HFMA Lone Star Chapter Winter Conference

ESG: Know the Symptoms

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S&P Global Ratings

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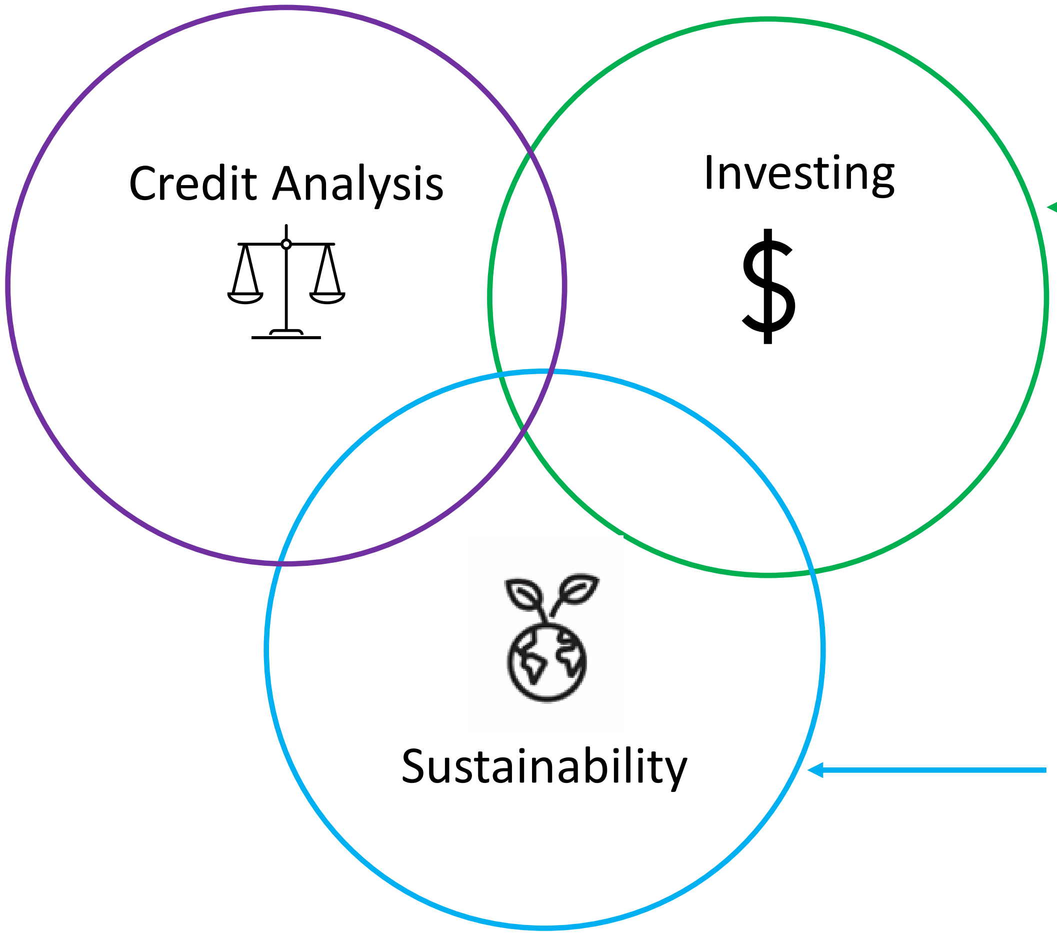
Publicly rated entities in Texas include…

CHRISTUS Health
Methodist Health System
Cook Children's
Medical Arts Hospital
Parkland
University Health
University Medical Center of El Paso
Houston Methodist Leading Medicine
Memorial Hermann
Harris Health System
Baylor Scott & White Health
Peterson Health
Guadalupe Regional Medical Center
Texas Health Resources
JPS Health Network Fort Worth, Texas
Wise Health System
Hendrick Health
children's health
Hunt Regional Healthcare
Winkler County Memorial Hospital
mch Medical Center Health System
Texas Children's Hospital

ESG in the Municipal Market | An Overview

How ESG factors affect an issuer's credit rating including disclosure requirements



- ESG investment mandates
- Dedicated exchange traded funds (ETFs) and indices
- Impact investing

Labeled bonds and general entity specific sustainability priorities

ESG Principles Criteria | General Principles of ESG Factors & Ratings

Environmental factors	Social factors	Governance factors
Climate transition risks	Health and safety	Governance structure
Physical risks	Social capital	Risk management, culture, and oversight
Natural capital	Human capital	Transparency and reporting
Waste and pollution	Other social factors	Other governance factors
Other environmental factors		

Principle One

Our long-term issuer credit ratings do not have a pre-determined time horizon.

