

FITCH REVISES TULARE LOCAL HEALTH CARE DISTRICT'S (CA) WATCH TO NEGATIVE FROM POSITIVE

Fitch Ratings-San Francisco-22 February 2017: Fitch Ratings has revised the Rating Watch to Negative from Positive on the 'BB-' rating on \$13,650,000 series 2007 fixed-rate bonds issued by the Tulare Local Health Care District d/b/a Tulare Regional Medical Center (TRMC) and on TRMC's Issuer Default Rating (IDR) of 'BB-'.

SECURITY

Debt payments are secured by a pledge of the gross revenues of Tulare Local Health Care District. A fully funded debt service reserve fund provides additional security for bondholders.

KEY RATING DRIVERS

FUNDING FOR TOWER COMPLETION: The Negative Watch is due to the failure of a ballot measure in August 2016 that would have authorized a \$55 million general obligation (GO) bond issuance to finish its new building project. TRMC is currently in the process of evaluating financing options and the Negative Watch reflects the sizeable amount of debt that will need to be supported from hospital operations.

FINANCIAL TURNAROUND: The current management team has been in place since January 2014 and led a financial turnaround with strong operating results in fiscal 2015 and 2016 (June 30 year-end) with 16.6% and 14.1% operating EBITDA margins, respectively. TRMC's financial profile has weakened through the six months ended Dec. 31, 2016 as a result of an information technology conversion and continued decline in volume. TRMC had 41.2 days cash on hand at Dec. 31, 2016 and 6.3% operating EBITDA margin through the interim period.

NEW BUILDING PROJECT: TRMC has been hindered by an unfinished construction project that was supposed to be complete in 2012, due to numerous construction issues and litigation with the contractor. After settling with the contractor, TRMC has spent its own funds to prepare the building for completion. The completion of the tower project will be key to stemming outmigration and enhancing services.

RATING SENSITIVITIES

UPCOMING FINANCING EXPECTED: Management expects to finalize its financing plan by summer 2017 and will issue bonds through the FHA 242 program or Cal Mortgage. The Negative Watch reflects Fitch's concern about the magnitude of the debt on Tulare Regional Medical Center's financial profile and will assess the impact on the rating at the time of the financing.

CREDIT PROFILE

Tulare Local Health Care District, d/b/a Tulare Regional Medical Center owns and operates a 112-bed hospital in the city of Tulare, CA. Total operating revenue in FYE June 30, 2016 (unaudited interim results) was \$81 million (excluding tax revenues related to GO bonds debt service). Since January 2014, TRMC has been managed by HealthCare Conglomerate Associates. The current management agreement runs until 2029 with possible extensions.

VARIATION FROM PUBLISHED CRITERIA

The analysis supporting the 'BB-' IDR includes a variation from the U.S. Nonprofit Hospitals and Health Systems Rating Criteria. Enhanced analysis under the variation relates to the assessment

of the benefits and risks of supplemental tax revenues available to the healthcare provider. This evaluation is supported by Fitch's new U.S. Tax-Supported Rating Criteria dated April 21, 2016, that includes refinements to the analysis of both tax revenue volatility, through the new Fitch Analytical Sensitivity Tool (FAST), and the value of taxing capacity relative to the issuer's potential revenue stress in a downturn.

DISCLOSURE

TRMC covenants to disclose annual financial statements within four months of fiscal year-end and quarterly unaudited financial statements within 60 days of quarter-end through the MSRB EMMA website. TRMC's fiscal year ended June 30, 2016 audit is still not available due to a change in auditors. Management expects the audit to be available shortly.

Contact:

Primary Analyst

Emily Wong

Senior Director

+1-415-732-5620

Fitch Ratings, Inc.

650 California Street

San Francisco, CA 94108

Secondary Analyst

Ryan Pami

Associate Director

+1-212-908-0803

Committee Chairperson

Jim LeBuhn

Senior Director

+1-312-368-2059

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at www.fitchratings.com

Applicable Criteria

Revenue-Supported Rating Criteria (pub. 16 Jun 2014)

<https://www.fitchratings.com/site/re/750012>

U.S. Nonprofit Hospitals and Health Systems Rating Criteria (pub. 09 Jun 2015)

<https://www.fitchratings.com/site/re/866807>

U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)

<https://www.fitchratings.com/site/re/879478>

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