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Square Feet

Hot Niche in the Rental Market: Housing for the Elderly

By [TERRY PRISTIN](#)

AFTER terrorists destroyed the World Trade Center, the owners of a nearby luxury retirement and assisted-living home wondered if their new project was also doomed. Would elderly people want to live just four blocks from Ground Zero?

Four years later, the 14-story building, known as the Hallmark of Battery Park City, is fully rented and there is a waiting list with 40 names.

In Palo Alto, Calif., a new \$370 million Classic Residence by Hyatt next to Stanford University charges entry fees ranging from \$586,500 to \$4.3 million. Monthly charges range from \$3,105 to \$7,430. The development opened in June and is already 88 percent full.

Only a few years ago, the commercial real estate sector known as senior housing was in trouble. Inexperienced (and sometimes unscrupulous) developers had overestimated the demand for assisted living and underestimated how long it would take to fill their units. With a strong economy and readily available capital, many companies went public, but by the late 1990's, their stocks had tumbled. Bankruptcies mounted, and many operators went out of business.

These days, however, the sector is in much better shape. "Without a doubt, the industry is quite healthy now," said David S. Schless, president of the American Seniors Housing Association, a trade group. "One of the things we're seeing is a growing acceptance on the part of institutional investors and others that typically have not been willing to invest in senior housing."

Unlike age-restricted housing developments for active people in their mid-50's or older, senior housing is aimed at a more frail population, usually people in their 80's.

Residents have their own apartments (with kitchens), but their monthly fees include two meals or more as well as many social activities. Medical care is generally an added expense. Many homes also include units for people who need help with daily activities and for Alzheimer's patients, and some — like the Palo Alto development — also offer nursing care.

Development has slowed considerably since the 1990's. Last year, the top operators built 23,000 units, compared with 62,000 in 1999, said Robert G. Kramer, president of the National Investment Center for the Seniors Housing and Care Industries, a research organization in Annapolis, Md.

The number of public companies operating senior housing with services has shrunk from 18 to 6, and share prices have soared. "The industry is absolutely in a rebound in terms of the stock performance,"

said Jerry L. Doctrow, a managing director at Stifel, Nicolaus & Company, a brokerage and investment banking firm.

Shares of Brookdale Senior Living, the rapidly expanding Chicago company that owns the Hallmark in Lower [Manhattan](#), have risen from \$19 at the company's public offering in November to \$31.93 at yesterday's close.

In recent years, senior housing operators have been experimenting with different models. Sunrise Senior Living, for example, which used to specialize in assisted living, now offers a variety of housing types and services, including home health care. The company is also building condominium developments in Bethesda, Md., and Dallas, which will have the type of common areas and treatment rooms usually found only in rental buildings.

"Anybody who thinks that one size fits all is somebody who's going to fail," Mr. Kramer said "The customer is looking for choice."

For investors, senior housing is often seen as an appealing alternative to traditional apartment buildings because the initial returns, or capitalization rates, are higher — an average of 9 percent, compared with 5 percent or less for conventional apartments.

Competition among investors for quality retirement homes has been increasing, however, and those properties are selling faster than they used to, said Mel Gamzon, president of Senior Housing Investment Advisors, a brokerage company in Fort Lauderdale, Fla. Some high-end homes are trading for as much as \$225,000 a unit, according to the trade group, and capitalization rates for some properties have fallen to 7 percent or less.

"There's absolutely no question that dollar for dollar you get a much better return," said Gary R. Lucas, managing director for senior housing in the San Francisco office of Marcus & Millichap, an investment firm. "But there is also a higher risk. It's not just real estate. It's not just a business. You're taking care of humans."

One reason these properties are risky is that ever-rising labor costs make up a high percentage of an operator's expenses. According to industry figures, operators offset these increases by raising monthly fees by 4 percent to 6 percent a year.

In an October 2005 report, based on telephone calls to 873 assisted-living homes in 87 major markets throughout the country, the MetLife Mature Market Institute, a research arm of the insurance company, found that monthly rates had increased by 15.1 percent from 2004 to 2005 — a figure that other senior housing specialists said was wildly off base. (When different levels of care were quoted, researchers used an average figure, which might have accounted for some of the discrepancy, said Sandra Timmermann, director of the institute.)

Operators need to know their market and avoid, say, installing chandeliers in places where they might not be welcome, said Noah R. Levy of Prudential Real Estate Investors, who manages senior housing funds. "If you give me a not-so-fancy building but you've got a great operator, it can be a spectacular investment," he said. "But give me a perfect building with a not-so-great operator, and I could lose a lot of money."

Mr. Levy said he has only recently begun investing in large-scale developments that offer a range of care within the same building or campus and require a sizable entry fee, which is usually partly or

mostly refundable when the resident moves or dies.

In the past, pension fund investors have tended to shy away from these so-called continuing care retirement communities because it was hard to pin a value on the real estate. About three-quarters of them are owned by nonprofit groups. Among them is the Amsterdam at Harborside in Port Washington, N.Y., which is being developed by Greystone Communities, now owned by Sunrise. Entrance fees will range from \$399,000 to \$1.9 million, and monthly charges will be \$2,600 to \$6,000.

The upscale version of this model is more profitable than other types of senior housing, but building such projects often requires years of planning. In New York, a state with only eight such developments, 70 percent of all the units have to be sold before developers can break ground, which means that potential residents have to be willing to wait.

"Some of my residents have told me, 'We don't even buy green bananas,' " said Randal J. Richardson, the president of Classic Residence by Hyatt, a subsidiary of the hotel company. "They say, 'We want to move in today.' " Hyatt hopes to get final approval soon on a long-delayed project in Briarcliff Manor in Westchester County that will be similar to the new development in Palo Alto.

While many companies are growing through acquisition, Sunrise has 50 projects under development, said Paul J. Klaassen, chief executive of Sunrise. Only a handful are condominiums, including the two projects in Bethesda and Dallas, where units will probably be priced from around \$500,000 to \$2 million, with monthly fees about twice what an ordinary condo would command. Two floors with rental units will be set aside for people who need more care.

Response has been good, Mr. Klaassen said, but it is too early to tell if the ownership model will catch on. "We don't know if it's going to be the next S.U.V. or minivan — or if it's just going to be a niche player," he said.