Healthcare Germany - June 2022

SPOTLIGHT
Savills Research

The Market for Care Properties

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How big the market is ● How liquid the market is ● Which topics become important

> **"In Germany, significantly more care homes as well as senior-friendly and assisted living apartments will be needed in the future."**

Care properties - a growing niche

Text: Matti Schenk

The market for care properties is characterised by a structurally growing demand: According to a forecast by the Scientific Institute of the AOK, the number of people in need of care will increase from currently about 3.5 million to about 4.4 million in 2040. The number of households with senior citizens will also increase from the current 12 million to 15.6 million. According to an analysis by ARGE, only eight percent of this group already live in housing suitable for the elderly. In Germany, therefore, significantly more care homes as well as senior-friendly and assisted living apartments will be needed in the future.

The structural growth of the sector is increasingly attracting real estate investors. However, the investment market for care properties is a niche segment and still relatively intransparent. In our Spotlight, we would therefore like to provide an overview of the investment universe of the German market for care properties and create transparency. To this end, we have estimated the market volume and analysed it in more detail. We also shed light on the liquidity of the market and its recent developments. Finally, we present developments that we consider important for current and future investment decisions.

Care properties - a clarification of terms

The world of care properties is characterised by a multitude of terms. For example, care homes, retirement homes, senior residences, residential homes, assisted living or even serviced living are advertised. Some of the terms are used synonymously and are not clearly distinguished from each other.

Two property types of care properties can be distinguished in Germany:

1. properties that mainly serve the inpatient care of people in need of care. In our spotlight, we call this type of property a care home.

2. properties in which residents largely run their own households independently and can access care and support services as needed. We refer to these properties as assisted living facilities.

In practice, care homes and assisted living facilities are increasingly combined or built on neighbouring properties. This has the advantage that residents of assisted living facilities only have to move within the building ensemble in the event of a greater need for care and can thus remain in their familiar surroundings. Many care homes therefore also have units for assisted living and vice versa.

The topics of our spotlight:

The volume of the market
The size of the investment universe

The liquidity of the market
Number and volume of transactions, active buyers

Opportunities and challenges
Which topics become important

64% of the market volume
About 128 billion euros or 64% of the market volume is accounted for by care homes and 73 billion euros or 36% by residential facilities for assisted living facilities.

The volume of the market

Investors interested in care properties in Germany are sometimes confronted with fuzzy terminology. The info box on page 2 shows how Savills defines care properties. Investors are also interested in how large the market is and how much capital can potentially be invested. We will go into this in this chapter.

17,700 care properties in Germany

Based on the data of Pflegemarkt.com and our own review and data enhancement, we have recorded the supply of care properties in Germany: There are currently around 16,300 care properties with about 910,000 full inpatient care beds and about 292,000 assisted living units (Table 1). At the beginning of May 2022, there were also about 1,350 care properties with an estimated 46,500 full inpatient care beds and 34,500 assisted living units under construction or in planning.

Investment universe is around 201 billion euros in size

The capital value of care properties is also interesting for real estate investors. There are no corresponding publicly available statistics or studies. We estimate that the investment universe of care properties currently has a volume of approximately 201 billion euros (for methodology see page 14).

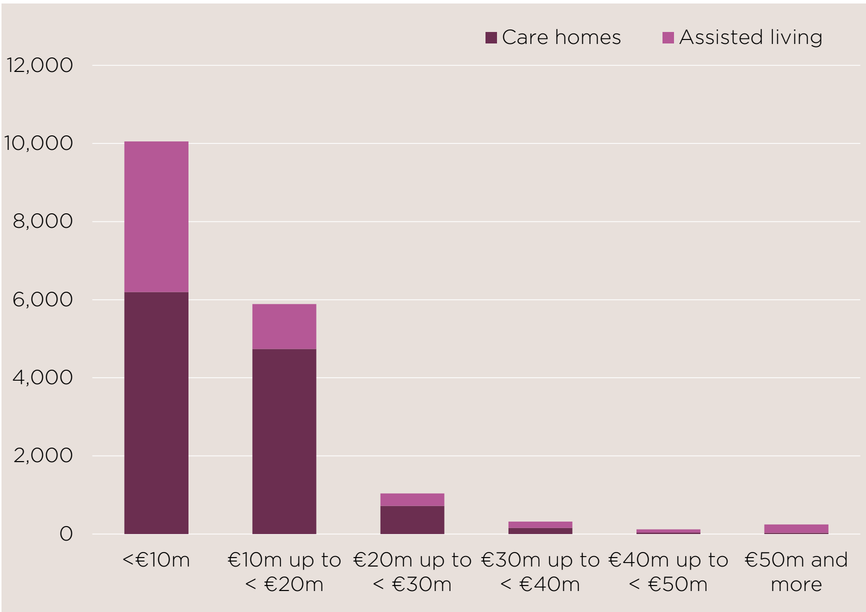
Approximately 128 billion euros or 64 percent of the market volume is accounted for by care homes and 73 billion euros or 36 percent by assisted living facilities. The volume of existing properties amounts to approximately 186 billion euros. A further 15 billion euros are accounted for by properties under construction or in planning.

Table 1: Number of care properties

Status	Type of use	Properties	Fully stationary care beds	Assisted living apartments
Stock	Care homes	11,317	891,186	49,673
	Assisted living property	4,995	18,375	242,212
	Total	16,312	909,561	291,885
Pipeline	Care homes	555	45,831	3,392
	Assisted living property	794	665	31,116
	Total	1,349	46,496	34,508
Total	Care homes	11,872	937,017	53,065
	Assisted living property	5,789	19,040	273,328
	Total	17,661	956,057	326,393

Source Savills based on Pflegemarkt.com

Graph 1: Number of care properties by volume of property*



Source Savills; own estimation based on Pflegemarkt.com / * Stock + Pipeline

Small property volumes dominate

Many care properties have a comparatively small volume (Graph 1): The median is 9.6 million euros. For assisted living facilities, the median is even only 7.1 million euros. Overall, about 57 percent of the care properties have a volume of less than 10 million euros. Another 33 percent are worth between 10 and 20 million euros, according to our estimate. Properties in the mid and

Non-profit operators dominate
About 56% of the existing care properties have a non-profit operator. Another 4% are operated by a municipal company.

higher double-digit million range are thus the exception. The large-volume properties are disproportionately often located in urban districts, while smaller properties are particularly common in rural districts.

