ZIEGLER INVESTMENT BANKING

SENIOR LIVING FINANCE Z-NEWS

FEATURED ARTICLE

EXAMINING REVENUE DIVERSIFICATION STRATEGIES

Many not-for-profit senior living providers are exploring ways to diversify revenue streams to largely combat pressures stemming from the skilled nursing side of our business. We know that skilled nursing occupancy is at record lows and that skilled care revenue is declining for a large proportion of providers. In their 33rd Edition of the Skilled Nursing Facility Cost Comparison Report, CliftonLarsonAllen reported that in 2017, the median operating ratio for nursing homes was 0%, meaning that half of providers did make some form of profit, while the other half ended the year in the red. So, what are the alternatives to make the organization's revenues sustainable, or even better, make them grow? There is no secret sauce or magic bullet, but there are options for providers to consider. They are not necessarily easier options, but for each of the considerations outlined below, there are examples of provider success stories.

- **Growth in Independent Living -** This is the most common strategy among senior living providers. Assuming you have the market demand to do so, adding Independent Living units has the opportunity to generate additional revenue for the organization. Admittedly, this also requires upfront investment and capital to do so, but if done right, can be a strategy to lessen dependency on healthcare revenue. This approach is particularly salient for providers who are arguably imbalanced in their unit mix, with heavier assisted living and skilled nursing than current Independent Living options.
- **Third-Party Management -**The 2018 LeadingAge Ziegler 200 (LZ 200) report revealed that slightly more than 30% of not-for-profit multi-sites manage a community that they do not own. We know that there has been tremendous growth within the for-profit seniors housing sector and many of those owners and developers are looking for high-quality management partners. Additionally, there are a number of not-for-profits, largely single-site providers, who explore third-party management. There is a portion of not-for-profit providers who have built fairly extensive management divisions (some even separate companies) and have demonstrated clear success.
- **Building On In-house Expertise -** What do you do really well? Where do you have the opportunity to take internal competencies and build out business lines to serve others outside of your organization? We have seen this within our sector along technology lines. There are several providers who have developed IT consultancies and have had the ability to build out significant platforms to serve others. Organizations can do an inventory of what they know they do very well, and assess their leadership capacity to build and scale a business model like this.
- **Growing HCBS -** We acknowledge up-front that this is not the end-all-be-all of diversifying revenue. Seven out of 10 not-for-profit providers who have HCBS platforms make less than $10 million a year in revenue. Margin in the HCBS service area can also be leaner than residential business lines. However, it is not an impossible goal. Scale is indeed important as is having the appropriate expertise. Organizations must hire experience and employ the type of leadership that understands how to operate these business lines. An option that could be considered is home-based services to specialized populations (e.g., pediatric home health services). An article in Home Health News this week referenced that children with complex medical conditions are more likely to remain in the hospital longer because of an inability to garner needed home-based care. The lack of home care was the reason for delayed discharge from the hospital in nearly 92% of the cases.
- **Sub-populations and Specialty Care -** Understanding what some of the specific needs are in the greater community can help determine where your organization may be able to play a role. For example, there are some not-for-profit providers who have developed strategic relationships with dialysis providers and who have onsite clinics on their campus for renal care. What about autism support services? Autism is a diagnoses that has grown exponentially, with CDC estimates at roughly 1 in 59 children in 2018 receiving the diagnosis. Many of these individuals are into young adulthood and the service demand is significant, if not for the individual, but the caregiver in need of respite services. These are just two examples and these may go beyond the mission boundaries of the organization, but these 'What if?' conversations are often what foster service line innovation.
- **Joint ventures -** This is a more generic category, but one worth spending time on. Joint ventures on alternative business lines have become quite common and really should be considered a viable option when thinking about future revenue streams. Many HCBS platforms are joint ventures of some sort and this structure allows for greater growth opportunities than if an organization chooses to move forward alone. Roughly one-third of the LZ 200 organizations are in at least one formal joint venture. It is important to appropriately structure joint ventures and to plan for exit strategies down the road if needed.

FEATURED ARTICLE

EXAMINING REVENUE DIVERSIFICATION STRATEGIES (CONTINUED)

Each of these growth areas has its own set of advantages and disadvantages. What each does, however, is offer some form of diversification of revenue and spreads risk across more than one business line. These are not easy fixes and are not platforms that are created overnight. These growth strategies do require leadership teams to be bullish at times and necessitate a board who is willing to take some risk. Some diversification ideas can be great ideas, but if the business plan falls apart or if the diversification grows revenue, but with a negative margin, it likely does not make sense. These conversations, when done right, also bring forth conversations around mission and identity. The organization's mission can at times create a tension with potential business decisions and it is important to periodically have checks and balances in place to ensure those two work in harmony.

