MANY *healthy* RETURNS

Ascot Hospital is one of Vital Healthcare Property Trust's flagship properties and is considered one of New Zealand's premier private surgical and medical facilities.

HEALTHCARE ASSETS SHOW RESILIENCE IN A CHANGING INVESTMENT ENVIRONMENT.

LEARNINGS FROM THE COVID-19 pandemic will undoubtedly reshape the healthcare industry globally and, as a result, the real estate that underpins it.

Even pre-COVID-19, medical-related property was garnering significant traction in the market.

Healthcare delivery models are evolving resulting in new investment opportunities and, with yield compression in other core asset classes, investors are looking for higher returns.

Private investors, syndicates and institutional investors have seen healthcare real estate morph into an increasingly sophisticated asset class. It's a segment of the market that seems recession-proof thanks to an ageing population, the generally non-discretionary nature of the provision of healthcare services and other property fundamentals such as higher yields and long weighted average lease terms.

Corporate and community trust ownership structures have seen some general practitioner (GP) remuneration models change, while property trusts and syndicated fund managers have given investors access to diversified healthcare real estate investment portfolios with scale.

New research from Bayleys' global real estate partner Knight Frank, says in 2019 in the UK, the healthcare asset class performed well relative to the broader commercial property market despite political and economic uncertainty and funding/regulatory issues within the sector.

Average total returns to the healthcare property sector in the UK have averaged 8.7 percent over the last five years.

Proposed major structural governance changes to New Zealand's health system at a macro level and a groundswell of change at the general practice and health asset ownership levels, means that things are interesting in New Zealand, too.

The recently-released Health and Disability Systems Review recommends big shake-ups to district health boards and primary health organisations including new entities and authorities to oversee changes.

General practice (GP) in New Zealand is supported by the Government bulk-funded model with payment directly related to the number of patients on practices' books and this is driving the acquisition path in the GP sector.

Jayson Hayde, Bayleys national director of business sales, says New Zealand's multi-layered healthcare system offers a number of investment channels and he's seeing proactive acquisition trails in the healthcare real estate and medical business operational arena.

"Large healthcare groups with scale and financial stability can offer administrative and delivery-of-care benefits for often overworked and under-resourced doctors who are entrenched in independent private practice," he says.

"It is a step-change from the traditional model of a sole practice family GP working from a villa in the suburbs.

"We're seeing broader community health hubs with radiology, laboratory, physiotherapy and other remedial health services all under the same roof with many located within retail and mixed-use precincts for convenience and accessibility."

> **"IT IS A STEP-CHANGE FROM THE TRADITIONAL MODEL OF A SOLE PRACTICE FAMILY GP WORKING FROM A VILLA IN THE SUBURBS."**
>
> JAYSON HAYDE, BAYLEYS NATIONAL DIRECTOR OF BUSINESS SALES

Disruptors to the pharmacy sector from "warehouse" and online business means the sole-charge pharmacist working from a retail frontage could also soon be a thing of the past.

Total Property checks up on some of New Zealand's leading players in the healthcare real estate market.

FLYING THE FLAG

NZX-listed Green Cross Health Limited is a New Zealand-owned and operated primary healthcare provider with multi-disciplinary healthcare teams working around the country with an emphasis on collaboration where GP practices intersect with other primary care services.

The group comprises 43 medical centres with most operating under The Doctors brand; 360 pharmacies under the Unichem and Life Pharmacy banners; Access Community Health and Total Care Health Services.

The latest Green Cross Health NZX report talks to "a continued strategy of targeting compelling acquisition opportunities" either as equity partners or owners, with patient rolls a key driver.

David Thompson, Green Cross Health medical division acquisitions manager, says a compelling business acquisition opportunity would demonstrate sustainable business performance, be a natural fit with Green Cross Health and its values, and would demonstrably benefit from being part of a collaborative network.

Thompson says there are any number of reasons for GPs wanting to sell or go into partnership.

