NIC Investment Guide

INVESTING IN SENIORS HOUSING & CARE PROPERTIES

SIXTH EDITION

EXECUTIVE SUMMARY

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The complete NIC Investment Guide is available for purchase at store.nic.org.


Maravilla Scottsdale
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Introduction

The *NIC Investment Guide: Investing in Seniors Housing & Care Properties, Sixth Edition* provides an overview of the seniors housing and care sector based on year-end 2019 time-series data, pre COVID-19 pandemic. This edition of the *Investment Guide* was prepared and reviewed by a subgroup of industry professionals within NIC's Future Leaders Council (FLC) and NIC staff. The *Investment Guide* helps fulfill NIC's mission to enable access and choice of seniors housing and care by providing data, analytics, and connections that bring together investors and providers.

Purpose

The *Investment Guide* is designed as a seniors housing and care primer that investors can use to investigate the opportunities, challenges, and risks of investing in the sector and help formulate an investment thesis. It serves as an introduction to the industry's investment characteristics, performance, and leading players. The *Investment Guide* is intended as a representative overview of the significant characteristics of the industry. Wherever possible, it provides information on seniors housing in comparison to other commercial real estate property. Sources used are listed in an appendix which readers can utilize to review more detailed information on specific issues that interest them.

Data Used

This data-based overview has been made possible by the tremendous progress in data collection by the industry over the past 14 years. The NIC MAP® Data Service (NIC MAP), which tracks and reports on 140 of the nation's metropolitan markets, has provided reliable time-series data for industry performance on occupancy, rent growth, supply, and construction. For time-series data in this publication, unless otherwise noted, we use aggregates for the NIC MAP Primary Markets—i.e., metropolitan markets—because data from those markets is available starting from 4Q05. For point-in-time comparisons, data for all of NIC MAP's 99 Primary and Secondary Markets as of year-end 2019 is used since it is more representative of the overall seniors housing and care market. (See Appendix O for a listing of all the metropolitan markets tracked by NIC MAP.)

Through NIC's strategic alliance with Real Capital Analytics, NIC MAP also reports pricing and volume metrics on closed sales transactions of seniors housing and care properties throughout the U.S. for the past 10 years. The National Council of Real Estate Investment Fiduciaries (NCREIF) has tracked the investment return performance of seniors housing properties since 2003, and the expanded and improved State of Seniors Housing provides yearly snapshots of industry performance in key areas such as expenses and operating margins. Together, these data sources offer essential information on net operating income (NOI), margins, and investment returns.

For data consistency, wherever possible, the *Investment Guide* uses data as of the end of 2019.

Throughout the development of the *Investment Guide*, we had to decide what information to include and what to exclude, either because the data integrity was questionable or because the information was considered beyond the scope of a primer. There were a number of places where it was recognized that quality data simply was not available, and that further work was needed to collect and report such data in the future. NIC is committed to working with other industry professionals to fill data gaps for future editions of this publication. Please share any comments and suggestions to improve future editions of the publication and advance industry transparency.

Organization of the Report

The *Investment Guide* begins with an executive summary that provides an overview and roadmap to the entire report. The sixth edition also includes the popular Emerging Trends and Observations section that was introduced in the third edition of the *Investment Guide*. While much of the publication relies on data to review past performance, the Emerging Trends and Observations section relies on expert opinions to provide a forward-looking perspective.

The technical chapters of the *Investment Guide* begin with a detailed description of each seniors housing and care community type that is covered in Sections 3-7. This sixth edition includes a separate section on properties focused primarily on memory care, rather than combining memory care with assisted living. The community type descriptions include resident profiles, supply data, industry operating structures, operating economics, and current trends. Section 8 discusses the development and construction of new properties and the acquisition of existing properties. Section 9 provides an overview of debt and equity sources of capital for the seniors housing and care industry. Finally, Section 10 discusses valuations, returns, and loan performance.

NIC has included a comprehensive set of appendices with information that is of interest to investors in seniors housing and care properties, such as demographics (Appendix B). The appendices also include detailed information on lender underwriting standards (Appendix I), and housing and healthcare collaboration (Appendix L).

Notes on Data Sources and Footnotes

Appendix P includes a list of all data sources referenced in the *Investment Guide*. Numbered footnotes throughout the report refer to the data sources in Appendix P. Sources in Appendix P are listed in order of those most frequently referenced in the *Investment Guide*. The numbering of the footnotes is often not sequential. In general, we have used the most timely, accurate, and reliable data available.

Acknowledgments

NIC would like to express our sincere appreciation to the following groups and individuals whose efforts were instrumental in the development and production of the *Investment Guide*. First, thanks to members of NIC's Future Leaders Council (FLC), whose responsibilities included writing an initial draft of select sections within the report, reviewing chapters written by NIC staff, and providing authorship for the Emerging Trends and Observations section. Members of the FLC task force included:

- Elyse Hanson, Director, Investments, Blue Moon Capital Partners, LLC
- Ross Holland, Managing Director, White Oak Healthcare Partners, LLC
- Jay Leo, President, Touchmark
- Alex Massopust, Vice President, Finance and Accounting, New Perspective Senior Living
- Dennis Murphy, Director of Investments, Benchmark Senior Living
- Kari Onweller, Vice President, Partner Relations and Portfolio Management, Invesque
- Adam Rybka, Vice President, Longview Senior Housing Advisors
- Julie Stande, Associate, Nixon Peabody
- Peter Trazzera, Vice President, KeyBank Real Estate Capital
- Sara Veit, Managing Director, Acquisitions, Hana2.0 Property Group, LLC
- Jennifer Zhao, Assistant Vice President, AEW Capital Management, L.P.

In addition to Zach Bowyer, MAI, JLL Valuation Advisory, Lee Delavaris, vice president, KeyBank Real Estate Capital, Matt O'Grady, senior trader, KeyBanc Capital Markets, and Jerry Taylor, vice president of operations, National Health Investors, NIC would like to acknowledge the significant contributions of NIC staff members, including Lana Peck, senior principal and project leader extraordinaire, Ryan Brooks, senior principal, Leighann Garcia, senior data and analytics manager, Chuck Harry, chief operating officer, Bill Kauffman, senior principal, Elisabeth Kerr, manager, brand and design, Beth Burnham Mace, chief economist, Molly McCarter, senior data analyst, Dan Raney, director, product solutions and technology, Anne Standish, research statistician, and Omar Zar, data analyst.

Foreward

At the time of drafting the *NIC Investment Guide: Investing in Seniors Housing & Care Properties, Sixth Edition*, the COVID-19 pandemic was happening in real time. As of August 1, 2020, approximately 18 million people worldwide had been infected with COVID-19, with approximately 700,000 deaths worldwide, including approximately 160,000 in the U.S.

