DaVita Inc. Reports 3rd Quarter 2005 Results

PRNewswire-FirstCall EL SEGUNDO, Calif.

DaVita Inc., today announced results for the quarter ended September 30, 2005. Net income for the three months and nine months ended September 30, 2005 was \$55.2 million and \$164.5 million, or \$0.53 and \$1.58 per share, respectively.

(Logo: http://www.newscom.com/cgi-bin/prnh/20020729/DAVITALOGO)

Net income for the quarter ended September 30, 2005 included pre-tax Medicare lab recoveries related to prior years' services of \$1.1 million and a net swap valuation loss of \$1.7 million.

Financial and operating highlights include:

- -- Cash Flow: Operating cash flow for the quarter ended September 30, 2005 was \$85 million and free cash flow was \$75 million. For the rolling 12-month period ended September 30, 2005 operating cash flow was \$334 million and free cash flow was \$287 million, excluding the tax benefit from stock option exercises and the after-tax benefit of Medicare lab recoveries related to prior years' services. Including those items, the rolling 12-month period operating cash flow was \$390 million and free cash flow was \$343 million.
- -- Operating Income: Operating income for the three months and nine months ended September 30, 2005, was \$111.2 million and \$324.9 million, respectively, excluding Medicare lab prior years' recoveries of \$1.1 million and \$3.8 million, respectively.
- Operating Income Margins: Operating income margins declined from 17.6% for the third quarter of 2004 to 16.5% for 2005. The decrease was primarily attributable to increases in labor and benefit costs, and higher G&A costs, driven primarily by legal and compliance professional fees, as well as integration costs associated with the Gambro Healthcare acquisition.
- -- Volume: Total treatments for the third quarter were 2,037,584 or 25,792 treatments per day, an increase of 12.9% per day as compared to the third quarter of last year. Non-acquired treatment growth was 5.2% for the third quarter.
- -- Effective Tax Rate: The effective income tax rate for third quarter 2005 was 37.5%. We expect the annual effective tax rate to be 38.0% for 2005, and within a range of 39% 40% for 2006, exclusive of valuation allowance adjustments.
- -- Center Activity: As of September 30, 2005, we operated or provided administrative services at 724 outpatient centers serving approximately 58,100 patients. During the third quarter we acquired 11 centers, opened 8 de novo centers and divested one wholly owned center.

Summary of Recent Transactions:

On October 5, 2005, we completed our acquisition of Gambro Healthcare, one of the largest dialysis service providers in the U.S. for an aggregate purchase price of \$3.055 billion. In connection with the acquisition we:

- entered into a new credit agreement for \$3.05 billion and used borrowings of \$2.85 billion under the facilities along with available cash of \$252 million to purchase Gambro Healthcare and pay related fees of \$47 million;
- entered into an Alliance and Product Supply Agreement with Gambro AB and Gambro Renal Products, Inc. for the next ten years, during which we are committed to purchase a significant majority of our hemodialysis products, supplies and equipment; and
- on October 6, 2005 we completed the sale of 70 freestanding renal dialysis centers to Renal Advantage. The sale of an additional three centers to Renal Advantage will be made upon receipt of Illinois state regulatory approval and is expected to close within the next 60 days. Also one other center was sold to a separate physician group and two management services agreements were terminated. We are receiving approximately \$328 million for all of the divested centers, and resulting tax payments are estimated at approximately \$95 million.

As of September 30, 2005, proforma for the Gambro Healthcare acquisition and divestitures, we would have operated or provided administrative services to over 1,200 outpatient centers in 41 states serving approximately 94,000 patients.

Outlook

Our 2006 operating income is currently projected to be in the \$600-\$670 million range, before the impact of FASB No. 123R related to stock option expensing. Major variables include integration of the Gambro Healthcare operations, government reimbursement rates, intensities of physician prescribed pharmaceuticals, payor contracting, and growth assumptions.

Kent Thiry, CEO, stated, "This is a difficult time to provide guidance because there is an unusual amount of change going on, internally and externally. The integration is off to a strong start and we remain confident the combination of these two teams was the correct long-term decision for shareholders. In addition we remain confident that the combination will lead to even better patient care."

DaVita will be holding a conference call to discuss its third quarter results for 2005 on October 31, 2005, at 11:30 AM Eastern Time. The dial in number is 800-399-4406. A replay of the conference call will be available on DaVita's official web page. http://www.davita.com/, for the following 30 days.

