SENIOR HOUSING INVESTMENT

S U R V E Y

VOLUME 26 | SENIOR LIVING VALUATION SERVICES, INC. | FALL 2020

The *Senior Housing Investment Survey* provides information concerning the investment criteria currently used or perceived to be used in the evaluation of senior housing properties. Survey participants included owners/operators, financial institutions/investors, brokers/mortgage bankers, appraisers and consultants.

Survey Methodology

The 26th annual *Senior Housing Investment Survey* was sent to 372 potential respondents about eight months into the dual health care and economic shocks caused by the Covid-19 pandemic, including those with membership in various national senior housing associations, parties responding to the survey in previous years and others involved in the senior housing industry and known to the editor. As of a October 30, 2020 cutoff date, 57 surveys or 15% of the total sent had been returned. Of the respondents, 26% represent market principals such as owner/operators or financial institutions/investors, a similar percentage compared with previous years.

Survey Results

Survey respondents were geographically dispersed throughout the country with a lower response from the East. Geographic location did not appear to bias the survey results as responses were not materially different between differing portions of the country. Approximately 54% of respondents this year identified themselves as having a national perspective, a higher percentage compared to previous years. The respondents indicated differences between projected annual cash flow growth factors in revenues (1.6% average) and expenses (1.9% average) reflecting widespread and ongoing pandemic related atrophying occupancies and revenues. Both cash flow growth factors were below projections of overall inflation (2.2% average).

A plurality 47% of all respondents noted that capitalization rates for senior housing properties in general are expected to increase by up to 100 basis points in the next 12 months (well above the 20% last year). 45% of respondents expect no material change in overall cap rates in the next year (well below the 73% last year). Few respondents expect capitalization rates to decrease or increase by over 100 basis points in the next year.

The specific overall capitalization rates, discount rates (internal rate of return) and equity dividend rates (cash on cash return) used or perceived to be used by respondents are presented on the following pages. The range and average of all responses and the range and average of all responses less the 5% highest and 5% lowest responses are shown.

The rate averages range from the lowest for age restricted apartments to the highest for licensed subacute skilled nursing facilities. These results are not surprising given the higher degree of management specialization, smaller profit margins and higher degree of licensing as one moves up the continuum of senior housing from age restricted apartments to unlicensed congregate facilities to licensed assisted living and memory care to licensed long term and subacute skilled nursing facilities. Rates for continuing care retirement or lifeplan communities which are typically combinations of each of the categories of senior projects, fell near the average of the rate range of the other categories of senior housing types.

Highlights of the 2020 survey results include modest increases from 2019 in overall capitalization rates for memory care facilities (50 basis points) and long term care nursing homes (40 basis points) but overall no material changes in overall cap rates for most senior housing property types. However, in one of the more significant findings in this year’s survey, equity dividend rates increased materially (about 15% to 25%) for most senior housing property types except for short and long term care facilities.

SENIOR LIVING VALUATION SERVICES, INC.
2020 SENIOR HOUSING INVESTMENT SURVEY

Indicate the classification that best describes your company or profession (% of total responses):

18%	Owner/Operator	36%	Appraiser
8%	Financial Institution/Investor	10%	Consultant/Other
28%	Broker/Mortgage Banker		

Indicate the region with which you are involved with/knowledgeable of (% of total responses):

0%	East	13%	West
11%	South	54%	National
22%	Midwest		

What annual growth factors are you using (or perceived to be used by others) for cash flow projections of senior housing properties in general:

Range	Average	
-5%-4%	1.6%	Revenues
-2%-10%	1.9%	Expenses
0%-3.5%	2.2%	General Inflation

What are your expectations of overall capitalization rate changes for senior housing properties in general over the next 12 months (% of total responses):

2020		2019	2018
5%	Increase more than 100 basis points	0%	0%
47%	Increase 0 to 100 basis points	20%	71%
45%	Flat, no significant change	73%	24%
0%	Decrease 0 to 100 basis points	7%	5%
3%	Decrease more than 100 basis points	0%	0%

Overall Capitalization Rate

	2020 All Responses		2020 Adjusted Responses (1)		Basis Point Change from 2019
	Range	Average	Range	Average	
Age Restricted Apartments	4%-7.8%	5.9%	5%-7%	5.9%	-10
Unlicensed Congregate Living	5%-12%	6.7%	5.8%-8%	6.6%	0
Licensed Assisted Living	6.3%-10%	7.5%	6.5%-9%	7.5%	+10
Licensed Memory Care	7%-10%	8.1%	7%-9%	8.4%	+50
Licensed Skilled Nursing-Long Term Care	10%-15%	12.5%	11%-13.3%	12.3%	+40
Licensed Skilled Nursing-Subacute Care	9.5%-14%	12.2%	10%-13.5%	12.3%	+10
Continuing Care Retirement Community	6.5%-12.5%	9.1%	7.5%-12%	9.0%	+10