71 percent of the market volume are properties in the double-digit million range

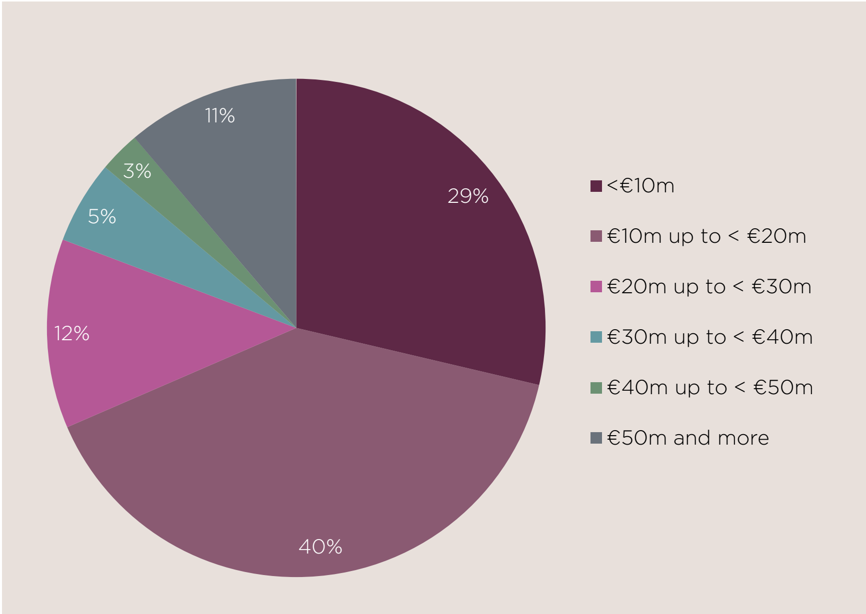
Even though large-volume properties are rare, they account for a larger share of the market volume. Based on a market volume of 201 billion euros, properties with a volume of less than 10 million euros account for around 29 percent. Approximately 11 percent of the market volume is accounted for by properties with a volume of at least 50 million euros (Graph 2).

Growth regions account for the largest volume

There are care properties in all districts and cities in Germany. The size of the stock correlates strongly with the size of the population. In terms of the investment universe, the volume is concentrated in regions with growing populations. According to our estimate, about three quarters of the market volume is accounted for by growing districts or districts with above-average growth (Graph 3).

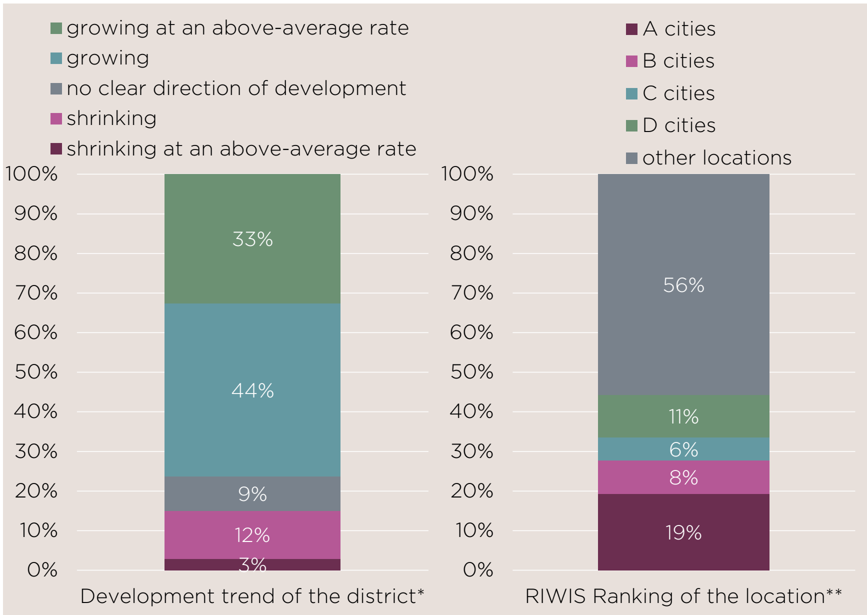
Around 112 billion euros or 56 percent of the market volume is in locations outside the so called 127 RIWIS cities and thus in smaller and predominantly non-transparent real estate markets. In the case of properties under construction or in the planning stage, such locations even account for about 70 percent of the volume. Some of these are municipalities in the suburbs of large cities. In many large cities themselves, on the other hand, new care properties can only be developed with difficulty due to scarce and expensive land.

Graph 2: Market volume by size of properties*



Source Savills; own estimation based on Pflegemarkt.com / * Stock + Pipeline

Graph 3: Market volume by type of location



Source Savills; own estimation based on Pflegemarkt.com; each stock + pipeline / * according to BBSR; ** according to Bulwiengesa

Our conclusion

With an estimated market volume of around 201 billion euros, care properties are a niche in the German real estate market. By way of comparison, according to the Federal Statistical Office, the value of all commercial and residential real estate is estimated at around 15 trillion euros. Accordingly, care properties account for only about one percent of the investment universe in the German real estate market. Nevertheless, the market for care properties offers diverse potential for investors and thus the opportunity to further institutionalise the investment market. However, interested investors have to deal with predominantly small property volumes and a large number of small and often intransparent locations. Low property volumes are unattractive for some investors in view of the process costs for the purchase or the acquisition audit, so that the bidding competition is particularly intense for the few large-volume individual properties. Due to the low property volumes, care properties are often combined into portfolios and put on the market. Overall, investors who can also handle

Growing districts and staff shortages

Districts that are growing are doing so largely through immigration. Accordingly, there is a greater opportunity there to address the staff shortage in the care sector. This reduces the risk with regard to the long-term stability of rental income.

small lot sizes therefore have advantages when looking for products on the market for care properties.

