StewartBrown

Integrity + Quality + Clarity

AGED CARE FINANCIAL PERFORMANCE SURVEY

Summary of Survey Outcomes

December 2015 Review




RESIDENTIAL CARE - COMMENTARY

Based on the survey results, the six months to December 2015 can be described as business as usual with respect to the overall financial performance of the residential aged care sector. The *average* Care Result across the 737 facilities in the December survey was **$11.30 per bed day** which is identical to the result for the six months to December 2014.

We saw profits spike in the September quarter as they do in most years, and we are now observing the same trends of a downward trajectory for overall profitability for the remainder of the year.

It is certainly a myth to suggest that the sector is reaping huge rewards and is riding on a wave of government largess. What we see is a sector that is sustainable at best, but only if the sector continues to strive for efficiency. We certainly still see potential for improvement.

We have seen in the database the plight of the facilities operating in outer regional and remote areas.

There are many providers that are performing very poorly and they will need to improve financially if they are to remain viable. ACFA's recent report *Financial Issues Affecting Rural and Remote Aged Care Providers,* in which StewartBrown assisted with the provision of data, confirms the financial and other difficulties faced by the outer regional and remote providers. These issues mean that future policy settings can't be made with a "one-size-fits-all" approach.

The December survey results show the sector's continuing drift towards and increasing focus on the provision of care to residents with high care needs. Of the 737 facilities in this survey, there were only **59 facilities** (8% of total) with an average ACFI income **less than $113 per bed day**. In contrast there were **610 facilities** (83% of total) with average ACFI income **in excess of $150 per bed day** and **468 facilities** (64% of total) with average ACFI income **in excess of $164 per bed day**.

This move towards caring only for residents with high care needs is likely to allow operators to achieve several things including:

- A more stable income stream
- A more stable staffing model and mix
- Increased profitability from achieving the above conditions

This trend will also bring challenges for the sector. A lot of the existing building stock was designed as hostels and provided low care services to residents. Therefore, in order to better accommodate the provision of high care services, a significant amount of capital expenditure to refurbish or rebuild these facilities will be required. However, a number of providers are unlikely to be in a position to do so given their poor operating results. This is one of the reasons that many providers are looking at strategic options with some considering the option to sell or merge. The ability of a potential suitor with access to capital to refurbish a facility and then gain access to higher accommodation income (RADs and DAPs) as well as to increase profitability through efficiencies may make these facilities attractive targets. As such, it is inevitable that there will be further consolidation of the sector.

The government is predicting that to meet future demand there will be a need to construct an **additional 82,000 places in the next 10 years** *(Aged Care Financing Authority, 2015*). Given that **just under 37,000 additional places were built in the previous decade**, it is very unlikely that all of the new places will indeed be built. The resultant effect of this is that demand, in most major centres at least, is likely to continue to be greater than supply. This in turn will allow providers to both maintain a relatively high occupancy rate and maximise their accommodation prices.

These additional beds will also require significant numbers of new staff. While the increased use of technology will assist aged care providers to gain productivity efficiencies, there will remain a need to skill large numbers of staff to meet future demand. Residential aged care will need to compete with other areas of the health sector for these staff including the home care and disability sectors.

There will also be the need for different skills in that workforce. Language skills in particular will be required as we are now seeing large numbers of persons that immigrated here in the fifties and sixties entering aged care homes. In addition, persons who may have come here as part of the family reunion programs are starting to enter residential aged care in larger numbers. Many of these people entered the country at an older age and do not have the English language skills of people that may have come here at a much younger age. There are many challenges ahead and these are but a few.

HEADLINE RESULTS

As mentioned earlier, if we were to provide a headline on the numbers it would be "business as usual". But that would be just scratching the surface of what the benchmark numbers are telling us about different elements of the financial performance and general activity within the sector.

The results of this survey are based on data accepted from 737 facilities across the nation. This represents **27%** of the **facilities** and **30%** of the **operational places** nationally. We note that we received data from several other facilities which we have not included due to our assessment of the data as unsuitable for its purpose.

The care result across **all facilities** averaged **$11.30** per bed day for the six months to December 2015. This is identical to the average result for the same survey period in 2014 (see Table 1). If seasonal trends continue unabated we would expect the operating results to decline for the remainder of the year as expenditure increases and it is likely that the 2016 full year results will be fairly similar to those of the 2015 financial year. The only thing that might alter this expectation would be a change in the Government's policy settings, which has been foreshadowed.

The results for the **top quartile** are slightly better than that for the same period last year at **$39.34** per bed day for the 2015 survey and $37.68 per bed day for the 2014 survey.

Since the results of the top quartile have improved but the survey average has remained the same then logically the results of those outside of the top quartile have declined. The average across **those outside the top quartile** was a care result of just **$2.83** per bed day for the December survey compared to $3.32 for the December 2014 survey. The December 2015 result is slightly better than at June 2015 ($2.11 per bed day), however if current trends are maintained we would expect the full year result for 2015/16 to be worse than last year's.

The *average* result of a loss of **$16.80** per bed day for those in the **bottom quartile** (184 facilities) means that their performance is already worse on average than both for the same period last year (loss of $15.61 per bed day) and for the full year to June 2015 (loss of $16.30 per bed day). These sort of results are not sustainable and means that these facilities are using income from accommodation or indeed from investing and fundraising to support their normal day to day Care Result. In fact the facility EBITDA for the bottom quartile group is now in negative territory at an average of negative $180 per bed day.

Table 1

	December 2015 $ per bed day	***June 2015 $ per bed day***	***December 2014 $ per bed day***
Care Result			
Average	**11.30**	9.84	11.30
Top 25%	**39.34**	35.20	37.68
Bottom 75%	**2.83**	**2.11**	**3.32**
Bottom Quartile	**(16.80)**	**(16.30)**	**(15.61)**
	$ per bed per annum	**$ per bed per annum**	**$ per bed per annum**
Facility EBITDA			
Average	**9,530**	8,652	9,034
Top 25%	**18,953**	16,811	17,287
Bottom 75%	**6,699**	6,679	6,366
Bottom Quartile	**(180)**	585	(72)

CARE RESULT EXPLAINED

Income	**Expenses**
Daily care fees	Direct care costs
Means tested fee	Catering
Extra service fees	Cleaning
Optional service fees	Laundry
ACFI subsidies	Utilities
Respite subsidies	Administrative & support services

Given the disparity between results of the top quartile and the bottom quartile there is definitely room for improvement for a large number of facilities in the survey.

The majority of facilities in the survey are not-for-profit organisations. While the results of the top quartile compare well with the for-profit sector, the not-for-profit sector is over-represented in the facilities that do not perform well financially.

Many of these not-for-profit organisations are mission or faith based, and while there will often be a cost to the bottom line associated with mission, it is important to ensure that the business model is sustainable so that the mission can be maintained into the future. There is a concern that if the financial performance of these facilities in the bottom quartile continue as they are then they will not be sustainable.

The other matter to consider is that on average, the Care Results are now at similar levels to those that were being achieved in December 2010. That year was probably a turning point because it was at this point that a large majority of residents in the system fully transitioned to ACFI funding. With the exception of a rise in average results during the 2012 financial year followed by a drop in profits in the 2013 year as ACFI rates were frozen the care result has stayed at this level.

What does this mean for the sector?

Generally it means that the additional income received as a result of higher subsidy rates is being expended on care costs - including on staff wages. It also means that return on income overall is less than it was in 2010 as shown in Table 2.

- Average Care Result was **$11.30** per bed day (June 2015: $9.84 per bed day and December 2014: $11.30 per bed day)
- Average Facility EBITDA was **$9,530** per bed per annum (June 2015: $8,652 per bed per annum and December 2014: $9,034 per bed per annum)
- Care income averaged **$212.76** per bed day (June 2015: $204.51 per bed day)
- The Care Result represents a return on care income of only **5.3%** (June 2015: 4.8%)
- **69.7%** of facilities in the survey achieved a positive care result (June 2015: 69.9%)
- **75.8%** of facilities in this survey (June 2015: 73.5%) made an overall surplus taking into account all sources of income and expenditure. This is higher than it has been for some time. The ratio was 77.8% at June 2012, 73.4% at June 2011, 65.0% at June 2010 and 63.5% at June 2009
- 91 facilities (**12.3%**) in the survey that had a negative EBITDA. This is worse than the level of 11.3% of the facilities in the June 2015 survey, which is a concern.
- The average Care Result of the top 50% of facilities in the survey was **$27.66 per bed day**
- In contrast, the average Care Result of the bottom 50% of facilities in the survey (369 facilities) was a **loss of $4.80** per bed day
- In fact, the average Care Result for the bottom quartile (184 facilities) was **a loss of $16.80** per bed day which is actually worse than for the June 2015 year where the average was a loss of $16.30 per bed day.
- If the results of the top quartile are excluded, the average care result for the remaining 75% of facilities (553 facilities) is a surplus of just **$2.83 per bed day.**

Figure 1 – Trends in the care results of residential aged care facilities

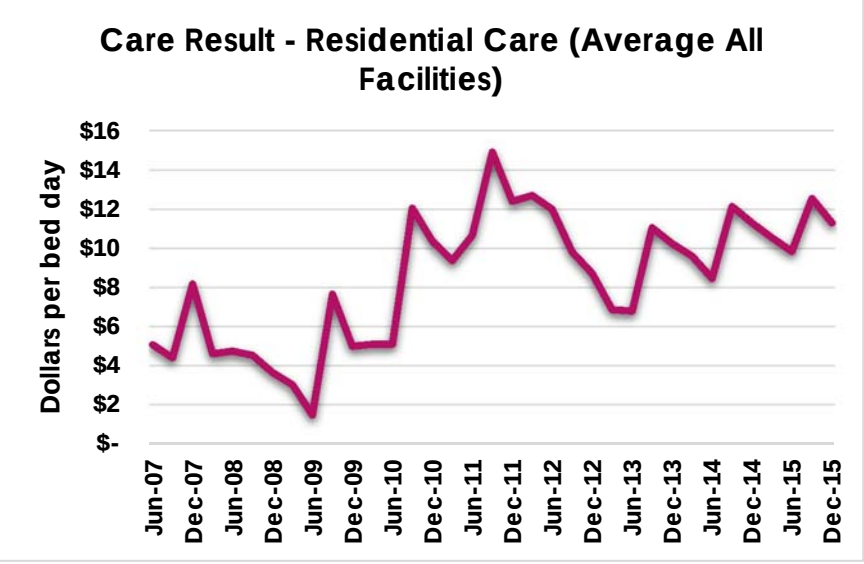


Table 2

	Dec 2010	Dec 2011	Dec 2012	Dec 2013	Dec 2014	Dec 2015
Care Result	$ 10.36	$ 12.41	$ 8.71	$ 10.24	$ 11.30	$ 11.30
Return on care income	6.5%	7.3%	5.0%	5.5%	5.6%	5.3%

Care income

Care income continues to rise at rates in excess of CPI and COPE (Figure 2) and reflects the trend towards caring for residents with higher care needs. The ACFI funding model design promotes this move to a "high care needs" model because the higher the level of income the greater the contribution to what are relatively fixed costs. So while direct care wages may increase in proportion with increased levels of income, the other costs such as hotel services costs, utilities and administration generally do not increase in the same proportion.

Simply put, if direct care costs represent 60% of care income, then for every additional dollar of care income 60 cents will go to paying additional care costs (variable). However, most of the other costs will not increase as a result of the resident having higher care needs so the other 40 cents, or a large proportion of it at least, should go to the bottom line.

Those facilities that are improving their results, and those that are consistently in the top quartile, tend to put this into practice. Unfortunately, too many facilities do not adhere to that practice and their financial performance reflects that.

The care income for the **top quartile** averaged **$213.29 per bed day** and the **bottom quartile** had average care income of **$210.07 per bed day** - not a significant difference. Yet the care results of the **top quartile** averaged **$39.21 per bed day** compared to that of the **bottom quartile** which averaged a **loss of $16.80 per bed day** - a difference of $56.01 per bed day. In a 100 bed facility this would represent a difference in profitability of close to $2 million per annum!

Figure 2 – Comparison of the cumulative increase in care income to that of care wages, CPI index, COPE index and overall increase in subsidy rates include CAP and COPE

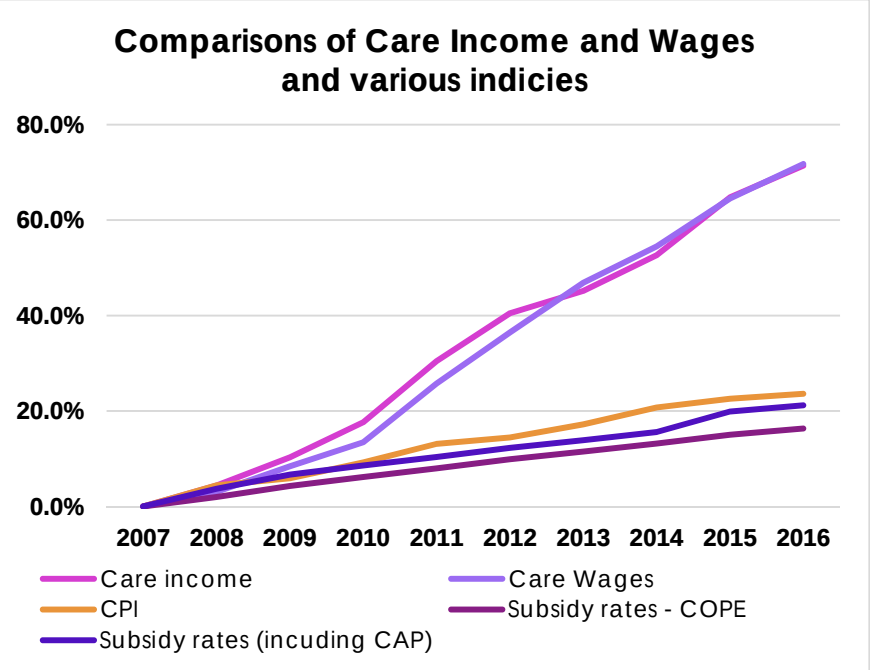
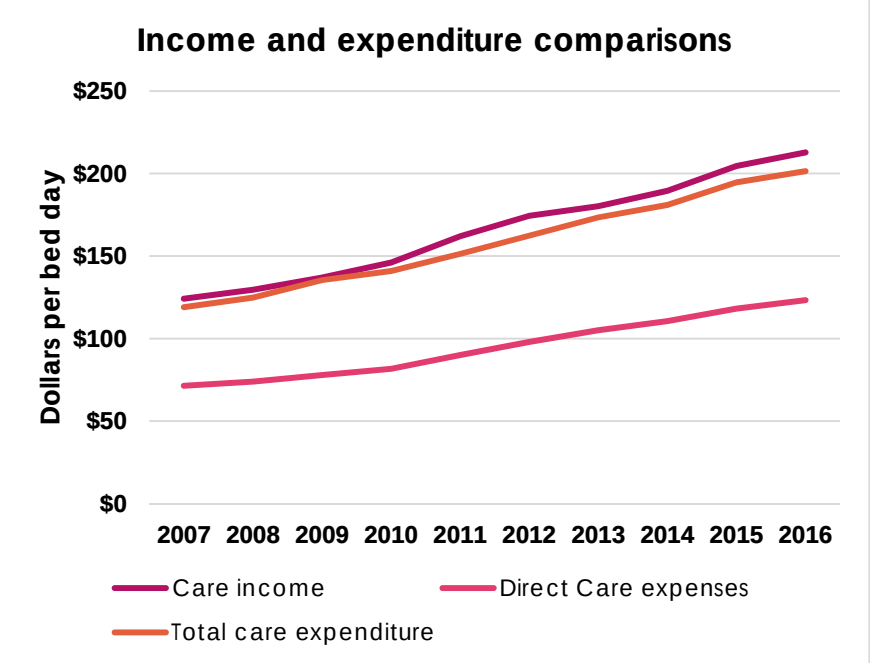


Figure 3 – Trends in care income, direct expenditure and total care expenditure



Again, we make the point that there is obviously room for improvement for these facilities. We are not suggesting that they will achieve the same results as those in the top quartile. Many providers do not want to achieve those results and they look at the difference as their cost of mission. But there should be room for these facilities to improve their results where there is a gap as big as $56.01 per bed day in which to move.

