An Exploration of the Risk and Return Spectrum
For Institutional Investors
in the Senior Living and Long Term Care Property Sector

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ABSTRACT

The senior living and long-term care property sector has expanded in response to changing demographics and the increased needs of an overall aging population. As the population in total, and baby boomers specifically, reach retirement age and move into the "sunshine" years, the demand for real estate products designed with elderly end users in mind is growing, and the risk/return profiles of these investments are shifting. This research examines the spectrum of seniors housing investment alternatives ranging from Independent Living Facilities (ILFs) to Assisted Living Facilities (ALFs) to Skilled Nursing Facilities (SNFs), and finally to Continuing Care Retirement Communities (CCRCs). Risk and return parameters vary from investments similar to apartment complexes to those more akin to special purpose properties, albeit with government entitlements (*e.g.,* state allocated certificates of need which restrict competition) and licenses to provide special health care services. The aim of this research is to provide a better understanding of the risks associated with the specific types of investments available in the seniors housing real estate sector. In addition, we summarize the recent performance of the alternative property types in this sector. Finally, we query the institutional investors who are actively engaged in real estate investing. We survey members of the Pension Real Estate Association (PREA) to ascertain their relative perceived risks and returns associated with various seniors housing property types as well as the investors' perceptions of alternative asset classes. We found that they do not appear to be investing in most of the senior housing product type available and they perceive it to have relatively high risk but low return compared to the more traditional real estate investments.

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I. Introduction

A. Industry Size and Overview

The seniors housing industry is one of the largest and most complex industries in the United States. The industry is fragmented by geographic region and type of senior living facility. The National Investment Center for the Seniors Housing & Care Industries (NIC) *2004 Update to the Size, Scope, and Performance of the Seniors Housing & Care Industry* estimated 33,000 market rate professionally managed properties (independent living, assisted living, nursing homes, and CCRCs) with a capacity to hold 3,675,000 seniors. Of these, independent living units represent 19% (600,000), assisted living units 17% (625,000), nursing home beds 46% (1.7 million), and CCRC beds/units 18% of the total (650,000). (Exhibit 1)

B. Distinct Property Types

Most seniors housing literature discusses four distinct property types:

- ***Independent Living Facilities (ILFs).*** Independent living facilities are for seniors who are still able to enjoy many benefits of an active, independent lifestyle. Independent living attracts people who are believed to be trading the responsibility of home ownership and maintenance for a range of social, educational, and leisure activities, including many that are provided on-site such as pools, spas, exercise centers, social halls, and, in some cases, golf courses. Meal plans, limited transportation services, and organized activities are common. Some communities offer varying forms of health care, either directly or via home health contract.

- ***Assisted Living Facilities (ALFs).*** Assisted living is the most broadly defined, all-encompassing form of senior living. The Assisted Living Federation of America defines an assisted living residence as a special combination of housing, personalized supportive services, and health care designed to meet the needs, both scheduled and unscheduled, of seniors who need help with some, but not necessarily all, activities of daily living, such as bathing, dressing, eating, walking, toilet help, and monitoring medications. In general, assisted living provides a balance of residential living, health and recreational services, and assistance with day-to-day living activities. Approximately 800,000 people live in assisted living communities nationwide. Living spaces are specially designed with custom handrails, wheelchair accessible rooms, corridors, bathtubs, and emergency-call devices. Assisted living residences are centers for increasingly aging and dependent seniors but are created to respect residents' privacy, independence, and lifestyle preferences. Most communities have personal care professionals to help residents manage the most basic daily activities and offer a wide array of fitness, crafts, leisure, and cultural activities. Residents often have choices in meal plans, laundry and housekeeping services, local transportation, and religious services. On-site security and property supervision are the norm.

- ***Skilled Nursing Facilities (SNFs).*** Skilled nursing facilities are living communities for seniors who require constant, or 24-hour, supervisory nursing care in a more controlled and institutional setting. There are currently about 1.56 million seniors living in nursing facilities in the U.S. This represents approximately 4.5% of the age 65+ population and 18.2% of the 85+ populations (US Census 2000). Nursing care residences are designed for people who need medical, rehabilitative, and restorative care. Living spaces include wide halls, handrails, and nurse stations. Residents live in single or shared rooms, but share community rooms for planned daily activities, social events, and dining. Meals are prepared to accommodate individual dietary needs. The type and amount of care each person receives depends on what is needed to maintain a 'normal' lifestyle. Basic care refers to basic activities of daily living (eating, walking, bathing and grooming, toilet help, dressing, and transport) for which residents may require help or supervision. Skilled care encompasses nursing care and related services for those who need medical or nursing care or rehabilitative and therapy services for the rehabilitation of injured, disabled, or sick persons. Sub-acute care refers to intensive, restorative care for a recent physical condition or impairment, is administered by health professionals and requires frequent health care assessment. Some communities offer individual or family counselling, physical or respiration therapies, post-hospital and surgical care, restorative care, and coordination of care services.

- ***Continuing Care Retirement Communities (CCRCs)*** allow seniors to "age in place," with flexible accommodations designed to meet health and housing needs as they change over time. Residents entering CCRCs typically sign long-term contracts that provide for housing, services, and nursing care, usually all in one location, enabling seniors to remain in familiar settings as they grow older. Many seniors enter into CCRC contracts while they are healthy and active, knowing they will be able to stay in the same community and receive nursing care throughout the aging process.

Besides the four basic types of seniors housing facilities described above, other facilities exist, including those that can provide more focused care for specific physical or health care needs, such as hospice and Alzheimer’s facilities. Hybrid independent living/assisted living and assisted living/Alzheimer’s facilities are similar to CCRC’s, where different care programs are available at one location. Additional products include multifamily developments that are age restricted, typically over age 55, for active adults as well as naturally occurring retirement communities (NORCs). There has also been recent growth in home health services offered by public agencies (such as the city or county) or by private companies that bring services to aging adults, and adult day care facilities serve about 400,000 elderly U.S. residents nationwide (Kaiser

Foundation 2008). This study will focus on three of the four major asset types, Independent Living, Assisted Living, and Skilled Nursing, although CCRCs will be included in some of the analysis for comparison purposes. These types have historically been, and should continue to be, the most likely candidates for investment by the institutional investment community, given the focus on income-generating assets as well as a longer term investment horizon.

C. Demographic Trends

Several important demographic trends are expected to increase the need for seniors housing and encourage development and investment in the sector. Due to need-based demand, these trends should supersede movements in the traditional business cycle and create steadily increasing requirements for independent living facilities, assisted living properties, and skilled nursing homes.

As people age, they develop needs for help with daily living activities and the assistance provided by various senior living facilities. Because aging is typically accompanied by physical or cognitive impairments and/or functional disabilities, specialized secure housing is required. As detailed in Exhibit 2, the U.S. Census Bureau has projected that the population over age 65 will increase from 35.0 million in 2000 to over 86.7 million people by 2050, and the population over the age of 85 will increase from 4.2 million in 2000 to 20.9 million people in the same period. Exhibit 3 shows the percentage of people over the age of 65 and 85 years old as a percentage of the entire U.S. population. Currently, approximately 12.4% and 1.5% of the U.S. population is over the ages of 65 and 85, respectively, and it is projected that by 2050, 20.7% and 5.0% of the U.S. population will be over the ages of 65 and 85, respectively. There is no doubt that as the U.S. population continues to live longer, the demand for senior living facilities will increase.

In addition to current population data and projections, certain societal changes over the past 35 years in the U.S. have contributed to an increased demand for seniors housing. An increasing percentage of women in the workforce, increased rate of divorce, smaller family size, and job mobility have combined to make traditional arrangements of family care, where aging relatives move in with adult children, more difficult and less common. The demand for alternative models of senior care has increased, and the upward trend is unlikely to change in the foreseeable future.

D. Legislative Impact on the Seniors Housing Investment Alternative

While residents in independent living facilities generally pay rent for use of the housing and its amenities, reimbursements from Medicare and Medicaid programs frequently support services at assisted living facilities and skilled nursing facilities. Medicare is a federal program that provides certain hospital and medical insurance benefits to persons age 65 and over and services to disabled persons and persons with end-stage renal disease. Medicaid is a medical assistance program jointly funded by federal and state governments and administered by each state's determination of which benefits will be made available to elderly residents and who are defined as eligible indigent citizens. The Medicare and Medicaid statutory framework is subject to administrative rulings, interpretations, and discretion that affect the amount and timing of reimbursements to assisted living facilities participating in the program and to skilled nursing facilities, making the income streams associated with these assets rather complex and uncertain.

Healthcare is one of the largest industries in the U.S. and continues to attract significant legislative and public attention. In an effort to reduce spending on healthcare, the federal government enacted the Balanced Budget Act in 1997. The Act changed Medicare reimbursement for nursing home care from an audited cost basis to a prospective payment system where payments are based on a set number of related resource utilization groups ("rugs") representing government-estimated costs of treating specified medical conditions. The Medicare prospective payment program was implemented on July 1, 1998. Throughout 1998 and 1999, Medicare reimbursements paid to senior living facilities decreased dramatically for many owners, primarily the larger publicly traded multi-facility owners, leading to a financial crisis for many companies within the seniors housing industry. The publicly-traded nursing home companies either went bankrupt or fell under severe financial stress. According to industry consultants interviewed for this study, investments in senior living facilities performed poorly, and many lenders and equity investors exited the senior care business.

The federal government modified the original act, reversing many of its original provisions and making changes that are beneficial to the industry. Over the last five years, cost structures have been established to account for the Balanced Budget Act, and today, more lucrative reimbursements are available to seniors housing owners and operators. As more stability has been established, credit quality and investment opportunities have improved. Since early 2000, interest in investing in assisted living and skilled nursing facilities has rebounded.

The aim of this project is to provide a resource to potential institutional investors who are either currently participating in, or considering participating in, the seniors housing market by identifying the risks and returns associated with alternative types of seniors housing and long-term care properties.

The remainder of the paper is divided into the following sections: 1) literature review as well as a review of some of the available data sources for tracking the performance of seniors housing; 2) consideration of seniors housing through traditional risk analysis; 3) current industry performance data and a comparison with more traditional real estate investments; 4) results of a survey created for this study and administered to the institutional investment community that is currently investing in real estate to determine relative risk and return perceptions of the seniors housing investment alternatives in comparison with more traditional real estate investment alternatives; and 5) implications of our findings as well as areas for further research into the seniors housing asset class.

II. Literature Review and Sources of Data

Over the last 40 years, the seniors housing industry has, in many respects, gone through an entire life and maturation cycle, from its birth as a product created to function within the world of government entitlements to its current multi-product status as an independent, institutionally-accepted niche investment option. Various studies in the past have attempted to promote investment in the industry. The most referenced are the studies completed by NIC in conjunction with numerous academics (See Mueller and Laposa, 1997, Laposa and Singer, 1999, NIC 2001a and 2004). In addition, there have been numerous studies focused on the supply and demand of seniors housing (Anikeeff, 1999; Doctrow et al. 1999, and Tessier and Mueller 1999) as well as several resource books written on the industry, including an excellent resource guide by NIC for the Seniors Housing and Care Industries (2001b), several focused on the assisted living sector (Pearce 1998, 2007, and Moore 2001) or the development of seniors housing (Brecht 1995, 2002; Suchman, et.al., 2001), and there are two information packets with a collection of materials on the assisted living and the active adult retirement communities (ULI 2006a and b). See also Mace and Srivastava (2007) for a short primer on the senior housing asset class.

There are also frequent surveys on the industry. Many are used in this study to help define the risks and returns associated with investing in the seniors housing asset class. These include the following:

1. *The State of Senior Housing Survey and the Overview of Assisted Living* produced by the American Seniors Housing Association (ASHA). The 2006 survey reports the results of 462 respondents with properties located nationwide. The publication is a very detailed report on a large number of performance statistics including (but not limited to) operating expense ratios, average length of stay, management type, labor related expense, total annual revenue, net cashflow, and rent changes for the major senior living property types, including independent living, assisted living, and CCRCs. Data is included on skilled nursing beds that are located in an assisted living or CCRC development.

2. *Seniors Housing Investment and Transaction Report* produced by the American Senior Housing Association. This report contains data on arms length, non-distressed sales and transactions involving arms length sales of distressed assets. The study examines key indicators for independent living, free-standing assisted living and Alzheimer's oriented assisted living, including high, low, and average price per unit, overall cap rates, operating expense ratios, and effective gross income multipliers. Data is also provided on multiple asset transactions.

3. *NIC Trends* 1999-2007 by the National Investment Center For the Seniors Housing and Care Industry (NIC). This annual survey compiles capitalization rates for transactions that have closed over a given period of time from leading investors, owner/operators, and appraisal professionals in the seniors housing industry.

4. *Seniors Housing Construction Trends Report* produced by NIC and ASHA. This report provides data on all seniors' housing projects under construction as of March 2006 in the 75 largest metro areas. Product types include senior apartments, independent living, assisted living, Alzheimer's/dementia care, nursing care, and continuing care retirement communities.

5. *Seniors Housing Investment Survey* from 1991-2007 produced by Michael Boehm of Senior Living Valuation Services. This annual survey is a compilation of practical experience, opinions, and perceptions of the investment criteria used by individuals, investors, appraisers, and other experts that specialize in the seniors housing industry.

6. *2003 Lenders Survey* produced by NIC and the CBIZ Valuation Group. This publication contains the results of two surveys: the *Lender Survey of Preferences in Financing Senior Housing and Long Term Care Projects* and the *Senior Living and Long Term Care (Equity) Investor Survey*. The results were obtained from over 100 responses from alternative sources of financing for the seniors housing industry and include data on preferences, opinions, and investment criteria, as well as information on the valuation parameters of the lending and investing community.