Principle Two

The current and potential future influence of ESG credit factors on creditworthiness can differ by industry, geography, and entity.

Principle Three

The direction of and visibility into ESG credit factors may be uncertain and can change rapidly.

Principle Four

The influence of ESG credit factors may change over time, which is reflected in the dynamic nature of our credit ratings.

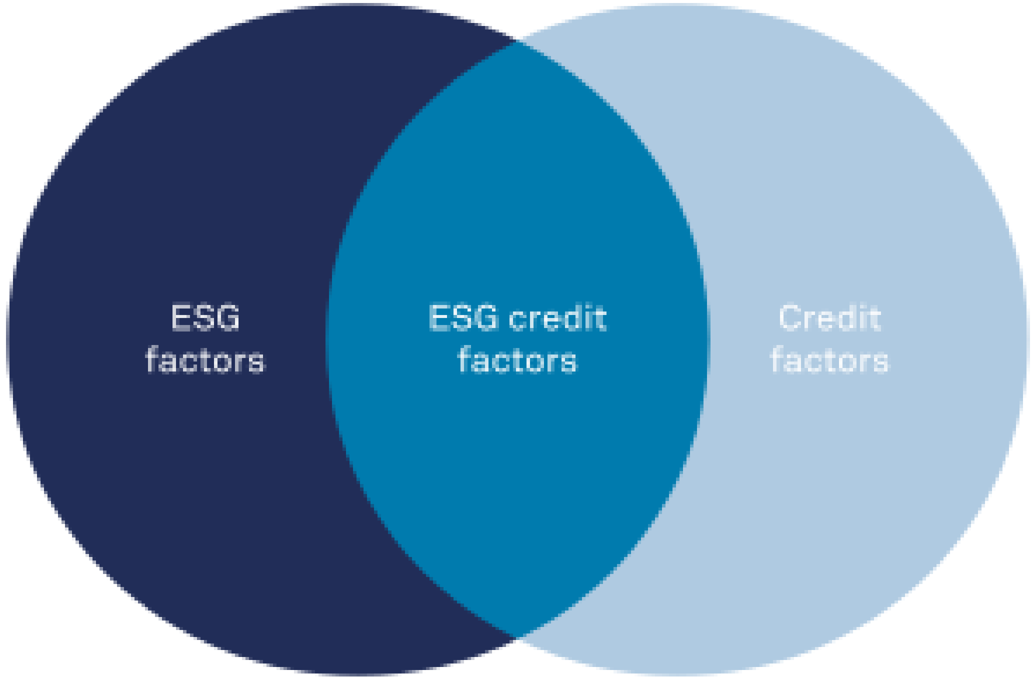
Principle Five

Strong creditworthiness does not necessarily correlate with strong ESG credentials and vice versa.

ESG--Environmental, social, and governance. Source: S&P Global Ratings.

ESG In Credit Ratings | Materiality Is Key

The materiality of ESG factors varies by sector and region and may or may not be relevant in our rating analysis.



ESG--Environmental, Social, and Governance. Source: S&P Global Ratings.

