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Jones Lang LaSalle predicts new signs of life in healthcare real estate

Uncertainty surrounding healthcare reform, a constrained capital environment and intense cost-containment demands represent the triple threat that put healthcare growth and construction on life support for the past several years. But since early 2011, improved liquidity in the capital markets and an increasing desire to enact a thoughtful, well-planned approach to meeting future demands are producing new signs of life, according to Jones Lang LaSalle's Healthcare Solutions group and its Healthcare Real Estate Summer Outlook.



Peter Bulgarelli

Chief Operating Officer

"Healthcare spending now encompasses more than 17 percent of the Gross Domestic Product in the United States healthcare systems must act now to prepare, address and integrate the needs of more than 32 million insured by 2014."

In its Healthcare Real Estate Outlook, Jones Lang LaSalle predicts the demand for healthcare real estate, particularly medical office buildings and other ambulatory care facilities, will continue to grow. Trends that will have the greatest impact for healthcare owners and operators include:

Healthcare development becomes more intentional

Development plans for outpatient facilities, ambulatory care and strategic links between hospitals and the communities they serve that had been put on ice for the past few years are now thawing and moving forward. More than ever, these developments are part of dynamic, need-based growth strategies and, in the absence of traditional financing outlets, are moving forward with creative financing sources.

One example is the construction of a medical office building by Piedmont Healthcare. Jones Lang LaSalle is representing Piedmont, the major tenant in the MOB. Piedmont is building the property to decongest their main campus and make outpatient services more accessible.



Mindy Berman

Director Capital Markets

"There is a great deal of pent-up demand from healthcare systems stymied these past few years by a near shutdown in the credit markets. Demographic growth and the push to outpatient services have created urgency for development."

Joe Euphrat, Managing Director in the firm's Healthcare Capital Markets group, added that the tax-exempt bond market essentially disappeared in the fall of 2008 and remains disrupted. The cost of funds has narrowed between tax-exempt rates and private/public healthcare capital investors which is causing more systems to seek alternative capital sources for funding.

Mergers and acquisitions will further accelerate growth

The consolidation of hospitals and systems will continue along with acquisitions of severely challenged hospitals by larger systems and, in some markets, not-for-profit organizations by for-profits. The main consolidation trend affecting healthcare real estate in the months to come will be a significant uptick in mergers as providers seek to capitalize on economies of scale and mitigate the impact of reduced rates of reimbursement. For example, a merger of two hospital systems will allow them to offer high-complexity services at just one facility—thereby eliminating the need for duplicate managers, supplies and specialists.



Scot Latimer
Director Strategy

“The autonomy and independence of the past has been supplanted by a desire to become part of a larger whole—securing better access to services for both patient and physician.”

Added Richard Taylor, Managing Director of Healthcare Solutions, “Less financially secure hospital systems will pay the price for lowered reimbursement rates due to healthcare reform. In order to survive and stay profitable, they will be required to seek scale, operating efficiency and standardization of care.”

Ambulatory facilities will serve greater demands

An influx of patients seeking access to care will force healthcare systems to re-evaluate where care is offered. Said Shawn Janus, Managing Director of the firm’s Development Advisory practice, “No matter their position on healthcare reform, most healthcare experts agree there needs to be a greater focus on providing coordinated care before a patient becomes acute and needs a hospital”.

Increasingly, providers are seeking ways to optimize their real estate portfolios and expressing far greater interest in ‘location intelligence’. Finding the right location for the right asset—one that supports both the patient’s needs and the facilities business strategy—has become more important than ever before.”

Cost containment strategies are on the rise

The U.S. currently spends more than \$2.5 trillion annually on healthcare and this amount could increase to \$4 trillion if nothing is done to control these escalating costs. Hospitals that are most cost-effective will be rewarded under healthcare reform. Those systems that enact changes to curtail their existing costs by eliminating inefficiencies will be the front-runners in the race to provide streamlined, quality healthcare.



Bill Conkling
Director Capital Markets

“We’re looking at everything from purchased services to labor models with an emphasis on energy, repairs and maintenance and enhanced service delivery. No line item is too small for scrutiny when it comes to cost containment efforts,”

Dramatic changes looming in accounting practices

Proposed changes to the principles of lease accounting will dramatically impact the healthcare real estate industry. The requirement to include all operating leases as balance sheet liabilities diminishes perceived credit worthiness, may infringe on covenant compliance and strain capital resources. Certainly, the changes will push providers to articulate and validate the reasons for leasing such as flexibility in occupancy and preservation of capital for core activities such as maintenance of existing infrastructure.

Healthcare systems will develop new facilities differently than they have in the past to respond adequately to future reform. The focus is on developing facilities that are operationally efficient and are designed with future flexibility. When the time comes to put shovel to ground—and it will come sooner than many expect—Jones Lang LaSalle has the ability to help those administrators reduce fixed costs and streamline project delivery while addressing Federal accounting standards.” The value of access to real estate capital to support the growth of hospital systems will serve as an important reminder as organizations navigate through the undoubtedly challenging time ahead with new lease accounting.



Real value in a changing world



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