



We believe today's rating action by S&P is extremely disappointing and oddly timed in light of the recent progress at the West Penn Allegheny Health System (WPAHS). We are pleased that S&P acknowledges several actions have had a positive impact on WPAHS' financials, such as the reopening of West Penn Hospital's emergency department, cost containment efforts put in place by current management and ongoing support from Highmark. Unfortunately, their action does not appear to take these activities into account, but rather overemphasizes year-over-year financial comparisons. We find this to be short-sighted given recent improvements and the system's potential for the future.

WEST PENN ALLEGHENY HEALTH SYSTEM

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West Penn Allegheny Health System, PA Series 2007A Bond Rating Lowered To 'B-' On Deterioration Of Overall 2012 Finances

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NEW YORK (Standard & Poor's) May 21, 2012--Standard & Poor's Ratings Services has lowered its long-term rating to 'B-' from 'B+' on Allegheny County Hospital Development Authority, Pa.'s \$737 million series 2007A bonds, issued for West Penn Allegheny Health System (WPAHS). The outlook remains developing.

"The downgrade to 'B-' reflects deterioration in WPAHS's overall 2012 finances. Although WPAHS's financial profile suggests that an even lower rating could be justified, the rating remaining in the 'B' category reflects the increased likelihood, since Standard & Poor's last review, that the affiliation with Highmark Inc. will proceed because approval from the Department of Justice and the Internal Revenue Service has been obtained," said Standard & Poor's credit analyst Cynthia Keller. "However, ample regulatory risk remains until approval from the Pennsylvania Department of Insurance is received. Highmark's financial support of WPAHS, as outlined under the affiliation agreement, with \$200 million of support expected or already received during fiscals 2011 and 2012, continues to be a positive rating factor. Maintenance of the developing outlook reflects the possibility of continued financial deterioration if the affiliation with Highmark is not approved and the potential for credit quality improvement if the affiliation with Highmark is approved," said Ms. Keller.

The downgrade to 'B-' reflects Standard & Poor's assessment of WPAHS's;

- Significantly escalated operating losses in fiscal 2012 following poor performance in 2011;
- Volume decreases and general turmoil in the Pittsburgh market;
- Relatively weak area demographics; and

- Strained balance sheet with high debt levels, ample capital needs, substantial pension funding requirements, and weakened unrestricted cash and investments.

Rating factors that prevent a lower rating at the current time include:

- All aspects of the potential affiliation with Highmark including previously received and projected financial support, potential post-affiliation strategic initiatives, and receipt of approval for the transaction from two agencies to date; and
- Critical mass of inpatient admissions at the system, despite volume decreases, with potential growth opportunities from physician recruitment and Highmark's outpatient development initiatives in the service area.

The developing outlook reflects Standard & Poor's opinion that the rating and outlook could either improve or deteriorate over the next 12 months. The future direction of this rating depends largely on whether the affiliation agreement with Highmark is approved and how quickly the assumed benefits of the arrangement are realized.

A lower rating is likely if the affiliation is not approved quickly or if WPAHS's financial results do not improve substantially as WPAHS's limited cash flow and low unrestricted cash and investment balances are insufficient to support its capital needs; however, the system has always funded pension and debt service at necessary levels.

A higher rating could be possible after the final affiliation agreement is signed, at which time further transfers from Highmark are secured and the two organizations will be free to implement a more integrated strategy in the Pittsburgh market.

WPAHS operates five acute-care hospitals at five locations in and around Pittsburgh.

RELATED CRITERIA AND RESEARCH

USPF Criteria: Not-For-Profit Health Care, June 14, 2007

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