Until a vaccine is developed and widely distributed, the COVID-19 pandemic will continue to threaten older adults. While seniors housing and care operators are implementing new systemic programs and protocols to keep staff and residents safe, the future is still unknown due to the nature and duration of the COVID-19 virus. As a result, the context of operating under these circumstances has shifted from that of a sprint to that of a marathon, but a marathon without a known finish line. NIC recognizes that this new normal will not revert to the old normal, and that the new normal is here now and will continue to evolve. With this in mind, NIC has identified a number of critical considerations:

- Frontline caregivers who are fighting 24/7 to protect 2.5 to 3.0 million frail elders are especially vulnerable to this virus and must be supported. Caregivers must have the equipment and assistance it takes to be effective. They need PPE, access to regular, timely, and effective testing, as well as supports, such as childcare and food security for their families.
- Innovative collaborations and partnerships with healthcare organizations help care for frail elders where they live, reduce trips to the hospital, and improve a resident's quality of life.
- Many need-based seniors housing and care settings are purpose-built to protect this disproportionately high-risk population from viruses, such as the flu, but require PPE, regular, timely, comprehensive testing, and support to fight COVID-19.
- The underlying fundamentals and drivers of seniors housing remain in place. The demographics alone support the growing need for care and housing for seniors. The surge in baby-boomers as residents of seniors housing is that much closer, as the oldest baby boomer born in 1946 will be age 83 (typical age of a resident to move into seniors housing) in 2029.
- The need for care and housing is especially acute for middle-income seniors. It's likely that, as a result of the pandemic and the secondary impact it has had on the economy, more Americans than ever will slip into the forgotten middle-income cohort, making the need for affordable care and housing ever more pressing.

Despite the new normal that is still evolving, the investment thesis for investing in seniors housing remains compelling, including the basic need for congregate living settings associated with an aging population and the sector's long-term attractive investment returns and portfolio diversification benefits. Additionally, this crisis has demonstrated that skilled nursing properties are also an essential part of the healthcare continuum. The sector offers compelling and emerging opportunities in both healthcare collaboration and population health management—critical elements to stave off potential staggering societal healthcare costs.

Time will tell the outcomes. Until then, this edition of the Investment Guide, based on year-end 2019 time-series data, serves as a benchmark to the seniors housing and care sector pre-COVID-19 pandemic. A key ingredient in moving the seniors housing and care sector forward is the data that helps support transparency which, in turn, builds trust. Transparency based on good data is good for everyone—residents, families, staff, operators, investors, and policymakers.

Lakewood
Henrico, VA

IN THIS SECTION

Section 1

Executive Summary

The *NIC Investment Guide: Investing in Seniors Housing & Care Properties* serves as a primer for understanding the seniors housing and care property sector. The *Investment Guide* covers the investment characteristics of the sector, as well as its performance and the leading players. Our aim is to provide the most current and reliable industry data for investors to help them evaluate opportunities, risks, and potential returns, and fine-tune their individual investment strategies. The *Investment Guide* is an outgrowth and reflection of NIC's mission to provide data, analytics, and connections, all of which advance the access and choice of seniors housing and care for America's elders—from independent living, assisted living, and memory care, to skilled nursing and post-acute care.

1.1 Seniors Housing and Care Properties

The seniors housing and care industry provides both housing and an array of services to seniors, generally to those over the age of 75. Care segments are commonly divided into four categories:

- Independent living (IL)
- Assisted living (AL)
- Memory care (MC)
- Nursing care (NC)

Nursing care has traditionally been provided in an institutional-style setting, although there is a growing movement toward a more homelike setting. The other care segments typically are provided in a multifamily setting. Seniors housing and care properties also include continuing care retirement communities (CCRCs), also referred to as life plan communities (LPCs), which must offer at least two care segments—independent living and nursing care—in a single community. For purposes of this report, the term "seniors housing" excludes nursing care properties and 55+ seniors apartments (also referred to as "active adult"), whereas the term "seniors housing and care properties" includes all of the properties providing the care segments outlined previously but not 55+ seniors apartments.

In the U.S., there currently are approximately 24,500 investment-grade seniors housing and care properties containing 3.1 million units. For the purposes of this report, we use "investment grade" to define age-restricted properties with at least 25 units/beds that charge market rates for the housing and services offered. These estimates do not include many smaller "board and care" properties, which are not considered for purchase by the typical institutional investor yet serve a sizable population of seniors. The total value of this investment-grade seniors housing and care property market is estimated at $474.5 billion—assuming an average $210,000 price per unit for seniors housing properties and an average $81,000 price per bed for nursing care properties.[1]

Exhibit 1.a shows the number of properties and units offered within the different community types, campus types, and care segments.

Exhibit 1.a

Supply of Investment-Grade* Seniors Housing and Care Properties in the U.S.

By Property and Unit Counts by Community Types, Campus Types, and Care Segments | Estimates as of 4Q19**

By Community Type	# Properties	# Units***
Independent Living	2,900	452,100
Assisted Living	7,900	666,700
Memory Care	1,500	80,100
Nursing Care	10,300	1,328,300
CCRC/Life Plan Community	1,900	620,700
Total	**24,500**	**3,147,900**
By Campus Type	**# Properties***	**# Units***
CCRC/Life Plan Community	1,900	620,700
Combined	7,700	932,000
Freestanding	14,900	1,595,200
Total	**24,500**	**3,147,900**
By Care Segment		**# Units***
Independent Living		722,600
Assisted Living		717,100
Memory Care		247,200
Nursing Care		1,461,000
Total		**3,147,900**

*Current estimates are not comparable to estimates from prior years due to different estimation techniques.
**Estimates are representative of properties with at least 25 units/beds that charge market rates and/or accept Medicaid for the housing and services offered.
***One nursing bed is equivalent to one unit.
Source: NIC MAP® Data Service, NIC

Care segments are defined as the type and level of services offered by properties. Community types are classified by the plurality of units by care segment offered. For example, an assisted living community with 10 independent living units, 60 assisted living units, and 30 nursing care beds is classified as an assisted living community, as is any combined property with a plurality of assisted living units or a freestanding assisted living property.

The campus type of a property depends on the number and possible combination of care segments offered:

- CCRCs offer independent living and nursing care at the same property, although assisted living and memory care are generally offered as well
- Combined campuses offer at least two different care segments—e.g., independent living and assisted living. However, these do not include properties that offer independent living and nursing care, because they are considered CCRCs
- Freestanding campuses offer only one type of care segment—e.g., independent living only

Exhibit 1.b highlights the array of services offered across the different property types.

Besides housing, including both shelter and amenities, seniors housing and care properties offer residents multiple services:

- Hospitality services—meals, transportation, housekeeping, entertainment, and concierge services
- Care services—assistance with bathing, grooming, dressing, eating, medication management, and other activities of daily living (ADLs)
- Medical services—skilled nursing, rehab therapy, and chronic care

The care and medical service mix at each property increases with residents' needs. Typically, independent living serves the most able residents and offers primarily hospitality services. On the other hand, nursing care serves residents with the greatest medical needs by providing the most intensive services.

