Fitch Affirms Montereau, Inc.'s (OK) Series 2017 Rev Bonds at 'BBB-'; Outlook Stable

Fitch Ratings-New York-08 February 2018: Fitch Ratings has affirmed the 'BBB-' rating on the following Tulsa County Industrial Authority, OK bonds issued on behalf of Montereau, Inc. (the corporation):

--$106.5 million senior living community revenue bonds refunding series 2017.

The Rating Outlook is Stable.

SECURITY

The bonds are secured by a gross revenue pledge, a first mortgage lien (per ground lease), and a debt service reserve fund.

KEY RATING DRIVERS

STRONG CENSUS: Montereau continued its strong census across all levels of care in fiscal 2017 as evidenced by its 90% occupancy in independent living units (ILUs), 99% occupancy in assisted living units (ALUs), and 99% in its skilled-nursing facility (SNF). The corporation has demonstrated consistent improvement in ILU census since its expansion project was completed in 2012 and its ongoing strategic relationship with the area's largest hospital, St. Francis Hospital, has supported consistently robust census in its ALUs and SNF.

IMPROVING OPERATIONAL PERFORMANCE: Montereau continued to improve its operational performance in fiscal 2017 with an 92.5% operating ratio, 20.1% net operating margin (NOM), and 34.5% NOM-adjusted which all compare favorably to Fitch's 'BBB' category medians of 97.4%, 7.7%, and 21.2%, respectively. Additionally, this solid performance has been maintained in the six-month interim period (ending Dec. 31, 2017) as illustrated by the corporation's 93.9% operating margin, 18.1% NOM, and 30.3% NOM-adjusted.

INCREASING LIQUIDITY POSITION: At Dec. 31, 2017, the corporation continued to increase its unrestricted cash and investment position to $43.1 million which translates into 498 days cash on hand (DCOH), 34.8% cash to debt, and 5.4x cushion ratio and shows mixed results when compared to Fitch's 'BBB' category medians of 396, 61.5%, and 8x, respectively. However, Montereau's liquidity position remains substantially higher than fiscal 2013 when it had $18.9 million in unrestricted cash and investments, reflecting its strong census and improving operational performance over the last few years. Fitch expects Montereau's liquidity levels to continue to grow over the coming years.

HIGH DEBT BURDEN: The corporation's debt burden remains elevated as maximum annual debt service (MADS) equated to a high 22.6% of fiscal 2017 revenues, which is well above the category median of 12.4%. However, Montereau has demonstrated sufficient coverage levels in fiscal 2017 as evidenced by its 1.9x MADS coverage and 1.1x revenue-only coverage which both remain on par or favorable to Fitch's 'BBB' category medians.

RATING SENSITIVITIES

WEAKENING OPERATIONS: The 'BBB-' rating incorporates expectations that Montereau will further build liquidity levels while maintaining sufficient coverage levels. Failure to improve its liquidity position in the short to medium term and/or an erosion of its current operating profile could result in negative rating action.

CREDIT PROFILE

Montereau, Inc. is a continuing care retirement community located on a 50-acre site in Tulsa, OK. The community originally opened in 2003 with 254 ILUs, 37 ALUs, and 45 SN beds. Following completion of their Phase II expansion project in 2012, and as it stands today, the community has 328 ILUS, 73 ALUs, and 74 SN beds. The corporation has 34 independent living garden homes/cottages and 29 memory support units which are factored into the total ILUs and ALUs, respectively. The corporation offers three types of resident contracts: 90% refundable contract (Type B), a 0% refundable contract (Type B), and a 70% refundable contract (Type A). All three contracts require an upfront entrance fee and ongoing monthly fees.

Members of Montereau, Inc. elect the Board of Directors. Currently, the three members of the corporation are the current President and CEO of Montereau, the President and CEO of Saint Francis Health System, and the CEO and Vice Chairman of The William K. Warren Foundation. Fitch views the working relationship between the corporation, Saint Francis Health System and The William K. Warren Foundation favorably. In fiscal 2017, the corporation had total operating revenues of $35.6 million.

