Stifel, Nicolaus & Company, Incorporated

Moderator: Jerry Doctrow
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Jerry Doctrow: Good morning, my name is Jerry Doctrow, I lead the healthcare real estate research effort at Stifel Nicolaus and I will be the host and moderator for this call.

This call will focus on the Senior Housing and Skilled Nursing Real Estate Transaction Markets and Pricing

And will be a conversation with Steve Monroe and Alan Plush.

I will provide a brief introduction, introduce our speakers and ask questions to guide a discussion. We will then open the discussion up to your questions.

Since July of last year, healthcare REITs and senior housing operators have announced over $15B in major real estate acquisitions including:

- $6.1B acquisition of Manor Care post-acute, skilled nursing, assisted living and memory care real estate by HCP
- $3.1B acquisition of Atria senior housing real estate by Ventas in management structure
- $2.4B acquisition of Genesis skilled nursing and assisted living real estate by HCN
- $2.0B acquisition from several operators of senior housing real estate by HCN in a management structure
- $1.2B acquisition of Sunwest senior housing real estate by Blackstone/Columbia Pacific/Emeritus joint venture

And those are just some of the big deals. These transactions have set a new price points for skilled nursing and senior housing real estate, with initial cash yields on triple net skilled nursing transactions at 8.8 percent to 8.25 and cap rates on senior housing below six percent. And at the same time, we've got one-off skilled nursing acquisitions being done by REITs at cash yields probably over 9.5 percent and senior housing profit being done in excess of eight percent.

So, the wide economy pricing between large and small transactions and the fact that REITs are driving pricing has really raised a lot of questions in the minds of analysts and the minds of investors about what are the cap rates out there in this business today that you can use to estimate public company NAVs.

I'm delighted to have two leading industry experts on this call today to review transaction pricing, current market conditions, and give us and our clients better insights on market dynamics, who is active in the market in addition to the REITs, and current market pricing.

Our speakers today are Steve Monroe, who's a Partner at Irving Levin Associates and Managing Editor of SeniorCare Investor and The Senior Care Acquisition Report. Irving Levin is the source for transaction data in the senior housing and care sector.

Steve's monthly publication, SeniorCare Investor, is a great way to keep up on the comings and goings in the industry, including comments on publicly traded operators and discussion of transaction activity. If you're going to invest in Health Care REITs or senior housing operators, they are publications worth getting.

Alan Plush, MAI, is one of the best regarded real estate appraisers in the senior housing and care industry. He's worked as a senior housing and healthcare appraiser for 25 years. He's the Senior Partner and Founder of HealthTrust, LLC. He's a member of the ASHA, American Seniors Housing Association Executive Board, a regular speaker at industry conferences, and has worked on many of the large transactions in the space. He's also an active investor in senior housing through Rittenhouse Senior Living, Contemporary Healthcare, Smith/Packett, and Energy Court Holdings.

I'd also add both Alan and Steve have been active in senior housing and care since before I started in the business which goes back to 1997 but somehow they both look younger than I do. They must have started very early in their careers.

With that, we'll get into questions and Steve, let me open with you, Irving Levin recently published its survey of skilled nursing and senior housing transaction pricing in 2010, can you share with us what you saw on averaging pricing, cap rates for skilled nursing and senior housing last year and perhaps some of your observations on the market based on this data?

Steve Monroe: Sure, and Jerry, thanks for allowing us the opportunity to be on your discussion today. We recently came out with our 16th edition of our Senior Care Acquisition Report and I will be the first one to say I was a bit surprised by a number of the statistics.

First off, while it didn't appear to be that great a year in 2010 for skilled nursing, the average price per bed jumped by 32 percent from 2009 to a record 62,500 per bed; that looks a lot very low compared to some of the recent REIT deals but nonetheless, that was a definite record. The median, which sometimes people like to use as a better example, only went up 19 percent to 51,500 per bed but both were records.

It was interesting with what happened, the majority of the higher-priced properties actually sold in the last four months of the year and that's why I was not thinking we would be having these record-setting numbers. The first eight months of the year was more on the lower-end side.

Cap rates were consistent. The average and median cap rates for skilled nursing in 2010 were coincidentally 13.1 percent for both. The average increased by 30 basis points, the median decreased by 20 basis points. So, there was really very little change there but that's been one of the most consistent numbers out there. For 15 to 20 years, the nursing home cap rates, every year, the average is somewhere between 12.5 and 14.5 with 13 percent right smack in the middle there.

The senior housing side, this is where I was expecting a bit more of an uptick but it was relatively flat in 2010. The average price per unit decreased just by a little over three percent to 112,000 per unit. But the median actually increased by five percent to – just under 108,000 per unit. Most of the sales in senior housing year after year are assisted living as the vast majority and so they do dominate the senior housing side. I was expecting a little bit better of the year but it's not what happened.

