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# 2014 Baseline

Victoria Park, Brisbane

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# Today's Agenda

1. Treasury Management
2. Financial Metrics
3. Strategy
4. Consumer Perspective
5. Governance
6. Capital Markets

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# Treasury Management

## The virtues of being prudent(ial)

# The financial DNA of a 'typical' aged care provider

(Source: Bentleys National Aged Care Survey, 2014)

## Three core business streams

Care

Accommodation

Services

### Liquidity

- Current assets to current liabilities (ex bonds) 3.4
- Current assets to total assets 25.64%

### Gearing

- Debt as % of total financing 37.73%
- Accommodation bonds as % of total financing 31.19%
- Debt to equity ratio 2.3

### Accommodation bonds

- Bond repayment capacity 110.42%

### Capital investment

- Asset cover (times) 2.07
- Net tangible assets per place \$290,212

### Financial performance

- EBITDA per place per annum \$12,777
- Net profit margin 5.86%
- % Return on Assets (ROI) 2.01%
- % Return on Equity (ROE) 3.5%

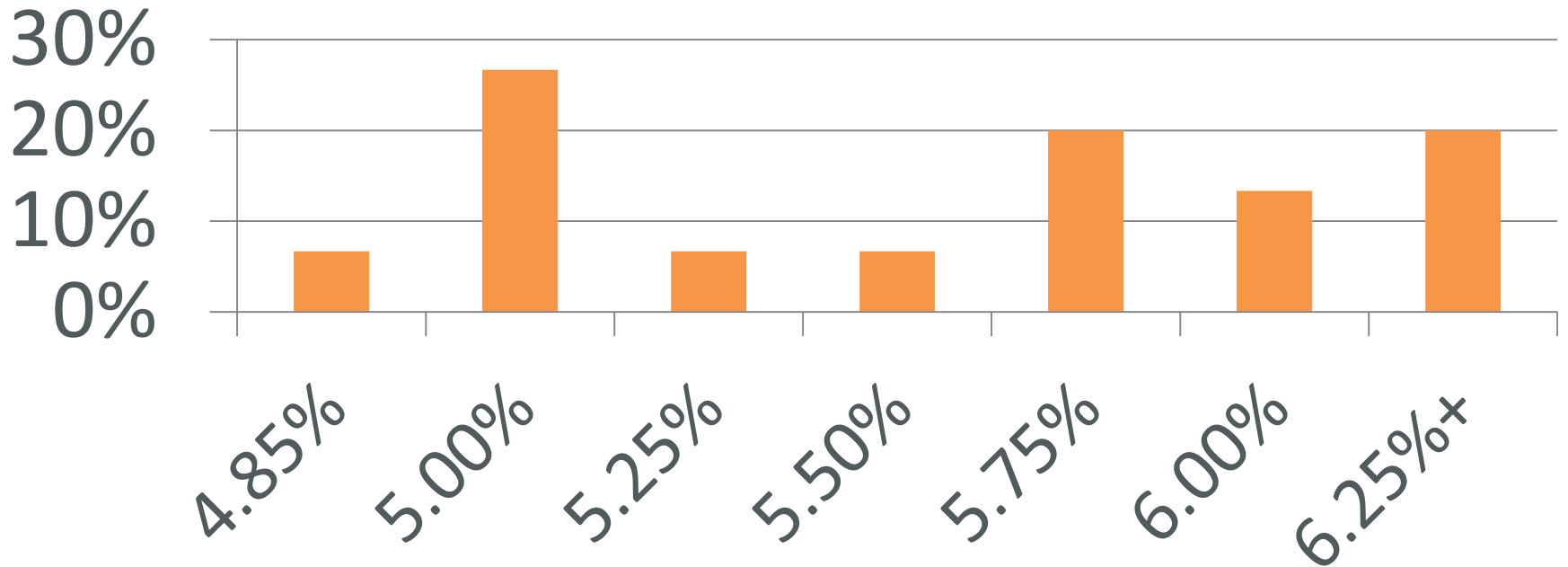
### Staff management

- Employee expenses as a % of total expenses 68.13%

### Working capital days

- Debtor days 14.19
- Creditor days 69.10

# Cost of Bank Debt



Sou



30 June 2014:

- Average cost of bank debt: 5.66%
- Risk margin over the RBA cash rate (2.5%) of 3.16%

Other considerations:

- Cost of consumer funding capital funding = NIL coupon rate (but admin costs)
- MPIR = 6.69%
- ATO GST 2011/1 para 16 = GIC rate (9.63%) – Uplift (7%) = 2.63%

# Weighted Average Cost of Capital (WACC)

## 1 WACC = $EV Ke + D/V Kd (1 - Tc)$

E/V	= portion of enterprise funded by equity
Ke	= Cost of Equity
D/V	= portion of enterprise funded by debt
Kd	= Cost of Debt
1 - Tc	= 100% - corporate tax rate (30%)

	For profit	NFP
	43%	90%
	11.2%	12.2%
	57%	10%
	7.0%	5.5%
	0.7	1
<b>WACC</b>	<b>7.6%</b>	<b>11.5%</b>

## 2 Using the CAPM model to calculate the **Cost of Equity (Ke)**

$$Ke = Rf + B (Erp) + a$$

Ke	= required return on equity
Rf	= the risk free rate of return
Erp	= the expected return on the market portfolio
B	= beta, the systematic risk of a stock
a	= the industry risk premium (residential aged care)

	For profit	NFP
	3.55%	3.55%
	6%	6%
	1.1	1.27
	1%	1%
<b>Ke</b>	<b>11.2%</b>	<b>12.2%</b>

a = specific risk premium, used to adjust the cost of equity for industry specific factors, including:

**Regulatory risk** - residential aged care is highly regulated by the Aust Government (supply and pricing)

**Funding risk** - The risk of inflationary pressures (on e.g. wages and utilities) compared to Government COPO revenue funding growth

**Debtor risk** - counter party risk associated with dealing with customers and their potential inability to pay

## 3 **Cost of Debt (Kd)**

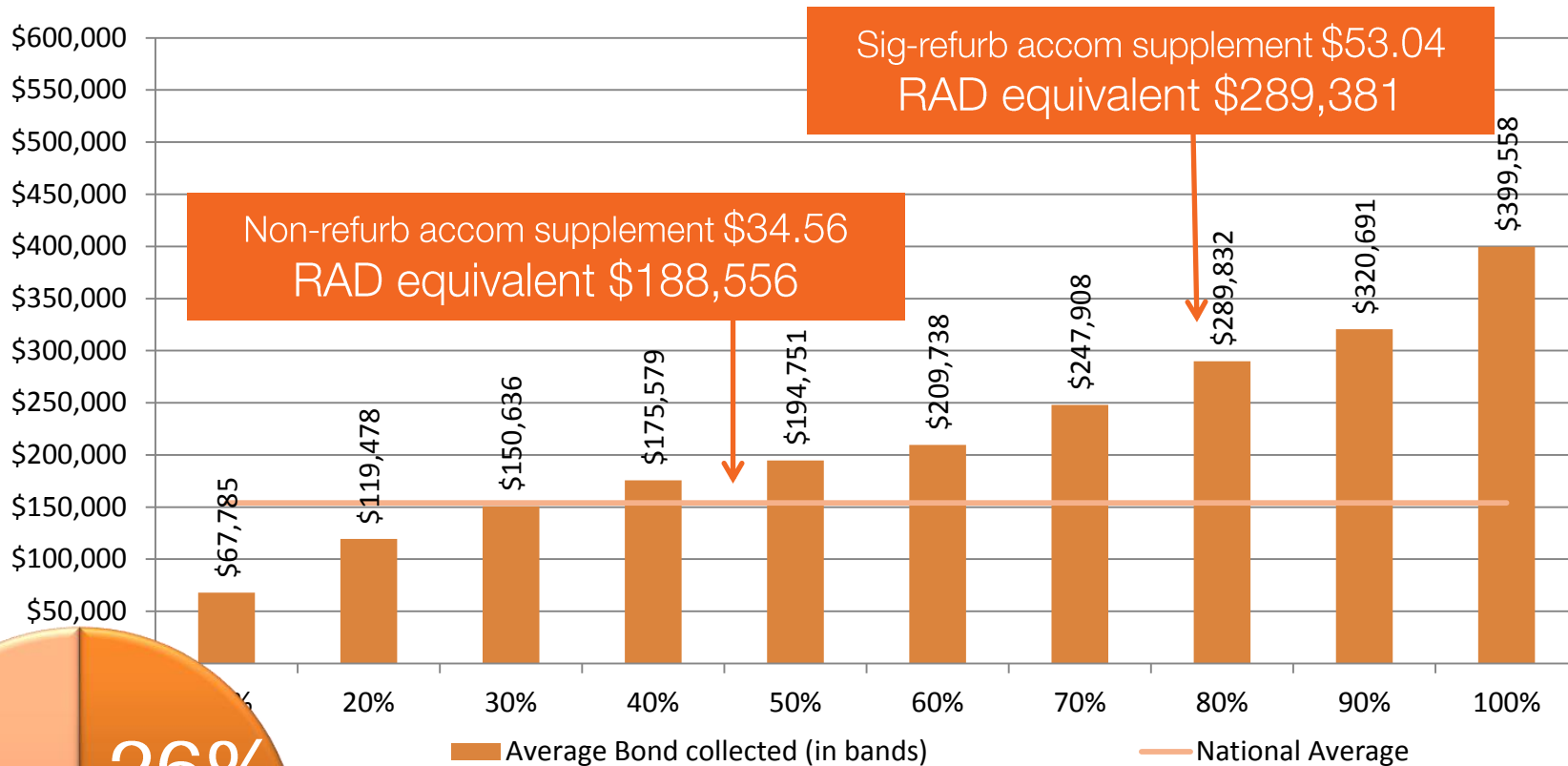
RBA cash rate
Risk premium

	2.50%	2.50%
	4.50%	3.00%
<b>Kd</b>	<b>7.0%</b>	<b>5.5%</b>

Note: To be used when considering the rate of return required on an investment in residential aged care – financed by both equity and debt.