SOLID CENSUS

Montereau has consistently improved its ILU occupancy levels following its expansion project in 2012. Over the last five fiscal years, the corporation's ILU occupancy rates were 90% (fiscal 2017), 89% (fiscal 2016), 89% (fiscal 2015), 82% (fiscal 2014), and 80% (fiscal 2013). Additionally, the corporation has maintained its 90% ILU census through the six-month interim period. The improvements in ILU occupancy over the last five years is largely attributed to increased marketing efforts, a strong reputation in the local community, and the corporation's favorable location in the heart of Tulsa. While Montereau has two nearby competitors, Inverness Village and Oklahoma Methodist Manor, its favorable location and strong reputation should continue to support ongoing demand for its services.

Additionally, Montereau has maintained robust census in their ALUs and SNF in recent years as evidenced by their 99% census averaged in both ALUs and SNF during fiscal 2017. The corporation has averaged 98% occupancy in their ALUs and 95% in their SNF during fiscal years 2013-2016. These strong occupancy rates are largely attributed to its strategic affiliation with St. Francis Hospital, which is a 704-bed acute care hospital that is located within a mile of Montereau's campus. The strategic relationship with St. Francis Hospital is viewed as a credit positive and should continue to support demand for the corporation's ALUs and SNF.

IMPROVING OPERATIONS AND LIQUIDITY LEVELS

The corporation has demonstrated consistent improvement in their operational performance since fiscal 2013 following their expansion project in 2012. In fiscal 2017, Montereau had an operating ratio of 92.5%, NOM of 20.1%, and NOM-adjusted of 34.5% which all compare favorably to Fitch's 'BBB' category medians of 97.4%, 7.7%, and 21.2%, respectively. Additionally, fiscal 2017's performance remains significantly better than fiscal 2013 when the corporation had a 115.6% operating ratio, 14.9% NOM, and 29% NOM-adjusted. The improvement in performance is attributed to improved ILU occupancy levels, coupled with solid expense/cost management.

In addition to consistently improving operational performance, the corporation has also consistently increased their liquidity position. Through the six-month interim period, Montereau improved their unrestricted cash and investment position to $43.1 million, which translates into 498 DCOH, 34.8% cash to debt, and 5.4x cushion ratio.

These metrics remain mixed when compared to Fitch's 'BBB' category medians of 396, 61.5%, and 8x, respectively. However, the corporation's total liquidity position at the interim period is 128% higher than fiscal 2013 levels, which reflects Montereau's solid census levels, improving operational performance, and effective cost management in recent years.

DEBT PROFILE

The corporation has approximately $121 million outstanding in long-term debt which is comprised of the $106.5 million in series 2017 bonds and approximately $14 million in series 2015AB bonds. The series 2015AB bonds are directly placed with Mabrey Bank. The corporation's long-term debt is entirely fixed-rate, has a final maturity of 2045, and has a MADS of approximately $7.9 million. Montereau's high debt burden remains a credit concern as MADS equated to a high 22.6% of total fiscal 2017 which remains weaker than the 'BBB' category median of 12.4%. However, the corporation's coverage levels have been solid as evidenced by MADS coverage of 1.9x and revenue-only coverage of 1.1x in fiscal 2017, which both remain on par or better than category medians of 2.2x and 0.8x, respectively. Overall, concerns over Montereau's debt burden are mitigated by its solid census across all levels, its increasing liquidity position, and its improving operational performance.

DISCLOSURE

Montereau covenants to provide audited financial statements, covenant calculations, and annual occupancy reports no later than 150 days after each fiscal year end. Additionally, the corporation covenants to provide unaudited financial statements, covenant calculations, and quarterly occupancy reports no later than 45 days following each fiscal quarter. All reports are expected to be made available via Municipal Securities Rulesmaking Board's EMMA website.

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Applicable Criteria
Not-for-Profit Continuing Care Retirement Communities Rating Criteria (pub. 04 Aug 2015) (https://www.fitchratings.com/site/re/868824)
Rating Criteria for Public Sector Revenue-Supported Debt (pub. 05 Jun 2017) (https://www.fitchratings.com/site/re/898969)

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