

CREDIT OPINION

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Rush System for Health, IL

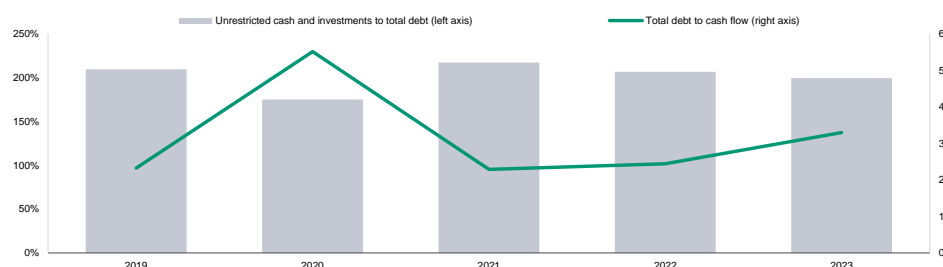
Update to credit analysis

Summary

Rush System for Health (Rush, A1 stable) will benefit from its reputable academic medical center (AMC) and its ongoing expansion in the ambulatory arena, which will help support its solid market presence. Its integrated medical school and streamlined governance structure provide greater flexibility than university-owned AMCs. Management will continue to build partnerships that diversify offerings in non-hospital settings. Rush's new neurology and oncology as well as other outpatient centers will offer growth opportunities. Fiscal 2024 capital spend will exceed muted cash flow, as it did in fiscal 2023, dampening cash levels. However, despite temporary moderation, balance sheet measures will remain solid and will rebound thereafter. Management forecasts meaningful improvement in operating cash flow (OCF) margins in fiscal 2025, aided by better volume trends and operating efficiencies. Ongoing challenges include an intensely competitive, fragmented market, with multiple prominent AMCs and significantly larger systems. Above average levels of Medicaid and high reliance on 340B benefits will also provide uncertainty.

Exhibit 1

Anticipate manageable leverage, as measured by cash to debt and debt to cash flow



Cash to debt ratios for fiscal 2020, 2021 and 2022 exclude Medicare advances and FICA funds.

Source: Moody's Investors Service

Credit strengths

- » Solid market presence supported by its reputable AMC; growth aided by focus on asset-light opportunities, including partnerships
- » More flexible AMC structure and streamlined governance structure aid ongoing efficiencies and growth
- » Days cash will moderate somewhat but remain solid; significant restricted cash will help bolster balance sheet

- » Manageable leverage as measured by cash to debt and debt to cash flow

Credit challenges

- » Highly competitive and dynamic market, with multiple AMCs, meaningfully larger health systems, and a major commercial payer
- » Sector-wide labor shortages and expenses will continue to contribute to more moderate margins compared to historical highs
- » Capital spend in excess of cash flow generation will reduce financial flexibility; achievement of 8%-9% OCF margins will be critical to funding future spend
- » Above average exposure to Medicaid highlights flagship's demographic challenges; 340B benefits provide some uncertainty

Rating outlook

The stable outlook reflects ongoing improvement in operating performance such that operating cash flow margins approach 8% within the next 12-18 months. The outlook also assumes the system will still sustain solid, albeit diminished cash measures as capital spending exceeds cash flow.

Factors that could lead to an upgrade

- » Material sustained improvement in liquidity and leverage including days cash and cash to debt
- » Larger enterprise size, improved market share and volume trends
- » Sustained and meaningful improvement in operating performance including OCF margins

Factors that could lead to a downgrade

- » Inability to realize and sustain operating performance that can fully fund capital needs and allows maintenance of debt to cash flow below 3 times
- » Decline in liquidity or increase in leverage including days cash or cash to debt sustained below 180 or 175%, respectively
- » Loss of market share or revenue pressures associated with a challenging payer environment

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

Rush System for Health

	2019	2020	2021	2022	2023
Operating Revenue (\$'000)	2,605,220	2,650,363	2,998,072	3,160,358	3,351,626
3 Year Operating Revenue CAGR (%)	6.4	5.4	7.6	6.7	8.1
Operating Cash Flow Margin (%)	7.8	3.4	9.7	8.4	5.6
PM: Medicare (%)	38.7	38.9	39.2	40.7	40.8
PM: Medicaid (%)	20.5	20.3	21.1	21.6	23.2
Days Cash on Hand	196	257	290	234	208
Unrestricted Cash and Investments to Total Debt (%)	209.4	185.2	243.3	212.7	199.5
Total Debt to Cash Flow (x)	2.3	5.6	2.2	2.4	3.3

Based on financial statements for Rush System for Health; fiscal year ending June 30; investment returns normalized at 5%. Cash ratios for fiscal 2020, 2021 and 2022 include Medicare advances and FICA funds.

