U.S. Seniors Housing

2023 Investor Survey Report

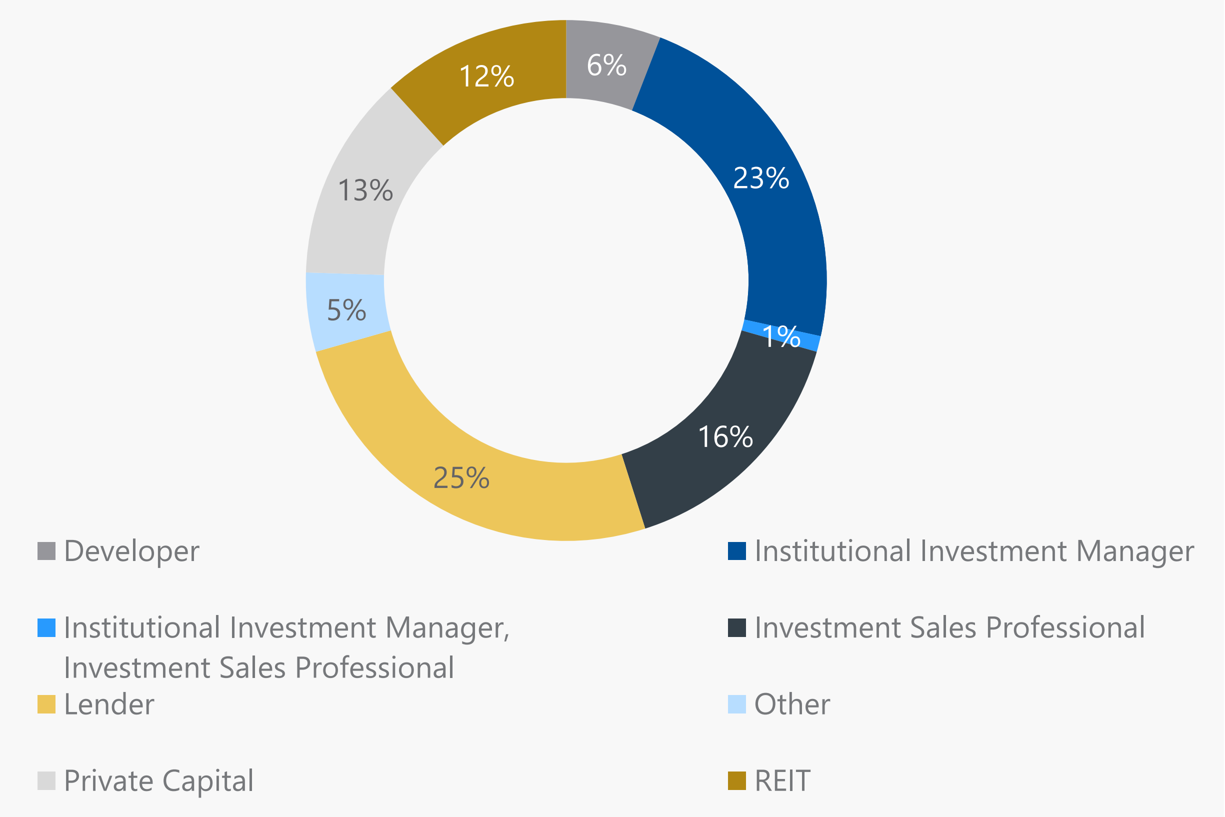
PARTNER Valuation Advisors

Our Survey

Completed in September 2023, this is the inaugural edition of our Seniors Housing Investor Survey Report. The sample set for this survey surpassed 100 respondents, encompassing some of the most influential leaders in the seniors housing industry including lenders, investors, developers, and investment sales professionals.

The purpose of the survey is to identify current trends in the seniors housing sector, which has seen numerous changes due to the impacts of increased interest rates/cost of debt and inflation. These factors led to declining transactional and lending volume in the first half of 2023.

Figure 1. Survey Participants by Categories



Executive Summary

The seniors housing industry is well-positioned for growth due to the foundational factors of limited new supply and ongoing strong demand; however, the broader capital markets have become less appealing with the increasing cost of capital.

The Federal Reserve seems inclined to maintain a vigilant stance on inflation, which means that interest rates are likely to remain high going into 2024. This sets the stage for what we expect will be increased headwinds in the investment real estate sector compared to the previous cycle. Despite these current challenges, the industry has had occupancy gains for nine consecutive quarters. Given the robust demographic trends and limited supply, the seniors housing sector will offer an attractive investment environment for committed, long-term investors with strong operational relationships.

