Savills Healthcare – October 2021

SPOTLIGHT
Savills Research

UK Care Homes

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CQC rating analysis • Supply and demand • Government reform

"The quality of care home buildings and of their operators are both vital factors, for residents and for investors"

CQC ratings have a huge impact on fees and occupancy

The Care Quality Commission (CQC) monitor, inspect and regulate elderly care services to make sure they meet fundamental standards of quality and safety

KEY POINTS

22%
Premium paid for 'outstanding' rated homes above 'good'

7%
Uplift in occupancy rate of 'outstanding' homes above 'good'

16%
Premium paid for stock built after 2010

29%
Total investment in 2020 was down on 2019

102
Care homes Aedifica now own, after first investing in 2018/19

7,700
Beds have closed each year since 2016

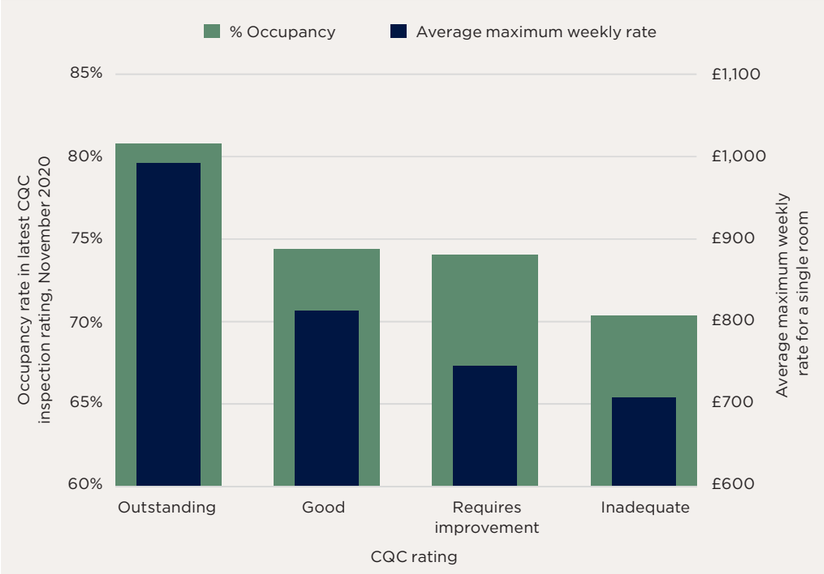
The CQC asks five key questions when inspecting a care service: are they safe, are they effective, are they caring, are they responsive to needs, and are they well led? The five key questions are each then broken down into a further set of questions, which are used as key lines of enquiry by the inspection team. CQC ratings can have a significant impact on the rates charged to service users and a homes occupancy level, meaning providers can charge more for 'outstanding' homes.

Across England, 'outstanding' homes charge 22% more on average compared with 'good' rated homes. Furthermore, the occupancy rate for 'outstanding' rated homes averaged 81% through 2020, compared to 74% for homes rated 'good'.

The quality of care home accommodation is clearly a very important factor in real estate investment but equally, the quality of the operator is also a key component, for both residents and investors.

This has never been more important than over the past 18 months, through the Covid-19 pandemic and the latest CQC inspection ratings for November 2020 show a clear correlation between ratings and occupancy rates.

CQC ratings by occupancy and weekly rate



Source Savills using CQC and A-Z, LaingBuisson

Occupancy is on the up but is still down on pre-pandemic levels

Due to the pandemic, occupancy was negatively impacted across the elderly care sector, with rates only recently starting to improve. Financial reports from the likes of Impact REIT, Target Healthcare, Four Seasons and Bupa all tell similar stories.

Occupancy levels across these operators and investors range from around 88% to 90% in 2020 Q1, falling to between 78% and 82% for the subsequent four quarters, and are only now starting to recover.

