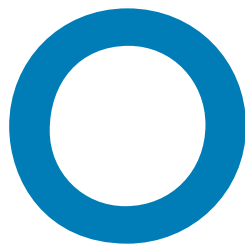


Interview with Rio Minami, managing director in charge of real estate operations at Carlyle Japan



# Offering Living Facilities for Seniors in Japan

## Carlyle Group Aims at Market for the Aged

Interviewer: Hiroshi OKABE



*Rio Minami, managing director in charge of real estate operations at Carlyle Japan*

The Carlyle Group, a major US equity investment fund, is actively investing in

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living facilities for seniors in Japan. Reflecting the fact that Japan is one of the world's fastest aging countries, demand for such facilities is growing strongly. But the supply of senior living facilities remains insufficient. Cashing in on its own experience and expertise amassed so far in the United States, Carlyle entered into senior living business in Japan. In an interview with *Japan SPOTLIGHT*, Rio Minami, managing director in charge of real estate operations at Carlyle Japan, discusses the group's business strategy and policies, positioning the rapid graying of Japanese population as a business opportunity.

### Immature Market

#### How do you position your equity fund's investment in senior living facilities?

**Minami:** In the area of real estate, there are various investment choices – ranging from office buildings to residences to operational assets that require management of facilities. Most understandable among operational assets are hotels. Senior living facilities, too, can be seen as an investment area needing operation management. In Japan, hotels have already been established as an investment sector. There is no denying, however, that the area of senior living and healthcare facilities is still immature as a target for real-estate investment. Buildings – so-called “bricks and mortar” – alone are of no use as senior living facilities. Such facilities can be viable only when operators use them as facilities. In this sense, they hinge heavily on the quality and credibility of operators. Senior living facilities are therefore an investment target whose value is greatly affected by their management.

#### Specifically, how does the Carlyle Group commit itself to investment in senior living facilities?

**Minami:** We don't take operational risks in principle because we don't have operational expertise in the area. Our business picture is that we own assets, join with experienced Japanese operators, have them use facilities, and we receive rent from them. In the United States, some equity funds venture into senior living business by taking operational risks themselves. We have not adopted such a way of business yet in Japan. In many cases, senior living facilities targeted for investment are developed for leasing to Japanese operators.

### Rising Needs of Society

#### Japan is graying at the fastest pace in the industrialized world. How do you forecast future developments in the market for senior living facilities?

**Minami:** Japan's population has already begun to decline, with the ratio of those aged 65 or older having exceeded 20%. The ratio is projected to rise at an accelerated pace in the years ahead and eclipse the 30% threshold in a decade. Actually, however, facilities for the aged to spend comfortable retired lives are still in short supply. We therefore believe needs for senior living facilities should grow steadily in Japan, but this sector is far from being established as a business model. The introduction of the nursing insurance program in 2000 has prompted numerous operators to enter the senior living sector. With the program set to be reviewed every five years for the present, insurance revenues could fluctuate depending on what policy the Japanese government is to take, and thus the structure of earnings from senior living facilities will become unstable if operators rely too much on insurance revenues.

### Active Seniors

#### Japanese society is aging rapidly indeed, but needs are diverse among elderly people. This, coupled with Japan's changing social structure, is expected to greatly affect nursing business, isn't it?

**Minami:** The size of the senior living market will grow in tandem with a rise in the ratio of the aged. Of the elderly in Japan, those who require nursing care account for around 30%, some 10% of

them with dementia. Namely, the ratio of those elderly people who live healthy and independent lives is much higher statistically. It then becomes necessary to offer facilities targeted for those people, who may be called “active seniors” capable of doing various things alone and enjoying healthy lives positively at age 70 or older. They prefer to live in convenient places near city centers, rather than in one-unit houses in suburban areas. The proportion of elderly people finding such a lifestyle attractive is increasing. Japan used to have large families, and it was not rare for three to even four generations to live together under one roof. Japanese households later became nuclear families in big cities after the era of rapid economic growth in the 1960s. Then, in reaction to the nuclear-family trend, duplex homes tended to gather popularity to some extent. Of late, however, not a few elderly people have come to adopt a lifestyle in which they design their lives themselves, choosing facilities for the elderly as their last domicile rather than relying on their children for nursing care. In the past, elderly people had psychological resistance to entering so-called retirement homes. Today, there seems to have been a change in social perception; an increasing number of elderly people prefer to enter facilities for the elderly before getting stuck in homes and enjoy daily lives there by joining various activities. Facilities in resort spots of scenic beauty gathered popularity at one time. Of late, preference has gained steam among elderly people to remain in places where they lived, with their children and grandchildren living nearby, and where they can enjoy cultural lives taking advantage of cultural facilities close by. This attests to steady growth in demand for elderly facilities from active seniors.