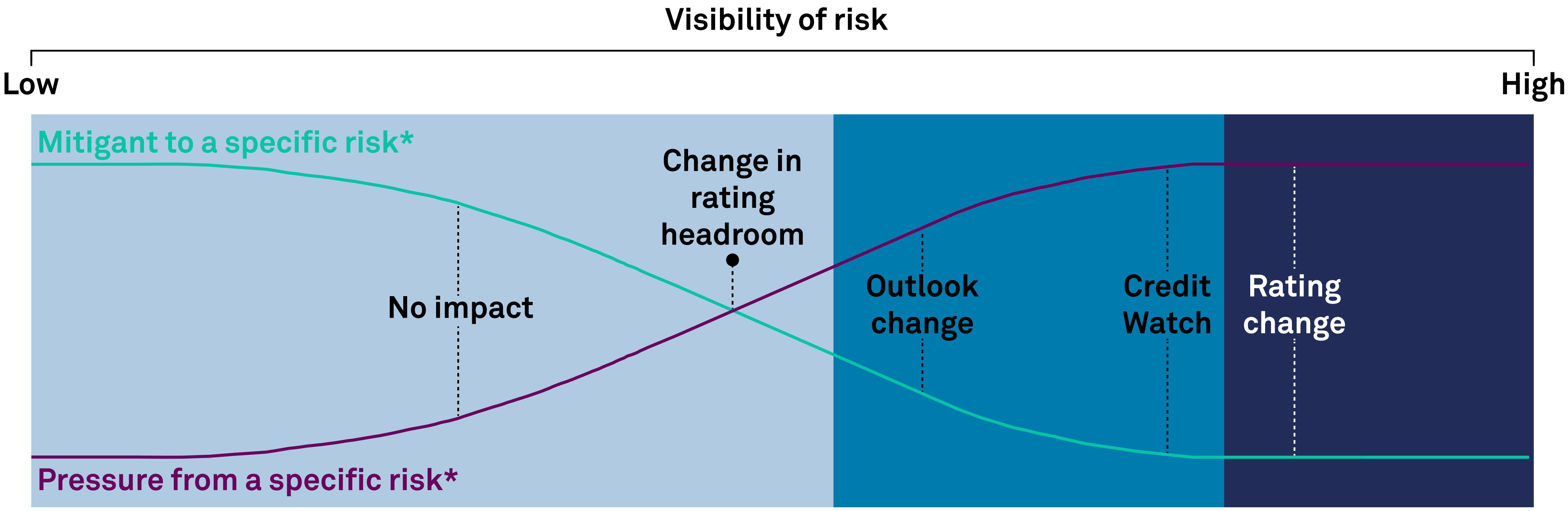
Source: Environmental, Social, And Governance Principles In Credit Ratings, published Oct. 10, 2021

- ESG factors incorporate an entity's impact from, and effect on the natural and social environment and the quality of its governance.
- **Not all ESG factors materially influence creditworthiness**.
- **ESG credit factors** are those ESG factors that can **materially influence the creditworthiness** of a rated entity and for which we have **sufficient visibility and certainty** to include in our rating analysis.