Average cap rates for senior housing declined to 9.4 percent in 2010, while the median declined to 9.1 percent. These may seem high but you got to remember that our statistics include the good, the bad and the ugly, not just the high-end stuff, not just the big corporate stuff, but all of our sales are arm's length sales that include both the real estate and the business.

Jerry Doctrow: And your numbers also exclude REIT transactions, Steve, if I understand right, so some of those yields were not in those stats.

Steve Monroe: These stats are closed deals, not announced, so it has been closed in the calendar year and only includes those REIT transaction where the seller is not going to be the lessee or the manager; or it's, you know, party A sells to the REITs and then leases it to party B, that would be included because it's a complete arm's length.

Jerry Doctrow: OK. Alan, do those numbers, particularly the cap rates and pricing, match up reasonably well with what you saw in the market last year?

Alan Plush: Yes, Jerry; in fact, they do pretty well and also thanks for letting me join the call and look forward to our conversation today. Yes, it's amazing. As Steve referenced, we've spent 25 years appraising nursing homes and I think the strongest measure of central tendency for the cap rates is 13 percent.

We don’t focus as much on the price per bed as an absolute metric because, you know, too many times when we do appraisals on nursing homes, it's always state-specific because of the uniqueness of the Medicaid reimbursement rate state to state and so we will look for sales within that state.

And really, because data set is so small from our perspective, oftentimes you just won't find transactions that are valued for property sales similar to or that are as nice as the one you're appraising, and then it's not a truly good comp. So, we focus more on cap rate and margin.

And I would say that the skilled nursing cap rate number, when the markets are very active, with a lot of the acquisition, and a lot of capital in the market, we'll see that number dip from 13. Several years ago kind of '06 or '07, I think we saw a down in the 11.5 to 12 range in some cases but by and large, I believe at 13, we're right back to where the industry has always traded.

And then in senior housing, because of the volume of appraisals we do both independent and/or assisted, we break it out separately. So, we're probably using an aggregate cap rate range of 7.5 to probably nine, let's say, for investment grade assets and that would include independent and assisted. And then, the total range is probably more like 7.5 or eight, let's say, to 10 and that would include both kind of your A and your B assets.

So, I think generally the information that Steve is discussing is absolutely corroborated by what we see in the market and I think there's a lot of similarity between the two data sets.

Steve Monroe: And Jerry, I think it's important to note that the average is for the whole year, so it doesn’t take into account, the market in the first quarter of 2010 compared with the last quarter or the first quarter of 2011. So, you don’t, you know – you don’t get the benefit of seeing the market improve as much as you might want.

Alan Plush: I would agree with that, Steve. I think we saw such a dramatic shift in 2010 from the beginning of the year to the end, and probably one of the quickest changes I think I've seen. And you're right, absolutely, and use of an average is somewhat misleading.

Jerry Doctrow: So, where would you think cap rates are now, at end of the year and moving into 2011 and in real time today? Let's talk about senior housing first of all.

Alan Plush: We're using on a regular basis, an aggregate range of 7.5 to nine and that's probably, with 7.5 to eight being institutional grade agency, agency financeable – excellent physical plant, more recent construction, good operational history, strong operator. I mean, those are the 7.5 to eight – to 8.5; it depends upon, what usually affects this market area.

But then, you know, we can go on your B assets; by that, I mean, a tertiary market, maybe a 15- to 20-year-old building, I'm just trying to kind of give a general example. A B asset might have a cap rate of nine to 10. The C assets, we just don't seem to see much of but those but they can be 10-plus because those are still pretty hard to come by.

Jerry Doctrow: And on skilled, is the cap rate still around that 13 percent figure?

Alan Plush: Well, 12.5 to 14 is our aggregate range and keep in mind that – and as with Steve's data set, we're talking about arm's length transactions, we're talking about these simple values that will be the cap rate supplied to the total income generated by the real estate and the business; and so, yes, 12.5 to 14.

When we run into non-stabilized assets or there's an operational problem or what not, the lease up maybe that needs to occur, those properties really aren't what we're referencing in this discussion. I think Steve, would you agree with that?

Steve Monroe: Yes, and I would also add that I agree with Alan in those ranges and it's always so property- and quality-specific.

But especially so far this year in talking to the brokers out there who are coming out with some very A-quality properties, their price talk is in the seven to 7.5 cap rate. Their clients are trying to push to see if they can get below seven, and that's kind of a barrier right now.

But you've got to remember, for a few years we had so few high-quality assets that when a real juicy institutional-quality property came on or a portfolio, the market has been so starved for that that they will find reasons to bid up the price.

Alan Plush: I would absolutely agree and I find this – of course, the whole paradigm almost – it's amusing because I remember, you know, 10 to 15 years ago – let's say, 15 to 20 years ago when really assisted living was valued very similar to nursing and 11.5% was kind of a normal cap rate for institutional assets in the assisted living space, and independent living was always 100 basis points below that.

And now, we've seen I think a total paradigm shift and there's a lot of demand for these assets in and yes, I know, there's a lot of pricing pressure for cap rates below eight and of course, as we're seeing them, we want to see the transactions close but I think that there probably will be some – some of those will happen maybe before the end of this year.