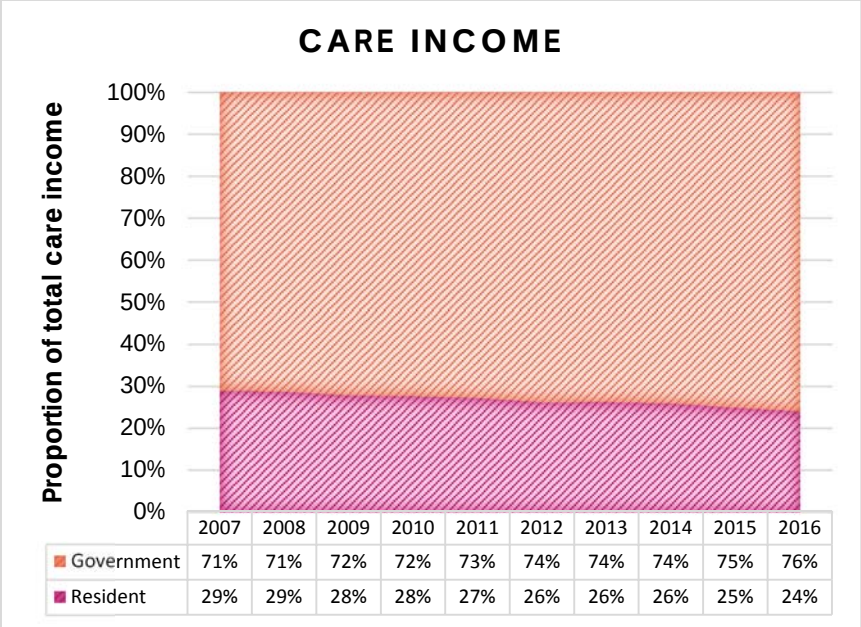
At this point in time, it would appear that, despite the new means tested fee, the government's share of the cost of care is rising rather than declining. Current trends are that resident fees, including the resident payment of the means tested fee, as a proportion of total care income, is declining (Figure 4).

It also must be noted that the rate of decline in the overall share of the total contribution from residents is less than the increase in overall income, so in adjusted terms, the trend might be heading in the right direction from the government's point of view.

These trends are also likely to be reflective of the not-for-profit bias in the survey in that there will be a greater number of supported residents in the mix. The **average supported ratio** across the facilities in the survey was **47%** so it is not unexpected that there would be fewer residents paying a means tested fee. We will examine this more closely in coming surveys and look at the mix between government and resident funding, and the supported resident ratios depending on the location of the facility.

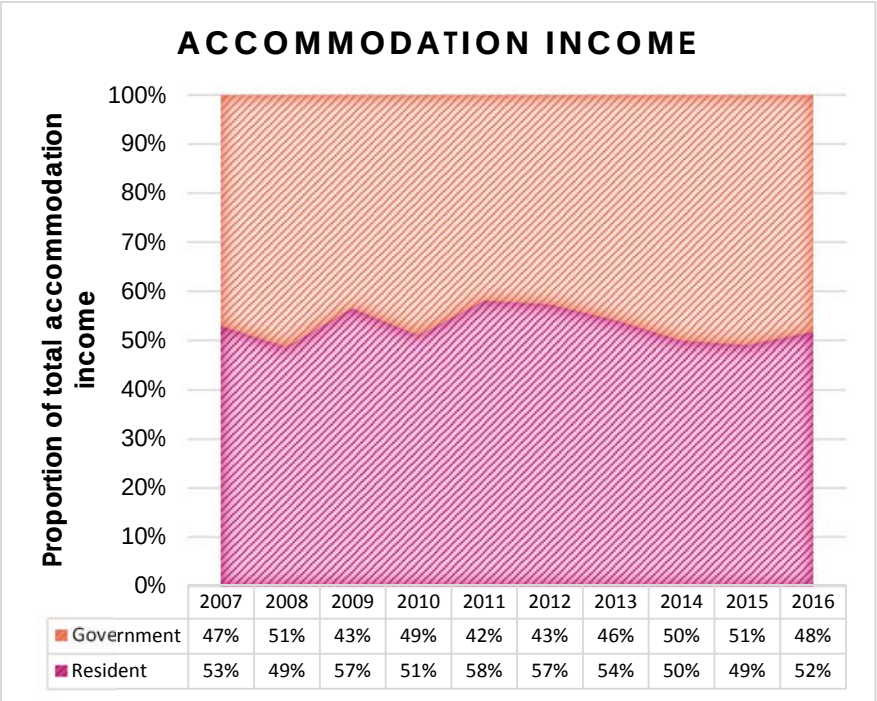
While providers continue to move away from catering for residents with low care needs and towards residents with high care needs the share of total care income provided by the government will continue to increase. Once the overall resident mix stabilises and the new means test is applied across the majority of residents in the system then we might see the governments share in percentage terms start to decline. Certainly this will be what the government will be hoping for.

Figure 4 – Source of Care income as a share of total



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Government	71%	71%	72%	72%	73%	74%	74%	74%	75%	76%
Resident	29%	29%	28%	28%	27%	26%	26%	26%	25%	24%

Figure 5 – Source of accommodation income - share of total



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Government	47%	51%	43%	49%	42%	43%	46%	50%	51%	48%
Resident	53%	49%	57%	51%	58%	57%	54%	50%	49%	52%

Accommodation income

Since 2007, accommodation income has increased from an average of $9.13 per bed day to **$24.35 per bed day** in this latest survey. This income comprises retentions from accommodation bonds, daily accommodation payments and charges and the various accommodation supplements paid by the Government. In the past the larger share of accommodation income has come from the resident, however in 2014 and 2015 the split was almost 50/50 with the residents share on a downward trend.

In the past two surveys we have seen that trend reversed with a shift back towards the resident contributing the larger share of accommodation income. We would expect that, due to the high supported resident ratios across this survey population, the figures would be overstating the government's contribution relative to the aged care sector as a whole.

Along with the location analysis on care income we will also look in the future at accommodation income at a location level to see how those in the major cities fare against those in the regional and more remote locations.

The performance gap

The performance gap can be described as the difference in financial performance of those facilities in the top quartile and the rest. When we stratify this data the gap between those in the second quartile and those in the top quartile may not be significant. However if we look at the gap between those in the top quartile and those in the bottom quartile then the gap is very large.

In the past we have assessed the gap between the survey average and the average of the top quartile, however this time we will look at the gap between the top quartile and the average of all the other facilities excluding those in the top quartile. Across all facilities the difference in the Care Result of the top quartile and the other facilities is an average of $36.38 per bed day as shown in Figure 7.

For the purpose of this analysis Band 1 facilities would have average ACFI income over $172 per bed day and Band 5 facilities would have an average ACFI income of less than $127 per bed day. There are $15 increments between Bands.

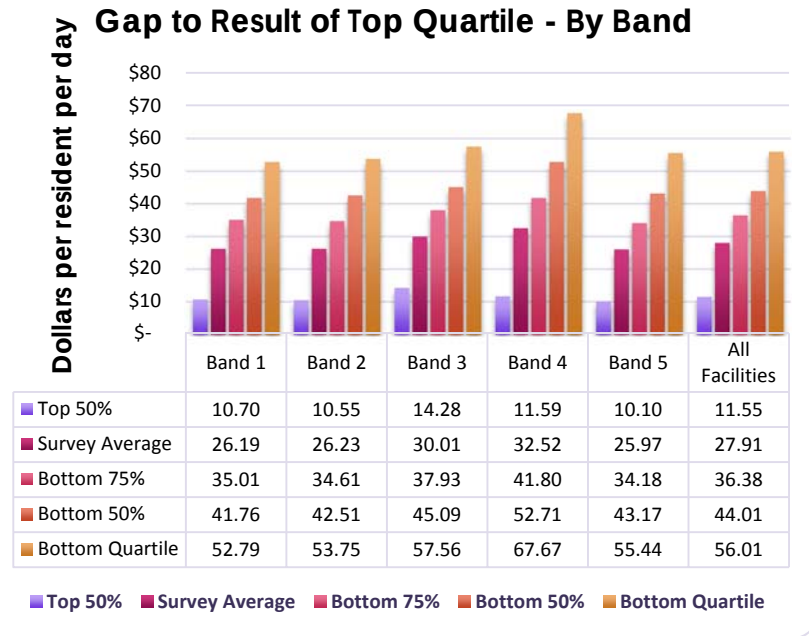
Figure 6 – Stratification of facilities - average care result by benchmark band

	Band 1	Band 2	Band 3	Band 4	Band 5	All Facilities
Top Quartile	38.17	37.43	39.66	47.25	34.16	39.21
Top 50%	27.46	26.88	25.38	35.66	24.06	27.66
Survey Average	11.98	11.21	9.65	14.73	8.19	11.30
Bottom 50%	(3.59)	(5.08)	(5.43)	(5.46)	(9.01)	(4.80)
Bottom 75%	3.15	2.83	1.73	5.45	(0.02)	2.83
Bottom Quartile	(14.62)	(16.31)	(17.91)	(20.42)	(21.28)	(16.80)

It is interesting to note that while those facilities in Band 4 have the best result for the top quartile, it also has the second worst average result for the bottom quartile. The gap in care result between the top quartile and the bottom 75% in Band 4 is an average of $41.80 per bed day

Figure 7 illustrates that there are significant gaps in financial performance across all the benchmark bands.

Figure 7 - Gap in care result between top quartile average and the average of other groups in survey



	Band 1	Band 2	Band 3	Band 4	Band 5	All Facilities
Top 50%	10.70	10.55	14.28	11.59	10.10	11.55
Survey Average	26.19	26.23	30.01	32.52	25.97	27.91
Bottom 75%	35.01	34.61	37.93	41.80	34.18	36.38
Bottom 50%	41.76	42.51	45.09	52.71	43.17	44.01
Bottom Quartile	52.79	53.75	57.56	67.67	55.44	56.01

The major driver of profitability in residential aged care continues to be the ability to get the balance between care income and direct care costs right. The major difference between those facilities in the top quartile and the other facilities in the survey is care costs and the majority of these costs is comprised of care staff costs.

The differences are even further amplified when the top quartile figures are compared to those of the bottom quartile. The total difference in care result is an average of $56.01 per bed day and **$34.52 per bed day** can be attributed to **care costs**. There are also significant differences in hotel service costs and in administration and support services.

What needs to be done to achieve these top quarter results? It is unlikely that the answer will be a one-size-fits all approach. Possible solutions include:

- Improved operating efficiencies leading to a reduction in staff costs
- Improved use of technology and monitoring equipment
- Changes to the cost mix of staff to an optimal level
- Ensuring staff hours are appropriate for the care needs of the residents and ACFI income is being claimed is at the appropriate level

For those in the bottom quartile, the answer can't continue to be "do nothing". With the low interest rate environment it is becoming increasingly difficult to subsidise through investment income returns.

It is critical for aged care providers to maximise operating profitability so that they remain viable and sustain their business into the future. Providers must be allowed to generate sufficient income to reinvest in the business and in the building stock to provide the standard of accommodation and services that consumers of today and the future will demand.

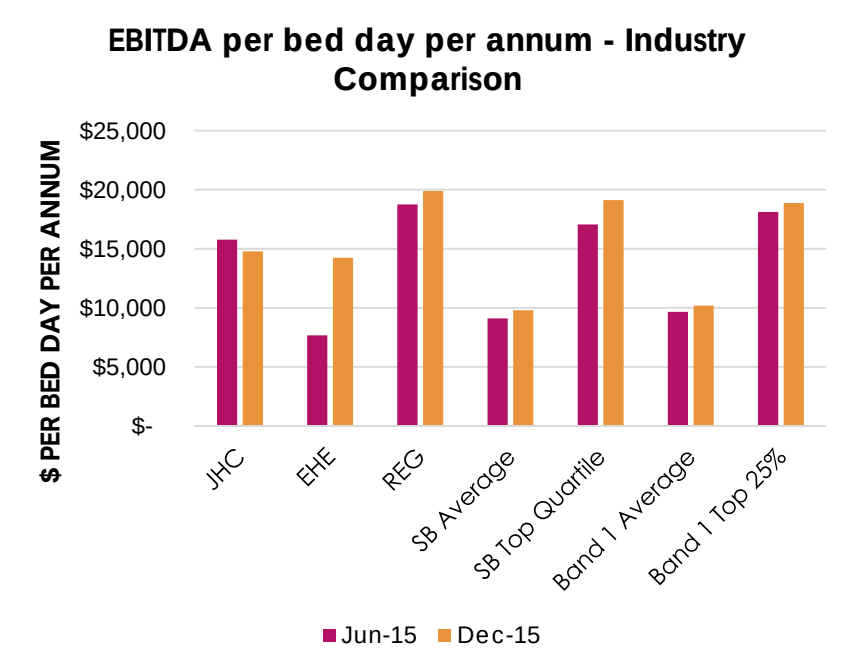
Unfortunately, far too many providers are relying on "capital" streams of income to subsidise their day to day operating costs and this is unlikely to be a sustainable business model. There may be insufficient reserves remaining to undertake the capital investment that will be necessary in the future and the ability to borrow will be hampered by the financial performance at an operational level.

A focus on the Listed Entities

In 2014 and 2015 three aged care providers, Japara (JHC), Estia (EHE) and Regis (REG), were listed on the Australian Stock Exchange. This was an exciting time for the sector and indicated the level of interest in the aged care sector and the willingness of institutions and individuals to invest in the future of aged care. It also indicated the confidence of the investor community in the future of the aged care industry.

So how have these companies been performing and how does their performance compare to the StewartBrown Survey results (which largely consist of not-for-profit aged care providers)?

Figure 8 – Comparison of EBITDA of listed entities compared to facilities in StewartBrown Survey



Profitability

The profits of the listed entities as measured on an EBITDA per bed per annum basis are in excess of the StewartBrown Survey average (Figure 8) but, with exception of Regis, are **below** the StewartBrown Survey average of the top

quartile of facilities. We have included data for Band 1 facilities which have similar ACFI income characteristics as the three listed entities.

In calculating the EBITDA per bed per annum, the listed entity results have been adjusted for some one-off transactions and these results may be inflated by some corporate income that, in respect of the StewartBrown survey may not be recognised at a facility level.

Estia has seen a significant improvement in profitability in their December 2015 half year results. It will be interesting to observe if this level of profitability continues as the organisation brings on the large number of additional beds it is either building or adding to its portfolio through acquisitions.

The results for Regis have been maintained in this latest half year on top of a good performance for the full year to June 2015. Again it will be interesting to see whether they can maintain or grow profits during a planned phase of growth through constructing new facilities and through the acquisition of existing facilities.

