

JLL Research Report

Seniors Housing

*Investor Survey and Trends
Winter 2018*



The seniors housing market is maturing, and more investors than ever view seniors housing as an asset class that they need to have in their portfolios. JLL has a Valuation & Advisory Services group and a Capital Markets team, both with dedicated experts in seniors housing and healthcare.

To help our team and our clients gain a better understanding of the seniors housing market, we are embarking upon a semiannual investor survey. This is the inaugural edition of the survey. Going forward, we will be conducting updates every year at midyear and year-end.

Each edition of the survey will feature market participant expectations relating to sector desirability, required return rates and go-forward expectations. Each edition will also have a Spotlight covering an important topic within the seniors housing sector.

We would like to thank all of the market participants who participated in our survey for this inaugural issue, and hope that all readers will find value in this publication. As always, please feel free to reach out to any of our team members, shown on page 15, if we can assist you in any way.

Survey Findings

Some of the more interesting results indicated by the survey are:

- The most desirable seniors housing subsector is a property offering a continuum of care including independent living and assisted living, but without nursing care. The subsector garnering the least favorable ratings is the freestanding nursing subsector.
- The seniors-only apartment space is an emerging subsector. The survey data bears out JLL's long-held hypothesis that the cap rates for seniors-only apartments should fall below the cap rates for independent living, given the fewer services provided and lower perceived risk. The survey indicated average cap rates by class to be 30 to 50 basis points lower for seniors-only apartments relative to independent living.
- Much of the historical cap rate data for seniors housing does not differentiate by investment class. Our survey included data for four classes for each property sector: – A+, A, B, and C. The spread between the investment classes, Class A+ to Class C, ranged from 150 basis points for net leased nursing to 290 basis points for entry-fee continuing care retirement communities (CCRCs).
- Emerging trends with the most staying power are the shift from single-level-of-care facilities to continuum-of-care facilities and the focus on urban infill locations. The emerging trend with the least staying power is dynamic rental rate pricing.
- The biggest risk factors identified by respondents are overbuilding, rising labor costs and the increasing challenge of attracting and retaining qualified staff.

Thanks to all those who participated in the survey. The intent of the survey is to garner some objective market opinion and to provide some insight into current market sentiment. While surveys only represent participant opinion, they are also helpful by providing up-to-date market trends and market direction.

4 key trends

Headwinds behind the seniors housing sector are strong even in the midst of changing operator dynamics and continuing pressure on occupancy. With the first wave of baby boomers now hitting age 72, and with 10,000 a day turning 65, the seniors housing sector will likely see continued strength not just in 2018, but for the next few decades.

Seniors housing occupancy holding steady. Seniors housing occupancy reached 88.8 percent at the end of 2017, down slightly from the same time last year. The year wrapped up with occupancy just above its cyclical low of 87.0 percent, reached during the first quarter of 2010, and below its most recent high of 90.2 percent in the fourth quarter of 2014. Demand is growing at a healthy clip, but increasing new supply will continue to challenge occupancy rates in 2018.

Independent and assisted living performance moving in opposite directions. The signs of a divergence of the property types' occupancy performance began mid-2012, when both independent and assisted living recorded an occupancy rate of 88.8 percent. Since that point, the occupancy rate of assisted living facilities has fallen by 220 basis points to 86.5 percent, while the occupancy rate for independent living properties rose 190 basis points to 90.6 percent as of the end of 2017. Occupancy for independent living is improving from a recent peak of 91.4 percent as inventory growth has slowed in many key markets.

Rent growth decelerating but continuing on an upward trend. At the end of 2016, same-store asking rent growth for seniors housing reached a cyclical high of 3.7 percent. While rent growth decelerated in the fourth quarter, 2017 year-over-year growth reached 2.6 percent, staying in line with the long-term average pace experienced since late 2006. With increasing expense pressure from a tight talent pool and increasing tenant demands for new amenities, rent growth will be a key metric to watch in 2018.

Sales transactions volume slowed in 2017. Preliminary reports on seniors housing show transactions volume slowing in 2017 to \$14.1B, with a relatively weak fourth quarter in terms of closed deals. Private equity and institutional investors from the United States and around the world have been increasingly focused on seniors housing assets, but this has been balanced by a deceleration of acquisitions by seniors housing REITs. Overall the number of transactions dropped by nearly 17.0 percent, despite several large portfolio transactions. In recent years, portfolio transactions have represented 20.0 percent of overall closed transactions.

Source: NIC



Seniors Housing

Each sector of the seniors housing market serves a slightly different market niche, and market dynamics vary greatly by sector.

