

The background image is a photograph of a large, multi-story stone building, likely a care home, with a well-maintained garden in the foreground. The building has a classic stone facade with numerous windows, some of which are open. A sign above the entrance reads 'Wetherby Manor'. The garden features a green lawn, a paved path, and several flower beds with red, pink, and white flowers. A small tree is visible on the right side of the garden.

RESEARCH



2015

# CARE HOMES

TRADING PERFORMANCE REVIEW

## HIGHLIGHTS

Occupancy rates increase marginally to 88.3% maintaining the post-recession recovery

Average weekly fees rise to £675 and at a rate ahead of RPI inflation for the first time in 5 years

Staff costs equate to 62% of revenue, with notable increases in agency staff costs, further eroding profit margins

# FOREWORD



Welcome to Knight Frank's fourth annual review of the latest trends in the trading performance of the UK's care homes sector, which we hope you find informative.

The Care Homes Trading Performance Index (CH-TPI) provides key performance benchmarks on staff costs, occupancy rates, average fee levels and profit margins (EBITDARM) across the care home sector. The sample underpinning the CH-TPI has been strengthened once again, with the further addition of leading care providers to the index. It now covers almost 60% of the care home beds provided by the UK's major operators. The sample is also well balanced geographically (Figure 1) but, as in previous iterations, remains weighted towards nursing rather than personal care homes.

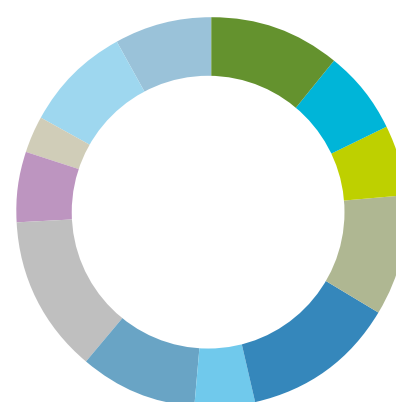
This 2014/15 review illustrates marginal increases in the rate of occupancy and fee levels accelerating in excess of RPI inflation. But they also point towards rising staff costs, and notable increases in the level of expenditure on agency staff, which has further eroded profit margins.

Typically there are clouds on the horizon, particularly in relation to staffing costs. Most notable here is the potential future impact of the National Living Wage. We anticipate changes in the index over the next few years as the National Living Wage becomes a reality and the extent to which additional costs are passed on to funders is bottomed-out. We are confident however that the sector will address this latest challenge and continue to perform robustly.

Finally, we would like to thank the growing number of leading care providers who have kindly contributed to the CH-TPI, and would encourage those who have not, to do so in the future.

Dr Lee Elliott  
Head of Commercial Research

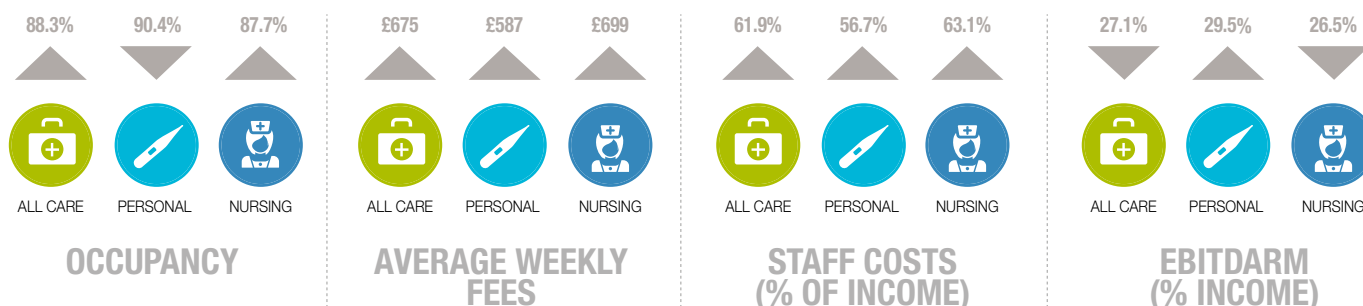
FIGURE 1  
**Regional share of the sample**  
% of total care beds



	FY 2014/15 SHARE OF BEDS
EAST	11%
EAST MIDLANDS	7%
GREATER LONDON	6%
NORTH EAST	10%
NORTH WEST	13%
NORTHERN IRELAND	5%
SCOTLAND	10%
SOUTH EAST	13%
SOUTH WEST	6%
WALES	3%
WEST MIDLANDS	9%
YORKS & HUMBER	8%

Source: Knight Frank Research

## 2014/15 RESULTS AT A GLANCE



Source: Knight Frank Research



# OCCUPANCY AND FEES

The care home occupancy rate increased during FY 2014/15, rising from 87.6% to 88.3%.