Seniors housing trends:

- The most preferred investor return for seniors housing was leveraged Internal Rate of Return (IRR) followed by cash-on-cash returns.
- In terms of levels of financing, over 50% of respondents prefer 65-70% Loan-to-Value (LTV), but over 40% are now seeing loan limits of 55-64% due to more conservative lending requirements.
- Capitalization rates are expected to continue to increase over the next 12 months. Thirty five percent of the respondents are expecting the rates to increase in excess of 25 basis points (bps).
- Seniors housing assets were typically on the market for 9 to 12 months from the day of listing to the day of closing, according to the majority of respondents.
- The top concerns of survey respondents were related to the availability of financing and increased interest rates.
- The consensus of respondents indicated that property values have declined due to the increased cost of capital and increased cap rates.
- Respondents indicated that the biggest investment opportunities in the seniors housing sector were related to active adult and assisted living communities.

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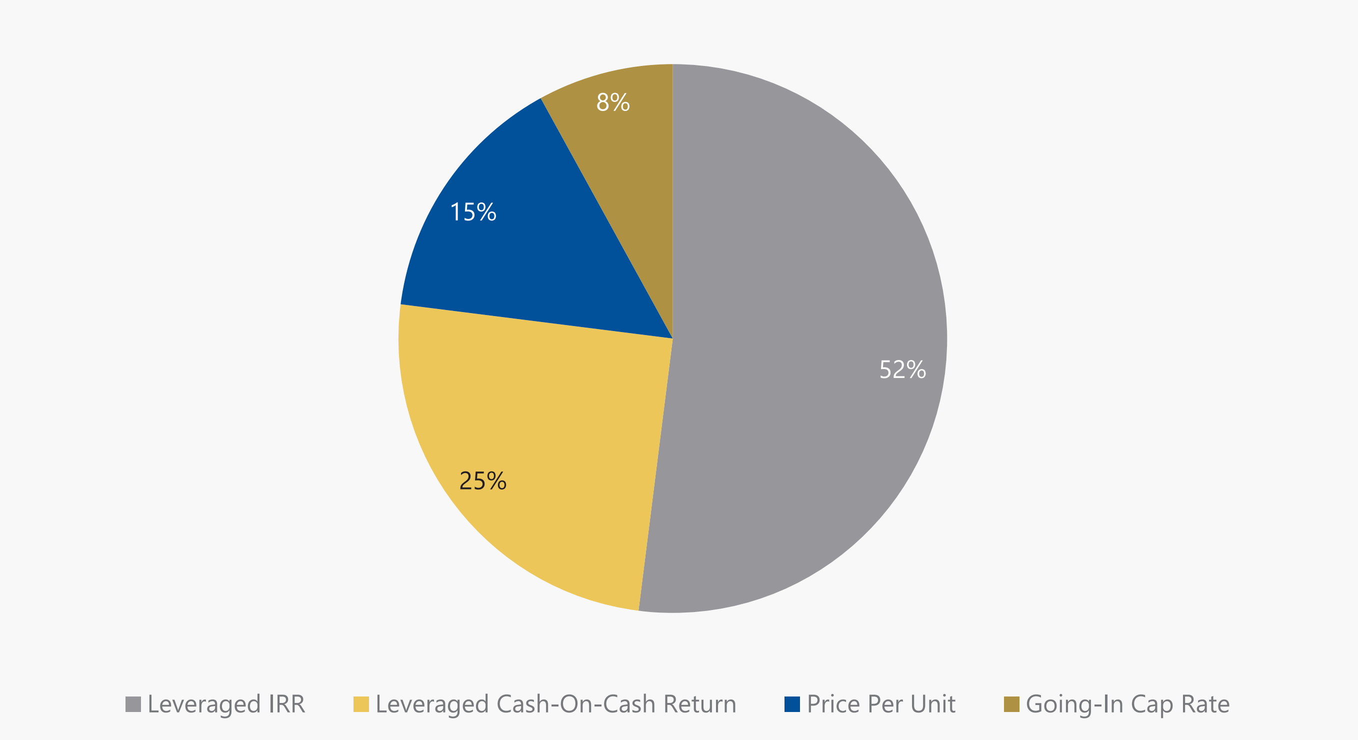
Investment Return Preferences

Investor sentiment indicated that the most preferred investment return measurement in seniors housing was by the leveraged IRR at 52% followed by leveraged cash-on-cash return at 25%.

Figure 2. The Most Reliable Measurement of Investment Return



Áegis Living Greenwood

Loan-to-Value Sizing

Rising inflation and fixed expenses create additional capital needs for borrowers, translating into higher LTV demands. These shifts in market circumstances and borrower requirements result in a more cautious credit strategy from lenders, who are less inclined to concede to higher loan-to-value ratios.