24-Hour Skilled Nursing

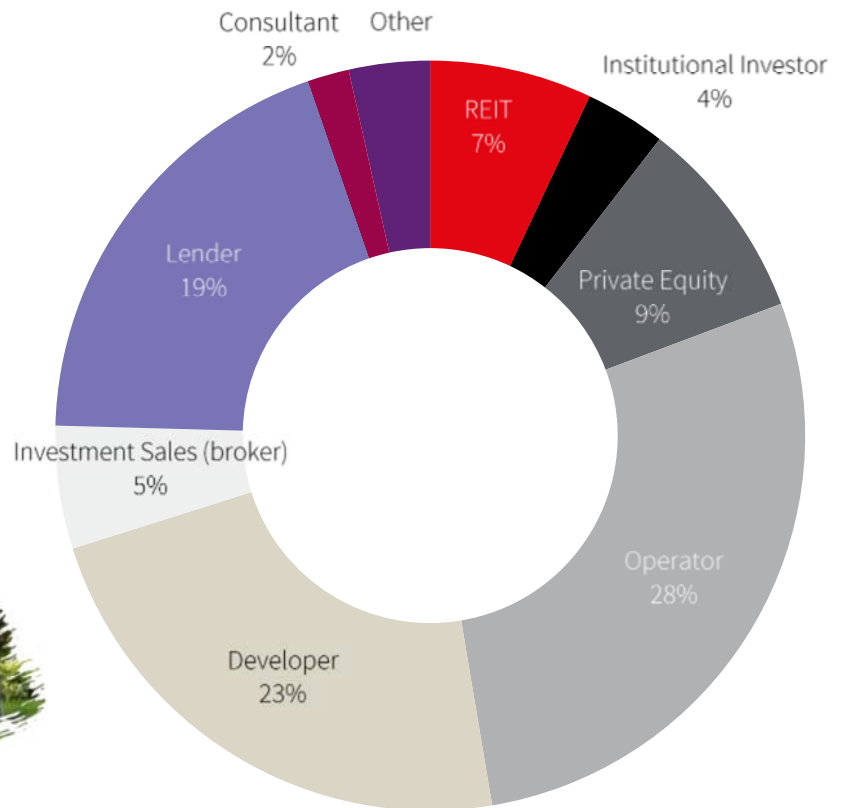
	Housing	Activities	Meals	Housekeeping & Laundry	Personal care services	Memory Care	Short-term post-acute care	Long-term chronic care
Seniors Apartments:	Real Estate Component							
Independent Living:	Real Estate Component	Services Component						
Assisted Living:	Real Estate Component	Services Component						
Memory Care:	Real Estate Component	Services Component						
Skilled Nursing:	Real Estate Component	Services Component						



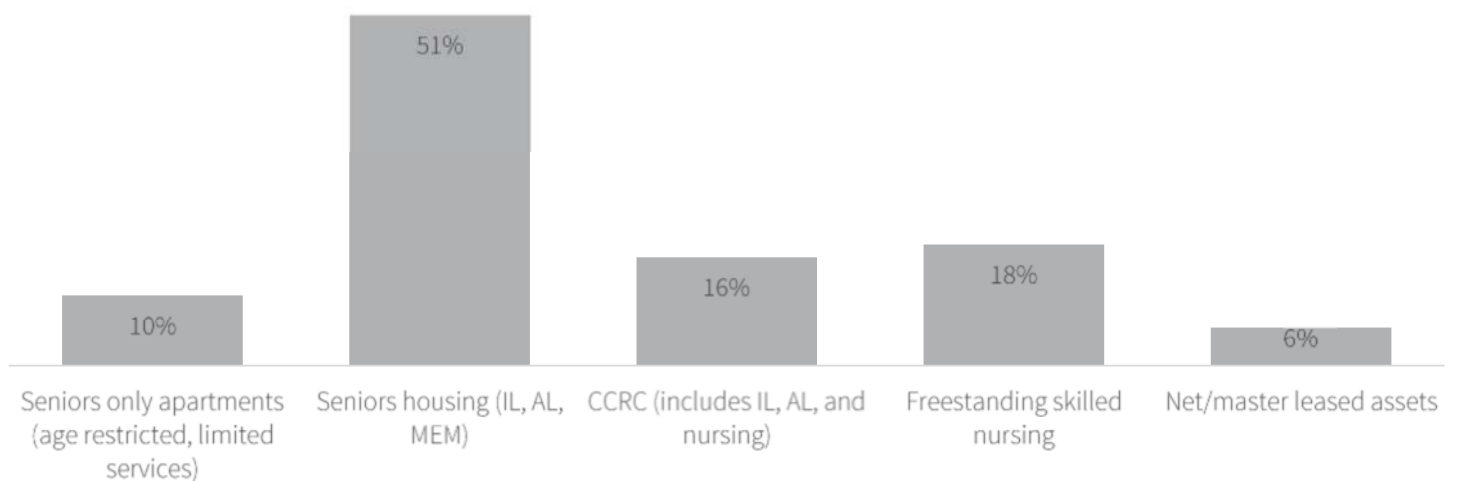
Survey Respondents

Our survey included more than 250 potential respondents with a focus on transactional professionals who specialize in the seniors housing and care space.

The majority of professional respondents included operators, developers and lenders at 28 percent, 23 percent and 19 percent respectively.



