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CREDIT OPINION
24 November 2017

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RATINGS

Hospices Civils de Lyon

Domicile	France
Long Term Rating	A1
Type	LT Issuer Rating - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Hospices Civils de Lyon

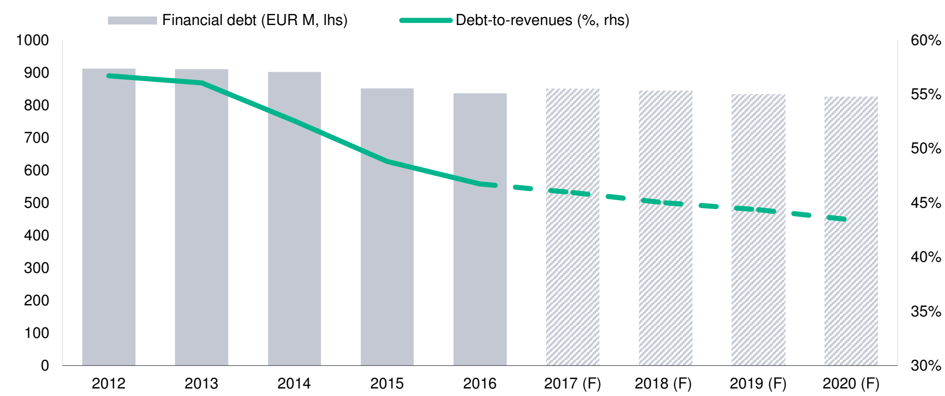
New rating

Summary

The Hospices Civils de Lyon's (HCL) A1/Prime-1 issuer ratings with a stable outlook reflect its strategic positioning and close relationship with the Government of France (Aa2 stable) which funds, regulates, oversees, monitors and controls the hospital. A high probability of central government support if HCL faced acute liquidity stress is a key factor in the ratings. Our view of HCL's creditworthiness is also supported by our expectation that its financial situation will further improve, and by the hospital's strong financial management, committed to efficiency. A still high debt burden and reduced liquidity levels are credit challenges.

Exhibit 1

Debt burden remains high, though debt deleveraging is on track



Sources: HCL, Moody's Investors Service

Credit strengths

- Strategic positioning and close relationship with the central government
- Excellent financial management, committed to efficiency
- Continued significant improvement in financial situation

Credit challenges

- Still high debt burden
- Reduced liquidity coverage by international comparison, though with regular and highly predictable cash flow

Rating outlook

The rating outlook is stable.

Factors that could lead to an upgrade

» A continued improvement in HCL's financial performance

» An upgrade of the Government of France's rating, given its close operational and institutional links with the hospital, could generate upward pressure on the rating

Factors that could lead to a downgrade

» A downgrade of the Government of France's rating

» A sustained deterioration in HCL's financial performance

» A significant increase in the hospital's debt burden

Key indicators

Exhibit 2

Key indicators

	2011	2012	2013	2014	2015	2016
Social security revenue as % of total revenue [1]	77.4%	75.9%	75.3%	73.6%	74.8%	74.7%
Surplus (deficit) as % of total revenue	0.6%	1.3%	0.7%	-0.2%	-0.6%	1.5%
Operating Cash Flow Margin (%)	3.8%	4.5%	5.2%	3.8%	5.1%	5.4%
Debt-to-total revenue (%)	59.8%	56.7%	56.1%	52.5%	48.8%	46.7%
Total debt to Cash flow	9.76	8.17	8.43	11.21	8.53	7.26

[1] HCL's main budget

Sources: HCL, Moody's Investors Service

Profile

Hospices Civils de Lyon (HCL) is a flagship French public hospital in the Auvergne-Rhône-Alpes region. Its 14 institutions, which are organised into five hospital complexes, offer a broad range of services, including general and specialised care. As a leading healthcare institution in France, both for patient care and research, the hospital is fully affiliated with the University of Lyon for teaching and research activities. This enhances its standing and capacity to attract leading physicians and scientists.

