**CommonSpirit Health**

**New Issuer**

**Summary**
CommonSpirit Health (Baa1 stable) represents the February 1, 2019 merger of Dignity Health and Catholic Health Initiatives. CommonSpirit Health will face the heightened execution, integration, governance and business risks of the combined organization, which has approximately $29 billion of pro-forma revenue, and operates 142 hospitals in 21 states. The organization’s broad footprint, regional focus, and diversity of revenue streams somewhat mitigate the challenges related to the complexity and magnitude of the pro-forma transaction. This is the largest domestic merger of not-for-profit health systems. The announced Office of the CEO structure (whereby each CEO has identified responsibilities and decision-making authority) is atypical and could be cumbersome, potentially affecting the rate of organizational and cultural change. Governance and execution risk - on a standalone basis, as well as pro-forma for the combination – constrain the Baa1 ratings.

The ratings favorably anticipate realization of net synergies and efficiencies from the proposed centralized operating model, smoothing some of the varying performance and financial health of certain under-performing existing divisions. Additional favorable rating factors include the benefits of a new amended/restated obligated-group-model Master Trust Indenture, with an obligated group comprised of historical Dignity Health and historical CHI entities. The proposed MTI provides improved contractual and structural support, and represents a particular improvement for historical CHI debt holders.

Affirmation of the VMIG2 and P-2 short-term ratings on debt that is backed by CommonSpirit’s own liquidity is a function of sufficient liquidity headroom at those levels, and the continuation of good treasury management practices.

**Exhibit 1**

Although revenues represent massive scale and good diversification, profitability is modest

2015-2018 based on consolidated pro-forma of audited results for CHI and Dignity Health, ended June 30. For Dignity Health, net benefit from The California State Provider Fee is normalized; benefit from Scripps Health is excluded; and the change in mark-to-market of interest rate swaps is removed from interest expense. For CHI, operating income excludes investment earnings.
and gains on business combinations, and includes cash-related restructuring expenditures. 2019 based on unaudited pro-forma management-prepared interim financial statements, annualized.

Source: Moody’s Investors Service

Credit strengths

» Very large national system with $29 billion in pro forma revenues; operations across 21 states will provide some offsets to sizable losses at some of the individual markets

» Strong brand in many of the local markets although competition, particularly in the ambulatory space, will remain high in some of the growth markets

» 2016 legislation in California may allow for more predictability the timing of cash receipts for the provider fee program

» Organizational integration presents the opportunity to achieve significant savings, though execution risk is high

» 2019 plan of finance will significantly improve debt structure, and decrease combined peak debt service cost

» Proposed traditional obligated group structure provides good debt security

Credit challenges

» Execution risk will be high given the infancy of the merger; successful blending of two established cultures into a unified mission will be integral in gaining synergies

» Operating measures are expected to remain below the medians for the rating category for the next several years, despite anticipated material improvement

» Reliance on California provider fees, while declining on a relative basis given the pro forma size of the system, will remain a driver of financial stability

» Continued financial pressure in the Texas market and the prolonged sale of the Louisville based operations will require additional resources and strong oversight by senior leadership

» Operations in several highly competitive and high-growth markets will continue to challenge margins, and will require active management

» Liquidity position will remain relatively pressured, with the expectation that cash-to-total debt will remain under 100% for the foreseeable future and that days cash on hand will remain below the median for the rating category; capital spending is expected to be actively managed which should help with cash management

» Pension obligations will remain material with unions in many of the California markets

Rating outlook

The stable outlook at the Baa1 rating level incorporates ongoing underperformance of several markets, including Kentucky and Texas; the reliance on the California State provider fee in California, which we view as a social risk consideration; the exposure to certain environmental risks in California and other regions; and high exposure to unions in certain markets. The outlook further reflects our expectation that pro-forma operating, balance sheet, and debt measures will remain modest throughout the intermediate term, despite anticipated improvements. Current analysis includes reliance on unaudited interim results and is absent a full-year of expertized pro-forma financial statements.