This release contains forward-looking statements. Factors which could impact future results include the uncertainties associated with governmental regulations, general economic and other market conditions, acquisitions and the risk factors set forth in the Company's SEC filings, including its Form 10-Q for the guarter ended June 30, 2005. The forward-looking statements should be considered in light of these risks and uncertainties. These risks and uncertainties include those relating to:

- -- the concentration of profits generated from preferred provider organizations (PPO) and private indemnity patients,
- -- possible reductions in private and government reimbursement rates,
- -- changes in pharmaceutical practice patterns or reimbursement policies.
- -- our ability to maintain contracts with physician medical directors,
- -- legal compliance risks, including our continued compliance with complex government regulations and the ongoing review by the U.S. Attorney's Office for the Eastern District of Pennsylvania and the OIG, the subpoena from the U.S. Attorney's Office for the Eastern District of New York, the subpoena from the U.S. Attorney's Office, Eastern District of Missouri and our ability to cause Gambro Healthcare to comply with its corporate integrity agreement, and
- our ability to complete and integrate acquisitions, including Gambro Healthcare.

We undertake no obligation to update or revise any forward-looking statements, whether as a result of changes in underlying factors, new information, future events or otherwise.

This release contains non-GAAP financial measures. For reconciliations of these non-GAAP financial measures to their most comparable measure calculated and presented in accordance with GAAP, see the attached reconciliation schedules.

DAVITA INC.

CONSOLIDATED STATEMENTS OF INCOME (unaudited)

(dollars in thousands, except per share data)

Nine months ended Three months ended September 30, September 30, 2005 2004 2005 2004 Net operating revenues \$676,820 \$595,531 \$1,935,825 \$1,682,592 Operating expenses and charges: 457,994 396,909 1,303,297 1,135,477 Patient care costs General and 50,600 administrative 60,820 174,939 138,931 Depreciation and amortization 26,372 22,257 77,080 63,454 Provision for uncollectible accounts 12.034 10.520 34.457 29.964 Minority interests

and equity income,

7,262 3,593 17,403 9,814 net

Total operating

expenses and

charges 564,482 483,879 1,607,176 1,377,640

Operating income 112,338 328,649 304,952 111,652

(36,635)Debt expense (24,297)(13,741)(66,728)

Swap valuation (loss)

gain (1,718)4,543 Refinancing charges (6.872)

2,074 1.010 Other income 5,777 3,120

Income before income

98,921 265,369 271,437 taxes 88,397

Income tax expense 33,180 38,535 100,875 105,785

Net income \$55,217 \$60,386 \$164,494 \$165,652

Earnings per share:

\$1.67 Basic \$0.55 \$0.61 \$1.64 Diluted \$0.53 \$0.59 \$1.58 \$1.61

Weighted average

shares:

Basic 101,307,461 99,168,930 100,399,902 98,972,666 Diluted 104,371,789 102,889,781 103,803,975 103,193,267

DAVITA INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited) (dollars in thousands)

> Nine months ended September 30, 2005 2004

Cash flows from operating activities:

\$164,494 \$165,652 Net income

Adjustments to reconcile net income to cash

provided by operating activities:

Depreciation and amortization 77.080 63.454 Stock options, principally tax benefits 37,021 30,465 Minority interests in income of consolidated subsidiaries 18,225 11,345 Distributions to minority interests (12,261)(6,966)Deferred income taxes (8,950)11,831 6,872 Refinancing charges Swap valuation gains (4,543)Non-cash debt expense 2,397 1,497 (Gain) loss on divestitures (2,213)59 Equity investment income (822)(1,531)Changes in operating assets and liabilities,

other than from acquisitions and divestitures:

Accounts receivable (39,953)(33,998)Medicare lab recoveries 10,707 (1,131)Inventories 5,065 (2,670)Other current assets (2,899)(755)2,109 Other long-term assets (2,134)Accounts payable 2,753 7,773

Accrued compensation and benefits 27,366 22,409 27.279 Other current liabilities 43.360

Income taxes 19,670 136 Other long-term liabilities (3,371)(8) Net cash provided by

302,210 332,604 operating activities

Cash flows from investing activities:

Additions of property and equipment, net (97,529)(89,872)Acquisitions and divestitures, net (130,113)(245, 284)

Investments in and advances to affiliates,

14,294 4,862 Intangible assets (779)(635)

Net cash used in investing activities (214,127) (330,929)

Cash flows from financing activities:

Borrowings 1,742,433 3,123,171 Payments on long-term debt (1,753,351) (2,903,648) Deferred financing costs (30,561)(3,934)

Purchase of treasury stock (86,559)

Stock option exercises 38,613 34,580

Net cash (used in) provided by

financing activities (2,866) 163,610

Net increase in cash and cash equivalents 85,217 165,285

Cash and cash equivalents at

beginning of period 251,979 61,657

Cash and cash equivalents at end of period \$337,196 \$226,942

DAVITA INC.

