NATIONAL HEALTHCARE CORP
Form 10-Q
August 06, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10 Q

S QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2008

OR

£ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____________

Commission file number 001 13489

(Exact name of registrant as specified in its Charter)

Delaware	52 2057472
(State or other jurisdiction of	(I.R.S. Employer
incorporation or organization	Identification No.)

100 Vine Street
Murfreesboro, TN

37130
(Address of principal executive offices)

(Zip Code)

(615) 890 2020

Registrant=s telephone number, including area code

Indicate by check mark whether the registrant: (1) Has filed all reports required to be filed by Section 13 or 15(d), of the

Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required

to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes S No. £

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. (as defined in Rule 12b-2 of the Act).
Large accelerated filer £ Accelerated filer T

Non-accelerated filer £ Smaller reporting company £

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as is defined in Rule 12b 2 of the Exchange

Act). Yes £ No S

12,782,905 shares of common stock of the registrant were outstanding as of August 4, 2008.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Statements of Income

(Unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
	(in thousands, except share and per share amounts)			
REVENUES:				
Net patient revenues	$ 143,163	$ 134,031	$ 287,128	$ 267,511
Other revenues	17,399	15,915	33,575	28,939
Net revenues	160,562	149,946	320,703	296,450
COSTS AND EXPENSES:				
Salaries, wages and benefits	86,312	81,539	173,853	160,713
Other operating	44,639	40,933	89,953	82,761
Recovery of notes receivable		(6,195)		(6,195)
Rent	7,876	10,486	15,794	21,009
Depreciation and amortization	6,024	3,828	12,021	7,584
Interest	170	294	389	570
Total costs and expenses	145,021	130,885	292,010	266,442
Income Before Income Taxes	15,541	19,061	28,693	30,008
Income Tax Provision	(6,055)	(7,169)	(11,035)	(11,076)
Net Income	9,486	11,892	17,658	18,932
Dividends to Preferred	2,168		4,336	

Shareholders								
Net income available to common shareholders	$	7,318	$	11,892	$	13,322	$	18,932
Earnings Per Common Share:								
Basic	$	.57	$	.95	$	1.04	$	1.51
Diluted	$	.56	$	.92	$	1.02	$	1.46
Weighted Average Common Shares Outstanding:								
Basic		12,779,58		12,538,104		12,773,63		12,532,200
Diluted		13,125,40		12,994,966		13,121,81		12,993,625

The accompanying notes to interim condensed consolidated financial statements are an integral part of these consolidated statements.

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Balance Sheets

(in thousands)

	June 30 2008 *(unaudited)*	December 31 2007
Assets		
Current Assets:		
Cash and cash equivalents	$ 29,791	$ 2,379
Restricted cash	86,492	72,238
Marketable securities	57,322	56,322
Restricted marketable securities	1,352	1,348
Investment in enhanced cash fund	18,234	35,492
Accounts receivable, less allowance for doubtful		
accounts of $5,203 and $4,381, respectively	66,862	69,606
Notes receivable	189	189
Inventories	6,837	6,654
Prepaid expenses and other assets	2,193	1,786
Total current assets	269,272	246,014
Property and Equipment:		
Property and equipment, at cost	545,960	519,983
Accumulated depreciation and amortization	(148,268)	(135,696)
Net property and equipment	397,692	384,287
Other Assets:		
Deposits	171	88
Deposits reserved for land acquisition		12,361
Goodwill	3,033	3,033
Notes receivable	20,591	18,392
Notes receivable from National		3,903
Deferred income taxes	21,324	21,303
	9,721	9,027

Investments in limited liability companies and other		
Total other assets	54,840	68,107
Total assets	$ 721,804	$ 698,408

The accompanying notes to consolidated financial statements are an integral part of these consolidated statements.

The interim condensed consolidated balance sheet at December 31, 2007 is taken from the audited consolidated financial statements at that date.

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Balance Sheets

(in thousands, except share and per share amounts)

	June 30 2008 *(unaudited)*	December 31 2007
Liabilities and Stockholders Equity		
Current Liabilities:		
Current portion of long-term debt	$ 7,503	$ 7,435
Trade accounts payable	12,700	13,418
Accrued payroll	45,973	46,792
Amounts due to third party payors	12,927	12,339
Accrued risk reserves	96,839	88,382
Deferred income taxes	3,295	3,797
Other current liabilities	15,093	12,110
Dividends payable	5,236	4,506
Accrued interest	618	46
Total current liabilities	200,184	188,825
Long-Term Debt, less Current Portion	10,000	10,000
Other Noncurrent Liabilities	24,173	23,790
Deferred Lease Credits	4,241	4,847
Deferred Revenue	17,056	15,238
Commitments, Contingencies and Guarantees		

Stockholders Equity:				
Series A Convertible Preferred Stock; $.01 par value;				
25,000,000 shares authorized; 10,841,062 shares				
issued and outstanding; stated at liquidation				
of $15.75 per share		170,555		170,555
Common stock, $.01 par value; 30,000,000 shares				
authorized; 12,782,905 and 12,757,907 shares,				
respectively, issued and outstanding		127		127
Capital in excess of par value		105,487		103,221
Retained earnings		171,576		164,003
Unrealized gains on marketable securities, net of taxes		18,405		17,802
Total stockholders equity		466,150		455,708
Total liabilities and stockholders equity	$	721,804	$	698,408

The accompanying notes to consolidated financial statements are an integral part of these consolidated statements.

