



INTEGRA Realty Resources
SENIORS HOUSING & HEALTH CARE SPECIALTY PRACTICE
SENIORS INDUSTRY OUTLOOK
2010

2010 SENIORS HOUSING OUTLOOK

Types of Seniors Housing

The following chart summarizes the primary types of seniors housing.

ITEM	SENIOR APARTMENTS	INDEPENDENT LIVING	ASSISTED LIVING	NURSING HOMES	CCRCs AND COMBINATIONS
State Licensing	Not Required	Not Required	Required	Required	Required
State Approvals Needed to Build	Not Required	Not Required	Not in most states, but there are a few with CON requirements	Most states require a CON or application for Medicaid funding	Most states have some state approval requirements
Resident Funding	Private pay or Section 8. Many Low Income Housing Tax Credits and have rent and income restrictions	Private pay	Primarily private pay, some Medicaid Waiver	Predominantly funded by Medicaid and Medicare	Primarily private pay, some Medicaid and Medicare in assisted and/or nursing components
Payment Type	Primarily rent by the month	About 3/4 rental by the month, 1/4 entry fee	Primarily rent by the month, a small percentage are entry fee	Primarily rent by the day, virtually none are entry fee	Majority of CCRCs require an entry fee for independent living, and some require for assisted living too
Typical Size	60 to 250 units average is +/-200 units	80 to 200 units, average is +/-125 units	40 to 100 units, average is +/-75 units	100 to 200 beds, average is +/-120 beds	Typically 200+ units/beds, many in the 300 to 500 range
Meal Service	Limited	Typically 1 to 3 meals per day included in rent	Typically 3 meals per day included in rent	Typically 3 meals per day included in rent	Varies by care types within the community
Typical Services Provided	Transportation and activities	All provided in senior apartments plus meal service, housekeeping, and 24 hour monitoring	All provided in independent living plus laundry and assistance with activities of daily living	All provided in assisted living plus 24-hour nursing care	Varies by care types within the community