It is positive that the majority of the market volume is located in growing districts. Due to demographic change, the demand for care properties is likely to increase in shrinking regions as well. However, the shortage of nursing staff will become particularly acute there and pose major challenges for operators - a risk with regard to the long-term stability of rental income. Districts that are growing are doing so largely through immigration. Accordingly, there is a greater chance of addressing the staff shortage there.

Table 2 summarises the volumes by property and location characteristics.

Table 2: Market volume by characteristics of properties and locations (in €m)

Characteristics of properties		Characteristics of locations					
		shrinking at an above-average rate	**shrinking**	**no clear direction of development**	**growing**	**growing at an above-average rate**	**Total**
Type of use	Care homes	4,897	19,539	13,175	58,000	32,627	128,238
	Assisted living property	922	4,783	4,298	30,058	32,903	72,963
Status	Stock	5,417	22,320	16,347	81,134	60,828	186,047
	Pipeline	402	2,002	1,125	6,924	4,702	15,154
Property volume	<€10m	3,012	11,623	6,521	25,575	10,987	57,719
	€10m up to < €20m	2,291	10,100	8,067	37,712	21,910	80,081
	€20m up to < €30m	442	2,094	1,806	10,392	9,956	24,690
	€30m up to < €40m	31	365	640	4,878	4,902	10,816
	€40m up to < €50m	43	89	173	2,051	2,997	5,352
		-	52	265	7,450	14,778	22,544
Total		5,819	24,322	17,472	88,058	65,530	201,201

Source Savills

Increasing market activity
Transaction volumes have risen noticeably in recent years due to the significant increase in demand and a progressive institutionalisation of the market.

The liquidity of the market

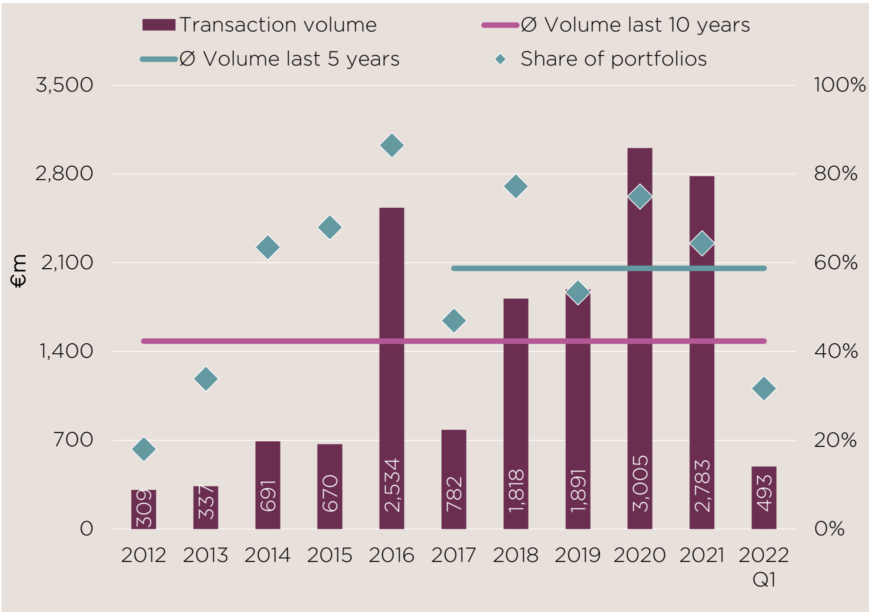
IIn this chapter we will now look at the liquidity of the market for care properties. The total volume of 201 billion euros on the investment market compares with an annual transaction volume of 2.1 billion euros on average over the past five years (Graph 4). Around two-thirds of the transaction volume was realised through the purchase of portfolios. Transaction volumes have risen noticeably in recent years, which is due to the significant increase in demand and a progressive institutionalisation of the market.

Liquidity is slightly below average

Looking at the last five years, between one percent and a maximum of 1.5 percent of the market volume was traded per year. This value is slightly below the level of the entire real estate market for non-residential properties in Germany. Based on the data of the land valuation boards, excluding share deals, around 2.3 percent of the net fixed assets of non-residential real estate were traded in 2020.

However, we assume that there is a significant number of unreported transactions in the care property sector. This is due to the small-scale nature of the market in terms of the operator and ownership structure with often regional or even local players. Even though detailed data on ownership is lacking, we assume a high share of owner-occupied properties. Given the dominance of non-profit and municipal operators, many properties are likely to be in the hands of smaller and medium-sized operators or non-profit organisations. We also assume a higher proportion of private individuals as owners. Another explanation for the limited transparency is that residents, relatives or other local stakeholders sometimes have reservations about selling care properties to real estate investors. Some players therefore do not make their transactions public. Nevertheless, the transactions we record reflect at least the institutional part of the investment market.

Graph 4: Transaction volume of care properties



Source Savills

Recently almost 100 transactions per year

In the past five years we have registered an average of 81 individual and portfolio transactions in care properties per year (Graph 5). By way of comparison, there were a total of around 12,270 commercial and residential property transactions during this period. This means that transactions of care properties represent 3.3 percent of the total transaction activity. Contrary to the trend of the market as a whole, the number of purchases of care properties also increased after 2016 and reached its peak so far in 2019 with 95 transactions. In total, around 870 care properties were traded in the transactions of the last five years. Around 62 percent of the traded care properties changed hands as part of portfolios.

The average transaction size over the last five years was 24.5 million euros, with strong fluctuations - depending on the number of larger portfolio transactions. In 2021, transactions weighed in at an average of 31.6 million euros. Despite stronger fluctuations over the course of the last ten years, we observe a clear growth in average lot sizes on the investment market. This is primarily due to the rising capital values, which are also reflected in the steadily increasing average volume of traded properties. In 2021, the average volume per traded care property was 13.4 million euros.

