

## A Healthcare Real Estate Professional's Perspective on the Medical Office Building Market

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Location, location, location. This steadfast retail mantra applies equally well to the medical office building (MOB) segment of the real estate market. All across the country, in the face of anemic occupancy rates, rents, and new development in the traditional office building segment of the real estate market, newer well-located MOB's continue to attract physicians and clinics. While the traditional office vacancy rate in the Puget Sound region hovers around 20 percent (about the same as the national vacancy rate) the MOB vacancy rate sits at a healthy six percent, compared to 12% nationally. The investment community is taking a hard look at these numbers--any real estate segment in a growth cycle gives the promise of healthy returns. The CB Rich-

ard Ellis Healthcare Capital Markets Group conducted a survey of MOB investors and developers in early 2010. Approximately 70% of the respondents said that they would be buying MOB's in 2010. In addition, 88% were looking for MOB's priced above \$10 million—the target range for newer, Class A, on-campus buildings.

high quality MOB's and, the ramifications for healthcare providers in the state of Washington:

### **Healthcare Reform**

Healthcare legislation passed by the United States Congress in March is feeding the appetite for an already robust product. Real estate professionals involved in the medical office market believe

this legislation will amplify an already growing industry. An increase in the number of insured patients should translate into more demand for MOB space. Clinics and other hospital-dependent entities are realizing the strength in the co-location of facilities as they position themselves to serve a growing community of patients. Consolidation should increase the demand for larger office spaces near hospitals, which often can be accommodated only in new buildings.



### **Overlake Medical Pavilion, projected completion date of September, 2011**

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Let's review the main factors that are contributing to the interest in

### **Limited Supply**

In the Puget Sound region, medi-

cal office development is experiencing a modest boom. There are currently 3.5 million square feet of public and private projects under construction or in the final stages of development. The majority of these projects are expansions on or adjacent to existing medical campuses. However, these new developments are not enough to keep pace with the demand, and the number of available sites on which to build new MOB's with immediate adjacency to a hospital, particularly in dense urban areas, is limited. This scenario will likely continue to keep vacancy rates low.

Healthcare Realty, a national real estate investment trust ("REIT") that integrates owning, managing and developing properties associated with the delivery of healthcare services, is an example of a firm believer in the growth potential in this region. They are currently developing the Overlake Medical Pavilion, a nine-story, 190,000-SF MOB on the campus of Overlake Hospital Medical Center in the Seattle suburb of Bellevue, Washington.

"We're very bullish on the Puget Sound (Seattle area) in general, but definitely Bellevue and the Overlake Hospital campus," states Amy Poley, Vice President of Real Estate Investments at Healthcare Realty.

### Quality Matters

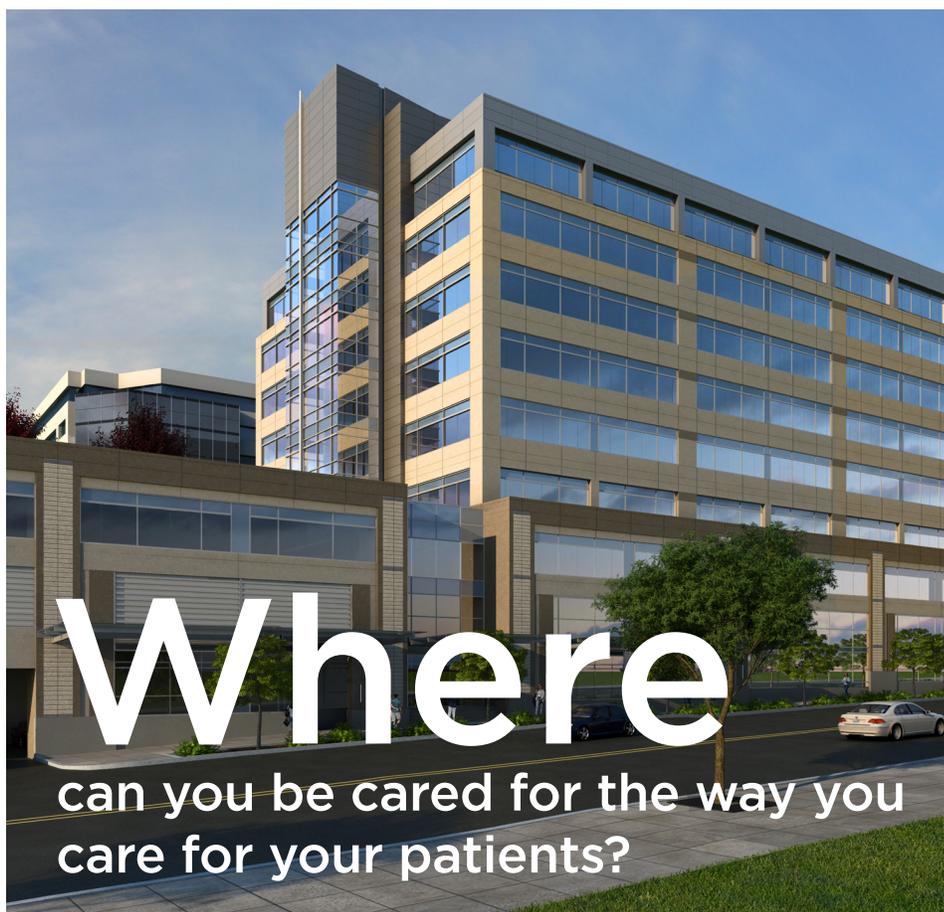
It may seem counterintuitive, but many clinics and physicians are choosing to pay more rent in a declining reimbursement environment. Many clinics are seeking a competitive advantage by locating in buildings that fit several criteria: on or directly adjacent to a hospital, built within the last few

years, and preferably "green." The reasoning is this: locations on hospital campuses improve referrals, a better image improves retention of patients and providers, new designs improve efficiency, and green features enhance the experience of patients as well as staff. April's issue of the American Medical News points out that "the nation will likely see a shortage of about 160,000 physicians by 2025." As clinics look ahead to the anticipated shortage, they know that a high

quality working environment is an important recruiting tool. Competing for patients means having such amenities as convenient parking, plenty of elevators, well-designed lobbies, and extras such as garden spaces. Clinics are calculating that additional revenue opportunities available in these locations outweigh the additional cost of rent.

### Conclusion

Class A MOB's will continue to be attractive to investors and medical



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tenants in the long term. The good news is that the benefits associated with locating in a new MOB will likely improve the experiences of staff and patients alike and allow for enhanced revenue to address both costs and declining reimbursements. The bad news for ten-

ants is that rental rates will likely either hold steady or increase (depending on the localized market). *Paul Carr is a First Vice President with CB Richard Ellis, focusing on investment sales and leasing transactions within the healthcare sector of commercial real estate.*

*As a member of CBRE's National healthcare services team, Carr advises physician groups, hospitals and investors on various leasing, acquisition and disposition requirements. He can be reached at paul.carr@cbre.com or 206-292-6005.*

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