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CREDIT OPINION
21 February 2022

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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 (France)

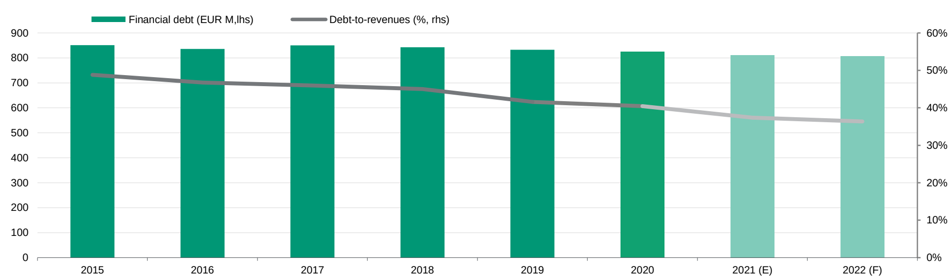
Update to credit analysis

Summary

The credit profile of Hospices Civils de Lyon (HCL, A1 stable/Prime-1) reflects its strategic positioning and close relationship with the Government of France (Aa2 stable), which funds, regulates, oversees, monitors and controls public hospitals. There is a high probability of HCL receiving central government support in case of acute liquidity stress, which is a key factor for the hospital's ratings. Our view of HCL's creditworthiness is also supported by its improved financial performance, and the hospital's strong financial management, with commitment to efficiency. The ratings are constrained by a high financial leverage, although metrics are improving, and relatively low liquidity levels. While the coronavirus pandemic is an operating and financial challenge, HCL benefits from the mitigating measures put in place by the central government.

Exhibit 1

HCL to continue deleveraging its high debt burden, despite the pandemic



E: Estimate; F: Forecast.
Source: HCL, Moody's Investors Service

Credit strengths

» Strategic positioning and close relationship with the central government

» Excellent financial management, with a constant commitment to efficiency

» Continued significant improvement in its financial situation

Credit challenges

» Financial leverage remains high, although constantly improving

» Reduced liquidity coverage compared with that of its international peers, although with regular and highly predictable cash flow

Rating outlook

The stable rating outlook reflects our expectation that the hospital will gradually reduce its debt burden while maintaining financial surpluses.

Factors that could lead to an upgrade

» A sustained improvement in HCL' financials, including a material impact from the central government's investment support plan and/ or improved operating margins, would exert upward pressure on the rating.

Factors that could lead to a downgrade

» A material deterioration in HCL's financial performance; a significant increase in the hospital's debt burden and/ or deterioration in the liquidity position would exert downward pressure on the ratings.

» Downward pressure on the ratings could also arise from a downgrade of France's rating. However, this is unlikely given the Government of France's current Aa2 rating with stable outlook.

Key indicators

Exhibit 2
Hospices Civils de Lyon (France)

	2016	2017	2018	2019	2020	E2021	F2022
Social security revenue as % of total revenue [1]	74.7%	74.6%	74.9%	73.6%	79.0%	77.2%	77.2%
Surplus (deficit) as % of total revenue	1.5%	2.3%	1.1%	1.8%	3.5%	1.6%	0.5%
Operating cash flow margin (%)	6.8%	7.6%	7.0%	7.3%	9.0%	6.5%	5.3%
Debt-to-total revenue (%)	46.7%	46.0%	45.0%	41.6%	40.5%	37.4%	36.4%
Total debt to cash flow	7.3	6.4	6.8	6.2	4.7	5.9	7.0

E: Estimate; F: Forecast
(1): Main budget
Source: HCL, Moody's Investors Service

Detailed credit considerations

HCL's credit profile, as expressed in an A1 stable rating, combines (1) a Baseline Credit Assessment (BCA) of a3, and (2) a high likelihood of extraordinary support from the French government in the event that the hospital faced acute liquidity stress.

