Four Seasons Health Care

Viability Analysis

Prepared by Impact Change Solutions

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Introduction

The West Midlands Joint Improvement Partnership Mobilising Community Capital Programme (MCC), delivered by Impact Change Solutions Ltd., has co-produced an approach to provider risk and viability as part of the market shaping work stream. The recent issues surrounding Southern Cross Healthcare have added extra impetus and focus to this area, and ADASS have requested that Impact Change Solutions apply the viability model developed as part of MCC to some of the bigger Southern Cross Landlords who have emerged as replacement providers. A first report on Four Seasons was produced in July 2011, and this revision is based on more recent financial statements and interviews with Four Seasons management.

Impact Change Solutions would like to thank the management team of Four Seasons for their open and honest approach to sharing information during the visit to their Head Office, and for the hospitality shown.

Executive Summary

Four Seasons has expanded rapidly from a small base, and in the mid to late 2000's took on a huge amount of debt as a result of private equity, and leveraged buyout deals. These were common at the time, but along with sale and lease back deals, they are now being questioned after the credit crunch and falling property values.

The latest published accounts for Four Seasons show an improvement in the overall financial position since the debt maturity extension in 2010. The revised level of debt (£755m) is still a risk, with a refinancing deadline of September 2012, but the risk is much reduced with a return to profitability after the 2009 financial restructuring and positive equity in the balance sheet.

The company recognises the risk of reducing fees in the sector due to the Coalition Government's public sector spending reduction plans. As well as a mature efficiency/cost reduction programme, the company is strategically moving to quality provision of high acuity care, which has an optimal profitability and steadier demand increase than more traditional residential care provision.

The Group accounts show a more positive viability after the 2010 debt maturity extension, with the caveat that the effect of the Care Principles purchase and the absorption of the ex Southern Cross homes have yet to be factored into a full set of published accounts. The effect of these is significant, with operational capacity growing 40% as a result.

Occupancy remains high at over 87% in the Care Home division, against current market trends. However this is an average occupancy rate and some regions are lower than this with the lowest occupancy region showing 76.5% at the time of writing this report.

The reduction of the company's debt from £1.5bn to £775m has undoubtedly lowered the financial risk and bolstered profitability and viability; however, it is still a key risk and is identified as such in the accounts. The company believes that the risk related to the debt is not expected to impact on the ongoing viability of the individual care homes.

Four Seasons now has a clear strategic position in order to cope with the reduction in fees from the public sector, and the risk rating could now be defined as medium rather than high. The major factors feeding into this rating of viability risk are:

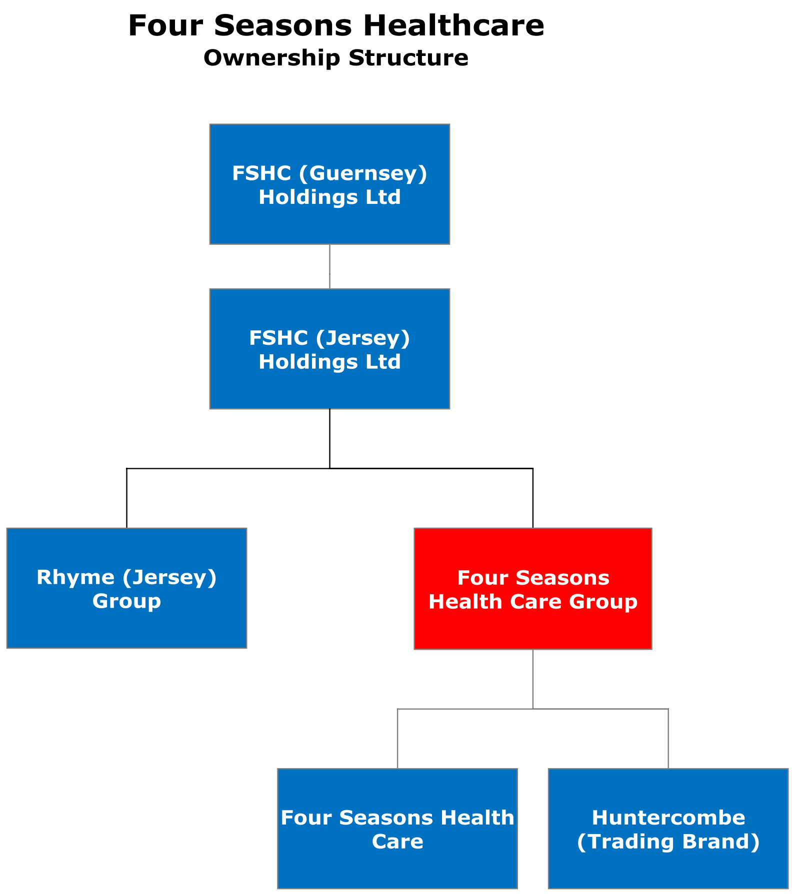
- the rapid growth of the company over a very short period of time (40%)