Factors that could lead to an upgrade

» Material improvement in operating, balance sheet, and debt measures

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Successful integration of historical organizations

Short-term ratings (VMIG 2 and P-2): Improvement in overall credit quality of borrower; improved coverage levels

Factors that could lead to a downgrade

- Decrease in operating performance
- Dilution of balance sheet measures
- Deterioration in debt metrics
- Negative complications resulting from the integration
- Short-term ratings (VMIG 2 and P-2): Decline in overall credit quality of borrower: further decline in coverage

Key indicators

Exhibit 2

<table>
<thead>
<tr>
<th>CommonSpirit Health</th>
<th>Proforma Consolidated</th>
<th>Proforma Consolidated</th>
<th>Proforma Consolidated</th>
<th>Proforma Consolidated</th>
<th>Proforma Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Revenue ($'000)</td>
<td>26,944,624</td>
<td>28,349,759</td>
<td>28,453,105</td>
<td>29,204,128</td>
<td>28,753,333</td>
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<tr>
<td>3 Year Operating Revenue CAGR (%)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>2.7</td>
<td>0.5</td>
</tr>
<tr>
<td>Operating Cash Flow Margin (%)</td>
<td>6.3</td>
<td>4.9</td>
<td>4.5</td>
<td>7.4</td>
<td>5.7</td>
</tr>
<tr>
<td>PM: Medicare (%)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>PM: Medicaid (%)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
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<tr>
<td>Days Cash on Hand</td>
<td>175</td>
<td>153</td>
<td>171</td>
<td>161</td>
<td>154</td>
</tr>
<tr>
<td>Unrestricted Cash and Investments to Total Debt (%)</td>
<td>88.4</td>
<td>79.3</td>
<td>92.3</td>
<td>88.3</td>
<td>87.5</td>
</tr>
<tr>
<td>Total Debt to Cash Flow (x)</td>
<td>5.8</td>
<td>7.2</td>
<td>7.0</td>
<td>4.8</td>
<td>5.8</td>
</tr>
</tbody>
</table>

2015-2018 based on consolidated pro-forma of audited results for CHI and Dignity Health, ended June 30. For Dignity Health: net benefit from The California State Provider Fee is normalized, benefit from Scripps Health is excluded; and the change in mark-to-market of interest rate swaps is removed from interest expense. For CHI: operating income excludes investment earnings and gains on business combinations, and includes cash-related restructuring expenditures. 2019 based on unaudited management-prepared interim financial statements, annualized, and adjusted to give effect to the Series 2019 financing. Investment returns normalized at 5%

Source: Moody's Investors Service

Profile

CommonSpirit represents the February 1, 2019 merger of Dignity Health and CHI, the latter of which changed its corporate name to CommonSpirit Health. CommonSpirit has approximately $29 billion of pro-forma consolidated revenues and is headquartered in Chicago. Larger markets include California, Colorado, Arizona, the Pacific Northwest and Texas.

Detailed credit considerations

Market position: size and scope of consolidated organization provides good diversification and a degree of overall stability

CommonSpirit’s large size and good diversification will provide a certain level of overall stability. Nevertheless, certain markets remain challenged, and will vie for management’s attention during this heightened period of transition and transformation. The combining of Catholic Health Initiatives (previously rated Baa1 stable) with Dignity Health (previously rated A3 stable) creates an organization with a presence in 21 states and nearly $29 billion of annual revenues.

Pro-forma for the combination, CommonSpirit’s single largest state exposure is California, at 28.5% of operating revenues, with other large markets consisting of the Southwest (which includes Nevada, at 10.3%), the Southeast (which includes Kentucky, at 9.7%), the Pacific Northwest (9.8%), Colorado (8.7%), Texas (8.1%), Arizona (8.1%) and Nebraska (71%). Management has created a divisional management structure which it hopes will allow it to optimize performance in particular markets, while coordinating overall operating
practices system wide. The success of the organization will hinge in large part on how well it can transform practices in certain markets that have long underperformed, while keeping the organization as a whole culturally unified, enabling it to optimize synergies, and take advantage of economies of scale. Given the large presence in California, CommonSpirit is particularly vulnerable to certain environmental risks, as well as to certain social risks reflected in the large unionized work force at historical Dignity.