4

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30	
	2008	2007
Cash Flows From Operating Activities:	*(in thousands)*	
Net income	$ 17,658	$ 18,932
Adjustments to reconcile net income to net cash		
provided by operating activities:		
Depreciation	12,021	7,563
Provision for doubtful accounts receivable	822	817
Amortization of intangibles and deferred charges		21
Amortization of deferred income	(127)	(822)
Equity in earnings of unconsolidated investments	(3,493)	(2,597)
Deferred income taxes	(924)	(12,810)
Stock-based compensation	1,460	1,561
Changes in operating assets and liabilities:		
Increase in restricted cash	(14,254)	(7,150)
Accounts (and other) receivables	1,922	4,925
Inventories	(183)	(99)
Prepaid expenses and other assets	(266)	(1,253)
Trade accounts payable	(718)	(4,652)
Accrued payroll	(819)	(2,327)
Amounts due to third party payors	588	(1,512)
Accrued interest	572	(7)
Other current liabilities and accrued risk reserves	11,440	9,628
Entrance fee deposits	(139)	175
Other noncurrent liabilities	383	9,322
Deferred income	2,084	1,799
Net cash provided by operating activities	28,027	21,514

Cash Flows From Investing Activities:		
Additions to and acquisitions of property and equipment	(14,612)	(8,422)
Decrease in deposits reserved for land acquisition	941	
Investments in notes receivable	(2,746)	
Collections of notes receivable	4,450	6,509
Sale of marketable securities, net		498
Changes in enhanced cash fund balance	17,258	
Distributions from unconsolidated investments	2,677	1,899
Net cash provided by investing activities	7,968	484
Cash Flows From Financing Activities:		
Proceeds from debt	7,500	
Payments on debt	(7,432)	(1,117)
Decrease in minority interests in consolidated subsidiaries	(19)	(10)
Tax benefit from exercise of stock options	314	195
Dividends paid to preferred shareholders	(3,999)	
Dividends paid to common shareholders	(5,356)	(4,503)
Issuance of common shares	492	494
Increase in deposits	(83)	(33)
Net cash used in financing activities	(8,583)	(4,974)
Net Increase in Cash and Cash Equivalents	27,412	17,024
Cash and Cash Equivalents, Beginning of Period	2,379	50,678
Cash and Cash Equivalents, End of Period	$ 29,791	$ 67,702

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Statements of Cash Flows

(continued)

	Six Months Ended June 30	
	2008	2007
(in thousands)		
Supplemental Information:		
Effective January 7, 2008, cash proceeds that were being held by a facilitator pending the completion of an IRC §1031 exchange were disbursed to acquire property and equipment		
Acquisitions of property and equipment	$ (11,420)	$
Deposits reserved for land acquisition	11,420	

The accompanying notes to consolidated financial statements are an integral part of these consolidated statements.

NATIONAL HEALTHCARE CORPORATION

Interim Condensed Consolidated Statements of Stockholders Equity

(in thousands, except share and per share amounts)

(unaudited)

	Preferred Stock		Common Stock		Capital in Excess of Par Value	Retained Earnings	Unrealized Gains (Losses) on Marketable Securities	Total Shareholders Equity
	Shares	Amount	Shares	Amount				
Balance at December 31, 2006		$	12,519,671	$ 125	$ 93,751	$ 129,681	$ 25,585	$ 249,142
Net income						18,932		18,932
Unrealized losses on securities (net of tax benefit of $956)							(1,699)	(1,699)
Total comprehensive income								17,233
Stock option compensation					1,561			1,561
Tax benefit from exercise of stock options					195			195
Shares sold - stock purchase plans (including 10,000 options exercised)			18,656		494			494
Cumulative impact of a change in						900		900

accounting for income tax uncertainties pursuant to FIN 48								
Dividends declared to common shareholders ($0.39 per share)						(4,888)		(4,888)
Balance at June 30, 2007		$	12,538,327	$ 125	$ 96,001	$ 144,625	$ 23,886	$ 264,637
Balance at December 31, 2007	10,841,062	$ 170,555	12,757,907	$ 127	$ 103,221	$ 164,003	$ 17,802	$ 455,708
Net income						17,658		17,658
Unrealized gains on securities (net of tax of $401)							603	603
Total comprehensive income								18,261
Stock option compensation					1,460			1,460
Tax benefit from exercise of stock options					314			314
Shares sold options exercised			24,998		492			492
Dividends declared to preferred shareholders ($0.40 per share)						(4,336)		(4,336)
Dividends declared to common shareholders ($0.45 per						(5,749)		(5,749)

share)													
Balance at June 30, 2008	10,841,062	$	170,555	12,782,905	$	127	$	105,487	$	171,576	$	18,405	$ 466,150

The accompanying notes to consolidated financial statements are an integral part of these consolidated statements.

7

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

Note 1 Consolidated Financial Statements

The unaudited financial statements to which these notes are attached include, in our opinion, all normal, recurring adjustments which are necessary to fairly present the financial position, results of operations and cash flows of National HealthCare Corporation (ANHC@ or the ACompany@). We assume that users of these interim financial statements have read or have access to the audited December 31, 2007 consolidated financial statements and Management=s Discussion and Analysis of Financial Condition and Results of Operations and that the adequacy of additional disclosure needed for a fair presentation, except in regard to material contingencies, may be determined in that context. Accordingly, footnotes and other disclosures which would substantially duplicate the disclosure contained in our most recent annual report to stockholders have been omitted. This interim financial information is not necessarily indicative of the results that may be expected for a full year for a variety of reasons. Our audited December 31, 2007 consolidated financial statements are available at our web site: www.nhccare.com.

