

MultiCare Health System Fourth Quarter 2022 Results December 31, 2022

MultiCare Health System (MHS), a Washington nonprofit corporation, is an integrated healthcare delivery system providing inpatient, outpatient, and other healthcare services primarily to the residents of Pierce, King, Spokane and Thurston Counties and, with respect to pediatric care, much of the southwest Washington region. As of December 31, 2022, MHS was licensed to operate 2,099 inpatient hospital beds, including 120 beds associated with a joint venture psychiatric hospital in Tacoma, Washington. MHS operates nine acute care facilities (Tacoma General Hospital, Good Samaritan Hospital, Allenmore Hospital, Mary Bridge Children's Hospital, Auburn Medical Center, Covington Hospital, Deaconess Hospital, Valley Hospital and Capital Medical Center) and one behavioral health hospital (Navos). MHS also operates eight outpatient surgical sites, five free-standing emergency departments, home health, hospice, and multiple urgent care, primary care and multispecialty clinics located throughout the MHS service areas. The consolidated financial statements include the operations of these services as well as those of four wholly owned subsidiaries (Greater Lakes Mental Healthcare, Medis, Inc., MultiCare Rehabilitation Specialists, P.C. (MRS), and PNW Pace Partners, LLC), a wholly owned professional services organization supporting cardiovascular services at MHS (CHVI Professional Corp), a wholly owned accountable care organization (MultiCare Connected Care), and two fundraising foundations (Mary Bridge Children's Foundation and MultiCare Foundations). MultiCare Foundations is doing business as MultiCare Health Foundation, Good Samaritan Foundation, MultiCare South King Health Foundation, MultiCare Behavioral Health Foundation and MultiCare Inland Northwest Foundation.

During 2022, agreements were signed to purchase additional units of Physicians of Southwest Washington, LLC (PSW) and Olympic Sports & Spine, PLLC (OSS). The transactions increased ownership of PSW and OSS with total consideration paid of approximately \$25 million.

In October 2022, MHS announced it had reached an agreement to affiliate with Yakima Valley Memorial Hospital. On January 17, 2023, the affiliation was completed after receiving regulatory approval and Yakima Valley Memorial Hospital became MultiCare Yakima Memorial Hospital.

In November 2022, MHS ended its engagement with Moody's for the rating of MHS debt. Moody's has withdrawn its ratings for MHS. MHS continues at this time to receive rating updates from Standard & Poor's and Fitch.

The following graphic depicts the breadth of services that MHS is providing across its service areas today:



As of 12/31/2022 unless specifically indicated.

*Wellfound Behavioral Health Hospital, our joint venture with Virginia Mason Franciscan Health, as well as its 120 licensed beds, are included in these counts.

Summary of Revenues and Expenses

The following summary of revenues and expenses has been derived from MHS's consolidated financial statements. The consolidated financial statements for the year ended December 31, 2021 have been audited by independent certified public accountants and should be reviewed in conjunction with the complete footnote disclosures contained within those audited year-end statements. The consolidated financial statements for the year ended December 31, 2022 have been derived from the unaudited financial statements of MHS and are prepared by MHS's management. The unaudited financial information presented includes all adjustments that MHS management considers necessary at this time for a fair presentation of the financial position and results of operations for the periods presented.

	Year Ended December 31, (in thousands)	
	2022 (Unaudited)	2021 (Audited)
Revenues:		
Patient service revenue	3,765,888	3,504,691
Other operating revenue	231,429	314,323
Net assets released from restriction	6,382	5,170
Total operating revenue	4,003,699	3,824,184
Expenses		
Salaries and wages	2,199,265	1,870,645
Employee benefits	297,613	278,185
Supplies	658,470	600,757
Purchased services	396,747	349,159
Depreciation and amortization	140,892	126,307
Interest	56,842	47,670
Other	541,246	486,005
Total expenses	4,291,075	3,758,728
Operating (loss) income	(287,376)	65,456
Nonoperating (loss) income:		
Investment (loss) income	(344,301)	213,993
Swap cash settlements	(5,439)	(9,374)
Change in fair value of swaps	133,126	35,247
Other nonoperating loss	(11,046)	(13,729)
Total nonoperating (loss) income	(227,660)	226,137
(Deficit) Excess of revenues over expenses	\$ (515,036)	291,593

