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SECTOR IN-DEPTH
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Healthcare – North America

Credit stress is rising, setting the stage for more downgrades and defaults

Summary

» **The healthcare sector's credit default risk is rising.** So far this year, the ratings of 25 North American healthcare companies[1] have been downgraded to B3 negative or lower, representing a material deterioration in the sector's credit quality. Healthcare now accounts for approximately 16% of the companies on our B3 Negative and Lower List, [2] compared to less than 4% at 31 December 2015. About 80% of North American healthcare companies are now speculative grade, compared to around 73% in 2015.

» **Nearly 90% of healthcare companies rated B3 negative or below are owned by private equity.** Attracted by healthcare's historical stability and buoyed by accommodative debt markets, financial sponsors have aggressively consolidated fragmented subsectors, including physician practices, emergency medicine and anesthesiology, to name a few. The resulting roll-ups carry high levels of debt, which will pressure their cash flow and limit their ability to adapt to the changing macroeconomic environment, as well as to increasing social risk, new legislation and litigation.

» **Capital structures will become unsustainable**. Many healthcare companies rated B3 negative or lower started 2022 with high financial leverage, high levels of floating-rate debt and weak operating performance. With interest rates rising, they now have to contend with higher financing costs amid a backdrop of persistent inflation and slowing economic growth that will pressure earnings well into 2023. Finding lenders willing to refinance will become increasingly difficult in the year ahead as the market retrenches.

» **Recent defaults offer insight into the future.** Thirteen healthcare companies have defaulted since January 2020, with high leverage and weak operating performance as the two main culprits. Operating weakness came from a variety of sources, including technological obsolescence, shortages in skilled labor or increases in labor costs, changes in the operating environment or simple mismanagement. For some defaulters, disruption caused by the COVID-19 pandemic was the last straw.

» **We expect distressed exchanges to remain the most common type of default**. Companies with unsustainable capital structures will need to cut their cash interest expense by either seeking to convert their debt to payment-in-kind (PIK) obligations, completing debt-to-equity conversions, or through debt extensions. Lenders will likely accept these maneuvers in order to avoid borrowers filing for bankruptcy, which would result in greater losses.

Healthcare's credit default risk is rising

Credit stress is rising in healthcare, which has long been considered a defensive sector for credit investors. So far this year, the ratings of 25 North American healthcare companies have been downgraded to B3 negative or lower. Among 193 rated North American-based healthcare companies, 34, or nearly 18%, were rated B3 negative or lower as of 30 November 2022, up from nine, or about 4% of rated healthcare companies at 31 December 2015. About 80% of North American healthcare companies are now speculative grade, as compared to around 73% in 2015 and 71% in 2010.

In another sign of rising credit stress, healthcare companies represent approximately 16% of the 207 companies on our B3 Negative and Lower List (B3N List) as of 30 November 2022, as compared to less than 4% of B3N List companies at 31 December 2015. Updated monthly, the B3N List includes all nonfinancial corporate issuers in the US that meet our proprietary definition of credit stress – those with a Probability of Default Rating (PDR) of Caa1-PD or lower, or B3-PD with a negative rating outlook or review for downgrade.

Exhibit 1 shows the issuers on the List that are rated under healthcare-specific methodologies; i.e. Pharmaceutical or Medical Device Industry rating methodologies. The remaining companies are largely rated under the Business and Consumer Services Industry methodologies, but are included as they derive a substantial majority of their revenue from providing healthcare-related services. Exhibits 2 and 3 show the healthcare companies on the List by subsector, demonstrating that the industry's credit stress is broad based.

Exhibit 1

Stress test

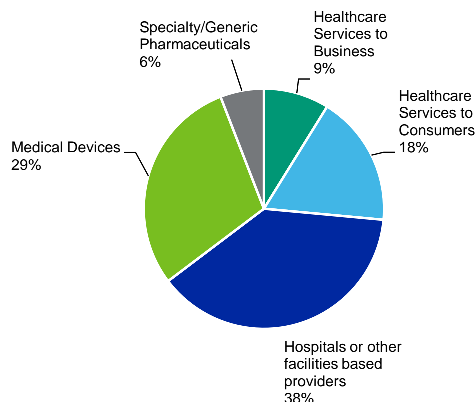
Healthcare companies with a probability of default rating (PDR) of B3-PD with a negative outlook, or lower, as of 30 November 2022