## Occupancy

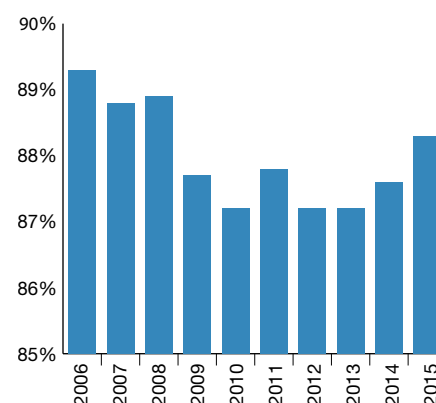
The overall care home occupancy rate increased from 87.6% to 88.3%. Occupancy rates have been recovering gradually over the past three years – having fallen relatively sharply during the height of the recession (Figure 2) – and are now at their highest level for six years.

Personal care homes continue to demonstrate stronger occupancy than nursing homes, with occupancy rates of 90.4% and 87.7%, respectively in FY 2014/15. The difference continues to be linked to a number of factors, namely: strong demand for privately funded care in personal care facilities, and the strengthening of demand for dementia care at homes without nursing.

Occupancy rates are unevenly spread across the UK regions and reflect a pattern broadly similar to that shown in previous editions of the CH-TPI (Figure 3). Greater London has the highest level of occupancy (90.2%). This is a simple function of demography and high barriers to market entry. At the other end of the spectrum are the South West and North East regions which continue to show occupancy rates of 85.0% and 83.8%, respectively. Low occupancy rates in the North East arise largely from continued pressure on social care budgets.

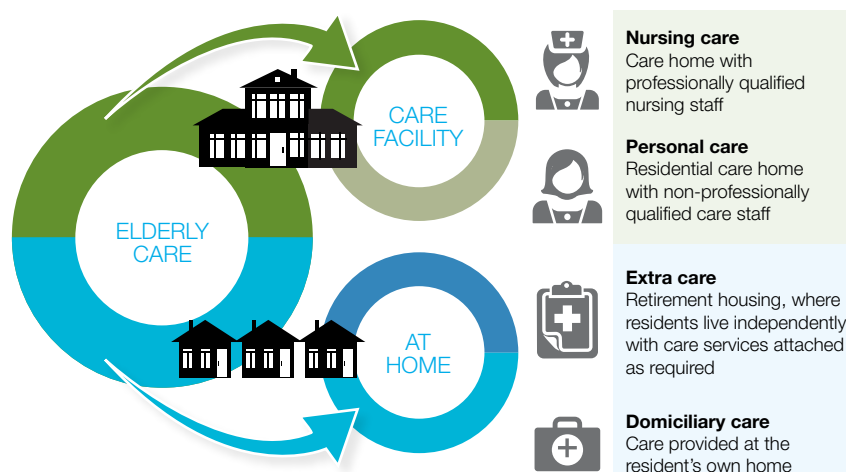
FIGURE 2

### UK care home occupancy rate %



Source: Knight Frank Research

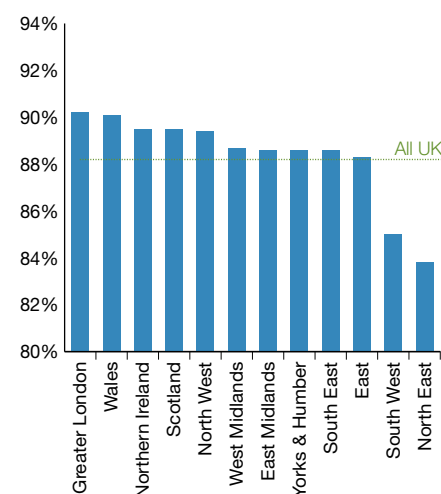
## ELDERLY CARE PROVISION



This report assesses **care facilities** with a bias towards nursing homes in our sample. Note that many facilities provide both nursing care and personal care on-site, and these fall under Nursing in our analysis.

