PREVIEW INCREASED INVESTMENTS AND DIFFERENTIATION IN HEALTH CARE REAL ESTATE

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ABSTRACT

In 2016, I conducted an initial study around healthcare real estate in the Netherlands on behalf of the Association for developers & builders (NVB) to provide a picture of developments around healthcare real estate for investors. This resulted in an essay (Veuger 2015a) and an book contribution (Veuger 2015b). Now six years later, it becomes curious how the healthcare real estate developments of the time have progressed to the present day. Before looking at the developments in 2022 compared to 2016, it is important to see how the healthcare real estate developments from 2009 through 2015 evolved where from 2009 only really shows an upward trend in real estate investments. This article consists of the 2016 study (Part I) and a 2023 update (Part II).

KEYWORDS _ *healt care, real estate, investments, the Netherlands*

INTRODUCTION: EDUCATION AND RESEARCH

The prospects for investing in healthcare real estate are positive and investments (Schie 2014) will therefore therefore increase. This is evident from the 2015 Healthcare Real Estate Barometer, among others. Dutch healthcare organizations have been responsible for their own real estate since 2012, and thus investing in care locations is still at the beginning of its development. This is different in other countries. There, it is common for different investors to invest in care and cure real estate. Foreign investors see opportunities when they look at the Dutch healthcare real estate market. A plus in that, for example, is that Dutch institutions, against the economic trend, have growing solvency and equity have.

The 2015 Healthcare Real Estate Barometer (Veuger et al. 2015b) includes a comparison with healthcare real estate investments in other countries included. Australia and the United Kingdom have a longer history in terms of healthcare real estate investments. The total return on investment in real estate is the highest (7.5 percent) in Australia over the 2007-2013 period. For healthcare real estate, that total return in Australia, for example, is higher (11.1 percent).

An important point is that within healthcare there are many differences. Take the difference between care and cure. Care currently still scores a lower return on real estate than cure. That is mainly caused by current developments within the General Act on Exceptional Medical Expenses (AWBZ) and the Long-Term Care Act (Wlz), as a result of which funded nursing homes are becoming vacant. In the United Kingdom (Veuger et al. 2015b), the care property portfolio has been reviewed to ensure that it fits well with the evolving demand for care and supply of care property which has also resulted in higher care property yields.

PART I
SIZE OF HEALTH CARE REAL ESTATE

The market value of Dutch healthcare real estate is ± 60 billion euros. There are ± 52 million m2 defined as healthcare real estate. This makes the sector larger in terms of floor space than, for example, the total retail or office real estate in the Netherlands. There are approximately 34 million m² of healthcare real estate of the desired future size of 2,000-100,000 m², according to the Economic Institute for Construction (EIB) (Elp and Konings 2015). Approximately 37% of the healthcare real estate falls outside this size range. These include small primary care and large hospitals. Of the size of the stock of healthcare real estate (Basic Records of Addresses and Buildings (BAG), from the Dutch municipalities and the Land Registry), about 22% is relatively new with a year of construction of 2000 or later. Based on the previous conditions segmented in the following overview.

	Metrage (1.000 m²)	Share in total segment (%)
Cure		
- First line	6.297	39
- Second and third line	6.285	62
- Private clinics	368	55
Care		
- Residential real estate	14.251	87
- Real Estate with care function	5.386	95
- Social service	1.637	32
- Private homes	41	50
Total	**34.266**	**63**

Figure 1: Healthcare real estate by segments, size range 2,000-100,000 m. (Elp and Konings 2015)

Looking at the large cities (G4 and G32) we see that of the desired size class of healthcare real estate 45% (15,370 sqm) is in the big cities according to the following table.

	Metrage (1.000 m²)		Share (%)	
	G4	G32	G4	G32
Cure				
- First line	1.452	1.788	23	29
- Second and third line	974	2.111	16	35
- Private clinincs	135	131	37	36
Care				
- Residential real estate	1.571	3.682	11	26
- Real estate with care function	917	1.497	16	26
- Social service	326	757	18	42
- Private homes	23	7	56	16
Total	**5.397**	**9.973**	**16**	**29**

Figure 2: Care real estate in large cities, size class 2,000-100,000 m2
(Source: BAG, EIB in Elp 2015 in Care Real Estate Barometer 2015 (Veuger et al., 2015)

TRENDS AND DEVELOPMENT

Trends and developments are:

- population composition is changing significantly;
- more private involvement in the Netherlands;
- healthcare real estate a proven investment category internationally;
- changing investment market for healthcare real estate; and
- large potential transaction volume.

