FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms HumanGood California Obligated Group's Rev Bonds at 'A-'; Outlook Stable

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Fitch Ratings - New York - 03 Aug 2020: Fitch Ratings has affirmed the 'A-' ratings on the $142 million revenue and refunding bonds, series 2019 A issued by the California Municipal Finance Authority on behalf of the HumanGood California Obligated Group (HGCOG) and the $26 million in series 2019B HGCOG taxable bonds. Additionally, Fitch has also affirmed the 'A-' ratings on the $64 million revenue bonds issued by California Statewide Communities Development Authority (CSCDA) on behalf of American Baptist Homes of the West (ABHOW), which is now known as HumanGood NorCal (NorCal) and the $46 million in revenue bonds issued by CSCDA on behalf of HumanGood Fresno (dba Terraces at San Joaquin Gardens or TSJG).

The Rating Outlook is Stable.

SECURITY

The bonds are secured by HGCOG's gross revenues. A debt service reserve fund also secures the NorCal bonds. Additionally, the NorCal series 2013A and 2015 bonds are also guaranteed by the income earned on HumanGood Foundation West's unrestricted net assets. As of Dec. 31, 2019, HumanGood Foundation West had $56.2 million of unrestricted net assets.

KEY RATING DRIVERS

DIVERSE OPERATING PLATFORM: The 'A-' rating primarily reflects HGCOG's diverse operating platform, which includes geographic diversity (14 campuses located throughout California), scale (3,478 total units and $309 million in total operating revenues), and broad service offerings. Fitch believes HGCOG's diverse operating platform reduces overall volatility and market risk, which leads to a more consistent operating performance.

SOLID DEMAND ACROSS MULTIPLE LOCATIONS: The affirmation also reflects HGCOG's solid census levels across all of its campuses as evidenced by the average 92.4% occupancy in its independent living units (ILUs), 92.1% occupancy in its assisted living units, 89% occupancy in its memory care units (MCUs), and 86.4% occupancy in its skilled nursing facility (SNF) beds in fiscal 2019. Additionally, HGCOG's various communities are located in good markets with favorable demographics and real estate trends.

CONSISTENT OPERATIONS: HGCOG's solid demand across its campuses and diverse operating platform has led to consistent operational performance in recent years. In fiscal 2019, HGCOG had a 98.8% operating ratio, 5.2% net operating margin (NOM), and 21.5% NOM-adjusted (NOMA). Additionally, HGCOG's consistent operations and solid net entrance fee receipts have produced a solid average 3.4x maximum annual debt service (MADS) and 1.1x revenue-only coverage over the last two fiscal years.

ADEQUATE LIQUIDITY POSITION: HGCOG improved its unrestricted cash and investments 11% year-over-year to $294 million in fiscal 2019, which translates into 408 days cash on hand (DCOH), 82.8% cash to debt, and 12.8x cushion ratio. While all three metrics remain somewhat light relative to Fitch's 'A' category medians, they are sufficient for HGCOG's rating level given its consistent operations, diverse operating platform, and strong coverage levels.

MANAGEABLE LONG-TERM LIABILITY PROFILE: HGCOG's long-term liability profile remains manageable as evidenced by MADS equating to 7.3% of fiscal 2019 revenues, which remains favorable to Fitch's 'A' category median of 9.5%. Additionally, debt to net available measured 4.5x in fiscal 2019, which remains on par with Fitch's 'A' category median of 4x.

ASYMMETRIC RISK FACTORS: There are no asymmetric risk considerations affecting the rating determination.

RATING SENSITIVITIES

The Stable Outlook reflects Fitch's expectation that HGCOG's solid financial profile and management's proactive cost containment strategies will provide enough financial cushion at the current rating level to absorb coronavirus pandemic related disruptions to census and revenues.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Maintenance of historical operational performance and coverage levels coupled with further improvement in key liquidity metrics near Fitch's 'A' category medians.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Any material deterioration in cash flow levels or unrestricted reserves.

--Should economic conditions decline further than expected from Fitch's current expectations or should a second wave of infections occur, Fitch would expect further pressures on HGCOG's revenue base due to the coronavirus pandemic. If this occurs and there is material deterioration in HGCOG's operations, cash flow levels, or unrestricted reserves, there could be downward rating pressure.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579].

CREDIT PROFILE

Effective May 1, 2016, ABHOW (now known as HumanGood NorCal) and Southern California Presbyterian Homes (SCPH; now known as HumanGood SoCal) affiliated and the organizations created a common governance and management structure known as HumanGood. Prior to the affiliation, ABHOW's sole corporate parent was Cornerstone Affiliates. Also prior to the affiliation, SCPH was doing business as be.group and served as the controlling member of its senior living and care system. With the affiliation, the sole member of NorCal and SoCal is HumanGood. Cornerstone Affiliates, now known as HumanGood Cornerstone became a sister entity to HumanGood and is the sole corporate member of the HumanGood affiliates who are not members of HGCOG.

HumanGood's integration activities since its inception include one executive management team, common payroll and benefits, group purchasing, and a single financial data platform. Other items accomplished include corporate services consolidation, a combined affordable housing business, and the creation of another obligated group that includes two of HumanGood Cornerstone's four non-California retirement communities.