Occupancy of the facilities of the listed entities is **generally lower** than the StewartBrown survey averages (Figure 9). This may be affected by the significant number of new facilities being brought on line by Estia and it will be interesting to see how this statistic develops over time.

There is a difference in the way the listed entities are financing their operations and growth strategies. Regis has a significantly higher proportion of their assets financed by resident liabilities than the other two entities as shown in Figure 10.

Figure 9 – Comparison of occupancy levels of listed entities compared to facilities in StewartBrown Survey

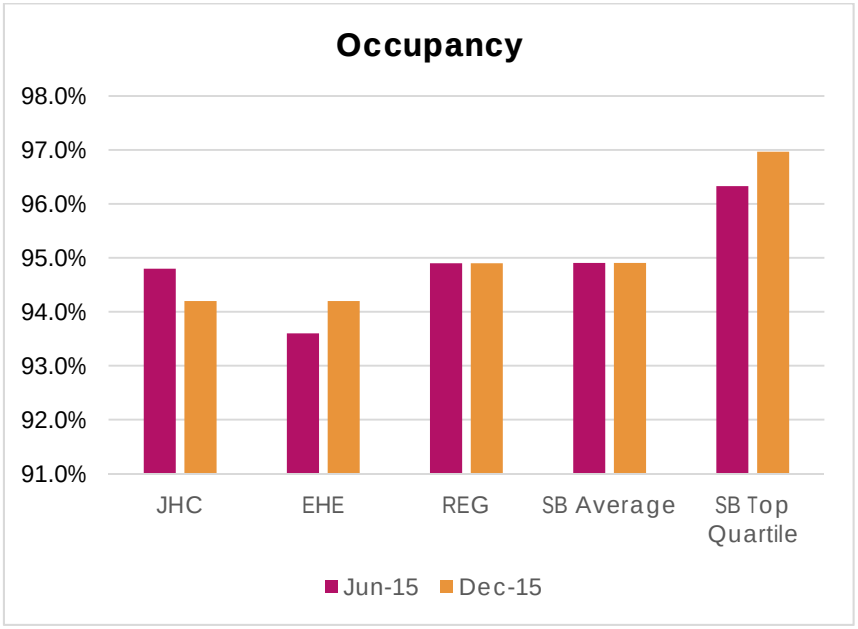
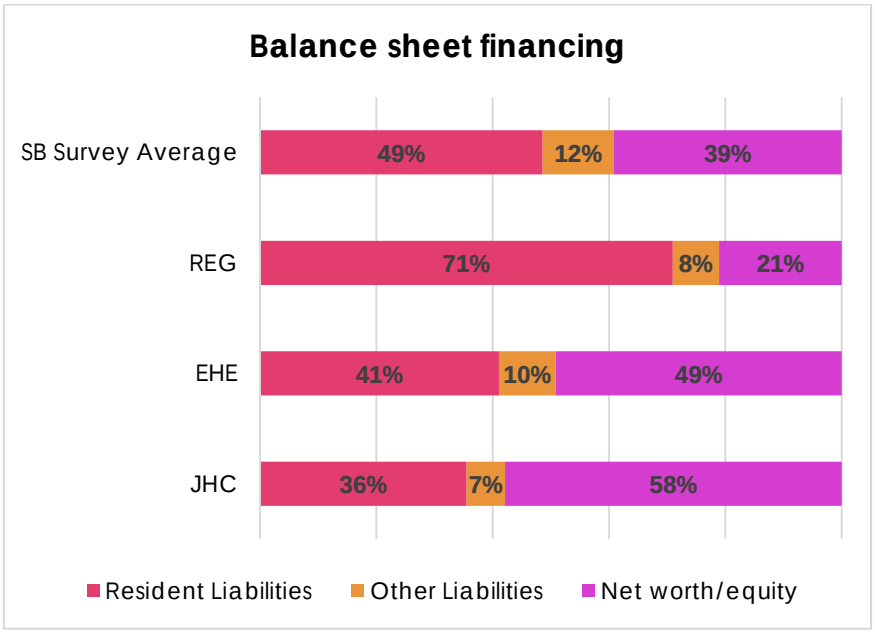


Figure 10 – Comparison of balance sheet financing of listed entities compared to facilities in StewartBrown Survey



There is a high level of **intangible assets** on the balance sheets of these entities. These are mainly comprised of good will and bed licences. The level of intangible assets on their balance sheets means that both Regis and Estia have in fact **negative tangible assets** at December 2015 (Figure 11).

There could also be some question marks over the value of these assets should the government alter its policy settings and deregulate the market which is likely to cause some impairment of the value of the bed licences in the books of those entities.

However, this concern has not affected the share prices of these companies. They continue to ride high on a wave of optimism regarding the future of the sector generally.

Another sign of the confidence in these for profit providers appears to have been indicated through the allocations of operational places in the 2015 ACAR, the results of which were recently released. The big ACAR winners this year has been the for-profit providers. The competition for places was extremely high with applications made for **38,859 places** and only **10,940 being allocated**, including 1,033 places to new providers.

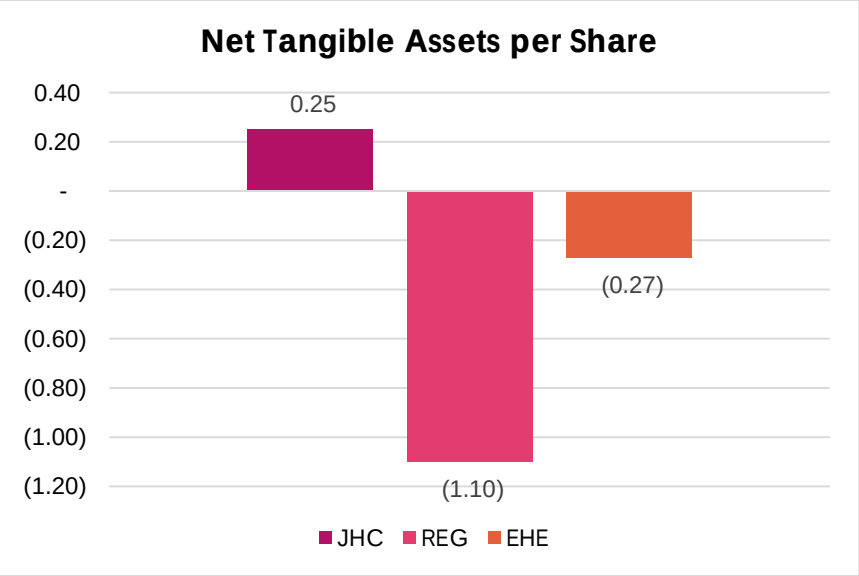
Around 62% of the places were for new aged care services with the remainder being allocated to existing services to extend their facilities or complete allocations for facilities under construction.

Variances in performance across State lines

With the recent release by ACFA of their report on *Financial Issues Affecting Rural and Remote Aged Care Providers* there has been considerable focus on the ability of aged care providers outside of the major centres to remain viable.

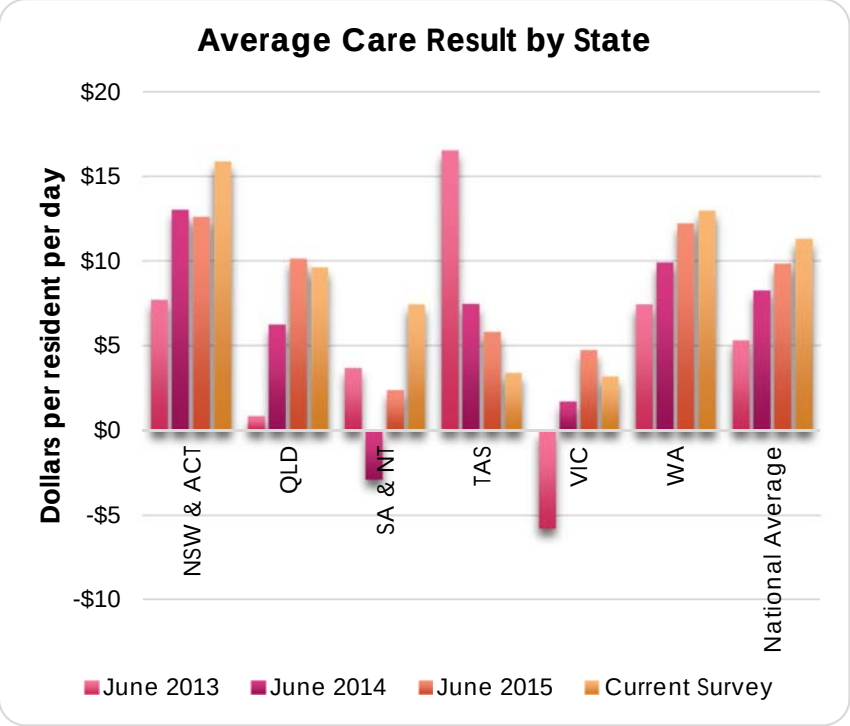
However, Figure 12 shows that there are differences in performance across the State boundaries as well. Given that the funding system is the same nationally and many of the wage agreements are now based on federal fair work awards, it is surprising to see the average results in facilities vary so significantly across a number of the states.

Figure 11 – Comparison of isted entities net tangible assets per share



The average care results of facilities in Western Australia have been trending in line with the survey average as a whole for some time. The average care results in New South Wales and South Australia are in line with trends in the current financial year. In total contrast, the average care results for facilities in Tasmania have been trending downward for some time and continue to do so. The Victorian facilities' average care results in the survey had been trending upwards but have now seen their results decline from last year for the second consecutive survey period. The average results for facilities in Queensland have also declined slightly this year.

Figure 12 – Care result (averages by State)



It is difficult to pinpoint any one particular reason for this. Indeed it would be surprising if it was due to any one particular reason. There are different regimes regarding work-cover resulting in different costs for providers, there are different energy costs across the States and there are likely to be costs attributable to freight on consumables that will affect providers in some States. We will be looking into this in greater detail and drilling down on the data during the course of this year to bring some further insight as to why these variances might be occurring.

Occupancy

Occupancy levels have continued to track at around **95%** (Figure 13) which is slightly lower than the peak prior to the start of the reforms in 2014 but similar to the levels in the years leading into those reforms.

Size as a factor

One of the questions most often asked is "what is the perfect size for an aged care facility?" The answer is not black and white. Certainly the data illustrated in Figure 14 would indicate that a facility with 40 to 60 beds is consistently more profitable on average than facilities of a different size. In addition when the data is sorted within each size group to assess the top Quartile by financial performance the highest average profit is in the group of facilities with between 40 and 60 places.

However, like many of these things it not as straight forward as that. Many of the surveyed facilities with 40-60 places are also in Band 4 which is the most profitable Band – mainly as a result of their resident mix and staffing models and these facilities were traditionally hostels which were generally smaller facilities.

Figure 13 – Average Occupancy across all facilities in survey

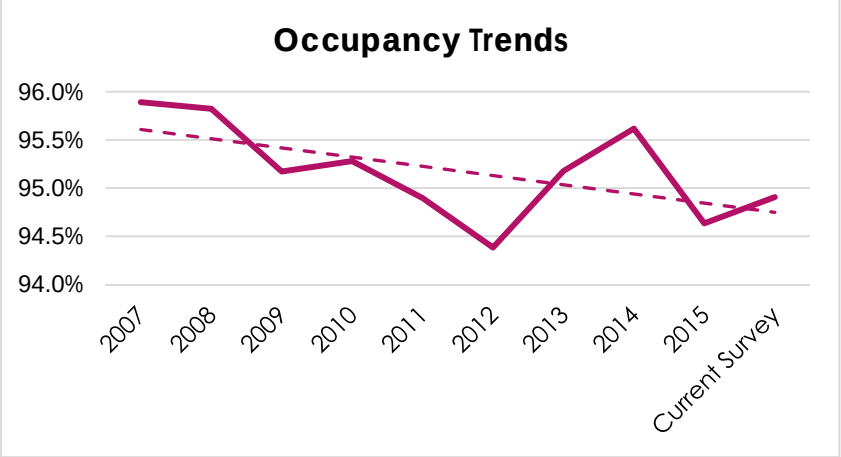
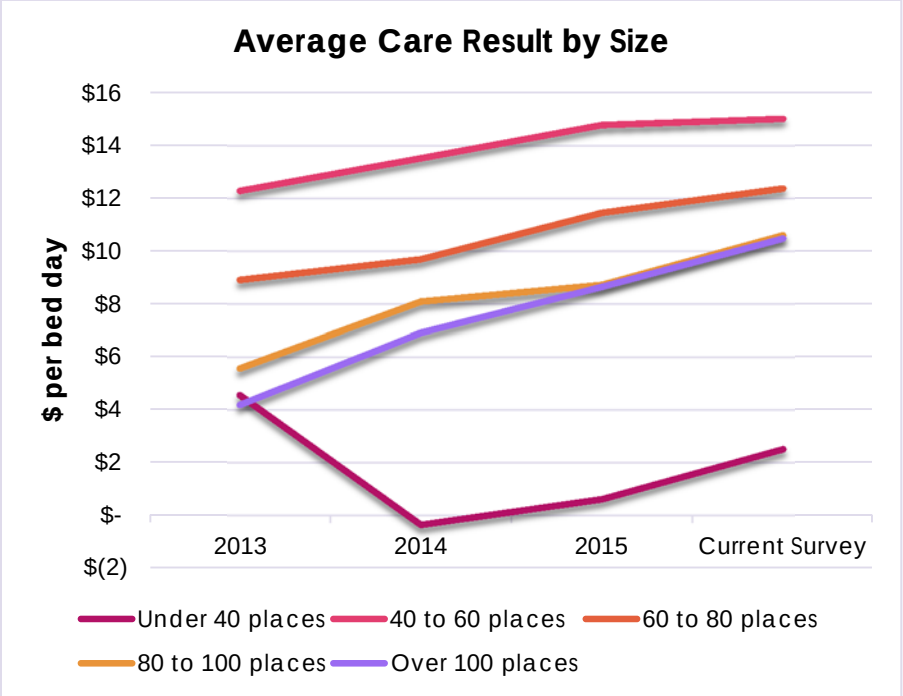


Figure 14 – Trends of care result based on size of facility - 2013 to current survey



The other factor that is important is the ability to maintain a high occupancy. If you were to construct a 100 bed facility in an outer regional area it may not be able to maintain a very high occupancy because demand for the services are unlikely to require a facility of that size. A smaller facility will be more suitable – and more profitable in that situation.

Over the last two years, larger facilities are becoming more common and are starting to bridge the gap. These large facilities are generally situated in areas of high demand and their managers are getting better at managing them and adapting their staffing models to better suit the larger facility.

It is also likely that over time, the use of technology will allow managers to gain further efficiencies within all facilities but it is likely to be amplified in a larger

facility. As all facilities move towards meeting higher average care needs, the ability of a larger facility to spread the administrative, support and hotel services costs over a larger number of residents will see these larger facilities become more profitable on average. So what is the best size facility? The jury is still out on that question.

Staff hours

The future of the aged care sector workforce is crucial to the ability of providers to cater for the needs of current and future older Australians. The Australian Senate Community Affairs References Committee is currently conducting an inquiry into the future of the workforce in the aged care sector and is due to report on 30 June 2016.

As a result of this inquiry, and others currently being held in NSW in relation to registered nurses in aged care facilities, the subject of nurses and hours of direct care time have been somewhat topical in recent months.

What does our data tell us?

The number of registered nursing hours as a proportion of total hours have been increasing. Total care hours are increasing but we have also seen margins being squeezed so providers are changing the mix of the staff to minimise overall cost while maintaining adequate care for the residents.

