Omaha, Nebraska

Medical Office Market Overview

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CUSHMAN & WAKEFIELD | LUND COMPANY

The Cushman & Wakefield / Lund Company Medical Office Report is produced annually for the benefit of owners, investors, owner-occupants, and tenants of medical office buildings throughout the metropolitan Omaha, NE area. Inventory as referenced in the Report includes traditional medical office buildings, owner-occupied community clinics, ambulatory surgery centers and specialized outpatient treatment facilities. If a property caters to both office and medical uses, at least one-half of building must be occupied by medical users to be included in the inventory.

The Report is prepared by Richard Secor, Jr., Associate, Cushman & Wakefield/Lund Company, a 39-year veteran of the commercial real estate industry and a member of Cushman & Wakefield's Healthcare Advisory Group. The Advisory Group is a national platform of real estate professionals with a focus on the sales, leasing, valuation, management, and financing of healthcare properties around the United States, including medical office, assisted living, skilled nursing, and hospital facilities.

The Economy

All countries, including the United States, continue to be impacted by COVID-19. Just when we thought we had the virus beaten, with the discovery and administration of the various vaccines, the reluctance among many citizens to take the vaccine and resulting mutations such as the Delta Variant and now the Omicron Variant, have prevented our ability to have herd immunity. Consequently, the virus will continue to be around for a while. COVID, to be sure, has redefined how we live, work and play.

Most of the world's office workers continue to work remotely. While we are experiencing positive Gross Domestic Product (GDP) growth (5.6%) and lower unemployment (4.2%) in the U.S., these promising signs of an economic recovery are being plagued now with a 6.8% inflation rate, the highest rate this country has seen since 1982. In hindsight, the inflation rate should not have been surprising recognizing the disruption in the supply chain due to the shutdown of manufacturing and transportation of goods during early 2020, when the Pandemic began to emerge rapidly. Although the production and movement of products is now back to pre-pandemic levels, receipt of many goods continues to be stalled at the ports due to the backlog of logistical support. Demand in the meantime has surged due to government relief checks, super-low interest rates and the roll-out of vaccines, that when combined, have given consumers the confidence and financial wherewithal to start spending again. We are currently experiencing a "goods-led inflation surge". In the labor market, employers are scrambling to meet this unexpected demand. Companies now complain that they can't find workers to fill job openings. Workers, finding themselves with bargaining clout for the first time in decades, are becoming choosier about jobs; a sign they have confidence in their ability to find something better. Although the inflation rate is believed to be just temporary, The Fed announced on December 15th two plans to combat inflation for the long term. It would accelerate its bond purchase reduction by $30 billion per month so that the program would end in March instead of June. In addition, there would be three interest rate increases during 2022.

The GDP growth and decline in unemployment, no doubt, was attributed to two major government spending bills, the Coronavirus Aid Relief and Economic Security Acts during 2020 and 2021 ("CARES ACT 1" and "CARES ACT 2"). The two combined bills amounted to nearly $3.1 trillion. More Government spending is forthcoming. The nearly $1 trillion Infrastructure Investment and Jobs Act ("IIJA") was recently passed by both the House and Senate. The result will be job creation and better infrastructure. Major allocations include funds for transportation, roads, bridges, freight and passenger rail, public transit systems, broadband expansion, and water system upgrades

As a matter of perspective, the three Acts, amount to nearly $4.1 trillion, which represents 18% of annual GDP or 14% of our national debt. This equates to approximately $33,000 per taxpayer or $13,000 per citizen. In the interim, all three bills are being funded by increasing our national debt.

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In addition, although the $1.75 trillion “Build Back Better Plan” bill, another spending act, which will focus on Universal Pre-K, Medicare Expansion, Renewable Energy Credits, Affordable Housing, Child Tax Credits and Obama Care Subsidies, is currently stalled in the Senate, it is believed that President Biden may be able to revive it by stripping out some of the programs and proposing them to be separate bills at a later date. Biden has proposed a new tax bill to pay for the proposed legislation, which is making the business community, including firms and higher wage earners, nervous, as these are the groups that will bear the brunt of the tax increases.

