S&P Global
Ratings

Industry Top Trends 2022

Health Care

Stable Outlook But Longer-Term Challenges Emerging

This report does not constitute a ratings action

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What's changed?

Outlook remains stable but with a modest negative bias. COVID-19 variant uncertainty, labor and supply chain difficulties, scrutiny of pricing and access, and the return of mergers and acquisitions (M&A) within the industry suggests negative rating actions may outpace positive ones in 2022.

Supply chain and labor challenges, especially the shortage of nurses and burnout among medical professionals, are impediments to capacity and margins.

M&A at scale has resumed, potentially putting downward pressure on ratings.

What are the key assumptions for 2022?

Supply chain, labor, and pandemic-related inefficiencies cut into margins. This, along with commensurate reimbursement increases lagging, results in lower margins and cash flows compared with those achieved of 2021.

Payor pressure continues. Build Back Better legislation, which includes proposals for Medicare Part B and D pricing reforms, has stalled at least temporarily. We do not expect disruptive reimbursement changes in 2022, though payor pricing pressure will continue to weigh on profitability.

Increasing M&A, potentially constraining credit quality.

What are the key risks around the baseline?

Pandemic-related fallout goes into extended overtime. The omicron variant has amplified the uncertainty and stressors on the health care system. An extended pandemic will tighten margins and cash flows for many industry participants.

Payor and labor/supply chain pressures could drive companies to increase efficiencies and/or limit procedure capacity, leading to lower margins.

U.S. health care reform efforts continue, though we believe they will be largely neutral for credit quality in 2022. We would consider unexpected pharma pricing reforms a negative credit factor for the pharma industry.