### Sense of Ethics Sought

**The Carlyle Group reportedly does not take operational risks of running senior living facilities. Are there any unique difficulties in the business operations?**

**Minami:** It is true there are difficult aspects specific to this business, and one example is the form of contract. In principle, operators offer living facilities to elderly users as their final homes. In many cases, elderly people buy the right to lifelong use rather than purchase real estate. Namely, they obtain the right to use and live in our facilities on a contract as long as they are alive. It is not like buying real estate such as a condominium. The duration of use differs depending on how long one lives. Operators are to provide good services to those elderly people who use our facilities so that they will be able to live as long as possible. In the meantime, there is the question of uncertainty growing as a business model unless users of our facilities are replaced by new ones at certain intervals that can be estimated objectively. Simply put, business profitability improves if the cycle of user turnover is shorter than estimated. That is, there is contradiction in a sense

between having users live long and seeking profitability. Doing this business thus requires a high sense of ethics. Aside from such problems, our facilities are basically in line with social needs. Although life expectancy has been increasing steadily, all human beings cannot live to be 100 years old. With this in mind, we are hammering out a reasonable cycle of user turnover on the basis of statistical and empirical data.

### How many facilities have you offered in Japan?

**Minami:** We have supplied six facilities in Japan. They are worth some ¥20 billion in total asset value. We believe the sector of senior living facilities has good growth potential. As a target for real-estate investment, the population of senior living facilities is not as large as those of office buildings and residences. It is also questionable if such facilities can really maintain adequate liquidity as real-estate merchandise. Given the advent of aged society, however, growth is expected as an investment target as well on the back of rising social needs. Therefore, we are doing this business in the spirit of a pioneer.

### Cashing in on US Results

**Carlyle reportedly has the experience of operating senior living facilities in the United States. How do you see the possibility of foreign investors entering the elderly business segment in Japan in the future?**

**Minami:** Japanese investors and businesses, too, are beginning to show interest in this investment area. The Carlyle Group as a whole has a considerable record of investments in the field of senior living facilities in the United States in partnership with major US operators. In that sense, we believe the level of understanding of the business and the level of our investment record are higher than those of other competing groups. The experience we have amassed so far, I believe, will never fail to help us do healthcare-related business in Japan as well. Since 2000, a great number of companies have launched senior living operations in Japan. They are now undergoing the process of selection based on their business record and creditworthiness. We believe senior living facilities become an appropriate investment target only after their operation, location and buildings are regarded as a set of quality combinations.

**The Japanese real-estate market is now in a severe climate in the aftermath of the financial crisis.**

**Minami:** Real-estate liquidation business has grown greatly in recent years. But it has caused the adverse side effect of excessive entries into the business, resulting in excessive liquidity. In the early 1990s when the real-estate bubble burst in Japan, there was a

sort of land myth, giving people the illusion that land prices would go up forever. After a certain period of time, the myth vanished. This time around, however, land price rises were justified by arguments that property investment is safe because it is evaluated based on the assessment of cash flow. As a result, the overconfidence in cash flow-generating real estate caused prices to rise. In fact, this led to excessive liquidity, leaving property prices deviated from realities. The problem, combined with the subprime loan crisis, dealt the real-estate market a hard blow. While few investors can apparently foresee future developments, investors have no choice but to accept correction moves in the property market as a backlash of excessive liquidity. Most worrisome is the fact that the real economy is being adversely affected to a great extent. All investors are keeping close eyes on when the property market will hit bottom. I believe a period of correction will continue for two to three years.

Photo: Carlyle Japan



*Hyldemoer Sankeien: a housing complex for elderly with nursing-care service, a project undertaken by the Carlyle Group*

## Senior Living Business to Be Developed

### What position does the healthcare sector occupy in your group's overall real-estate business?

**Minami:** Looking at the scale of real-estate business, there are indeed a variety of sectors, and the healthcare sector is only one of them. But given the fast graying of Japanese society, it is certainly a sector to be developed in the medium to long term.

### Not only Japan but some other Asian countries face the problem of aging population. As the supervisor of the Carlyle Group's operations in the Asian region, how do you see future developments in the business of senior living facilities in Asia?

**Minami:** Both in China and India, elderly people are increasing. At the same time, however, there are a large number of young people there. The age pyramid of population in the two countries greatly differs from that of Japan. In Japan, an increasing number of elderly people have the mindset of leading their lives independently and seeking their final houses themselves, thus generating the need for high-value-added apartments. In China and India, by contrast, most sought after are houses for emerging new middle-class people. There are a great number of people who

want to buy houses for the first time, but demand for houses for the elderly is not visible yet. A population explosion is under way there, however, indicating an aging population will develop into a big issue in the future. Actually, a certain Chinese insurance company recently approached us and expressed their intention to start their study for future demand. **JS**

*The Carlyle Group is a global private equity firm founded in 1987. It has thus far invested in more than 20 countries in Asia, North America and Europe in a variety of fields, including telecommunications/media, consumer goods, technology services and healthcare. The group's Japan unit, Carlyle Japan, is managed by Japanese investment professionals well-versed in Japanese business practices. It features friendly – not hostile – investments in Japanese corporations with the aim of raising corporate value from a medium- to long-term perspective through close collaboration with the existing management of the companies invested. One of its successful investments is industrial crane manufacturer Kito Corp., which, with the support of Carlyle, successfully turned around its business by global expansion and other measures, and was re-listed on the Tokyo Stock Exchange.*

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