Jerry Doctrow: Just a couple of maybe technical points to make clear because I think a lot of institutional investors are more used to looking at, initial yields on REIT deals rather than cap rates; but a couple of things, one is just when you're on cap rates, you're doing trailing 12 months, would that be fair?

Alan Plush: No, and I should have probably outlined this upfront. The methodology that appraisers use, and I'm an MAI, Member of the Appraisal Institution, we have adopted the appraisal foundation which all the appraisal groups are members of as kind of standard definitions for cap rates.

You know, cap rate is extracted from the buyer's expectation of net income divided into the purchase price and is applied to the appraiser's expectation of net income on a forward basis; that can amount to a 25 to 50 difference in the cap rate using forward versus trailing numbers.

Steve Monroe: I should interject that all of Irving Levin's stats are pretty much based on either trailing or the last three or six months annualized, we looked at it as the buyer looked at it in term of in place income. The appraiser has got to come out with some forecast and we don't because we're not appraising, we're looking at what was – what was in fact going on at that time, so that's why there can be some differential.

Alan Plush: Right.

Jerry Doctrow: Although, I think Alan both and Steve indicate a fairly narrow range for cap rates despite the fact that maybe one's looking trailing, one's looking forward, is that – is that fair to say?

Alan Plush: Yes, we did a comparison just for this and I think that the difference was I thinks was about a 34 basis point difference on average. And so, you know, if it's seven – 7.5 versus eight, it's seems material but if it's eight versus eight and a quarter, you know, it doesn’t feel material.

Jerry Doctrow: And just one other thing just to be clear. If I'm thinking about it on a REIT lease and I assume, Alan, you do some of this REIT lease stuff as well. How would you go from cap rates on a typical non-REIT deal to REIT initial leave yields? Or saying it another way, what are you seeing in terms of lease coverage if they're going to make that translation?

Alan Plush: Sure, Jerry. I mean a lot of – a lot of what we do is value the asset for the REIT rather than the asset and the business and so we don’t get as much into that side, but my sense is 1.25 to 1.50 lease coverage and probably eight to nine on initial yields again very broadly. And I know some REITs out there that are more in the 10 to 11 percent range for initial yields but I think that the preponderance of the investment rate stuff is in the eight to nine range.

Jerry Doctrow: Are you talking skilled or senior housing?

Alan Plush: You know, I'm trying to think what we've done lately and I don’t see a huge distinction and I could be wrong there. I don’t know, Steve, if you do or not; but that seems to most of what we’re seeing that’s how it's getting done.

Steve Monroe: Well, Jerry, the coverage is higher on the skilled side and then you have the big three on the REITs and everyone else. And the smaller the REIT it seems, the higher the cap rate or the yield, and they're looking at trying to get nine – 9.5 to 10 to 11 percent initial yield, and they're getting it sometimes.

Alan Plush: I think a lot of times those REITs will also do maybe slightly older properties or smaller portfolios and the REIT transactions that get the very best pricing are usually the marquee transactions that involves more than just real estate but it's a play on a platform as opposed to, you know, smaller collection of assets.

Jerry Doctrow: And Alan, do you have any sense of the REIT deal today what they're looking for in coverage, say, on senior housing or maybe assisted living or what they're looking for in coverage on skilled?

Alan Plush: Yes, I mean, coverage is out of the box; my feeling – and I don't know if I have an answer to that or not. I mean, my guess – my intuition is about 135 to 150.

Jerry Doctrow: OK, and higher on the skilled?

Alan Plush: On the skilled, yes.

Jerry Doctrow: OK. Let's switch gears a little bit, so back to Steve; there are two precedent-setting transactions that I'd like to focus on; one is the ManorCare acquisition by HCP and the other is the Atria acquisition by Ventas. Both had record low cap rates, certainly below the kind of numbers we have been talking about here. So, are these numbers and are these transactions unique or are they really setting the valuation precedent? I mean, how do you think about them versus the averages we've been talking about?

Steve Monroe: Well, obviously, the numbers are a lot higher at least on the per bed and per unit valuation, and cap rates are much lower than the rest of the market but I would definitely call them unique. I mean, HCR ManorCare was always a unique entity. So, you know, they're at the highest end of the large SNF operators with good facilities.

That said, you know, that pricing in my mind really reflected their business income and their excellence in their pursuit of Medicare revenues more than their property values. So, I think that's where the real value was. So, I don't think it's setting the precedent for pricing, although it changed the market psychology or help changed it.

Atria was similar, with a great cluster of locations and very expensive markets, and they were repositioning several of their facilities so there's significant room to improve and expand cash flow. So, that was unique in that way. And secondly, you know, with Ventas, I really think they're looking at Atria as being a platform for them to grow and to build on and possibly with other acquisitions, and expand the management business of Atria.

So there are a lot of different things going on there, and I would put them in the unique camp.

