2025 Medical Outpatient Building Perspective

Healthcare providers expand outpatient services, driving an increase in innovation and MOB occupancy

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Research
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Key findings

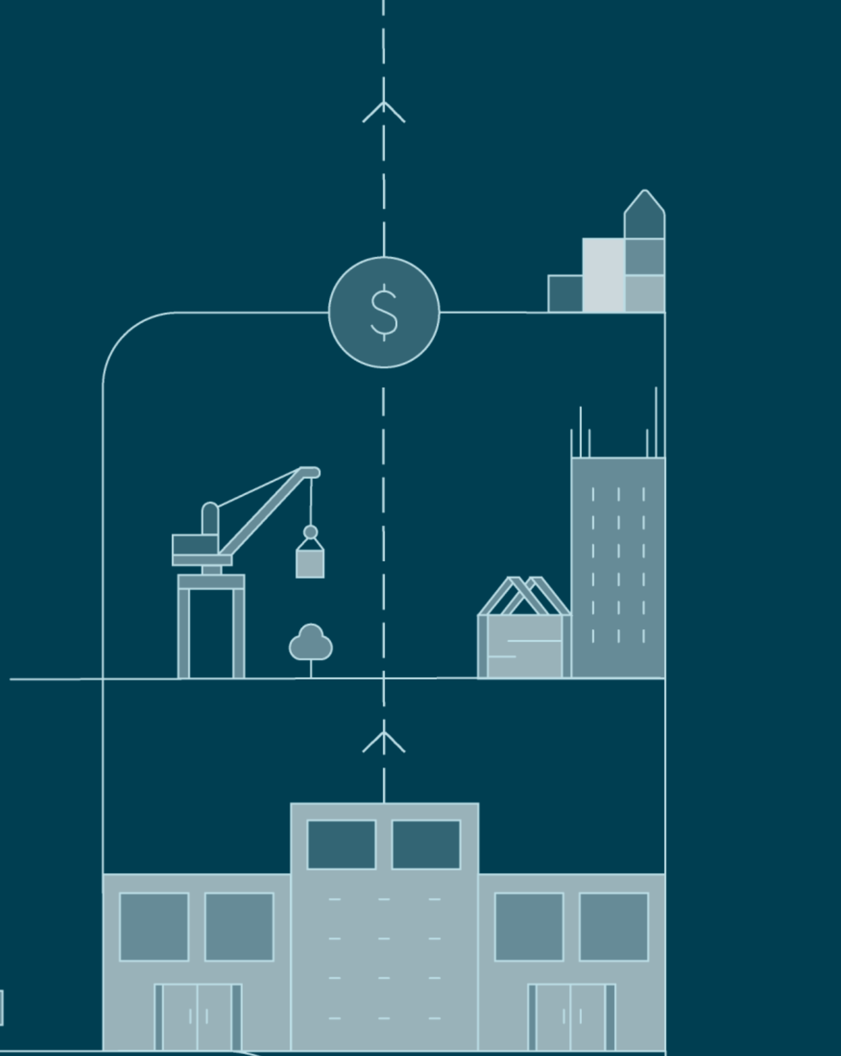
1 Health systems and corporate medical groups are leading the way in the outpatient shift

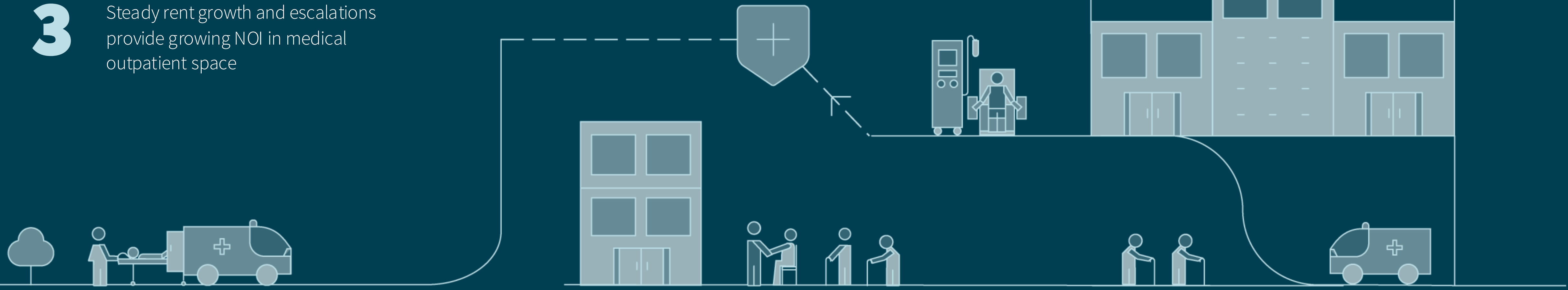
2 Rising occupancy and limited construction for purpose-built MOBs may cause increased spillover into adjacent property types