Ratings trends and outlook

Global Health Care

Chart 1

Ratings distribution by region

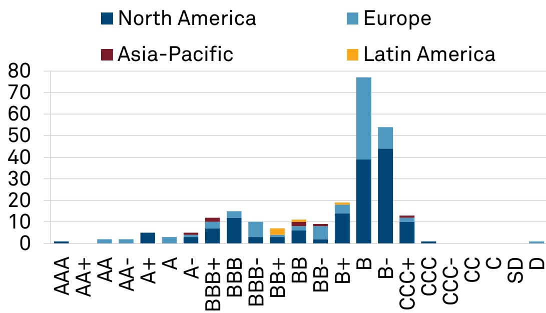


Chart 2

Ratings distribution by subsector

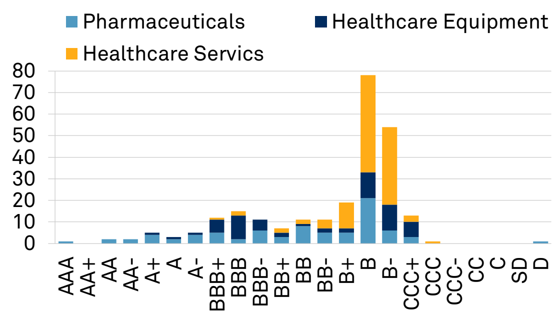


Chart 3

Ratings outlooks

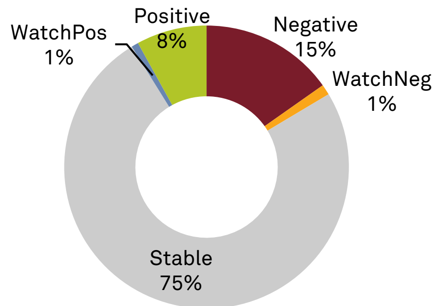


Chart 4

Ratings outlooks by subsector

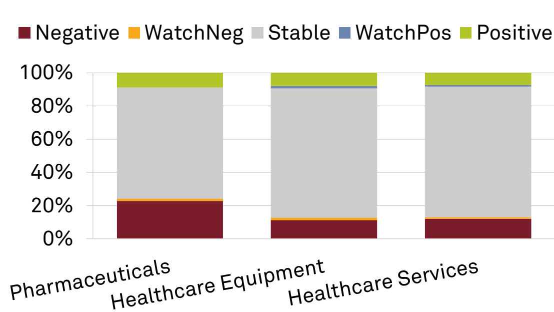


Chart 5

Ratings outlook net bias

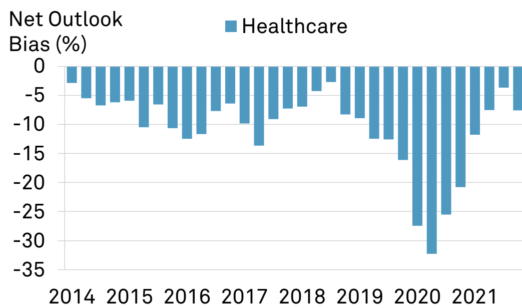
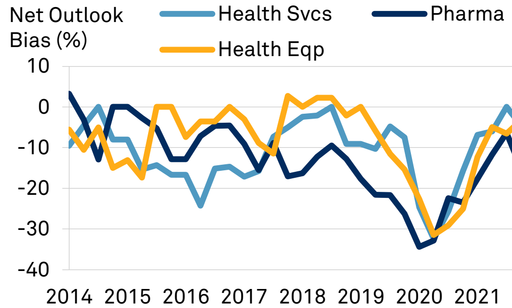


Chart 6

Ratings net outlook bias by subsector



Source: S&P Global Ratings. Ratings data measured at quarter end.

Health Care

Ratings trends and outlook

Our ratings outlook for the overall health care industry remains stable, with stable outlooks for the health care services and medical device subsectors and a negative, though gradually improving, outlook for the pharmaceutical sector. The health care industry has continued to weather the fallout from the COVID-19 pandemic relatively well, some 22 months, and counting. Patient and procedure volumes having returned to near pre-pandemic levels in many specialties. Ongoing heavy demand for testing, safety-related medical products, and COVID-19 testing and vaccines are creating positive ratings momentum for pockets of the health care ratings universe, such as lab companies, life sciences, and pharma. Our 2021 rating actions reflected the improving fundamentals, with positive ratings actions (upgrades and positive outlook revisions) significantly outpacing negative ratings actions by a margin of 79-40. This led to the significant improvement of our net outlook bias for all subsectors (see chart 6).

That said, we expect negative rating actions will outpace positive ones in 2022 for a number of reasons:

- The uncertainty created by the pandemic is on the rise given the more contagious omicron variant taking hold and the health care workforce, already strained due to the pandemic and nursing shortage, threatens providers' capacity to handle patients and procedures.
- Labor and supply chain constraints will likely last for at least a few more years. Nursing shortages and burnout among medical professionals were already a problem before the pandemic. The pandemic's added demands have further strained the labor supply and resulted in higher costs, such as paying higher salaries and bonuses and using more expensive temporary nurse staffing companies to meet immediate needs. Labor costs, supply chain challenges, and inflation all have hampered health care companies' margins and cash flows and they will likely continue to do so for a while because reimbursement improvement tends to occur with a lag.
- M&A is resuming in the health care industry and will put downward pressure on ratings. Meanwhile, the stress on pricing and scrutiny on transparency and health care access from governments, payors, and the public continues to increase for health care companies.
- And, the decidedly positive ratings performance in 2021 was partially due to the benefits of the subsiding pandemic, which is now reflected in our ratings, so 2022 positive rating actions will not be significantly bolstered by further recovery from the pandemic.

Hospitals and providers again subject to growing strains as the pandemic drags on. The re-resurgence of the pandemic due to the omicron variant threatens to again hurt operating performances, with hospitals and service providers that have already had to contend with the pandemic's fallout over an extended period, brace themselves for more of the same. Hospitals are seeing increasing COVID-19 cases while still dealing with staffing shortages, once more leading to the suspension of elective procedures in some regions. While patient and procedure volumes have rebounded to near pre-pandemic levels in certain specialties, it has not in others, and the situation remains fluid. Elective procedures make up an average 60% of a hospital's procedure volume, and are often more profitable, subsidizing other departments. Thus, a suspension of elective procedures has a disproportionate impact on profitability. Patient mix and acuity levels have yet to normalize as well, with emergency room admissions still below pre-pandemic levels (because patients are reluctant going to a hospital, so they seek alternative sites of care) and acuity levels elevated (due to sicker patients, including COVID-19 patients), distorting revenues and EBITDA margins.