A continuing trend in seniors housing and care has been the rising acuity levels of residents upon initial move-in across all care segments. As a result, independent living and assisted living operators often care for residents who already have some ADL needs. In addition, skilled nursing operators increasingly are serving residents in need of short-term rehabilitation services or those with high-acuity medical care needs who were previously served for a more extended period of time in an acute care hospital, a long-term acute care hospital, or an in-patient rehabilitation facility. Some independent living and assisted living operators now provide home healthcare, therapy, and other services to residents to better meet the needs of residents within their properties. Others allow residents independently to engage third-party service providers to meet care needs that could not otherwise be accommodated in their properties either by the decision of the operator or by the state regulatory framework.

Exhibit 1.b

Property Types by Services Provided

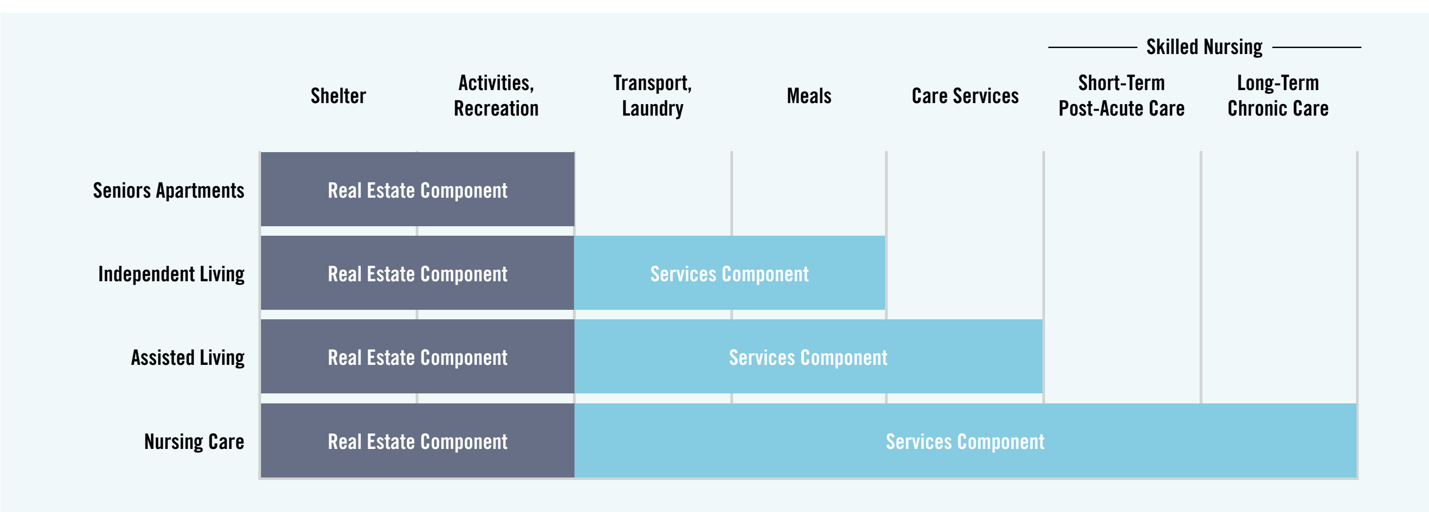


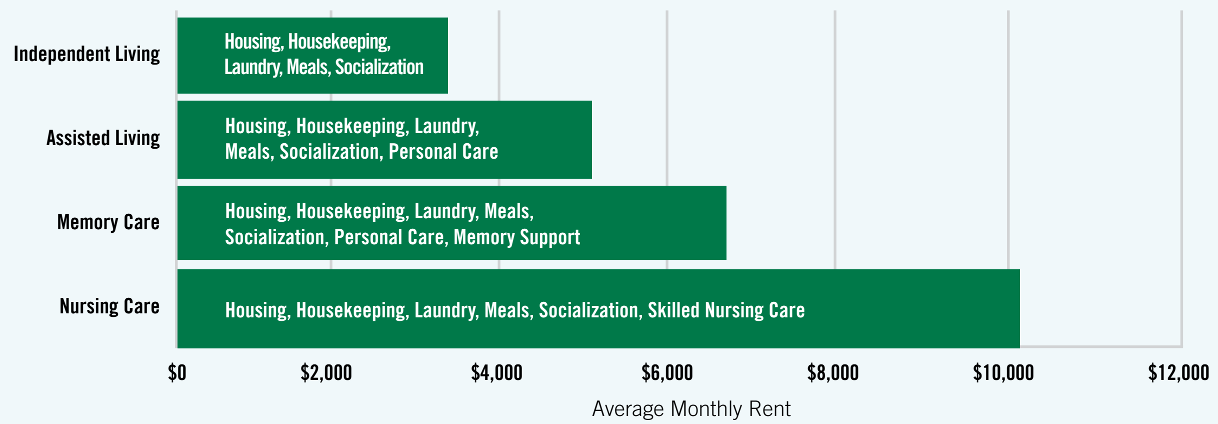
Exhibit 1.c highlights the average asking monthly rents for each care segment, reflecting the needs level and the accompanying service mix. (See Appendix C for more details regarding needs assessment and pricing.)

Exhibit 1.d provides select metrics that further quantify distinctions between different seniors housing and care community types.

Exhibit 1.c

Average Monthly Rent by Care Segment

As of 4Q19



*The nursing care monthly rent is the average private-pay per diem rate calculated on a monthly basis; see Section 6 for the Medicaid and Medicare rates. ***Source: NIC MAP® Data Service***

Exhibit 1.d

Selected Metrics by Community Type

As of 4Q19

	Independent Living	Assisted Living	Memory Care	Nursing Care	CCRC/LPC
Average Monthly Rent	$3,239	$4,977	$6,709	$10,078*	$3,353
Median Number of Units	141	80	48	120	290
Median Age of Buildings (years)	19	20	14	40	35

*The nursing care monthly rent is the average private-pay per diem rate calculated on a montly basis; see Section 6 for the Medicare and Medicaid rates. ***Source: NIC MAP® Data Service***

1.2 Seniors Population

Seniors and their families in need of services drive demand for seniors housing and care properties. The average age of residents in seniors housing is estimated to be in the mid-80s, while the average move-in age is in the low- to mid-80s. The population of individuals age 80 years and older provides a reasonable benchmark for potential demand. The population estimate of individuals age 80 years and older for 2018 was 12.7 million, which represented 4% of the U.S. population.

Exhibit 1.e shows the breakout of age cohorts by individuals and households.[7]

The sizes of the 80+ and 85+ populations are expected to increase at a rate of approximately 3.2% and 1.9% per year, respectively, between 2020 and 2025 and then accelerate to an average of 4.6% and 3.9%, respectively, from 2025 until 2030. (See Exhibit 1.f.) More precision can be found by looking at the 82- to 86-year-old age cohort, which best captures the average move-in age of seniors housing residents. This population cohort is projected to expand by 3.5% in the first part of this decade and then accelerate to an average yearly pace of 5.7% through the latter half of the decade.[8]

One way to measure the use of seniors housing by seniors is through a penetration rate. Industry penetration may be calculated in a variety of ways and will vary by region, age, and population cohort. Dividing the total U.S. inventory of seniors housing units by the U.S. population age 80 years and older yields an estimate of 13.3% as of 2019. Dividing it by the U.S. population age 75 years and older yields an estimate of 7.7% during the same period. NIC measures penetration rates using U.S. households age 75 and older. In other instances, population and household estimates are income-qualified. (See Appendix B for more details about demand drivers.)