# Consumer Capital Funding

Accommodation bond values for new residents in FY2014



26%

% of providers who collected bonds > RAD equivalent of higher accomm. supplement

Source: 2014 Bentleys National Aged Care Survey

# Feasibility Analysis

## Net Present Value (NPV)

	Downside 1	Base	Upside 1
<i>Operating cashflows before interest and CAPE.</i>	1,088,640	6,003,518	10,125,302
<i>Cashflows after interest and CAPEX</i>	(1,689,806)	4,514,389	9,040,476

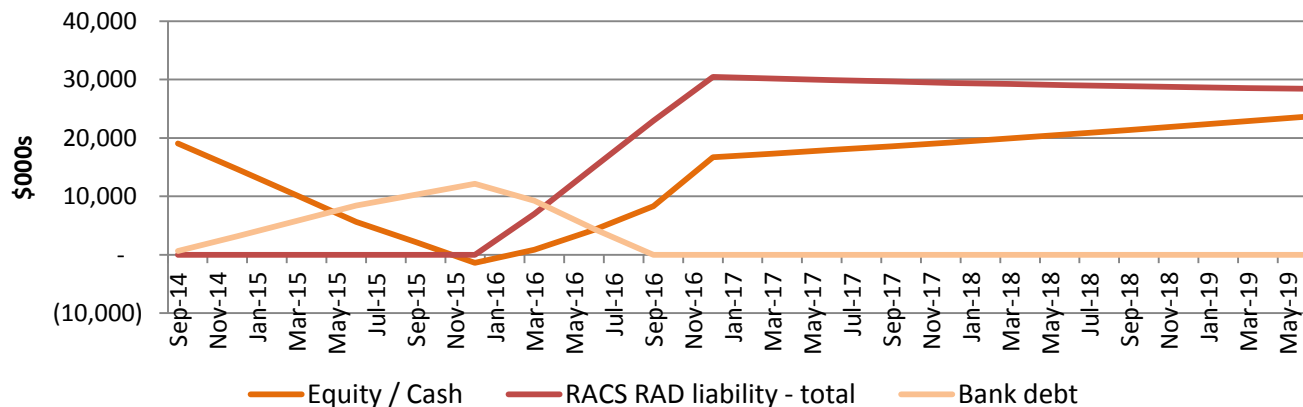
## Internal Rate of Return (IRR)

<i>Operating cashflows before interest and CAPE.</i>	3%	19%	28%
<i>Cashflows after interest and CAPEX</i>	No return	15%	24%

Compare  
to WACC

## Payback period on initial investment (yrs)

<i>Operating cashflows before interest</i>	No payback	6.96	4.70
<i>Cashflows after interest and CAPEX</i>	No payback	9.67	5.65



## Key sensitivities:

- RAD/DAP profiles
- Occupancy
- Length of stay
- Resident frailty
- Staffing profiles



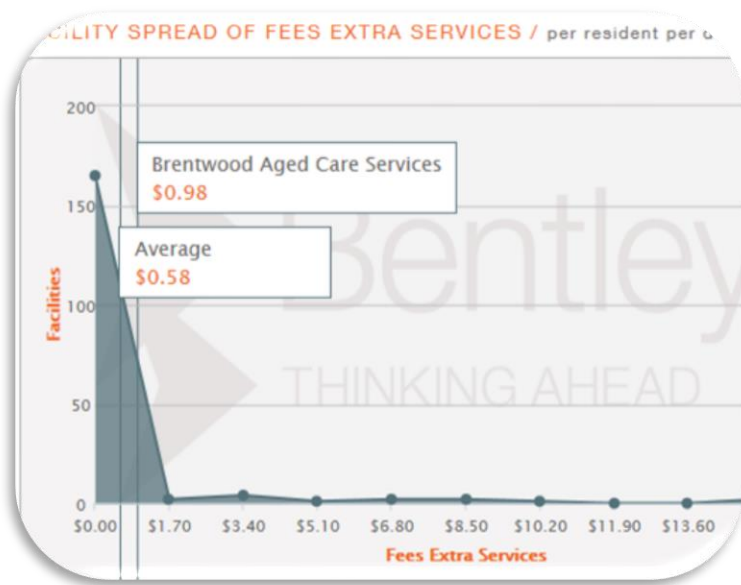
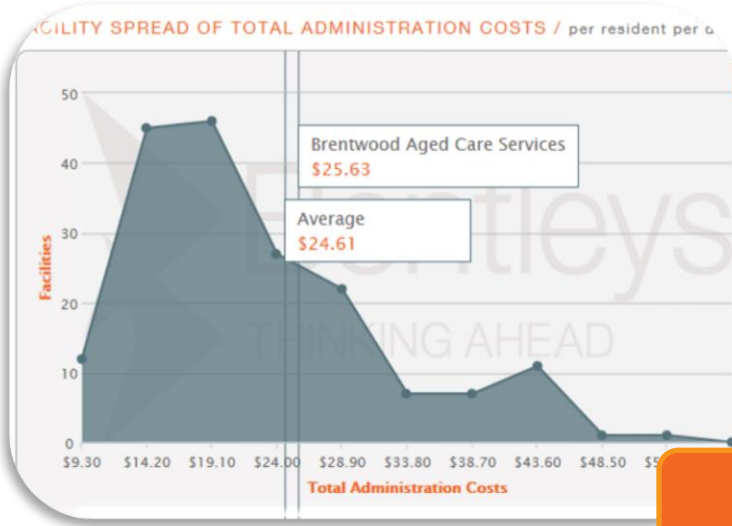
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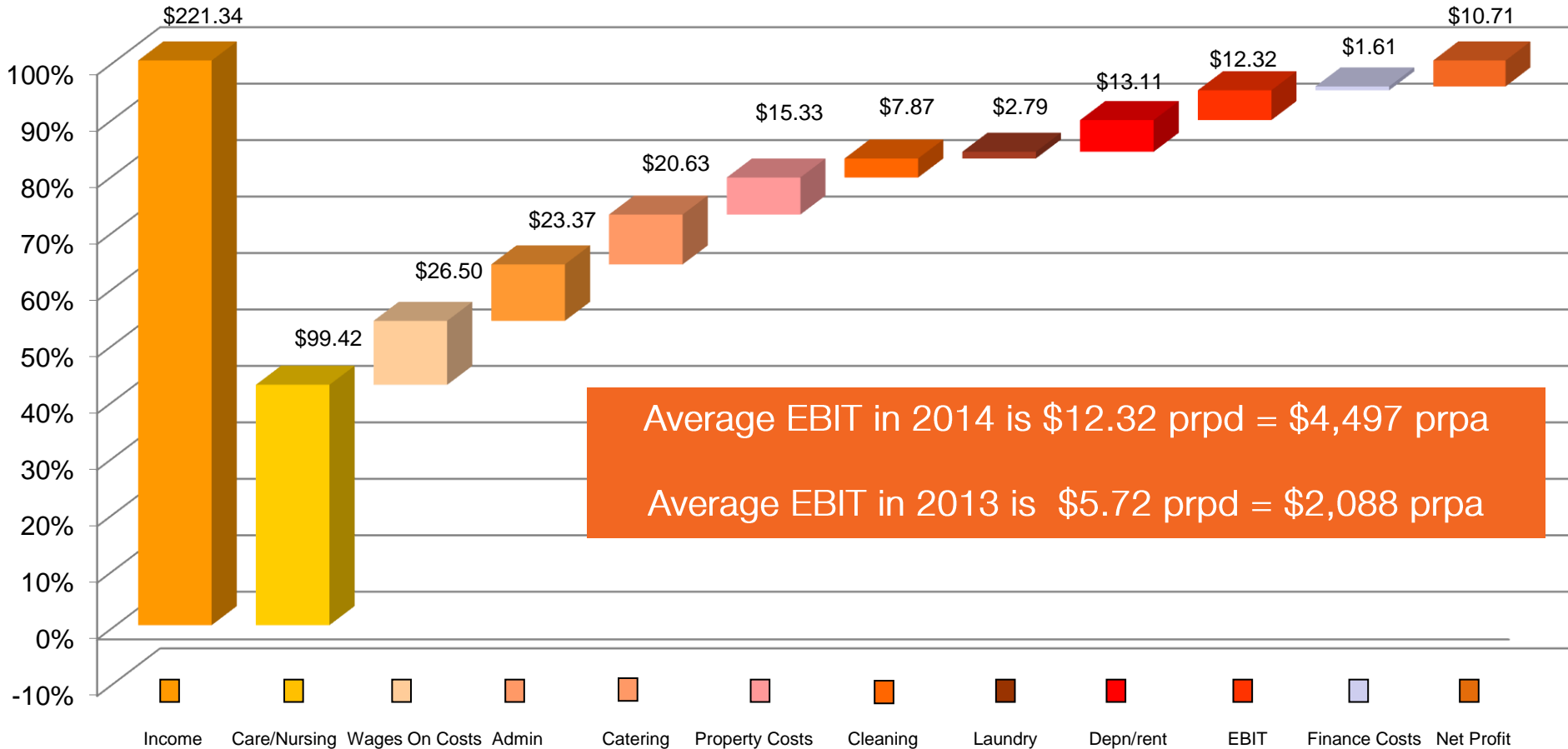
# Financial Metrics

