ZIEGLER INVESTMENT BANKING
SENIOR LIVING FINANCE Z-NEWS
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FEATURED ARTICLE

THE ANNUAL "LOOK BEHIND…AND LOOK AHEAD": 2022 RECAP & 2023 PREDICTIONS

Each year, we use the initial weeks of Ziegler ***Z-News*** to reflect on the year behind us and what to anticipate for the year ahead. It has certainly been an interesting several years, with 2022 handing us economic challenges along with a mixed bag of continued recovery from the COVID-19 pandemic, but also fierce headwinds that will continue into the year ahead.

In 2022, we continued to see **outbreaks of COVID-19**, particularly in the early months, but for the most part, communities have been able to create stability in pandemic management, achieve high levels of resident vaccination and booster status and transition to a more 'normal' standard of operations. We saw steady **gains in occupancy** throughout the year, with many providers reporting occupancy figures at or above pre-pandemic figures. Unfortunately, in the care settings, occupancy has often been hindered by **workforce shortages**. This has also caused many organizations to revisit their overall **skilled nursing commitment**. **Expense pressures and inflationary realities** have likely captured the most significant headlines, impacting everything from the lending environment, pace of growth and construction projects, margin and fee increases among others.

As one forecaster noted in early 2022, it was predicted to be a year of the "best-ever" and "worst-ever" and that largely held true.

What can we expect for 2023?

One observation of the current not-for-profit senior living and care landscape is the variation in the current status and forward strategy across organizations. For many, they see the current environment as one that is ripe for growth and they are boldly moving forward with affiliation and acquisition opportunities, campus expansion projects, and revenue diversification initiatives. At the same time, some are hitting pause on planned projects due to inflation while others are hitting the reset button because they may be in need of organizational repositioning to remain viable long-term. Regardless, each of the trends that will unfold in 2023 will be fairly universal across provider organizations.

So, what do we see as the hot topics and areas of greatest focus as we forge ahead in 2023? The topics below are not mutually exclusive, but represent areas of opportunities, areas in transition, and certainly some areas that will challenge us as a sector.

- **Revenue and Expense Pressures**: Even as occupancy continues to advance, gains in revenue are being offset by inflationary pressures. Providers continue to increase wages *(23 states saw an increase in minimum was as of January 1st)*, pay more for just about every type of supply needed. It is more important than ever for provider organizations to be prudent with fee increases as well as entrance-fees. You cannot price yourself out of the market, but you cannot also create a greater deficit if increased occupancy costs you more than it brings you.

- **Labor**: We are hearing of some glimmers of hope on this front whereby a proportion of providers have weaned themselves down from peaks of agency usage and are observing a plateau in staffing shortages. We clearly are not out of the woods and most would agree that staffing is still the number one challenge and will be throughout 2023. However, we are adapting and have learned to survive in this difficult environment. This has resulted in some difficult decisions around downsizing, or even exiting, certain service lines. We are going to need to continue to reinvent in this space, whether it be alternative staffing models, revisiting the type of person we hire, the integration of workforce technologies, or even workforce housing.

- **Technology**: Speaking of the glimmer of hope! Please do not set this aside as a "nice to have" in 2023. It is so important for organizations to devote resources to staying on top of the technology-enabled innovation in our space. This is a vast space that is moving quickly and there are many solutions that will help ease some of the pressures that organizations are facing. Additionally, to truly stay on top of consumer and workforce expectations, we need to be able to compete at a certain level on the technology front.

- **Continued Consolidation**: This trend has been unfolding at a more rapid pace for a number of years now. There can be great benefit from concentrated scale and the ability to grow through affiliation or acquisition activity which is generally a quicker strategy today than new community development. Having said that, there are a vast number of organizations that talk about growing in this regard, with a limited inventory of high-quality providers that have the potential to be accretive to the organization. Being proactive and in the ready-stance will be necessary. Conversely, it is anticipated that 2023 will continue to see sales of nursing-centric or financially distressed not-for-profits to private sector buyers.

- **Skilled Nursing Disrupted**: This is one of those trends that is very much inter-twined with the workforce challenges. The skilled nursing disruption has been underway for a number of years now. The regulatory environment is only getting more difficult, staffing is a challenge and generally reimbursement levels do not cover the cost of care. The handful of states who have put forth Medicare or Medicaid increases in 2023 are welcome, but are simply narrowing the existing financial loss. The demand for skilled care services has not and will not go away. What is changing is our ability to offer these services as we have in the past. The when and the where this care is provided will continue to shift.

- **Creative Business Models**: We need to continue to explore alternative business models and diverse revenue streams. This might mean ownership in services that are new for the organization, such as pharmacy, behavioral health, rehab or physician services to name a few. For others, it might be venturing into some of the more traditional home care or home health services that had not previously been explored. In some cases, these service lines might be structured as for-profit ventures and might be in joint ventures with others. We need to think creatively, finding the right intersection between the business mind and the heart of the mission.