- the need to restructure the debt in the next few months
- identification of the long term intentions of owners/lenders

Four Seasons has robust strategic, investment and operational plans to deal with these risks, and ADASS, along with constituent Local Authority bodies, will want to continue an open dialogue with Four Seasons to shape the market and inform commissioning behaviours and decisions.

Four Seasons Health Care Structure and Operations

Four Seasons is part of a large and complex Group structure. The Care Homes operation, managed through the Four Seasons Health Care Group, delivers residential and nursing care, day care, domiciliary care and specialised care services; the group also includes a number of capital holding and property investment companies, under the Rhyme (Jersey) Group. The immediate parent company is FSHC (Jersey) Holdings Ltd and the ultimate group parent is FSHC (Guernsey) Holdings Ltd, a Guernsey-registered holding company.



Four Seasons was formed in the late 1980's and has expanded to its current size through both the acquisition and construction of care facilities. The company has a track record of buying out smaller chains of care homes and re-branding them as evidenced by the takeovers of Tamaris (formerly Quality Care Homes) and Bettercare. In 2010 it acquired a further 12 homes and 2 specialist units, and in 2011 it took ownership of the business operations of another specialist service provider, Care Principles, after securing CQC regulatory approval.

Acquisitions therefore continue to be a major part of the company's future plans and their aspiration to become the leading independent provider of quality healthcare services in the UK.

The group owns and operates over 500 Nursing and Care Homes and specialised Care Centres in England, Scotland, Northern Ireland, Jersey and the Isle of Man, with circa 24,500 beds. FSHC homes provide:

- Personal care
- Nursing care
- Dementia care
- Intermediate care
- Short-term respite care
- End of life palliative care

In addition there are a small number of specialist centres which offer dedicated care for alcohol related brain damage and for people with short and long term diagnosed mental illnesses, learning disabilities and physical disabilities.

FSHC also operates a Glasgow children's nursery, a North Yorkshire based Domiciliary Care service, a specialist day centre in South West London, retirement apartments in North Yorkshire and Jersey, retirement villages in Scotland, Northern Ireland and the Isle of Man.

Under the Huntercombe brand the Group provides specialised care for people with mental disorders, learning disabilities, acquired brain injury or physical neuro disabilities and care for children and adolescents with special mental health needs. Huntercombe operates from over 50 hospitals and specialised care centres throughout England and Scotland with around 1,200 beds (including recent acquisitions).

The Group operates 2 defined contribution pension schemes for certain of its UK and Isle of Man employees, with pension fund assets held and administered separately from those of the Group.

Financial Background and Issues

Beginnings and expansion

Four Seasons started out as a small healthcare operator working only in Scotland. The business underwent an acquisition programme that saw Four Seasons become one of the biggest care home operators in the UK. The business was an attractive proposition for many prospective purchasers, and was eventually sold for £775m in 2004.

Purchase by Three Delta - leveraged buyout

The 2004 purchase of Four Seasons saw Alliance Capital Partners pay £775m to Alchemy, the venture capital specialist run by John Moulton. Alchemy had supplied the finance that had enabled the previous aggressive acquisition programme.

In 2006, 2 years later, Alliance Capital Partners sold Four Seasons to finance group Three Delta for £1.4bn, almost twice the value of the 2004 sale. It is important to note that these sales, much like the sale of Southern Cross to Blackstone, represent the removal of 'value' from the system when the seller in effect 'cashes in'. At this point in time, Three Delta was acting on behalf of the State of Qatar and its sovereign wealth fund.