Baseline Credit Assessment

Strategic positioning and close relationship with the central government

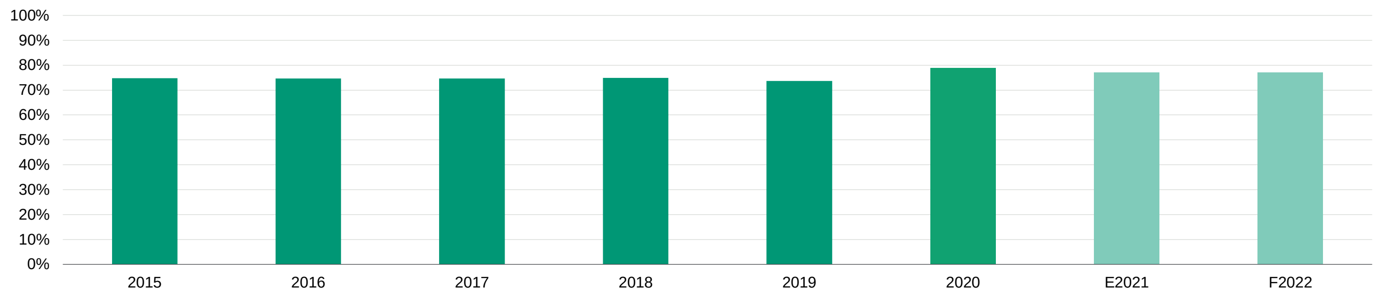
Being the second-largest public hospital in France, with 22,000 employees and over €2.0 billion of total revenue in 2020, HCL has a reputation for providing high-quality care and has top specialists in a wide range of medical disciplines among its staff. It held a strong 38% share of the local healthcare market in 2020 and 11% of the Auvergne-Rhône-Alpes region[1]. In addition to serving the local community and the surrounding areas, the hospital is considered a benchmark for medical technologies and innovation at national and international levels, providing services and support to other local hospitals. HCL's market position is also enhanced by its strong research profile, because of its affiliation with the University of Lyon. The hospital's status as a cornerstone of France's healthcare system is a strong credit positive.

Favourable service area demographics add to HCL's strong market position. The Auvergne-Rhône-Alpes Region, HCL's local service area, is France's second-wealthiest region, accounting for 12% of the national population, 11.5% of national GDP (2018 data) and registering lower-than-average unemployment rates (estimated at 7% versus 8.1% in mainland France as of the end of the third quarter of 2021). In addition, HCL is one of the largest property and land owners in the Lyon area, accumulating them through gifts and bequests since the 17th century.

The central government funds, regulates, oversees, monitors and controls the health care sector. French public hospitals have the special legal status of public health bodies (*établissements publics de santé* or EPS), enacted by the French Public Health Code (*Code de la Santé Publique*), and their debt is consolidated in France's Maastricht debt. Hospitals are monitored and controlled by regional health agencies (*Agences Régionales de Santé* or RHAs), the ANAP (*Agence Nationale d'Appui à la Performance*), a state agency and the newly created interministerial committee CNIS (*Conseil National de l'Investissement en Santé*), which replaces the COPERMO following the "Ségur de la santé" agreements in 2020-2021. New loans, capital spending, budgets and liquidity plans are subject to authorizations and are closely monitored.

Like all the French public hospitals, HCL earns a large and stable share of revenue from social security contributions (expected at 77% of its main budget revenue in 2022). We consider the strong regulatory and institutional framework, as well as the high operational and financial links between the central government and HCL, as key factors for its ratings.

Exhibit 3
Social security contributions account for a large and stable share of HCL's revenue
Share of social contributions as a percentage of HCL's main budget



E: Estimate; F: Forecast.
Source: HCL, Moody's Investors Service

Excellent financial management, with a constant commitment to efficiency
We consider HCL's financial management excellent. The hospital has successfully put in place multi-annual efficiency programmes, which aim to improve the hospital's financial performance through cost-cutting measures, optimisation of its medical activities and generation of new revenue. HCL's current programme, *Pulsations 2023*, aims at further improving its financials and at increasing fixed capital investment.

Past efficiency measures included reduction of personnel headcount; process improvement programmes, such as the enhancement of the invoicing and purchasing policy; and scale back of capital spending policies. Because of these measures, HCL reached its objective of achieving €50 million of cost savings on procurement during 2016-19. HCL has also merged and restructured several of its locations, generating economies of scale, and has developed its ambulatory surgery activities to increase revenue.