While nearly 1.7 million people live in seniors housing, demand may be constrained by many seniors' hesitancy to leave their homes and anxiety concerning monthly rent payments, particularly for those households who own their homes. Because of this preference, many businesses provide services to seniors within their existing homes as an alternative to the housing and services offered by seniors housing and care properties. We refer to these services as "alternative services."

(See Appendix E for detailed descriptions of alternative housing and services.)[1]

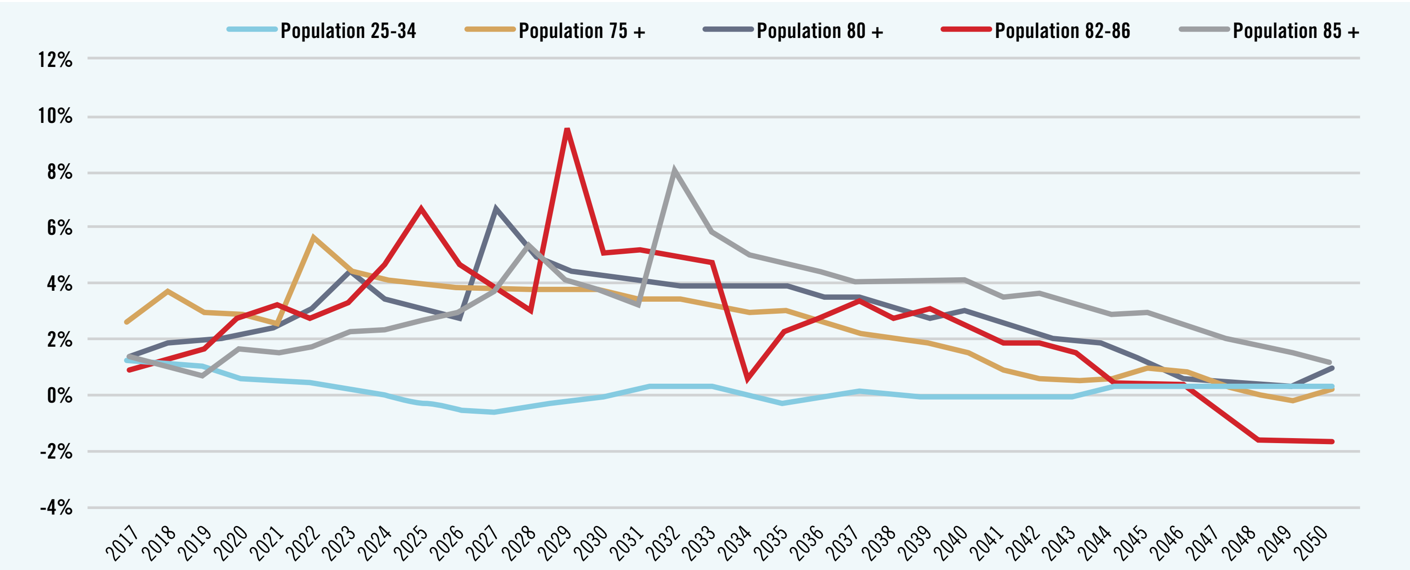
Exhibit 1.e
U.S. Population and Households by Age Cohort*

	Population (millions)		Households (millions)	
	Number	% of Total	Number	% of Total
45-64	83.9	26%	46.2	36%
65-74	30.5	9%	19.7	15%
75-84	15.4	5%	N/A	N/A
75+	21.9	7%	14.5	11%
80+	12.7	4%	N/A	N/A
85+	6.5	2%	N/A	N/A

*Population estimates for 2018 and household estimates for 2019

Source: U.S. Census Bureau

Exhibit 1.f
Annual Population Growth Rate Projections
2017–2050



Source: U.S. Census 2017 Population Projections

1.3 Performance Comparisons

For many investors, the combined components of real estate, hospitality, and needs-driven services give seniors housing and care properties a unique resiliency, offering the benefits of a real estate investment with the attributes of healthcare and hospitality investments The resiliency of this combined set of characteristics was evident during the 2008–2009 real estate downturn when seniors housing and care properties outperformed other commercial real estate property types in terms of investment returns and rent growth.

The NCREIF Property Index (NPI) is a leading U.S. quarterly time series composite total rate of return measure of investment performance (gross of fees) of a very large pool of individual commercial real estate properties acquired for investment purposes only. (NCREIF is the acronym for the National Council of Real Estate Investment Fiduciaries.) Most properties in the NPI have been acquired, at least in part, on behalf of tax-exempt institutional investors—the great majority being pension funds. As such, all properties are held in a fiduciary environment. As of 4Q19, the NPI comprised 8,263 properties with a combined market value of $658.5 billion.[11]

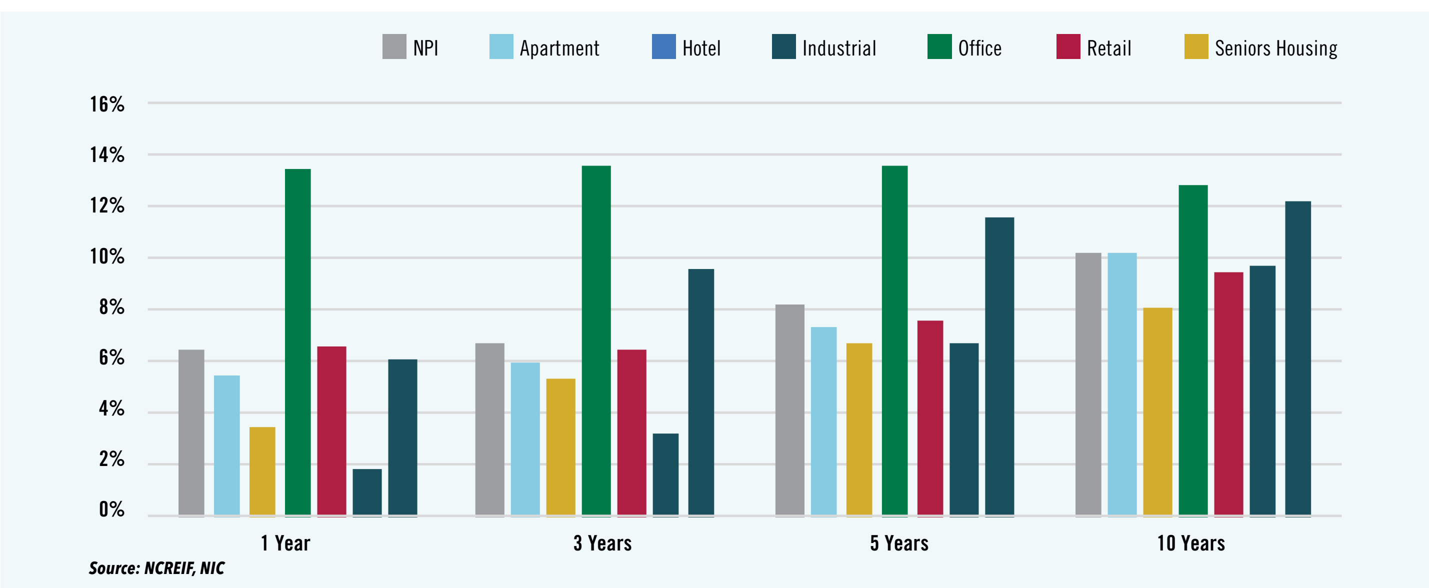
Over the past 10 years, the nominal returns on the seniors housing properties within NCREIF's database, but which are not included in the NPI, have outperformed the nominal performance return measurements for the broad NPI as well as for the other individual NPI indices. As of 4Q19, seniors housing properties had generated an annualized return of 12.1% since 4Q09. This compares to an annualized return of 10.2% for both the apartment index and the entire NPI. Seniors housing has also outperformed the NPI property types in terms of the appreciation and income components, both of which are discussed in Section 10. As of 4Q19, data on 124 stabilized seniors housing properties was reported to NCREIF. The value of these assets totaled $6.5 billion.[11]