Analysing the purchase, although the Qatari government had invested in the company, the remainder was funded with debt. In a complex deal, the entire loan of £1.2bn was provided by Credit Suisse, with a special purpose company, Titan Europe 'securitising' the loan (i.e. selling it on to investors in the form of bonds, notes etc.). Additionally, outside of the Titan package there were 2 Pay in Kind (PIK) notes of £165m (from the Royal Bank of Scotland) and £60m – these are short term loans where instead of interest being paid, the total amount of debt accrues quickly before being repaid.

The financing deal had a 2 year life span, and by the time it was due to be refinanced, the 'credit crunch' had hit. Property values were falling, and wholesale credit markets had ground to a halt. At the same time, Four Seasons care homes operations, whilst maintaining historic profit levels, were not displaying the incremental profit that had been factored into the sale price, on average failing to achieve all of the last 10-15% occupancy that provides the greatest margin. As a result, the business was in a position where it was breaching its banking covenants. In April 2008, RBS started demanding that Three Delta invest hundreds of millions of pounds back into the business, while hedge funds started buying Four Seasons debt at a discounted rate, hoping to make a quick profit. To make matters worse, the hedge funds banded together with some of the financial institutions with a stake in the company in order to be represented by Houlihan Lokey - a company with a reputation for playing hardball in debt negotiations.

Debt for Equity swap – RBS take a major stake

Due to the protracted restructuring discussions with the Group's lenders and option to sell the company was considered as a solution. By December 2009 the debt had risen to £1.55bn, partly because losses were being capitalised (i.e. funded by further borrowing rather than revenue), more than the original purchase price. Eventually a deal was agreed whereby Four Seasons' £1.55bn debt was reduced to c£780m, in exchange for certain lenders converting their debt to equity in the company, with RBS receiving a stake of c.38%. At this point in time, Three Delta surrendered their equity stake in Four Seasons, effectively writing off their £100m investment and walking away from the deal. This was a short term deal that allowed breathing space in order to conduct further restructuring in 2010. It should be noted however that the care home operations of the Group were not impacted by the protracted restructuring discussions.

2010 – Debt maturity extension

In 2010, Four Seasons was forced back into talks with bondholders of the remaining £600m Titan debt in the Group. Negotiations were complicated by the fact that a group of bondholders, largely made up of the distressed debt hedge funds referred to above, were insisting on repayment, despite offers of a significant increase in interest on the notes.

In a deal that is seen as innovative, the note maturity date was extended to September 2012 by a majority vote.

The latest accounts (2010) show that FSHC (Guernsey) Holdings Ltd have a consolidated group debt of £775m, reduced from £788m in 2009. The company is also managing its interest rate risk through the use of interest rate swaps, which effectively fix £595.3m of the debt at a lower rate of interest, making the interest payments more affordable on an ongoing basis. The interest rate swap deal ends in September 2012, on the same date that the notes are due to be repaid.

2011 – Southern Cross Collapse

Southern Cross announced that it was entering into a solvent wind down process in July 2011 after negotiations to reduce rents with Landlords had collapsed. Four Seasons were a major Southern Cross Landlord, owning 45 of the former Southern Cross Homes, and were therefore one of the leading stakeholders.

As part of the wind down, Four Seasons have become the operator of the former Southern Cross properties, bringing the 45 owned homes back into its freehold portfolio. They also took the opportunity to take operational responsibility for a number of other homes on a leasehold basis. In total, 139 homes were transferred to Four Seasons due to the demise of Southern Cross.

Financial projections for the new operations are positive, with an estimated contribution of £10m to EBITDA (Earnings Before Interest, Taxation, Depreciation and Amortisation). There were some concerns in the sector that operating care homes from leasehold properties may replicate the Southern Cross business model, but the company has negotiated downside protection into most of the property rents, avoiding the punitive increases that caused Southern Cross to collapse. In addition, the fact that the Group owns some 60% of its operational care homes on a freehold basis further mitigates the risk.

Absorbing 139 operating units would be a shock to the system for any organisation in the sector, and Four Seasons has change plans in place. Specifically, there is a focus on bringing the transferred homes up to Four Seasons' own quality standards and instilling a Four Seasons ethos and culture amongst its new employees. The Group set aside £7m to address any infrastructure investment at the ex Southern Cross units. Operational teams have been asked to deploy this amount as quickly as required in order to drive the turn around. In addition, Four Seasons intends to spend (on average) £900 per ex-Southern Cross bed (consistent with the rest of the FSHC group) per annum going forward. The management team believes that this amount is materially above the market average of c.£600-700 per bed, and is appropriate to protect the group's philosophy of driving quality of care and service.

