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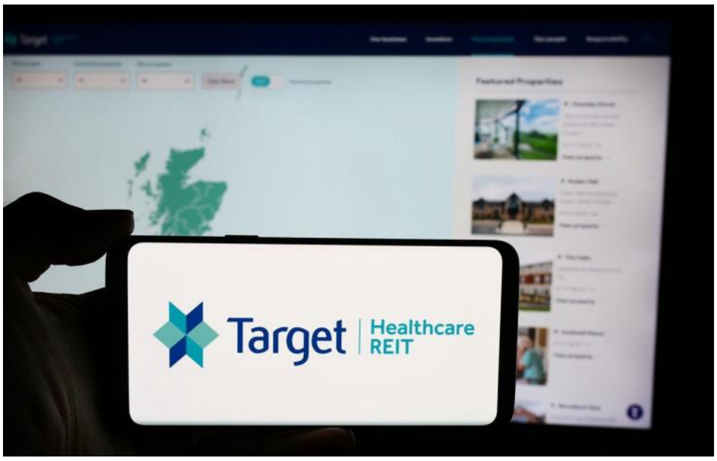
Five questions for Target Healthcare REIT

17 Mar 2025 | 08:20 | London | by Jessica Middleton-Pugh

Listed care home specialist posted half-year results on Friday to warm stock market reception



Listed purpose-built care home specialist Target Healthcare released its six- month results on Friday, with positive figures across the board including a portfolio valuation increase, fresh from a surge in its share price which reached its highest in a year.

Adjusted earnings per share increased 2.6% to 3.13p, the quarterly dividend increased by 3%, contractual rent was up 3%, and portfolio market valuation increased by 1.8% to £924.7m.

Some of the gains may seem small, but Target has been consistent in its returns to shareholders, and according to chief executive Kenneth MacKenzie, it is this "boring but reliable" approach that is its USP, especially considering the ageing population its properties serve.

Green Street News spoke to MacKenzie and chief financial officer Gordon Bland.

What are the highlights of your results this week?

Kenneth MacKenzie (KM): I remember seven or eight years ago saying we just wanted to be a boring, long-income fund, which provides long, boring returns.

Fifteen years ago, a very senior person in property said to me: "Kenneth, it's not about what you do in the next year or two, it's what do you do over 10 and 15 years." The results show that we do do it over 10 or 15 years.

The best evidence is to compare us to all of the healthcare funds that MSCI tracks, and there's just under £10bn of assets in that – over the last 10 years we've been number two in that index, and over the last couple of years we've beaten the index average of just over 5%, by 5.5% one year and 5.4% this last year.

I think it's totally right that you don't just think about results over one or two years. It is all about 10 and 15 years. We had a private fund previously which over 12 years beat the index, and this fund is now 12 also years old, and we have given similar really long, stable returns. The way we go about this is, this is the way we think you wisely invest in care homes over the long term. We are quite unrepentant about this being the appropriate approach.

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>
> KENNETH MACKENZIE, TARGET HEALTHCARE

Various analysts flagged the quality of your portfolio – is that your USP?

KM: The quality of the assets, and the quality of the people choosing them. We have a view as the fund management house of how we do it which we feel robustly, and we get such important feedback from many people around us about being uniquely different.

It would be really easy to buy product at the wrong price and it'd be three times the size. The market wants massive scale, but our fear would be that it would not be at the sustainable rent levels that we think will provide long-term stable returns over the longer period. We are boring, cautious, people-centred.

What does the takeover of Care REIT this week say about your sector?

KM: The reality is that even some of the poorer stock is in demand, and is currently undervalued by the listed markets in the UK. If that goes on, there will be less and less of a listed market. We feel that what we are doing is the right thing to do and we're happy to stand on that, and we hope that in time the markets will recover.

Gordon Bland (GB): We've been disposing of assets for the last 12-18 months at and ahead of the book value, which I think is important. There is demand for our assets and they are priced appropriately. With the Care REIT portfolio, they're selling it all and they're not getting NAV for it. There's a clear differentiation in the quality of the assets.

Target-owned care home in Dartford

Why is it important that more than 70% of your income comes from privately funded tenants?

KM: We have 78% private pay. All of us know that the Labour government is going to have to cut welfare costs. We know that the NHS is under challenge. We know that social care is under challenge, so where do care homes get paid? And the over-65s, according to recent numbers, have £6tr of net worth. This sector only burns up £25bn, so you better be in the private pay place. A hundred years at £25bn uses up £2.5tr of the £6tr the over-65s have. So be in private pay, be in premium, and expect to get squeezed anywhere else.

> *"The boomers are not going to accept moving into a property that doesn't have a private en-suite wet room"*
>
> GORDON BLAND, TARGET HEALTHCARE

GB: The demand is going to keep rising. The boomers are not going to accept moving into a property that doesn't have a private en-suite wet room. They don't want to a shared bathroom. It's just not acceptable. Therefore the demand supports the profitability of our tenants and to the extent that national insurance and other costs go up, they can pass those on to residents to make sure that they are profitable and investing in their business the long term. The residents have the wealth to pay that.

That private fee chunk has outstripped inflation over the last five years and beyond, the local authority or public funded pay hasn't moved to the same extent and there are just going to be more challenges on that going forwards.

Are you continuing to be acquisitive? Are you also continuing to process out older or less appropriate stock?

GB: We'll continue to recycle capital to make sure our portfolio is getting better. We've got brand new assets in our pipeline to acquire, and also we have a disposal programme to keep churning the poorer end of our portfolio, which just allows us to keep making the portfolio better.