Political bickering continues to permeate all levels of government, local, state and national. Social unrest still exists either because of real or perceived systemic racism. All these issues make individuals and businesses more fearful of the future and thus uncertain about the economy. Regardless of all these issues, our economy appears resilient and it’s future bright. The stock market continues to seem oblivious to all our troubles; the Dow Jones Industrial Average (“DJIA”) reached an all-time high (36,338). This reflects an 18.7% increase year-over-year. In contrast, year-ending comparisons of 2019 and 2020 yielded a 7.2% increase.

Healthcare

Post COVID-19

The Pandemic will influence forever how and where care will be provided in the future. Fundamental shifts are occurring in the areas of design and construction of facilities, training of healthcare workers and the sourcing and management of critical care equipment and personal property equipment and optimal settings for care. For example, there is an increasing trend for hospitals to care for only the critically ill and consequently many can readily convert some of their regular beds to critical care beds. COVID patients are separated from regular critical care patients. Virtual Intensive Care Units are being established outside of the hospital setting. Nurses, managed by specialists at the hospitals, are administering critical care to patients at home. Physical care at ambulatory facilities and at home are flourishing as patients avoid hospital admission because of COVID concerns. On-line health and telehealth will continue to emerge as alternative sources of care, reducing the number of physical meetings with a physician in an office/hospital setting, and in some cases, eliminating a visit.

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Currently, facilities delivering healthcare whether it be hospitals, ambulatory centers or physician offices within a medical office building or traditional building, have set up protocols for all visitors and occupants. Policies for masks and pre-screening at building entrances and suite entrances are required with requests or mandates for social distancing in common areas and suite open areas. Hand sanitizer stations have been strategically placed throughout common areas of facilities and physician offices to accommodate patients. Janitorial services in medical buildings have increased both in frequency and scope of work, including the use of stronger disinfectants on surfaces. Existing HVAC systems are being adapted with more filtration and fresh-air intake. Finally, touchless technology is being addressed to provide sanitary ways to access entrance/exit doors, elevators, plumbing and lighting.

Healthcare Trends

Healthcare, to be sure, is not only vital to living but is a large part of our economy. U.S. national healthcare expenditures approximate $4 trillion. Healthcare spending is estimated to increase at an average annual rate of 5.5% through 2027, reaching nearly $6 trillion by 2027, at which time healthcare will represent approximately 20% of the U.S. GDP. The rapid growth in healthcare spending is attributed to the aging U.S. population and the higher-than-average inflation on the price of healthcare goods and services. By 2030, one in every five people in the U.S. will be 65 or over. Interestingly, people over 65 accounted for 36% of all healthcare spending, yet they only represent 16% of the population. The healthcare industry is a large employment sector. Nearly one in every 10 people employed in the economy have jobs in healthcare and that ratio is expected to rise in the future.

Three major trends are occurring: 1) The shift toward care in the home; 2) the shift from fee-for-service to value-based care; and 3) the ongoing professionalization and investment in behavioral healthcare.

Moreover, “retailization” of healthcare continues to evolve. Medical practitioners are establishing facilities closer to the patients in more accessible suburban locations. In addition to single-purpose medical office properties, we continue to see a proliferation of co-location facilities where primary care physicians, for example, occupy space within supermarkets and drugstores.

