National Investment Center for Seniors Housing & Care

2015 INSIDER NEWSLETTER

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In the Insider January 2015 Issue

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Industry Leaders Look Ahead to 2015: Part 2

The seniors housing market is expected to continue to improve, according to a September survey of industry executives conducted by National Investment Center for Seniors Housing & Care (NIC) and National Real Estate Investor (NREI). Most survey respondents believe occupancies and rents will rise. About half expect the volume of seniors housing property sales to increase, while another 46 percent think it will remain the same.

To provide more in-depth commentary, we asked a handful of the executives profiled in the NIC Insider over the last year for their thoughts on several important questions facing the industry in 2015. Here's a recap of their comments.

> *"Understanding the incredibly dynamic health care landscape will be a challenge for every player as they make their plans for 2015 and beyond."*
>
> -Joel Treffert, Aptura

NIC: Most experts expect an increase in new development. Will this be a cause for concern for capital providers in 2015, or are we still very much on the upward slope of the cycle?

Joel Treffert, executive vice president and general manager, Aptura, the design and development arm of Milwaukee-based Direct Supply: Opinions differ here, but we remain bullish about development in nearly every seniors housing segment. Long-term demographics attract the most attention, but other underlying fundamentals are strong as well. The best option for everyone is to create enough of the right product to attract new customers to the market. We believe improved penetration rates could support increased development for a long time to come. If there is a contraction in the next few years – a likely occurrence – it should be fairly short lived.

Justin Hutchens, CEO, National Health Investors, Inc., a health care REIT based in Tennessee: New supply risk is evident in the assisted living and memory care categories. The key is to be very in tune to local market fundamentals before entering a new market.

Lauralee Martin, president and CEO, HCP, a fully-integrated REIT, based in Irvine, Calif., that primarily invests in real estate serving the health care industry: New supply during the great recession was muted while demand continued to increase with the aging population. As a result, the overall market remains quite healthy. We do see significant development in low-barrier-to-entry markets where the development decision may not be based on supply/demand fundamentals. As a result, there will be pockets of concern, but one needs to look at the micro-markets and not paint a broad brush across an entire market. For example, Chicago and Houston are seeing large increases in new supply relative to other markets, but certain sub-markets in Chicago and Houston are under-supplied. New isn't always better. Location and the operator are both very important. A well-located property, that is well maintained and well-managed, will effectively compete in the face of new supply.

Brian Beckwith, CEO, Formation Capital, a private investment firm, based in Georgia, specializing in seniors housing and care, post-acute and health care real estate investments: Development has certainly increased and the activity levels are high. We still believe the industry is able to absorb the product in the pipeline, but the dynamics of a local market are the most important, as always.

Sheila Miller, director of seniors housing production and lender relationships, Fannie Mae, Washington D.C.: I think we are still on the upward slope of development cycle, but we are watching activity. It has been dispersed throughout the country, not in one particular market, but we are monitoring it closely. We are starting to see and hear from some borrowers looking at new construction that it's getting difficult to find contractors.

Steven Schmidt, national director, seniors housing group, Freddie Mac, Chicago: When you look at NIC data, annual absorption and inventory growth are in good balance in independent and assisted living. But freestanding memory care has seen occupancy drift down since 2010, from about 89 percent to 85.5 percent. Independent and assisted living have generally been increasing their occupancies since 2010. Annual inventory growth of memory care was 9.0 percent, according to NIC MAP's third quarter 2014 report. That compares to 3 percent for assisted living and 0.8 percent for independent living. I've heard anecdotally of a few cases where memory care is being converted to assisted living. But overall, I'm not too concerned about overbuilding. The last time the industry had overbuilding was in late 1990s before NIC had a robust data set. Investors today know where there's construction and can't ignore it.

NIC: What is the biggest challenge facing the industry in 2015?

Treffert: Understanding the incredibly dynamic health care landscape will be a challenge for every player as they make their plans for 2015 and beyond. We know changes are coming with bundled payments and the continued evolution of ACOs. Predicting the future may not be possible, but remaining nimble enough to navigate a variety of scenarios should be the goal of every operator.

Hutchens: Interest rate uncertainty is my biggest concern for 2015 given the direct relationship between cap rates and interest rates. As rates rise, cap rates will follow, but any delay will slow down deal flow while valuations get sorted out.

Martin: Talent. At the community level, hiring and retaining leadership is critical. Strong executive directors are a significant success factor for a community, as are program directors, marketing directors and care givers.