Staffing remains in tight supply, especially nurse staffing, and the health care workforce is facing burnout as the pandemic extends beyond 22 months. Hospitals say they have benefitted from their COVID-19 experience, such as adopting more flexible scheduling procedures and stockpiling key medical supplies, enabling them to avoid some of the disruption seen earlier in the pandemic. However, hospitals have had to increase pay and offer bonuses as well as resort to expensive nurse and health care staffing companies to meet its personnel needs. Along with pandemic-related inefficiencies and increased costs for critical medical products, we believe EBITDA margins and cash flows will be squeezed in 2022 and likely beyond, given that labor tightness, supply chain inefficiencies, and inflation will likely remain past the pandemic.

Federal aid, such as the Coronavirus Aid, Relief, and Economics Security (CARES) Act in the U.S., provided a financial cushion against the pandemic's disruptive consequences. However, for 2022, that safety net is unlikely to be significant because the bulk of federal aid has already been disbursed and we are not currently expecting more. The longer-term impact of COVID to the industry, including the degree to which mortality among the medically vulnerable during the pandemic may reduce demand for health care services as well as the degree to which delayed medical care over the course of the pandemic and potential for higher disease rates among those who had COVID (especially severe cases) may result in increased utilization of health care services, is not yet clear.

A less negative outlook for the pharmaceutical industry? The highly rated pharmaceutical industry continues to have a more negative bias among rating outlooks than the other health care subsectors (see chart 4). The segment has also seen several multi-notch downgrades the past two years due largely to M&A. However, we believe the ratings outlook bias for the industry is improving for 2022 for several reasons, including improving product pipelines at many companies because of all the M&A in previous several years, a lower degree of concern regarding drug pricing legislation in the U.S., progress resolving the opioid litigation, and more stable pricing for the generic drug companies. The pharmaceutical industry has scored a major success, both financially, for companies such as Pfizer, and from a public relations standpoint for the industry. The speed of development and approval as well as the success of the COVID-19 vaccines have resulted in a somewhat improved public opinion of the industry.

On the legislative front, The Build Back Better bill, which includes Medicare Part D and Part B drug pricing reform, has seemingly stalled, at least temporarily. And, even if passed, the proposal as written, is limited in scope, and not disruptive to economics. We understand the reforms would target insulin, for which Novo Nordisk, Eli Lilly, and Sanofi are significant players. However, the proposed legislation is relatively limited, including earmarking prices on only 10 drugs starting in 2025, 15 in 2026 and 2027, and expanding to 20 drugs in 2028. Furthermore, it would only target drugs that have been on the market more than nine years for small molecule-based drugs and 13 years for biologics. Thus, we do not expect the legislation, if passed as proposed, to have a substantial impact on financial results for most issuers.

We also believe that major pharmaceutical companies' pipelines are improving, partially due to the significant amount of M&A in the industry over the past several years. More than ever, a powerful research and development (R&D) engine launching new innovative drugs will therefore be the key factor to success because existing blockbuster drugs could face pricing pressure. Also, only new products with clear therapeutic efficacy will obtain attractive pricing at launch. The increasingly healthy pipelines of many of the large U.S. and large EMEA players also mean that large acquisitions are not needed to fuel future growth. Unmet needs are still many, and we expect health care spending to rise, not only because of the current pandemic.

Main assumptions about 2022 and beyond

1. Health care spending growth rate moderates, but spending remains elevated, distorted due to COVID-19

U.S. health care spending grew 9.7% in 2020 due to pandemic-related spending and 2021 spending was distorted as well given the delta variant. Spending growth will moderate from the accelerated level in 2020, but will return to the steady increases pre-COVID.

2. M&A returns fully in 2022, stressing credit metrics and ratings

Health care M&A increased in 2021 following a significant drop in 2020 due to pandemic-related uncertainties, especially in the pharmaceutical and medical device and product subsectors. We expect M&A to continue at a high level and more broadly, including the hospital and health care service subsectors.

3. Margin pressures on the health care services segments will persist

Hospitals and health care service providers are dealing with the multiple challenges of lower-than-normal patient and procedure volumes, higher-than-typical patient acuity, and tight labor supply.