Issuer Name	PDR	CFR	Outlook	Industry Sector
Air Methods	Caa3-PD	Caa3	Stable	Healthcare Services to Business
Akorn Operating Company	Caa2-PD	Caa2	Stable	Specialty/Generic Pharmaceuticals
Akumin	Caa2-PD	Caa2	Stable	Hospitals or other facilities based providers
Alcami Corporation	Caa1-PD	Caa1	Stable	Healthcare Services to Business
Athletico Holdings	B3-PD	B3	Negative	Hospitals or other facilities based providers
Avalign Holdings	Caa1-PD	Caa1	Stable	Medical Devices
Aveanna Healthcare	Caa1-PD	Caa1	Negative	Hospitals or other facilities based providers
Bausch Health Companies	Caa3-PD	Caa2	Negative	Specialty/Generic Pharmaceuticals
BVI Holdings Mayfair Limited	Caa1-PD	Caa1	Negative	Medical Devices
BW NHHC Holdco	Caa3-PD	Caa3	Stable	Hospitals or other facilities based providers
Cano Health	Caa1-PD	Caa1	Stable	Hospitals or other facilities based providers
Covenant Physician Partners	Caa1-PD	Caa1	Stable	Hospitals or other facilities based providers
Envision Healthcare Corporation	C-PD	C	Stable	Hospitals or other facilities based providers
Exactech	Caa2-PD	Caa2	Stable	Medical Devices
Femur Buyer	Caa2-PD	Caa2	Stable	Medical Devices
Gordian Medical	Caa1-PD	Caa1	Stable	Hospitals or other facilities based providers
Lannett Company	Ca-PD	Ca	Stable	Specialty/Generic Pharmaceuticals
LifeScan Global Corporation	Caa2-PD	Caa2	Stable	Medical Devices
Medical Depot Holdings	Caa2-PD	Caa2	Stable	Medical Devices
Midwest Veterinary Partners	B3-PD	B3	Negative	Hospitals or other facilities based providers
National MENTOR Holdings	Caa1-PD	Caa1	Stable	Healthcare Services to Consumers
NMN Holdings III	B3-PD	B3	Negative	Medical Devices
One Call Corporation	Caa1-PD	Caa1	Stable	Healthcare Services to Business
Pluto Acquisition I	B3-PD	B3	Negative	Healthcare Services to Consumers
Quorum Health Corporation	Caa1-PD	Caa1	Stable	Hospitals or other facilities based providers
Radiology Partners	Caa1-PD	Caa1	Stable	Healthcare Services to Consumers
SM Wellness Holdings	B3-PD	B3	Negative	Healthcare Services to Consumers
Sound Inpatient Physicians	Caa2-PD	Caa2	Stable	Hospitals or other facilities based providers
Team Health Holdings	Caa3-PD	Caa3	Stable	Healthcare Services to Consumers
TecoStar Holdings	Caa3-PD	Caa3	Stable	Medical Devices
U.S. Renal Care	Caa1-PD	Caa1	Stable	Hospitals or other facilities based providers
US Radiology Specialists	B3-PD	B3	Negative	Healthcare Services to Consumers
Viant Medical Holdings	Caa1-PD	Caa1	Stable	Medical Devices
Vyaire Medical	Caa2-PD	Caa2	Stable	Medical Devices

Source: Moody's Financial Metrics

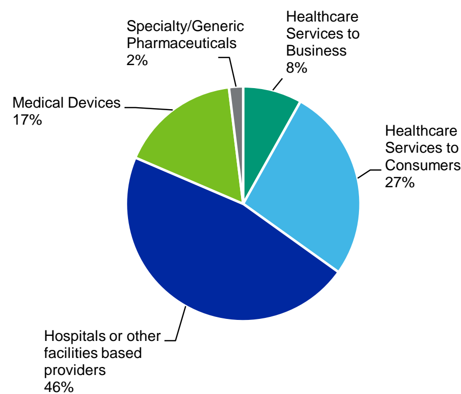
This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on https://ratings.moodys.com for the most updated credit rating action information and rating history.

Exhibit 2
Representation on the List is broad-based
Percentage of healthcare companies rated B3N or lower, as of 30 November 2022, by subsector*



*excluding Bausch Health
Source: Moody's Investors Service

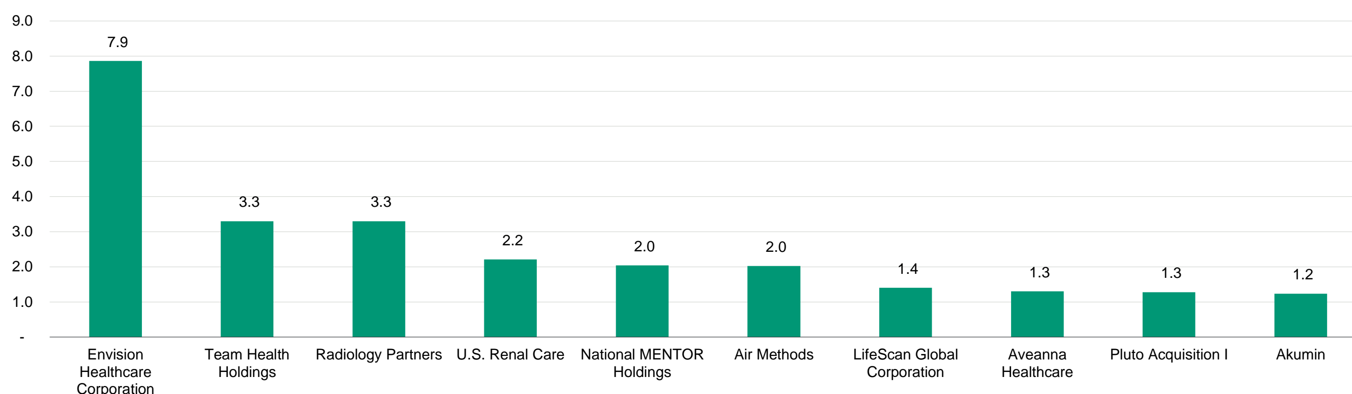
Exhibit 3
Facilities-based providers lead when ranked by debt outstanding
Percentage of healthcare debt outstanding on the B3N List as of 30 November 2022, by subsector*