Private and public companies that service the seniors housing industry also conduct industry reports and trend analysis. The following firms' publications have been used to help frame the discussion found in this study.

1. Marcus & Millichap (2007a and b, 2005, 2006a and 2006b)
2. Cushman Wakefield (2005)
3. Legg Mason Wood Walker, Inc. (2005) and Stifel and Nichols (2006 and 2007), who focus on the public market and report on the performance of REITS invested in seniors housing, including operating companies for seniors housing.
4. C.B. Richard Ellis (2006)

In addition, there have been several academic studies focused on the awareness, attitudes and perceptions of seniors toward seniors housing. These studies are survey based focused on the user/tenant. For example, Gibler, Lumpkin and Moschis (1997) found that many seniors are unaware of the alternative product types available. They think a nursing home is their primary option outside of aging in place and they have a very negative opinion of that alternative (1997). In 1998, these same authors studied the decision-making process of moving to seniors housing and found although the decision is primarily made by the seniors their children as well as the medical professionals helped to make the decision to enter the seniors housing alternative (Gibler 1998). Family members and medical professionals were more involved in decisions to move to housing with higher levels of care. In 2003, Gibler focused on the lower income constituent and subsidized housing finding the current service levels insufficient to fulfill the needs of the aging subsidized housing residents in the inner cities (Gibler 2003). Finally, Lee and Gibler (2003) completed a survey of seniors that were planning to live in retirement housing and found that these individuals tended to be wealthier and healthier. They were interested in housing that provided personal care, home care, social, and security services.

A few studies have focused on the performance of the companies involved in the seniors housing industry typically comparing investments in seniors housing with the performance of other asset classes. Laposa and Singer compare the size and scope of seniors housing to alternative investments in the lodging and apartment industries in the late 1990's. They conclude seniors housing compares favorably on many different dimensions and should be considered seriously by the institutional investment community. Mueller and Anikeeff (2001) examine the performance of 6 REIT types including seniors housing and examine how the inclusion of operating business affects the risk and return characteristic of the alternative REITs. They find that the REITs that have more operational income (hotels and retail) rather than just rental income are more volatile than those that do not (industrial and office), with seniors housing and health care REITs being the exception. This aberration is explained by the fact that in seniors housing rental revenues are often collected separately from the revenues generated by services. Terris and Meyer (1995) focus on the correlation between the healthcare REITs and the health care companies and found that there is a significant correlation between the performances of these two investment types.

In a more recent study, Eicholz et al. (2007), compared the performance of these two assets as well, healthcare REITS and seniors housing operating companies from 1996-2005. Their analysis focused on the type of seniors housing owned by the companies. They found that the healthcare based REITs outperformed seniors housing operating companies if the product held by the company was less service intensive, such as independent living. As the needs for services increased, these researchers found the fully integrated operating companies tended to outperform the healthcare REITs.

This current study extends the existing literature as it breaks down the perceived risks and returns associated with the seniors housing asset class on a property specific basis. That is, we separate the sector into the three basic property types: Independent Living, Assisted Living and Skilled Nursing Facilities, and define the current risks/returns associated with each type of seniors housing. We then summarise current performance statistics for these property types as they relate to alternative investments that might be considered more likely to be held by the institutional investment community. Finally, we go to the institutional investment community to ask for their perception of the risk/return associated with making investments in 21 different types of real estate including direct and indirect investments in the seniors housing marketplace.

III. Seniors Housing Risk Analysis: A Traditional Risk Primer

Traditional risk analysis examines factors that lead to variance in cashflows. When the potential for variance is reduced, risk declines, and a lower return is required from the investment. Within the seniors housing asset class, cash flows vary significantly between alternative property types, especially skilled nursing facilities, and this variance drives the level of expected return. When examining a real estate investment, it is often useful to divide risk attributes into categories. Graaskamp suggested the following attributes: physical, legal/political, dynamic, and linkages/location (Graaskamp 1981). Our analysis will examine how each risk component affects the cash flow viability, integrity, and sustainability of alternative seniors housing investments.

Physical. Different types of seniors housing have specific building codes, and construction costs fluctuate, so the price and risk associated with investing in the different types of properties vary. Independent living properties are the least complicated to design and build. This property type is also easier to maintain as construction is relatively simple and there is less wear and tear from senior residents than from other age groups.

Typically, independent living residents move in on their own reconnaissance as frequently as having the decision made by adult children. The more amenities offered to support an active lifestyle, the more likely the property will appeal to the marketplace. Additional housing types in a single complex increase the opportunity for conversion of residents from one product type to another. To attract younger couples, some complexes include owner-occupied single or duplex housing in a campus setting. In this type of development, residents can begin with ownership models (condominiums) and, as their needs increase, they can move into rented, multifamily units, all within the same independent living community.

For the independent living product, cashflows include monthly rental income from a lease structure plus additional income from limited services offered to improve the residents' quality of life. Additional income might include payments for entertainment fees, health clubs, medical checkups, and other pay-as-you-go services -- similar to *a la carte* services received from hotel investments or the parking income from office buildings in central business districts.

These are variable sources of revenue and highly dependent on the needs of the resident clientele.

Because prospective independent living residents often decide to move based on quality of life issues, the independent living product should be designed to accommodate seniors for longer periods of time. Viewed as “active adult” (over 55) or retirement housing, cashflows will hold steady if units are filled. An investment in a stand-alone independent living facility is limited by the length of time each tenant can remain. As acuity intensifies the need for specialized care, tenants may be forced to move to alternative facilities, and existing independent living units must be re-leased. Income variance is more controlled in complexes with combinations of independent living and assisted living units. On the other hand, expenses for independent living/assisted living hybrids are less predictable than expenses for stand-alone independent living, because management runs a risk of mispricing the level of care that will be needed by individual residents. However, if leases are structured so that tenants pay for additional services as needed, investors can offset, or mitigate, the risk of underestimating the level of required care. In traditional commercial real estate, these resemble triple net leases

Stand-alone assisted living facilities are marketed to a different clientele from than independent living market, and the rental streams are more complicated. Assisted living tenants typically pay a monthly or, possibly, a daily rate for the real estate and a daily rate, often *a la carte* charges, for services. Since assisted living properties focus more on the service side of the business, cashflows are more variable. In some ways, this asset is like an investment in a neighborhood shopping center, with percentage rent leases that remain relatively stable unless something occurs to dissuade consumers from spending money at the local stores. With assisted living, the potential for the service need to shift is greater than for other categories of seniors housing, and profit is more variable. Assisted living has higher labor costs that are fairly predictable if occupancy is steady and the health of patients does not decline unexpectedly. A random occurrence like a flu epidemic could be costly.

For independent living/assisted living hybrid properties, more attention must be paid to design. Developers might want to separate the two different types of facilities, because individuals living in independent living often do not want to admit that they are moving toward the need for assisted living. In other cases, independent living tenants may choose to be close to the assisted living units, especially couples who require separate levels of care. In addition, friends who have varying service needs may elect to stay close by to provide assistance and support. This type of real estate development requires more common areas and more space for services. Since independent living/assisted living hybrids are more service based than stand-alone independent living, the extent of fixed income depends on the proportional mix of the two types of units. With the combination product, a single community can retain both spouses if they age differently and progress from one need category to another at different times. Since turnover costs are expensive in any real estate business, retention of tenants reduces risk by maintaining cash flows per unit at higher and more predictable levels.

As developers move up the care spectrum, properties become more expensive to build. The assisted living/Alzheimer's product has unique design requirements to insure that Alzheimer's patients don't become confused and walk away, causing an "event" that can impact the image of the facility.

At the top of the risk/return spectrum, skilled nursing home facilities entail a new range of construction issues: the medical condition of patients is more acute, buildings are more like hospitals, and materials and equipment are more costly. In comparison to other seniors housing sub sectors, costs to operate and maintain the real estate are higher and more difficult to predict. Skilled nursing facilities have rental structures similar to the hospitality industry, where rents are paid on a daily basis and staffing levels required for rooms/beds remain constant while occupancies are level. If occupancy rates fluctuate, rental income and expenses become harder to predict.

Another issue to consider is long-term flexibility of the cash flow. Design flexibility can lower the risk associated with holding an investment, so products designed to be modified according to market trends have more marketability and investment appeal. This characteristic resembles flex space in the industrial market. In the case of flex space, the size of the office portion of the property can be readily altered depending on the needs of the tenant. For independent living/assisted living hybrids, if the property is set up to provide a wide range of services but the market does not demand them, offerings for one type of seniors housing can be reduced, and overall returns can be protected. Conversion of use is relatively easy in independent living/assisted living, assisted living, and independent living, but becomes more difficult for the riskier investments including assisted living/Alzheimer's facilities and skilled nursing facilities, since more permanent design details are built-in to insure the safety of patients and residents.

These structures have significantly more fixed costs and are difficult to convert or reconfigure if demand changes.

In summary, there are two sources of cash flows: one from rental of building space and one from fees for services offered. Building rent is relatively easy to predict, while the need for services is more variable, but services generate additional income, so investors are rewarded for assuming the related risks. If priced on a pay-as-needed basis (*a la carte*), expenses can be more manageable, performing like charges in net leases where investors pass on the risks of predicting service needs of tenants (plus earn a percentage). Due to the phenomenon of captive tenants who will pay for additional services, if income streams are structured correctly, service profit centers can yield increasingly profitable returns to seniors housing investments.

Legal/Political Attributes. Independent living facilities have limited regulations and few entitlement issues. In fact, reverse NIMBYism is prevalent: there is increased understanding that for-profit seniors housing can enhance the tax base of a community while requiring fewer services and having less impact on schools and transportation than other residential developments.

Assisted living facilities and assisted living portions of hybrid independent living/assisted living projects face legal/political risks associated with state regulations and a dependence on reimbursements from the state and federal governments. Regulations for assisted living are more extensive and the care offerings are subject to more scrutiny by not only the senior resident but also family members who have made the decision to consider seniors housing. In addition, as federal and state budgets wrestle with ongoing deficits, and reimbursements from Medicare and Medicaid are in jeopardy of cutbacks, revenue streams remain uncertain. Finally, compliance issues are changing and, depending on the location of the projects, could become more restrictive. On the other hand, state and federal regulations raise barriers to entry, creating a positive impact on returns. Depending on the unit mix and the regulatory environment of the state where the facilities are located, the independent living/assisted living hybrid has less overall risk than many of the other product types

Moving up the acuity level from assisted living brings ever stricter licensure issues. Because the possibility of an “event” adds liability and drives up insurance costs for Alzheimer’s property investments, assisted living/Alzheimer’s buildings must be designed for patient safety. Regulations differ from state to state, so compliance demands vary and are not predictable.

Although premiums can be assessed for additional services, predicting how much and how many extra services will be needed depends on resident patients' experiences as they move through the stages of Alzheimer's. The combined variances add levels of uncertainty that can make assisted living with Alzheimer's more risky than stand-alone independent living, independent living/assisted living, and stand-alone assisted living. Experienced marketing staff may lower occupancy risk in independent living and hybrid independent living/assisted living complexes, but skilled professionals are the critical mitigating factor against liability risk in the more intensive care facilities.

For skilled nursing facilities, state certificates of need limit the number of properties in any given market. High barriers to entry afford the ability to achieve and maintain high occupancy levels and more predictable income and expenses. As regulations change and compliance requirements increase, labor and insurance costs rise, contributing additional variance to cash flows and producing uncertainty for investors. However, in many markets, where currently strict barriers to entry allow rents in skilled nursing facilities to be increased regularly, rising expenses can be neutralized.

Dynamic Attributes are in the eye of the beholder. They represent societal or cultural views that are unique to individual decision makers. Who is ultimately responsible for making payments to the investor -- and responsible for signing the checks? Typical consumers for the independent living property type are not frail elderly, and they are not in need of a lot of care. To be able to live in an independent living unit, the tenant must be active and feel capable of remaining independent, and the move-in decision is a lifestyle decision that is made voluntarily. Services should be available and attractive enough to convince potential residents to decide to move, and management needs to set expectations up front.

With independent living investments, individuals or couples making decisions based on quality of life criteria provide the cash flow. The independent living product must appeal to an active aging population, but can be a hard sell as seniors may not want to admit that they are growing older or are "ready" for a move. The numbers of potential customers are increasing as the baby boom generation begins to retire, but so are lifestyle alternatives. For this investment type to be successful, the owner/investor must create a value proposition that is enticing and a pricing structure that makes sense. Services and amenities have to overcome the inertia of the aging population and the desire to remain in familiar surroundings. Unlike the other seniors housing property types, there are alternatives like inner-city cooperative home health services and naturally occurring retirement communities, or NORCs.

When investors move up the spectrum to higher risk/return levels, to assisted living or assisted living/Alzheimer's developments, they must meet a different set of expectations for those who decide if services are adequate and the quality of care is appropriate. Adult children become increasingly involved, as well as medical professionals and other caregivers. Decisions to enter these facilities are typically made out of necessity. The lease structure is complicated, and it is more difficult to know what the competition is doing and what the market will bear. High-quality, experienced management is extremely important. Once moved to an assisted living facility and if the services provided are acceptable and attractive, aging tenants are likely to remain because increasing acuity prevents them from shopping around and moving to competing properties. Because the facilities provide for high levels of care, experienced, qualified management is crucial.

For skilled nursing facilities, even more individuals are likely to be involved in entrance decisions. In nursing facilities, income is generated on a per-day basis as well as from *a la carte* services offered by trained nursing staffs. Income depends on the acuity levels of in-house patients and can vary daily. As with assisted living and assisted living/Alzheimer's, family members, medical professionals, and Medicare/Medicaid reimbursement policies are responsible for, or contribute to, decisions about levels of care and ultimately the net income streams of the investments.

