

CBRE U.S. Healthcare Capital Markets



2018

Healthcare Real Estate Investor
& Developer Survey Results

CBRE

2018 HEALTHCARE REAL ESTATE INVESTOR & DEVELOPER SURVEY RESULTS

Dear Healthcare Real Estate Providers, Investors & Developers,

CBRE's U.S. Healthcare Capital Markets is pleased to present the 2018 findings of our ninth annual Investor & Developer Survey. In developing the survey, our main objective was to identify key patterns and forces influencing the healthcare real estate industry, which we hope will help our clients to better understand the state of the market and the projected trends over the next year.

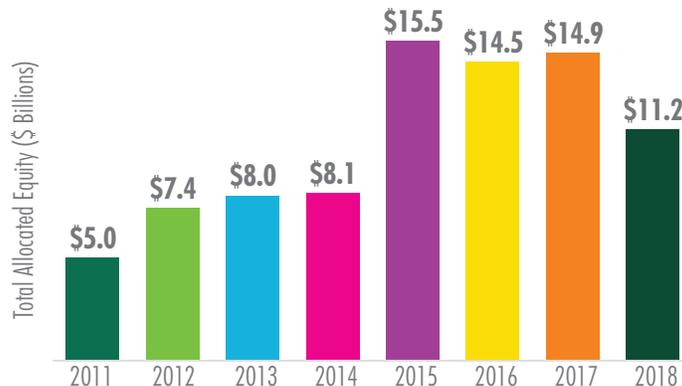
METHODOLOGY

- This year's survey contained 24 questions surrounding various facets of the healthcare real estate market.
- The survey was distributed to approximately 500 of healthcare real estate's most influential real estate investment trusts (REITs), private capital investors, and developers throughout the United States, with 109 providing responses.
- To ensure the accuracy of our survey results, we removed all duplicate responses from the same firms to attest we do not overstate results or demand within the market.

HIGHLIGHTS

This primary research produced qualitative industry data that provides a snapshot of investor and developer return requirements, investment criteria, and – most importantly – the market shifts and progressions these key influencers anticipate in the near future. Some of the more interesting findings resulting from this year's survey include:

INVESTMENT CRITERIA: When asked about the amount of equity their firm has allocated to healthcare real estate investment and development activity in 2018, the total for all the firms combined equated to nearly \$11.2 billion, which is approximately 25% lower than the estimated \$14.9 billion that was reported in our 2017 survey results. However, while the amount reported in the survey results is lower than previous years, it is important to note that only 15% of the unique firms surveyed consider themselves healthcare REITs or institutional healthcare investors. In addition, the amount of equity estimated in 2018 is still higher than in prior years 2011-2014 and is approximately 110% of the total market transaction volume that traded in 2017.



RETURN REQUIREMENTS: Value for core product, namely Class “A” on-campus medical office buildings, continues to be high with 44% of the survey respondents reporting that cap rates are projected below 5.50%. There also continues to be a spread in cap rates between core Class “A” and Class “B” medical office product; however, the survey results show that the cap rate spread between Class “A” on-campus and off-campus product types narrowed significantly between the 2017 to 2018 survey. We believe this reflects the growing supply of high-quality medical office buildings that are strategically positioned away from campus by health systems. Many of these assets are positioned in affluent, high-growth, suburban secondary and tertiary markets as healthcare providers continue to establish themselves closer to patients’ residences and seek to gain market share. Half of respondents (50%) expect cap rates for Class “B” off-campus product to be in the range of 6.00% - 6.99% in 2017.

PLANNED INVESTMENT ACTIVITY: 77% of the respondents classified themselves as a “Net Buyer” of medical office buildings for 2018, representing a 1% decrease year-over-year from 2017.

SUPPLY & DEMAND: Respondents reported that they expect supply and demand to largely remain stable across every healthcare real estate asset type in 2018 when compared to 2015, 2016 and 2017. For medical office specifically, nearly half of respondents (47%) expect demand to increase in 2018. It is clear that the supply-demand imbalance will continue as the total allocation of funds to purchase medical office buildings is far greater than the available supply of medical office buildings.

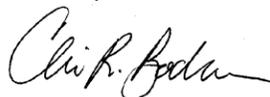
MARKET FUNDAMENTALS: Market leasing fundamentals have continued to strengthen over the last year. 54% of respondents reported that their medical office portfolio occupancy rate has increased compared to a year ago, while just 3% reported a lower occupancy rate.

HEALTHCARE REFORM: In our 2017 survey we included two questions related to expected changes to the Patient Protection and Affordable Care Act. More than half of the respondents believed that the new administration would eliminate the individual mandate for coverage, rollback Medicaid funding, and limit the state and federal insurance marketplace exchanges. In exchange, more than half of the respondents also believed the new administration would support healthcare insurance to be sold across state borders, expand the use of private Health Savings Accounts, and have the government negotiate drug prices for Medicare/Medicaid. Of these predictions, several came to fruition via an executive order signed by President Trump in October 2017 and new tax reform in December 2017. Resulting policy changes include the elimination of the individual mandate, permitted sale of health insurance policies across state lines, and increased HSA contribution limits. Congress was unable to pass a bill to reform healthcare in 2017, but new proposed legislation will likely return during 2018.

We would be pleased to create a customized benchmark comparison of the responses of your firm to responses from the national sample. Please contact the U.S. Healthcare Capital Markets via email at either chris.bodnar@cbre.com or lee.asher@cbre.com to coordinate a presentation of our findings or request a personalized benchmarking of your firm’s assets.

Thank you to all the participants in this year’s survey.

Sincerely,



Chris Bodnar
Vice Chairman
CBRE U.S. Healthcare Capital Markets



Lee Asher
Vice Chairman
CBRE U.S. Healthcare Capital Markets



Ryan Lindsley
Senior Director
CBRE U.S. Healthcare Capital Markets



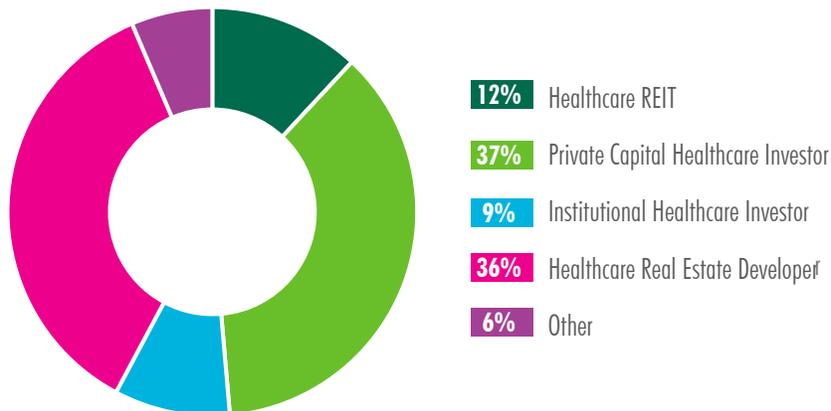
Sabrina Solomiany
Senior Director
CBRE U.S. Healthcare Capital Markets

PROFILE OF PARTICIPATING FIRMS

We received feedback from a diverse mix of respondents, with no single investor or developer category making up more than 37% of the result set. Healthcare real estate investment trusts (REITs) comprise 12% of the survey set, private capital healthcare real estate investors comprise 37% of the survey set, institutional healthcare real estate investors comprise 9% of the survey set, and healthcare real estate developers comprise 36% of the survey set.

Please describe the type of company you represent:

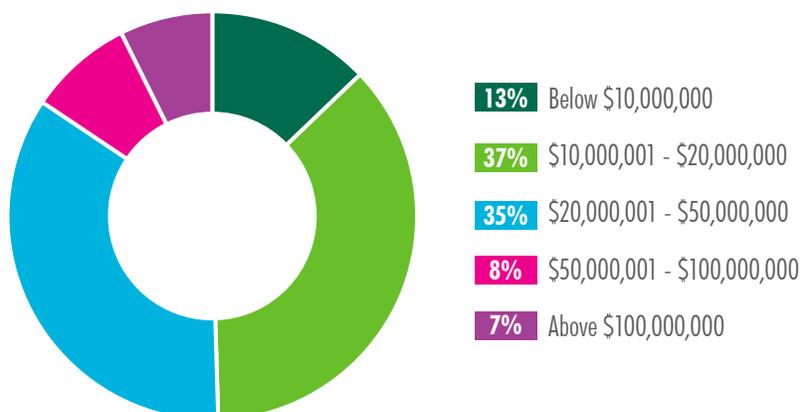
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INVESTMENT CRITERIA

What is your preferred healthcare real estate transaction size?

