Investment Insights

Invesco Fixed Income

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What a difference 180 days make

Spotlight on Municipal Investment: CCRCs

A path to the "new normal"

Municipal bonds are securities issued by states, cities, counties and other government entities to fund day-to-day obligations and finance capital projects, such as the construction of schools, highways and sanitation systems. Local and state governments also issue private activity bonds to address public needs. As noted in the following case study, an example of this is municipal bonds issued by continuing care retirement communities (CCRCs). CCRCs are retirement communities with a distinguishing feature – they offer residents the ability to "age in place." CCRCs provide lifetime care with a full suite of housing options on one campus. Independent living options suit seniors who are healthy and independent, assisted living options offer light health care and assistance with daily activities, and nursing options offer full health care capabilities, including memory care units on many campuses. Some consider CCRCs to be the ultimate paradigm of planning ahead.

CCRC sponsors are overwhelmingly classified as non-profit entities and issue bonds in the tax-exempt municipal bond market as a low-cost and efficient means of obtaining capital. Bonds issued by CCRCs have historically offered above-average yields relative to other sectors in the municipal market, and we believe they are an attractive investment alternative to lower-yielding municipal securities. We believe Invesco Fixed Income's large team of experienced research analysts is uniquely equipped to determine the financial health of each CCRC, using a broad range of analytic tools, including stress scenario modeling and competitive, demographic and real estate value analysis.

Our "Spotlight on Municipal Investment" is designed to provide insight into investment opportunities like CCRCs by offering a closer look at a particular issuer or sector of the municipal market.

Coronavirus presents challenges for retirement communities

On January 21, 2020, the first patient in the US was diagnosed with the novel coronavirus, or COVID-19, by the State of Washington and the US Centers for Disease Control and Prevention. Approximately one month later, Life Care Center of Kirkland, a suburban Seattle nursing home, became the virus's epicenter in the US. At least 81 of the 120 residents in that home tested positive for the virus, and by late March, 34 had died, accounting for a fourth of the coronavirus fatalities in the US at the time.[1] The crisis in Kirkland illustrated how vulnerable the elderly are to this virus and heightened concerns in nursing homes across the country.

On the opposite coast, New York City was experiencing its own nursing home coronavirus crisis. On March 25, New York's Health Department mandated nursing homes to accept COVID-19 patients and barred requiring any COVID-19 tests for admission. This mandate was enacted to ease the burden on hospitals besieged with COVID-19 patients by removing elderly patients that were still infected and sending them to nursing homes that had empty beds. By the end of May, it was estimated that 12,000 nursing home and assisted-living residents had died from COVID-19, representing half of all the virus deaths statewide.[2]

The events in Kirkland and New York resulted in a wave of jarring media headlines regarding senior living facilities. A New York Times headline from April 17 read, "'They're Death Pits':

1 Centers for Disease Control and Prevention, March 27, 2020. Seattle Times, March 18, 2020.

2 https://nypost.com/2020/05/29/new-yorks-nursing-home-horrors-are-even-worse-than-you.think. /https://www.upi.com/Top_News/US/2020/05/31/NY-coronavirus-death-rate-declines-de-Blasio-says-protests-wont-affect-reopening/1641590949860/.

Virus Claims at Least 7,000 Lives in U.S. Nursing Homes." On April 24, CNN declared "COVID-19 is ravaging nursing homes." While both CNN and The New York Times specifically identified nursing homes, many other media outlets identified the crisis as striking senior living facilities in general. The following headline appeared in The Wall Street Journal on April 10: "Coronavirus Strikes at Least 2,100 Senior Facilities Across U.S., Killing 2,300 People."

Understanding the difference in terms

Invesco Fixed Income invests in bonds issued by CCRCs, and given these headlines, we know that many investors may have questions about the impact of COVID-19 on these facilities.

While recognizing that people's concerns are first and foremost around the human toll of the virus, we think it is important to clarify some of the misconceptions created by those alarming headlines. Although the two terms "senior living facility" and "nursing home" may have been used interchangeably in the press, the two are not synonymous.

