Westpac

Mr Chris Barton

National Manager Health Sector, Westpac

Medical Property Development - Concurrent Workshop Repeated

Sunday, 12 June 2011	Start 8:30am	Duration: 50mins	Sovereign
	Start 9:25am	Duration: 50mins	Sovereign

Medical Property Development

GP CME Conference 2011

(Image sourced from Vital Healthcare Property Trust website “Eastmed Medical Centre”. June 2011.)

Your Presenters Today

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Director | Clinical Design Consultant
The Health Planner Limited

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National Health Sector Manager
Westpac NZ Limited

Overview

This workshop is structured to give a high level overview of quick tips and tricks if you are considering an IFHC or medical property development project.

Idea	What do you want to create
What	Develop and articulate high level principles of MoC
Localities	Work out who are the key players in your area
Motivation	What drives you and your potential shareholders
Process	Understand the planning process
Team	Carefully select your project team
Financially viable	Assess the financial feasibility of a project
Construction risk	Tips for managing a project
Resources	What resources are available to assist you

Idea

Start the process of developing a vision by:

- Determining what services you want to deliver
- Work out how you how you want to deliver these service
- Work out where you want to deliver these services
- Decide out of what you want to deliver these services

What is an IFHC

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“The development of centres will provide the physical space required to support the delivery of the Government’s priority for Better, Sooner, More Convenient health care in the community and are the key physical infrastructure to enable a generational change in the health system.” (Ministry of Health, 2010).

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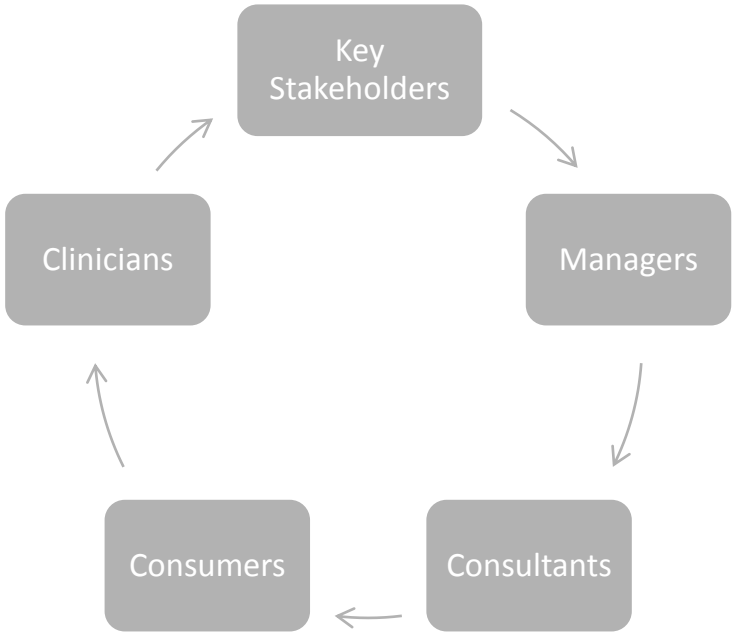
Localities

