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CREDIT OPINION
20 June 2017

Update

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Genesis HealthCare System, OH

Update - Moody's affirms Genesis HealthCare System's (OH) Ba2; outlook stable

Summary Rating Rationale

Moody's Investors Service affirms the Ba2 rating assigned to Genesis HealthCare System (Genesis), OH's debt issued through the County of Muskingum, OH. This action affects approximately $292 million of outstanding rated debt. The outlook is stable.

Affirmation of the Ba2 reflects the organization's favorable and leading market position, improved operating performance and balance sheet growth. The rating also favorably incorporates Genesis' limited debt structure risks comprised largely of fixed rate bonds. Genesis is challenged by its outsized debt load translating to weak debt coverage and leverage metrics. Additional challenges include a weak payor mix and above average allocation of investments to equities and alternative investments.

Credit Strengths

- Favorable and leading market position with 49% market share over a six county service area
- Material improvement in operating performance through FY 2016
- Healthy growth in unrestricted cash and investments through FY 2016 provided for improved cash on hand to 111 days
- Conservative debt structure with mostly all fixed rate revenue bonds

Credit Challenges

- Debt levels remain elevated with 58% debt to operating revenue and debt coverage is weak with reported 2.5 times maximum annual debt service (MADS) coverage at FYE 2016; proforma debt coverage tempers moderately
- Assets are heavily allocated to equities, hedge funds and alternative investments
- Challenged payor mix given high reliance on government reimbursement with 22% Medicaid and 49% Medicare
- Despite its frozen status, the organization's cash balance pension plan remains lowly funded as its unfunded pension liability continues to grow

Rating Outlook

The stable outlook incorporates our expectation that improved operating performance will be sustained allowing for continued balance sheet growth and the gradual strengthening of debt coverage. Moreover, we expect no additional debt borrowings in the near future, beyond the upcoming private placement, and manageable levels of capital spending.

Factors that Could Lead to an Upgrade

» Sustained trend of improved operating performance

» Strengthening of all debt measures

» Continued liquidity growth

Factors that Could Lead to a Downgrade

» Return to prior year levels of weak operating performance

» Deterioration of liquidity and/or debt coverage

» Additional debt that further dilutes debt coverage metrics

Key Indicators

Exhibit 1

Genesis HealthCare System, OH

	2012	2013	2014	2015	2016	Proforma FY 2016
Operating Revenue ($'000)	419,213	427,559	462,273	476,137	511,531	511,531
3 Year Operating Revenue CAGR (%)	9.2	6.9	6.7	4.3	6.2	6.2
Operating Cash Flow Margin (%)	4.6	2.7	5.5	4.2	7.7	7.7
PM: Medicare (%)	50.0	49.2	49.6	49.0	49.5	49.5
PM: Medicaid (%)	16.5	17.1	21.4	23.0	22.2	22.2
Days Cash on Hand	117	126	127	107	111	111
Unrestricted Cash and Investments to Total Debt (%)	225.7	47.7	50.5	45.3	49.4	47.8
Total Debt to Cash Flow (x)	2.0	14.2	8.5	10.8	6.3	6.5

Based on audited financial statements for Genesis HealthCare System and Subsidiaries for fiscal year ended December 31
Proforma FY 2016 assumes $10 million of incremental leverage
Investment returns normalized at 6% prior to 2015, and at 5% in 2015
Source: Moody's Investors Service

Recent Developments

Recent developments are incorporated in the Detailed Rating Considerations section.

Detailed Rating Considerations

Market Position: Favorable market position in fair service area

Genesis' position remains favorable in its primary service (PSA) with leading 49% market share. The organization's PSA is comprised of six counties including Muskingum County, Guernsey County, Noble County, Morgan County, Perry County and Coshocton County. Competition in the area is modest with Genesis' two closest competitors, Southeastern Ohio Regional Medical Center and Coshocton County Memorial Hospital, located approximately 35 miles and 28 miles away, respectively. However, Genesis does lose some patients to larger more tertiary providers in Columbus, OH, primarily in orthopedics and high end pediatric care.

Demographics in Genesis' PSA are modest, with above average unemployment rate and little population growth. Moreover, the system relies heavily on government payors, with Medicaid and Medicare representing 22% and 49%, respectively, of gross revenue.