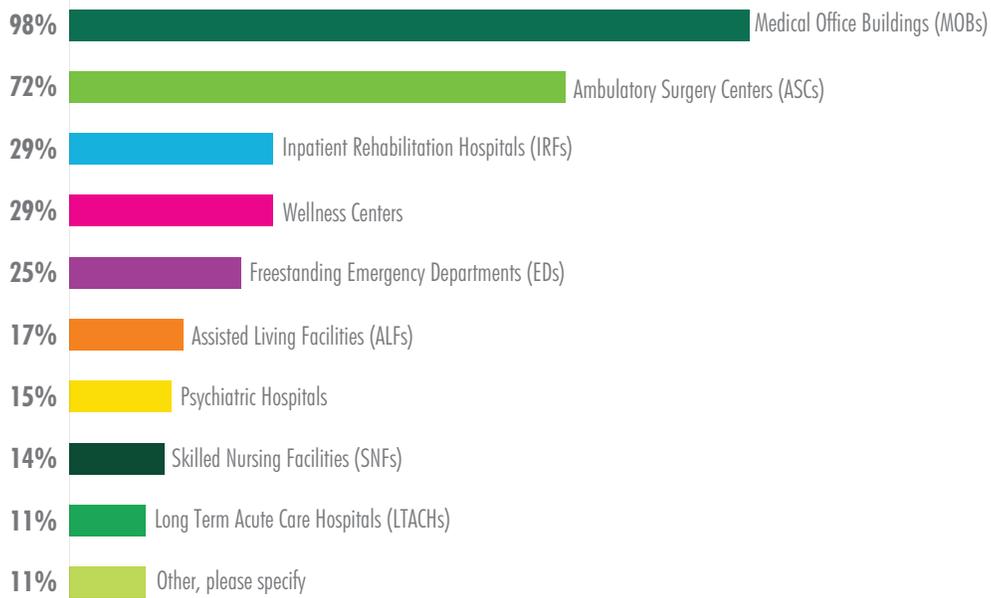
When asked to identify their preferred healthcare real estate transaction size, the majority of respondents (72%) were split between healthcare real estate transactions with a value of '\$10,000,001 - \$20,000,000' and transactions valued at '\$20,000,001 - \$50,000,000'. This response was especially consistent with those who classified themselves as developers and private capital investors. Developers and institutional investors represent 89% of respondents that prefer transactions with a value between '\$50,000,001 - \$100,000,000', while 63% of respondents that preferred healthcare real estate transactions 'Above \$100,000,000' were publicly traded healthcare REITs.



INVESTMENT CRITERIA

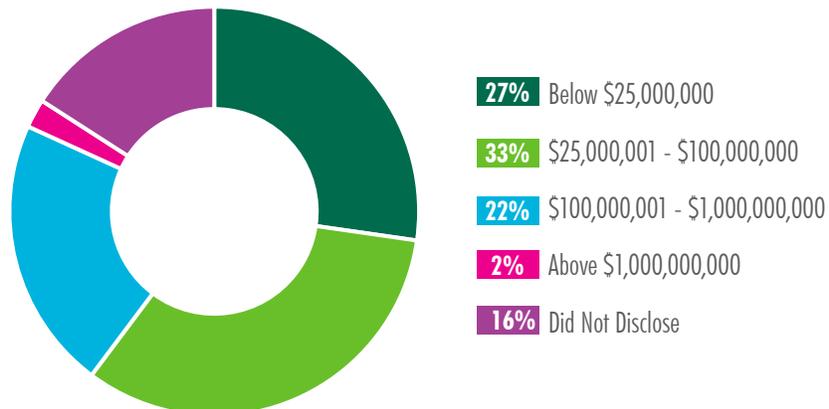
What type of healthcare real estate properties meet your acquisition criteria?

In 2018, once again, the vast majority of respondents indicated that they were most interested in Medical Office Buildings (98%) when asked which types of healthcare real estate properties meet their acquisition criteria. Inpatient Rehabilitation Hospitals (IRFs) saw the largest increase, up 6% over 2017. Assisted Living Facilities and Freestanding Emergency departments both saw double-digit declines at 11% and 10%, respectively year-over-year.



How much equity has your firm allocated to healthcare real estate investment and development activity in 2018?

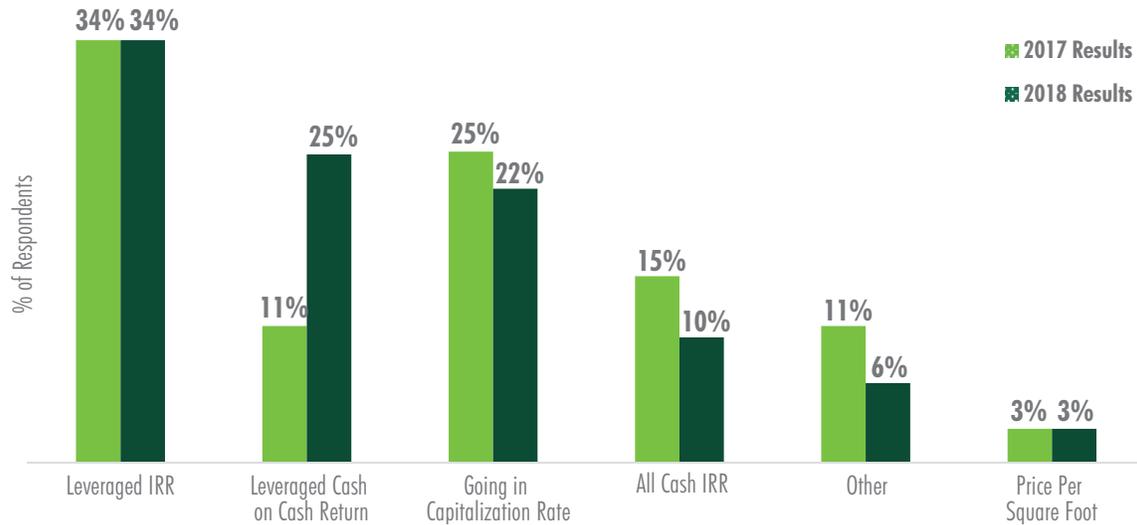
Of the 86 exclusive firms who responded to this question, 63 disclosed an approximate total of \$11.2 billion worth of equity that has been allocated for healthcare real estate investments and developments in 2018, which is approximately 110% of the total market transaction volume that traded in 2017. This represents a sharp decrease from the amount of equity allocated in 2017, but it is important to note that of the 63 unique firms who responded to this question, only 9 consider themselves either a 'Healthcare REIT' or an 'Institutional Healthcare Investor'.



INVESTMENT CRITERIA

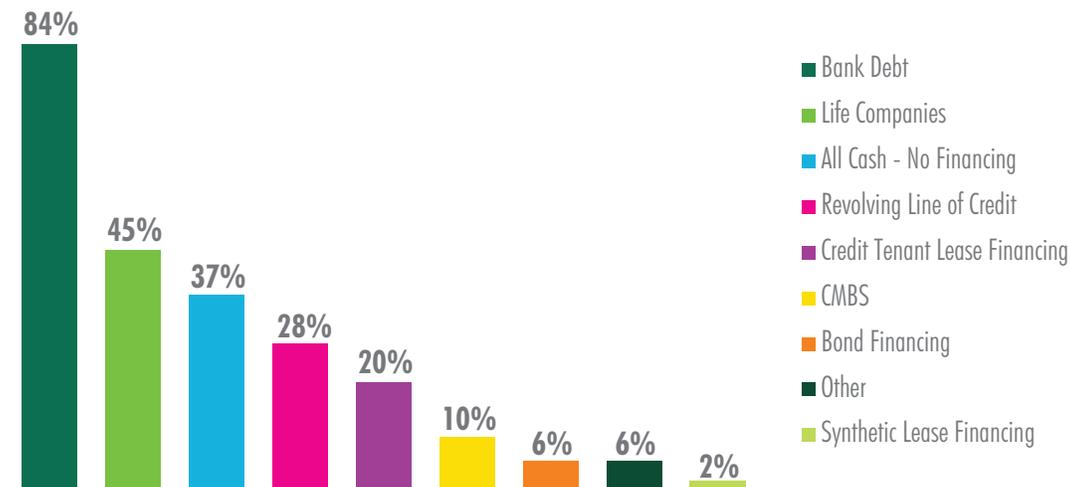
What measurement of investment return do you rely on most?

The majority of respondents identified 'Leveraged IRR' (34%) as the investment methodology they relied on most, followed by 'Leveraged Cash on Cash Return' (25%), 'Going in Capitalization Rate' (22%) and 'All Cash IRR' (10%). 'Leveraged Cash on Cash Return' had the largest year-over-year increase, with a 14% positive change over 2017's results. Developers and healthcare REITs dominated the selection for the 'Going in Capitalization Rate' category with approximately 71% of the responses. The bulk of respondents that chose 'Leveraged Cash on Cash Return' or 'Leveraged IRR' as the investment methodology they relied on most were private investors and developers at 85% and 86%, respectively.



What types of financing sources are you utilizing?