Jerry Doctrow: Alan, how about you?

Alan Plush: Yes, and I absolutely agree with Steve 100 percent. These are not – you know typical transactions. We ran into these same type of transactions in the last cycle, let's say, when Holiday Retirement was sold at roughly a 5.75 cap rate and you know, certainly the next day, as soon as that got out in the market, then every converted hotel that offered independent services thought that they qualified for that cap rate.

The reality is that there are in any cycle always a certain number of marquee transactions and these are, as Steve said, involve purchasing a lot more than just sticks and bricks, they're actually buying into a platform and a business model that certainly they believe it can not only sustained but be grown.

And I think that’s when you look at ManorCare and even Genesis and Atria for sure and, I think even the Merrill – they're all very good examples of cherry-picking and I think that ‘s what you're seeing reflected in those transactions. Plus I think – I wouldn’t say abnormally low but certainly uniquely low cost of capital on the part of the REITs. I think all that factors together.

I’m remembering that, at the top of the last cycle, we had other players that had harnessed very low capital cost and that’s what brought transactions with very low cap rates at the time to market. And now, I think we have a similar set up and REITs have harnessed a low cost capital and have infrastructures in place that make it attractive to put money to work.

If you have the luxury of time, you're going pick a good time in the cycle to show and sell your assets and it's all kind of coming together 'in those circumstances. I don't think it sells again. If you look at Steve and my cap rate conversations about the kind of measure of central tendency, let's just pick nursing, you know, 13; and you look at some of these other transactions that are below that and clearly there's something else going on.

Jerry Doctrow: You mentioned Genesis; you touched Merrill Gardens and obviously Silverado and some others RIDEA transactions as well. My sense is, and I just want to clarify this, that you would put all of these kind of RIDEA transactions in the unique category as well, I don't know if you, Steve, want to a little more color to some of those deals?

Alan Plush: Yes, and Steve, you're on.

Steve Monroe: Well, in turning more color in terms of...

Jerry Doctrow: Yes, I mean, would you definitely consider them unique as well. Do you see them sort of this precedent setting or a sort of very special deal?

Steve Monroe: Well, I think what its doing is it's basically setting the precedent for REITs. You look at it and all these deals that were basically were announced in a very short period of time and all prices that raised eyebrows everywhere. And the pricing is understandable in many regards but I think what it does is it separates out these rates in one column, you know, basically the three big ones, HCP, Health Care REIT, and Ventas.

And so, they have now set their own pricing parameters based on their cost capital and that's going to right now price-out financial buyers. I mean, Blackstone cannot compete with the REITs right now because, one, the return requirements are higher based on their cost of capitals. So, what I think is you have two different markets and no one is going to be able to come in on a price and compete with the big REITs.

So, I think that's what you have to always keep in mind, is that it's – there's the REIT world and really the three big REITs and then there's the rest of the market.

Alan Plush: And I think it's much like the cap rate conversation with agency versus non-agency financeable assets and I think you're absolutely right, Steve. You kind of got this segment of the market that would be within the big three's appetite and then you kind of have the rest of the world.

Steve Monroe: And then, the other thing is, you know, using the so-called ideal structure for management as opposed to leasing. You know, it's great and it's great to capture the excess cash flow growth if management does its job. But what no one is focusing on is, you know, what happens if there's other than good performance and what happens if income growth is flat or negative unlike the lease structure.

And there is a risk to that but the price that's being paid for the management deal is generally higher than with a triple-net leave because of the potential for excess cash flow. But no one is pricing in that risk, not on the higher price that risk would typically get.

Alan Plush: I absolutely agree that and in terms of how you price that in I think the market is probably going to reward or penalize it as it plays out. But I agree that the REITs have taken on a larger share of risk with management acquisition structures and, if operations perform as one would like to think they would, then maybe there isn't as much of a risk kind of haircut. But if there is a slip, then I think that structure is going to be certainly scrutinized. But, you know, any time you employ a new technology or structure, there's always a little bit of adjusting as you go through.

Jerry Doctrow: Let's switch gears a little bit. So, you made a point, Steve, that there are the big three REITs and then everybody else. Who is the everybody else? I mean, are you seeing individual operators who buy properties. Beyond the big three large portfolio market, who's out there today?

Steve Monroe: Well, in addition to the big three REITs, the smaller REITs are all active but not doing the billion dollar deals. But on top of that, I mean, there's just a huge number of operator buyers out there, everywhere from the guy who owns two or three properties to the five, 10, 15, 20 property, local, state, regional company that are all looking to expand and most of them would rather buy than build. Some would prefer to build then buy but will still but under the right circumstances. But the depth of the demand is pretty significant.

You know, we were talking to one broker and I posed the question, "If you have a stabilized, high-performing, relatively-new, A-quality property, how long will it take you to sell?" And he said, "Well, I would have more than a dozen bidders within 30 days compared with a B-minus, non-stabilized property, you might get three bidders in nine months." So there is incredible demand across the spectrum for good properties, very deep.