52% 65-70%

45% 55-64%

3% >70%

Historically, lenders in the seniors housing sector take a conservative approach to LTV ratios. Prior to 2023, lenders typically capped the LTV at 70-75%, to mitigate risk. This ensured that there was a significant equity cushion in the property.

According to 52% of respondents, the level of financing (LTV sizing) most often seen falls within the range of 65-70%, while 45% of respondents indicated an LTV range of 55-64%. This shift reflects more conservative lending standards due to concerns about decreased property valuations.

Borrowers can potentially mitigate risk and secure more favorable LTV terms by offering additional collateral, improving property performance, or partnering with experienced operators in the seniors housing sector.

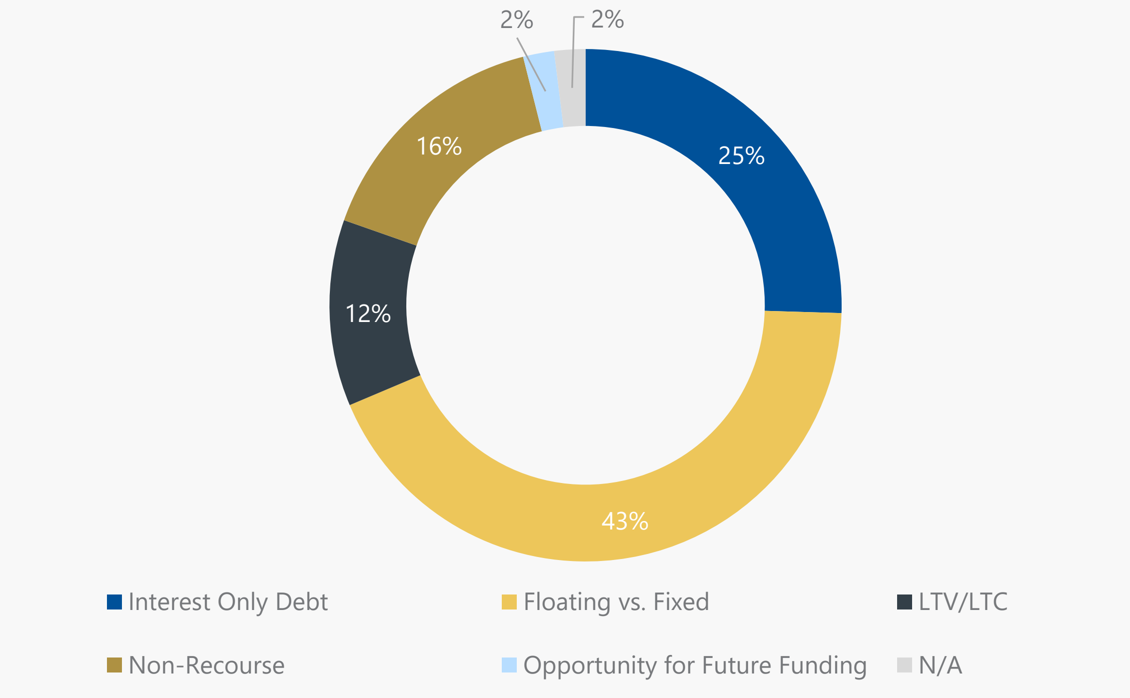
The balancing act in LTV and loan terms is relative to current market conditions and availability of capital. Fixed rates have historically dominated loan terms due to the low base rate indexes over the last 16 years.

As the Federal Reserve has increased rates, causing indexes to reach record highs, floating rates have become attractive for borrowers. Lenders have the ability to adjust loan rates from floating to fixed as borrowers are looking for flexibility until rates normalize.

As new investors/borrowers consider additional avenues of entry, interest-only loans become ideal to conserve short-term cash flow while upfront/ramp-up expenses give way to stabilized operations.

Financing Terms Preferences

Figure 3. Most Important Financing Terms When Choosing a Lender/Loan



Non-recourse loans have become more of the standard in commercial real estate; however, as credit concerns escalate, lenders will consider alternate ways to offset risk.

