CENTRE FOR THE
HEALTH ECONOMY

MACQUARIE University

The role of RADs

Professor Henry Cutler (Presenter)

Dr Yuanyuan Gu (Presenter)

Dr Megan Gu

Mona Aghdaee

Associate Professor Mostafa Hasan

Dr Carl Shen

Presentation overview

1. Reflection on RADs
2. Trends in RADs
3. Factors driving RAD choices
4. Provider survey results
5. Views from providers
6. Views from other stakeholders
7. RADs and provider financial performance
8. Conclusions
9. Discussion

Reflection on RADs

A short history lesson

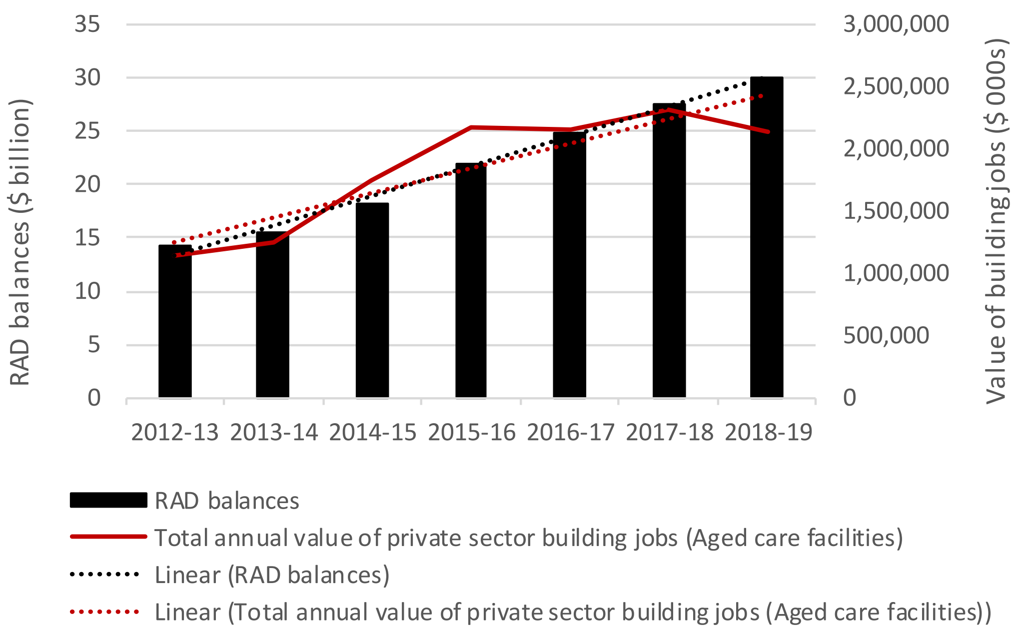
- Accommodation bonds were first introduced the *Aged Care Act 1997*.
- Capital stock was poor, new building standards were introduced
- Government stated providers could not attract enough debt and equity due to poor economic conditions
    - Unemployment was above eight per cent, there was a national savings problem, investment in housing was low, and the Budget deficit equalled two per cent of GDP
- But was also projected to save the Australian Government $479 million over four years within the 1996-97 Budget

Capital expenditure

- The Aged Care Financing Authority (ACFA) projects that approximately 80,000 new beds are required in the next decade
- Most capital expenditure in residential aged care is funded by RADs
  - Assets are made up of 57.4 per cent RADs, 4.1 per cent bank debt, 4.4 per cent related parties, and 25.7 per cent equity
- RAD balances have grown by approximately 93 per cent between 2014 and 2019 (now $32 billion) despite a shift to DAPs
- RADs have allowed providers to build better and more facilities, thereby meeting consumer preferences and needs

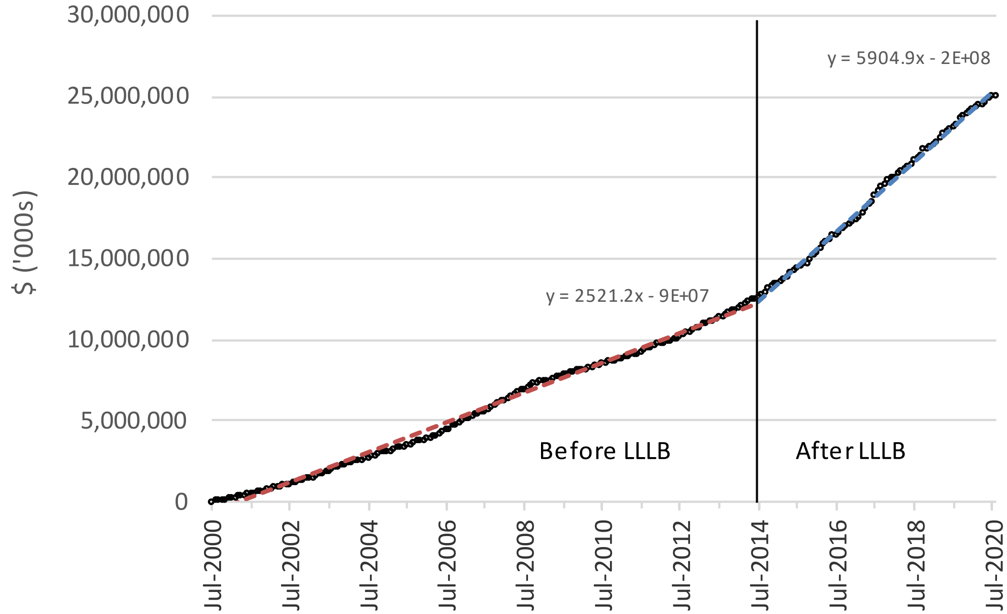
Capital expenditure

Chart 1.2: RAD balances and annual value of private sector building jobs for aged care facilities



