

For-Profit Senior Living: Its Impact on the Not-for-Profit Sector

Steve Coma, Managing Director

As head of the Housing Group at BB&T Capital Markets, Steve focuses on providing tailored structures to housing projects of all types, including affordable, senior and student housing projects. He has more than 29 years of experience in capital markets and derivatives as an investment banker, trader and advisor.



As many of our clients consider their competitive position within their markets, especially “rental models,” we hear a common theme regarding the impact of private, for-profit developers. Anecdotal evidence suggests an increasing number of for-profit developments are encroaching on both the primary market and product mix of our not-for-profit clients.

In fact, the for-profit sector has historically been a significant provider of senior living. Evidence as provided in NIC’s “The State of Senior Housing, 2014” is that for-profit entities hold:

- Approximately 98% of the stand-alone independent living units
- 97% of the stand-alone assisted living/memory care units
- 37% of the CCRC units

However, there is reason to suggest that for-profit development is accelerating, largely due to the expected returns from the senior living product and availability of capital. As NIC stated in its Investment Guide, “For many investors, the combined components of real estate, hospitality and needs-driven services give seniors housing and care properties a unique resiliency, offering the benefits of real estate investment along with the strength of the healthcare field.” As of the fourth quarter of 2013, senior housing projects generated an annualized return of 14.6%

“For many investors, the combined components of real estate, hospitality and needs-driven services give seniors housing and care properties a unique resiliency, offering the benefits of real estate investment along with the strength of the healthcare field.”

since the fourth quarter of 2003, compared to a return of 8.6% for the entire NCREIF Property Index.

That, combined with available capital, has led to increased construction (while not at peak levels seen in the past, at higher levels than recent years) and may be causing certain markets to have some fee pressure. In addition, economies of scale have led for-profit entities to develop communities simultaneously throughout the nation, thereby diversifying certain costs, such as architecture fees, while reaping the rewards of various revenue streams of each development.

The For-Profit Developer and the Rental Model

The affordable multifamily housing sector has been dominated by for-profit development, largely due to federally subsidized programs that provide ready access for private development. Low Income Housing Tax Credits (for both the 9% program and the 4% program) provide sufficient equity to fund the projects designed for low- and moderate-income families. HUD programs, and programs from FNMA and Freddie Mac, either as stand-alone financings or in combination with conventional bank financing, have historically composed much of the market. As such, for-profit developers are very skilled at obtaining either conventional debt or accessing the capital markets, using products similar to those used by not-for-profit entities.

For-profit developers typically think beyond regional boundaries, but tend to focus on a single product type (see the contrast between IL ownership and CCRC ownership). Additionally, they may also have a different investment horizon, depending on the type of capital deployed. They often are aiming at assembling a portfolio of similar properties, where they can apply the principles of scale to their operations. Entering into large contracts for food services, etc., may reduce overall operating costs and provide a more robust bottom line. However, typically the differentiating factor in efficiency is labor. For-profits are driven to make the labor costs absolutely as efficient as possible, where not-for-profits may have mission-driven reasons for various positions or functions within their staff.

Therefore, as our not-for-profit clients evaluate the competition, it is useful to think more broadly about the differentiating factors including size, the full continuum of care, and branding that set the not-for-profit apart from the for-profit model, and whether they can utilize certain aspects of the for-profit model in their own strategic planning.

Strategies for Not-for-Profit

Campus perspective versus stand alone: A primary difference between the typical for-profit development and the not-for-profit development is the concept of a campus, or continuum of care provided. The marketing process will be entirely different and take deep-seeded knowledge of the specific market area and demographic preferences.

Brand: Also, not-for-profit entities can benefit greatly from their not-for-profit branding. In an industry which the media scrutinizes immensely, a not-for-profit association can assuage the public's fears, as the mission primarily drives operations instead of a focus on the bottom line. It is important for not-for-profit entities to leverage such branding, especially if that branding involves increased costs. There is no reason those special features of the mission can't be recouped in overall revenues, if that is necessary to maintain the financial health of the institution.

Co-development and/or Acquisition: Using the for-profit's expertise and construction capital to co-develop raises some interesting possibilities,

especially given the for-profit's potential access to efficient capital for construction and its potential desire to sell the asset after stabilization. Post stabilization may be an excellent time for the not-for-profit to provide a takeout solution, since the not-for-profit may be less concerned about real estate value (and loan-to-value ratios), and more concerned about cash flows. While the not-for-profit may be competing with REITS and other conventional funding sources, its different objectives may allow it to make a reasonable winning bid. Prior to providing a take-out proposal, non-profit providers should work with their investment bank and bond counsel to understand financing options as not all financing options are available for acquisition of certain levels of care.

For-profits and not-for-profits operate under different primary incentives, but each can learn from the other's business model and perhaps even merge or affiliate. For-profits can learn from the mission of not-for-profits and enhance their own branding as a quality care provider. Not-for-profits can learn from certain economic efficiencies of for-profits and aim toward strengthening operations and building up cash to be as financially agile as for-profits are in the realms of capital financing and expansion of campuses. Both organizations can learn from various technological tools and structures. An integration of all methods, if done well, will benefit our aging population and fortify the overall quality of care model.

To discuss this information further or if we can assist you in any way, please visit BBTCapitalMarkets.com/Healthcare to access contact information. Any member of our team would be happy to speak with you.



CORPORATE BANKING • INVESTMENT BANKING • RISK MANAGEMENT

BBTCAPITALMARKETS.COM/HEALTHCARE

BB&T Capital Markets is a division of BB&T Securities, LLC, member FINRA/SIPC. BB&T Securities, LLC, is a wholly owned nonbank subsidiary of BB&T Corporation. Securities or insurance products and annuities sold, offered or recommended are not a deposit, not FDIC insured, not guaranteed by a bank, not guaranteed by any federal government agency and may go down in value.

© 2016, Branch Banking and Trust Company. All rights reserved.

Connect with us on [LinkedIn](#)