POPULATION COMPOSITION IS CHANGING SIGNIFICANTLY

The composition of the population in the Netherlands will change in the coming decades. The number of elderly people will rapidly increase during that period. CBS indicates that the number of 65+ people will increase from 2.7 million in 2012 to 4.7 million in 2041. Until 2060 the number moves around about 4.7 million, see Figure 3. In the coming years, first the share of 65-79-year-olds will rise sharply. From 2025, the group of 80+ year olds will also increase sharply, the so-called double aging. In 2040, the Netherlands will reach the peak of the number of 65+ people. An estimated (Rotscheid 2015) 26% of the population will then be over 65. About 10% will be older than 80 at that time. In 2013, only about 4% of the population is older than 80. In the coming decades, the "gray pressure" will increase sharply. In 2012 this is about 27%, while this will be about 51% in 2040. This pressure indicates the ratio between the number of people over 65 and the potential labor force. It provides insight into the ratio of older people to the potential working portion of the population that must absorb the burden of aging. In 2012 there are still four people working for every elderly person. By 2040, this has decreased to two employed people for every person over 65. After 2040, the gray pressure remains stable until about 2060.

In the coming years, the demand for nursing home and nursing home care will develop differently start to develop differently than in the previous decade. Several developments can be identified, each affecting the total demand for care for the elderly in a different way. These developments are:

- The elimination of demand for nursing home capacity due to the introduction of separate living and care.
- The increasing demand for concepts of assisted living as a result of more frequent and longer independent living by the elderly.

- The increasing demand for nursing home care as a result of the increasing number of seniors with heavy care needs.
- The insured package will possibly be further limited in connection with the collective financing of care and the macroeconomic manageability of costs.

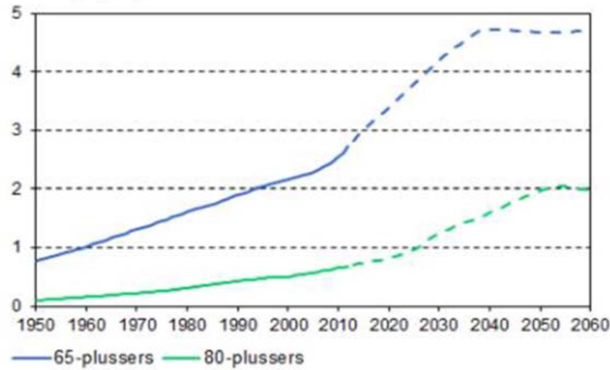

Figure 3: Number of millions of 65- (blush line) and 80+ people (green line) 1950-2012 and forecast number of 65- and 80+ people, 2013-2060 (source: CBS Bevolkingsstatistiek; CBS Bevolkingsprognose voor 2013-2060)

MORE PRIVATE INTERFERENCE IN THE NETHERLANDS

The government's influence in the Netherlands is waning with the restructuring of long-term care. The allowance for housing for those in light care - the so-called care package 1 to 4 - has been abolished. In addition, the government is making an appeal to society through the Participation Act. In Europe, historically large differences are visible between different countries and how long-term care is or is not regulated. In southern and eastern European countries, the role of the family in care is greater than in Northern Europe where the role the government is dominant. A combination of family and government is found more in Central European countries (see figure 4). There are large differences between all these countries significant differences when looking at the percentage share of national income spent on long-term care. There is also more of a convergence in terms of a care system in which family and government will play an important role together.