The term "senior living facility" is a broad moniker often applied to nursing homes, assisted living facilities and continuing care retirement communities. But there are distinct differences between these types of facilities and some striking differences with regard to their experiences with COVID-19.

A nursing home normally provides the highest level of medical care for older adults outside of a hospital, making them different from other senior housing facilities. A licensed physician supervises each patient's care, and skilled nursing care is available on site, usually 24 hours a day. A nursing home resident enters because of a medical necessity. As such, it stands to reason that these residents are medically vulnerable. According to the Centers for Disease Control and Prevention, there are approximately 15,600 nursing homes in the US, with 1.7 million licensed beds occupied by 1.4 million patients.[3] In 2016, the proportion of nursing homes with for-profit ownership was 69.3%.[4]

Assisted living facilities offer residents assistance with routine daily tasks such as bathing, dressing, grooming, mobility, medications and meal preparation. Because the service level is assistance, not medical care, it is not suitable for people who need daily nursing services. However, individuals residing in assisted living facilities are also not able to live independently. According to a Statista Research report published in 2016, there are approximately 16,000 assisted living facilities in the US.

CCRCs (also known as life plan communities), by contrast, are facilities with access to multiple levels of care on a single campus. The primary benefit of this type of facility is that residents can age in place through the health care continuum. Typically, a CCRC offers some combination of independent living, assisted living or nursing care. Those who fall into the independent living group most often represent the largest segment of the campus. There are approximately 2,000 CCRCs in the US, and about 80% are owned by not-for-profit organizations that are "mission-driven."[5] Senior citizens typically choose to enter these facilities as healthy, independent residents, much like they would choose their next home purchase, rather than out of medical necessity. This fact differentiates them from assisted living facilities and nursing homes, which are often chosen because seniors or their families are concerned about the senior's health and believe independent living is no longer an option.

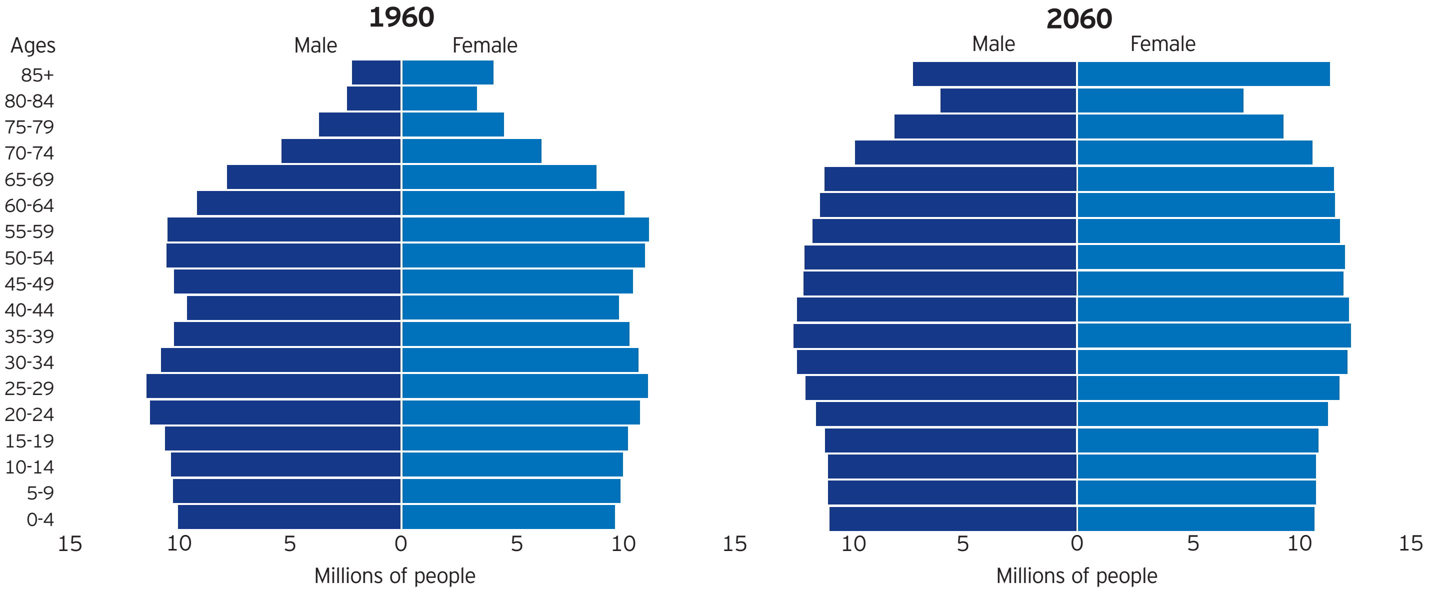
A lifestyle choice for the baby boomer generation