- **Hospital & Post-Acute Relationship**: FitchRatings released their 2023 Outlook for U.S. Not-for-Profit Hospitals and Health Systems and designated it as “Deteriorating.” There has always been the need for ensuring strong relationships with area hospitals, but the past year or so has reinforced how inter-dependent we are on one another. Similar to our sector, they are feeling pressured by wages and inflationary costs. Additionally, however, they are experiencing increased length of stays as many nursing homes are turning away admissions (due to staffing) and home health agencies are often at maximum level, also because of staffing challenges. Hospitals are actively working to remedy these challenges and it is prudent for senior living organizations to have a seat at that table.

- **Cost of Capital**: For a decade, we have benefitted from record-low cost of capital and had gotten used to the lower rates. We are now back to 20-year averages. Organizations will need to continue to reassess their capital needs and compare with growth and construction plans. We predict that in 2023, a proportion of providers will continue to move forward with campus (re)development projects, while others might scale back plans to be smaller than originally planned or executed in multiple phases.

Regardless of the current status of the organization, the forces at play are generally impacting everyone. We all need to be prepared for these ongoing changes and be bold in our strategic planning efforts moving forward. As we hit the three-year anniversary of the onset of COVID-19, we cannot live in a pandemic mindset. Those realities are still present, but boards and leadership teams need to visualize a future independent from the pandemic. Do not be afraid to change and advance on opportunities to strengthen your organization and mission.

Ziegler remains committed in the year ahead to bringing forth the most up-to-date research and trend information and feeding that back out to the sector. We offer up this thought leadership to organizations who are looking to educate their boards and leadership teams, and for those embarking upon strategic planning processes.

If you have questions related to the topics mentioned in this article or other related items, please contact the Ziegler banker in your region.

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NOT-FOR-PROFIT SENIOR LIVING RATINGS ACTIONS

AS OF JANUARY 2, 2023

ORGANIZATION	RATING AGENCY	RATING/ OUTLOOK	TYPE OF ACTION	DATE
The Forest at Duke (NC)	Fitch	BBB Stable	Downgraded Rating and IDR*	12/21/22
Eskaton Properties (CA)	S&P	BBB- Negative	Affirmed Rating Revised Outlook	12/23/22

* *IDR – Issuer Default Rating (FitchRatings)*
Any non-Ziegler sources referenced in this Z-News are believed to be reliable but cannot be guaranteed.

FEATURED FINANCING

THE HIGHLANDS AT WYOMISSING®

HIGHLANDS AT WYOMISSING
Wyomissing, Pennsylvania

$67,685,000
Bank Direct Purchase / New Money

$45,830,000
Cinderella Bonds / New Money

$21,855,000
January, 2023

INTEREST RATES/YIELDS

WEEK ENDING DECEMBER 30, 2022

	CURRENT	LAST WEEK	52-WK AVG
30-Yr MMD	3.58%	3.49%	3.00%
Senior Living 30-Yr "A"	5.15%	5.08%	4.37%
Senior Living 30-Yr "BBB"	5.60%	5.53%	4.76%
Senior Living Unrated	6.35%	6.28%	5.50%
Senior Living New Campus	7.25%	7.18%	6.42%
SIFMA Muni Swap Index	3.66%	3.80%	1.23%

	CURRENT	WEEKLY AVERAGE	SPREAD TO MMD
ZSLMLB Index†	5.63%	5.63%	2.08%

† Ziegler Senior Living Municipal Long Bond Index
Source: Bloomberg BVALS

MARKET REVIEW

MONEY MARKET RATES

	12/30	Last week
Prime Rate	7.50	7.50
Federal Funds (weekly average)	4.32	4.32
90 Day T-Bills	4.39	4.21
30-Day Commercial Paper (taxable)	4.25	4.27
Libor (30-day)	4.36	4.38
SOFR	4.30	4.30
7 Day Tax-Exempt VRDB	3.66	3.80
Daily Rate Average	3.71	3.80

COMPARATIVE YIELDS

TAXABLE REVENUE

	GOVT	A
2 Year	4.36	5.46
5 Year	3.94	5.29
7 Year	3.90	5.40
10 Year	3.81	5.66
30 Year	3.90	6.30

	MMD	NR*	BB	BBB	A	AAA
1 Year	2.86	5.06	4.71	4.01	3.26	2.94
5 Year	2.52	4.82	4.47	3.77	3.02	2.67
7 Year	2.54	4.94	4.64	3.94	3.14	2.79
10 Year	2.63	5.13	4.83	4.23	3.28	2.93
30 Year	3.58	6.33	5.98	5.43	4.58	4.08

(Representative of institutional sales)*

TAX-EXEMPT MARKET INDICATORS

Bond Buyer	THIS WEEK	LAST WEEK	CHANGE
20 Bond Index	3.72	3.66	+0.06
11 Bond Index	3.62	3.56	+0.06
Revenue Bond Index	4.00	3.94	+0.06
30 Year MMD	3.58	3.49	+0.09
Weekly Tax-Exempt Volume (Bil)	0.00	0.16	-0.16
30 Day T/E Visible Supply (Bil)	3.69	3.73	-0.04
30 year “A” Rated Hospitals as a % of 30 Year Treasuries	117.4	120.0	-2.60

Source: Bloomberg