NIC

National Investment Center for Seniors Housing & Care

2015 INSIDER

NEWSLETTER

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25th NIC National Conference Recap

The 25th NIC National Conference was held from September 30 through October 2, 2015, at the Gaylord National in National Harbor, Maryland. This year's theme, The Next 25, reflected on where the seniors housing and care industry is heading over the next 25 years.

Highlights of this year's conference included:

- **NIC Talks,** a series of 12-minute presentations given by industry insiders and outside disruptors who answer the question, "What do you envision happening over the next 10 years that will revolutionize the aging experience of the first boomer turning 80 in 2026?"

- **NIC Seniors Housing and Care Boot Camp,** which gave newcomers (1-3 years) to the industry an overview of the basics of seniors housing and care and strategies for making sound financial decisions.

- **NIC Technology Innovation Challenge,** which pitted four technology startups in front of a panel of well-known senior care providers in a Shark Tank-type competition to find practical, relevant, and scalable products or services for seniors.

- **Networking opportunities** at the conference's multiple networking lounges, meeting spots, and receptions
that were offered throughout the three days of the conference.

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Check out our full conference coverage for additional information.

Thoughts from NIC's Chief Economist

Beth Mace, Chief Economist, NIC

"A butterfly can flutter its wings over a flower in China and cause a hurricane in the Caribbean" is an oft-repeated and popular phrase from the 2004 movie The Butterfly Effect. Inspired by the thoughts of MIT meteorologist Edward Lorenz, the idea is that an event someplace far away can produce a significant outcome somewhere else.

How does this relate to seniors housing? The seemingly distant changes going on in the Chinese economy and stock market may have rippled through the U.S. seniors housing market in the third quarter.

Occupancy rates rose 20 basis points in the third quarter, a welcome improvement from the 60-basis-point decline seen between late 2014 and June 2015, but the improvement in the quarter was less than would have been expected given the normal summertime bounce, when loved ones often move their parents into seniors housing.

China Syndrome?

Perhaps the improvement would have been stronger had the global stock market not lost $11 trillion between mid-June 2015 and late September 2015, which was the cumulative result of several factors. These factors included the stock market plunge in China on August 24, now labeled Black Monday, which was propelled by fears of a significant slowdown in the Chinese economy and its effect on commodity prices and emerging market economies, among other factors. The global correction also stemmed from general skittishness over the sustainability and length of the six-year bull market in stocks, which ran from 2009 to 2015.

The inter-relationships are not easy to categorize but are indeed complex and broad. And while a direct causal relationship is not statistically evident, there is anecdotal evidence that sharp movements in the stock market can affect consumer confidence and the psychology and timing of moving into seniors housing. Time will tell if this was a one-quarter alteration.

Blip or Portent?

Meanwhile, the investment total return performance of the private seniors housing sector slowed in the second quarter (most recent data available), according to analysis conducted by NIC with the NCREIF data. The total return performance of 2.45% was down from 4.66% in the first quarter and below the NCREIF Property Index (the NPI, which logged in a total return of 3.14%) and apartments (2.98%). (Note that seniors housing is not included at this time in the NPI total property index). Income returns continued to be strong for seniors housing, but the capital appreciation component of the total return was relatively low at 0.98%—half that of the NPI and apartments.

This was an unusual appreciation return result for seniors housing. One quarter certainly does not make a trend, and time also will tell if this was a one-time occurrence or not. On a longer-term basis, seniors housing has had stellar returns and outperformed apartments as well as the other three major property types: office, industrial, and retail. Indeed, on a 10-year basis, the total returns for seniors housing were 14.2%, significantly outpacing the NPI (8.2%) and apartments (7.8%).

Where Does Seniors Housing Fit In the Investment Spectrum?

In general, investor interest (both debt and equity) in seniors housing is strong and growing. This was evident by the record attendance for NIC's Fall Conference, as well as by the number of new inquiries being received by NIC staff on both the investment thesis and the risks associated with investing in the sector.

Questions about where seniors housing fits into the investment spectrum for a multi-asset real estate portfolio—core, core-plus, value-add, and opportunistic—are also being asked. While the definitions of these investment types remain subjective, because the sector historically was not well understood and data was fairly limited, many investors placed the property type into the opportunistic or value-added bucket.

However, transparency in the sector has improved markedly in the last several years. (While this may sound self-serving, NIC itself has made significant contributions to this greater transparency.) Today, data and experience show that seniors housing has many core-like characteristics. These include its steady and predictable income and cash flow characteristics, its high income yield, and its relatively strong "tenant" credit quality. Properties located in major urban areas and with limited leverage would have additional "core-type" investment characteristics.

Traits Attracting Capital?

Because of these characteristics, investor interest in the sector is likely to expand, bringing more capital into the sector and increasing the overall liquidity of the sector, which can give it an additional core-like trait. In addition to domestic capital, foreign capital flows into the U.S. continues to rise, as sovereign funds try to hit their commercial real estate investment targets, and a share of those dollars likely will go into seniors housing as well.

That said, it's important to keep in mind that seniors housing has a more significant operational component than that of other commercial real estate property types, and its total return performance is not completely based on its real estate component. As a result, seniors housing properties in general will likely never be regarded as a pure core real estate property type and will always carry some operationally-related risk premium.

As always, I welcome your thoughts, comments, and feedback.