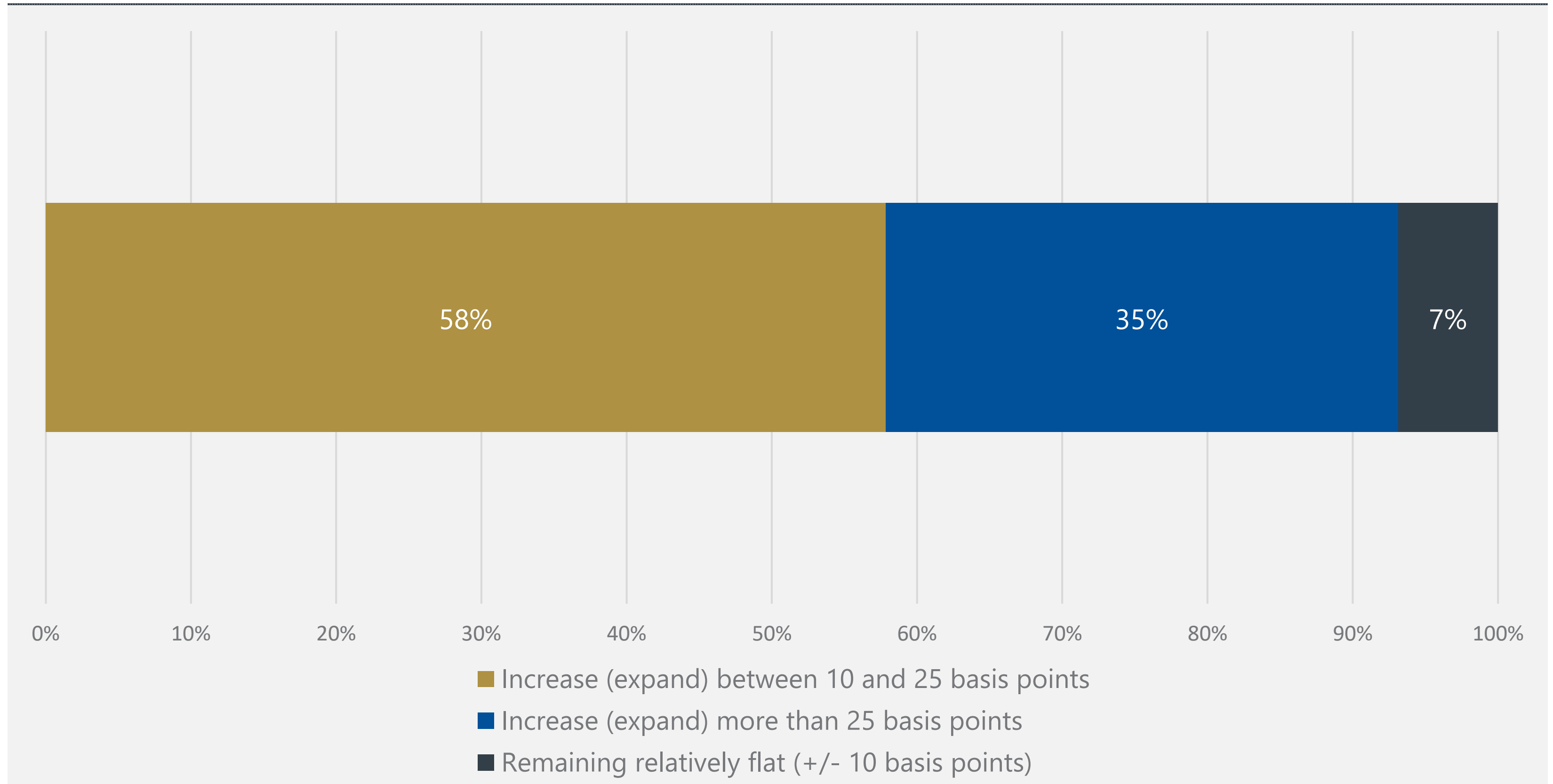
Respondents indicated their priorities for financing terms by highlighting the most important aspect when choosing a loan or lender. Floating vs. fixed debt was indicated as the most important, followed by interest-only loans. Non-recourse debt and LTV/Loan-to-Cost (LTC) options combined represented roughly a quarter of the respondents.

MorningStar Senior Living of Arvada

Capitalization Rate Trend

The majority of respondents anticipated that capitalization rates would continue to rise over the next 12 months. Just 7% of respondents anticipated capitalization rates to remain relatively flat. Fifty eight percent of respondents expected capitalization rates to increase by 10 to 25 basis points (bps), while 35% of respondents expected cap rates to increase over 25 bps in the next 12 months.

Figure 4. 12- Month Outlook for Seniors Housing Capitalization Rates



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Marketing Time

Respondents were asked to indicate a typical marketing time for seniors housing assets. Marketing time was defined as the number of months between the date a property is listed through the date of closing. The majority of respondents (62%) indicated marketing time was between 9 to 12 months, while 37% indicated a 6 to 9 month marketing time.

62% 9-12 Months

37% 6-9 Months

1% 3-6 Months

Top Concerns

When considering market fundamentals that could negatively impact the industry over the next year, respondents ranked the availability of financing and rising interest rates among the highest of their concerns. Availability and/or the cost of workforce were ranked as less concerning.