Detailed credit considerations

Baseline credit assessment

HCL's rating combines: 1) a baseline credit assessment (BCA) of a3; and 2) a high likelihood of extraordinary support from the central government if it faced acute liquidity stress.

Strong regulatory framework and increased ongoing support in the context of national fiscal consolidation

The central government, which funds, regulates, oversees, monitors and controls the healthcare sector, is responsible for delivering core healthcare services in France. French public hospitals have the special legal status of "public health establishments" (établissements publics de santé, or EPS), enacted by the Code de la Santé Publique (Public Health Code). As such, they fulfil the central government's mandate to provide healthcare services in their respective local areas.

To implement national policy locally, regional health agencies (RHAs) monitor and control hospitals in their respective regions. State agency ANAP (Agence Nationale d'Appui à la Performance des établissements de santé et médico-sociaux) also supports hospitals, particularly during periods of internal reorganisation or property management projects. Healthcare provision is funded through social security contributions, which cover the overwhelming majority of clinical services. Public hospitals' debt is consolidated in France's Maastricht debt.

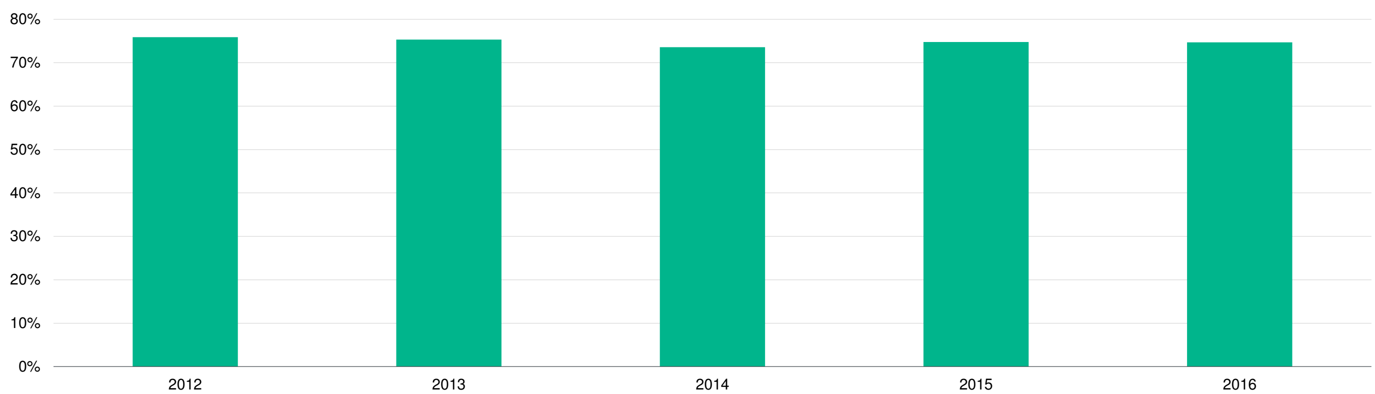
Since 2012, the central government has reaffirmed the centralisation process and tightened its oversight of the healthcare sector in the context of national fiscal consolidation. Interministerial committee COPERMO (Comité interministériel de la performance et de la modernisation de l'offre de soins hospitaliers) coordinates investment plans at the national level, while hospitals' new borrowing, capital spending, budgets and liquidity plans are currently subject to authorisation. These framework enhancements allow the central government to act long before a hospital experiences serious financial difficulties. For hospitals facing financial distress, their respective RHA establishes and monitors a financial recovery trajectory. The RHA also has the authority to place hospitals under provisional administration.

As a hospital that has experienced financial difficulties, HCL signed an agreement with the Auvergne-Rhône-Alpes RHA to balance its budget (contrat de retour à l'équilibre financier, or CREF) by 2019, which COPERMO validated. The agreement defines performance benchmarks in respect of clinical volumes and financial outcomes. The RHA also pre-approves the hospital's budget, capital spending and financing plans. HCL's "flagship" status enhances the institutional proximity between the hospital and the central government. Moreover and as for all the French public hospitals, Social security contributions account for a large and stable share of HCL's revenue (74.7% of its main budget revenue in 2016).