Sectors respondents are active in

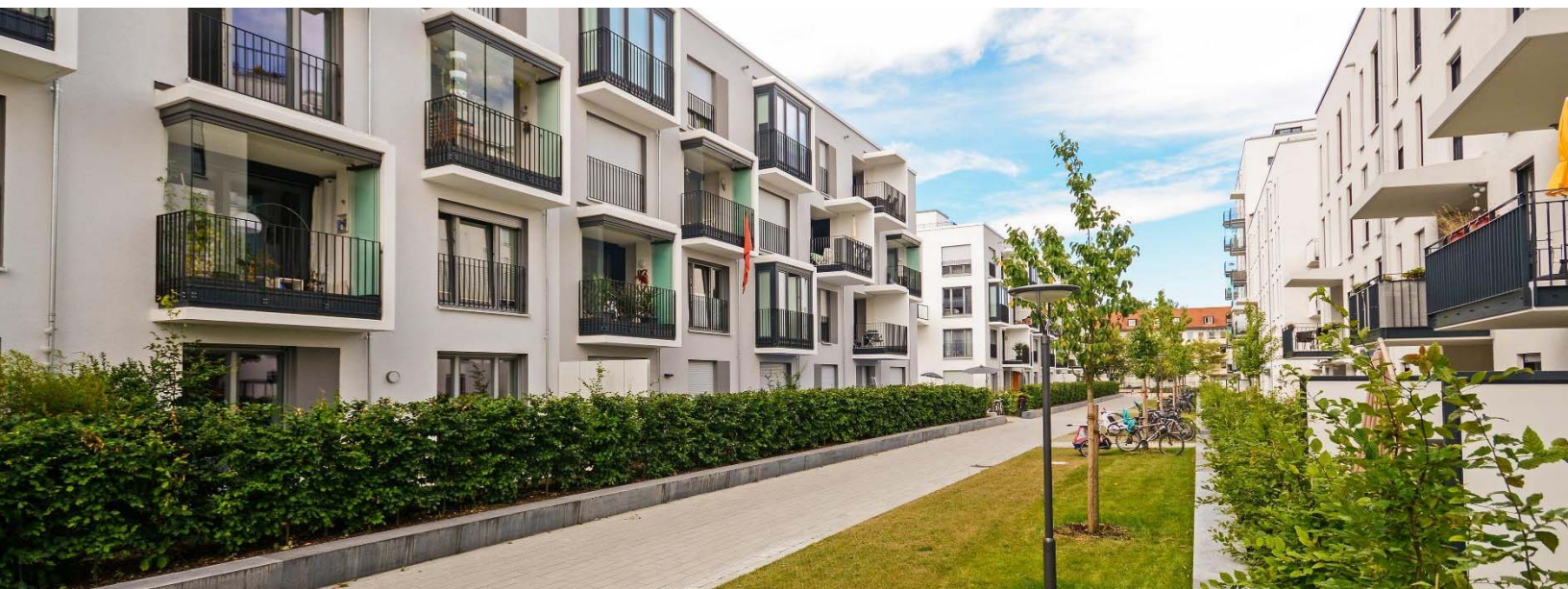
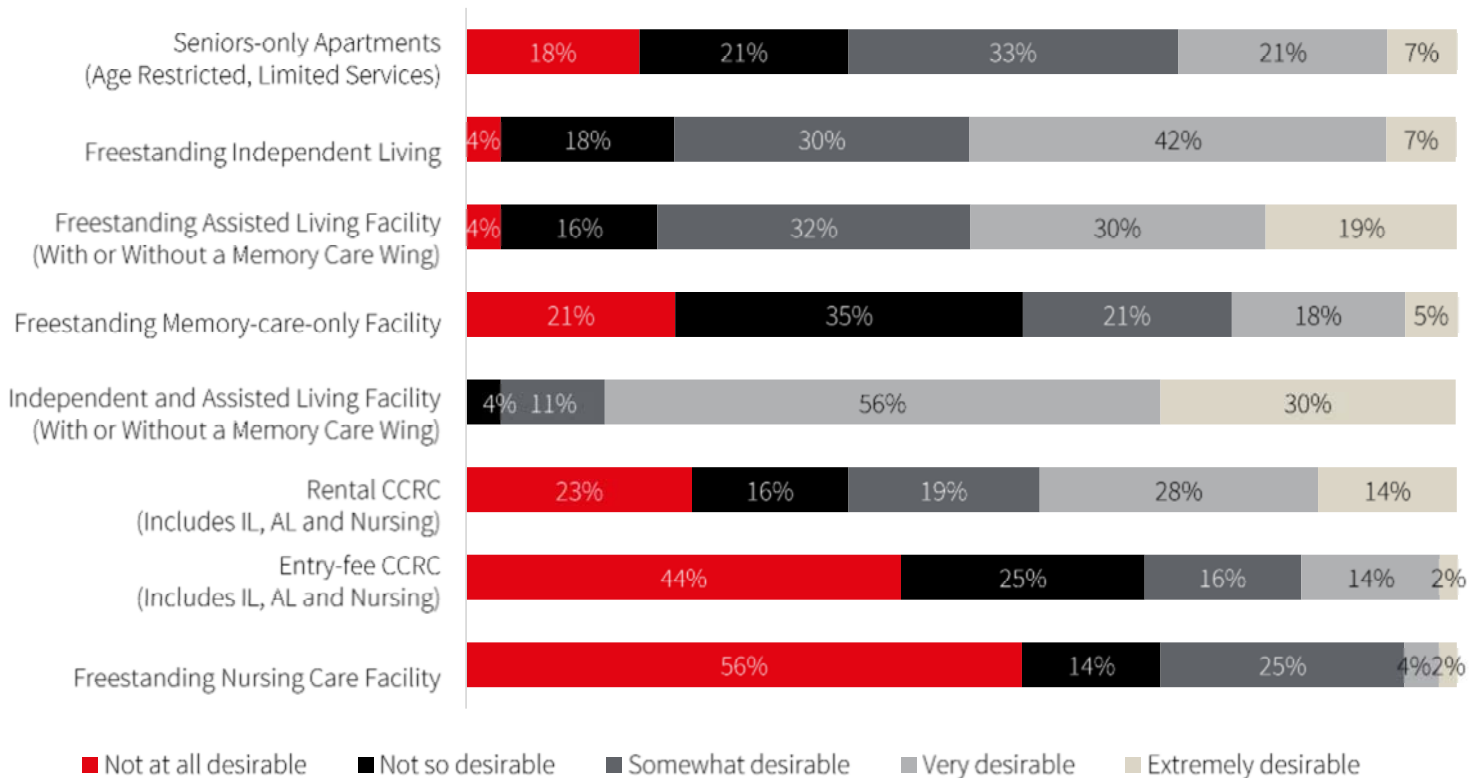


Sector Desirability

Survey respondents were asked which sectors they see as the biggest opportunity for investment.

According to the ULI 2018 *Emerging Trends in Real Estate*, overall seniors housing ranks **third** among 24 commercial/multifamily subsectors in 2018 for best investment and development prospects. Seniors housing also ranks **first** among seven residential property types in 2018 for best investment and development prospects.

Nearly 30.0 percent of survey respondents ranked independent and assisted living facilities as an extremely favorable investment. Meanwhile 56.0 ranked nursing care investment as not at all desirable.