Consolidated Balance Sheets (in thousands)

	December 31, 2022 (Unaudited)	December 31, 2021 (Audited)
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 600,557	\$ 308,732
Patient Accounts Receivable, Net	511,727	460,569
Supplies Inventory	60,070	60,056
Other Current Assets, Net	165,586	96,361
Total Current Assets	1,337,940	925,718
DONOR - RESTRICTED ASSETS	119,526	96,775
LONG-TERM INVESTMENTS	1,909,715	2,610,531
PROPERTY, PLANT AND EQUIPMENT:		
Land and Improvements	164,041	138,910
Buildings	2,360,383	2,313,543
Equipment	1,051,004	940,116
Total Property, Plant and Equipment	3,575,428	3,392,569
Less: Accumulated Depreciation	(1,640,005)	(1,500,929)
Net Property, Plant and Equipment	1,935,423	1,891,640
Construction in Progress	173,830	118,494
Total Property, Plant and Equipment, Net	2,109,253	2,010,134
RIGHT OF USE LEASE ASSET, NET	186,621	161,176
OTHER ASSETS	564,105	554,625
TOTAL ASSETS	6,227,160	6,358,959
LIABILITIES		
CURRENT LIABILITIES		
Accounts Payable and Accrued Expenses	326,664	283,004
Accrued Compensation and Related Liabilities	329,672	340,029
Accrued Interest Payable	23,643	18,059
Current Portion of Long-Term Debt	18,496	43,609
Current Portion of Right of Use Lease Liability	34,873	30,659
Total Current Liabilities	733,348	715,360
INTEREST RATE SWAP	9,470	119,100
RIGHT OF USE LEASE LIABILITY, NET	159,607	137,206
LONG-TERM DEBT, NET	1,972,137	1,572,235
OTHER LIABILITIES	212,067	208,307
NET ASSETS		
Controlling interest	2,930,546	3,430,009
Noncontrolling interest	34,471	-
Without donor restrictions	2,965,017	3,430,009
With donor restrictions	175,514	176,742
Total Net Assets	3,140,531	3,606,751
TOTAL LIABILITIES & NET ASSETS	\$ 6,227,160	\$ 6,358,959

Consolidated Cash Flow Statements
(in thousands)

	Year Ended December 31, (Unaudited) <u>2022</u>	Year Ended December 31, (Audited) <u>2021</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (499,120)	\$ 352,589
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	140,912	126,307
Amortization of bond premiums, discounts, and issuance costs	(2,163)	(2,433)
Realized and change in unrealized gains on investments, net	378,740	(188,615)
Change in fair value of interest rate swaps	(133,126)	(35,247)
(Gain) Loss on disposal of assets, net	(3,009)	2,373
(Gains) Losses on joint ventures, net	7,032	(513)
Restricted contributions for long-term purposes	(4,968)	(16,952)
Changes in operating assets and liabilities:		
Accounts receivable	(51,158)	(73,590)
Supplies inventory and other current assets	(49,380)	(17,586)
Right-of-use lease asset	(25,445)	40,614
Other assets, net	76,068	(38,219)
Accounts payable and accrued expenses and interest payable	27,421	67,751
Accrued compensation and related liabilities	(14,765)	38,053
Right-of-use lease liability	31,000	(30,721)
Other liabilities, net	2,865	(8,287)
Net cash (used in) provided by operating activities	<u>(119,096)</u>	<u>215,524</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant and equipment	(237,315)	(216,973)
Proceeds from disposal of property, plant and equipment	6,360	7,629
Purchase of additional ownership in PSW and OSS	(24,735)	-
Purchase of Capital Medical Center and related real estate	-	(179,662)
Investments in joint ventures, net	(11,445)	(10,373)
Purchases of investments	(8,060,868)	(5,634,748)
Sales of investments	8,364,222	5,175,627
Change in donor trusts	(2,833)	5,700
Net cash provided by (used in) investing activities	<u>33,386</u>	<u>(852,800)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of long-term debt	(415,646)	(8,522)
Proceeds from bond issuance	798,300	-
Payment of debt issue expenses	(5,702)	-
Principal payments on finance lease obligations	(4,385)	(8,645)
Restricted contributions for long-term purposes	4,968	16,952
Net cash provided by (used in) financing activities	<u>377,535</u>	<u>(215)</u>
Net change in cash and cash equivalents	291,825	(637,491)
CASH AND CASH EQUIVALENTS, beginning of year	308,732	946,223
CASH AND CASH EQUIVALENTS, end of period	<u><u>\$ 600,557</u></u>	<u><u>\$ 308,732</u></u>

SUMMARY OF REVENUE SOURCES

The following table shows the combined gross patient service charge percentages for MHS by payor. The percentages for the year ended December 31, 2022 include Capital Medical Center.