## Measuring what Matters

# Phase 2: Detailed P&L Financial Outcomes & Activity Drivers



# Net profit bridge all services - 2014



Source: 2014 Bentleys National Aged Care Survey



# National Averages

	All Services	Top 25%	Variance	Variance
	\$	\$	\$	%
Subsidies	157.04	165.49	(8.45)	(5.38%)
Fees	57.94	63.66	(5.72)	(9.87%)
Other	6.36	5.34	1.02	16.04%
	<b>221.34</b>	<b>234.49</b>	<b>(13.15)</b>	<b>(5.94%)</b>
	\$	\$	\$	%
Care / nursing	99.42	92.24	7.18	7.22%
Cleaning	7.87	6.07	1.80	22.87%
Laundry	2.79	2.54	0.25	8.96%
Catering	20.63	20.54	0.09	0.44%
Property	15.33	14.66	0.67	4.37%
Administration	23.37	18.93	4.44	19.00%
Wage oncosts	26.50	23.41	3.09	11.66%
Depreciation/rent	13.11	11.36	1.75	13.35%
	<b>209.02</b>	<b>189.75</b>	<b>19.27</b>	<b>9.22%</b>
EBIT	<b>12.32</b>	<b>44.74</b>	<b>(32.42)</b>	<b>-263%</b>
Financing/Investment	1.61	2.28	(0.67)	(41.61%)
<b>NET SURPLUS / (DEFICIT) - PRPD</b>	<b>10.71</b>	<b>42.46</b>	<b>(31.75)</b>	<b>(296.45%)</b>

## EFFICIENCY SAVING

Admin variance  
= \$4.44 prpd

Yearly  
variance:  
80 bed facility  
=\$129,648 pa

# National Averages

	All Services		Top 25%	
	Operating Revenue	Operating Revenue	Operating Revenue	Operating Revenue
	\$	%	\$	%
Subsidies	157.04		165.49	
Fees	57.94		63.66	
Other	6.36		5.34	
	<b>221.34</b>		<b>234.49</b>	
	\$	%	\$	%
Care /nursing	99.42	46.25%	92.24	40.25%
Cleaning	7.87	3.66%	6.07	2.65%
Laundry	2.79	1.30%	2.54	1.11%
Catering	20.63	9.60%	20.54	8.96%
Property	15.33	7.13%	14.66	6.40%
Administration	23.37	10.87%	18.93	8.26%
Wage oncosts	26.50	12.33%	23.41	10.22%
Depreciation/rent	13.11	6%	11.36	5%
	<b>209.02</b>	<b>97%</b>	<b>189.75</b>	<b>83%</b>
EBIT	<b>12.32</b>	<b>6%</b>	<b>44.74</b>	<b>20%</b>
Financing/Investment	1.61	0.75%	2.28	0.99%
<b>NET SURPLUS / (DEFICIT) - PRPD</b>	<b>10.71</b>	<b>5%</b>	<b>42.46</b>	<b>19%</b>

**EFFICIENCY SAVING**

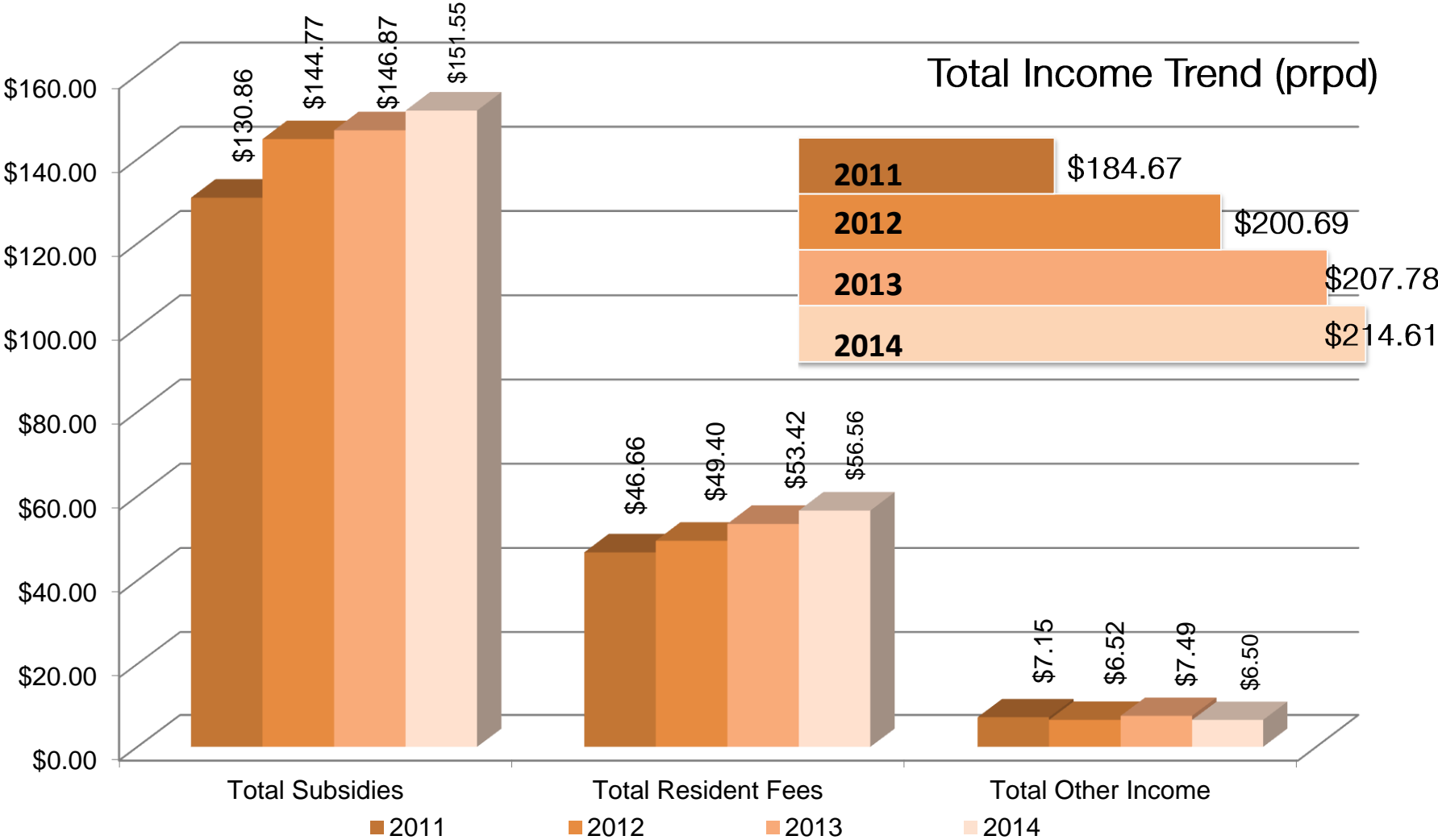
Care/Nursing costs as % of revenue:

**6% lower for top 25% operators**



Source: 2014 Bentleys National Aged Care Survey

# Same Pool

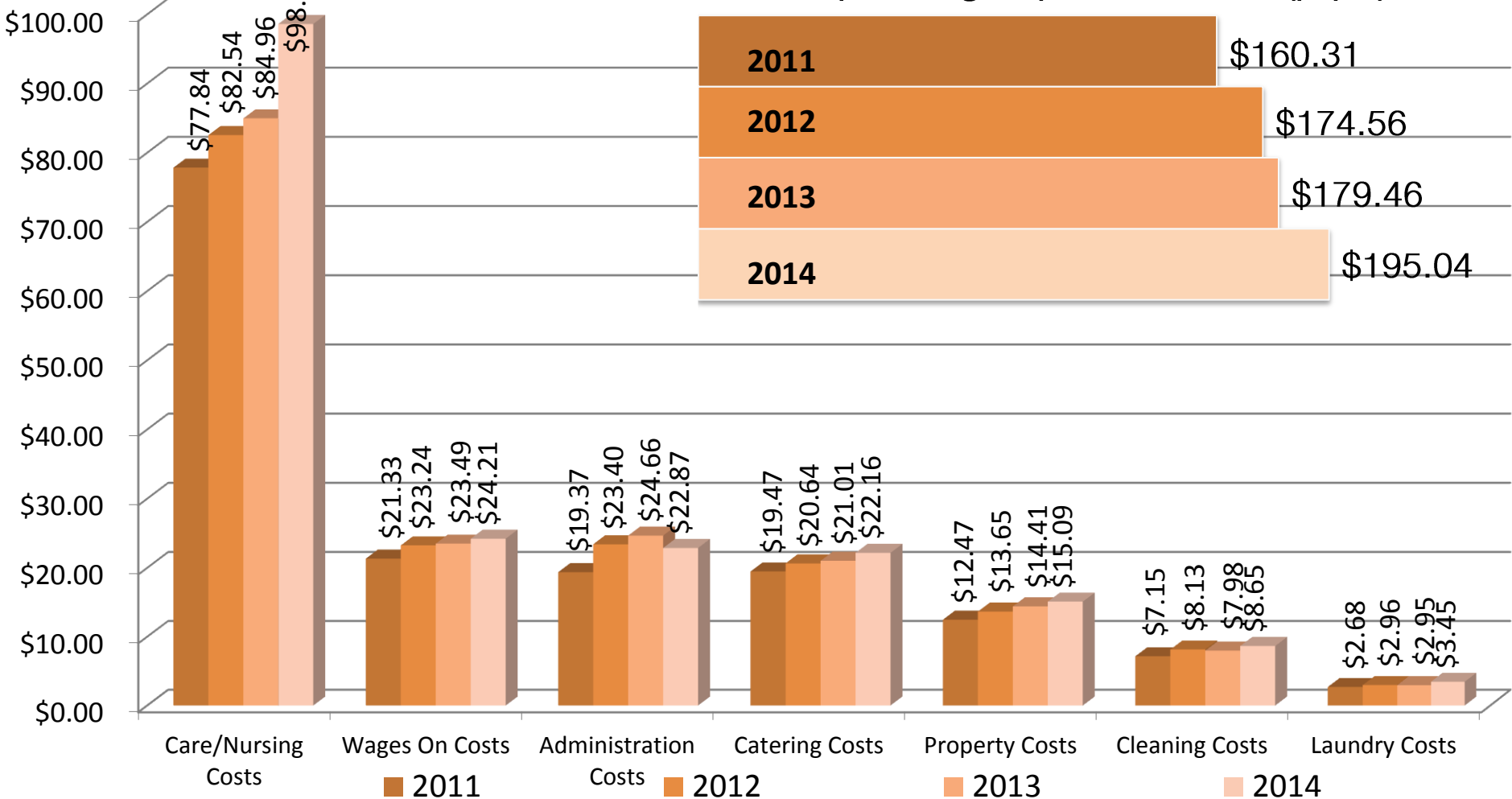


Source: 2014 Bentleys National Aged Care Survey



# Same Pool

Total Operating Expenses Trend (prpd)

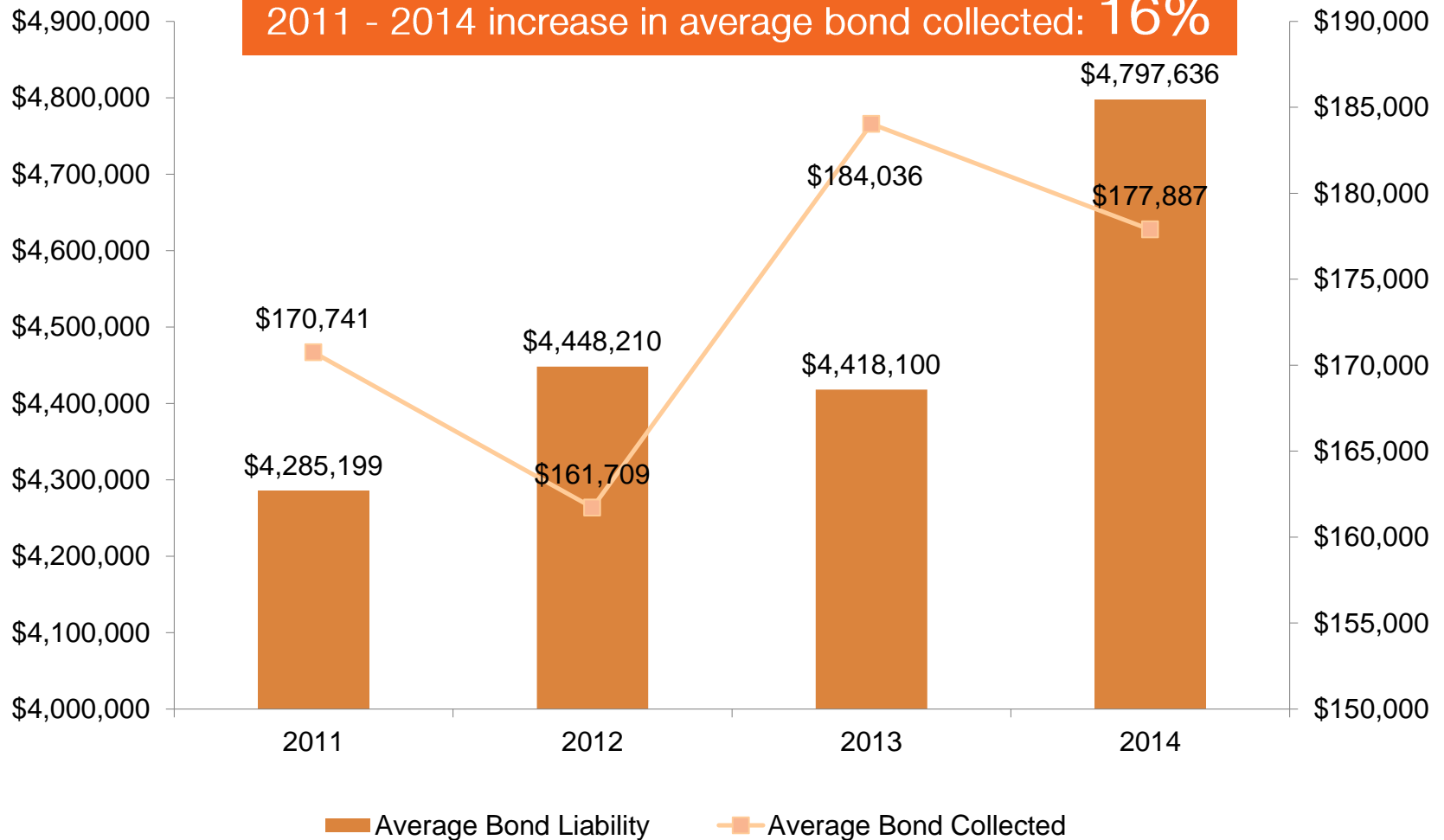


Source: 2014 Bentleys National Aged Care Survey

# Same pool – Accommodation Bonds

2011 - 2014 increase in total bond liability: **12%**

2011 - 2014 increase in average bond collected: **16%**



Source: 2014 Bentleys National Aged Care Survey



# Care, Accommodation and Services

National Averages 2014	FY 2014	% of total operating costs	% of resident running costs
<b>Expenses (p.r.p.d)</b>	\$	%	%
Care	99.42	47%	68%
Services	31.29	15%	21%
Accommodation	15.33	7%	10%
<b>Total resident running costs</b>	<b>146.04</b>	<b>69%</b>	<b>100%</b>
Administration	23.37	11%	
Wages on costs	26.5	13%	
Interest, Depreciation & Rent	14.72	7%	
<b>Total admin, wages on costs and finance</b>	<b>64.59</b>	<b>31%</b>	
<b>Total operating expenses</b>	<b>210.63</b>	<b>100%</b>	
<b>Total cost of accommodation</b>			
Accommodation	15.33		
Interest, Depreciation & Rent	14.72		
% of Wages & Administration	5.23		
<b>Total accommodation costs</b>	<b>35.28</b>		
<b>Total cost of care</b>			
Care	99.42		
% of Wages & Administration	33.95		
<b>Total care costs</b>	<b>133.37</b>		
<b>Total cost of services</b>			
Services	31.29		
% of Wages & Administration	10.68		
<b>Total services costs</b>	<b>41.97</b>		

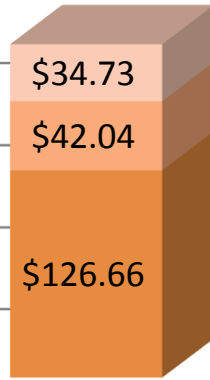
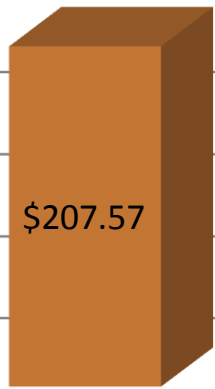
Unit costing using activity base analysis is required to understand divisional profitability

Source: 2014 Bentleys National Aged Care Survey

# Profits have increased

2013  
National  
Average

Difference  
\$4.14 prpd

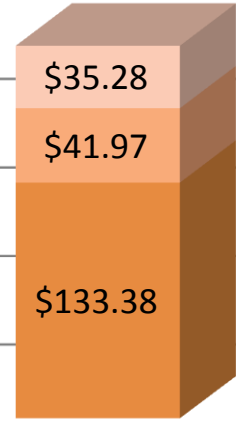
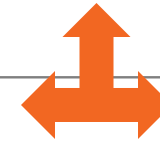
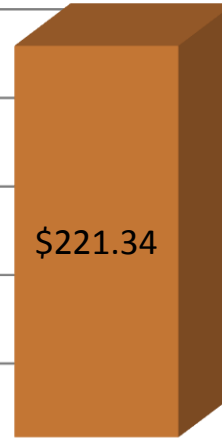


INCOME

EXPENSES

2014  
National  
Average

Difference  
\$10.71 prpd



INCOME

EXPENSES

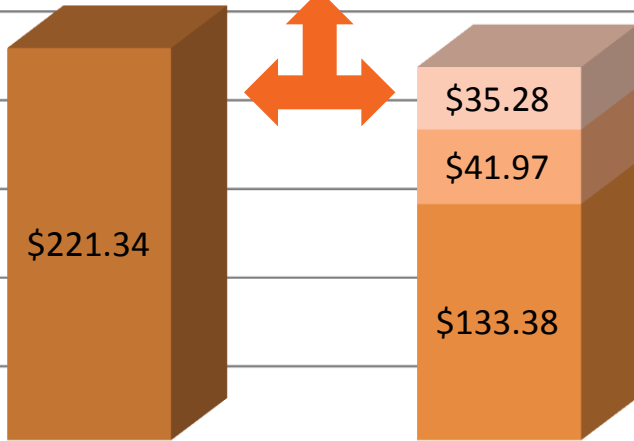
■ Income ■ Care Costs ■ Services (hotel) ■ Accommodation