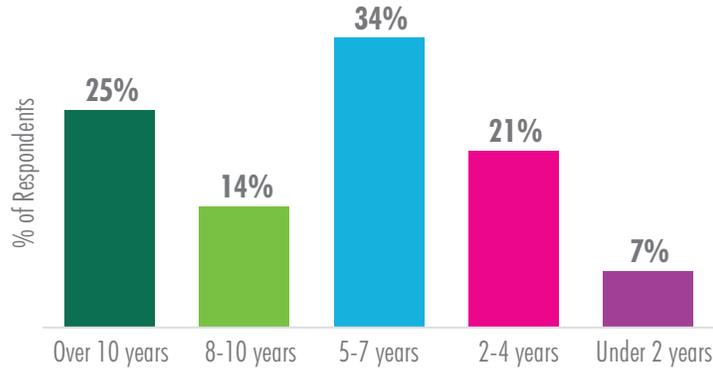
Among respondents, 'Bank Debt' ranked as the number one financing source (84%), followed by debt from 'Life Companies' (45%), then 'All Cash' (37%) from funds on their balance sheet. 85% of the healthcare REIT respondents declared that they would use 'All Cash - No Financing'. 95% of developers declared that they would use 'Bank Debt', but only 15% of developers would use 'All Cash'.



INVESTMENT CRITERIA

What is the average hold-time frame for your medical office investments?

While there was a wide variation for the average hold-time for the respondents' healthcare real estate investments, '5-7 years' ranked number one (34%), followed by 'Over 10-years' (25%) then '8-10 years' (14%), then '2-4 years' (21%), and lastly 'Under 2-years' (7%). 85% of the healthcare REITs who responded indicated 'Over 10-years' as their average hold time, while healthcare real estate developers were the only type of company to indicate 'Under 2-years'.



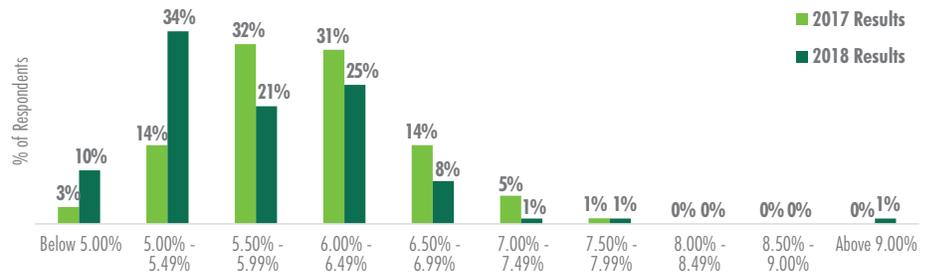
RETURN REQUIREMENTS

What will be a “market” capitalization rate for multi-tenant medical office in 2018?

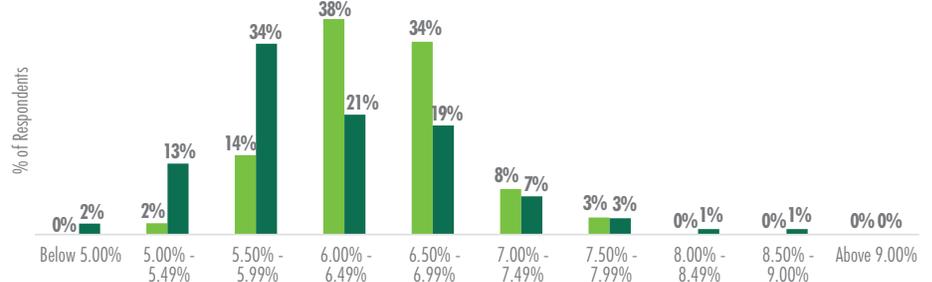
The Class “A” on-campus medical office product type continues to price at the most aggressive levels over Class “A” off-campus medical office product; although, the Class “A” off-campus medical office product made large strides in the 2018 results and continues to narrow the difference. Approximately 44% of the respondents indicated that a market capitalization rate for Class “A” on-campus product would be below 5.50%, compared to 17% of respondents in 2017. Meanwhile, 49% of the survey respondents indicated that a market capitalization rate for Class “A” off-campus product would be below 6.00%, versus 16% of respondents in 2017. We attribute this trend to the continued increase in demand for high-quality healthcare real estate and new capital sources that are actively seeking alternatives to traditional real estate investment products.

The Class “B” on-campus medical office buildings priced slightly less aggressive than the Class “A” off-campus product type. 81% of the survey respondents indicated that a market capitalization rate for Class “B” on-campus would be less than 7.00%, compared with 72% of respondents the previous year. Class “B” off-campus medical office priced at the least aggressive levels with 56% of the survey respondents indicating that a market capitalization rate for this product type would be less than 7.00%, versus 38% of respondents in the 2017 results.

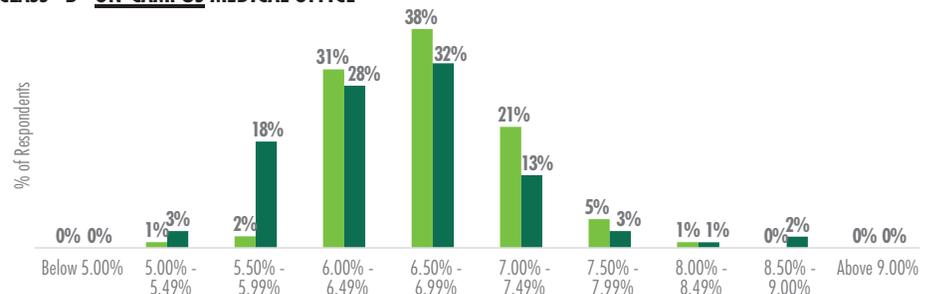
CLASS “A” ON-CAMPUS MEDICAL OFFICE



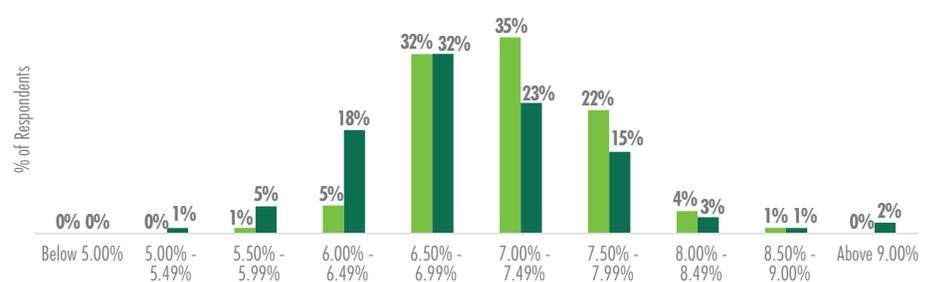
CLASS “A” OFF-CAMPUS MEDICAL OFFICE



CLASS “B” ON-CAMPUS MEDICAL OFFICE



CLASS “B” OFF-CAMPUS MEDICAL OFFICE



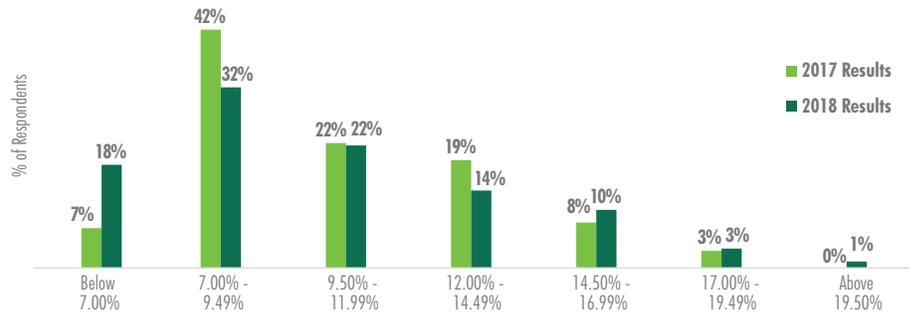
RETURN REQUIREMENTS

What is your target 10-year Internal Rate of Return (All-Cash) for multi-tenant medical office in 2018?

Survey respondents indicated a wide spread in their 10-year target all-cash Internal Rate of Return (IRR) requirements for 2018 depending on the product type. Target all-cash IRRs for Class “A” on-campus product between ‘7.00% - 9.49%’ decreased substantially from the previous years’ results, as only 32% of respondents indicated this was their target range for 2018, compared to 42% in 2017. However, a group of respondents indicated more aggressive underwriting with 18% indicating a target all-cash IRR ‘Below 7.00%,’ compared to 7% in 2017. Target all-cash IRRs for Class “A” off-campus product were slightly more aggressive in 2018 with 36% of respondents indicating that their target all-cash IRR is between ‘7.00% - 9.49%’ compared to 32% in 2017, and 7% of respondents indicating a target ‘Below 7.00%’ compared to only 1% in 2017.

Investor attitude for Class “B” on-campus product targeting an IRR between ‘7.00% - 9.49%’ strengthened year-over-year, with 30% of respondents now indicating an interest within this range, compared to 18% in 2017. The survey results for Class “B” off-campus were wide-ranging as approximately 63% of respondents indicated a target all-cash IRR between 9.50% - 16.99%.