We have been observing an **increase** in overall hours worked, both in respect of the survey average but also in individual bands. Figure 16 shows the average hours worked per resident per day for the average across all facilities as well as for Band 1, which are the facilities with the highest ACFI subsidies.

Figure 15 – Average facility result for Top 25% of facilities based on size of facility

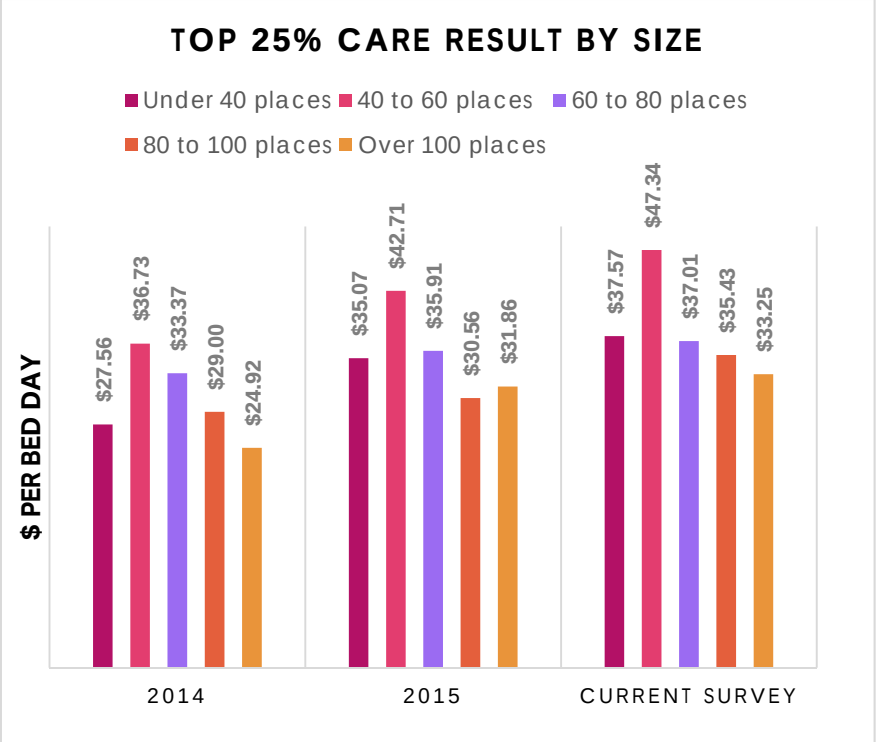
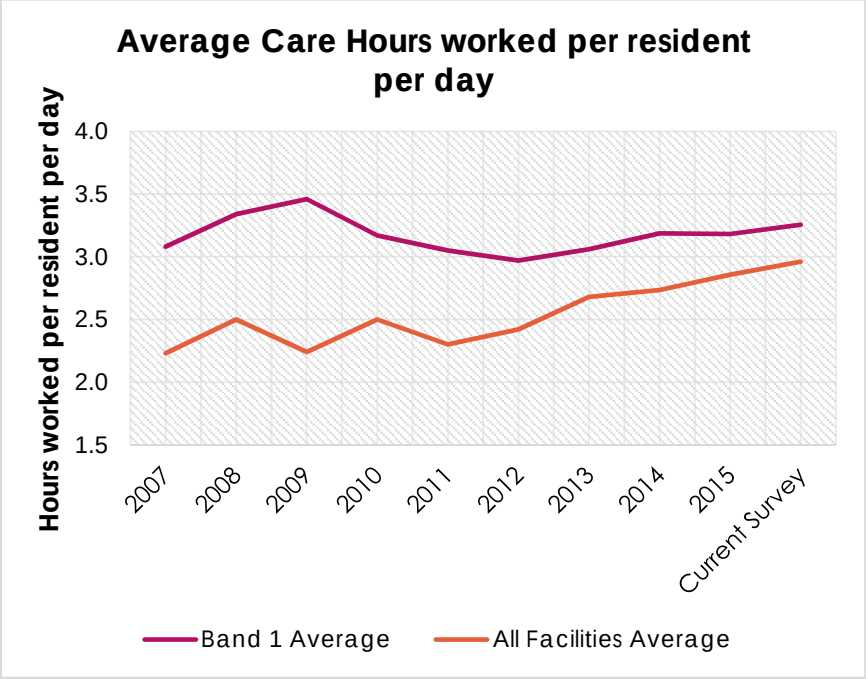


Figure 16 – Average care hours worked per resident per day for survey average and benchmark Band 1



In both cases the average hours worked per resident per day have been on an upward trend for a number of years, including the period in which subsidy rates were frozen. This means that despite a freeze on income rates, and in the face of increasing wage rates, providers, on average, increased the number of direct care hours worked per resident per day and continue to do so.

It is important to examine staff hours data in detail rather than look at the head line statistic of "reduction in care hours" to see the real story.

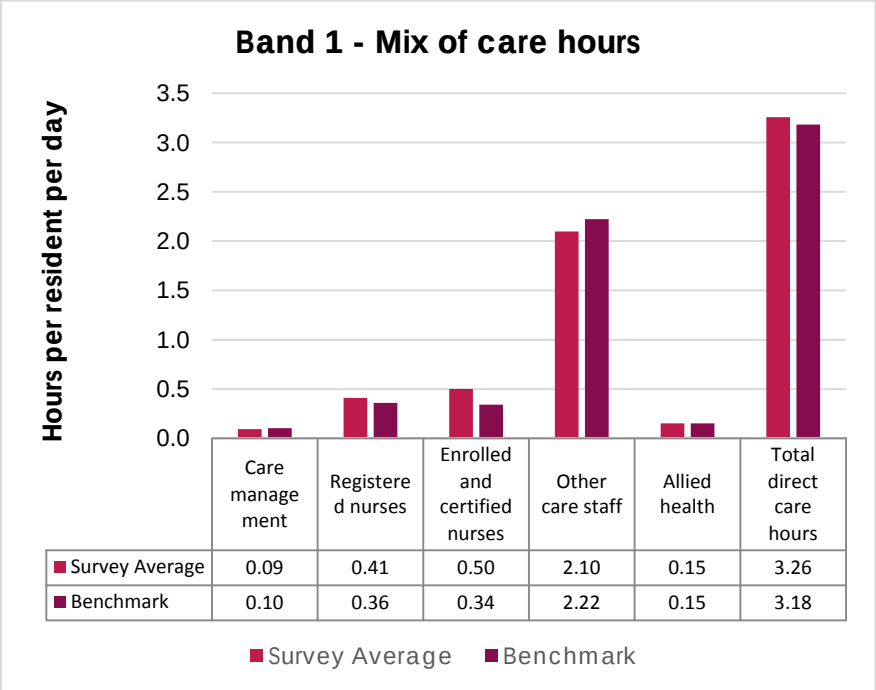
The number of hours worked by other care staff compared to registered nurses has been increasing due to the change in staff mix to accommodate the pressure on costs.

We have noted in the past that the total care hours worked by those facilities in the top quartile are less on average than the survey average. But we should not draw any major conclusions about that in relation to the standard of care being provided. Instead we can drill down a little further.

Figure 17 shows the care hours worked per resident per day in a facility with average care income greater than $220 per day (ACFI income averaging greater than $173 per resident per day). The survey average for total direct care hours worked per resident per day across the 261 facilities in Band 1 was 3.26 hours. The average for the facilities in the top quartile of Band 1 (Benchmark) was 3.18 hours, a difference of 0.08 hours per resident per day. That equates to 5 minutes per resident per day. That type of saving can often be achieved through rostering and other efficiencies. However let's drill down further.

The difference in hours worked by a registered nurse was just 3 minutes per resident per day. For enrolled and certified nurses it was 9.6 minutes per resident per day. In respect of care management and allied health staff the hours are almost identical. Other care hours provided by the benchmark group is on average 8 minutes more per resident per day than the survey average so by slightly reducing the number of hours of the more costly staff, there are additional hours able to be provided by less expensive staff. It is important to examine staff hours data in detail rather than look at the head line statistic of "reduction in care hours" to see the real story.

Figure 17 – Average mix of care hours worked per resident per day for Band 1



	Care management	Registered nurses	Enrolled and certified nurses	Other care staff	Allied health	Total direct care hours
Survey Average	0.09	0.41	0.50	2.10	0.15	3.26
Benchmark	0.10	0.36	0.34	2.22	0.15	3.18

Accommodation Analytics

For the first time in our survey we have been able to provide our participants with some new accommodation pricing analytics.

Using published accommodation price data sourced from the My Aged Care website and property market price data supplied by Core Logic – RP Data we are now able to provide participants in our survey with some up-to-date accommodation pricing analysis.

The reports provided to all participants include a comparison of their published accommodation prices to:

- ✓ Published accommodation prices of other aged care facilities within their local area
- ✓ Median house and unit prices within their local area

This gives management and Boards an up-to-date and easily accessible reference point to assess how their facility's accommodation prices positions them in the local marketplace.

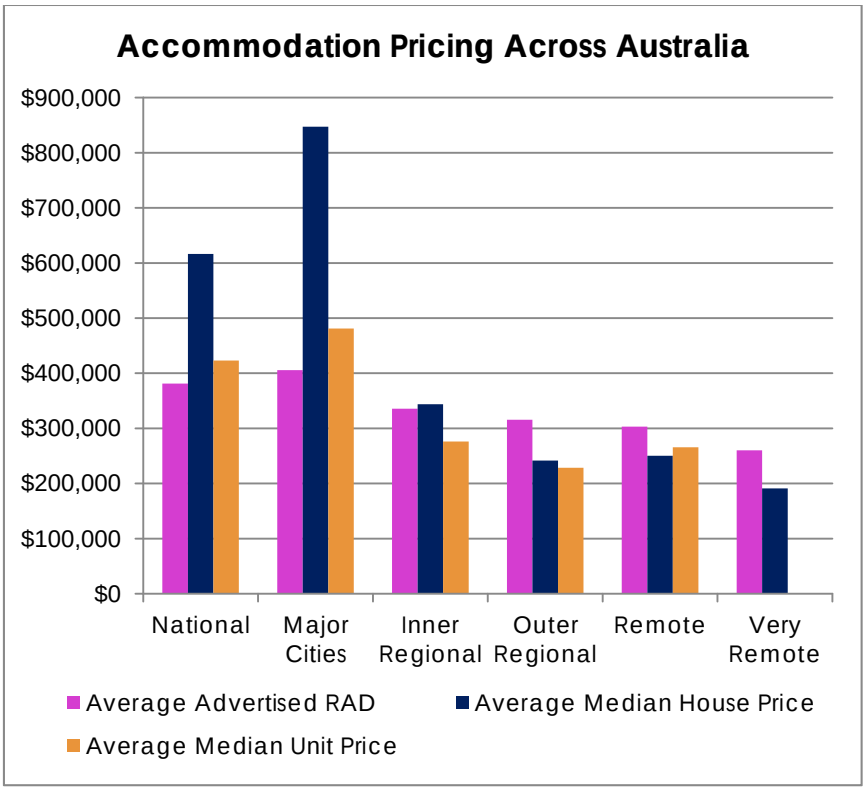
This data also allows us to conduct an analysis of accommodation prices on a broad scale but also to do the same at a much more granular level.

One of the by-products of conducting this analysis is that we have discovered that there are significant number of aged care facilities that are not appearing on the My Aged Care web site. While this is of a concern from a marketing point of view, it also means that the aged care provider may not be complying with the *Aged Care Act 1997* in relation to publishing its facility accommodation prices and key features. It appears that some of these issues occurred after changes to the My Aged Care Website occurred in July 2015. **We recommend that all Providers regularly check that their facility is appearing on the My Aged Care website and that all of the required information appears in relation to each of their facilities.**

We have observed for some time that the accommodation prices of facilities in major cities have generally been well below median house and unit prices and this continues to be the case.

In contrast providers in regional areas are setting prices much closer to median property prices, in many cases by necessity rather than by choice. It is a means of obtaining sufficient accommodation income in order to remain sustainable as well as to adequately recover the cost of construction of the facility.

Figure 18 – Comparison of average published accommodation prices with median house and unit prices sorted by ABS remoteness



As shown in figure 18, in the major cities there is a significant gap between the average accommodation price and the median house price. However, outside of the major cities, the accommodation prices are set at, or above median house prices. In fact the more remote the facility, the higher the accommodation price is likely to be above the median house price.

We believe that, particularly in the major cities, there is likely to be some room for providers to increase their accommodation prices. Of course this will also depend on the standard of accommodation and the price behaviour of competitors.

There also appears to be differences between States both in relation to where accommodation prices are being set but also the relativity of those prices to residential property prices as illustrated in Figure 19.

In Victoria for example the average accommodation price at $423,149 is higher than the prices of the other States with only the average price in the ACT ($482,444) exceeding it. Those prices are also closer in real terms to the median house prices than in NSW - where the average median house prices across those suburbs in which aged care facilities are located are almost $820,000 yet the average published RAD price is just over $380,000.

There also appears to be subtle differences in pricing behaviour between for-profit and not-for-profit providers as shown in Figure 20. Nationally, the average RAD prices of the For-Profit sector are higher than the combined Not-for-profit (NFP) and Government sectors. This reverses the original position of the NFP sector setting their prices at higher levels than the for-profit sector. It may be a sign that the for-profit sector has been more likely to adjust their accommodation prices since published prices were instituted.

Accommodation pricing is going to be an increasingly important area for providers to manage. The tools that we can now give providers access to in relation to accommodation pricing should assist them in maximising the benefit of the new pricing regime while maintaining their competitiveness.