3 Steady rent growth and escalations provide growing NOI in medical outpatient space

4 Population growth is driving expansion in Sunbelt markets, but established brands also bolster growth

5 Medical buildings continue to offer stability for investors, and health systems also see benefits to ownership

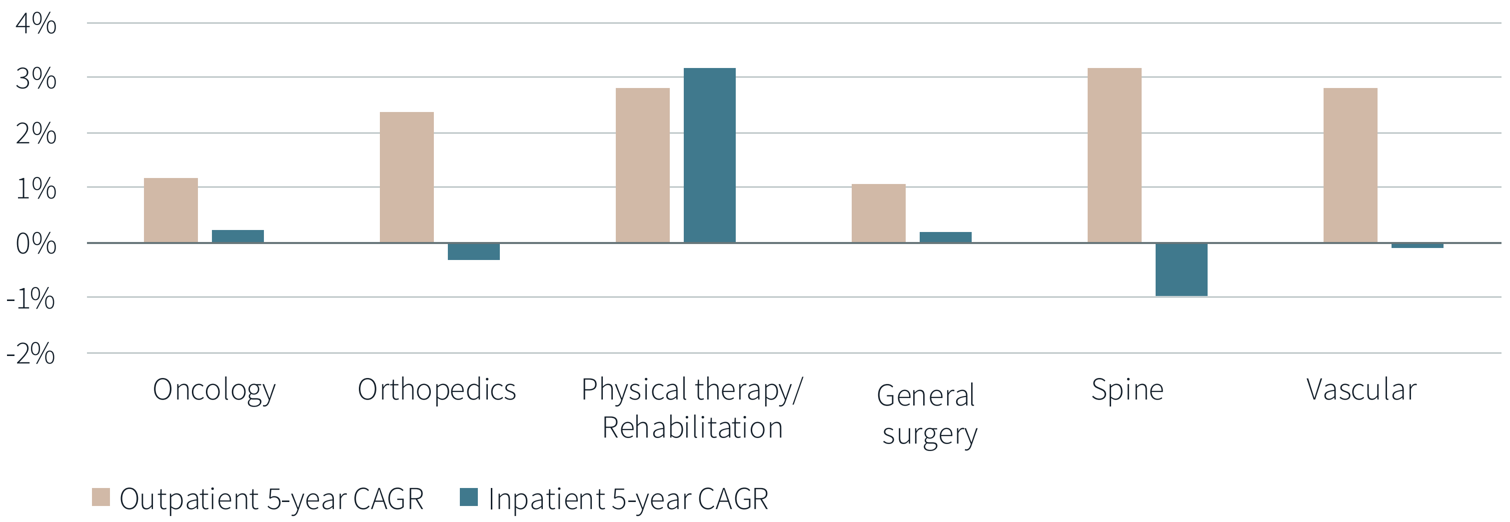




1 Health systems and corporate medical groups are leading the way in the outpatient shift

Demand for healthcare services continues to accelerate, with outpatient volumes in the U.S. anticipated to grow 10.6% and inpatient volumes increasing 0.9% over the next five years, according to Advisory Board. An aging population and increasing disease prevalence continues to drive the overall need for care. The shift in the site of care from inpatient to outpatient will continue as technology and patient preference are driving advances in medical care, making treatments less expensive, safer and less invasive.

Service lines such as orthopedics, spine, vascular and oncology are seeing rapid growth in outpatient settings



Sources: Advisory Board Market Scenario Planner, JLL Research

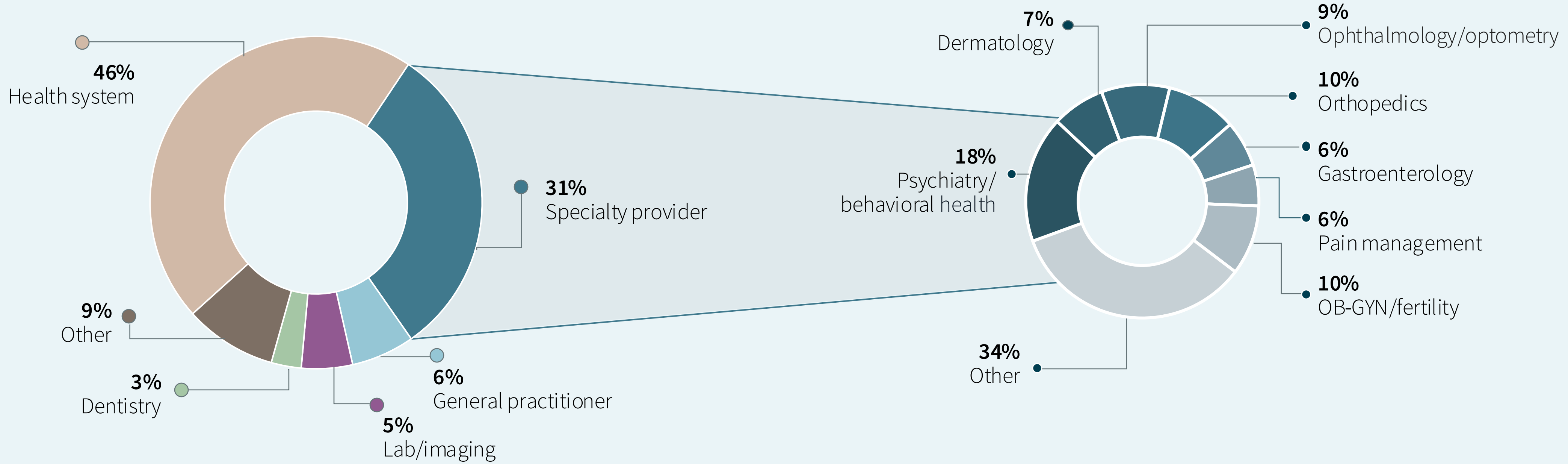
Health systems increasingly are implementing an ambulatory care strategy to complement their inpatient strategy. Benefits include following a patient throughout their care continuum, increasing the revenue capture and providing better health outcomes through care coordination. While historically hospitals achieved higher margins on inpatient care, rising labor costs have squeezed the margin on these labor-intensive services. From December 2023 to December 2024, outpatient revenue per calendar day increased 10% for hospitals in Kaufman Hall's National Hospital Flash Report , compared to 5% for inpatient revenue per calendar day. Top-performing health systems are expanding outpatient care and other revenue streams.

To drive outpatient growth, health systems are expanding their real estate footprint and either acquiring or contracting with physician groups to add specialties. 16,000 additional physicians became employees of a hospital system from 2022 to 2023, according to a report from PAI and Avalere.

Health systems accounted for 46% of the 2.9 million square feet of leases signed in 2024 in JLL's database. Specialty providers constituted 31% of the medical office space leased, with psychiatrists and behavioral health providers making up the largest group of these, accounting for 18% of this square footage.

Medical office leases signed in 2024

Specialty providers



Sources: JLL Research, Medical office leases >10,000 s.f.