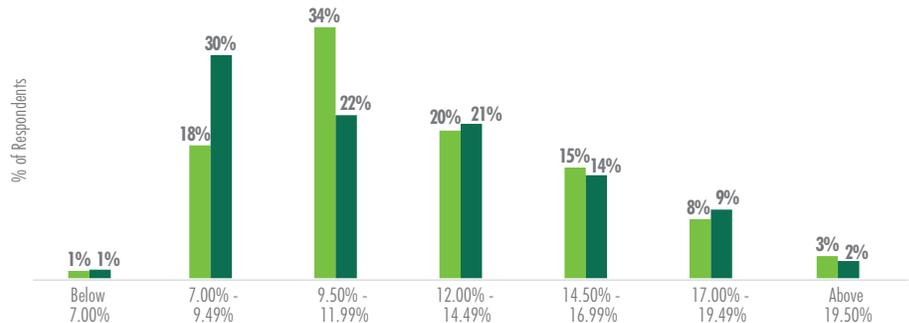
CLASS “A” ON-CAMPUS MEDICAL OFFICE



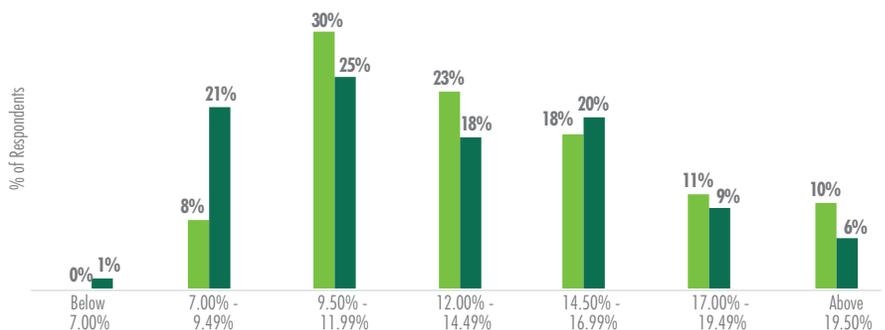
CLASS “A” OFF-CAMPUS MEDICAL OFFICE



CLASS “B” ON-CAMPUS MEDICAL OFFICE



CLASS “B” OFF-CAMPUS MEDICAL OFFICE



RETURN REQUIREMENTS

What will be a “market” capitalization rate for the following single-tenant healthcare investments in 2018? Assume 10-years of lease term remaining and average credit.

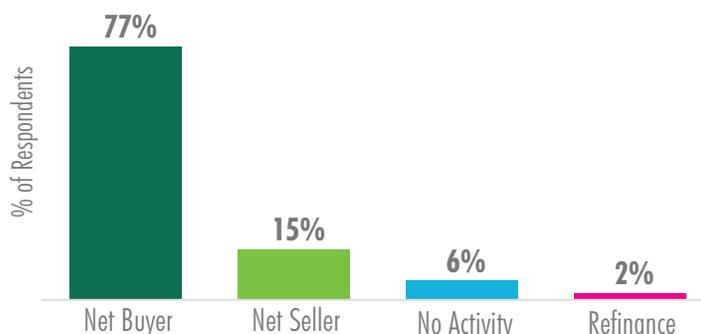
Net lease medical properties continue to be the focal point from an investment perspective, remaining steadfastly appealing in an ever-evolving healthcare market. Expectations that single-tenant healthcare investment pricing will continue tightening remained a common thread among respondents, as at least 50% of respondents for every asset type indicated a cap rate below 7.50%. Single-tenant Medical Office Buildings (MOB’s) are expected to remain the most competitively priced asset type, with 82% of the respondents expecting the market cap rate to be within a 4.50% - 6.49% range. Investors in single-tenant Ambulatory Surgery Centers indicated a similar expectation, with 85% of survey respondents expecting a market cap rate range between 5.00% - 6.99%.

CAP RATE	Above 9.00%	8.50% - 8.99%	8.00% - 8.49%	7.50% - 7.99%	7.00% - 7.49%	6.50% - 6.99%	6.00% - 6.49%	5.50% - 5.99%	5.00% - 5.49%	4.50% - 5.00%	4.00% - 4.49%	Below 4.00%
Medical Office Building	1%	0%	0%	0%	4%	11%	18%	24%	29%	11%	1%	0%
Freestanding Emergency Department	0%	0%	4%	10%	25%	15%	27%	15%	1%	1%	0%	0%
Ambulatory Surgery Center	0%	0%	0%	5%	9%	29%	25%	18%	13%	0%	1%	0%
Wellness Center	1%	0%	6%	14%	17%	27%	20%	10%	4%	0%	0%	0%
Acute Care Hospital	0%	0%	8%	11%	34%	20%	17%	6%	2%	0%	2%	0%
Long Term Acute Care Hospital	5%	3%	15%	25%	26%	15%	7%	3%	2%	0%	0%	0%
Rehabilitation Hospital	0%	2%	11%	21%	33%	18%	12%	2%	2%	0%	0%	0%
Psychiatric Hospital	2%	10%	20%	28%	15%	18%	5%	3%	0%	0%	0%	0%
Skilled Nursing Facility	12%	17%	18%	13%	20%	13%	3%	3%	0%	0%	0%	0%

PLANNED INVESTMENT ACTIVITY

For 2018, how would you characterize your medical office investment activity?

The overwhelming majority of survey respondents (77%) indicated plans to be “Net Buyers” of medical office product in 2018. Of these respondents, 100% of all REITs consider themselves to be “Net Buyers”, while the overwhelming majority of private and institutional investors also consider themselves to be “Net Buyers” of medical office product.

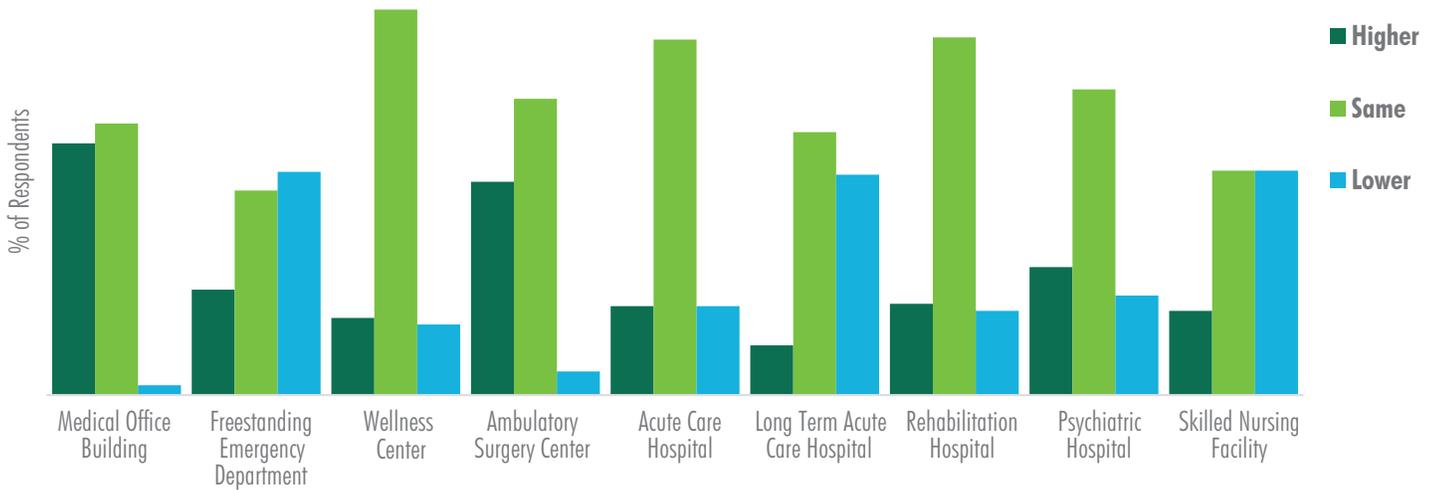


SUPPLY vs. DEMAND

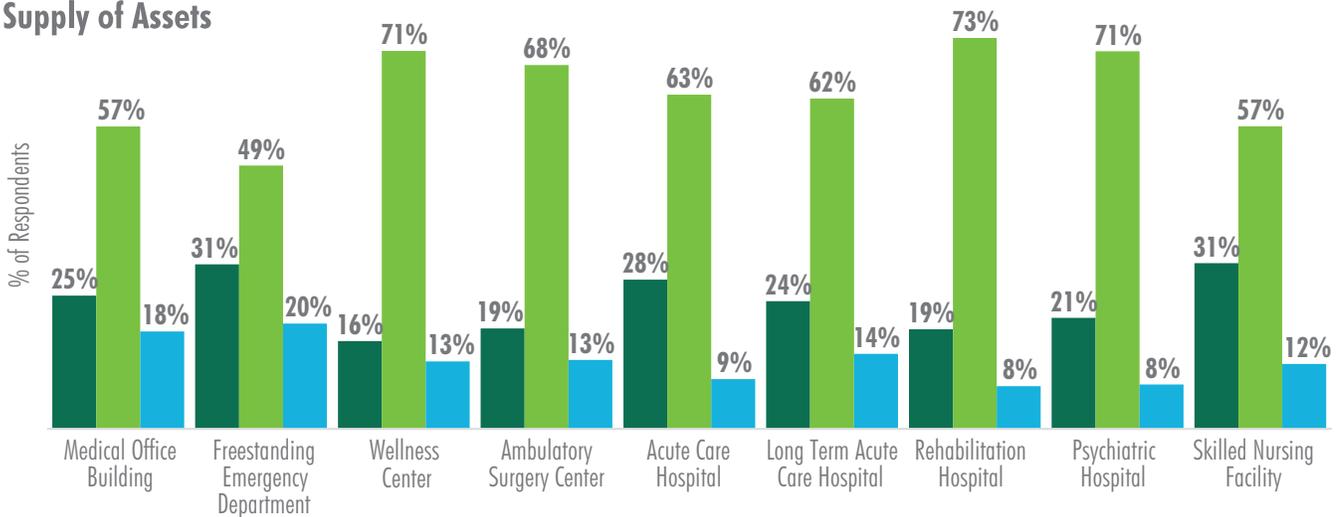
Where do you see investment demand and supply for the following product types in 2018 compared to 2017?