Internal Rate of Return (Discount Rate)

	2020 All Responses		2020 Adjusted Responses (1)		Basis Point Change from 2019
	Range	Average	Range	Average	
Age Restricted Apartments	7%-25%	9.3%	7.5%-12%	8.4%	-30
Unlicensed Congregate Living	7.5%-25%	9.5%	7.5%-13%	8.8%	-40
Licensed Assisted Living	8%-25%	10.6%	8.5%-14%	10.0%	+10
Licensed Memory Care	8%-22%	10.6%	8.5%-14%	10.1%	-30
Licensed Skilled Nursing-Long Term Care	10%-18%	14.9%	13.5%-16%	15.0%	+60
Licensed Skilled Nursing-Subacute Care	10%-20%	15.0%	13.5%-16%	15.0%	+10
Continuing Care Retirement Community	6%-22%	11.5%	7.5%-14%	11.1%	+10

Equity Dividend Rate (Cash on Cash Return)

	2020 All Responses		2020 Adjusted Responses (1)		Basis Point Change from 2019
	Range	Average	Range	Average	
Age Restricted Apartments	6%-15%	10.5%	8%-15%	10.5%	+210
Unlicensed Congregate Living	6%-18%	11.7%	6.5%-15%	11.1%	+190
Licensed Assisted Living	7.5%-18%	12.7%	8%-15%	12.6%	+150
Licensed Memory Care	7.5%-18%	13.1%	9%-15%	13.0%	+180
Licensed Skilled Nursing-Long Term Care	13%-25%	17.3%	13%-20%	17.0%	+20
Licensed Skilled Nursing-Subacute Care	12%-25%	17.4%	13%-20%	17.2%	+60
Continuing Care Retirement Community	7%-18%	11.6%	9.5%-17.5%	13.7%	+200

(1) Minus 5% Highest and 5% Lowest Responses

It appears as though the large increases in equity dividend rates have been largely offset by decreases in the costs of debt capital (when available) leading to no material changes in overall cap rates to date.

The difference between overall cap rates and discount rates tightened slightly for some senior housing property types to a spread more indicative of a market relationship, or that used by most appraisers. Most appraisers rely on an industry accepted relationship between overall cap rates and discount rates that can be summarized in the following formula: overall cap rate plus annual cash flow growth rate less 100 basis points = discount rate. This formula does not appear to be widely used or known by many (non-appraiser) senior housing industry participants. The discount rate (also known as the yield rate or the internal rate of return rate) is a difficult financial concept that is subject to varying interpretations.

Survey Relevance

2020 has seen significant and ongoing market disruption from the Covid-19 pandemic. Market transaction activity and new construction is down as operators and potential sellers are concentrating on maintaining the safety of staff and residents and financially treading water until we reach the other side of the health care crisis. Potential sellers are not yet under strong pressures to sell and gaps between ask and bid prices are large leading to fewer market transactions although potential buyers with capital are available. The paucity of market transactions have created a fog of uncertainty in the short and medium term.

Overall long term prospects for industry recovery and strength are strong, supported by undeniable favorable long term demographics (only 5 years to the first baby boomers turning 80 years old!) and projected historically low interest rates into the foreseeable future.

The results of this survey can be an asset in the evaluation of new development or acquisitions by lenders and investors. However, market illiquidity and the specialized management driven characteristics of the industry overall and on individual properties specifically, mute the impact of more traditional measures of real estate such as capitalization, discount and return on equity analysis. Other limiting factors include a lack of confidence in the uniform application and understanding of these criteria – especially for non stabilized or more complicated properties, the difficulty in quantifying general and specific property risk and illiquidity, concerns over reliable future cash flow projections and their unproven relevance for some not-for-profit owners/investors.

Other investment criteria used include the terms and availability of debt and equity financing, replacement cost comparisons, property age and size, debt coverage ratios, market share, portfolio effect, geographic concentration value surcharges and opportunities for significant cash flow gains in distressed or underutilized properties. These criteria have their own significant limitations such as the inability to objectively account for property specific risk and to comprehensively assess the impact of a potential default and resale of a property.

Inquiries, comments or requests of interested parties wanting to participate in the 27h annual 2021 survey can be directed to:

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