US nursing homes: A goldmine for real estate and private equity firms

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This is the second of a two part series. Read part one here.

Seemingly overnight the COVID-19 pandemic has jeopardized large sections of the nursing home and long-term elderly care industry. Multiple senior housing-related stocks suddenly dropped as part of the stock market crash at the beginning of March, and some remain at levels comparable to their prices following the 2008 economic crisis.

Ventas, Healthpeak Properties and Welltower—known as the "big three" health care real estate investment trusts (REIT)—all experienced sharp drops in their stock prices as a result of the virus. Ventas declined from a stock price of $59.77 per share on February 14 to $22.52 on April 3, while Healthpeak's stocks fell from $31.64 per share on February 28 to $20.96 on March 20. Welltower, which is the most senior-oriented of the three, saw stocks drop from $89.32 per share on February 14 to $37.26 on April 3.

Once considered a safe investment in a growing industry, nursing home advocates have requested the federal government set aside $15 billion to help the industry handle the crisis brought on by the COVID-19 pandemic. The $15 billion would come on top of the Centers for Medicare and Medicaid Services (CMS) advancing payment to nursing homes and providing as much as $1.5 billion in aid.

The seemingly sudden crisis within the long-term elderly care industry is particularly astonishing given previous estimates that the sector would be rapidly expanding. By some estimates the value of the US long-term care market was expected to reach $737.1 billion by 2026 with a compounded annual growth rate of over 7 percent.

Many companies saw the potential for growth in the industry as "baby boomers," the roughly 73 million Americans born between 1946 and 1964, become senior citizens. Some business analysts also noted the possibility of consolidating the nursing home industry. It is now becoming apparent, as the coronavirus rips through the nursing home population, claiming thousands of lives, that these estimates had no relationship with providing quality care for the largest number of people, or insulating the industry from a potential health crisis.

Industry breakdown

In the US there are roughly 15,400 nursing home facilities that are tasked with taking care of about 1.5 million residents. Approximately 70 percent of nursing homes in the US are run for profit with the rest run either by non-profits or government owned.

The nursing home industry has a complex ownership structure, which partially hides the influence of other corporations and trusts in the operation of a facility. According to the *New York Times*, six large healthcare REITs have business interests in more than 1,500 nursing homes mostly through long-term lease agreements related to the properties the nursing homes rent. While the REITs owned a diverse array of nursing homes, elder care facilities and medical buildings, the lease agreements often included substantial rent increases every year.

In 2017 Kaiser Health News reported that almost three-quarters of nursing homes in the US, which would total more than 11,000 facilities, outsource goods or services with companies they are invested in or owned. These types of arrangements between companies with a shared investment or owner are known as "related party transactions." As a result of these agreements owners of nursing homes can grant themselves extremely favorable agreements, but not include the profits on a nursing home's account. In 2015 nursing homes paid related companies $11 billion.

The use of "related party transactions" creates certain legal difficulties for individuals and families attempting to sue nursing homes because it is harder to get payments from the other companies. Kaiser Health News also found that nursing homes that use this corporate structure on average employed eight percent fewer nurses and aides, were nine percent "more likely to have hurt residents or put them in immediate jeopardy of harm," and "were fined 22 percent more often for serious health violations" compared to independent nursing homes.

According to the most recent analysis from the *Times*, almost half of residents in for-profit nursing homes were living in facilities with below-average staffing. In comparison 23 percent of residents of non-profit or government nursing homes were in facilities with below-average staffing.

There has also been a growth of private equity investment within the nursing home industry which has further negatively impacted care. One study from 2017 into facilities owned by Golden Living found that facilities had significantly fewer deficiencies than competitors but rose to roughly the national average after they were purchased by a private equity firm.

HCR ManorCare, at one time the second-largest nursing home operator in the US, was bought in 2007 by Carlyle Group, a private equity firm, and experienced a rapid decline in subsequent years. According to the *Washington Post*, the number of health-code violations rose by 26 percent every year between 2013 and 2017. These violations included failure to prevent or treat bedsores, medication errors and not assisting residents with eating and personal hygiene. In 2018 the healthcare provider declared bankruptcy and ownership was transferred to its then landlord, Quality Care Properties.

A separate study released on March 9, titled "Does Private Equity Investment in Healthcare Benefit Patients? Evidence from Nursing Homes," found that after a private equity buyout a nursing home's rating based on the CMS five-star system declined on average by eight percent. Since 2015 there have been almost 190 private equity deals related to nursing homes, compared to 116 between 2010 to 2014. The total worth of such deals grew from $1 billion between 2010–2014 to $5 billion between 2015–2019.

Where the money comes from

The largest source of revenue for nursing homes is government programs, particularly Medicaid. The nonprofit National Investment Center for Seniors Housing & Care (NIC), reported last year that over 67 percent of all skilled nursing facility patient days were covered by Medicaid in the third quarter. While this was the greatest share covered by Medicaid since NIC started reporting this data in 2012, Medicare covered just short of 11 percent of patient days.

Medicare has the highest reimbursement for nursing home facilities and Medicaid has the lowest.

John Whitman, a lecturer at the Wharton School focused on aging and long-term care management, described the dangers of Medicaid becoming the primary means of paying nursing homes. At the National Summit on the Future of America's Nursing Home Industry in 2017, he stated, "Medicaid in 35 of 50 states pay an average of $23 below the actual cost of providing care. So, unable to attract Medicare or private pay residents [due to changes in the industry] these facilities then start admitting even *more* Medicaid residents to help fill their beds—as financial losses continue to increase."

It is apparent that the response by the industry has been to rely on a variety of cost cutting measures, and further government support.

Over 2,300 nursing homes use an affordable loan program run by the Department of Housing and Urban Development. The program, which guarantees $20 billion in mortgages, is used by roughly 15 percent of the country's nursing homes compared to around five percent 25 years ago. In 2018 the Rosewood Care Center in Inverness, Illinois, defaulted on a $146 million loan from the program.

Amid the ongoing COVID-19 pandemic, more public money is being pumped into the private health care and nursing home industry. Out of the $2.2 trillion emergency rescue passed last March with the support of both the Democrats and Republicans, $30 billion was allocated for hospitals and health care facilities such as nursing homes. Undoubtedly this money will do more to line the coffers of real estate trusts and private equity investment firms than it will to improve conditions for nursing home residents, patients and health care workers.