Current Medical Office Building Statistics | *Omaha, Nebraska*

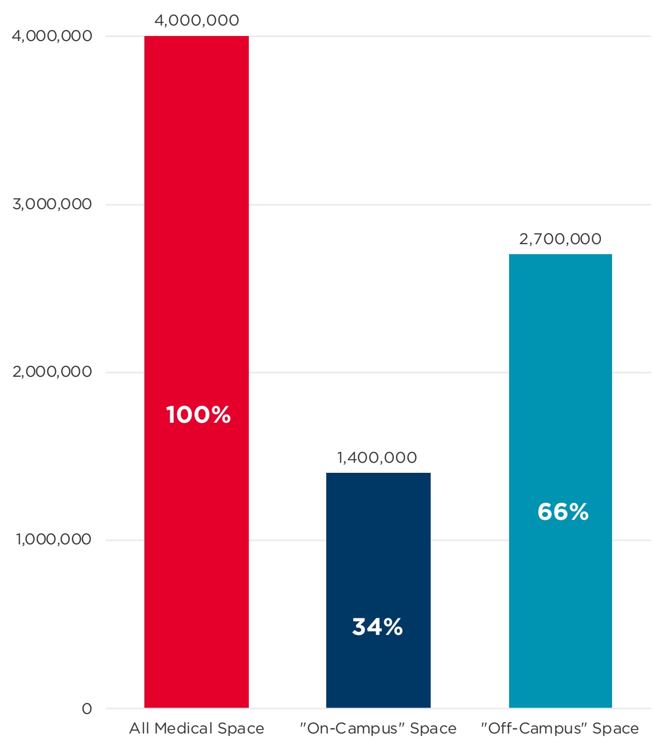
Space Availability

Among 143 buildings recently surveyed, there is approximately 4.1M square foot (SF) of Medical Office Building (MOB) inventory in the metropolitan area. Available space reflects approximately 172K SF or approximately 4.2% of all medical space. In contrast, nationwide, the average medical office space vacancy approximates 8.6%. Omaha, to be sure, continues to possess a healthy Medical Office Building market.

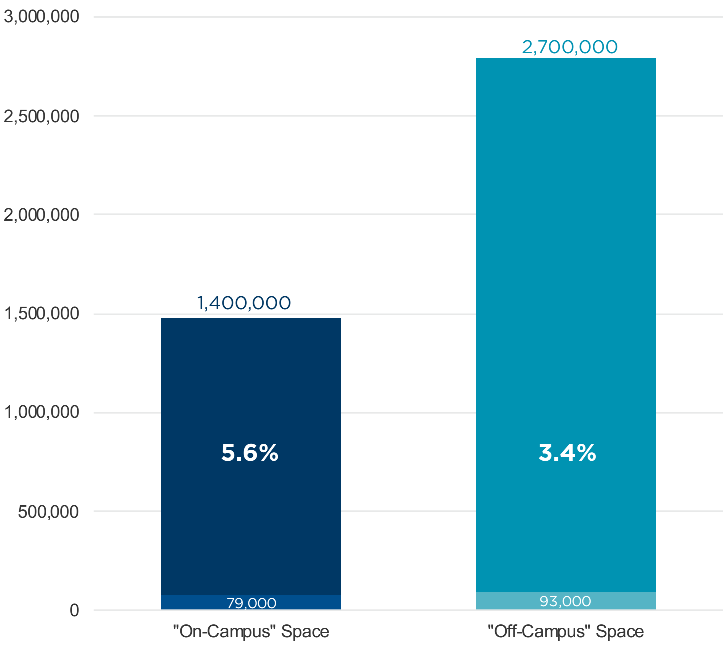
Approximately one-third (1.4M SF) of total MOB space reflects "on-campus" space, square footage located on hospital campuses; while the remaining two-thirds (2.7M SF), "off-campus" space. Space availability in each category reflects 79K SF (5.6%) and 93K SF (3.4%), respectively.

It is important to note that several hospitals continue to categorize some of their current vacant space in their on-campus MOBs as "unavailable" as they are reserving it either for temporary relocation space to accommodate displaced medical operations due to construction activity or are reserving such space for long-term use.

