

## **RATING ACTION COMMENTARY**

### **Fitch Rates UPMC Health System, PA's 2025A, B&C Bonds 'A'; Revises Outlook to Negative**

Thu 06 Mar, 2025 - 3:52 PM ET

Fitch Ratings - New York - 06 Mar 2025: Fitch Ratings has assigned an 'A' rating to the following bonds to be issued on behalf of UPMC Health System, PA:

--\$315,000,000 Pennsylvania Economic Development Financing Authority, series 2025A;

--\$400,000,000 Pennsylvania Economic Development Financing Authority, series 2025B;

--\$35,000,000 Monroeville Finance Authority, series 2025C

In addition, Fitch has affirmed UPMC's Issuer Default Rating and the outstanding parity debt issued on behalf of UPMC at 'A'.

The Rating Outlook has been revised to Negative from Stable.

The bonds are expected to be issued as fixed-rate, tax-exempt bonds. Proceeds from the 2025A bonds will provide about \$265 million for capital projects. The remainder, together with other funds, will be used to refund a portion of the outstanding series 2020D taxable notes.

Proceeds of the series 2025B bonds will provide about \$200 million for capital projects. The remainder, together with other funds, will be used to refund the outstanding Pennsylvania Economic Development Financing Authority series 2014A.

Proceeds of the series 2025C bonds will be used to refund the series Monroeville Finance Authority 2014B bonds.

The bonds will be sold via negotiation on or about March 17, 2025.

RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡			PRIOR ⚡
UPMC Health System (PA)	LT IDR	A Rating Outlook Negative	Affirmed	A Rating Outlook Stable
UPMC Health System (PA) /General Revenues/1 LT	LT	A Rating Outlook Negative	Affirmed	A Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

The Negative Outlook reflects two years of significant operating losses, leading to break-even operating cash flow and slightly weaker liquidity metrics. The consolidated system reported an operating loss of nearly \$700 million in fiscal 2024 (unaudited), which is equal to a 0.8% operating EBITDA margin, driven by substantial losses in UPMC's insurance division. (Fitch includes \$242 million of academic support and interest expense in operating income.)

The insurance division losses were driven by higher utilization, increased pharmaceutical costs, and compressed Medicaid rates. The provider division showed meaningful operational improvement, achieving a 4.9% operating EBITDA margin. However, this was not sufficient to offset the significant challenges faced by the insurance division.

Management aims to return the system to profitability in FY 2025 by leveraging improved Medicaid rates, which were finalized in November 2024 and became effective Jan. 1, 2025. UPMC will continue implementing efficiency and margin initiatives, targeting significant improvements with the expectation for incrementally better operating EBITDA margins over the five-year forward look.

While higher rates are likely to drive improvement for UPMC's insurance division, Fitch believes the system still faces additional challenges in FY 2025 that could slow progress. These challenges include transitioning to a single electronic health record (EPIC), uncertainties in the current federal policy environment, and persistent sector headwinds, which are all reflected in the Negative Outlook.

The affirmation of the bonds and IDR at 'A' is based on UPMC's leading market share position in its core markets of Western Pennsylvania. The rating also reflects UPMC's significant level of revenue diversity across several markets in Pennsylvania and adjoining western New York and north-western Maryland. The rating is further supported by UPMC's large insurance division, which accounted for 54% of the consolidated system operating revenues in fiscal 2024 (year-end Dec. 31). This provides some revenue predictability.

While UPMC's operating EBITDA margins have historically been lower than the 'bbb' midrange' operating risk assessment, Fitch views the presence of the large UPMC health plan, which tends to dampen profitability, as a positive offsetting credit factor. This provides a strategic advantage, and typically natural hedge to revenue volatility.

## **SECURITY**

The bonds are secured by a gross revenue pledge of the obligated group (OG) and constitute parity debt under UPMC's 2007 master trust indenture. The Insurance Division, which is not in the OG but is owned by the corporate parent, accounted for approximately 54% of fiscal 2024 system operating revenues (before eliminations).