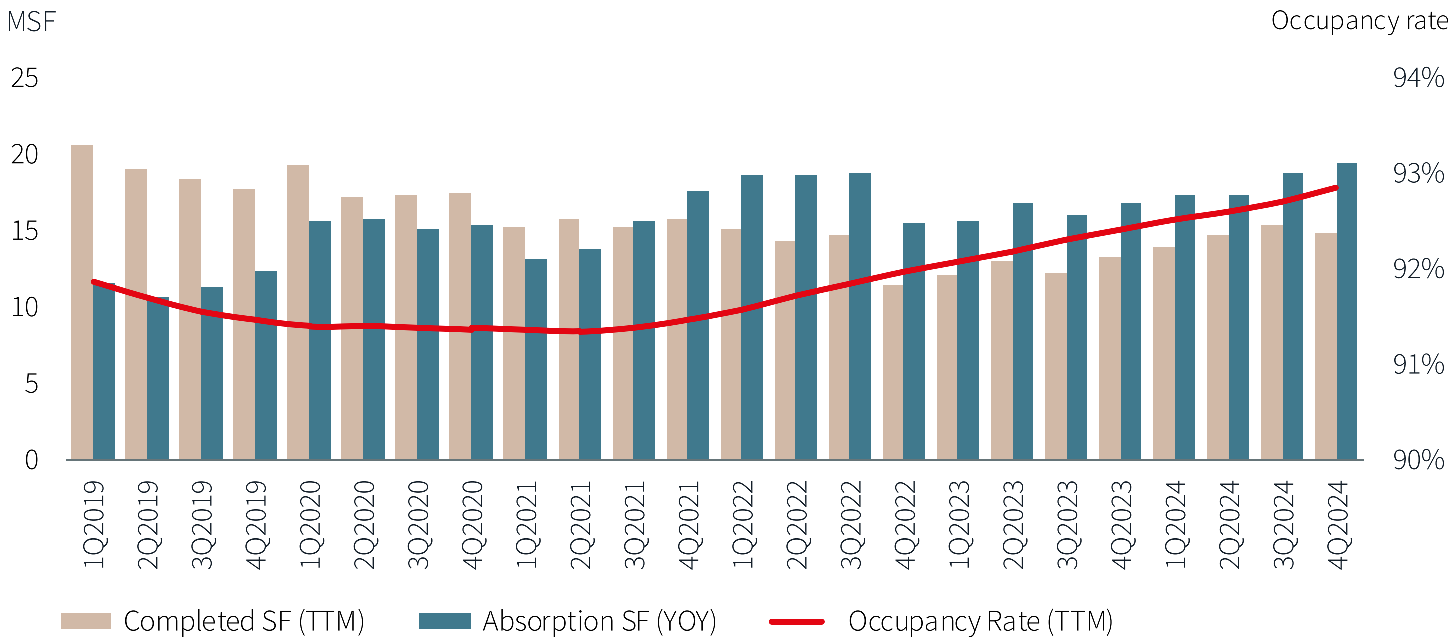
Finding the right location to serve patients and grow market share is top priority

Identifying the right geography for an outpatient service is the top concern for health systems and providers. Healthcare tenants are more akin to retailers than to office tenants and focused on speed to gain market share when opening a new location. Their site selection decision is complex. Providers examine patient data and demographics of the surrounding communities to identify gaps in care, weighing demographic growth, insurance coverage, referral patterns and proximity to other services.

2 Rising occupancy and limited construction for purpose-built MOBs may cause increased spillover into adjacent property types

With steady demand from health systems, corporate medical groups and independent providers, absorption for medical outpatient buildings (MOB) continued to accelerate in Q4 2024. Absorption topped 19 million square feet for the top 100 markets, an increase of 15% from full-year 2023. Strong demand and limited construction have driven occupancy steadily upward. MOB occupancy increased to 92.8% in Q4 2024, up from 92.4% one year prior.

MOBs are defined by how much is medical tenancy or spaces built out for such tenants (typically 50-70%). However, outpatient services have also expended into traditional office properties (typically for lower-acuity tenants) or standalone or in-line retail especially if there is limited MOB availability in the target area.



Sources: JLL Research, Revista

Construction of MOBs remains subdued because of elevated construction costs, developers' need for higher return on costs due to an increased inflationary environment and added volatility in the larger capital markets, and tenants' desire to hold down rental expenses. Borrowing costs have increased as interest rates rose from 2022 to 2023. The decline in construction starts began in late 2022 and accelerated in 2023 and 2024, leaving limited new supply for tenants in 2024. Construction starts were at an all-time low in Q4 2024 at only 0.8% of inventory, compared to 2.1% of inventory in Q4 2017. Construction was 92% preleased in Q4 2024, leaving options limited for tenants looking for new space.

Health systems led all other owners in construction starts in 2024, with 53% of the total square footage. As recently as 2019, hospitals and health systems owned only 41% of new MOB starts. New MOB construction has been centered around high-value services such as cancer and cardiovascular services. New construction is often more efficient for high-acuity uses than renovating existing buildings when considering the addition of the necessary electrical, plumbing and technology. Leading health systems with strong credit ratings and doctor groups in place can undertake new development to expand services and revenue, although obtaining favorable financing in the high-interest-rate environment can still be a challenge.

Developers and investors have taken a larger role in conversions and renovations — composing 59% and 32% respectively (although these are only 13% of the total square footage). Buildings undertaken by developers and investors in 2024 were smaller as well — the average size of a health system start was over 100,000 SF and the average for an investor was around 35,000 square footage.

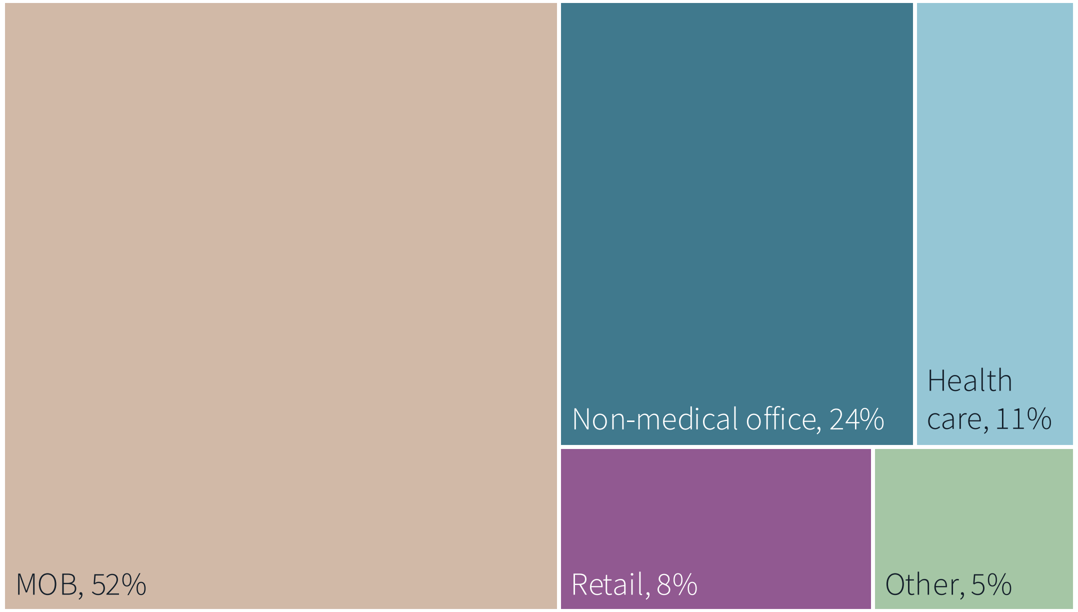
With limited availability and limited new spaces on the horizon, healthcare tenants, especially those of low to mid-acuity, are increasingly considering office and retail space that is near their target patient population or near a hospital campus. However, medical office conversions for higher acuity or resource-intensive services like imaging can be difficult due to the cost of renovations and adding electrical and plumbing. Traditional office landlords may also be hesitant to lease to healthcare uses given increased foot traffic, negative impact to parking ratios and increases in operating costs.