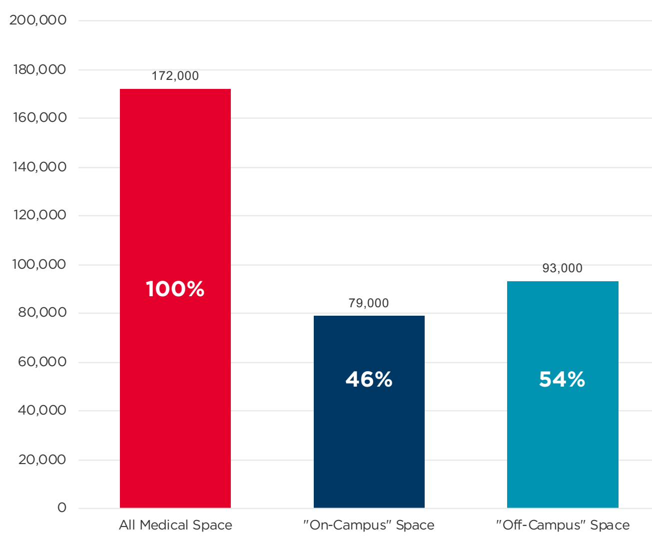
Market SF
Omaha, Nebraska



Campus Available SF
Omaha, Nebraska



Market Available SF
Omaha, Nebraska



Note: All numbers have been rounded.

Investment Activity & Pricing

Local Investment Activity & Pricing

An investor has acquired the two-story medical office building (26K SF), 11704 West Center Road, for $4.2 million or approximately $162 per square foot (PSF). The reported cap rate was 7.33%. The building is primarily occupied by orthopedic physicians.

An investment group has acquired the Midwest Professional Center (29K SF), 13500 California Street, for $7.4M or approximately $255 PSF. The reported cap rate in the "off-market transaction" was 6.5%. Midwest Eyecare occupies approximately 67% of the building.

National Investment Activity & Pricing

MOBs are still considered a favored asset class among all commercial real estate sectors given the strong demand for office space due principally to an aging population needing healthcare services. By 2030, all baby boomers will be older than 65, representing 20% of the U.S. population. This 65-and-older age segment is expected to live longer than ever before, which will undoubtedly result in a rise in healthcare related services. As a result, there remains a strong appetite for "cycle-resilient" real estate investment that medical and healthcare real estate offers. Moreover, Investor recognition of the "retailization" of healthcare, a location emphasis of MOBs in affluent suburban markets that are closer to the patients and creditworthiness of tenants, continues to drive premium pricing for off-campus medical products.

"As in 2020, 2021 saw nominal changes in capitalization rates. There was no change in Class "A" on-campus or off-campus product." Class "B" on-campus and off-campus product had slight increases (each, 10 basis points)."

Investors are now considering a broader range of healthcare users and tenant types, including behavioral health. Although telehealth has enjoyed a recent surge in popularity, the widespread adoption and use has not substantially altered the demand for medical office space. Telemedicine is a great supplement, but not a replacement for traditional medical practice. Physicians will still require medical office space to perform traditional office visits.

Buyer profile continues to transition from a market dominated by institutional and Public/REIT buyers (27%) to the current market that is dominated by more non-traditional private equity and private investors (59%). The balance of the investor pool for medical office buildings is users (14%).

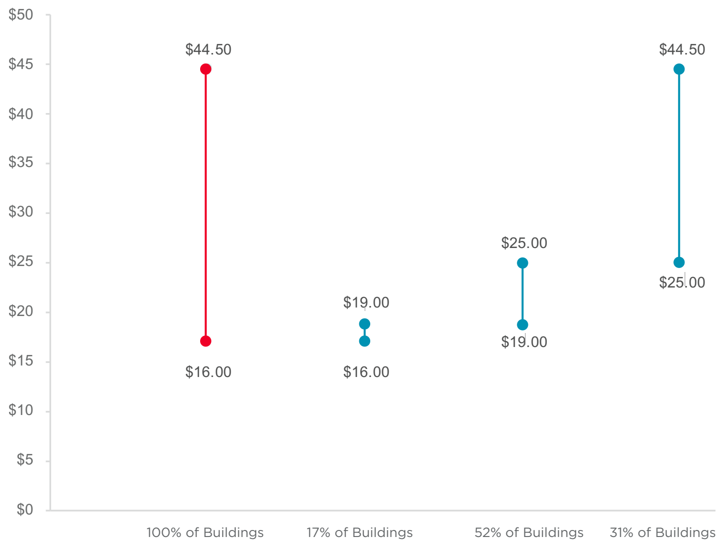
As in 2020, 2021 saw nominal changes in capitalization rates. There was no change in Class A on-campus or off-campus product. Class B on-campus and off-campus product had slight increases (each, 10 basis points). Current national averages are 5.7% and 6.0% for Class A product on and off campus, respectively; 7.4% and 8.1% for Class B product, correspondingly.