On the operational front, HCL has well articulated business strategies and internal policies associated with long-range forecasts. In our view, its multiyear financial projections and financing plan, approved by the central government, are conservative and confirm HCL's further commitment to efficiency.

Continued significant improvement in its financial situation
The coronavirus pandemic has been disturbing French hospitals' operations since March 2020, but we expect the impact on their finances to be limited thanks to the central government's support. On the revenue side, the central government put in place a guarantee on tariff-based activity proceeds (*tarification à l'acte, T2A*) in 2020 and extended it to H1 2022 [2], representing approximately 50% of HCL's revenues. We expect this guarantee to be extended as long as hospitals remain under pressure. On the expense side, the central government announced it would fully compensate (1) the coronavirus-linked expenses as well as (2) the salary increases and bonuses put in place. Being a flagship hospital with diverse income, HCL face losses on foreign patient income and other activities which to date are not compensated by the central government. Nevertheless, this marginal and transitory loss of income has no impact on the credit quality of the issuer.

Thanks to the central government' support and the continued effects of the efficiency measures put in place in the previous years, we expect HCL to maintain its surplus budget and operating cash flow margin in 2021. The issuer estimates its operating cash flow to amount to €137 million in FY2021, or 6.5% of total revenue, down from €175 million and 9% of total revenue in 2020 but in line with the trend set between 2016 and 2019. 2020 was an exceptional year in which HCL benefitted from emergency State support schemes which temporarily increased its metrics. The Segur de la Sante agreements also provided for an increase in the hospital's payroll (8% in 2020 vs an annual growth rate of 1.3% over 2013-2019 period). Although the central government took a clear commitment to compensate this increase, this was done with ad-hoc measures in 2020 and 2021. The evolution target of social security spending (Objectif National de dépenses d'assurance maladie, ONDAM) has increased by +6.7% in 2021 and +3.8% in 2022, excluding Covid-related expenses, in order to compensate for the increase in spendings induced by the Segur de la Sante. We expect HCL to maintain a tight control of personnel expenses, in line with the central government policies.

We expect HCL to benefit from the French government's 2022 roadmap for the health care sector, "Ma Santé 2022", with the shift towards quality based funding under IFAQ provision (higher quality hospitals receive more funding)[3]. HCL quality-based revenue increased in 2021, at €7.9 million against €3.2 million in 2019. However the amounts for 2022 are yet to be decided and we do not quantify and integrate this positive effect into our financial projections for HCL.

Financial leverage remains high, although constantly improving

HCL has a prudent debt structure and cost-effective debt management, guided by diversification with five bond issuances and a diverse portfolio of loans. In 2020, 72% of its direct debt had fixed rates, with an average interest rate of 2.88%, down from the 2019 average of 3.01%. HCL benefits from a very good presence in capital markets, as illustrated by its 2020 debt campaign, where it was offered 6x the amount requested (€40 million) by banks. While the hospital has 6 bullet payments, maturing in 2023, 2025, 2027, 2028, 2029 and 2030, HCL's debt repayments are evenly spread in terms of maturity. HCL completed its first bullet repayment in 2019 without any difficulties.

HCL estimates its direct debt stock at €812 million at year-end 2021 or 37% of its revenue, representing a relatively low level compared with that of its French peers. HCL's debt position has been on a downward trend since 2017 and should continue to decrease to €806 million or 36% of its revenue by 2022, thanks to the continuous improvement in HCL's financial performance. We consider the continuous debt deleveraging as a credit positive development. However the financial leverage as calculated by the unrestricted cash-to-total debt metric remains high at 35% in FY2021, given the hospital's reduced liquidity buffers (see paragraph on liquidity below).

As part of the Segur de la sante agreements the central government also announced it would fund an additional €2.5 billion of hospitals' capital spending over the next five years. The 10-year debt relief/ investment support mechanisms is detailed in individual contracts between hospitals, their RHA and the central government. HCL's share of the funding was agreed in late 2021 to €50 million to refit one of their hospitals, plus an envelope of €157 million for their capital expenditure program, paid down over 10 years. The additional funding in combination with its positive financial performance, will allow HCL to increase its capital spending to over €150 million annually over the next three years, from €134 million in 2020.