General Principles | ESG Credit Factors Can Influence Credit Ratings

– Principle Four: Our credit ratings are dynamic

Visibility of Risks: Impact on Ratings

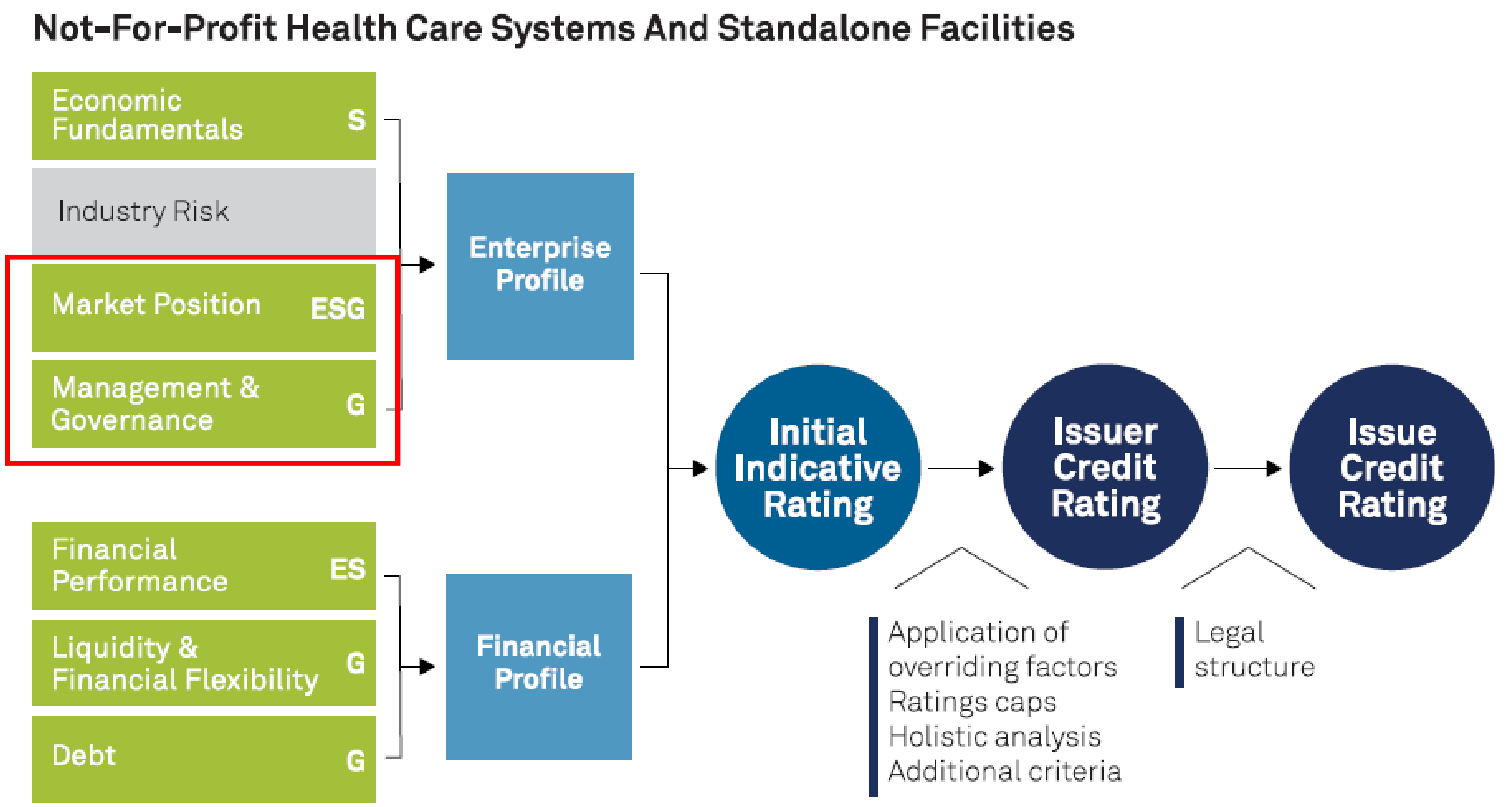


*Both the pressure from the risk and the mitigants to the risk can change or stay the same over time. This chart shows how the influence of a specific ESG risk – or opportunity – may change over time as visibility increases.

Source: S&P Global Ratings.

S&P Global Ratings

Sector Specific Criteria | ESG Credit Risks Embedded In Analysis



Credit risks identified in the Enterprise Profile can affect the Financial Profile. But good governance and risk management practices underscore important mitigants for credit rating stability.

Source: Through the ESG Lens 3.0: The Intersection of ESG Credit Factors and U.S. Public Finance Credit Factors, published March 2, 2022

Environmental | Materiality: Acute – For Now

Climate transition risks
- Costs or benefits from transitioning to net-zero away from carbon-based energy supply
- Policy or regulatory changes related to managing carbon and curtail greenhouse gas emissions

Physical risks
- Acute (i.e., increased severity of extreme weather events such as hurricanes, flooding, wildfires, and drought and their impact on water supply, economic or service areas, and facilities and/or infrastructure)
- Chronic (i.e., longer-term shifts in climate patterns including precipitation and temperature that may result in chronic heat and cold waves and their impact on water supply, economic or service areas, and facilities and/or infrastructure, as well as sea level rise)
- Natural disasters (e.g., earthquakes, tornados)

Natural capital
- Water scarcity or supply limitations that affect operations or an entity's economic base or service area
- Biodiversity and land use related to development patterns in protected or preserved areas