Although capitalization rates have been relatively flat the past couple of years, they are expected to compress in the future as more capital rotates from the more volatile office/retail/hospitality sectors to medical office. It is projected that the decline will be 50 – 150 BPS.

Local Rental Rates

Of reported rents of 58 buildings, representing 41% of total buildings surveyed, local on-campus MOB full-service rental rates range from $18.50 to $31.00 PSF with off-campus $16.00 to $44.50 PSF. The significantly lower rate range, particularly in the off-campus sector, reflects older MOBs, containing available space that probably will not be used as medical office space again because of location, size, or condition. The higher rate range in both classifications reflects newer specialty medical space. Local rental rates have generally followed national rental rate increases of 2-3%/year.

Full Service Rent PSF
Omaha, Nebraska



*Based upon 58 buildings surveyed.

> ***"Local rental rates have generally followed national rental rate increases of 2-3%/year."***

Recent Project Completions

- Nebraska Medicine has completed a new adult psychiatric emergency center at the Med Center Campus, 42nd & Dewey Streets. (160K SF).
- Nebraska Medicine has also recently completed the Millard Primary Care Clinic (13K SF), 13325 Millard Avenue.
- Munroe-Meyer Institute (MMI), which serves people with intellectual and developmental disabilities, has completed its renovation of one of the former First Data Resources buildings at Aksarben Village (220K SF), 69th & Pine Streets. The remodeled facility represents twice the square footage that MMI had at the Med Center Campus. MMI now employs 550 people, representing the second-largest academic unit within UNMC, behind the College of Medicine. The new facility can now attract 150K annual visits, an 80% increase over its former location. The majority of the project's $91 million cost came from charitable donations supplemented by $10 million in state bond money.
- Children's Hospital has completed its $450 million, 460K-SF expansion and renovation, at its campus, 84th & Dodge Streets. The expansion portion of the project included construction of a 10-story building to house relocation of the NICU from Methodist Hospital, new and expanded pediatric intensive care unit (PICU), surgical areas, a larger emergency department, a fetal care center and expansion of hematology and oncology. Bed capacity has now increased from 140 to 250.
- Madonna Rehabilitation Hospital, 176th & Burke Streets, has completed the addition of approximately 8K SF to its 263K-SF facility. The $5.5 million addition accommodates outpatient physiatry and therapy services.
- NewStreet Development has completed construction of OrthoNebraska's 30K-SF Orthopedic & Physical Therapy facility, at the southwest corner of 204th & Vinton Streets. The new facility includes 16 exam rooms, two procedure rooms, radiology services and approximately 9.5K SF of physical therapy space. Seven-day orthopedic urgent care is also available at the facility.

Project Activity | *Omaha, Nebraska*

- A private development firm has completed its construction of the Papillion Micro Hospital (22K SF), 529 Pinnacle Drive, Papillion, Nebraska. The facility accommodates individuals that may need urgent care or short-term overnight care.
- The Veterans Administration (VA) has completed development of an $18.8 million, 29K-SF, medical office building for physical therapy and prosthetics at its campus, 42nd & Center Streets.