We expect this increased funding from the Central Government to translate into an increasing attractiveness of HCL, both on the national and international scale, in the medium term.

Reduced liquidity coverage compared with that of its international peers, although with regular and highly predictable cash flow

Designed as a public, not-for-profit hospital, HCL exhibits low cash positions compared with its international peers. This is mainly because of HCL's obligation to place its liquidity reserves in a non-interest-bearing account with the French Treasury, in line with other local public-sector entities in France, and the resulting incentive not to have cash inn excess. HCL's liquidity profile is nevertheless supported by its funding framework with highly predictable and regular social security payments.

At year-end 2021, HCL's cash reserves were estimated at €211 million, or 4.3x its debt service, down from a € 289 million of cash reserves or 6x of its debt service in 2020. Although decreasing, 2021 expected level is still above 2019 figures and in line with the continuous buildup of a cash buffer observed since 2016. Additionally, HCL maintains €71 million in committed credit lines and a €20 million factoring contract, neither of which was used in 2019 or 2020. HCL's liquidity ratios remain low compared to international peers and we expect them to decrease in 2021 at 54 days cash on hand, against 74 in 2020 and 69 in 2019. HCL's deleveraging is partly offsetting the decrease in their cash position. The low level of liquidity reserves, structurally part of the framework for French hospitals, represents a weakness of the issuer's credit profile, exposing them to external shocks.

HCL is also one of the five French public hospitals that the central government authorizes to issue short-term debt on financial markets. HCL regularly uses its commercial paper programme, which was increased to €100 million in 2020. In 2021, HCL's issuances averaged €35.9 million, at very favorable interest rates, -0.5% on average.

Extraordinary support considerations

We assess that there is a high likelihood of extraordinary support coming from the Government of France. This reflects our expectation of a 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. The central government's interventions during the coronavirus crisis, especially cash advances to vulnerable hospitals and liquidity facilities offered by State-owned banks, support our assessment.

ESG considerations

How environmental, social and governance risks inform our credit analysis of HCL

Moody's takes account of the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of HCL, the materiality of ESG to its credit profile is as follows:

Environmental risks are not material to HCL's credit profile. Natural hazards pose two types of risk to French public hospitals: high patient influx and/or damaged infrastructure. To mitigate the first one, prevention campaigns have been put in place at the national level and French hospitals have effective emergency plans ("*plan blanc*") to face their consequences. The second one is not material as hospitals are insured against it and the central government would step in if it was to be declared "natural disaster".

Social risks are material to HCL's credit profile through changing trends in demographics and demand for health care in the territory where the hospitals operate but also through the need to have a highly skilled work force. Factor 1 – "Market position" – in our scorecard captures those aspects. We also view the coronavirus pandemic as a social risk under our ESG framework, given the increased expenditure for hospitals and the disruption to their operations and consequently their revenues. This risk is mitigated by the central government's support and willingness to compensate the financial impact of the pandemic.

Governance considerations are material to HCL's credit profile. We assess financial management, budgetary practices, multiyear forecasts as well as the level of fixed capital investment in our scorecard.

All of these considerations are further discussed in the "Detailed credit considerations" section above. Our approach to ESG is explained in our report on how ESG risks influence sovereign credit profiles and our cross-sector methodology General Principles for Assessing ESG Risks.

Rating methodology and scorecard factors

The principal methodologies used for these ratings are the Not-For-Profit Healthcare rating methodology, published in December 2018, and the Government-Related Issuers Methodology, published in February 2020. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

Ratings

Exhibit 4

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

Source: Moody's Investors Service

Endnotes

1 According to ATIH (*Agence technique de l'information sur l'hospitalisation*).

2 See Public Hospitals – France Tight liquidity levels pose challenges amid coronavirus, but mitigants limit risks , *Arrêté du 6 mai 2020 relatif à la garantie de financement des établissements de santé pour faire face à l'épidémie du covid-19, and Loi du 22 janvier 2022 renforçant les outils de gestion de la crise sanitaire et modifiant le code de la santé publique*

3 Hospices Civils de Lyon and CHU de Lille Peer comparison – Health care sector reform is credit positive, but divergence in debt affordability will persist

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