It's essential for stakeholders in the seniors housing and healthcare industry to remain vigilant, adaptable, and prepared to address these challenges. Strategies for managing risks and seizing opportunities are key to navigating potential negative impacts effectively.

1. Debt Capital Markets (availability of financing and/or interest rates)
2. Competition of Capital Placement
3. Development Costs
4. Construction Activity (new supply)

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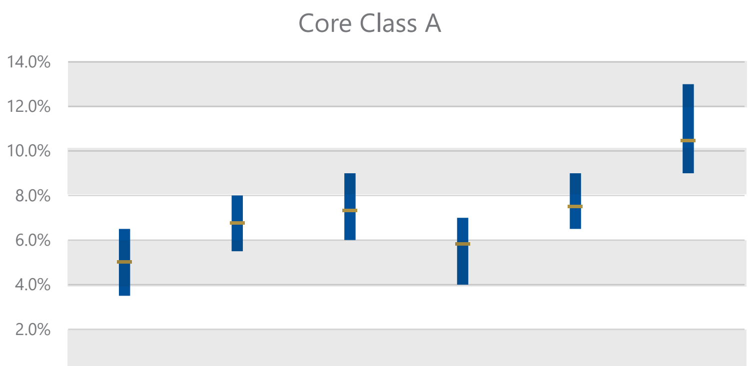
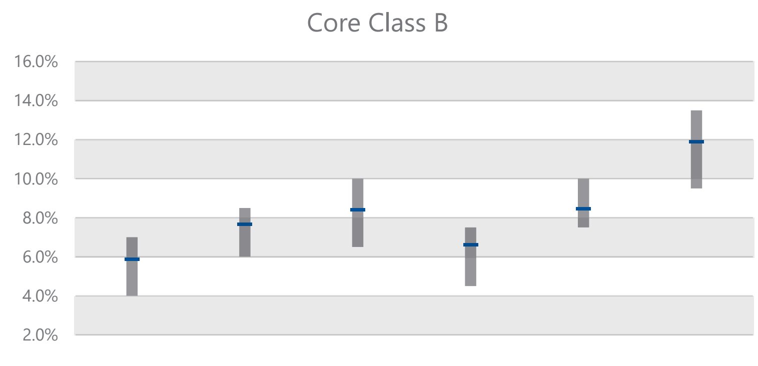
Core Capitalization Rates

Figure 5. Appropriate Capitalization Rates for Core or Primary Market Locations



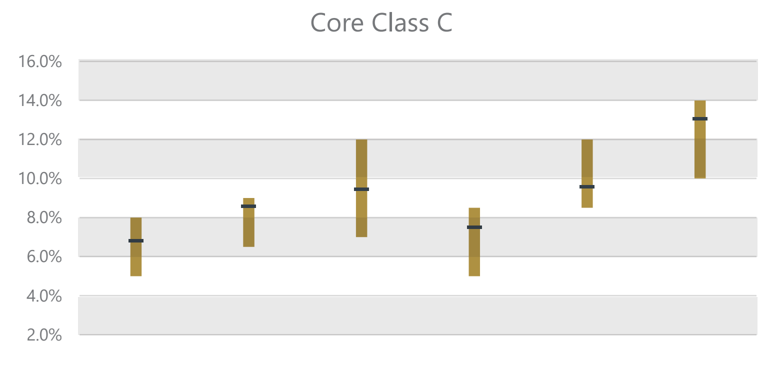
	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	3.5%	5.5%	6.0%	4.0%	6.5%	9.0%
MAX	6.5%	8.0%	9.0%	7.0%	9.0%	13.0%
– AVG	5.0%	6.8%	7.3%	5.8%	7.5%	10.5%

– AVG



	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	4.0%	6.0%	6.5%	4.5%	7.5%	9.5%
MAX	7.0%	8.5%	10.0%	7.5%	10.0%	13.5%
– AVG	5.9%	7.7%	8.4%	6.6%	8.5%	11.9%

– AVG



	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	5.0%	6.5%	7.0%	5.0%	8.5%	10.0%
MAX	8.0%	9.0%	12.0%	8.5%	12.0%	14.0%
– AVG	6.8%	8.6%	9.5%	7.5%	9.6%	13.1%

– AVG

Respondents were asked to select the most appropriate stabilized capitalization rate range by asset class for core/primary and non-core/secondary locations. The selections were based upon year one stabilized net operating income, inclusive of market level management fees and replacement reserves.

Going forward into 2024, it is anticipated that capitalization rates will either increase or stay stable across all seniors housing care categories. According to the survey participants, active adult and independent living communities are projected to have the lowest cap rates, with active adult communities expected to have the lowest rates among all the care levels that were examined. The spread between Class A and Class B rates averaged 84 bps for active adult and 79 bps for independent living.