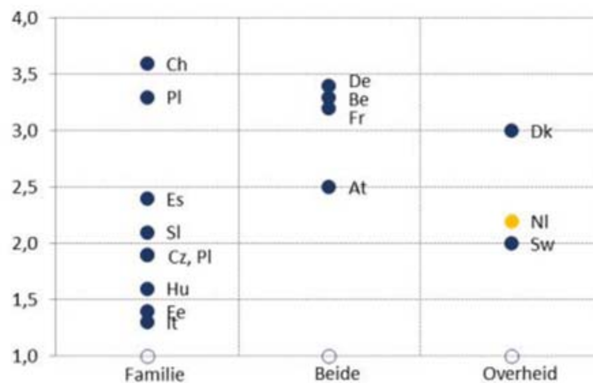

Figure 4: Long-term care responsibility by country and home care spending as % of GDP (source: SCP 2014, editing Syntrus Achmea Real Estate & Finance in Veuger et al. 2015. Bron: SCP 2014, editing Syntrus Achmea Real Estate & Finance in Veuger et al. 2015). [Familie is Family, Beide is Both and Overheid is Government]

The transition of care in the Netherlands means that there is less and less government involvement with the result that housing for those in need of light care is no longer funded by the government funding. This group must now provide for their own housing. Developments of new solutions to rent housing from investors in the immediate proximity to care facilities offer opportunities. General practitioners in primary care facilities a major role to relieve the more expensive second line. We increasingly see first and second-line facilities clustering in health centers. These can be attractive investment propositions for investors, developers and building entrepreneurs.

HEALTHCARE REAL ESTATE INTERNATIONALLY A PROVEN INVESTMENT CATEGORY

In the Netherlands, investments in healthcare real estate are limited compared to abroad. Out of total invested assets, Syntrus Achmea Real Estate & Finance estimates that approximately 500 million euros in healthcare real estate is held by Dutch institutional investors. If we compare this with the total invested assets in real estate in the Netherlands of approximately 50 billion euros, then healthcare real estate is only 1% of that. When the United States, the two largest public healthcare real estate funds have a combined market of approximately $50 billion, with the total healthcare real estate market being as much as $1 trillion. The maturity of investing in healthcare real estate is also determined in part by the fact that Australia, for example, has already had a professional return series: the MSCI Healthcare index. A comparable index in Netherlands does not (yet) exist, although the market clearly indicates a need for one. is. The potential for potential investment for the attractive healthcare real estate market and is, for example, larger in size than the entire retail market real estate in the Netherlands

LARGE POTENTIAL FOR TRANSACTION VOLUMES

The development and investment market of healthcare real estate has received increasing attention since 2012. More national and international (institutional) investors are expressing their ambition to set up a fund for healthcare real estate or to conduct research in this market so that its transparency can be increased. Private investors are also showing increasing interest in this segment, and healthcare bonds are going to develop further in various forms. Looking at registered healthcare real estate investment transactions by DTZ Zadelhoff, for example, in 2013, the following picture emerges. In 2013 it recorded approximately 120 million euros in investment transactions and in 2014 this increased to approximately 180 million euros. These investment transactions concern only a small part of the investment volume in 2014 of approximately 10 billion euros. This shows that this development and investment category is growing rapidly.

The ambitions of various investors, and thus opportunities for developers and builders, are substantial given that over EUR 2.5 billion is available from investors to invest in healthcare real estate in the coming years. What is important here are a number of - non-exhaustive - preconditions because the healthcare real estate market is and will continue to be very dynamic. Preconditions include:

- (new) construction and less than two years in operation;
- investment or a new lease, possibly in the form of a sale & leaseback
- construction;
- long-term lease, for example at least 10 years;
- alternative financial and functional use;
- a robust business case of the healthcare institution;
- relevant (healthcare) real estate location; and
- gross initial yield between 6.5% and 8.0%.

TRANSNATIONAL VOLUMES

Long-term overviews

Long term overviews of transaction volumes and initial yields of healthcare real estate in the Netherlands are not (yet) available. However, this is developing more strongly in the Netherlands. If we look at investment volume in the Dutch healthcare real estate market and disregard transactions between healthcare institutions and housing corporations as well as the fact that not all transactions are always public and/or complete, we see that from 2013 to 2015 investment volume has tripled from around EUR 100 to EUR 300 million (see figure 5).

