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S&P U.S. Not-For-Profit Health Care Small Stand-Alone Hospital Median Financial Ratios -- 2019 vs. 2018

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Small hospitals (defined as a subset of stand-alone hospitals and representing those hospitals with $150 million or less total operating revenue) typically have stronger financial metrics compared with similarly rated stand-alone hospitals, in part to compensate for increased risk and volatility associated with modestly sized organizations. The added risk is reflected in a rating distribution that skews toward the lower end of the rating spectrum, with 41% of the small hospitals rated in the speculative grade categories compared with just 13% of all stand-alone hospitals (see chart 1). The outlook distribution, with almost half of the small hospitals carrying a negative outlook (see chart 2), also reflects these risks.

Historically, the outlook distribution for small hospitals and stand-alone hospitals has been similar, however a significantly higher percentage of small hospitals carry negative outlooks at June 30 compared with stand-alone hospitals. This is partially due to the multi-credit action we took in mid-April that affected many small hospitals (see “Outlooks Revised On Certain U.S. Not-For-Profit Health Care Organizations Due To Potential COVID-19 Impact,” published April 21, 2020, on RatingsDirect). We expect that the financial repercussions associated with the pandemic, which have largely triggered unfavorable rating and outlook actions throughout the sector this year, will be evident in the medians based on fiscal 2020 results published in 2021.

The relatively limited sample size of small hospitals and the movement of credits from one rating category to the other can affect medians from year to year. Between 2019 and 2018 there has been some improvement within the ‘A’ category on many financial metrics, while the ‘BBB’ and speculative grade category medians are more mixed (see table 1). This is consistent with rising volatility as credits move down the rating scale.

In general, small hospitals face unique risks that differentiate them from their larger stand-alone counterparts. Typical risks associated with small hospitals include weaker enterprise profiles, inclusive of demographics and economic characteristics, more-limited physician staffs that can have higher turnover and recruitment difficulty, and smaller clinical volume that can create vulnerability to changes in clinical practice such as inpatient-to-outpatient shifts. With total operating revenues of less than $150 million, small hospitals also can have fewer opportunities to offset revenue pressures or reduce costs during periods of operating stress. As a result, in order to offset these inherent risks, small hospitals generally need to have stronger financial metrics than their larger stand-alone counterparts to achieve comparable ratings (see table 2). This traditionally includes healthier balance sheets with higher unrestricted reserves and lower leverage. We view this balance sheet strength as a key offset to the volatility inherent in the business profiles of small hospitals.

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