

Ascension Health

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following information should be read with Ascension Health's audited consolidated financial statements and related notes to the consolidated financial statements.

Volume Trends and Net Patient Service Revenue

For the year ended June 30, 2011, Ascension Health experienced a 1.9% increase in equivalent discharges as compared with the year ended June 30, 2010. Outpatient revenue as a percentage of total gross patient service revenue increased from 45.4% for the year ended June 30, 2010 to 46.6% for the year ended June 30, 2011. Observation days increased 13.8% as compared to the prior fiscal year.

	Year Ended June 30,	
	2011	2010
Acute Care Admissions	633,372	636,687
Total Admissions	685,035	686,734
Case Mix Index	1.49	1.48
Equivalent Discharges	1,284,333	1,259,803
Acute Average Length of Stay (days)	4.51	4.48
Observation Days	200,373	176,109
Emergency Room Visits	2,367,953	2,339,373
Surgical Visits (IP & OP)	530,843	537,235

Net patient service revenue grew 5.4% for the year ended June 30, 2011 as compared with the year ended June 30, 2010. Net patient service revenue per equivalent discharge increased 3.4%.

Ascension Health

Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Income from Operations

For the year ended June 30, 2011, income from operations was \$424 million compared to \$569 million for the year ended June 30, 2010. This change is attributable to the following:

- An increase in total operating revenue of \$808 million or 5.5% as a result of a 1.9% increase in equivalent discharges over prior year, primarily due to growth for new and existing facilities and physician office visits, and a 3.4% increase in net patient service revenue per equivalent discharge. This increase is primarily due to increases in commercial rates, offset by:
 - A 1.1% shift in payor mix from commercial to governmental payors, coupled with a 9.0% increase in charity care (measured at cost).
 - A reduction in Medicare rates effective October 1, 2010 and reductions to Medicaid rates in certain states.
- An increase in total operating expenses of \$907 million or 6.4%.
 - \$502 million of the increase is due to growth in salaries and benefits reflecting moderate merit increases, an 18% increase in employed physicians and their staffs, and transitioning support for Information Systems to internal resources from a third party provider. Additionally, employee benefits per FTE increased 5.6% primarily in the areas of health claims and pension.
 - Professional fees account for approximately 16% of the increase primarily due to physician fees.
 - Other expense accounts for approximately 19% of the increase primarily due to increased provider tax expense as well as increased repairs and maintenance, minor equipment, rent, and utilities.
- Impairment, restructuring, and nonrecurring expenses increased \$61 million from the prior year primarily due to the following:
 - An increase of \$36 million of expenses related to the System-wide enterprise resource planning initiative.
 - An increase of \$10 million in impairment charges related to long-lived assets that were retired due to the construction of replacement facilities.
- The unpaid cost of providing care to persons living in poverty and community benefit programs was \$1.2 billion, a \$152 million or 14.1% increase over the year ended June 30, 2010. This increase is primarily attributable to increases in previously mentioned charity care costs as a result of economic conditions in certain markets as well as increased unreimbursed costs of emergency and trauma programs, medical education and community clinics.

Ascension Health

Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Investment Return

For the year ended June 30, 2011, the Health System Depository recorded a 16.8% annual return. As discussed in the notes to the financial statements, investment return recognized by Ascension Health is summarized as follows:

	Year Ended June 30,	
	2011	2010
	<i>(in thousands)</i>	
Investment return in the Health System Depository	\$ 1,152,338	\$ 756,437
Interest and dividends	17,051	15,872
Net gains on investments reported at fair value	80,814	38,760
Restricted investment income	6,163	1,594
 Total investment return	 \$ 1,256,366	 \$ 812,663

Investment return is recognized in the consolidated statements of operations and changes in net assets as follows:

	Year Ended June 30,	
	2011	2010
	<i>(in thousands)</i>	
<u>Included in operating income</u>		
Realized investment return	\$ 58,520	\$ 27,933
Net change in unrealized gains/losses on investments	31,882	46,043
	90,402	73,976
<u>Included in nonoperating income</u>		
Realized investment return	607,743	371,468
Net change in unrealized gains/losses on investments	532,582	351,402
	1,140,325	722,870
<u>Included in the change in restricted net assets</u>		
Realized investment return	8,233	2,350
Net change in unrealized gains/losses on investments	17,406	13,467
	25,639	15,817
 Total investment return	 \$ 1,256,366	 \$ 812,663

Ascension Health

Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Excess of Revenues and Gains over Expenses and Losses

The excess of revenues and gains over expenses and losses for the year ended June 30, 2011 was \$1.5 billion. This represents an increase of \$284 million compared to the year ended June 30, 2010. This increase is primarily due to the \$417 million increase in nonoperating investment return.

Balance Sheet Ratios

Ascension Health has 215 days of cash and investments on hand at June 30, 2011, which represents an increase of 25 days from June 30, 2010. The increase was driven by cash generated from operations as well as favorable investment returns partially offset by capital expenditures of \$730 million for the year ended June 30, 2011.

Cash-to-senior debt and cash-to-debt was 234.8% and 201.6%, respectively, at June 30, 2011 as indicated in the following table, representing increases compared to those at June 30, 2010. Ascension Health continues to focus significant efforts on maintaining a strong balance sheet.

Balance Sheet Ratios		
	June 30,	
	2011	2010
Days Cash on Hand	215	190
Net Days in Accounts Receivable	44	44
Cash-to-Senior Debt	234.8%	192.5%
Cash-to-Debt (Senior and Subordinated)	201.6%	165.2%
Senior Debt to Capitalization	24.2%	28.8%
Debt to Capitalization	27.1%	32.0%