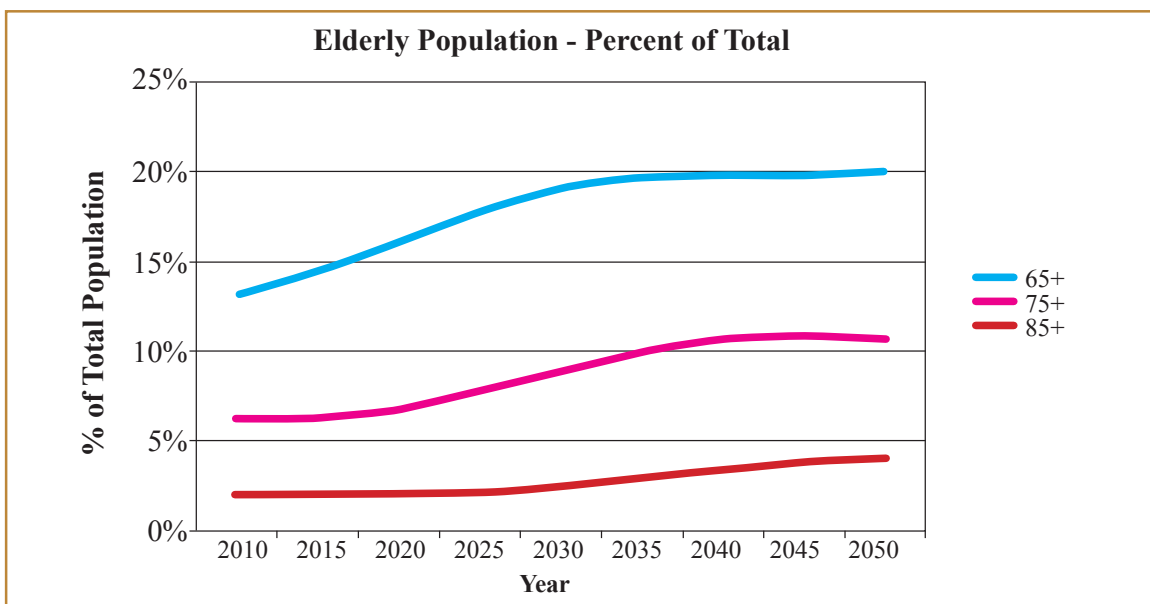
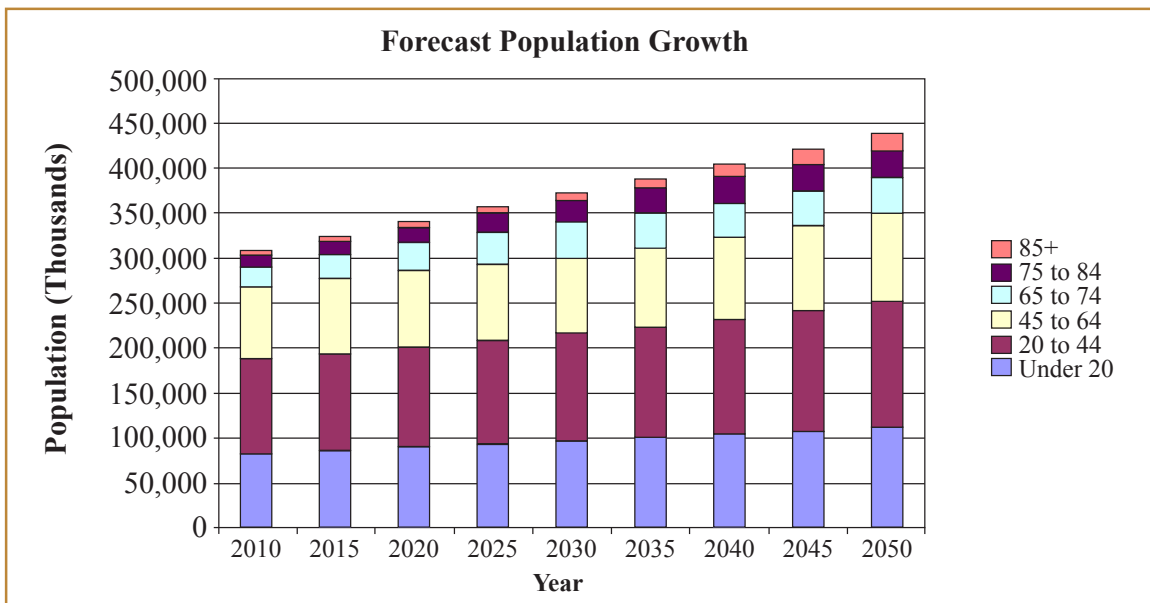
Another type of care is Alzheimer's/Dementia care, which is normally provided using an assisted living license and is generally considered a subset of assisted living. Many properties feature a combination of care types, such as assisted and independent living. CCRC stands for a continuing care retirement community. A true CCRC includes independent living, assisted living and nursing care, but the term is also often applied to any entry fee facility even if it does not offer the full spectrum of care.

2010 SENIORS HOUSING OUTLOOK

Demand Trends

There is no denying that the demographic trends impacting the seniors housing sector are positive. As of the 2000 Census, there were 34.1 million elderly Americans (those aged 65 and older), making up nearly 13% of the total population. The elderly population is expected to more than double by the year 2030 to 72 million, to make up 19% of the total population. As of the 2000 Census, there were 3.8 million Americans aged 85 and older, just over 1% of the total population. This population is expected to more than double by 2030 and become 2.3% of the total population. In 2050, as many as one in five Americans could be elderly.

Much of the forecast growth will occur between 2010 and 2030, when the “Baby Boom” generation enter their elderly years. This is most apparent when comparing growth rates. Between 2010 and 2030, the overall US population is forecast to grow at an annual pace of 0.9% per year. But growth in all three elderly sectors is much stronger: 3.0% per year for the 65+ population; 2.9% per year for the 75+ population and 2.1% per year for the 85+ population. These strong rates of growth will lead to growing demand for seniors housing.



2010 SENIORS HOUSING OUTLOOK

Supply Trends

The supply of senior apartments and independent living is typically expressed in terms of units, while assisted living and nursing supply is expressed in terms of beds. The *2009 Seniors Housing Construction Trends Report* published by the American Seniors Housing Association estimated there were 2,035,303 units/beds in 2008 in the 100 largest MSAs, with 41,040 under construction. Assuming these were all completed in 2009, year end 2009 supply was about 2,076,343 units/beds in the 100 largest MSAs. These MSAs are 66% percent of the total US population. So, assuming the remainder of the country to have a similar ratio of supply to population, the total inventory of senior apartment units, independent living units, assisted living beds and nursing beds is about 3,146,000 units/beds.