Note 2 Other Revenues

Other revenues are outlined in the table below. Revenues from insurance services include premiums for workers compensation and professional liability insurance policies that our wholly-owned limited purpose insurance subsidiaries have written for certain long-term health care centers to which we provide management or accounting services. Revenues from management and accounting services include management and accounting fees and revenues from other services provided to managed and other long-term health care centers. Other revenues include non-health care related earnings.

Other revenues include the following:

	Three Months Ended	Six Months Ended

	June 30		June 30	
	2008	2007	2008	2007
	(in thousands)			
Insurance services	$ 4,184	$ 4,288	$ 8,232	$ 8,060
Management and accounting service fees	5,306	5,053	9,376	8,386
Advisory fees from NHR		125		250
Dividends and other realized gains on securities	1,062	983	2,250	1,898
Equity in earnings of unconsolidated investments	1,954	1,423	3,493	2,598
Interest income	1,403	2,962	2,641	5,547
Rental income	3,061	651	6,730	1,294
Other	429	430	853	906
	$ 17,399	$ 15,915	$ 33,575	$ 28,939

Interest income decreased in 2008 compared to 2007 due primarily to the expenditure of approximately $89,600,000 in cash to complete the merger with National Health Realty, Inc. (NHR) effective on October 31, 2007. Rental income increased in 2008 compared to 2007 due primarily to the acquisition of (1) the real estate of nine leased properties in Florida in the October 31, 2007 merger with NHR (total revenue of $3,609,000) and (2) the fixtures and real estate of a leased 544 bed long term care center and associated 66 unit assisted living facility in Chattanooga, Tennessee in a November 1, 2007 purchase and subsequent lease to a third party operator ($1,200,000).

Certain of our affiliates manage five long-term care centers owned by National Health Corporation (National). During the six months ended June 30, 2008 and 2007, National paid and we recognized no management fees or interest on management fees.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

The unpaid fees from the five centers owned by National, because the amount collectable could not be reasonably determined when the management services were provided, and because we cannot estimate the timing or amount of expected future collections, will be recognized as revenues only when fixed or determinable and collectibility of these fees can be reasonably assured. Under the terms of our management agreement with National, the payment of these fees to us may be subordinated to other expenditures of the five long-term care centers. We continue to manage these centers so that we may be able to collect our fees in the future and because the incremental savings from discontinuing services to a center may be small compared to the potential benefit. We may receive payment for the unrecognized management fees in whole or in part in the future only if cash flows from the operating and investing activities of the five centers are sufficient to pay the fees. There can be no assurance that such future improved cash flows will occur.

Certain of our affiliates manage 18 long-term care centers that were previously owned by National Health Investors, Inc. (NHI). During the six months ended June 30, 2008 and 2007, we recognized $1,506,000 and $1,425,000, respectively, of management fees and interest from these 18 long-term care centers.

Of the total 18 centers managed, the management fee revenues from eight centers were currently paid and recognized on the accrual method in 2008 and 2007. The fees from the remaining ten centers, because of insufficient historical collections and the lack of expected future collections, are recognized only when realized. Under the terms of the management agreements, the payment of these fees to us may be subordinated to other expenditures of each of the long-term care providers. Our affiliates continue to manage these centers so that we may be able to collect our fees in the future and because the incremental savings from discontinuing services to a center may be small compared to the potential benefit. We may receive payment for the unrecognized management fees in whole or in part in the future only if cash flows from operating and investing activities of the centers are sufficient to pay the fees. There can be no assurance that such future improved cash flows will occur.

Note 3 Accounting for Uncertainty in Income Taxes

We believe that our liabilities reflect the anticipated outcome of known uncertain tax positions in conformity with Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48). Our uncertain tax position liabilities are presented in the consolidated balance sheet within Other Noncurrent Liabilities.

NHC continually evaluates for uncertain tax positions. Uncertain tax positions may arise where tax laws may allow for alternative interpretations or where the timing of recognition of income is subject to judgment. We believe we have adequate provisions for uncertain tax positions. However, because of uncertainty of interpretation by various tax authorities and the possibility that there are issues that have not been recognized by management, we cannot guarantee we have accurately estimated our tax liabilities. We believe we have made adequate provision for unrecognized tax benefits related to uncertain tax positions.

On January 1, 2007, we adopted the recognition and disclosure provisions of FIN 48. Under FIN 48, tax positions are evaluated for recognition using a more likely than not threshold, and those tax positions requiring recognition are measured at the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information.

Prior to January 1, 2007, we maintained a liability for the estimated amount of contingent liabilities for income tax matters in accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies (SFAS 5).

In accordance with the adoption of FIN 48, the Company has established a liability for unrecognized tax benefits, which are differences between a tax position taken or expected to be taken in a tax return and the benefit recognized and measured pursuant to this Interpretation. Generally a liability is created for an unrecognized tax benefit because it represents a company s potential future obligation to a taxing authority for a tax position that was not recognized per above.

As a result of adopting FIN 48, we reported a $900,000 increase to our January 1, 2007, balance of retained earnings and a decrease in our accruals for uncertain tax positions and related interest and penalties of a corresponding amount. On January 1, 2007, we had $21,051,000 of unrecognized tax benefits, composed of $11,409,000 of deferred tax assets, $ 0 of deferred tax liabilities, $4,117,000 of permanent differences, and $5,525,000 of accrued interest and penalties payable.

At June 30, 2008, we had $24,173,000 of unrecognized tax benefits, composed of $13,627,000 of deferred tax assets, $-0- of deferred tax liabilities, $4,595,000 of permanent differences, and $5,951,000 of accrued interest and penalties. Unrecognized tax benefits of $6,489,000 (including $1,894,000 of accrued interest and penalties) at June 30, 2008, attributable to permanent differences, would favorably impact our effective tax rate if recognized. We do not expect to recognize significant increases or decreases in unrecognized tax benefits within twelve months of June 30, 2008, except for the effect of decreases related to statute of limitations lapse estimated at $6,282,000, composed of temporary differences of $2,101,000, permanent tax differences of $2,137,000 and interest and penalties of $2,044,000.