Beckwith: For the first time in a while, the biggest risks for the industry luckily don't seem to include material reimbursement changes. The biggest risk seems to be managing the exuberance and the aggressiveness that can come with very strong access to capital and new entrants to the market.

Miller: Owners and operators are looking to grow, but it's difficult to acquire assets. REITs and institutional players are running up acquisition prices. It's more challenging for small and mid-size operators to find properties in a reasonable price range to make it work for them.

Schmidt: Short term, the concern is overbuilding in select markets—both what is under way and what is permitted. Longer term, the challenge is to create affordable housing for seniors. As with college education, you reach a point where people can't afford it. We're catering to the upper quartile or 50 percent of the senior population in terms of income. If you want to grow, you don't want to price yourself too high. But I don't see anything on horizon technologically to have an impact on operating expenses. This is a very labor intensive business, and it takes kind and dedicated people to care for seniors. We would love to work with those who have interesting, new models in that respect.

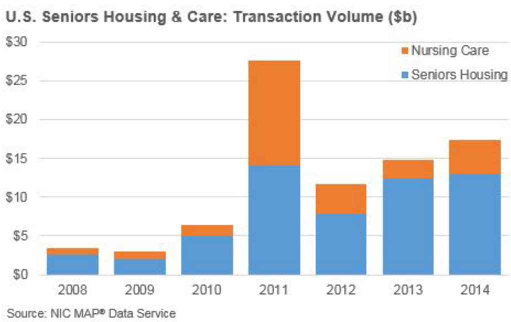
Didn't catch Part 1? Read more on what top executives in the industry think of what's to come in 2015 in the first part of this two-part series.

Transaction Market Ends Year on Strong Note

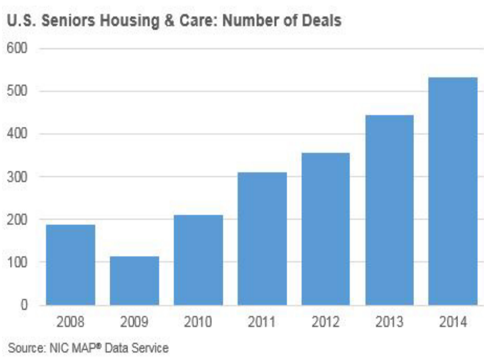
More than 500 Deals Closed in 2014

The robust investment activity in seniors housing and care continued through the end of the year, with preliminary figures showing nearly $4 billion in property sales during the fourth quarter. Overall, more than $17 billion in seniors housing and care properties were acquired in 2014, up nearly 20% from the previous year.

Sales volume in 2014 was second only to 2011's record total of $27.6 billion, which was dominated by a handful of multi-billion dollar REIT transactions. In terms of the number of deals, 2014 was the most active year on record, with more than 500 deals closed.



The market continued to be dominated by the publicly-traded companies, with their volume totaling nearly $10 billion last year. Private companies also remained very active, with their acquisitions at more than $5 billion in 2014. Institutional investors continued to be the smallest investor type, but their activity has been consistently growing over the last few years. In 2014, institutional players acquired $1.8 billion in seniors housing and care real estate, up 13% from the previous year.



Future Leaders Council: New Member Spotlight

Susannah Myerson, vice president, Wells Fargo Bank, CRE– Senior Housing Finance

An industry advocate with particular expertise in market feasibility, Myerson joined the FLC in 2014 seeking to explore best practices and identify new initiatives in an effort to advance the industry. Myerson recently spoke with current FLC members, Amy Coppens of Senior Resource Group (SRG), and Melissa Owens of Elmcroft Senior Living. Here is an edited transcript of the conversation which highlights Myerson's goals for the FLC.

FLC: What do you hope to gain from your term with the FLC? How would you characterize your experience so far?

Myerson: I hope to gain a deeper understanding of forces affecting the industry, and how those forces will help shape the industry in the next 10 to 20 years. And I hope to be part of the group that helps shape the industry!

What I have experienced so far with FLC is great. I am enjoying getting to know others at NIC and discussing topics for conferences, generating new ideas and helping to advance the mission of NIC.

FLC: What's the biggest trend impacting senior living today?

Myerson: I think affordability is a major issue. Millions of age 75+ households have incomes that are too high for them to qualify for affordable housing, yet too low for them to comfortably afford market-rate seniors housing. I think there is a huge need for the development of moderate priced seniors housing that operates in a way that does not sacrifice quality.

FLC: How do you hope to impact the industry through the FLC?