Assuming no change in industry acceptance and growth in demand of roughly 3% per year, the industry will need to add about 94,000 units/beds a year to keep up with demand. Between 2010 and 2030 this means the existing supply will need to increase by about 60%. But this likely understates the level of demand that will be experienced as it is evident that seniors housing utilization rates are rising as the industry matures and the public becomes more knowledgeable about the myriad of seniors housing options available to them.

As of the third quarter of 2009, the supply of new units under construction in the top 100 MSAs was only 22,000 units/beds according to NIC MAP. This is well below the level needed to meet new demand. Furthermore, with construction financing exceptionally difficult to obtain at present, it is anticipated that the number of new units/beds added to the market will remain very low through at least 2012.

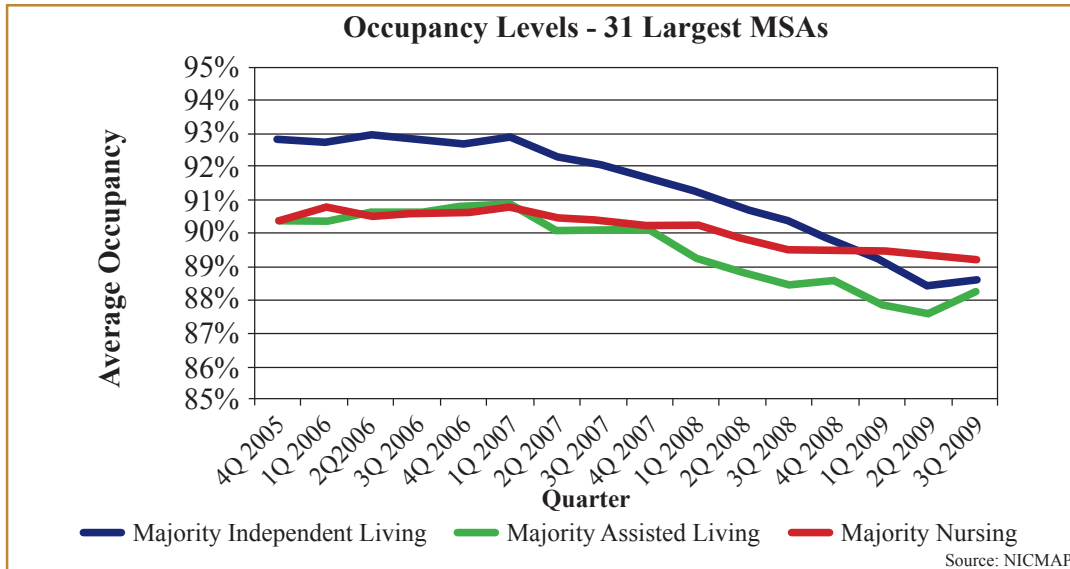
Occupancy Trends

Despite the positive long term demand outlook for seniors housing, each of the three primary seniors housing types was negatively impacted by the national recession that began in December of 2007. According to NIC MAP independent living occupancy levels decreased the most, from 92.3% in the first quarter of 2007, to a low of 88.0% in the second quarter of 2009 (for product in the 31 largest MSAs). This was caused by issues in the housing market and the decline in consumer confidence, which forced many seniors to delay this lifestyle choice. It appears that the market is now in recovery, with occupancy trending up in the third quarter of 2009.