FIGURE 3

### Occupancy rates by region (FY 2014/15)

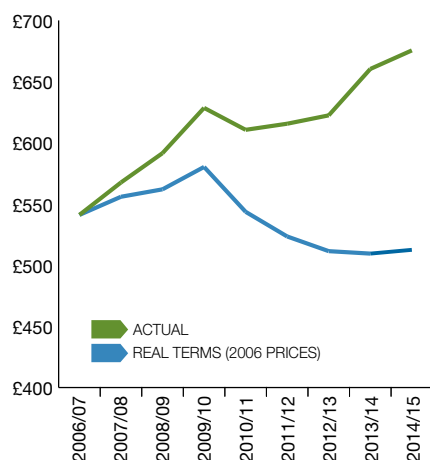


Source: Knight Frank Research

FIGURE 4

**Average weekly fees**

£ per week

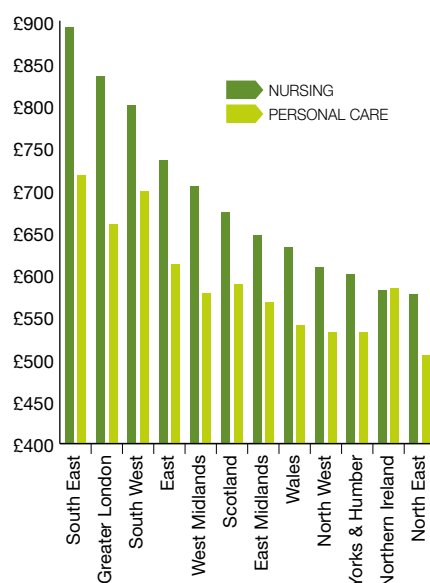


Source: Knight Frank Research

FIGURE 5

**Average weekly fees by region (FY 2014/15)**

£ per week



Source: Knight Frank Research

## Average weekly fees

The CH-TPI reveals average weekly fee levels of £675 in FY 2014/15 for the UK as a whole. This is higher than last year's figure of £660 per week – an increase of 2.3%. This is a further improvement on the 2.1% rise during 2013/14 and is also significantly above RPI inflation over the same period (0.9%).

In absolute terms, average weekly fees in 2014/15 remained much higher for nursing homes (at £699 per week) compared with personal care (at £587 per week).

The two types of care show a significant difference between the extent of fee increases, with personal care witnessing markedly higher growth compared with nursing homes. This divergence continues to reflect the bias towards self-funded care that is evident in personal care homes, where fee rises have reflected individuals' ability to pay, rather than being dictated by local authority budgetary constraints.

On a regional basis, the UK's southern regions lead the way in terms of the highest average fee levels (Figure 5). For nursing homes, the South East has the highest average fee levels, at £893 per week, followed by Greater London (£834







per week). This again reflects the greater prevalence of private paying residents who provide the funding required to cover the higher staff costs and land values associated with these regions.

For nursing care, average fee levels are correspondingly lower in the northern regions of England, and significantly lower than the overall UK average of £699 per week. The North East continues to have the lowest average fees of any region, at £577 per week, driven by the private pay market being less prevalent here and local authority fees typically accounting for the majority of a care home's revenues.