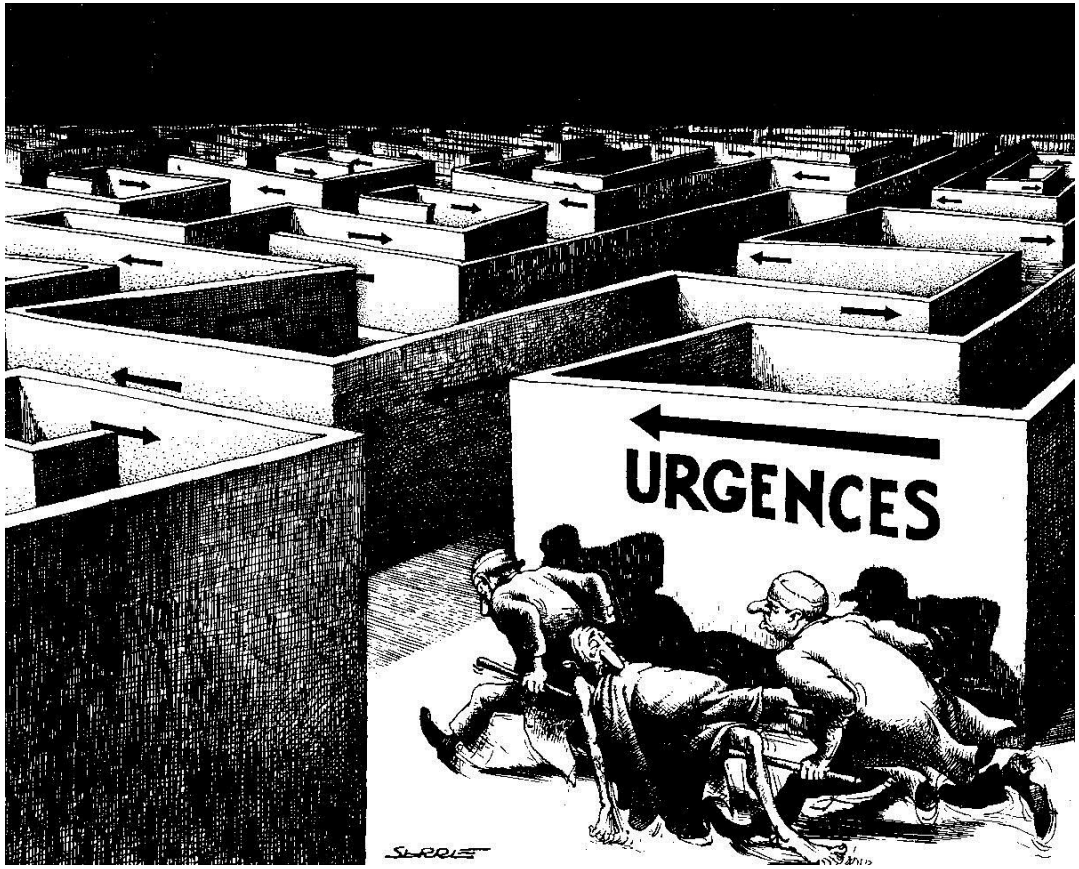
- Strategic intent of the DHB
- Who are the key players in your area
- What are other primary care practices planning in the area
- Do you have GPs with specialist interest in your area
- Strategic alliances
- What building stock is available and at what cost

Project Team

Core Team

- Carefully select and hand pick your team
- The team should include key stakeholders
- Small and diverse
- Expand to take on new temporary members as required
- Team members attributes




URGENCES

Motivation

- What return are you looking for on your investment in this project?
- How much risk are you taking on, and what is the appropriate return?