CONSOLIDATED BALANCE SHEETS

(unaudited)

(dollars in thousands, except per share data)

September 30, December 31,

2005 2004

ASSETS

Cash and cash equivalents \$337,196 \$251,979

Accounts receivable, less allowance

of \$68,379 and \$58,166 502,887 462,095

Medicare lab recoveries 1,131

Inventories 36,032 31,843

 Other current assets
 47,163
 44,210

 Deferred income taxes
 104,772
 78,593

 Total current assets
 1,029,181
 868,720

Property and equipment, net 452,033 412,064
Amortizable intangibles, net 83,683 60,719
Investments in third-party dialysis businesses 2,526 3,332

Other long-term assets 44,889 10,898 Goodwill 1,256,223 1,156,226

\$2,868,535 \$2,511,959

LIABILITIES AND SHAREHOLDERS' EQUITY

Accounts payable \$99,080 \$96,231 Other liabilities 184,666 157,214

 Accrued compensation and benefits
 162,219
 133,919

 Current portion of long-term debt
 4,349
 53,364

 Income taxes payable
 20,677
 1,007

 Total current liabilities
 470,991
 441,735

 Long-term debt
 1,360,665
 1,322,468

Long-term debt 1,360,665 1,322,468
Other long-term liabilities 25,096 22,570
Deferred income taxes 163,491 148,859
Minority interests 75,759 53,193

Commitments and contingencies

Shareholders' equity:

Preferred stock (\$0.001 par value,

5,000,000 shares authorized; none issued)

Common stock (\$0.001 par value, 195,000,000 shares authorized;

 134,862,283 shares issued)
 135
 135

 Additional paid-in capital
 565,071
 542,714

 Retained earnings
 775,781
 611,287

Treasury stock, at cost

(33,239,209 and 36,295,339 shares) (579,455) (632,732) Accumulated comprehensive income valuations 11,001 1,730

Total shareholders' equity 772,533 523,134

\$2,868,535 \$2,511,959

DAVITA INC.

SUPPLEMENTAL FINANCIAL DATA

(unaudited)

(dollars in millions, except for per share and per treatment data)

Nine months

Three months ended ended
September June 30, September September
30, 2005 2005 30, 2004 30, 2005

Financial Results: Net income, excluding Medicare lab prior years' recoveries, swap

valuations and refinancing charges \$55.6 \$52.6 \$55.3 \$163.6 Basic EPS \$0.55 \$0.52 \$0.56 \$1.63 Diluted EPS \$0.53 \$0.51 \$0.54 \$1.58	
Operating income, excluding Medicare lab prior years' recoveries \$111.2 \$107.7 \$103.4 \$324.9 Operating income margin 16.5% 16.7% 17.6% 16.8%	,
Other comprehensive income Unrealized gain (loss) on securities, net of tax benefit (expense) of \$(7.1), \$5.7, \$1.6, and \$(8.2) \$11.1 \$(9.0) \$(2.5) \$13.0	
Business Metrics: Volume Treatments 2,037,584 1,964,098 1,804,534 5,870,469 Number of treatment days 79.0 78.0 79.0 234.0 Treatments per day 25,792 25,181 22,842 25,087 Per day year over year increase 12.9% 15.2% 11.0% 13.9% Non-acquired growth 5.2% 5.5% 4.8% 5.5%	
Revenue Total operating revenue \$677 \$649 \$596 \$1,936 Medicare lab prior years' recoveries \$1 \$3 \$8 \$4 Total operating revenue, excluding Medicare lab prior years' recoveries \$676 \$646 \$587 \$1,932 Dialysis revenue per treatment \$315.69 \$312.52 \$313.60 \$313.11 Per treatment increase from previous quarter 1.0% 0.5% 0.7% - Per treatment increase from prior year 0.7% 0.3% 2.4% 0.3%	
Expenses A. Patient care costs Percent of revenue 67.8% 67.3% 67.6% 67.5% Per treatment \$224.77 \$221.66 \$219.95 \$222.01 Per treatment increase	

