Moody's
INVESTORS SERVICE

Rating Action: Moody's assigns Aa3 to Advocate Aurora Health's Ser. 2019; outlook revised to positive

29 Oct 2019

New York, October 29, 2019 -- Moody's Investors Service has assigned a Aa3 rating to Advocate Aurora Health's proposed Taxable Bonds, Series 2019 ($363.2 million). The bonds are expected to be issued as fixed rate with a bullet maturity in 2049. Concurrently, the outstanding ratings on Advocate Aurora Health's obligations, which include legacy borrower Aurora Health Care, Inc., WI, have been affirmed at Aa3, Aa3/VMIG 1 and Aa3/P-1. The outlook has been revised to positive from stable. These actions affect approximately $2.3 billion of debt

RATINGS RATIONALE

Affirmation and assignment of the Aa3 reflect Moody's expectation that Advocate Aurora Health (AAH) will continue to benefit from size and scale as a market leader within two relatively large service areas and will be able to expand and leverage its experience in value based care across its regions. Moody's expects AAH will be able to integrate, as it has thus far, its two legacy systems without major disruption. Also, the system will be better positioned to realize further synergies because of its more streamlined management structure and a common IT platform. Additionally, Moody's expects AAH will maintain low leverage, a favorable liquidity position, and healthy margins (absent non-recurring expenses), as seen over the last 18 months. Offsets include fierce competition in rapidly consolidating markets, pricing pressure and unfavorable payor mix shifts, particularly in the Illinois region, as well as elevated capital spend over the coming two years.

The VMIG 1 rating reflects the availability of bank standby bond purchase agreements for unremarketed tenders of variable rate bonds. The P-1 rating for bonds in the Windows mode reflects market access based on the system's ample liquidity and notice to pay unremarketed tenders.

RATING OUTLOOK

The revision of the outlook to positive from stable reflects Moody's expectation that over the next two years, AAH will continue to achieve normalized operating cash flow margins in the 9.5% to 10% range, aided by diversification of revenues and achievement of synergy targets. Moody's expects that this successful execution will continue to be supported by a more streamlined management structure. Likewise, Moody's expects cashflow growth will continue to result in incremental strengthening of balance sheet measures.

FACTORS THAT COULD LEAD TO AN UPGRADE

- Ability to see improvement in and sustain strengthening of balance sheet measures

- Able to sustain very good operating cash flow margins

- For the unenhanced short-term rating: Not applicable

- For the enhanced short-term rating: Not applicable

FACTORS THAT COULD LEAD TO A DOWNGRADE

- Meaningful liquidity decline

- Lower than expected operating cashflow margins

- Increased leverage resulting in notable impairment of debt metrics

- For the unenhanced short-term rating: downgrade by Moody's of AAH's long-term rating below A2

- For the enhanced short-term ratings: a downgrade by Moody's of the short-term Counterparty Risk Assessment of the Bank that provides the SBPA

LEGAL SECURITY

Under an Amended and Restated Master Trust Indenture, issued in 2018, security is a general, unsecured obligation of the obligated group. There is no additional indebtedness tests. The members of the obligated group under the Master Indenture are: Advocate Aurora Health, Inc., Advocate Health Care Network, Advocate Health and Hospitals Corporation, Advocate Sherman Hospital, Advocate North Side Health Network, Advocate Condell Medical Center, Aurora Health Care, Inc., Aurora Health Care Metro, Inc., Aurora Health Care Southern Lakes, Inc., Aurora Health Care Central, Inc. d/b/a Aurora Sheboygan Memorial Medical Center, Aurora Medical Center of Washington County, Inc., Aurora Health Care North, Inc. d/b/a Aurora Medical Center Manitowoc County, Aurora Medical Center of Oshkosh, Inc., Aurora Medical Group, Inc., Aurora Medical Center Grafton LLC. The Amended and Restated MTI contains a substitution of notes provision.

USE OF PROCEEDS

Bond proceeds will be used to refund outstanding debt of AAH.

PROFILE

Advocate Aurora Health, Inc. (AAH; $12 billion revenue), provides a continuum of care through its 27 acute care hospitals, an integrated children's hospital and a psychiatric hospital, which in total have over 6,500 licensed beds, primary and specialty physician services with approximately 3,700 employed physicians, outpatient centers, physician office buildings, pharmacies, behavioral health care, rehabilitation, home health and hospice care in northern and central Illinois, eastern Wisconsin and the upper peninsula of Michigan.

METHODOLOGY

The principal methodology used in the long-term underlying ratings was Not-For-Profit Healthcare published in December 2018. The principal methodology used in the short-term underlying rating was US Bond Anticipation Notes and Related Instruments Methodology published in October 2019. The principal methodology used in the long-term enhanced ratings was Variable Rate Instruments Supported by Conditional Liquidity Facilities published in March 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

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