IN SUMMARY

The takeaway messages for Residential Care from the December 2015 survey are:

- **It has been "business as usual" during the six months to December 2015**
- **The increasing focus on caring for residents with high care needs has continued**
- **We believe there is room for improvement of financial performance across large parts of the sector but there is no "one-size-fits-all" approach to achieving those improvements**
- **The performance gap between the top quartile and the bottom quartile is widening and the poorer performing facilities need to address this. We are not suggesting that they should achieve the same results as those in the top quartile but they need to be sustainable.**
- **Outer regional and remote providers face financial and other difficulties**
- **Demand will continue to increase with additional beds and staff required in the future. Increased competition for staff is likely with an additional emphasis being placed on language skills**

Figure 19 – Comparison of accommodation prices to median house and unit prices sorted by State and Territory

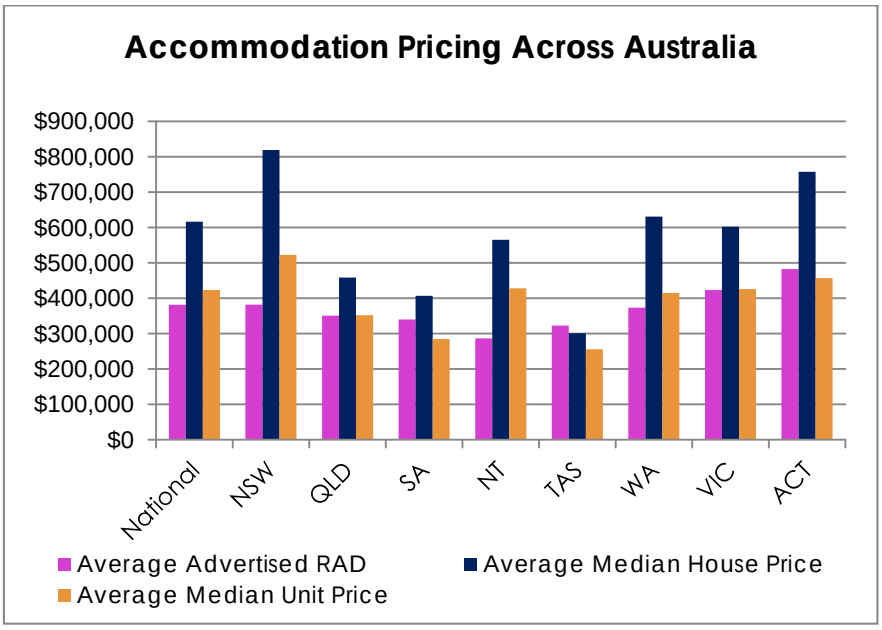
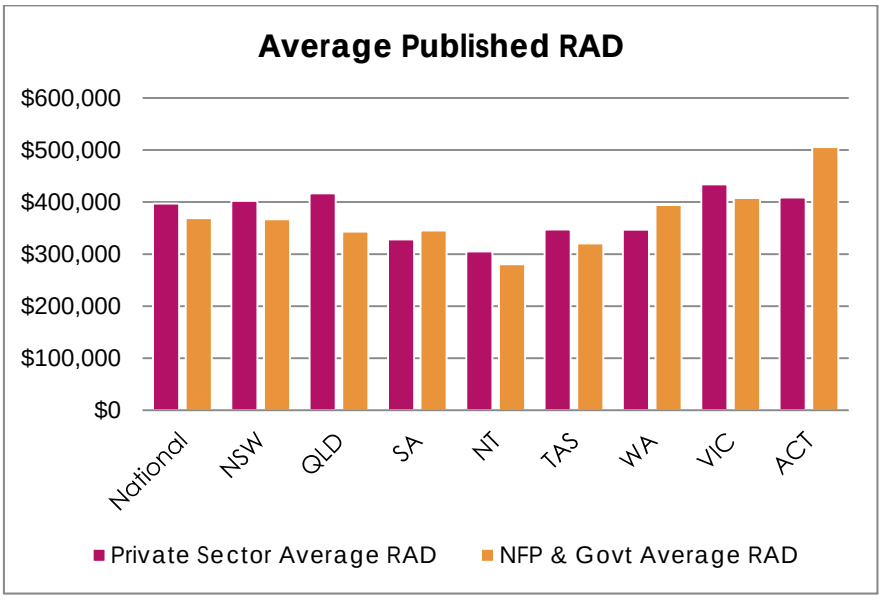


Figure 20 – Comparison of accommodation prices by state and by ownership type



2015 ACAR Results

The big ACAR winners this year has been the for-profit providers. The competition for places was extremely high with applications made for **38,859 places** and only **10,940 being allocated**, including 1,033 places to new providers.

The not-for profit sector was awarded around **3,000 places** and the allocations were generally spread across a larger number of providers. In contrast the for-profit sector was awarded close to **7,000 places** and these were spread across fewer providers meaning the allocations to individual for profit providers were generally larger.

As can be seen in Figures 21 and 22, the allocations have been biased to the larger for-profit providers rather than the not-for-profit sector. This is a continuation of the allocations from the 2014 ACAR.

In total, some 73 not-for-profit providers were allocated 2,977 new residential places, with 10 providers allocated more than 100 places, an analysis by the Ideal Consultancy found. In contrast, 50 for-profit providers were awarded 6,740 places, with 15 providers allocated more than 100 places. Three for-profit providers were allocated more than 500 places.

When looking at the last two ACARs combined, the top 8 for-profit providers were allocated a total of 7,168 operational places. This growth comes on top of an aggressive program of acquisitions by some of the same providers.

This is starting to see a significant change in the mix in the for profit and not-for-profit sectors – one which appears to be happening partly as a result of government policy.

Figure 21 – Allocations of residential aged care places – Top 15 providers

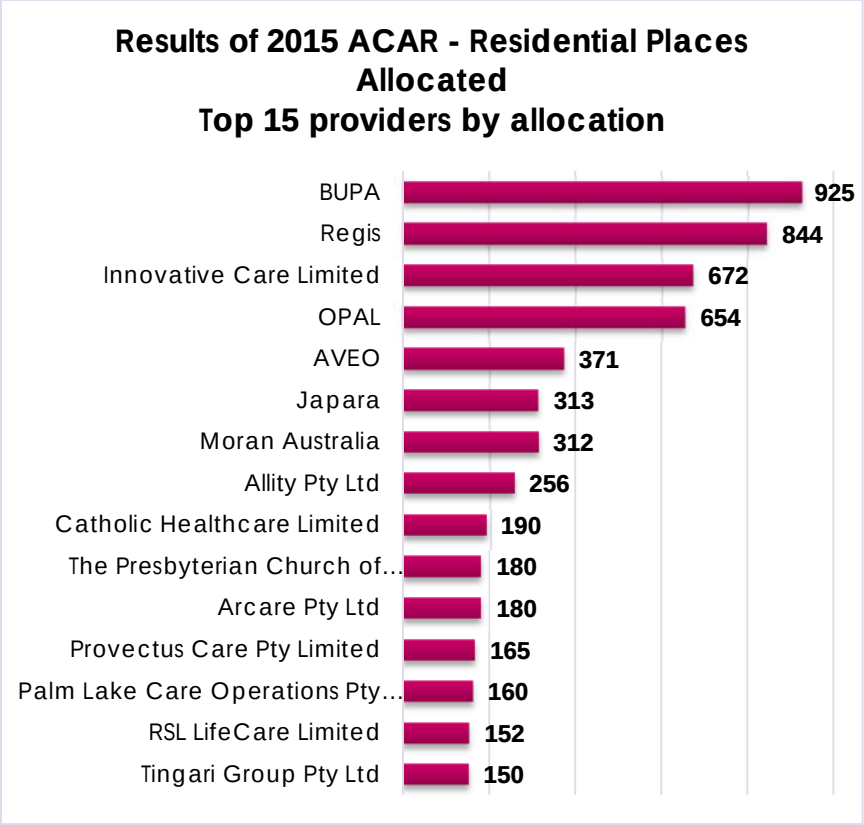
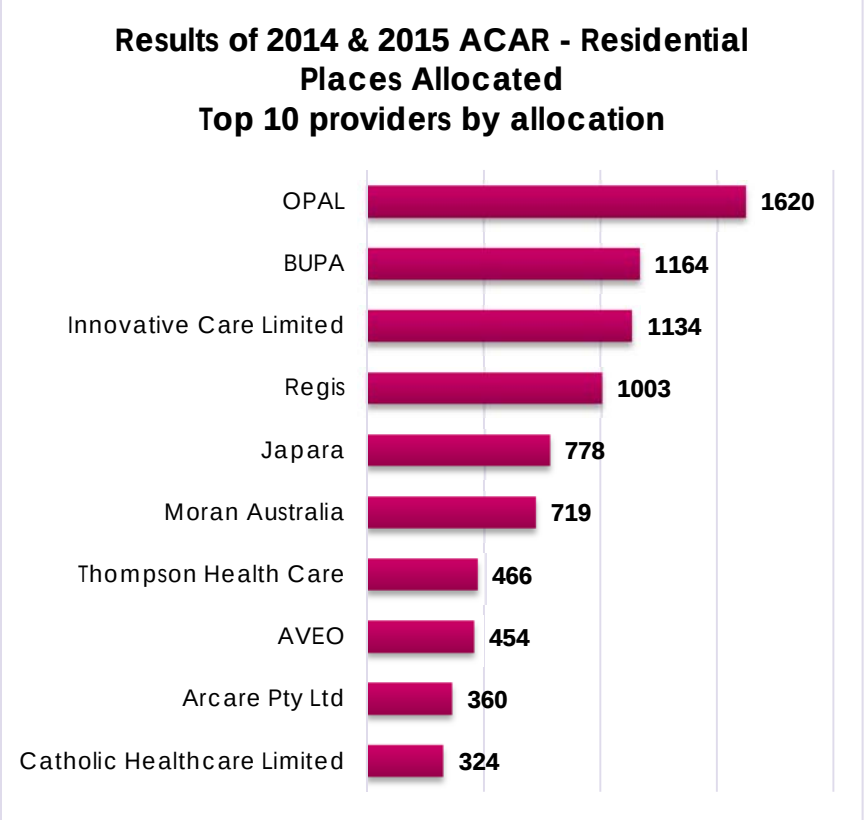


Figure 22 – Combined allocations for 2014 & 2015 ACAR – Top 10 Providers



FACILITY REPORT FOR PERIOD ENDED 31 DECEMBER 2015

2016 SAMPLE FACILITY REPORT

	2016 Sample Facility Report Band 2 (120 Places) $ pbd	Results of 1st Quartile Band 2 (52 Facilities) $ pbd	Results of 2nd Quartile Band 2 (52 Facilities) $ pbd	Average by Line Item Band 2 (104 Facilities) $ pbd	Overall Average Band 2 (207 Facilities) $ pbd
CARE					
INCOME					
RESIDENTS					
Resident fees - care	47.32	50.11	50.35	50.67	50.67
Extra service fees	-	0.70	0.29	3.31	0.37
Income - residents	47.32	50.81	50.64		51.04
GOVERNMENT					
Government subsidies - care	157.87	163.44	159.91	161.08	161.08
Grants - not capital	-	0.01	0.00	0.24	0.02
Income - government	157.87	163.44	159.91		161.10
TOTAL CARE INCOME	205.20	214.25	210.55		212.15
EXPENDITURE					
CARE SERVICES					
Labour costs					
Care management	0.57	5.73	7.45	6.55	6.09
Registered nurses	19.26	15.48	19.06	19.16	18.64
Enrolled and certified nurses	6.70	7.57	13.77	15.97	12.39
Other nurses	88.80	66.87	65.88	72.04	71.68
Allied health	-	5.46	5.57	6.41	5.72
Agency staff	2.49	1.79	3.13	5.08	3.31
Total labour costs	117.83	102.90	114.86		117.83
Medical & incontinence supplies	1.86	2.74	3.20	3.36	3.35
Chaplaincy	0.77	0.40	0.39	0.96	0.41
Other resident care	5.42	1.71	1.70	2.48	2.27
Expenditure - care services	125.89	107.76	120.15		123.86
Care costs as a % of care income	61.4%	50.3%	57.1%		58.4%
HOTEL SERVICES					
CATERING					
Labour costs	13.10	12.57	14.60	15.96	14.70
Consumables	4.17	7.94	8.44	8.47	8.12
Contract catering	9.74	5.21	3.26	12.96	4.44
Income from sale of meals	(0.03)	(0.14)	(0.14)	(0.32)	(0.21)
Total catering	26.98	25.58	26.16		27.06
CLEANING					
Labour costs	3.69	3.89	4.90	5.90	4.66
Consumables	1.19	1.44	1.34	1.45	1.42
Contract cleaning	0.01	1.06	1.05	1.92	1.18
Total cleaning	4.89	6.39	7.29		7.25
LAUNDRY					
Labour costs	1.79	2.05	2.10	2.46	1.98
Consumables	0.13	0.42	0.57	0.53	0.47
Contract laundry	2.07	1.04	0.74	2.00	1.14
Total laundry	3.99	3.51	3.41		3.59
Expenditure - hotel services	35.85	35.49	36.86		37.90
UTILITIES					
Electricity	3.11	3.01	3.05	3.15	3.15
Gas	0.45	0.98	0.75	0.93	0.83
Rates	0.76	1.34	1.07	1.32	1.32
Rubbish removal	0.38	0.75	0.62	0.70	0.69
Total utilities	4.70	6.09	5.49		5.99
ADMINISTRATION AND SUPPORT SERVICES					
Administration recharges	23.53	15.06	15.77	19.57	17.47
Labour costs - administration	9.88	4.54	5.23	5.96	5.89
Other administration costs	1.62	3.49	3.79	4.01	4.01
Workers' compensation	2.34	2.72	4.02	3.81	3.77
Quality & education - labour costs	1.19	0.48	0.78	1.47	0.80
Quality & education - other	0.05	0.45	0.45	0.53	0.45
Insurances	1.05	0.76	0.67	0.89	0.80
Expenditure - other services	39.66	27.49	30.73		33.19
TOTAL EXPENDITURE	206.10	176.82	193.23		200.94
CARE RESULT	**$ (0.90)**	**$ 37.43**	**$ 17.33**		**$ 11.21**

FACILITY REPORT FOR PERIOD ENDED 31 DECEMBER 2015

2016 SAMPLE FACILITY REPORT

	2016 Sample Facility Report *Band 2* *(120 Places)* *$ pbd*	Results of 1st Quartile *Band 2* *(52 Facilities)* *$ pbd*	Results of 2nd Quartile *Band 2* *(52 Facilities)* *$ pbd*	Average by Line Item *Band 2* *(104 Facilities)* *$ pbd*	Overall Average *Band 2* *(207 Facilities)* *$ pbd*
ACCOMMODATION					
INCOME					
Residents					
Accommodation charges	7.18	3.77	5.20	5.41	5.13
Daily accommodation payments	4.41	4.34	4.52	4.82	4.43
Bond - retentions	1.09	2.28	1.82	1.85	1.77
Bond/RAD - interest income	4.82	1.95	0.78	2.01	1.48
Income - residents	17.49	12.34	12.31		12.81
Government					
Government supplements - accom.	-	10.46	12.45	12.75	12.08
Significant refurbishment supplement	27.29	1.62	0.45	18.18	1.94
Income - government	27.29	12.08	12.90		14.02
TOTAL ACCOMMODATION INCOME	44.78	24.42	25.21		26.83
EXPENDITURE					
Labour costs - maintenance	2.88	2.25	2.07	3.20	2.48
Repairs & maintenance	6.53	7.23	7.61	6.89	6.89
Motor vehicle expenses	0.17	0.32	0.26	0.34	0.31
Depreciation - building	17.09	9.05	9.95	10.90	9.85
Depreciation - non building	18.27	4.50	3.84	4.51	4.35
Property rental	-	1.02	0.50	4.81	0.74
Refurbishment	-	0.71	0.43	1.31	0.40
Bond/RAD interest expense	0.05	1.05	0.65	1.08	0.81
Expenditure - accommodation	45.00	26.13	25.31		25.83
ACCOMMODATION RESULT	**$ (0.21)**	**$ (1.71)**	**$ (0.10)**		**$ 1.00**
PROVIDER					
INCOME					
Donations, bequests & fundraising	-	0.08	0.32	0.50	0.24
Grants - capital	-	-	0.20	2.48	0.06
Investment income - interest	-	1.30	2.20	5.14	1.44
Investment income - other	-	0.06	0.00	1.23	0.04
Sundry income	0.81	0.35	0.56	0.66	0.55
Income - provider	0.81	1.79	3.27		2.33
EXPENDITURE					
Impairment	-	-	-	(0.13)	(0.00)
Interest expense - other	-	0.38	0.16	3.12	0.35
Other provider expenses	-	0.37	0.78	1.56	0.52
Expenditure - provider	-	0.75	0.94		0.87
PROVIDER RESULT	**$ 0.81**	**$ 1.04**	**$ 2.33**		**$ 1.46**
TOTAL RESULT FOR THE PERIOD	**$ (0.30)**	**$ 36.76**	**$ 19.56**		**$ 13.67**

Column Definitions

Column 1 - Facility Report	**the result for this facility**
Column 2 - Results of 1st Quartile	**the Benchmark Top 25% or the average of the top 25% of facilities in this band**
Column 3 - Results of 2nd Quartile	**the average of the second 25% of facilities in this band**
Average by Line Item	**the average of facilities that supplied data for the line item for this band**
Overall Average	**the average across all facilities in this band**