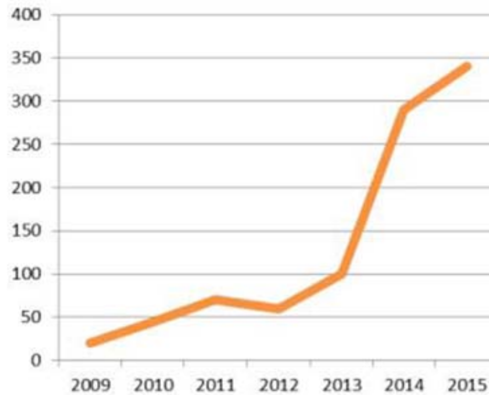

Figure 5: Investment volume 2009-2015 in Dutch healthcare real estate by market participants (y-axis in millions (source: Syntrus Achmea Real Estate & Finance & CBRE (2016). Syntrus Achmea Real Estate & Finance & CBRE (2016)

YIELDS

Investment and development opportunities for healthcare real estate become apparent when compared to other real estate segments such as offices, retail, residential and logistics. A comparison of gross initial yields of these different real estate segments with healthcare real estate in 2015 indicates (Syntrus Achmea Real Estate & Finance & CBRE (2016: 14). Dit is op basis van alleen de toprendementen. Van belang is om te constateren dat de bandbreedte van aanvangsrendementen zeer groot kunnen zijn) that the yields may look as follows compared to traditional segements (figure 6).

	Gross initial yield in approximately %
Traditional segments	
- Offices	5
- Stores	3,5 - 4
- Houses	5
- Logistic	6 - 6,5
Zorgvastgoed	
- Extra hosipital	5 - 6,5
- Intra hospital	5,5 - 7
- First line care	6,5 - 8
- Second line care	7 - 8,5

Figure 6: Gross initial yields traditional segments and healthcare properties (Elp and Konings 2015)

These yields show that the different ranges of four healthcare real estate segments are similar and sometimes higher than those of offices, retail, residential and logistics. Transactions at the top of extramural real estate therefore appear to be comparable to returns of residential properties. In cure and care, returns are higher than those of traditional real estate segments.

DIRECT AND INDIRECT RETURN ON HEALTHCARE REAL ESTATE INTERESTING

The total return on real estate consists of two parts:

- the direct return: expresses net income as a percentage of value;
- the indirect return: expresses the change in value - corrected for (dis-)investments - as a percentage of the value.

In the following figure 8 the total, direct and indirect returns for cure and care over the period 2003-2013 are juxtaposed. It shows that cure and care real estate show stable direct returns over this period. However, the total return on healthcare real estate over the last few years is negatively influenced by the negative indirect return from 2008 onward. One explanation for this is the many vacant nursing homes.

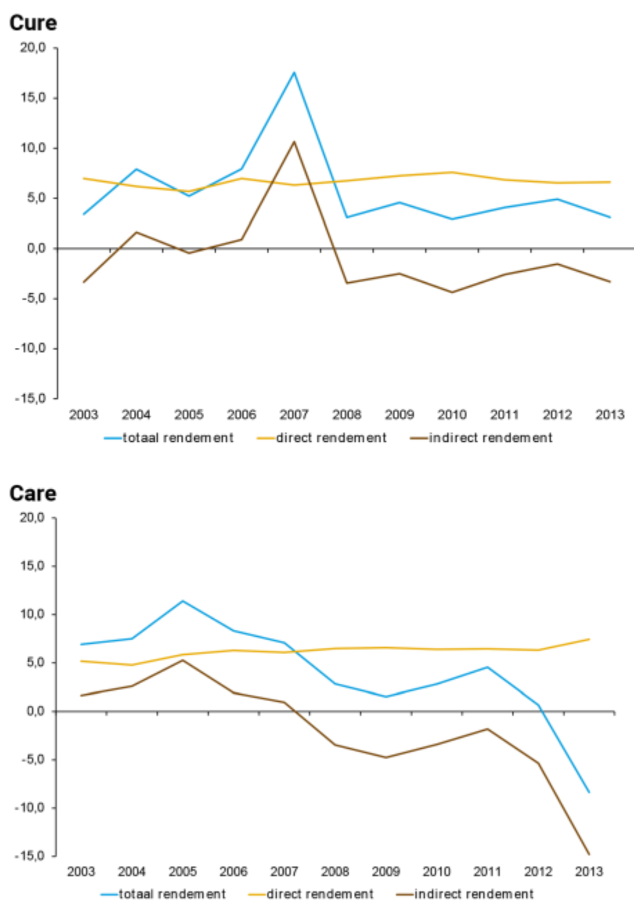

Figure 7: Total, direct and indirect returns (BAR in %) Dutch Healthcare Real Estate Cure and Care 2003-2013 (source: Elp and Konings 2015). Blue line is total return; yellow line is direct return and brown line is indirect return