Health care expenditure growth remains distorted, longer-term projections difficult. U.S. health care spending increased 9.7% in 2020 (the latest year available) to $4.1 trillion, faster than the 4.3% increase in 2019 and now accounts for 19.7% of U.S. GDP. However, GDP is somewhat distorted due to increased demand for health care and pandemic-related federal spending. Spending growth was distorted in 2021 as well due to the delta variant, and at least partially into 2022, due to the omicron variant. The Centers for Medicare & Medicaid Services (CMS) is projecting average annual growth of roughly 5.4% from 2019-2028, down slightly from the previous pre-pandemic 5.5% projection for 2018-2027. The pandemic- related portion of health care spending in 2020 will eventually recede, to be partially replaced by the health care spending it displaced when many patients delayed care during the pandemic. For 2022, health care spending will likely remain elevated due to the pandemic, but with growth rates lower and closer to the 4.2-4.5% growth rate seen in 2017-2019. Spending will remain distorted though, as patient visits and procedures have yet to fully recover and pandemic related spending remains significant.

Global health care M&A continues to surge. Health care M&A has more-than-recovered to exceed pre-pandemic levels, though M&A volume for the hospital segment remains below historical levels. We also expect M&A to significantly grow in 2022. The pandemic severely disrupted health care M&A in the first half of 2020, especially in the hospital and many health care services segments, given uncertain prospects and distracted management teams. Health care M&A recovered strongly in the second half of 2020, led by the pharmaceutical sector, which was less affected by the pandemic relative to other industries. Still, given the significant drop in the first half of 2020, total health care M&A volume for 2020 declined steeply to $205.4 billion, versus $348.8 billion in 2019 and $310.5 billion in 2018.

However, for the first three quarters in 2021, total health care M&A totaled $297.6 billion and should readily exceed 2019’s total of $332.5 billion because a backlog of transactions as well as ongoing strong interest in health care from special purpose acquisition companies (SPACs) and private equity contributed to the number. We believe M&A in 2022 will remain strong, as health care companies seek to improve their competitive positions and diversify their offerings to counter increasing pressure from payors and potential legislative reforms. In addition, private equity remains very active in the sector. The past-year's health care industry's M&A highlights include AstraZeneca

PLC's $40 billion acquisition of Alexion, Thermo Fisher Scientific's acquisition of PPD Inc. for $21.9 billion, Baxter international Inc's acquisition of Hill-Rom Holdings Inc. for $12.3 billion, and the acquisition of Medline by private equity group in a $30 billion transaction. Health care services transactions were typically smaller, though interest level remains high for physician groups and behavioral health businesses. Meanwhile, in Europe, we expect continuing rapid consolidation across the contract development and manufacturing company (CDMO) and medical devices sectors in Europe. The same is true of the laboratory and specialist health care service sectors: Laboratories experienced strong demand during the first stages of the COVID pandemic, which helped them rationalize and strengthen operations. Specialist health care showed resilient performance in Europe despite the pandemic, resulting in attractive enterprise values.

Service providers' margin constraints will persist beyond 2022. Hospitals worldwide continue to incur pandemic-related costs and contend with salary inflation and medical staff shortages. With the pandemic far from over, however, we expect general hospitals and care homes to experience challenging operating conditions owing to staff on sick leave until the end of the winter cold and flu season. The omicron variant has again led to the suspension of elective procedures, which are key to a hospital's financial performance. Supply chain issues have eased since the early days of the pandemic; however, costs remain elevated for key medical supplies. Burnout among medical personnel, especially among doctors and nurses, is an ongoing risk. Increased use of medical staffing companies are a temporary solution and rates have increased, weighing on hospitals' bottom lines. We believe labor and supply chain issues will persist for many years, even after the pandemic has ended.