Respondents expect that demand and supply for nearly every healthcare real estate asset type will remain stable in 2018 when compared to 2017 levels. It is interesting to note that while the majority of respondents (51%) have projected that 'Medical Office Buildings' will have the same supply in 2018 as in 2017, 47% expect that demand will be higher this year.

Demand for Assets



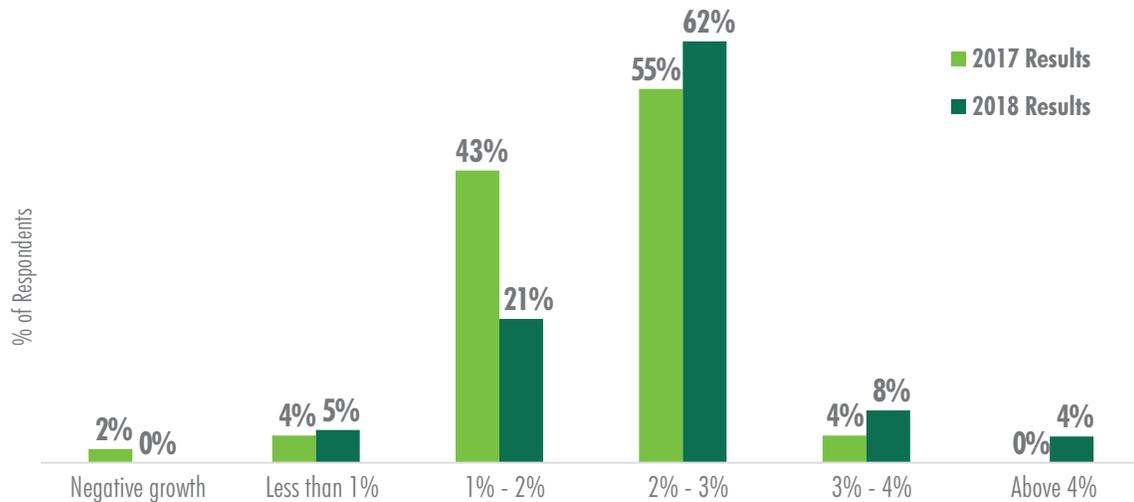
Supply of Assets



MARKET FUNDAMENTALS

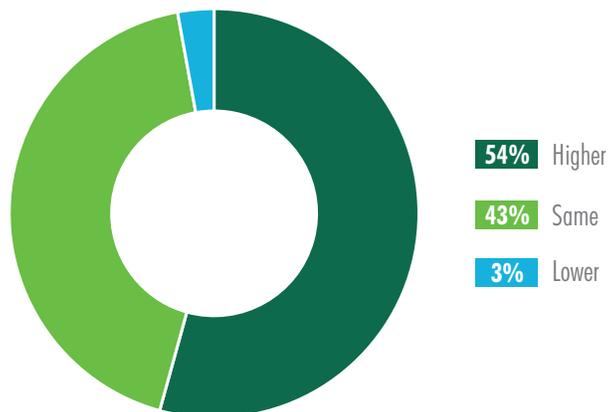
Where would you project annual growth for medical office lease rates in the coming year?

Survey respondents appear to have an expectation of rising medical office lease rates, substantiated by the 74% of responders who indicated annual rates will increase by at least 2% or more, compared to 59% in 2017. Only 5% of all respondents indicated an expectation of lease rates growing by less than 1%.



Where is the occupancy of your medical office portfolio compared to a year ago?

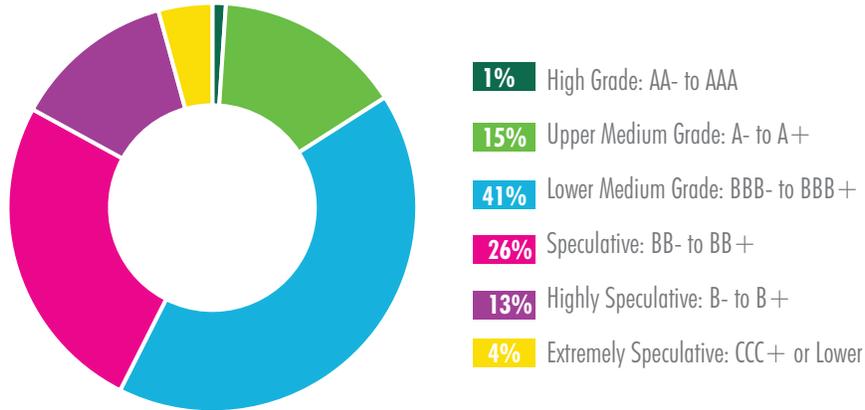
The majority of respondents (54%) stated that medical office occupancy was 'Higher' than last year, while only 3% stated that their portfolio occupancy was 'Lower' than last year. 43% of respondents stated that their portfolio occupancy was the 'Same' as last year.



HEALTH SYSTEM MONETIZATION AND DEVELOPMENT CRITERIA

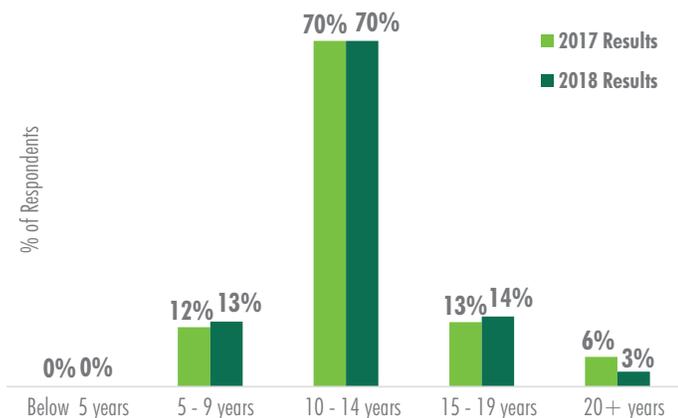
What is the minimum hospital credit rating you would consider for investment?

A portion of the survey was dedicated to medical office investors and developers seeking monetization or development opportunities with health systems. The first question inquired about the minimum hospital credit ratings preferred for real estate investment in 2018. Of those surveyed, the largest share (41%) responded with 'Lower Medium Grade of BBB- to BBB+' credit, followed by 'Speculative Grade of BB- to BB+' credit (26%), then 'Upper Medium Grade A- to A+' (15%) and 'Highly Speculative B- to B+' (13%).



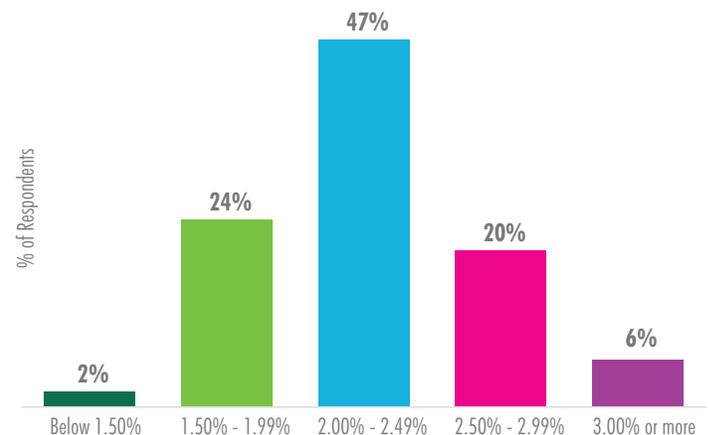
What is the minimum lease term you would consider for a sale-leaseback by a health system?

87% of the survey respondents indicated that the minimum lease term for a sale-leaseback by a health system would need to be for at least 10 years, while most of the respondents (70%) indicated a need for a lease term of at least '10 to 14 years'. In 2018, 14% of respondents indicated a minimum lease term of '15-19 years', while only 3% indicated '20+ years' as their minimum, revealing a slight increase in risk tolerance by investors.



What is the minimum annual rental rate escalation you would consider for a sale-leaseback by a health system?