In order to manage the integration/turn around, Four Seasons have scaled up their regional and central support teams. For example, the company has moved from 10 homes per Regional Manager to 8 homes per Regional Manager. In contrast, Southern Cross operated at a ratio of 25 homes per Regional Manager. The additional support also extends to essential support services such as HR, H&S, Estates, Training, Quality assurance etc. Together with the Care Principles acquisition, the resultant incremental costs are significantly more than a pro-rata increase given the increase in the number of homes/specialised units that Four Seasons now operate – a c.40% increase in the number of homes has seen a c.45% increase in regional and central support costs which management believe is necessary to bring these operations up to the Four Seasons quality standard. The company believes this is money well spent to ensure the efficient turn around in the ex-Southern Cross homes and to implement the Four Seasons' policies and procedures as quickly as possible - once the turnaround is complete there is scope to relax the ratio and therefore costs to historic levels if deemed appropriate at that time.

Strategically, Four Seasons have positioned themselves as providing high acuity care, and the transfer of more 'traditional' residential services from Southern Cross provides opportunity for transformation and re-provision of these services.

2012 – Debt Maturity

2012 is a key year for Four Seasons, and they will be working with their debt servicing agent (Hatfield Philips) as the maturity date of the Group's debt approaches in September. The 2012 position is different from the 2009 position in that the company has returned to positive equity. A recent revaluation shows that the Group's properties are worth c£940m, while the debt position has been managed down to £775m as stated above. This is in stark contrast to 2009 where the £1.55bn debt was in excess of asset values and equity.

The company is confident that it can successfully refinance its debt in 2012, and has a number of scenarios based around various options. Financially, the focus is on EBITDA and the contribution that is being made by operations.

EBITDA is essentially net earnings with interest, taxes, depreciation, and amortisation added back to it, and can be used to analyse and compare profitability between companies and industries because it eliminates the effects of financing and accounting decisions. EBITDA is a good metric to evaluate profitability, but not cash flow. EBITDA also leaves out the cash required to fund working capital and the replacement of old equipment, which can be significant.

By focussing on EBITDA, the effect of capital financing is essentially ignored, and this is in tune with the company's confidence that the operation is generating cash and profitability at a level that allows them to invest in quality and service the debt.

The debt is still a risk, but lower than it was in 2009 when essentially the company stopped paying all of its interest. In the short to medium term, the risk is being actively managed, made easier by a return to profitability and cash generation at group level.

In the longer term as the company returns to profitability and creates retained earnings at group level, the tolerance of the lenders and owners for accepting the debt in future market conditions and their plans for either holding the debt or selling on/refinancing will dictate refinancing options and financial strategy.

Financial Performance

This analysis is primarily concerned with the ultimate parent, FSHC (Guernsey) Holdings Ltd ('the Group') as reported in the consolidated statutory accounts for 31st December 2010. Group performance reflects the contributions of the care home operation Four Seasons Health Care Ltd ('the Company') and the property operation Rhyme (Jersey) Ltd ('the PropCo').

Consolidated accounts strip out inter-group transactions, which can have a distorting effect on the performance of individual companies. For example, the Company made rent payments for the care homes it runs totalling £98m in 2010 although this includes some £70m paid over to the PropCo in respect of freehold properties owned within the Group. Group accounts discount the effects of these transactions as there is a net neutral contribution to the Group performance.

Whilst it is important to understand the performance at Company level (since this provides an indication of the viability of the Company as a standalone enterprise) it is more appropriate to consider Group viability. Comments on the performance of the Company and the PropCo are, however, included where appropriate to add context.

Financial performance is measured in 4 domains: liquidity, solvency, efficiency and profitability.

Liquidity

Liquidity considers the ability to meet current liabilities from current assets and is identified by the Directors as one of the principal financial risks facing the Group.

In 2010 Group current liabilities (£106.5m) exceeded current assets (£83.9m) by £22.6m and this implies a risk of inadequate working capital. However, cash balances (£53.3m) are relatively high and the care home operation generates large amounts of cash. This should enable the company to meet debts as they fall due. Debtors are well spread and with 80% of fee income generated from Local Authority and NHS commissioned beds, the risk of bad debts is low. In this context, servicing short term liabilities is unlikely to be problematic while bed occupancy remains high.