Number of investors on the rise for years

The rising capital values in recent years also result from an ever-increasing number of active investors and consequently very intensive bidding processes. In each of the years 2019 to 2021, around 36 investors known by name came forward as buyers (Graph 6). During this period, approximately every second investor recorded in the respective year appeared as a buyer of German care properties for the first time. Many of these first-time buyers have only been involved in

> **The investor universe in the market for care properties is likely to be larger than ever before.**

a few transactions. Since many of them want to build up a larger portfolio, we assume that they will remain active on the market in the longer term.

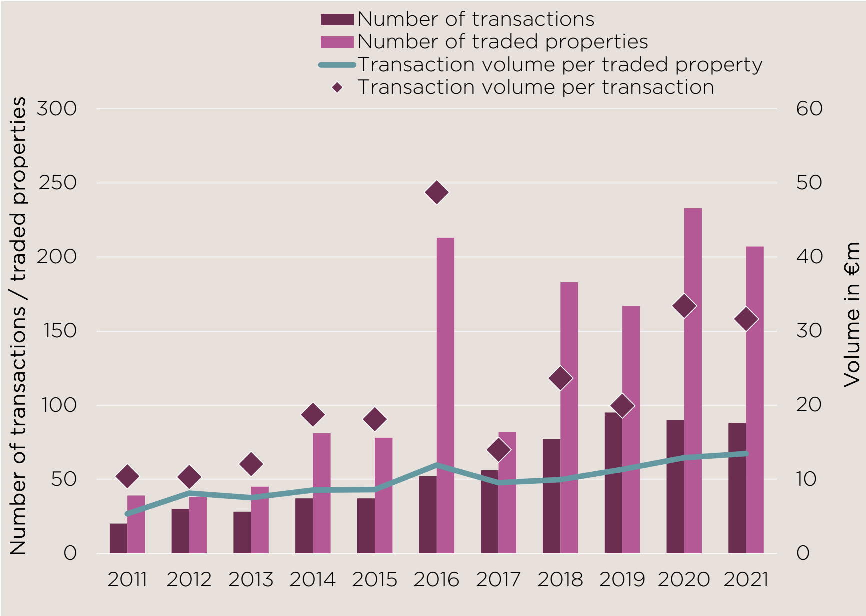
In total, around 80 investors known by name have purchased German care properties within the last three years (Graph 6). Five years ago, this number was 44 percent lower. In addition to the buyers active in the recent past, there are all those investors who have only recently decided to enter the market and have not yet started building up their portfolios. The investor universe in the market for care properties is thus likely to be larger than ever before. Nevertheless, only a few buyers account for a large part of the transaction volume. In the last five years, the top 5 buyers in a given year accounted for between 50 and 70 percent of the total volume. In terms of purchase volume, these are the five largest buyers of the last two years: Vonovia (due to the acquisition of Deutsche Wohnen including its care home portfolio), INP Holding, Swiss Life, Aedifica and Cofinimmo. In total, they were responsible for 47 percent of the transaction volume in the last two years. Despite the increasing number of players, the market thus remains highly concentrated in terms of volume shares.

Our conclusion

Measured in terms of the number of transactions and the transaction volume as well as in terms of the number of active investors, the market for care properties is a niche in the German real estate investment market. Even though liquidity is still below average, the investment market for care properties has experienced a noticeable upswing in recent years. In particular, the transaction volume has developed considerably more dynamically over the course of the last ten years than on the market as a whole (Graph 7). The number of transactions and active buyers have also increased at an above-average rate and recently remained relatively stable, contrary to the trend on the market as a whole.

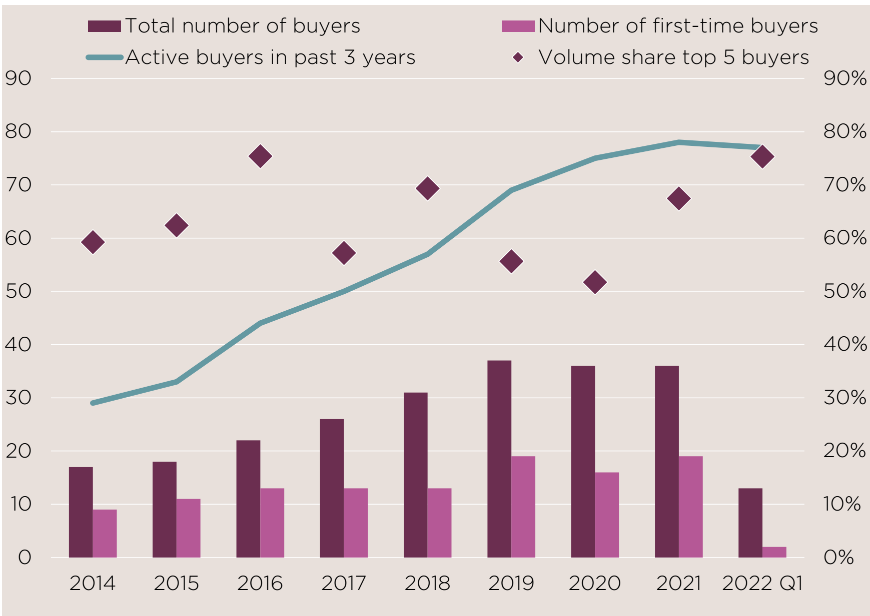
Despite the above-average growth of the market, it is likely to be more difficult for investors to place large sums of capital than for other types of use. In view of the low property volumes, the lot sizes on the investment market are also predominantly low. In conjunction with the significantly