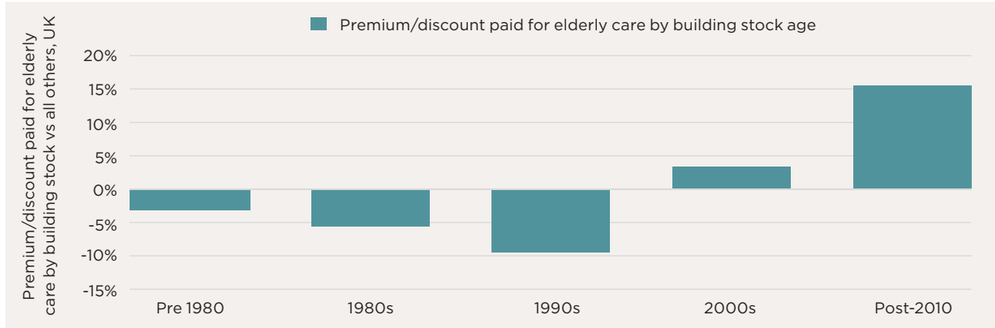
"Of all the beds rated outstanding, 81% have an en-suite"

Elderly care stock built after 2010 demands a higher premium

The majority of the UK's care homes were first registered in the mid-1980s and mid-1990s during a boom in development by the private sector. A large number of those homes were developed in the north of England due to the quantum and affordability of land. It was only by the turn of the century that we saw purpose-built homes begin to form the majority of new registrations.

Homes built since 2010 demand a 16% premium over all other stock across the UK this compares to weekly fees on average being 9% lower than the average for care homes built in the 1990s.

Care home stock by decade of build and premium analysis

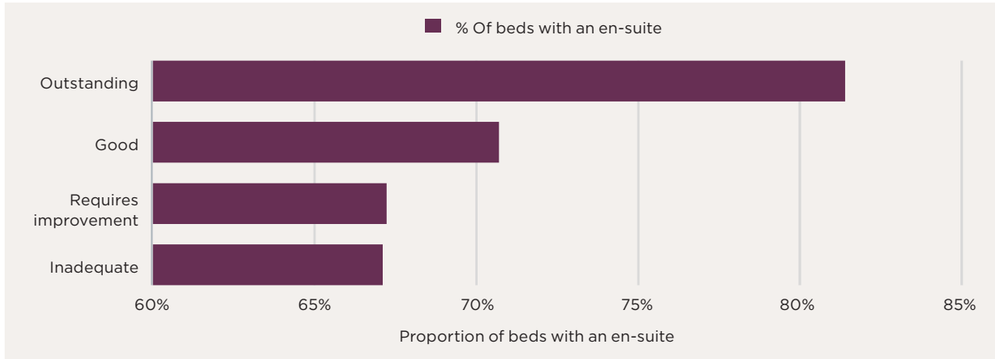


Source Savills using CQC, A-Z

There is a strong correlation between prevalence of en-suite bathrooms and ratings, too. Of all the beds rated 'outstanding', 81% have an en-suite. By contrast, of those rated either 'inadequate' or 'requiring improvement', 67% have an en-suite.

It is a combination of all the above factors - including year of build, percentage of en-suites and CQC rating, as well as other key factors such as location, which contribute to the fees and occupancy a particular care home can expect to achieve.