Expenses A. Patient care costs				
Percent of revenue	67.8%	67.3%	67.6%	67.5%
Per treatment	\$224.77	\$221.66	\$219.95	\$222.01
Per treatment increa	se			
from previous quarte	er 1.4%	1.0%	-	-
Per treatment increa	se			
from previous year	2.2%	0.7%	2.7%	1.0%

B.	General	ጴ	administrative
ບ.	acricia	u	administrative

expenses						
Percent of revenue	9.0%	9.3%	8.6%	9.1%		
Per treatment	\$29.85	\$30.48	\$28.04	\$29.80		
Per treatment increase						
(decrease) from						
previous quarter	(2.1%)	5.0%	4.5%	-		
Per treatment increas	se					
from previous year	6.5%	13.6%	14.1%	10.8%		

C. Bad debt expense as a

percent of current-period

revenue 1.8% 1.8% 1.8% 1.8%

D. Consolidated effective

38.0% 39.0% 38.0% tax rate 37.5%

DAVITA INC.

SUPPLEMENTAL FINANCIAL DATA-continued (unaudited)

(dollars in millions, except for per share and per treatment data)

Nine months Three months ended ended

September June 30, September September 30, 2005 2005 30, 2004 30, 2005

Cash Flow Operating cash flow

\$106.2 \$115.9 \$302.2

Operating cash flow,

excluding Medicare

lab prior years'

recoveries and tax

benefit from stock

option exercises \$75.3 \$92.8 \$110.4 \$263.6

Free cash flow, excluding Medicare lab prior years'

recoveries and tax

benefit from stock option

exercises \$78.2 \$99.5 \$231.7 \$65.6

Capital expenditures:

\$24.9 Development \$22.2 \$22.8 \$65.2

Routine maintenance/

IT/other \$11.4 \$18.6 \$11.0 \$37.7

Acquisition expenditures,

net \$46.1 \$81.5 \$213.50 \$130.1

Accounts Receivable

Net receivables \$503 \$490 \$435

DSO 70 70 68

Debt/Capital Structure

Total debt \$1,365 \$1,366 \$1,388 Net debt, net of cash \$1,161 \$1,028 \$1,053

Leverage ratio -

(see Note 1) 1.78x 1.86x 2.14x

Clinical (quarterly averages)

Dialysis adequacy

% of patients with

Kt/V > 1.294% 94% 94%

Patients with arteriovenous

fistula 46% 45% 41%

DAVITA INC.

SUPPLEMENTAL FINANCIAL DATA-continued (unaudited) (dollars in thousands)

Note 1: Calculation of the Leverage Ratio

The leverage ratio under the Company's senior secured credit agreement as in effect for the quarter ended September 30, 2005 (the Prior Credit Agreement), is defined as all funded debt plus the face amount of all letters of credit issued, minus cash and cash equivalents, divided by "EBITDA". The leverage ratio determines the interest rate margin payable by the Company under the Prior Credit Agreement by establishing the margin over the base interest rate (LIBOR) that is applicable. The following Leverage Ratio was calculated using "Consolidated EBITDA" as defined in the indentures governing our recently issued senior notes. Such calculation is on a basis that is materially consistent with the definition of "EBITDA" contained in the Prior Credit Agreement, except that EBITDA under our Prior Credit Agreement is based on the last twelve-months and is not based on annualized EBITDA, and pro forma incremental "EBITDA" relating to acquisitions is included in the calculation of "EBITDA" under the Prior Credit Agreement and is not included in the following calculations.

Three months ended

September 30, June 30, September 30,

2005 2005 2004

Net income \$55.217 \$52.943 \$60.386 Debt expense 24,297 24,897 13.741 32,420 33,180 Income taxes 38,535 Depreciation and amortization 26,372 25,860 22,257

Minority interests and

equity income, net 7.262 6.125 3.593

Swap valuation loss 2,131

"Consolidated EBITDA" as

defined in the indentures \$148,046 \$144,376 \$138.512

Annualized "Consolidated EBITDA" as defined in the

\$592.184 \$554,048 indentures \$577,504

> September 30, June 30, September 30,

2005 2005 2004

Total debt \$1,365,014 \$1,365,867 \$1,387,964 Letters of credit issued 23,959 22,959 22,984 1,388,826 1,388,973 1,410,948

Less: cash and cash

(337,196)(312,761)equivalents (226,942)Consolidated net debt \$1,051,777 \$1,076,065 \$1,184,006

Annualized "Consolidated EBITDA" as defined in the

\$592,184 \$577,504 \$554,048 indentures Leverage Ratio 1.78x 1.86x 2.14x

As a result of the Gambro Healthcare acquisition and our related borrowings under our new senior secured credit agreement, we anticipate that our post-acquisition leverage ratio will initially be in the range of 4.5x to 5.0x, which is in compliance with the leverage ratio covenants contained within the new credit agreement. The leverage ratio calculation in our new credit agreement is materially consistent with our Prior Credit Agreement, existing at September 30, 2005.