Source: Moody's Investors Service

Profile

Rush System for Health is comprised of 738-bed Rush University Medical Center (RUMC), an academic medical center in the city of Chicago with a health sciences university that has 2,800 students; 210-bed Rush Copley Medical Center (RCMC) in Aurora, IL; and 185-bed Rush Oak Park Hospital (ROPH) in Oak Park, IL, as well as the various subsidiaries and joint ventures of these entities. The system's clinically integrated network includes over 2,500 affiliated providers.

Detailed credit considerations

Market position

Rush will continue to operate in an intensely competitive, highly fragmented, but also consolidated market. The Chicago area includes four other academic medical centers (AMCs) and larger health systems, as well as a leading commercial insurer, Blue Cross Blue Shield of Illinois (part of [Health Care Service Corporation](#)). Rush's market presence and growth will be aided by its position as an integrated AMC with numerous health sciences programs and meaningful clinical research. Its flagship, RUMC, offers tertiary and quaternary services and is clinically renowned in several specialties, including orthopedics, neurosciences and cancer care, the latter two service lines bolstered by a new ambulatory care center. A streamlined governance structure will help Rush expand via partnerships.

Inpatient volume trends will continue to be soft with ongoing shifts to outpatient care and observation stays. Expansion of non-hospital based services, including strategically located outpatient centers, will aid growth and payer mix. High reliance on Medicaid (23.2%) provides risk especially as revenue from Medicaid managed care plans represent a key area of growth for Rush. On an individual facility basis, RUMC's inpatient and observation stay market share (3.6% as reported by management, across eight-counties) is in line with University of Chicago's AMC (at 3.8%) but below including Northwestern Memorial's AMC (at 5.6%). RCMC and ROPH are likely to retain leading positions in their respective local service areas. On a system-wide basis, however, Rush's share (5.8%) will be considerably below that of [Advocate Aurora Health](#) (19%), [Northwestern Memorial HealthCare](#) (16.6%), [Northshore-Edward-Elmhurst Health](#) (13.8%), [Ascension](#) (10.9%) and the [University of Chicago Medical Center](#) (8.2%).

Operating performance and liquidity

Fiscal 2024 OCF margins will remain moderate (in the mid 5% range) and in line with fiscal 2023, excluding 340B recoupment of about \$49.2 million. Despite an unexpectedly weak Q1 FY24, management believes a continued rebound in suppressed volume trends, as well as cost and revenue generating initiatives, will allow Rush to achieve close to 8% OCF margins in fiscal 2025.

Rush will continue to receive significant operating income benefits from the 340B federal drug discount program. Despite ongoing push-back by manufacturers on contract pharmacy participation, management expects operating income from the program to increase as its oncology program expands.

Liquidity

Days cash will decline but remain solid, at about 190 days in fiscal 2024. Because capital spend will again exceed OCF levels, this will reflect an anticipated decline of another 10 days as it did in fiscal 2023. To be noted, Rush will also benefit from the presence of restricted cash, which was about \$760 million at fiscal year end 2023.

Although annual capital levels will be lower than prior years, having completed the 10 story ambulatory facility in 2022, spend will be in the \$1.2 billion range over the next five years. Management believes it will need to generate OCF margins in the 8%-9% range to fully support capital needs including strategic investments. No new debt is anticipated, but philanthropy will continue to help fund projects.

Debt structure and debt covenants

Leverage as measured by debt to cash flow will improve from somewhat elevated but still manageable fiscal 2023 levels (of over 3.0 times) as OCF margins improve. The rating and outlook assume this measure will fall to and be sustained below 3.0 times. Cash to debt will remain solid and roughly in line with fiscal 2023 levels of close to 200% in fiscal 2024 but will likely improve as absolute cash levels rise thereafter. Rush repaid ROBOC debt of about \$40 million in November 2023. However, beginning in fiscal 2023, Moody's included a five year loan that Rush guarantees related to a JV with Select Medical for its rehabilitation expansion. The loan amount at fiscal year end 2023 was about \$39.6 million but will rise to about \$75 million by fiscal year end 2024.

Debt structure

Rush's debt structure will remain relatively straightforward, limiting debt structure risk. About 90% of total gross debt is fixed rate.

Rush will have sufficient covenant cushion over the coming year. If historical debt service coverage falls below 1.1 times, it would require a consultant call-in. Issuance of additional debt would require: (1) minimum pro-forma debt service coverage of 1.10 times; or (2) minimum historical debt service coverage of 1.1 times.

Pensions

Effective December 31, 2022, Rush merged its two separate plans; combined overfunding was about \$.5 million at fiscal 2023. With moderate operating leases, cash to total adjusted debt will be good (coming in at about 179% for fiscal 2023.)