It is now also interesting to look at a return picture of healthcare real estate compared to the IPD Dutch annual real estate index. Over the period 2003-2012, it appears that care and cure real estate returns follow the index. In 2013, it appears that the total return of care real estate is significantly lower than in previous years. One explanation for this is that this concerns a large part of the stock of traditional care homes where alternative use is very limited.

Figure 8: Direct and total return (BAR in %) Dutch healthcare real estate care and cure compared to Dutch real estate index, 2003-2013 (Source: Elp, M. and P. Konings (2015). Blue line is total return; yellow line is direct return and brown line is indirect return

PART II
HEALTH CARE REAL ESTATE INVESTMENTS 2019-2022 IN THE NETHERLANDS

If we follow the developments from 2016 (Veuger 2016) and see the result of hair 2022, a very sharp increase in investments in healthcare real estate can be seen. In 2016 the volume was 465 million euros and in 2022 1,344 million euros (Capital Value 2023), a more than doubling of the volume compared to 2016. In four consecutive years from 2019 to 2022, investments exceeded 1 billion euros and mainly concern care housing (88%, Capital Value, 2023) and primary and secondary care real estate. New construction orders remained stable.

Figure 9: Healthcare real estate investments 2019-2022 in million euro's (Capital Value 2023)

DOMINANT INSTITUTIONAL INVESTORS IN THE NETHERLANDS

The largest market share (Healthcare Real Estate Market 2023) in transaction volume is achieved by instutional investor with a 71% share. They invested 85% more in 2022 than in 2021 (Capital Value 2023). The three most substantial investments by instutional investors in 2022 were:

- The LUXOR-I portfolio consisting of 32 private residential care complexes of Dagelijks Leven spread across the Netherlands.
- Syntrus Achmea acquired the portfolio on behalf of the Achmea Dutch Healthcare Property Fund from the international listed healthcare company Orpea. Orpea decided, due to financial circumstances, to sell part of the portfolio through a sale & lease back transaction (Achmea 2022).
- The acquisition of 144 inpatient care units and 149 care homes for the Bouwinvest Healthcare Fund in The Hague (Bouwinvest 2022).

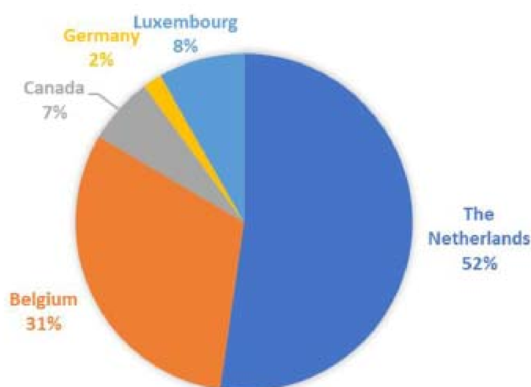

Figure 10: Composition of healthcare real estate transaction volume by nationality of buyer 2022 (Capital Value 2023). Editing Veuger 2023

POSSIBLE STABILIZATION

After an explosive increase from 2016 through 2022, a number of factors are now visible that may stabilize investment in healthcare real estate. This is possible due to three developments (Capital Value 2023):

1. Interest rate hike felt in second half of 2022

   Dutch investors invested in opportunities created by rising interest rates on bank financing. As a result, investors became more dependent on outside capital. International investors showed signs of becoming less active in the healthcare real estate market in the second half of 2022, as did listed healthcare real estate investors due to low stock market levels. Due to possible uncertain market conditions, fewer new (institutional) investors may enter the healthcare real estate market in the coming period.