Linkage/Location Attributes. Location is important. Seniors still desire to share recreational, cultural, and educational advantages of cities and metropolitan areas that offer nearby shopping and attractive events. Active retirees have traditionally looked forward to days in the sun, although recent overbuilding in southern retirement communities has made the draw less compelling (Streitfeld 2008).

The location of property classes can vary depending on the property type, so land costs can be shifted. For independent living facilities, a central location is not required, and the location of adult children does not necessarily factor in to the location decision. Since many residents are still able to drive to food stores, libraries, medical services, and recreational activities, minimal on-site transportation is necessary. Once aging tenants require assisted living care elements, proximity of adult children or other family members and access to out-patient and emergency medical services become relevant, and central locations in denser suburban or urban areas are more highly valued.

IV. Summary of Current Performance Data in the Seniors Housing Industry

Growth over the last two decades in the seniors housing and care industry has resulted in size and market capitalization levels that warrant the attention of large investors (NIC, *Size* 1999). The following discussion outlines current investment performance of the alternative seniors housing subsector including: occupancy rate, turnover, revenue growth, service component, profitability, expenses, management, trend analysis of key financial performance statistics, and capitalization rates.

Occupancy Rate. One of the strong investment attributes (and a risk mitigation factor) for the seniors housing sector is a persistently high occupancy rate. As illustrated in Exhibit 4, current occupancy rates for the various seniors housing property types vary from a low of 90.7% for assisted living facilities (because of rehabilitative services, residents have more frequent, shorter stays than in independent living facilities) to a high of 93.6% for independent living facilities and 94.1% for CCRCs. This compares favorably with occupancy rates in some of the more traditional real estate investments, including a national average of 94.7% for apartments (Marcus and Millichap 2007b) and a much lower average occupancy rate of 63.4% for hotel investments (Korpacz 2007).

Turnover. Along with occupancy, the often costly and disruptive turnover of tenants is an extremely important variable for any real estate investment. This rate varies significantly between the subsectors of the seniors housing industry. Average or mean lengths of stay range from a low of 18.5 months for residents in Alzheimer's beds, as detailed in Exhibit 5, to over 36 months for residents in stand-alone independent living units. Other industry sub sectors have average lengths of stay from 22 to 23 months, compared to the general multifamily rental housing sector where a recent study showed that 46% of the tenants in apartments with elevators stayed less than one year and 37% of the residents in apartments with no elevator left within one year (Deng 2003).

Revenue growth. While the combination of longer lengths of stay and lower vacancy rates helps control the risks associated with investments in the independent living category, the ability to maintain or raise rents mitigates the wider occupancy variances in assisted living, Alzheimer's, and skilled nursing facilities. Consistent with data on lengths of stay, Exhibit 6 illustrates that median rent increases for existing residents that are in independent living facilities lag behind "market rents" charged to new or prospective tenants (4% vs. 4.6%), but this is not the case for the other subsectors.

Profitability. As detailed in Exhibit 7, median total revenue ranges from $26,333 for independent living facilities to almost $50,000 for assisted living with Alzheimer's care. Median total operating expenses range from $17,800 for independent living to almost $34,874 for assisted living with Alzheimer's care. Because of additional care and services provided in Alzheimer's facilities, the market commands higher rents. The median annual revenue for assisted living with Alzheimer's care ($48,576) is almost 54% higher than median annual revenue for assisted living without Alzheimer's care ($32,212). The increased revenue translates to higher net cashflows: the median net cashflow for assisted living with Alzheimer's care is the highest at $7,733, followed by independent living and the independent living/assisted living hybrid, while assisted living without Alzheimer's has the lowest median net cashflow.

Expenses. Although median total revenue for independent living facilities is $26,333, almost 41% lower than assisted living with Alzheimer's care, median total operating expenses are comparatively low as well ($17,800) so that the median net cash flow is $3,074, 16% higher than independent living/assisted living hybrid facilities ($2,649), and almost 44% higher than assisted living without Alzheimer's care (Exhibit 7). Not surprising, the percentage of labor-related expenses to total operating expenses increases with acuity and care needs of the residents. As detailed in Exhibit 8, median labor-related expenses are 47.9% of total median operating expenses for independent living projects, while median labor expenses for assisted living facilities providing Alzheimer's care is substantially higher at 56.4% of total operating expenses.

Trend analysis of key financial performance statistics. At this point in time, there appears to be only one good source of industry trend data for comparing financial statistics of seniors housing investments. Exhibit 9 details financial statistics reported by the same properties from one year to the next (2005 – 2006). With low levels of new construction occurring in most markets, supply and demand factors are at play. As the industry improves in terms of occupancy and rents, total revenues have risen faster than expenses. The cumulative effect has yielded significant NOI growth across the various alternative seniors housing investment alternatives, with CCRCs gaining the most (26%), followed by independent living facilities (18%). Assisted living facilities had the lowest average growth in NOI, albeit a respectable 8% annual growth rate.

Capitalization rates. The Boehm Survey is completed annually by investors, appraisers, and others in the senior health care industry. Exhibit 10 reflects the downward trend of capitalization rates for all types of seniors housing. The steeper declines began in 2004 as capital became increasingly available for all types of real estate, and investors sought opportunities that provided higher rates of return including seniors housing. Age-restricted apartments commanded the lowest capitalization rates throughout the period (7% in 2007) and skilled nursing facilities the highest (12.1% for short term facilities in 2007).

Exhibit 11 reflects expected risk premiums over ten-year U.S. Treasury bonds for seniors housing based on the average capitalization rates provided from the *Senior Housing Investment Survey* from 1994 to 2006 (Boehm ,1994-2007) for the three major seniors housing sub sectors. Investors perceived that independent living facilities should command a premium ranging from a low of 216 basis points in 1994 to a high of 557 basis points during the 2002 downturn in the industry. In 2007, experts were projecting an average of 269 basis point premium over the ten-year Treasury bond. Over the same time period, investments in assisted living facilities followed a similar trend with premiums ranging from 426 to 747 basis points settling in at 429 in 2006. Investors' sentiment toward skilled nursing facilities led to anticipated premiums of 500 basis points at the beginning of the study period, accelerating to 937 basis points above ten-year Treasury bonds in 2002, and dropping at a less accelerated pace in the last few years to 739 in 2006. For all classes of seniors housing investment, capitalization rate premiums over ten-year U.S. Treasury bond returns reached their peak in 2002 and declined as interest rates started to rise in 2003.

Exhibit 12 compares alternative return expectations, reflected in capitalization rates, for various classes of real estate investment, including age-restricted apartments, independent living facilities, assisted living, Alzheimer's-dementia care, and skilled nursing, during the first quarter of 2007. Return expectations range from a 5.89% average capitalization rate for investments in the apartment market to 11.6% capitalization rates for investments in skilled nursing facilities. The average capitalization rate for all categories in the first quarter of 2007 was approximately 8.16%, with expectations for investments in independent living facilities generating capitalization rates of 8.20% and expectations for investments in assisted living facilities generating only slightly higher returns of 8.50%.

Exhibit 12 shows that certain classes of seniors housing investments, including independent living and assisted living facilities, generate return expectations that are below the expected returns for investments in the hospitality sector, specifically for full service lodging, limited stay lodging, and extended stay lodging. Expected returns from investments in CCRCs and Alzheimer's/dementia care facilities fall below returns expected from limited service and extended stay lodging, while skilled nursing facilities/long term care investments generate the highest expected returns and, theoretically, also generate the highest level of risk compared to the other real estate investment alternatives.

Capitalization rate spreads over ten-year Treasury bond rates for the first quarter of 2007 appear on the right side of Exhibit 12. These spreads ranged from an additional 124 basis points for investments in apartments to a 695 basis point premium for investments in skilled nursing facilities.

VI. Survey of the Institutional Investment Community

Research Design

To ascertain the current risk and return perceptions of the institutional investment community toward alternative investments including seniors housing, a survey was conducted of the plan sponsor members of the Pension Real Estate Association (PREA). This organization has a significant number of members that are vendors to the pension fund community, but this study is focusing on the smaller group of investors that are employed by the pension fund community. The intent is to examine the attitudes and perceptions of the risk and return levels of alternative investments extending Worzala, *et. al.* (2000) to include the sub sectors of the seniors housing marketplace.

The survey was conducted by email using SurveyMonkey. The 2005-2006 and 2007-2008 PREA directories were used to create the email lists. Respondents were sent an initial email requesting them to participate in the study. They were directed to a survey hosted on the SurveyMonkey.com website in mid November of 2007. A follow-up email was sent about a month later in early December. A total of 286 respondents received the first email request to complete the survey, but 88 of the emails came back as undeliverable. A more recent version of the PREA directory (2007/08) was provided, and returned email addresses were individually reviewed. The initial database was purged of incorrect emails, and additional members were added to the list. The second email was sent to a total of 327 plan sponsors, and 22 were returned with unknown addresses. A total of 46 usable surveys were returned from a total of 304 individuals receiving the survey for a response rate of 15%. This relatively low response rate is not surprising given the busy lives of pension fund executives that are currently investing in the real estate sector.

Results

As illustrated in Exhibit 13, the vast majority of respondents were representatives from the government pension funds (61% or 28 funds) with the corporate funds making up just over 15% of the sample. The unions, endowments, and foundations were not nearly as well represented. Respondents were predominantly from the larger pension funds with 85% of the responses coming from the larger pension funds that have investment portfolios greater than $5 billion. By job title, the respondents were primarily executives of the pension plans. As detailed in Exhibit 14, 41% of the respondents held the job title of a pension fund executive (VP, CIO, COO, or Sr. VP), and 41% held a slightly lower title but were in charge of the real estate investments (real estate manager, director, investment officer, or portfolio manager).

To ascertain the types of decisions that the pension fund investors made, respondents were asked if they were responsible for the decision, played an advisory role, or were not responsible for the investment decisions – first, as they related to the investment alternatives found in a mixed-asset portfolio (stocks, bonds, and real estate) and second, as their investment decisions related to the real estate portfolio of the pension plan, endowment, or foundation. Exhibit 15 details the responses to this question and points out that the majority of the respondents were responsible for the real estate investments rather than the other asset classes. Only 5% reported they were involved directly in the mixed asset portfolio investment decisions although slightly more than one-fourth (28%) played an advisory role, while 68% said they played no part in these investment decisions. The respondents were close to investment decisions regarding the real estate portfolio, with 66 % indicating they were responsible for the asset allocation decisions, and only 7% indicating the decisions were something with which they were not involved.

Given the uncertainty in the investment community of how direct and indirect real estate decisions were made, respondents were also asked if they actively assisted in these allocation decisions. Clearly, they are actively involved with these decisions with more of the respondents claiming direct responsibility for the indirect real estate investments than the direct real estate investments. In both cases, about 25% had an advisory only role, but 70% of the respondents were directly responsible for indirect real estate decisions, while only 53% were directly responsible for making direct real estate investment decisions. This could be due to the fact that many pension funds delegate investment decisions for direct real estate investments to their advisory firms are in the form of sole discretion for separate accounts, or it is representative of the shift towards pension funds holding real estate as an indirect vehicle, striving for the liquidity and transparency that is often associated with the REIT investment alternative.

Not only is there a debate in the pension plan community about how decisions are made, but there is also a split in terms of how real estate related investments are accounted for in a portfolio. As illustrated in Exhibit 16, private REITS, real estate operating companies, and joint ventures in real estate are typically accounted for in the real estate portfolio. However, in some cases public REITs are considered real estate (74%), but in other portfolios they are counted as equities in the mixed asset portfolio (30%). Operating companies are also split with some funds accounting for these investments as real estate, and others considering them as components of the equities portfolio. Also, mortgages and commercial mortgage backed securities are not always accounted for similarly, with some investors considering them as fixed income securities rather than real estate investments. Mortgages were slightly more likely to be considered real estate (52%), while the CMBSs were more likely to be accounted for as fixed income (69%).

Another series of questions was asked to determine what real estate investment alternatives the responding pension plans are currently holding, looking to hold, or not at all interested in holding. The responses to these questions are detailed in Exhibit 17, and it appears that, at present, the seniors housing alternatives are not significant holdings of pension fund investors. Indirect seniors housing, both independent living and assisted living, were the most common subsectors of seniors housing to be held in a real estate portfolio, but only slightly more than half of the respondents held these investment alternatives. Somewhat less than a third held age-restricted apartments, while the remaining seniors housing alternatives are not presently held in most pension fund portfolios.

When queried about looking to invest in the real estate investment alternative, respondents placed seniors housing at the bottom of the list. The only non-seniors housing in the bottom 10 property types were direct hotel investments and direct international real estate investments. The desire to follow global trends is reflected in Panel B of Exhibit 17, as 37% of the respondents indicated they were currently looking to add indirect international real estate investments to their portfolios. The top seniors housing investment alternatives on the “likely to invest” list were the indirect independent living investment and age-restricted apartments, where 16% (or 6 pension funds) were contemplating adding these two investment alternatives.

Panel C asks the question one more time to determine which investments pension funds are currently considering. Apparently, most seniors housing investment alternatives are not on the radar screen for the pension plans that responded to this survey. Close to 90% of the respondents placed skilled nursing facilities high on their list of no interest. Once again, direct hotels and direct international investments were the only two non-seniors housing investment alternatives on the top of the “not at all interested” list. This indicates that the investment community, at least as far as the pension community is concerned, does not intend to be active in the seniors housing marketplace without a significant amount of education from the seniors housing investment community.

