

Standing Out From a Crowd:
Seniors Housing Occupancy and Absorption Rise in the Third Quarter

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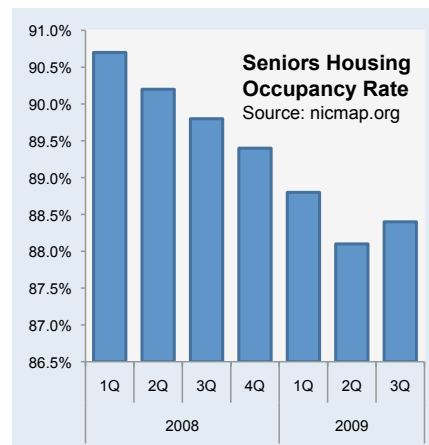
Monday, December 14, 2009 – Notwithstanding a resumption of growth in sundry measures of economic activity, multifamily and commercial real estate fundamentals continue their slide across the swath of US metropolitan areas. Real Estate Econometrics projects that national occupancy rates will only stabilize in late 2010 and 2011, first in the apartment and industrial sectors; later, at office and retail properties. In contrast, the third quarter's seniors housing occupancy and rent trends evince the sector's distinct relationship to broader economic and housing market conditions. Across the nation's metropolitan areas, seniors housing rent growth has slowed as occupancy rates have edged down. But by both measures, the sector has thus far avoided core commercial real estate's more precipitous slump in fundamentals. In fact, the seniors housing occupancy rate rose in the third quarter as absorption surpassed completions for the first time in almost three years. Whether a trend of rising occupancy rates develops and can be sustained depends upon whether absorption holds up in parallel with the next year's elevated inventory additions.

Headline Trends in Seniors Housing

The National Investment Center for the Seniors Housing and Care Industry (NIC) announced the results of its third quarter property data collection and aggregation just before the Thanksgiving holiday. Both in terms of asking rents and occupancy rates, the seniors housing sector is able to boast broad-based, albeit modest, improvements in fundamentals in the three months ended September 30.

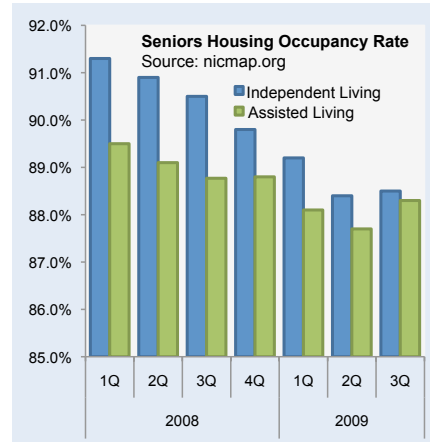
The occupancy rate of seniors housing increased by 30 basis points between the second and third quarters – rising to 88.4 percent – in spite of material additions to the national inventory. In fact, absorption strengthened markedly in the third quarter, eclipsing the trend rate of the previous three and a half years to reach the highest level in NIC's record. The resulting improvement in the occupancy rate, the first in two and a half years, follows a sustained period of deterioration: over the last year, the seniors housing occupancy rate has fallen by 140 basis points; peak-to-current, the occupancy rate has fallen by 380 basis points.

As the seniors housing occupancy rate has edged up, year-over-year asking rent growth has slowed but has remained positive. Like the occupancy rate, asking rent growth peaked in the first quarter of 2007. Since then, it has slipped from 4.7 percent to 1.8 percent in the third quarter of 2009.



Dimensions of Variation

Disaggregating the headline measures of the sector's performance, variation in property types within the seniors housing sector is as rich as for any class of core commercial real estate. In the independent living (IL) sector, which accounts for roughly two-thirds of the national seniors housing inventory, the occupancy rate increased from 88.4 to 88.5 percent in the third quarter. Similar to the headline trend, rent growth at IL properties slowed from 2.4 percent in the second quarter to 1.7 percent in the third. At assisted living (AL) properties, which account for the balance of seniors housing properties, the occupancy rate jumped 60 basis points, from 87.7 percent in the second quarter to 88.3 percent in the third. Rent growth was relatively stronger than for IL properties, slowing by just 10 basis points, from 2.1 percent year-over-year in the second quarter to 2.0 percent in the third.



Only a small subset of properties report year-over-year declines in rents. The slowdown in rent growth is evident, however, in the plurality of properties that report increases below 1.0 percent. Illustrative of the nuanced relationship between macroeconomic and housing market trends and seniors housing performance, metro areas reporting the strongest rent growth include Baltimore, Boston, Philadelphia, Portland (Oregon), and St. Louis.

Retirement Communities The occupancy rate for continuing care retirement communities (CCRCs) with an entrance fee model[‡] increased by 20 basis points in the third quarter. In spite of a 410 basis point decline in peak-to-current occupancy rates, the average entrance fee increased by 0.9 percent from the second to third quarters, rising to just over \$240,000. Entrance fees have trended up by 2.2 percent over the last year. Both in terms of occupancy rates and rent growth, entrance fee CCRCs continue to outperform rental retirement communities in spite of negative spillovers from the housing market.

Newer entrance fee CCRCs are showing evidence of strains from the interplay with housing. Cancellations have increased at these properties even as operators have offered larger concessions. Stabilization in house prices and an uptick in sales activity may temper these pressures, however. Thus far, households for whom the sale of a primary residence has been a necessary condition for transitioning to an entrance fee community have been constrained, to the greatest extent in markets where the housing downturn has been most severe. On account of new properties representing a de minimis share of in-place inventory, the middling uptake of units at newer properties is not readily observable in the more stable, aggregate statistics.

The Outlook

The relative stability of the seniors housing sector is in contrast with the continuing deterioration in core commercial fundamentals that has necessarily followed the inward shift of the economy's aggregate demand curve. Long-term, demographic trends will continue to support the seniors housing sector and fuel demand for new space. In the short- and medium-term, however, the downturn in the economy and housing market, and constraints on credit availability, still present challenges for the development and operation of seniors housing properties. Inevitably, these challenges are leading to more observable variation across operators of differing skill and experience.

[‡] CCRCs include communities that charge an entrance fee for the right of occupancy as well as a recurring fee, and those that do not charge an entrance fee and derive their revenues primarily from rents and fees.