows of our tenants, owing to the fact that we exclusively invest in profit

centers. While the execution is complex, the principle is not. At the static corporate level (that's excluding external growth that benefits shareholders) our average 10 basis point loss on performance for the end of 2017 equates to what you might expect from an A credit rating, which is materially higher than the reported historic base STORE Scores we have reported. Only, unlike A-rated notes, our gross levered property-level returns are materially higher (like around 900 basis points higher), which you can see from our better than 13% gross levered returns realized from our investments made this quarter. And therein lies the alchemy. Achieving investment-grade risk through diversity and contract seniority, but with impressive equity rates of return that have enabled double digit rates of return for our shareholders for each of our first three years as a public company.

And with this, operator, I will now turn the call over to you for questions.

QUESTIONS AND ANSWERS

Operator

Yes, thank you. We will now begin the question-and-answer session. To ask a question you may press star (*) then one (1) on your telephone keypad. If you are using a speakerphone, please pick up the handset before pressing the keys. To withdraw your question, please press star (*) then two (2). At this time we will pause momentarily to assemble the roster. Okay, and the first question comes from Craig Mailman with KeyBanc Capital Markets.

Laura Dickson

Hey, everyone. This is Laura Dickson here with Craig. I guess this question is for you, Cathy. As you said, you had an active capital markets quarter. Was this a function of upcoming maturities for the ATM program and credit facility or just being proactive, and I also want to know if you're still considering preferreds?

Catherine Long

Okay. Hey, good morning. And so this quarter we had always talked about doing the public offering of bonds, and so that was part of the plan this year and the timing in the first quarter looked right. As far as the ATM renewal, yes it was. We were coming towards the end of our prior program and that was just really refreshing it. And for the revolver, we were really looking towards expanding liquidity going into the year, so allowing us to have a little bit more optionality as to when we would do long-term debt by having a larger revolver. And pushing out the maturity, we always believe that having longer revolvers is good.

Laura Dickson

Okay, that makes sense. And then Mary, I noticed in the pipeline it looks like entertainment has been deemphasized to 6% from like 11% in 4Q and then restaurants and other retail have increased, so I was just wondering if that's indicative of where you're seeing the best opportunities currently?

Mary Fedewa

Yes, probably Laura, it's fair. Essentially, the pipeline is pretty fluid and things move in and out pretty well. So, I would say that we're still looking at plenty of family entertainment, it's still a big category, but there was probably some movement of a transaction that moved away from us or we actually looked at.

Laura Dickson

Okay, great. Thank you.

Operator

Thank you. And the next question comes from Kevin Egan with Morgan Stanley.

Kevin Egan

Hi, good morning everyone. I just had a quick question in terms of just acquisition funding. So essentially kind of looking at what you've done this quarter, you raised some equity and we just assume about \$100 million per month and then dispositions of \$300 million to get to \$900 million net, it looks like you have done more acquisitions and probably less dispositions, so I was just wondering, are you thinking about funding more acquisitions with dispositions that mature or just rely on equity?

Catherine Long

Hi, this is Cathy. Yes, you know, the disposition activity is pretty lumpy, so I don't know that I would think that taking the first quarter and annualizing it would necessarily be what would really happen. So we will continue to look at disposition activity, as Mary mentioned. There are a couple different kinds of dispositions we do; one is opportunistic and that tends to be a little more where the timing may or may not be predictable, because some of it might be reverse inquiries and things like that. And then we do active portfolio management. And that's going to create lumpiness. So I think that, assuming that we'll have a decent amount of property sales, last year we did about \$250 million, and I believe we'll be higher than that this year somewhat. So yes, that will be a source of funding for the year, for sure.

Christopher Volk

I think your assumption is okay, if we say \$100 million a month and \$300 million worth of sales, I think that's a rational assumption there.

Kevin Egan

Okay. And then so just in terms of just cap rates on acquisitions, have you seen any movement there? I know a lot of your peers have said they stayed pretty flat, but are you seeing anything just maybe in the deals you look at?