Finally, a series of questions were asked to determine the perceived risk and return levels for alternative investments available to today’s pension fund investors. First, respondents were asked to apply a Likert scale of 1-5 to rate the relative risk and return of investing in the more traditional asset classes (stocks, bonds, and real estate). Exhibit 18 details the mean ratings as well as the responses by grouping responses with 4 and 5 as higher risk, 3 as moderate risk, and 1 and 2 as lower risk. Mean risk ratings were not surprising, with venture capital viewed as the most risky of the alternative investments, with 85% of the respondents rating it a 4 or 5 on the Likert scale. This was followed by international equities, company stock, and US equities. Investors found indirect real estate to be more risky than direct real estate investments while CMBS investments were considered slightly less risky. Given the recent turmoil in the financial markets in terms of mortgage backed securities, these risk levels may be shifting. Straight mortgages had one of the lower risk ratings (2.77), and these investments were found to have mean risk rating levels similar to bonds. Panel B details the relative return ratings for each investment, and the order of mean return ratings shifts. Venture capital and international equities are still perceived to have the highest mean return ratings, but direct real estate has the third highest mean return rating (3.42), and REIT investments, particularly private REITs, move up on the list.

Exhibit 19 details the responses for investors considering investment alternatives for the real estate portfolio. Respondents appear to associate higher risk ratings with a wide range of seniors housing alternatives, as the four highest investment alternative mean risk ratings were attributed to seniors housing, with licensed Alzheimer's/dementia care at the top, followed by skilled nursing facilities (sub acute and rehab), followed by hybrid independent living/assisted living, and finally long term care skilled nursing facilities. Similar to the seniors housing alternatives, luxury lodging, private international real estate funds, and extended stay hotels also had higher mean risk ratings. The more traditional real estate investment alternatives were all rated with more moderate risk while regional malls, warehouses, and net properties all had lower mean risk ratings. A lack of knowledge about seniors housing is evidenced by the number of respondents indicating they were not familiar with the property type. Close to 40% of those who rated the licensed Alzheimer's/dementia facility indicated they were not familiar with the asset class, and most of the seniors housing alternatives had at least 6 respondents indicating they were not familiar with the investment alternative.

Panel B details the mean return ratings as well as the responses grouped by higher, moderate, and lower levels for the real estate investments. The order of properties by levels of returns shifts with international real estate (both direct and indirect) and commingled real estate funds moving to the top of the list. All of the seniors housing alternatives were considered to have more moderate returns, ranging from 3.5 for skilled nursing facilities to 3.26 for age-restricted apartments. These responses indicate why the pension plan investors have not made significant investments in the seniors housing property sector, given that they perceive many of the options to have a lower return relative to the risk associated with the investments. Again, many of the respondents reported lack of familiarity with the seniors housing market, with 10 respondents indicating they were not familiar with skilled nursing facilities or licensed Alzheimer's/dementia facilities. In fact, a significant number of respondents had limited familiarity with most of the seniors housing subsectors as investment alternatives.

VII. Conclusions

This study provides an in-depth analysis of three of the four major alternative subsectors of the seniors housing marketplace. Investments in independent living, assisted living, and skilled nursing facilities are described in detail. As with any real estate investment, the majority of the unique risks are due to the uncertainty associated with the cash flows generated by the investment. As one moves up the risk spectrum for seniors housing there is more variance because the cash flows are more dependent on the services being offered to the tenants of the investment. These variances are highlighted, and we have provided the seniors housing investor with ways to mitigate these risks, including diversifying the product type on a single campus, so residents can "age in place"; turnover can be reduced, and cash flows can be stabilized. Average occupancy and length of stay are significantly longer for the seniors housing investments than in the apartment market or the hotel sector. Paying close attention to management is essential, particularly as one progresses up the risk spectrum. "Pay as you go" contracts will help minimize the likelihood that expenses will be forecasted inaccurately and could enhance the return on an investment.

We also report the results of a survey of plan sponsor members of the Pension Real Estate Association. Respondents were asked their perceptions on the risk and return levels associated with the seniors housing sectors in comparison to more traditional real estate investments and to more conventional financial assets, including stocks and bonds. The results of the survey show clearly that members of the pension fund investment community are not currently invested nor are they looking to invest in seniors housing. They rate the risks higher than some of the other more traditional real estate investments but the returns lower than some of the alternative investments that might be considered relatively risky, such as international real estate investments.

We believe this mismatch of risk and return levels is due to a lack of understanding of the seniors housing sub sectors and hope this research provides a clearer picture of the market and will allow for a better understanding of the seniors housing investment alternatives. Continued research is needed to expand the data that is available, particularly as it relates to revenues and expenses associated with the various subsectors of the seniors housing market. In addition, a significant number of respondents admitted a lack of familiarity with the investment alternative, thereby providing evidence that NIC's mission to educate the institutional investment community may not be complete. With increased education and data about the performance characteristics of the properties, as well as ways that the risks can be mitigated while holding seniors housing investments, investors will gain a better appreciation for industry. That is, they will realize that many of seniors housing sub sectors are not significantly different from assets with which they are already familiar, including apartments and hotel properties. As more investors consider seniors housing, they will give this property type a higher degree of scrutiny and hopefully expand investments, given the ever increasing need for new development as our population continues to age.

Appendix A
Seniors Housing Experts Interviewed for the Study

Appraisers

Michael Boehm
Senior Living Valuation Services, Inc
www.slvsinc.com

Alan Plush
HealthTrust, LLC
www.healthtrust.com

Sterling Short
Tellatin, Short, Hansen, & Clark, Inc
www.tellatin.com

James Tellatin
Tellatin, Short, Hansen, & Clark, Inc.
www.tellatin.com

Brokers

Mary Christianson
CBRE Senior Housing Services
www.cbre.com

Mel Gamzon
Senior Housing Investment Advisors, Inc
http://www.snrhousing.com

Jacob Gehl
Marcus & Millichap
www.marcusmillichap.com

Allen McMurty
CLW Health Care Services Group
http://www.clwhcsg.com/

Mark Myers
Marcus & Millichap
www.marcusmillichap.com

David Rothschild
CBRE Senior Housing Services
www.cbre.com

Consultants

Norm Gamzon
Senior Housing Investment Advisors, Inc
www.snrhousing.com

Norm LeZotte
Cushman & Wakefield
www.cushwake.com

Jim Moore
Moore Diversified Services, Inc.
www.m-d-s.com

Meredith Oppenheim
Oppenheim Real Estate Ventures
www.oppenoffice.com

David Passero
HTG Consultants
www.htgconsultants.com

Member Organizations

Michael Hargrave
National Investment Center
www.nicmap.org

Robert G. Kramer
National Investment Center
www.nicmap.org

Sarah Powell Cooper
National Investment Center
www.nicmap.org

David Schless
American Senior Housing Association
www.seniorhousing.com

Associations Focused on Seniors Housing

American Association of Homes and Services for the Aging
www.aahsa.org

American Health Care Association (AHCA)
www.ahca.org

American Senior Housing Association (ASHA)
www.seniorshousing.org

Continuing Care Accreditation Commission
www.carf.org

The Henry J. Kaiser Family Foundation
www.kff.com

National Conference of State Legislatures (NCSL)
www.ncsl.org

National Center for Assisted Living (NCAL)
www.ncal.org

National Investment Center for the Seniors Housing & Care Industry
www.nic.org

US Department of Health and Human Services
www.medicare.gov

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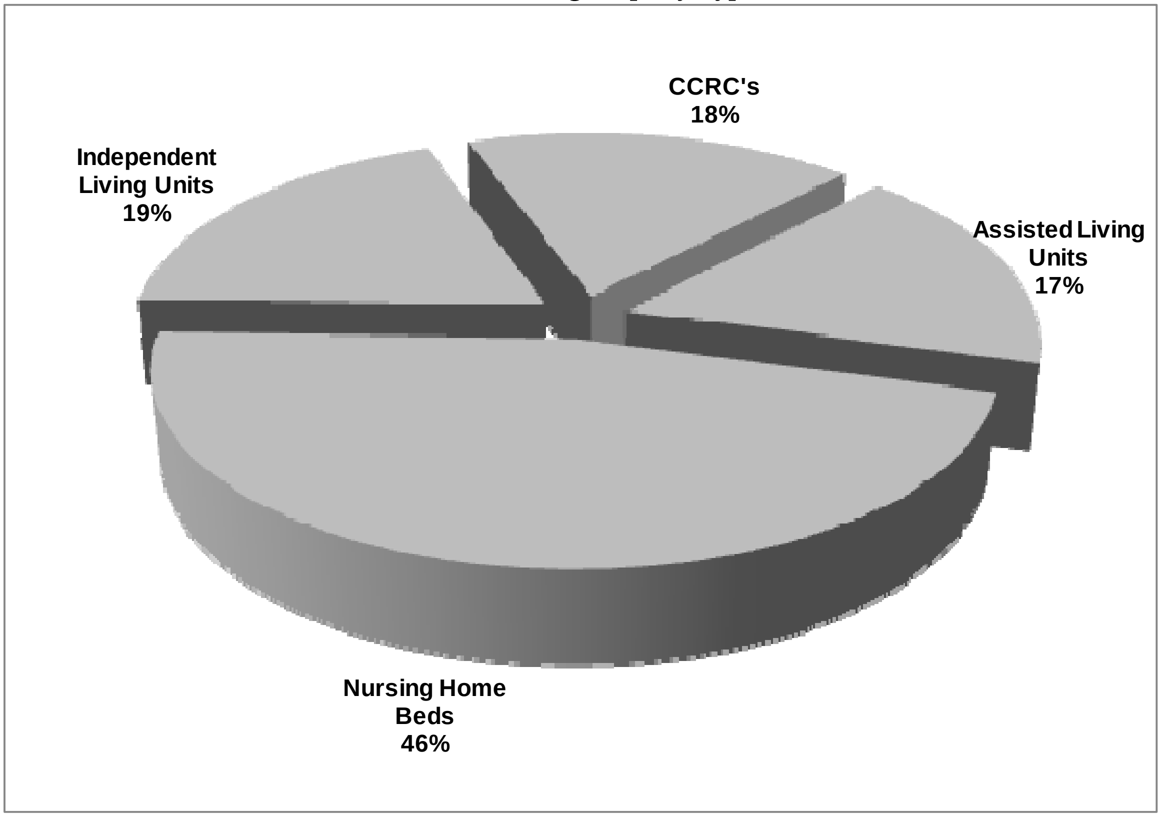
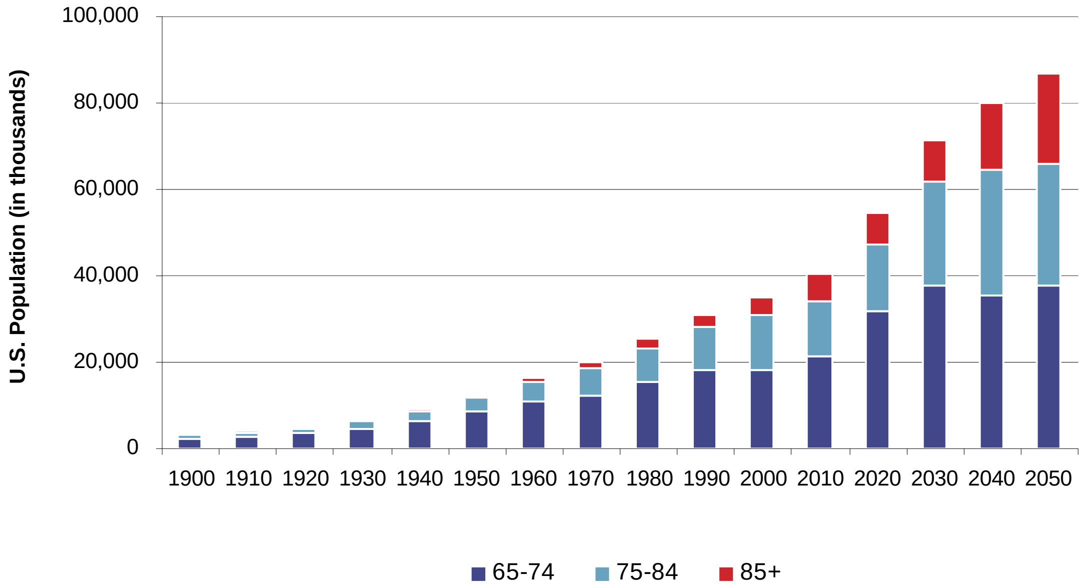
Exhibit 1
Seniors Housing Property Types



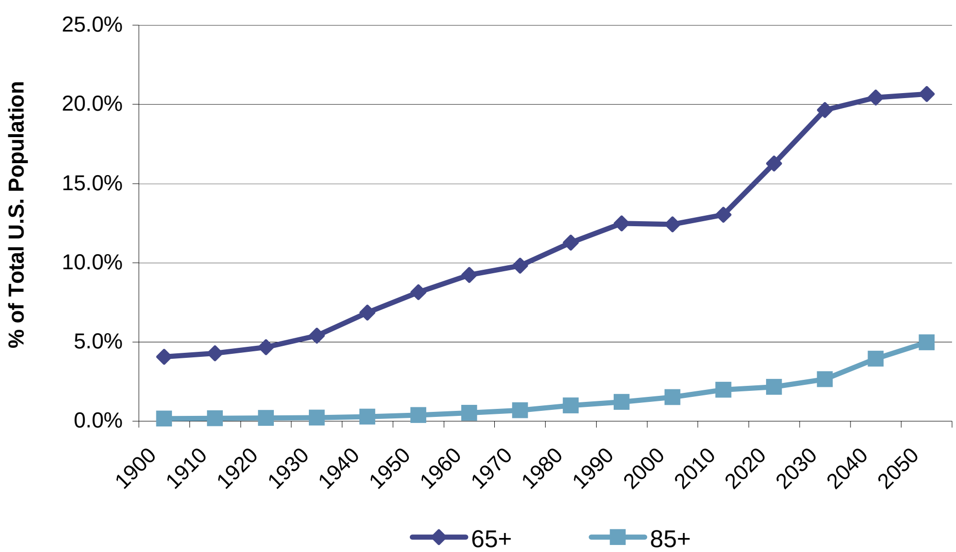
Source: NIC, *Size, Scope and Performance of the Seniors Housing & Care Industry, 2004 Update*