STEWARTBROWN AGED CARE FINANCIAL PERFORMANCE SURVEY

FACILITY REPORT FOR PERIOD ENDED 31 DECEMBER 2015

2016 SAMPLE FACILITY REPORT

	2016 Sample Facility Report *Band 2* *(120 Places)*	Results of 1st Quartile *Band 2* *(52 Facilities)*	Results of 2nd Quartile *Band 2* *(52 Facilities)*	Average by Line Item *Band 2* *(104 Facilities)*	Overall Average *Band 2* *(207 Facilities)*
REPORT CARD					
Profile Data					
Number of places	120	3,950	4,363	16,544	16,544
Number of occupied days	21,860	701,072	774,505	2,895,698	2,895,698
Occupancy rate	99.00%	96.46%	96.48%	95.13%	95.13%
Ranking	139	-	-	-	-
Summary of Results					
Care Income					
Resident	47.32	50.81	50.64		51.04
Government	157.87	163.44	159.91		161.10
Total care income	205.20	214.25	210.55		212.15
Care Expenditure					
Care services	125.89	107.76	120.15		123.86
Hotel services	35.85	35.49	36.86		37.90
Utilities	4.70	6.09	5.49		5.99
Other services	39.66	27.49	30.73		33.19
Total care expenditure	206.10	176.82	193.23		200.94
Care result	**$ (0.90)**	**$ 37.43**	**$ 17.33**		**$ 11.21**
Accommodation Income	44.78	24.42	25.21		26.83
Accommodation Expenditure	45.00	26.13	25.31		25.83
Accommodation result	**$ (0.21)**	**$ (1.71)**	**$ (0.10)**		**$ 1.00**
Provider income	0.81	1.79	3.27		2.33
Provider expenditure	-	0.75	0.94		0.87
Provider result	**$ 0.81**	**$ 1.04**	**$ 2.33**		**$ 1.46**
Result for the period	**$ (0.30)**	**$ 36.76**	**$ 19.56**		**$ 13.67**
EBITDA	$ 35.07	$ 49.39	$ 31.31		$ 26.77
FACILITY EBITDA	$ 34.25	$ 49.27	$ 31.02		$ 26.40
EBITDA PER BED PER ANNUM	$ 12,672	$ 17,389	$ 11,025		$ 9,294
FACILITY EBITDA PER BED PER ANNUM	$ 12,378	$ 17,345	$ 10,923		$ 9,166
Staff Hours Analysis					
Hours worked per resident per day					
Care Management	0.02	0.10	0.10	0.10	0.09
Registered nurses	0.43	0.29	0.36	0.38	0.36
Enrolled and certified nurses	0.19	0.19	0.40	0.46	0.36
Other nursing	2.00	2.05	1.90	2.04	1.99
Therapy	-	0.08	0.11	0.17	0.10
Total Care Hours	2.63	2.71	2.87		2.90
Hotel services	0.58	0.52	0.66	0.75	0.66
Maintenance	0.08	0.07	0.07	0.10	0.08
Administration	0.16	0.14	0.15	0.18	0.16
Quality and Education	0.01	0.01	0.02	0.05	0.02
Total Hours	3.47	3.45	3.77		3.81
KPIs					
Expenses as % of Care income					
Care Services	61.4%	50.3%	57.1%		58.4%
Hotel Services	17.5%	16.6%	17.5%		17.9%
Utilities	2.3%	2.8%	2.6%		2.8%
Other Services	19.3%	12.8%	14.6%		15.6%
	100.4%	82.5%	91.8%		94.7%
Wages as % of Care income					
Care Services	57.4%	48.0%	54.6%		55.5%
Hotel Services	9.1%	8.6%	10.3%		10.1%
Other Services	5.4%	2.3%	2.9%		3.2%
	71.9%	59.0%	67.7%		68.8%
Total staff costs	150.35	128.69	144.54		148.34
Workers compensation expense as % of wages	1.6%	2.1%	2.8%		2.5%

FACILITY REPORT FOR PERIOD ENDED 31 DECEMBER 2015

2016 SAMPLE FACILITY REPORT

	2016 Sample Facility Report *Band 2* *(120 Places)* *$ pbd*	Results of 1st Quartile *Band 2* *(52 Facilities)* *$ pbd*	Results of 2nd Quartile *Band 2* *(52 Facilities)* *$ pbd*	Average by Line Item *Band 2* *(104 Facilities)* *$ pbd*	Overall Average *Band 2* *(207 Facilities)* *$ pbd*
ACCOMMODATION ANALYTICS					
Accommodation income					
Resident	17.49	12.34	12.31		12.81
Government	27.29	12.08	12.90		14.02
Total income	44.78	24.42	25.21		26.83
Imputed DAP (based on refundable deposit holdings)	16.14	23.91	17.68	17.72	17.72
Benchmark Accommodation income	**$ 60.92**	$ 48.33	$ 42.89		$ 44.55
Accommodation Expenditure					
Maintenance	9.58	9.80	9.94		9.69
Depreciation	35.36	13.55	13.79		14.19
Rent	-	1.02	0.50		0.74
Refurbishment	-	0.71	0.43		0.40
Other	0.05	1.05	0.65		0.81
Total expenditure	45.00	26.13	25.31		25.83
Benchmark Accommodation result	15.93	22.20	17.58		18.72
Significant Refurbishment					
Uplift in accommodation income attributable to significant refurbishment	**$ 2.31**				
Current MPIR	6.15%				
Supported resident ratio	46%				
Accommodation Pricing					
Published accommodation prices of facility					
Low	550,000				
High	550,000				
Median	550,000				
Published accommodation prices of nearby facilities					
Low	150,000				
High	550,000				
Median	335,000				
Number of Competitors included in analysis	10				
Radius of Competition analysis	10.00Km				
Market Data					
Suburb: Brisbane					
Median House price	621,000				
Median Unit Price	490,000				
Post Code: 4000					
Median House price	700,000				
Median Unit Price	468,000				
Accommodation Payment Analysis					
Number of RADs/RACs & bonds at reporting date	41	1,783	1,782	6,394	6,394
Average RAD/RAC & bond value at reporting date	296,436	273,690	239,253	245,575	245,575
Number of RADs/RACs taken (this financial year)	4	196	291	994	994
Average RAD/RAC taken (this financial year)	540,833	306,106	279,099	289,175	289,175
Number of full DAP/DAC clients at reporting date	5	226	324	1,086	1,086
Number of combination DAP/DAC clients at reporting date	2	169	216	789	789

Note: Accommodation pricing is as published on the My Aged Care website as at the end of current survey period

Market Data listed supplied by CoreLogic RP Data as at the end of the current survey period

CoreLogic RP Data

HOME CARE - COMMENTARY

Home Care (HCP) providers continue the path of reform with amendments to the *Aged Care Act 1997* passed on 3 March 2016 by the Australian Senate. One of the key areas dealt with is how Unspent Funds will be treated in the case of a care recipient moving to another provider or a care recipient's package being terminated.

We will assess the implications of all the amendments in more detail later in this report as they are likely to have some short term consequences for providers, particularly given the level of unspent funds currently being reported by providers.

But the challenges for providers are not just attributable to what will happen in the future. There are quite a few issues that providers are dealing with in the here and now:

…the amendments to the Aged Care Act are likely to have some short term consequences for providers, particularly given the level of unspent funds currently being reported by providers

- the method of accounting for Consumer Directed Care (CDC)
- setting prices and margins
- recovery of fixed overheads
- method of charging for package administration
- changes to business models and
- the "elephant in the room" - unspent funds.

CDC continues to deliver challenges for providers and their systems. It has also provided challenges in providing appropriate benchmarking data to participants.

Benchmarking for CDC

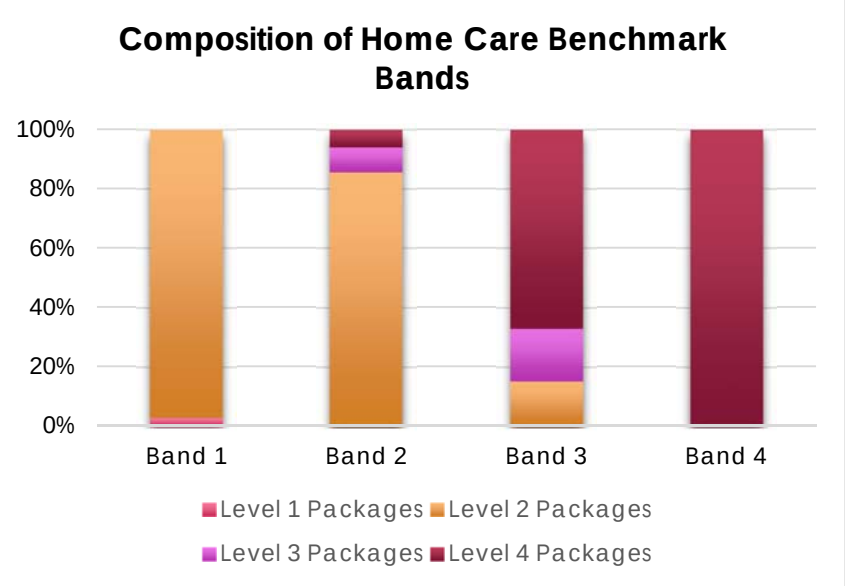
In the September 2015 survey we introduced our new method of benchmarking home care using Income Bands rather than package levels. We also expressed the view that we would need to examine the thresholds used to sort packages into bands over the coming surveys until the data started to mature. Well our predictions held up as we have had to tinker slightly with the thresholds this quarter. The thresholds are set out in Table 3.

Table 3 – Band thresholds used for benchmarking purposes

Benchmark Band	Total Reported Income Six Months to December 2015	Total Reported Income Quarter ended September 2015
Band 1	Under $40	Under $45
Band 2	Between $40 and $75	Between $45 and $85
Band 3	Between $75 and $120	Between $85 and $130
Band 4	Over $120	Over $130

Figure 23 shows that as expected Bands 1 and 2 are predominantly composed of low care packages, with a small number of programs that contain a mixture of package levels but have been entered under the name of a program that may have been previously identified as a level 4 program. Similarly the Bands 3 and 4 are dominated by level 3 and 4 packages with a sprinkling of those programs with mixed package levels but having been entered as a Level 2 program.

Figure 23 – Distribution of packages across benchmark bands



As promised in our September report we have performed some analysis at a package level basis, however the results are not unexpected given the mix of package levels in each of the bands and the results of those bands. These results are summarised in Figure 24.

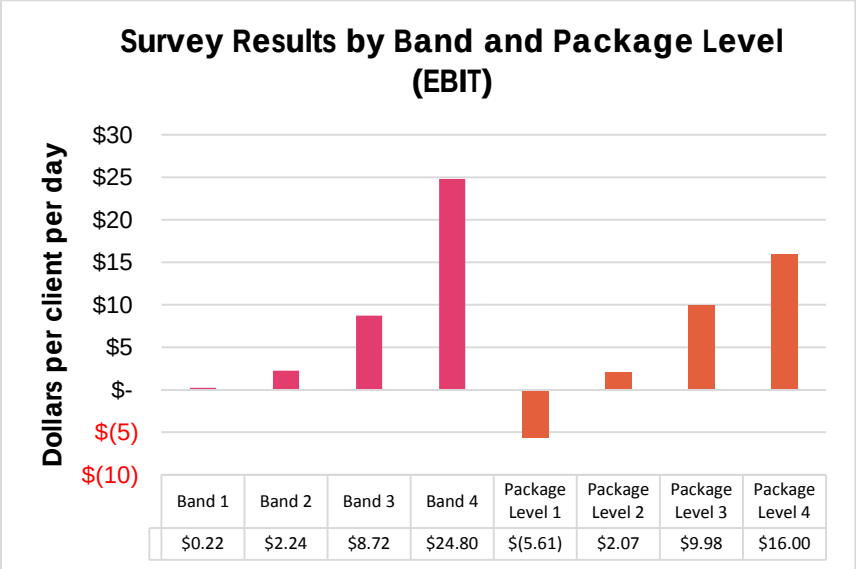
What is clear is that the results of Level 4 packages are very mixed depending on the level of activity being achieved. The results of Band 3 in our benchmarking is influenced by the results of Level 3 packages (lower on average than Level 4 packages) as well as those Level 4 packages that, on average do not achieve a revenue utilisation rate that is as high as those that make it into Band 4.

We will provide some further analysis of the results of packages when sorted by Package level, however it must be said that this type of analysis may be less likely as time goes by as more providers submit data with a mixture of package levels included.

Qualification of results

The September 2015 Quarter was the first time that we had collected this data in this new reporting format and there was bound to be some limitations on the ability of some of the participants to convert old reporting styles to the new way of doing things. For example some participants may have found it challenging to split the reported income into the various income categories. The cost side of the equation should not have been as big a challenge. However, the categorisation of income does affect individual margin analysis so we will be working with providers over coming surveys to ensure more consistency in their data submission. We have spent a lot of time this quarter validating data and chasing missing data, especially in relation to unspent funds. However, after only two surveys using this new format and new methods for accounting for home care packages, it is still difficult to pick trends in the data and some of the observations will be somewhat qualified. To this end we have also used the information gathered from speaking to a large number of providers to assist us to analyse the data and make observations from it. Over time the data set will mature and we will be able to start to report with more authority on trends in the data.

Figure 24 – Comparison of survey average EBIT between data sorted by package level and data sorted by benchmark band

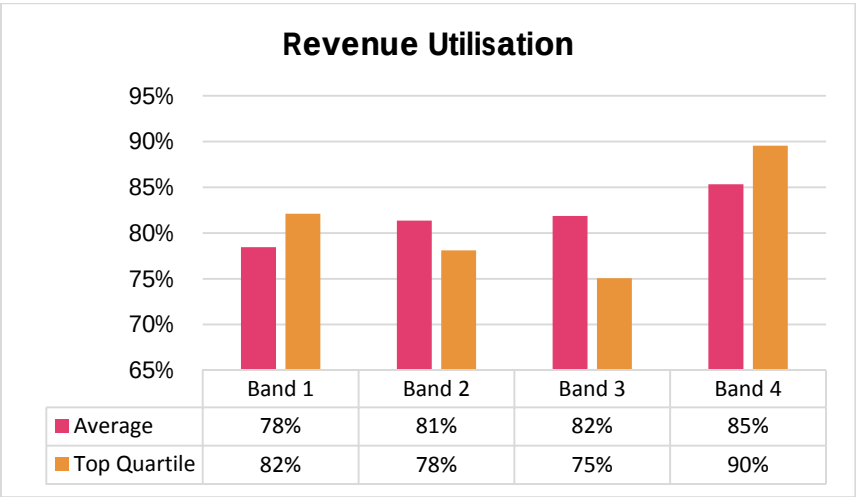


HEADLINE RESULTS

Unspent Funds

One of the first observations that we can make is that there is a **significant build-up of unspent funds** in the system and unless providers take steps to minimise this practice then the balances are only likely to grow. The revenue utilisation rates for the various groups of packages are shown below:

Figure 25 – Revenue utilisation rates



This utilisation rate tells us that for packages in Bands 1 through 3, an average of **20% of available income** is residing in unspent funds in the balance sheet. This means that these funds are not contributing to profit (via a margin) and that providers are somewhat relying on bringing this income to account when the client moves out of the system.