Cap Rates

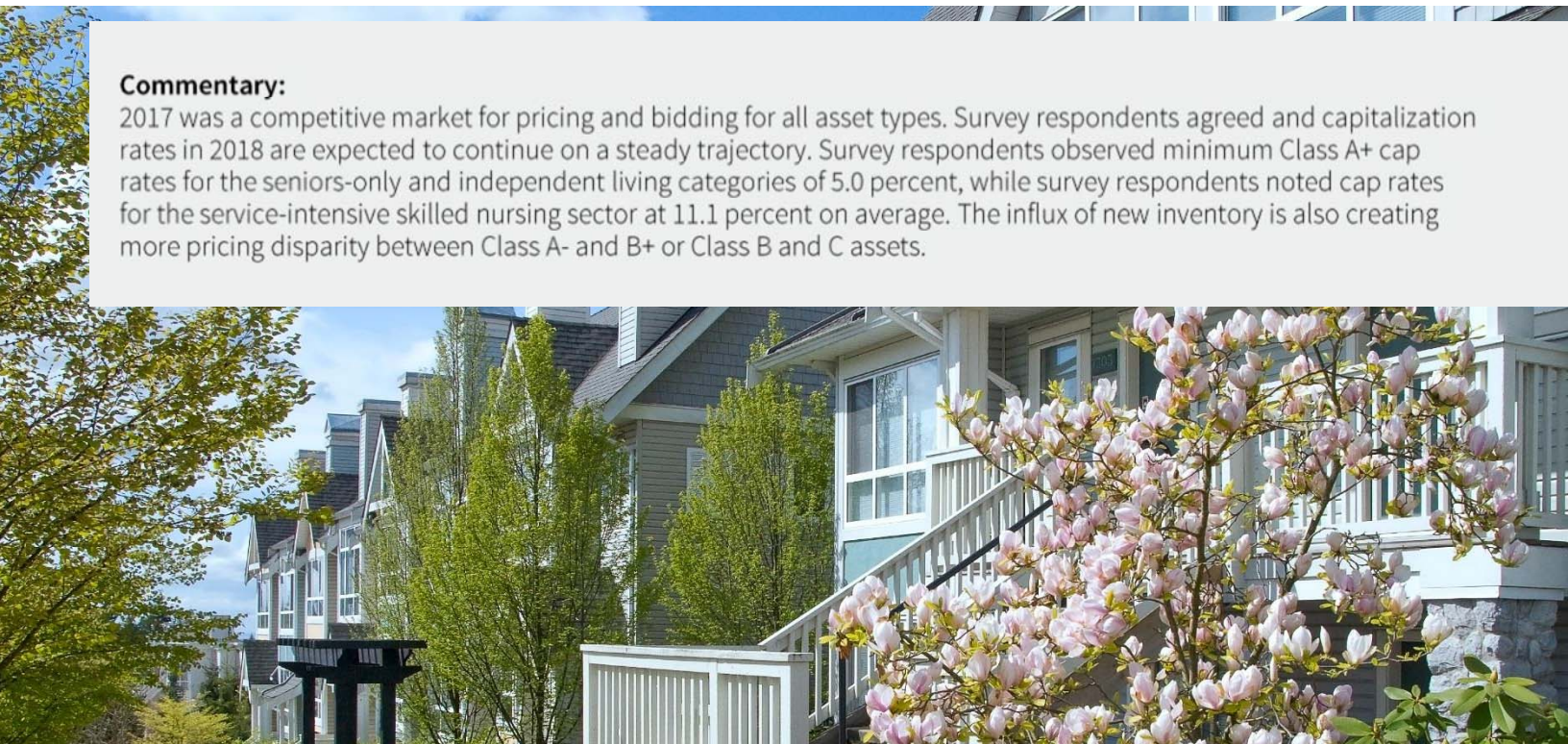
Survey respondents were asked for the appropriate capitalization rate for assets based upon sector and class, and utilizing first-year pro forma net operating income.

	Seniors-only Apartments				Freestanding Independent Living				Freestanding Assisted Living				Memory Care			
	A+	A	B	C	A+	A	B	C	A+	A	B	C	A+	A	B	C
Min	5.0%	5.0%	6.0%	7.0%	5.0%	5.3%	6.0%	6.5%	5.5%	5.8%	6.5%	7.0%	6.0%	6.5%	7.3%	7.8%
Max	6.0%	6.5%	7.5%	8.5%	7.0%	7.3%	8.0%	10.0%	8.0%	9.0%	10.0%	11.0%	10.0%	11.0%	12.0%	13.0%
Avg	5.5%	5.8%	6.5%	7.6%	5.9%	6.3%	7.0%	7.9%	6.5%	6.9%	7.6%	8.7%	7.3%	7.7%	8.4%	9.3%

	Independent and Assisted Living				Rental CCRC				Entry-fee CCRC				Nursing				Net Leased Nursing			
	A+	A	B	C	A+	A	B	C	A+	A	B	C	A+	A	B	C	A+	A	B	C
Min	5.0%	5.5%	6.3%	6.8%	5.3%	5.5%	6.3%	6.8%	5.0%	5.3%	6.0%	6.5%	10.0%	10.5%	12.0%	12.0%	8.5%	9.0%	9.5%	10.0%
Max	7.0%	8.0%	9.0%	10.5%	8.0%	8.0%	9.0%	12.0%	9.0%	9.5%	10.0%	12.0%	12.0%	12.5%	13.0%	15.0%	8.5%	9.0%	9.5%	10.0%
Avg	6.0%	6.5%	7.2%	8.1%	6.6%	7.0%	7.6%	8.8%	7.5%	7.9%	8.8%	10.4%	11.1%	11.6%	12.4%	13.5%	8.5%	9.0%	9.5%	10.0%

Commentary:

2017 was a competitive market for pricing and bidding for all asset types. Survey respondents agreed and capitalization rates in 2018 are expected to continue on a steady trajectory. Survey respondents observed minimum Class A+ cap rates for the seniors-only and independent living categories of 5.0 percent, while survey respondents noted cap rates for the service-intensive skilled nursing sector at 11.1 percent on average. The influx of new inventory is also creating more pricing disparity between Class A- and B+ or Class B and C assets.