In closing, there are opportunities to consider, but organizations need to spend time doing their homework and need to understand the ramifications of choosing to diversify revenue options or not.

If you have any questions about the content of this issue of ***Z-News*** or other related items, please contact the Ziegler banker in your region.

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NOT-FOR-PROFIT SENIOR LIVING RATINGS ACTIONS

NOVEMBER 29 - 30, 2018

ORGANIZATION	RATING AGENCY	RATING/ OUTLOOK	TYPE OF ACTION	DATE
Edgemere (TX)	Fitch	BB- Negative	Downgraded Rating	11/29/18
Lutheran Social Ministries at Crane's Mill (NJ)	Fitch	BBB+ Positive	Affirmed Rating Revised Outlook	11/29/18
BHI Senior Living (IN)	Fitch	BBB Stable	Downgraded Rating Assigned Rating Removed Rating Watch	11/30/18
Kendal at Lexington (VA)	Fitch	BBB- Stable	Affirmed Rating	11/30/18

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INTEREST RATES/YIELDS

(AS OF NOVEMBER 30, 2018)

	CURRENT	LAST WEEK	52-WK AVG
30-Yr MMD	3.24%	3.28%	3.00%
Senior Living 30-Yr "A"	4.14%	4.18%	3.81%
Senior Living 30-Yr "BBB"	4.39%	4.43%	4.05%
Senior Living Unrated	5.09%	5.13%	4.79%
Senior Living New Campus	6.50%	6.50%	6.50%
SIFMA Muni Swap Index	1.69%	1.69%	1.38%

	CURRENT	WEEKLY AVERAGE	SPREAD TO MMD
*ZSLMLB Index	4.93%	4.93%	1.67%

**Ziegler Senior Living Municipal Long Bond Index*
Source: Ziegler Capital Markets

FEATURED FINANCINGS

COVENANT RETIREMENT COMMUNITIES
Skokie, Illinois
Colorado Health Facilities Authority, Revenue Bonds, Series 2018A
$59,780,000

COVENANT RETIREMENT COMMUNITIES
Skokie, Illinois
State of Connecticut Health and Educational Facilities Authority, Revenue Bonds, Series 2018B
$46,850,000

CALIFORNIA ARMENIAN HOME
Fresno, California
California Municipal Finance Authority, Insured Revenue Bonds, Series 2018
$24,660,000

CHRISTIAN HORIZONS OBLIGATED GROUP
St. Louis, Missouri
Health and Educational Facilities Authority of the State of Missouri, Senior Living Facilities Revenue Bonds, Series 2018
$29,365,000

MARKET COMMENTARY

FROM A CAPITAL MARKETS PERSPECTIVE

The major stock indexes surged around 5% last week, forming a V-shaped recovery on the steep losses they posted in the week prior, leaving stocks almost exactly where they were in mid-November. As last week ended a turbulent November, the S&P 500 added around 2% on the month, despite the nearly 7% gap between the index's peak on November 7th and low point on November 23rd. Apple's seven-year reign as the world's most valuable company by capitalization is over, as Microsoft took the top spot on Tuesday when it's stock rallied, boosting the equity market value of Microsoft's shares to $816B, just above Apple's $814B.

The value of all U.S. goods and services increased by $829B on the back of fiscal stimulus, which increased both government spending and household consumption. Jerome Powell eased fears of a more aggressive pace of interest-rate hikes when he states that rates are currently just below estimates of a neutral level, which sent major indexes soaring between 2% and 3% on Wednesday. After nearly a two-month slide, crude oil prices found some stabilization, but not before U.S. oil prices briefly dropped below $50 on Thursday, it's first time below that mark in 14 months.

The yield on the U.S. 10-year benchmark briefly fell below 3.00% on Thursday for the first time in more than two months. The benchmark has declined 11 times in the last 13 trading sessions. The recent decline in oil atop cooling inflation is expected to keep bond yields contained, in turn suggesting a more cautious Fed in 2019. Investors are expected to prepare for a more moderate growth in the coming year, shifting to more high-quality duration with fixed income, while remaining slightly overweight to stocks.

ADAM J. BUCHANAN
SENIOR VICE PRESIDENT

See pages 5-6 for current market rates

Market and other data within this report derived from Bloomberg and other sources deemed to be reliable.