Efficiency

Analysis of the Company accounts shows that there are no significant issues arising from either debt collection or creditor payment terms. Debt collection is well controlled, with monies owed being collected in under 15 days on average. This is somewhat to be expected from a turnover that is largely generated by publicly commissioned medium to long term occupancy beds, with LA and Health commissioners paying on regular monthly payment schedules.

Long term debtors (outstanding for longer than 90 days) stand at around £1.5m, which at less than 10% of the December 2010 trade debtors, appears well managed. Group variable costs (excluding depreciation, amortisation of goodwill and rent) were 69.6% of turnover in 2010 (up from 69% in 2009*)* and in the context of rising utilities costs and general price inflation, continue to be satisfactorily controlled.

Solvency

In December 2010 the Group had fixed assets valued at £829m, net current liabilities of £22.6m, borrowings of £775m and other long term liabilities of £23.7m, leaving shareholders' funds of £7.4m (up from just £766k in 2009). On this basis, Gearing (the proportion of the Group's assets that are financed by long-term borrowing) remains high at 99% and while Group solvency can be seen to have improved in 2010, this would be reversed by a decline in profits or a reduction in asset values (or both). Both factors – profitability and asset values – are therefore likely to be a key consideration in the ongoing negotiations between Four Seasons and its lenders on debt refinancing.

The Group's principal assets remain its operational and investment property portfolio, valued in the December 2010 accounts at £892m.

The refinancing of group borrowings is recognised as one of the principal financial risks for the Group. The two-year extension to the maturity date of the debt negotiated in 2010 expires in September 2012 and the Directors continue to meet regularly with the Group's lenders to report on financial performance and lending covenants. They report that they have a good relationship with their lenders and fully expect a further refinancing package to be in place before September 2012. However, even if this does not transpire as anticipated, the Directors are confident that the Company would be able to continue to operate as it would not be in the financial interests of its lenders to foreclose operations. Ongoing cash receipts are demonstrably servicing the debt and generating a return for lenders in the form of interest payments. Lenders are unlikely to jeopardise these returns by demanding immediate repayment.

Profitability

Group turnover of £503.6m in 2010 was principally derived from the Company (£488.1m), with the PropCo generating £15.5m from its property investment operations. After operating costs this resulted in Group earnings before exceptional items, interest & tax (EBIT) of £79.5m – a return on capital employed (ROCE) of 9.9%. Discounting the effects of depreciation and amortisation of goodwill, EBITDA of £99.5m has been achieved, in line with Group performance targets.

Profits have been achieved despite fee decreases of c.4% on NHS commissioned beds and of 0.4% on LA commissioned beds; general price inflation and exceptional rises in food, heating and lighting costs have been seen, and wage increases of 2.25% for those earning the National Minimum Wage.

Occupancy levels are a key factor in turnover and hence profit. Across the sector, operators report that most of the margin is made at the last 10-15% of occupancy, as at the higher end, variable overheads do not increase proportionately. On an average basis across the group, each extra 100 residents will contribute £1.7m to EBITDA. Currently its care homes are operating at an average occupancy of over 87%. Whilst there are substantial local and regional variations in the levels of occupancy, management effort is focussed on increasing occupancy across the whole of the estate and the average figure reported here reflects year-on-year growth since 2006. The renegotiation of debt maturity in 2010 resulted in the waiver of some £18.3m in debt and this had the effect of reducing the net interest charge for the Group to £33.4m. The refinancing deal included an element of interest rate 'hedging' with various loans attracting interest at marginal rates linked to LIBOR, and this hedging arrangement provides a degree of protection against fluctuating interest rates.

The tax charge for 2010 amounted to £9.8m. Underlying this figure are a number of taxable effects. For example, significant non-deductible costs (£35.3m) are partially offset by the utilisation of tax losses from across the Group structure (£21.6m).

As a result the Group produced retained profits of £6.6m (after net exceptional items of £11.3m) and saw its net asset value rise to £7.4m. No dividend was paid to shareholders.

Ongoing profitability is identified as a principal operational risk for the Group, with the Directors recognising the potential for fee increases to fall behind the rising costs of care. The Company considers that it is protected from this risk to a degree by the nature of its business model (with a focus on high acuity care), on the quality of its offer (see Quality below) and by its flexible approach to fees (where high occupancy levels provide the basis for price negotiations with LA and NHS commissioners).