Legal security

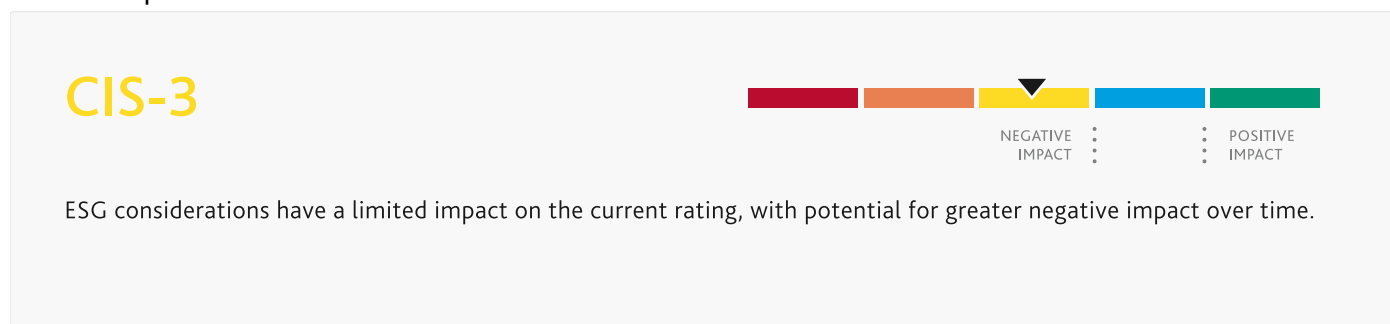
All bonds are secured by a gross revenue pledge of the Rush Obligated Group, consisting of Rush System for Health (the system parent), Rush University Medical Center, Copley Memorial Hospital, Rush Copley Medical Center, Rush Copley Foundation, Copley Ventures, Rush Oak Park Hospital, and Rush Copley Medical Group NFP.

ESG considerations

Rush University Med. Ctr. Oblig. Group, IL's ESG credit impact score is CIS-3

Exhibit 3

ESG credit impact score

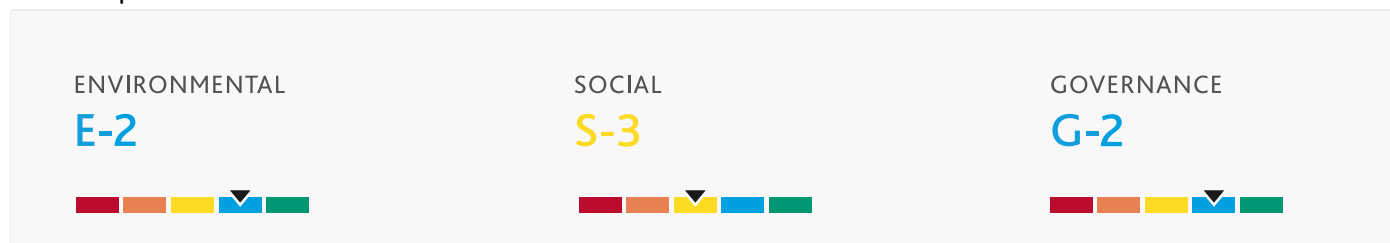


Source: Moody's Investors Service

ESG considerations have a limited effect on Rush's credit quality, with the potential for greater impact over time. The system has moderate exposure to industry-wide risk stemming from reliance on governmental payers and labor challenges. These risks are mitigated by the presence of unrestricted cash.

Exhibit 4

ESG issuer profile scores



Source: Moody's Investors Service

Environmental

Credit exposure to environmental risk is immaterial, with all subfactors in line with sector norms.

Social

Credit exposure to social considerations is moderate, reflecting a balance of several factors. Rush's exposure to demographic and societal trends is consistent with the sector norm and reflects industry reliance on governmental payers and the potential impact of regulatory issues. Rush's reliance on Medicaid is somewhat above average at about 23% of gross revenues. Industry-wide labor challenges also contribute to moderate risk for human capital. Rush's customer relations score compares favorably to the sector, reflecting its flagship's standing as a reputable tertiary and quaternary academic medical center (AMC), which is integrated with its health sciences university (comprised of its school of medicine, nursing school and other programs). Rush's focus on non-hospital based services will help expand its presence in a an intensely competitive and highly fragmented, but also consolidated market, which includes four other AMCs.

Governance

Credit exposure to governance considerations is limited, in line with the industry norm. Senior management, including a new COO with prior experience at a large integrated health system, will focus on partnerships and asset-light investments. Rush will continue to benefit from a streamlined single parent governance structure, which includes a smaller and more focused parent board, instituted in 2017. Management believes that this structure will position Rush well for further expansion.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

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