*excludes Bausch Health due to large amount of debt and its disproportionate impact on chart
Source: Moody's Investors Service

The 34 healthcare companies on the B3N List have nearly $65 billion of outstanding debt, an increase of 57% compared to March 2020 at the onset of the pandemic and more than double the nearly $33 billion in debt outstanding in January 2019. The increase is largely attributable to two recent additions to the List's healthcare's roster that together account for nearly half of its total debt: Bausch Health Companies Inc. (Caa2 negative) with about $21.8 billion of outstanding debt; and Envision Healthcare Corp. (C stable) with about $7.9 billion. As shown in Exhibit 4, excluding Bausch Health, Envision has the largest debt load among healthcare companies on the List, accounting for 18% of total debt outstanding, followed by Team Health Holdings Inc. (Caa3 stable) and Radiology Partners Inc. (Caa1 stable), each accounting for nearly 8%.

Exhibit 4
Top 10 B3 negative and lower healthcare companies by total reported debt*
$ in billions, as of 30 June 2022



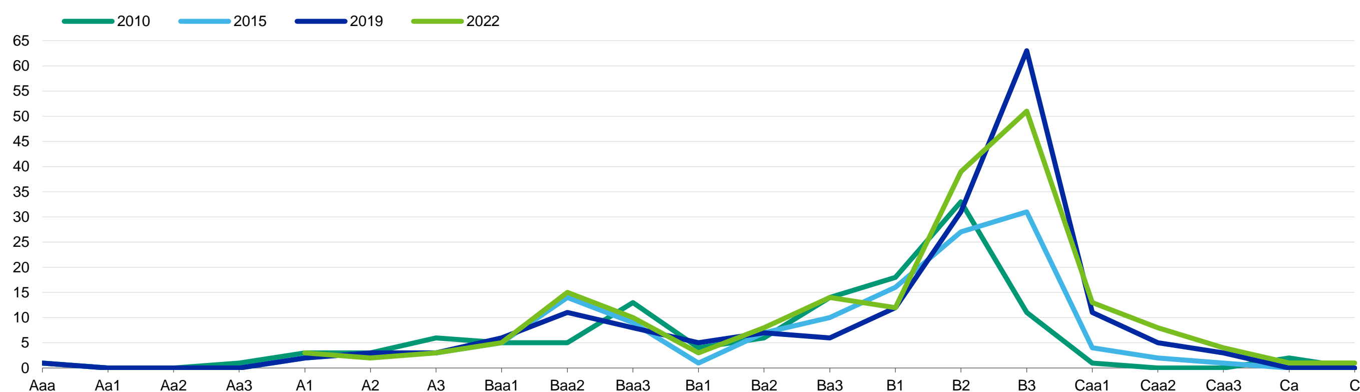
*excluding Bausch Health
Source: Moody's Financial Metrics, company reports

In another sign of the sector's material deterioration in credit quality, around 80% of North American healthcare companies have speculative-grade ratings, compared to around 73% in 2015 and 71% in 2010. As shown in Exhibit 5, within the speculative grade category, the proportion of healthcare issuers rated B3 and below has increased to 40% from 28% in 2015 and 11% in 2010. This reflects the multiple challenges that healthcare companies are contending with, including a weakening macroeconomic environment and ongoing pressure by private and public payers to reduce healthcare costs. The industry's social risk is also rising, exemplified by credit negative legislation such as the No Surprises Act and ongoing litigation around opioids. As discussed in the next section, private equity (PE) activity in the sector has also contributed to the uptick in companies on the lower end of the ratings scale.

Exhibit 5

The B3 and lower population continues to grow

Ratings distribution of North American healthcare companies over the years



As of 30 November 2022

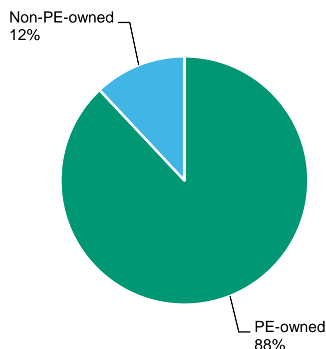
Source: Moody's Investors Service

Private equity fuels higher leverage – and risk

Over the past decade, the North American healthcare segment has attracted interest and investment from private equity sponsors. This reflects the essential nature of healthcare products and services, which can help drive earnings stability, in addition to the sector's favorable longer-term trends, including significant technological advances and aging populations. Fueled by accommodative leveraged financing markets, many sponsors undertook serial debt-funded acquisitions to "roll-up" small healthcare providers into large, cross-regional organizations, hoping to reap the benefits of size and scale. This activity occurred in a variety of segments, including general physician practices, emergency medicine, anesthesiology, gastroenterology, nursing, urgent-care clinics and dental practices, to name a few.

