ProMedica Health System

Municipal Bond Research

Rating: Appropriate for Aggressive Income

Investment Classifications

Investment Category: Aggressive Income

Sector: Health Care

Recommended Sector Weight: 0% - 5%

Entity Description

ProMedica is a not-for-profit health system based in Toledo, Ohio, that operates 11 hospitals in Ohio and Michigan; 332 skilled-nursing, assisted-living, hospice and rehabilitation facilities in 28 states; a health insurance company (Paramount) with 88,000 members; and a dental plan (Health Resources) with 300,000 members.

Related Bonds

Lucas County Ohio Hospital Revenue

Credit Ratings

Moody's	Ba2 / Negative
S&P	BB / Negative
Fitch	BB+ / Negative

Analyst: Brian Therien, CFA

INVESTMENT SUMMARY

We rate ProMedica Health System bonds as Appropriate for Aggressive Income. ProMedica's finances have worsened in recent years, driven by debt taken on to acquire and lease a system of skilled-nursing and assisted-living facilities, lower occupancy in these facilities due to COVID-19, and higher expenses. Occupancy has begun to recover in recent quarters, which we expect to drive improved financial performance, as this trend likely will continue over the next few years. ProMedica's market leadership position in a concentrated hospital market and diverse revenue sources should also help to stabilize its operations.

BOND OVERVIEW

Financial performance has declined. Key drivers of weaker performance have been lower occupancy rates at its skilled-nursing and assisted-living facilities, along with higher expenses. Occupancy rates in these types of facilities have declined for many issuers due to health concerns related to COVID-19. Higher expenses are the result of inflation and a shortage of nurses and other health professionals. Occupancy has begun to recover in recent quarters, which we expect to drive improved financial performance, as this trend likely will continue over the next few years.

Significant debt load reduces cushion to pay interest and principal from cash flow. ProMedica increased its debt load to $2.3 billion to fund the acquisition of skilled-nursing and assisted-living provider HCR ManorCare out of bankruptcy in 2018. It also entered into $2.6 billion of leases related to these facilities. This large debt load and these lease obligations reduce the cushion to pay principal and interest on its bonds from available cash flow.

Insurance business removed from Ohio Medicaid program. ProMedica's insurance business - branded Paramount - was not renewed as an Ohio Medicaid provider in 2022. The Medicaid business has been sold to Anthem, which will reduce revenues from this segment.

Market leadership position in concentrated hospital market can provide pricing power. ProMedica is the inpatient market leader in northwest Ohio and southeast Michigan, with a 43% market share. The No. 2 inpatient provider has a 36% share; the No. 3 provider has a 9% share, and the No. 4 provider has an 8% share. A concentrated market structure like this is typically favorable for providers, as competition can be less intense, potentially improving pricing power.

Diverse revenues should help stabilize performance. ProMedica generates revenues from multiple sources, including hospitals, health and dental insurance, skilled nursing, assisted living, hospice, home health, and rehabilitation. This diversification should help stabilize performance while occupancy recovers.

Valuation - Valuation is based on our analysis of yields relative to bonds of comparable quality and potential recovery in the event of a payment default.

Risks - Primary downside risks include the possibility that ProMedica's market position could decline and recovery of the senior care business could be delayed or not fully achieved, which could drive credit ratings and bond prices lower. Upside risks include the possibility that ProMedica's senior care business could recover more quickly than expected, improving financial performance.

Please see important disclosures and certification on page 2 of the report.

Required Research Disclosures

Appropriate for Income	Appropriate for Aggressive Income	Sell	FYI
Appropriate for Income – We consider bonds to be an appropriate holding for investors seeking Income within a well-diversified portfolio. Our time horizon is 3-5 years.	**Appropriate for Aggressive Income –** We consider bonds appropriate only as a small Aggressive Income portion within a well-diversified portfolio. Bonds within this category are riskier, with a higher possibility of loss due to default, than bonds classified as Income. Our time horizon is 3-5 years.	**Sell –** We recommend investors sell these bonds. We believe these bonds are no longer an appropriate fixed-income holding because, in our opinion, they offer an unattractive risk/reward scenario at current prices. Our time horizon is 3-5 years.	FYI - For informational purposes only; factual, no opinion.

Initiated Coverage (Appropriate for Income) 11/05/19.....(Appropriate for Income) 11/05/19-05/03/22...(Appropriate for Aggressive Income) 05/03/22-

Analyst Certification

- I certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers; and no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in the research report. Brian Therien, CFA

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