En-suite beds and CQC rating



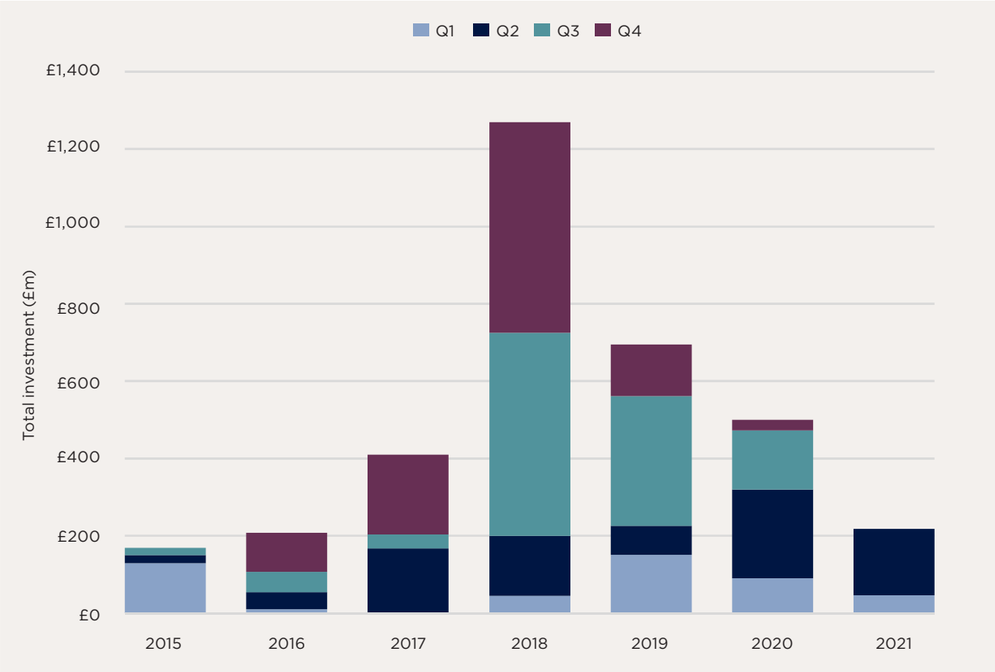
Source Savills using CQC, A-Z

Transactions subdued due to the Covid-19 pandemic

Investment in 2020 was subdued due to the impacts of Covid-19. Although, with the pandemic playing out and elderly care homes amongst the hardest hit, it is remarkable that total investment was just 29% down on 2019 and 43% down on the average of the past three years.

2021 so far appears to be another quiet year in terms of investment, compared to the previous few years. We will need a strong H2 just to get to the same level as 2020.

UK care home investment by year and quarter



Source Savills using Health Investor, CoStar, RCA, LaingBuisson

European heavyweights continue to strike deals

For a long time, the elderly care sector was dominated by UK players. More recently, these incumbents have faced growing competition from across Europe. New entrants such as Aedifica and Korian have shown that it's possible for investors with experience elsewhere to achieve substantial scale in the UK market quickly. We should expect to see more new entrants from Europe and North America over the next few years.

Impact Healthcare REIT, Target Healthcare REIT and Octopus Healthcare are among the most active domestic investors - all specialists in healthcare real estate investment. Over the past three or four years, they've invested a total of around £250m each. Lately these firms have faced competition with Aedifica, a Belgian elderly care home specialist. Since 2018 they've invested more than £625m.

After entering the UK market for the first time in 2018/19, Aedifica quickly built up a portfolio of 102 assets with 6,700 residents with another nine projects soon to complete. The portfolio is now worth more than £685m.

Another new entrant from the continent is Korian Real Estate. The Paris-headquartered investor is Europe's largest owner of elderly care beds. Building off its footprint in France, Spain, Germany, Belgium and Italy, it entered the UK for the first time in 2021, acquiring a portfolio of six high-end care homes with a combined 425 beds from Berkley Care Group. Care home operators and owners will be on the lookout to see if they or other new arrivals will be as acquisitive as Aedifica has been.