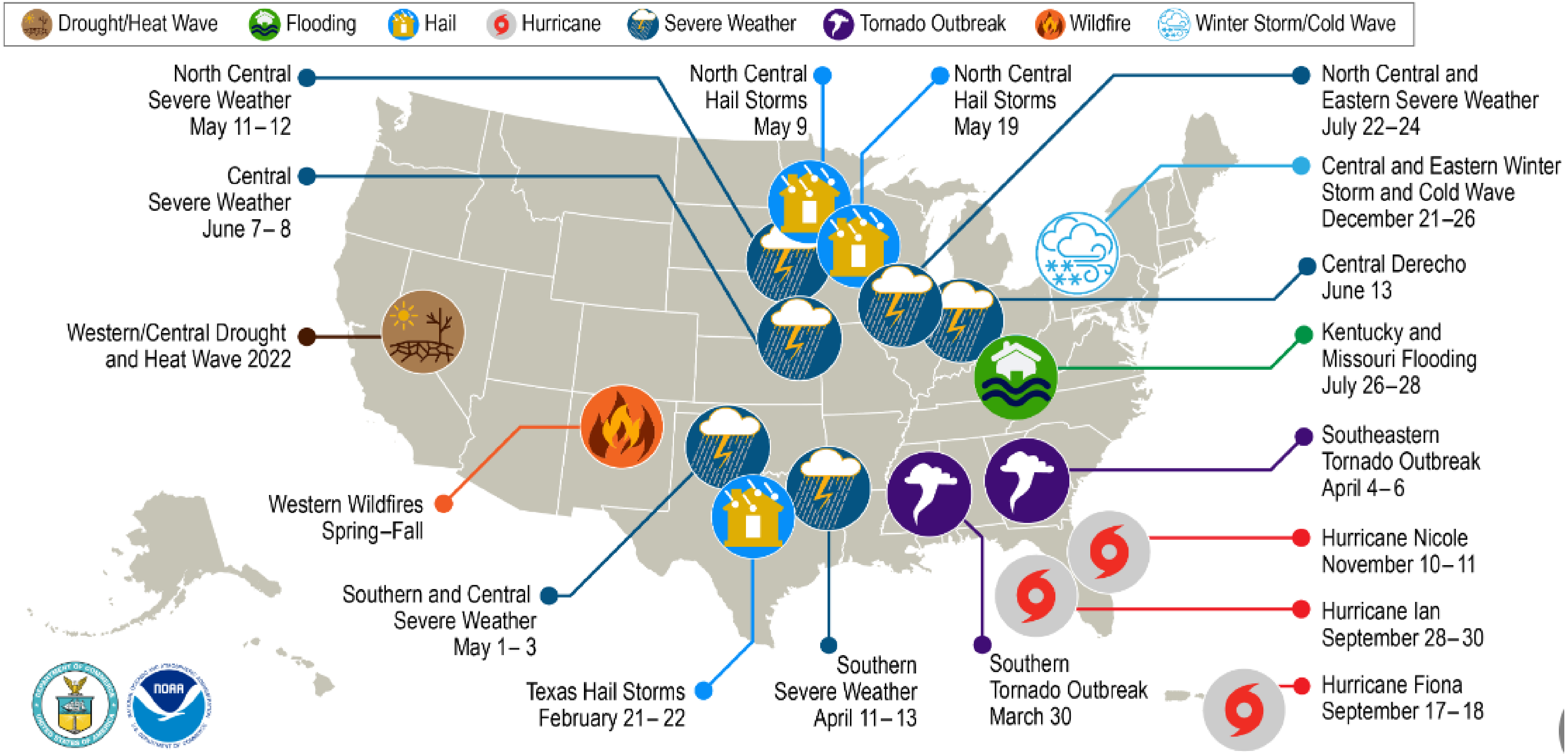
Waste and pollution
- Environmental considerations relative to sewer overflows; consent decrees stemming from pollution issues
- Impact of environmental regulations related to water or wastewater

Risk	Potential Credit Impact
Extreme weather (ex. Hurricanes, heat days)	Facility damage; unplanned operating costs; demand changes from population displacement
Energy transition	Power utilities typically wrestle with storage and reliability when increasing reliance on renewable power
GHG emissions	Buildings contribute about 13% to annual GHG emissions
Water scarcity	Population and economic development pressures

Read more: Through the ESG Lens 3.0: The Intersection of ESG Credit Factors and U.S. Public Finance Credit Factors, published March 2, 2022

U.S. Faces Increasing Number of Large-Scale Climate Disasters

U.S. 2022 Billion Dollar Weather And Climate Disasters – 18 Totaling $165 billion in losses



Source: National Oceanic and Atmospheric Administration (NOAA).

Social | Materiality: Short and Long-term

Health and safety

- Demand, revenue, or expense driven changes related to health and safety events that alter social behaviors
- Emerging contaminants in water supply as well as lead and copper pipes that could affect residents in the enterprise's service area

Social capital

- Demographic and population trends that affect a government's services or demand for a not-for-profit enterprise's product or infrastructure
- Income levels, income inequality, disparity in access to services by vulnerable groups
- Affordability of services provided by an enterprise
- Political unrest stemming from community or social issues

