TAX-EXEMPT CREDIT PERSPECTIVES: HEALTHCARE REVENUE BONDS APRIL 27, 2020

Healthcare Revenue Bonds

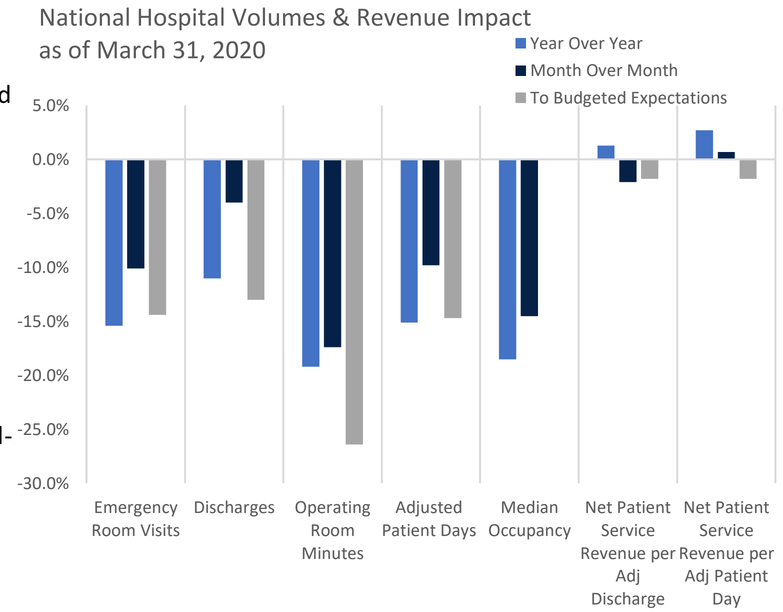
Non-profit hospitals and other healthcare facilities have long issued tax-exempt debt as part of their funding plans to help finance construction, facility improvements and other capital projects. Revenue generated from these institutions is used to pay debt service after covering the costs of running the healthcare facilities themselves. Hospital revenue are a meaningful part of the tax-exempt market mix, with 2019 bond issuance of $38.9 billion according to Bond Buyer.

An Altered Business Mix Creates Strains

Although hospitals are highly essential service providers, a global pandemic has significantly impacted their business mix and introduced financial strains. Elective, higher margin procedures and services are on hold as hospitals struggle to isolate and treat COVID-19 patients while managing the health and welfare of their employees.

Healthcare System Credit Profiles Differ Considerably

We are cautious on the healthcare sector but see significant credit differentiation among individual bond issuers. Volatility should continue as the economy slowly begins reopening, and the potential for a second wave of illness is a meaningful risk factor. Lower-rated hospitals, including those with smaller operating bases, weaker balance sheets, lesser financial resources, and stand-alone entities, face greater likelihood of downgrade or even bankruptcy and closure. However, as states pass their peak case loads and the economy starts to regain momentum, many hospitals, particularly larger, more sophisticated operators, will begin implementing well-planned transitions back towards more normal operations.



Source: Bond Buyer, Kaufman Hall

Stress-Testing Our Holdings

Appleton's Healthcare Revenue bond holdings are comprised of larger systems with diverse revenue streams, balance sheet strength and geographic diversity. We have stress-tested our holdings by modeling financial impact scenarios and believe the names we hold are well positioned to manage through this downturn, albeit with some financial and credit rating pressure in certain cases. Furthermore, our analysis did not account for $100 billion that will be directed to hospitals under the CARES Act, or any potential additional Federal funding.

What Credit Factors Are Most Important?

Our credit analysis is tailored to the nature of the healthcare sector and emphasizes the following metrics.

Unrestricted Cash & Days of Cash on Hand	Liquidity is essential as hospitals will draw on cash and equivalents to manage through the revenue and expenditure challenges they are experiencing. Those with more days cash on hand rank higher in our analysis.
Debt service coverage	Operating cash flow relative to debt service over the next 12 months offers a measure of the cushion available to absorb revenue shortfalls.
Cash to debt	Assessing cash and equivalents relative to outstanding debt offers an indication of financial health and leverage. We look for cash reserves to comfortably exceed debt obligations.
Operating revenue	This data point speaks to the size and potential financial flexibility of a healthcare organization's operating base.
Revenue diversity	We believe larger systems with broad geographic reach and revenue diversity will face less operational impact than more narrowly constrained providers. For this reason, our analysis looks at operational concentration and the number of states in which each system operates.

After evaluating each of our Healthcare Revenue bonds against these and other metrics, we believe all the names we hold are positioned to successfully manage through this strained environment. We are also comfortable adding to our healthcare holdings when our investment team feels market prices adequately compensate for perceived issuer specific risk.

Accessibility and communication are important in any environment, although these attributes are especially valuable during uncertain and volatile times. Appleton Partners is committed to sharing our market and portfolio management perspectives as developments unfold. We hope these briefs are helpful and also invite you to reach out to us directly and/or visit www.appletonpartners.com/Insights for additional commentary and insights.

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