The impact of the acquisition of former Southern Cross homes is not reflected in these accounts and the Directors have recognised both the risk and the potential that is inherent in this new addition to their portfolio. In the short-term, support and operations capacity has been bolstered to allow for integration and turnaround activities, and this will have an effect on operating costs. However, the Directors forecast a positive contribution to Group profits from the former Southern Cross homes, particularly as they move from traditional residential care to high acuity care over time. The group also reports a c0.75% occupancy uplift in ex Southern Cross homes in the first 12 weeks at a time when occupancy is typically seen to dip.

Other Factors

Quality

The Group has a strong focus on Quality, both in terms of its service offering and its asset base.

FSHC has defined and published its service standards and 'aims to involve and inform all our residents, in all our homes, all of the time about the care and services we deliver'.

Four Seasons state that they 'listen to the comments of others including our regulators and those that receive our services and act accordingly to continually improve the service we give'. They do this through frequent inspection, quarterly residents' surveys and through their daily interaction with residents and their families.

FSHC operate a formal complaints system, encouraging local resolution but offering both line management and regional management escalation. Service standards for complaints are in place and well embedded.

The Group operates a structured quality assurance framework that involves frequent auditing of each home. Audits consider a range of factors including care outcomes, clinical standards, administration of medication, personal care plans, administrative processes, service user feedback and, in the case of dementia sufferers, measures of personal happiness. Audits also consider the care home environment.

Quality and compliance exceptions are escalated through regional management structures, with the most serious concerns added to a 'watch list' and discussed at Operational Board and Senior Management Team meetings monthly. Action plans are created and monitored until issues are resolved, either through training or, in the case of infrastructure failings, through capital investment.

The Company has introduced e-Learning into all of its homes as a means of providing focus on corporate priorities and giving staff access to high quality training. Since its introduction 18 months ago, over 350,000 courses have been fulfilled by over 27,000 staff members. The Directors report that there has been a reduction in the number of incidents and complaints since e-Learning was introduced.

Quality is also driven through the PEARL quality accreditation programme within its specialised dementia care facilities. The programme was developed in January 2008 and rolled out in 2009 to help homes work towards a number of set criteria to ensure that they are providing the most up to date training, communication and interventions for residents with dementia. The criteria follows the VIPS framework (Brooker, 2007) and addresses four main themes of person centred care:

- Valuing - A value base that asserts the absolute value of all human lives regardless of age or cognitive ability
- Individual - an individualized approach, recognising uniqueness
- Perspective - understanding the world from the perspective of the service user
- Supportive psychology providing a social environment that supports psychological needs

The Directors report an overall improvement in the dignity and wellbeing of residents, positive benefits for staff and improvements in the working culture since PEARL was introduced. Success measures include reductions in drug use, increased uptake in creative activities, a reduction in distress reactions amongst residents and a general increase in wellbeing.

The Group invests in excess of £20 million per annum in the quality of its homes and has committed £22m during 2012. This equates to around £900 per bed, which compares to an industry average (based on FSHC market analysis) of £600 - £700 per bed. They report that they are one of the highest quality rated providers in the independent sector, with 88% of homes in England rated Good or Excellent by CQC (against a sector average of around 84%) and enjoy above sector average occupancy rates (over c87% for FSHC and c.75% for Huntercombe facilities). They regard quality as a key driver for improved occupancy and manage their operations accordingly.

The Directors acknowledge that there will always be local examples of low quality provision but have put in place the structures to identify, address and improve underperformance in a timely manner. They report that at any one time there may be 10 – 20 homes on the 'watch list'. There are currently 17, but this is larger than usual due to the recent acquisition of Southern Cross homes. Most of these issues are addressed although the Group has on average closed one home each year because of quality and performance issues and this provides further evidence of their commitment to high quality care.

Personalisation

The Group has diversified its service model in recognition of the government's vision for adult social care and NHS reforms. Whilst predominantly a residential and specialist nursing care provider, it does offer a diverse range of domiciliary and private services, although these are concentrated in a small number of locations rather than being offered across their whole operation.

Its care homes have embraced the principles and philosophy of person centred care. Each resident has a personal care plan and is assigned a key worker whose role is to ensure the appropriate level of care is provided. Care plans are regularly reviewed to make sure needs continue to be met. Residents, and where appropriate their families, are involved and encouraged as far as is practical in the decisions regarding their care and their living environment.

