RESEARCH

AUTUMN 2010

UK HEALTHCARE

Development opportunities

Knight Frank

HIGHLIGHTS

- Since our 2009 report, the care homes sector has seen a notable increase in development opportunities, with developers marketing sites for C2 use that were previously intended for alternative land uses, predominantly residential.
- Obtaining finance remains a significant constraint to care home operators seeking to develop new premises. Consequently, operators have increasingly turned to leasehold turn-key opportunities as an alternative to freehold ownership.
- Knight Frank's Healthcare Development Hotspots model reveals Northamptonshire as 2010's top ranked county in England and Wales, rising from fifth place in 2009. Warwickshire, Berkshire and last year's top ranked county, Buckinghamshire, make up the following three positions.
- A separate new model developed this year for the counties of Scotland reveals that Lothian, with Edinburgh as its urban heart, is Scotland's top ranked hotspot for healthcare development.

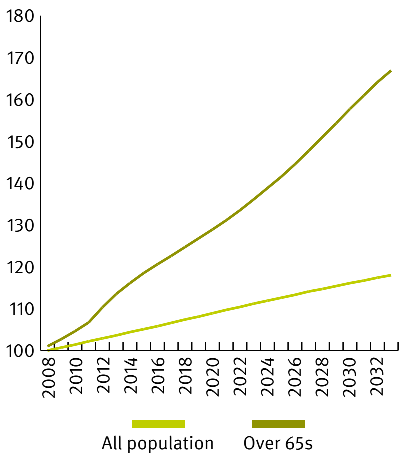
DEMAND IS STRONG, BUT HEAVILY FOCUSED ON SITES IN RELATIVELY AFFLUENT LOCATIONS OFFERING SOUND DEMOGRAPHIC PROSPECTS.

Overview

Since Knight Frank's last healthcare development trends report in 2009, the sector has seen a notable increase in the number of development opportunities being presented to the market. Part of the reason is healthcare's perceived strengths relative to other sectors at present, namely its tendency to offer index-linked rents on very long leases and its underpinning by positive long-term demographic trends, as demonstrated in Figure 1.

Consequently, landlords and developers have been actively marketing sites for healthcare use as an alternative to previously intended land uses, particularly residential. Typically, this is occurring where house builders have either opted to sell their land banks or where healthcare operators have done likewise with pre-let agreements in place. The structural decline seen in some specific sectors has also assisted operator expansion. This has been particularly prevalent with former public houses being redeveloped for care home use.

Figure 1
Forecast population growth in England
Population growth index



Source: National Statistics

"At Castleoak, we have seen that one consequence of the recent downturn has been a rise in the number of new sites available for care home development. In addition to an increase in site availability, reduced development costs and strong investor appetite means now is a great opportunity to develop future proofed facilities, particularly in areas where there is an under provision of care homes."

Mel Knight, Castleoak Group Chief Executive

Front cover image: Sir Aubrey Ward House, Marlow (Castleoak Group)

This increase in the supply of development opportunities has been followed by an increase in care home development activity, at least compared with 2009. In England & Wales demand is strong, but heavily focused on sites in relatively affluent locations offering sound demographic prospects. Although high alternative land values can restrict development in these locations, opportunities are being found.

A current feature of the care home sector is a relative lack of operators looking to sell their facilities. Thus, organic expansion or development currently provide the two means by which operators can grow their revenues. In terms of the former, there is increasing evidence that operators are exploring more intensive use of their existing care home facilities through asset management strategies such as building extensions.

However, obtaining finance remains a significant barrier to developing facilities for freehold ownership, with operators either lacking the necessary capital and / or equity checks for lender approval. Consequently, as predicted in our 2009 report, the trend towards pre-lets as an alternative means of securing additional facilities has gathered momentum, with pre-let opportunities being offered from a range of funding sources, including property companies, construction companies and small funds.

This growing pre-let market has been dominated by the UK's larger operators. Typically, they are demanding that facilities are future-proofed ahead of existing regulations and are increasingly providing input to the property's design & layout. However, while the number of opportunities is plentiful, operators require a very strong case before proceeding.

Location is paramount and those C2 sites which remain undeveloped tend to be where land is cheap or dominated by local authority provision. Determining where and what to develop is being considered in ever greater detail and this has resulted in a marked increase in the number of feasibility studies being undertaken for both developers and operators.

Lancaster Court in Watford, Hertfordshire (Runwood Homes PLC)

England & Wales hotspots

In addition to the current trends influencing the development market, key to identifying future opportunities is an understanding of the comparative prospects for successful development across the country. The Knight Frank Healthcare Hotspots model was developed in 2007 with the objective of identifying where the best opportunities and prospects for care home provision may be located.

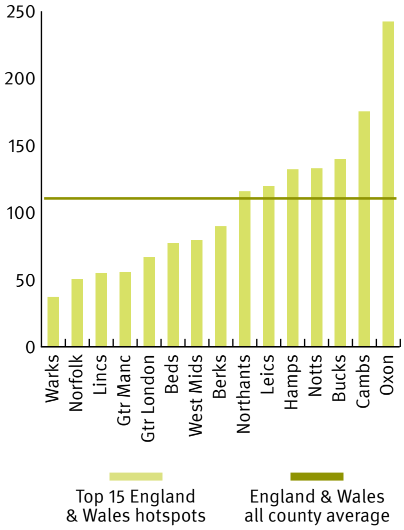
The model is a county-based assessment using a matrix of eight criteria incorporating economic, demographic and healthcare specific commercial factors. A key focus is the anticipated growth in healthcare demand relative to current and pipeline supply and, therefore, the prospects for both development and investment. The model also encompasses economic strength, bed values and the cost of land for development.