Some providers are choosing to purchase rather than lease space due to favorable bank financing and limited availability in MOB product. The number of medical office condo sales increased 12.9% from 2023 to 2024, and transaction volumes increased 11.4%, according to CoStar data. Users comprised 24% of this volume, while private investors were 69% of the purchases.

While geography and proximity to patients is essential and oftentimes the first priority when opening a new location, tenants also need to understand the cost to occupy and whether they can achieve a healthy margin. Balancing expansion with cost are key goals for health systems and providers: adding new services and achieving organizational efficiency were top goals for healthcare respondents in JLL's 2024 Future of Work Survey.

With location being the top factor in opening a new outpatient site, physicians consider a variety of property types

Property type for offices of physicians moving into new space in 2024

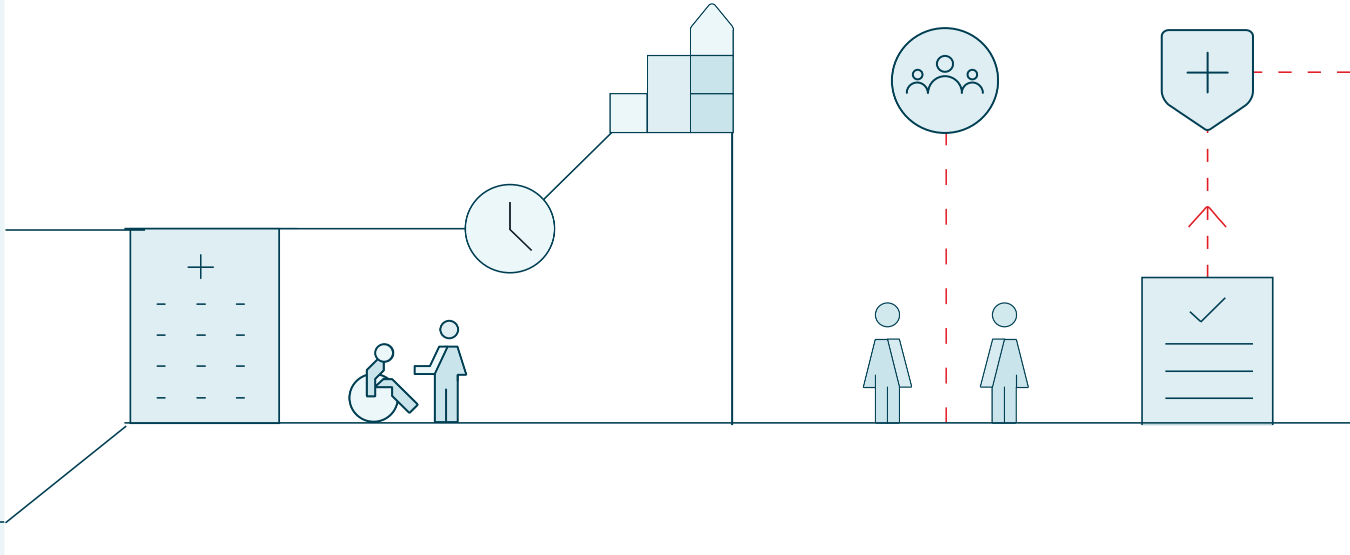


Sources: JLL Research, CoStar

3 Steady rent growth and escalations provide growing NOI in medical outpatient space

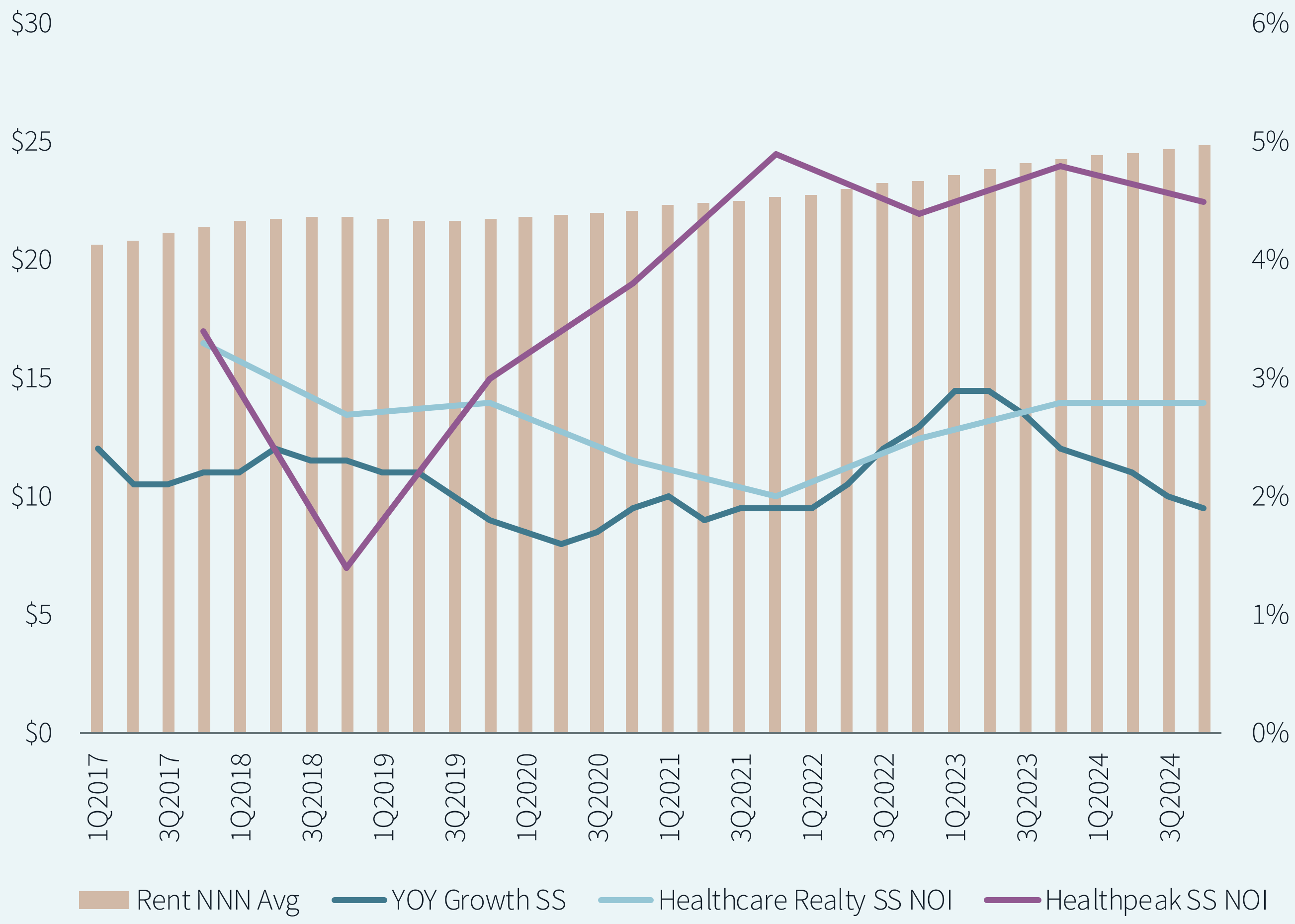
Average asking rents for MOB product continue to grow; however, the year-over-year growth rate for asking rents slowed from 3.7% in 2023 to 2.5% in 2024. Like with general office product, rates at the top end of the MOB market have grown faster than mid and low-tier rents. Rents in the 90th percentile of Revista's Top 100 markets grew at a 2.4% compounded annual growth rate (CAGR) from 2019 to 2024, compared to a 1.8% CAGR for rates in the 50th percentile.

