MOODY'S
INVESTORS SERVICE

Rating Action: Moody's Affirms Baylor Scott & White Health's (TX) Aa3 and Aa3/P-1; Outlook Stable

Global Credit Research - 19 Apr 2017

New York, April 19, 2017 -- Summary Rating Rationale

Moody's Investors Service affirms the Aa3 and Aa3/P-1 ratings for Baylor Scott & White Health (TX) (BSWH) and Baylor Scott & White Holdings, affecting $2.1 billion of debt. The outlook is stable.

The Aa3 is attributable to BSWH's position as the largest not-for-profit health system in Texas, geographic diversity, favorable demographics driving very good revenue growth, strong cashflow margins, and proven track record of executing integration and growth strategies. Margins recently moderated primarily due to health plan exchange losses, but BSWH took swift actions to address the issue by exiting the Individual Public Health Insurance Exchange, moderating overall capital spending and identifying certain assets to divest. Challenges include high competition and no Certificate of Need regulations, a leveraged balance sheet, managing an aggressive growth strategy, and potential reduction in sizable Medicaid supplemental funds if the Texas Medicaid waiver program is not extended.

The P-1 short-term rating on BSWH's Windows debt reflects our estimation of the system's market access and ability to pay the purchase price of a mandatory tender when due at the end of the mandatory tender window.

Rating Outlook

The stable outlook reflects strong management ability to respond to challenges quickly and effectively and expected improvement in operating cashflow in FY 2018, following actions to address health plan issues and continued cost reduction initiatives. While capital spending may increase for strategic and IT needs, we expect the system will balance spending with cashflow to maintain liquidity; BSWH has a history of underspending capital budgets when cashflow underperforms. No material new debt is expected at this time in the absence of cashflow growth.

Factors that Could Lead to an Upgrade

Meaningful deleveraging of balance sheet and operation

Significant reduction in competition or increase in market share

Sustained improvement in operating margins

Factors that Could Lead to a Downgrade

Material amount of incremental debt and notable weakening of leverage metrics

Multi-year decline in operating margins or inability to absorb significant decline in Medicaid funding

Contraction in liquidity

Dilution of key measures from acquisition or merger

Legal Security

The bonds are an unsecured general obligation of the Obligated Affiliates. Obligated Affiliates include Baylor Scott & White Holdings, Baylor Health Care System, Baylor University Medical Center, Baylor All Saints Medical Center, Baylor Regional Medical Center at Grapevine, Baylor Medical Center at Waxahachie, Baylor Regional Medical Center at Plano, Scott & White Memorial Hospital, Scott & White Healthcare, Scott & White Clinic, Scott & White Hospital-Round Rock, Scott & White Continuing Care Hospital, Hillcrest Baptist Medical Center, Baylor Medical Centers at Garland and McKinney, Scott & White Hospital College Station, and Baylor Scott & White Health.

Use of Proceeds

Not applicable.

Obligor Profile

BSWH is the largest not-for-profit healthcare system in Texas with 48 hospitals in North and Central Texas, a large network of affiliated physicians, the large Scott & White Health Plan with approximately 250,000 members and the Baylor Scott & White Quality Alliance with approximately 330,000 covered lives.

Methodology

The principal methodology used in this rating was Not-for-Profit Healthcare Rating Methodology published in November 2015. The additional methodology used in the short term rating was Rating Methodology for Municipal Bonds and Commercial Paper Supported by a Borrower's Self-Liquidity published in January 2012. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

Regulatory Disclosures

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