MARKET REVIEW

MONEY MARKET RATES

	11/30/18	1 WEEK AGO	1 MONTH AGO	1 YEAR AGO
Prime Rate	5.25	5.25	5.25	4.25
Federal Funds (weekly average)	2.18	2.18	2.18	1.13
90 Day T-Bills	2.35	2.39	2.25	1.26
30-Day Commercial Paper (taxable)	2.27	2.25	2.25	1.18
Libor (30-day)	2.34	2.31	2.31	1.37
7 Day Tax-Exempt VRDB	1.69	1.69	1.61	0.97
Daily Rate Average	1.72	1.69	1.61	0.93

COMPARATIVE YIELDS

	TAXABLE REVENUE									
	GOVT	A		MMD	NR**	NR*	BB	BBB	A	AAA
1 Year	2.67	3.12	1 Year	1.87	3.12	3.22	3.02	2.57	2.27	2.07
5 Year	2.83	3.68	5 Year	2.17	3.57	3.67	3.42	3.02	2.77	2.52
7 Year	2.91	3.96	7 Year	2.31	3.86	4.06	3.66	3.31	3.11	2.76
10 Year	3.00	4.25	10 Year	2.54	4.38	4.54	4.04	3.69	3.44	2.99
30 Year	3.30	4.90	30 Year	3.24	5.09	5.24	4.74	4.39	4.14	3.69

(Representative of retail sales.); (** Representative of institutional sales.)*

TAX-EXEMPT MARKET INDICATORS

Bond Buyer	THIS WEEK	LAST WEEK	CHANGE	2018 HIGH	LOW
20 Bond Index	4.22	4.26	-.03	4.37	3.44
11 Bond Index	3.73	3.76	-.03	3.85	2.94
Revenue Bond Index	4.68	4.75	-.07	4.88	2.92
30 Year MMD	3.24	3.28	-.04	3.44	2.56
Weekly Tax-Exempt Volume (Bil)	4.92	0.58	+4.34	11.11	0.71
30 Day T/E Visible Supply (Bil)	10.40	6.09	+4.31	14.29	0.63
30 year “A” Rated Hospitals as a % of 30 Year Treasuries	125.45	126.66	-1.21	128.37%	111.81%

INTEREST RATE COMPARISON

DATE	7-DAY T/E VRDB	PRIME RATE	FED FUNDS WEEKLY AVG.	13-WEEK T-BILL RATE	C.P.RATE TAXABLE	LIBOR (30-DAY)	30-YEAR T/E BONDS (A-AAA)		
11/30/18	1.69	5.25	2.18	2.35	2.27	2.34	4.14	-	3.69
11/23/18	1.69	5.25	2.18	2.39	2.25	2.31	4.18	-	3.73
11/16/18	1.66	5.25	2.18	2.36	2.34	2.31	4.25	-	3.80
11/09/18	1.62	5.25	2.18	2.35	2.29	2.31	4.34	-	3.89
11/02/18	1.61	5.25	2.18	2.25	2.25	2.31	3.83	-	3.38
10/26/18	1.60	5.25	2.17	2.32	2.23	2.29	4.24	-	3.79
10/19/18	1.57	5.25	2.17	2.26	2.27	2.28	4.30	-	3.85
10/12/18	1.53	5.25	2.16	2.21	2.24	2.27	4.26	-	3.86
10/05/18	1.53	5.25	2.16	2.21	2.21	2.28	4.11	-	3.76
09/28/18	1.56	5.25	1.97	2.19	2.13	2.24	4.01	-	3.66
09/21/18	1.48	5.00	1.91	2.12	2.10	2.21	4.03	-	3.68
09/14/18	1.49	5.00	1.91	2.10	2.06	2.16	3.94	-	3.59
09/07/18	1.49	5.00	1.91	2.13	2.04	2.12	3.86	-	3.51
08/03/18	1.29	5.00	1.90	2.00	1.94	2.08	3.80	-	3.50
07/06/18	1.19	5.00	1.90	1.91	1.96	2.09	3.67	-	3.37
06/01/18	1.06	4.75	1.69	1.91	1.86	1.98	3.62	-	3.32
05/04/18	1.61	4.75	1.68	1.83	1.85	1.92	3.80	-	3.50
04/06/18	1.60	4.75	1.68	1.71	1.82	1.89	3.78	-	3.48
03/02/18	1.09	4.50	1.38	1.63	1.65	1.67	3.82	-	3.52
02/02/18	1.08	4.50	1.39	1.48	1.49	1.57	3.73	-	3.43
01/05/18	1.47	4.50	1.41	1.40	1.50	1.55	3.36	-	3.06
12/01/17	0.97	4.25	1.13	1.26	1.18	1.37	3.59	-	3.29

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