The California obligated group, HGCOG, which was formed in August 2019 concurrent with the date of the issuance of the series 2019 bonds, primarily includes HumanGood's California retirement communities operating within NorCal and SoCal, with NorCal serving as the obligated group representative. Additionally, HGCOG includes the corporate office of HumanGood and HumanGood Fresno (TSJG). The HumanGood corporate office provides management services and share overhead expenses to HGCOG members and three of HumanGood Cornerstone's four retirement communities. The corporate office also provides certain functions through annual cost recoveries from other affiliates. TSJG was a member of NorCal's obligated group prior to 2012 but was removed in order to accommodate a repositioning project that included a substantial increase in debt. The campus stabilized in 2016 and is performing well.

NorCal consists of seven life plan communities (LPC) that include Terraces at Los Altos in Los Altos, CA, Grand Lake Gardens in Oakland, CA, Piedmont Gardens in Oakland, CA, Plymouth Village in Redlands, CA, Valle Verde in Santa Barbara, CA, Rosewood in Bakersfield, CA, and Terraces of Los Gatos in Los Gatos, CA.

SoCal includes six LPCs in southern California. Two of the LPCs are located in north central Los Angeles County (Westminster Gardens in Duarte and Royal Oaks in Bradbury), two in Orange County (Windsor in Glendale and Regents Points in Irvine), and two in San Diego County (White Sands in La Jolla and Redwood Terrance in Escondido).

Fitch's analysis is based upon the obligated group financial statements. In fiscal 2019, HGCOG reported total operating revenues of $309.2 million.

The outbreak of the coronavirus and rise in related government containment measures worldwide has created an uncertain environment for the entire healthcare system in the near term. While HGCOG's financial performance through the most recently available data (March 31, 2020) has not indicated any material impairment as a direct result of the pandemic, material changes in revenue and costs profiles will occur across the sector. Fitch's ratings are forward-looking in nature, and Fitch will monitor developments in the sector as a result of the virus outbreak as it relates to severity and duration and incorporate revised expectations for future performance and assessment of key risks.

STABLE FINANCIAL PROFILE EXPECTED DESPITE CORONAVIRUS

HGCOG's solid demand across multiple campuses and diverse operating platform has translated into a consistently solid operational performance in recent years. Over the last two fiscal years, HGCOG has averaged a 99% operating ratio, 5.3% NOM, and 21.6% NOMA, which all remain or par with or somewhat weaker than Fitch's 'A' category medians of 93.3%, 5.9%, and 22.9%, respectively. Overall, HGCOG's operational performance remains sufficient for its current rating level given its size, scale, and stable operations. HGCOG's core operations remain stable through the three-month interim period (ending March 31, 2020) as evidenced by its 98% operating ratio and 4.9% NOM. However, HGCOG's NOMA remained somewhat weak at 11.3% reflecting disruptions to marketing, census, and turnover levels as a result of the coronavirus pandemic.

Fitch expects HGCOG's census, marketing efforts, and operating revenues to experience disruptions throughout fiscal 2020 as a direct result of the pandemic. In response to these disruptions, HGCOG management has taken proactive cost containment strategies including furloughs, salary and wage reductions, non-labor expense cuts, and capex deferrals. Additionally, while HGCOG does not qualify for a PPP loan under the CARES Act like many single-site LPCs, it has received approximately $7 million to date in grants and stimulus money to help mitigate revenue pressures. HGCOG also will be able to defer an additional $7 million of 2020 payroll tax payments into 2021 and 2022. Fitch expects the stimulus money and management's cost mitigation efforts to largely offset any pressures on census or operating revenues in fiscal 2020. Furthermore, HGCOG's manageable debt burden and solid core operations reduce reliance on net entrance fee receipts for debt coverage levels which mitigates concerns over a short-term decline in cash flow from net entrance fee receipts due to coronavirus disruptions. The Stable Outlook reflects Fitch's expectation that HGCOG will maintain its solid financial metrics throughout the pandemic due to its diverse operating platform, solid demand indicators, and cost mitigation efforts.

HGCOG's consistent operations and solid cash flow levels have driven an 11% increase in unrestricted cash reserves year-over-year to approximately $294 million in fiscal 2019, which translates into 408 DCOH, 82.8% cash to debt, and 12.8x cushion ratio. While these metrics remain light relative to Fitch's 'A' category medians of 638, 122%, and 15x, respectively, they remain adequate for HGCOG's rating level given its diverse operating platform. However, HGCOG's unrestricted reserves declined 12% through the three-month interim period due to large unrealized losses ($16 million) and weaker net entrance fee receipts. Despite the decline, Fitch's believes HGCOG's key liquidity metrics remain adequate for its rating level. Furthermore, Fitch expects its unrestricted cash reserves to remain stable or improve throughout the fiscal year due to improvement in equity markets, receipt of stimulus funds, and implementation of its cost containment initiatives.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING		
HumanGood California Obligated Group (CA)			
• HumanGood California Obligated Group (CA) /General Revenues/1 LT	LT	A- Rating Outlook Stable	Affirmed

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

U.S. Public Finance Not-For-Profit Continuing Care Retirement Community Rating Criteria (pub. 29 Mar 2018) (including rating assumption sensitivity)

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 27 Mar 2020) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

California Municipal Finance Authority	EU Endorsed
California Statewide Communities Development Authority	EU Endorsed
HumanGood California Obligated Group (CA)	EU Endorsed

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