Northamptonshire is the top ranked county in 2010 rising from fifth place in 2009 and beating the all-county average by a substantial 84%. As well as being the top performer for long-term demographic prospects and employment growth, it is a top-ten performer in terms of its relatively low land values. Indeed, the county's only clear weakness is its above average bed supply

Figure 2

Healthcare development pipeline

sq m per 000 over 65s



Source: Knight Frank

per person, but even on this category it only marginally underperforms the all-county average.

Of the 51 counties assessed, the 2010 standings reveal a clear 'top four' tier of performers, all with a total score of over 50% above the all-county average. In addition to Northamptonshire, the group is made up of Warwickshire, Berkshire and Buckinghamshire. While there has been some switching of positions from 2009, it is notable that each has been consistently in the top bracket of performers since Hotspots was launched in 2007. The addition of six areas covering Wales this year had no impact on the top 12, with South Glamorgan the strongest Welsh performer with a ranking of 18th.

The range of criteria from which the top 12 hotspots draw their elevated ranking varies significantly, however. For example, Berkshire, Buckinghamshire and Cambridgeshire share similar attributes relating to care homes demand, with strong demographic, economic and employment prospects together with relatively high bed values. All three are also disadvantaged by relatively high land values, which hinders viability to some extent.

In contrast, Warwickshire, Bedfordshire and Greater Manchester (ranked 2nd, 5th and 6th respectively) all benefit in the rankings on the supply side, with each having a relative lack of current supply in terms of existing care bed provision, and also future supply, in terms of per capita planned healthcare development.

Table 1 sets out the 12 hotspots and is once again dominated by counties in the South and the Midlands. For the second year running, Greater Manchester, ranked 6th, is the only hotspot outside these areas. Notable in the 2010 results has been the sharp rise in the ranking of two major metropolitan areas with Greater London and the West Midlands comprising new entrants to the top 12, moving up 19 and 13 places respectively. This is primarily the result of a relative shortage of current and future supply when considered on a per capita basis.

Table 1

Top 12 ranked counties of England & Wales in 2010

2010 Rank		Forecast growth in 65+ population	Forecast economic growth	Current supply	Future supply	Change in rank	Total score index
1	Northamptonshire	1	7	32	30	up 4	1.84
2	Warwickshire	12	15	11	8	no change	1.78
3	Berkshire	16	1	10	22	up 1	1.75
4	Buckinghamshire	4	2	17	38	down 3	1.57
5	Bedfordshire	11	14	14	20	up 8	1.40
6	Greater Manchester	49	13	5	14	up 6	1.39
7	Cambridgeshire	3	4	31	47	down 4	1.32
8	West Midlands	46	20	2	21	up 13	1.29
9	Greater London	50	6	7	15	up 19	1.27
10	Lincolnshire	10	24	35	13	up 9	1.27
11	Oxfordshire	13	12	6	50	down 5	1.22
12	Leicestershire	15	28	15	31	down 4	1.20

Source: Knight Frank

Avery Healthcare opened Brampton View in Northampton in October 2008

Scotland hotspots

This year's Healthcare report also marks the launch of a healthcare hotspots evaluation in Scotland. The model aggregates the country's council areas into 12 larger areas, many of which make up the former traditional Scottish counties. The model relies on exactly the same data inputs as that employed for England & Wales, but is kept in isolation from the England & Wales rankings due to the fact some data inputs derive from separate sources.


Westerfield Care Centre in Paisley
(Southern Cross Health Care PLC)

The first analysis of care home development prospects for Scotland reveals Lothian as the top ranked of the twelve areas, with a total score at 56% above the average for all 12 areas. With Edinburgh as its urban heart, Lothian's main strengths are its demographic and economic prospects, being ranked top in Scotland for population growth in over 65s and uppermost in terms of economic growth prospects. As with England's home counties, Lothian is disadvantaged by relatively high land values.

Similarly to other areas throughout Britain, there has been a notable increase in the number of sites being offered to the care homes sector, albeit these are often within relatively less affluent and sought after locations. As reflected by the hotspots' performance, Edinburgh is particularly sought after by developers and operators albeit relatively affluent locations such as this possess greater barriers to market entry.

After Lothian, the top four ranked areas in Scotland are Lanarkshire, Fife, the Scottish Borders and Dumfries and Galloway.


Guthrie House in Edinburgh
(Four Seasons Health Care Limited)

Lanarkshire shares Lothian's positive attributes on the economy and demographic outlook, being ranked third for both criteria. However, Lanarkshire, together with the Scottish Borders, draws its main strength from its shortage of future supply of care home facilities, with the pipeline analysis showing that both areas do not presently have a single care home with planning permission in the pipeline.


Baillieston in Glasgow
(Four Seasons Health Care Limited)

Table 2
Top five ranked counties of Scotland in 2010

2010 Rank		Forecast growth in 65+ population	Forecast economic growth	Current supply	Future supply	Total score index
1	Lothian	1	1	6	7	1.56
2	Lanarkshire	3	3	10	1=	1.46
3	Fife	2	2	5	11	1.37
4	Borders	4	7	2	1=	1.19
5	Dumfries & Galloway	6	10	3	5	1.08

Source: Knight Frank

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