Exhibit 2
U.S. Population by Age



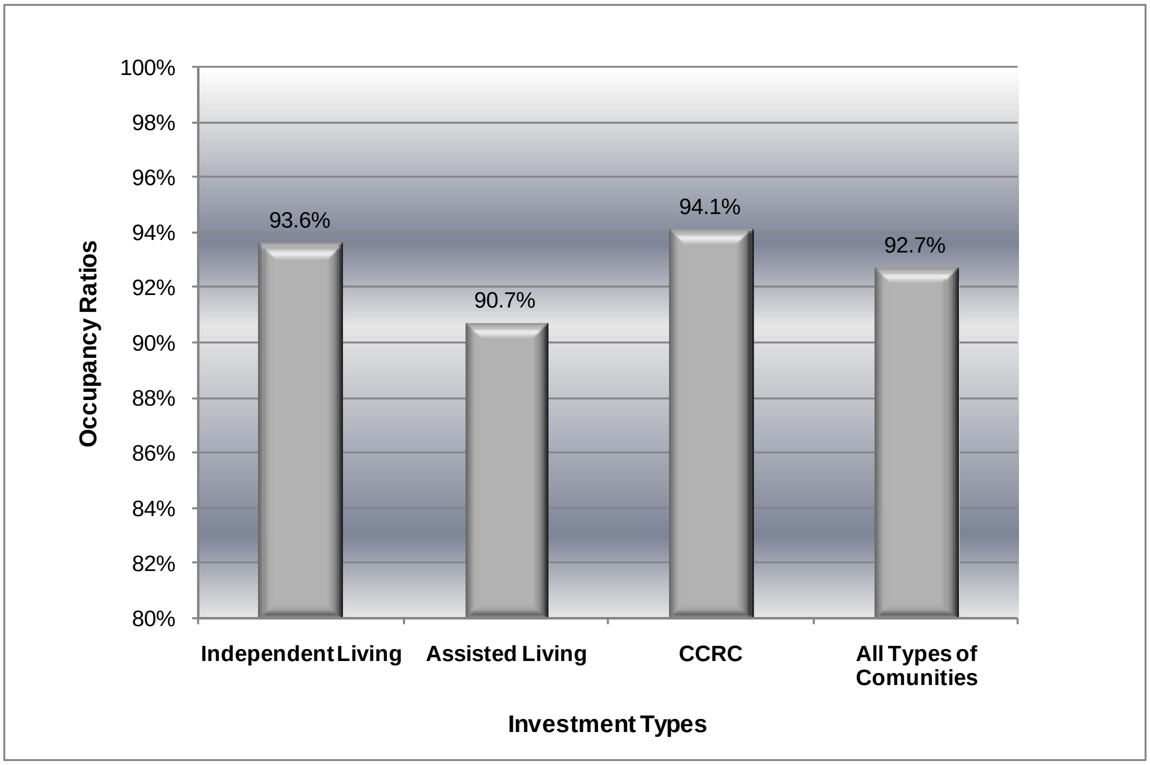
Source*: U.S. Bureau of Census*

Exhibit 3
Percentage of U.S. Population Over the Ages of 65 and 85



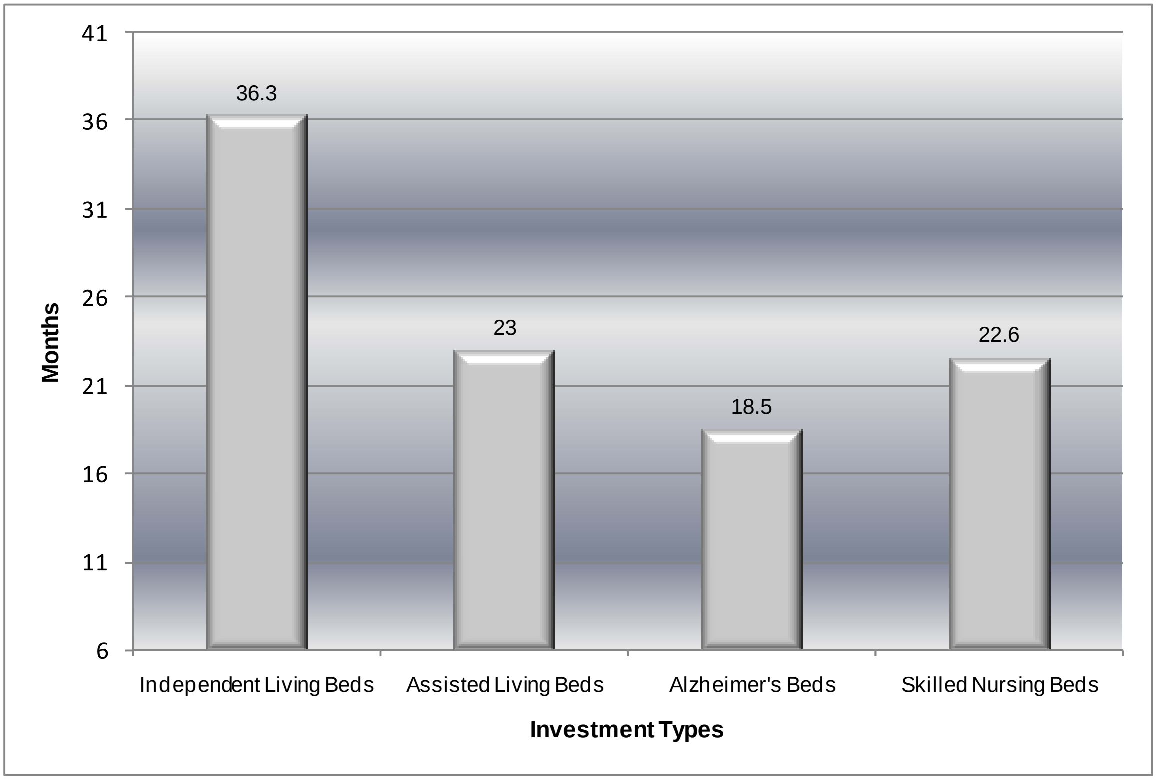
Source*: U.S. Bureau of Census*

Exhibit 4
Occupancy Rates in For-Profit Communities



Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 5
Average Length of Stay

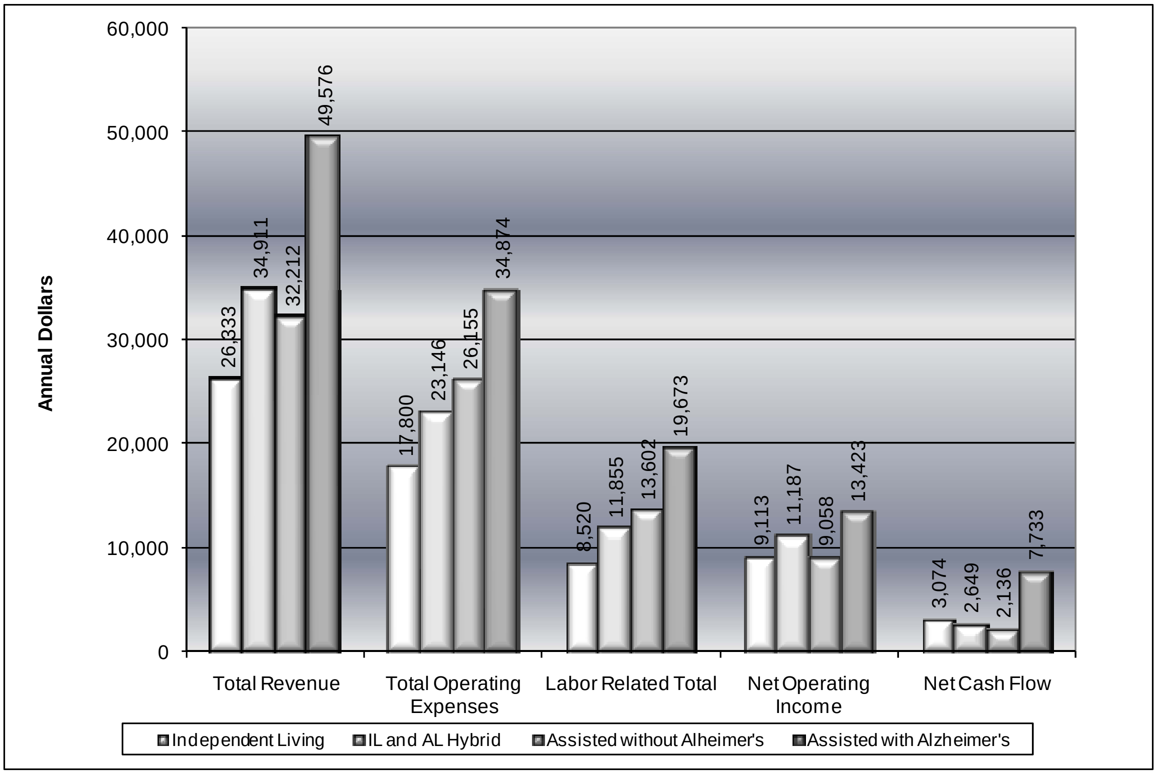


Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 6
Annual Changes in In-House Rents vs. Annual Changes in Market Rents
2004-2005

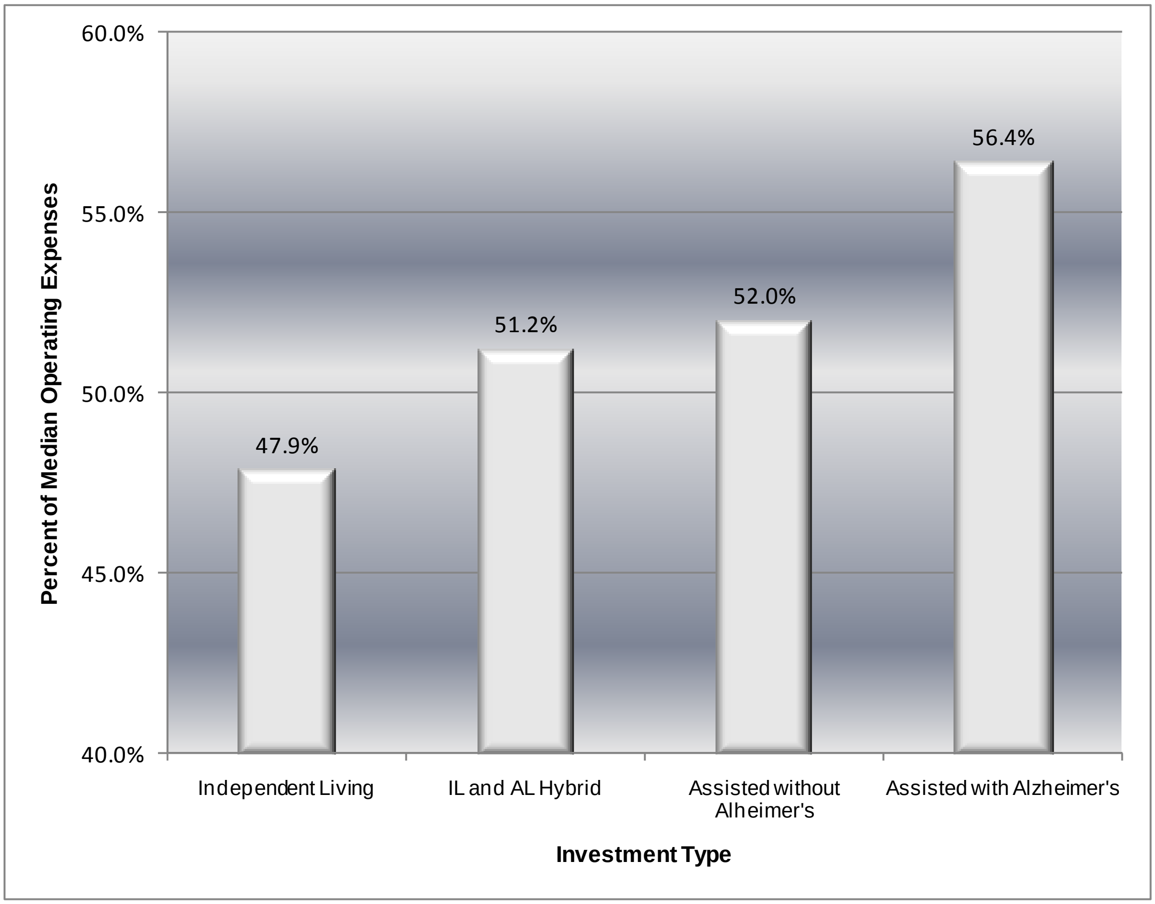
Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 7
Median Financial Values
2005



