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The state of the care home market in the UK: How are current, and future opportunities to build the UK's care home sector being shaped by Covid – 19 and Brexit?

15th December, 2020

Arlington Capital is increasing its focus on the care home sector with a vision to create new high-quality homes and enhance existing properties. A lack of investment over the past years, and the aftermath of COVID suggests a high degree of consolidation can be expected. New investment is needed to service both an expanding private paying and local government assisted payee market. Well delivered care homes should offer superior returns when compared to some other sectors of the real estate industry in the UK. We are advising our investors to closely monitor current opportunities.

The current picture:

In the United Kingdom both the government and private sector providers struggle with rising demand and quality in this highly specialised segment of the real estate industry.

Some 51% of existing care homes in the UK are properties converted from hotels, residential blocks and other conversions, and of these 73% are over 20 years of age. Just 22% are new, purpose-built care homes, and only 2/3 of units in the care homes have ensuite bathrooms.

New demand to 2030 is estimated at 10,000 beds per annum over a stock of 465,000 in 2020, shrinking from 470,000 in 2019 and a decline in capacity of around 55,500 beds since 2015. Some 2,840 care homes, representing 80,000 beds, have been lost in the last 10 years, and, so far, these have not been replaced.

The underlying businesses and properties serving this market are challenged by a low average number of beds per property, just 28 compared to an average of 53 for new built care homes in the UK and similarly larger average in the EU. Market demand is moving to larger, purpose-built units with ensuite bathroom, better finish, more shared facilities and, with size, increased commercial stability.

Europe wide including the UK, 2020 new build investment is down 8.1% in the first three quarters. Still a robust performance given the pandemic, but nonetheless the industry is substantially behind a predicted investment upward trend to make up for the structural deficiencies in provision.

Demand, Geographies, and Performance:

Against this background of continuously increasing demand and shortage of supply is a morphing demography, increased demand for specialist care, and a labour shortage at a time when hiring from traditional European pools of labour are strained by Brexit while new sources are not fully developed.

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The core demographic segments catered to by care homes are traditionally 65+ years and, separately, 85+ years. The latter segment is particularly interesting as this pool of potential residents is expected to grow by 27.5% to the year 2030, and when just 13% of the 85+ age range are currently in care or nursing homes. Worryingly, the expected rise of 35% to 2030 in need of dementia care leaves the industry with a further growing recruitment challenge in hiring the highly trained care staff needed.

Financing differs across the regions of the UK. The affluent South-West of the UK has been increasingly focussing on the private payment sector (self-payers) for newly constructed care homes. The Midlands and the North have a more consistent balance of demand between local authority assisted payment and the private paid sector. The increasing demand on local authority assisted payment places increases the financial strain at local government level and is a central challenge which all the UK's political parties have accepted is in urgent need of solutions from central government to ensure bed availability for the elderly in need.

The industry is also extremely fragmented in the UK, with the large operators only having an overall market share of 15%, and is expected to be marked by consolidation.

From an investment perspective the expected return profiles differ quite substantially. In the South-West yields average level at around 4.25%, whereas in the North where returns are as high as 8%. Profitability has been hit hard in 2020 as necessary COVID-19 measures such as PPE supply, staffing levels, and increased cleaning and disinfection activities have seen costs surge.

Against this shifting backdrop and the large gap between constrained supply, government spending reviews and rising demand, private and institutional investors are looking anew to how aging populations can better be served in later life.

Arlington Capital would like to speak to care home owners in seek of capital, developers interested in the market, and investors and co-investors who wish to learn more of our plans.

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