Increase the value of my practice

Make my practice easier to sell

Increase the profits from my practice

- Retain and grow patients
- Create economy of scale
- Create referral networks

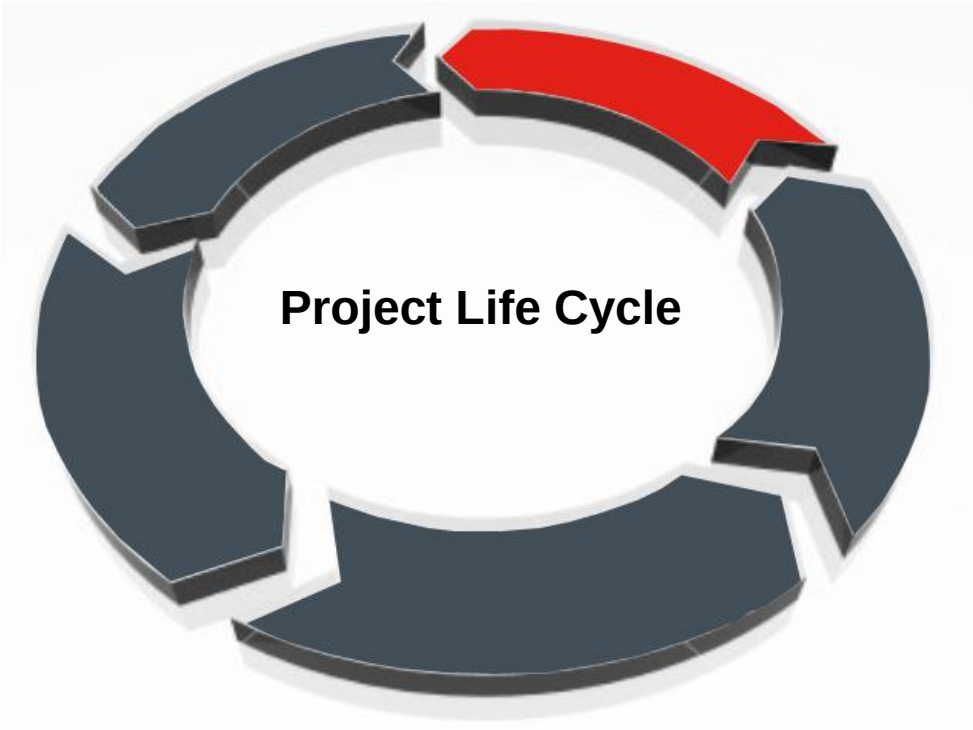
- Better Sooner More Convenient healthcare
- Improve services for patients
- Clinical networks
- Professional development

- Profit on the property upon completion
- An attractive income stream e.g. return on investment
- A capital gain on sale

Project Life Cycle

Strategic Business Case

- MoC priorities / outcomes
- Facilities options
- Workforce / IT impacts
- Potential new services



Project Life Cycle

GO / NO GO Decision

Strategic Business Case

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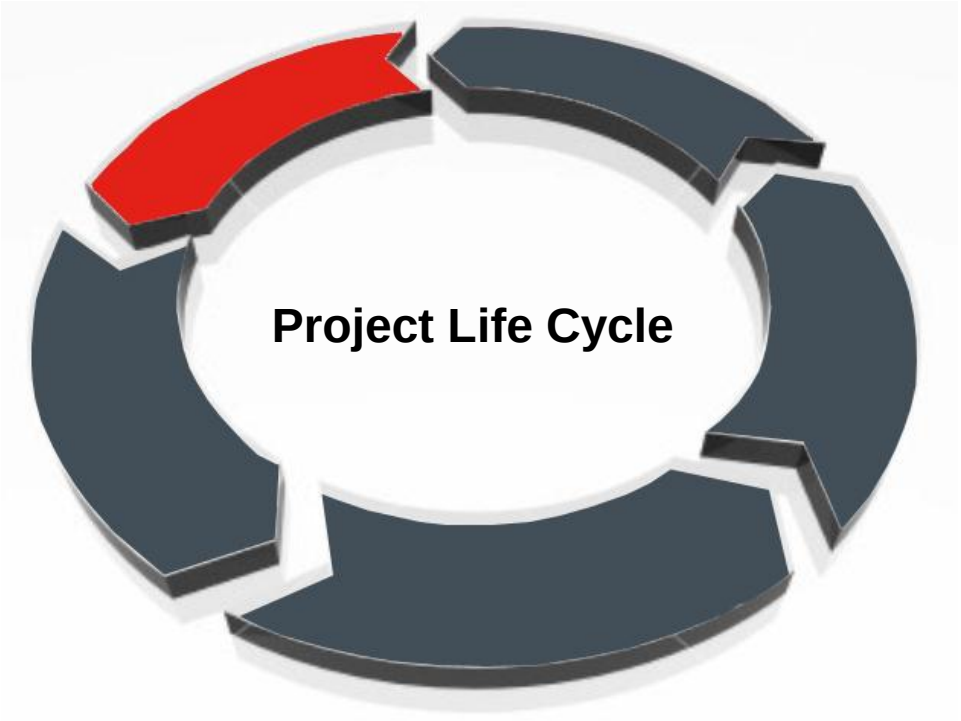
- Financial parameters



