

Washington State Medical Office Real Estate Continues Frenetic Pace

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The summer season is not bringing a slowdown in medical office real estate activity, as is sometimes the case. I mentioned running the Boston Marathon in last quarter's newsletter. The recent uptick in activity has caused me to switch to a faster transportation mode, which will be tested this weekend in the Courage Classic Bicycle Tour to support the Rotary Endowment for the Intervention and Prevention of Child Abuse and Neglect. Please wish me luck while I ride over the Cascades twice and Blewett Pass once.

Leasing News

Hospitals in the Puget Sound region are in an expansion mode on or adjacent to their main campuses. The Affordable Care Act appears to be helping the bottom line of hospital systems in states that opted to expand Medicaid access, like Washington. The national press offers some evidence: FitchRatings reported on July 16: "The CEA (Council of Economic Advisors) estimates that states that participate in expanded Medicaid coverage will receive \$83.6 billion in additional federal funding from 2014-2016 while states choosing not to expand Medicaid will be giving up approximately \$88.1 billion in additional funding over that period. Fitch is beginning to see the beneficial aspects to providers in "expansion states" through improved payor mix and reductions in bad debt in the first quarter of 2014." ("ACA Beginning to Hurt Hospitals in States that Opted Out"). Locally, I've heard hospital executives say there has been an 80% swing from uninsured to Medicaid insured, making a dramatic positive impact to the bottom line.

In Washington, medical office demand and construction near hospital campuses remains strong. On Harborview's First Hill campus in Seattle, King County's Harborview Hall redevelopment is said to be moving forward, aiming to break ground in the fall of 2014. Near the Swedish main campus, The First Hill Medical Pavilion is under construction to deliver 150,000 sq. ft. of medical office space in July 2015. On Cherry Hill, neighbors have voiced their concerns with the 1.61 million square feet expansion of Swedish's Cherry Hill Major Institution Master Plan, however all signs point toward the proposal moving forward. There are several additional significant leases currently in the confidential phase that I should be able to describe next quarter.

In addition to the continued strength, from a real estate perspective, of the centralized campus, hospitals in this region (and nationally) are signing leases in shopping centers old and new. The upcoming demographic shift resulting in 71 million adults over the age of 65 anticipated by 2030, and the name recognition

that comes with increased auto and pedestrian traffic are driving the move to retail locations. After a first run of smaller regional retail clinics such as UW Medicine's Neighborhood Clinics, providers are now becoming even more dedicated to a retail approach, opening larger clinics with more specialties offered. Virginia Mason has opened their 20,000 sq. ft. pediatric/multi-specialty clinic in University Village. UW Medicine is placing a 30,000 sq. ft. clinic in Ballard's 1455 Leary Way building. Swedish has leased 20,000 sq. ft. adjacent to the University Village. In Federal Way, Seattle Children's is planning to redevelop a former Circuit City space in West Campus Square—a Costco-anchored retail center—into a 35,000 sq. ft. multi-specialty clinic. Construction is slated to begin July 2014 with a delivery in mid-2015.

I am also paying close attention to the trend towards telemedicine, which may be causing certain large health systems to pause prior to signing new leases to expand primary care in neighborhood settings. I am speculating on this point, but the speculation is based on conversations with hospital executives. The delivery method is gaining credence; in June at its annual meeting in Chicago, the American Medical Association released guiding principles for the employment of telemedicine services: "the principles aim to help foster innovation in the use of telemedicine, protect the patient-physician relationship and promote improved care coordination and communication with medical homes." ("AMA Adopts Telemedicine Policy to Improve

Access to Care for Patients," 6/11/14, AMA Press Release.) New telemedicine staff may be able to locate remotely, away from the "medical home," thereby potentially moderating some real estate needs.

Sales News

Sales of medical office properties in the Puget Sound region have picked up steam in the last few months, reflecting a national trend. According to Real Capital Analytics, sales volume in Q2 2014 was up 26% over Q2 2013, and cap rates are trending down.

Recent Washington State sales deals include the following: Puget Sound Surgical Center purchased the 15,265 sq. ft. Ballinger Way Medical Building for \$4,800,000, or \$314/sq. ft. This purchase is an owner/user acquisition. In Richland, the Corrado Medical Building traded for \$9,002,133, or \$218/ sq. ft. to the Kadlec Regional Medical Center. The 36,023 SF 780 Swift Boulevard in Richland also changed hands. In Bellevue, the Family Medical Center at 1200 116th Ave NE traded for \$3.2 million.

Hospital News

The big news on the Olympic Peninsula is the plan for Harrison Medical Center to move its main campus from Bellingham north to Silverdale, with plans to build a new \$240 million hospital financed by Harrison's new affiliate, Franciscan Health System.

Vancouver-based PeaceHealth's planned affiliations with Cascade Valley Hospital in Arlington and Skagit Regional Health in Mount

Vernon have been placed on hold.

In an interesting Eastside development, Overlake Hospital has been identified as a potential purchaser of Snoqualmie Hospital, currently being developed by Benaroya Companies, extending Overlake's service east along the Interstate-90 corridor.

Overall, with interest rates remaining low and demand for healthcare strong in our region, I am seeing an unusually active summer in the medical office world. After healthcare decision makers return from well-deserved vacations, I predict the momentum will continue into the autumn, like riding a bicycle down a mountain.

Paul Carr is a First Vice President with CBRE, focusing on investment sales and leasing transactions within the healthcare sector of commercial real estate. As a member CBRE's national healthcare services team, Carr advises physician groups, hospitals and investors on leasing, acquisition, disposition and build-to-suit development requirements.

Carr has assisted with the leasing requirements for some of Seattle's largest multi-specialty physician groups, the monetization of medical office buildings and excess land for a variety of regional and community hospital systems and the acquisition of medical office buildings for investors and physician groups alike. He has been with CBRE since 2001 and consistently ranks among the top CBRE Brokers in Washington State. He can be reached at paul.carr@cbre.com or 206-292-6005.