Human capital

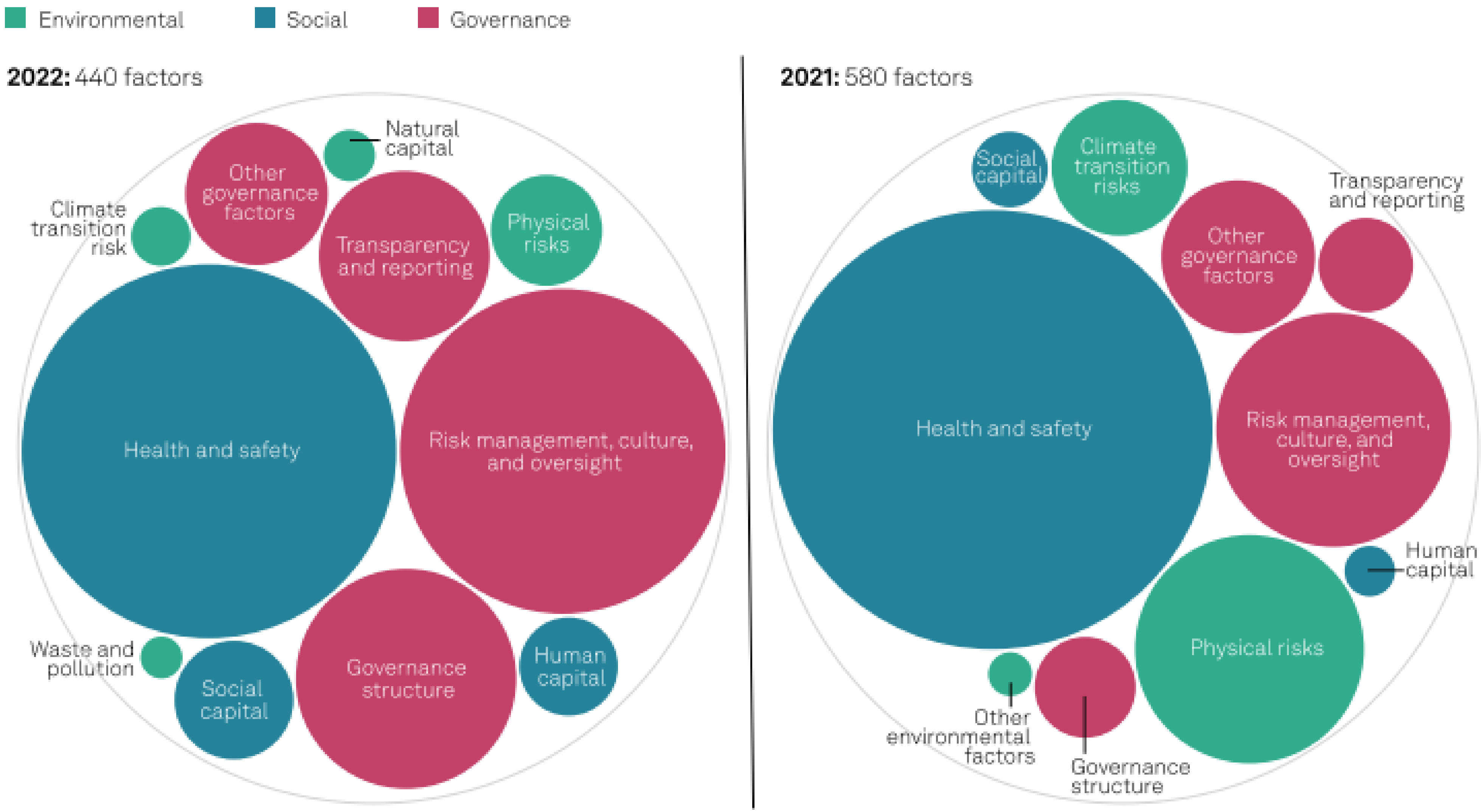
- Operational pressures related to renumeration, recruitment or retention of an entity's workforce
- Exposure to labor unrest or challenges and costs related to union negotiations and settlements
- Diversity and succession planning when it broadly affects a government or not-for-profit enterprise

Risk	Potential Credit Impact
Pandemic	Pause on elective surgeries; overwhelming demand during surges
Demographics of service area	Changes in demand for certain services; clinician recruitment and retention challenges; payer mix
Affordability	Reimbursement pressure to hospitals; increased bad debt expense
Labor	Retirements and burn out; agency labor; union settlements

Read more: Through the ESG Lens 3.0: The Intersection of ESG Credit Factors and U.S. Public Finance Credit Factors, published March 2, 2022

Social Credit Factors Led To Majority Of Rating Actions In 2021 and 2022

For healthcare entities, Human Capital credit risks were material in nine rating actions; Six were downgrades to non-investment grade



Read more: ESG in Credit Ratings Newsletter – January edition, published January 18, 2023

Governance | Materiality: Important Mitigant or Risk

Governance structure
- Elected or appointed board relationship with management
- Federal/state regulatory framework
- Key person succession planning
- State government support (or lack of support) for distressed entities, typically considered as part of the Institutional Framework score for municipalities and counties