Interest and penalties expense related to U.S. federal and state income tax returns are included within income tax expense.

The Company is no longer subject to U.S. federal and state examinations by tax authorities for years before 2004. Currently, there are no U.S. federal or state returns under examination.

Note 4 Earnings per Share

Basic earnings per share is based on the weighted average number of common shares outstanding during the period.

Diluted earnings per share assume the exercise of options using the treasury stock method and the conversion of the Series A Convertible Preferred Stock using the if converted method, to the extent dilutive.

The following table summarizes the earnings and the weighted average number of common shares used in the calculation of basic and diluted earnings per share.

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Basic:				
Weighted average common shares outstanding	12,779,582	12,538,104	12,773,639	12,532,200
Net income	$ 9,486,000	$ 11,892,000	$ 17,658,000	$ 18,932,000
Dividends to preferred stockholders	2,168,000		4,336,000	
Net income available to common stockholders	7,318,000	11,892,000	13,322,000	18,932,000
Earnings per common share, basic	$ .57	$ .95	$ 1.04	$ 1.51
Diluted:				
Weighted average common shares outstanding	12,779,582	12,538,104	12,773,639	12,532,200
Dilutive effect of stock options	345,820	456,862	348,171	461,425
Assumed average common shares outstanding	13,125,402	12,994,966	13,121,810	12,993,625
Net income	$ 7,318,000	$ 11,892,000	$ 13,322,000	$ 18,932,000
Earnings per common share, diluted	$ .56	$ .92	$ 1.02	$ 1.46

Excluded in the above table are 244,043 shares of stock options and 2,623,971 preferred stock potential common shares issuable upon the conversion of the preferred stock due to their anti-dilutive impact.

Note 5 Investment in Enhanced Cash Fund

At June 30, 2008, we reported in current assets in our Consolidated Balance Sheets an investment of $18,234,000 in the Columbia Strategic Cash Portfolio Fund (the Fund). The Fund invests in obligations denominated in U.S. dollars consisting of asset backed securities, corporate bonds and notes, certificates of deposit, short-term corporate debt obligations, commercial paper, extendible commercial notes, and municipal bonds.

We received notice on December 6, 2007 at a time when our carrying value in the Fund was $39,500,000, that the Fund cash redemptions were suspended and that the Fund would begin an orderly liquidation and dissolution of its assets for distribution to the Fund holders, including to NHC. Activity in the Fund may be summarized as follows:

	Three Months Ended June 30	Six Months Ended June 30

	2008	2007	2008	2007
Fund balance, beginning of period	$ 23,116	$	$ 35,492	$
Realized gains (losses)	12		(161)	
Reduction to adjust the Fund balance to its net asset value and charged to earnings			(259)	
Cash distributed to NHC	(4,894)		(16,838)	
Fund balance, end of period	$ 18,234	$	$ 18,234	$

Not included in the periods shown above, in December 2007, we reported realized losses of $42,000, reductions to adjust the Fund to its net asset value of $453,000 and cash distributed from the fund to NHC of $3,513,000.

The Fund s valuation fluctuates based on changes in the market values of the securities held by the Fund. In addition to the transaction gains or losses reported by the Fund to us, since December, 2007 we have adjusted our carrying value to the Fund s net asset value, which adjustments have required us to charge earnings and reduce our carrying value in the Fund. Because the Fund is invested in financial instruments with exposure to the current turmoil in the credit markets in the United States, we consider the write-down amount to be an other-than-temporary impairment. It is difficult to predict the timing or magnitude of these other-than-temporary impairments and additional impairments may occur. Under such circumstances, our earnings will be negatively affected.

As to balance sheet classification, prior to December 6, 2007, we classified the investment as a cash equivalent in the Consolidated Balance Sheets because the funds were immediately available for distribution. Since the suspension by the Fund manager of Fund redemptions, we no longer consider the investment in the Fund to be a cash equivalent and classify it instead as Investments in Enhanced Cash Fund. We have classified the Fund as a current asset because we believe that the Fund will be substantially liquidated during the next twelve months.

Note 6 - Purchases of Property

On January 2, 2008 we purchased a 109-bed skilled nursing and rehabilitation facility from the St. Mary s Health System for $6,347,000 in cash. Holston Health and Rehabilitation Center is located in Knoxville, Tennessee.

June 30, 2008

(unaudited)

In January, 2008, we purchased for $5,073,000 in cash two tracts of land located in the state of South Carolina and one tract of land located in Tennessee. The tracts were undeveloped and are held for future development.

Note 7 - Long-Term Debt and Commitments

Long-Term Debt

Long-term debt consists of the following:

	Weighted Average Interest Rate	Maturities	Long-Term Debt 6/30/08	Long-Term Debt 12/31/07
(dollars in thousands)				
Term loan, interest payable monthly	Repaid	–	$ –	$ 7,050
Revolving Credit Facility	Variable, 2.7%	2008	7,500	–
Senior notes, secured, principal and interest payable quarterly	Repaid	–	–	382
Notes and other obligations, principal and interest payable periodically	Variable, 12%	2008	3	3

Unsecured term note payable to National, interest payable quarterly, principal payable at maturity	Variable, 4.2%	2018	10,000	10,000
			17,503	17,435
Less current portion			(7,503)	(7,435)
			$ 10,000	$ 10,000

Our Credit Facility is available for general corporate purposes, including working capital and acquisitions. At June 30, 2008, $7,500,000 was borrowed under the Credit Facility primarily to repay our term loan ($7,050,000). The Credit Facility provides for a $75,000,000 line of credit which matures on October 27, 2008.

