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Life Sciences: A Burgeoning Asset Class

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COVID-19 put life sciences in the spotlight, stimulating further interest from commercial real estate companies in an asset class increasingly earmarked for growth.

In the past decade, growth in life sciences-related employment has been three times stronger than total United States employment. With vacancy levels in the U.S. below 9%, lab rent delivering high compound annual growth rates (CAGRs), supply-demand imbalance and strong market fundamentals, the sector appears to be increasingly attractive[1].

Growth drivers

Over the past 10 years, the sector has been driven by factors such as increased life span, and technology and artificial intelligence facilitating scientific breakthroughs. This has catalyzed growth in funding, outsourcing and decentralization.

"Historically, the sector comprised a number of vertically integrated big players," says Transwestern life science broker David Klein. "Today, innovation is mostly funded by venture capital and private equity. More decentralized capital inflows mean a broader base of investment and growth of the industry well beyond the major bio-pharmas. COVID-19 has stimulated a sector already stimulated prior to the pandemic."

Funding availability—a crucial component for research and development—is strong. And according to MassBioEd, funding is being made available to biotech earlier than before, with about 60% coming from new investors.

The importance of life science sclusters

Life sciences is characterized by clusters. STEM institutions expand the science workforce and hatch new technologies. A nucleus of educators, researchers, investors, entrepreneurs and regulatory officials forms in a close-knit collegial atmosphere around which companies cluster. "Employees often do fairly short stints at companies. They may specialize in a certain stage of discovery and so will move around after their company matures to the next stage, says Carolyn Wheatley, Vice President of the Life Science Practice Group at CBRE.

"Large pharma and biotechs are interdependent. Rather than limiting themselves to only their own innovation being done in-house, large pharma companies position themselves near startups, so that they can absorb those that are launching new technologies."

Liz Berthelette, Director of Research at Newmark, reinforces this. "Clustering (means) you're with likeminded people. There are many stories about the birth of Kendall Square in Cambridge. You're out having lunch and getting access to people in the industry. Spontaneous meetings (are) where innovation happens."

Yet traditional clusters are expanding. Says Berthelette: "As traditional areas like Kendall Square have little to no vacancy and high lease rates (>USD100 SF), other clusters—with good transit connectivity—continue to emerge. Once you get one or two tenants to move, more tend to be right behind them."

The opportunity for commercial real estate

Breakthrough Properties[2] states: "Creating a life science ecosystem takes much more than fantastic science... It requires high-quality lab facilities to create an environment that fosters innovation."

The template to create lab-ready space is fairly straightforward. While initial fit-out costs may be high, customers (developers or tenants) invariably incur many of these costs. Space is easily let to future customers, at an appreciating rate, given the need to have space available, quickly.

"The opportunity, the kind of science, the team and chemistry behind these teams is what matters most. Decision makers will consider how the building will attract talent. Giving them the spaces that allow for this is important, but not in the same way as seen in other asset classes," says Wheatley.

For start-ups and emerging companies, incubators provide move-in ready lab space, with the supporting resources, facilities and equipment needed to produce valid results. "Real estate considerations can be a distraction from the work of science," explains Klein. And incubators are expanding, enabling start-ups to move through their growth life cycle more quickly and cost-efficiently, in one place.

The pandemic has also highlighted the shortcomings of just-in-time supply chains, with growth in onshoring spurring a shortage of biomanufacturing facilities in some markets.

Cautionary signals

Data suggests that the life sciences industry is relatively recession-proof. While fundamentals are strong, increased competition, changes in the regulatory environment, talent availability, and the push for lower costs could impact its growth.

Currently, the premise of "if you build it, they will come" mainly holds true. Yet with the amount of planned and active spec-builds and conversions of office and industrial space underway, there is a risk that supply will, in time, outstrip demand.

(1) Life sciences 2020: the future is here: Cushman Wakefield

(2) How COVID-19 has fueled unprecedented advances in medicine – STATS ebook