

# Institutional and Foreign Investors Enter Health Arena as Healthcare Goes from Opportunistic to Core

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A continuation of the trends that shaped last year, such as more development of outpatient facilities and little change in cap rates or MOB pricing, should carry over to 2018, says **Beth Young of Colliers** in this GlobeSt.com **EXCLUSIVE**.



HOUSTON—A continuation of the trends that shaped last year, such as more development of outpatient facilities and little change in cap rates or pricing for medical office buildings, should carry over to 2018. Furthermore, there will be strong [demand from investors](#) for healthcare properties, particularly now that institutional and foreign investors have set their sights on the healthcare property sector.

These are some of the healthcare market tendencies that Beth Young, [Colliers International](#) senior vice president specializing in medical and investment properties, recently in a GlobeSt.com **exclusive**. She also shared insight into expansions/contractions and hospital designs.

**GlobeSt.com: What are some of the expansions and contractions that are evident throughout the metro?**

**Young:** Demonstrating the importance of providing healthcare in locations close to the consumer, numerous Houston-area hospitals expanded to the outer submarkets including The Woodlands, Katy, Pearland and Cypress. Although Houston health systems are increasing the size of footprints on the Houston landscape with new hospitals in major markets, hospitals are reducing the number of beds while expanding other departments. For example, in 2007, Memorial Hermann (Houston's largest health system during the past 10 years) had 10 acute care hospitals and more than 3,000 licensed beds. At the end of 2017, the system had approximately 50% more hospitals and one-third the number of beds it had 10 years ago. Meanwhile, the population data shows the greater Houston area has increased 20% during that time.

Driven by higher deductibles, better technology and drugs, shrinking reimbursement and patient demand for convenience and lower costs, health systems are incentivized to promote prevention and keep patients with chronic diseases out of the hospital, while providing care throughout Houston's major markets. Expect to see

fewer overnight beds and growth in cardiac surgery, operating rooms, ICU beds and health system-sponsored clinics in locations citywide. Some hospitals are using available floors for hospice or rehab space, while others are doing a straight real estate deal, offering the floors for lease. The shift to outpatient care is well underway and accelerating.

**GlobeSt.com: What are some of the features of the modern medical center?**

**Young:** Patients throughout Houston will choose where they go for care based on the customer experience. Retail settings near residential communities may include urgent care, freestanding emergency centers, MOBs, imaging centers, ambulatory surgery centers, oncology care, post-acute care facilities and perhaps senior-care properties. Some larger healthcare systems will provide multiple services in one location near homes, ranging from primary care visits, imaging, cardiology, gastroenterology and orthopedics to entertainment and exercise (to keep patients busy while waiting to see doctors) and casual dining options in one building.

Not only do successful hospitals and health systems increase locations, but successful physician groups and specialty services are also following the trend, opening locations in major submarkets around the city. Often, physicians share clinic space with compatible specialists in multiple locations so they can refer business to each other.

**GlobeSt.com: How have hospital designs evolved in recent years?**

**Young:** A growing recognition of the need to treat behavioral and mental health (including addiction management) is resulting in a demand to accommodate cognitively impaired patients more effectively and sensitively. In larger hospitals, emergency departments are being reconfigured to reduce risk while ensuring compassion and dignity for these patients. Because they often require longer stays in the emergency department, an emerging design practice is adding features like bathroom showers, storage areas for belongings and decompression space. Occasionally, smaller vacated hospitals are converted into behavioral and mental health treatment facilities and some of these buildings are used for substance abuse clinics for children, teens and adults.

Patients in smaller towns in 19 states are benefiting from micro-hospitals, providing services similar to larger hospitals, but on a smaller footprint, often 15,000 to 50,000 square feet with between five and 15 inpatient beds.

Another hospital trend is learned from the hospitality industry, says Noe Ramirez, a healthcare architect with [RS&H Architects](#). Besides design changes that include a trend toward soothing interiors, immune-compromised patients, like those needing bone-marrow transplants, need a different type of hospital setting for extended care. After the surgery and post-op, these patients are vulnerable to infection and require monitoring for complications, but they don't need full hospital services. So the new design for this time in a patient's stay will feel more like a hotel than a hospital, with a more comfortable interior design including some suite-style rooms and possibly a skilled concierge rather than a nurse.



New medical building designs will provide more private rooms and fewer shared rooms.