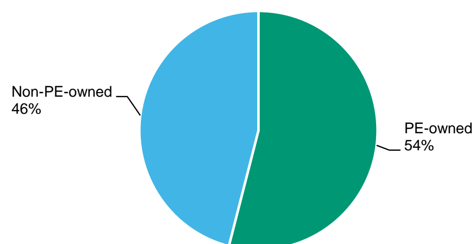
As a result, nearly 90% of the North American healthcare issuers on the B3N List are controlled by private equity, reflecting aggressive financial policies, high leverage and debt structures predominantly funded with floating-rate loans. (See Exhibits 6 and 7.) As credit conditions worsen and interest expense rises, these companies' cash flow have increasingly come under pressure, which limits their ability to adapt to changing industry dynamics, such as increasing social risk, new legislation and litigation. Two of the largest healthcare companies on the B3N List are owned by private equity: physician staffing companies Envision Healthcare, which has defaulted on its debt twice since January 2020; and Team Health, which we downgraded to Caa3 in October.

Exhibit 6
Private equity is prevalent among low-rated companies...
Ownership of healthcare companies on the B3N List, as of 30 November 2022



Source: Moody's Investors Service, company reports

Exhibit 7
... as well as among defaulters
Ownership of healthcare companies that defaulted from January 2020 through November 2022



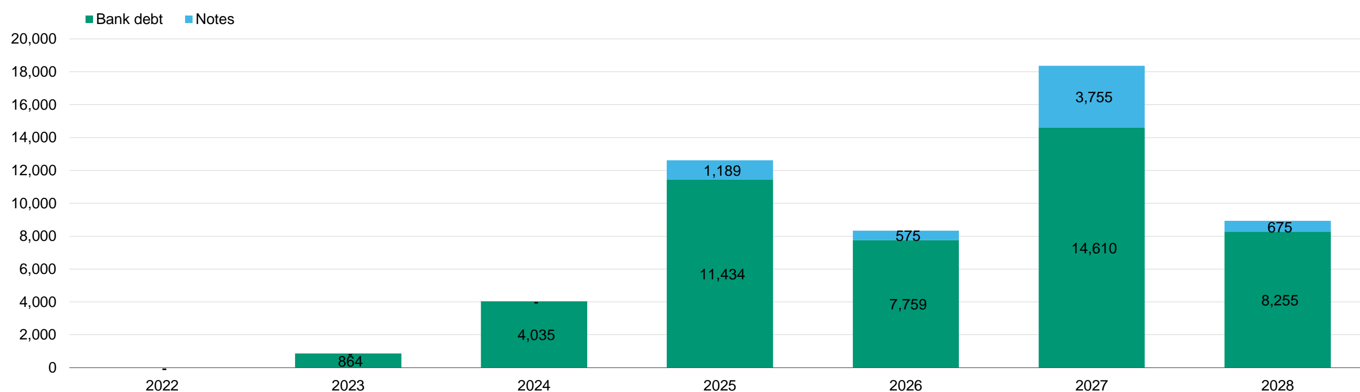
Source: Moody's Investors Service, company reports

As rates rise and performance lags, many capital structures will become unsustainable

Many healthcare companies rated B3 negative or lower entered 2022 with high leverage, a high level of floating rate debt and weak operating performance. For these companies, weaker earnings and higher interest rates worsened their interest coverage in 2022 and will likely continue to do so well into 2023. Some of these companies will find their capital structures to be unsustainable, given the quickly rising cost of their financing. And their ability to refinance will becoming increasingly difficult as economic growth slows, interest rates and credit spreads rise and market access declines.

While contractual debt maturities are fairly modest for healthcare companies on the B3N List in 2023, they start to dramatically accelerate in 2024 and 2025. (See Exhibit 8.) Given their very high financial leverage and fragile capital structures, some companies in this group will seek to preemptively address their maturity walls, with mixed support from lenders. This will likely result in transactions that we would consider to be distressed exchanges, which we view as defaults.