# Care, Services & (Hotel) Accommodation

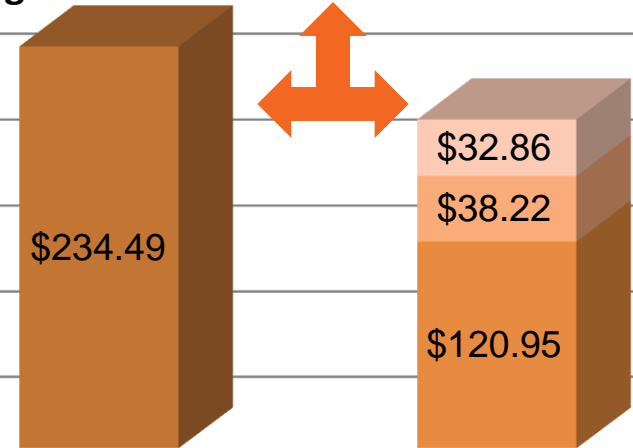
2014  
National  
Average

Difference  
\$10.71 prpd



2014  
Top 25%  
Average

Difference  
\$42.46 prpd



INCOME

EXPENSES

INCOME

EXPENSES

■ Income ■ Care Costs ■ Services (hotel) ■ Accommodation

# Financial Profile of a Successful Provider

Top 25% of Providers based on positive EBITDA

Measure	Results
EBITDA	100% of providers recorded EBITDA > \$39prpd (EBIT > \$23prpd)
Room configurations	38% of providers offered all single rooms with ensuites
Age of buildings	56% of providers have buildings aged between 16-30 years (28% with buildings less than 15 years old)
Average ACFI funding levels (frailty measures)	64% of providers with Average ACFI funding levels > \$117.01 prpd
Care staff to support staff ratio	69% of providers have a care staff to support staff ratio greater than or equal to 3:2

EBITDA performance is different to sustainability!

Source: 2014 Bentleys National Aged Care Survey

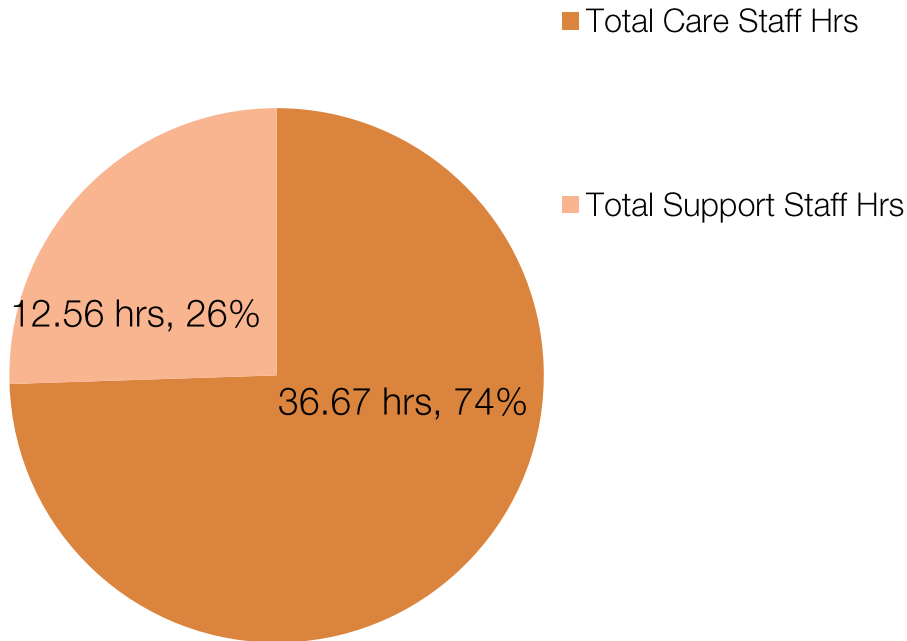
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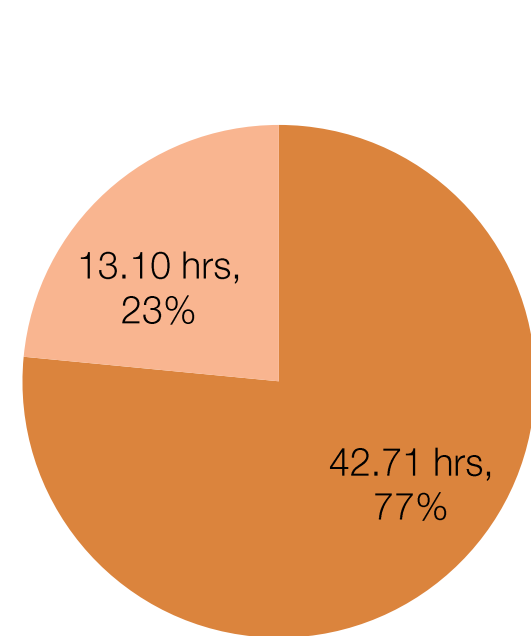
# Strategy Playing to Win

# Staffing Profiles

2004



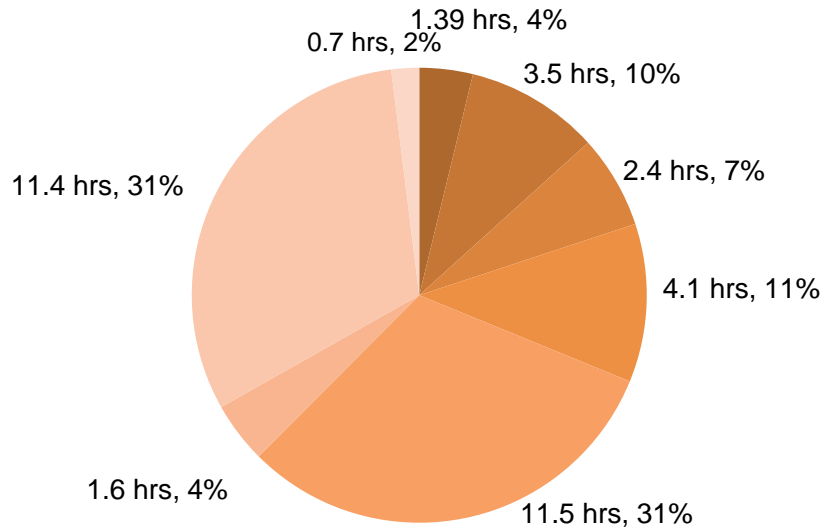
2014



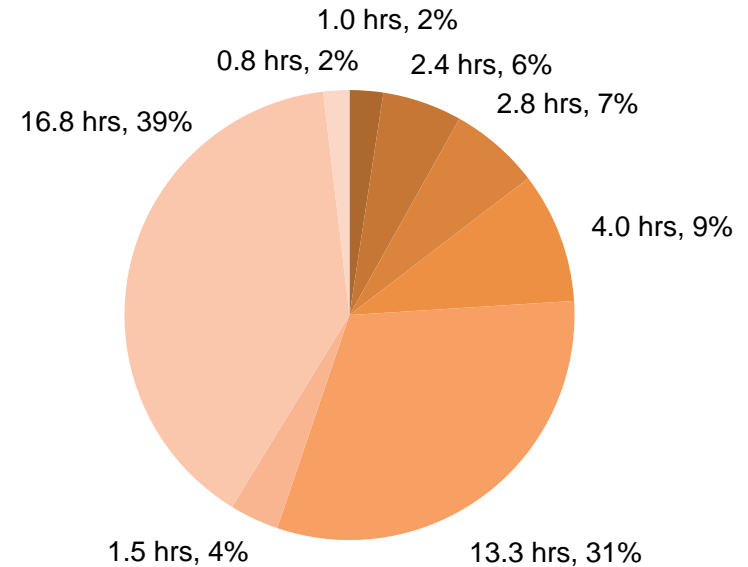
Providers have been forced to find efficiencies in care staffing profiles

# Care Staff Hours Dissection

2004



2014

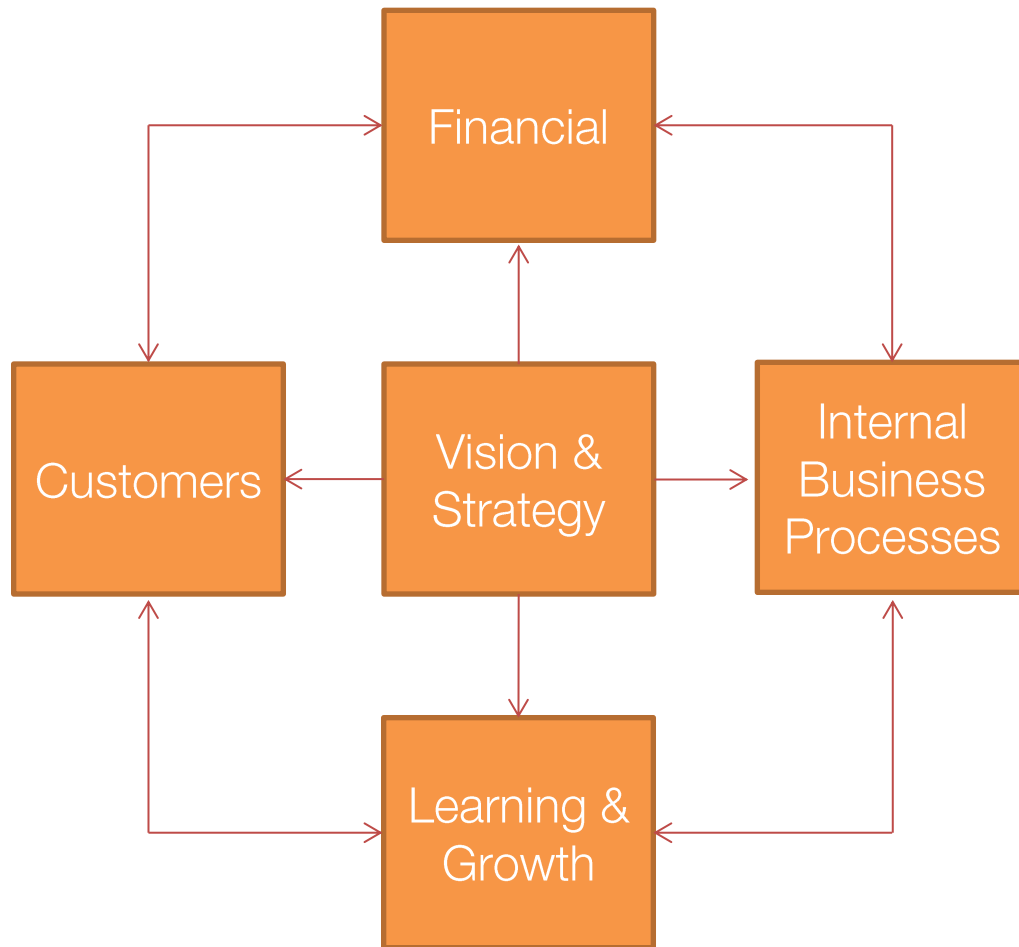


- DON/Care Mgr    ■ Lvl 2,3,4 RN    ■ Lvl 1 RN    ■ EN
- AN    ■ Activities    ■ PCA/HCA    ■ Therapists



