

# WEEKLY REPORT COVID-19

## HEALTHCARE REAL ESTATE : FACING THE PANDEMIC... AND THE WORLD AFTER

BY DANIEL WHILE  
HEAD OF RESEARCH & STRATEGY



*The world is experiencing an unprecedented crisis. Information is evolving continually, and we therefore deemed it useful to provide a weekly update on our view of events and of their impact on the real estate markets. Such is the purpose of this report which we will send you each Friday. It is a non-binding document and exclusively reflects Primonial REIM's market sentiment based on the information available at the time of writing. You can find all the reports written by Primonial REIM's Research & Strategy department at <https://www.primonialreim.com/etudes> and all our reports on the subject of Covid-19 at <https://www.primonialreim.com/covid-19-coronavirus>.*

Week of 30 March to 3 April 2020.

### **Economic environment: the latest information**

- The world is entering, almost simultaneously, the weeks that will be decisive in reversing the expansion of the pandemic and limiting the overwhelming impact on health systems. Spain has become the second most affected country - after Italy - in terms of the number of deaths. On 31 March the US President, like the British Prime Minister, came over to scientific consensus advocating a lockdown for several weeks. In India, the largest lockdown in the world (1.3 billion people) has been implemented. There is now unanimity both on the seriousness of the crisis but also on a «whatever it takes» approach as a monetary and budgetary response.
- INSEE has published an initial assessment of the economic impact in France, along with the necessary precautions. It shows that economic activity and consumption will be at 65% of their normal level. One month of lockdown would result in a contraction of 12 points of quarterly GDP, i.e. 3 points of annual GDP.
- In the shadow of the global pandemic, the «oil war» continues, with the end of the alliance between

Russia and OPEC. Russia's decision to ignore OPEC's production restrictions triggered a barrel price war, which reached a low of close to \$20.

### **Healthcare real estate, a status report**

Healthcare real estate covers several real estate formats, which fulfil different functions. A distinction is made between:

- the health sector, i.e. clinics. They are structured between short stay facilities (medical, surgical and obstetric clinics) and medium stay facilities (follow-up care and rehabilitation, as well as psychiatric facilities);
- the long-stay medico-social sector, whose formats vary in line with the degree of occupant dependence, from the heaviest (nursing homes) to the lightest (senior residences).

In terms of operators, the health sector is characterised by a strong predominance of public and non-profit players, which account for between 60% and 90% of existing beds. The private players include a few groups with European scope: Korian, Orpea and DomusVi.

The private sector has seen growth in institutional investment since 2015, through the outsourcing of facilities by operators and the sale of portfolios held by real estate companies (Gecimed, Foncière des Murs). There is also a strong trend towards the construction of new facilities through operator/investor partnerships. The volume of investment (senior residences and nursing homes) varies in France between €0.5 billion and €1.5 billion (€0.6 billion in 2019), and in Europe between €5 billion and €10 billion (€7.3 billion in 2019, +20% year-on-year). This sector therefore remains «alternative», compared with the volumes we see for commonplace asset classes such as office space (€130 billion invested in 2019).

<sup>1</sup>Source: DREES, 2017, *Les dépenses de santé depuis 1950*.

The consequence of this rise of institutional investors, driven by the search for rental income secured by long leases that are not very vulnerable to economic cycles, has been a compression of yields on acquisitions. In France, the highest quality nursing homes are purchased at a rate of 4% or less and clinics are purchased at a rate of around 5.15%.

It should be noted that the premium offered by healthcare real estate over offices in 2019 is the same as in 2010 (230 basis points for clinics, 170 basis points for nursing homes), which confirms the rational valuation of the sector despite its growth.

	Return 2010	Return 2019	Premium versus Offices in 2010	Premium versus Offices in 2019
<b>Offices</b>	450	280		
<b>Clinics</b>	675	515	225	235
<b>Nursing homes</b>	600	400	150	120

Returns expressed in basis points for prime assets.  
Sources for figures: DTZ, BNP PRE, Primonial REIM

### **What resilience for healthcare real estate investors ?**

From the point of view of the fundamentals that motivate investment in healthcare real estate, we should consider that they remain relevant today:

- The shortage of bed supply in the face of Europe's ageing populations, not only for the health sector but also for the medico-social sector and accommodation for senior citizens, which is a factor that supports investment, and therefore indirectly values.
- The level of performance, which maintains a justified premium over office assets.
- The ability of operators to sign long leases (typically around 9 to 12 years in France, but often more than 20 years in Germany or Italy), which enable a continuous flow of rental income.