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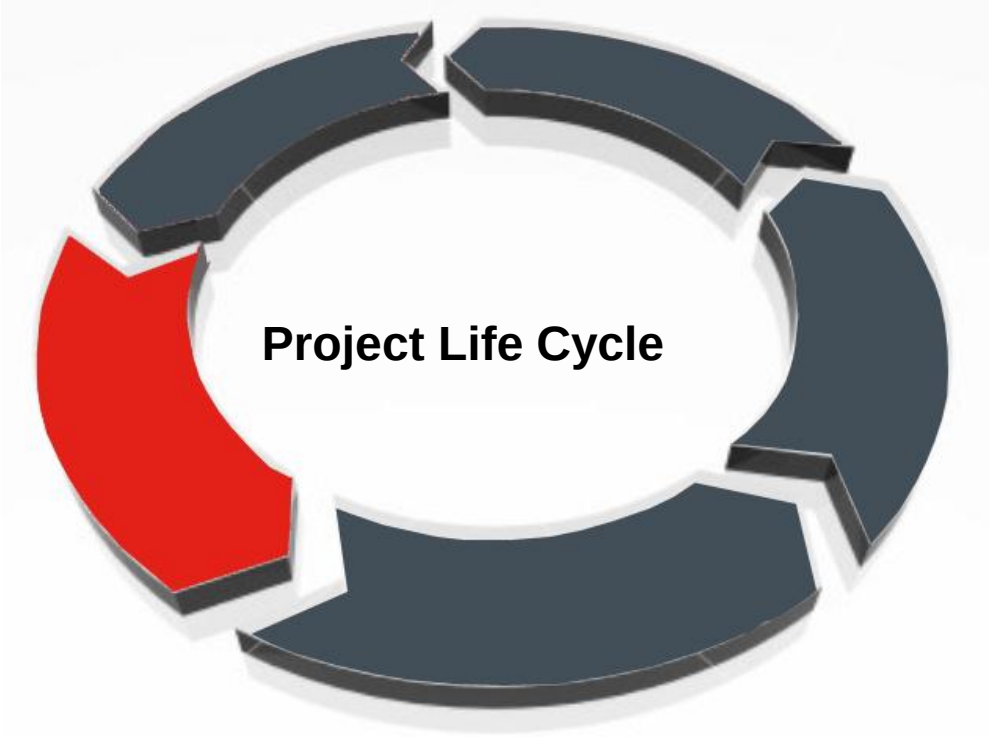

Detailed Options Analysis

- MoC and revenue options
- Workforce development
- Facilities site and scope
- Infrastructure required
- Decide preferred options
- Financial options

Project Life Cycle

GO / NO GO Decision

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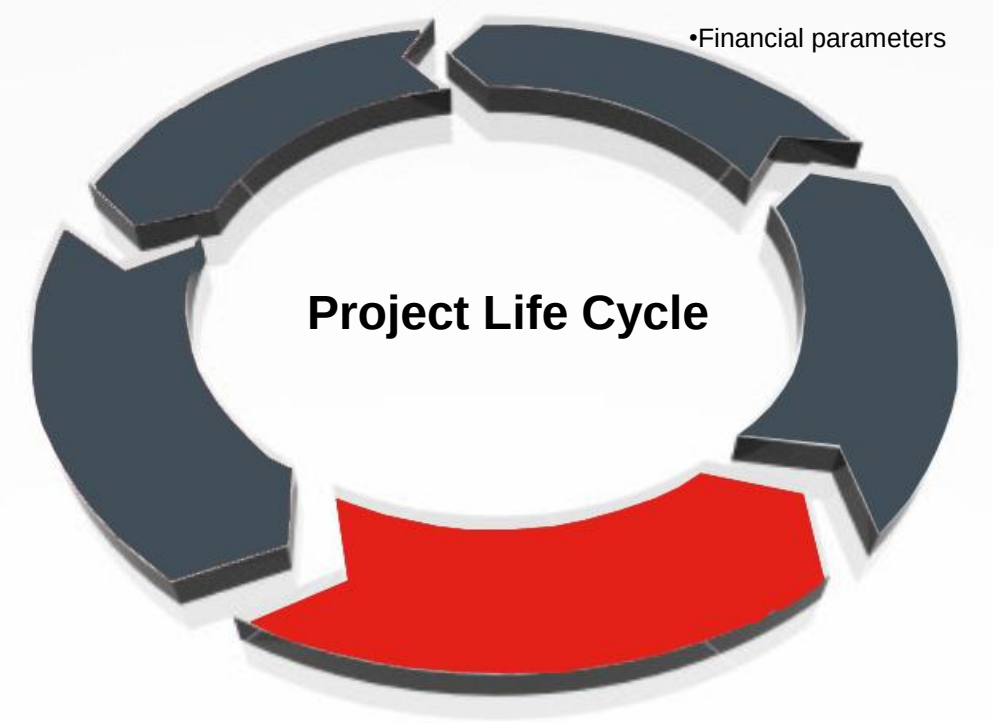