Unleveraged Yields

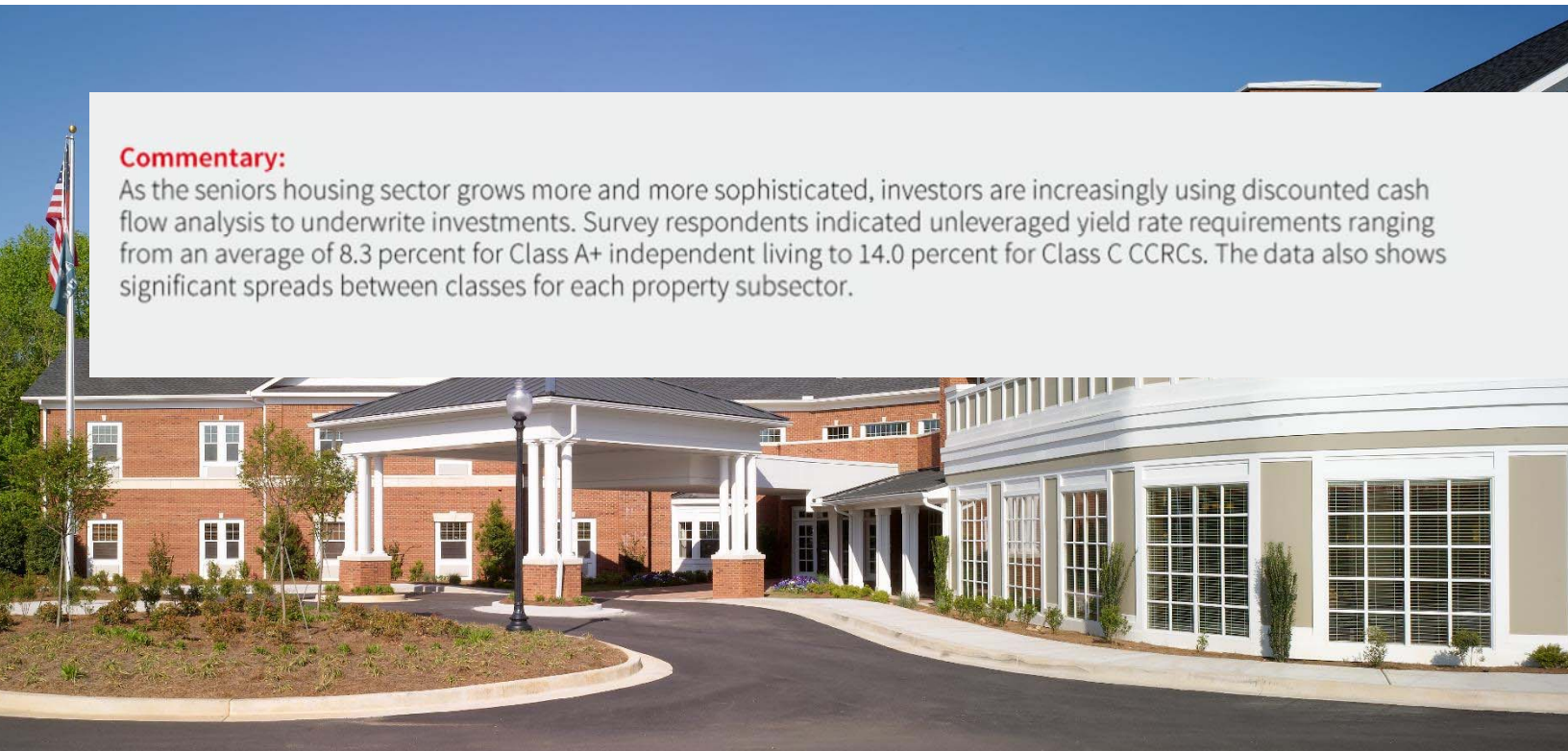
Survey respondents were asked to indicate the appropriate required unleveraged yield rates by sector and class.

	Freestanding Ind. Living				Freestanding Assist. Living				Freestanding Memory Care				Independent and Assisted Living			
	A+	A	B	C	A+	A	B	C	A+	A	B	C	A+	A	B	C
Low	6.0%	6.5%	7.5%	8.5%	6.0%	6.5%	7.5%	8.5%	6.5%	7.5%	8.0%	9.0%	6.5%	7.0%	7.5%	8.5%
High	10.0%	12.0%	15.0%	18.0%	10.5%	12.5%	15.0%	18.0%	12.0%	15.0%	18.0%	20.0%	10.0%	12.0%	15.0%	18.0%
Avg	8.3%	8.9%	10.0%	11.6%	8.6%	9.7%	11.0%	12.4%	9.3%	10.5%	11.8%	13.1%	8.2%	9.1%	10.2%	11.8%

	Rental CCRC				Entry-fee CCRC				Freestanding Nursing Care			
	A+	A	B	C	A+	A	B	C	A+	A	B	C
Low	9.0%	10.0%	11.0%	14.0%	9.0%	10.0%	11.0%	14.0%	8.8%	9.0%	9.3%	10.0%
High	9.0%	10.0%	11.0%	14.0%	9.0%	10.0%	11.0%	14.0%	12.0%	12.5%	13.0%	14.0%
Avg	9.0%	10.0%	11.0%	14.0%	9.0%	10.0%	11.0%	14.0%	10.4%	10.8%	11.1%	12.0%

Commentary:

As the seniors housing sector grows more and more sophisticated, investors are increasingly using discounted cash flow analysis to underwrite investments. Survey respondents indicated unleveraged yield rate requirements ranging from an average of 8.3 percent for Class A+ independent living to 14.0 percent for Class C CCRCs. The data also shows significant spreads between classes for each property subsector.