For tenants, looking at past rent growth is not fully indicative of their cost, as rate escalations (typically 3%) exceed year-over-year same-store rent growth of 1.9%. Due to their slim operating margins, healthcare tenants cannot afford steep jumps in rent. Health system average operating margins were 4.9% in December 2024 according to the Kaufman Hall Operating Margin Index. Additionally, practices are facing declining reimbursement costs from Medicare, with the conversion factor dropping by 2.83% from 2024 to 2025.



With such small availability (only 6.9% in Q4 2024), advertised rates represent only part of the picture on income growth. Many tenants renew in place — MOB-focused REITs posted retention rates of over 80% in Q3 2024 according to a Green Street report, and many health system owners do not publicly advertise space and rents. Healthcare REITs continue to see steady net operating income (NOI) growth. Escalations for new leases in 2024 averaged 3%, according to JLL data, and with terms averaging 107 months for new leases, investors have steady increases locked in. With increasing cost pressures on tenants, same-store MOB rent growth will continue to be steady but not see outsized jumps in rent like seen in select office submarkets with a flight to quality.

Steady but slow asking rent growth masks NOI growth for MOB properties



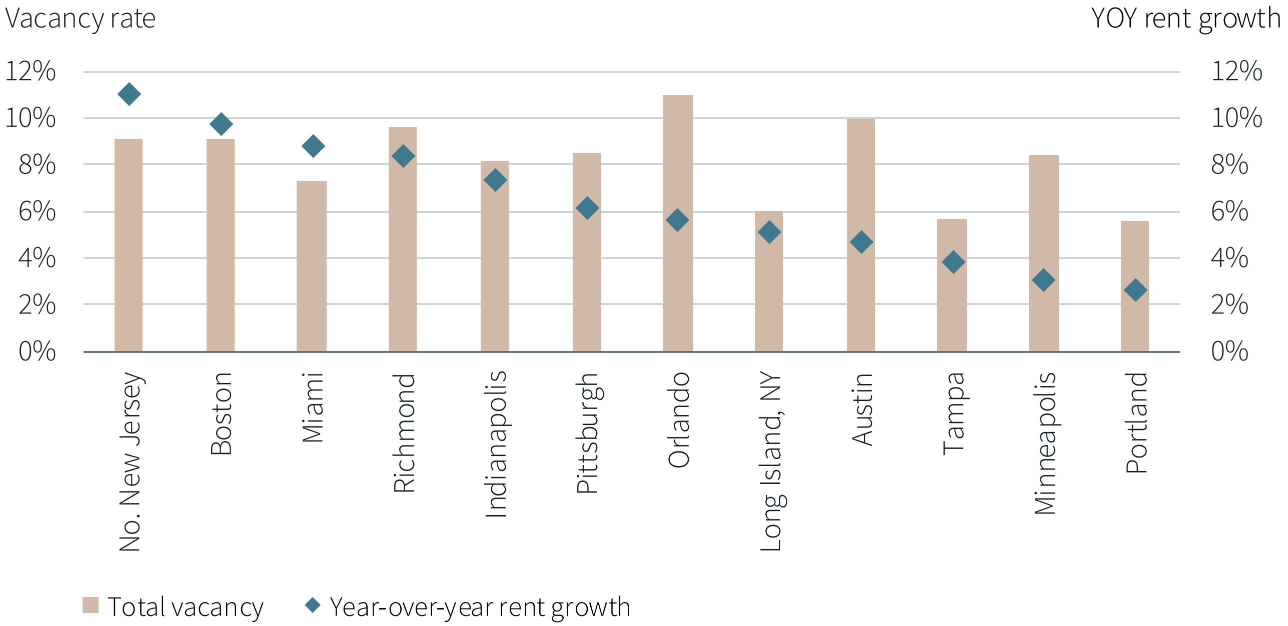
Sources: JLL Research, Revista, Green Street

4 Population growth is driving expansion in Sunbelt markets, but established brands also bolster growth

Rents

Markets with strong rent growth and occupancy were spread throughout the country, and four Sunbelt markets saw rent growth of over 3% from 2023-2024. Other markets, such as Boston and Northern New Jersey, are bolstered by the presence of strong, growing health systems. Leading cutting-edge health systems have strong brand recognition and are able to grow through fundraising and drawing high-value specialties, supporting the medical ecosystem in the market. All but one of the top markets for rent growth have vacancy under 10%, and as healthcare is highly localized, certain areas and submarkets have even tighter supply.