With constraints shown in changing nature of care provision – transition from RNs/ENs to PCAs/HCAs

# The Balanced Scorecard



## Four interlinked quadrants

enables focus on driving long term financially viable delivery on mission by:

- creating value for current and future clients;
- build/enhancement of internal capabilities;
- making investments in people, systems and procedures necessary to improve performance.



# Factors that Matter

# of family / resident contact episodes - face to face + online

% Enquiry conversion to occupancy

Resource investment (time + financial) into R&D

R&D outcomes commercialised / implemented

Resource investment (time + financial) into Training

# of community visits (schools etc)

% compliance with regulatory expectations- accreditation, WH&S etc

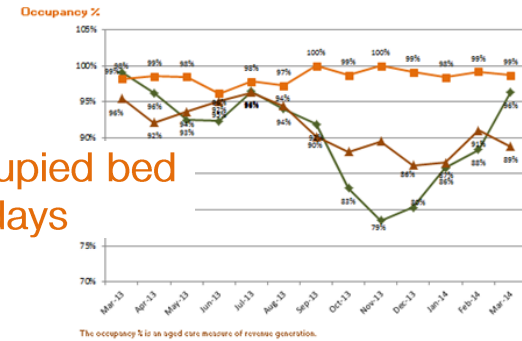
Client /resident/family satisfaction index (measured quarterly / half yearly)

## Balanced Score card



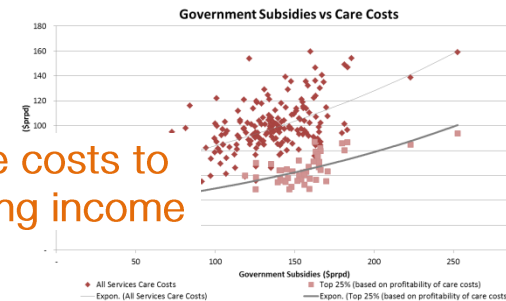
Employee engagement

Unoccupied bed days



Average room night revenue recovered - split between care, accommodation and services

Care costs to staffing income



Staff turnover; average length of service per employee; absenteeism

# Emerging Themes

## Technology & Sales/Marketing

National Averages 2014	prpd	% Operating Costs	100 residents pa
Technology / Computer	\$0.42	0.10%	\$15,330
Sales / Marketing	0.19	0.21%	\$6,935

*Asset exclusions – capital expenditure/depreciation*

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# Consumer Perspective

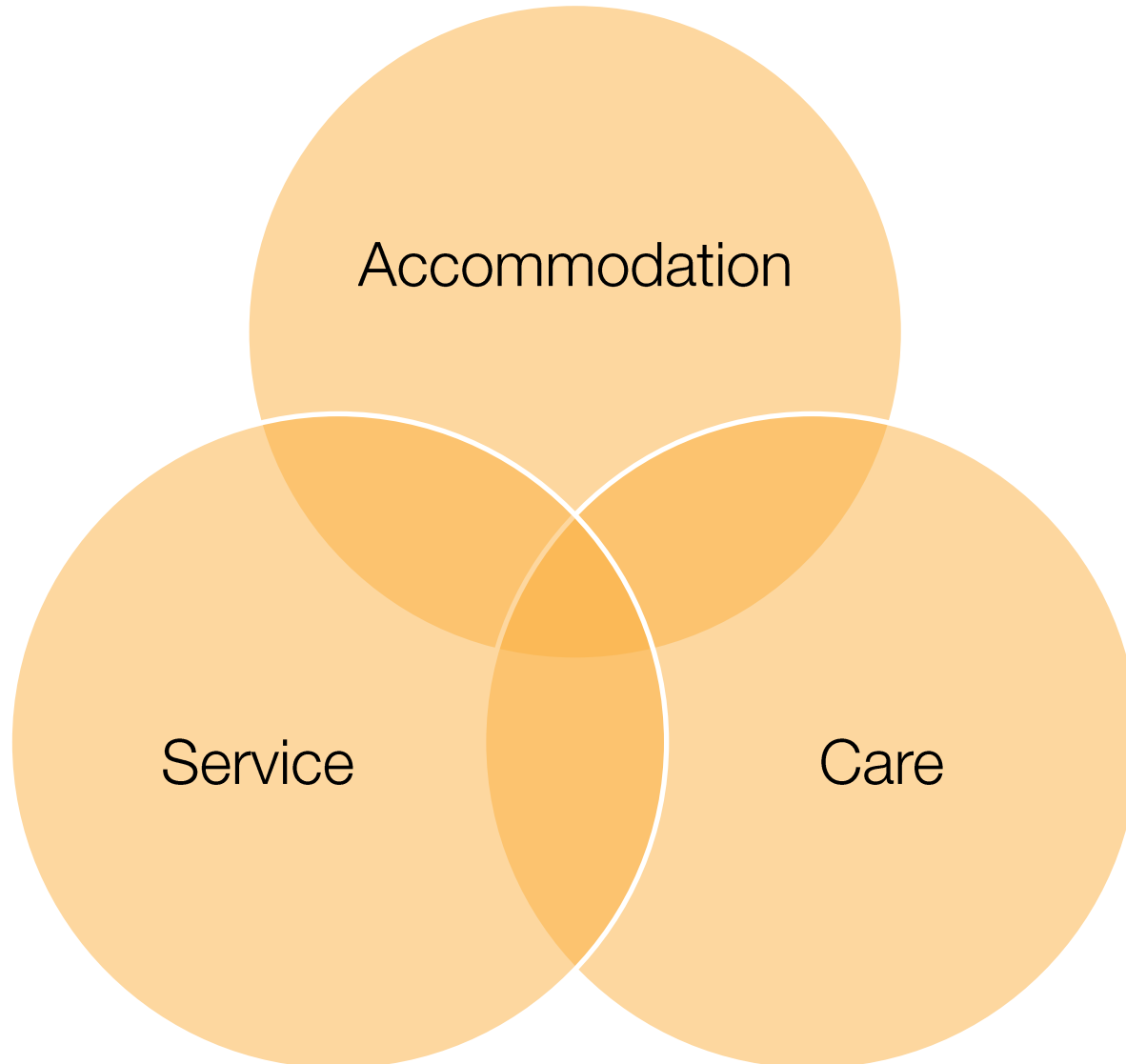
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# Three Key Messages



- Industry duty of care to our ageing population
- The value of a well informed family
- The provider's role

# The Aged Care Choices



# Industry Duty of Care

- Holistic view
- Raising the awareness
- Planning well in advance
- Value of advice



# A well informed family



- Emotionally ready
- Sensitive family discussions
- Organised, ready, informed
- Recent case study
- Rewarding area of advice

# Where does the provider fit in?



- Encouragement and awareness
- Family's experience – building the relationship and trust
- Confidence levels of front line staff



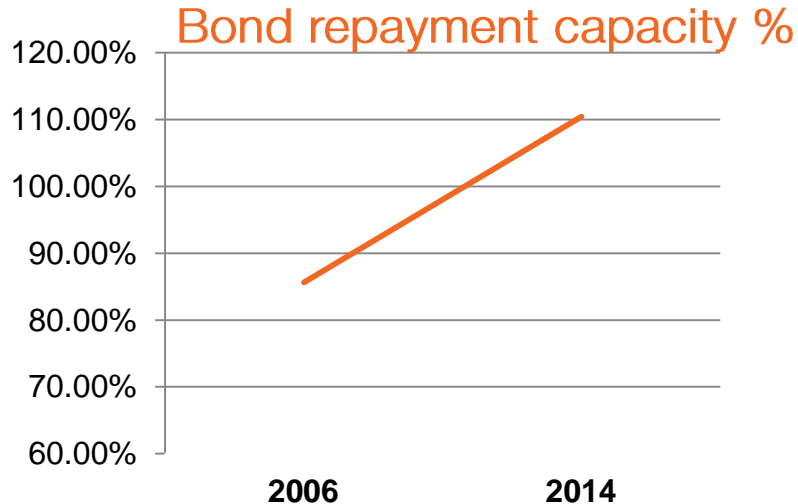
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# Governance

## Constitution of Good Corporate Governance

# Prudential Standards



Source: 2014 Bentleys National Aged Care Survey  
Calculated as: Cash and investments / Total bond liability

## RISKS POST REFORM:

- DAPs erode consumer's capital funding base
- Manage outflow of existing bonds
- Market forces will likely provide downward pricing pressure in the short to mid-term as providers seek to maximise occupancy levels

- Clarify the **permitted uses** of refundable deposit balances, accommodation bond balances;
- Introduce a **new governance standard** for approved providers holding refundable deposit and accommodation bond balances;
- Increase reporting and **disclosure**;
- Introduce additional information gathering powers for **monitoring compliance**;
- Arrangements by approved providers for the **management** of refundable deposit balances and accommodation bond balances
- Provision of information about **financial management** of approved providers

# Investment Management Strategy

## 50 Requirement for investment management strategy

- (1) This section applies to an approved provider that invests a refundable deposit or an accommodation bond in:
  - (a) a financial product covered by any of paragraphs 52N-1(3)(b) to (e) of the Act;
  - (b) a fund, but not a controlling entity of a fund, listed in item 2 of the first Schedule to Banking exemption No. 1 of 2013 made under the *Banking Act 1959*.