## **KEY RATING DRIVERS**

**Revenue Defensibility - 'bbb'**

## Leading Market Position Enhanced by Large Insurance Division

UPMC is the largest healthcare system and the largest non-governmental employer in Pennsylvania, as well as one of the largest integrated healthcare delivery networks in the country. It is also one of the world's leading organ transplant centers.

UPMC's leading market share in Allegheny County and the western Pennsylvania market remains a significant credit strength. Fitch views UPMC's revenue diversification and integrated delivery model; large, aligned physician base; extensive health plan division and sizeable geographically distributed delivery network with a 40 hospital and extensive ambulatory network with 800 clinical locations as material credit differentiators.

UPMC reported market share of 45% in the 29 counties of western PA, 25% in central PA and strong, and 58% in Allegheny County itself. There was slight 1% increase in both Allegheny County and Western PA but a 1% decline in Central PA. The completion of UPMC Vision and Rehabilitation Tower and the acquisition of Washington Health System have been accretive to market share. The 636-bed patient tower under construction in Pittsburgh will also support market share growth. Additionally, management continues to expand its outpatient footprint in Central PA, which has experienced stronger population growth than other parts of the Commonwealth.

Allegheny County is a competitive market served by two integrated delivery systems, UPMC and the Allegheny Health Network (AHN; Highmark's affiliation with West Penn Allegheny Health System).

Fitch views the approximately 54% of UPMC's gross revenues generated by its health plan division favorably. UPMC is the largest medical insurer in Western Pennsylvania with approximately 36% of the insurer market, up from 21% in 2014.

Favorably, less than 19% of UPMC's gross patient revenue were represented by Medicaid and self-pay in fiscal 2024, supporting the 'bbb' assessment for revenue defensibility.

Pennsylvania's population grew by 1.2% over the last five years, while Allegheny County's grew by 1.1%. The county has an older profile than the U.S., with median income and poverty relatively similar to national figures.

## Operating Risk - 'bbb'

### Challenged Operating Results Since FY 2022

The system has failed to meet its operating budget over the last three years, with FY23 and FY24 showing exceptionally weak performance. FY24 ended with a \$691 million operating loss, excluding one-time restructuring costs of \$128 million. This resulted in a 0.8% operating EBITDA margin, falling short of management's target in the 3% range. This follows a similar pattern in FY23, which resulted in a \$651 million operating loss or a 0.9% operating EBITDA margin. Fitch includes academic and research support (\$253 million in FY24 and \$247.3 million in FY23) as part of operating expenses, which is consistent with how this expense is treated in Fitch's hospital sector, whereas UPMC reports it as a non-operating expense.

The loss in FY24 was primarily driven by significant pressures in the insurance division due to higher medical costs not matched by rate improvements, increased pharmacy costs, and declining enrollment partially due to Medicaid redetermination. The provider division demonstrated sound improvement, returning health services to profitability through workforce recruitment that reduced agency use, expanded lower cost ambulatory access points and various cost saving opportunities. However, challenges persisted, including a still elevated length of stay, high labor cost, and inflation.

Management FY 2025 budget incorporates a material improvement which is expected to generate a stronger operating EBITDA margin. The budget is grounded in the expectation for better performance in the insurance division driven by better rates, particularly on the Medicaid business which represents most of the division's revenue. Weaker-than-performance could result in a change to the operating risk profile.

Fitch believes that UPMC's strong market position, revenue diversification and scale provide opportunities to better manage revenues and expenses within its integrated network. Management is refocusing the operating improvement plan on workforce retention, building a strong talent pipeline, reducing length of stay, increased access, capital rationalization and improved clinical outcomes. The budget also includes permanent ongoing efforts, such as supply costs management and evaluating real estate needs.

UPMC's operating risk profile is midrange, although its metrics are lower than normal for that assessment. Its operating cash flow margin tends to be lower than provider-only systems due to a lack of depreciation expense related to the health plans. Fitch incorporates in the midrange operating risk assessment UPMC's typically accretive health insurance operations and manageable capital capex relative to depreciation expense.