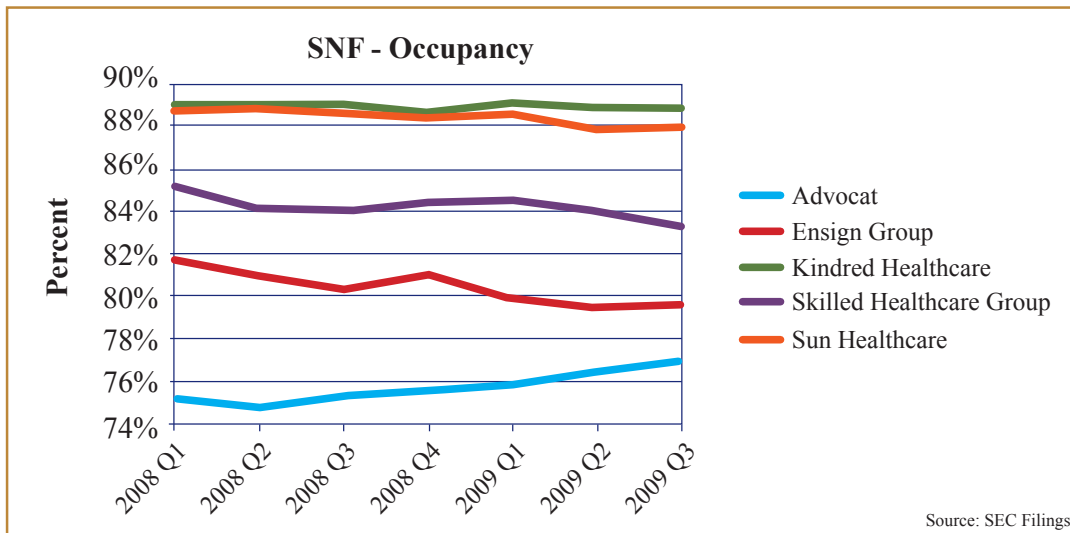
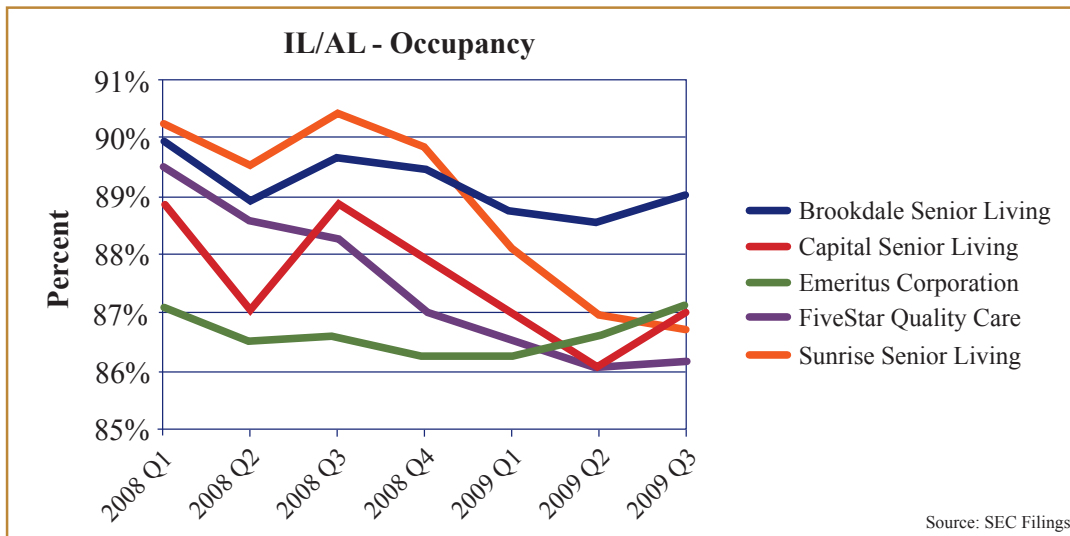
Assisted living, which is more need based, was impacted to a lesser degree. Still, assisted living and dementia care occupancy levels did fall in 2007, 2008 and the first half of 2009. It is apparent that caregivers had been delaying the decision to move a loved one into a facility. As a result, seniors entering assisted living facilities are frailer. Occupancy in the 31 largest MSAs stood at 88.3% for the third quarter of 2009, down from 91.1% in the first quarter of 2007.

Lastly, the skilled nursing sector has been experiencing a very slow decline in occupancy nationally. For the third quarter of 2009, nursing home occupancy levels stood at 89.1%, down from 90.9% in the first quarter of 2007. Since the majority of nursing home stays are funded by Medicaid, Medicare and private insurance, the financial health of the senior and their family is less of an issue, thus the impact on occupancy due to the recession has been less dramatic.

2010 SENIORS HOUSING OUTLOOK



The same trend in occupancy may be seen in the quarterly occupancy figures reported by the largest public operators, as shown in the following charts.