Graph 5: Number and size of transactions



Source Savills

Graph 6: Number of buyers

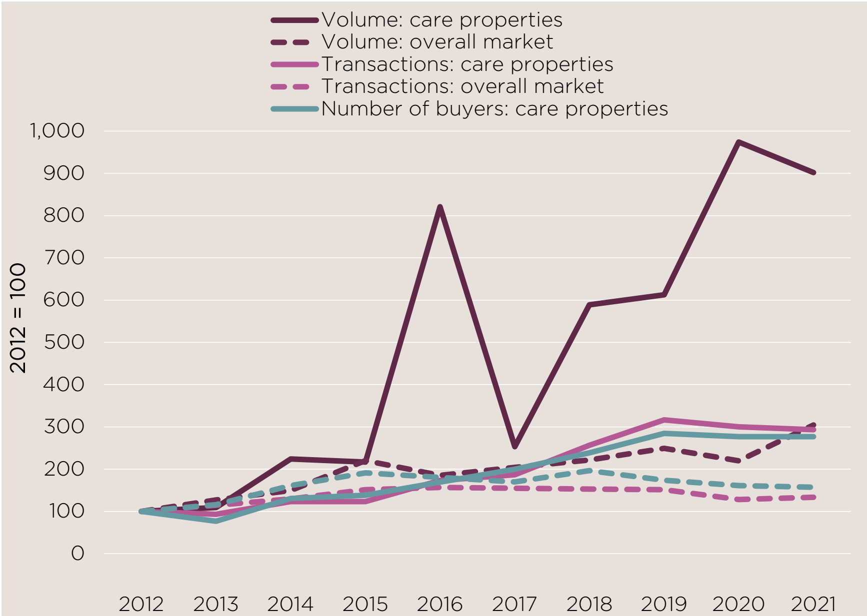


Source Savills

“In the market for care properties, investors who can also handle smaller transaction volumes have an advantage.”

increased field of bidders, competition for the few available products has intensified in recent years. This is particularly the case for portfolios or for the quite rare large-volume individual properties. In this competitive environment, investors who can also handle smaller transaction volumes have an advantage. It is also advantageous to enter into a cooperation with an operator or to found or buy one’s own operator. In this way, properties with expiring leases or project developments at a very early planning stage can be acquired. For properties without long-term leases, the field of bidders is usually much smaller. Joint ventures and cooperations with project developers have also been increasingly observed in recent years. This makes it possible to secure a project pipeline at an early stage. However, in view of the massive increase in construction costs, early forward deals are currently linked with greater risks.

Graph 7: Care properties and overall market in comparison



Source Savills

Origin of the buyers
Around 48% of the transaction volume in the last 5 years was attributable to foreign buyers.

20% Volume share
Assisted living facilities accounted for 20% of the volume in the last five years.

24.5 million euros
Over the last five years, transactions have averaged 24.5 million euros.

> **“Unlike other uses, care properties will not be substitutable in the foreseeable future. Together with the structural growth in demand, this should lead to care properties attracting greater attention from more and more investors.”**

Current opportunities and challenges

Measured against the demand from investors, which has been increasing for years, the supply of care properties remains scarce. In our view, the developments in the coming months and years will lead to opportunities for investors. Many of these developments are ambivalent and represent both opportunities and risks for investors. In the following, we take a closer look at some of these developments.

Despite interest rate rises and the like: care properties remain in demand in the long term

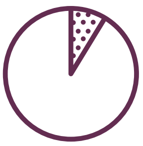
The beginning of 2022 was associated with much optimism for the real estate market: The effects of the pandemic seemed to have been overcome and many real estate investors wanted to further expand their portfolios. However, the war of aggression against Ukraine and the interest rate turnaround have noticeably dampened the mood on the German real estate market and led to significantly fewer transactions. We are currently assuming a temporary effect and a normalisation of the markets towards the end of the year. Investment pressure remains high and bond yields are still not at an adequate level despite a noticeable increase. Properties in markets with long-term positive fundamentals will continue to attract capital in our estimation.

Care property is one of the segments that we believe will benefit from an influx of capital in the long term. Since the pandemic at the latest, the risk perception of many real estate investors has changed. This manifests itself, among other things, in a more critical assessment of future space requirements. Above all, sectors and properties that are classified as systemically relevant or relatively crisis-resistant are experiencing higher demand on the investment market. These include, above all, care properties. In addition, the pandemic is acting as a digitalisation accelerator in many sectors and is leading to uncertainty among investors regarding future space requirements. In contrast to other uses, we do not currently expect any far-reaching structural change in demand for care properties due to digitalisation. On the contrary: care homes and assisted living facilities will not be substitutable in the foreseeable future. The different trends and long-term perspectives on the occupier markets should lead to more and more investors readjusting their risk assessments. In many cases, the capital to be invested in the real estate market is likely to be reallocated. Due to the structurally growing demand on the occupier markets, we assume that care properties will be among the types of use that receive increased attention from many investors.

New construction in the area of conflict between demand and cost explosion

In addition to rising interest rates, it is above all the massively increasing construction costs - caused by supply and personnel bottlenecks as well as rising energy and raw material costs - that are currently causing concern for many real estate market players. In the current mixed situation, project developments of care properties in particular must be reassessed. In order to obtain modern care properties at all, many investors have bought properties still under construction or in planning via forward deals in recent years. In 2021, such project development purchases accounted for around 570 million euros or about 20 percent of the transaction volume. It is to be expected that some construction projects will have to be stopped, postponed or cancelled. This is due, among other things, to the partially capped refinancing possibilities through the so-called investment costs (‘Investitionskosten’) to be paid by the residents. These now clearly lag behind the actual building costs. For example, the appropriateness limit for the construction costs of new buildings in North Rhine-Westphalia is a maximum of €2,478 per sq m. At the same time, a maximum of 53 sq m net floor space is considered adequate for a care place. According to this, new construction costs of a maximum of €131,342 per care place are used in the assessment of investment costs in North Rhine-Westphalia. According to the BKI Construction Cost Index, however, typical new construction costs already amounted to €150,900 per care place in 2020. Since then, the rise in construction prices has accelerated once again. According to the Federal Statistical Office, the producer prices of building materials alone rose by 10.5 percent in 2021. Further significant price increases were reported for the beginning of 2022. Due to the capping of investment costs, operators can hardly pay rents that contribute to the profitability of a project development. As a result, either the margins of project developers decline or they have to switch to more peripheral locations with lower land costs but also lower achievable purchase price multipliers. Or new projects are abandoned altogether.