Source	Calendar Year Ended December 31,	
	2022	2021
Medicare	39.7 %	38.2 %
Medicaid	25.4	25.8
Premiera/Blue Cross	8.4	9.1
Regence/Blue Shield	6.0	7.5
Personal Pay	2.1	1.9
All Other	18.4	17.5
Total	100.0 %	100.0 %

SUMMARY OF OPERATING DATA

The following table presents selected statistical indicators of MHS's patient activity:

	Calendar Year Ended December 31,	
	2022	2021
Statistical Summary		
Admissions ¹⁾	79,558	76,043
Adjusted Admissions	200,486	184,634
Patient Days ¹⁾	480,092	449,118
Average Length of Stay (Days)	6.03	5.91
Average Daily Census	1,315	1,230
Percent Occupancy (of beds in service)	79.2%	75.0%
Emergency Room Visits	545,137	458,921
Provider Visits (primary, specialty, & urgent care)	3,086,106	3,127,452
Outpatient Visits ²⁾	902,741	892,591
Overall Case Mix Index	1.66	1.65
Surgical Cases	58,463	55,741

1) Admissions and patient days include acute care and rehabilitation volumes and exclude newborns.

2) Outpatient visits exclude ER visits, physician visits, outpatient surgery and lab tests.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Operational impact of COVID-19.

MHS continues to be impacted by the COVID-19 pandemic in 2021 and 2022, and experienced significant waves of hospitalizations due to the Delta variant in the latter part of 2021 as well as the Omicron variant in the first quarter of 2022. The increase in COVID patients led to postponement of non-emergent procedures due to a lack of available beds and staffing challenges within all hospitals during these waves. MHS is still impacted by staffing challenges and capacity constraints with an increase in patients seeking care in our facilities. Our hospitals also are experiencing difficulties in discharging patients to lower acuity settings, which increased length of stay without additional net revenue.

MHS continues to be impacted by higher expenses due to inflationary pressures and other market conditions. MHS has seen these conditions mainly impact salaries and wages and supplies due to increases in employee pay rates, increases in contract labor rates and usage, and supply chain issues increasing costs within supplies. MHS continues to maintain a strong balance sheet and appropriate liquidity to withstand the continued challenges of COVID-19, thereby ensuring resource availability for the provision of patient care.

MHS has accessed federal, state and insurance programs to secure funding to offset lost revenue and increased expenses associated with the pandemic. MHS filed applications and obtained reimbursement of additional expenses from FEMA based on criteria due to the national emergency declaration made in early 2020. MHS submitted an expedited funding application with FEMA that covered the period from the start of the national disaster declaration through June 30, 2020, which allowed MHS to recover in an expedited timeline up to 50% of the total funding applied for on the application. Management filed the completed application with FEMA representatives to receive the remaining 50% of the funding due MHS. MHS also completed several other applications and filed those with FEMA seeking reimbursements for COVID-19 expenses related mainly to labor and supplies from the start of the public health emergency to June 30, 2022. MHS will continue applying for funding pertaining to later periods (either through FEMA or CARES Act) until the national disaster declaration is no longer in effect.