Risk management, culture, and oversight
- Vulnerable financial management assessments when it stems from pervasive budgetary imbalances or missed debt service payments
- Cyber security protocols or lack of preparation when results in operational or financial impacts
- Pension/OPEB plan governance related to legal flexibility to modify benefits, adherence to a control framework that controls the liability funding schedule
- Headline risk: self-inflicted corruption and mis-dealings, adverse publicity that results in reputation risk or operational pressure

Transparency and reporting
- Adherence to reporting standards as identified in policies and practices
- Transparency of information provided to stakeholders related to key decision making
- Lack of statutory requirements for certain types of accounting standards that results in credit weakness or transparency concerns

Risk	Potential Credit Impact
M&A activity	Financial and debt impacts; service diversification and expansion; integration risks
Persistent budgetary imbalances	Management preparation and board support to pivot & respond to risks
Cybersecurity	Prepare, respond, recover from attacks or intrusions
Covenant violations	Advance discussions for waivers; financial forecasting and planning to anticipate cash flow weaknesses
Key position turnover	Succession planning; stabilization of operations and priorities

Read more: Through the ESG Lens 3.0: The Intersection of ESG Credit Factors and U.S. Public Finance Credit Factors, published March 2, 2022

How Management Teams Can Mitigate Risks

Environmental

Adaptative Building Materials

Emergency Planning

Electricity Redundancy; Procurement Modifications & Facility Optimization

Social

Regular review of services to match demographics

Innovative techniques toward staffing and recruitment; relationships with labor groups

General health and safety events and how these surges can affect regular operations

Governance

Reserves & Liquidity

Financial & Capital Planning

Prioritization & Execution

Longer-term strategies likely to involve data/technology for care delivery redesign & efficiencies, clinical developments, M&A and affiliations, and/or broader diversification.

Examples | Excerpts from published credit reports

Lonestar Health

Credit Overview

The rating reflects our view of Lonestar's exceptional financial strength and operating flexibility, coupled with our view of the system's leading inpatient market share in its growing and economically strong service area. Heading into 2022, the system weathered the COVID-19 pandemic well and finished fiscal 2021 with operating performance soundly positive due to both strong volume and patient revenue recovery aided by management's demand reclamation initiatives and higher acuity care, as well as the receipt of meaningful CARES Act provider relief funds. Specifically, the system generated an impressive operating margin of over 5% in 2021 (per S&P Global Ratings calculation) which remains healthy even when excluding recognized CARES Act provider relief funds. Moreover, the robust fiscal 2021 results include a very weak start to the year given the effects of Winter Storm Uri in February 2021, exemplifying the strength of Lonestar's earnings recovery as the year progressed.

Environmental, social, and governance

We view Lonestar's large service area, with healthy demographic trends such as high population and employment growth, as a positive social capital aspect that drives demand and underscores its operations. However, this is somewhat tempered by the core mission of health care facilities to protect the health and safety of communities, which led to challenges for this sector when serving surges in COVID-19 patients while also maintaining clinical capacity for other emergent cases. Furthermore, we believe this heightened health and safety risk for Lonestar and its peers will likely continue to present financial pressure and uncertainty in the near term, particularly relative to margin pressure from certain indirect challenges and human capital social risks related to staffing shortages and higher labor costs.

Lonestar releases an annual social purpose report that shares certain organizational priorities and accomplishments, and tracks specified metrics against environmental, social, and governance goals over time, including charity care and community benefit costs, consumer survey scores and quality measures, and environmental measures such as energy consumption, water consumption, and waste generated. We believe this transparency and reporting initiative is indicative of the system's top-level management focus on these issues that provides visibility on standardized data points that can be tracked over time for key stakeholders.

Texas County Hospital District

Credit Overview

The rating reflects the district's tax-supported operations and debt service, as well as its strong trend of performance improvement throughout the COVID-19 pandemic, which has been sustained through fiscal 2022 (based on unaudited results), moderating as expected from one of the strongest years in the district's history in 2021. Recent results were ahead of budget and reflect the district's maturing productivity and efficiency initiatives, as well as strong volume growth from years of investment in physicians, service lines, and capacity. In addition, all major operating units of the district, including its health plan, remain profitable per S&P Global Ratings, which is a marked contrast from performance ahead of the pandemic. In part due to its revenue diversity, we anticipate sustained stable operations, which should generate adequate cash flow to support routine capital spending and debt service coverage.