Credit metrics and financial policy

While we still hold an overall stable ratings outlook for the health care industry, we expect some deterioration in credit metrics stemming from the pandemic-related fallout, tight labor markets, supply chain challenges, and ongoing heavy M&A, particularly in the pharmaceutical industry. Not all the major pharmaceutical companies will pursue M&A, given recent sizable share buy-backs initiatives announced by Novartis AG and Roche Holding AG, suggesting capital allocation will target shareholder remuneration. However, we note that GlaxoSmithKline plc will receive up to £8 billion of pre-split dividends in 2022 on the demerger of its consumer health business. The company could use these proceeds to strengthen its pipeline. Along with other companies such as Pfizer Inc., which has also streamlined its business portfolio, we believe the industry will remain focused on delivering returns on research and development (R&D) via M&A.

Key risks or opportunities around the baseline

1. Resurgence of COVID-19 cases, margin pressure could worsen

The recent resurgence of COVID-19 cases has led to disruption in hospitals and the delay or cancellation of elective procedures because COVID-19 patients swamp hospital capacity. We consider the risks of disruption to surgical procedures volumes generally low in 2022. Elective surgeries cannot be postponed forever. Thus, we are not expecting the same degree of disruption seen earlier in the pandemic and hopefully this latest surge will be shorter and less severe. However, should procedure volumes remain depressed over a longer period or patient and acuity mix remain distorted, it could have a greater-than-expected impact on margins and EBITDA.

2. Labor and supply chain challenges are longer term problems

The sector is facing a shortage in nurses and key medical staff spurring inflation and higher labor costs. The pandemic exacerbated an already increasing nursing shortage and rising levels of medical staff burnout. The heightened and sustained use of personal protective equipment, disrupted supply chains, and rising inflation leading to higher costs of basic medical products, together will weigh on margins. We have modeled in some erosion of EBITDA margins due to the challenges associated with labor and supply chain and our analysis incorporates that the challenges will likely outlast the pandemic. However, a sharper or prolonged increase in costs could result in revised lower projections and negative pressure on ratings.

3. U.S. health care reform is neutral for credit quality in 2022

The currently proposed $1.75 billion Build Back Better bill, which has Medicare drug pricing reform embedded in it, remains stalled. It is uncertain whether Democrats, who hold a slim majority in both the House and Senate, will be able to secure the votes to pass the bill ahead of mid-term elections in November 2022. Should the Democrats lose control of either the House or Senate, the chances of the bill being passed as proposed is limited. Health care reform does have significant bi-partisan support, though the process of getting something done starts all over again after the elections. Even if the bill does pass, the impact to the pharmaceutical industry will be bound by the limitations of the proposals and not likely to result in many negative ratings actions. Nevertheless, the reforms could affect some companies disproportionately, and would increase add to the industry's uncertainty because it would give future administrations a base from which to expand legislation. However, drug pricing reform remains a hot topic and additional proposals could emerge.

4. Extended pandemic tailwind for certain select subsectors

With the uncertainty created by the pandemic and COVID-19 cases on the rise once again, and some subsectors having experienced significant tailwinds the past few years, we expect high demand for many products and services to carry further into 2022. Laboratory testing companies that reported all-time high revenues in 2021 will see ongoing strong demand, as will life science and medical product companies that provide diagnostic tests and supplies, particularly those that support COVID testing and vaccine development and production. Temporary nurse and medical staffing companies have also seen strong demand due to the nursing shortage and disruption to hospitals and providers. We have not taken many positive rating actions on companies that have benefitted from COVID-19-related tailwinds because we don't know how long the benefits will last or how companies will use the related financial windfalls. However, as the pandemic and the tailwind, goes into extended time, the possibility of positive rating actions increases.

Related Research

- ESG Credit Indicator Report Card: Health Care, Dec. 16, 2021
- The Healthcare Credit Beat: Reflections on Biogen, Danaher, Eli Lilly, Molina Healthcare, and Quest Diagnostics, Nov. 5, 2021
- The Healthcare Credit Beat: Reflections on Bausch Health, HCA, Merck, Teva, and ATI Physical Therapy, Aug. 5, 2021
- Pharma Outlook: Eighth Straight Year of Credit Deterioration in 2021, Feb. 23, 2021

Industry forecasts

Global Health Care

Chart 7

Revenue growth (local currency)