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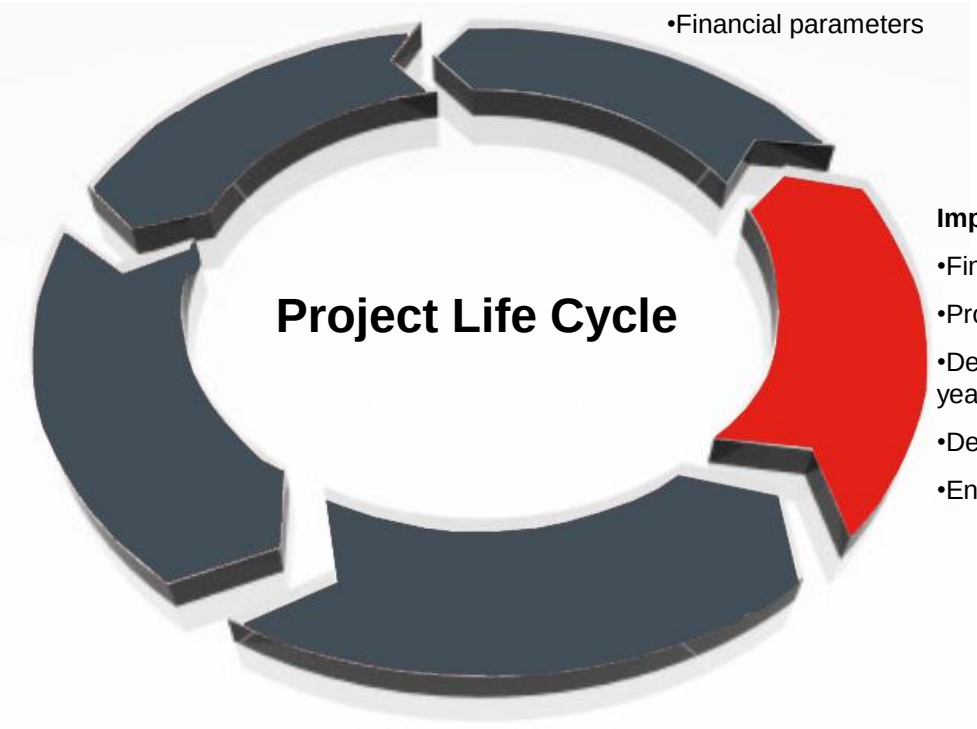

Implementation Plan

- Finalise MoC
- Provider contracts and agreements
- Determine priority actions 12 months – 3 years
- Design and develop facility
- Engage workforce

Detailed Options Analysis

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- Workforce development
- Facilities site and scope
- Infrastructure required
- Decide preferred option
- Financial options

GO / NO GO Decision

Financial Snapshot

How do you decide if a property development project will be financially viable ?