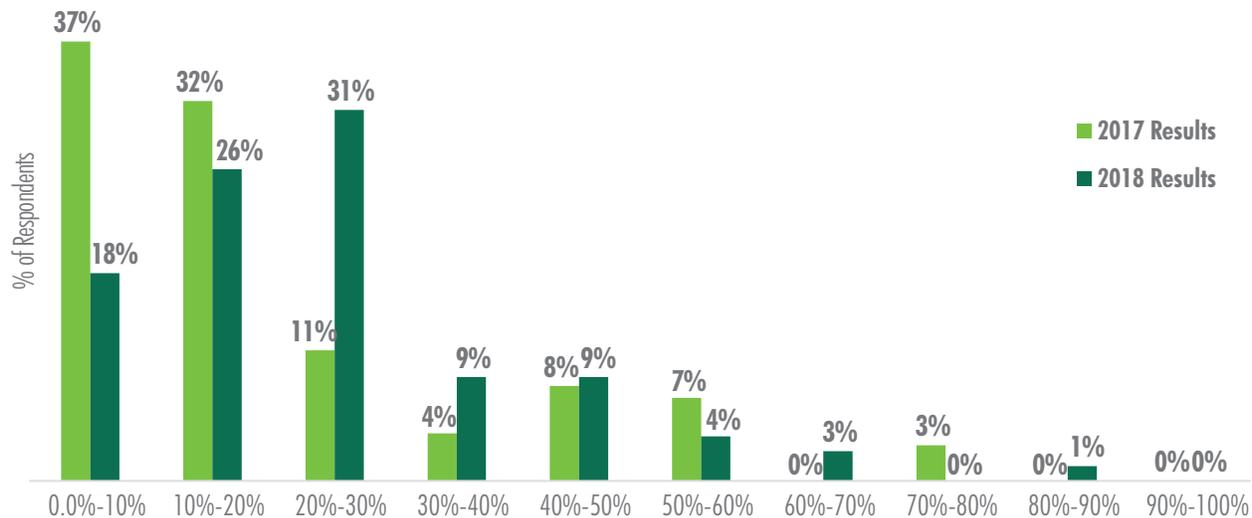
The largest group of survey respondents (47%) stated that they would require at least a '2.00% - 2.49%' annual rental rate escalation. Approximately 26% of the respondents indicated that they would accept an annual rental rate escalation of 1.99% or less, and 26% of the respondents indicated that they would require an annual rental rate escalation of 2.50% or more.



HEALTH SYSTEM MONETIZATION AND DEVELOPMENT CRITERIA

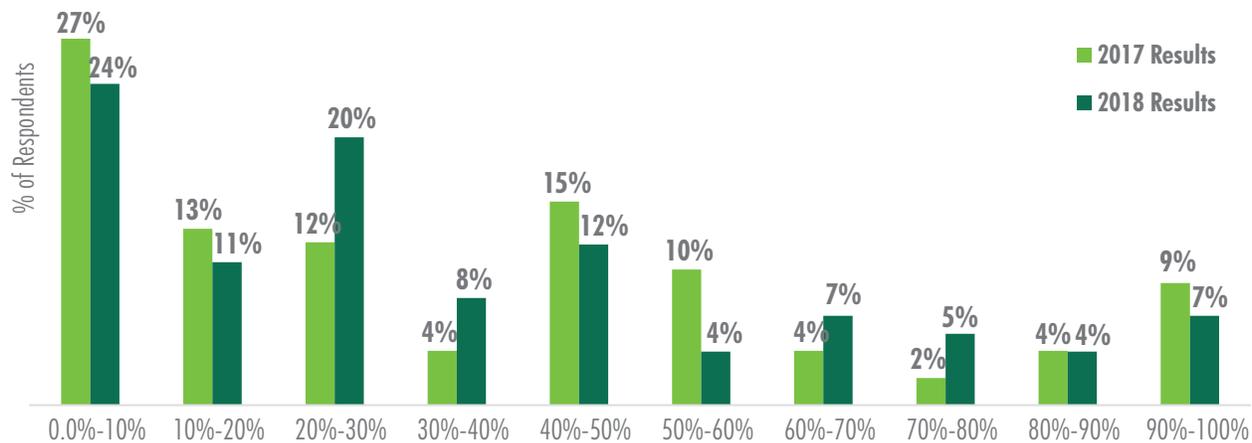
In your experience, what percent of the time do hospitals exercise their Right of First Refusal (ROFR) to purchase the medical buildings on their campus as outlined in a typical ground lease?

75% of survey respondents reported that hospitals exercised their Right of First Refusal (ROFR) up to 30% of the time, and 84% of respondents reported that hospitals exercised their right up to 40% of the time. This represents a slight shift upward from the responses in 2017. Most significantly we see that only 18% of respondents reported that hospitals exercised their right up to 10% of the time, as opposed to 37% in 2017. While most hospitals are still waiving their right to purchase, the rise in number of hospitals that do exercise will continue to increase competition for available assets.



In your experience, what percent of the time does the hospital have a price floor on their purchase option as part of the ground lease?

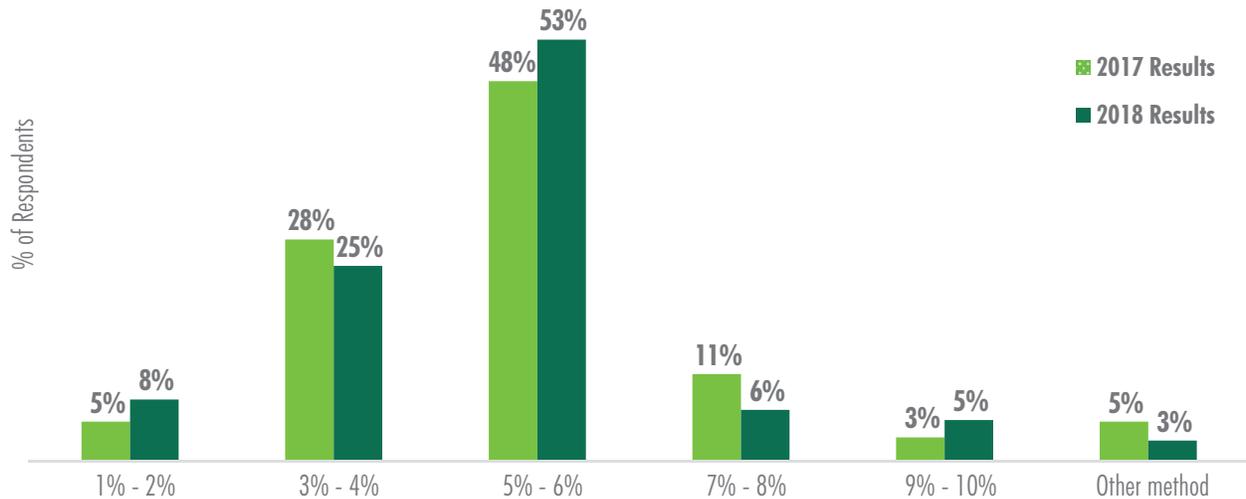
55% of respondents indicated that they see a price floor on a purchase option included in the ground lease up to 30% of the time, while only 11% of respondents indicated that they see a price floor on ground lease purchase options more than 80% of the time.



HEALTH SYSTEM MONETIZATION AND DEVELOPMENT CRITERIA

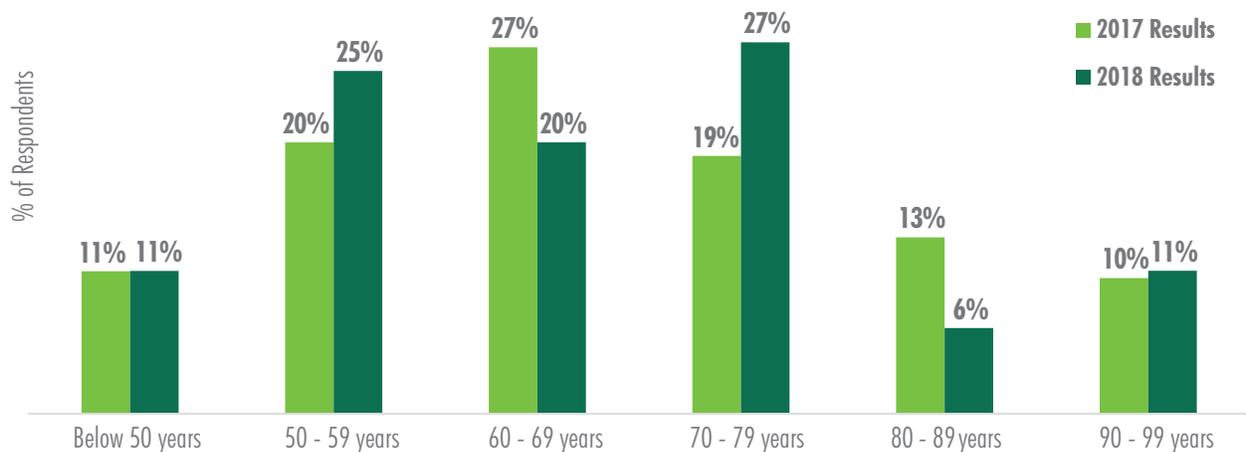
When working with a hospital to structure a ground lease, an investor or developer will typically use the footprint of the building, plus a 5-to-10-foot apron, to determine the annual cost to lease the ground. For an on-campus MOB, what do you believe is a fair percentage of the land value to use in the calculation to determine annual rent under the ground lease?

