

After a hiatus, John Smelter is back

Pioneering sales broker is now a buyer with White Oak Healthcare MOB REIT

By John B. Mugford

As the medical office building (MOB) sector has grown in stature among investors of all types in recent years, including institutional capital sources, so have the yearly sales volumes, which in recent years have consistently topped \$10 billion.

This increase in demand for the product type, as one would expect, has fueled an increase, especially in the last decade or so, in the number of professionals solely focused on brokering MOBs.

Before it became commonplace for professionals to focus solely on brokering the sale of MOBs – and before a growing number of commercial real estate (CRE) firms began dedicating teams fully focused on the product type – one professional based on the West Coast was doing just that.

His name, as many involved in the sector know, is John Smelter, who, prior to 2020, worked in investment real estate sales for 35 years, 30 of those being focused primarily on healthcare real estate (HRE) facilities, with a heavy emphasis on MOBs. A good portion of his career was spent in the San Diego office of Calabasas, Calif.-based Marcus & Millichap Inc. (NYSE: MMI), where he spent 22 years as senior director of the firm's Healthcare Real Estate Group and was, according to his biography, the "No.1 MOB agent in the United States or the western 11 states for over 20 years."

"John was brokering medical office buildings way before medical office was the 'cool' sector of real estate that it is today, more than 30 years ago when we both got into the business," says Thomas W. "Tommy" Tift III, executive VP with the Healthcare Group of Lincoln Harris CSG and, previously, the president, CEO and founder of Atlanta-based HealthAmerica Realty Group, a 25-year-old firm focused on the HRE sector.

"He was for many years the top broker in the country when it came to medical office, going back to the days, believe it or not, when cap rates for MOBs were as high as 14 percent because most people involved in real estate did not understand the healthcare real estate sector," Mr. Tift recalls.



John Smelter

Well, after a hiatus from the business, during which time he traveled and prepared to return to the HRE sector in some capacity, Mr. Smelter has indeed returned.

But instead of selling MOBs, he's now buying them, as Mr. Smelter was recently named senior managing director with White Oak Healthcare MOB Holdings and is part of the team that is building a new business line in White Oak MOB REIT LLC. White Oak Healthcare MOB Holdings was established in the third quarter (Q3) of 2020 and is part of White Oak Healthcare Finance and its parent organization, San Francisco-based White Oak Global Advisors.

The REIT is led by David Lynn, president and chief investment officer, who was previously the founder, chairman and CEO of Everest Healthcare Properties LLC, a private equity real estate firm.

We recently caught up with Mr. Smelter, a longtime member of the **HREI**™ Editorial Advisory Board, to ask him to reflect a bit on his years in the sector and to find out more about his new role with White Oak Healthcare MOB Holdings.

HREI: John, first off, congratulations on your new role with White Oak Healthcare MOB Holdings. Please tell us what you will be focusing on and how you ended up joining the firm.

Smelter: My primary responsibilities are implementing and developing company strategy, managing acquisitions, supervising the UPREIT platform, new business development and building long-term client relationships. As for joining White Oak, within a few months of resigning from Marcus & Millichap, I received many calls from clients that wanted me to come back as their broker. Most of my clients recommended that I start my own company. I also received calls from brokerage firms that wanted me to head up their healthcare real estate divisions. I told everyone that I was enjoying my time off but that I may have interest in getting back in the industry on a full-time basis in a year or so, as at that time I was not proactively searching for a job but rather was only in a reactive mode. In addition to the brokerage inquiries, I also received calls from private equity firms to join as a partner. Of all the calls I received, I started to realize that I would really enjoy getting back in the industry as a principal.

David Lynn, whom I originally met shortly after he started Everest Healthcare Properties in 2015, and with whom I worked on many transactions with and developed an excellent working relationship with, approached me in February to see if I would join him in a new venture. He had sold Everest.

I told him I would really enjoy partnering with him if he started a new firm.

Unfortunately, COVID changed things and I quickly realized it may take a bit longer to get back into healthcare real estate, as most of the equity was frozen. But, as business started to get back on track over the summer, I was seriously considering a position with a startup private equity firm as their CEO when David Lynn called me again in late July. He was announcing that he had received a term sheet from White Oak and that he wanted me to join him. I preferred David's business plan over the company I was considering. Additionally, I wanted to join forces with someone that I had successfully worked with in the past. So, I agreed to join White Oak in October and started in mid-November.

HREI: Please tell us a bit more about White Oak MOB Holdings. For example, what type of transactions are you targeting?

Smelter: White Oak Healthcare MOB Holdings is actively seeking acquisitions of medical office buildings and portfolios across the United States with a target portfolio size of \$1 billion or more. We are buying core, core plus and 'light value-add' medical office buildings with a minimum price of \$10 million to a maximum of \$300 million. We are focused primarily on primary and secondary markets in the United States for the core and core-plus properties that can be on- or off-campus properties. We will also consider tertiary markets for off-campus, value-add properties.

