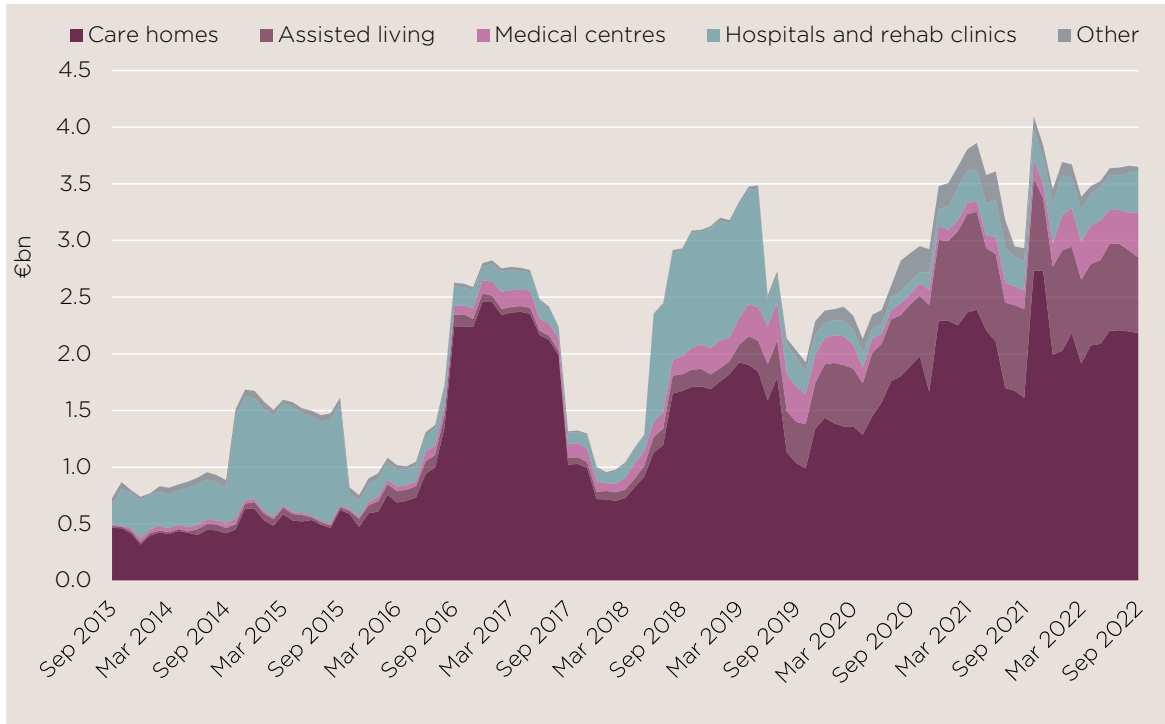


Healthcare Properties Germany



Graph 1: Transaction volume Germany (past 12 months rolling)



Source Savills

Investors are becoming more cautious

In the first three quarters of 2022, healthcare properties were traded in Germany for approx. €1.8bn (Graph 1). This means that the transaction volume was around 12% higher than the result for the same period in the previous year. However, the third quarter was noticeably weak in terms of turnover, with a transaction volume of €339m. By comparison, the quarterly average of the last five years was more than twice as high at €725m.

Demand for healthcare properties remains high among investors, as the demand for such properties will grow strongly in the occupier markets in the long term. At the same time, supply cannot keep pace with the massive growth in demand due to staff shortages among operators and challenges in project development. The value of healthcare properties is therefore likely to remain high in the long term. However, this positive long-term outlook is countered by current economic difficulties at more and more operators. In addition, many existing properties on offer do not meet the quality requirements of investors, so that attractive purchase opportunities are scarce. On top of that, the purchase price expectations of buyers and sellers are currently often significantly different. All these factors have made it more difficult to find suitable properties and successfully conclude transactions.

Fewer investment transactions, rising initial yields beyond Core

The number of transactions in the investment market for

healthcare properties has declined noticeably since the spring of this year. Fewer than 20 transactions were recorded in the third quarter (Graph 2), the lowest number since the fourth quarter of 2017.

In our opinion, the reasons for the currently subdued transaction activity are the initiated interest rate turnaround and challenges on the operator side. While the interest rate turnaround means that sellers' and bidders' purchase price expectations often do not match, economic difficulties on the part of operators are thinning out the product supply for risk-averse investors. The process of price discovery has not yet been completed and is likely to continue for some time. In the case of core care homes, there are still some purchase price bids at the level of the beginning of this year, so that the prime yield still remains at 3.9%. In the long term, however, a price adjustment can be expected in the top segment as well. For properties with average building and operator quality, we have observed a decline of 1.5 to 2.5 purchase price multipliers so far. Overall, the range of bids is noticeably wider than at the beginning of the year. This is due to the fact that many investors are currently only acting very selectively and risk aversion has increased.

Stronger demand for assisted living and medical centres

In the course of the year to date, care homes have been by far the turnover-strongest property type on the investment market for healthcare properties, with a transaction volume

Focus on selected figures



+57%

In the first three quarters of the current year, medical centres were traded for €315m. That is 57% more than in the entire year 2021.



