

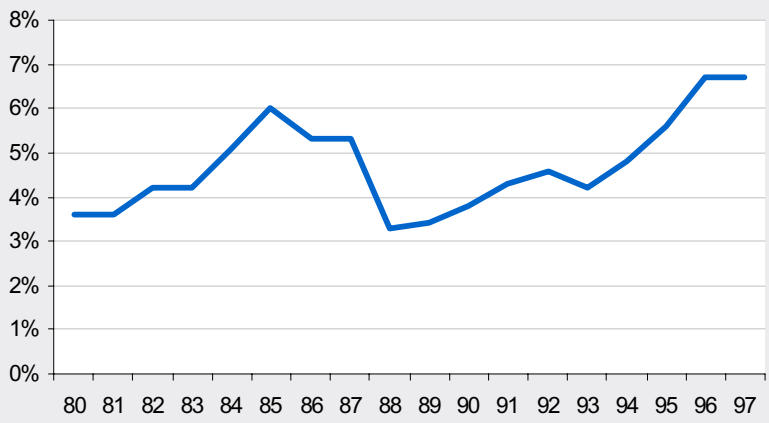


TrendWatch is a quarterly report produced by the American Hospital Association and The Lewin Group that highlights important and emerging issues and trends in the hospital and health care industries.

TRENDWATCH

Although margins have increased in recent years...

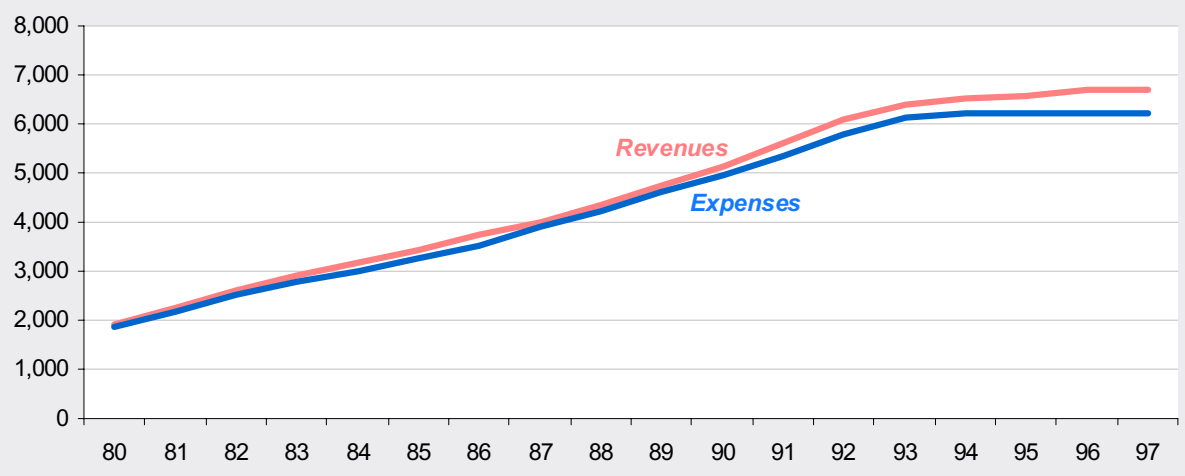
Chart 1: Aggregate total margins for all community hospitals



Since 1988 hospital performance has improved. In 1997, average total margin was 6.7% compared to less than 5% in the early 80's. Cost controls implemented by hospitals have improved hospital performance, as have revenue increases. Not all hospitals have prospered, however. In the last few years nearly 30% of hospitals have had margins of less than 2%.

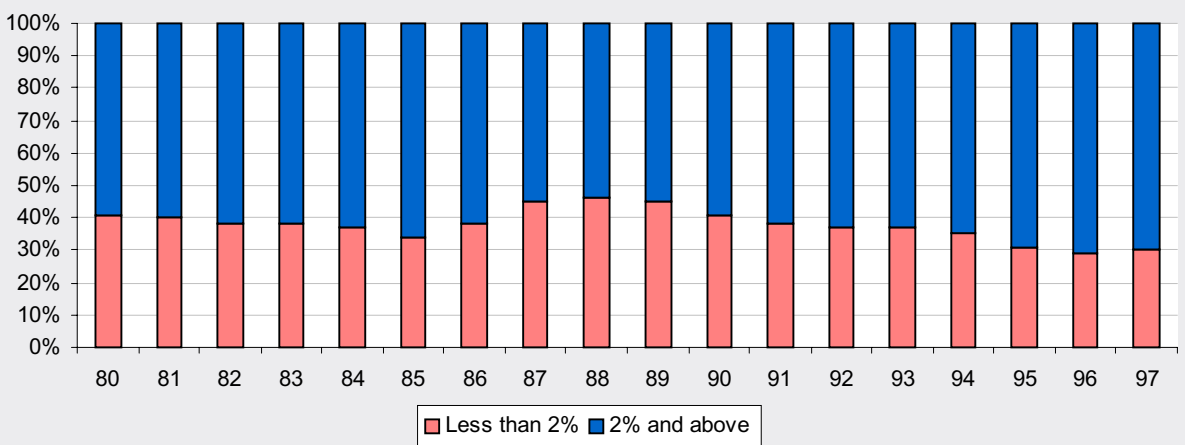
Resulting in large part from cost control measures...

Chart 2: Comparison of total revenues and expenses per adjusted admission



29% of hospitals still have low margins

Chart 3: Percent of hospitals with margins above and below 2%



Hospitals diversify services

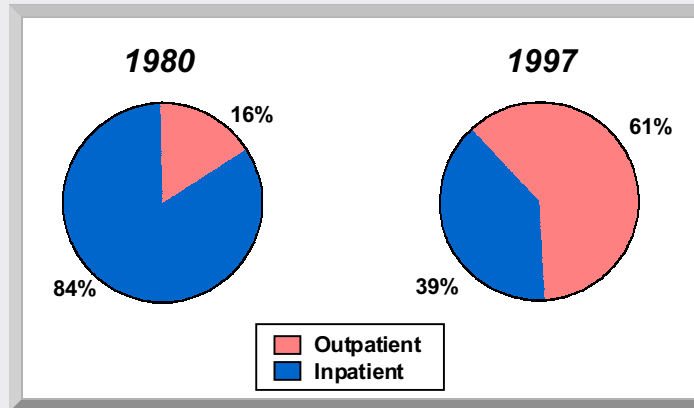
Quote from the field -

The BBA's Impact on Home Health...

"Home health is being hit a 'double whammy' caused by the more restrictive rules on the use of home health and the lower payment. Volume is down at the same time payments have decreased. A lot of home health agencies have closed."

The percentage of surgeries performed on an outpatient basis has increased...

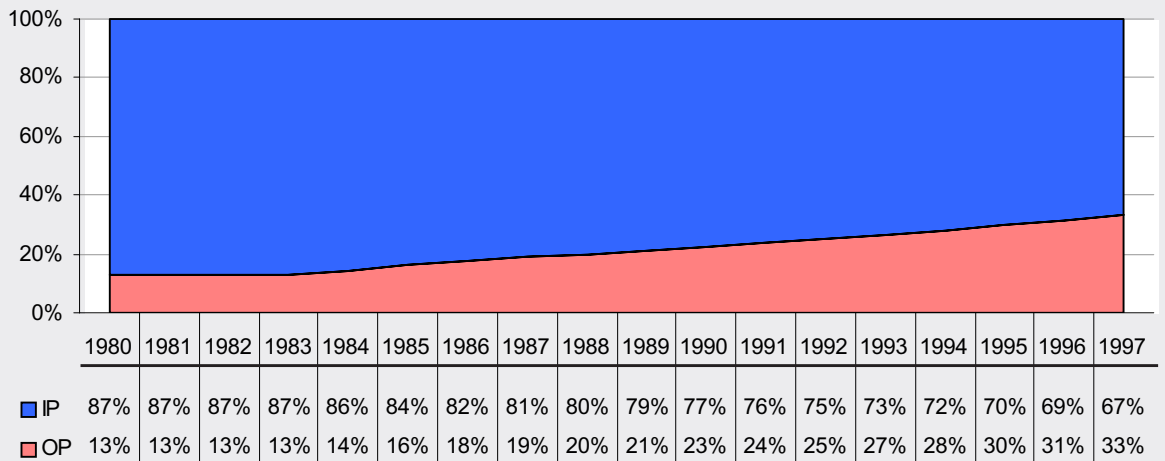
Chart 5: Inpatient versus outpatient surgeries



Hospitals have diversified the services they offer and formed health systems to improve margins, maintain their share of the health care dollar, provide a continuum of care and manage their referral base. A total of 61% of all surgeries are now performed on an outpatient basis. Almost 50% of hospitals have home health services and over 40% have long term care.

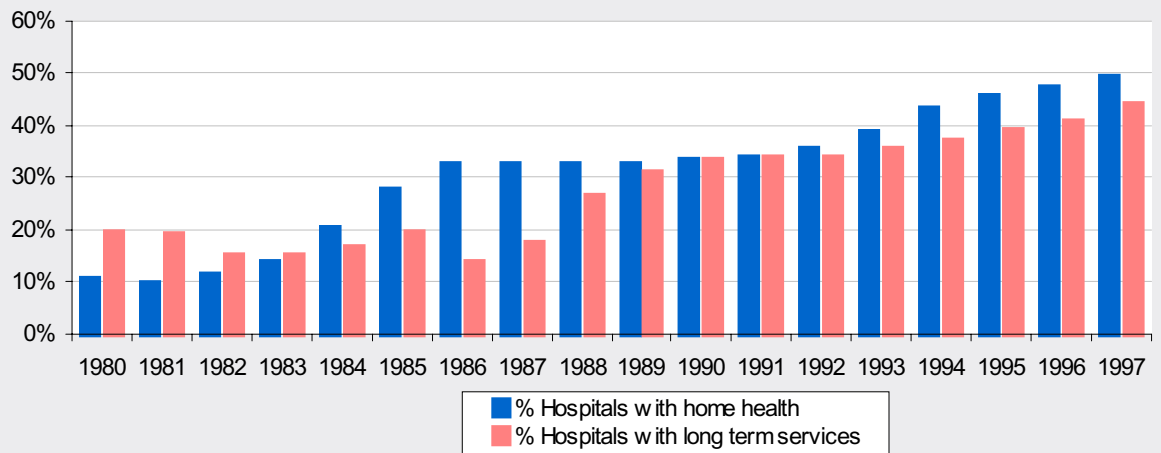
Meanwhile, almost one third of hospitals' gross charges are now for outpatient services...

Chart 6: Inpatient versus outpatient as a percent of total gross charges



And the proportion of hospitals with post-acute services has grown

Chart 7: The percentage of hospitals with facility based home health and long term care services

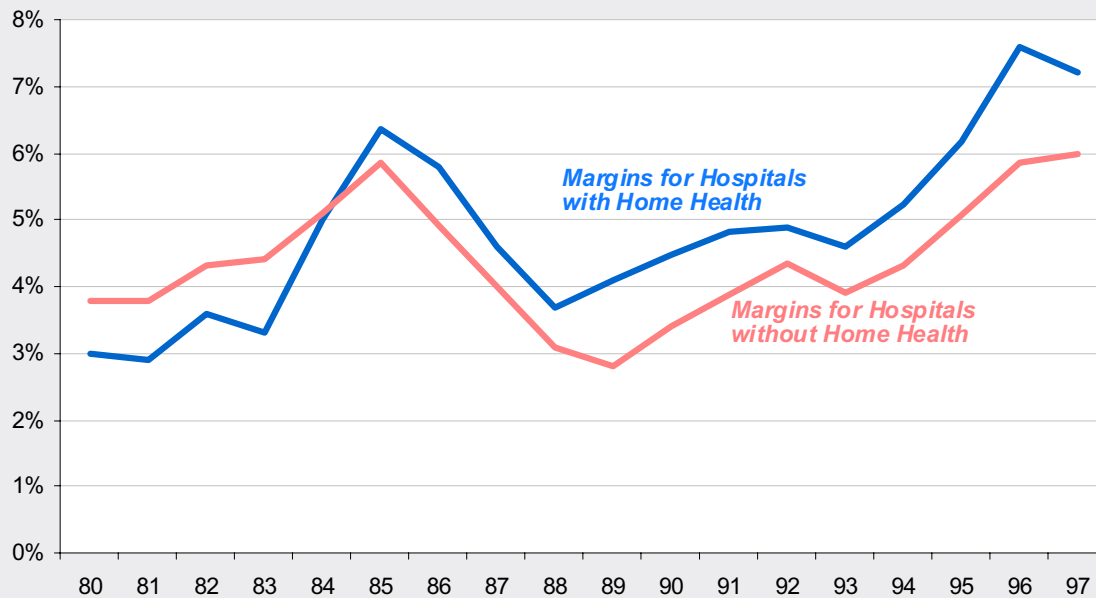


Hospitals that have diversified have outperformed their peers

Hospitals have maintained their total share of national health expenditures by diversifying, expanding into home health, long term and outpatient services. Hospitals with home health care services have consistently higher margins as do those in systems.

Hospitals with home health agencies have done better than other hospitals

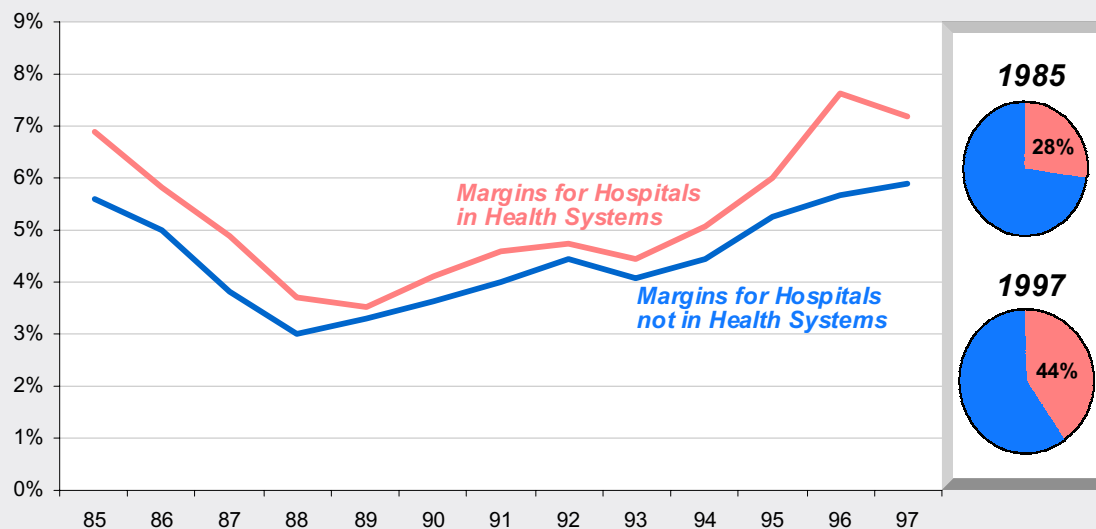
Chart 8: Aggregate Total Margins: Hospitals with and without hospital-based home health agencies



As have those in health systems

Chart 9: Aggregate total margins by system status

Percentage of hospitals in systems



Quote from the field -

The BBA's Impact on Continuity of Care...

"We will have to begin saying no to our hospital's requests to take subacute patients. This will disrupt the critical pathways (we) have developed."

Hospitals in high managed care communities face rough times

Quote from the field -

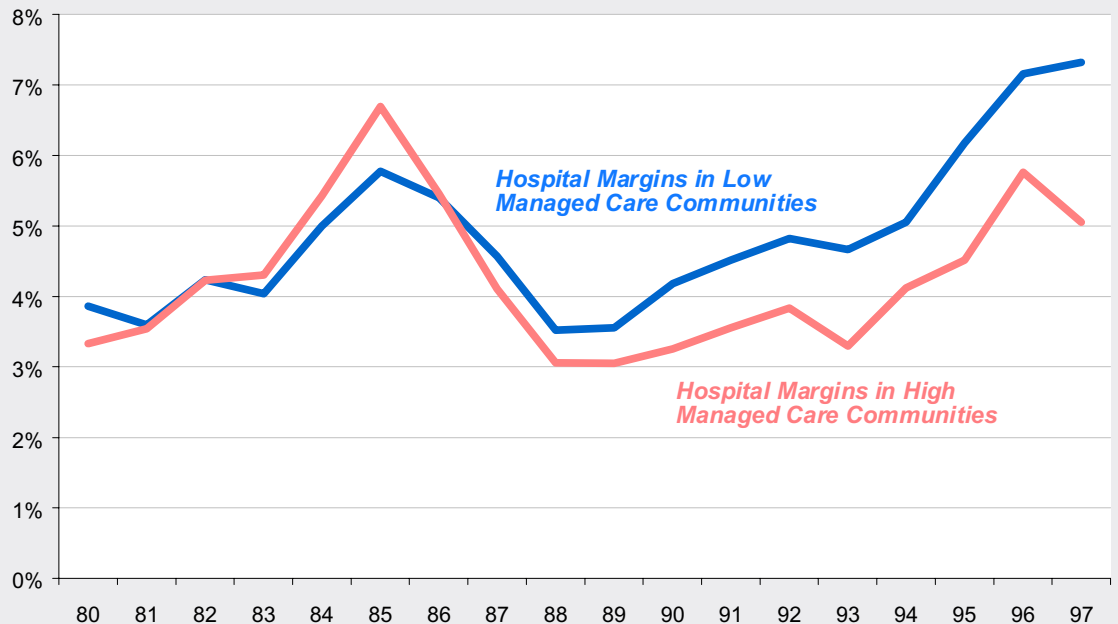
Impact of Medicare managed care...

"Notwithstanding all of the above, Medicare is our best payer. The CEO estimates we are making 25%-30% profit on Medicare PPS patients. Problem comes when these same patients sign up with Medicare HMOs and come back into the hospital at substantially reduced payments."

Hospitals in communities with high managed care penetration - above 30% - have experienced margins below those for low managed care areas. In the last years, costs per case have decreased in high managed care communities, and increased elsewhere. However, this did not compensate for declining revenues.

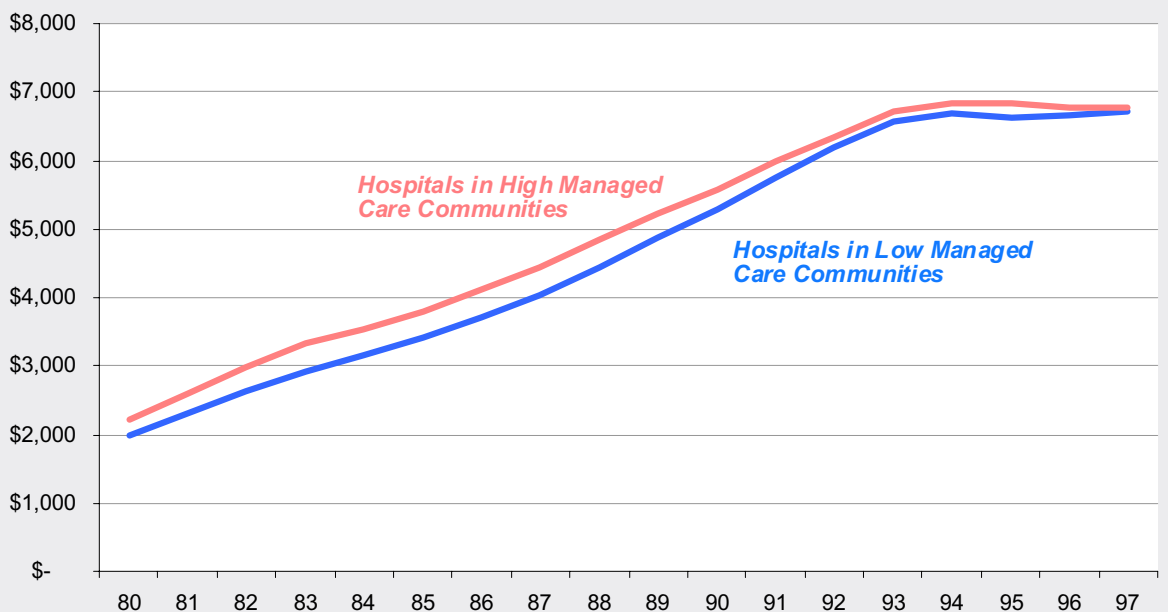
Hospitals in high managed care communities have lower margins...

Chart 10: Aggregate hospital margins by managed care penetration



Despite recently declining costs

Chart 11: Hospital expense per admission by managed care penetration

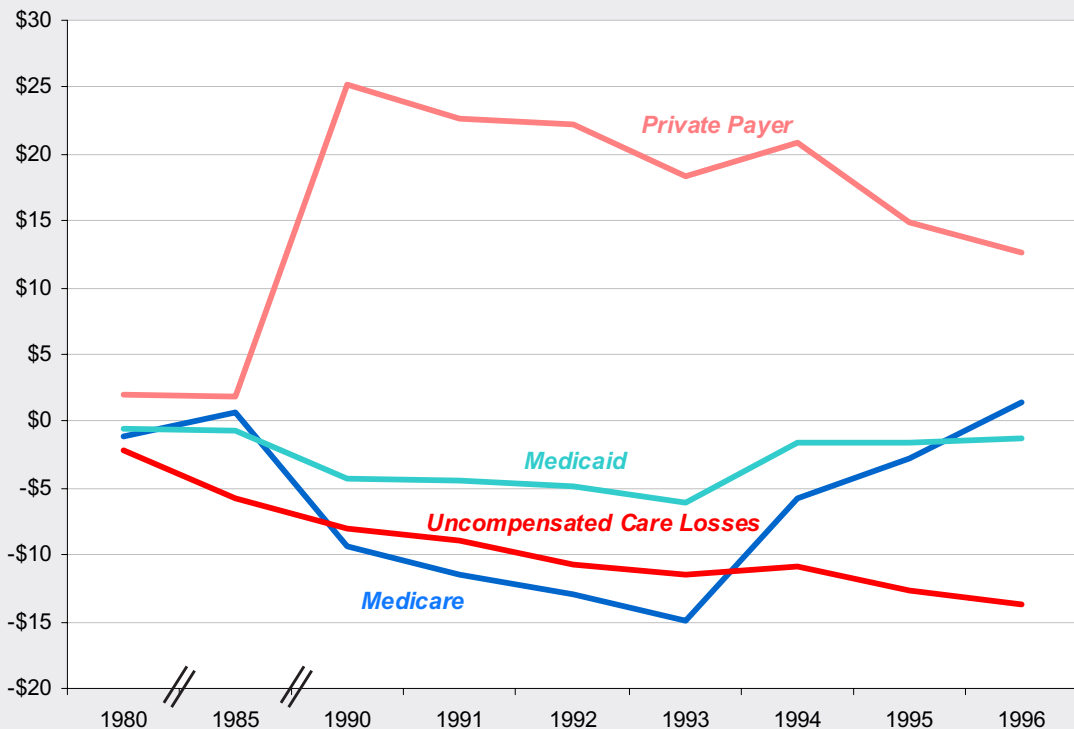


After years of losses, hospitals are relying on Medicare to maintain margins

Historically hospitals have been able to recoup large Medicare losses from private payer gains. As Medicare losses increased, so did the proportion of hospitals with negative inpatient PPS margins. With the recent ratcheting down in private payments likely to continue, and improved Medicare performance, the two groups have moved closer together. Hospitals have started to depend on Medicare, expecting to break even, if not make some margin on their Medicare business.

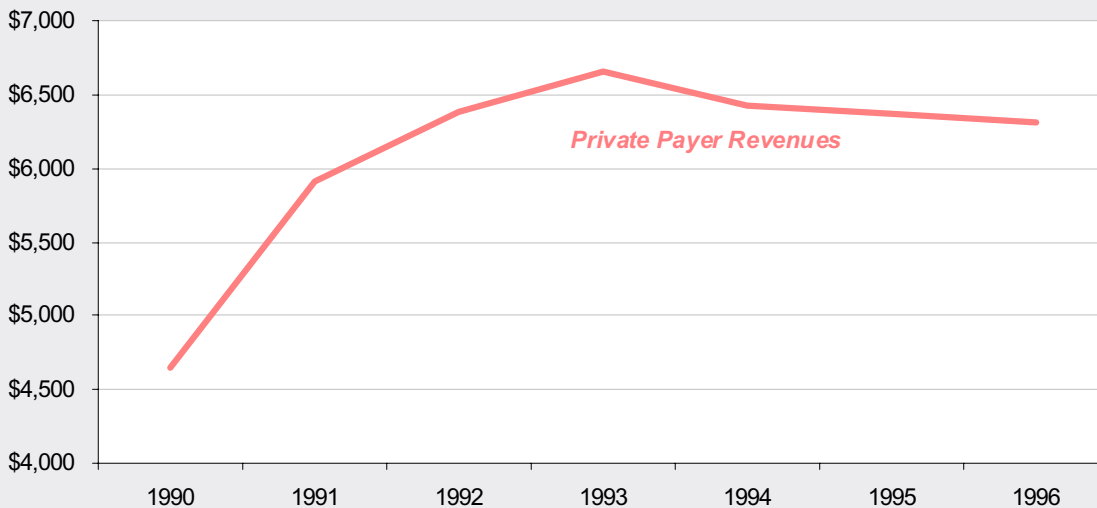
As hospitals have controlled costs, they eliminated Medicare losses, reducing the need to cost shift to other payers...

Chart 12: Aggregate loss or gain by payor category, in billions



Meanwhile, private payments are decreasing

Chart 13: Aggregate private payer revenues per adjusted admission



Quote from the field -

Difficult to separate impact of BBA...

"Can't detect differences between impact of BBA versus managed care and other market forces... BBA, managed care and all the rest is the 'death of a thousand cuts.'"

Will hospitals be forced to continue discounts to private payers as Medicare payments decrease due to the BBA?

- Hospitals that have diversified to maintain higher margins, reduce costs, and improve continuity of care are most at risk due to BBA provisions.
- Hospitals will be under extreme pressure if costs return to the historical rate of increase. Cost pressures, private payer pressures and BBA cuts combined may prove too much for many hospitals.
- Hospitals will lose more than \$40 billion due to the BBA, not including hospital-based SNF and home health services. Over 52% of the cuts occur in the last 2 years of the BBA period.
- The combined impacts of the BBA may endanger hospitals' ability to provide an appropriate continuum of care. As a result, quality of health care may become an issue.

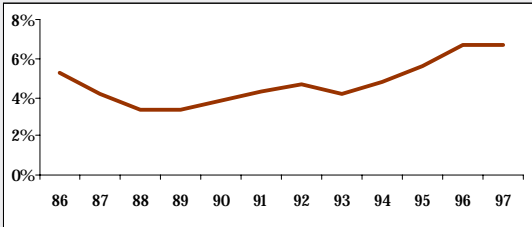
The Lewin Group and AHA's Regional Executives conducted a survey of 73 hospital CEOs and CFOs. All of those interviewed are concerned about the BBA.

The BBA is having an impact on...	Percentage of surveyed hospitals which mentioned an impact
Home Health	48%
SNF	38%
Transfer Policy	19%
GME/ IME	5%
Outpatient payments	14%
Overall drop in margin	30%
Other BBA Concerns	34%
No Major Effect Yet	10%

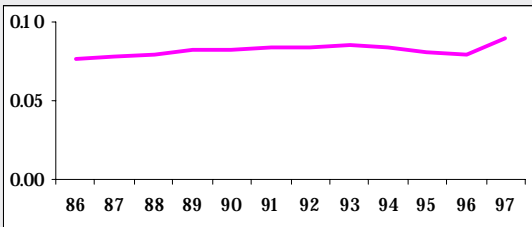
Stats to know

Hospital Sector

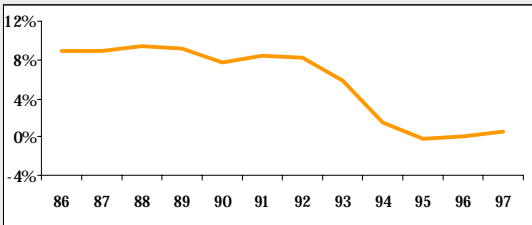
Total Margin:	1995	1996	1997
86 to 97 Trend	5.6%	6.7%	6.7%



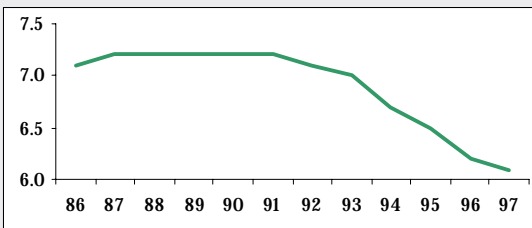
FTE per Adjusted Admission:	1995	1996	1997
86 to 97 Trend	0.08	0.08	0.09



Percent Change in Cost per Case:	1995	1996	1997
86 to 97 Trend	-0.2%	0.2%	0.6%

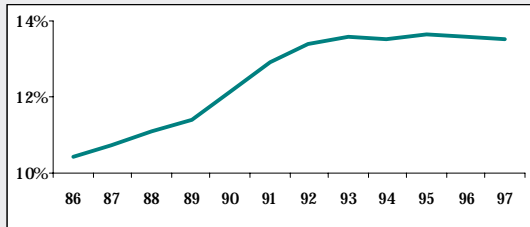


Average Length of Stay (in Days):	1995	1996	1997
86 to 97 Trend	6.5	6.2	6.1

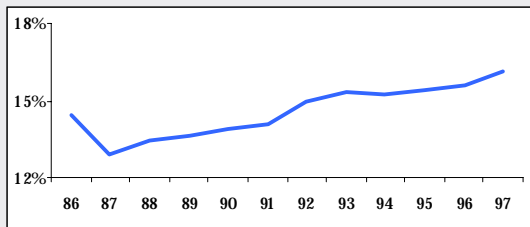


Healthcare Industry

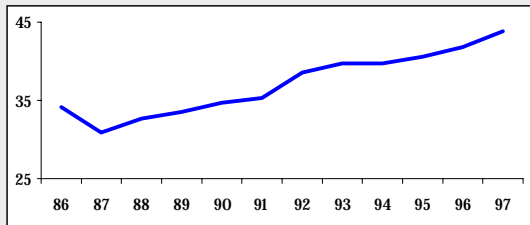
National Health Expenditure as a % of GDP: 86 to 97 Trend	1995	1996	1997
	13.6%	13.6%	13.5%



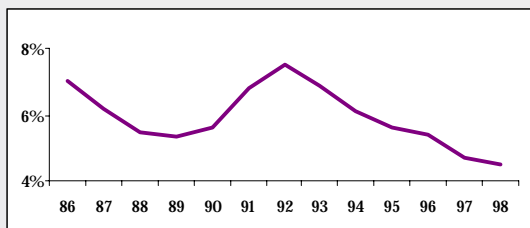
Percent Uninsured: 86 to 97 Trend	1995	1996	1997
	15.4%	15.6%	16.1%



Number Uninsured (in Millions): 86 to 97 Trend	1995	1996	1997
	40.6	41.7	43.7



Percent Unemployed: 86 to 98 Trend	1996	1997	1998
	5.4%	4.7%	4.5%



Sources:

Chart 1-13: *AHA Annual Survey, 1980 - 1997*

Sources for "Stats to Know":

Total Margin: *American Hospital Association Annual Survey, 1986-1997*

FTE/Adjusted Admission: *American Hospital Association Annual Survey, 1986-1997*

Percent Change in Cost per Case: *American Hospital Association Annual Survey, 1986-1997*

Average Length of Stay: *Hospital Statistics, 1999 Edition, Healthcare InfoSource, Inc.*

National Health Expenditure as a Percent of GDP: *Compiled by HCFA on www.hcfa.gov/stats/nhe-oact/tables/t09.html*

Percent Uninsured: *Compiled by Bureau of the Census on <http://www.census.gov:80/hhes/www/hlthins.html>*

Number Uninsured: *Compiled by Bureau of the Census on <http://www.census.gov:80/hhes/www/hlthins.html>*

Percent Unemployed: *Compiled by Bureau of Labor Statistics on <http://stats.bls.gov:80/wh/cpsbref2.html>*

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