Outlook for revenue and expenses

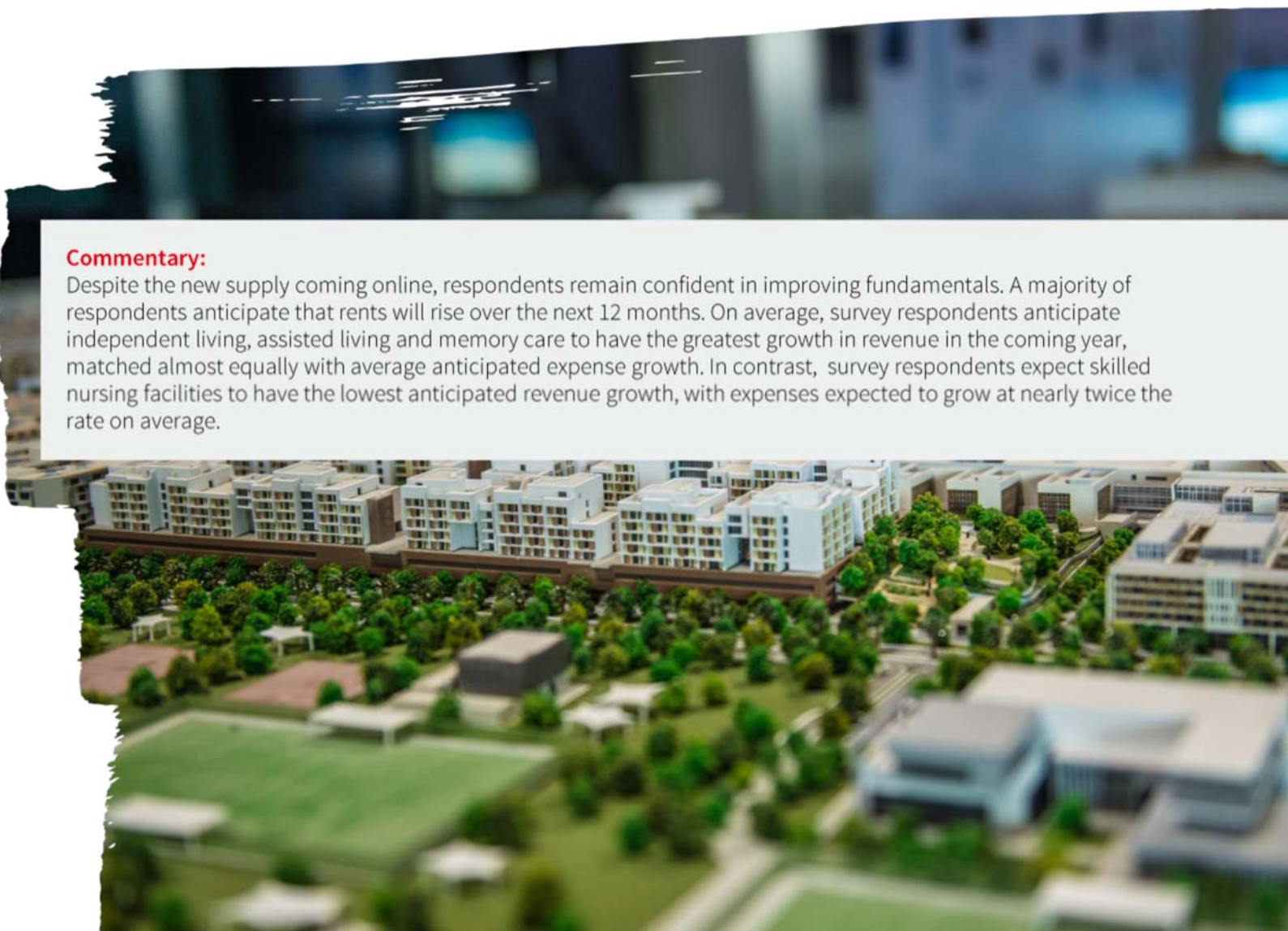
Survey respondents were asked to indicate anticipated change in revenue and expenses for the next 12 months by sector.

Annual growth in revenue (percent change), Annual growth in expenses (percent change)

	Seniors-only Apartments		Independent Living		Assisted Living		Memory Care		Skilled Nursing	
	Revenue	Expenses	Revenue	Expenses	Revenue	Expenses	Revenue	Expenses	Revenue	Expenses
Low	3.0%	3.0%	2.5%	2.5%	0.0%	2.5%	-10.0%	2.5%	0.0%	2.0%
High	3.0%	3.5%	8.0%	6.0%	8.0%	6.0%	8.0%	6.0%	3.5%	4.0%
Avg	3.0%	3.2%	3.7%	3.4%	3.5%	3.6%	3.0%	3.6%	1.4%	2.8%