The bifurcation of assisted living and memory care in the primary markets shows an increasing spread between Class A (73 bps), Class B (78 bps), and Class C (102 bps). The stand-alone memory care market currently faces unique challenges that include unstable occupancy levels and elevated labor costs, but at amplified levels due to some of the inherent characteristics of memory care assets [e.g., shorter length of stay, smaller properties, more labor intensive due to higher acuity of residents]. With relatively thin margins and fluctuating occupancy rates, memory care assets tend to have volatile net operating incomes. For these reasons, investors have a very challenging time owning, operating, and financing memory care assets.

Capitalization rates for nursing care were the highest of the segments surveyed. The spread between Class A and Class B rates averaged 144 bps.

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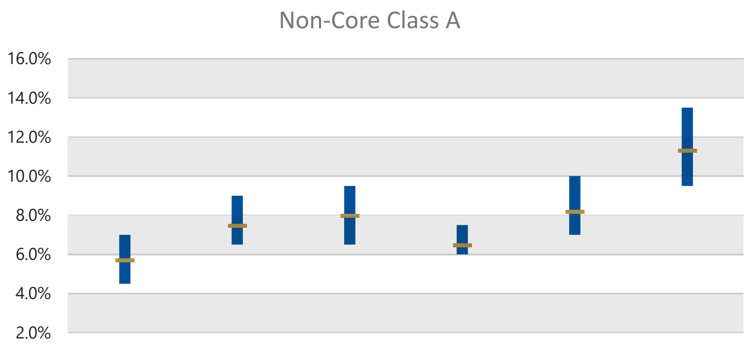
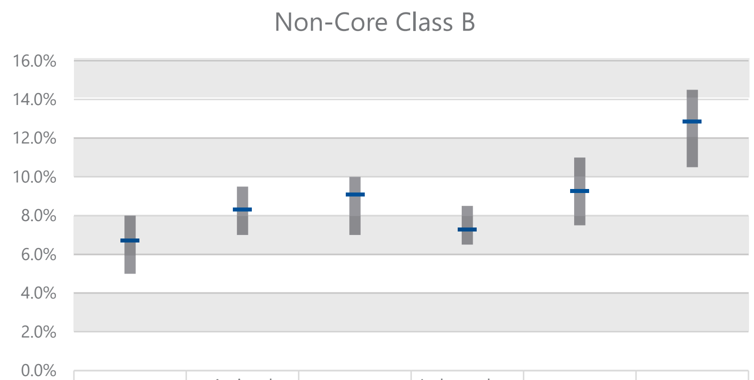
Non-Core Capitalization Rates

Figure 6. Appropriate Capitalization Rates for Non-Core or Secondary Market Locations



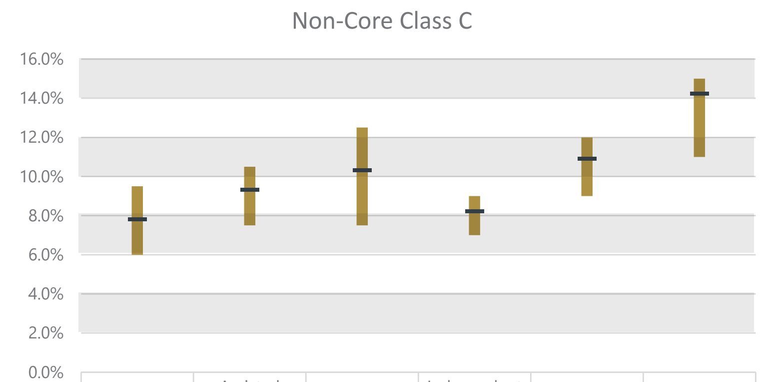
	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	4.5%	6.5%	6.5%	6.0%	7.0%	9.5%
MAX	7.0%	9.0%	9.5%	7.5%	10.0%	13.5%
AVG	5.7%	7.5%	8.0%	6.5%	8.2%	11.3%

AVG



	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	5.0%	7.0%	7.0%	6.5%	7.5%	10.5%
MAX	8.0%	9.5%	10.0%	8.5%	11.0%	14.5%
AVG	6.7%	8.3%	9.1%	7.3%	9.3%	12.9%

AVG



	Active Adult	Assisted Living	CCRC/LPC	Independent Living	Memory Care	Nursing Care
MIN	6.0%	7.5%	7.5%	7.0%	9.0%	11.0%
MAX	9.5%	10.5%	12.5%	9.0%	12.0%	15.0%
AVG	7.8%	9.3%	10.3%	8.2%	10.9%	14.2%

AVG

The capitalization rate spreads between core and non-core locations for Class A and Class B assets were generally 70 to 80 bps while spreads were higher for Class C assets ranging between 75 to 100 bps. In non-core locations, active adult and independent living segments still had the lowest capitalization rate ranges, with nursing care representing the highest cap rate segment.