As a public safety net hospital with significant tax support and flexibility, we do not require the district to generate operating margins and maintain balance-sheet measures on par with those of private hospitals of the same rating. We do, however, expect the district to operate at a sustainable operating baseline and have a sound liquidity cushion to mitigate the cyclicality of its cash position. We believe it has made considerable progress toward this goal, creating some positive rating pressure.

Environmental, social, and governance

We consider the district's social risk to be an elevated risk within our credit rating analysis, given its relatively elevated Medicaid exposure and supplemental funding, though its payer mix is more typical when compared with those of other safety net and pediatric providers. In addition, we consider the district exposed to additional human capital risks tied to higher labor and salary pressures within the sector, though we believe management has responded to this quite well and note many contract labor measures have improved to historical levels. We view health and safety risks tied to the COVID-19 pandemic as easing but continue to monitor COVID-19 and its variants heading into the winter flu season.

HealthTex

Credit Overview

The rating is based on our view of HealthTex's expansive and growing market position, characterized by a diverse portfolio of access points and strong revenue and earnings diversity, which has contributed to the system's healthy operating performance and robust cash flow amidst the COVID-19 pandemic and ensuing inflationary pressures. Despite the added debt and recent investment market volatility that has pressured unrestricted reserves, the system's pro forma balance sheet is in line with the current rating, particularly when considering the system's comparatively larger size and scale compared with rating peers. We expect increased investment in access points in key growth markets, but also more emphasis on capital-effective expansions through joint ventures and partnerships. In addition, we anticipate investments in access and growth will continue to include digital, home, and other consumer-centric investments.

We believe several factors drive the system's strong financial performance including healthy volumes and increased patient acuity above pre-pandemic levels, strong results at its health plan and meaningful integration with its care network, execution of management's performance improvement strategies, and solid demographics in its generally high-growth service areas. Profitability has remained robust despite tapering of CARES Act provider relief funds, and we expect sustained positive results albeit likely softer than recent periods. We anticipate the industry's labor challenges will continue to affect HealthTex over the outlook period and generally compress performance, but we believe the system is well-positioned to continue weathering this pressure and note significant progress has been made in key labor measures over calendar 2022.

Environmental, social, and governance

We view HealthTex as having lower social capital risk within our credit rating analysis as the system operates in several markets with healthy demographic trends such as population and employment growth; the system's markets typically outpace the state in terms of commercial insurance and population growth levels. That said, these strengths are somewhat tempered by additional human capital risks tied to higher labor and salary pressures within the sector, though we believe management has responded to this quite well. We view health and safety risks tied to the COVID-19 pandemic as easing but continue to monitor COVID-19 and its variants heading into the winter flu season.

GulfWell

Credit Overview

The rating reflects our view of GulfWell's very strong enterprise profile, with a portfolio of well-placed inpatient facilities and access points across a growing metropolitan statistical area (MSA). GulfWell's highly regarded flagship is an academic medical center and is positioned as one of the state's premier health care institutions, with a national reputation for clinical excellence in multiple tertiary and quaternary service lines. Financially, the system continues to weather challenges related to COVID-19 and the current inflationary environment exceptionally well, with sustained above budget performance through interim 2022 aided by its strong commercial payor mix. GulfWell has also showcased its clinical and research strength throughout the pandemic, contributing to COVID-19-related testing, treatment, and vaccination efforts.

We anticipate GulfWell will retain healthy and positive operations over the outlook period, as its high demand and consumer preference in the region continue to support exceptional volumes, most of which are already well above pre-pandemic levels, and drive the need for further capital expansion.

Environmental, social, and governance

GulfWell's location near the Gulf Coast makes it susceptible to significant weather events, elevating our view of the system's environmental risk with our credit rating analysis. The system began targeted investments to key facilities in 2001 to mitigate the risk of damage and business interruption from major storm events, including regular facility inspections and investments in flood gates, retaining walls, and high-impact glass, and has managed recent storms, such as Hurricane Harvey in 2017, quite well.

We view GulfWell's social risk as a lower risk factor within our credit rating analysis as the system operates in a large market with healthy growth trends, consistently capturing a strong commercially-insured patient base given the system's clinical offerings and methodical portfolio buildout. We view the system's exposure to the health and safety risks from the COVID-19 pandemic to be more neutral within our analysis, though the entire sector is exposed to additional human capital risks including through indirect pressures such as elevated labor and inflationary costs.

GulfWell's governance risks are also a lower risk factor supported by the organization's long track record of exceptional financial strength, which it has maintained through conservative financial practices and disciplined execution of numerous forward-looking strategic initiatives.

Questions?

spglobal.com/ratings