Top markets by rent growth 2023-2024



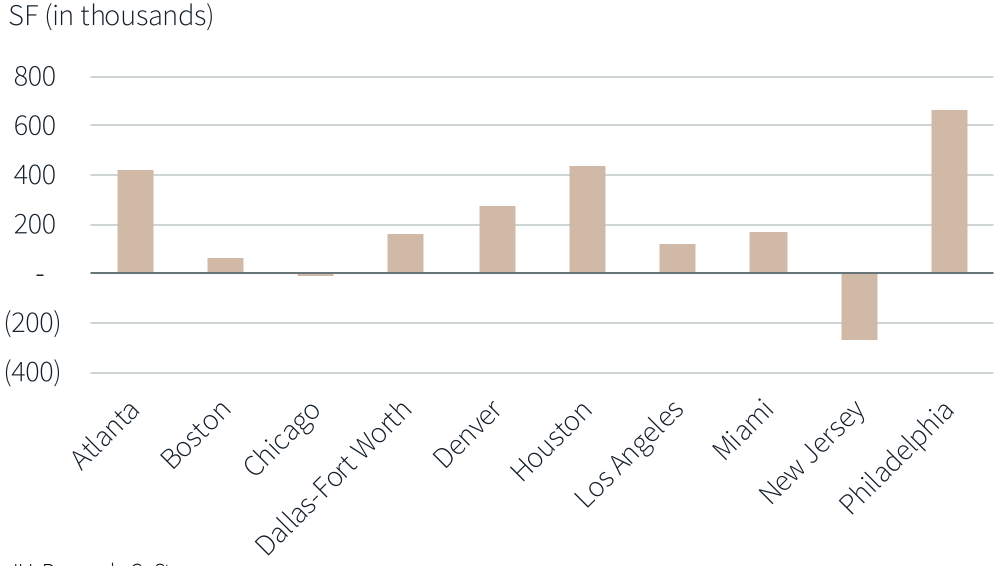
Sources: JLL Research, CoStar

Occupancy

The New York area led all markets with new outpatient services move-ins (to both leased and owned office space) in 2024. In Manhattan especially, medical space is not concentrated in MOBs, and over two-thirds of office space newly occupied by healthcare tenants in 2024 was in non-medical properties (for this reason, New York is not shown in the charts below). Just across the river, New Jersey saw negative net absorption from tenants upgrading from class B and C space.

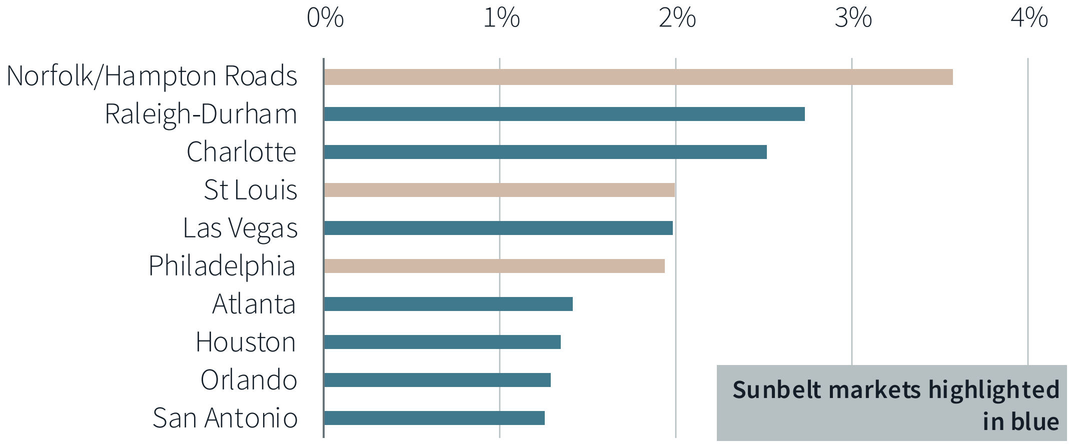
Philadelphia led all markets for net absorption in 2024, while Houston and Atlanta both had over 400,000 square feet of net absorption. Norfolk/Hampton Roads, Virginia saw the highest rate of absorption compared to inventory, and just a state to the south, two North Carolina markets led seven other seven Sunbelt markets with rapid occupancy growth. A favorable climate and low cost of living continue to drive population growth in the South, especially for those over 55.