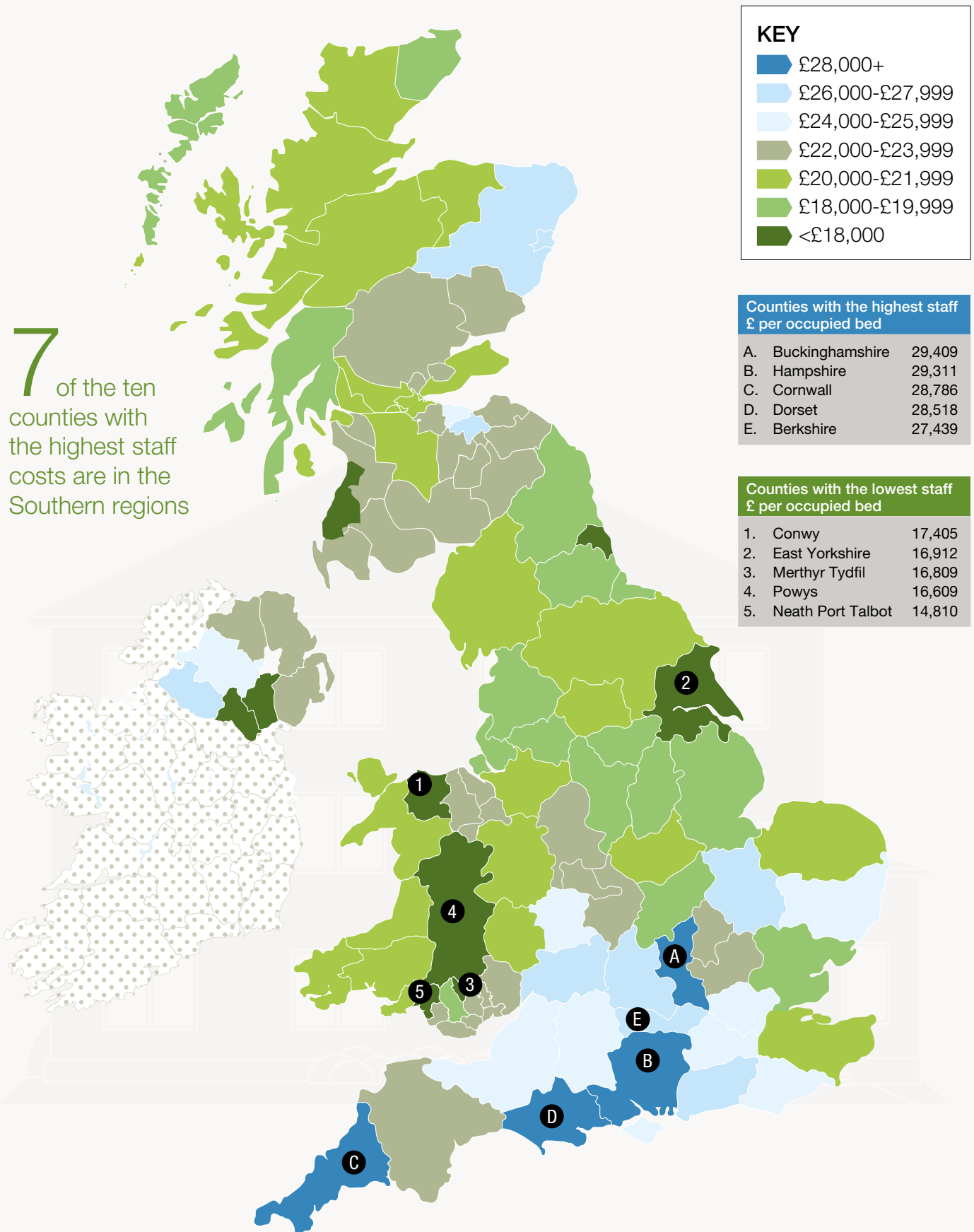
The regional ranking of fee rates for personal care is broadly in line with that of nursing homes. England's southern regions again show the highest fees, while the northern regions have lower fees.

Nursing care's 'premium' over personal care fees is also more pronounced in the South compared with elsewhere. In Greater London average nursing fees are 26% higher than personal care fees, compared with a difference of 16% for the majority of other UK regions.

### AVERAGE WEEKLY FEES

	AVERAGE WEEKLY FEE	ANNUAL CHANGE (LFL)
Personal Care 	£587	3.7% 
Care with Nursing 	£699	1.6% 
All Care Homes 	£675	2.3% 
RPI inflation (FY 2014/15)		0.9%

## STAFF COSTS PER OCCUPIED BED (£) 2015



“Agency staff costs increased to 5.8% of total staff costs in 2014/15.”

## COSTS

Average staff costs amounted to £21,756 per resident for the FY 2014/15. Meanwhile, as a percentage of income, staff costs increased to 61.9%.

### Staff costs

Care home staff costs have followed an upward trend over the past five years. During 2014/15 staff costs increased from 57.6% to 61.9% of total income (Figure 6). The South East has the highest staff costs for both nursing care, averaging c. £25,857 per resident in FY 2014/15, and for the personal care sector, at an average of £21,749 per resident (Figure 7).