Some of the strength in the 10-year investment performance of seniors housing and care properties can be attributed to relatively steady leasing trends when compared with other real estate property types, especially during the recession of 2008-2009. As compared with the property types within the NPI, seniors housing is the only real estate property type that did not experience declining asking rents during the economic recession. As seen in Exhibit 1.i, asking rent growth for seniors housing reached a cyclical low of 1.2% in 4Q10, which was well above the cyclical lows of the core commercial real estate types of apartments and offices—respectively, -6.0% and -16.0% in 2009. From 2007-2011, asking rent growth averaged 2.4% for seniors housing properties, half the pace of apartments, which experienced outsized rent growth following the rent declines incurred during the recession. It is also notable that rent growth in seniors housing was steadier and less volatile than other commercial real estate property types.[1, 19]

Exhibit 1.g

NCREIF Annualized Total Returns by Property Type

Periods ending 12/31/2019



In the past 10 years, public healthcare REITs, for which seniors housing and care properties represent a significant share of their investment portfolios, have lagged the FTSE NAREIT Equity REIT Index, and the S&P 500 Index. An investment made 10 years ago in the S&P 500 would have realized an annualized total return of 13.5%, while an investment in the FTSE NAREIT Equity REIT Index would have realized an annualized total return of 12.6%. The healthcare REIT sector index is the third-best performing sector behind industrial and apartments, with an annualized return of 10.1% during the same 10-year period. This was better than the return performance in office, retail and hotels. [20, 21]

1.4 Property Ownership and Large Operators

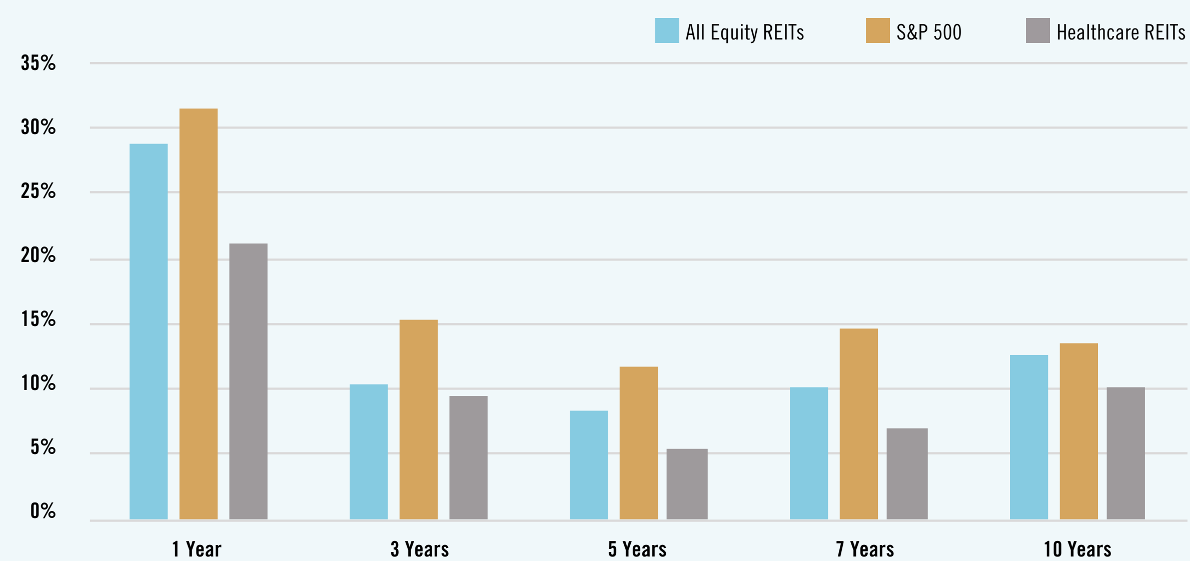
Exhibits 1.j and 1.k outline the property ownership composition within seniors housing and care. The largest owner category of seniors housing and care properties are private for-profit entities with ownership of 55.4% ($198.2 billion) of units in seniors housing properties and 67.2% ($78.6 billion) of units in nursing care properties. Publicly traded REITs own 11.6% ($41.4 billion) of units in seniors housing properties and 6.5% ($7.5 billion) of units in nursing care properties.[1]

Exhibits 1.l, 1.m, and 1.n list the largest operators of seniors housing (majority independent living and assisted living properties), nursing care properties, and CCRCs/life plan communities. The 10 seniors housing operators in Exhibit 1.l control 21.7% of units within seniors housing properties in the Primary and Secondary Markets tracked by NIC MAP®. In many cases, seniors housing and care properties are owned by an entity other than the operator. These ownership entities include publicly traded healthcare REITs and institutional investors. The structures of the relationships often vary by ownership, with institutional investors often entering into a joint venture ownership structure with an operator, while REITs engage in either a triple net lease (NNN) structure, or a structure associated with the REIT Investment Diversification and Empowerment Act (RIDEA) of 2007. The latter provides exposure for REITs to the financial performance and healthcare operations of the properties they acquire, while NNN structures essentially make the REIT a landlord that receives previously negotiated rent checks at a specified interval.[1]