2024 MOB net absorption, largest markets



JLL Research, CoStar

2024 MOB net absorption as percent of inventory

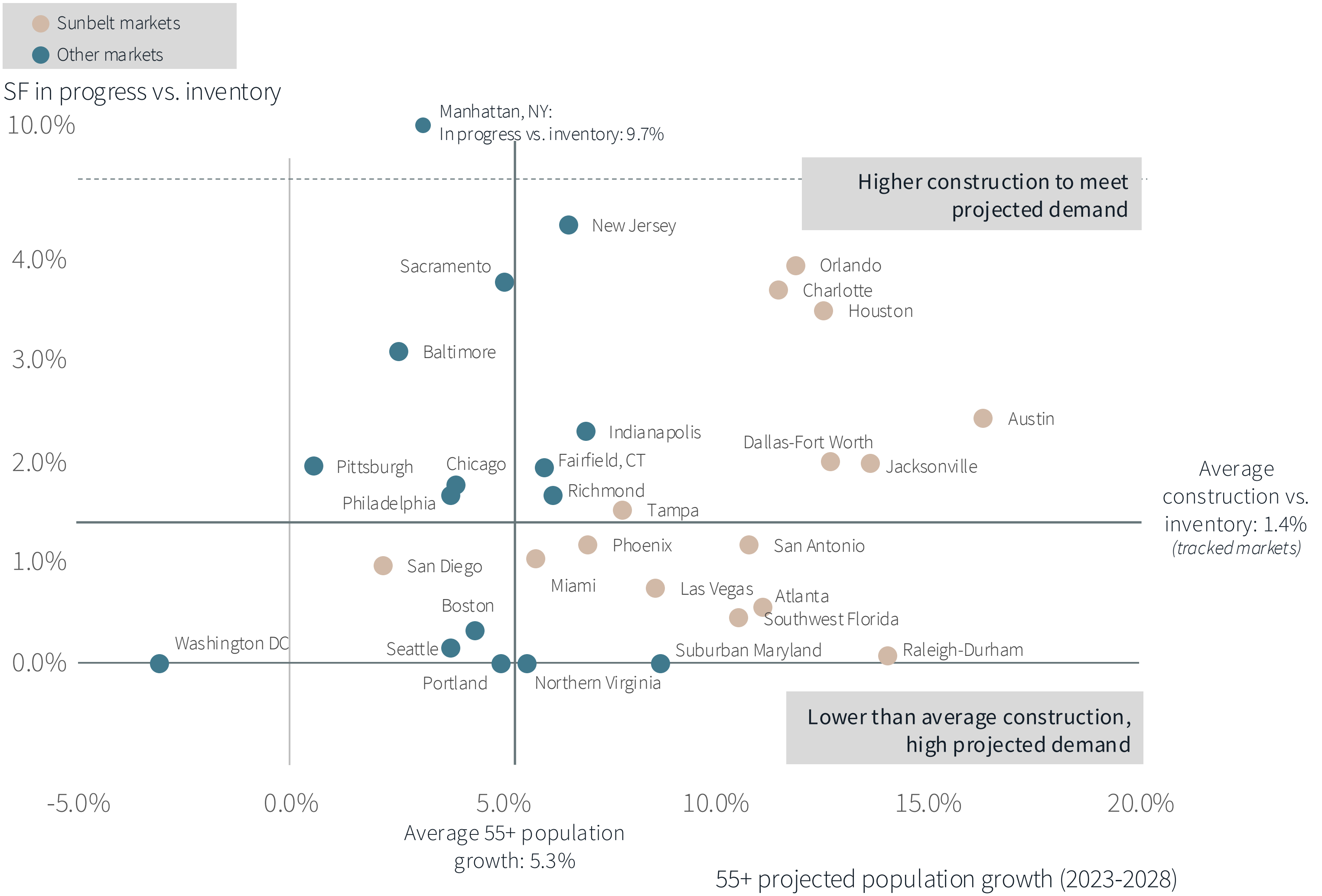


Construction

New construction in many markets has occurred in the suburbs, chasing population growth and supporting hospital campus expansions. Additionally, renovations or replacements of urban buildings have added additional hospital outpatient space to main hospital campuses, especially at leading health systems in established markets such as New York and Chicago.

Manhattan and Northern New Jersey saw the highest percentage of construction in progress with respect to its inventory in 2024. Behind New Jersey, Houston has the largest amount of inventory under construction with 1.1 million square feet. New product is supporting expansions to the Texas Medical Center and in the suburbs to support its high population growth. Markets in the bottom right quadrant of the chart have higher than average 55+ population growth but lower levels of construction, which could present an opportunity for MOB expansion.

55+ Population growth vs. construction



Sources: JLL Research, CoStar, Revista, Lightcast

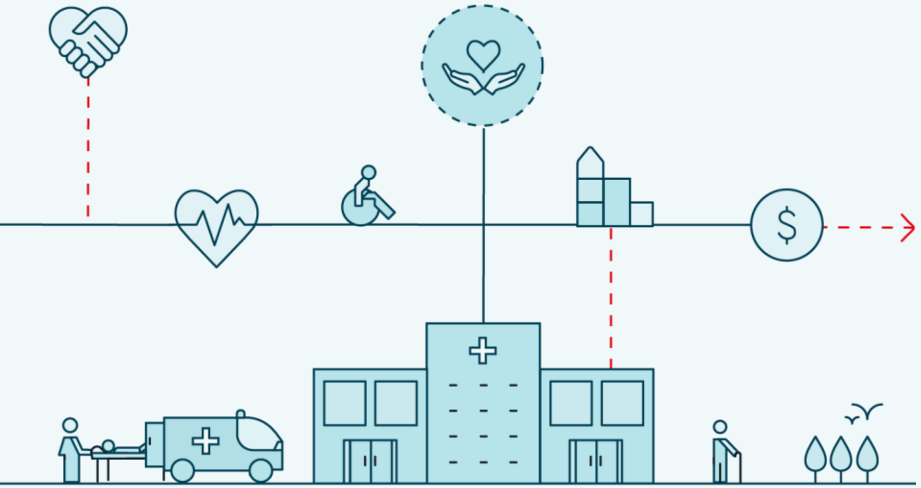
5 Medical buildings continue to offer stability for investors, and health systems also see benefits to ownership

Due to the stability of their tenancy and higher likelihood of renewal, medical outpatient buildings remain an attractive asset class for investors.

Medical outpatient transaction volume increased in 2024, as the $4.6 billion acquisition of Physicians Realty Trust by Healthpeak bolstered volumes. Even without this entity-level transaction, portfolio and individual property sales marked a slight year-over-year increase in 2024.

Health systems and providers own approximately 50% of the 1.4 billion stock of medical outpatient buildings. With increased focus on their outpatient strategies, some health systems value ownership in being able to curate their own tenant mix to drive revenue within their health systems. If lending costs fall, these health systems may be active buyers of adjacent real estate and development sites.

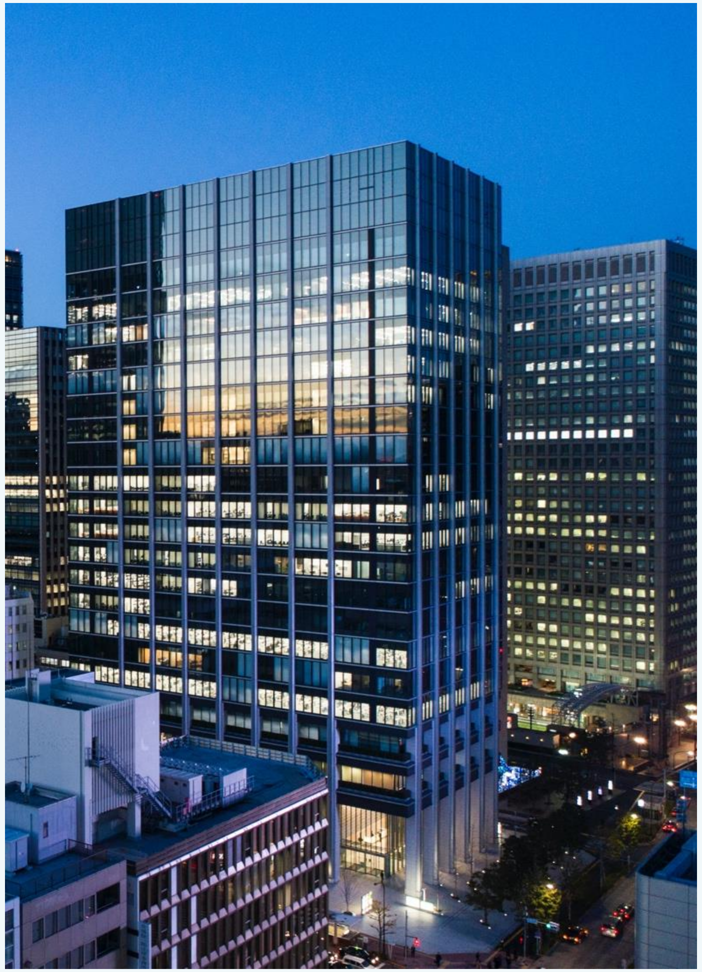
	Medical outpatient buildings		Office	
Occupancy Q4 2024	92.8%	(Revista)	77.7%	(JLL Research)
Average term (new leases over 10,000 s.f.)	107 months	(healthcare leases) (JLL Research)	107 months	(JLL Research)
Asking rent growth (same store 2023 Q4–2024 Q4)	1.9%	(Revista)	0.2%	(JLL Research)
Total return Q4 2024	1.4%	(NCREIF)	-0.6%	(NCREIF)



In 2025, investors will increasingly consider opportunities to re-tenant existing office with medical uses to add value. To be perceived as a "medical outpatient building" upon sale, a property typically has 70% or higher medical tenancy. However, adding some lower-acuity uses below this threshold can benefit a property through increasing the weighted average lease term (WALT) and renewal likelihood of tenants.