Mary Fedewa

Yes, same. Very stable and not seeing...maybe a little upward pressure out in the auction marketplace just because interest rates are rising, but we haven't seen it really come through. They're very stable.

Kevin Egan

Okay. And then just back on dispositions, are there any properties that you're looking at or that you have in mind that are fairly low cap rate properties that you feel like you can dispose of that would create minimal dilution or is that not something you're really looking at or have in mind right now?

Christopher Volk

This is Chris. Well, first of all if you look at our acquisition activities, 784, the sales activity that we've been doing is less than that, I mean from a cap rate perspective, so it's all accretive. And I think it's really important that the sales activity be accretive. And on the opportunistic side it's exceptionally accretive, so we have transactions that fell off well into the 6s, and sometimes even lower than that. So – and it's partly because we're able to just originate stuff directly. And then over time what will happen, since we're dealing with BB tenants, it's an interesting thing. If

you're dealing with BB tenants, your chances of upward and downward credit migration are about the same. So, whereas your chances of downward credit migration or just the highest you're dealing with investment grade tenants, you have only one way to go. And, but if you're in BB territory, you sort of have some moves out – in either direction and then when you have moves upward, it represents a huge opportunity for us sometimes to sell off assets and make serious money on them. So we're been able to do that, and we will take advantage of that going forward.

Kevin Egan

Okay, sounds good. Thanks a lot.

Operator

Thank you. And the next question comes from Rob Stevenson with Janney.

Rob Stevenson

Good afternoon, guys. Chris, how are you feeling these days about early childhood centers and movie theaters? You trimmed a little bit in the quarter, is that something that we should expect to see you do or is it just opportunistic this time around?

Christopher Volk

I would say right this time around, it's been opportunistic. Theaters have always been kind of 6% or less in that neighborhood. So, I mean you're not going to see us go long and big time into theaters. It's not something we would do. Early childhood education we like a lot and we like the customers that we have. And we think it's just such a fundamental industry that has great size and strength. So you will see us do more of that.

Rob Stevenson

Okay. And then what is Zips Holdings? What type of stores are those?

Christopher Volk

Zips Holdings-- Mary, you talk about Zips Holdings.

Mary Fedewa

Zips is the second largest carwash in the U.S. They have about 108 locations. It's a fragmented industry as you can appreciate, so they're actually doing a big – pretty much a good rollup of that. They have a private company, so I can't talk a whole lot about the size in financials, but they have a nice membership program which really sets them apart. Good express washes. They have a large footprint in the company size, so they have good economies of scale, so a really strong player.

Rob Stevenson

So a competitor of Mr. Carwash?

Mary Fedewa

Yes, that's fair. Yes, there is carwash, yes, that's exactly.

Rob Stevenson

Are they regional or are they national?

Mary Fedewa

They're national.

Rob Stevenson

Okay.

Christopher Volk

Yes. I mean, I would say they are national, but they have regional areas of strength since they only have 100 units, so Mr. Carwash is meaningfully larger from a number perspective.

Mary Fedewa

Yes, a couple hundred, I think. The second largest.

Rob Stevenson

Okay, thanks.

Operator

Thank you. And the next question comes from Michael Knott with Green Street Advisors.

Michael Knott

Hey, this one is maybe for Mary. On the pipeline velocity slide, can you just speak to, I guess I would describe it as continued parabolic ascent of the total pipeline and then also the recent uptick in the number of deals reviewed?

Mary Fedewa

So I'll try and explain this. So, the pipeline – the trend line of the pipeline that you see going up is our total pipeline. It's \$12.3 billion. It's a dynamic pipeline, as you can imagine, things go on and go up with a lot of velocity, so for example in the first quarter, we might have looked at \$2.7 billion and then we may have decisioned \$2.7 billion. So, it sort of stayed at a little over \$12 billion in total. The bottom line talks about the deals that we are actually decisioning on. So, those are transactions that we are either passing on or we're funding, so that we're closing them or we're passing on them. So, you will see that in the first quarter we just had more of the pipeline sort of move through from a decision perspective, and it's pretty fluid. One quarter doesn't really make a trend or anything like that, but that's essentially what's happening on that chart.