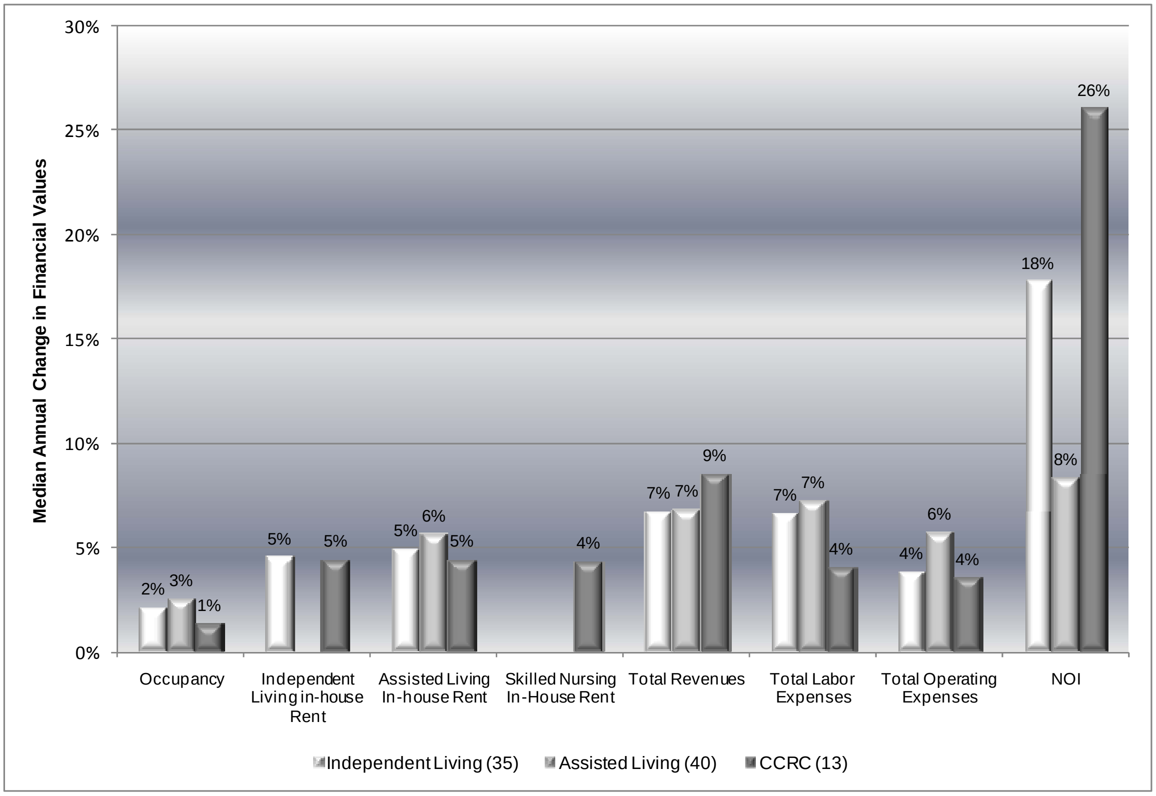
Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 8
Median Labor Related Expenses
(Percent of Median Total Operating Expenses)



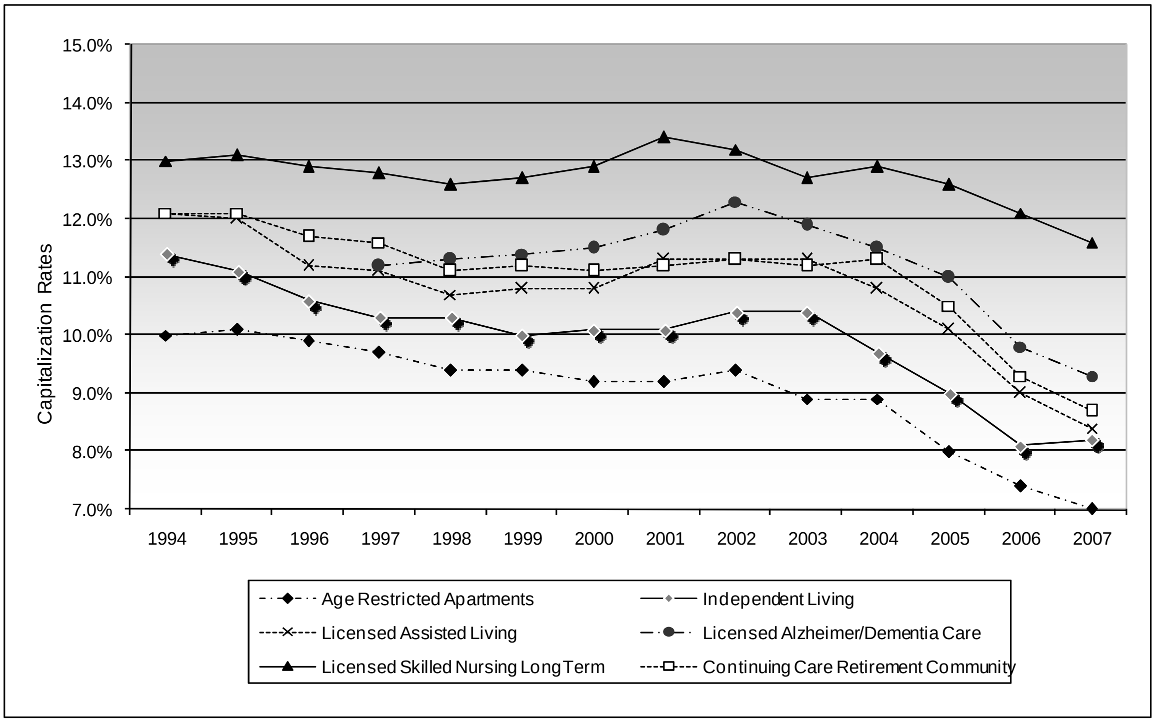
Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 9
Trend Analysis of Key Financial Statistics 2005-2006



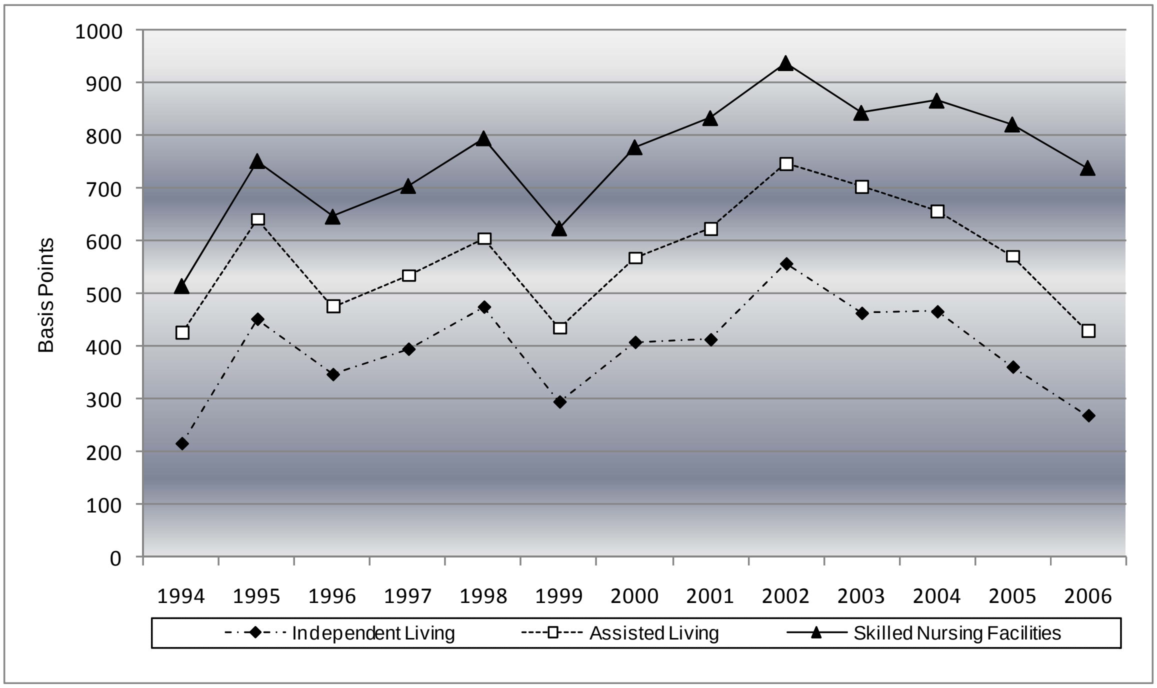
Source: ASHA, *The State of Seniors Housing 2006*

Exhibit 10
Trends in Return Expectations for Alternative Seniors Housing Investments
(based on the Boehm Survey)
1994 – 2007



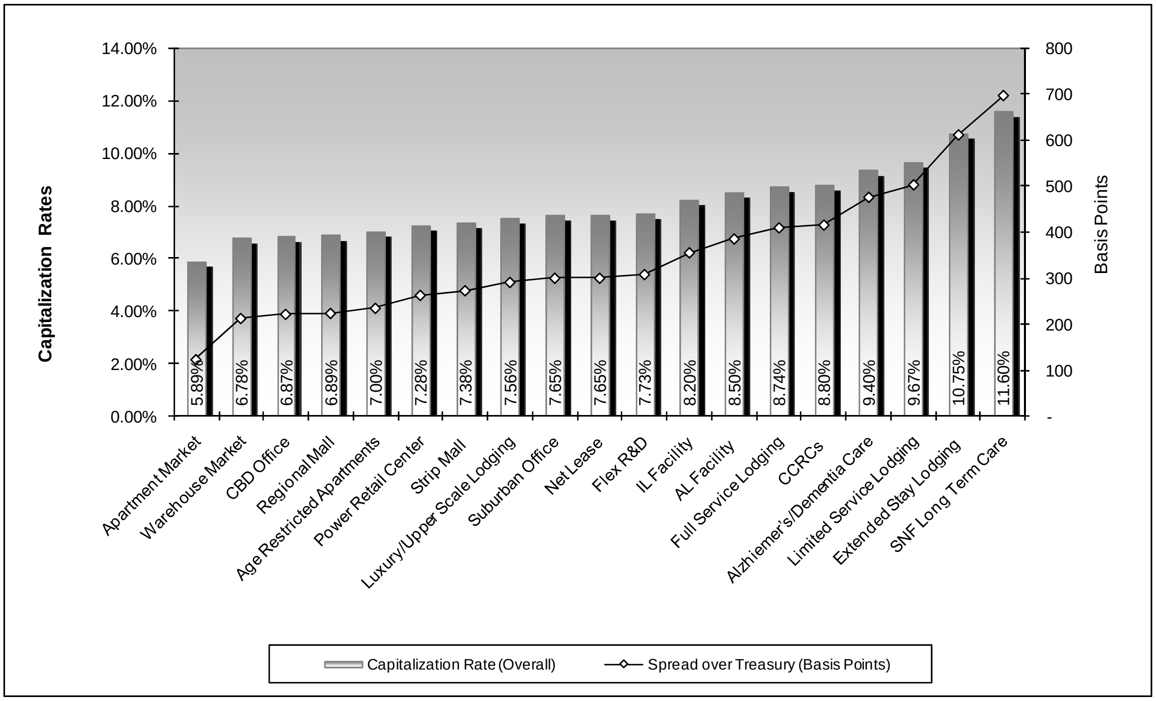
Source: Boehm, *Seniors Housing Investment Survey, 1994-2007*

Exhibit 11
Comparison of Spread Over 10-Year Treasury Bond for Expected Returns from Alternative Seniors Housing Investments



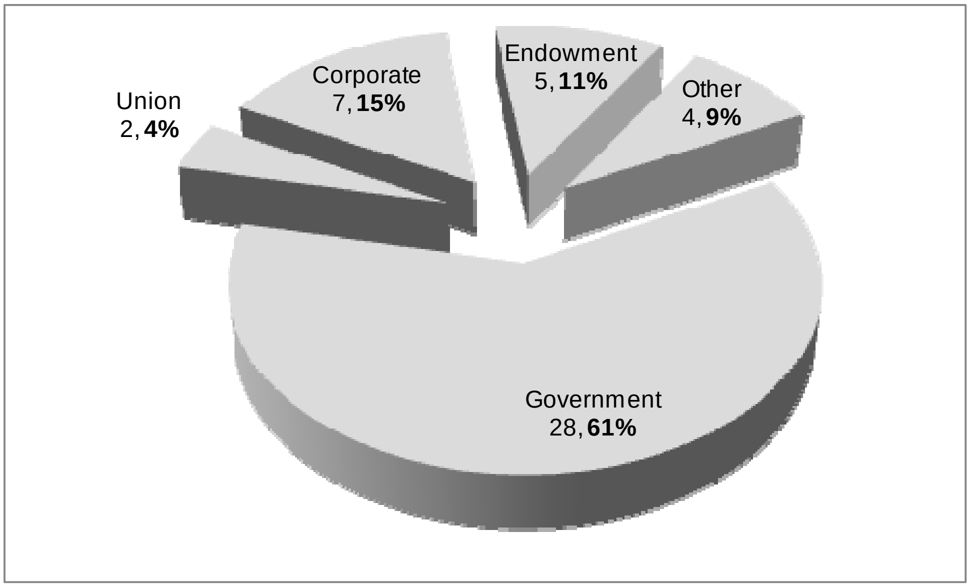
Source: Boehm, *Seniors Housing Investment Survey*, 1994-2006 and US Department of the Treasury

Exhibit 12
Traditional vs. Seniors Housing Investment Alternatives Return Expectations and Spread Over the 10-Year Treasury Bonds
First Quarter 2007