Unfortunately, this is not a sustainable position, particularly given recent amendments to the *Aged Care Act 1997* which will see unspent funds either go with the consumer to another provider or be returned proportionately to the consumer (or consumer's estate) and the government. This will affect all fees and charges received since 1 July 2015 so in some respect this is retrospective legislation.

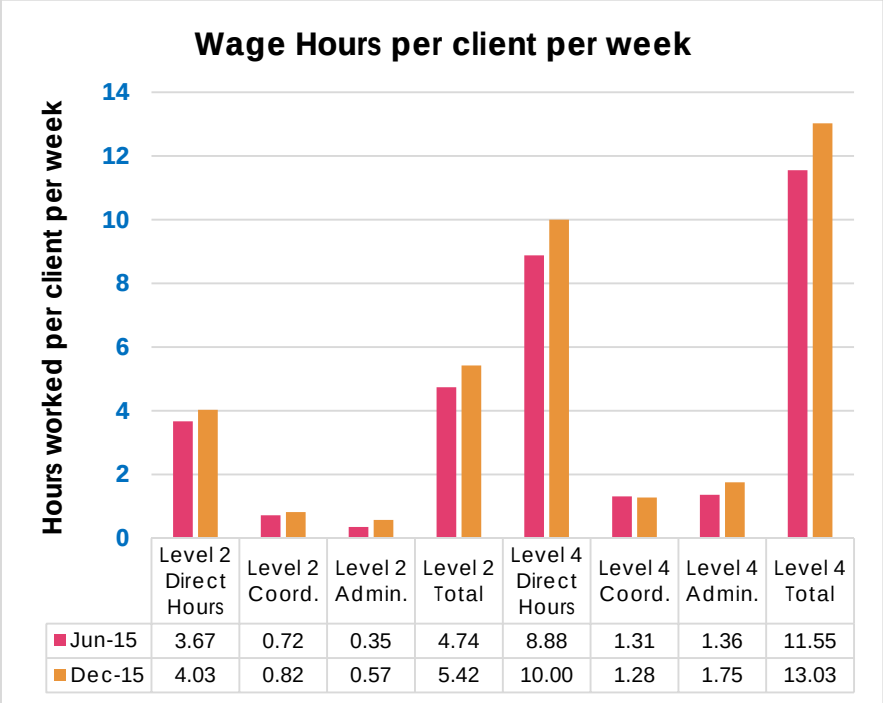
It will become important that unspent fund balances are minimised and that the level of activity and service provided to consumers is maximised.

Recent amendments to the Aged Care Act 1997 will see unspent funds either go with the consumer to another provider or be returned proportionately to the consumer (on consumer's estate) and the government.

What is surprising is that if we measure activity by means of direct hours of service, then the number of hours of service by package level has actually increased, so the client is getting a greater level of service, yet the provider is not utilising the whole of the income available for the package.

The graph below looks at the wage hours per client per week based on the level of package (not benchmark band).

Figure 26 – wages worked per client per week based on package level comparing averages for six months to December 2015 with year ended June 2015



	Level 2 Direct Hours	Level 2 Coord.	Level 2 Admin.	Level 2 Total	Level 4 Direct Hours	Level 4 Coord.	Level 4 Admin.	Level 4 Total
Jun-15	3.67	0.72	0.35	4.74	8.88	1.31	1.36	11.55
Dec-15	4.03	0.82	0.57	5.42	10.00	1.28	1.75	13.03

A word of caution. The mixing of package levels in programs will distort these figures to some degree, but even if we were to say that service providers were giving clients the same level of service and activity as they were six months ago, then you would expect the whole of the package income to be utilised yet we see that 20% of the package income is still to be spent. While this might be attributable to competition, we believe it has more to do with providers not understanding their true costs of operation and having, for the first time, to set "retail" prices for their services.

In our discussions with providers they have indicated to us that consumers wish to put aside a little bit for a "rainy day" and more importantly are choosing services that are not direct care services. These may be some form of brokered or one-off service that does not contribute much, if any, profit to the provider. Providers will need to start putting margins on these brokered services – as we are starting to see happen.

Due to the changes that are coming in February 2017 providers will have to consider their pricing structures and business models so that the services that are being provided contribute sufficient levels of profit to cover the fixed overheads and maximise the use of the package income available while remaining competitive. This is obviously a challenge however as a sector it is one that will have to be met.

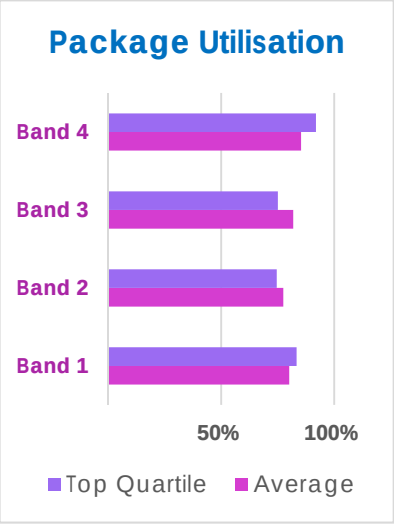
Package Utilisation

This represents the utilisation rate of the package itself, similar to occupancy in a residential aged care facility - it measures subsidised days as a proportion of available days.

The trends that we had seen for some time continue into this new financial year. Low care packages are less utilised than high care packages (Figure 28). The graph shows the utilisation rates for the survey averages both by band and package level.

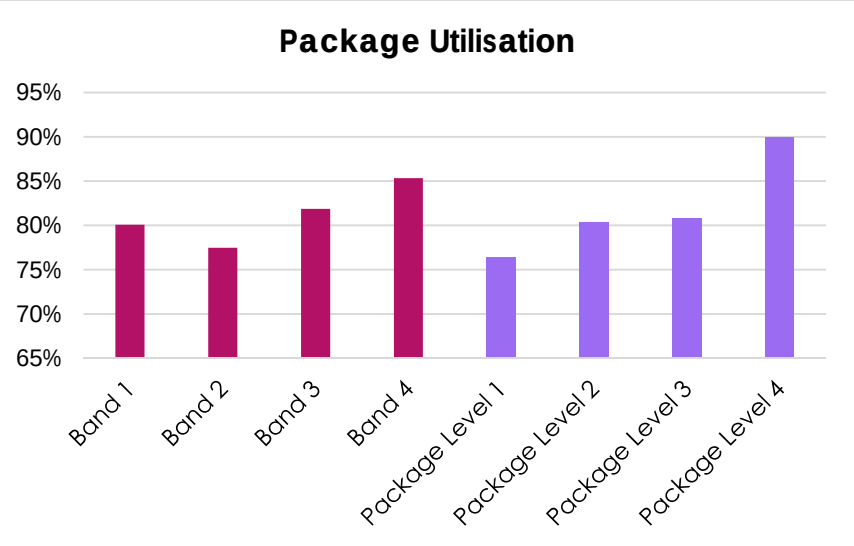
With the exception of high care packages that have an average utilisation rate of 90%, the other package levels are somewhat underutilised at around 80% with Level 1 packages averaging 76% utilisation.

Figure 27 – Package utilisation by benchmark band (six months ended December 2015)



Interestingly, as Figure 27 shows, the top quartile does not necessarily have a higher utilisation rate. Similarly, they did not necessarily have the highest revenue utilisation rate. The top quartile appeared to be far more consistent in the level of margin achieved across the income that is earned.

Figure 28 – Package utilisation rates

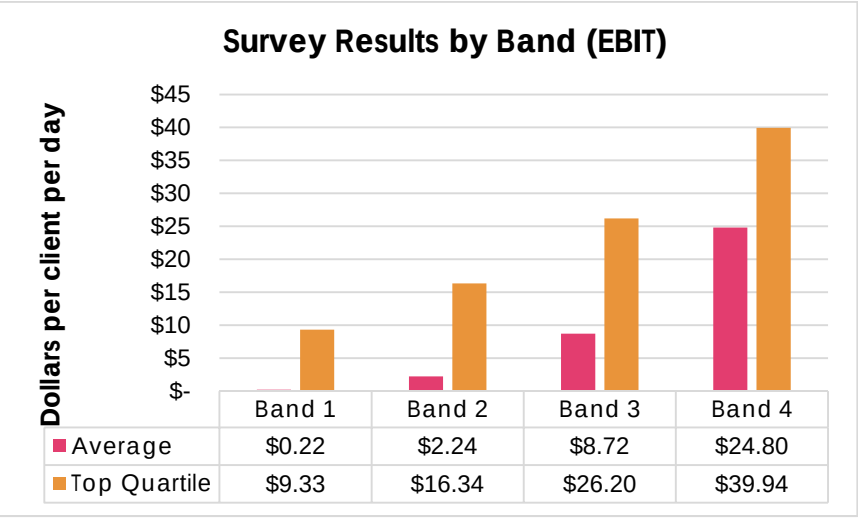


It is important to note that post February 2017, the package utilisation rate will become irrelevant over time. The more important KPIs will be utilisation of capacity, employee productivity, revenue utilisation and profit margins.

Profitability

As mentioned earlier in this report, it is still too early in this data cycle to start talking confidently about trends. It is also clear that there are a combination of factors that are contributing to profitability. These include the revenue utilisation and package utilisation rates. Overwhelmingly it does appear that those that are achieving the best performance are those that are achieving the better average margins across their services. This makes sense and is the core of any retail business model – it is all about volume and margins. The higher the volume the greater the spread of fixed costs and the greater the margin the better the contribution to those fixed costs are on a per unit basis and the greater the level of profitability.

Figure 29 – EBIT by benchmark band



	Band 1	Band 2	Band 3	Band 4
Average	$0.22	$2.24	$8.72	$24.80
Top Quartile	$9.33	$16.34	$26.20	$39.94

ANALYSIS OF MARGINS

Direct Services

The direct services income includes the charges against client's budgets for those services provided directly by the employer. It is also likely to include any unspent funds brought to account as income during the survey period. As expected the margins achieved should be reasonably high as we understand that many providers are relying on the margins earned on direct services to contribute towards the recovery of some of their fixed costs.

As Figure 30 illustrates, the average margins on direct services are all positive with those in the top quartile achieving considerably higher margins than the rest. We are still seeing margins fluctuate as data matures and, we suspect, as providers bring to account unspent funds that have accumulated over time. With the changes to the rules in February 2017 we believe that these fluctuations will start to diminish. They are also likely to diminish over time as the data matures.

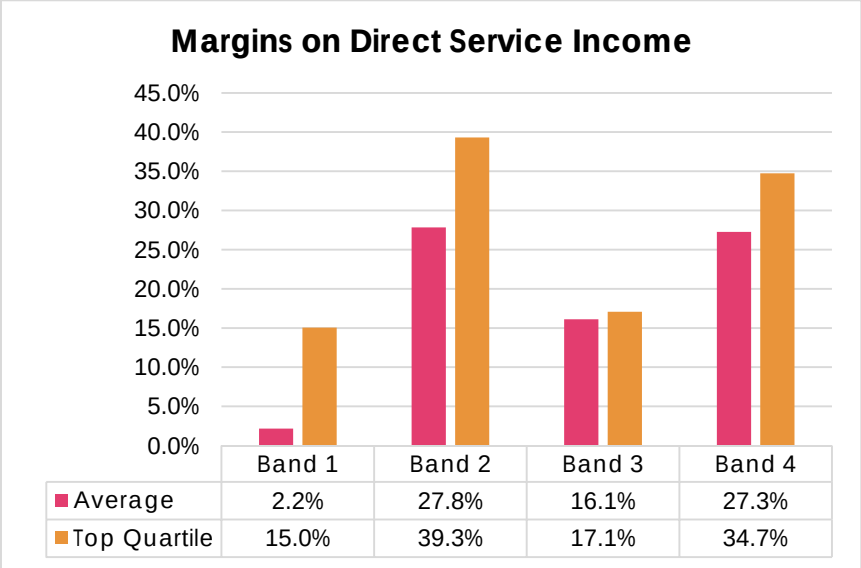
As shown in Figure 31, the costs of package administration are considerably higher in most cases than the income recovered through direct administration fees (as indicated by the negative margins).

We are certainly starting to see more providers charge a lower administration fee and build an element of their administration costs in the direct cost of services upon which a margin is placed. Again it is early days and providers are still positioning themselves in a changing marketplace. However it could make sense to charge a lower administration fee and charge a higher price for direct services.

This is because the direct services price being higher than the competition is an easier sell than the administration fee being higher. People can see value in the service price but the administration fee has no value in it for the consumer – it is a necessary evil.

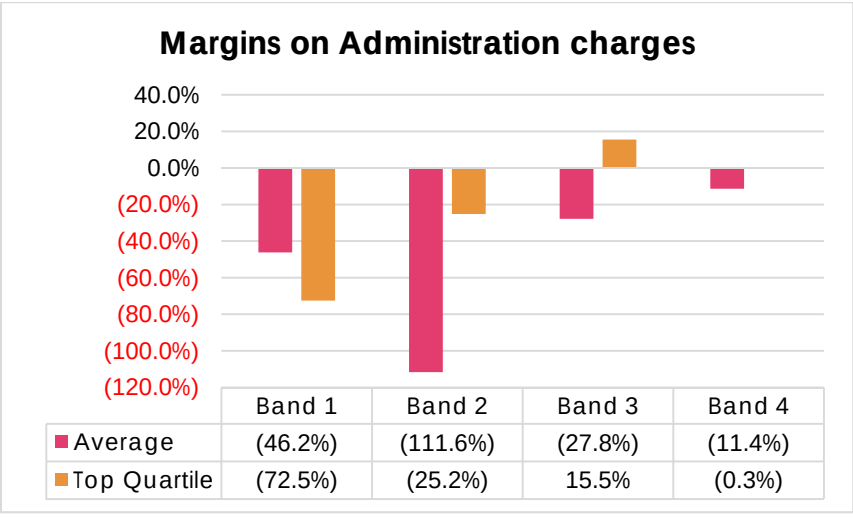
The margins on most of the other services are also minor or in the negative. Although it appears as if more providers are starting to charge a margin or handling fee on brokered services. Again this is going to be essential moving forward as more and more services are likely to be brokered to a third party.

Figure 30 – Average margins on direct services income



	Band 1	Band 2	Band 3	Band 4
Average	2.2%	27.8%	16.1%	27.3%
Top Quartile	15.0%	39.3%	17.1%	34.7%

Figure 31 – Average margins on package administration income



	Band 1	Band 2	Band 3	Band 4
Average	(46.2%)	(111.6%)	(27.8%)	(11.4%)
Top Quartile	(72.5%)	(25.2%)	15.5%	(0.3%)

Once again, at the moment it appears that many providers are relying on the fact that at some point the unspent funds will be brought to account as profit. This will no longer be the case from February 2017 so it is essential that providers review their business models accordingly.

Overall, margins increase moving from Band 1 through to Band 4. This is not surprising because high care packages have always achieved a better return than low care packages. This can be seen in the graph in Figure 33 where the data has been sorted by package level rather than benchmark band.

What is also clear is that the higher the level of activity – the higher the level of reportable income (through a combination of high occupancy and high revenue utilisation), the better the overall return. Bands 1 and 2 are largely comprised of level 2 packages. Those in band 1 have a lower reportable income than those in band 2. They also have a lower average return on income resulting in a lower profit overall.

Similarly, the majority of packages in both bands 3 and 4 are level 4 packages. Those in Band 3 have a lower level of reportable income than those in Band 4 and they also have a lower overall margin resulting in a lower profit.

