

2023 Sector Outlook

U.S. Not-for-Profit Life Plan Communities
WHEFA Insights into Capital Finance

Margaret Johnson, CFA
Senior Director
March 27, 2023





While Fitch expects demographic trends to continue to support healthy demand, decelerating real estate price growth and cost inflation are significant headwinds that may stall the life plan community (LPC) sector's recovery in 2023.

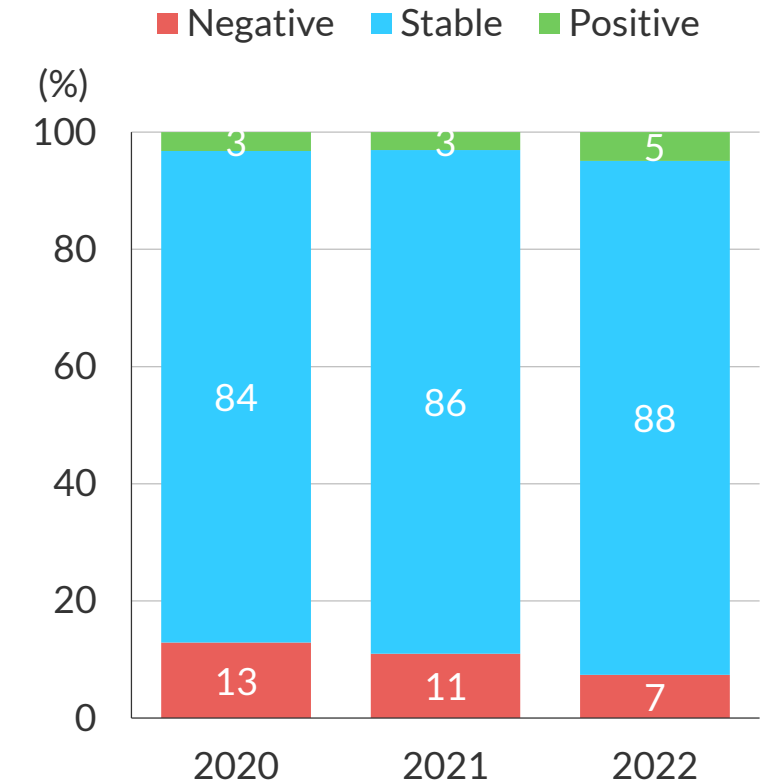
Fitch Ratings

Fitch's LPC Portfolio in 2022

Fitch Rates 163 Life Plan Communities (LPCs)

- Median rating is 'BBB' and the number of ratings in this category remains the most numerous at about 50% of ratings versus 21% in the 'A' rating category and 28% below investment grade
- Fitch's net outlook balance recovered in 2022 compared to 2021 and 2020, reflecting an uptick in Positive Rating Outlooks and a decrease in the number of Negative Rating Outlooks compared to the two previous years
 - 2022: Nine (9) Upgrades / 12 Downgrades
 - 2021: Six (6) Upgrades / 17 Downgrades
 - 2020: No (0) Upgrades / 20 Downgrades
- Despite more negative sector outlook, Fitch does not expect a material increase in negative rating actions in 2023

Life Plan Community - Rating Outlooks



Source: Fitch Ratings

LPC Sector Outlook: Demand Remains a Sector Strength

Demographics to Support Healthy Demand

- Fitch expects stable to improving ILU occupancy in 2023, supported by demographics (aging population, Baby Boom generation)
- Independent living unit (ILU) occupancy at most Fitch-rated LPC issuers has been improving over the last two years
- Concerns about broader declines in demand for the LPC model due to coronavirus have proven to be unfounded
- Skilled nursing occupancy continues a slow recovery driven more by staffing challenges than demand issues
- Assisted living and memory care occupancy have recovered more quickly, and occupancy is expected to remain steady in 2023

Drivers of 'Deteriorating' Outlook

Labor Shortages Driving Increased Operating Expenses

- Higher wages to recruit and retain staff were the main driver of escalating operating expenses in 2022
- Despite incremental signs of improvement, job openings remain elevated, and most healthcare providers continue to experience shortages of nurses, certified nurse aides, and other staff
- LPCs have more flexibility than hospitals in responding to labor pressures (more limited clinical operations, can take units/wings offline)
- Monthly service fee increases well above typical levels for 2023 should help absorb expense increases, but some longer term concern about the ability of LPC providers to continue to raise rates at elevated levels should inflation persist

Drivers of 'Deteriorating' Outlook (Cont.)