Note: Financial products for paragraph 52N-1(3)(e) of the Act are specified in section 64 of these principles.

- (2) The approved provider must implement and maintain a written investment management strategy that sets out the following:
  - (a) the approved provider's investment objectives;
  - (b) the approved provider's assessment of the level of risk to the provider's ability to refund refundable deposit balances or accommodation bond balances in accordance with the Act;
  - (c) a strategy for achieving the investment objectives while ensuring that the approved provider is able to refund refundable deposit balances and accommodation bond balances in accordance with the Act;
  - (d) the asset classes the approved provider may invest in;
  - (e) investment limits for each asset class that are consistent with the investment objectives;
  - (f) key personnel with appropriate skills and experience who are responsible for implementing the investment management strategy.
- (3) The investment management strategy must be approved by the key personnel who are responsible for the executive decisions of the approved provider.
- (4) The approved provider must:
  - (a) ensure that any investment of refundable deposits or accommodation bonds is in accordance with the provider's investment management strategy; and
  - (b) ensure that the provider's investment management strategy is kept up-to-date and complies with the requirements set out in subsection (2); and
  - (c) modify, or replace, its investment management strategy if the provider becomes aware that the investment management strategy no longer complies with the requirements set out in subsection (2).

Investment objectives

Risk assessment

Investment  
limits

Repayment profiles

Consolidation of  
asset classes and returns

Key personnel with skills

# Liquidity Management Strategy

## Division 2—Liquidity Standard

### 43 Requirement for sufficient liquidity

If an approved provider holds one or more refundable deposit balances, accommodation bond balances or entry contribution balances, the approved provider must maintain sufficient liquidity to ensure that the approved provider can refund, in accordance with the Act and these principles, any of those balances that can be expected to fall due in the following 12 months.

### 44 Requirement to implement, maintain and comply with liquidity management strategy

- (1) An approved provider that holds one or more refundable deposit balances, accommodation bond balances or entry contribution balances must implement and maintain a written liquidity management strategy that sets out:
  - (a) the amount (expressed as an amount of whole dollars) required to ensure that the approved provider has sufficient liquidity for the purposes of section 43 (the *minimum level of liquidity*); and
  - (b) the factors that the approved provider had regard to in determining the minimum level of liquidity; and
  - (c) the form in which the approved provider will maintain the minimum level of liquidity.
- (2) An approved provider must:
  - (a) maintain, in the form specified in the provider's liquidity management strategy, the minimum level of liquidity; and
  - (b) ensure that the provider's liquidity management strategy is kept up-to-date and complies with the requirements set out in subsection (1); and
  - (c) modify, or replace, its liquidity management strategy if the provider becomes aware that the strategy no longer complies with the requirements set out in subsection (1).

Source: <http://www.comlaw.gov.au/Details/F2014L00829>

Cash requirements

Historical pattern of  
bonds

Time taken for  
new residents to  
pay  
accommodation  
bonds

Characteristics of

Average value of  
bond balances

Average time taken to  
replace residents

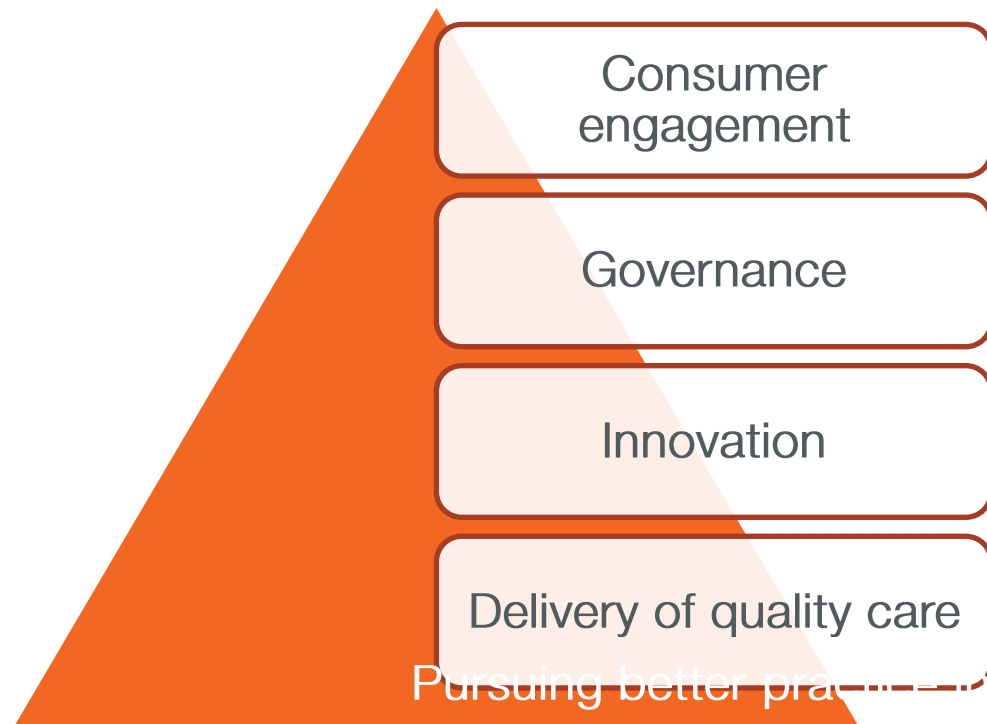
Expected number & amount of  
new accommodation bonds

# Good Corporate Governance

- Roles and responsibilities
- Board composition
- Purpose and Strategy
- Recognition and management of risk
- Organisational performance
- Board effectiveness
- Integrity and accountability
- Organisation building
- Culture and ethics
- Engagement

## South Australian Innovation Hub

– Government pilot to test ‘earned autonomy’ to aged care regulation.

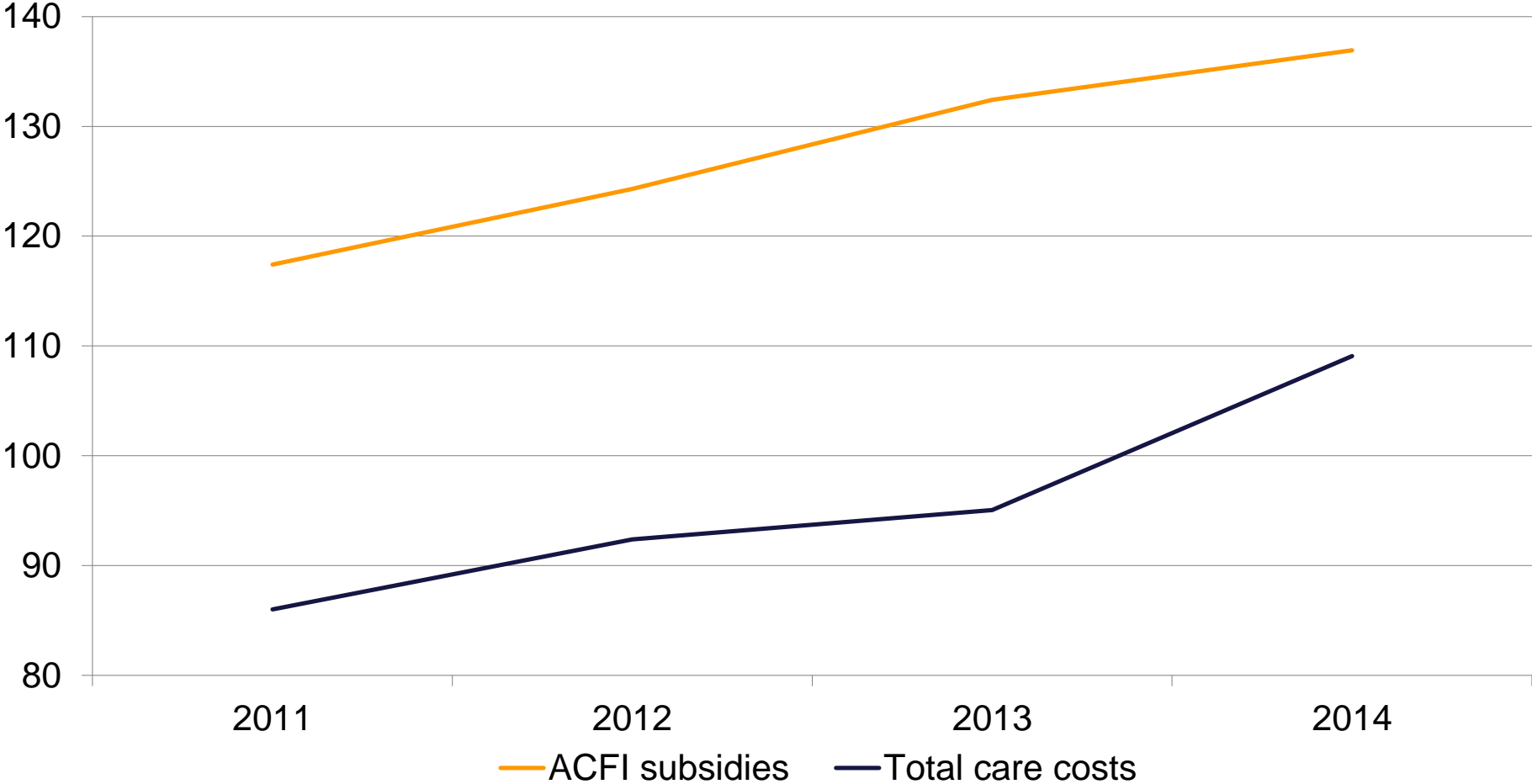


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# Capital Markets

# ACFI Subsidies vs Care Costs



Source: 2014 Bentleys National Aged Care Survey





# Thematics are strong

The Sydney Morning Herald  
**BusinessDay**

**JAPARA**  
HEALTHCARE

News Markets Quotes Portfolio Money Property Focus Small Business Executive S  
Today's News & Views Comment & Analysis World Business Mining & Resources Banking  
You are here: Home » BusinessDay