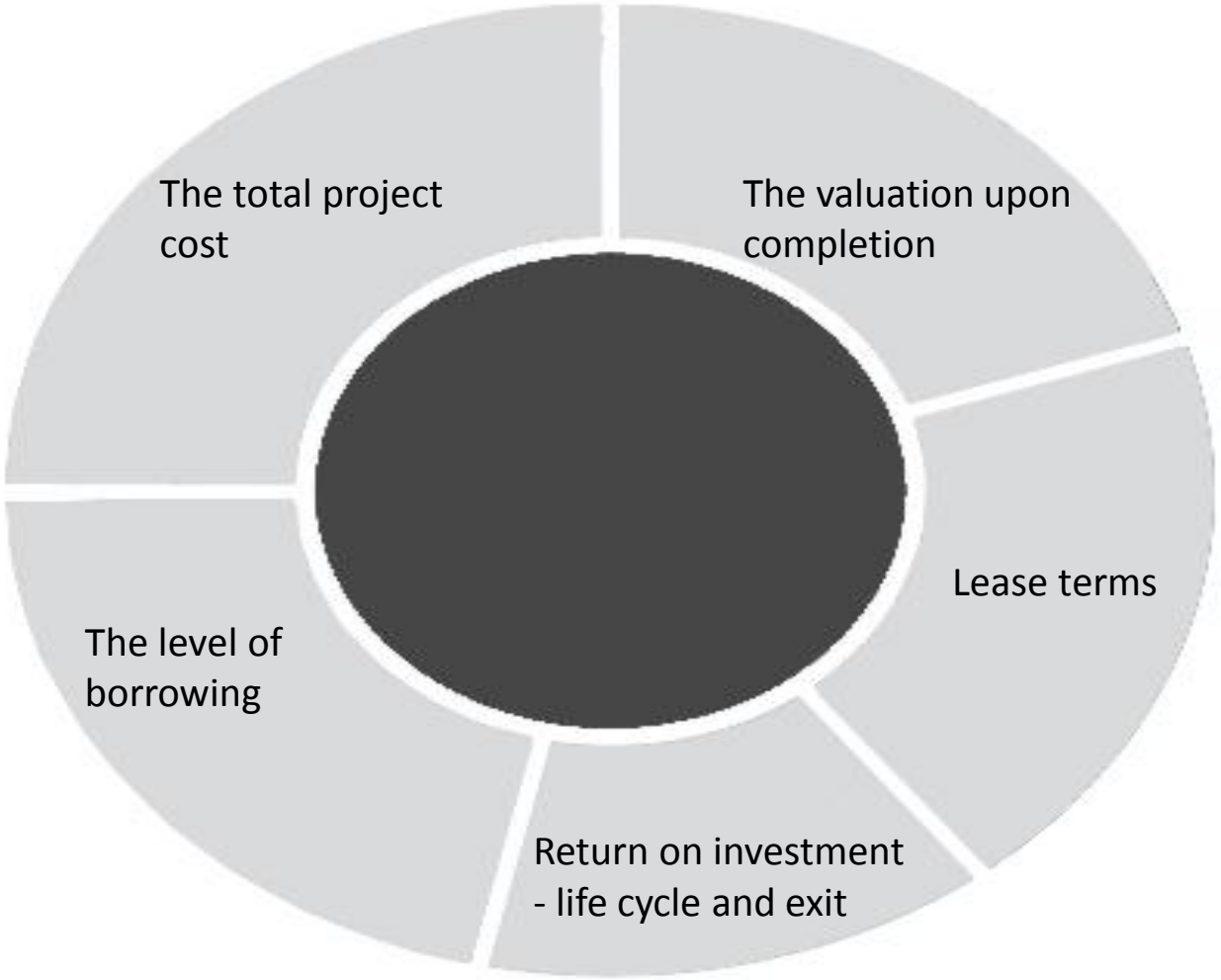
Financial Scorecard

- The property is valued at more than Total Project Cost to reward investors for the risk
- The property is fully leased on market terms with scope for future uplift in value
- The lease income can comfortably service the borrowing
- The annual cash surplus is sufficient to meet shareholder dividend expectations
- The level of borrowing allows for future revaluation / devaluation or future capital requirements
- The property could be sold easily at a profit

Financial Scorecard – Medical

- As an owner occupier, the practice profitability compensates for lack of profit on the development
- As an owner occupier, the shares in the practice increase in value or liquidity

Financial Feasibility



Total Project Cost - Budget

A quantity surveyor ("QS") is the best source of advice for estimating total project cost.