Market Shaping

The Group recognises that commissioning policy continues to move towards home based care services rather than traditional residential care for lower dependency clients who would previously have typically been admitted in to residential care settings. There is an acknowledgement that this is driven by user needs and choice, with forecast demographic change causing an increase in the demand for both residential and domiciliary care services and an increasing strain on the public purse.

The group has a history of partnering with the NHS in a number of areas where they have expertise, particularly providing specialist care and out-of-hospital care in patients' homes and in their own care homes. The Group's care homes and specialist homes primarily cater for higher acuity needs and their provision in this area accounts for approximately 79% of the total bed capacity. The Directors forecast that demand for this type of provision will grow and feel that the Company is well placed to meet this demand.

The Group also recognises the competitive nature of the residential care market and sees its competitive advantage as being its market leading position, high quality asset base, high quality services and focus on high acuity care. It has successfully grown occupancy levels in both care homes and specialist care provision, against market trends, and is comfortable negotiating discounted fees where high occupancy is being achieved.

Four Seasons has piloted approaches to hospital admissions avoidance and to facilitating early discharge from hospital, offering intermediate care facilities in a number of locations. Models include post-discharge rehabilitation, palliative support and respite care and an 'acute community facility'. It sees these facilities as being part of the future supply of community care services and is keen to develop the model in partnership with LA and NHS commissioners.

There is a commitment to building strong and open relationships with both LA and NHS commissioners at the local level and to continue to strengthen relationships with national bodies (DH, ADASS). The Directors see this as a 'two way street' and hope for more productive engagement in the future. They are contributing to the ADASS-supported review of 'Fair Costs of Care' and would be keen to explore the links between Viability and Fair Costs of Care once this work is complete.

Conclusions

Four Seasons overall financial position as a group has improved during 2010 and 2011.

The 2009 debt for equity deal has provided a return to profitability, and a recent valuation of assets has shown that the company is back in positive equity (i.e. the value of the fixed assets are greater than the long term loans attached to them).

The Company has absorbed 139 care homes from the wind down of Southern Cross. The transferred homes are projected to make a positive contribution to profits (EBITDA), but there will be a requirement for short term investment in the new estate to bring it up to standard. Along with the Care Principles purchase, this has meant that the group has grown by 40% in a short space of time, and until a published set of accounts and quality metrics are available, this remains as a risk. The company believes that the probability of this risk materialising is low, and that it is unlikely to impact on the day to day operations or the care of residents.

Four Seasons own c60% of the properties they operate (a materially different model to the Southern Cross leasehold model) and are therefore much less affected by increases in RPI which may affect rents.

Four Seasons is aware of spending cuts within the sector, and has differentiated based on a quality offering of high acuity care as well as implementing a mature efficiency programme 'the Fundamental Review' to keep costs down. Success is being reflected in occupancy rate increases, which appear to be bucking market trends.

The Group has a strong focus on quality, and actively invests in quality. They see this as a key differentiator in an increasingly competitive market.

The level of debt and the need to refinance in September 2012 is still a risk. However, given the return to profitability and positive equity, this is now a much reduced risk in the short to medium term. The longer term prospects will depend on how the lenders and owners of the company react to a more positive financial outlook and how they intend to recoup their return on investment.

Disclaimer

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Appendix A – FSHC (Guernsey) Holdings Ltd Consolidated Accounts:

Balance Sheet Extract

Balance Sheet Extract			
	Notes	31/12/2010	31/12/2009
		£000	£000
Tangible Fixed Assets	1	764,628	747,872
Investment Properties		127,675	146,080
Intangible Fixed Assets - Goodwill	2	-63,418	-65,933
Total fixed assets		**828,885**	**828,019**
Trade Debtors		15,726	20,124
Prepayments, other debtors & accrued income		14,913	19,160
Cash & Bank		53,261	75,075
Total Current Assets		**83,900**	**114,359**
Total Assets		**912,785**	**942,378**
Bank Loans	3	0	787,689
Creditors & Accruals		64,126	79,753
Taxation owed		23,974	21,307
Monies owed to related parties		18,368	14,817
Total Current Liabilities		**106,468**	**903,566**
Net Current Assets		**-22,568**	**-789,207**
Total Assets less Current Liabilities		**806,317**	**38,812**
Creditors: amounts falling due >1year (bank loans)	3	775,190	0
Provisions for liabilities & charges	4	23,721	38,046
Net Assets		**7,406**	**766**
Called up share capital		0	0
P&L Account		7,406	766
Shareholders Funds		**7,406**	**766**