Projects Under Construction

- Methodist Hospital, 84th & Indian Hills Drive, is doubling the size of its Emergency Room Department from 12 to 24 rooms. The $25 million project, occurring in six phases, will be completed in 2022.
- CHI Health and the VA Nebraska-Western Iowa Health Care System are partnering on the $11 million renovation of the fifth and sixth floors of the Midlands Hospital in Papillion for a 30K-SF, 34-bed short-stay rehabilitation, skilled nursing care and memory care for veterans.
- Noddle Companies has broken ground on the Nebraska Medicine, 90K-SF Outpatient Specialty Center, Village Pointe Health Center, east of 111 N. 175th Street. The building will expand existing clinical services and add new services. The project is a part of the expansion and redevelopment of the UNMC Physicians Village Pointe Medical Office Campus that will ultimately contain approximately 337K SF of MOB space and two parking garages. Expansion/Redevelopment costs are estimated to be $100 million. The expected delivery date is late 2022 or early 2023.
- Construction is underway for the C.L. Werner Center for Health Sciences Education, Creighton University School of Medicine, SEC Cuming Street & HWY 75. The $75 million five-story facility will serve as the new home of Creighton University's School of Medicine, and as a hub for all the University's health sciences schools and colleges. Programs will include medicine, nursing, pharmacy, physical therapy, occupational therapy, behavioral health and other disciplines via classrooms, a simulation center, study areas, labs, and administrative areas. It is expected that 5,900 students, faculty and staff will use the center annually. Completion is slated for fall 2023.
- R & R Realty, a Des Moines, IA developer, has broken ground on the MD West One, single-story, 38K-SF, MOB, located at Fountain Ridge Office Park, NWC 192nd & Burke Streets. The project is a joint venture between R & R Realty and MD West One, a physician group that provides orthopedic, neurosurgery and spine care services. Construction completion is slated for spring 2023.

Munroe-Meyer Institute (MMI), 69th & Pine Streets

Papillion Micro Hospital, 529 Pinnacle Drive

Announcements

- The University of Nebraska Medical Center has announced a $45 million renovation of the former Omaha Steel Works, Saddle Creek between Farnam and Leavenworth Streets. Koelbel and Company (Denver) and GreenSlate Development (Omaha) have been selected as developers. The existing two-structure 140K-SF facility will be renovated into a mixed-use innovation technology campus that will include a food hall, market, an event center, and office space. The innovation hub will house several existing UNMC operations, including UNeMed, UNMC's tech transfer office, and UNeTech, which coordinates the creation of business startups from UNMC and the University of Nebraska at Omaha research. In addition, other occupants planned include UNeHealth, UNMC's contracting and fiscal arm for industry-funded clinical trials, and UNO's Nebraska Business Development Center. Additional uses include space for new health technology start-ups, restaurants, and retail operations. This is one component of the area's redevelopment. A new administrative tower (350K SF), complete with a parking garage, near the southwest corner of Farnam Street and Saddlecreek Road will complement the project. A pedestrian connection also is planned across Saddle Creek to allow pedestrians to move safely across back and forth to the medical center campus.

- The University of Nebraska Medical Center has announced preliminary plans for a $2.6 billion project that would effectively serve local patients for a variety of needs, while potentially caring for victims of pandemics and natural disasters. The project, identified as "Project NeXT", will be a partnership between UNMC and Nebraska Medicine. The Nebraska Legislature has approved $300 million in contingency funding, provided those resources are matched by $1.3 billion in private donations and federal government funding. The City of Omaha has pledged $93 million toward the project. Omaha is one of five pilot sites for the United States to develop a federal program to bolster the Nation's disaster response capacity. This is a key step toward the project's reality. No timetable for construction commencement nor completion has been announced.

MD West One, 192nd & Burt Street

C.L. Werner Center for Health Sciences Education, Creighton University School of Medicine, SEC Cuming Street & HWY 75

Market Report Sources: The Omaha World Herald, U.S. Bureau of Labor Statistics, The Federal Reserve, U.S. Debt Clock.org, U.S. Inflation Calculator, Cushman & Wakefield: 2021 Medical Office Investor Survey, Cushman & Wakefield: Fall 2021 Vital Signs Healthcare and Medical Office Report, Healthcare in a Post-Covid-19 World: Three Trends to Watch (Andrew Kadar June 8, 2021, Webinar), Shopping Center Business (July 2021), Goldman Sachs/Economic Research/Global Economics Analysist, GS Macro Outlook 2022: The Long Road to Higher Interest Rates (November 8, 2021), The Conference Board Economic Forecast for the U.S. Economy (November 10, 2021), The Conference Board U.S. Economic Outlook (December 15, 2021), U.S. News & World Report, U.S. Jobless Claims Hit Record 52-Year Low After Seasonal Adjustments (November 24, 2021), Market Watch (December 15, 2021), Brookings Institution (Elaine Kamareck article, December 21, 2021)