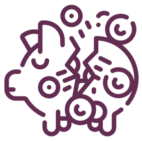
The current challenges surrounding new construction have various consequences from an investor’s point of view. Rising construction costs will reduce new construction of care properties. As a result, there will be a shortage of supply and owners of care properties can expect very high occupancy rates for their existing properties in view of the high demand in the long term and consequently stable rental income. The value of the existing stock should therefore increase relatively. It cannot be ruled out that politicians and funding bodies will react to



20%
Forward deals accounted for around 20% of the transaction volume in 2021.

150,900 Euro
The construction costs per care place averaged 150,900 euros in 2020.

Rising construction costs
Producer prices of building materials alone increased by 10.5 % in 2021.



Risk of insolvency
Even before the pandemic began, one fifth of the operators were in danger of insolvency.

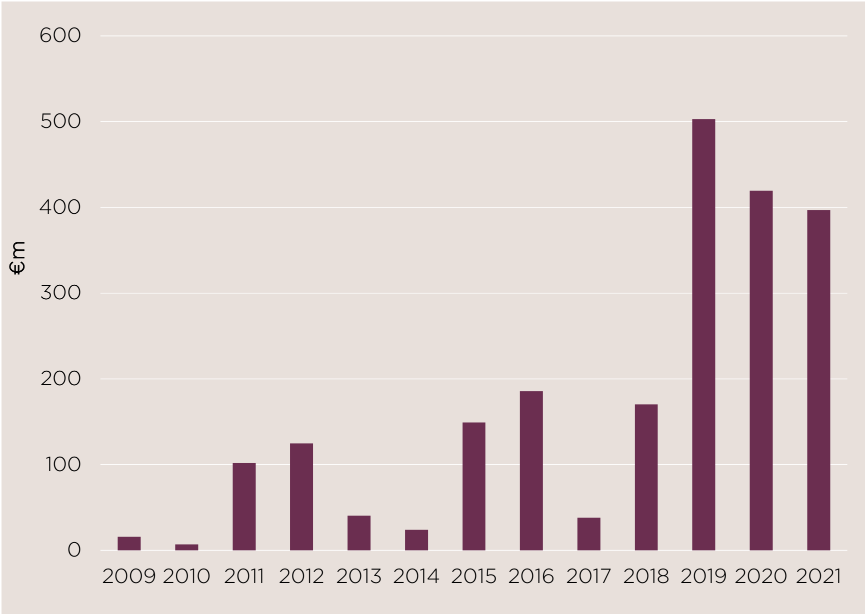
a reduced rate of new construction in care homes and provide additional subsidies or at least increase the investment cost rates.

Because project developments have become riskier, many investors are likely to become more reluctant to conclude early forward deals. Instead, we expect competition for modern existing properties to become even more intense and prices for such products to remain high. For investors willing to bear the higher risks of project developments, interesting opportunities could currently arise. For example, some project developers may be forced to sell at conditions that are less favourable for them in order to obtain capital at an early stage. At the same time, the number of prospective buyers will probably be lower than a few quarters ago, putting bidders in a better negotiating position. Meanwhile, the market volume of project developments is considerable. According to our estimates, the construction projects scheduled for completion by the end of 2024 alone have a market volume of at least 9 billion euros. Even if many properties have already been sold to an end investor and some projects may not be realised as planned, it should still be possible to place a lot of capital in such products.

Wave of sale-and-leasebacks in sight?

Not only construction companies and project developers are affected by rising costs, but also operators of care properties. In the course of the pandemic, costs for operators have already increased considerably due to additional hygiene measures. The shortage of staff also poses a high risk, since if the statutory care ratio is not met, some of the care beds can no longer be occupied and thus income is lost. Since the operators' revenues cannot be increased at will due to the strong regulation of care cost rates, many companies are increasingly getting into economic difficulties. According to the Pflegeheim Rating Report 2022 prepared by RWI - Leibniz Institute for Economic Research and other project partners, around one fifth of German care homes were already in danger of insolvency in 2019. Around a quarter were in the red in the year before the pandemic

Graph 8: Sales volume of operators



Source Savills

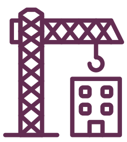
began. It is to be expected that the number of operators at risk of insolvency has increased due to the burdens during the pandemic - and will increase further due to the current higher inflation rate. In order to obtain additional liquidity to maintain business operations, operators with own stock could increasingly divest themselves of their properties. Already in recent years, a significantly higher volume of sales by operators was observed than in previous years (Graph 8).

In the future, this could lead to an additional offer for real estate investors on the market. However, such products are likely to appeal primarily to investors with a higher affinity for risk, as operators forced to sell have a poor credit rating. Here, too, investors who have their own operator competencies or have entered into a cooperation with a cost-efficient operator have an advantage.

The growing insolvency risks on the part of the operators, on the other hand, will further limit product availability for very risk-averse investors. As a result, care properties with long-term leases from operators with strong credit ratings are likely to become even more sought-after. Sooner or later, it is inevitable for society to spend more money on care services. It remains to be seen, however, when and in what form adjustments will be made, for example, to social long-term care insurance. Until then, a close examination of the economic performance and staffing of an operator remains one, if not the most important component of due diligence.

New regional care home legislation in sight

Investors in care properties operate in a highly regulated market environment. In the case of care homes, the equipment and thus also the usability depends very much on the respective care home legislation of the federal states ('Landesheimgesetze'). In recent years, there have been various amendments to the laws. For example, existing buildings in North Rhine-Westphalia must have a single room quota of 80 percent since 2018. For new buildings, even 100 percent single rooms have been stipulated in the



At least 9 billion euros
The construction projects, which are to be completed by the end of 2024, are worth at least €9bn.

