OakNorth Sector Pulse
June 2025

CARE

OakNorth

Industry overview

The UK care home and retirement living sector has navigated an increasingly challenging landscape in the first half of 2025, marked by intensifying financial, workforce, and regulatory pressures. Persistent underfunding remains a critical issue, with Care England estimating a £2.2bn shortfall for residential care.

Workforce shortages in the sector have deepened over the last six months, and are likely to exacerbate further this year following the Government's announcement in May that care workers will no longer be recruited from overseas as part of a crackdown on visas for lower-skilled workers. Instead care businesses will be expected to hire British nationals or extend visas of overseas workers already in the country. With over 131,000 vacancies - triple the UK average - providers are struggling to fill roles, especially amid surging payroll costs following increases to the National Living Wage and employer National Insurance Contributions, which came into effect in April.

Despite these headwinds, strong underlying demand has supported occupancy rates above 88%, with average fees rising nearly 10% year-on-year. Local authority and NHS funding uplifts (6.1–7.4%) have provided some relief, though they remain insufficient to close the widening financial gap.

The investment climate has been notably active, underscored by large-scale M&A deals in May, including: CareTrust REIT's £448mn acquisition of Care REIT plc, and Omega Healthcare's £260mn purchase of 45 care homes. Consolidation continues as well-capitalised investors pursue platform strategies to scale in a fragmented market.

Key trends of the last six months

Financial strain amid rising costs

In the first half of 2025, UK care home operators faced escalating financial pressures. Staffing costs surged due to a 6.7% increase in the National Living Wage, the rise in employer National Insurance contributions from 13.8% to 15%, and the lowering of the earnings threshold to £5,000 - all of which came into effect in April. These changes, combined with soaring utility bills and commercial water rate hikes of up to 50%, have disproportionately impacted smaller providers already operating on thin margins.

50%

sharp cost surge amid wage increases, higher national insurance, and lower earnings threshold

Persistent workforce shortages

Workforce challenges have intensified due to restrictive immigration reforms. An 81% drop in overseas care worker visas, coupled with the closure of the care worker visa route and stricter eligibility thresholds, has led to significant recruitment gaps. The Department of Health & Social Care's April 2025 workforce survey revealed that 71% of adult social care providers find recruitment challenging, with 37% expressing concerns about sustaining service levels over the next six months. Better pay in other sectors was cited as a primary factor affecting both recruitment and retention.

81%

drop in overseas care worker visas, and 71% of providers report recruitment challenges, 37% fear they can't sustain services

Investor confidence and consolidation

Despite operational headwinds, the sector has attracted strong investor interest. Deal activity continues to favour platform-based acquisitions, with real estate investment trusts and private equity backing experienced operators to drive scale and efficiency. According to Cushman & Wakefield's Q1 2025 MarketBeat report, US investors accounted for over 68% of the £531mn invested in the UK elderly care market during the first quarter. This trend underscores growing international confidence in the sector's long-term prospects.

68%

of £531mn invested in UK elderly care in Q1 2025 from US investors—driven by platform deals and private equity backing

Regulatory pressure and development slowdown

Development has slowed sharply amid new regulatory requirements - such as mandatory sprinklers and enhanced energy efficiency standards - and severe planning delays. Planning approvals remain at a 45-year low, while high construction costs and labour shortages further constrain new projects. This stunted pipeline, combined with rising demand, signals an urgent need for policy and funding reform to ensure sustainable sector growth.

45-year

low in planning approvals, rising costs, and labour shortages are stalling new care projects

> **The UK care home sector is facing undeniable headwinds - from acute staffing shortages and mounting cost pressures to planning delays and tightening regulations. With delayed discharges from hospitals and rising dementia cases driving demand, the sector faces a critical juncture - balancing urgent capacity expansion with pressing financial and regulatory constraints. Yet, these challenges are driving much-needed innovation and consolidation across the market. We're seeing well-capitalised operators adapt by modernising facilities, embracing sustainability, and enhancing care quality to remain competitive. At the same time, strong underlying demand - fuelled by an ageing population and rising occupancy levels - continues to make the sector an attractive long-term opportunity. Operators that can demonstrate resilient trade performance, regulatory compliance, and a clear growth strategy are well-positioned to thrive. With strategic investment, policy reform, and smarter delivery models, we believe the sector can emerge stronger, more efficient, and better equipped to meet the needs of future generations."**
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> Ben Barbanel
> Head of Debt Finance at OakNorth

Outlook for the next six months

Cautious optimism in capital markets

While the recent rise in inflation to 3.5% (from 2.6% in March) may slow the pace of Bank of England rate cuts, investors remain cautiously optimistic. A more supportive macroeconomic outlook and strong underlying demand continue to drive interest, especially from equity-backed investors seeking resilient, long-term income. Rental growth is expected to persist, bolstered by high occupancy and trade performance, helping offset operating cost inflation and maintain sustainable rent cover ratios.

3.5%

inflation may slow the pace of rate cuts, yet robust demand and high occupancy are sustaining rental growth and investor confidence

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Sustainability pressures and retrofit imperatives

With the 2027 energy performance deadline approaching, care home operators face growing pressure to upgrade assets. Around 70% of the sector's stock will require retrofitting to meet the EPC B target by 2030. Rising energy and utility costs will accelerate the push for efficiency, but capital constraints - especially among smaller providers - may limit action. Funding access and government support will be crucial to unlock these upgrades.

70%

of care homes need retrofitting to meet EPC B by 2030—rising energy costs add pressure, but funding support is vital

Closures and capacity risk remain high

The risk of closures remains elevated. With 39% of providers reportedly considering exiting the market and past closures already displacing 20,000 residents, further financial strain could trigger additional capacity losses in the latter half of the year. Operating costs, particularly payroll and utilities, are likely to remain high, and systemic underfunding remains unresolved.

39%

of providers are considering exiting the market; 20,000 residents already displaced

Policy reform could be a turning point

The next six months may bring clarity on long-awaited planning and regulatory reforms. Updates under the Levelling-Up and Regeneration Act and potential expansion of the Temporary Shortage List could provide relief on labour shortages and development bottlenecks. However, outcomes will depend on execution and local authority uptake. If reforms are effectively implemented, they could mark a critical turning point - unlocking capacity, boosting investor confidence, and supporting sustainable sector growth.

6-months

may be pivotal, planning and labour reforms may ease bottlenecks and unlock growth

Pension Reforms and 'Megafunds'

The UK government has announced plans to consolidate defined contribution pension schemes into large-scale "megafunds" managing at least £25bn by 2030. This initiative aims to enhance investment returns and reduce charges, potentially adding an estimated £6,000 to the average pension pot. If successful, this could materially improve retirees' financial flexibility, enabling more people to afford higher-quality retirement living options or upgrade from basic care settings. It could also broaden the customer base for mid-market and premium Integrated Retirement Communities (IRCs), particularly rental and part-ownership models. In time, these "megafunds" could become major investors in healthcare, social infrastructure, and retirement housing. This could attract long-term patient capital into the elderly care sector, and increase funding for new developments, especially in underserved regions or in sustainable, energy-efficient stock.

£25bn

megafunds by 2030 could boost pensions by £6k and unlock demand for premium retirement living while attracting long-term investment into care infrastructure

Get in touch with the team at questions@oaknorth.co.uk or visit oaknorth.co.uk for more information.