Alan Plush: Yes, absolutely, and I think that the investment case has been certainly validated over the course of this recession and I think that’s a large part of what we're seeing. I think that the asset appreciation play may be off the table for a while in terms of buy low, sell high. I think the sell high point is going to come but it's going to take longer than it did last time.

But that being said, you're absolutely right, I see a lot of local, regional folks that want to go from five to 15 to 20 properties and that’s the growth strategy and they’ve got investors. And you know they demonstrated expertise at operations, that’s where the next – and I see a lot of that kind of smaller level but still very significant, consolidation is going on.

Remember, as we always say, I mean, this is a local business and so that’s really organically how I see the business regenerate and grow over time.

Steve Monroe: Except – I disagree with you on one thing; on the Genesis health deal, they bought that three years ago. They bought high at the peak of the market and then just three short years later, sold even higher.

Alan Plush: Yes, I agree.

Steve Monroe: You know, that was – that was kind of a fabulous situation for them.

Alan Plush: There's always one out there that busts my theory but you're absolutely correct.

Jerry Doctrow: Do you see any sign of more money coming in from pension funds and that sort of thing particularly maybe in senior housing or is there plenty of money already?

Alan Plush: My sense is there is a little bit more money coming from pension but I just have this intuitive feeling there's a lot of money lined up on the sidelines for this space. I don't know, Steve, if you're seeing the same or not.

Steve Monroe: Yes. Well, first of all, I think there's a lot of money in the sidelines, period. Secondly, senior housing and care has always been tempting but it's – you know, everyone – it depends on who the guy is. They always have a reason not to as opposed to some other real estate asset class, and it gets back to the whole thing about being a business and having the operational risk.

But there's certainly money there. It's creeping back in, you know. My gut is just like Alan but, that said, they want to pounce but you know, what's – what's going to cause them to pull the trigger and I haven't figure that one yet.

Jerry Doctrow: Let's shift a little bit to the skilled nursing; there are a couple of large skilled nursing portfolios out there that may need refinancing, Golden Living, Sava. How do you believe these transactions get done today? I mean, we're hearing HUD may not be an option – really an option for some of these big deals. How do you see them getting done? Do you maybe see even a REIT eventually in the mix for some of that stuff as well?

Steve Monroe: Well, yes, certainly, you know, with HUD, there've been several large portfolios in the queue and actually Golden Living was in the queue for I believe over a billion dollars but they are just recently in the market for private financing. I guess they're supposed to get today the indications of interest from buyers for 1.5 billion in secured financing which would be an alternative to HUD and that could be priced at LIBOR or pricing was LIBOR plus 350 to 375 for that; they'll find out whether that was going to work or not. So, it looks like they are going to bypass HUD for the time being.

One of the other large ones as you said was Sava, the former Mariner, you know, they're stuck in HUD. I think that could be a tough one with all the litigation going on. I don't see the REIT doing the Sava because of all the problems. I don't see the big three doing the Golden Living. I think, you know, quality-wise, it's beneath Genesis and HCR ManorCare. I am sure for the private equity owners of these companies one very likely exit would be to go to a REIT. I'm just not sure what REIT would take it.

It could happen but I'm just not sure which one would want to – would want to have that exposure to that company right now.

Alan Plush: I would agree with all that, Steve. I don't have a whole lot to add rather than I will tell you we're seeing, you know, traditional commercial banks starting to nibble at the space a little heavier than they have in the past but I don't see that this is an option for any of those large transactions.

Jerry Doctrow: And how much maybe while we're on this subject of financing availability, in term of agency financing, HUD financing, CMBS financing, are the clients that you're dealing with on transactions still seeing capital relatively easily available maybe with the exceptions of big deals with HUD?

Alan Plush: Yes, and again, with the institutional grade assets absolutely, I'm not seeing a problem in that, plus you couple that with a sprinkling of lenders, commercial lenders that are getting interested in. I'm not going raise the all-clear flag but it's just that things are starting to loosen up.

Now, you know, when I start to see – we've had a handful of new construction assignments come through for banks and REITs, there's only one REIT that's really active in the new construction space, at least that we work with. But we've seen kind of a scattering of lenders looking at new construction. I understand that the terms are not pleasant but that to me is kind of the last impediment. When commercial lenders become active in the construction space, that's when things are kind of back to normal.

Steve Monroe: And Jerry, people overlook HUD. They know how difficult it is and all that. You know, what people forget is that the HUD volume has just gone so up in the last couple of years. And last year and HUD versus Fannie and Freddie are a little bit different; HUD is assisted living and skilled nursing, Fannie and Freddie is assisted living and independent living.

The HUD lending volume was $3.2 billion last year. Fannie and Freddie combined did about $1.3 billion. So, HUD was almost three times the volume last year and that's huge. HUD has processed 40 to 50 loans a month. So, they used to be the lender of last resort 10 years ago, it's now the lender of choice because of its terms and rate – if you can wait.