Sales for 1.3 billion euros
In the past three years, operators have sold properties for about 1.3 billion euros.

Operator competence
Access to an own or associated operator brings advantages in product identification.

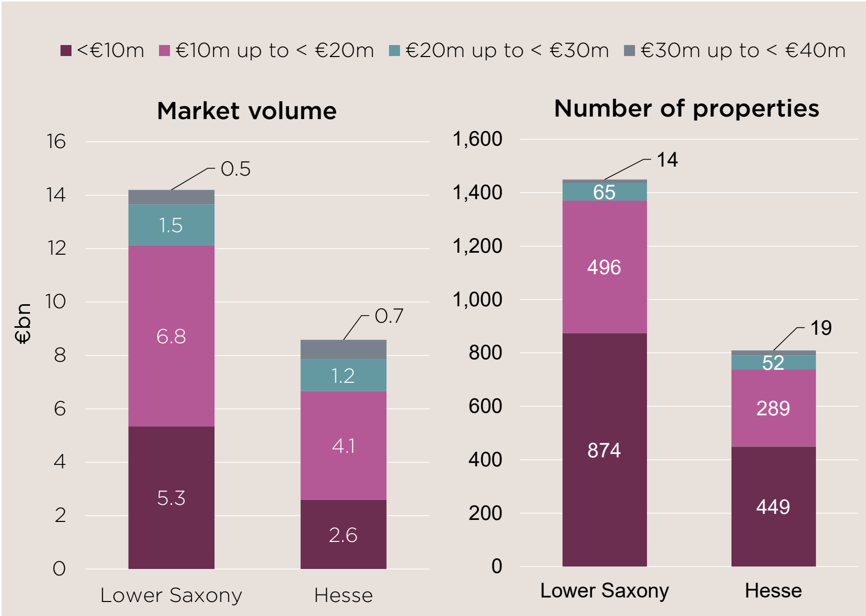
Single room rate

In the course of the amendment of care home legislation, mandatory and high single-room quotas were set in many cases. This development is likely to continue and lead to investment needs in the existing stock.

course of the amendment of the legislation. A single room quota of 100 percent has also been set in Baden-Württemberg. The owners of care homes usually have several years to implement the changed framework conditions. In any case, the adjustments mean conversions in many existing properties and thus considerable investment needs.

Amendments to the care home legislation in Lower Saxony and Hesse are currently on the horizon. In Lower Saxony there is no binding single room quota so far, and in Hesse the protection of existing buildings will expire at the end of the year. In Hesse, single rooms are already the standard for new buildings, although requests for double rooms can be taken into account. The exact form and date of entry into force of the two amendments to the law cannot yet be estimated as of June 2022. However, in our estimation, it is likely that single room quotas will be set for existing buildings. This should soon result in additional investment needs in these federal states as well. In view of the already heavy financial burden on many landlords and care providers, it can be expected that some owners will want to sell their properties to developers or attract investors as joint venture partners. Thus, there are prospective opportunities for investors in these two federal states. Currently, the estimated market volume of existing care homes in Lower Saxony and Hesse is 14.2 billion euros and 8.6 billion euros respectively (Graph 9). In total, there are more than 2,250 existing care homes in both federal states.

Graph 9: Volume and number of existing care homes in Hesse and Lower Saxony



Source Savills; own estimation based on Pflegemarkt.com

Where is ESG in care properties?

In addition to regulation by the federal states and cost units, the European Union's Taxonomy Regulation, better known by its acronym ESG, is likely to have a growing influence on market activity in the future. ESG regulation has led to a massive shift of capital in the European capital markets into investment vehicles declared as sustainable. According to a PwC survey in September 2021, 79 percent of investors surveyed said ESG is relevant in their investment decisions. Furthermore, PwC predicts that by 2025, half of institutional financial capital in Europe will be allocated to ESG-compliant products. The topic of ESG will therefore also gain in importance in the investment market for care properties.

For investors, care properties offers both opportunities and risks in this respect. At first glance, the social and governance aspects - the S and G in ESG - should be quite easy to comply with in the case of care properties. The social aspects are aimed at positive interaction with employees, residents and the neighbourhood. Many providers of care services are likely to take these aspects into account out of self-interest, in order to have satisfied residents or to be attractive for new employees. The provision of real estate for care services or assisted living also has a high social benefit per se. Satisfactory governance is also likely to be very important for the reputation of care providers. Nevertheless, corresponding measures and activities need to be identified, documented and made measurable. Challenging here could be the different expectations and responsibilities of landlords and operators. For example, the operator has a significant influence on many aspects of the ESG performance of a care property. Measuring and processing the relevant data means additional work for the operator; in many cases, however, the information obtained is primarily useful for the property owner. In order to regulate the provision of ESG-relevant data and information, corresponding clauses could increasingly be included in lease agreements in the future. At present, however, it can be difficult in many cases to provide evidence of good performance in S and G.

It is likely to be even more challenging to comply with the ecological aspect - the E in ESG. Also due to the low investment cost allowances, high energy building standards are often not available for care properties. Assisted living facilities are often likely to perform better. Even if they do not guarantee ESG compliance, many investors currently look for a sustainability certificate when selecting properties. But care properties with such a certificate are almost non-existent in Germany. The major certifiers DGNB, LEED and BREEAM have so far only awarded a sustainability certificate to four care properties in Germany. By comparison, there are currently more than 3,200 certified properties in Germany. This could lead to ESG-compliant investment vehicles in other types of use, such as office or logistics, finding it easier to obtain appropriate properties. It is possible that buyers who are actually interested in purchasing will refrain from buying care properties in the future.

In view of the lack of certified buildings, investors have the opportunity for a so-called manage-to-green strategy, i.e. for the purchase of existing properties and the subsequent refurbishment and possible certification. When selling such a property, an intense bidding war between investors with sustainability goals and high achievable purchase prices can be expected.