The differential between nursing and personal care, reflects the higher pay that qualified nurses receive compared with care staff at personal care homes. However, this differential varies markedly between UK regions, and is the lowest in Greater London, with staff costs per resident at nursing homes standing only 13% above those for personal care homes.

While staff costs in the relatively affluent South East are highest on a per resident basis, they are relatively low when considered as a proportion of total revenue. Staff costs as a percentage

of income are correspondingly higher elsewhere in the UK and it is these regions which are more exposed to upward pressures in staff costs, driven by labour shortages. Northern Ireland provides an example of this. While Northern Ireland's staff costs are marginally higher than the UK average, they translate to the highest costs of any region as a proportion of revenue, standing at 74%, and considerably higher than the South East, at 57%.

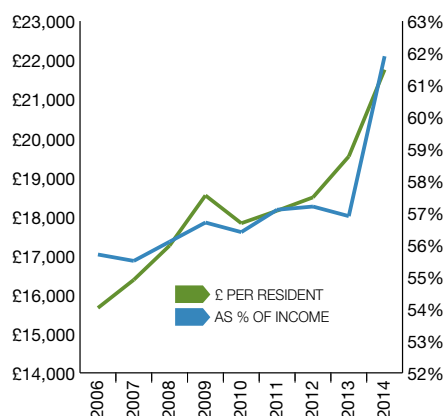
Further headwinds are likely in terms of staffing costs, as the sector responds to the National Living Wage (NLW). The full impact is uncertain but will be felt strongest outside London and the South East. More concerning may be the accretive impact of the NLW across the care homes sector.

Agency staff costs as a proportion of total staff costs increased from 4.8% last year to 5.8% for the FY 2014/15, reflecting the growing difficulties with staff resourcing

FIGURE 6

#### Staff costs

As £ per resident (LHS) vs % of income (RHS)

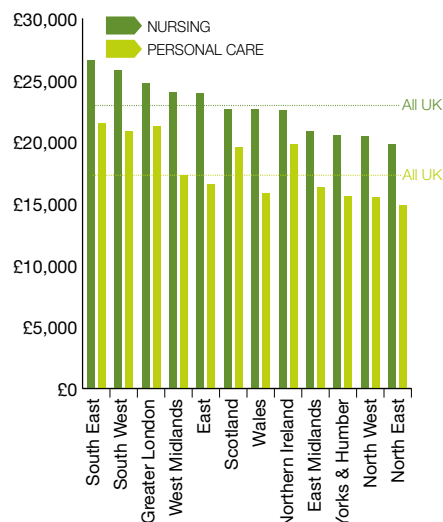


Source: Knight Frank Research

FIGURE 7

#### Staff cost per resident

£ per resident



Source: Knight Frank Research

### Staff Costs FY 2014/15

Region	Per resident p.a.	As a % of revenue
South East	<b>£25,527</b>	57.3%
South West	£25,084	61.5%
Greater London	£24,189	57.7%
Scotland	£22,478	64.6%
Northern Ireland	£22,386	<b>73.9%</b>
West Midlands	£22,268	63.8%
East	£21,855	60.1%
Wales	£20,926	66.1%
North West	£19,556	63.4%
East Midlands	£19,358	60.1%
Yorks & Humber	£19,305	63.6%
North East	£18,286	63.4%
<b>All UK</b>	<b>£21,756</b>	<b>61.9%</b>

Source: Knight Frank Research

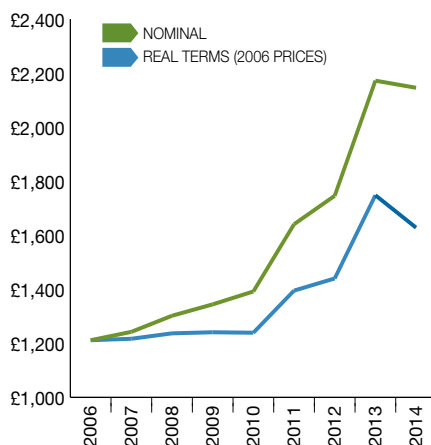
## The National Living Wage



Since 1998, the National Minimum Wage has been set by the Low Pay Commission based on their calculation of the highest level which would not adversely affect employment. In July 2015 the Chancellor effectively replaced the National Minimum Wage with a new National Living Wage for those aged 25 and over. This new rate would no longer be set with regard to employment, but would instead move towards a target 60 per cent of median income by 2020.

and retention. It should also be noted that reliance on agency staff is greater in nursing rather than personal care homes. There is also a notable degree of regional variation, with agency staff costs making up the highest share of overall staff costs in the Northern Ireland at 8.8%, and the lowest share in Wales, at only 3.3%.

