
S&P: U.S. Not-For-Profit Senior-Living Sector Remains Stable Despite Mixed Financial Results.

Median ratios for the U.S. not-for-profit senior-living sector were mixed in 2013, with weaker operating and excess margins offset by balance sheet improvements, particularly liquidity.

We expect the trend of weaker margins to wane over the next several years, as providers continue to leverage improvements in the U.S. economy and housing sector and focus on achieving stronger revenue growth. However, Standard & Poor's believes meaningful revenue growth will be difficult without occupancy levels in excess of 90%. While occupancy levels have certainly improved from the post-recession lows, they have hovered in the mid to upper 80% range, though the latest data suggests some facilities approaching 90% or higher. The sector's other challenges include general expense pressures; changes in consumer preferences and care delivery models (for example home health services; remote monitoring or assisted living green house model); and the need for capital investment to reposition dated communities or provide the necessary services and amenities to attract today's senior population.

We noted last year that it might be difficult for senior-living providers to find the next level of savings to improve operating results. This concern was validated as the operations for providers continued to decline. While the overall median revenue was up in fiscal 2013, the growth rate did not keep pace with the increase in expenses, causing a further decline in the overall median operating margin. We believe expense pressures will persist, as some of the drivers revolve around finding ways to improve occupancy, such as increased sales and marketing expenses. While many organizations experienced some degree of success with their more extensive marketing initiatives, these actions have come at a cost and weakened, in our view, some organizations' operating performance, though we understand these are often short-term solutions to shore up occupancy.

On the positive side, liquidity metrics for most organizations offset these operating pressures, with strong year over year gains, enabling the sector to remain stable. Standard & Poor's believes that, despite some near-term operating pressure, the senior-living sector demonstrates general credit stability, evidenced by the vast majority of sector ratings being affirmed. While we anticipate that there will be continued pockets of operating stress through 2015 and possibly beyond, demand should become more robust as the U.S. economic outlook improves (including the housing sector), baby boomers age, and providers introduce new care delivery models and technologies that can provide higher quality care and reduce cost. Furthermore, many of our rated senior-living providers have experienced management teams and are located in markets with strong demand and limited direct competition.

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