HREI: As a private REIT, are there plans to go public?

Smelter: Great question. We have a business plan that we keep confidential. Like a good coach, I will respond by saying we will focus on our closings each month by hitting our monthly goals. Certainly, by staying focused on our monthly and quarterly goals, we will achieve our annual goals. We are solely focused on building a portfolio of quality MOB assets in excess of \$1 billion and do not have a specific plan to go public at this time.

HREI: The MOB sector has continued to grow over the years, and for good reason, as the product type has proven that it is

a strong investment even during difficult times. But if there is one headwind facing investors, it is perhaps that there doesn't seem to be enough product to meet such strong demand. Are you seeing many opportunities?

Smelter: Medical Office Buildings have been a supply constrained property type since they started to become a popular investment type in the late 1990s. Each year since then, there has been a significant amount of new capital and new buyers entering this small niche market, especially in the last decade. We are seeing plenty of opportunities — both on- and off-market deals — and are excited about our acquisitions and closings. I believe that most owners and brokers will select a buyer not only based on price but also the probability of closing. The probability of closing has many factors that must be considered, such as having the debt and equity to write an all-cash offer, having a substantial track record, having a great reputation and not re-trading at closing. We have assembled a great team with a significant amount of experience, more than 125 years, and we all have all the aforementioned elements in place to successfully compete as one of the top buyers in the United States.

HREI: How is White Oak going about finding opportunities and acquiring properties? Will you compete strongly as well as find off-market, but competing with others?

Smelter: Certainly, we will be competing and we will be looking at all opportunities. We are reviewing both listed properties as well as off-market opportunities that are brought to us by brokers. Additionally, we are buying properties that we source through our business development efforts. We have several unique programs that are very compelling for owners that are considering a sale of their property or portfolio.

HREI: John, you've been in this business and this sector for a long time. What stands out to you as the biggest changes you've seen during your career, perhaps starting with the technical aspects of the business?



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John Smelter
Senior Managing Director
White Oak Healthcare MOB Holdings

Smelter: There are several things that stand out but two are most significant. First, technology has changed our industry. I started in brokerage when we had to look up the ownership of facilities on microfiche machines. I was given a phone, legal pad and kept my client information on 3-by-5 inch index cards. There were no comps, computers or fax machines. We had to meet clients in person to sign listings, look at their properties and do our own rent surveys. It was critically important to know what properties were on the market by looking at the newspaper classified ad sections as well as knowing what had sold in the submarket by doing our own research. In the first 15 years of my real estate career, I specialized in apartment building sales and sold my first MOB six years into my real estate career.

As I became more successful, I had a team of assistants early on that helped me put together photos of all the properties in my submarkets. Eventually, by the late 1980s, we had personal computers and had a subscription to COMPS, a San Diego company that CoStar purchased. When I began putting my medical office database together in 1991, I had binders with a page of every medical office building in Southern California per the COMP submarkets of San Diego, Orange County, Riverside, San Bernardino and Los Angeles counties.

Today, I find myself with three computers on my desk... I have my database of over 8,000 MOB owners, as well as data from Revista and CoStar. I think back at my original proposals and listing offering memorandums as compared

to the proposals later in my career. The information and technology we have available today is significant compared to when I started.

HREI: Continuing with the theme of change, what has changed about the sector itself?

Smelter: Well, MOBs have gone from being one of the least-desirable property types in commercial real estate to being one of the top three most-desired property types, along with industrial warehouse and data centers. I can remember when on-campus MOBs that were subject to a long-term ground lease would only get attention from buyers if the cap rate was above 12 percent.

I would add that the healthcare REITs really changed the cap rates that are associated with leasehold projects, as well as other institutional buyers, with private equity firms following suit years later.

As for how much this sector has grown, I can remember being called, in 1999, by folks with BOMA (the Building Owners and Manager Association International) and being asked if I would attend a conference in San Francisco, if they indeed had a conference for healthcare real estate. I recall that Bob Rosenthal, the founder of Pacific Medical Buildings (today known as PMB), said he also received a call. Both of us helped contact some of the other larger MOB owners in California, asking them to attend what turned out to be the first BOMA (MOB + Healthcare Real Estate Conference.) Approximately two dozen people attended the conference. Certainly, things have

changed a lot since then, but the MOB market remains a somewhat small niche market that pales in comparison to both the number of sales transactions and the dollar volume of sales of other larger property types, such as multifamily, office, industrial and retail.

As I have mentioned, the number of buyers in the sector has grown significantly but so has the number of brokers and brokerage firms. It is surprising to me the number of brokers that have entered into healthcare real estate compared to the other CRE property types with significantly more sales volume. I do not see the supply and demand dynamics changing as new development will not catch up with the demand for medical office in the foreseeable future.

