



UNIVERSITY MEDICAL CENTER
OF EL PASO

DATE: Oct. 1, 2018

TO: David Crowder
El Paso Inc.

FROM: Jacob Cintron
UMC President & CEO

SUBJECT: Ratings Downgrade Response to Media Query

On Tuesday, Sept. 18, 2018, Moody's Investors Service ("Moody's") changed the Bond Rating of the El Paso County Hospital District ("EPCHD") from an "A2" to a "Baa1" with a negative outlook, a ratings reduction of two levels. This change reflects a new methodology adopted by Moody's (and similar ratings services) which places an emphasis on liquidity in relation to leverage. Before this change, public healthcare systems were treated as government entities with taxing authority. The new methodology now treats public healthcare systems like a health enterprise focused on healthy margins and cash reserves. Tuesday's grade adjustment is reflective of that change in methodology, rather than a change in EPCHD's financial position. *(In June, Fitch Ratings downgraded EPCHD from an "AA-" with a stable outlook to an "A-" with a stable outlook; while S&P Global Ratings changed the Bond Rating of the EPCHD to 'BBB+' from 'A-', a ratings reduction of only one level.*

Of note:

- We do not expect this adjustment to have any impact on EPCHD financially, as we have no current plans to issue or refinance general obligation bonds.
- We expect the majority of public healthcare systems across the country to experience similar adjustments when their annual credit reviews come around and ratings agencies have acknowledged as much.
- Ratings agencies expect around 60 percent of the nation's public healthcare systems to receive credit rating downgrades, up to three grades lower, even if their performance has improved over the last year, as EPCHD's has.

While EPCHD focuses on fiscal prudence and resource accountability, our policy is to not have large margins or cash reserves because every dollar we tie up in those activities is a dollar that was not used on our legal mandate of providing care to El Paso's indigent and uninsured populations.



UNIVERSITY MEDICAL CENTER
OF EL PASO

In addition, the state of Texas relies heavily on six urban public healthcare systems to provide the vast majority of state match for Medicaid supplemental programs that pay for indigent care in all of Texas's 254 counties - EPCHD is one of those public healthcare systems. This obligation makes it difficult for us to carry cash on hand in amounts similar to private health systems even if we wanted to.

FREQUENTLY ASKED QUESTIONS

Q: What change in bond rating was announced by Moody's on Tuesday?

A: EPCHD's bond rating has been downgraded from an "A2" to a "Baa1" with a negative outlook. This rating downgrade is reflective of a change in the three major rating agencies' methodology, rather than a change in EPCHD's financial position and we expect the majority of public healthcare systems across the country to also face a credit rating downgrade as their annual reviews come up.

Q: What impact does this have on EPCHD or in particular, UMC?

A: There is no immediate financial impact to EPCHD / UMC. This rating would mainly affect us if we were to issue or refinance general obligation bonds. But we have no current plans to issue such bonds.

Q: What potential long-term financial impact could this have for EPCHD / UMC?

A: Should the need arise for UMC to issue general obligation bonds in the future, the lower rating would mean a higher debt service cost to taxpayers.

Q: What changes to rating agencies' methodology are you referring to?

A: The ratings agencies used to classify EPCHD as a taxing entity (which it is). This allowed a higher credit rating and allowed for some downward adjustment for our lack of cash on hand and healthy margin. Now, the agencies look at EPCHD and other public healthcare systems as healthcare enterprises whose performance is primarily based on carrying a healthy margin and holding cash in reserves and they will then consider a rating upgrade based on our access to tax revenue. So we are being graded more like private health enterprises and we get less consideration for being a taxing entity.

Q: So what is EPCHD going to do to improve its margin and days cash on hand?

A: While the credit agencies may group EPCHD / UMC in with private healthcare systems for rating purposes, the fact is that we are not a private healthcare system and we



UNIVERSITY MEDICAL CENTER
OF EL PASO

cannot do business as they do while fulfilling our mission to deliver high quality care to low-income patients.

Our priority is to avoid running large margins or storing away excessive cash reserves. Any revenue we generate must be prioritized towards patient care. Storing large reserves or focusing on profit margins means fewer people are receiving care than otherwise could be.

UMC is going to stay true to its mission. We have no plans to attempt a change in payer mix or to store away large cash reserves.

Of course, we do need to ensure we provide high quality care as efficiently as possible.

Q: Is the EPCHD / UMC in financial trouble?

A: No. This rating adjustment is reflective of a change in the rating top three ratings agencies' methodology, not EPCHD's current financial performance. In fact, UMC is in a stronger financial position today than it was in each of the last two years when we had a higher rating. Our earnings are higher, and our outstanding long-term debt is decreasing.

This rating adjustment is just a reflection of the new methodology.

Q: UMC has greatly increased volumes of patients. Doesn't that translate into higher revenue?

A: No. UMC provides care to El Paso County's indigent and uninsured. Even when a patient presents to us with a payment source such as Medicaid, that payment source often doesn't cover the full cost of care. So more volume can sometimes mean greater costs for UMC that is usually higher than revenue. This is the opposite of what you would generally see in private healthcare systems.

Q: What's the bottom line?

A: This change in methodology will cause a credit rating downgrade for a majority of US public healthcare systems. UMC cannot switch its operations to mirror those of a private healthcare system or we would be unable to fulfill our legal mandate of caring for low-income patients while minimizing reliance on El Paso County taxpayer support. But we must do everything we can to improve efficiency as possible while providing high quality care.



UNIVERSITY MEDICAL CENTER
OF EL PASO

cc: Lorena Navedo, Chief Administrative Officer
Letty Flores, EPCHD Controller