The largest group of respondents, both in 2017 and 2018, chose '5%-6%' as a fair percentage of land value to use in the calculation to determine rent under a ground lease.



What is the minimum ground lease term you would consider for investment?

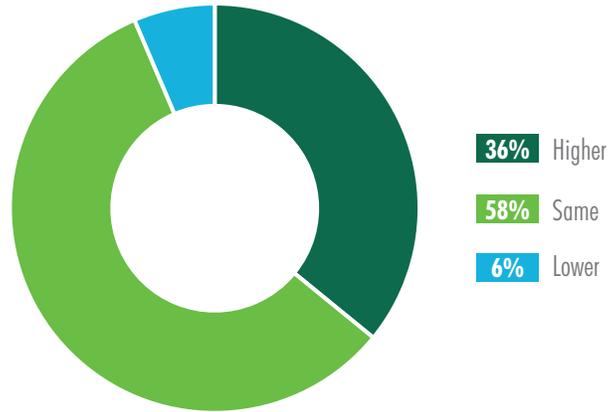
The final question regarding transactions with health systems inquired about the minimum ground lease term required by investors and developers. Investors and developers indicated a preference for at least 50 years of remaining ground lease term. It is also interesting to note that in 2018, 27% of respondents preferred '70-79 years' of remaining term versus 19% in 2017, and 20% of respondents prefer at least '60-69 years' of remaining term in 2018 compared to 27% in 2017.



MEDICAL OFFICE DEVELOPMENT

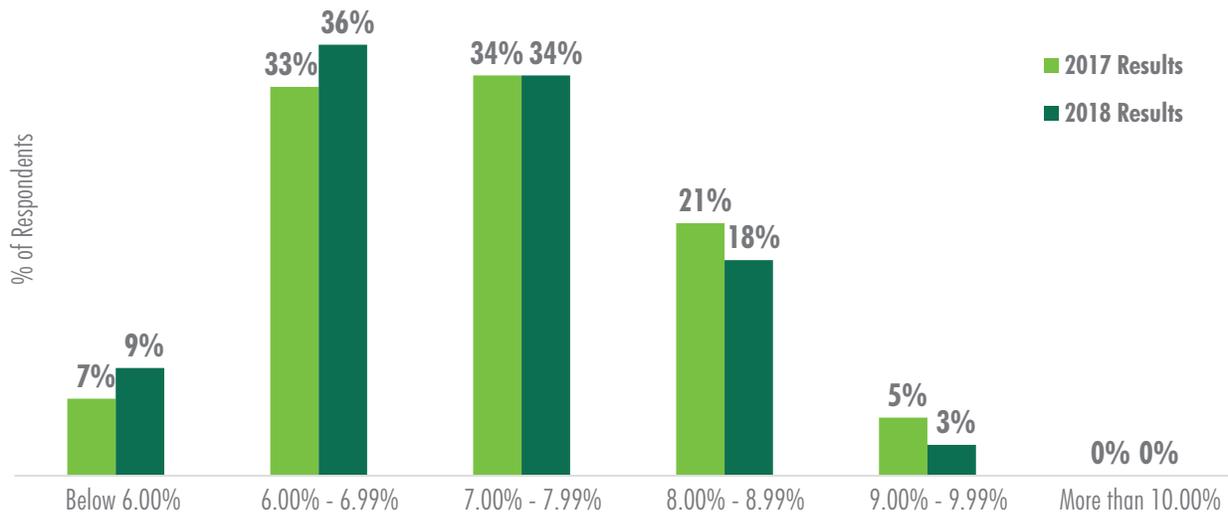
For developers, where do you expect health system development RFP activity in 2018 compared to a year ago?

This section of the survey exclusively focused on medical office developers. The first question inquired about development request for proposal (RFP) activity in 2018 compared to a year ago. Of those surveyed, a majority (58%) projected that RFP activity would be the 'Same' as last year, while 36% projected a 'Higher' level of activity.



For developers, what is the minimum lease constant you would consider for a healthcare development opportunity meeting your highest standards?

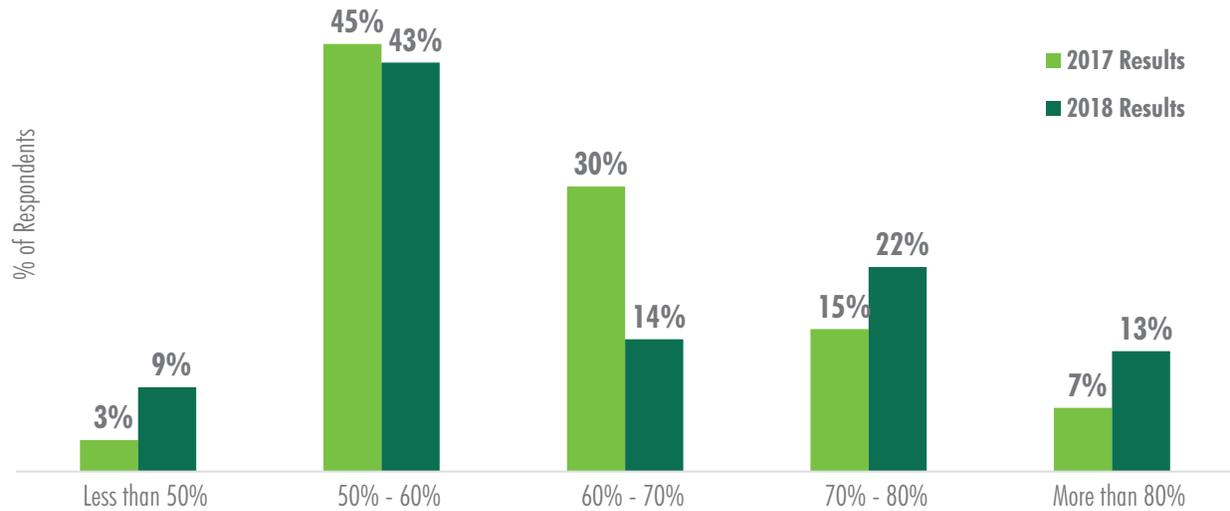
Return requirements for developments remain extremely competitive, with nearly half of respondents (45%) reporting that they would consider a lease constant below 7.00%, while 34% of respondents would consider lease constants between '7.00% - 7.99%'. These return requirements have compressed substantially since 2010, when 0% of the respondents indicated that they would consider a lease constant below 8.00% for a new development. In 2016, 66% of the respondents indicated that they would consider a lease constant below 8.00% for a new development. This increased to 74% of the respondents in 2017, and now 79% of the respondents in 2018 indicated that they would consider a lease constant below 8.00%.



MEDICAL OFFICE DEVELOPMENT

For developers, what is the minimum pre-leased threshold percentage you (or your lender) would consider for a medical office development meeting your highest standards?

Developers' year-over-year risk profiles have become more conservative. While nearly half of 2018 respondents (45%) still prefer at least '50%-60%' of a project to be pre-leased, there has been a significant shift for developers who require a higher threshold, with 35% of respondents now requiring more than 70% of a project to be pre-leased.