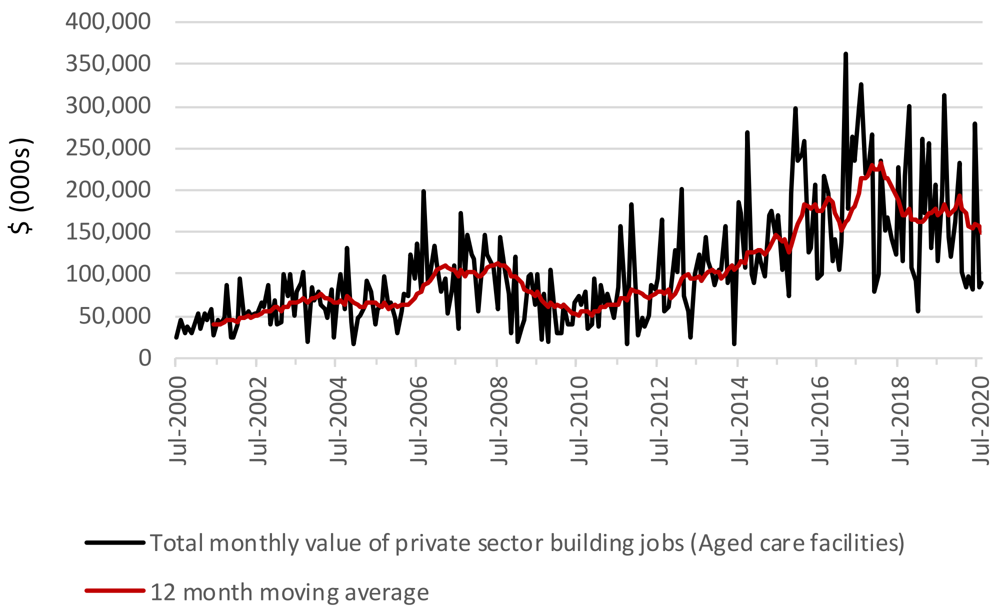
Capital expenditure

Chart 1.1: Cumulative value of monthly private sector building jobs for aged care facilities



Capital expenditure

Chart 1.3: Total monthly value of private sector building jobs for aged care facilities



Ongoing RAD debates

- Ongoing debates on improving prudential requirements since 2009

- StuartBrown found many providers were facing liquidity risks (mid June 2018)

  - $9.6 billion worth of lump sum accommodation payments were held by providers with a high or very high liquidity risk rating

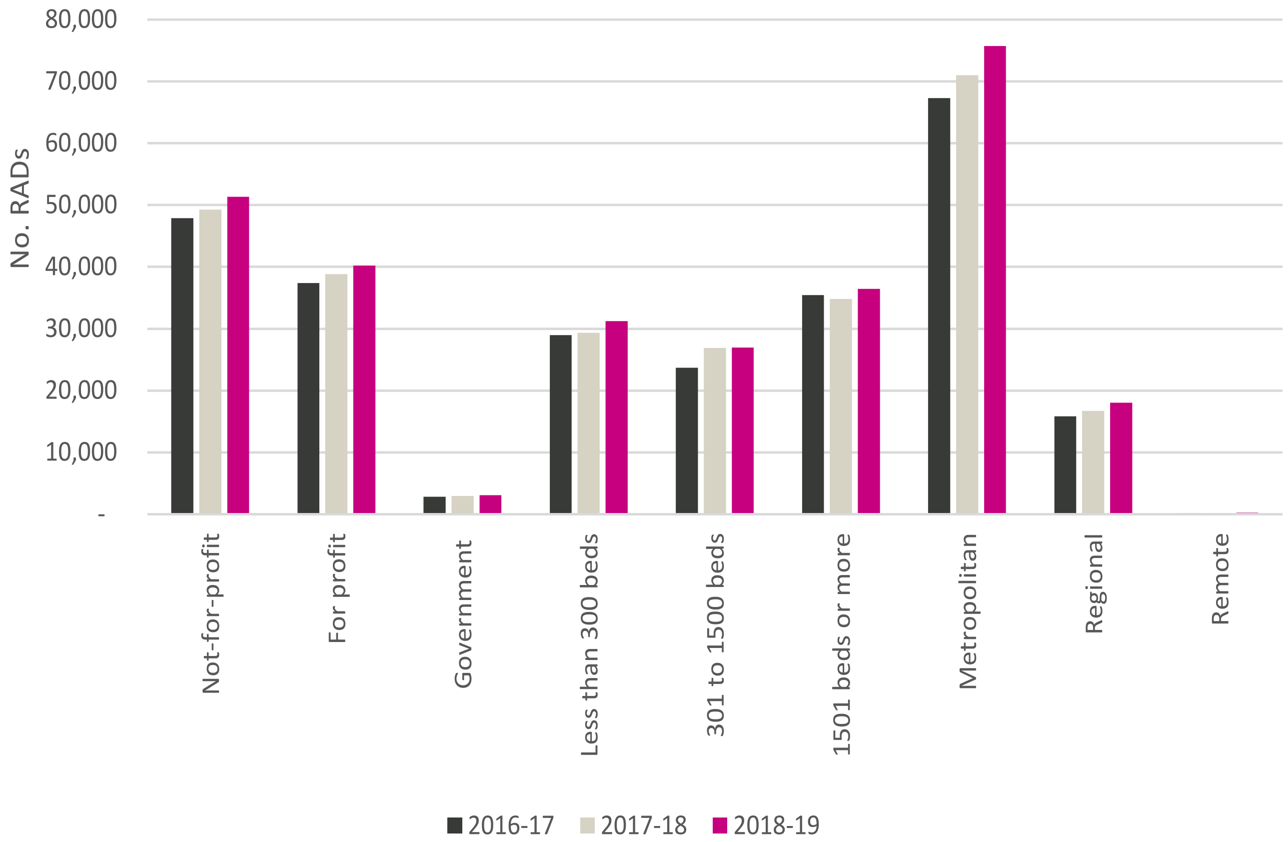
  - 164 providers were at risk of not complying with the permitted use rules, with around $1.6 billion at risk