Deceleration in Real Estate Price Growth

- Growth in residential real estate prices is slowing
 - National home prices were 12.2% overvalued as of 3Q22 (source: Fitch's 3Q U.S. RMBS Sustainable Home Price Report)
- Home prices expected to moderate further with elevated mortgage rates
 - Housing market crash as occurred in 2008-2009 is unlikely
- Fitch believes entrance fee pricing can remain largely stable even if home prices decline beyond our overvaluation estimates

Drivers of ‘Deteriorating’ Outlook (Cont.)

Financial Market Volatility / Higher Cost of Capital

- Capital investment will remain a core theme in LPC sector
 - ILU expansions to meet rising demand and satisfy consumer preferences for unit configuration and community amenities
 - “Repositioning” projects to right-size assisted living and skilled nursing facilities or add service lines (memory care)
- Global macroeconomic outlook has deteriorated, cost of capital has risen
 - A negative for LPCs pursuing expansion projects in the current environment
 - Many of our rated LPCs refinanced at lower rates over the last several years
- May result in delayed borrowing plans
 - LPCs have flexibility on capital spending and can generally delay projects
 - A slowdown or delay in borrowing could keep balance sheets stable offsetting investment market volatility

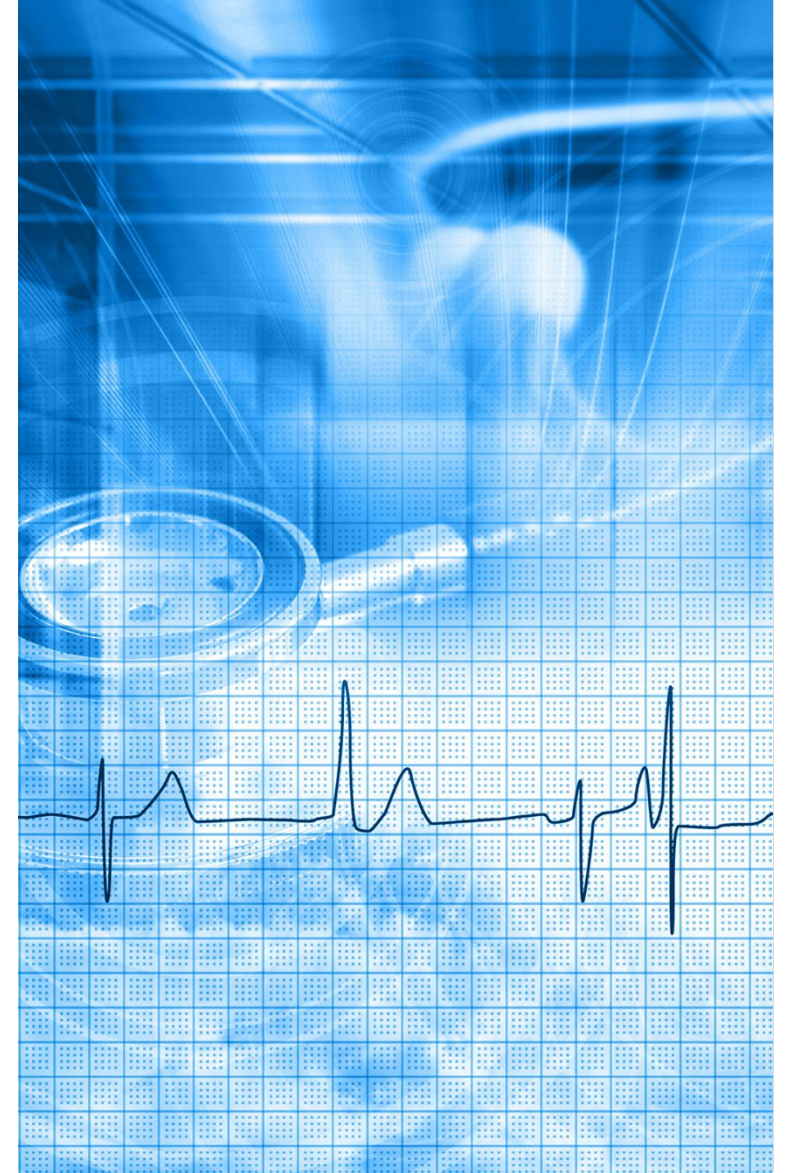
What to Watch: “Tridemic” and Regulatory Environment