Exhibit 1.h

Annualized Total Returns by REIT Type and the S&P 500

Periods ending 12/31/2019

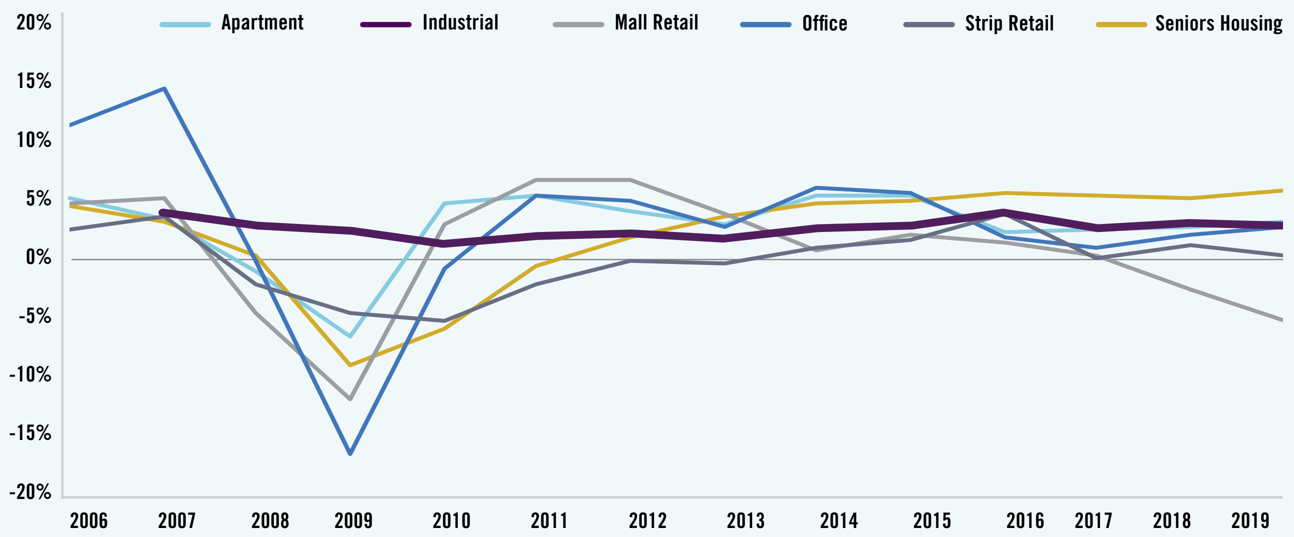


Source: FactSet, NAREIT, S&P

Exhibit 1.i

Commercial Real Estate Year-Over-Year Asking Rent Growth Trends

As of 12/31/2019

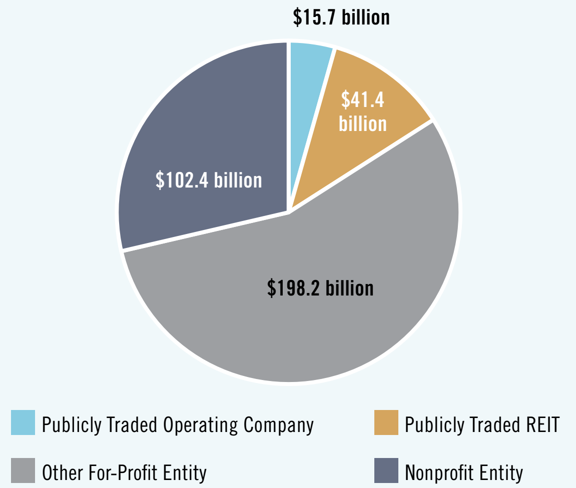


Source: NIC MAP® Data Service, Green Street Advisors

Exhibit 1.j

Implied Market Value of Seniors Housing Properties

As of 4Q19

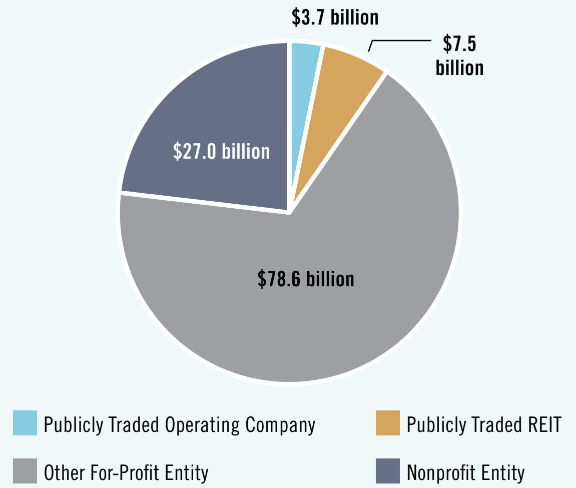


Source: NIC MAP® Data Service, NIC

Exhibit 1.k

Implied Market Value of Majority Nursing Care Properties

As of 4Q19



Source: NIC MAP® Data Service, NIC

The 10 nursing care operators in Exhibit 1.m control 13.0% of beds within majority nursing care properties in the 99 Primary and Secondary Markets.[1]

The 10 CCRC/life plan community operators in Exhibit 1.n control 22.8% of units in the 99 Primary and Secondary Markets.[1]

Exhibit 1.l
Largest Seniors Housing Operators in the 99 Primary and Secondary Markets
As of 4Q19

	Number of Properties Operated*	Number of Units Operated**
Brookdale Senior Living	472	43,756
Sunrise Senior Living	257	21,462
Atria Senior Living	173	21,278
Holiday Retirement	158	19,283
Five Star Senior Living	135	14,344
Senior Lifestyle Corporation	96	11,651
Capital Senior Living Corporation	82	8,695
Watermark Retirement Communities	42	6,938
Eclipse Senior Living	66	6,154
Leisure Care, Inc.	37	6,087
Share of Total Units among the 10 Largest Operators		**21.7%**

*Includes idepdendent living, assisted living, and memory care communities.
**Includes all units within the property. May also contain nursing beds.

Source: NIC MAP® Data Service

Exhibit 1.m
Largest Nursing Care Operators in the 99 Primary and Secondary Markets
As of 4Q19

	Number of Properties Operated*	Number of Units Operated**
Genesis HealthCare	215	27,394
HCR ManorCare	115	16,477
Sava Senior Care	91	11,298
Life Care Centers Of America	88	10,808
The Ensign Group, Inc.	77	8,615
CommuniCare Health Services	62	7,990
Consulate Healthcare	64	7,906
National Healthcare Corporation	40	6,264
Athena Healthcare Services	33	4,559
Saber Healthcare Group	42	4,319
Share of Total Units among the 10 Largest Operators		**13.0%**

*Includes nursing care communities.
**May include independent living, assisted living, or memory care units in addition to nursing care beds.

Source: NIC MAP® Data Service

Exhibit 1.n
Largest CCRC/Life Plan Community Operators in the 99 Primary and Secondary Markets
As of 4Q19

	Number of Properties Operated*	Number of Units Operated**
Erickson Living	18	23,855
Life Care Services LLC	44	17,587
Brookdale Senior Living	29	11,092
Five Star Senior Living	26	7,002
ACTS Retirement-Life Communities	15	5,739
Lifespace Communities	11	4,524
Covenant Retirement Communities	11	4,292
HumanGood	15	4,145
Presbyterian Homes & Services	12	3,549
Vi Senior Living	8	3,052
Share of Total Units among the 10 Largest Operators		**22.8%**

*Includes CCRC/life plan communities.
**Includes all units within the property, including nursing beds.