- The Royal Commission recommended stronger prudential requirements but ultimately phasing out RADs with assistance from the Australian Government

Trends in RADs

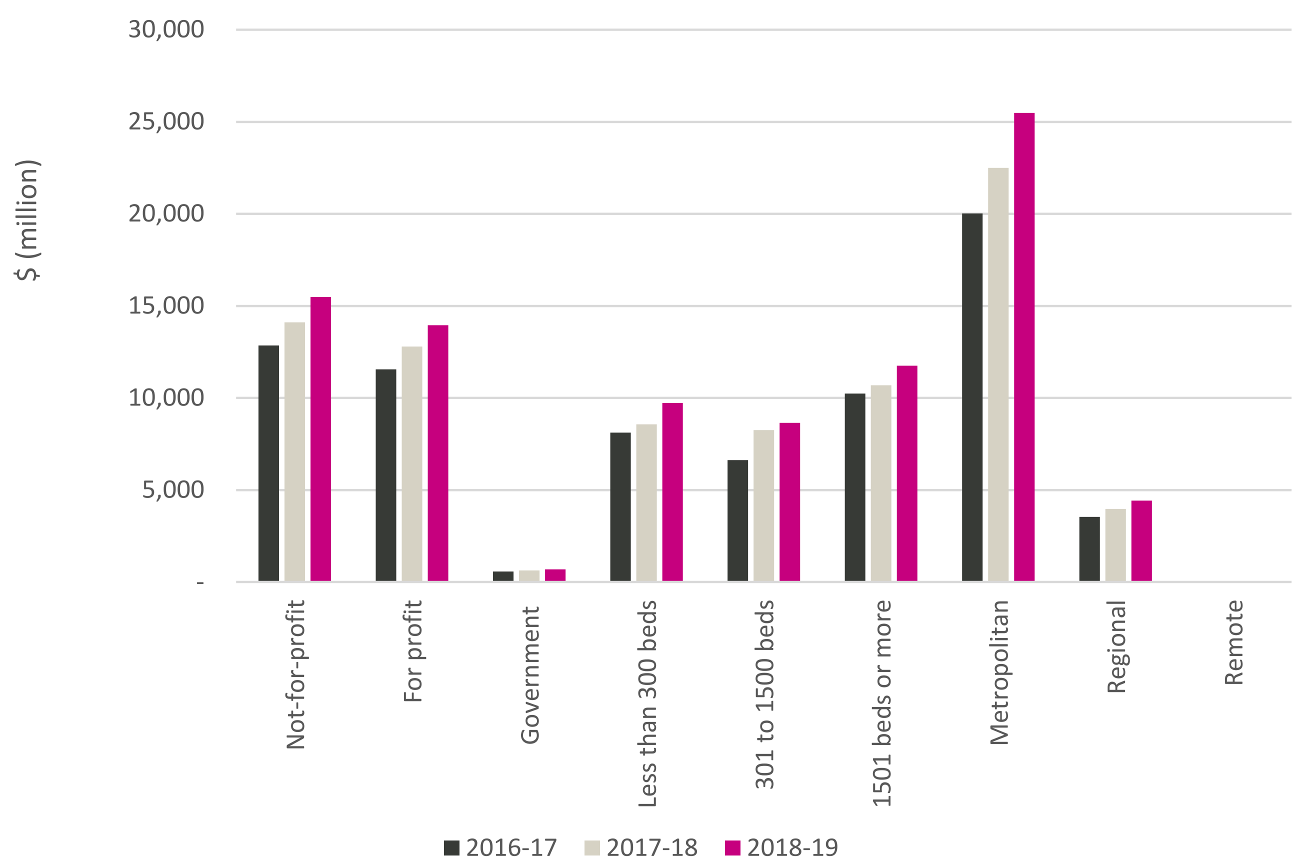
Trends in the volume

Chart 2.1: Number of RADs held by provider characteristics



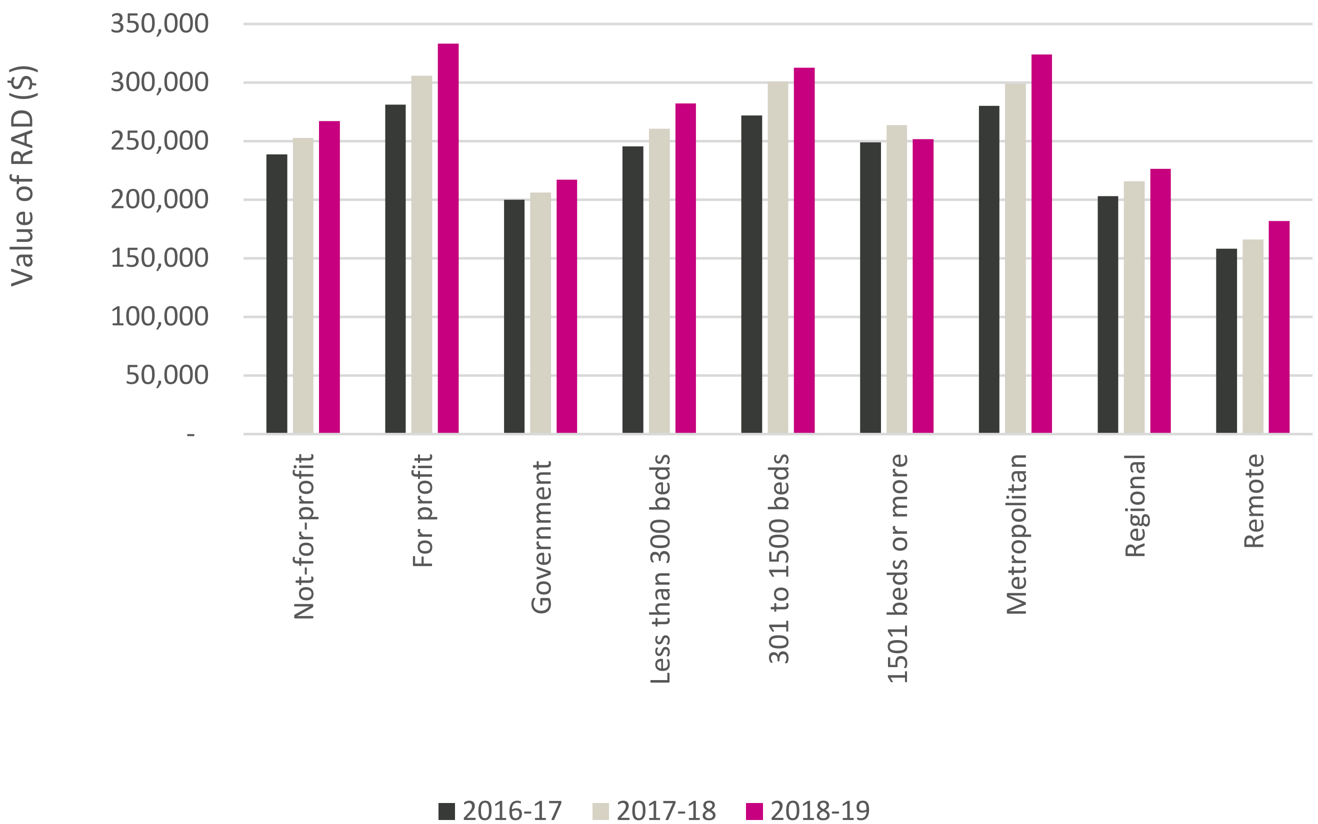
Trends in RAD balances

Chart 2.2: Total RAD balance by provider characteristics



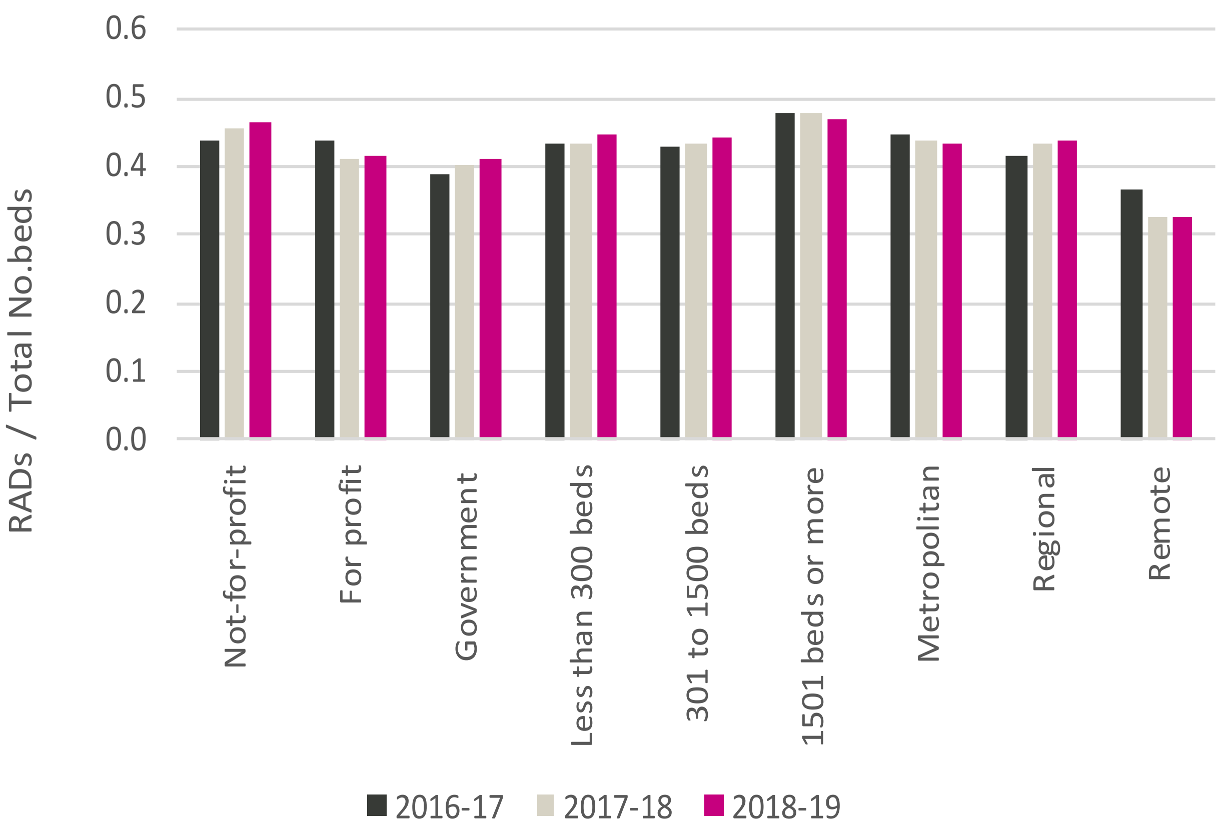
Trends in RAD balances

Chart 2.3: Average RAD value by provider characteristics



Trends in RAD balances

Chart 2.4: Proportion of total beds paid for by RADs



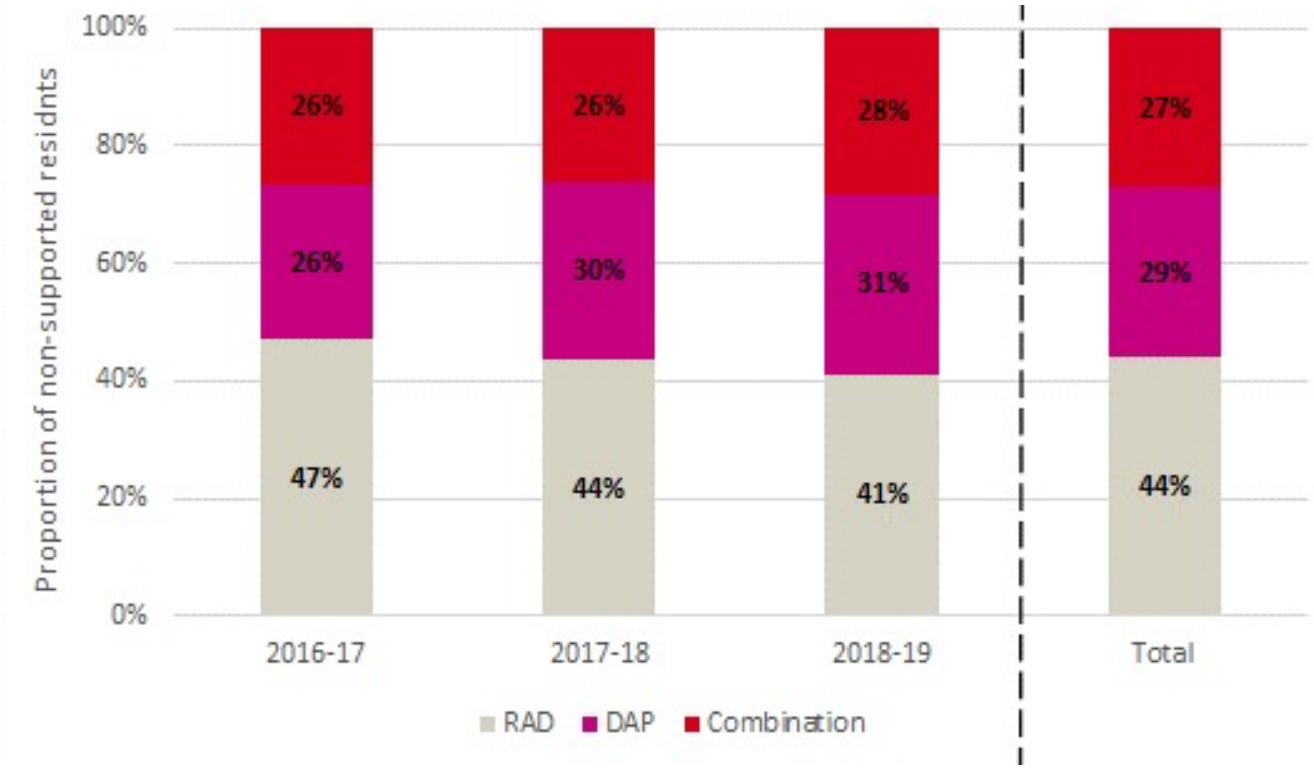
Factors driving RAD choices

Consumer choice analysis

- Trends in RADs are determined by trends in consumer choices
- Using two de-identified administrative datasets from the DoH:
  - the annual survey of aged care homes (SACH) and
  - resident's characteristics collected by Service Australia
- 57,508 **non-supported residents** & 18,129 partially-supported residents
- Regression analyses were used to estimate the associations between the accommodation payment choice and a number of factors

Trends in consumer choice