Beth

Seniors Housing Occupancy Gets Seasonal Assist

Signals of Peak Occupancy Mounts

Chris McGraw, Senior Research Analyst, NIC

Seniors housing occupancy received its typical third-quarter boost, rising 20 basis points to 89.9%. The third quarter usually comes with a gift of increased absorption, but the acceleration was softer than it has been in previous years. After stripping out the seasonal component, seniors housing occupancy was essentially unchanged from the second quarter.

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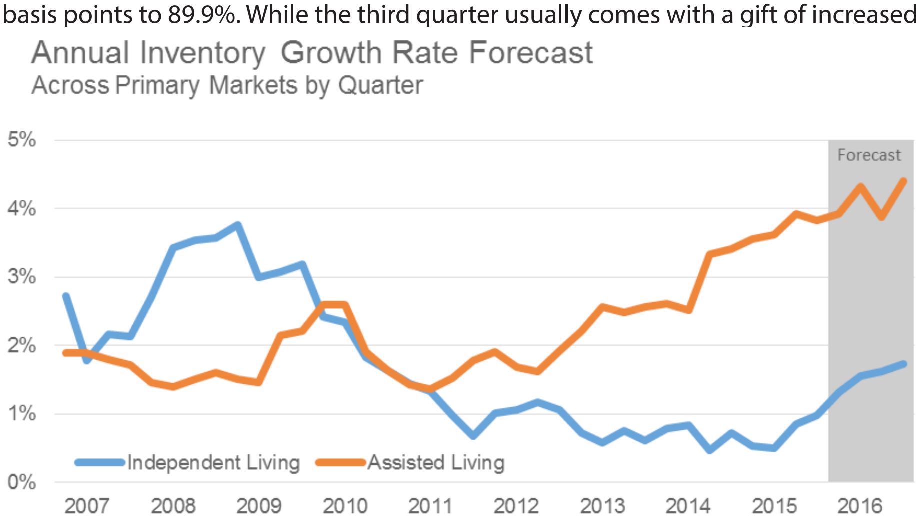
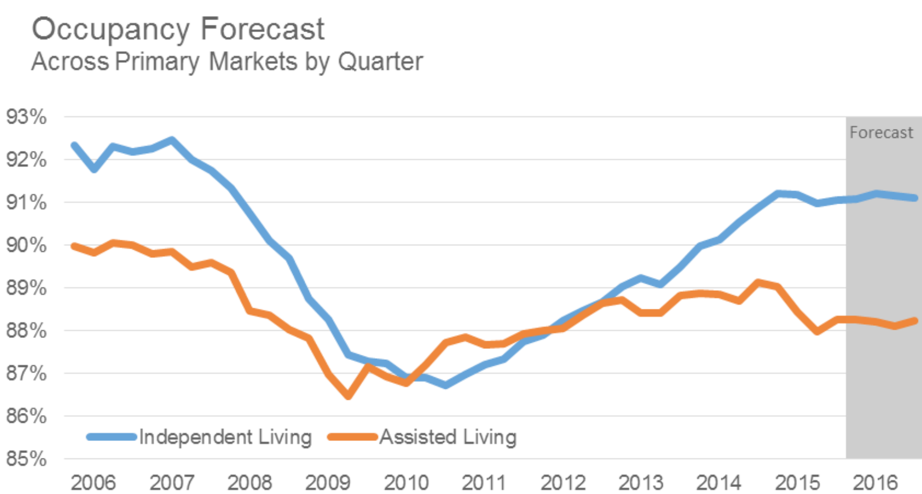


Source: NIC MAP® Data Service

the acceleration during this third quarter was softer than it has been in previous years. If one strips out the expected seasonal component, seniors housing occupancy was essentially unchanged from the second quarter.

When compared to independent living, assisted living benefited more from the third quarter, with occupancy rising 30 basis points to 88.3%. However, all of that gain for assisted living (and then some) was likely purely seasonal and not reflective of improvement in the underlying fundamentals. Seasonally adjusted, assisted living occupancy declined 10 basis points during the third quarter, which coincides with the deceleration in the rate of annual absorption. Independent living occupancy was unaffected by seasonality and rose 10 basis points during the third quarter.

The third quarter's performance, together with NIC's forecast, puts more weight behind the notion that the aggregate occupancy rates are peaking for this market cycle. NIC's forecasts for the next four quarters suggest that occupancy is likely to hold steady at its current rate. As inventory growth begins to materially accelerate, the market is expected to be increasingly challenged to fully absorb all of the new units and increase occupancy. Annual inventory growth for independent living and assisted living is expected to reach 1.7% and 4.4% respectively by the third quarter of 2016. These inventory growth rates mean that downward pressure on the occupancy rates is likely, especially for assisted living, if the market's actual pace of absorption falls short of the pace currently forecasted by NIC.



Source: NIC MAP® Data Service

If NIC's forecast for independent living holds true, that would put occupancy essentially unchanged over a period spanning two years, which suggests it has plateaued. NIC's forecast for assisted living also points to occupancy remaining relatively flat over the next four quarters, although that will be largely at the mercy of the severity of the flu season. The 2013 and 2015 flu seasons were quite severe, and absorption (and consequently occupancy) was negatively impacted. A similar severity for this coming season could push occupancy rates lower.

Seniors Housing & Care Industry Calendar

November 2015:

1-4 LeadingAge Annual Meeting, Boston, MA

11-13 NCREIF Fall Conference 2015, Orlando, FL

17-19 REITWorld: NAREIT's Annual Convention, Las Vegas, NV

December 2015:

1-4 ALFA Chief Executive Summit, Scottsdale, AZ

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