Michael Knott

Okay. And then maybe for Chris, on your closing commentary about the slight downticks in the STORE Score investment grade percentage, just curious, and then you also gave the reminder, the very useful reminder that credit migration tends to be down when you have an investment-grade rated tenant. Do you see an analogy there over time with your STORE Scores and is that part of the recent downtick in your STORE Score investment grade percentage? Is there sort of a corollary there?

Christopher Volk

No. First of all, the downgrade migration comment is totally correct for corporate credit ratings, so unsecured corporate credit ratings, which you see. I mean, so – and there is evidence, the strong evidence that if you're investing in, let's say, a BBB company, you probably have a better than 50-50 shot at being non-rated over 10 years, something like that. In our case, we're not rating companies per se, we're rating contracts. So, we're basically doing a twofold type rating. So the migration capability is going to be a little bit different I would say, and you have to understand, you have by the way, just to appreciate the full magnitude of this -- the difference between a AAA rated company and a BBB- rated company is a whopping 60 basis points of

default probability. I mean, that's the entire spread. So you're talking about just incredibly small moves and risks that can cause things to move up or down. And so what we've seen is that we've looked across the portfolio, most of it has to do with things like growth. So for example, let's say you're growing, you add a lot of debt, your balance sheet looks more levered, but you don't have a run rate income yet to show for it. So there's some of that that's happening. There are some people that have done actual buyouts where you do have some higher leverage but the leverage is unsecured, so we're not really worried about it. And so we're going to be peeling back all the reasons for all of this, but I thought that it was important for us to tell you sort of what's happening overall.

Michael Knott

Yeah, thanks for that proactive commentary. That was helpful. Thanks.

Operator

Thank you. And the next comes from John Massocca with Ladenburg Thalmann.

John Massocca

Good morning everyone.

Christopher Volk

Hi John.

Catherine Long

Good morning.

John Massocca

So can you maybe give us a little update on the progress with either selling or leasing up the vacant Gander stores and potentially maybe even returning those two that are under CMBS debt to the lender?

Catherine Long

Yes, this is Cathy. As far as the two that we've returned to the lender, we had talked about that last quarter that there were two properties that were CMBS financed. And recovery-wise, turning that back to the lender was the most effective recovery, time-wise as well, to put that to bed and move on. And then eight of the properties that Mary mentioned we re-let, and those are the Gander Outdoors. And they are all online as of now. So they're all paying rent and they came on throughout the first four or five months.

Mary Fedewa

And we sold one for 100% and then we have two that we're working on in special servicing and we're getting a lot of activity on those two sites.

Christopher Volk

So out of the seven empty properties we have that are not paying, two of them are Ganders.

Mary Fedewa

Yes. Of the seven empty, two are Ganders.

John Massocca

Is it, okay, so, okay – so essentially just the two and then the rest, just the two left to resolve at this point?

Mary Fedewa

Yes.

John Massocca

CMBS has already been handed back to the lender at this point?

Christopher Volk

Basically the recovery on that would have been close to what the loan was anyway. So, it just made sense for the CMBS lender to service it.

John Massocca

Understood. And then can you just maybe breakout what your coverages are between the service retail and manufacturing components of your portfolio, just generally speaking?

Christopher Volk

Well, I would say that the median coverage is around two for the portfolio. I would say that the retail is probably a little bit higher than that. So I would say that the service component sector of our portfolio, if I had to do this broad speaking, it's going to be kind of in line, maybe a touch lower. The manufacturing coverage is going to be considerably higher, which is why we basically talk about median coverage as opposed to weighted average coverages, because sometimes you will have a manufacturing company and the cover will be 16 to 1, or something like that. And by the way, having high coverages isn't always something that you sleep well at night on too, because when you have high coverages, it just means your rent is so insignificant that they might decide to move elsewhere, so you have to really focus on other issues as well.