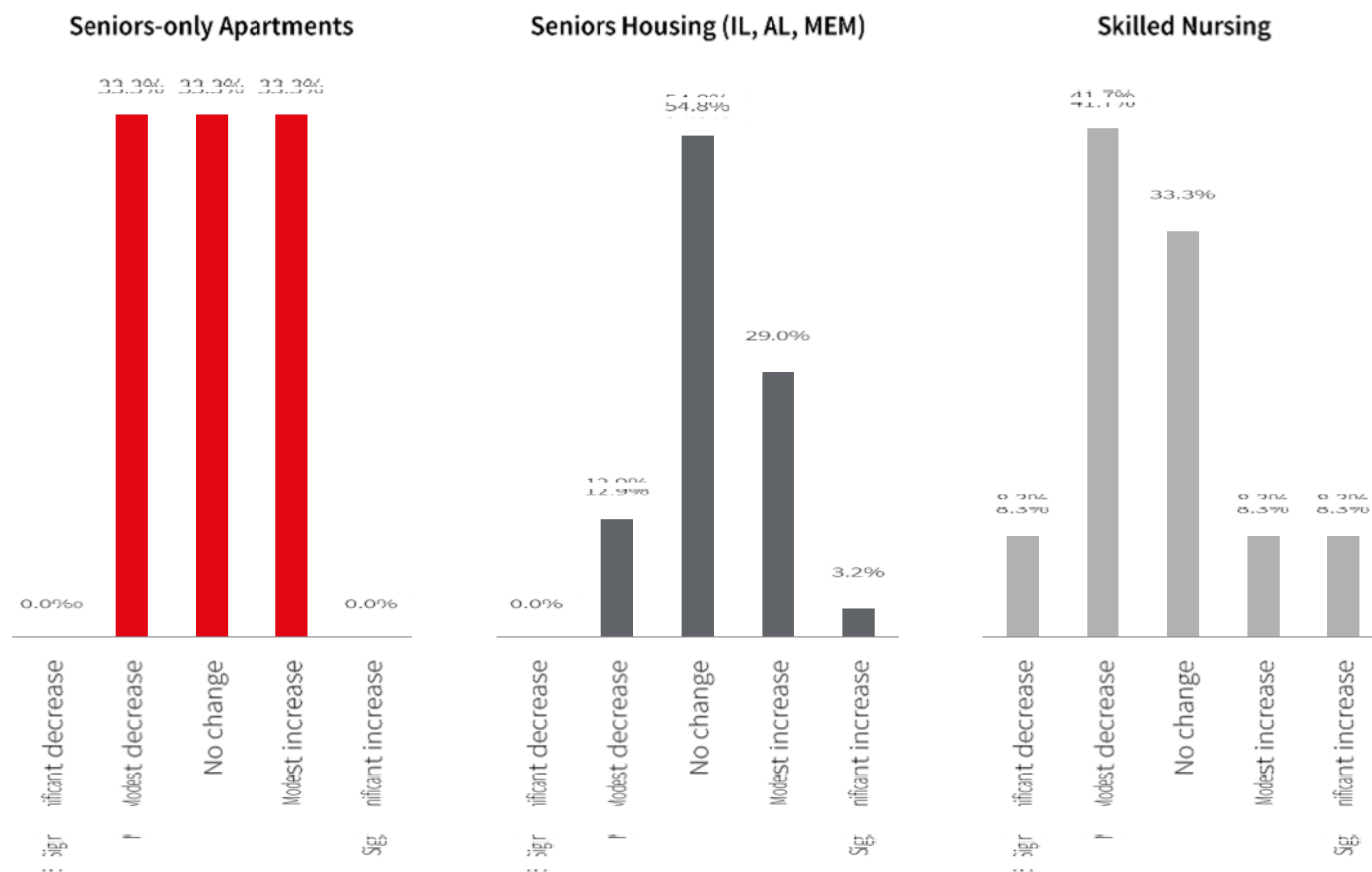
Commentary:

Despite the new supply coming online, respondents remain confident in improving fundamentals. A majority of respondents anticipate that rents will rise over the next 12 months. On average, survey respondents anticipate independent living, assisted living and memory care to have the greatest growth in revenue in the coming year, matched almost equally with average anticipated expense growth. In contrast, survey respondents expect skilled nursing facilities to have the lowest anticipated revenue growth, with expenses expected to grow at nearly twice the rate on average.



Anticipated Value Changes for 2018

Survey respondents were asked by what degree they anticipated values changing over the coming 12 months.



Commentary:

Survey respondents were confident that seniors-only apartments would hold firm, anticipating values would most likely change modestly or not at all in the next 12 months. Survey respondents were more optimistic for seniors housing (IL, AL, memory), with nearly 30.0 percent expecting a modest increase in value, while nearly 42.0 percent of survey respondents expect skilled nursing to moderately decrease in the coming year.

Sales Cycle

To dig deeper into investor appetite and gauge a typical marketing time, survey respondents were asked how many months typically pass from the date the property is placed on the market through the date of closing.

	Marketing Time (months)			
	Seniors-only Apartments	Independent Living	Assisted Living	Skilled Nursing
Low	3.0	3.0	6.0	3.0
High	6.0	9.0	9.0	12.0
Avg	5.0	6.6	6.8	7.1

Commentary:

Survey respondents reported expected marketing time for seniors-only apartments to be the shortest at five months on average, an indication of the limited supply and investor appetite. Independent and assisted living were anticipated to be marketed for more than a month and a half longer on average. However, survey respondents indicated the length of the marketing period for skilled nursing could be up to 12 months, or over 7 months on average.



Risk Factors

What risk factors are most concerning to market participants.

	Not a risk	Low risk	Moderate risk	High risk
Overbuilding and market saturation	0%	9%	47%	44%
Increases in interest rates	0%	47%	44%	9%
Difficulty obtaining equity	16%	69%	16%	0%
Difficulty obtaining debt	13%	50%	31%	6%
Rising labor costs for facility staff	0%	0%	47%	53%
Difficulties attracting and retaining qualified staff	0%	0%	44%	56%
Increasing construction costs	0%	13%	66%	22%

Attracting talent and the rising cost of retaining staff were the two highest risk factors noted by survey respondents.

The battle for talent in seniors housing is no surprise as the Bureau of Labor Statistics reported healthcare occupations added more jobs than any of the other occupational groups in 2016. Employment of healthcare occupations is projected to grow 18.0 percent from 2016 to 2026, much faster than the average for all occupations, adding about 2.3 million new jobs. The BLS attributes this growth primarily to an aging population, leading to greater overall demand for healthcare services.