Sustainability certificates
Currently, only four care properties in Germany have a sustainability certificate from DGNB, LEED or BREEAM.

In order to prevent ESG from becoming a massive barrier to investment in care properties, landlords and operators should begin to develop appropriate ESG strategies as soon as possible. Furthermore, data necessary for ESG due diligence should be collected and processed. This will make it easier to approach ESG-compliant investors.

“There is a massive need for investment in both existing and new buildings in order to meet demand and achieve higher energy standards. This mammoth task cannot be accomplished without private investors. Overall, there is much to be said for long-term structural growth in the investment market for care properties.”

Our overall conclusion

The investment market for care properties has become much more dynamic in recent years. However, more and more investors and a larger amount of investment capital are facing below-average liquidity and thus a lack of available products. It is particularly critical that many properties are de facto not available for institutional investment due to the quality of the property as well as a prospective non-compliance with the legal framework. This creates a product shortage on the market despite the large number of potential investment properties. However, product availability could improve in the next few years, although increasing economic pressure on operators and owners will also contribute to this. In principle, the pressure to modernise existing buildings is likely to increase in the coming years. This is because the German climate goals in the building sector can only be achieved through a higher renovation rate in the existing stock. The sharing of CO_2 costs between owners and occupants depending on the building standard is likely to be only the first step in stronger regulation. In addition, there are likely to be higher single-room occupancy rates in some federal states. To meet all these requirements, a lot of capital is needed for existing care properties. Some landlords do not have the necessary capital or are unwilling to make these investments, so selling to other investors is likely to be an option. In addition, significantly more care properties are needed in Germany to meet the growing demand for care. A lot of capital will therefore also be needed in the new construction segment in the coming years. It is already becoming apparent that these mammoth tasks cannot be accomplished without private investors. The high investment demand should thus lead to investment opportunities and a larger supply for investors. Overall, there is much to be said for long-term structural growth in the investment market for care properties. The fact that the majority of the market volume is to be found in growth regions should suit the investment preferences of many investors. In order to address a broad spectrum of institutional investors, however, the current deficits in the area of ESG and sustainability must be remedied quickly.

While the need for investment is growing overall, rising costs are leading to higher risks for project developers and care home operators. The massive increase in construction costs is likely to reduce new construction activity and thus counteract the actually foreseeable expansion of supply, at least temporarily. Meanwhile, increasing economic difficulties of many care home operators are leading to a further thinning out of suitable supply for risk-averse investors. Instead, the current market environment offers a variety of opportunities for investors with a higher risk appetite. For such investors, it can make sense to build up or take over their own operator competencies or to enter into long-term cooperation with a cost-efficient operator with a strong credit rating.

In contrast to care homes, rents in assisted living facilities can be adjusted to market levels much more easily. For risk-averse investors who find it difficult to find suitable products in care homes, assisted living facilities can be worthwhile.

The economic difficulties of many operators must be a cause for concern in view of the ever-increasing need for care. Sooner or later, we believe that politics must react to this dilemma and provide additional funds for the operation of care properties. This could attract additional capital from real estate investors and make the market attractive for new players. It remains to be seen when such extensive and very cost-intensive reforms will come about.

Download the charts and raw data here

An indication of market size

Our estimate of the market volume is an indication of the size of the market. In practice, however, many properties are likely to be de facto ineligible for institutional investors.

Methodology for determining the market volume

We have estimated the market volume of care properties as follows.

1. Our basic assumption is that investors can theoretically acquire any care property. Particularly in the case of assisted living facilities, properties are divided up among various private investors, so that they are de facto not available for global investment. How high their share is not known.

2. To determine the market volume, we have estimated the volume for each existing and currently planned property. The basis for our property list is the database of Pflegemarkt.com.

3. In the absence of property information on the number of care beds or assisted living units, we have used average values for existing buildings and new construction projects in each case. For care homes, this is 78 beds in existing buildings and 81 beds in construction projects. For assisted living facilities, we assume 43 units in existing buildings and 39 units in construction projects. 4.

4. To estimate the volume of care homes, we have derived typical capital values based on comparable transactions from 2020. Care homes can be divided into three categories in terms of building age: All new buildings or modernised existing buildings completed from 2015 onwards are considered as *new*. Properties that were built or last renovated between the years 2000 and 2015 are classified as *modern*. All older properties are assigned to the *old* category. We have also assigned existing properties without information on the year of construction to the *old* category.

In the next step, we applied typical average capital values per care bed for the three categories. These are 150,000 euros per bed in the category "*as new*", 130,000 euros per bed in the category "*modern*" and 112,000 euros per bed in the category "*old or unknown*". We did not take location information into account.

5. In order to estimate the volume of assisted living facilities, we used key figures from the open apartment markets.

In the first step, we used the maximum rent for apartments in first occupancy for the respective district in 2021. The data is taken from Bulwiengesa. For all assisted living facilities built or refurbished in 2015 or later, we applied a rent premium of 50 percent. For all older buildings, the premium is 30 percent. These assumptions are based on empirical values.

In a second step, we have set the average size of an assisted apartment at 55 sq m due to a lack of property-specific information on the size of the space. This value is based on a market report by Terragon.

In the third step, we determined a purchase price factor for the global sale. To do this, we first used the average multiplier for apartment buildings in the respective district in 2021. The data here is also taken from Bulwiengesa. We then applied a yield premium of 100 basis points. This corresponded to the difference between the prime yields of multi-family buildings and assisted living facilities at the beginning of 2022.

In the fourth step, we multiplied the annual rental income by the determined purchase price multiplier.

6. For properties that have both care home beds and assisted living units, we applied the methodology for the respective use and then added both volumes.

Due to data gaps, our methodology is a rough estimate. Thus, our average results may differ significantly from the actual property value in individual cases. However, after comparing them with actual purchase prices, we believe our methodology provides a rough indication of market size. Our estimate is based on capital values at the beginning of 2022, so the market volume we have determined is a snapshot and further development depends on future conditions on the capital and investment market.

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