Chart A.1: Non-supported residents' choice of payment



Length of stay (LOS)

- Should not directly impact the payment choice because that choice is made at the beginning of their stay
- Statistically significant though - a consumer that stayed for a relatively short period was more likely to choose a DAP
- Consumers with a short LOS may have formed **expectations** that their LOS was going to be short
- A short period in residential aged care can reduce the consumer's ability to pay a RAD

Consumer health

- The less healthy consumers are when entering residential aged care, the less likely they will choose a RAD

- This reflects the impact of consumer health on choosing a RAD with LOS controlled

- Another proxy of expected LOS (LOS may not perfectly proxy it)

Assets and income

- The more assets reported by the consumer, the more likely they will choose a RAD
- Income is also statistically significant but negatively associated with the probability of choosing RAD
- This likely reflects the increased ability for a consumer to pay a DAP as income increases

Accommodation price & the MPIR

- Consumers are more likely to choose a combination payment when faced with a high accommodation price but are also more likely to choose a DAP within that combination payment
- Consumers may find it more difficult to pay a RAD when the accommodation price is high
- Consumers are more likely to choose a RAD as the MPIR increases
- When the MPIR increases, the cost of DAPs would increase, making them less affordable for consumers

Resident characteristics

- An older person, or married person, entering residential aged care is more likely to choose a RAD and less likely to choose a DAP
- They are also more likely to choose a greater proportion of RAD within a combination payment
- Male consumers are more likely to choose a DAP

Facility characteristics

- Capturing unobserved factors such as cultural differences in attitudes towards accommodation payment types, differences in financial literacy and access to financial advisors, etc.
- Compared to those who entered facilities in NSW, consumers who entered facilities in all other states except ACT were more likely to use the combination payment with a lower proportion of RAD component
- Consumers who entered facilities in remote areas are more likely to choose a DAP than a RAD. If they do choose a combination payment, the proportion of the RAD component is likely to be lower.