The basis for demand, and the foundation on which the senior living industry is built, is the graying of the baby boomers. Since January 1, 2011, when the oldest baby boomer turned 65, 10,000 baby boomers have turned 65 every day, and this is forecast to continue until 2030.[6] By then, it is estimated that roughly 18% of the US will be 65 or older.[7] This phenomenon - often referred to as the "silver tsunami" - presents a compelling argument for the need for these communities.

But it is important to remember that, for these independent seniors, entering a CCRC remains a lifestyle choice. Baby boomers want an abundance of activities, dining venues, events, social experiences and opportunities. And, according to the real estate database company Zillow, baby boomers spend 18% more time than millennials on their home searches, averaging around five months.[8] Therefore, successful marketing of a CCRC to the baby boomer generation involves connecting these facilities to their communities and creating a living experience through campus visits and social interactions with community members. Given baby boomers' selectivity, this marketing campaign may require several months of effort before a facility can secure a deposit from a prospective resident.

3 Centers for Disease Control and Prevention, Jan. 25, 2019.
4 Long-Term Care Providers and Services Users in the United States, 2015-2016, Appendix III. Detailed Tables, table V.
5 www.mylifesite.net › blog › post › examining-ccrc-mark. https://www.aarp.org/caregiving/basics/info-2017/continuing-care-retirement-communities.html. https://seniorhousingnews.com/2018/05/24/only-22-of-ccrcs-in-the-u-s-are-for-profit/.
6 www.pewsocialtrends.org, as of Dec. 20, 2010.
7 Pew Research Center population projections, as of Dec. 20, 2010.
8 https://www.zillow.com/report/2017/buyers/the-home-search-process/. http://www.metrostudy.com/wp-content/uploads/2018/06/Webcast-Generational-Trends-Combined-PDF-2018-Jun-19.pdf.

Figure 1 - From pyramid to pillar: A century of change



Source: US Census Bureau, Population Division
Original Release Date: March 2018; Revised Release Date: September 2018
Erratum Note: The 2017 National Population Projections were revised after their original release date to correct an error in infant mortality rates. The files were removed from the website on August 1, 2018, and an erratum note was posted. The error incorrectly calculated infant mortality rates, which erroneously caused an increase in the number of deaths projected in the total population. Correcting the error in infant mortality results in a decrease in the number of deaths and a slight increase in the total projected population in the revised series. The error did not affect the other two components of population change in the projections series (fertility and migration). Major demographic trends, such as an aging population and an increase in racial and ethnic diversity, remain unchanged.

The contagion conundrum
Due to the high number of deaths experienced in the nation's nursing homes, and in recognition of the elderly population's vulnerability to the coronavirus, CCRCs cautiously implemented strict lockdown procedures to protect residents from contagion. Communal dining, social activities and the use of fitness areas were discontinued. Visitors were barred from entering campuses and residents were discouraged from leaving and were required to quarantine upon return if they did. Staff was required to use personal protective equipment.

As a further response, the CCRCs stopped their marketing campaigns to attract new residents, which most often featured on-campus tours. These preventative health efforts created a contagion-born conundrum: How to market a community without being able to showcase it. This dilemma, coupled with the fear created by the alarming media headlines about the large number of nursing home deaths, brought CCRC marketing efforts to a virtual standstill. To protect existing residents, CCRCs also stopped allowing new residents who had already made deposits from moving into the community.