Details of all COVID-19-related funding received and recognized are noted below through December 31, 2022:

COVID-19 Relief Funding Summary		Amount recognized in other operating revenue			
In thousands (000's)					
Sources of external relief funding	Total cash and receivables recorded cumulative to date	2020	2021	2022	Total recognized
CARES Act PRF Funding	300,697	118,965	181,732	-	300,697
FEMA	20,197	4,214	1,405	14,578	20,197
CARES Act CRF Funding	2,922	2,922	-	-	2,922
Insurance proceeds	1,003	1,003	-	-	1,003
Total proceeds received and recognized	324,819	127,105	183,136	14,578	324,819

Operating Income Summary. MHS generated an operating loss of \$287.4 million (7.2% operating loss) for the year ended December 31, 2022 compared to an operating margin of \$65.5 million (1.7% operating margin) for the year ended December 31, 2021¹. Included in 2022 and 2021 operating margin is \$14.6 million and \$183.1 million, respectively, of external relief funding received to help offset losses and increased expenses related to the operational impacts of COVID-19. MultiCare management developed and implemented plans to improve revenue generation and address rising costs and those plans continue. Initiatives include reducing contract labor reliance, recruitment and retention of employed staff, increase in surgical volumes, increased use of technology to optimize patient experience and improve capture of all revenue, reducing average inpatient lengths of stay where appropriate, review and optimization of other expense areas, especially supplies and purchased services, along with a number of other areas of focus, with the overall expectation of improving the operating margin of the health system moving forward.

Operating Revenue. Total operating revenue increased \$179.4 million (4.7%) to \$4.00 billion in 2022 compared to \$3.82 billion in 2021. The increased revenue is mainly due to increased volumes. Key volume increases driving the revenue growth stemmed from admissions (4.6%), emergency department visits (18.8%), and surgical cases (4.9%). Gross charges increased due to volumes, and

reimbursement rate increased slightly compared to prior year due to MultiCare's focus on improving reimbursement, despite higher Medicare volumes than the prior year and the return of Medicare sequestration.

Operating Expenses. Total operating expenses increased \$532.3 million (14.1%) to \$4.29 billion for the year. In addition to volume-driven expense increases, average length of stay was 2.5% higher compared to 2021. Total salaries and wages increased \$327.1 million (17.5%) from the prior year, due to higher volumes, general wage rate increases for employed staff, and reliance on contract labor. Contract labor rates have increased significantly, especially for RNs, but have improved throughout 2022. Average Contract RN labor rates were approximately 33% higher than prior year and double the average rate from 2020, and account for \$131.6 million of the increase in expenses from prior year. Both reliance on contract labor and contract labor rates remain a significant challenge, but contract labor expense in December 2022 was the lowest since August 2021. MHS continues to see higher supply expenses associated with increased length of stay and higher inflationary increases in this area. Additionally, MHS experienced increases in purchased services and other costs due to inflationary impacts in technology licenses and fees and other required services. Interest expense increased 19.2% from prior year from the issuance of additional debt during the year and rising variable rates.

Nonoperating Income. MHS recognized a nonoperating loss of \$227.7 million in 2022, compared to nonoperating income of \$226.1 million in 2021. Investment performance generated a \$344.3 million loss, compared to the gain of \$214.0 million in 2021. The remaining variance primarily resulted from changes in the estimated fair value of interest rate swaps, which produced a gain of \$133.1 million in 2022 compared to a gain of \$35.2 million in 2021. The gains and losses on the interest rate swaps are due to fluctuations in the global interest rate environment, with interest rates increasing in both 2021 and 2022.

Net Income. Operating loss of \$287.4 million, combined with the nonoperating loss of \$227.7 million, produced a net loss of \$515.0 million for year ended December 31, 2022 compared to an excess of revenues over expenses of \$291.6 million in 2021.

Balance Sheet / Financial Position. As of December 31, 2022, unrestricted cash and investments were \$2.51 billion, a decrease of \$408.7 million from December 31, 2021. The decrease is driven by investment and operating losses and other cash uses.

As of December 31, 2022, total net assets were \$3.14 billion compared to \$3.61 billion as of December 31, 2021. Net assets without donor restrictions decreased \$465.0 million to \$2.96 billion as of December 31, 2022. Despite significant challenges during the pandemic, especially during recent months, MHS' balance sheet and cash position remain strong.

KEY BALANCE SHEET INDICATORS

	<u>December 31, 2022</u>	<u>December 31, 2021</u>
Days cash on hand	221	293
Cash to long-term debt	126.1%	180.7%
Long-term debt to capitalization	40.2%	32.0%

¹ Note that, unless stated otherwise, all comparisons described in the Management Discussion and Analysis above compare the results of the year ended December 31 of each year referenced.