FIGURE 8  
**Property cost per bed**  
£ per bed



Source: Knight Frank Research

## Property costs

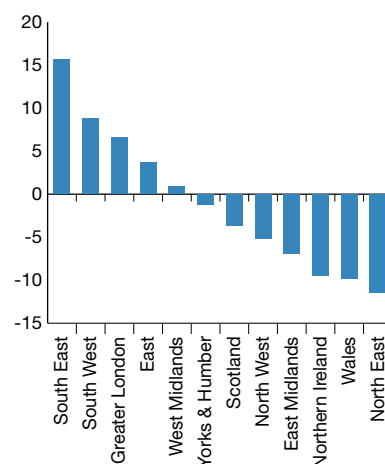
Following the sharp rise in care home property costs last year, this year saw the cost per bed fall to £2,146 (Figure 8). The underlying trend in property costs in both nominal and real terms is upwards. While energy and water price rises have in recent years helped push property costs above the rate of inflation, last years' significant increase was more closely associated with insurance costs and increased repair and maintenance costs, as catch-up capex was applied to the sector.

Property costs now equate to 6.1% of total income, having stood relatively stable at c. 5% during the years prior to 2010.

## Food costs

Average food costs per resident in FY 2014/15 were 9% below the previous year. As last year, food costs per resident were highest in the South East during 2014/15 at 16% above the overall UK average, and lowest in the Wales and the North East, at 9.8% and 11.4%, respectively below the average. (Figure 9).

FIGURE 9  
**Food cost index (FY 2014/15)**  
% difference from all UK



Source: Knight Frank Research



## Property costs

These are the costs which relate to the day-to-day running and servicing of the property. They include utilities, council tax, insurance and repairs & maintenance, but exclude any rental obligations in the case of leased care homes.



## TOTAL COSTS AS % OF INCOME

	< 40 Beds	40-59 Beds	60-79 Beds	80-99 Beds	100+ Beds
Nursing	75.4%	74.4%	71.6%	69.8%	71.2%
Personal Care	70.0%	68.1%	66.5%	70.2%	61.0%



“Almost a third of care homes in the 2014/15 CH-TPI have EBITDARM in excess of 30%.”

## EBITDARM

**Earnings before Interest, Tax, Depreciation, Amortisation, Rent and Management.**

This is a particular measure of profitability which allows for direct like-for-like comparison between individual care homes, before costs of rent and management charges are accounted for.



# PROFITABILITY

Trading performance is under pressure from rising costs but remains strongest in the South East and Greater London.

The profitability of the care homes sector continues to be under downward pressure. Despite slight improvements in occupancy rates, EBITDARM as a percentage of income has slipped from 27.5% in 2013/14 to 27.1% in the latest index (Figure 10). This margin erosion reflects the aforementioned increases in operating costs, and in particular the uplift in staffing costs.

In assessing the CH-TPI on the basis of care home registration type, a strong variation in performance is discernible. In absolute terms, EBITDARM for nursing care (£9,639 per occupied bed) is some 7% higher than for personal care homes (£8,995 per occupied bed). It should be noted, however, that personal care homes display higher profitability when expressed as a percentage of income, with margins at 29.5% compared with 26.5% for nursing homes. Once again this relates to both the type and cost of staffing required. The additional income received by nursing care homes is more

than offset by the cost of employing skilled nursing staff in a labour market which is chronically under supplied.