But Fannie and Freddie's volume just really dropped down; one, the quality of acquisitions were not out there; two, they didn't have the burn-off of new construction and then two years later, they would re-finance Fannie and Freddie; but that market kind of disappeared too. So, the money is there but the product has not been there for them.

Jerry Doctrow: I want to just touch on one or two issues and then we'll open it up to questions. Maybe, Alan, for you, various states are looking at Medicaid cuts and Medicare seems to be doing relatively well at the moment. Are you seeing any impact on pricing or are any of your clients dealing with reimbursement issues in Texas or Ohio or somewhere that's talking more actively about Medicaid cuts and how's that impacting SNF prices?

Alan Plush: I think that the seasoned veterans are used to kind of the politicalization of reimbursement for long-term care and when I talk to folks who have been in the business for years, I – we all kind of talk the same language and that is we understand the cuts are threatened, they always are; the legislator takes it up the various interest groups get involved, voice their opinion and then there's a three percent increase.

Now, I don't want to oversimplify because obviously we're not in normal times right now but at the same time, I don't believe many states – I mean I think that most of the fat has been wrung out of the nursing home or long-term care sector and I don't think most states really want to tinker with draconian cuts.

So, my feeling is – you know, a lot of folks that I talked to are kind of handicapping a low probability of draconian cuts. There may be some flat years in there but not too many folks are worried about egregious cuts at this point.

Steve Monroe: And yes, remember, Jerry, that when buyers are looking at these properties in Texas and California where two of the highest proposed cuts; remember, they are proposed. Buyers don't make money in Medicaid. So, they're looking at their acquisition on the Medicare side, maybe a little on the private pay side.

So, you have a three percent cut, a five percent cut in the Medicaid rate, we are losing money already. Well, they're looking at, how can I make that up in Medicare, can I increase on Medicare volumes, can I increase my or enhance my Medicare census mix in terms in type of Medicare patients.

So, I don't think the buyers are paying as much as attention to that as one would think because, Medicaid for nursing homes, that's not going to make any money.

Jerry Doctrow: Let's see, I just want to come back to kind of the gap between some of the big deals and the small deals because I think there's something that we struggle with a bit and some of the clients struggle with and I think you guys probably see it as well.

And maybe, Alan, if we can start with you here but I think both of you have talked about sort of this wide-range sort of institutional quality or non-institutional quality versus the B- quality or small transactions. Can you maybe give us a little color on geographic differences and other factors driving that range of pricing?

Alan, I think you've touched down on some of the state differences but maybe to just give people a little bit of color for some or the things that you see between seven percent versus 8.5 cap rates and what's kind of driving some of that range?

Alan Plush: Certainly, Jerry. I feel – I feel it as it's ultimately from an appraisal perspective and certainly from an investor's –it all comes down to predictability and stability of cash flow, then comes strength of operator.

So, if I'm in a high barrier-to-entry market which are typically larger gateway cities, than I am less likely to have pricing pressure because the amount of new competition is going to be limited, those are properties that are likely to have a very good operating history even through the recession, it's not as much geography per se as it is those characteristics as opposed to maybe – you know, in Florida, we have a lot of vacant land and barriers to entry don't really come into play in most markets and I'll just pick Florida as an example.

And I think you see a lot more hesitancy on the part of operators in low barrier to entry markets because quite frankly, margins tend to be more compressed and this affects various parts of the country and also smaller tertiary or raw markets.

So, you know, if you look at what score card is for your best case scenario, it's going to be wealthy, with a large stable population of wealthy seniors, high barrier-to-entry market, stable to growing population base so that sale of houses is relatively easy and modest employment.

So, you look at all those factors and you match that with the facility that has a great location, has a good physical plant and good operations, and that's going to get your premium pricing there. This is senior housing as opposed to skilled nursing. Skilled nursing is more quality-mix driven in terms of what we get to the premium pricing on the nursing facilities.

So then you look at the other side of the senior housing, what comes if you're in a rural market that's got an abundance of vacant land and the senior population is small and you don't have a lot of pricing pressure, then you're going to see cap rates essentially adjust for risk and return at the same time. So, you know, my return characteristics may be generally the same between the two, maybe a little better because I could probably get cheaper debt on a – you know, on a stronger facility but my equity return is going to be higher on the facility where I anticipate more risk and then your cap rate is going to correspondingly rise.

Steve Monroe: And I'll add to that, Jerry, what Alan was talking about, you know, the top market to build versus one with a lot of land, that's one of the reasons I think why Ventas paid out for Atria. A number of their assets are in hard-to-build, hard-to-zone locations where the competition probably will not come, even though there's demand because it'll take so long even if they can find the property, the land will be expensive; it'll take so long to take them through the zoning and that so many people will say no, no, no to their zoning.

So, what Ventas was looking at is, hey, everyone else is getting three percent rent increases, the Atria probably – they can probably get six percent because there's no threat.

Alan Plush: And so, you will pay up for that platform, any buyer would for that exact reason.