We consider the strong regulatory and institutional framework, as well as the high operational and financial links between the central government and HCL, to be key factors in the ratings.

Exhibit 3

Social security contributions account for a large and stable share of HCL's revenue
HCL's main budget



Sources: HCL, Moody's Investors Service

Regional approach to healthcare provision reinforces strategic positioning

HCL is the second largest public hospital in France, with total revenue amounting to €1.8 billion as at FYE2016 and 23,000 employees. The hospital has a reputation for providing high quality care and counts specialists in a wide range of medical disciplines among its staff. As of the end of 2016, it had a strong 35% market share of the local healthcare market[1]. In addition to serving the local community and surrounding areas, the hospital is considered as a benchmark for medical technics and innovation at the national and international level, providing services and support to other local hospitals. HCL's market position is also enhanced by its strong research profile, being fully affiliated with the University of Lyon. We consider the hospital's status as a cornerstone of France's healthcare system to be a strong credit positive factor.

Favourable service area demographics add to HCL's strong market position. The Auvergne-Rhône-Alpes region, its local service area, is France's second wealthiest region, accounting for 12% of the national population and 11.4% of national GDP (2014 data). The region also systematically records lower than average unemployment rates (estimated 8.3% versus 9.3% in mainland France at the end of Q1 2017). In addition, HCL is one of the largest property and land owners in the Lyon area. Assets have been accumulated through gifts and bequests since the 17th century, and comprises urban land and real estate.

Excellent financial management, committed to efficiency

We consider HCL's financial management to be excellent. Since 2009, the hospital has put two multi-annual efficiency programmes in place – CAP 2013 and Horizon 2017. The programmes aim to improve the hospital's financial performance through cost-cutting measures, optimising its medical activities and generating new revenue.

During this period, HCL has also reduced its personnel headcount and scaled back its capial expenditures policies. It has merged and restructured several of its locations, generating economies of scale, and developed its ambulatory surgery activity. The hospital has also implemented process improvement programmes, including enhancing its invoicing and purchasing policy. On the revenue side, HCL's management has systematically sought new sources of income. The hospital's property policy is a good example as HCL has been looking for opportunities to sell its real estate, realising an additional €130 million of revenue between 2009 and 2013.

On the operational side, HCL has developed good articulated business strategies and policies associated with long-range forecasts. In our view, its multi-year financial projections (état prévisionnel des recettes et dépenses) and financing plan (plan global de financement pluriannuel), approved by the central government, are conservative and confirm HCL's further commitment to efficiency.

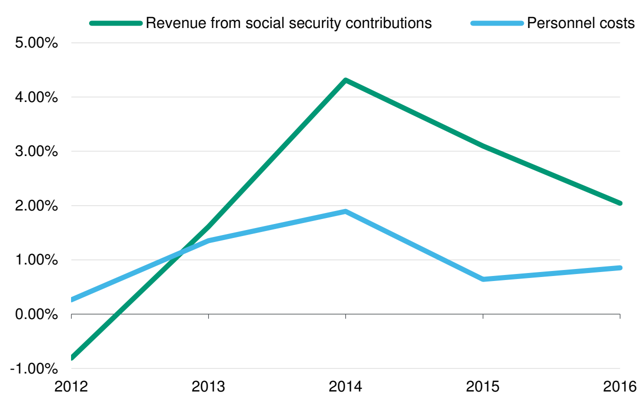
Significant improvement in financial situation to continue

After eight years of financial recovery measures, 2016 was the first year in which HCL achieved a quasi-balanced budget on its core operations (main budget). At the end of 2016, the hospital posted a financing deficit of €3.4 million, a significant improvement on its 2008 result (-€94.4 million). HCL also posted a consolidated surplus of €26.2 million in 2016, bolstered by its active asset sale policy.

