



Demographics support the investment case for senior housing

A Q&A with Julie Robinson, managing director and head of healthcare with Clarion Partners

As baby boomers age, what are their primary considerations when considering a move into a senior housing community?

Senior housing communities provide healthcare and hospitality services to the elderly based on their required level of care, with the typical market segmentation falling into three categories: independent living, assisted living and memory care. Demand for independent living is typically more discretionary and strongly influenced by the health of the broader economy and housing market. Demand for assisted living and memory care is typically driven by an immediate need, usually prompted by an event-driven occurrence, such as a fall, declining memory, or poor diet or health, resulting in the need for assistance with activities of daily living.

Senior housing residents and their families highly value amenities that promote health and wellness, socialization, safety, and programming that helps preserve their independence. As such, facilities with services and amenities including on-site physical and occupational therapy, social activities, housekeeping and laundry services, reliable transportation, and gourmet dining options are likely to outperform. A fully stocked bar is also key.

The opportunity to invest in senior housing has been touted as a "homerun" during the past two decades, but it hasn't always panned out. Is that different now? Why or why not?

The United States has an aging and wealthy population, with the massive baby boomer cohort now having reached the age when the need for assistance with everyday tasks becomes more acute. During the past decade or so, the U.S. senior housing market experienced oversupply driven mostly by overzealous developers erroneously timing the demand – believing seniors move into a community in their mid-70s instead of early 80s. And then within the past five years, specifically, we experienced the two-pronged impact of COVID-19: (1) significant occupancy decline given both the impact and threat of the disease on the frail resident population; and (2) the need to right-size wages to entice the front-line staff to come back to work. In this case, the past is not prologue.

The growth rate for the 80-plus population during the next 10 years is approximately 2.5 times the growth rate for that cohort during the past 10 years. We feel that this demographic

tailwind combined with the slowdown in construction activity will result in a severe demand/supply imbalance (Figure 1), not to mention today's communities have beautiful design features and offer amenity spaces for improved physical and mental health and wellness and socialization – key ingredients to appeal to the baby boomer cohort and, importantly, their adult children.

You mentioned senior housing operators recently right-sizing wages. Are you concerned with labor availability putting more pressure on wages going forward?

Labor availability is and has always been top of mind for everyone, but we should couch the concern with a few relevant facts. First, adult children have typically provided caregiving support for aging parents; however, today's smaller family sizes reduce the number of available caregivers within families. Second, reduced labor availability puts even more pressure on home health costs, making congregate living relatively even more attractive. Third, a strong historical correlation exists between labor cost and rent growth, reflecting the sector's inelastic demand. And, lastly, we can't ignore the rapid advancements in technology particularly as they relate to healthcare that creates an opportunity to relieve the labor cost burden while still providing a living space for socialization and, therefore, improved physical and mental health outcomes. Remote monitoring, UTI detection and fall prevention and detection are great examples of ways to utilize technology to assist with caregiving. Additionally, the anticipated growth in the target market and cost of current alternatives should incentivize even further advancements in medical technology and services aimed at making aging-in-place at a vibrant, amenity-rich senior housing community more cost effective.

Who can afford to live in a senior housing community?