Note 8 Stock Option Plans

Our shareholders approved the 2005 Stock Option, Employee Stock Purchase, Physician Stock Purchase and Stock Appreciation Rights Plan (the APlan@) which provides for the grant of stock options to key employees, directors and non employee consultants. Under the Plan, the Compensation Committee of the Board of Directors (Athe Committee@) has the authority to select the participants to be granted options; to designate whether the option granted is an incentive stock option (AISO@), a non qualified option, or a stock appreciation right; to establish the number of shares of common stock that may be issued upon exercise of the option; to establish the vesting provision for any award; and to establish the term any award may be outstanding. The exercise price of any ISO=s granted will not be less than 100% of the fair market value of the shares of common stock on the date granted and the term of an ISO may not be any more than ten years. The exercise price of any non qualified options granted will not be less than 100% of the fair market value of the shares of common stock on the date granted unless so determined by the Committee.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

Under the Plan, options issued to non employee directors are granted automatically on the date of our annual shareholder meeting, vest immediately upon grant and have a maximum five year term. Options issued to employees in 2000 vested over a six year period and had a maximum six year term. Options issued to employees in 2004 vest over a five year period and have a maximum five year term. Options issued to employees in 2007 vest over a 2.1 year period and have a maximum 2.1 year term.

Effective January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004), AShare Based Payment@ (ASFAS 123(R)@), using the modified prospective application transition method. Under this method, compensation cost is recognized, beginning January 1, 2006, based on the requirements of SFAS 123(R) for all share based payments granted after the effective date, and based on Statement of Financial Accounting Standards No. 123, AAccounting for Stock Based Compensation (ASFAS 123@), for all awards granted to employees prior to January 1, 2006 that remain unvested on the effective date. Prior to January 1, 2006, we applied Accounting Principles Board Opinion No. 25, AAccounting for Stock Issued to Employees@ (AAPB 25@) and related interpretations in accounting for our employee stock benefit plans. Accordingly, no compensation cost was recognized for stock options granted under the plans because the exercise prices for options granted were equal to the quoted market prices on the option grant dates and all option grants were to employees or directors. Results for prior periods have not been restated.

The fair value of each option award is estimated on the grant date, using the Black Scholes option valuation model with the weighted average assumptions indicated in the following table. Generally, awards are subject to cliff vesting. Each grant is valued as a single award with an expected term based upon expected participants and termination behavior. Compensation cost is recognized over the requisite service period in a manner consistent with the option vesting provisions. The straight line attribution method requires that compensation expense is recognized at least equal to the portion of the grant date fair value that is vested at that date. The expected volatility is derived using weekly historical data for periods immediately preceding the date of grant. The risk free interest rate is the approximate yield on the United States Treasury Strips having a life equal to the expected option life on the date of grant. The expected life is an estimate of the number of years an option will be held before it is exercised. The following table summarizes the assumptions used to value the options granted in the periods shown.

Six Months Ended

	June 30	
	2008	2007
Risk-free interest rate	2.60%	4.64%
Expected volatility	25.5%	27.9%
Expected life, in years	2.0 years	2.1 years
Expected dividend yield	2.36%	1.92%
Expected forfeiture rate	0.00%	0.00%

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

The following table summarizes option activity:

	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value
Options outstanding at December 31, 2005	1,431,000	$ 21.72	–
Options granted	122,394	42.33	–
Options exercised	(239,174)	24.33	–
Shares cancelled	(22,901)	38.13	–
Options forfeited	(2,140)	37.00	–
Options outstanding at December 31, 2006	1,289,179	23.13	–
Options granted	161,748	53.67	–
Options exercised	(229,480)	24.95	–
Options forfeited	(1,797)	55.45	–
Options cancelled	(53,000)	20.90	–
Options outstanding at December 31, 2007	1,166,650	27.06	–
Options granted	112,586	51.39	–
Options forfeited	(1,543)	50.94	–
Options exercised	(24,898)	19.60	–
Options outstanding at June 30, 2008	1,252,795	$ 29.36	$ 20,629,000
Options exercisable at June 30, 2008	380,000	$ 43.10	$ 1,037,000

Options Outstanding June 30, 2008	Exercise Prices	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life in Years

858,752	$20.90 to $27.01	$21.27	0.8
394,043	$32.01 to $55.00	$47.00	3.0
1,252,795			

At June 30, 2008, 380,000 options outstanding are exercisable. Exercise prices on the options range from $20.90 to $55.00. The weighted average remaining contractual life of options outstanding at June 30, 2008 is 1.5 years The weighted average fair value of options granted during the six months ended June 30, 2008 and 2007 were $7.36 ($829,000) and $9.47 ($1,532,000) per share, respectively. The total intrinsic value of shares exercised during the six months ended June 30, 2008 and 2007 was $653,000 and $343,500, respectively.

Additionally, we have an employee stock purchase plan that allows employees to purchase our shares of stock through payroll deductions. The plan allows employees to terminate participation at any time.

Our policy is to issue new shares to satisfy share option exercises. In May 2005, our shareholders approved the 2005 National HealthCare Corporation Stock Option, Employee Stock Purchase, Physician Stock Purchase and Stock Appreciation Rights Plan. We have reserved 940,889 shares of common stock for issuance under these plans.