DAVITA INC.

RECONCILIATIONS FOR NON-GAAP MEASURES (unaudited)

(dollars in thousands)

1. Net income excluding Medicare lab recoveries related to prior years' services, swap valuations and refinance charges:

Nine months

Three months ended ended September June 30, September September 30, 2005 2005 30, 2004 30, 2005

Net income \$55,217 \$52,943 \$60,386

Less: Medicare lab recoveries

for prior years' services (1,131) (2,641) (8,293) (3,771)Related income tax expense 440 1,027 3,234 1,467

Net income excluding

Medicare lab recoveries 54,526 51,329 55,327 162,190 Swap valuation loss (gain) 1,718 2.131 (4,543)

6.872 Refinancing charges

Related income tax expense (668)(829)(906)\$52,631 \$55,576 \$55,327 \$163,613

2. Operating income, excluding Medicare lab recoveries related to prior years' services:

Nine months

Three months ended ended September June 30, September September

30, 2005 2005 30, 2004 30, 2005

Operating income \$112,338 \$110,315 \$111,652

Less: Medicare lab prior

(1,131) (2,641) (8,293) vears' recoveries (3.771)\$111,207 \$107,674 \$103,359 \$324,878

3. Operating cash flow, excluding Medicare lab recoveries related to prior years' services, and tax benefit from stock option exercises:

Three months ended

September 30, June 30, September 30,

2005 2005 2004

Cash provided by operating

activities \$84.609 \$106.195 \$115.852

Less: Medicare lab prior years'

recoveries (2.641)

Related income tax expense 1,027

Operating cash flow, excluding

Medicare lab prior years'

recoveries 84,609 104,581 115,852

Less: Tax benefit from stock

option exercises (9,313)(11,774)(5,417) Rolling 12-

Nine months month period ended ended

September 30, September 30,

2005 2005

Cash provided by operating

\$302,210 \$389,551 activities

Less: Medicare lab prior years'

Medicare lab prior years'

recoveries (2,641)(10,934)

Related income tax expense 1,027 4.261

Operating cash flow, excluding

Medicare lab prior years'

recoveries 300.596 382.878

Less: Tax benefit from stock

option exercises (37,021)(49,326)

\$263,575 \$333,552

DAVITA INC.

RECONCILIATIONS FOR NON-GAAP MEASURES

(unaudited) (dollars in thousands)

4. Free cash flow and free cash flow, excluding Medicare lab recoveries related to prior years' services, and tax benefit from stock option exercises:

Free cash flow represents net cash provided by operating activities less non-development capital expenditures. We believe free cash flow is a useful adjunct to cash flow from operating activities and other measurements under generally accepted accounting principles in the United States since it is a meaningful measure of our ability to fund acquisition and development activities and meet our debt service requirements. Free cash flow is not a measure of financial performance under generally accepted accounting principles in the United States and should not be considered as an alternative to cash flows from operating, investing or financing activities as an indicator of cash flows or as a measure of liquidity.

Three months ended

September 30, June 30, September 30,

2005 2005

Cash provided by operating

activities \$84,609 \$106,195 \$115,852

Less: Expenditures for routine maintenance and information

(14.614)technology (9.656)(10.956)Free cash flow 74,953 91,581 104,896

Less: Medicare lab prior years'

recoveries (2,641)1,027

Related income tax expense Free cash flow, excluding

Medicare lab prior years'

74.953 recoveries 89,967 104,896

Less: Tax benefit from stock

option exercises (9,313)(11,774)(5,417)\$65,640 \$78,193 \$99,479

Rolling 12-

Nine months month period ended ended September 30, September 30,

2005 2005

Cash provided by operating

\$302.210 activities \$389.551

Less: Expenditures for routine maintenance and information

technology (31,904)(46,787)Free cash flow 270,306 342,764 Less: Medicare lab prior

years' recoveries (2,641) (10,934) Related income tax expense 1,027 4,261

Free cash flow, excluding Medicare lab prior years'

recoveries 268,692 336,091

Less: Tax benefit from stock

option exercises (37,021) (49,326)

\$231,671 \$286,765

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