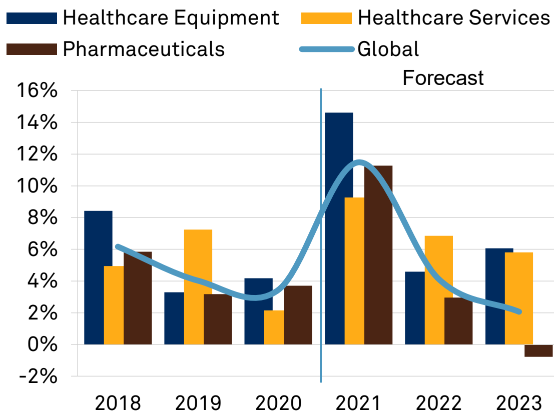


Chart 8

EBITDA margin (adjusted)

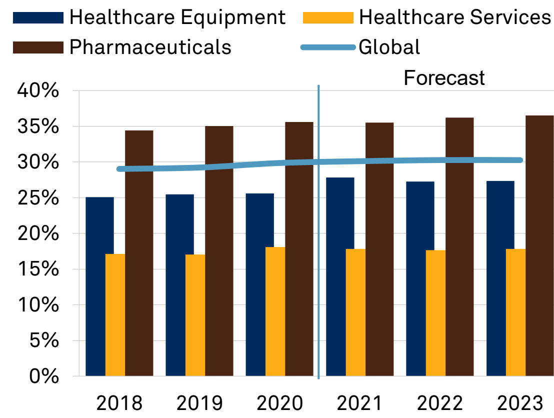


Chart 9

Debt / EBITDA (median, adjusted)

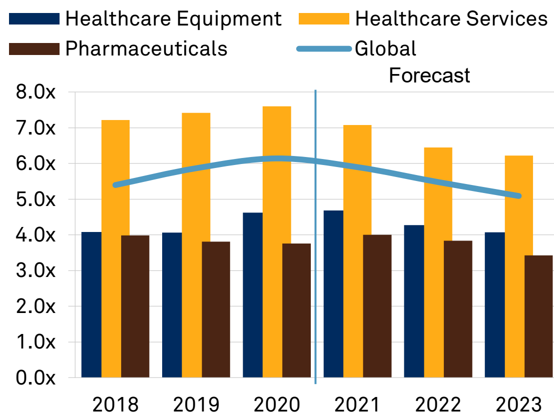
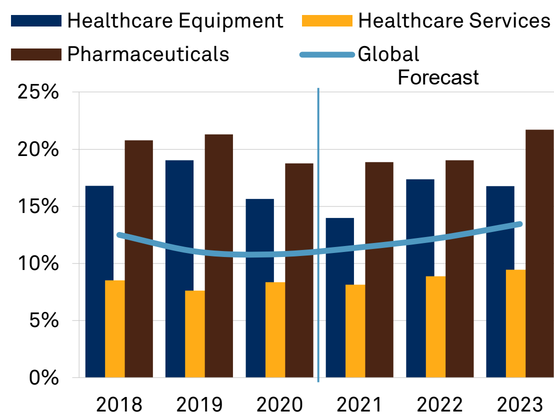


Chart 10

FFO / Debt (median, adjusted)



Source: S&P Global Ratings. Revenue growth shows local currency growth weighted by prior-year common-currency revenue-share. All other figures are converted into U.S. Dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO—Funds from operations.