### **GlobeSt.com: What were some of the newest medical office buildings to hit the market in 2017?**

**Young:** An impressive 19 new buildings were added to the list of CoStar's medical office properties in Houston in 2017. With that expansion came a 0.9% increase in direct vacancy, although sublease space remained at the same 0.3% during the year. In 2016, 495,000 square feet of medical office space was absorbed, but as of December 2017, only 95,000 square feet was calculated by CoStar as the net absorption amount for the year. Further, 13 medical office buildings with more than 700,000 square feet were under construction and expected to open in 2018.

Gross lease rates have increased about \$1.00 per square foot in the past year, and net rates have increased about \$0.43 per square foot. During that time, tenants offering sublease space paid attention to the difficulty in finding sublessees and have reduced sublease rates from \$22.52 to \$20.24 per square foot.

### **GlobeSt.com: What are the size ranges for clinic buildings?**

**Young:** Because of the trend toward efficiency and consolidation in healthcare, the average clinic has grown in size. An average doctor's office was perhaps 2,500 square feet in the past, but now a single physician may lease closer to 5,000 square feet. As technology improves, allowing for more outpatient procedures, physicians continue to locate offices with more services that include labs and imaging to provide more convenience for patients near their homes. It's not unusual for neighborhood clinics to average between 10,000 and 20,000 square feet.

### **GlobeSt.com: How have Baby Boomers affected the healthcare landscape?**

**Young:** The growth of the senior population has spurred a new trend: the sale of many of their homes in exchange for apartments in denser urban areas. That presents the need for nearby modern and easily accessible medical offices, often in the form of urgent care facilities. Those will be found in mixed-use centers that include a grocery store, retail shops, restaurants and perhaps a movie theater and/or neighboring residential tower.

Although hospitals are reducing the number of beds due to the growth of outpatient facilities, remaining inpatients will be the sickest and most acute, requiring longer hospital stays. New designs will provide more private rooms and fewer shared rooms.

Investors and developers expect the senior housing sector to grow this year. Most aging Baby Boomers are still active in the workplace, but demand is expected to increase in the coming years, which will encourage investors to add more senior living assets to their portfolios.

### **GlobeSt.com: What is the latest at the Texas Medical Center?**

**Young:** The Texas Medical Center/TMC is the largest medical complex in the world. It is the eighth largest business district in the US and continues to expand like an island built on an active volcano. In the last year, a new word has been used to describe what is happening in the TMC—collabitation. As the CEO of the TMC told audiences recently, the institutional leaders of the TMC are now collaborating to compete with international medical centers rather than with each other. Construction projects totaling \$3 billion are underway and there is a clear passion about the determination to drive the next generation of life science advancements from Houston. The goal is to become the world leader by leveraging the collective power of TMC's renowned institutions in a shared, centrally managed environment. The result will be a research collaborative unlike anything healthcare has ever seen. With 1,345 total acres and \$25 billion in GDP, the TMC continues to expand, renovate and develop healthcare space for new accelerator programs that will drive innovation. Projects include incubation space to accelerate technology commercialization and a research park to co-locate early-stage companies alongside pharma, biotech and venture capital. In addition, a new 25-story 550,000-square-foot healthcare tower will break ground in the second or third quarter.

A major addition adjacent to the Texas Medical Center is planned by Medistar, scheduled to break ground in the second half of 2018. More details will be coming, but expect 32,000-square-foot floorplates in approximately 550,000 total square feet with an oversized parking garage and retail at grade level.

**GlobeSt.com: How would you sum up the healthcare investment climate in Houston?**

**Young:** Healthcare has changed from being an opportunistic investment to a core investment. Most private investors and REITs hope to acquire off-market transactions. However, when it comes to dispositions of their own properties, investors prefer to use qualified brokers to fully market a property, saying they want to set up the competitive environment knowing they will usually achieve a better sale prices.

Healthcare real estate is still considered less expensive than some of the other asset types, but that is changing. Quality assets are very competitive. Value-add properties attract fewer investors because of the expertise or disposition that is required to be successful.

[Lisa Brown >](#)

Lisa Brown is an editor for the south and west regions of GlobeSt.com. She has 25-plus years of real estate experience, with a regional PR role at Grubb & Ellis and a national communications position at MMI. Brown also spent 10 years as executive director at NAIOP San Francisco Bay Area chapter, where she led the organization to achieving its first national award honors and recognition on Capitol Hill. She has written extensively on commercial real estate topics and edited numerous pieces on the subject.

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