One matter of interest is the level of consistency in the overall margin achieved by the top quartile group in each band. They all average a little over 25% return on revenue with Band 4 achieving the highest average return on revenue of 28.6%. These returns in Band 4 are not as high as used to be achieved by the top quartile for level 4 packages so it will be of some interest to see where these profits trend over time as the market matures and more competition in introduced.

IN SUMMARY

The takeaway messages for Home Care from the December 2015 survey are:

- **Providers will need to modify business practices to minimise levels of unspent funds and maximise service levels to clients**
- **The better performers are achieving a consistent return on revenue (overall margin) of just over 25%**
- **There are a mix of methods now being employed to charge for package administration including a direct charge, build it into the service fees or a combination of the two**
- **Providers are now starting to put margins on brokered services**
- **Providers are continuing to position themselves for the reforms in 2017**
- **Post February 2017 the package utilisation rate will become irrelevant over time. The important KPIs will be utilisation of capacity, employee productivity, revenue utilisation and profit margins.**

Figure 32 – EBIT as a percentage of total revenue (overall margin) sorted by benchmark bands

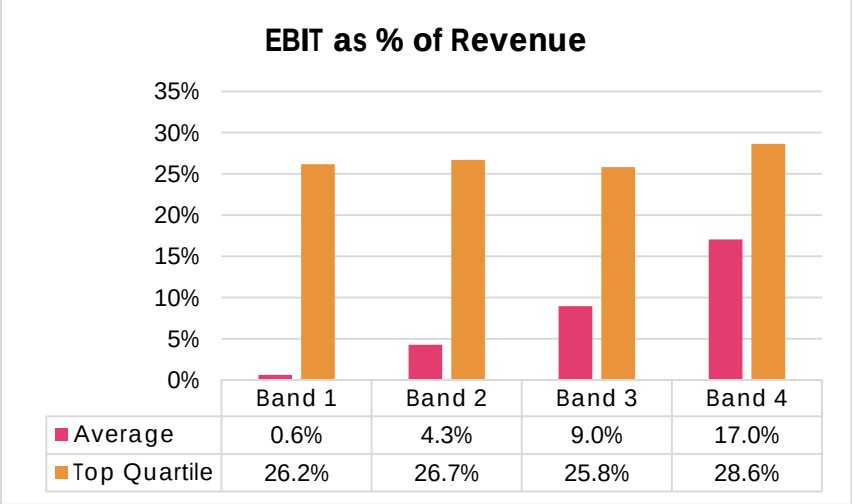
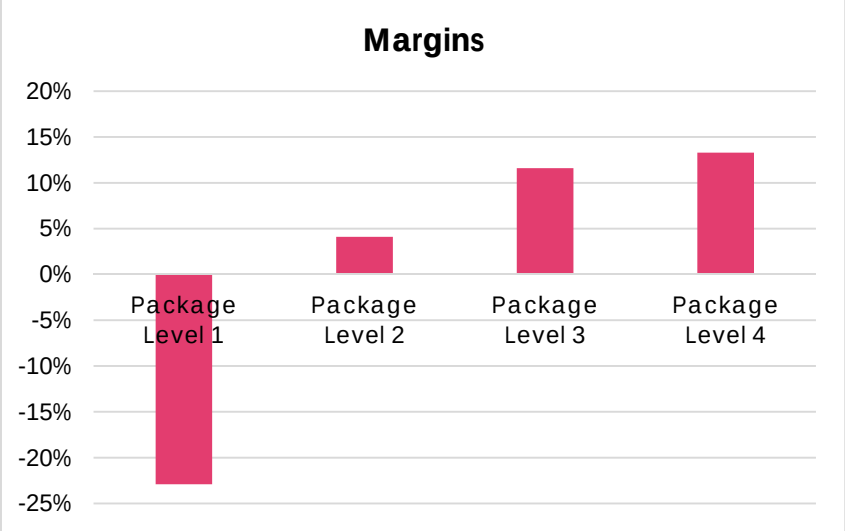


Figure 33 – EBIT as a percentage of total revenue (overall margin) sorted by package level



2015 ACAR Results

The competition for the allocation of Home Care places was even fiercer than for residential care. There were 6,045 places advertised and there were applications for 126,808 places. In total there were 6,455 places made available which is a slight reduction in the number of places allocated in the 2014 ACAR (6,653).

Unlike the situation with the allocation of residential places, home care places were allocated in a manner that reflected the existing ownership mix of home care packages. With only 10% of packages owned by the for-profit sector nationally, it might have been expected that more packages would have been released to private operators if the pattern of the residential place allocations were to be followed.

Instead the majority of packages were allocated to the not-for-profit sector. The big winners were Uniting, Feros Care and Integrated Living and this followed a similar pattern to the 2014 allocations so that these three providers top the list of allocations over the last two rounds. Hammond Care have also been consistent in the numbers of packages awarded over the past two years with 230 packages awarded this year and 205 awarded in the previous round.

It will be interesting to see how quickly the mix of providers change once the 2017 reforms take hold. Will the larger for-profit residential providers move into the home care market? Will some of the big private retirement village operators start to target their residents for home care services?

The big question is whether the larger providers in the home care market will be able to use their current market penetration to their advantage in warding off the loss of business that will come from the inevitable move by new entrants to the market and increased levels of competition.

Figure 34 – Allocations of home care places – Top 15 providers

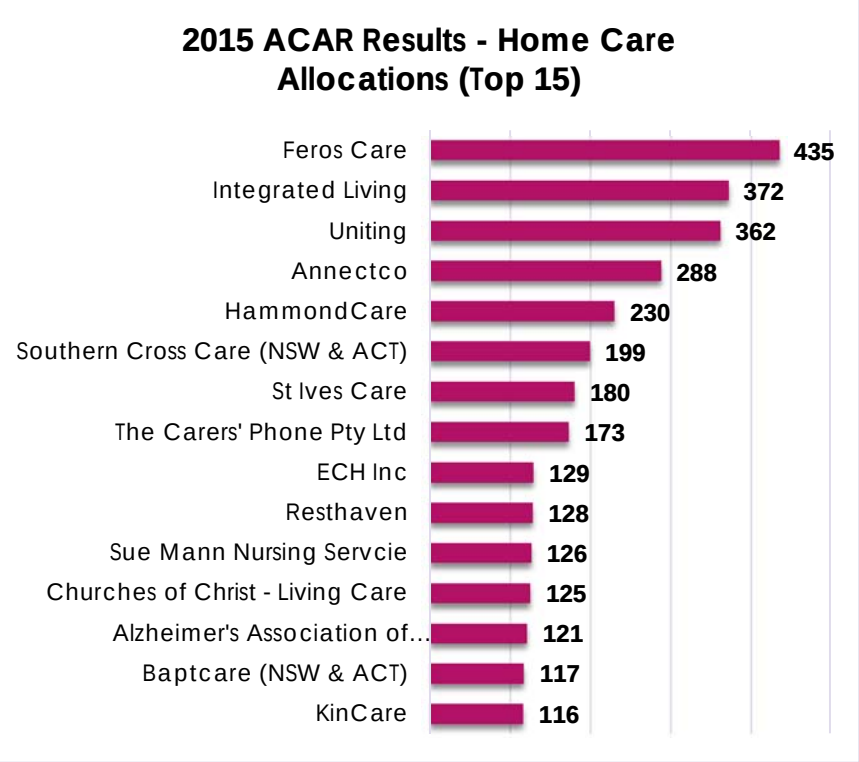
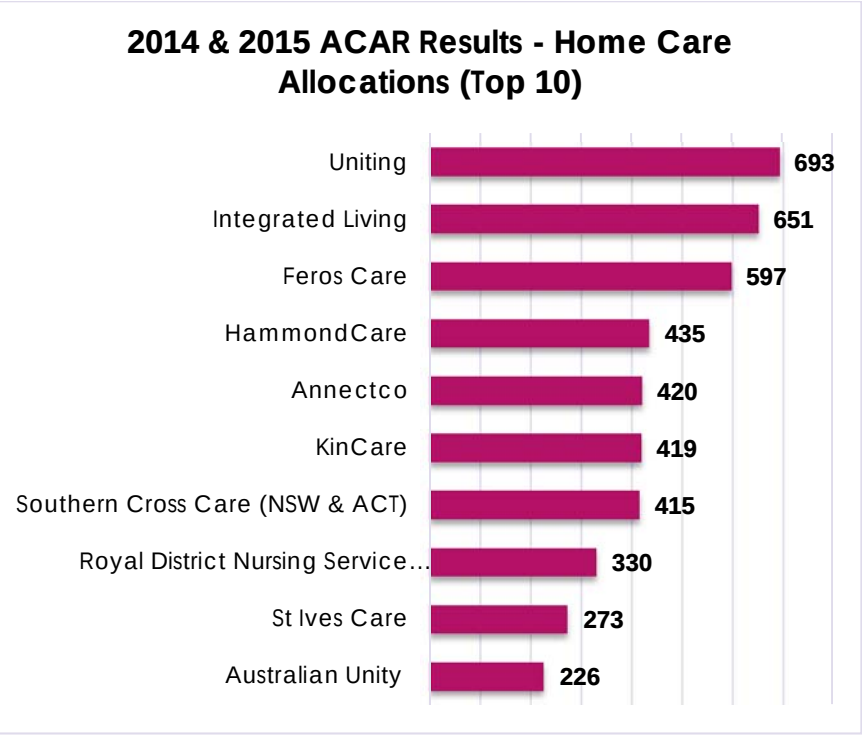


Figure 35 – Allocations of home care places – Top 10 providers



HOME CARE - PACKAGES
PERIOD ENDED 31 DECEMBER 2015
2016 SAMPLE HOME CARE REPORT

	Survey Average December 2015 Band 4 (46 Programs)	Survey Top 25% December 2015 Band 4 (12 Programs)	2016 Sample Report Band 4
REVENUE			
Direct services	91.76	81.20	79.70
Brokered services	3.38	3.13	
Case management and coordination	9.53	7.94	18.48
Package administration	40.82	47.28	38.86
TOTAL REVENUE	145.49	139.55	137.03
EXPENDITURE			
Direct service costs			
Staff costs	50.89	38.88	45.17
Agency costs	3.29	2.84	1.89
Consumables	5.60	4.77	8.86
Transport expenses	5.72	4.82	5.10
Other direct service costs	1.24	1.67	
Total direct service costs	66.73	52.99	61.03
Sub-contracted or brokered costs	4.31	2.84	6.32
Case management & coordination			
Staff costs	12.70	12.22	6.68
Agency costs	0.02		
Transport expenses	0.17	0.03	0.02
Total case management & coordination	12.89	12.25	6.70
Administration & support			
Corporate recharge	15.48	9.71	20.62
Staff costs	13.61	16.37	25.81
Workers compensation insurance	1.90	1.64	3.14
Education & quality control expenses	0.58	0.57	0.99
General insurances	0.18	0.14	0.27
Rent	0.97	0.64	1.70
Telecommunications	0.58	0.32	1.02
IT expenses	0.54	0.43	0.30
Utilities	0.24	0.15	0.40
Other administration & support service costs	1.98	0.88	3.51
Total administration & support services	36.07	30.85	57.76

HOME CARE - PACKAGES
PERIOD ENDED 31 DECEMBER 2015
2016 SAMPLE HOME CARE REPORT

	Survey Average December 2015 Band 4 (46 Programs)	Survey Top 25% December 2015 Band 4 (12 Programs)	2016 Sample Report Band 4
Depreciation	0.69	0.69	0.35
TOTAL EXPENDITURE	120.69	99.61	132.16
RESULT FOR THE YEAR (EBIT)	$ 24.80	$ 39.94	$ 4.87
EBITDA PER PACKAGE PER ANNUM	$ 8,728	$ 13,632	$ 1,826
Package Utilisation Analysis			
Paid care days	211,407	117,221	8,818
Number of funded packages	1,225	693	50
Package Utilisation rate	**93.8%**	**91.9%**	**95.8%**
Efficiency Ratios			
Total funding and resident fees received	170.49	155.84	172.17
Total income recognised	145.49	139.55	137.03
Unspent funds at period end	25.00	16.29	35.13
Revenue utilisation rate	85.3%	89.5%	79.6%
Staff Hours Analysis			
Average staff hours per package per week			
Direct service provision	10.63	8.20	9.22
Agency	0.39	0.44	0.73
Case management & coordination	1.40	0.66	1.88
Administration & support services	0.99	0.54	2.42
Total Staff Hours	13.41	9.84	14.24
Workers compensation as a % of total wages	2.5%	2.4%	4.0%

Home Care Band Information

Based on Total Income (Direct Care + Brokered + Case Management + Administration)
Band 1 - Under $40
Band 2 - Between $40 and $75
Band 3 - Between $75 and $120
Band 4 - Over $120

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HOME CARE - PACKAGES
PERIOD ENDED 31 DECEMBER 2015
2016 SAMPLE HOME CARE REPORT

	Survey Average December 2015 Band 4 (46 Programs)	Survey Top 25% December 2015 Band 4 (12 Programs)	2016 Sample Report Band 4
Gross Margin Analysis			
Total direct services income	91.76	81.20	79.70
Total direct services costs	66.73	52.99	61.03
Result - Direct services	25.03	28.21	18.66
Direct services % margin	27.3%	34.7%	23.4%
Total brokered services income	3.38	3.13	-
Total brokered services costs	4.31	2.84	6.32
Result - Brokered services	(0.92)	0.29	(6.32)
Brokered services % margin	-27.3%	9.3%	0.0%
Total case management & coordination income	9.53	7.94	18.48
Total case management & coordination costs	12.89	12.25	6.70
Result - Case management & coordination	(3.36)	(4.31)	11.78
Case management & coordination % margin	-35.3%	-54.3%	63.8%
Total administration & support income	40.82	47.28	38.86
Total administration & support costs	36.07	30.85	57.76
Result - package administration	4.75	16.43	(18.90)
Administration & support % margin	11.6%	34.7%	-48.6%
Total Revenue	145.49	139.55	137.03
Total Expenses	120.69	99.61	132.16
Total Result	24.80	39.94	4.87
Total Result % margin	17.0%	28.6%	3.6%
Administration charge as % of services income	42.9%	56.1%	48.8%
Case management & co-ordination charge as % of services income	10.0%	9.4%	23.2%

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STEWARTBROWN AGED CARE EXECUTIVE TEAM

Stuart Hutcheon

Managing Partner

Stuart Hutcheon is the firm's Managing Partner and the head of our Audit & Assurance Division, and also provides consulting services to a diverse client base. He has had considerable experience with both commercial and not-for-profit organisations. This experience covers all areas of professional services including auditing, management accounting, budgeting, salary packaging and FBT advice. Stuart has been involved in providing professional services to the aged care and community care industry sectors for over 20 years.

David Sinclair

Director

David Sinclair has been with the firm for 20 years and has been involved in the Aged Care Financial Performance Survey for the duration of that service and now heads the team undertaking the survey. David is also heavily involved in consulting assignments for aged care and community service clients including strategic planning, financial modelling, budgeting and governance reviews.

StewartBrown currently has over 25 qualified professional staff that have specific experience assisting businesses in the aged care and community services sectors. Call today to find out how we can assist your business to improve.

Grant Corderoy

Senior Partner

Grant Corderoy is the head of the national Aged and Community Care and Business Consulting Division. Grant first established the Aged Care Financial Performance Survey in 1995. He specialises in a range of services for his clients including undertaking complex accounting assignments, organisation and governance reviews, system reviews, management consulting, specialised audits and general business advice. He also has considerable experience in advising clients on the sale and purchases of businesses, business valuations and due diligence.

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