

## U.S. Health Care REITs Are Well-Positioned For The Long-Term

By Charles Keenan

U.S. health care REITs have come of age, attracting more investors than ever and positioned well demographically for the long run, according to presenters at REITWeek2008: NAREIT's Investor Forum®.

Health care spending represented 16 percent of gross domestic product in the United States in 2007, according to the Congressional Budget Office. That figure that is expected to climb to 25 percent by 2025.

"There are a lot of positive trends that are combining to give the health care REITs really good visibility and very strong prospects as we look to the next decade," said Debra Cafaro, chairman, president and chief executive officer of **Ventas, Inc.** (NYSE: VTR), a Chicago based REIT.

Much of that comes from the rising average age of the population, which will boost demand for facilities such as hospitals, assisted living, independent living and skilled nursing centers—which make up the bulk of the largest health care REIT portfolios.

"There's no other fundamental economic trend in the U.S that is as strong as the aging of the population," said James Flaherty, III, chairman and chief executive officer of **HCP Inc.**, (NYSE: HCP) a Long Beach, Calif.-based REIT. "It is the certainty here that makes our underlying fundamentals [stronger] than all the other sectors."

Meanwhile, institutional investors have turned to health care as capitalization rates dipped in recent years in asset classes such as apartments, retail, industrial and office. Those classes have been referred to as the "four food groups," but health care now is becoming seen as the fifth.

"The asset type has become more accepted by institutions," Cafaro said. "We have worked very hard to educate the marketplace about the size and the characteristics of healthcare real estate. Investors have grown to appreciate the asset quality and stability of cash flows."

No doubt, institutional investors have recognized health care REITs, pouring plenty of dollars into the sector. The group reached \$28 billion in equity market capitalization in May, versus \$15 billion two years ago, according to NAREIT. This sector have outperformed all other REIT asset classes, notching annual average total returns of 24.1 percent for the last five years, according to the FTSE/NAREIT Health Care REIT Index. That compares with 18.7 percent for the FTSE/NAREIT Equity REIT Index.

That might make health care REITs more of an investment risk for now. “The run up in share prices vs. other companies such as malls and offices is hard to reconcile,” said Jim Sullivan, a managing director at **Green Street Advisors**, a Newport Beach, Calif., research firm.

In their growth, health care REITs have expanded well beyond the traditional classes of skilled nursing, assisted living and hospitals to include medical office buildings, health clubs and biotechnology buildings. These asset classes perform more like regular real estate, rather than being dependent on Medicare and Medicaid reimbursements.

As a result, REITs are bidding up prices for medical offices, for example. But buyer beware, said George Chapman, chairman and chief executive officer of **Health Care REIT Inc.** (NYSE: HCN), based in Toledo, Ohio. “There has been a lot of competition for medical office buildings—some on speculation,” Chapman said at a company presentation. “We find that very problematic.”

Yet health care REITs overall have served as a defensive tack for investors. “Health care assets are recession resistant,” Carfaro said. “Every asset type is affected by very large economic trends. Demand drivers in the health care space are very positive and continue to hold up very well in all kinds of economic cycles. If you look at the continuum of asset types, a lot of them are need driven, such as independent living, skilled nursing and hospitals.”