2. Decrease in transactions

   Looking at the stable transaction volume over 2016-2022, it does appear that the number of transactions decreased by 20% in the last two years and became most visible in the second half of 2022: the fourth quarter of 2022 saw a total of 20 transactions compared to 40 in 2021 and 71 in 2020. The average investment per transaction did increase by an average of 10.9 million euros. In comparison, in 2020 this was still 8 million euros per transaction. These figures are heavily influenced by two trends, though: (a) in 2022, almost 90% of the number of transactions took place within a range of up to 20 million euros, collectively accounting for about half of the total transaction volume, and (b) in addition, there are several large portfolio transactions every year. In 2022, there were nine transactions larger than 30 million euros that collectively account for over 43% of the total transaction volume (Capital Value 2023). In addition, supply is stagnating.

3. Less new construction

   The Dutch Health Care Institute (Zorginsituut Nederland 2023) indicates that there will be a 70% increase in acute nursing home admissions in 2022, in absolute numbers 4,737 people. This necessary increase cannot (yet) be seen in the increase of new construction and/or transformation and shows a slight decrease at this time. In addition, the transaction volume shows only a 2% increase compared to 2021. The feasibility of new construction projects in healthcare real estate came under further pressure due to the confluence of several market developments: (a) construction costs that rose again in 2022 and (b) declining initial yields due to the rise in interest rates. With the announced rate decrease of the Normative Housing Component (NHC) (Actiz 2022), the pressure on housing revenues is increasing.

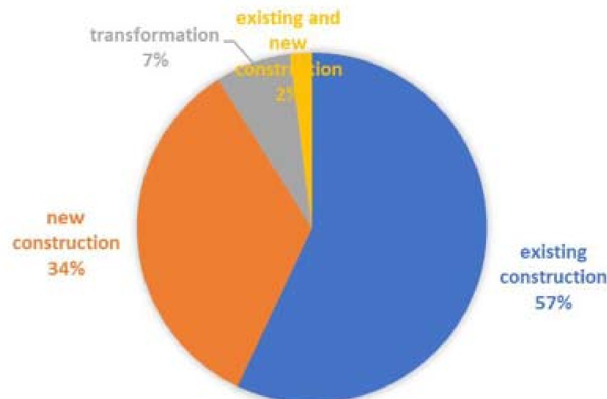

Figure 11: composition transaction volumes by construction status 2022 (Capital Value 2023). Editing Veuger 2023

Kuipers, director of healthcare real estate Capital Value (Capital Value 2023) argues that pushing ahead with new construction is essential right now: “*Healthcare institutions are seeing their capacity decrease due to the postponement of new construction projects and staff shortages, while waiting lists continue to grow. New healthcare real estate and smart buildings offer an opportunity for implementing more efficiency in healthcare. These include changes in floor plans, hybrid buildings and new techniques in home automation. Sustainability is also becoming a major focus in the healthcare sector. This also applies to investors and corporations in acquisitions. There is therefore more and more common ground between care institutions and market parties to work together on a future-proof stock.”*

CONCLUSIONS

During the last few years, the healthcare real estate market is moving towards becoming a stable and mature investment market. More players are operating in this market with a number of issues in healthcare real estate creating appeal: (1) demographics and not economics are driving the healthcare sector making it less correlated with economic cycles and recessions, (2) building a differentiated property portfolio in which locations are geographically dispersed reduces risks, (3) alternative uses of properties located in a good environment within a local community gives the property more development potential when vacant, (4) care providers can enter into longer-term contracts and can provide the security to continue to provide care activities and be locally anchored over that term and this gives an investor security for a longer (rental) term and a lower risk of being faced with property that is too specific and (d) fixed, annually indexed rents that reduce inflation risk.

Interest rate hike felt in second half of 2022. Due to possible uncertain market conditions, fewer new (institutional) investors may enter the healthcare real estate market in the coming period.

Decrease in transactions. In 2022, there were nine transactions larger than 30 million euros that collectively account for over 43% of the total transaction volume (Capital Value 2023). In addition, supply is stagnating (Real Estate Market 2022).

Less new construction. With the announced rate decrease of the Normative Housing Component (NHC) the pressure on housing revenues is increasing.

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