4%

Listed property companies and REITs were responsible for only 4% of the purchasing volume in Q1-Q3 2022. The five-year average was 36%. Private equity funds, on the other hand, increased their market share.



€22.5m

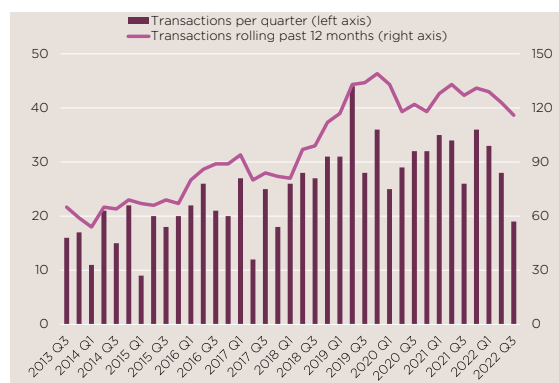
The average transaction size in the year to date was €22.5m. In 2020 and 2021, the figures were €29.5m and €26.4m, respectively.

of €864m or a volume share of 48%. Assisted living properties followed in second place with a volume of €389m and a share of 22%. Third place was taken by medical centres with a volume of €315m euros and a share of around 18%. This means that the share of care homes has fallen. By comparison, care homes accounted for around 60% of the volume on average over the last five years.

In the meantime, many investors are turning more towards other healthcare properties. One reason for this is likely to be challenges on the operator side of care homes. Care home operators are currently under increasing economic pressure. High inflation and, in particular, rising ancillary costs are being compounded by significantly rising personnel costs due to the recently agreed collective wage agreement. In addition, many lease contracts include an indexation clause. In contrast, the operators can only increase their income to a very limited extent. In view of the cost pressure on the operators, some landlords are currently prepared to renegotiate lease agreements. In some cases, for example, a waiver of indexation was offered in exchange for a simultaneous extension of the lease. However, such measures have to be examined and weighed up individually. Declining credit ratings among operators are leading to greater restraint among real estate investors overall. In Lower Saxony and Hesse, there are also unanswered questions about the introduction of new care home legislations, which is why investors often price in higher risks when examining existing properties in these federal states.

In contrast, operators of assisted living properties can more easily pass on increased costs to residents. In the case of medical centres, there is usually a larger number of predominantly very solvent tenants, which minimises the risk of rent default. These factors, among others, explain the increasing interest of investors. In the case of medical centres, we are observing increasing interest from both healthcare property investors and typical office buyers. On the one hand, the properties are very similar to classic office buildings; on the other hand, doctors are very loyal tenants and very often sign long-term leases. Exactly such risk profiles are in demand.

Graph 2: Number of transactions



Source Savills

Noticeable decline in forward deals

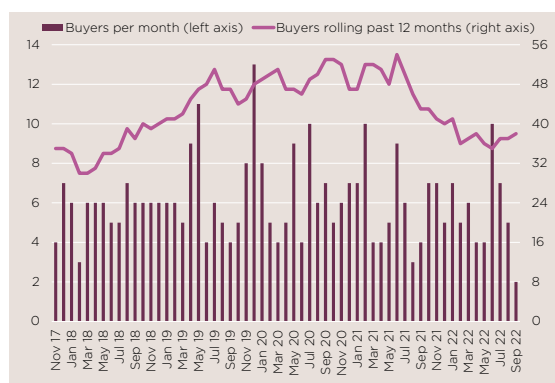
In addition to care home operators, many project developers are also likely to be under increasing pressure. Rising construction and financing costs, cancelled KfW subsidies and stagnating or probably soon falling purchase price multipliers are leading to a challenging situation. In the third quarter, such transactions accounted for only about 5% of the transaction volume. In the two previous quarters, it was still around one third in each case. In our view, investors are generally still prepared to make forward deals if the general conditions regarding location and tenant quality are right, because the purchase of properties under planning or under construction is one of the few possibilities to obtain modern and high-quality properties. Many of the existing properties offered for sale, on the other hand, have deficits in terms of property quality. In the meantime, however, higher risks are being priced into forward deals, so that the purchase price expectations of many developers are not being met. As a result, fewer forward sales are currently taking place.

Outlook: Supply remains scarce and more property types are coming into focus

For the coming quarters we expect that the purchase price expectations of buyers and sellers will gradually converge, so that more transactions will be notarised again. Larger portfolio sales on the horizon should also lead to a boost in the transaction volume. However, the long-term growth prospects of the sector will be countered by the risks among care home operators, which means that supply will remain scarce for many risk-averse buyers. In this context, we expect that property types such as rehabilitation clinics will also come more into the focus of investors. As the megatrend of demographic change continues to speak very strongly in favour of investments in healthcare properties, the sector can be expected to continue to gain in importance on the German real estate investment market.

[Download the charts and raw data here](#) ↓

Graph 3: Number of active buyers



Source Savills

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