Myerson: One of the committees I am serving on is the University Internship Program, which I think is so important. I really enjoy helping to get this industry in front of students and attracting the best and the brightest to this business. Most college students probably have never considered working in the seniors housing field – much less visited a facility. But once they realize all the intricacies of the business, the rewarding career opportunities, and the great growth potential of the industry, I think they'd certainly be interested.

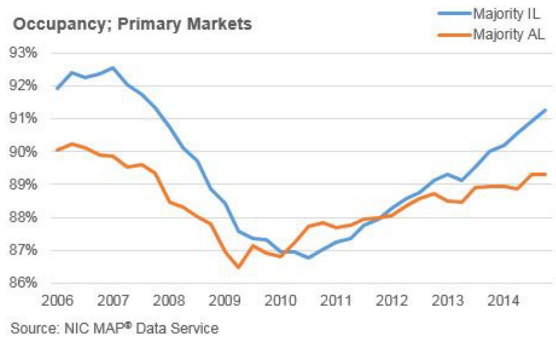
FLC: Is there any specific issue you hope to address during your tenure?

Myerson: That is a good question. One issue I'd like to help address is broadening the scope of the industry – both in terms of product type (such as including age-restricted apartments or co-housing communities) and in terms of geography (looking at seniors housing in other countries).

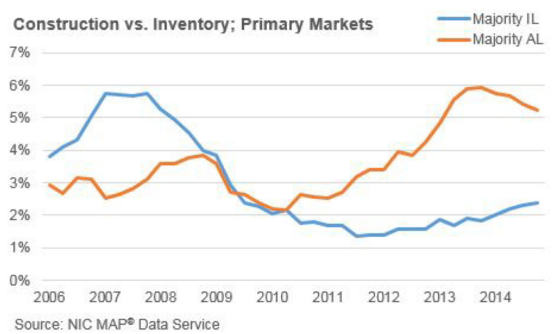
Independent Living Drives Fourth Quarter Occupancy Gains

Assisted Living Occupancy Flat Despite Solid Absorption

Independent living occupancy continued its recovery during the fourth quarter, while assisted living occupancy remained flat despite a healthy absorption rate. During the fourth quarter, independent living occupancy rose 40 basis points to 91.3 percent, while assisted living occupancy remained unchanged at 89.3 percent.



Despite assisted living's stable occupancy, absorption remained rather strong, however, it was offset by equally robust inventory growth. Both absorption and inventory for assisted living increased by 0.8 percent. To put into context, independent living's absorption increased at a 0.5 percent rate, but its supply only grew by 0.1 percent.



Recent construction trends continued with moderation in assisted living and slight acceleration in independent living, though assisted living continues to maintain a higher overall construction rate. As of the fourth quarter, assisted living construction represented 5.2 percent of its supply, compared to 2.4 percent for independent living. Compared to a year ago, assisted living construction has slowed by 70 basis points, while independent living construction has risen by 60 basis points.

Based on current construction activity, inventory should continue to grow at rates close to recent levels for each property type. Assisted living will continue to experience relatively healthy gains in new supply, while independent living will see little impact from new supply. Despite the likelihood that assisted living will continue to grow at a robust pace, NIC Research forecasts a fairly balanced supply-demand scenario for 2015. Independent living occupancy will likely continue at its current trajectory, enjoying the benefits of a moderated supply.

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Long-Term Care Policy Expert Dr. Bruce Chernof to Headline NIC Forum

As the health care system undergoes a dramatic shift to focus on value-based outcomes, seniors housing and care providers will be a powerful voice in the discussion of how best to improve the quality of life for elders. "We are on the cusp of the health system starting to understand the importance of the living environment to sustain independence," says Dr. Bruce Chernof, president and CEO of the SCAN Foundation, a California-based non-profit organization dedicated to transforming care for older adults.

Much of the failure to improve the quality of life of older people is really a failure to address their functional needs, explains Dr. Chernof, former Chair of the Commission of Long Term Care—a bi-partisan committee appointed by President Obama and members of Congress in 2013 to find comprehensive funding solutions for long-term care. He notes that people's physical environment—where they live and the support services they receive—is often the biggest factor affecting their health and quality of life. "When the physical environment fails, that's when they end up in the emergency room," he says.

The intersection of seniors housing and care and the evolving health care system will be detailed by Dr. Chernof as keynote speaker at the NIC 2015 Capital & Business Strategies Forum, March 31- April 2, in San Diego. The presentation will be followed by a panel discussion among senior level industry leaders on Dr. Chernof's observations.

Offering a preview of his NIC presentation, Dr. Chernof notes that housing and care providers have the tools to help people age in place, wherever they happen to live. "That is not what the medical system knows how to do," he says. For example, seniors housing and care providers can act as an early warning system to help avoid hospital admissions and readmissions often with simple, low-cost interventions such as medication management.