Jerry Doctrow: So, just last question before we open up to the audience, you know, we've seen there is a torrent of deals, both REIT deals and non-REIT deals as well that are more under the public investors' radars. Do you see this pace continuing, or are we seeing more deals drawn into the market just over the balance of 2011? What's your sense of transaction activity going forward? Steve, go ahead and start.

Steve Monroe: Sure, I think the REIT transactions are just one side and I just can't imagine that we will see in the next eight months the same kind of volume with the REITs that we saw in the past four months because that was unprecedented, and I don't see that many large acquisitions like that. But I believe the large transactions are bringing a change in the market psychology and there's this more positive feeling about the industry.

I think 2011 will be stronger than 2010 in the smaller market, you know, the one-off, two-off small portfolio market because the changed psychology from what I'm hearing is bringing higher quality properties in small portfolios back in the market like we saw in 2006 and 2007. So, that will kind of feed on itself and I see a better non-REIT market, a better year than 2010. The REITs are still going to acquire, I just don't expect them doing the same volume in the remainder of the year.

Alan Plush: I would agree with that, Steve. I don't know as I look back at my forecasting abilities to mid to late 2010 that I saw nearly this much coming, so I don't know that I'm a good one to answer the question in general. But I would agree.

I talked to the senior folks at the various REITs; their expectation is that there's a lot more – a lot of consolidation left to happen, a lot of transactions left to come. But again, I'm not seeing how many other Atria and Genesis and ManorCare there are out there to be taken down.

But, you know, I'm surprised on a periodic basis, so I'm just kind of all eyes and all ears. I think that the capital markets and the REITs are positioned to do more and either they or as we slowly make our way out as a whole from the recession, maybe other groups enter the fray and there's more activity through that.

So – but I would agree with Steve. I think we see a lot of smaller transactions being done and not so much always. I mean, there's a fair amount of them are going to the non-big three REITs but there's also just a lot more general activity with, you know, financing, re-financing of those small- to mid-size groups of assets.

Jerry Doctrow: Right, and with that Operator, why don't we open it up for questions from our audience?

Operator: Certainly. At this time, I'd like to remind everyone, in order to ask a question, press star and then the number one on your telephone keypad. We'll pause for just a moment to compile the Q&A roster.

Once again, that's star one on your telephone keypad.

There are currently no questions in the queue. I turn the call back over to the presenters.

Jerry Doctrow: I have a couple more items. – We've sort of touched on this but I wanted to come back and asked you specifically, do you think the REITs are stretching the cap rates too much, stretching the per bed prices too much, particularly as we focus on some of these big deals or are you comfortable they got reasonable value and sort of paid up for the right ally?

Alan Plush: I would answer that by going through Steve's Genesis example and it's almost like betting against the Fed, you know you don't want to do it, and I know there are some pretty bright folks there at the time of Genesis exactly as you said, Steve. And even now, some of these transactions seem very frothy but in the long term, you know, it worked for Genesis.

I mean, even Atria; remember when Lazard bought Atria, it was the same type of situation. So, I'll let Steve take the bulk of the answer on that.

Steve Monroe: Well, I would only add that – Alan earlier said that, he doesn't really look per bed and per unit as much as cap rate and cash flow, and that's true. We don't really talk per bed and per unit, and so these high, $130,000 and $135,000 per bed SNF deals for big portfolios, I mean, that's a big number.

And I guess I continue to come back to that the building, the real estate, is not is not really worth that. The cap is coming from operations and management. Management has done a great job in doing what they're doing and while the cap rates were aggressive, the per bed announced price were certainly way above market and if they falter on operations, what's the likelihood of reselling those assets.

You know, we're talking about breakup value of a public company. Well, what happens if you've got the breakup one of these things because of a problem, then we'll trade at a $65,000 bed or less if there's a problem. And that's what I think people have to keep in mind but I think – and I'll go back again, those are unique transactions and unique platforms.

Jerry Doctrow: We are just entering the first quarter earnings season for senior housing particularly, any feel for –how are you guys feeling about just the senior housing markets based on fundamental occupancy and rate, in first quarter specifically, even of course across 2011? Steve, going back to you, do you want to start with that?

Steve Monroe: You know, our April SeniorCare Investor just came out and one of the headlines in our recent newsletter issue was about the fourth quarter, the industry is performing on the senior housing side and it's performing pretty well; profits are all up and all that. I still am surprised that occupancy – I was expecting bigger increases in occupancy and maybe I'm always the optimist but it's still been a little on the slow side to get up.

And that's where some of the REIT industry, you had the deals; they're in there obviously for long term and over the long term, you know you're going to see much bigger occupancy increases but I think the operators concentrated so much on cost control that the money and the cash flows is coming in, I just still think occupancy is coming more slowly than I would have expected, rising a little bit but not uniformly across the board.