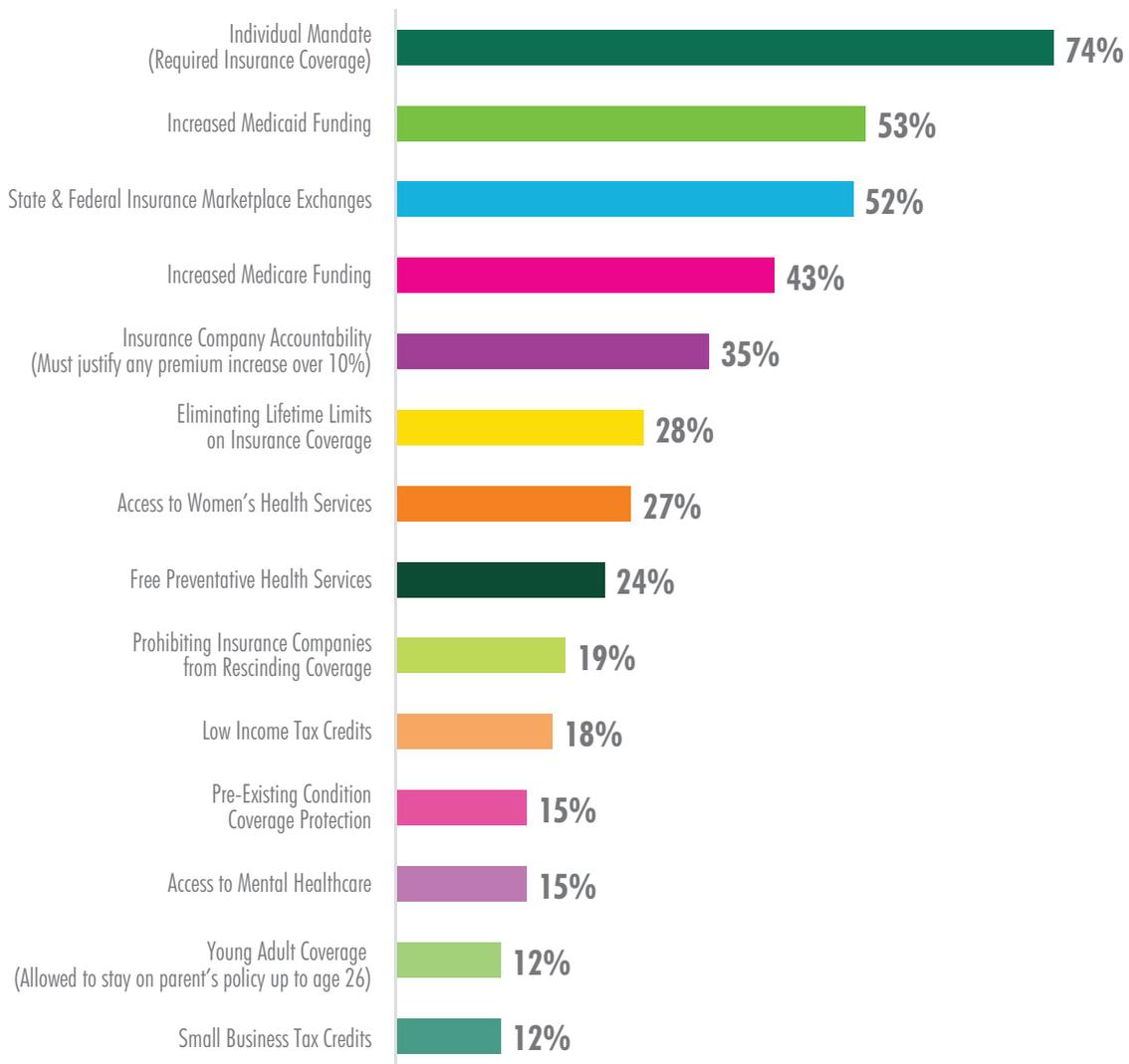


HEALTHCARE REFORM OUTLOOK – 2017 PREDICTIONS REVISITED

In our 2017 survey, we asked respondents to identify the features of the Affordable Care Act (ACA) that they thought may be repealed and replaced by the new administration. While there are many features to the ACA, we focused on those commonly identified as targets for reform. Below are the responses to two survey questions from 2017 requesting predictions surrounding the future of the Affordable Care Act, followed by our commentary about what actually transpired during 2017.

2017 Survey Question 1: Which of the following features of the Affordable Care Act (ACA) do you believe will be repealed and replaced by the new administration?

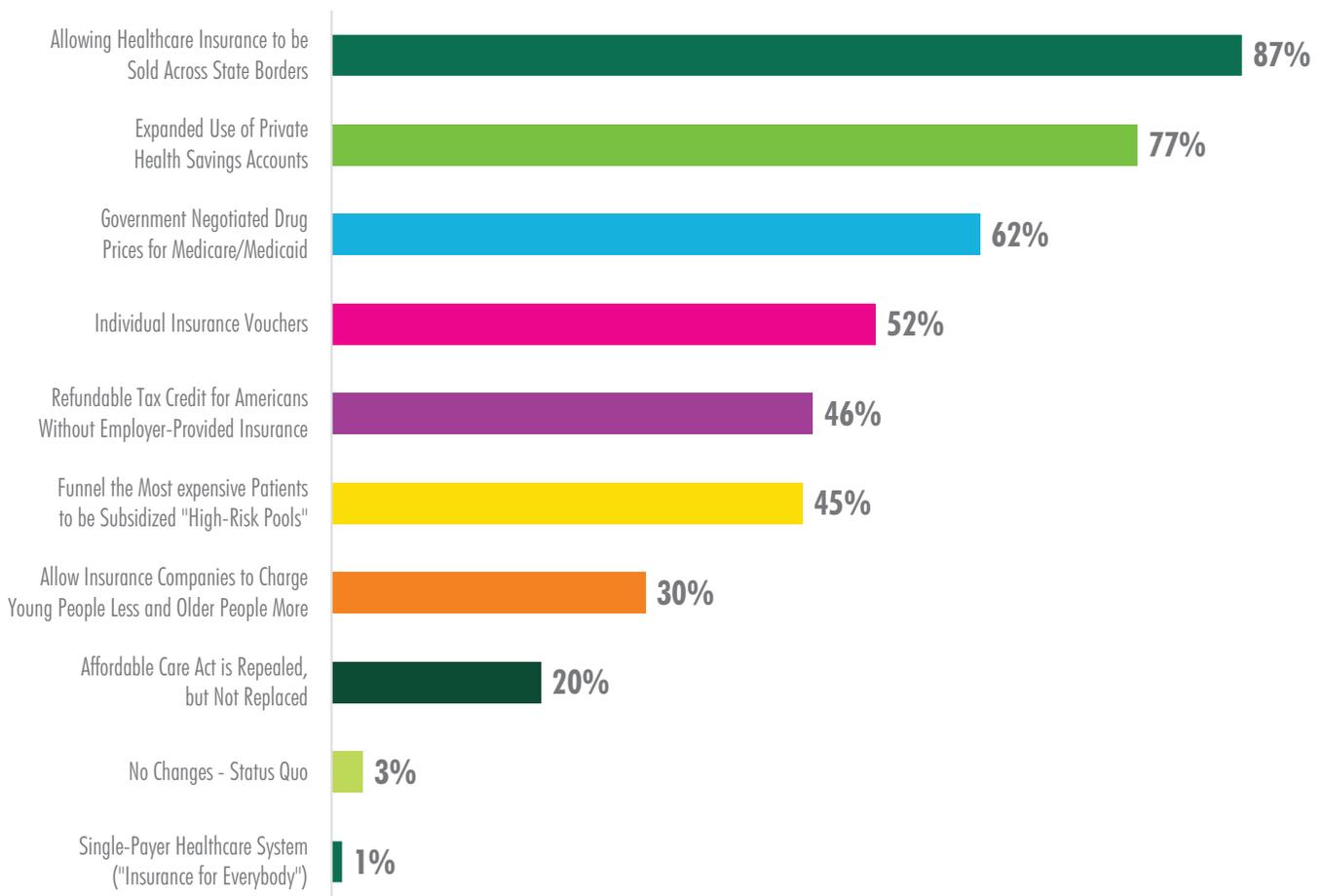
In our 2017 survey, an overwhelming majority (74%) of survey respondents predicted the Individual Mandate, that requires citizens to purchase some form of insurance coverage, would be repealed. After Congress failed to pass a bill to repeal and replace the Affordable Care Act, the elimination of this mandate occurred when the “Tax Cuts and Jobs Act” was signed into law on December 22, 2017. In addition, more than half of the respondents (52%) thought that the State and Federal Insurance Marketplace Exchanges would be repealed. While the Insurance Marketplace Exchanges are still intact, they remain under continual pressure and will most likely see significant changes in the near term. In October 2017, the current administration ended subsidies that were paid to insurers who waived deductibles and copayments for low-income customers. This change increased premiums, and coupled with the repeal of the individual mandate, is expected to drive many customers out of the exchanges.



HEALTHCARE REFORM OUTLOOK – 2017 PREDICTIONS REVISITED

2017 Survey Question 2: Which of the following proposed changes to the nation's healthcare system do you expect will be passed into law under the new administration?

As a follow-up to the prior question about which ACA features may be repealed and replaced, we asked the survey respondents to choose from a list of the most cited proposed changes to the nation's healthcare system and select all of the changes they think will most likely occur. Respondents overwhelmingly believed that the new administration will favor 'Healthcare Insurance to be Sold Across State Borders' (87%), 'Expanded Use of Private Health Savings Accounts' (77%), and 'Government Negotiated Drug Prices for Medicare/Medicaid' (62%). About half of respondents also think that changes could include 'Individual Insurance Vouchers' (52%), 'Refundable Tax Credit for Americans Without Employer-Provided Insurance' (46%), and that insurance companies would be able to 'Funnel the Most Expensive Patients to Subsidized "High-Risk Pools"' (45%).



ABOUT CBRE'S HEALTHCARE CAPITAL MARKETS

CBRE Group, Inc. (NYSE: CBG), a Fortune 500 and S&P 500 company headquartered in Los Angeles, is the world's largest commercial real estate services and investment firm and is the leading real estate advisor to the healthcare industry. With offices in 400 markets across the world, CBRE's more than 70,000 professionals provide exceptional outcomes for clients in 60+ countries by combining local market insight, broad services, specialized expertise and premier tools and resources. Our U.S. Healthcare Capital Markets specializes in providing healthcare real estate investors with acquisition, disposition, and recapitalization strategies; assisting healthcare providers with strategic capital planning (including monetization and capital raising efforts); and advising health systems and physician groups in the developer selection process.

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