Exhibit 8
Due dates
2022-2028 annual maturities for bank debt and bonds of healthcare companies rated B3 negative or lower, in $ millions



Source: Moody's Investors Service, company reports

Recent defaults offer insight into the future

As shown in Exhibit 9, since January 2020, 13 North American healthcare companies have defaulted on their debt, proving that the industry is not immune to the profit and cash flow pressures that are challenging many industries today. Of the 13, 10 were due to transactions we considered to be distressed exchanges, which we view as defaults, while three were due to bankruptcy. (Envision Healthcare defaulted twice, in April 2020 and April 2022)

We examined these 13 companies to learn the warning signs that they flashed, that, on a look-back basis, turned out to be key signals that default was highly likely, which we have listed in Exhibit 9. Although hindsight is 20-20, we believe the experience of these 13 companies provides a useful illustration of predictors of possible future defaults. At the end of this report, we provide brief case studies on several companies that recently defaulted as well as several that we recently downgraded to B3 negative or below in order to highlight the variety of different factors that can lead to credit distress.

Some of the issues that these companies experienced in the run-up to default are common at companies with deteriorating credit profiles. Very high/excessive leverage and weak operating performance combined to sap most of these companies of adequate financial flexibility to withstand subsequent adverse shocks or events, pushing them to default. Much of this excessive leverage was the result of debt incurred for leveraged buyouts or acquisition-led growth strategies. Fundamental weakness in operating performance came from a variety of sources, including technological obsolescence, increases in labor costs and skilled labor availability, changes in the business operating environment, including new regulations or simple mismanagement. For some companies with excessive leverage and weak performance, disruptions caused by the onset of the COVID-19 pandemic were the last straw.

What we consider excessive leverage differs among borrowers, based on their unique earnings and cash flow characteristics in relation to their debt loads. However, for healthcare companies, we frequently view financial leverage – as measured by debt/EBITDA – above 7 times as very high, and that which exceeds 8 or 9 times or higher as excessive. At these levels, it becomes increasingly difficult for healthcare companies to meet their interest and debt amortization burdens, while still maintaining, investing in and growing their underlying businesses. Many defaulters with excessive leverage were buffeted by a variety of factors that caused their operating performance, earnings and cash flow to deteriorate, significantly worsening their cash generation profile in relation to their debt burdens.

Exhibit 9

Early warning signs of potential default

Issues facing healthcare companies that defaulted in 2020-2022*

		Financial policies/governance			Weak operating performance					Liquidity		
Issuer	Date of default	Private equity ownership	Very high/ Excesssive leverage	Debt-funded M&A	COVID impact	Labor costs	Change in industry dynamics	Integration issues/ Managing expansion	Other	Weak liquidity (6-12 mths prior to default)	Refinancing risk (12-24 mths prior to default)	Litigation
Affordable Care Holding Corp.	3/31/2020	Yes	Yes	Yes	Yes			Yes				
Quorum Health Corporation	4/7/2020		Yes		Yes				Yes (1)			
Envision Healthcare Corporation	4/30/2020	Yes	Yes		Yes	Yes	Yes			Yes		
Akorn, Inc.	5/20/2020		Yes	Yes			Yes		Yes (2)		Yes	Yes
NAPA Management Services Corporation	6/30/2020	Yes	Yes		Yes					Yes		
Mallinckrodt International Finance SA	10/12/2020			Yes	Yes		Yes		Yes (3)	Yes	Yes	Yes
Alliance Healthcare Services, Inc.	10/13/2020	Yes	Yes	Yes	Yes		Yes		Yes (4)	Yes		
CDRH Parent, Inc.	11/6/2020	Yes	Yes				Yes			Yes	Yes	Yes
CHS/Community Health Systems	12/9/2020		Yes					Yes	Yes (5)	Yes	Yes	
Medical Depot Holdings	3/26/2021	Yes	Yes				Yes	Yes		Yes	Yes	
Endo International plc	8/16/2022		Yes	Yes			Yes			Yes	Yes	Yes
Carestream Health, Inc.	8/23/2022	Yes					Yes		Yes (6)	Yes	Yes	
Bausch Health	9/27/2022		Yes	Yes					Yes (7)			Yes
Total		7	11	6	6	1	8	3	7	9	7	5
% of total		54%	85%	46%	46%	8%	62%	23%	54%	69%	54%	38%

(1) Issues operating as standalone entity (billing and collection), (2) Internal control issues, filing delays, (3) Adverse patent challenge, (4) Reimbursement cuts from health insurers, (5) Bloated cost structure, (6) Technology obsolescence and (7) Adverse litigation (patent invalidation).
*Envision Healthcare defaulted twice: in April 2020 and April 2022
Source: Moody's Investors Service

Recent downgrades face similar issues as recent defaulters

So far this year, we have downgraded the ratings of 25 North American healthcare companies to B3 negative or lower. As shown in Exhibit 10, many of these downgrades were driven by the same factors that caused the 13 companies in Exhibit 9 to default.

Labor costs, which have risen in most industries, have been particularly credit negative for healthcare companies, which have also been plagued by labor shortages. Labor issues led to ratings downgrades to B3 negative or below for several healthcare staffing companies, which have struggled to find sufficient labor to provide necessary care at a cost at which they can remain profitable. Technological obsolescence is another factor that has led to recent downgrades. For instance, Lifescan Gobal Corp. (Caa2 stable) is seeing its traditional blood glucose monitoring equipment being replaced with newer technology that is much more popular with patients. Another example is Carestream Health Inc. (B3 stable), which specializes in traditional medical film for X-rays – a technology that is being rapidly replaced by digital imaging.