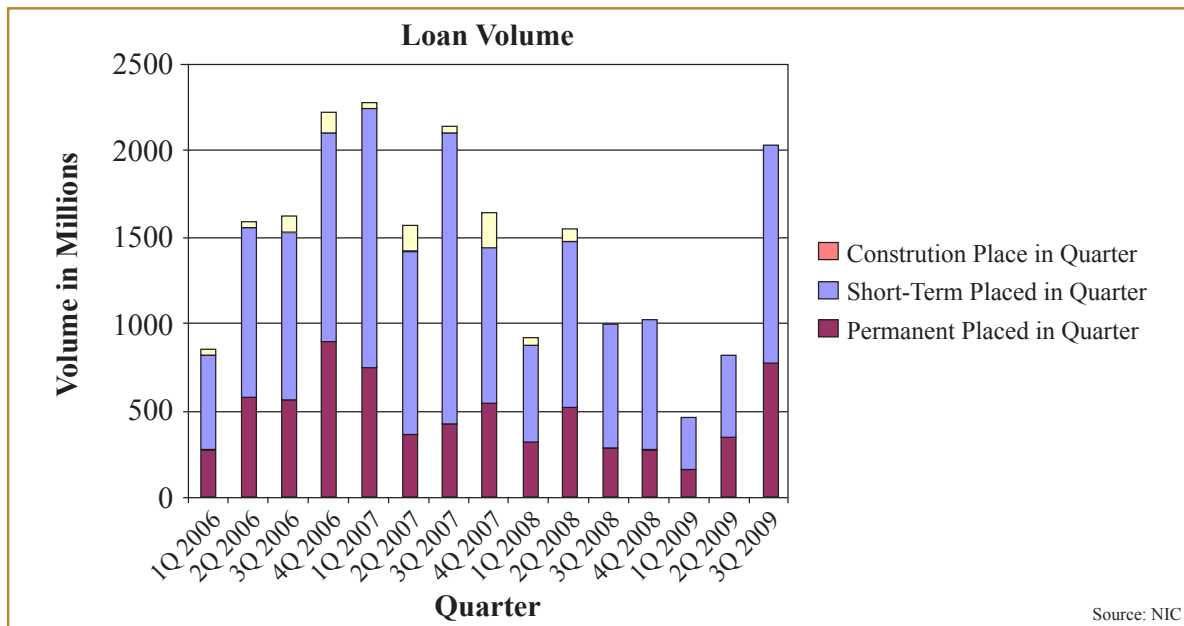
2010 SENIORS HOUSING OUTLOOK

Capital Markets

Seniors housing has not been immune to the credit crunch. CMBS debt, used to fund some of the sector's large transactions such as the sales of ManorCare and Holiday Retirement, is not available at present. Banks have severely curtailed lending volume to seniors housing, and tightened underwriting. Non-bank sources such as GE Capital are still active, but to a much lesser extent than prior to the credit crunch.

A saving grace has been the continued availability of financing through the GSEs – HUD, Fannie Mae, and Freddie Mac. All three continue to lend. But of the three, only HUD provides construction financing, and the volume of seniors housing construction loans closed by HUD has been extremely low. Still, for stabilized properties, the GSEs offer attractive loan terms. Continued availability of financing from the GSEs is needed for the industry to continue to grow and meet the needs of the nation's aging population.

Loan volume by type for the lenders that report volume to NIC is shown below.



Source: NIC

Loan performance in the seniors housing sector remains strong. As of the third quarter of 2009, the lenders that report statistics to NIC reported that 98.5% of seniors housing loans were performing, within only 0.6% restructured and 0.9% delinquent.

The REITs in the seniors housing industry have fared pretty well over the past five years when looking at total assets, with the majority showing an upward trend. Six of the nine REITs we are tracking have had an increase in total assets from 2007 to 2008, most notably Senior Housing Properties Trust who has had an increase of 47%. This shows that these REITs are able to thrive even when the capital markets are frozen and not too many acquisitions are occurring. Needless to say, the larger acquisition opportunities have become less prevalent; so much of their focus has been on smaller acquisitions and asset management. Recently, several of the larger REITs have announced their intention to begin to aggressively pursue acquisitions.