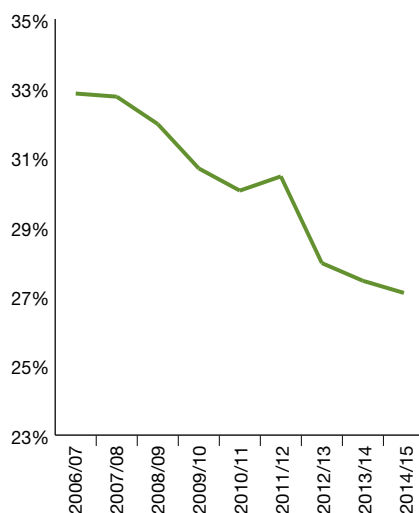
On a geographical basis, a southern bias is once again evident (Figure 11). The South East and Greater London strongly outperform the other regions of the UK in terms of profitability, with EBITDARM as a percentage of income standing at 32.5% and 31.1% respectively for FY 2014/15. This reflects the higher occupancy rates achieved in these regions, together with the greater prevalence of private pay residents who sustain higher fee levels.

Combining care home registration and geography also highlights marked variance across the sector. On a per bed basis, nursing homes in the South East and Greater London are more profitable than personal care homes, contributing to the overall UK trend (Figure 12). However, the inverse is true in less affluent regions such as the North East and Northern Ireland, essentially because these areas are more exposed



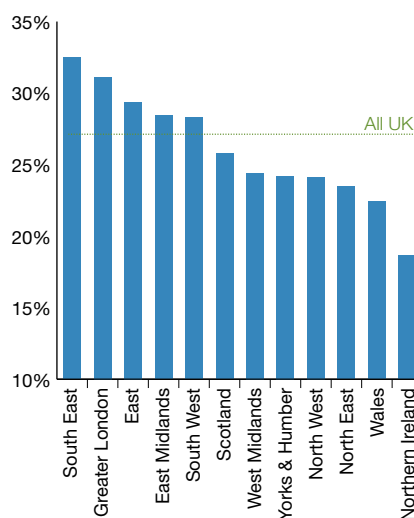
Bucklesham Grange, Hallmark Care Homes

FIGURE 10  
EBITDARM as a % of income



Source: Knight Frank Research

FIGURE 11  
EBITDARM as a % of income  
(FY 2014/15)



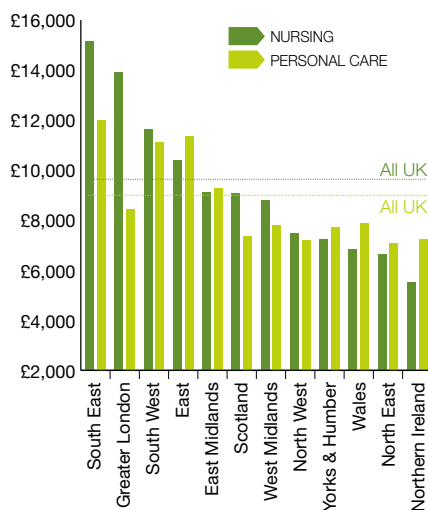
Source: Knight Frank Research



to heightened nursing staff costs and tight budgetary controls on local authority care funding.

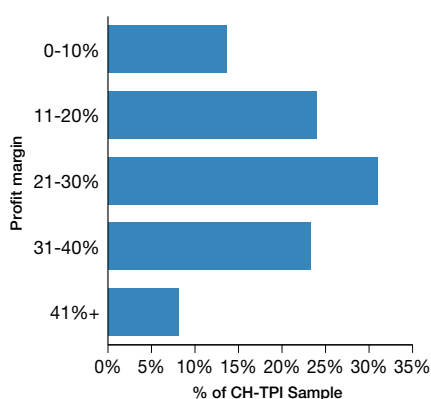
Significant variation in operating profit across the care home sector is clear. This variance is also in evidence when one assesses margin levels across our sample (Figure 13). Almost a third of the care homes assessed within the 2014/15 index are generating EBITDARM as a percentage of income in excess of 30%. Indeed, 9% of the homes assessed are generating profit margins of 40% or more. In contrast 14% of all care homes assessed are generating EBITDARM of less than 10%.

FIGURE 12  
**EBITDARM per bed (FY 2014/15)**  
£ per bed



Source: Knight Frank Research

FIGURE 13  
**Distribution of profit margins across the CH-TPI (FY 2014/15)**



Source: Knight Frank Research



Reuben Manor, Stockton-on-Tees, Silk Healthcare

“Overall profitability remains highest in the 80-99 bed size category.”