## **Capex**

UPMC's capital investments averaged 122% of depreciation over the last five years, with an average age of plant at 11 years at 2024 FYE. In FY23 management scaled back capital spending to \$714 million. However, FY 24 spending was closer to historical levels with UPMC spending \$958 million. Management targets approximately 1.2x depreciation expense, which is approximately \$1 billion of spend. Fitch projects UPMC will maintain this level over the medium term, except in 2025, which will be higher at \$1.4 billion.

The FY 2025 capital budget includes the 636-bed, \$1.5 billion patient tower at UPMC Presbyterian, which is expected to be completed in 2027. Other major capital spend will include a system-wide EPIC conversion that will begin in Q3 of 2025. There are no other major projects planned currently, though the system will continue to invest in ambulatory touchpoints.

## **Financial Profile - 'a'**

### **Liquidity and Leverage Metrics Lower but Generally Maintained**

UPMC's liquidity has always been low vis-a-vis the system's debt position due to the large insurance division. Unrestricted cash and investments were reported at \$7.5 billion at FYE24, a decrease over the prior year's \$8.2 billion. Cash-to-adjusted debt and days cash on hand declined to 100% and 92 days, respectively at FY 2024, compared with 110% and 108-days cash on hand at FY 2023. Cash-to-adjusted debt has been relatively stagnant over the past five years, averaging 114% due to unfavorable investment environments, weaker operating cash flow, and a large new money issuance in FY 23. Fitch includes operating leases in its calculation of debt.

UPMC's net adjusted debt to adjusted EBITDA (NADAE) was a still favorably negative 1.0x in FY 24. Fitch does not include any adjustments to debt, as UPMC's defined benefit pension plan has historically been funded above Fitch's 80% threshold.

Fitch's forward-looking stressed scenario assumes a portfolio stress of -10.7% based on UPMC's relatively conservative asset allocation and applies revenue stress in the initial two years of the stressed case. Fitch assumes a gradual improvement in operating EBITDA margins and leverage in the outer years of the stressed scenario. Additionally, Fitch assumes annual capex spending at about \$1 billion and new money debt issuance only to the extent that it is offset by debt amortization, and not intended to increase the overall debt position.

### **Asymmetric Additional Risk Considerations**

There are no asymmetric risk considerations factored into this rating analysis.

### **RATING SENSITIVITIES**

#### **Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade**

--Further margin compression, failing to return the system to operating EBITDA margins of near 3% over the two-year period.

--High capital spending that requires significant additional cash or debt commitments such that cash-to-adjusted debt falls below 100%.

#### **Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade**

--A return to stable would be based on UPMC demonstrating improvement in performance, returning operating EBITDA margin to a minimum 3% range.

--A rating upgrade is not likely in the outlook period.

### **PROFILE**

UPMC is the largest health care system and non-governmental employer in Pennsylvania. It has 40 hospitals, over 800 clinical locations, over 5,710 employed physicians and nearly 4.2 million covered lives in its network of health insurance plans. UPMC

reported total revenues of over \$29.9 billion in fiscal 2024 (year-end Dec. 31). Its international division owns, operates, or plans to operate as a partnership or joint venture facilities in Ireland, Italy, Kazakhstan, China, and Croatia.

Mary Beth Jenkins was appointed CEO of the health plan in October 2024. She has been with the organization since 1998, serving in multiple roles. Frederick Hargett was appointed as CFO in September 2023, after serving in that capacity at Novant Health, NC.

### **Sources of Information**

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by data from Lumesis.

### **REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING**

The principal sources of information used in the analysis are described in the Applicable Criteria.

### **ESG CONSIDERATIONS**

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

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**APPLICABLE CRITERIA**

[U.S. Not-For-Profit Hospitals and Health Systems Rating Criteria \(pub. 12 Nov 2024\) \(including rating assumption sensitivity\)](#)

[U.S. Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 10 Jan 2025\) \(including rating assumption sensitivity\)](#)

## **APPLICABLE MODELS**

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Portfolio Analysis Model (PAM), v2.0.1 ([1](#))

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UPMC Health System (PA)

EU Endorsed, UK Endorsed

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