NHC recognized $1,460,000 and $1,561,000 of share-based compensation expense for the six month periods ended June 30, 2008 and 2007, respectively. SFAS 123(R) requires that the benefits of tax deductions in excess of amounts recognized as compensation cost be reported as a financing cash flow, rather than an operating cash flow, as required under prior accounting guidance. Tax deductions in excess of amounts recognized as compensation costs totaled $314,000 and $195,000 for the six months ended June 30, 2008 and 2007, respectively. No share based compensation cost was capitalized during the current periods. The total compensation cost related to non vested awards not yet recognized at June 30, 2008 is $1,039,000 and the weighted average period over which it is to be recognized is 1.5 years.

Note 9 Guarantees and Contingencies

Accrued Risk Reserves

We are self insured for risks related to health insurance and have wholly-owned limited purpose insurance companies that insure risks related to workers compensation and general and professional liability insurance claims both for our owned or leased entities and certain of the entities to which we provide management or accounting services. The liability we have recognized for reported claims and estimates for incurred but unreported claims totals $96,839,000 and $88,382,000 at June 30, 2008 and December 31, 2007, respectively. This liability is classified as current based on the uncertainty regarding the timing of potential payments. The liability is included in accrued risk reserves in the consolidated balance sheets. The amounts are subject to adjustment for actual claims incurred. It is possible that these claims plus unasserted claims could exceed our insurance coverages and our reserves, which would have a material adverse effect on our financial position, results of operations and cash flows.

As a result of the terms of our insurance policies and our use of wholly-owned limited purpose insurance companies, we have retained significant insurance risk with respect to workers compensation and general and professional liability. We use independent actuaries to estimate our exposures for claims obligations (for both asserted and unasserted claims) related to deductibles and exposures in excess of coverage limits, and we maintain reserves for these obligations. Such estimates are based on many variables including historical and statistical information and other factors. It is possible that claims against us could exceed our coverage limits and our reserves, which would have a material adverse effect on our financial position, results of operations and cash flows.

Workers Compensation

For workers compensation, we utilize a wholly-owned Tennessee domiciled property/casualty insurance company to write coverage for NHC affiliates and for third-party customers. Policies are written for a duration of twelve months and cover only risks related to workers compensation losses. All customers are companies which operate in the long-term care industry. Business is written on a direct basis. Direct business coverage is written for statutory limits and the insurance company s losses in excess of $1,000,000 per claim up to $10,000,000 are covered by reinsurance.

For these workers compensation insurance operations, the premium revenues reflected in the consolidated financial statements within Other Revenues for 2008 and 2007, respectively, are $3,062,000 and $3,722,000. Associated losses and expenses are reflected in the consolidated financial statements as Other operating costs and expenses .

General and Professional Liability Lawsuits and Insurance

Across the nation, the entire long term care industry has experienced significant amounts of personal injury/wrongful death claims and awards based on alleged negligence by nursing facilities and their employees in providing care to residents. As of June 30, 2008, we and/or our managed centers are currently defendants in 67 such claims covering the years 1996 through June 30, 2008. Eleven of the 67 suits are in Florida, where we have not operated or managed long-term care providers since September 30, 2000. Of the eleven Florida suits, four suits relate to events before and seven suits relate to events after our cessation of business in Florida. These latter seven suits assert allegations of continued exposure even after we ceased operations.

When bids were solicited for third party professional liability insurance coverage for 2002, only two companies would quote coverage. Both quotations were so onerous and expensive that we elected to pay the premiums into a wholly-owned licensed captive insurance company, incorporated in the Cayman Islands, for the purpose of managing the Company s losses related to these risks. Thus, for years 2002-2008, insurance coverage for incidents occurring at all providers owned or leased, and most providers managed by us, is provided through this wholly-owned insurance company. Policies are written for a duration of twelve months.

Our coverages for all years include both primary policies and excess policies. Commencing with 2002, deductibles were eliminated with first dollar coverage being provided through the wholly-owned insurance company. The excess coverage is provided by a third party insuror for 2002.

For the period 2003-2008, both primary and excess professional liability insurance coverage is provided through our wholly-owned liability insurance company. Primary coverage is in the amount of $1 million per incident, $3 million per location subject to an annual primary aggregate limit. That limit is $16 million for 2008. Excess coverage under a $7.5 million annual excess aggregate policy is applicable to years 2003-2007. The 2008 year is subject to annual excess aggregate policies in the total amount of $29 million.

For these professional liability insurance operations, the premium revenues reflected in the financials within Other revenues for the quarters ended June 30, 2008 and 2007, respectively, are $2,008,000 and $1,733,000. Associated losses and expenses including those for self-insurance are included in the consolidated financial statements as Other operating costs and expenses .

Debt Guarantees

In addition to our primary debt obligations, which are included in our consolidated financial statements, we have guaranteed certain of the debt obligations of National and the ESOP. This guarantee, which is not included as debt obligations in our consolidated financial statements, totals $1,030,000 at June 30, 2008.

The $1,030,000 of guarantees of debt of National and the ESOP relates to senior secured notes held by financial institutions. The total outstanding balance of National and the ESOP s obligations under these senior secured notes is $1,030,000. None of this obligation has been included in our debt obligations because we are not a direct obligor on this indebtedness. The $1,030,000, which is not included in our debt obligations because we are not a direct obligor, is due from NHI to National and the ESOP.

The $1,030,000 guarantee described above has cross-default provisions with other debt of National and the ESOP. We currently believe that National and the ESOP are in compliance with the terms of their debt agreements.

As of June 30, 2008, our maximum potential loss related to debt guarantees and financial guarantees is $1,030,000.