## Profitability and care home size










Our analysis of the 2014/15 CH-TPI data clearly demonstrates the effect of care home size on overall profitability, a variable which remains of interest to both prospective developers and operators. The data shows the optimal size of care home, in terms of overall profitability, is in the 80-99 size bed category. Average EBITDARM per bed in this 80-99 bed care home category stands at £11,303, which is 19% above the all index average and 34% higher than the weakest performing under 40 bed category.

While these results stem from a number of factors acting in combination, the

main driver relates to fee levels, which stand at £729 per week in the 80-99 bed category, or 8% higher than the all index average (see below infographic).

Whilst the largest 100+ bed category clearly illustrates the benefits of economies of scale with the category having the lowest staff cost per bed, these efficiencies are also offset by comparatively weak occupancy and fee levels. This impacts profitability, with EBITDARM per bed in this care home category at £8,850 – or 7% below the all index average.

### Key Performance Indicators by size of care home (FY 2014/15)

		Average weekly fee	Occupancy	Staff cost per bed	EBITDARM per bed
< 40 beds		£651	 90.0%	£21,292	£8,409
40-59 beds		£657	89.2%	£21,503	£8,868
60-79 beds		£697	87.3%	£22,282	£10,370
80-99 beds		 £729	87.6%	£23,108	 £11,303
100+ beds		£653	86.5%	 £20,790	£8,850
All care homes		£675	88.3%	£21,756	£9,500

Source: Knight Frank Research

# TRADING PERFORMANCE OUTLOOK



**JULIAN EVANS**  
Head of Healthcare

Within the last twelve months the UK healthcare arena has seen the resurgence of mergers and acquisitions; arguably back to the levels experienced before the collapse of Lehman Brothers Holdings in 2008. Healthcare continues to attract both domestic and international capital and is now firmly considered to be a core asset class.

However, this year's announcement of the National Living Wage has caused angst in the sector and there is much anticipation of the Chancellor of the Exchequer's approach to the National Living Wage in his Spending Review on Wednesday 25 November.

The National Living Wage is the next challenge we must face. The Healthcare sector has navigated around such obstacles in the past and it is unlikely to fetter additional inward investment in to the sector. This is in part due to the structural under supply of bedroom capacity which is further accentuated when one considers the vast amount of poor existing stock.

Knight Frank estimates it would cost circa £15bn to upgrade the 250,000 non en suite bedrooms to wet room status. There is a desperate need for new future proof facilities but the inflationary cost of raw materials has stymied many new build developments. The quality of the existing built environment remains a major concern but is further compounded by only circa 6,000 new care beds constructed per annum and an ageing population. It is a basic issue of supply and demand.

Our research shows a marginal increase in average occupancy to 88.3%. Interestingly the National Living Wage is likely to adversely impact care homes with less than 30 bedrooms. There are approximately 7,300 care homes that operate with less than 30 beds which have a very real chance of closing down in the near future as they will be unviable businesses. Should this happen then approximately 117,000 beds are at risk which will be devastating for owner operators but ironically possibly good news for the major providers who will benefit from an increase in occupancy due to the extra demand for beds. This will drive the further maturation of the sector towards corporate operators.

For the UK as a whole, the CH-TPI reveals average weekly fee levels of £675 in FY 2014/15, up 1.4% in real terms. Anecdotally we are aware of several local authorities agreeing to April 2016 fee uplifts of 5%, which is welcomed news.

Notwithstanding the issue of the National Living Wage, appetite for UK healthcare fixed income, going concerns and development sites continues to attract global investors because of the sector's defensive characteristics. Moreover, Knight Frank's 2015 Care Homes Trading Performance Review demonstrates sustained robust performance. Given this, we anticipate increasing levels of new investors and deal announcements over the next twelve months.

“The sustained robust performance of the UK care home sector will fuel new investment and deal announcements over the next 12 months.”



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Front cover image: Wetherby Manor, Wetherby (Hadrian Healthcare)

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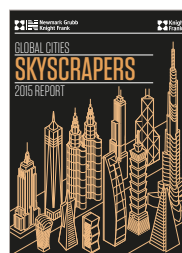
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