Appendix B – FSHC (Guernsey) Holdings Ltd Consolidated Accounts:

Profit & Loss Account Extract

P&L Account Extract		31/12/2010
Turnover	5	**503,617**
Depreciation		-23,387
Amortisation of Goodwill		3,364
Rental charges		-28,901
Other variable costs		-350,721
Cost of Sales		**-399,645**
Gross Profit		**103,972**
Admin Expenses - ordinary		-24,501
Other operating income		
Operating profit		**79,471**
Admin expenses - exceptional	6	-29,600
Profit /Loss on sale of assets		
Net Profit before Interest & Tax (PBIT)		**49,871**
Interest payable		-51,719
Interest payable - exceptional		
Interest Receivable		23
Waiver of debt and debt-like items - exceptional	7	18,318
Net interest		**-33,378**
Profit Before Tax		**16,493**
Tax on Profit / Loss	8	-9,853
Tax on Profit / Loss - exceptional		
Total Tax on Profit/Loss		**-9,853**
Retained Profit / Loss		**6,640**

Appendix C – FSHC (Guernsey) Holdings Ltd Consolidated Accounts:

Notes

Notes	Commentary
1	After depreciation. Includes land & buildings £700.4m, Buildings under construction £0.8m, equipment & fixtures £61.9m and vehicles £1.6m.
2	Negative goodwill of £66.1m arose on change of ownership of the Group in 2009. Other smaller amounts of goodwill - both positive and negative - are included in the total, which also reflects the effects of amortisation (a net credit of £3.4m) during the year.
3	The effect of debt restructuring in Sept 2010 is to reclassify debt and accrued interest "due within 1 year" at 31 Dec 2009 as "falling due after >1 year" in Dec 2010.
4	Comprises deferred taxation £5.1m and provisions for onerous contracts £18.6m. Such provisions are typically released to P&L over the life of the relevant contracts although £15.3m has been utilised in 2010 (down from £32.9m in 2009).
5	Turnover from the Care Home operation was £488.1m and Property Leasing contributed a further £15.5m.
6	Includes exceptional costs of £25.1m relating to the extension of the group's debt facilities , £1.5m relating to the impairment of property, £0.7m from the aborted sale of investment properties and £1.6m relating to closed homes and redundancy costs.
7	An exceptional credit of £18.3m arose from the waiver by lenders of debt and debt-like items on renegotiation of the Group's lending facilities.
8	Tax on profits was £4.6m; a further £35.3m liability arose in respect of costs not deductible for tax purposes; tax losses across the group reduced the liability by £21.6m; a further reduction of £8.1m arose because of differences in overseas tax rates.

Appendix D – FSHC (Guernsey) Holdings Ltd Consolidated Accounts:

Key Ratios

				Dec-10
Liquidity	Current Ratio	Current assets/current liabilities	Ratio:1	0.8
Efficiency	Cost/Income %	Variable costs excluding depreciation, amortisation and rent/turnover x100	%	69.6
	Average collection period in days	(Average trade debtors / average turnover) x365	Days	13.0
Solvency	Gearing	Total Borrowing / Equity (or funds) + long term borrowing x100	%	99.1
Profitability	Retained Profit (Net Operating Profit After Tax - NOPAT)	Net addition / (reduction) to Shareholders' Funds	£	£6.6m
	Profit Before Tax (PBT)	NOPAT + net tax charge	£	£16.5m
	Net Profit %	PBT / Turnover x100	%	3.3
	Adjusted PBT	PBT before exceptional items	£	£27.8m
	Adjusted Net Profit %	Adjusted PBT / Turnover x100	%	5.5
	Net Earnings	NOPAT before exceptional items	£	£17.9m
	Earnings before interest & tax (EBIT)	Net earnings + interest + tax	£	£79.5m
	Earnings before interest, tax, depreciation & amortisation (EBITDA)	EBIT + Depreciation + amortisation of goodwill	£	£99.5m
	Return on Capital Employed (ROCE)	EBIT / (Total Assets - Current Liabilities) x100	%	9.9