Certain markets are particularly challenged. Texas (8.1% of revenues through 9 months 2019) continues to face financial and operational changes given certain clinical events at Baylor St. Luke’s Medical Center (BSLMC), including within its cardiac transplant program. The Houston area is highly competitive with several larger tertiary systems in the Texas Medical Center. CHI has changed local and divisional management multiple times but has been thus far unable to show material improvements. The clinical issues outlined by CMS have been addressed and BSLMC has reapplied for CMS certification of its cardiac transplant program. Management reports that volumes have already begun to improve, however we expect that it may be a protracted period of time before financial performance fully rebounds.

CommonSpirit’s KentuckyOne’s Louisville market is also in flux as it seeks a buyer for its assets. While represented as a discontinued operation, Louisville will continue to require management’s time and resources until it is divested or resolved. Louisville is also a highly competitive market. Conversely, there are other markets which have historically performed well and are likely to continue to generate strong margins, including Colorado, the Pacific Northwest, and portions of Arizona and California. This portfolio approach, and diversity of revenue streams, helps generate a certain level of stability. Nevertheless, CommonSpirit will need to improve performance overall in order for the organization to begin to perform closer to its potential.

Operating performance, balance sheet, and capital plans: measures are modest for the rating category and are expected to slowly improve over time

Pro-forma consolidated operating results for fiscal 2019 (ended June 30) are likely to be materially under budget, and represent a significant decline from proforma consolidated results for the previous year. While 2019 results include a number of one-time items relating to the merger, and also reflect the challenge of combining such large organizations, they nevertheless are also indicative of operating challenges across many markets, including the overall softening of utilization measures, weaker rate improvements, and systemic cost pressures. Management has modified its budget for 2020, and recently announced additional impairments at some of the historical CHI facilities that are likely to be included with the 2019 audit.

Favorably, the merger will reduce the relative reliance on the California provider fee which historically has represented up to 50% of Dignity’s operating cash flow. Pro-forma for the combination, the provider fee will represent about 26% of operating cash flow based on fiscal 2019 projections. Prior funding had been variable in timing and amount, but 2016 state legislation has created greater predictability, and smoother program cashflows.

Despite lowering budgeted expectations for 2019, management is optimistic that the long-term trajectory of the organization is positive, and has identified some $2 billion of improvements which it believes it can achieve in the next four years. Favorably, management has also been clear about what its long term performance targets are, which consists of an operating cashflow margin target of 8%, debt to capitalization of 40%, MADS coverage of 3.5 times, and days cash on hand of at least 150 days. We believe performance will improve over the long term, however we expect results to remain below the medians for the rating category for at least the next several years. Failure to show consistent improvement could result in credit pressure.

LIQUIDITY

Proforma consolidated liquidity is somewhat modest for the rating category, with proforma days cash on hand (inclusive of $600 of reimbursement from the financing) at 154 days, compared to the Baa median of 172 days. Management’s intention is to maintain liquidity at at-least 150 days cash on hand going forward. Capital spending will be adjusted depending on available resources with this target in mind although certain inflight or prior large commitments will be funded. The historical organizations currently still maintain separate investment pools, which will be brought together over time.

Debt Structure and legal covenants: somewhat modest debt measures for the rating category

The 2019 financing represents significant improvement to the historical debt structures, increasing exposure to fixed rate debt from 47% to 64%, and overall decreasing consolidated maximum annual debt service (MADS) by over $100 million. Nevertheless, debt
measures are modest for the rating category, with cash to debt at 88% (Baa1 median is 121%), debt to cashflow at 5.6 x (Baa1 median is more favorable at 3.7 times), and MADS coverage of 2.8 times (Baa1 median is 2.9 times).