Downsizing (1,200 jobs were cut between 2008 and 2016) and controlled growth in payroll has allowed HCL to outperform other French hospitals on average in respect of personnel costs. HCL's annual personnel growth rate has been below 2.0% since 2012 (0.9% in 2016 vs. an estimated 1.4% for the sector). Operating cash flow reached €94.9 million, or 5.4% of total revenue, in 2016, representing a continuous increase from its lowest level in 2008 (€9.3 million, or 0.6%). As a result, debt repayment coverage as measured by operating cash flow to debt repayment increased to 2.05x, compared with 0.03x in 2008.

Exhibit 4

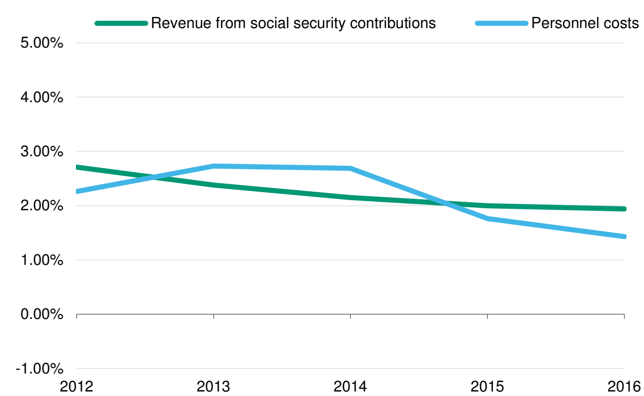
HCL's personnel costs growth vs. growth in revenue from social security contributions



Social securities contributions data pertains to HCL's main budget
Sources: HCL, Moody's Investors Service

Exhibit 5

Personnel costs growth vs. growth in revenue from social security contributions for the French hospitals sector

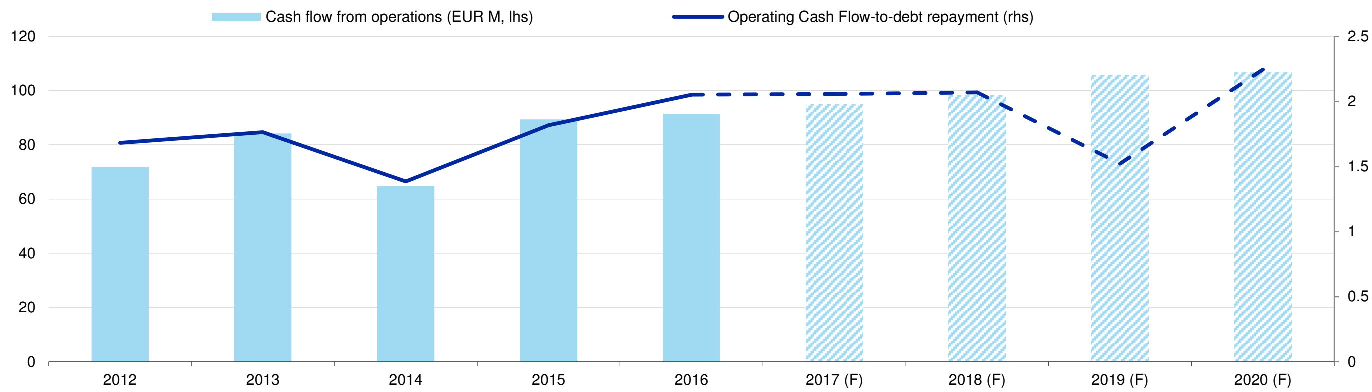


Source: Ministry of Heath, Moody's Investors Service

We expect the significant improvement in HCL's financial situation to continue. Based on the hospital's multi-year projections, we expect medical activities to grow by around 2% per year on average by 2020, thanks to plans to increase hospitalisation and HCL's recognised competitive advantage – the quality of its patient care. Moreover, in the context of the CREF signed with the Auvergne-Rhône-Alpes RHA in 2013, HCL committed to a further €108 million of savings by 2019. HCL's property policy will also generate additional revenue in the medium term, with real estate sales expected to realise €63.5 million by 2020. As a result, we expect operating cash flow to increase to around €107 million, or 5.6% of the hospital's revenue, by 2020, which will cover debt repayment for the year by 2.25x.