Source: NIC MAP® Data Service

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Minneapolis, Minnesota

IN THIS SECTION

Section 2

Emerging Trends and Observations

Throughout most of this document, NIC relies on data-driven observations to inform investors about the seniors housing and care property market. This section is different because it draws upon the judgment of industry participants to make observations and discuss emerging trends for which reliable empirical data may not be available. The observations are presented in the spirit of contributing to a timely and forward-looking report. The observations and trends fall into five broad areas: supply and demand, operating strategies, capital markets, labor markets, and regulations.

2.1 Supply and Demand

- **Capital for New Construction.** The historically strong operational and investment performance of seniors housing, expectations for strengthening demand due to demographic growth, and availability of capital have all helped fuel investment activity in the seniors housing market in recent years. Demand for existing high-quality seniors housing properties by institutional buyers and others has generally outpaced available transaction volumes and deal flow in recent years. This, in turn, has driven average transaction prices to near record high levels. These conditions have caused some investors to turn toward new development opportunities to grow their seniors housing portfolios in pursuit of higher investment returns.

  Despite a 6.4% increase in development costs in 2019, the construction market has remained generally very active, with new development focused on private-pay independent living, assisted living, and memory care. Assisted living construction remained elevated as a share of inventory at 6.8% in 4Q19, although that was down from a peak of 9.9% in 4Q17, while construction as a share of inventory in independent living was 5.8% of inventory in 4Q19. On the other end of the spectrum, construction of nursing care units as a share of inventory remained low at 0.5%.

  The rising costs of construction, longer construction schedules, changes of unit mix, complexity of projects, changing regulatory environments, and protracted labor shortages may prove to be mitigating factors going forward. As a result, some investors speculate that the best return opportunities may shift in the coming years toward acquiring failed development projects, or repositioning older properties through investment in capital improvement projects.

- **Addressing Affordability.** Industry participants continue to explore ways to make seniors housing and care more affordable to less affluent residents. Among these efforts, NIC awarded a research grant in 2017 to NORC at the University of Chicago, which published its results as an article in the *Health Affairs* journal in 2019. As evidence of interest in the topic of affordable care and housing options for seniors, the article was the fifth most read item in the prestigious journal that year. The research defined and quantified "middle market" seniors by their demographic characteristics as well as by their housing and healthcare needs now and in 2029. The study defined middle market as those Americans who have too much in financial resources to qualify for government support programs, such as Medicaid, but not enough to pay most private pay options for very long. As many baby boomers born between 1946 and 1964 have not sufficiently saved, there will be an increasing need for lower-cost seniors housing and care options.

While most new construction activity has been focused on private-pay, higher-end market-rate projects, some developers and operators have been innovating to address demand for more affordable seniors housing. New development approaches have been pursued to reduce costs, including redeveloping existing real estate, rather than ground-up new construction. Additionally, operational costs have been examined for innovative approaches to lower costs and provide more affordable care and housing options for seniors. (See Appendix D for more information on middle market opportunities.)

- **Age-Restricted Housing Development.** Age-restricted housing, also referred to as "active adult" or "55+" housing, is not a new concept, but has attracted renewed interest from developers and investors. Age-restricted communities do not directly provide care services, but rather offer lifestyle housing options for older adults, often centered on socialization and recreational activities. Historically, since personal care services are not provided, age-restricted properties have been traditionally distinct from the seniors housing continuum and considered to be a variation of multifamily housing and other residential real estate products. However, some investors who are active in the seniors housing industry or the multifamily housing sector are directing capital toward the development of these communities. Rationale for their investment interest includes a view that age-restricted housing may be in greater demand from the baby boomer generation based on the trend of seniors delaying entry into higher-service communities until they are older and have greater care needs. (See Appendix F for more information on the active adult opportunity.)

- **Product Obsolescence and Aging Seniors Housing Stock.** The stock of seniors housing inventory is aging. Indeed, more than 32% of the property inventory in the NIC MAP Primary Markets is at least 25 years old, while nearly two of every three properties were built prior to 2002. Only 25% of the stock is less than 10 years old. As a result, some of the country's older properties are approaching the end of their useful lives, which is causing investors and operators to explore alternative uses for obsolete properties. Some potential conversion strategies include changing design, layout, and unit counts. In addition, the age of the inventory is generating discussions about how to retain useful property life in older buildings and the appropriate amount of money to be spent on capital expenditures (Capex). The NIC Future Leaders Council (FLC) is working with NIC Leadership on a long-term project geared toward tracking various aspects of Capex with actionable data output.

- **Architecture and Design Trends.** Changes in architecture and design trends are influenced by four factors: demographics, consumer needs and preferences, economics, and technology. The goal is to develop flexible community designs that can easily be adaptive to change. Developers and operators continue to work together to create spaces with intelligent designs that improve resident satisfaction while also providing better health outcomes. The most challenging element of these changing trends is completing enhancements while maintaining market-specific cost structures. This is being accomplished by identifying more revenue-generating spaces within each property.

2.2 Operating Strategies

- **Growth of Provider Partnerships.** Healthcare reform, the growing number of seniors using managed care plans, and various demonstration programs are driving the integration of acute care, post-acute care, and long-term care. As the lines blur across the continuum of care, seniors housing and nursing care operators are identifying ways to partner with acute care hospitals, managed care companies, and other healthcare providers up and down the care continuum. For nursing care providers, the need for such partnerships is becoming clear. Financial incentives increasingly are being tied to producing better health outcomes and opportunities to improve payer mix and margins through relationships with hospitals and insurers. While seniors housing operators may also find a need for partnerships along the healthcare continuum as value-based payment models evolve and resident acuity increases, there are currently diverging strategies among operators, with some focusing on care and ancillary service offerings, while others are focusing on housing and hospitality services. (See Appendix L for more information on housing and healthcare.)

- **Technology Innovations.** There has been a growing interest in both complementary and potentially disruptive technologies that may allow seniors housing providers to achieve greater operating efficiency. From an operations perspective, new leads are being generated over the internet. IT systems and remote monitoring of residents is generating staff efficiencies. Payers throughout the healthcare continuum are relying on technology to track outcome metrics, which are becoming more important as quality has become a cornerstone of financial success.

From a health and wellness perspective, telehealth and virtual care systems have the potential to reduce healthcare costs and improve healthcare coverage by allowing instant video conferencing at call centers with live doctors. Smart phones and appliances, remote sensors, handheld devices with medical applications, and mobile personalized connectivity applications and software systems have the potential to better allow aging in place, independence, and virtual socialization.

On average, seniors are older and frailer at the time of moving into a seniors housing community today than they were in the past. The trend implies a current shift in consumer decision-making for seniors housing toward more needs-driven factors that arise with age and declining health rather than lifestyle-driven factors. Technology is playing a role in improving care and efficiencies at senior care communities. (See Appendix G for more information on new technologies and innovations.)

- **Data Sharing, Data Privacy.** Data collection is exploding in the seniors housing industry, but there are concerns surrounding how data is shared. Collectively, the industry has the opportunity to use collected data to help predict trends, while maintaining privacy needs.

