



VITAL2015

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Leading a Hospital Turnaround in a Non-Expansion State

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Mini-Session 1



**AMERICA'S
ESSENTIAL
HOSPITALS**



Key Takeaways

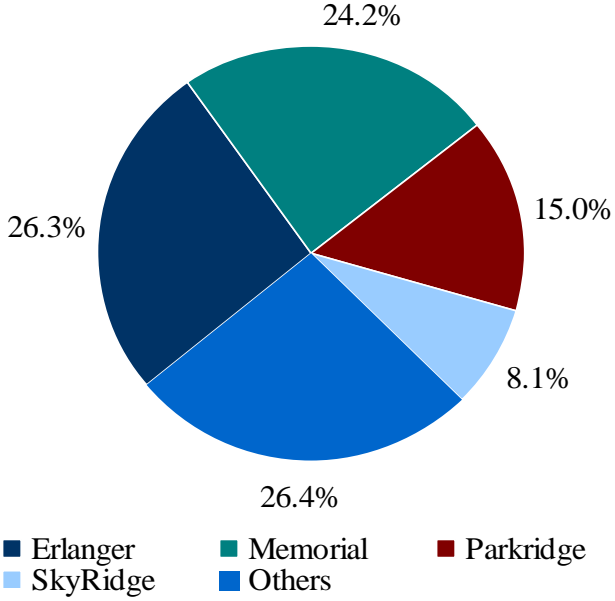
- **Essential Service Provider** – Erlanger Health System is the only Academic Medical Center and leading provider of high-acuity, essential services to the region
- **Leading Market Position** – Market share for the primary and secondary service areas has continued to strengthen from 30.9% to 32.1% despite a flat market
- **Strategic Partnerships** – Important strategic relationships have been solidified (Blue Cross, UTCOM) while others have been discontinued (Hutcheson)
- **Operating Improvements** – Significant new revenues and expense reductions produced a \$26 million operating turn-around and \$18 million in income from operations
- **Key Investments** – Key strategic investments are planned to accelerate positive momentum and strengthen market position
- **Recapitalization** – Comprehensive recapitalization plan will fund key strategic investments while improving Erlanger's credit metrics



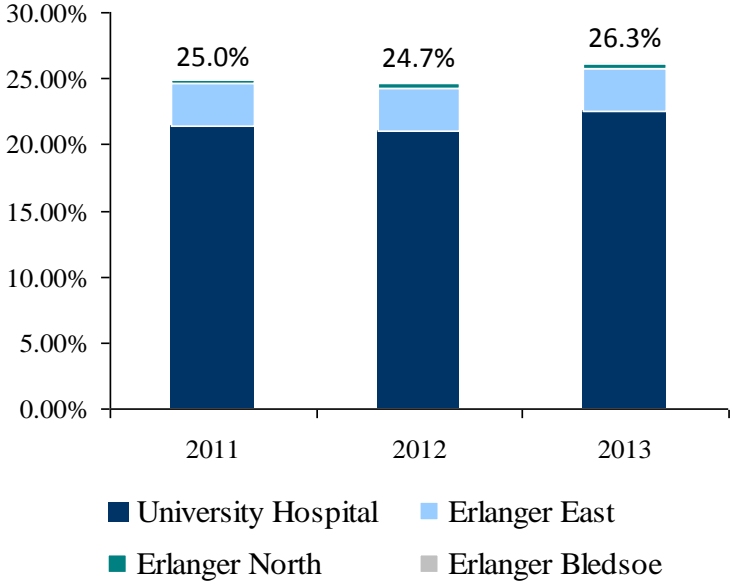
Essential Service Provider in the Region

Erlanger has increased market share in its primary and secondary service areas from 30.9% to 32.1% and continues to lead the market in most tertiary services

2013 Market Share (Primary Service Area)

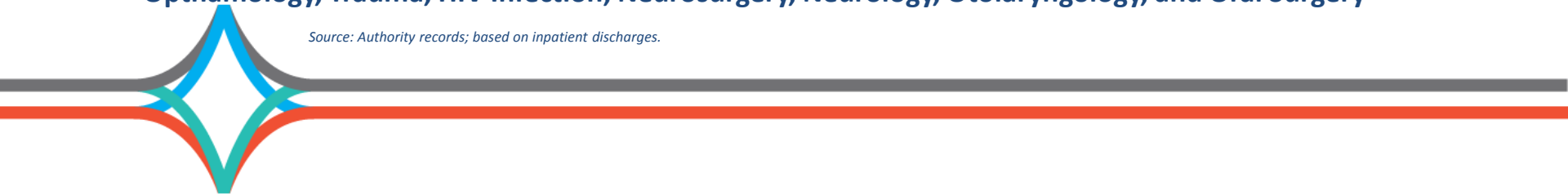


Historical Market Share (Primary Service Area)



- **Leading market share in the following high acuity services: Neonatology, High Risk Obstetrics, Ophthalmology, Trauma, HIV Infection, Neurosurgery, Neurology, Otolaryngology, and Oral Surgery**

Source: Authority records; based on inpatient discharges.



Partnership with UT-COM

Erlanger has entered into a new 10-year partnership with UTCOM strengthening its role as the region's only Academic Medical Center



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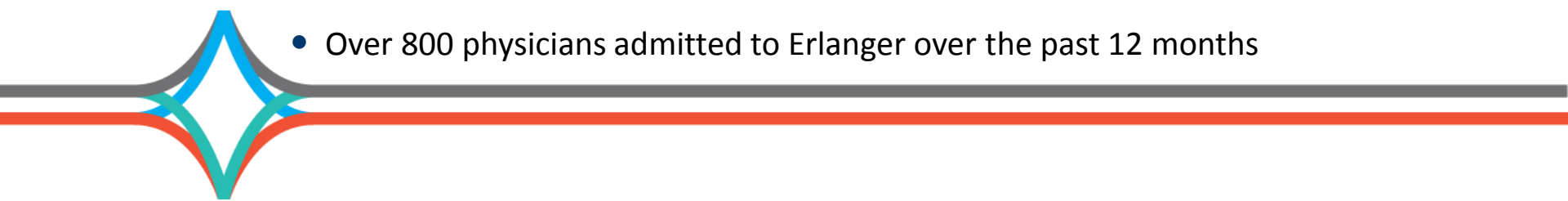


- Partnership provides Erlanger:

- Vital network of community-based programs
- Access to and recruitment of high-caliber physicians
- Clinical practice support, call coverage, and physician extender services
- Better clinical outcomes
- Exclusive relationship with a 10-year term and auto renewals for successive 10-year terms

- Erlanger CEO and Campus Dean are responsible for coordination of teaching program
- Partnership requires Erlanger and UTCOM to move forward in developing a Physician Organization
- Over 800 physicians admitted to Erlanger over the past 12 months

Total Employed Physicians		
	EHS	UTCUM
Pediatrics	42	3
Adult Primary Care	35	18
Medical Sub-Specialists	33	4
Hospitalists	20	2
Surgical Specialists	18	51
OBGYN	7	18
Total	155	96



Partnership with Blue Cross Blue Shield of Tennessee

Erlanger has entered into a 5-year partnership with BCBST to be the exclusive provider for new members under the health insurance exchange



- 5-year Partnership between Tennessee's largest insurer and Chattanooga's largest provider
- Key provisions include:
 - Effective July 1, 2013 – June 30, 2018
 - Exclusive provider in new Network E and continued participation in all other products
 - Pay-for-performance to promote quality improvements
 - \$1 million grant to develop exclusive new products (ACO, state-wide preferred network)
 - Combined marketing effort aimed at major Chattanooga employers

Improvements – Delivered Results

Erlanger has implemented the following operational improvements resulting in an annualized benefit of \$47 million

1. Public Hospital Supplemental Payment Pool	\$19.5 mm
2. Changes to Pension and Employee Benefits	\$8.3 mm
3. 340(b) Pharmacy Program	\$6.0 mm
4. Other Operating Improvements	\$13.2 mm
Total Operating Improvements	\$47.0 mm



Operational Improvement Detail

Erlanger has made significant operational improvements, adding additional revenue sources, while curtailing and adjusting certain operating expenses and benefits

1. After significant lobbying, Erlanger was added to the Public Hospital Supplemental Payment Pool in FY2014, generating \$19.5 million of new revenue for the System
 - Pool originated for Federal Matching Funds for Tennessee Public Hospitals
 - Support from local, state and federal elected officials
 - Three-year minimum with renewal tied to the ongoing approval of the TennCare waiver
2. Erlanger has taken significant steps toward market-based benefits, reducing annual expense by \$8.3 million
 - Froze defined benefit pension plan effective July 1, 2014 (\$4 million of annual savings)
 - Adjusted Health Insurance employer contribution (\$1.4 million of annual savings)
 - Redesigned employee Pharmacy Plan Benefit (\$1.4 million of annual savings)
 - Eliminated post retirement benefits effective January 1, 2015 (\$1.5 million in annual savings)



Operational Improvement Detail

3. Erlanger has secured access to lower-cost drugs through the federal 340(b) program for Disproportionate Share hospitals, saving \$6 million annually
 - Erlanger is the only hospital in the area that is qualified to utilize the program
 - Acquired large infusion center that doubles the size of Erlanger's existing infusion center
 - Contracted with Walgreens and CVS to deploy eligible 340(b) prescriptions
 - \$6 million of annual savings (full impact to be felt in FY 2015)

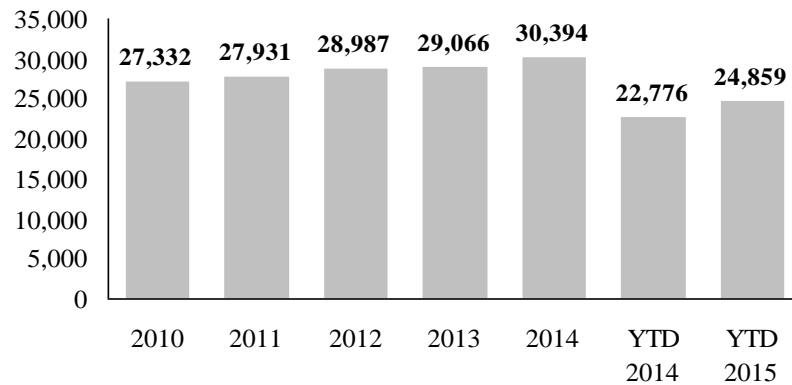
4. Management's focus on transforming operations and outside-the-box thinking has generated an additional \$13.2 million on annual savings
 - Average Length of Stay reductions: \$3.1 million
 - Professional services contracts renegotiated: \$3.0 million
 - Supply savings in partnership with GPO: \$2.0 million
 - In-quality staffing and reduction of premium wages: \$1.1 million
 - Outsourcing of EVS and Food Services: \$2.0 million plus \$10 million of capital infusion
 - Revenue cycle fine-tuning: \$1.0 million
 - Reducing ancillary leakage from employed physicians: \$1.0 million



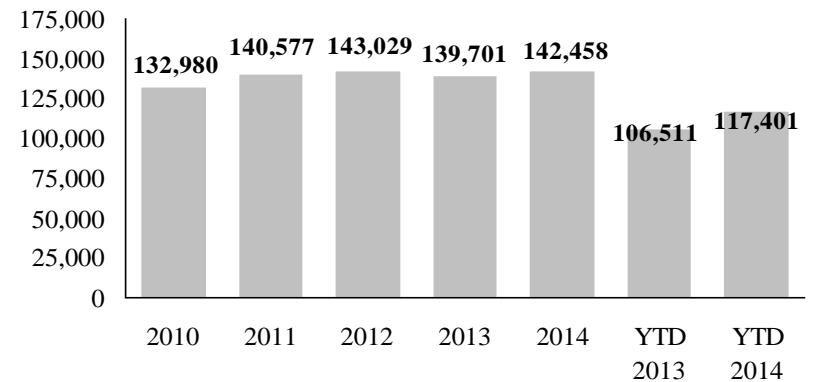
Utilization Statistics

Volumes improved significantly in FY 2014 and FY 2015

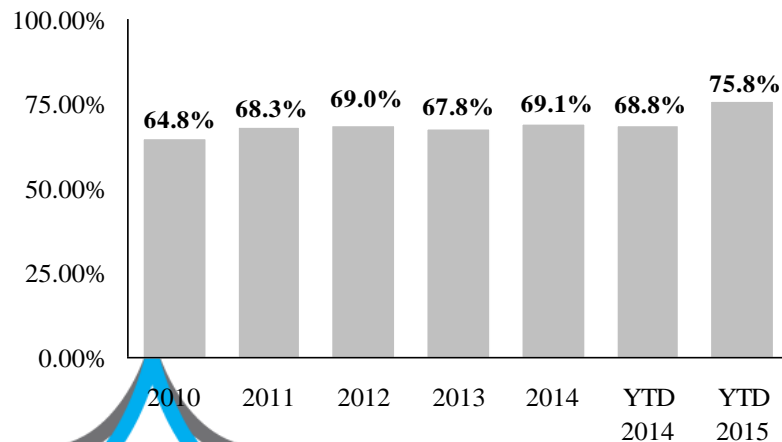
Total System Admissions



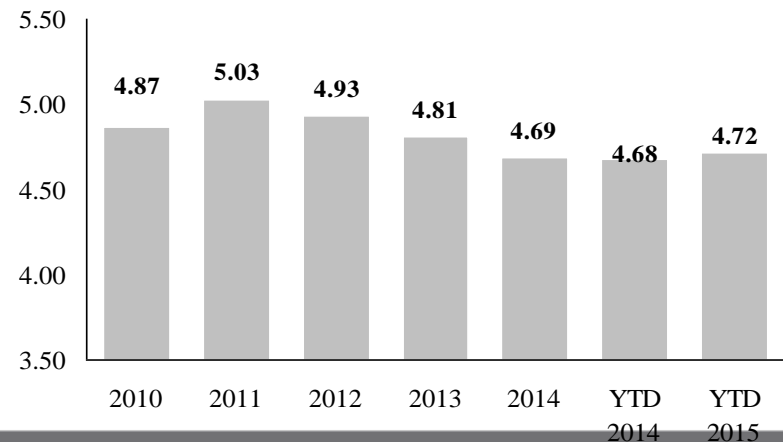
Patient Days



Occupancy Rate



Average Length of Stay

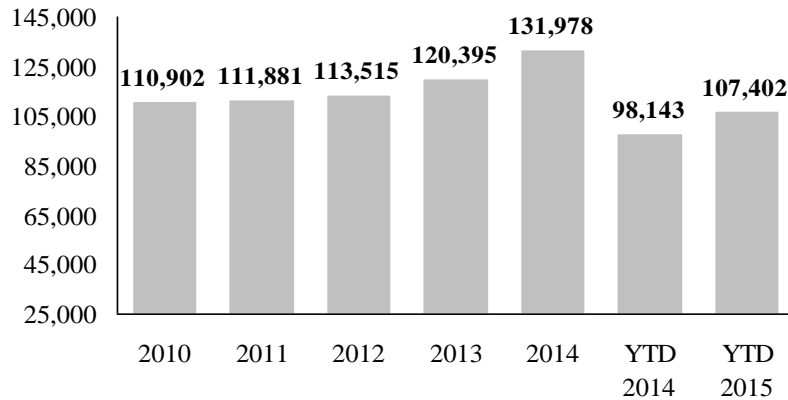


Note: Represents 3-Months ended September 30.

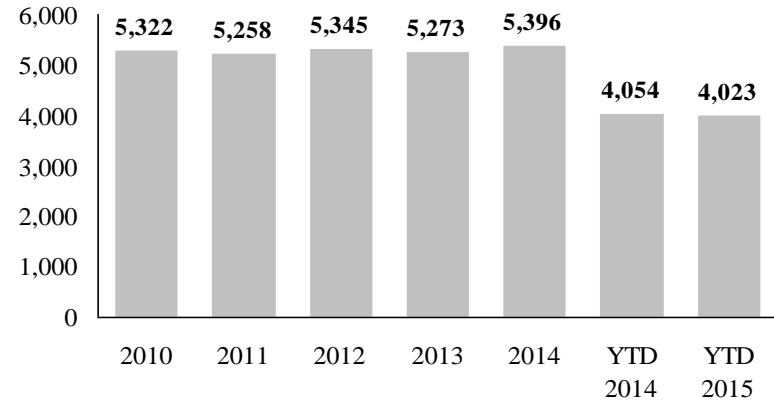
Utilization Statistics

Other volumes including surgeries have also continued to improve

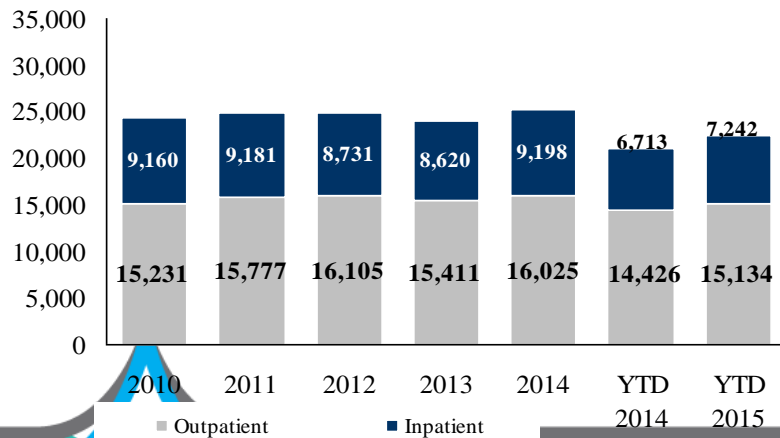
Emergency Room Visits



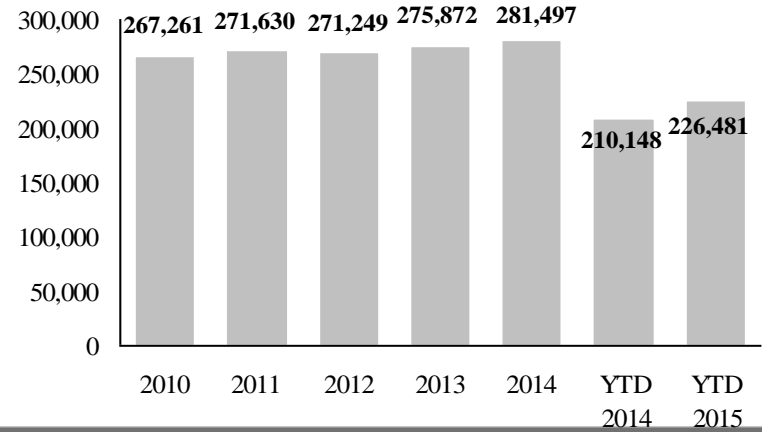
Births



Total Surgical Patients



Outpatient Visits



Note: Represents 3-Months ended September 30.

Financial Performance

Significant new revenues and expense reductions produced a \$27 million operating turn-around and an \$11 million bottom line

(\$ in thousands)

	Fiscal Year Ending June 30					Three Months Ended Sep. 30,	
	2010	2011	2012	2013	2014	2013	2014
Total Operating Revenue	\$519,715	\$553,459	\$563,027	\$570,985	\$618,532	\$147,661	\$164,403
Total Operating Expenses	511,133	548,104	572,578	578,956	600,519	148,358	156,680
Operating Income	8,582	5,355	(9,551)	(7,971)	18,013	(697)	7,723
Other Nonoperating Revenues (Expenses)	(4,275)	(6,254)	(7,184)	(6,344)	(6,679)	(1,541)	(1,312)
Excess of Revenue Over Expenses	4,307	(899)	(16,735)	(14,316)	11,334	(2,237)	6,411

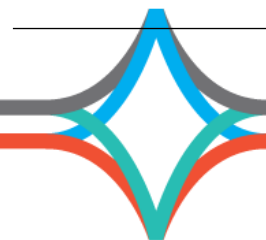
- Dramatic financial improvements in FY14 vs. FY13:
 - \$47 million increase in Total Operating Revenue
 - \$27 million increase in Operating Income (including interest expense)
 - \$26 million increase in Excess of Revenues over Expenses



Historical Financial Ratios

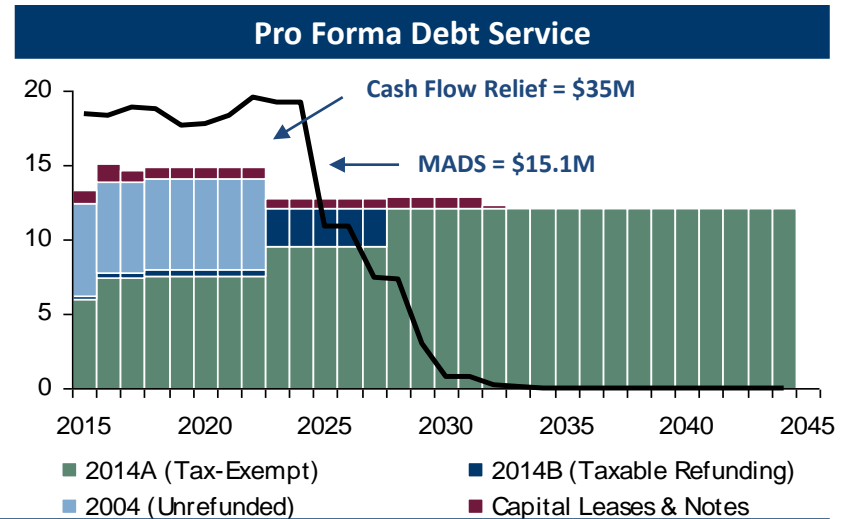
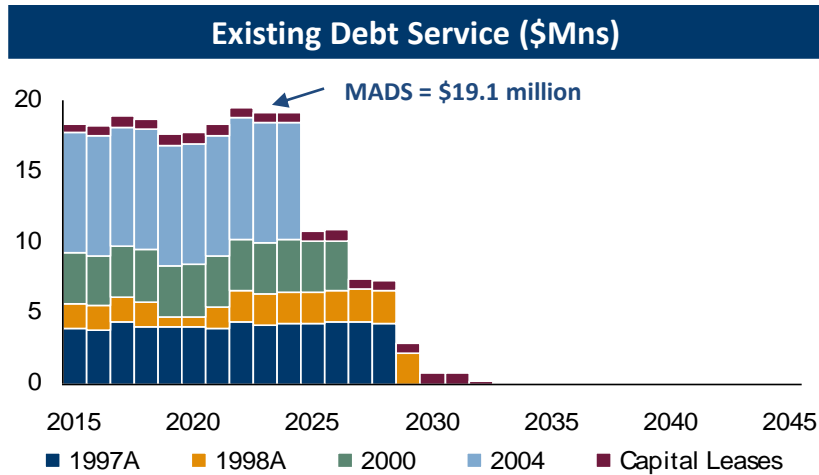
Profitability and liquidity measures have rebounded significantly year-over-year and leverage metrics have also improved

	Fiscal Year Ending June 30,				
	2010	2011	2012	2013	2014
Profitability:					
Operating Margin(%)	1.7%	1.0%	-1.7%	-1.4%	2.9%
Excess Margin (%)	1.1%	-0.5%	-2.8%	-2.9%	1.7%
Operating Cash Flow Margin (%)	8.5%	7.4%	5.0%	5.3%	8.0%
Liquidity:					
Days Cash on Hand (days)	121.3	106.1	80.9	70.4	87.4
Cash to Debt (%)	101%	97%	78%	69%	82%
Cushion Ratio (x)	10.9x	10.2x	7.9x	6.7x	7.3x
Leverage:					
MADS Coverage (x)	2.4x	1.9x	1.2x	1.1x	2.4x
Debt to Cashflow (x)	5.9x	8.0x	16.2x	15.4x	4.6x
Debt to Capitalization (%)	47.9%	47.2%	48.9%	51.4%	47.8%



\$71 Million New & Refunding

Blending \$71 million new money with a refunding, Erlanger extended its debt, lowered MADS by approximately \$4.0 million and created \$35 million of cashflow savings over 10 years



Pro Forma Capital Structure

(\$000)	Sept. 30, 2014	Pro Forma	Change
Long Term Debt	\$169,900	\$208,997	\$39,097
Debt to Capitalization	46.27%	52.21%	5.94%
Maximum Annual Debt Service (MADS)	\$19,098	\$15,102	(\$3,996)
MADS Coverage (x)	2.40x	3.03x	0.63x

Note: Assumes market conditions as of October 1, 2014 and Series 2014 closing on December 11, 2014. Assumes the 10 year average of LIBOR (2.00%) for taxable variable rate debt. MADS based on 6/30/14 financials, inclusive of capital leases.

Major Service Expansions and Capital Investment in the Past Year

- Patient physiological monitoring equipment - \$7 million
- PET Scanner - \$2M
- 3.0 TESLA MRI - \$3M
- Breast Cancer Resource center with 3D Tomosynthesis imaging \$1M
- Adult hybrid operating room - \$2.4 million
- Day surgery area with improved street access - \$2.9 million
- Pre/post operative areas in Children's Hospital - \$1.8 million
- Integrated operating suites in Children's Hospital - \$1.4 million
- Cardiac Cath Lab upgrade - \$1.4 million
- Epilepsy Monitoring Unit - \$1.2 million



Capital Investments

Series 2014A bond proceeds will fund the following key strategic projects

Project	Description	Bond Proceeds
Expansion of Erlanger East to Full Service Hospital	<ul style="list-style-type: none"> ▪ Increase acute care beds from 43 to 107 ▪ New diagnostic cardiac catheterization lab, infusion center, other administrative, support and ancillary services 	▪ \$50 million
Children's / Women's Ambulatory Center	<ul style="list-style-type: none"> ▪ State-of-the-art Children's and Women's Center ▪ Partially philanthropy funded (total cost \$30 million) 	▪ \$11.5 million
University Hospital Master Facilities Plan Phase 1	<ul style="list-style-type: none"> ▪ Construction of new vascular operating rooms ▪ Construction of dedicated orthopedic center with inpatient beds 	▪ \$9.5 million
Total of New Funding		\$71 million
Routine Capital		<u>\$25 million</u>
Total Capital Investment		<u>\$96 million</u>

Note: In addition, \$100 million investment in a new EMR over the next three years.

Current Fiscal Year – Impressive Results

Third Quarter

- \$11.4 million total net income
- \$15.7 million improvement over previous fiscal year Third Quarter

Year-to-date

- \$25.3 million total net income
- \$34 million improvement over previous fiscal year



Continued Strong Growth FYTD

Admissions ↑ 9%

I/P Surgical Volumes ↑ 8%

Emergency Room Visits ↑ 10%

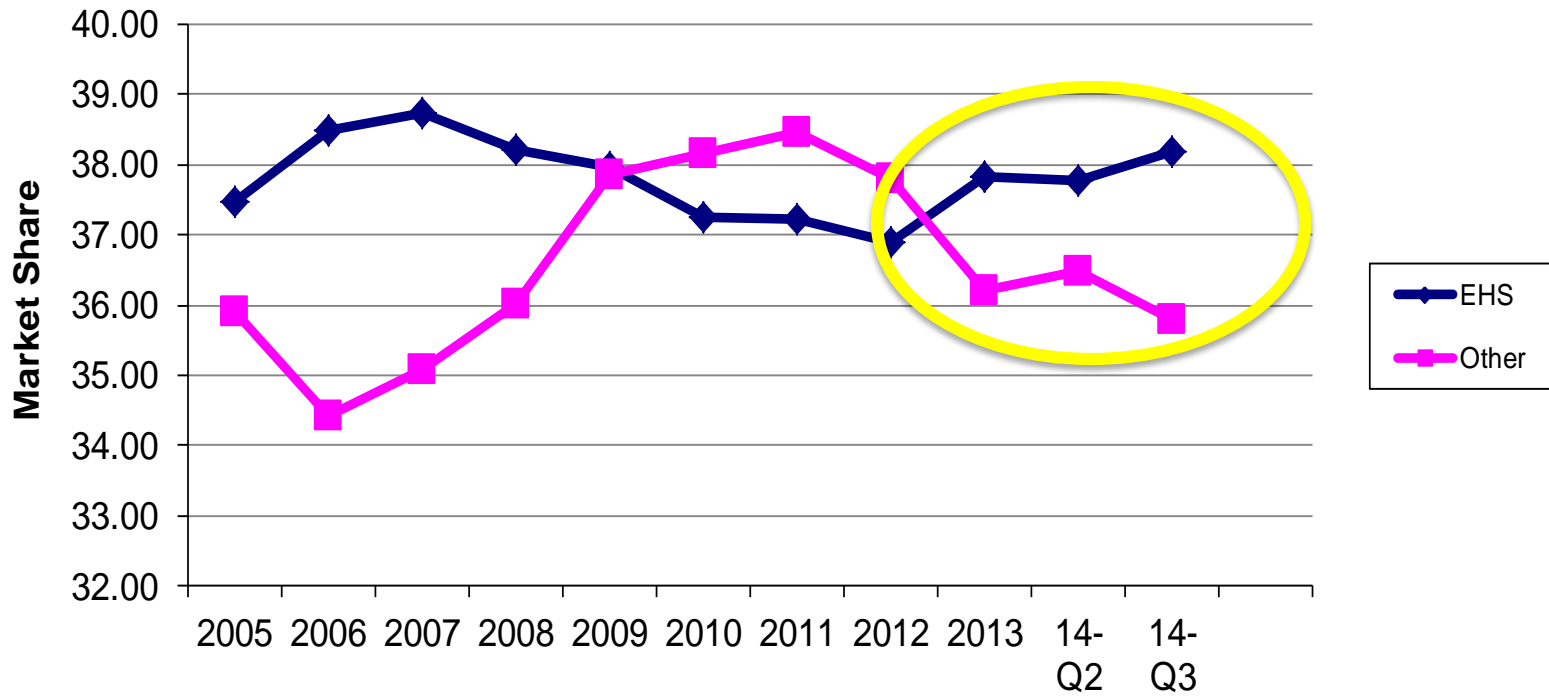
Neonatal ICU ↑ 31%

Commercial Discharges ↑ 9%

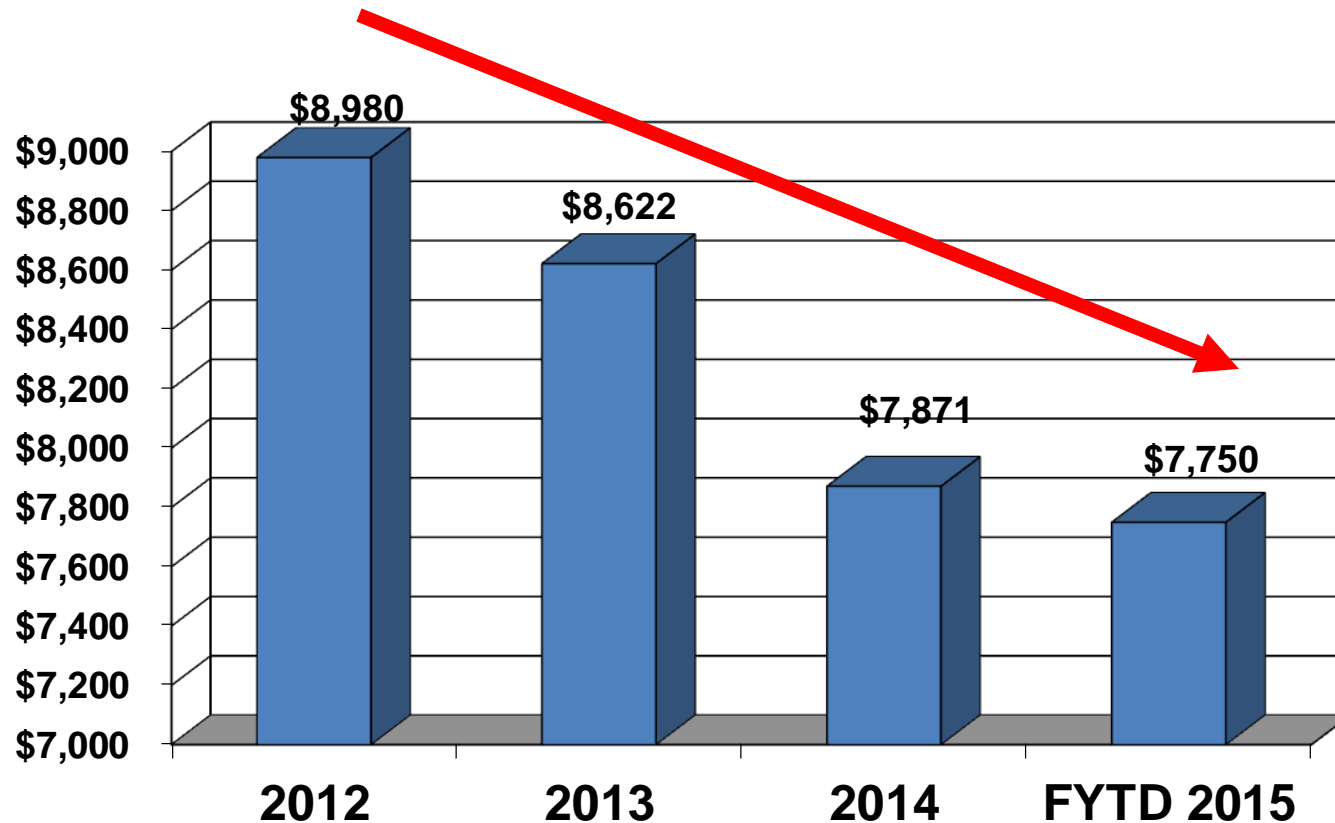
Physician Practice Visits ↑ 25%



Market Share Comparison Hamilton County



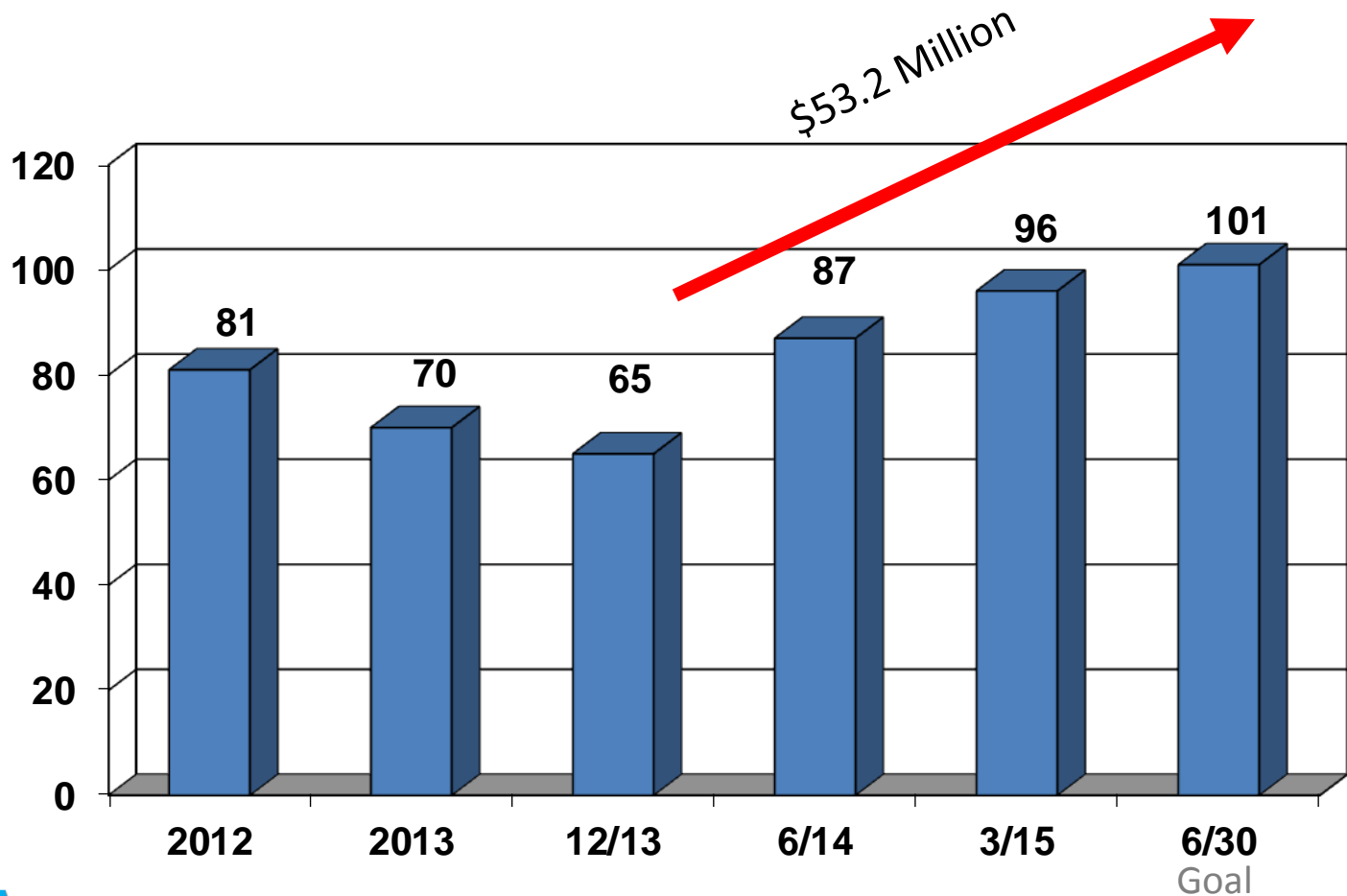
Bottom Line Cost Management



Cost per Adjusted Discharge



Cash-On-Hand



Questions???