Changing industry dynamics, including new legislation or regulations, can cause additional headwinds and drive downgrades. For instance, the No Surprises Act of 2021, which essentially curbed balance billing, reduced revenue and profits for Air Methods Corp. (Caa3 stable), an air ambulance company. And the Center for Medicare and Medicaid Services' (CMS) implementation of a new competitive bidding process for certain ambulatory devices caused revenue and profits to fall at companies such as Medical Depot Holdings Inc. (Caa2 stable).

Exhibit 10

Flashing red?

Issues faced by companies downgraded to B3 negative and below in 2022 are similar to those that drove defaults since 2020

			Financial policies/governance			Weak operating performance					Liquidity		
Issuer	Date of downgrade	Downgraded to (CFR)	Private equity ownership	Very high/ Excesssive leverage	Debt-funded M&A	COVID Impact	Labor costs/ Supply chain	Change in industry dynamics	Integration issues/ Managing expansion	Other	Weak liquidity	Refinancing risk	Rising interest rate impact
BW NHHC Holdco	1/31/2022	Caa3	Yes	Yes	Yes		Yes		Yes		Yes		
Vyaire	4/27/2022	Caa2	Yes	Yes		Yes			Yes		Yes	Yes	
U.S. Renal Care	6/28/2022	Caa1	Yes	Yes		Yes	Yes					Yes	
Avalign Holdings	6/28/2022	Caa1	Yes	Yes		Yes	Yes				Yes		
National MENTOR Holdings	9/9/2022	Caa1	Yes	Yes	Yes		Yes			Yes (1)	Yes		
Akorn Operating Company LLC	9/15/2022	Caa2	Yes	Yes				Yes		Yes (2)			
Envision Healthcare Corporation	9/21/2022	C	Yes	Yes		Yes	Yes	Yes		Yes (3)	Yes	Yes	Yes
One Call Corporation	9/27/2022	Caa1	Yes	Yes		Yes							
Medical Depot	9/28/2022	Caa2	Yes	Yes		Yes	Yes	Yes			Yes		Yes
LifeScan Global Corporation	10/4/2022	Caa2	Yes					Yes			Yes	Yes	
Sound Inpatient Physicians	10/10/2022	Caa2	Yes	Yes				Yes		Yes (4)	Yes	Yes	
Team Health Holdings	10/13/2022	Caa3	Yes	Yes		Yes				Yes (5)	Yes	Yes	
Cano Health	10/13/2022	Caa1	Yes	Yes	Yes		Yes		Yes		Yes		
Covenant Physician Partners	10/14/2022	Caa1	Yes	Yes	Yes		Yes					Yes	
Lannett	10/17/2022	Ca		Yes				Yes		Yes (6)			
Exactech	11/2/2022	Caa2	Yes	Yes		Yes				Yes (7)	Yes		
Air Methods	11/4/2022	Caa3	Yes	Yes			Yes	Yes			Yes	Yes	Yes
Athletico Holdings	11/4/2022	B3	Yes	Yes	Yes		Yes				Yes		
TecoStar Holdings	11/9/2022	Caa3	Yes	Yes		Yes	Yes				Yes	Yes	Yes
US Radiology Specialists	11/10/2022	B3	Yes	Yes	Yes	Yes	Yes						
NMN Holdings III	11/11/2022	B3	Yes	Yes			Yes				Yes	Yes	
Aveanna Healthcare	11/17/2022	Caa1		Yes	Yes		Yes		Yes				
Radiology Partners	11/18/2022	Caa1	Yes	Yes	Yes		Yes						
Gordian Medical	11/21/2022	Caa1	Yes	Yes			Yes			Yes (8)			Yes
Akumin	11/28/2022	Caa2		Yes	Yes			Yes	Yes	Yes (9)			
Total			22	24	9	10	16	8	5	9	15	10	5
% of total			88%	96%	36%	40%	64%	32%	20%	36%	60%	40%	20%

(1) Shareholder distribution, (2) Internal control issues (FDA warning letter), aborted merger with Fresenius, (3) Reimbursement risk due to out-of-network status, (4) CMS reimbursement change, (5) Payer disputes, (6) Generic manufacturing facility, (7) Product recall, (8) CMS audits and (9) Downward pressure on reimbursement rates and regulatory issues including financial reporting delays.

Source: Moody's Investors Service

Distressed exchanges will remain the most common form of default

Saddled with unsustainable capital structures, many healthcare companies rated B3 negative or lower will likely pursue transactions that we consider to be distressed exchanges (DEs). DEs have always been popular among private equity sponsors when the companies they own get into financial difficulties and we expect their popularity to continue. We consider a transaction to be a distressed exchange if it allows a company to avoid default or bankruptcy and results in an economic loss for creditors.