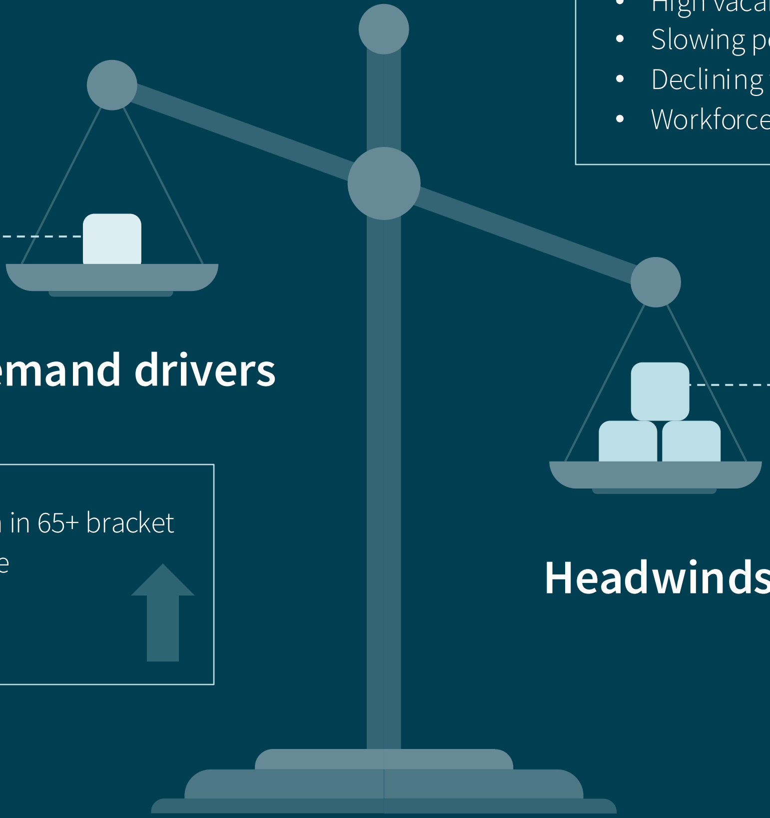
What to consider when converting an office to an MOB:

- Tenant improvement allowances may need to be higher than traditional office
- To attract general practitioners or higher acuity tenants, additional plumbing and electrical will be needed
- Not every building can support medical uses — evaluate the building with an expert
- Health practitioners have tight margins that they need to keep steady or increase, so keep this in mind when pushing rents



Future perspective

Looking ahead to 2025 and beyond, healthcare demand is strong from an aging population and increased disease prevalence, combined with a surge in outpatient demand and the ever-present need for services near growing populations. However, the shift of sites of care even further to the home or telehealth may reduce demand for purpose-built medical outpatient space. Additionally, slowing long-term population growth, rising costs for supplies and labor and tumult within the health insurance sector create headwinds for the sector. The change in political administration and uncertainty of policy from an untested Health and Human Services lead are likely to shake up the sector.



Demand drivers

- Population growth in 65+ bracket
- Disease prevalence
- Population shifts
- Site of care shift

Headwinds

- Shift to home health and telehealth
- High vacancy in other property types
- Slowing population growth
- Declining trust in U.S. healthcare system
- Workforce shortages

Open questions

- Will insurance coverage decline from policy changes?
- Will there be increased focus on primary care?
- Will the shift to value-based care from a fee-for-service model accelerate?
- How will tariffs and other policy changes impact health system expenses?

Here are some perspectives on what's ahead:

For developers

The low construction environment will not abate unless interest rates drop and rising prices for materials costs slow. Potential (or actual) tariffs and labor shortages will exacerbate the slowdown. Markets with high land and labor costs will be especially difficult for developers. Partnerships with health systems adding high-value services will continue, and with strong demand and fundamentals for medical space, developers will try to achieve the Goldilocks balance between construction cost and providers' rent budget. Examining community need for high-value services can help in justifying demand at the necessary rents and tenant improvement allowances.

For health systems

Lender activity is picking up heading into 2025, and all-in borrowing costs are easing, making it easier to invest in system growth. Certificate of Need laws that limit development (such as in the Atlanta market, which has high population growth and low construction) are being revisited, and legislation has been introduced in many states to loosen restrictions. Systems with strong brand recognition are seeing volume growth, and fundraising can help finance expansions especially for services such as pediatrics.

For tenants

Occupancy will continue to rise for purpose-built medical outpatient space, increasing competition for prime spaces. In most markets, rental rate growth will continue to grow steadily but not rapidly, and concessions are expected to be stable, even as availability is increasingly constrained. Tenants' cost consciousness and ability to consider other property types will limit rent growth. However, many office landlords are hesitant to lease to medical uses due to increased foot traffic and high TI requirements. New locations will continue to be driven by patient population, and savvy tenants will evaluate how the cost of buildout and total occupancy costs affect their margins before signing a lease.

For investors

Existing medical outpatient space continues to provide steady returns, and investors continue to seek to expand their allocations to alternatives sectors. Medical properties, together with seniors housing, are the largest alternatives sectors, affording investors the ability to gain greater scale. Asset values have stabilized, borrowing costs marked some easing at various points in 2024 vs. 2023 levels, and cap rates stand to mark some compression during 2025 amid increased investor bidding activity and healthy debt markets.

Conversions from traditional office to medical office face challenges as properties confront physical challenges from low ceiling heights and lack of sustainability features. As location and proximity to other providers is key, many low-performing office buildings are not candidates for medical uses. However, retail properties can often be attractive to healthcare tenants due to open layouts and proximity to consumers.

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