Land
- Acquisition cost, legal, real estate, valuation, holding costs
- Market rates

Contingency
5% to 10% of construction cost

Council fees
Resource consent, building consent, development contributions

Construction
- Siteworks, carparking, base build, hard fitout, soft fitout
- Market rates

Professional fees
- Architect, health planners, engineers, traffic management, design consultant, QS, project manager, legal, finance

Capitalised interest
6 to 18 months build time

Total Project Cost - Examples

Building Cost per SQM	Auck	Wgtn	Chch	Dun
Group practice surgery.	$1800-$2000	$1750-$1950	$1725-1925	$1650-1850
Private hospital. 40 bed. Ex-aircon. Op Theatre.	$2700-$3000	$2600-$2900	$2650-2950	$2600-2900

Source: Rawlinson QS Construction Handbook 2010

Case Study Scenarios	Low rent 65% LVR ($000)	100% debt ($000)	High rent 65% LVR ($000)
Land (2,400 sqm) *Per sqm*	$1,085 $452 per sqm	$1,085 $452 per sqm	$960 $400 per sqm
Construction (750smq floor plan) *Per sqm*	$1,725 *$2,300 per sqm*	$1,725 *$2,300 per sqm*	$1,500 *2,000 per sqm*
Professional	$225	$225	$225
Council (10% of land)	$109	$109	$96
Contingency (10% of cost)	$173	$173	$150
Capitalised Interest	$75	$120	$86
Total Project Cost	**$3,391**	**$3,436**	**$3,017**

Valuation

The value of a commercial property will generally be determined by how much investors will pay for the quality of the future lease income, and the potential for capital gain.

Capitalisation of Earnings or "Cap Rate"

- What the market has paid for similar income streams / properties
- A low cap rate indicates low risk, higher demand and higher value
- A higher cap rate indicates more risk, less demand, and lower value

- Medical property valued at approx 8% - 9% capitalisation rate
- Medical property historically sold for approx 7% - 8.5% yield

Case Study Scenarios	Low rent 65% LVR ($000)	100% debt ($000)	High rent 65% LVR ($000)
Lease Income (750 sqm) *Per sqm*	$280 *$373 per sqm*	$321 *$428 per sqm*	$321 *$428 per sqm*
Capitalisation Rate	8.5%	9.0%	*8.5%*
Valuation Upon Completion	**$3,291**	**$3,567**	**$3,776**
Total Project Cost	**$3,391**	**$3,436**	**$3,017**
Profit	**-(100)**	**+130**	**+760**

Valuation

Cap Rate Influencers

Market forces and **economic conditions**
will dictate required returns for investors e.g. surplus commercial space (supply), tenancy default risk

Recent **sale prices / yields** of comparable properties

Lease terms
longer term with regular rent reviews increases value

Quality of tenant
government, blue chip, medical are stable, low risk tenancies

At market
above market rental dilutes future capital gain so value is lower

Location, building condition

Below market
depending on lease expiry can increase or decrease value

Market Evidence

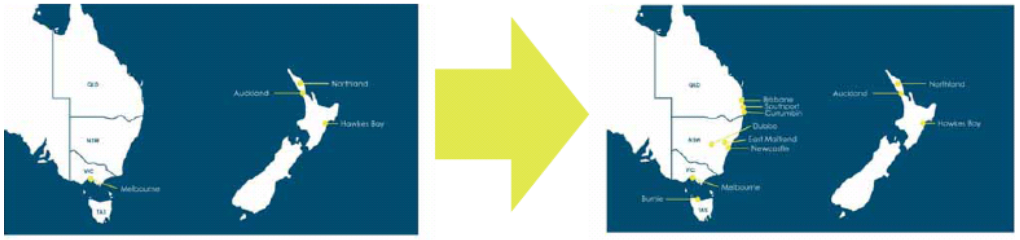
(Sourced from Vital Healthcare Property Trust, Kiwi Income Property Trust, Goodman Property Trust, and AMP Property Trust websites 2010 / 2011 reports.)