For companies with deteriorating operating performance, lenders will likely be unwilling to refinance upcoming debt maturities unless they believe their economic loss would be less than it would be if the borrower filed for bankruptcy. Companies that are unable to meet greatly increased cash interest expense may seek to convert their debt to payment-in-kind (PIK) obligations, pursue debt-to-equity conversions, or even enter bankruptcy, in order to shed debt and revise their capital structures to make them more sustainable. Here too, lenders will often agree to such transactions because they represent less economic loss than their alternatives.

We view distressed exchanges as defaults because they are normally undertaken to avoid other types of defaults under which creditors would incur some type of loss. These types of transactions can often be viewed as out-of-court restructurings. Completing a distressed exchange is often less expensive than undergoing a formal bankruptcy process, and often enable financial sponsors to retain control of a company, which may well not occur in a bankruptcy.

Case studies of select 2022 downgrades

Team Health Holdings Inc. (Caa3 stable)

Team Health is a physician staffing company specializing in doctors for emergency rooms. Owned by Blackstone since early 2017, the company has had an aggressive financial policy, with very high financial leverage. Team Health entered the COVID-19 pandemic weakly positioned, and the shock of dramatically reduced emergency room volumes led to a CFR downgrade to Caa2 negative in April 2020 from B3 negative, subsequently raised to Caa1. The company's 2022 attempt to extend a term loan was only partially successful, with some lenders agreeing to the extension, but others not. This led to a "ladder" of debt maturities as follows:

» November 2023: $300 million revolver expires

» February 2024: $1.2 billion of Term Loan B matures

» November 2024: $1.4 billion of Term Loan B (with amended maturity of March 2027) springs forward and becomes due if Team Health is unable to reduce the amount outstanding of the 2025 notes to below $250 million.

» February 2025: $714 million of Senior Unsecured notes mature

Given this schedule and mixed support from its lenders, it is unlikely that any particular lender group will agree to extend their commitments or loans past the next maturity in the ladder. For this reason, we expect that Team Health will be forced to refinance its entire capital structure sometime in 2023. Given the company's very high financial leverage and weak operating performance, this will be very difficult. On 13 October 2022 we downgraded Team Health's CFR to Caa3 to reflect the high probability of the company pursuing a transaction – such as a distressed exchange – that we would view as a default.

Lannett Co. Inc. (Ca stable)

Lannett, a generic drug manufacturer and distributor, suffered in recent years due to is inability to offset intense competitive pricing pressures on its base portfolio of oral generic drugs with new product launches. This caused a 48% decline in revenue since fiscal 2019 (ending in June), but the impact on earnings is much more pronounced due to fixed costs. Leverage spiked with debt/EBITDA (Moody's adjusted) rising from 4.2x at the end of fiscal 2019 to 11.6x at fiscal year end 2021, and "undefined" at 30 June 2022 due to negative EBITDA (but $615 million of funded debt). A bright spot in Lannett's profile are two diabetes drugs in its pipeline, which, if approved, would provide promising new sources of revenue.

We further downgraded the company on 17 October 2022, taking its CFR to Ca from Caa1. Operating performance continues to be extremely weak. And although the company has plentiful cash ($88 million in balances, plus the expectation of receiving an approximate $20 million tax refund before year end 2022) we expect Lannett's liquidity to be weak over the next 12-15 months. We expect the company to be materially cash flow consumptive over the next year, with the expectation of negative EBITDA. And even if Lannett receives regulatory approval for the drugs in its pipeline, it may lack the resources to commercialize those drugs. Lannett's debt is trading at distressed prices, and the company's stock has fallen below $1 per share, raising the risk of delisting from the NYSE. Given these significant headwinds, we believe the risk is extremely high that the company will pursue a transaction – such as a distressed exchange – that we would view as a default.

LifeScan Global Corp. (Caa2 stable)

LifeScan is a manufacturer and distributor of blood glucose monitoring (BGM) equipment and supplies, owned by Platinum Equity, LLC. The business has been in steady decline because it focuses on traditional BGM testing (requiring finger pricks), which is being replaced with the next generation of continuous glucose monitoring (CGM) systems (no finger prick). LifeScan is working with a partner for a possible CGM product, but success is uncertain, including the timing of any regulatory approvals and the magnitude of any potential income if and when a product is launched.

On 4 October 2022 we downgraded LifeScan to Caa2 stable from B3 stable due to ongoing headwinds, increased business risk, accelerating revenue declines, weak liquidity and increasing refinancing risks. The company now has a ladder of debt coming due in July 2024, October 2024 and October 2025. Given its deteriorating operating performance, it is unlikely that any particular lender group will agree to extend their commitments or loans past the next maturity in the ladder. In addition, we believe that the looming refinancing effort will be challenged by the company's weak track record in the debt capital markets, including an unsuccessful

refinancing effort in 2021. For this reason, we expect that LifeScan will be forced to refinance its entire capital structure sometime before July 2024. In our view, operating underperformance, high leverage and negative cash flow (after mandatory amortization), will likely make the capital structure unsustainable, thus elevating the risk of the company undertaking a transaction that we would view as a default.