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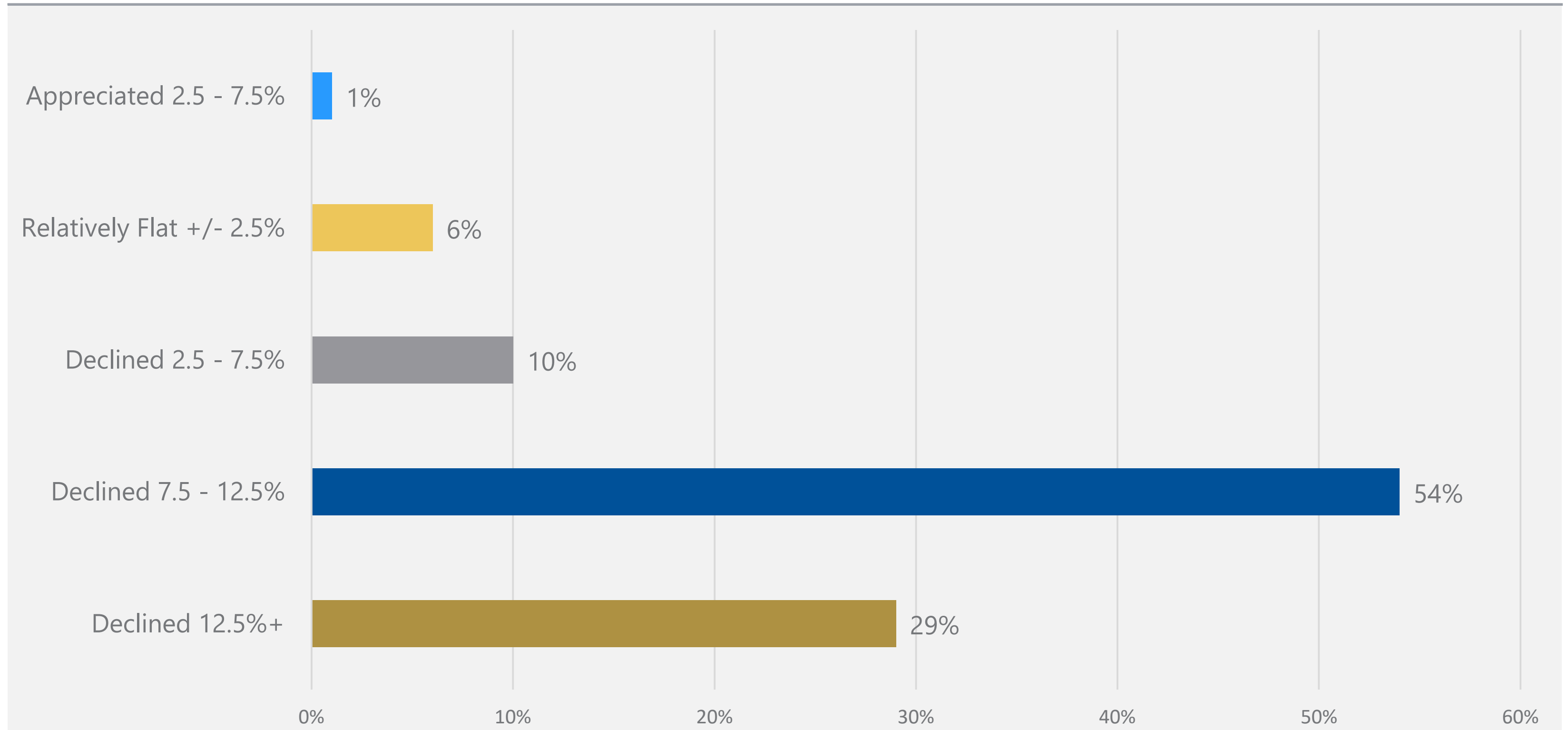
The Ridge Pinehurst

Property Value Change

There has been a consensus that property values have declined due to the rising cost of capital and increasing capitalization rates. However, many seniors housing properties have reported annual rent growth well in excess of 3%, which has helped to mitigate the overall impact to property values. Nonetheless, 54% of respondents felt that property values had declined 7.5-12.5% over the past 12 months with an additional 29% of respondents indicating a decline greater than 12.5%.

Figure 7. Total Property Value Change for Seniors Housing Properties Over the Past 12 Months



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Investment Opportunities

The active adult and assisted living segments were viewed as the biggest opportunities for investment over the coming year by 54% and 33% of survey respondents, respectively.