Facility characteristics

- Consumers who entered a not-for-profit or government facility were less likely to choose a RAD and more likely to choose a DAP or combination payment

- Different types of ownership may attract different types of consumers

- Some providers may manipulate accommodation payment choices towards RADs - evident in our provider survey and provider focus groups

Relative impact of choice predictors on choosing a RAD

Choice predictor	Scenario	Impact on probability
LOS	one sd increase	2.3%
ACFI: ADL score	one sd increase	-0.5%
ACFI: BEH score	one sd increase	0.2%
ACFI: CHC score	one sd increase	-0.8%
Asset amount on entry	one sd increase	13.6%
Income	one sd increase	-1.2%
Agree accommodation price	one sd increase	-4.4%
MPIR	one sd increase	1.0%
Age at admission	one sd increase	1.0%
Male	compared to female	-0.5%
Currently married	compared to not married	2.1%
State: VIC	compared to NSW	-5.2%
State: QLD	compared to NSW	-16.8%
State: SA	compared to NSW	-13.9%
State: WA	compared to NSW	-24.1%
State: TAS	compared to NSW	-0.3%
State: ACT	compared to NSW	-1.0%
State: NT	compared to NSW	-14.3%
Remoteness: Inner regional	compared to major cities	-7.4%
Remoteness: Outer regional	compared to major cities	-12.7%
Remoteness: Remote	compared to major cities	14.9%
Ownership: Non for profit	compared to "for profit"	-8.4%
Ownership: Government	compared to "for profit"	-7.7%

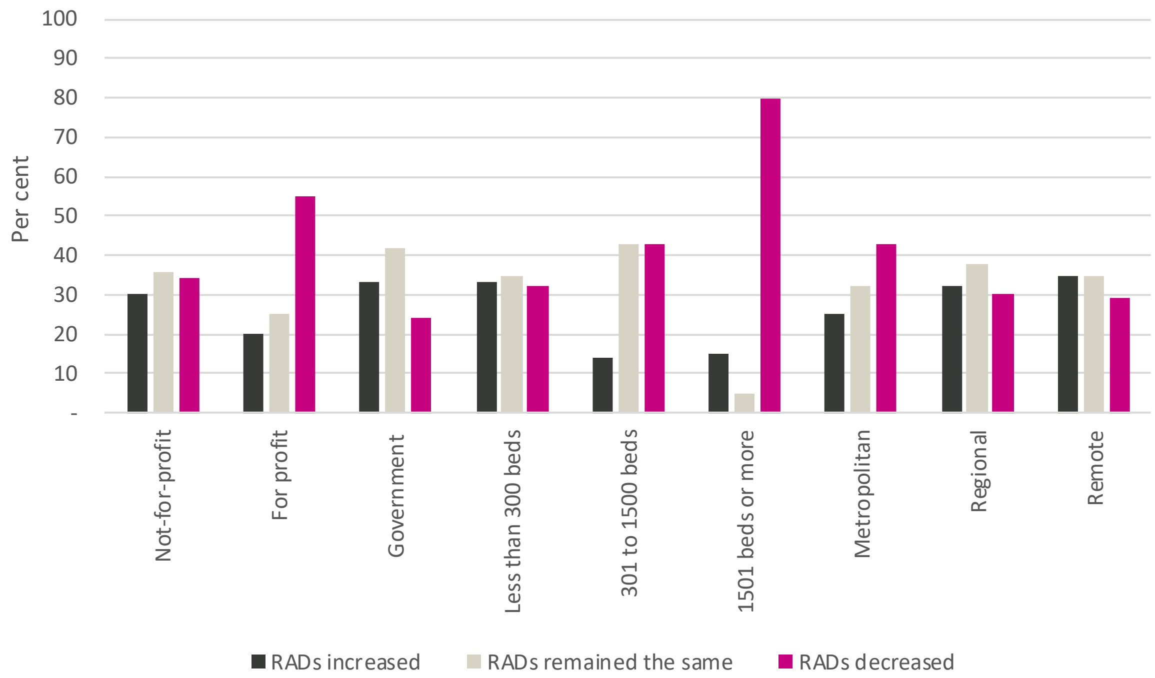
Provider survey results

Survey overview

- We surveyed 300 residential aged care providers to capture the current and future use of RADs
- The survey was open between 26 October 2020 and 13 November 2020
- Respondents reflected the sector's composition. Some over representation of provider types:
  - mid-sized providers (301-1,500 approved beds),
  - providers with most facilities located in remote regions, and
  - not-for-profit providers.