Capacity is not rising in line with the UK's ageing population

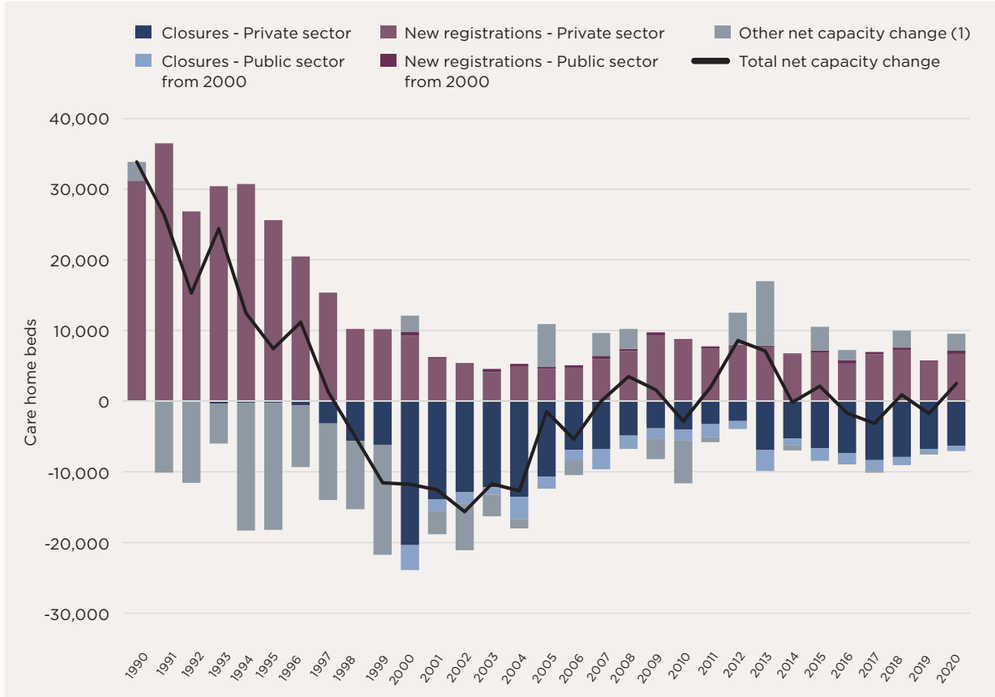
The UK's ageing population is well documented. As more people live longer and diseases such as dementia and Alzheimer's become more prevalent, the demand for elderly care is only going to increase.

However, the number of new elderly care beds is hardly increasing. LaingBuisson data shows that the number of new registrations has been roughly in line with closure rates since 2005.

Over the past 16 years the net capacity change is just 13,000 beds in total, equal to only 800 or so per year. Since 2015, there has been a net increase of just 91 beds.

Whilst closure rates have slowed since their peak between 2000 and 2004, when they averaged around 17,000 beds each year, there have been around 7,700 closures each year since 2016.

Care home capacity changes - closures and registrations



Source LaingBuisson, (1) Other net capacity change includes extensions and reductions to existing homes as well as re-registrations of care homes to and from client groups other than old age and dementia

Homes that close are much more likely to be rated poorly

The positive spin to put on this high closure rate is that since 2016, a high proportion of the beds that were de-registered were in homes that were rated as either 'requiring improvement' or 'inadequate' by the CQC.

In total, 46% of beds across England that closed in that time were rated in either of those two categories. This compares to only 21% of existing operational stock that is rated in those categories.

7,700

Care home beds closed each year since 2016.

> Individual care costs will be capped at £86,000 from October 2023

Government reform of social care will provide greater certainty of long-term funding

With so many recent false dawns and promises of reform, the Prime Minister's recent announcement of a major restructure to adult social care in England will be welcomed. Over the past 20 years there have been 12 White and Green Papers, as well as five independent commissions looking at how to reform adult social care. In that time there has been no structural reform.

The government's plans to increase funding include an increase in National Insurance and a tax on dividends of 1.25% from April 2022. These will be hypothecated to fund health and social care and are expected to raise £36 billion over the following three years.