Vital

Healthcare Property Trust

PORTFOLIO PROFILE

	VHP Existing	Acquired Properties	VHP Expanded
Number of properties	13	12	25
Investment properties	$300.6m	$216.9m	$517.5m
WALT (years)	8.4	15.4	11.5
WACR	8.7%	10.1%	9.3%
Occupancy	98.2%	99.9%	99.2%
5 year lease expiry	29.6%	5.0%	18.1%



KIWI INCOME PROPERTY TRUST

Operational performance

WALT	Occupancy
4.0 yrs	97.1%
2010 4.3 yrs	2010 97.0%

Goodman

AMP NZ OFFICE

Occupancy increased to 92%

Strong balance sheet 23% gearing

WALT (years)	4.6 yrs

highlights+

Debt as a percentage of property assets[1,2]	Weighted average lease term	Occupancy across the portfolio
37.0%	5.5 years	95%

Lease Considerations

The lease terms have a major impact on valuation and project feasibility so consult a registered valuer or leasing specialist for advice on current market rentals.

Rental Income

- Per sqm rates depend on location, demand, building quality, tenant feasibility
- Ensure that lease assumptions are at market
- Property management / maintenance / occupancy costs
- Carparks included?
- Common areas included for all tenants

Tenancy Mix

- The clinical model of care critical to create demand from tenants
- Referral tenancy rates often higher eg pharmacy, pathology, specialist , radiology

Basic Lease Considerations

- Use the latest Auckland District Law Society Format
- Term should be for at least 5 years
- Termination clauses - related party leases
- Assignment

Level of Borrowing

The level of gearing impacts the risk and investment profile of the project

Vested interest
Gain share / pain share: Do shareholders have skin in the game?

How do you subsidise shortfall in market lease?
- Are equity top ups tax efficient?
- Can all shareholders meet their obligations?

Fluctuating property values, construction costs or future investment
Is there a safety net to protect against shifting asset values and potential changes in shareholder circumstances?

The impact of creditor disputes and meeting solvency test
- Does your property company pass the solvency test?
- Think about legal costs in resolving disputes

Volatility of interest rates
High gearing magnifies interest rate increases

Liquidity - the impact on selling the property or shares in the property
A property company with a lease that services its debt can provide more options if you need to sell e.g. better liquidity

Is it financially viable?

Case Study Scenarios	Low rent 65% LVR ($000)	100% debt ($000)	High rent 65% LVR ($000)
Total Project Cost	$3,391	$3,436	$3,017
Valuation Upon Completion	$3,291 (8.5% CR)	$3,567 (9.0% CR)	$3,776 (8.5% CR)
Development Profit	**-(100)**	**+130 (4%)**	**+760 (25%)**
Equity	**$1,252 (35% value)**	**$0**	**$562 (35% value)**
Lease Income (750 sqm)	$280	$321	$321
Debt servicing	$150	$464	$172
Net cashflow	**$91**	**-($167)**	**$104**
5 year cashflow	$398	-($807)	$456
5 year gain on revaluation / sale	$171	$424	$1,071
Total return	**$569**	**-($382)**	**$1,527**
Return on Investment	17%	-(11%)	51%
Annual Return on Investment	**3%**	**-(2%)**	**10%**

Best Practice

- Processes are often habitual and ritualistic, they have usually evolved to accommodate the needs of the superceded environment
- Research
- Re evaluate, explore, visit other facilities, look for improvement & pitfalls
- Talk to anyone and everyone
- Ensure the new environment facilitates best practice

Resources

- MoH Implementation Support Groups (ISG)
- DHB
- PHO
- Regional Networks
- GPSI and NSI
- Primary and secondary colleagues
- Your project team
- Anybody who has done this before
- The Consultants - Architects, Health Planners, Project Managers, QS, Bank
- Everybody who works in your facility – the frame and lenses are different