On the other hand, the focus should now more than ever be on contractualisation with private operators on a national and European scale: this conditions the ability to adapt uses to new technologies and new medical protocols; to build a fruitful relationship with public players; to attract healthcare personnel in a context of shortage; to bring financial security to a group in addition to profitability at the operating level.

### **What can we expect after the current health crisis ?**

In the short term, it is a question of the players managing the emergency: the shortage of beds equipped with respirators, the saturation of telephone emergency lines, the exhaustion of healthcare workers who are also, in part, infected. Clinics

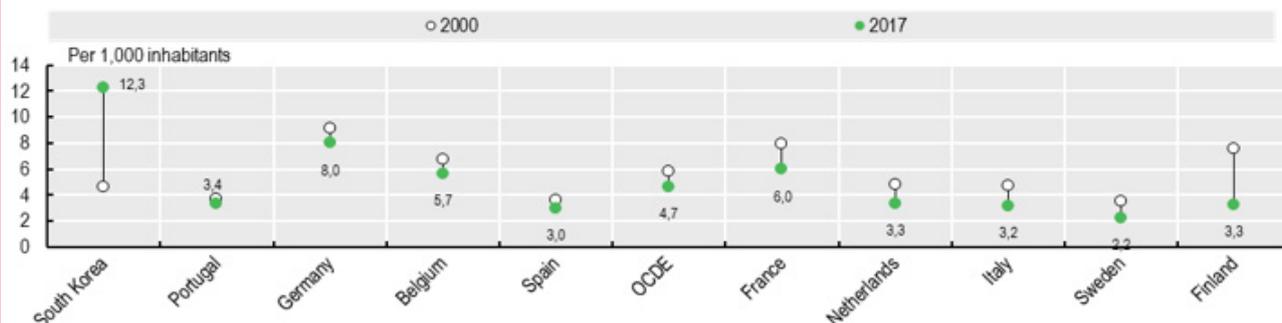
have already been mobilised to provide emergency medical treatment, in order to relieve hospital capacities, in the place of more remunerative services relating to patient comfort. This effort made in solidarity should not jeopardize their economic viability or their ability to honour their rental commitments, particularly in the light of government statements concerning the economic support that the State wishes to provide to them via the Health Insurance scheme and via an «investment and career development plan» announced by President Macron. In Germany, a €3 billion support plan has been approved by Parliament.

**We believe that healthcare real estate, due to the particular nature of the Covid-19 shock, will be at the heart of «post-crisis» issues.** The health drama has in fact been an opportunity for populations and decision-makers to become aware of the weaknesses of health systems, whether Italian, French or American. It could lead, if not to a reassessment of the health policies implemented so far, at least to questions being raised about them.

The share of health expenditure in GDP has increased (in France, consumption of health care and medical goods has increased 3.5-fold since 1950, reaching 8.9% of GDP in 2015<sup>1)</sup>, due to the increase in the proportion of elderly people and the cost of the most sophisticated medical equipment. This goes hand in hand with an increase in life expectancy.

However, if we look at the resources allocated to health care, we observe different developments from one country to another in terms of the infrastructure dedicated to care and in particular the number of beds.

### NUMBER OF HOSPITAL BEDS PER 1,000 INHABITANTS, 2000 AND 2017



Source : OECD Health Statistics 2019

Since 2000, the number of beds per 1,000 inhabitants has generally decreased in OECD countries, with the notable exception of South Korea, whose Covid-19 management has been recognised as the most efficient. For France, the ratio was 8/1000 in 2000, declining to 6/1000 in 2017.

Of course, a country's health system cannot be reduced to the number of hospital beds: investment in prevention, access to consultations, the number of doctors and nurses, the level of technological equipment (especially MRIs), etc. are other key variables. The reduction in the number of long-stay hospital beds is the result of reforms that give priority to the search for better organisation of care and better accountability of players, not forgetting the progress in medical technology which, with the trend towards ambulatory care, makes it possible to shift the burden to follow-up care and local services.