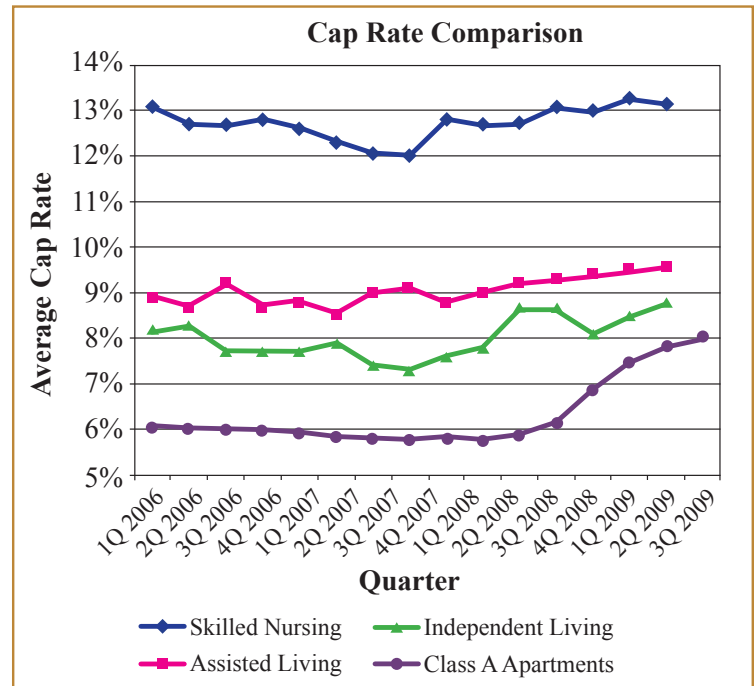
While loan performance is generally strong, there are some distressed deals in the seniors housing sector. These range from the large Sunwest Management portfolio to ill conceived "one-off" deals put together by inexperienced developers. There are a lot of vulture funds looking to pick off these distressed deals, but we believe that the majority will be worked out in some fashion, with only a trickle of deals selling at steep discounts.

2010 SENIORS HOUSING OUTLOOK

Capitalization Rates

Historically, seniors housing capitalization rates have moved in lock step with cap rates for other asset classes (the sole exception being SNF cap rates which have remained in a fairly narrow band).

Looking forward, the other asset classes are going to be impacted by the huge wave of CMBS debt maturities, which peaks in 2013. Many loans will not qualify for refinance, so many are likely to go into default or have negotiated modifications, which will create additional stress in the market. This alone could lead to rising cap rates. In addition, demand for office space, retail space, industrial space and apartments is likely to be stagnant for several years. Add to that the potential for rising inflation and interest rates, and it is evident that there is a much higher probability that cap rates will rise rather than decrease in the four primary sectors.



On the other hand, seniors housing is becoming more and more attractive to investors, who view it as being somewhat recession resistant. Furthermore, due to the aging population, demand for seniors housing is increasing, while the supply is not likely to grow much over the next few years due to limited availability of construction financing. These dynamics will likely lead to increased investor activity in the seniors housing sector, which may serve to compress capitalization rates relative to other sectors of the market.

2010 Forecast

It appears that occupancy levels bottomed out in 2009 and absent a setback in the economic recovery will begin to improve. The exception is nursing home occupancy levels which have been relatively stable throughout the recent past. There is very little new construction underway in the seniors housing market, but demand will continue to grow and should remain stable. Thus, it is likely that occupancy levels and rent levels will increase for several years as supply tightens.

New capital is likely to continue to flow into the sector. The REITs that focus on seniors housing have built large war chests of funding, and will need to deploy it over the next few years. In addition, a number of institutional and opportunity funds have been raised and are seeking opportunities to invest this capital. Even banks are starting to lend again, although the volume of bank lending remains very low. While 2009 saw very few sales transaction, it is expected that 2010 will see many more deals get closed. Due to sound fundamentals and the opportunities for income growth, we do not expect to see capitalization rates increase much, if any, over 2009 levels.

One wild card is health care reform. Any bill impacting Medicaid and/or Medicare reimbursement for nursing homes, or impacting health insurance costs for operators could negatively impact the seniors housing industry as a whole. However, with the recent election of Republican Scott Brown in Massachusetts, it appears more and more likely that significant changes in health care will not occur.

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Integra Realty Resources, Inc. provides world-class commercial real estate valuation, counseling, and advisory services. Routinely ranked among leading property valuation and consulting firms, we are now the largest firm in the United States, with more than 55 local offices coast to coast.

IRR's Seniors Housing and Health Care Specialty Practice provides valuation and consulting services to a wide array of clients involved in the seniors housing and health care sectors. From 2002 through-2009, the Specialty Practice completed in excess of 3,000 assignments related to seniors housing and health care properties. Assignments have been completed in all 50 states, the District of Columbia, and Canada.