HREI: Do you see the need for MOBs diminishing, what with the advent of new technologies in which to deliver care?

Smelter: No. Even though COVID-19 has changed doctor visits with the increased use of video calls, the growing aging population will not diminish the need for the shortfall of MOB space.

Medical office buildings have outperformed other sectors due to strong fundamentals – such as long-term net leases, strong credit, limited leasing risk – that will continue to strengthen through demographic forces and systematic changes in the healthcare delivery model. Plus, limited supply and robust demand for MOBs will continue as procedures are moved from inpatient settings to outpatient facilities and new

construction does not keep up with the demand accelerants of the aging population and increasing lifespans amplify these trends.

As far as I see it, this growth is anticipated to create greater demand for healthcare services and the healthcare facilities as the country is at the front end of a demographic tsunami. The population of people over 65 is expected to increase from 40 million in 2010 to 92 million in 2060.

On the other hand, owners of traditional office buildings will continue to feel the effect of many tenants downsizing as their staff is working remotely from home, as many companies now realize that their employees are more efficient working from home and most companies are planning to downsize their office footprints.

Historically MOB vacancy rates over the last two decades have varied by 100 to 200 basis points, with MOB vacancies having the lower vacancy rate. I expect this margin to grow significantly in the future, which will only make MOBs more desirable to investors.

HREI: You've had lots of success in this sector for many, many years. To what do you attribute this?

Smelter: It is a mindset that you must have. I always tried to be number one in everything in my life, starting with sports and carrying those same expectations into my professional career. A good work ethic should come naturally for people who want to exceed. I am certainly a perfectionist, as many of my team members and clients have learned throughout my career.

In real estate, I always have said that I am only as good as my last closing. No matter how substantial my market share might be or how strong my track record was, I knew that I had to earn being one of the top agents each and every day.

It is important to specialize and know your market. Soon after I started in

commercial real estate in multifamily, I decided to focus on apartment properties of 50 to 100 units in San Diego County. I toured every property and met every owner. My client relationships ultimately determined my business success, and I certainly sold properties under 50 units and above 100 units.

When I started in MOB sales a few years later, I did the same thing and toured all of the properties as I was building my data base in Southern California. Again, I was specialized but in a niche market that had little or no competition. But even so, my strategy was to know the properties and every submarket before calling on and meeting the clients. In addition to property and market knowledge, I've always thought that it is equally important to know your client and take interest in their business objectives. Many clients also became friends and we played golf, had family dinners, took ski trips together, etc.

I have always enjoyed meeting clients, looking at new assets and figuring out ways to increase the NOI (net operating income) before going to market. I have always put my clients' interests before mine. It is not about the fees earned but rather accomplishing your clients' objectives and being better than your competition.

With my new role at White Oak, it will be very similar with property/market knowledge and developing long-term client relationships by creatively meeting their objectives with our platform.

HREI: In addition to having such a long tenure in the sector, do you think you were the first broker to expand your services to a national platform?

Smelter: Yes, absolutely. After dominating MOB sales in the western part of the country, I decided to take my business nationally and I built a national database of all properties in excess of 20,000 square feet in MSAs (metropolitan statistical areas) with populations exceeding 1 million. During that time, I also started writing my

National Medical Office Newsletter, which I authored for more than two decades. Until 2010, there were only a handful of investment banking firms and my team at Marcus & Millichap that had the bulk of MOB sales in the U.S. After 2010, most of the national brokerage firms had started healthcare real estate divisions.

HREI: John, when you do take some time off from your job, what do you enjoy doing most? Read any good books lately?

Smelter: Anyone who knows me will tell you that skiing is my favorite sport. I have relocated to the Vail, Colo., area and love skiing the double diamond-rated runs. Bring on the powder, moguls and tree skiing! When it is not ski season, golf is a very close second favorite sport of mine. I really enjoy playing beautiful and challenging courses. As a competitive tennis player in school, tennis still ranks as my third sport, but unfortunately my sons now beat me at tennis, unlike in golf and skiing.

My other interests include hiking with my dog, body surfing, swimming, working out in the gym, driving my sports car or motorcycles and last but certainly not least is spending time with family and friends. World travel will also be a top priority if and when my work schedule allows me to have a few weeks to vacation.

As far as books go, I must admit that I have not picked up a book in almost a year despite the interesting times we are in with COVID-19, when you would think the opposite would be true. However, being outdoors is my preference and there is always something I find myself doing outside in my spare time. I just recently picked up cross country skiing just in case the alpine ski resorts close early again this year.

When I am indoors, I am typically working, but when I have free time I like watching sports or a good movie. Although I have not read any books lately, I read the WSJ, business magazines and of course the best publication of all, **Healthcare Real Estate Insights™**. □