Sound Inpatient Physicians (Caa2 stable)

Sound Inpatient Physicians is a physician staffing company focused on hospital-based medicine. The company is majority owned by Summit Partners (50.6%) and United Healthcare's OptumHealth (41.4%). We downgraded the company to B3 from B1 on 6 May 2022 due to significant underperformance in 2021, with earnings coming in well below management's forecasts. The company also reported material downward expectations for revenue associated with its participation in the government's Bundled Payments for Care Improvement (BPCI) program. Continued underperformance and cash burn into 2022, as well as increasing refinancing risk, led us to downgrade the company to Caa2 stable on 10 October 2022. With the company's financial leverage at approximately 14.9x at the end of June 2022 (on Moody's adjusted basis) and uncertain prospects of profit recovery, the risk of the company pursuing a transaction that we would consider to be a distressed exchange (and hence a default) has increased.

Bausch Health (Caa2 negative)

Publicly-traded Bausch Health is a manufacturer of a range of pharmaceutical, medical device and over-the-counter products, primarily in the therapeutic areas of eye health, gastroenterology and dermatology. On 29 July 2022, we downgraded the CFR to Caa1 from B2 following an adverse court ruling in a patent dispute over Xifaxan, Bausch's largest product. As a result of this ruling, we foresaw material earnings erosion and rapidly increasing leverage from a generic launch, althought its timing remains uncertain. Furthermore, the sustainability of the capital structure became more uncertain. On 31 August 2022, we downgraded Bausch to Caa2 following the company's announcement of a proposed debt restructuring transaction that would replace existing senior unsecured debt with new first lien and second lien secured bonds. The debt exchanged was considered a distressed exchange.

Case studies of select defaults since January 2020

Endo

Publicly-traded Endo offers branded and generic pharmaceuticals. Its credit profile had been under pressure for many years before its 2022 default, reflecting a combination of aggressive debt-funded acquisitions, mounting litigation liabilities (vaginal mesh) and strong competition in its core generic drug business. As these pressures intensified, liquidity rapidly deteriorated in 2019, leading Endo to rely heavily on its revolver to fund its business. We downgraded its CFR to B3 CFR on 1 July 2019 and to Caa1 on 25 August 2021 due to potential cash outflows related to opioid litigation. On 31 May 222, we lowered the CFR to Caa3 on heightened restructuring risk. Endo filed for Chapter 11 in August 2022.

CDRH Parent

CDRH – the owner of Healogics – runs specialized care centers that treat patients with chronic, non-healing wounds. CDRH displayed a very aggressive capital structure from its initial rating post leverage buyout by Clayton, Dubilier and Rice. Pro forma debt/EBITDA was 8x for a relatively small and narrow business focused on a nascent wound care treatment. When financial performance deteriorated due to lower hyperbaric oxygen treatment volumes and growing legal risk facing this business, CDRH's capital structure became untenable. On 10 October 2019, we downgraded its CFR to Caa1 from B3. An amendment to its second lien term loan was negotiated, leading to the first default in March 2020, then a capital restructuring that we deemed a default in May 2021.

NAPA Management Services Corp.

NAPA is a provider of anesthesia services and is owned by private equity sponsors American Securities and Leonard Green & Partners. The company was already battling weak operating performance when the coronavirus pandemic hit. We downgraded its CFR to Caa1 from B3 on 27 March 2020 on anticipation of a steep decline in surgical procedure volumes. Our expectation of weak liquidity and mounting refinancing risk prompted us to further downgrade to Caa2 on 19 June 2020. On 30 June 2020, the company amended its second-lien credit agreement in a manner that allowed it to pay the interest in kind in order to preserve cash, which we considered a distressed exchange and hence a default.

Akorn

Akorn, a manufacturer of specialty generic pharmaceuticals, operated for many years with low leverage in a highly competitive and regulated industry. However, an active M&A strategy and undisclosed integration issues resulted in various earnings restatements. A modest-sized niche player in the highly competitive generic pharmaceutical industry, Akorn agreed to a merger with Fresenius, a German healthcare company. But Fresenius terminated the deal, leaving Akorn with a deteriorating standalone business. Steep earnings declines followed, and drove an increase in leverage to over 10x, resulting in an unsustainable capital structure. In February 2020, we downgraded to Caa3 from Caa1 reflecting the high risk of bankruptcy given ongoing litigation and mounting refinancing risk. The company filed for Chapter 11 in May 2020.

Endnotes

1 Includes only those rated by Moody's corporate finance group. Excludes not-for-profit hospitals and other healthcare issuers rated by other areas of Moody's.

2 Our B3 Negative and Lower List includes all US nonfinancial corporate issuers with: a Probability of Default Rating (PDR) of Caa1-PD or lower; a B3-PD PDR with a negative rating outlook; or a B3-PD PDR on review for downgrade.

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