Note 10 - Fair Value Measurements

As described in Note 11, we adopted the provisions of SFAS No. 157, Fair Value Measurements (SFAS 157) as of January 1, 2008 for financial assets and financial liabilities. SFAS 157 is a technical standard which defines fair value, establishes a consistent framework for measuring fair value, and expands disclosures for each major asset and liability category measured at fair value on either a recurring or nonrecurring basis. SFAS 157 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. Valuation techniques are the market, cost or income approach.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

As a basis for considering such assumptions, SFAS 157 establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows: Level 1 quoted prices for identical assets or liabilities in active markets, Level 2 quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and model-based valuations in which significant inputs are corroborated by observable market data and Level 3 valuation techniques in which significant inputs are unobservable.

Financial assets and financial liabilities measured at fair value on a recurring basis during the period are as follows (in thousands):

	Fair Value At June 30, 2008	Quoted Prices in Active Markets For Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Valuation Technique
Marketable securities	$ 57,322	$ 57,322	$	Market
Restricted marketable securities	1,352	1,352		Market
Investment in enhanced cash fund	18,234		18,234	Market

Note 11 New Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements . This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. The new FASB rule does not supersede all applications of fair value in other pronouncements, but creates a fair value hierarchy and prioritizes the inputs to valuation techniques for use in most pronouncements. It requires companies to assess the significance of an input to the fair value measurement in its entirety. Statement 157 also requires companies to disclose information to enable users of financial statements to assess the inputs used to develop the fair value measurements. SFAS 157 is effective for fiscal periods beginning after November 15, 2007 and interim periods within those fiscal years, with the following exception. FASB Staff Position (FSP) FAS 157-2, Effective Date of FASB Statement No. 157, defers the effective date to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years, for all nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The implementation of FAS 157, for financial assets and financial liabilities, did not have a material impact on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115 . This Statement amends FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities , with respect to accounting for a transfer to the trading category for all entities with available-for-sale and trading securities electing the fair value option. This statement allows companies to elect fair value accounting for many financial instruments and other items that currently are not required to be accounted as such, allows different applications for electing the option for a single item or groups of items, and requires disclosures to facilitate comparisons of similar assets and liabilities that are accounted for differently in relation to the fair value option. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The implementation of FAS 159 did not have a material impact on the Company s consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations* which replaces SFAS No. 141, *Business Combinations*. This Statement establishes principles and requirements for how the acquirer (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. This Statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company will adopt this standard at the beginning of the Company s fiscal year ending December 31, 2009 for all prospective business acquisitions. The Company has not determined the effect that the adoption of SFAS 141(R)

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

will have on its consolidated financial statements, but the impact will be limited to any future acquisitions beginning in fiscal year 2009.

In December 2007, the FASB issued SFAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51.* This Statement requires all entities to report noncontrolling interests in subsidiaries as equity in the consolidated financial statements. This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The Company will adopt this Statement effective January 1, 2009. The Company has not determined the effect that the adoption of SFAS No. 160 will have on its consolidated results of operations or financial position.

In May 2008, the FASB issued Statement of Financial Accounting Standards No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS No. 162). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP in the United States (the GAAP hierarchy). The current GAAP hierarchy is set forth in the AICPA Statement on Auditing Standards No. 69, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles (SAS No. 69). The FASB believes the GAAP hierarchy should be directed to entities because it is the entity (not its auditor) that is responsible for selecting accounting principles for financial statements that are presented in conformity with GAAP. Accordingly, the FASB concluded that the GAAP hierarchy should reside in the accounting literature established by the FASB and has issued SFAS No. 162 to achieve that result. SFAS No. 162 is effective 60 days following the SEC s approval of the Public Accounting Oversight Board amendments to SAS No. 69. We do not expect the adoption of SFAS No. 162 to have an impact on our consolidated financial position, results of operations, or cash flows.

Note 12 Subsequent Event

On August 1, 2008, we purchased a 132-bed skilled nursing and rehabilitation facility and a 60-bed assisted living facility for $13,757,000 in cash. These health care facilities are located in Charleston, South Carolina.

Item 2.

Management's Discussion and Analysis of Financial Condition and Results of Operations.

Overview

National HealthCare Corporation (ANHC@ or the ACompany@) is a leading provider of long term health care services. We operate or manage, through certain affiliates, 75 long term health care centers with 9,642 beds in 10 states and provide other services in two additional states. These operations are provided by separately funded and maintained subsidiaries. We provide long term health care services to patients in a variety of settings including long term nursing centers, managed care specialty units, sub acute care units, Alzheimer's care units, hospice programs, homecare programs, assisted living centers and independent living centers. In addition, we provide management and accounting services to owners of long term health care centers.

Summary of Goals and Areas of Focus

Earnings To monitor our earnings, we have developed budgets and management reports to monitor labor, census, and the composition of revenues. Inflationary increases in our costs may cause net earnings from patient services to decline.

Development and Growth - During the first quarter of 2007, we placed in service 60 bed additions to existing long term care facilities located in Garden City and Columbia, South Carolina. We expect to complete construction in the summer of 2008 of a 60 bed addition to an existing facility located in North Augusta, South Carolina (expected cost

$6,403,000). We expect to break ground in the summer of 2008 for construction of a new 120 bed health care center in Bluffton, South Carolina and a new assisted living facility in Parklane, South Carolina (expected cost of $21,657,000).

In January, 2008, we purchased a 109-bed skilled nursing rehabilitation facility from the St. Mary s Health System for $6,437,000 in cash. Holston Health and Rehabilitation Center is located in Knoxville, Tennessee.

Also in January 2008, we purchased for $5,073,000 two tracts of land located in the state of South Carolina and one tract of land located in the state of Tennessee. The tracts are undeveloped and are held for future development.