Overbuilding, market saturation and increasing construction costs were next on the minds of survey respondents.

While increases in inventory outpaced annual absorption in 2017, there are signs in the market that seniors housing construction starts are potentially plateauing. 2017 ended with a slower pace in construction starts for both the independent and assisted living sectors. Since 2014, nearly 79,000 units were added to inventory primarily in the major markets. Nearly one-third of this growth in inventory (26,000 units) occurred in eight metro areas: Dallas, Minneapolis, Chicago, Atlanta, Houston, Boston, Phoenix and New York. Dallas alone accounted for 5.0 percent of all new seniors housing inventory in the past three years. In addition, 11 secondary markets experienced gains in inventory of more than 20 percent over the course of the past three years (NIC MAP Q42017).

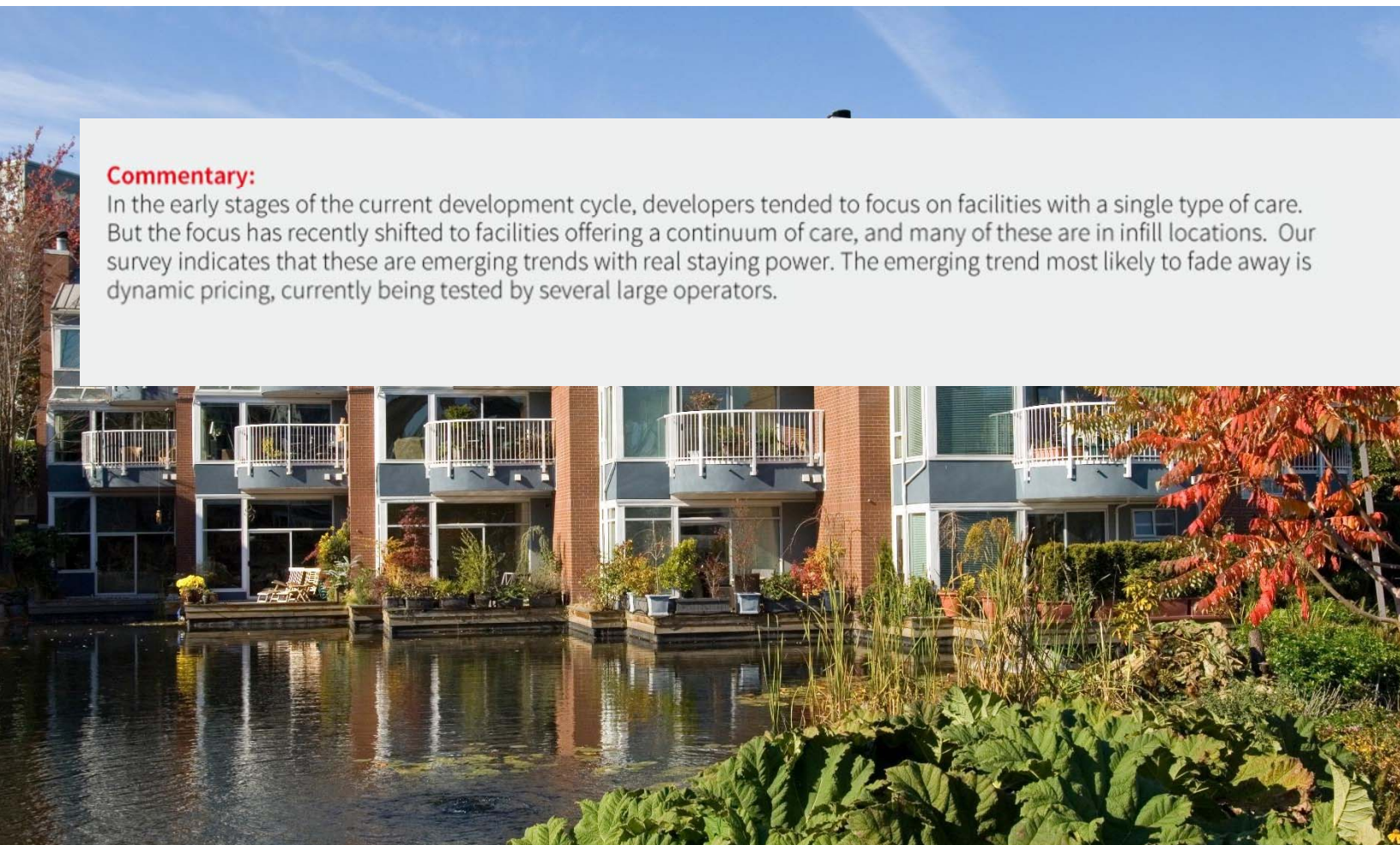
Spotlight: Staying Power of the Industry Trends

JLL has noted a number of emerging trends in the seniors housing sector, and to get a sense of the possible staying power of these trend, the survey respondents were asked to evaluate them.

	"Flash in the pan" — won't last	Could have legs	Definitely here to stay
Focus on urban infill locations for new development	6.3%	40.6%	53.1%
Shift from single-level-of-care facilities to continuum-of-care facilities	0.0%	31.3%	68.8%
Operating companies getting smaller and regionally focused as opposed to larger and national in scale	9.4%	46.9%	43.8%
Optional a la carte pricing of services in independent living	3.1%	53.1%	43.8%
Emergence of private-pay "seniors-only" apartments as a major subsector	15.6%	53.1%	31.3%
Dynamic pricing whereby rents adjust weekly or even daily based on demand and competition	50.0%	37.5%	12.5%

Commentary:

In the early stages of the current development cycle, developers tended to focus on facilities with a single type of care. But the focus has recently shifted to facilities offering a continuum of care, and many of these are in infill locations. Our survey indicates that these are emerging trends with real staying power. The emerging trend most likely to fade away is dynamic pricing, currently being tested by several large operators.





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About JLL

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