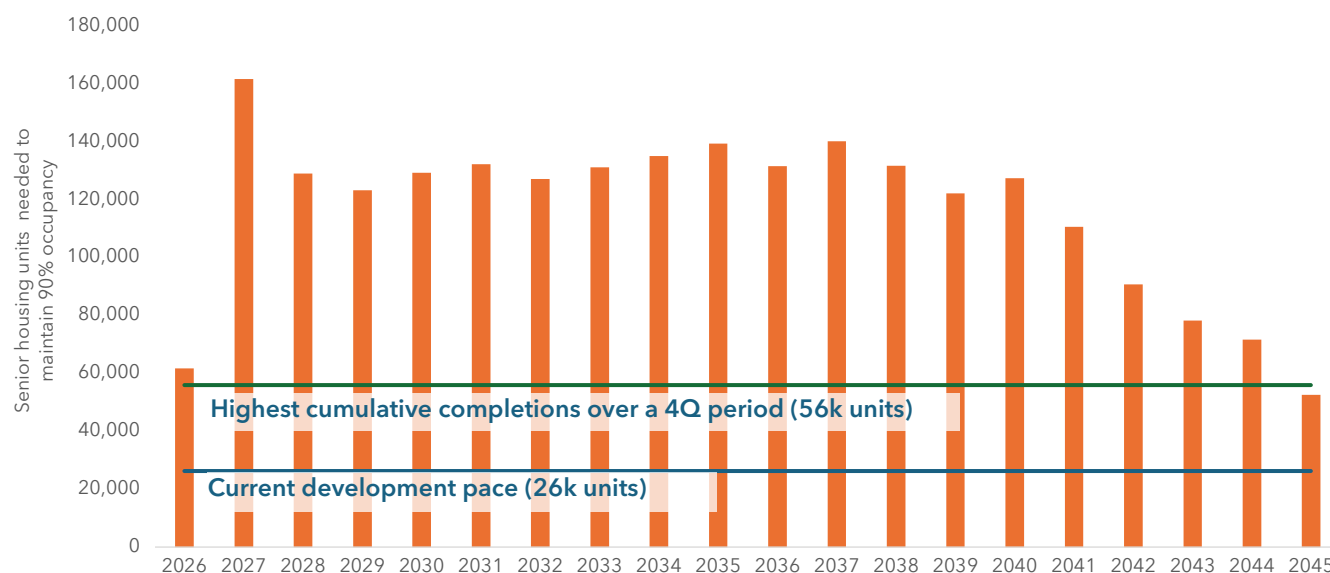
In addition to the sheer size and growth of the 80-plus cohort, today's senior population is wealthier than the senior populations of prior generations, improving the accessibility of senior housing. Fueled by healthy home price and stock market appreciation in recent decades, more than half of baby boomer households have a net worth exceeding \$250,000, making senior housing more accessible to more of the population. Growth in the median net worth for both seniors and their adult children has outpaced the

increase in median net worth across all other age cohorts by a wide margin. The improved wealth of seniors and their adult children should have a direct correlation to both higher uptake of senior housing and the ability to afford higher rental costs. The median net worth of seniors alone (excluding any supplemental assistance from their adult children) can pay for a six-year stay in a senior housing community, nearly three times the typical length of stay. You can also see this affordability component play out in the sector's all-time high product acceptance with more than 1 million occupied units, which is a more than 20 percent increase over the past 10 years. Increased operating efficiencies from the adoption of new technologies, such as wearable devices, robotics and telemedicine, could reduce the cost of senior housing, improving affordability. In addition, the ongoing adoption of value-based care by health insurance plans – and the potential expansion of medical insurance coverage to include senior housing services – is also a potential, longer-term tailwind for senior housing accessibility.

How should this sector fit into capital flows and allocations, going forward?

Senior housing has demonstrated resiliency through multiple economic cycles, delivering long-term outperformance with historical total returns exceeding that of the Expanded NPI by an average of 275 basis points per year during the past 20 years. Notwithstanding the once-in-a-generation impact of the COVID-19 pandemic – causing the sector's underperformance during the past five years – the needs-driven nature of demand in the sector, particularly for the higher-acuity segments, has contributed to not only its historical outperformance but also lower volatility. We expect this sector to outperform as demand is forecast to remain very strong, new supply is significantly muted, and profit margins are improving – driven by rising rental rates exceeding expense growth. The higher operating leverage in the sector will lead to outsized NOI growth, and that, combined with the previously discussed positive factors, will continue to attract new entrants, thus improving valuations over the long term.

Figure 1. Senior housing units needed to maintain 90 percent occupancy for population aged 80-plus



Source: Clarion Partners Investment Research

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