Operating Performance, Balance Sheet and Capital Plans: Improvement in operating performance following weak trend; balance sheet growth and moderate capital spending plans

Profitability margins significantly improved through FY 2016 following multiple years of weak performance. Genesis reported a .3% operating margin and 7.7% operating cash flow margin through FY 2016 compared to (2.6%) and 4.2% in FY 2015. Improved financial performance follows completion of the organization's campus consolidation project which has allowed Genesis to realize a variety of cost savings with reductions in duplicative services and streamlining processes. Moreover, although total admissions (inpatient admissions and observation stays) remained relatively flat through FY 2016, the organization realized 24% growth in total surgeries, a 3% increase in outpatient visits and 2% growth in emergency room visits.

Operating performance weakened through the first quarter of FY 2017 following physician turnover and increased labor costs. Through March 31, 2017, Genesis recorded (.3%) operating margin and 6.7% operating cash flow margin. Genesis has budgeted for a 1% operating margin and 8% operating cash flow margin for FY 2017.

LIQUIDITY

Through FY 2016, Genesis' liquidity position demonstrated good growth with $148 million of unrestricted cash and investments reported at FYE 2016, providing for 111 days cash on hand compared to 107 days at FYE 2015. Improved liquidity follows materially improved operating performance and favorable investment returns. Moreover, unrestricted cash and investments have further improved through the interim period, at March 31, 2017 the organization reported $152 million of unrestricted cash and investments; days cash on hand declined to 109 days given increased expenses through the first quarter compared to FYE 2016.

Genesis maintains adequate levels of monthly liquidity with 87% of unrestricted cash and investments available. However, investments are heavily allocated to 46% equities and 15% hedge funds and alternative investments, the remaining 39% consists of cash and fixed income. We view this as a relatively aggressive asset allocation, given the hospitals modest liquidity position and high debt load.

Genesis has budgeted $25 million for capital projects in FY 2017, including routine and strategic initiatives, to be funded with cash flow and bond proceeds. Major projects include expansion of the hospital's Perry County Medical Center to include freestanding emergency services, IT infrastructure development and replacing equipment. Given expectations of better operating performance and moderate capital requirements we expect the balance sheet to strengthen over the next several years.

Debt Structure and Legal Covenants: Very weak debt coverage counterbalanced by limited debt structure risks

The organization's debt levels remain outsized relative to operations and its liquidity position providing for weak debt coverage. Albeit healthy balance sheet growth and improved operating performance through FY 2016 provided moderate improvements, Genesis reported 58% debt to operating revenue, 49% cash to debt and 2.5 times MADS coverage. Genesis' proposed $10 million of privately placed bonds are expected to slightly temper debt metrics, however at this time we do not believe the impact is material.

Genesis has a MADS coverage covenant as part of the Series 2013 financing (1.1 times to bring in a consultant and 1.0 times is an event of default). The obligated group (see Legal Security section) is subject to additional and more restrictive covenants under its revolving credit loan facility with PNC Bank, N.A. and Huntington Bank, including 1.3 times MADS coverage (measured at each fiscal year end), minimum 75 days cash on hand (measured semiannually) and maximum 70% debt to capitalization (measured at each fiscal year end). Headroom to covenants has improved from prior years but remains constrained.

DEBT STRUCTURE

Debt structure risks are limited as the organization's debt is predominantly fixed rate.

DEBT-RELATED DERIVATIVES

The system does not have debt-related derivatives.

PENSIONS AND OPEB

The organization sponsors a frozen cash balance pension plan. The funded status was a low 62% at FYE 2016, a decline from the prior year of 64%. When incorporating the organization's direct debt, operating leases, and underfunded pension plan, unrestricted cash and investments to total adjusted debt measured 39% at FYE 2016.

Management and Governance

Genesis has a well-seasoned management team; there have been no recent changes.

Legal Security

The Series 2013 Bonds and system's outstanding notes are equally and ratably secured by mortgages on the Mortgaged Property and a security in the Gross Revenues of the obligated group. The obligated group is comprised of Genesis HealthCare System, Genesis HealthCare Foundation, Good Samaritan Medical Center Foundation, Bethesda Health Foundation, CareServe, Genesis CareGivers, CareLife, LLC, Professionals PRN LLC, CareEquip, LLC, Genesis Medical Group LLC, Genesis Emergency Physicians LLC, Genesis Urgent Care Physicians LLC, Genesis Primary Care Physicians LLC and Genesis Surgical Services LLC.

Use of Proceeds

Not applicable.

Obligor Profile

Genesis is a stand-alone community hospital located in Zanesville, Ohio. In addition to the acute care hospital, Genesis provides patients in the community access to outpatient care, including primary and specialty physician clinics, urgent care facilities, an outpatient surgery center, outpatient therapy and an ambulance service.

Methodology

The principal methodology used in this rating was Not-for-Profit Healthcare Rating Methodology published in November 2015. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REPORT NUMBER 1074501

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