An Unexpected Surge in Highly Infectious Disease(s)

An unexpected surge in a highly infectious variant of coronavirus or another disease, or any other disruptor that causes prolonged restrictions on move-ins into an LPC could counteract current strong demand and would pressure issuers and the sector beyond considerations in Fitch’s ‘deteriorating’ sector outlook.

Heightening of Regulatory Requirements

With a few exceptions, most states have not enacted material new regulations on long-term care providers in the last two years. However, meaningful actions by legislators is still possible, especially if viral surges are more severe than currently expected. Heightened regulatory requirements would likely increase operating costs and exacerbate headwinds in the LPC sector.



What to Watch: Mergers & Acquisitions

Mergers & Acquisitions (M&A) to Continue

- Fitch expects the increased pace of M&A activity to continue in 2023
- Competitive pressures are driving smaller LPCs to seek a larger system's resources
- Often the “first” step goal stabilizes and financially improves a newly acquired campus before integrating it into the system
Obligated Group

Appendix

Wisconsin LPC Ratings and Contract Types^a (as of February 22, 2023)

Transaction Name	State	Rating	Outlook	Contract Type
Saint John's Communities, Inc. (WI)	WI	BBB-	Positive	A
Three Pillars Senior Living Communities (WI)	WI	BBB+	Negative	C

^a Predominant contract type(s) indicated for LPCs that offer multiple contract types



Contact



Margaret Johnson, CFA
Senior Director
Sector Lead for Senior Living

margaret.johnson@fitchratings.com



fitchratings.com

New York
33 Whitehall Street
New York, NY
10004

London
30 North Colonnade
Canary Wharf
London, E14 5GN

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers. Please read these limitations and disclaimers by following this link: <https://www.fitchratings.com/understandingcreditratings>. In addition, the following <https://www.fitchratings.com/rating-definitions-document> details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at <https://www.fitchratings.com/site/regulatory>. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.

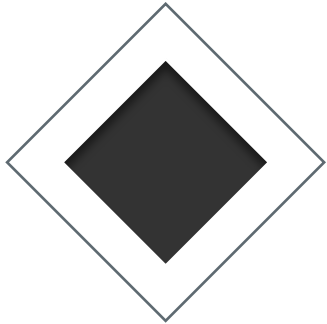
Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

Copyright © 2023 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved.

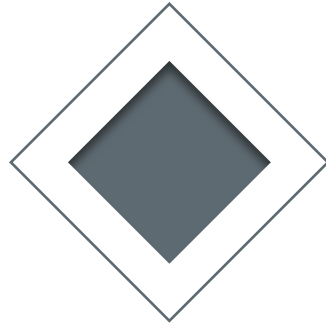
Resources

Accessing the Fitch Ratings Image & Icon Library

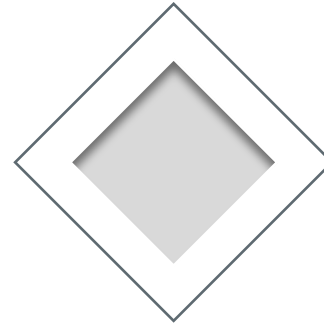
Click “slide show”  and select an option below:



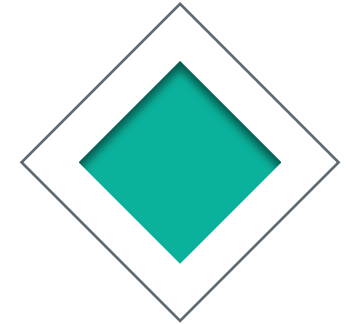
Brand
Approved
Images



Sector
Specific
Images



Icons



Tips &
Tricks

If images selected are not to your preference please
replace using the links above