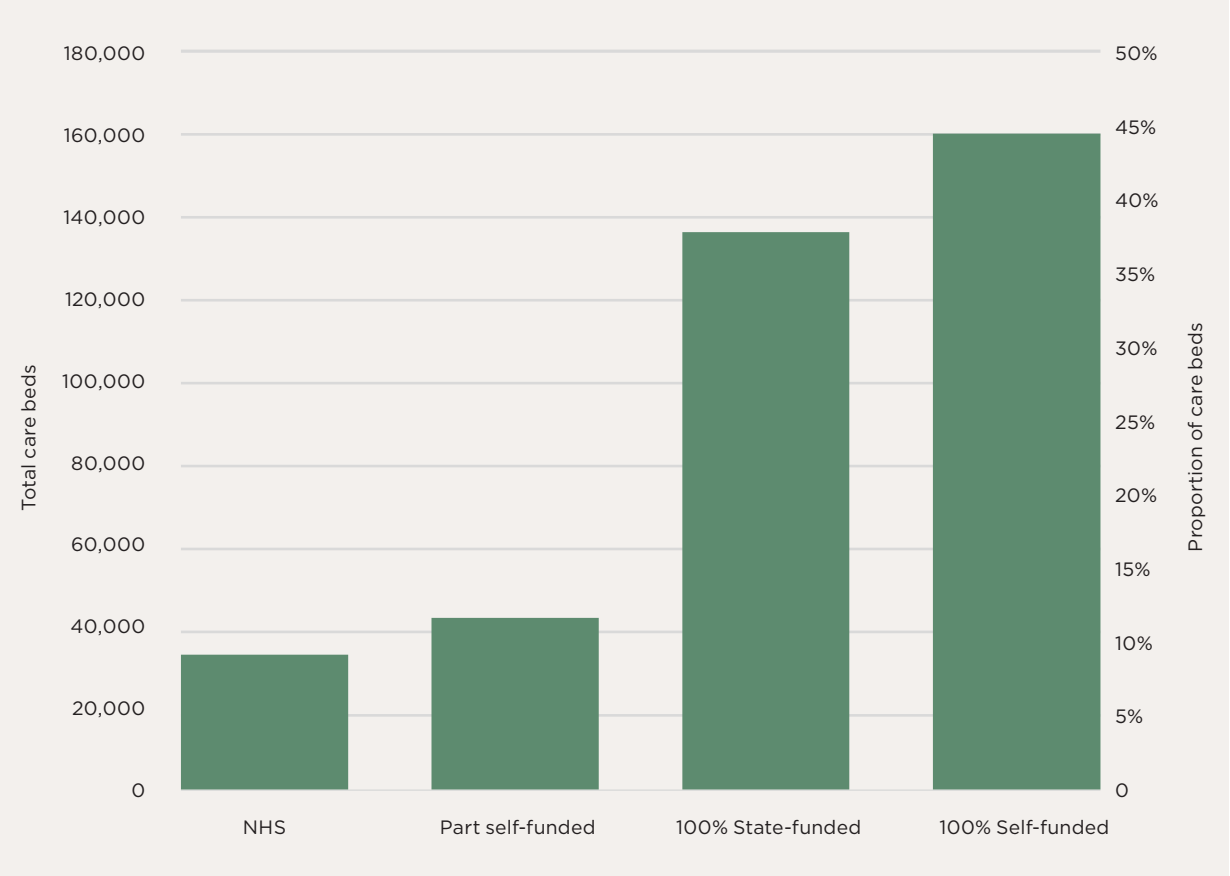
This funding is unlikely to be enough. It does, at least, represent the first meaningful step government has taken to address the problem in decades.

The move gives care operators greater funding certainty and will, we hope, be the first of many steps towards ensuring elderly social care has the resources it needs.

Individual care costs will be capped at £86,000 from October 2023 and anyone who has assets of less than £20,000 will have their care costs fully met by the state. Around 37% of all elderly care residents currently have the state pay for 100% of their care costs.

Those with assets between £20,000 and £100,000 will receive some means-tested support (up from £23,250 as it currently stands).

Total care beds by funding type



Source The King's Fund

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Savills Research is a dedicated team with an unrivalled reputation for producing well-informed and accurate analysis, research and commentary across all sectors of the UK property market.

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