The importance of technology and testimonials
The CCRCs found a creative solution to their conundrum, discovering that generations entering these facilities today are tech-savvy. In fact, the Pew Research Center has found a significant growth since 2012 in technology adoption among older generations – especially Gen Xers and baby boomers. The marketing staffs at CCRCs across the nation capitalized on their target market's comfort with tech and created virtual experiences. They offered everything from virtual walking tours to drone flyovers and even drive-through open houses. This approach satisfied prospective residents' need for connecting to a community before deciding whether to move in.

As the realities of seniors living on their own during the pandemic have increasingly emerged, the benefits of CCRCs have also become even more apparent and valued. Since the onset of the pandemic, many studies have highlighted the effects of isolation on seniors' physical and mental health, including the potential for depression. Lockdowns and the need for social distancing have also placed strains on families of seniors living independently. As families have recognized their older relatives' vulnerability to infection, many have stepped in to shop for groceries and make pharmacy runs to limit their risks of exposure. This has created additional obligations for family members already dealing with the effects of the crisis.

CCRCs were able to avoid or effectively mitigate many of these issues for residents and their families. Meals, medicine and groceries were delivered to residents' doors daily. Virtual experiences, from town halls to group exercise and crafting, were offered to help residents stay engaged and avoid feeling isolated or depressed. Residents were also encouraged to walk campuses' outdoor pathways and see fellow residents while still social distancing.

All of these efforts kept residents safe and reassured their families. In turn, many residents and family members created credible and powerful testimonials about the value of these communities. The CCRCs have utilized these testimonials as effective marketing tools with prospective residents.

Navigating the new normal

It has been six months since the Life Care Center of Kirkland became the epicenter of the coronavirus crisis in the US. Immediately afterward, all types of senior living facilities became associated with the tragic death toll in nursing homes.

In our view, the CCRCs responded effectively to the challenge. Many acted quickly to protect the safety of their residents and developed creative ways to keep their businesses viable. Today, minor COVID-19 outbreaks on campuses are calmly controlled, managed and reported without the hysteria seen in the early days of the crisis. This has encouraged more facilities to be fully transparent about infections and how they are handling them on their campuses.

Today, as facilities can again accept new residents, the track record of CCRCs in handling the virus, testimonials supporting that record and pent-up demand have enabled new sales of CCRCs to gradually return toward pre-COVID-19 levels. Hospitals in many markets are also performing elective surgeries again as state restrictions have eased. This has helped CCRCs fill the nursing home components of their campuses with higher-fee residents since the needs of these residents are more extensive.

We remain optimistic about this overall segment of the market. In our view, the CCRCs acted responsibly to protect residents' health while also demonstrating creativity and resiliency to ensure that their businesses would remain viable. Still, challenges lie ahead for the sector, and we recognize that some businesses, especially those in already weakened states, may not survive this ongoing crisis. We recognize that our role as professional investors is to help clients assess which of these communities are best positioned to survive and eventually thrive in this environment.

Our optimism on the sector stems from how effectively it has addressed the challenges that engulfed it at the start of the year. To paraphrase the 1959 Grammy Award-winning song sung by Dinah Washington, "What a difference 180 days make."

This case study is presented for illustrative purposes only. There can be no assurance that any investment process or strategy will achieve its investment objectives. This material does not constitute a recommendation as to the suitability of any investment and a tax or financial professional should be consulted. Past performance is not necessarily indicative, or a guarantee, of future results.

Risks

Municipal securities are subject to the risk that legislative or economic conditions could affect an issuer's ability to make payments of principal and/ or interest.

In the case of revenue bonds, notes or commercial paper, the credit risk is the possibility that the user fees from a project or other specified revenue sources are insufficient to meet interest and/or principal payment obligations. Private activity bonds used to finance projects may also be negatively impacted by the general credit of the user of the project.