Trends in RADs

Chart 4.1: Change in the choice of payment by characteristic



Trends in RADs

Table 4.5: Reasons for a decline in RAD balances

List of reasons	Per cent
Decline in the proportion of residents choosing to pay a RAD in full	41.7
Decline in the proportion of residents choosing to pay a RAD in combination with a DAP	23.3
Decline in occupancy rates	20.0
Decline in accommodation prices	5.8
Decline in the number of approved places held by the organisation	0.8
Other reasons:	
Increase in number of supported residents	6.7
Opening new facilities	0.85
Government Legislation has encouraged residents/families to pay a DAP	0.85

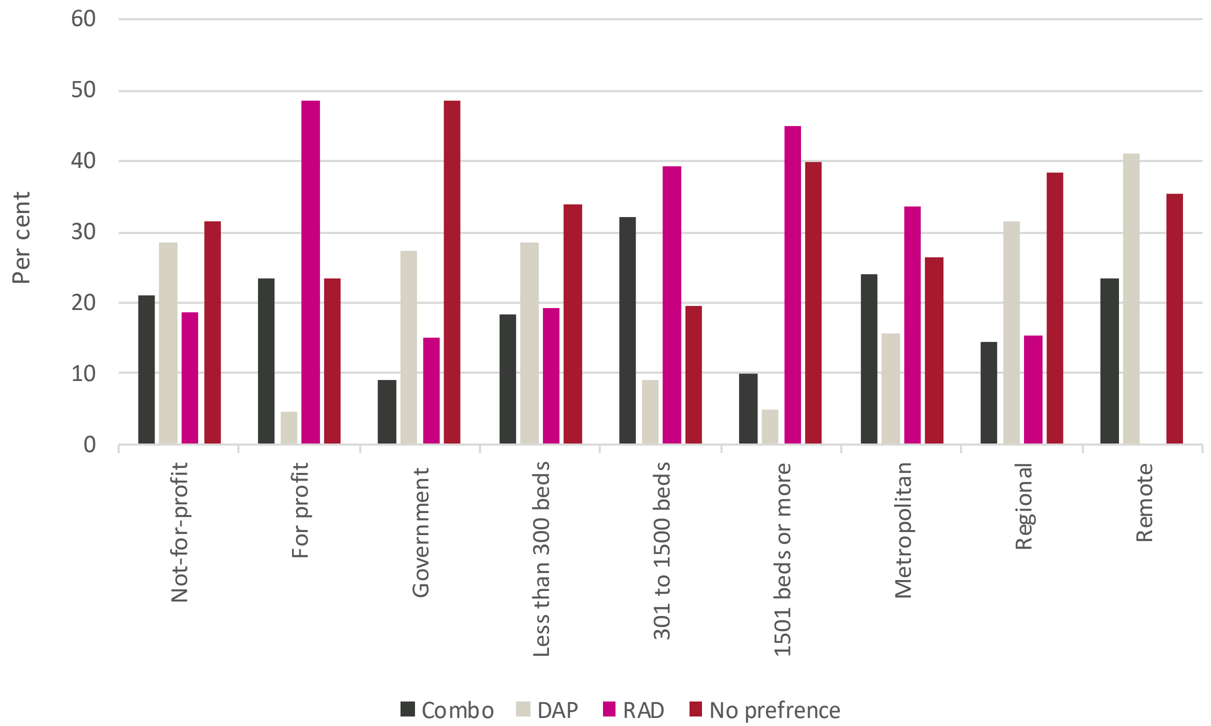
Current use of RADs

Table 4.6: Provider preference for accommodation payment types

Choice of payment	No. of respondents	Per cent
Only RAD	74	24.7
Only DAP	70	23.3
Combination of RAD and DAP	61	20.3
No preference	95	31.7

Current use of RADs

Chart 4.2: Provider preference for accommodation payment type by provider characteristic



Current use of RADs

Table 4.8: Proportion of RADs used for other purposes

Investment type	Per cent
Held as cash in a deposit account	80.4
Other	7.7
Invest in managed funds	6.7
Invest in bonds	1.7
Invest in stocks	1.6
Invest in other securities	1.4
Invest in a debenture	0.4
Make a loan	0.2

Future use of RADs

Table 4.10: Is your RAD balance significantly exposed to a reduction in housing prices?

	Yes	No
	per cent	*per cent*
Organisation type		
Not-for-profit	47.8	52.2
For-profit	51.6	48.4
Government	21.2	78.8
Remoteness region		
Metro	53.6	46.4
Regional	35.0	65.0
Remote	41.2	58.8
Number of approved beds		
1-300 beds	40.6	59.4
301-1500 beds	55.4	44.6
more than 1500	75.0	25.0
All providers	**45.7**	**54.3**

Future use of RADs

Table 4.11: Is your RAD balance significantly exposed to other events?

	Per cent
Yes (Reduction in occupancy rates)	20.8
Yes (Reduction in interest rates)	20.5
Yes (Increase in residents choosing a DAP)	20.2
Yes (Reduced expected length of stay for residents)	18.7
Yes (Reduction in accommodation prices)	10.4
Yes (Discontinuation of the Aged Care Approvals Round)	6.3
No	3.1

Future use of RADs

Table 4.13: Would a 10 per cent reduction in RAD balances impact your capital expenditure?