54% Active Adult

33% Assisted Living

13% Others

The growth of active adult communities is driven by a combination of demographic trends, changing preferences among baby boomers compared to the prior generation, and the limited amenities and services these communities offer. As the baby boomer population continues to age, it is likely that this segment of the seniors housing market will continue to expand and evolve to meet the needs and desires of retirees.

This generation is living longer than previous generations, which increases the likelihood of developing chronic conditions over time. Additionally, advancements in medical technology have led to improved diagnosis and management of chronic conditions, allowing more baby boomers to live with these illnesses, thereby increasing their prevalence. This is one of the driving factors behind the investment interests in assisted living communities.

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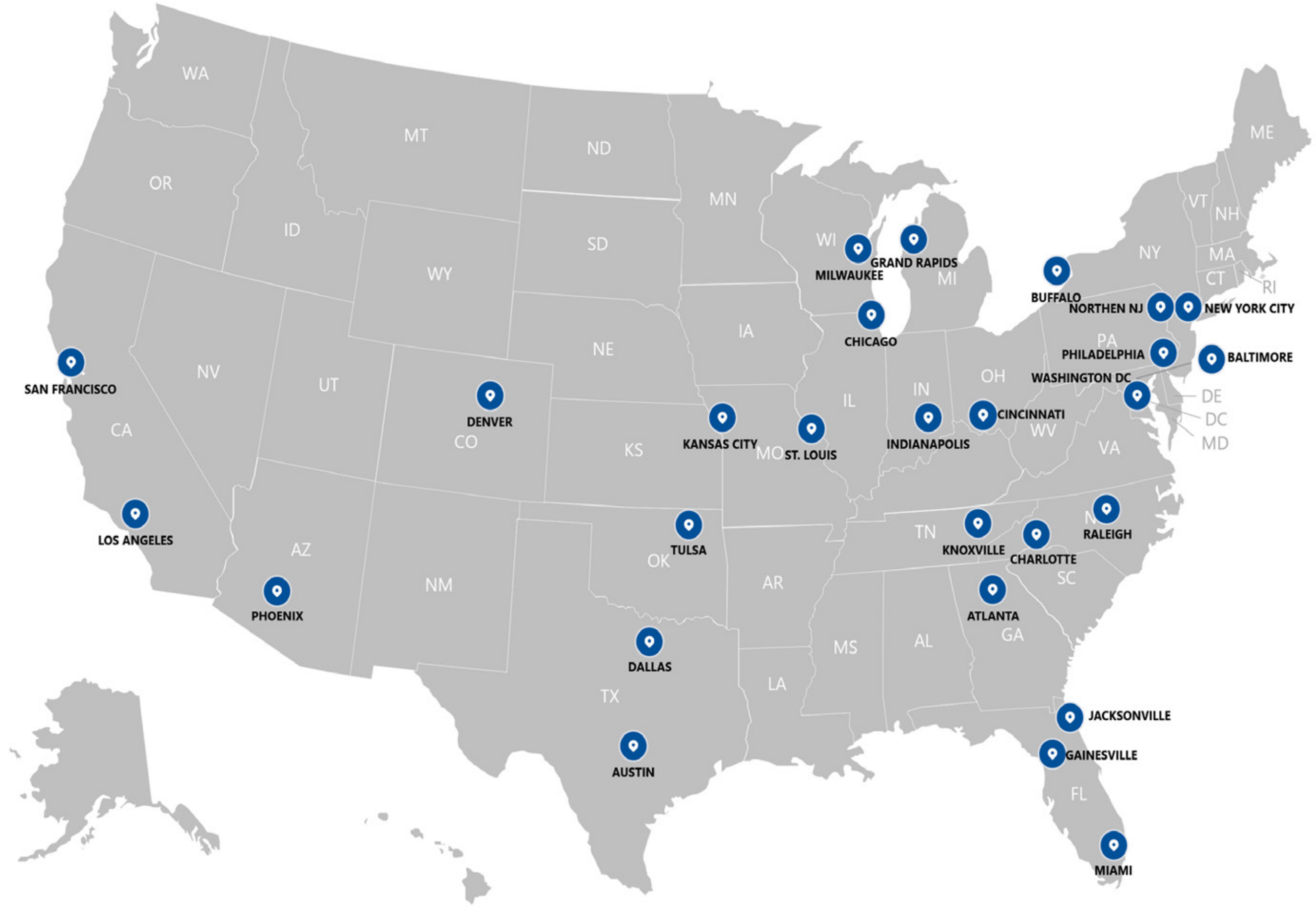

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