## Regis Healthcare and Japara Healthcare give confidence for future aged-care provider IPOs

October 8, 2014



An analyst who declined to be named said the rush of aged-care operators to the market was based on the high prices they were able to get. Regis shares closed at \$4.02, a 10 per cent rise from the \$3.65 offer price. At that price the \$1.1 billion company is valued at about 25 times its net earnings in 2015-16.

“Japara Healthcare is now one of Australia's largest operators in the aged care and retirement industry and our core objective is to provide the best available quality of life for the elderly population of Australia.”



Regis deserved to trade at a premium to Japara because it has higher earnings per place, has more urban places and excess capacity to take in clients.





# Equity Investors are keen for sector exposure

ORDERS WITHOUT BORDERS  
ASIAN HealthCare REITS > 7%

AMP Capital Investors Limited  
ABN 59 001 777 591, AFSL 232497

Media Release

AMPCAPITAL

19 AUGUST 2013

## AMP Capital to grow residential aged care investment

AMP Capital today announced Singapore-based G. K. Goh Holdings Limited (GK Goh) will acquire a 47.62 per cent stake in the AMP Capital managed residential aged care provider Domain Principal Group (DPG), for A\$136.7 million.

In addition, AMP Life will increase its ownership from 42.5 per cent to 47.62 per cent. This means that GK Goh and AMP Life will both hold equal 47.62 per cent interests in DPG as other clients re-weight portfolios and exit the investment. The remaining stake in the company is held by DPG management.

AMP Capital will continue to manage the investment on behalf of all shareholders.

As part of the transaction, AMP Life and GK Goh plan to invest an additional A\$50 million to finance further investment in Australia's aged care sector.

AMP Life has invested in the aged care sector in Australia since 1999. GK Goh, through a fund it has a significant stake in, is also a part owner of retirement villages in Western Australia.

AMP Capital Head of Aged Care Sally Evans said: "We're really pleased that AMP Life and GK Goh will be partners in the continued growth of DPG."

"The transaction gives DPG the opportunity to grow through investment in the existing 55 facilities, as well as building new state-of-the-art homes and potential acquisitions."

"Since AMP Capital acquired its initial aged care investment asset on behalf of clients in 2005, we've managed the acquisition of Domain Aged Care and significantly invested in the business, including recruiting a professional and dedicated management team, putting in place new systems, training and stronger governance to ensure that DPG's residents are receiving quality care."

"The DPG business is performing strongly with increased occupancy and a recent allocation from the Federal Government for another 385 new beds at DPG facilities."

"With the residential aged care sector expected to grow by 40 per cent in the next 10 years, as the population ages, an estimated A\$25 billion of capital will be needed to fund new places and rebuild existing homes." Ms Evans said.

Allity

[www.allity.com.au](http://www.allity.com.au)

Archer Capital acquired Allity in March 2013. Allity is one of Australia's leading private sector providers of residential aged care services with a portfolio of 31 facilities located in Victoria, New South Wales, Queensland and South Australia.

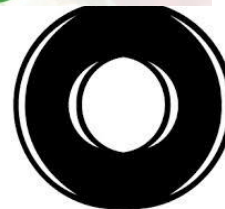
Allity provides services to over 2,400 residents with a roughly equal mix of high care and low care licences, plus a small number of extra service beds. The facilities range in size from 30 beds to as large as 225 beds and are located predominantly in metropolitan areas. The portfolio also includes an additional 180 retirement units, some of which are being converted into aged care beds.

Allity has a strong pipeline of brownfield and greenfield development opportunities, several of which are underway or expected to begin construction in the coming months. The business remains committed to meeting the needs of Australia's ageing population and ensuring that every day is the best it can be for all residents.



- Archer completed acquisition in March 2013
- Allity is Australia's fifth largest for-profit residential aged care provider
- Focus is on operational improvement and organic/acquisitive expansion

Estia Health



MACQUARIE  
BANK



Bentleys  
THINKING AHEAD

# Equity investors are interested in a variety of business model components

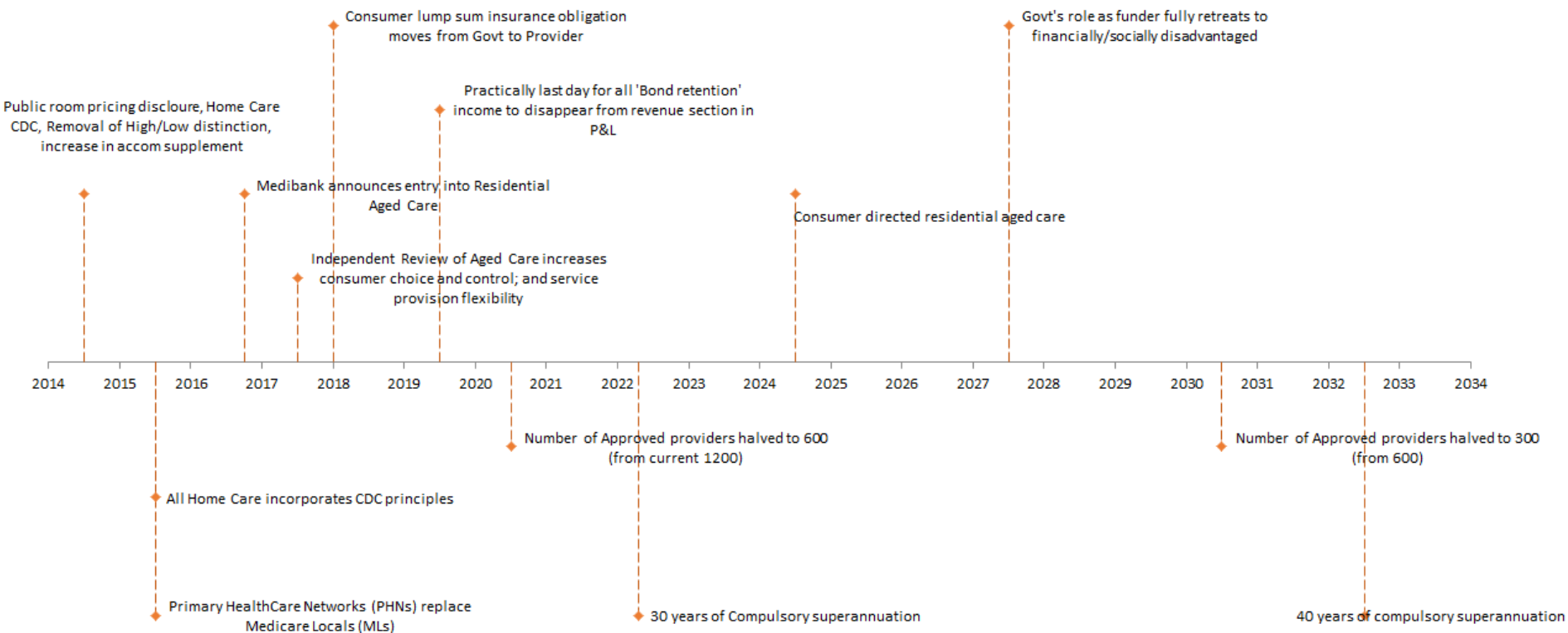
Problem	
Solution	1. Defensible recurrent government funding
Product	
Market	2. Market forces and affordability slowly increasing eg SGC
Leadership team	
Advisory board	3. Revenue growth opportunities eg brownfields development, acquisition etc
Competition	
Business model	4. Positive impact of proposed regulatory environment
Go to market strategy	
Financial projections	
Current equity raise	5. Tenancy risk mitigated by recurrent government funding paid to provider (reduces debtor risk)
Future equity raises	
Exit/liquidity events	

# Existing BUY Mandates

We act for pre-qualified institutional investors seeking:

- Full service providers – from single service to 1,000+ places
- Sub acute property only \$20M to \$2B – rental yield / expense
- Services / approved places only; no property
- Hotel service providers
- Mission based providers looking to exit residential aged care to focus on other parts of mission (or be one asset ‘light’ / care ‘heavy’)

# Thinking Ahead



- Consumer Directed Care in Residential Aged Care likely be much sooner than 2024. Policy challenge will be to define minimum level of care.
- The likely regulation of Home Care - increases regulatory compliance obligations, provides a value creating barrier to entry.

[www.agedcaresurvey.com.au](http://www.agedcaresurvey.com.au)

Thank You.

Questions?