"Because every situation is different, we work with owners to build a plan that suits them – be it planning a staged exit strategy, providing much-needed capital investment to grow their practice, or simply relieving the day-to-day operational burden," he says.

"We offer a tailored partnership complemented by full clinical leadership and governance to provide operational excellence.

"We act as an enabler for practices to grow, provide quality care, meet compliance and health and safety regulations, and have resource in human relations, payroll, recruitment and training."

Thompson says "lifestyle" is now a real priority for GPs and is a strong reason to reassess their practice responsibilities.

"Having Green Cross medical division as an equity partner or owner allows GPs to get some of their life back."

Green Cross Health's The Doctors Te Whare Hāpara, Gisborne.

The modern premises of Green Cross Health's The Doctors, Huapai, opened in December 2017.

"WE OFFER A TAILORED PARTNERSHIP COMPLEMENTED BY FULL CLINICAL LEADERSHIP AND GOVERNANCE TO PROVIDE OPERATIONAL EXCELLENCE."

DAVID THOMPSON, ACQUISITIONS MANAGER, GREEN CROSS HEALTH MEDICAL DIVISION

Green Cross has a rapidly growing network of medical centres supporting more than 270,000 enrolled patients across the country.

"The Doctors has developed into a strong local brand particularly in Whangarei, Auckland, Tauranga/Mt Maunganui, Whakatane, Napier and Hastings," Thompson explains.

"The consolidated, established model in these regions means we can provide deeper support and collegiality.

"We are actively looking for new opportunities and would like to develop our presence in the Waikato, lower North Island and the South Island."

Thompson says the wider health system's response to COVID-19 has reaffirmed the primary care sector's ongoing role in healthcare delivery making it an even more compelling place to be doing business.

VITAL HEALTHCARE DELIVERY

Vital Healthcare Property Trust is the only NZX-listed dedicated healthcare property fund.

It owns 40-plus high-quality medical and healthcare facilities across New Zealand and Australia including private hospitals, aged care, mental health facilities, acute and rehabilitation hospitals.

New Zealand accounts for 25 percent of its asset portfolio and includes Ascot Hospital in Remuera, Kensington Hospital in Whangarei, Bowen and Wakefield Hospitals in Wellington, and Royston Hospital in Hawke's Bay.

Aaron Hockly, fund manager for Vital, says the removal of ideology around real estate ownership in the health sector would assist growth in this asset class.

"Politics can be a handbrake at both a healthcare delivery level and at a real estate level and I believe the Government focus should shift from ownership to 'how does the Crown get the best value' across healthcare delivery, risk and financial returns," he proffers.

Hockly says private sector landlords – including listed entities like Vital, mutuals like Southern Cross and charitable organisations like Sisters of Mercy – are typically better owners of property than the Government.

"The private sector is well set-up for carrying out due diligence, construction management, reporting to deal with building issues and other responsibilities that come with property ownership," he says.

"Building failures at Middlemore Hospital are an example where things could have been very different had a reputable landlord been at the helm.

"The Government has already moved away from owning its office buildings with an explicit preference for leasing, and this should be extended to other classes of real estate – including healthcare assets."

Hockly says the COVID-19 pandemic – while far from over – has underscored the pivotal role of the healthcare sector and operators within it.

"Globally, COVID-19 has reminded communities of the importance of healthcare facilities and the operational capacity of these," he says.

"In New Zealand and Australia in particular, we've been reminded that most of our healthcare is delivered outside of public hospitals including private hospitals, GP clinics and specialist facilities."

Vital Healthcare Property Trust has committed to an expansion project for private Royston Hospital in Hastings, Hawke's Bay.

Owned by Vital Healthcare Property Trust, Ormiston Hospital in Flat Bush, Auckland is the only private surgical hospital in the Counties Manukau District Health Board catchment.

