



NET LEASE REPORT March 2018

MEDICAL SECTOR

Savvy net lease investors have their eyes on the medical sector. No wonder. First, there is the inherent stability typically associated with medical tenants. Investments in specialized equipment, large build-out costs, long-term leases and strong demand for services further contribute to that stability.

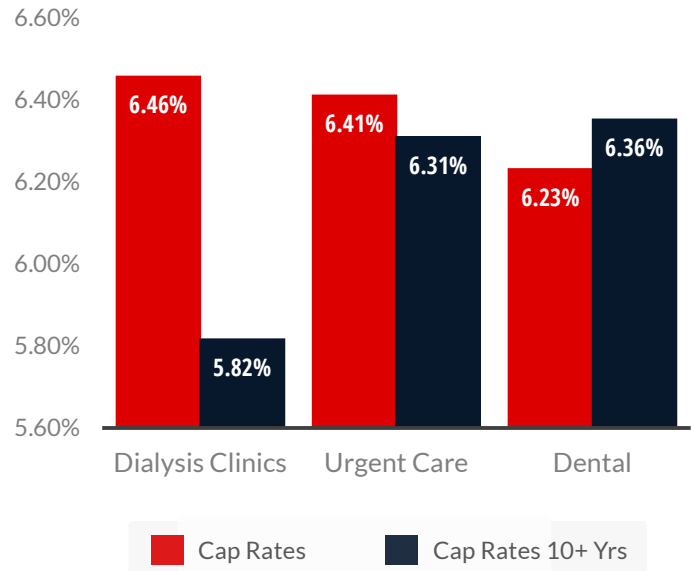
Second, since medical care, in general, requires face-to-face interaction between patient and physician, something online vendors cannot provide, the sector is resistant to web-based competition, and so is positioned well for the growth in demand for services as the average age of the US population continues to grow. As a result of these drivers, medical net lease represents a prime opportunity for investors.

In terms of asset types, the medical sector in net lease is comprised of dialysis centers, dental offices and minute clinic/urgent-care locations. Dental offices and clinics are a fragmented portion of this market, consisting of smaller tenants. By contrast, the dialysis portion of the sector is dominated by two large tenants: DaVita and Fresenius, and they account for the largest portion of the overall market share in the sector.

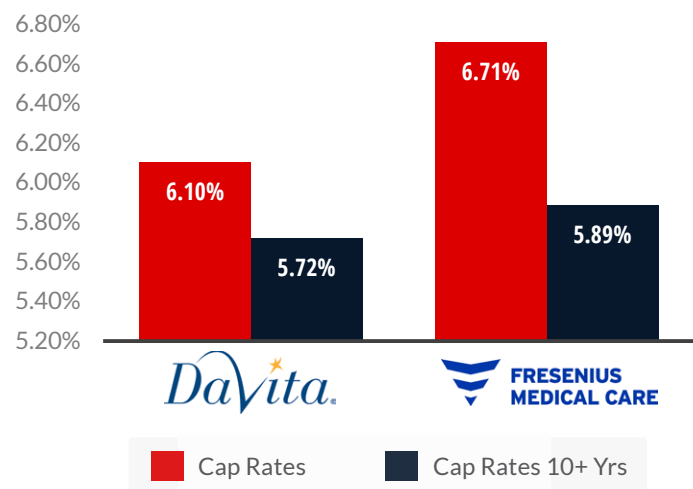
These two dialysis tenants have remained attractive investments because of their strong returns as well as all of the above-mentioned market benefits. The leases typically have increases built in, creating a hedge against inflation. In addition, the dialysis centers tend to trade at cap rates higher than properties of similar credit ratings.

Fresenius is investment-grade credit while DaVita is just two ratings below the threshold for investment-grade. Both levels of credit off investors a strong guarantee behind the leases, however, we would expect this difference in credit rating to result in Fresenius trading at lower cap rates, the opposite has occurred over the last 12 months. DaVita had slightly more lease years remaining (0.8 years) than Fresenius and more sales occurred in California, a region known for a high demand for properties.

Cap Rates From the Past 12 Months



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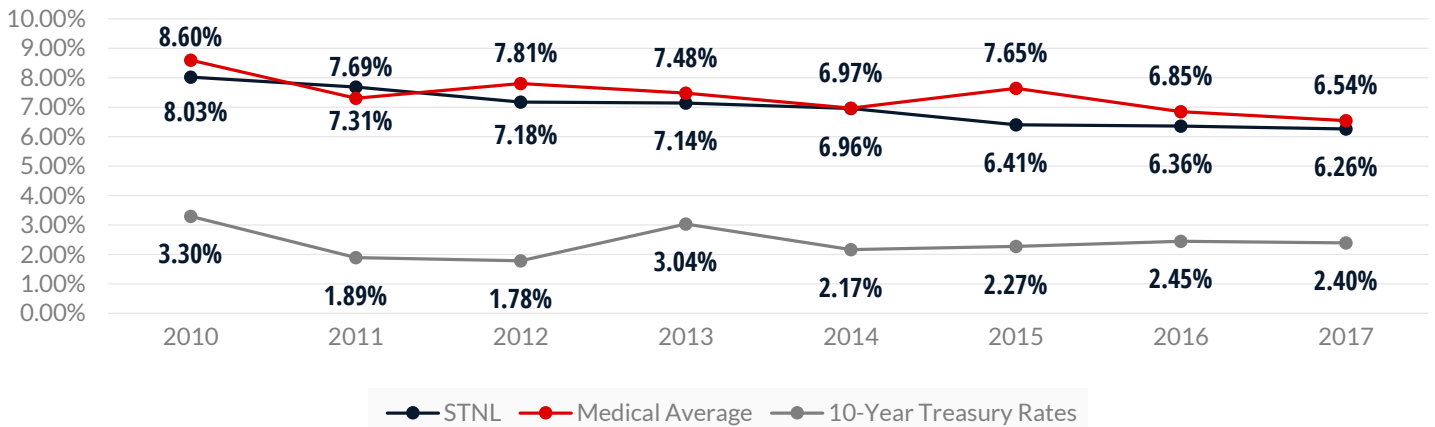
This high demand has led to lower cap rates in the state of California when compared to the rest of the country.

Credit Ratings	S&P	Moody's
	BB	Ba2
	BBB-	Baa3



There is also a strategic, locational benefit to dialysis centers, which are typically situated near hospitals and doctors' offices. This, obviously, provides convenient access to the service, providing a synergy that is beneficial to both the clinic and patients.

STNL Cap Rates vs. Medical Sector Average vs. 10-Year Treasury Rates



Over the last five years, the medical sector has averaged a 50-bp discount to the single-tenant net lease average. This provides investors returns greater than other net lease investments.

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DISCLOSURES: As part of our market research, we collect sales price, cap rate, and lease years remaining for all publicly advertised and sold STNL properties. a) We are not able to capture 100% of the off-market transactions that occur; however the nature of off-market typically limits their value as true market comps. b) Sources include public records, sales announcements, Calkain sales, and appraiser obtained sales amongst others. c) Our collection process, while thorough, is not all encompassing and there may be biases in the data as it relates to geography, tenancy, or brokers involved in the transaction. d) Public records often lag behind when transactions actually close, months in some cases. Consequently the data supplied here for any given quarter is likely to miss a material amount of transactions that actually closed in it.