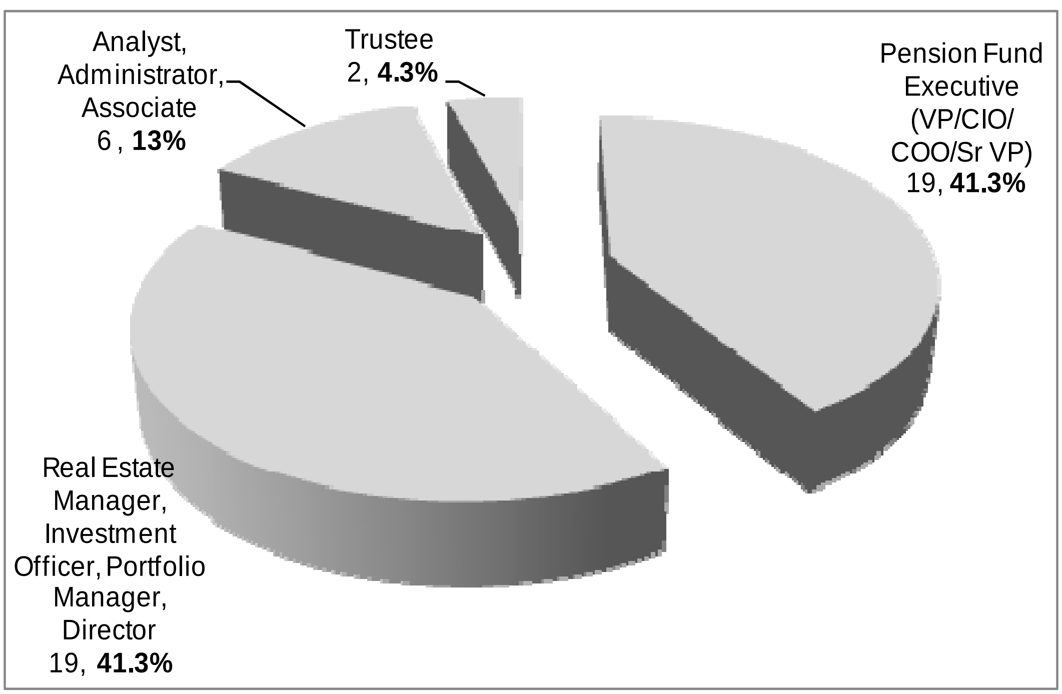
Source: Boehm, *Seniors Housing Investment Survey* (2007), *Korpacz Report*, 2007; US Department of the Treasury, 2007

Exhibit 13
Number and Percent of Plan Sponsor Survey Respondents by Type of Fund
(n=46)



Source: Authors' calculations

Exhibit 14
Respondent's Current Job Title
(n=46)



Source: Authors' calculations

Exhibit 15
Responsibility of Respondents toward Investment Decisions

Real Estate Investment Alternatives	I advise only		I am responsible for making these		I am not responsible for		Response Count
Mixed asset investment decisions (allocations between stocks, bonds, real estate)	11	27.5%	2	5.0%	27	67.5%	40
Within the property asset class investment decisions (allocations between property types)	11	26.8%	27	65.9%	3	7.3%	41
Specific investment decisions for a given indirect real estate investment	11	26.8%	29	70.7%	1	2.4%	41
Specific investment decisions for a given direct real estate investment	10	25.6%	21	53.8%	8	20.5%	39

Source: Authors' calculations

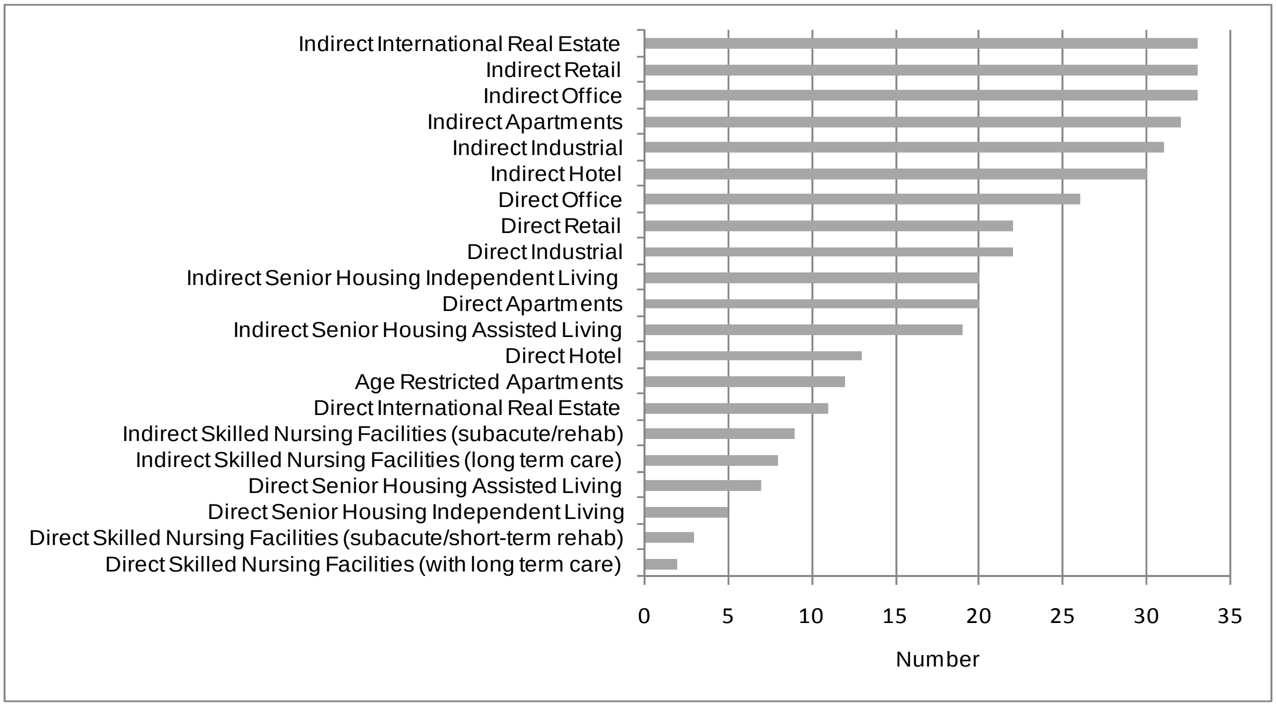
Exhibit 16
Accounting for Real Estate Investments in Mixed Asset Portfolios

Investment Alternatives	In the real estate portfolio		In the equities portfolio		In the fixed income portfolio		Not sure which portfolio		Response Count
Private Real Estate Investment Trusts	36	97.3%	2	5.4%	0	0.0%	0	0.0%	37
Real Estate Operating Companies	36	97.3%	2	5.4%	0	0.0%	0	0.0%	37
Joint Ventures in Real Estate	33	97.1%	0	0.0%	0	0.0%	1	2.9%	34
Public Real Estate Investment Trusts	29	74.4%	12	30.8%	1	2.6%	0	0.0%	39
Operating Companies	21	63.6%	8	24.2%	0	0.0%	6	18.2%	33
Mortgages	18	52.9%	0	0.0%	19	55.9%	1	2.9%	34
Commercial Mortgage Backed Securities	14	38.9%	0	0.0%	25	69.4%	2	5.6%	36

Source: Authors' calculations. In some cases respondents chose two or more categories for the investments so percentages will not add to 100%.

Exhibit 17

Panel A: **Number of Respondents Currently Holding the Real Estate Investment Alternative**

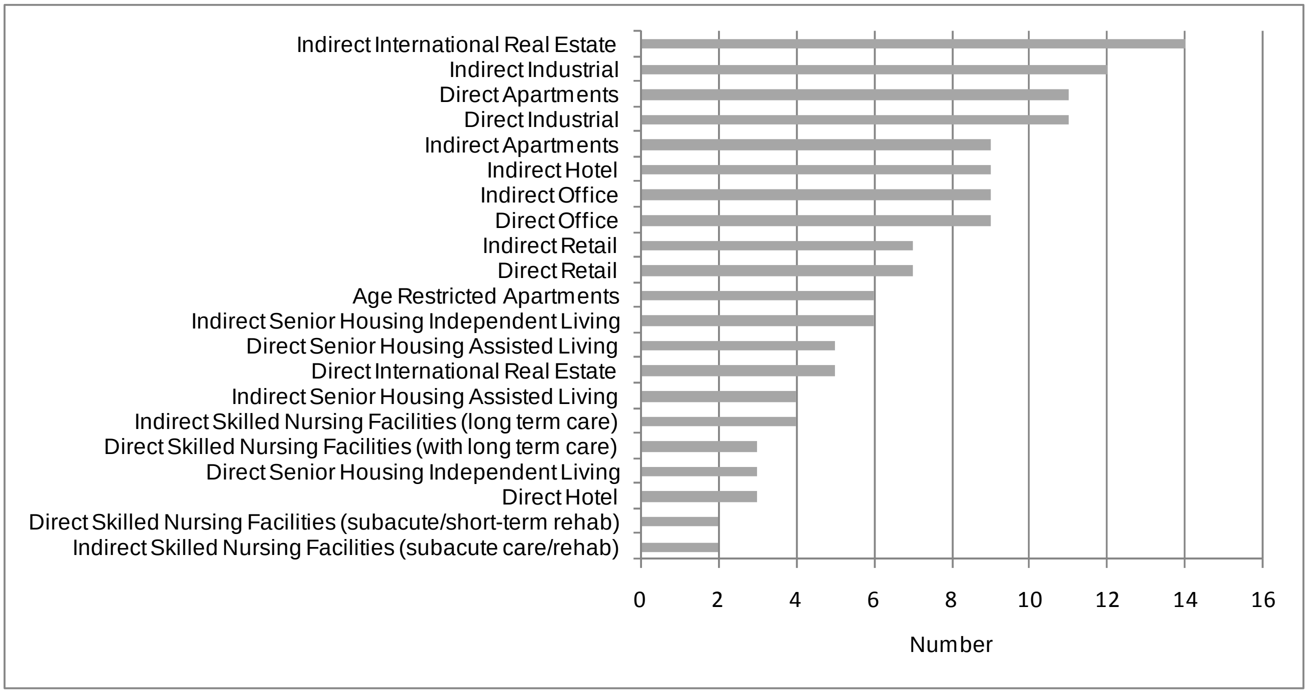


Real Estate Investment Alternatives	Currently Hold	Response Percent	Response Count
Indirect Office	33	89.2%	41
Indirect Retail	33	89.2%	40
Indirect International Real Estate Investments	33	89.2%	40
Indirect Apartments	32	86.5%	41
Indirect Industrial	31	83.8%	40
Indirect Hotel	30	81.1%	40
Direct Office	26	70.3%	37
Direct Industrial	22	59.5%	37
Direct Retail	22	59.5%	37
Direct Apartments	20	54.1%	36
Indirect Senior Housing Independent Living (with congregate dining and other services)	20	54.1%	38
Indirect Senior Housing Assisted Living	19	51.4%	38
Direct Hotel	13	35.1%	37
Age Restricted Apartments	12	32.4%	35
Direct International Real Estate Investments	11	29.7%	36
Indirect Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	9	24.3%	36
Indirect Skilled Nursing Facilities (primarily with long term care)	8	21.6%	37
Direct Senior Housing Assisted Living	7	18.9%	36
Direct Senior Housing Independent Living (with congregate dining and other services)	5	13.5%	36
Direct Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	3	8.1%	36
Direct Skilled Nursing Facilities (primarily with long term care)	2	5.4%	37

Source: Authors' calculations

Exhibit 17 (continued)

Panel B: **Number of Respondents Looking to Add the Real Estate Investment Alternative**

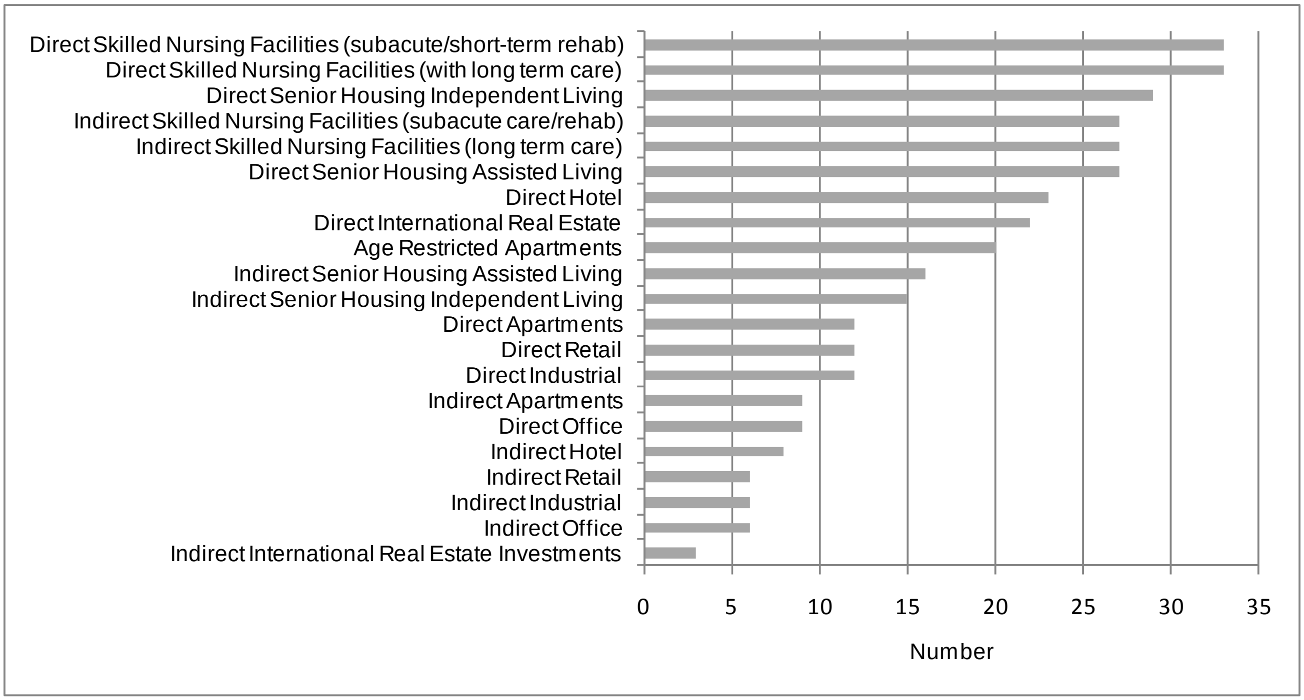


Real Estate Investment Alternatives	Looking to Add	Response Percent	Response Count
Indirect International Real Estate Investments	14	37.8%	40
Indirect Industrial	12	32.4%	40
Direct Industrial	11	29.7%	37
Direct Apartments	11	29.7%	36
Direct Office	9	24.3%	37
Indirect Office	9	24.3%	41
Indirect Hotel	9	24.3%	40
Indirect Apartments	9	24.3%	41
Direct Retail	7	18.9%	37
Indirect Retail	7	18.9%	40
Indirect Senior Housing Independent Living (with congregate dining and other services)	6	16.2%	38
Age Restricted Apartments	6	16.2%	35
Direct International Real Estate Investments	5	13.5%	36
Direct Senior Housing Assisted Living	5	13.5%	36
Indirect Skilled Nursing Facilities (primarily with long term care)	4	10.8%	37
Indirect Senior Housing Assisted Living	4	10.8%	38
Direct Hotel	3	8.1%	37
Direct Senior Housing Independent Living (with congregate dining and other services)	3	8.1%	36
Direct Skilled Nursing Facilities (primarily with long term care)	3	8.1%	37
Indirect Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	2	5.4%	36
Direct Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	2	5.4%	36