Hockly says while "location" may be paramount in a global real estate asset context, COVID-19 has demonstrated the importance of the operator in the healthcare sector, as evidenced by glaring shortfalls in America's aged care market.

"Vital continues to partner with high quality hospital, aged care and other healthcare operators to ensure the delivery of quality care and to allow stability and growth of our earnings," he explains.

"As part of our full year results released on 10 August, we revised our subsector target weightings in the following order: hospitals, aged care, outpatient/medical office buildings and life sciences/research.

"These target weightings reflect our learnings from COVID-19 – including the benefits of geographic, tenant and asset diversification – and will likely result in some further re-weighting of our portfolio over time."

Vital Healthcare's New Zealand asset manager Drugh Woods, says it's happy with the 75-25 percent split of assets across Australia and New Zealand but would be happy to increase exposure to either country if suitable opportunities arose.

"We have seen steady leasing demand for our properties since the end of Alert Level 4 in New Zealand and have concluded some smaller leasing transactions subsequently," he says.

"Given Vital's long weighted average lease term and high occupancy, the portfolio doesn't tend to experience significant vacancies and as many of our tenants invest heavily in their fitouts, they're often keen on early lease renewals."

Woods says construction-wise, Vital has $280 million worth of redevelopment and expansion projects underway in New Zealand and Australia, with around $200 million left to complete.

INVESTMENT OPPORTUNITY

Augusta Funds Management has relaunched its Augusta Property Fund after a COVID-19 hiatus, with the fund's initial asset being Anglesea Medical Centre in Hamilton's CBD.

Established in 1992, Anglesea is one of New Zealand's largest private healthcare centres occupying a 2.4 hectare freehold site and comprising three main buildings with 12,573.2sqm net lettable area. Recent developments include a café and retail block completed in 2017 and the pharmacy extension in 2018.

Head of Bayleys syndication and investment products team Mike Houlker, says Anglesea Medical Centre offers income diversification through 28 tenants.

"The nine largest tenants have been on site for 14-28 years illustrating their commitment to the site and location," says Houlker.

"THE ECONOMY ITSELF IS NOT THE KEY DEMAND DRIVER FOR THIS SECTOR, THEREFORE THIS TYPE OF PROPERTY PRESENTS DESIRABLE NON-CYCLICAL AND DEFENSIVE CHARACTERISTICS."

MARK FRANCIS, MANAGING DIRECTOR, AUGUSTA

Major tenants include Pathlab, one of New Zealand's largest pathology service providers with one of the most advanced laboratories in the southern hemisphere; Hamilton Radiology's main facility, and Fertility Associates, the Waikato's only public and privately-funded fertility treatment provider.

It also houses Anglesea Clinic Urgent Care, Hamilton's leading 24/7 private urgent care facility and the delegated after-hours care provider for the majority of GPs in the wider Waikato region.

Augusta managing director Mark Francis says prospects for New Zealand's medical and healthcare property sector remain attractive and it's well-placed to outperform other sub-sectors within the property market.

"The economy itself is not the key demand driver for this sector, therefore this type of property presents desirable non-cyclical and defensive characteristics," he says.

"Further, demand for private medical services in the Waikato should remain strong, driven by continued population and economic growth, constraints on the public health sector and an ageing population."

Samara Philips, Bayleys syndicated investment manager, says the property provides value-add opportunities through several strategies including Augusta's intention to actively engage with tenants to extend or renew leases along with a planned and budgeted capital expenditure programme.

"Flexible local zoning allows a broad range of potential uses and building heights and there is relatively low site cover at the property which bodes well for potential refurbishment and reconfiguration opportunities."

The Augusta Property Fund is expected to evolve to expose investors to a variety of property investments within the one investment vehicle, with diversification by asset class, sector, geographic location and tenancy mix.

Augusta Property Fund's initial asset is Anglesea Medical Centre in Hamilton's CBD – one of New Zealand's largest private healthcare centres.