Cash, debt, and returns

Global Health Care

Chart 11

Cash flow and primary uses

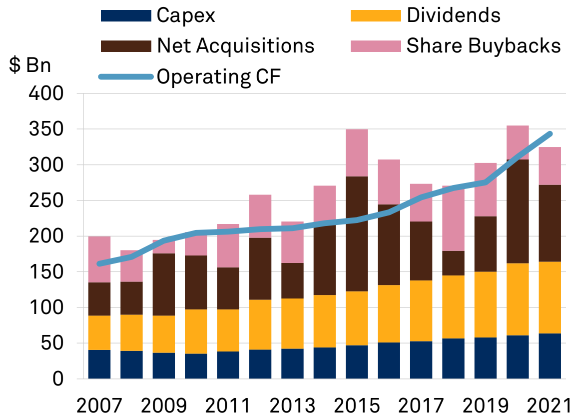


Chart 12

Return on capital employed

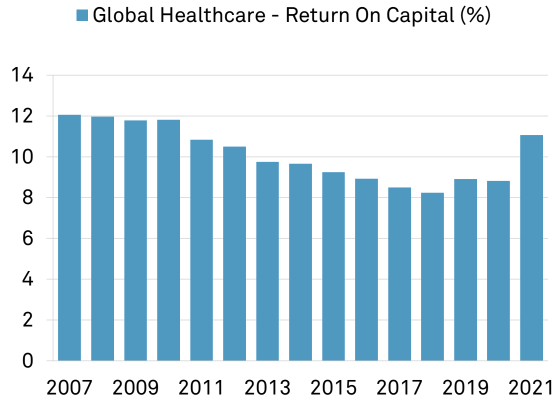


Chart 13

Fixed versus variable rate exposure

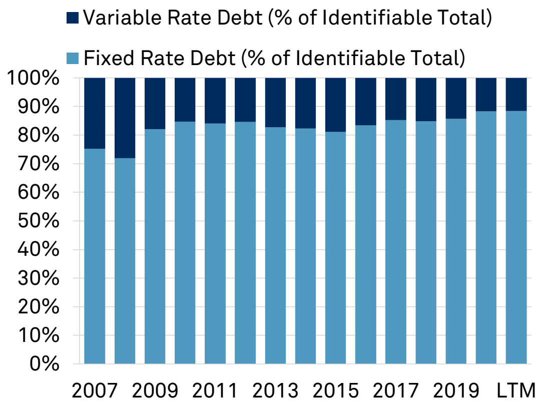


Chart 14

Long term debt term structure

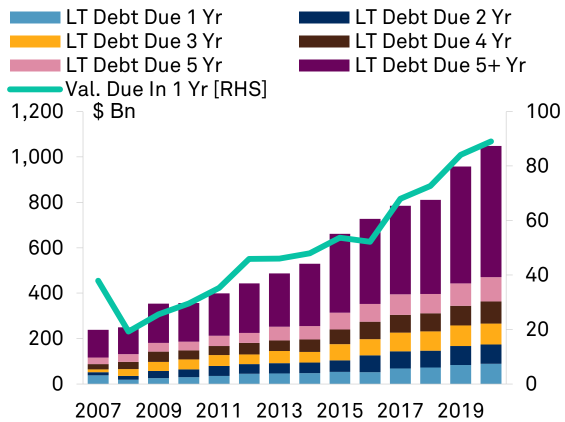


Chart 15

Cash and equivalents / Total assets

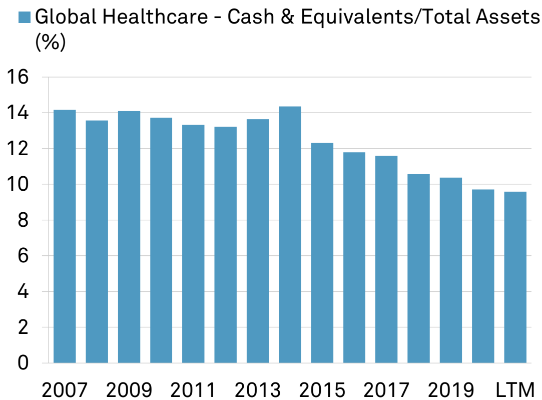
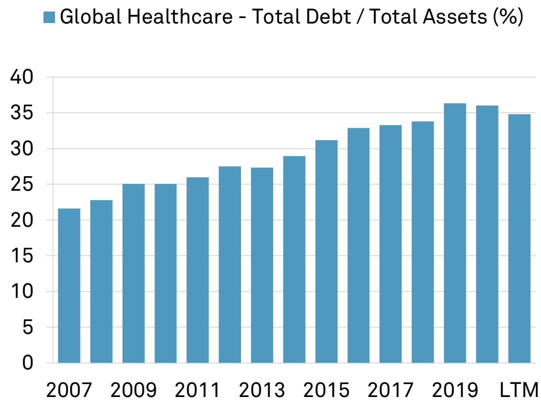


Chart 16

Total debt / Total assets



Source: S&P Global Market Intelligence, S&P Global Ratings calculations. Most recent (2021) figures are using last twelve months (LTM) data.

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