**After the Covid-19 crisis: from a logic of efficiency to a logic of effectiveness?** The health policies put in place were justified by the observation of a hypertrophy of health facilities, in view of the modernisation of technologies, and despite the increase in demand due to the ageing of the population. They were based on efficiency (achieving the objective while minimising costs) rather than effectiveness (achieving a maximum objective, irrespective of the cost). However, the pandemic has revealed the extreme economic cost mobilised to cope with a shortage of beds or even to have a choice in its strategy for managing the health crisis, which far exceeds the cost of the beds if they had been kept in excess. This is what the CEO of the Finnish pension fund Varma<sup>2</sup>, was referring to when he suggested the introduction of healthcare risk buffers, similar to the prudential solvency ratios applied to financial institutions after the 2008 crisis. The way in which Germany - which has a higher ratio of

beds per inhabitant than other major European country - will weather the crisis will be an interesting indicator in this respect. The example of some Asian countries (e.g. South Korea) also makes this case. There is no doubt that this will be the issue political leaders are faced with<sup>3</sup>.

This logic of efficiency over time is ultimately the same as that underlying the energy transition: a major investment today to limit a colossal cost tomorrow, carried forward and passed down to future generations.

### **Conclusion: is health care real estate at the heart of future investments in «social infrastructure»?**

One of the lessons of the crisis is the need to «over-invest» in the healthcare sector, a message that Primonia REIM sent out in 2012 with the creation of the Primovie Fund.

This will require the involvement of both private and public players. It has often been pointed out that it is difficult for public hospitals and private clinics to cooperate during a patient's care process. Their dual mobilisation in the fight against the pandemic could be the starting point for a new vision of a country's overall healthcare mix.

The factors supporting the healthcare real estate market are structural and will continue to be so: demand for healthcare due to the ageing population, financial viability of the major pan-European operators, attractive risk/return profile thanks to the signing of long leases, low correlation between the turnover of facilities and economic cycles. On the front line in the face of the pandemic, healthcare infrastructure will be at the heart of the post-pandemic world.

<sup>2</sup> Source: <https://www.ipe.com/news/varma-covid-19-crisis-lesson-is-healthcare-needs-risk-buffers/10044576.article?adredir=1&adredir=1>

<sup>3</sup> See. E. Macron, in his televised speech of 13 March: «What this pandemic reveals is that there are goods and services that must be placed outside the laws of the market.»

**PRIMONIAL REIM AND HEALTH REAL ESTATE**

**Primonial REIM is the European leader in healthcare real estate with:**

- More than 6 bn € of assets under management
- 340 facilities
- 2,151,986 sqm managed

Figures as at 31 December 2019

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**Next meeting**

You will soon be able to listen to our upcoming podcast, in the meantime please send your questions to : [communicationpreim@primonial.fr](mailto:communicationpreim@primonial.fr)



Primonial Real Estate Investment Management (PREIM) is a portfolio management company authorised by the Autorité des Marchés Financiers (AMF - French Financial Markets Authority) on 16 December 2011.

It received AIFM authorisation on 10 June 2014. Its business consists of creating, structuring and managing long-term real estate investments for individual and institutional investors.

Primonial REIM has a comprehensive range of expertise:

- multi-product: SCPI, OPCI and SCI funds,
- multi-sector: offices, retail outlets, residential assets, hotels, and healthcare and education facility real estate,
- multi-national: France, Germany, Spain, Italy, Belgium, Ireland, Netherlands.

At 31 December 2019, Primonial REIM had:

- More than €21 billion of assets under management,
- 67,841 associates,
- 46 independent real estate advisors,
- Assets worth 4,251,623 sq. m. and 7,000 tenants, including a large share of major corporate tenants (e.g. Samsung, Korian, Crédit Agricole and SNCF).

[www.primonialreim.com](http://www.primonialreim.com)

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#### HEADQUARTER OFFICE

36 rue de Naples - 75008 Paris

[www.primonialreim.com](http://www.primonialreim.com)

## CONTACT

### DÉPARTEMENT RECHERCHE & STRATÉGIE RESEARCH & STRATEGY DEPARTMENT

Daniel While • Head of Research & Strategy • [daniel.white@primonial.fr](mailto:daniel.white@primonial.fr)  
Henry-Aurélien Natter • Head of Research • [henry-aurelien.natter@primonial.fr](mailto:henry-aurelien.natter@primonial.fr)

The Research & Strategy Department's role is to formalise Primonial REIM's real estate investment strategies, based on continuous monitoring of the French and European markets. Although collective real estate accounts for a growing share of institutional portfolios and household savings, it is at the crossroads of financial (hierarchy of rates), economic (tenants' business models), demographic (the metropolisation phenomenon) and societal (changes in usage) factors. This is why a cross-cutting analysis is needed, which is also long term and therefore in keeping with the horizon of most real estate investors.

