Credit, Financial and Medical Implications of the Affordable Care Act (ACA) for Colleges & Universities

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ACA: A Credit Perspective

- ACA became law in 2010;
- The ACA is large, complex, phased-in over a number of years and enacted without bi-partisan congressional and full state support thus leading to significant operational and legal challenges;
- Initial reaction from a credit markets perspective for the not-for-profit higher education and healthcare sector has been negative due to uncertainty and financial impact on margins;
- Impact to date has been less pronounced than media headlines suggest as reform slowly evolves with healthcare impacted more from consolidation and change in revenue model than higher education sector where impact has largely been confined to benefit structure re-alignment and some organizational change;
Why the Continuing Credit Market Concern About the ACA? - Transformation Costs Largely Borne By Providers

• In municipal finance the higher education and healthcare sectors share these traits:
  • Negative sector outlooks with downgrades exceeding upgrades for the past few years (the rest of the municipal market has generally seen improving credit trends post Great Recession);
  • Some industry experts in these sectors forecast stronger competition leading to sluggish growth rates and pressured financial metrics;
  • Both are capital intensive industries requiring periodic capital infusion to maintain and enhance competitive position (access to capital is more of a credit differentiator when the cost of capital is high);
  • Rated issuers with average ratings in the ‘A’ category signifying a strong ability to repay financial obligations on a timely basis, however, we are seeing a number of issuers relying upon balance sheet strength from returns on investment portfolios rather than cash flow from earnings to support debt service and longer term this could become a credit issue;
Why the Continuing Credit Market Concern About the ACA? (continued)

• The ACA’s key tenet is access expansion through a variety of means and reforms such as encouraging a shift to value-based purchasing from a fee-for-service payment model in healthcare;

• We see the federal government and states pursuing similar objectives in higher education, at a slower pace, through different means that seek to constrain (tuition) pricing and make a portion of the revenue stream at risk from attainment of performance benchmarks;

• These various reform initiatives seek a fundamental transformation of the industry by shifting the risk and accountability for the transformation to the providers (colleges and universities or hospitals);

• The key levers of transformation are: value-based purchasing (pricing), greater integration (for efficiency leading to consolidation and decline of the private practitioner or full-time faculty member) and some level of risk and/or cost sharing;