John Massocca

And then, so service you'd expect kind of to be basically because of the bulk portfolio in line with the median number?

Christopher Volk

Yes.

John Massocca

Okay. That's it for me. Thank you guys very much.

Operator

Thank you. And once again, please press star (*) then one (1) if you would like to ask a question. And the next question comes from Collin Mings with Raymond James.

Collin Mings

Hey, good morning.

Mary Fedewa

Good morning Collin.

Catherine Long

Hey, Collin.

Collin Mings

First question for me, just kind of going back to the manufacturing side of the deal pipeline, can

you just maybe provide an update on the growth opportunities there. Again, the deal pipeline looks pretty flat there, but just over the last couple of years clearly the exposure there has picked up a little bit. Where do you see that going over, call it the next six months, year or so?

Mary Fedewa

Hey Collin, it's Mary. Manufacturing, we've always thought around 15% is kind of where it is, I wouldn't expect it to move much higher than that or maybe much lower either. There has actually been a lot of manufacturing transactions out in the market right now. As you know, a lot of people moved away from retail, so manufacturing's gotten a little bit hotter on the asset class side of, in the auction marketplace for sure. So, but we're still – we're looking at everything, as we do no matter what it is, so as long as it has a P&L and they will do the master leases and they'll report financials, you know, we'll look at the opportunity. So, I would say, 15% has really been our sort of guideline there.

Collin Mings

Gotcha. But I guess, the other part of that question was, and I think you touched on it, which is you are actively seeing a little bit more competition for deals there, just given the market dynamics?

Mary Fedewa

Yes, I think that's fair. I think some people call it industrial, we call it manufacturing, most of ours make a product, not all. And so yes, on the industrial side we've seen a lot more activity out there. And again, I would probably attribute that to people kind of running from retail a little bit.

Collin Mings

Okay. And then lot of my questions have been answered, but just two more housekeeping ones, just can you expand on the loan loss recognized in the quarter?

Catherine Long

Sure, that was – this is Cathy. That was a loan that we made a couple of years ago that was secured by assets and we took back most of the assets and the remaining amount was written off during the quarter. We may still collect on some of it, but to be conservative, it was just written off.

Collin Mings

Okay, fair enough. And then just, you touched on, provided a little bit more color around Zips Holdings, but just maybe talk a little bit more. Is there, could there be some repeat business there and just how do you think about that in terms of the diversity of your portfolio?

Catherine Long

Sure. There will definitely be. As you know 30% of our business is repeat and when we work with customers we expect that they're going to go to grow and that we're going to be able to do more business with them. The relationship piece is really important to us and it's how we get paid for the value we add, as you know. So, I do expect that we'll do some more Zips. I guess I will defer to Chris on carwashes in general in the portfolio, and I don't think that we will do a whole bunch of them.

Christopher Volk

Yes, we don't have a stated objective in terms of what our carwash limitations are, but suffice it to say it's a small sector, and so we're going to keep our exposure limited.

Catherine Long

Yes.

Collin Mings

Appreciate the color. Thanks. I'll turn it over.

Operator

Thank you. And as there are no more questions, I would like to turn the conference to Chris Volk for any closing comments.

CONCLUSION**Christopher Volk**

And thank you operator. Many of you listening attended to our recent April 11th Investor Day at the New York Stock Exchange, which was terrific and provided a deeper dive into STORE and our highly evidence-based real estate investment net lease investing methodology. We're going to return to New York City for the NAREIT Conference on June 4-7, so if you'd like to see us there, please reach out to us or Financial Profiles. And finally, we're posting Lesson 10 -- exciting, exciting -- of STORE University, which will be on our website fully at the end of May and STORE U also now has its own YouTube channel for easier access and massive binge watching. So, thanks all for listening. We'll be around today and tomorrow for any follow-up questions. Goodbye.

Operator

Thank you. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines.