

Healthcare Industry Brief

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Healthcare: News Pipeline to Accelerate Over the Next Few Weeks

Concurrent with the New Year, the new administration and a large healthcare conference by one of our competitors, we expect a healthy dose of news flow within our coverage universe over the coming weeks. In this report, we attempt to parse out some of the expected “chatter” in an effort to provide investors a useful checklist as we approach the C4Q08 earnings season, which begins later this month.

- ◆ Within our universe, we expect only one company, Health Management Associates, to announce CY09 earnings guidance before releasing C4Q08 results. We believe the company will offer up guidance prior to presenting at one of our competitor’s healthcare conferences on Tuesday, January 13 at 6:00 p.m. ET.
- ◆ That said, while official guidance may not be offered, we expect several of the companies within our universe to offer some sort of commentary (at the aforementioned conference) surrounding C4Q08 operating trends and expectations for 2009 in light of the weakening operating environment. Within this group, we would expect an update on: (1) inpatient hospital admissions and bad debt trends from the hospitals (LifePoint, Community Health Systems, Universal Health Services, and Health Management Associates); (2) physician visit trends from the med-surg distributors (PSS World Medical, McKesson, and Cardinal); (3) hospital capital budgeting decisions and the impact on HIT/equipment purchases (McKesson and Cardinal); and (4) front-end and Rx sales expectations from the drug stores (CVS and Rite Aid). In the aggregate, we believe commentary at this healthcare conference will likely drive these stocks in either direction before more formal expectations are established over the coming months.
- ◆ Besides company-specific updates, we believe a more formal discussion surrounding Obama’s fiscal stimulus plan, including specific details with respect to the timetable and total dollar amount, will likely emerge over the coming weeks. Within this bill, we would expect an increase in federal matching dollars for Medicaid (although the dollar amount is yet to be determined), which would be a positive for the widening state budget crisis. In addition, we would not be surprised to see the SCHIP debate heat up again over the near term, as well as further discussions surrounding Obama’s \$50 billion HIT initiative. We believe companies exposed to these issues will likely remain volatile until further certainty is established, something that could take months given the current economic situation and the growing federal deficit.
- ◆ Finally, we expect MedPAC’s January meeting (January 8-9) to also spur some potential “noise” surrounding certain segments within our coverage universe, particularly home health (Gentiva Health Services and Amedisys) and skilled nursing. We note that the January meeting is the most influential meeting of the year, as the commission makes its formal recommendations to Congress with respect to reimbursement for FY10. While we believe most of the issues were telegraphed by the commission during the December meeting, we think the incremental push toward potential freezes or cuts to reimbursement in the post-acute space could cause some additional “noise” over the coming weeks. Given the new administration and its fervor for healthcare reform, we believe MedPAC, which was largely overlooked during the Bush reign, could regain some of its importance over the coming year.

With the influx of data over the coming weeks, we will be diligently monitoring the information and will provide updates, when needed, to accommodate the news flow. Stay tuned...

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Public companies mentioned in this report.

Company Name	Ticker	Priced as of 01/02/09	RJ&A Rating (if Applicable)
Amedisys	AMED	\$40.72	Strong Buy
Cardinal Health Inc.	CAH	\$35.22	Market Perform
Community Health Systems, Inc.	CYH	\$14.77	Outperform
CVS/Caremark Corporation	CVS	\$29.38	Strong Buy
Gentiva Health Services	GTIV	\$29.08	Market Perform
Health Management Associates	HMA	\$2.07	Outperform
LifePoint Hospitals, Inc.	LPNT	\$23.23	Market Perform
McKesson Corporation	MCK	\$39.02	Strong Buy
PSS World Medical	PSSI	\$19.03	Outperform
Rite Aid Corporation	RAD	\$0.34	Underperform
Universal Health Services, Inc.	UHS	\$38.12	Strong Buy

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- Strong Buy (SB1)**..... Expected to appreciate and produce a total return of at least 15% and outperform the S&P 500 over the next six months. For higher yielding and more conservative equities, such as REITs and certain MLPs, a total return of at least 15% is expected to be realized over the next 12 months.
- Outperform (MO2)**..... Expected to appreciate and outperform the S&P 500 over the next 12 months. For higher yielding and more conservative equities, such as REITs and certain MLPs, an Outperform rating is used for securities where we are comfortable with the relative safety of the dividend and expect a total return modestly exceeding the dividend yield over the next 12 months.
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- Underperform (MU4)**..... Expected to underperform the S&P 500 or its sector over the next six to 12 months and should be sold.

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Specific Investment Risks Related to the Industry or Issuer

Healthcare Sector General Risks

Potential risks such as reimbursement cuts, acquisition integration, and higher-than-expected operating costs (we note continued cyclical pressure on labor, supply and malpractice costs), as well as a slowing managed care pricing cycle, could negatively impact the healthcare sector.

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