DEBT STRUCTURE
CommonSpirit’s proforma consolidated debt structure consists of 64% traditional fixed rate bonds, with the rest spread among a wide variety of products, including variable rate demand bonds, self-liquidity backed commercial paper, put bonds, bank loans, and floating rate notes, among other products. MADS of $810 million is a smoothed calculation (as permitted by the MTI). Actual MADS is $1.6 billion, occurring in year 2025, with additional bullets occurring in 2023, 2030, and 2050. Given the material amount of bullets and short term debt, CommonSpirit will remain highly reliant on market access to manage its debt service obligations. Nevertheless, CommonSpirit’s $11.6 billion of unrestricted cash and investments more than amply covers the largest bullets, giving the organization flexibility and protection in the case of temporary market disruptions.

LEGAL SECURITY
Proposed bonds, as well as the outstanding debt of Dignity Health and CHI, will be secured by a gross revenue pledge of the obligated group under an amended Master Trust Indenture (MTI). All proposed and outstanding debt will be on parity. As part of the system’s plan of finance, CommonSpirit intends to amend and consolidate CHI’s COD and Dignity’s Master Trust Indenture into a new MTI for CommonSpirit.

CommonSpirit’s security package represents a strengthening to the existing security on the Catholic Health Initiatives debt which heretofore utilized a restricted affiliate structure. Approximately 92% of the system’s revenues will be in the obligated group. Proposed covenants under the MTI is limited to a 1.1x debt service coverage test. Coverage below 1.0x constitutes an Event of Default (with a 60-day cure period and consent of 25% of bondholders).

Per the MTI, operating leases will be excluded from the calculations. Key definitions of the covenant calculations include the exclusion of extraordinary losses, non-recurring losses and non-cash losses from daily expenses. Long-term indebtedness includes guarantees for longer than one year and financing leases. A substitution of notes is permitted if the pro-forma obligation is rated in one of the three highest rating categories (Aaa, Aa or A) and the revenue pledge to be maintained with an A3, A- or A- rating. A reorganization (such as a sale, merger or divestiture) is permitted by an obligated group member but must meet 1.1x pro-forma coverage unless rated Aa3 or equivalent. Any new owner must assume the associated-debt of that member or asset. Amendments with bondholder consent require 51% of bondholders.

Covenants included in the proposed bank documents include: 1) 75-days cash on hand (measured annually); 2) debt to capitalization not to exceed 65%; and 3) bond rating requirement of at least two investment grade ratings (Baa3 or BBB-, or better).

DEBT-RELATED DERIVATIVES
Dignity Health was a counterparty to a number of swap agreements, with total notional of $1.7 billion, equal to 32% of Dignity Health’s debt. Dignity included the change in the mark-to-market of its swap portfolio in interest expense, which we exclude in our calculations. CHI and its affiliates had 19 different swap agreements with a total notional amount of $1.6 billion, equal to approximately 18% of all of its debt. The current size of the combined swap portfolio is $3.1 billion, equal to 23% of all debt, and the consolidated mark to market is -$597 million, $208 million of which is currently posted as collateral. All swaps (with the exception of one small affiliated swap) will be secured under the new MTI.

PENSIONS AND OPEB
Dignity carried an unfunded pension liability of $1.2 billion, as of FYE 2018, equal to a funded ratio of 86%. The program is a church plan and is one of many church plans currently subject to litigation. It is not known when the suit will be resolved. CHI has approximately 15 different defined benefit plans held within a single trust. The aggregate unfunded liability as of FYE 2018 was $854 million, equal to an aggregate funded level of 83%. Additionally, CHI and Dignity combined have the debt equivalent of nearly $2 billion of operating leases (calculated at 4 times lease expense). Management has not yet calculated what the debt equivalent of leases will be under new accounting requirements.

Management and Governance
CommonSpirit will employ an office of the CEO model with the two CEOs of Dignity and CHI each serving in separate capacities, with a clear delineation of responsibilities. The success of this model will depend on how well it is executed. The board is constituted
from equal representation from the prior historical system boards, and includes the two CEOs and one external individual that has yet
to be named (15 in total). The senior management team is comprised of senior executives from both systems that are charged with
executing the near, intermediate and long-term integration goals to gain savings and efficiencies. We view execution risk as high given
the infancy of the merger, the size of the system, and the blending of cultures which will be integral to the success of CommonSpirit.
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