Source: Authors' calculations

Exhibit 17 (continued)

Panel C: **Number of Respondents Not Interested in Holding the Real Estate Alternative**



Real Estate Investment Alternatives	Not Interested	Response Percent	Response Count
Direct Skilled Nursing Facilities (primarily with long term care)	33	89.2%	37
Direct Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	33	89.2%	36
Direct Senior Housing Independent Living (with congregate dining and other services)	29	78.4%	36
Direct Senior Housing Assisted Living	27	73.0%	36
Indirect Skilled Nursing Facilities (primarily with long term care)	27	73.0%	37
Indirect Skilled Nursing Facilities (primarily with subacute care/short-term rehab)	27	73.0%	36
Direct Hotel	23	62.2%	37
Direct International Real Estate Investments	22	59.5%	36
Age Restricted Apartments	20	54.1%	35
Indirect Senior Housing Assisted Living	16	43.2%	38
Indirect Senior Housing Independent Living (with congregate dining and other services)	15	40.5%	38
Direct Industrial	12	32.4%	37
Direct Retail	12	32.4%	37
Direct Apartments	12	32.4%	36
Direct Office	9	24.3%	37
Indirect Apartments	9	24.3%	41
Indirect Hotel	8	21.6%	40
Indirect Office	6	16.2%	41
Indirect Industrial	6	16.2%	40
Indirect Retail	6	16.2%	40
Indirect International Real Estate Investments	3	8.1%	40

Source: Authors' calculations

Exhibit 18
Investment Alternatives Ranked by Risk and Return Ratings
Panel A: Risk Ratings

Investment Alternatives	Higher Risk		Moderate Risk		Lower Risk		Unfamiliar with Category	Mean Rating	Response Count
Venture Capital	22	84.6%	1	3.8%	0	0.0%	3	4.83	26
International Equities	17	65.4%	5	19.2%	1	3.8%	3	3.83	26
Company Stock	12	46.2%	11	42.3%	0	0.0%	3	3.61	26
US Equities	12	46.2%	12	46.2%	0	0.0%	2	3.58	26
Private REITs	13	50.0%	10	38.5%	3	11.5%	0	3.38	26
Public REITS	12	46.2%	12	46.2%	2	7.7%	0	3.38	26
Direct Real Estate	9	34.6%	14	53.8%	3	11.5%	0	3.27	26
CMBS	8	30.8%	14	53.8%	4	15.4%	0	3.23	26
US Indexed Equities	8	32.0%	13	52.0%	3	12.0%	1	3.21	25
Mutual Funds	6	23.1%	11	42.3%	5	19.2%	4	3.09	26
International Bonds	7	26.9%	11	42.3%	5	19.2%	3	3.09	26
Mortgages	5	19.2%	10	38.5%	11	42.3%	0	2.77	26
Corporate Bonds	2	7.7%	10	38.5%	12	46.2%	2	2.58	26
US Bonds Other Than Government Bonds	2	7.7%	9	34.6%	13	50.0%	2	2.42	26
US Government Bonds	0	0.0%	1	3.7%	24	88.9%	2	1.20	27

Source: Authors' calculations. Respondents used a Likert scale with 5=high risk, 1=low risk, Higher Risk combines 4 and 5, Lower Risk combines 1 and 2. Not all respondents rated each alternative so the n differs from investment to investment.

Exhibit 18 (continued)
Investment Alternatives Ranked by Risk and Return Ratings
Panel B: Return Ratings

Investment Alternatives	Higher Return		Moderate Return		Lower Return		Unfamiliar with Category	Mean Rating	Response Count
Venture Capital	22	84.6%	1	3.8%	0	0.0%	3	4.61	26
International Equities	16	61.5%	6	23.1%	0	0.0%	4	3.82	26
Direct Real Estate	10	38.5%	13	50.0%	3	11.5%	0	3.42	26
Company Stock	8	30.8%	13	50.0%	1	3.8%	4	3.36	26
Private REITs (Indirect Real Estate)	10	38.5%	14	53.8%	2	7.7%	0	3.35	26
US Equities	6	23.1%	17	65.4%	0	0.0%	3	3.30	26
Public REITs (Indirect Real Estate)	9	36.0%	11	44.0%	5	20.0%	0	3.16	25
Mutual Funds	2	7.7%	19	73.1%	0	0.0%	5	3.10	26
US Indexed Equities	5	19.2%	15	57.7%	3	11.5%	3	3.09	26
CMBS	4	16.0%	10	40.0%	11	44.0%	0	2.76	25
Mortgages	3	12.0%	12	48.0%	10	40.0%	0	2.72	25
International Bonds	3	12.0%	8	32.0%	11	44.0%	3	2.59	25
Corporate Bonds	2	7.7%	5	19.2%	16	61.5%	3	2.39	26
US Bonds Other Than Government	1	3.8%	5	19.2%	17	65.4%	3	2.22	26
US Government Bonds	0	0.0%	2	7.4%	22	81.5%	3	1.25	27

Source: Authors' calculations. Respondents used a Likert scale with 5=high risk, 1=low risk, Higher Risk combines 4 and 5, Lower Risk combines 1 and 2. Not all respondents rated each alternative so the n differs from investment to investment.

Exhibit 19
Alternative Real Estate Investments Risk and Return Ratings
Panel A: Risk Ratings

Investment Alternatives	Higher Risk		Moderate Risk		Lower Risk		Unfamiliar with Property Type	Mean Rating	Response Count
Licensed Alzhiemer's/Dementia Facility	13	48.1%	2	7.4%	1	3.7%	11	4.25	27
Skilled Nursing Facilities (subacute care/rehab)	1	3.7%	4	15.4%	1	3.7%	7	4.15	27
Hybrid Independent Living and Assisted Living Facilities	14	53.8%	2	7.7%	1	3.8%	9	4.00	26
Skilled Nursing Facilities (primarily with long term care)	12	46.2%	4	15.4%	1	3.8%	9	4.00	26
Luxury/Upper Scale Lodging	18	69.2%	8	30.8%	0	0.0%	0	3.96	26
Private International Real Estate Funds	20	76.9%	6	23.1%	0	0.0%	0	3.92	26
Extended Stay Lodging	16	61.5%	9	34.6%	0	0.0%	1	3.92	26
Continuing Care Retirement Communities	14	53.8%	5	19.2%	1	3.8%	6	3.90	26
Licensed Assisted Living Facility (Stand Alone)	12	46.2%	4	15.4%	1	3.8%	9	3.88	26
Health Care Operating Companies	11	42.3%	5	19.2%	1	3.8%	9	3.88	26
Limited Service Lodging	14	53.8%	8	30.8%	1	3.8%	3	3.87	26
Public International Real Estate Funds	18	69.2%	8	30.8%	0	0.0%	0	3.85	26
Full Service Lodging	18	69.2%	6	23.1%	1	3.8%	1	3.84	26
Senior Housing Independent Living	12	46.2%	6	23.1%	1	3.8%	7	3.74	26
Real Estate Mortgage Investment Conduits	14	53.8%	6	23.1%	1	3.8%	5	3.71	26
Senior Housing Specialized REITs	13	50.0%	7	26.9%	0	0.0%	6	3.70	26
Suburban Office	15	57.7%	11	42.3%	0	0.0%	0	3.69	26
Private Commingled Real Estate Funds (CREFs)	11	44.0%	12	48.0%	1	4.0%	1	3.58	25
Flex R&D	12	46.2%	12	46.2%	0	0.0%	2	3.54	26
Strip Mall	10	38.5%	14	53.8%	2	7.7%	0	3.38	26
CBD Office	9	34.6%	14	53.8%	2	7.7%	1	3.32	26
Age Restricted Apartments	8	30.8%	10	38.5%	3	11.5%	5	3.29	26
Diversified Private Real Estate Investment Trusts	9	34.6%	13	50.0%	4	15.4%	0	3.23	26
Diversified Public Real Estate Investment Trusts	7	26.9%	15	57.7%	4	15.4%	0	3.12	26
Power Retail Center	4	15.4%	16	61.5%	6	23.1%	0	3.00	26
Apartment Market	3	11.5%	16	61.5%	5	19.2%	2	2.96	26
Regional Mall	4	15.4%	14	53.8%	8	30.8%	0	2.88	26
Warehouse Market	2	7.7%	11	42.3%	10	38.5%	3	2.70	26
Net Lease Properties	1	3.8%	4	15.4%	20	76.9%	1	2.04	26

Source: Authors' calculations. Respondents used a Likert scale with 5=high risk, 1=low risk, Higher Risk combines 4 and 5, Lower Risk combines 1 and 2. Not all respondents rated each alternative so the n differs from investment to investment.

Exhibit 19 (continued)
Alternative Real Estate Investments Risk and Return Ratings
Panel B: Return Ratings

Investment Alternatives	Higher Return		Moderate Return		Lower Return		Unfamiliar with Property Type	Mean Rating	Response Count
Private International Real Estate Funds	19	73.1%	5	19.2%	1	3.8%	1	4.08	26
Public International Real Estate Funds	17	68.0%	7	28.0%	1	4.0%	0	3.84	25
Private Commingled Real Estate Funds (CREFs)	12	48.0%	10	40.0%	1	4.0%	2	3.65	25
Luxury/Upper Scale Lodging	17	65.4%	6	23.1%	2	7.7%	1	3.64	26
Hybrid Independent Living and Assisted Living Facilities	9	36.0%	6	24.0%	1	4.0%	9	3.56	25
Full Service Lodging	13	50.0%	9	34.6%	2	7.7%	2	3.54	26
Extended Stay Lodging	13	50.0%	10	38.5%	2	7.7%	1	3.52	26
Skilled Nursing Facilities (subacute care/rehab)	9	34.6%	5	19.2%	2	7.7%	10	3.50	26
Health Care Operating Companies	9	36.0%	5	20.0%	3	12.0%	8	3.41	25
Skilled Nursing Facilities (primarily with long term care)	9	34.6%	4	15.4%	4	15.4%	9	3.41	26
Licensed Alzhiemer's/Dementia Facility	8	30.8%	5	19.2%	3	11.5%	10	3.38	26
Senior Housing Independent Living	7	26.9%	9	34.6%	3	11.5%	7	3.37	26
Diversified Private Real Estate Investment Trusts	11	44.0%	10	40.0%	3	12.0%	1	3.33	25
Licensed Assisted Living Facility (Stand Alone)	8	30.8%	8	30.8%	2	7.7%	8	3.33	26
Continuing Care Retirement Communities	9	34.6%	6	23.1%	3	11.5%	8	3.33	26
Senior Housing Specialized REITs	7	26.9%	7	26.9%	3	11.5%	9	3.29	26
Age Restricted Apartments	5	20.0%	13	52.0%	1	4.0%	6	3.26	25
Limited Service Lodging	10	38.5%	10	38.5%	4	15.4%	2	3.25	26
Strip Mall	5	20.0%	17	68.0%	3	12.0%	0	3.12	25
Suburban Office	7	28.0%	14	56.0%	4	16.0%	0	3.12	25
CBD Office	8	32.0%	11	44.0%	6	24.0%	0	3.08	25
Diversified Public Real Estate Investment Trusts	7	26.9%	14	53.8%	4	15.4%	1	3.08	26
Flex R&D	5	19.2%	13	50.0%	7	26.9%	1	2.96	26
Apartment Market	5	19.2%	13	50.0%	6	23.1%	2	2.96	26
Real Estate Mortgage Investment Conduits	5	20.0%	9	36.0%	6	24.0%	5	2.95	25
Warehouse Market	2	8.0%	13	52.0%	7	28.0%	3	2.82	25
Regional Mall	4	16.0%	12	48.0%	9	36.0%	0	2.76	25
Power Retail Center	3	12.0%	14	56.0%	8	32.0%	0	2.76	25
Net Lease Properties	2	8.3%	5	20.8%	17	70.8%	0	2.21	24

Source: Authors' calculations. Respondents used a Likert scale with 5=high return, 1=low return, Higher Retrun combines 4 and 5, Lower Return combines 1 and 2. Not all respondents rated each alternative so the n differs from investment to investment.