Alan Plush: And I would echo all of that, Steve. I'm happy when I look at past downturns and how the industry has weathered this on an occupancy and margin basis, and because I don't think we saw a huge overhang of new development leading into this that we had in prior downturn. So, I'm still optimistic and I haven't seen a huge wave of new development, we're seeing, you know, a fair amount of activity but nothing on the scale of what preceded the prior downturns.

So, I'm kind of cautiously optimistic and I think it's ultimately going to be employment and housing recovery driven as to housing we see and even more as I like to phrase that, I like to use a positive rate of climb and until we see a little more positive rate of climb in those, I think we're going to have to see some macro improvement.

Jerry Doctrow: I think one of the things that our friends at NIC often look a little bit more under the hood and get away from the averages because I think, some of the data we're looking on the NIC side makes the same things you have. It has A-quality assets performing better than any of the others that are just way underperforming and so the averages may not totally reflect what's really going on out there but that's something where we need some more digging.

Alan Plush: And Jerry, I could just add that from our present prices, I absolutely agree with that. For example, the industry is at 88 percent average occupancy but I see individual market areas where the average occupancy is 95 to 97 for all of the comparables.

So, in that case you're right that when you mix up all senior housing you may not get an accurate picture of the market. You can plug ASHA (American Seniors Housing Association) a little bit too. I think when the State of Seniors

Housing report comes up this year, I think that'd be about a sample size of 1,400 properties, and I think you will see a more select group of properties that will probably show stronger operating results.

Jerry Doctrow: Operator, any questions that popped in yet from our audience?

Operator: Currently, there are no questions in the queue.

Jerry Doctrow: OK, I think last one for me and then we'll wrap up. If there's only one thing I worry about in this business, it would be the potential for a higher level of new construction on the senior housing side, the threat of new construction really popping. Alan, you talked a little bit about bank money getting a little bit more available and we're certainly hearing private operators feel good enough about the business to think about new construction again. Is a pop in senior housing construction levels over the next year or two something we should be worrying about or will it still remain under control?

Alan Plush: I don’t see it as being a huge threat. I think the money right now is flowing primarily to existing developer operators with a strong track record and if you kind of listen to my definition, you'll realize how narrow the group is, with a strong track record that have the ability to attract equity, that have found a site that’s in a strong market.

And I think when you start – you know, the big national (multis) are not really doing a lot of new developments to speak of. So, it's really a pretty small component of what's going on and so I don’t see it as being a huge threat at least over the next couple-of-year period.

Steve Monroe: And I would agree with that. The difference today compared to the past is in the past, it was a real shotgun approach with new development and yes, they also did due diligence and all that but I think the new construction today is so much more targeted to a specific market and a specific price point that the lenders have to be very comfortable with that that it's not going to be a problem. I mean, take the private company like Legend Senior Living. I think it was the first half of the recession, they opened up a new property in Florida that was filled in six weeks; six weeks, not six months, not 18 months; six weeks and you know, they target their market and they knew that it was going to do that.

Alan Plush: And they continue to have pretty good success, I mean, not all that level but that in particular and that's a perfect example, so you're right, what's going on; I mean, they've continue to select markets that have given very strong performance.

Steve Monroe: Oh, I'm sorry, that one was in Oklahoma that is owned, the one in Florida I think took two or three months; you know, not the 18 months...

Alan Plush: That was the slow one.

Steve Monroe: That was the slow one but if you target the right location at the right price point and you're smart about it, you know, it s not causing a problem. It caused problems for the competitors but the developer was very successful.

Jerry Doctrow: And I think we're just about out of time, any other last thoughts that either one of you want to provide?

Steve Monroe: Alan, why don't you go first?

Alan Plush: Oh, well, thanks, Steve. No, I have had a pretty good opportunity here. I think – and Steve always enjoyed speaking with you on this – on this topic. I maintain and I continue to maintain that I think that the worse is behind us for the industry, I think I see a nice kind of slow stable period for the next couple of years, and I think that's going to be reflected in valuations and investor interests in this space.

I've always been a big proponent of this space and there are a lot of folks out there that do a very good job. At the end of the day, you have to remember, it's all about people, it's all about caring for seniors and you know, I never – I never liked to forget the fact that none of the economics work unless you have a dedicated group of providers that really believe in the industry.

Steve Monroe: And I agree with that and I might just add that one of the reasons why we are not seeing a big uptick in senior housing occupancy as the example is because we didn't see the big downtick what the other sectors had. So, there's not a whole lot to come up from, so – and its here, that's why investors like the other sectors because they really lost their shirts and are coming off the bottom.

This sector did not lose their shirts; we're off a few hundred basis points on occupancy but we're still cash flow positive. So, that's why there's a little bit slower turnaround because it just never go that bad.

Alan Plush: Absolutely.

Jerry Doctrow: And with that, well wrap up. Steve and Alan, again, thank you for the time and the insights. There's going to be a replay available and thanks for joining us again.

Steve Monroe: Thank you, Jerry.

Alan Plush: Yes, thanks a lot, Jerry.

Operator: This concludes today's conference call. You may now disconnect.

END