Dr. Chernof will detail other points of convergence between the health system and seniors housing and care, including:

- Transparency. Housing and care providers will be involved in health outcomes by tracking data and making it available to medical groups, insurance companies and hospitals. Dr. Chernof proposes that shared data and outcomes should result in shared reimbursements with housing and care providers. "It's a value proposition," he says.
- Managed care. Risk-bearing organizations that provide payments will incorporate more social supports, such as community based services. Housing providers in particular could offer services outside their walls to prevent unnecessary medical care.
- Person-centered approaches. Medical and personal goals will be aligned. Instead of treating a series of ailments, medical providers will consider the person's goals and then work to structure supports, including housing and care services, to meet those goals.
- Technology. The latest computer application or monitoring system may look intriguing, but Dr. Chernof asks: "Is there value?" Seniors housing and care providers can bring a dose of realism to the discussion since they work in a built environment that demands practical approaches.

Dr. Chernof challenges the notion that health systems are well acquainted with the wide array of services offered by housing and care providers. Housing and care providers can emerge as the champions of the elderly in the quality of life discussion, he says, and fill the void left by the medical system. He adds: "I would encourage the housing and care sector not to misread the shift taking place. There will be a number of years of shift and more opportunities to be part of a broader solution as providers re-imagine their role as a community resource."

New Educational Program Highlights Latest Management Tools

Amid an industry-wide effort to develop leaders and shape the future of the sector, a three-day Senior Housing Institute will be held the weekend of Feb. 6-8 at the University of Southern California (USC) Davis School of Gerontology, Los Angeles. Sessions will cover a broad range of subjects related to the direction of the industry, building operations, and the latest research on the science of aging.

The Institute is designed for C-level executives, officers and managers in seniors housing, post-acute and long-term care. Institute graduates are eligible for 12 continuing educational units.

The program will consist of informative lectures, case studies, and experiential learning opportunities. Participants will:

- Learn key aspects of gerontology, normal aging process
- Explore effective leadership and decision-making strategies
- Examine marketing approaches
- Discover best industry practices
- Identify successful financial strategies
- Develop for crisis communication skills

Other topics include design trends, changing regulations and healthcare policies, risk management, transforming end-of-life care, demographics, the impact of new technologies, and how to prepare for court depositions.

As a relatively young industry, the seniors housing sector has been working to further professionalize the sector and attract new talent. NIC has already established an internship program for promising graduate and undergraduate students interested in senior living through its University Outreach program.

Several years in the making, the Institute is the result of a partnership between the seniors housing industry and the USC Davis School of Gerontology and the USC Marshall School of Business. Sessions will be led by USC professors, seniors housing industry professionals, and legal experts in senior care.

The opening panel, comprised of seniors housing executives, will discuss challenges faced by the industry. The keynote lecture on personalized aging will be given by Pichas Cohen, Dean of the USC Davis School of Gerontology.

Other notable speakers include USC professors Victor Regnier, a pioneer in senior living design, and Susan Eguidanos, a well-known researcher in the field of palliative care. A number of top senior living industry leaders will also appear including **Randy Richardson**, president and CEO at Vi Living; **Loren Shook**, president and CEO at Silverado Senior Living; **Patricia Will**, founder and CEO of Belmont Village Senior Living; **Andy Kohlberg**, president and CEO at Kisco Senior Living; **Molly Forrest**, president and CEO at the Los Angeles Jewish Home for the Aging; **Sue Farrow**, CEO of Integral Senior Living; and **Bob Kramer**, CEO at NIC.

For the compete program & registration information, visit gero.usc.edu/seniorhousingexecutive

Seniors Housing & Care Industry Calendar

January 2015:

25-27 ASHA Annual Meeting, Dana Point, CA

28-30 IREI Visions, Insights & Perspectives Conference, Dana Point, CA

February 2015:

9-11 NASL 2015 Winter Conference, Washington, D.C.

22-25 Association of Jewish Aging Services Conference, San Diego, CA

24-26 12th Annual HJ Sims Late Winter Conference: Financing Methods and Operating Strategies for the Senior Living Industry, Carlsbad, CA

March 2015:

1-4 Senior Living 100, Key Biscane, FL

31-April 2 NIC 2015 Capital & Business Strategies Forum, San Diego, CA

May 2015:

5-7 ALFA 2015: The Senior Living Executive Conference, Tampa, FL

13-14 ULI Spring Meeting, Houston, TX

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