Exhibit 6

HCL's cash flow margins will continue to improve until 2020



Source: HCL, Moody's Investors Service

Debt burden remains high

As of YE 2016, HCL's direct debt stock amounted to €836.1 million or 46.7% of its revenue, representing a relatively high ratio compared with French peers. However, this level is considerably lower than the €911.9 million it posted at the end of 2012. The deleveraging was achieved due to the continuous improvement in HCL's financial performance, in line with targets set by the CREF signed with the Auvergne-Rhône-Alpes RHA.

Based on HCL's current financing plan, which comprises relatively stable capital spending until 2020 at around €120 million per year, we expect its debt stock to fall further, to €825.7 million, or 43.4% of revenue, by 2020. In addition, we expect the hospital's active propriety management policy to generate €63.5 million to finance capital spending and contribute to debt deleveraging. The payback ratio as measured by debt to adjusted cash flow (operating cash flow and asset sale surplus) should strengthen to 6.5 years vs. 7.3 years as of the end of 2016.

We consider HCL to have a prudent debt structure and cost-effective debt management, guided by diversification. As of YE 2016, 62.60% of its direct debt was at fixed rates, with an overall interest rate of 3.39%, slightly down from 3.45% as of YE 2015. We note that the hospital has access to a diversified pool of banks and that it has participated in three separate stand-alone bond issues. In 2016, it benefited from a zero-rate loan from French public bank Caisse des Dépôts et Consignations (Aa2 stable), as well as a loan from the German bank Bayern LB (€15.0 million). While HCL's debt repayments on average are evenly spread in terms of maturity, the hospital makes annual provisions (€7.2 million in 2016) in anticipation of bullet payments in 2019, 2023, 2025 and 2026.

Reduced liquidity coverage by international comparison, but regular and highly predictable cash flow

By design as a public not-for-profit hospital, HCL exhibits low cash positions when compared with international peers. This is mainly due to HCL's obligation to place its liquidity reserves in a non-interest-bearing account with the French Treasury, in line with other public sector entities in France. HCL's liquidity profile is mainly supported by its funding framework. Social security payments (72.6% of total revenue in 2016) are highly predictable and regular.

As of the end of 2016, HCL's cash reserves amounted to €44.8 million, or 1.0x its 2017 debt repayment. Moody's notes that this is materially higher than the level recorded in 2015 (€8.3 million). In addition, the hospital maintains €159 million in committed credit lines and a €33 million factoring contract, which it has not used in 2017. As these facilities are committed, we include them in our liquidity analysis.

HCL was also one of five French public hospitals that the central government authorised to issue short-term debt in 2016. Since then, it has regularly used its €85 million commercial paper programme. In 2017, it issued on average €25.0 million for a maturity of 30 days at very favourable interest rates.

Extraordinary support considerations

We assign a high likelihood of extraordinary support from the Government of France. This reflects our assessment of timely intervention by the central government, as illustrated by a bailout track record for French hospitals, coupled with HCL's strategic position in the French healthcare sector.

Rating methodology and scorecard factors

The principal methodologies used in these ratings were the Not-For-Profit Healthcare Rating Methodology, published in November 2015, and Government-Related Issuers Rating Methodology, published in August 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

Ratings

Exhibit 7

Category	Moody's Rating
HOSPICES CIVILS DE LYON	
Outlook	Stable
Issuer Rating	A1
Commercial Paper	P-1
ST Issuer Rating	P-1

Source: Moody's Investors Service

Endnotes

1 Agence Nationale d'Appui à la Performance des établissements de santé et médico-sociaux

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