	Yes	No
	per cent	*per cent*
Organisation type		
Not-for-profit	26.6	73.4
For-profit	64.1	35.9
Government	3.0	97.0
Remoteness region		
Metro	44.0	56.0
Regional	17.9	82.1
Remote	11.8	88.2
Number of approved beds		
1-300 beds	22.8	77.2
301-1500 beds	57.1	42.9
more than 1500	65.0	35.0
All providers	**32.0**	**68.0**

Views from providers

Provider focus groups

- We conducted five focus groups with 23 providers in October 2020
- Providers were selected based on their significant RAD balances, reflecting primarily large for profit and not-for-profit providers
- Each focus group discussion was recorded and transcribed.
- A thematic analysis was undertaken by coding and analysing discussion transcripts using the software NVivo

Provider focus groups

- All providers shared the view that RADs have encouraged and facilitated capital expenditure in residential aged care
- The reliance on RADs varied by provider characteristics and the stage of their capital expenditure program.
- Some providers believe RADs limit their ability to optimize their financial performance (due to permitted use restrictions)
- Others believed RADs imposed a barrier to REITs given consumers choose

Provider focus groups

- Providers noted they have little control over a residents' accommodation payment choice.
  - Some wanted to restrict consumer choice
- Providers doubted they could obtain enough debt or equity to replace a significant reduction in RAD balances.
- Providers thought any alternative financing system to replace RADs must be supported by the Australian Government
- There was no consensus among providers on whether RADs encouraged accommodation innovation or imposed barriers

Views from other stakeholders

Stakeholder interviews

- We conducted semi-structured interviews with 14 aged care stakeholders in September 2020
- Stakeholders represented banks, aged care peak bodies, consumer peak bodies, and valuers
- Responses were recorded and transcribed.
- A thematic analysis was undertaken by coding and analysing discussion transcripts using the software NVivo

Stakeholder interviews

- All stakeholders recognised that RADs have been essential for capital expenditure

- Some noted that RADs created a more volatile capital structure

  - At risk to fluctuations in consumer preferences

  - Require continual monitoring and management by providers

- Consumer peaks noted RADs were complex and many lacked the financial literacy to make informed choices

- Consumers mistrusted financial advisors and some cannot afford to use one

Stakeholder interviews

- Stakeholders had different views on the impact of a significant reduction in RADs
  - Some noted a slow reduction could be managed by providers
  - DAPs were considered more appealing by some providers
  - Others thought capital expenditure would reduce
- Banks thought a significant reduction in RADs could not be covered by bank debt
  - Would not have the capacity, and many small providers would miss out
- No consensus on whether RADs are appropriate in a future aged care system.

RADs and financial performance

RADs and financial performance

- We undertook analysis of provider financial data to estimate the relationship between RADS and financial performance
    - Annual Prudential Compliance Statement and Aged Care Financial Reports for three years (2016-17 to 2018-19)
- Financial performance was measured across profitability, capital expenditure, liquidity and solvency
    - A total of 16 financial metrics was used to measure financial performance
- Other provider factors that impact financial performance were controlled for in the model
    - Assets, provider size, leverage, retained earnings, property plant and equipment, geography, ownership type, year effects

RADs and financial performance

Table 7.1: Trends in provider financial statistics

	2016-17	2017-18	2018-19
RAD (million)	26.411	29.155	31.795
Number of Bed	218.797	226.532	231.593
For-profit Provider	301	291	278
Non-profit Provider	502	495	487
Government Provider	103	101	100
Average Number of Facilities	3.043	3.048	3.010
Profitability			
NPBT/TI	0.032	-0.009	-0.001
EBITDA/TI	0.090	0.049	0.058
NPBT/TA	0.017	-0.004	0.001
EBITDA/TA	0.041	0.020	0.024
NPBT/BED	0.004	0.001	0.001
EBITDA/BED	0.009	0.006	0.007
Capital expenditure			
CAPX/TA	0.038	0.032	0.032
CAPX/BED	0.009	0.008	0.008
CAPX/PPE	0.110	0.102	0.092
Liquidity			
LIQ/TL	0.518	0.474	0.517
LIQ/TA	0.253	0.249	0.268
EXL/CL	0.315	0.262	0.319
EXL/TL	0.283	0.246	0.296
Solvency			
EBIT/INT	131.3	50.1	46.8
EBITDA/INT	250.0	142.6	119.0
Z-SCORE	-0.301	-0.865	-0.712

Modelling results

RADs have a significant and varied relationship with provider financial performance

Profitability

- Positive with RADs
- Stronger for for-profit providers
- Stronger for larger providers
- No relationship to government providers
- Significance lost when accounting for other factors

CAPEX

- Positive with RADs
- Stronger for not-for-profit providers
- Stronger for larger providers
- No relationship for government providers
- Significance remains when accounting for other factors

Liquidity

- Negative with RADs
- Stronger for not-for-profit providers
- Stronger for smaller providers
- Weak relationship for government providers
- Significance remains when accounting for other factors

Solvency

- Negative with RADs
- Stronger for not-for-profit providers
- Stronger for smaller providers
- Weak relationship for government providers
- Significance remains when accounting for other factors

Conclusions

Will there be a reduction in RADs?

- Trends in RAD balances suggest these will continue to increase
- No significant reduction in RAD balances in the immediate future
  - Average health of consumers entering care and average length of stay is stable
  - MPIR seems like the primary driver of a shift towards DAPs but limited scope to reduce much further
  - Home Care packages have increased, but so too has demand. Wait times have remained constant for the last two years
  - Occupancy rates are declining, which may reduce RAD balances relative to beds
- Some providers have managed the shift to DAPs using price increases

Should the Government intervene?

- A significant reduction in RAD balances would impact providers differently

- Most impacted are those with a business model developed around a high proportion of RADs

  - Large, for-profit providers located mostly in metropolitan regions

- A reduction in RADs would benefit many providers with a business model developed around DAPs

- The Australian Government should only intervene if access to care is at risk from provider failure

Intervention options

- Increasing capital grants
- Developing a loan facility for providers
- Providing commercial debt insurance
- Allowing providers to restrict consumer choice
- Attracting REITs
- Attracting commercial debt
- Replacing the MPIR
- Reducing the need for intervention

Questions