  In the Data Breach Investigations Report for 2019, Verizon ranked ransomware attacks as one of the biggest threats for the year, specifically in the healthcare sector. Hackers are attracted to Personally Identifiable Information (PII) because Social Security numbers and birth dates can be used to create fake resident profiles for illegal use. Hackers also use this information to forge prescriptions for opioids and other narcotics. Operators need to continue to improve their cyber security measures to make sure they protect valuable information.

2.3 Capital Markets

- **Joint Venture Preferences.** Historically, REITs were exclusively real estate owners and sought triple net lease (NNN) structures with operators. In the past decade or so, many REITs and operators have shifted away from traditional NNN structures and have actively pursued new structures for their business relationships. These structures include joint venture structures through the REIT Investment Diversification and Empowerment Act of 2007 (RIDEA) for their seniors housing properties, which allows them to share in the operating income along with their operating partner. Not all REITs favor this structure because of the additional risks created through exposure to operations. To give themselves more control, REITs have also begun to buy stakes in operators outright. Joint ventures between private equity firms and operators have become more common, while straight fee-management arrangements have waned.

- **Aggressive Underwriting.** With an abundance of capital in the market, much of which is being driven by large private equity firms, investors are in some cases taking more risk for the same opportunities, which is evidenced by historically low acquisition cap rates and higher price per unit metrics. Furthering this competition has been an influx of non-traditional debt financing sources, which have less oversight than banks. Like all asset classes, favorable conditions for capital markets have allowed for aggressive underwriting, which could subject those investments to economic risk, especially in lower acuity settings that are less needs-based and more exposed to rent compression.

- **Economic Cycle Resiliency.** While higher wage rates for caregivers and other staff have presented headwinds for operators (see Section 2.4), seniors housing has been resilient to market volatility and the overall economic cycles. Its needs-based nature has resulted in sustained demand, and as such, significant investor capital has been attracted to the space over other real estate asset classes, though concerns of oversupply exist in certain metropolitan markets**.**

2.4 Labor Markets

- **Rising Cost of Labor.** Through year-end 2019, U.S. labor markets continued to tighten, with the unemployment rate at near 50-year lows of 3.5%. Tight labor markets translated into upward pressures on wage rates, which have been further influenced by state legislatures across many states that have mandated increases in the minimum wage. Bureau of Labor Statistics (BLS) and NIC MAP data for 4Q19 show wage growth as measured by average hourly earnings, far exceeds asking rent growth for assisted living properties. Since labor costs are typically the largest expense of operating a seniors housing property, these changes can have a significant impact on operating margins.

- **Labor Shortages.** Shortages of labor have affected the seniors housing and care sector across the country. This has been particularly challenging in the recruitment of executive directors, nurses, and care assistant positions. Moreover, there continues to be growing competition among operators to hire experienced staff from incumbent operators in response to a shortage of qualified labor. Projections from Argentum, University of California, and others estimate the need for 1 million to 2.5 million additional long-term care workers by 2030. The limited availability of labor within local markets is becoming a key investment criterion for operators considering the acquisition or development of a seniors housing property.

- **Recruitment and Retention.** Employee recruitment and retention is a key concern in the seniors housing industry because the labor market continues to be competitive and the cost of labor turnover can be high. Some companies have begun investing in high school training programs to try to grow the seniors housing work force in their communities, and many other companies have strategic plans to address this challenge. With respect to retention of employees, operators have invested in creative benefits to offer their staff as a strategy for retaining talent and recruitment, including subsidized housing for frontline staff, meals, transportation, and childcare.

2.5 Regulation

- **CMS Strategies.** The Centers for Medicare & Medicaid Services (CMS) continues to develop new strategies to adequately manage healthcare access and costs as the U.S. approaches a time of unprecedented growth in the population of older adults. In July 2018, CMS finalized a new case-mix classification model, the Patient Driven Payment Model (PDPM), that became effective October 1, 2019, and has been used under the Skilled Nursing Facility (SNF) Prospective Payment System (PPS) for classifying skilled nursing patients in a covered Part A stay. This revised payment methodology is driven by the patient's clinical characteristics rather than volume-based services. One significant element of PDPM is a limitation on the use of group and concurrent therapy combined at 25% of all therapy provided to the patient, per discipline. Due to this limitation, immediately following the implementation of PDPM, there were reports of a significant number of therapist layoffs and cuts in therapy hours at skilled nursing properties.

- **Growing Market Share for Managed Care.** Medicare Advantage plans continue to increase their market share, as enrollment in Medicare Advantage has nearly doubled over the past decade. There is expected to be an increase in Medicare Advantage Special Needs Plans (SNP), which serve frail, disabled, and chronically ill patients. SNPs focus on emphasizing primary care, chronic care management, and integrated care services.

- **Fragmented Seniors Housing Regulation.** While the skilled nursing industry is highly regulated at federal and state levels, regulation of assisted living and memory care communities differs by state. Despite the large amount of public funding in assisted living communities, there is little to no federal oversight, leaving regulation to the individual states. Regulation differences state by state include, but are not limited to, staffing ratios, registered nurse employment requirements, and staff credentialing. Investors should seek awareness of local regulatory requirements and understand how they affect the costs and underwriting of a seniors housing property. (See Appendix N for more information on state regulations.)

2.6 COVID-19*

With little doubt, the most significant emerging trend for 2020 is the COVID-19 pandemic. COVID-19 is the infectious disease caused by the recently discovered coronavirus. This new virus and disease were unknown before the outbreak began in Wuhan, China, in December 2019. The outbreak was declared a Public Health Emergency of International Concern on January 30, 2020. Due to the COVID-19 pandemic, the U.S. has experienced a historic stock market crash, record federal government spending, eye-popping spikes in unemployment insurance claims, and an economic cycle that may prove to be the worst since the Great Depression. COVID-19 is a novel disease, which causes viral respiratory illnesses and other symptoms through person-to-person transmission.

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Current data indicates that the virus is mainly transmitted during close proximity—approximately within 6 feet—to an infected person, often via exposure to respiratory droplets produced when the carrier coughs or sneezes. Seniors and individuals with pre-existing medical conditions such as diabetes, Chronic Obstructive Pulmonary Disease (COPD), and heart disease are at a heightened risk of developing severe complications.

The COVID-19 pandemic has implications for operators, developers, and capital providers across the seniors housing and skilled nursing sectors. The recent spread of the coronavirus around the world is justifying significant concern among senior living operators and raising questions about how to prepare for and respond to the disease as it affects residents, staff, and visitors. This concern is exacerbated by the fact that seniors tend to be more vulnerable to communicable diseases and live in close quarters with others at a community, dining together and participating in group activities.

**As of August 1, 2020, approximately 18 million people worldwide had been infected with COVID-19, with approximately 700,000 deaths worldwide, including approximately 160,000 in the U.S.*

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The complete NIC Investment Guide is available for purchase at store.nic.org.

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