Effective February 1, 2008, we were selected by the McKendree Village, Inc. to manage under a five-year contract McKendree Village, a continuing care retirement community located on 42 acres in the Nashville, Tennessee suburb of Hermitage. McKendree Village offers nursing care in the 300-bed McKendree Health Center, assisted living services in the 85-unit McKendree Manor, and independent senior care living in a 234-unit residential tower and in 30 individually designed cottages.

In 2008, we are continuing to develop an active hospice program in South Carolina independently of our partnership with Caris Healthcare and are also exploring opportunities to expand our home health care services. Also during 2008, we will apply for Certificates of Need for additional beds in our markets and also evaluate the feasibility of expansion into new markets by building private pay health care centers or by the purchase of existing health care centers.

Accrued Risk Reserves   Our accrued professional liability reserves, workers= compensation reserves and health insurance reserves totaled $96,839,000 at June 30, 2008 and are a primary area of management focus. We have set aside restricted cash to fund substantially all of our professional liability and workers= compensation reserves.

As to exposure for professional liability claims, we have developed for our centers performance certification criteria to measure and bring focus to the patient care issues most likely to produce professional liability exposure, including in house acquired pressure ulcers, significant weight loss and numbers of falls. These programs for certification, which we regularly modify and improve, have produced measurable improvements in reducing these incidents. Our experience is that achieving goals in these patient care areas improves both patient and employee satisfaction. Furthermore, we are continuing efforts to identify and restructure the ownership or management of our higher risk operations and locations to eliminate NHC liability exposure.

Application of Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and cause our reported net income to vary significantly from period to period.

Our critical accounting policies that are both important to the portrayal of our financial condition and results and require our most difficult, subjective or complex judgments are as follows:

Revenue Recognition Third Party Payors Approximately 60% (2007), 63% (2006), and 63% (2005) of our net revenues are derived from Medicare, Medicaid, and other government programs. Amounts earned under these programs are subject to review by the Medicare and Medicaid intermediaries. In our opinion, adequate provision has been made for any adjustments that may result from these reviews. Any differences between our estimates of settlements and final determinations are reflected in operations in the year finalized. At June 30, 2008, we have made provisions of approximately $13,157,000 for other various Medicare and Medicaid issues for current and prior year cost reports. Consistent with our revenue recognition policies, we will record revenues associated with the various issues when the approvals, including the final cost report audits, are assured. Revenues for such cost report adjustments in the three and six months ended June 30, 2008 and 2007 were not significant.

Revenue Recognition Private Pay For private pay patients in skilled nursing or assisted living facilities, we bill room and board in advance for the current month with payment being due upon receipt of the statement in the month the services are performed. Charges for ancillary, pharmacy, therapy and other services to private patients are billed in the month following the performance of services. All billings are recognized as revenue when the services are performed.

Valuations and Impairments to our Investment in Enhanced Cash Fund At June 30, 2008, we reported an aggregate investment of $18,234,000 in the Columbia Strategic Cash Portfolio Fund (the Fund) which invests principally in high quality corporate debt, mortgage-backed securities and asset-backed securities. During December, 2007 the Fund s manager notified us that due to turmoil in credit markets in the United States (1) Fund cash redemptions to investors were suspended, (2) the Fund s valuation will be based on the market value of the underlying securities instead of amortized cost, (3) interest would continue to accrue and be paid and (4) the Fund would begin an orderly liquidation and dissolution of its assets for distribution to the Fund holders that is expected to be completed in early 2009. As the Fund is liquidated, we expect to receive our pro rata share of the Fund in cash distributions.

The Fund s valuation fluctuates based on changes in the market values of the securities held by the Fund. In addition to any transaction gains or losses reported by the Fund to us, since December, 2007 we have adjusted our carrying value to the Fund s net asset value, which adjustments have required us to charge earnings and reduce our carrying value in the Fund by a total of $712,000, of which amount $453,000 was expensed in the fourth quarter of 2007 and $259,000 in the first quarter of 2008. We will continue to evaluate our investment in the Fund for other-than-temporary impairments. It is possible that future events could require us to make significant adjustments or revisions to our estimates of the Fund value.

Accrued Risk Reserves We are principally self insured for risks related to employee health insurance, workers= compensation and professional and general liability claims. Our accrued risk reserves primarily represent the accrual for self insured risks associated with employee health insurance, workers= compensation and professional and general liability claims. The accrued risk reserves include a liability for reported claims and estimates for incurred but unreported claims. Our policy with respect to a significant portion of our workers= compensation and professional and general liability claims is to use an actuary to support the estimates recorded for incurred but unreported claims. Our health insurance reserve is based on our known claims incurred and an estimate of incurred but unreported claims determined by our analysis of historical claims paid. We reassess our accrued risk reserves on a quarterly basis.

Professional liability remains an area of particular concern to us. The entire long term care industry has seen personal injury/wrongful death claims based on alleged negligence by nursing homes and their employees in providing care to residents. As of June 30, 2008, we and/or our managed centers are defendants in 67 such claims inclusive of years 1996 through 2008. It remains possible that these pending matters plus potential unasserted claims could exceed our reserves, which would have a material adverse effect on our financial position, results of operations and cash flows. It is also possible that future events could cause us to make significant adjustments or revisions to these reserve estimates and cause our reported net income to vary significantly from period to period.

We maintain insurance coverage for incidents occurring in all provider locations owned, leased or managed by us. The coverages include both primary policies and umbrella policies.

For 2002, we maintain primary coverage through our own insurance company with excess coverage provided by a third party insurance company. For 2003 2008, we maintain both primary and excess coverage through our own insurance subsidiary. In all years, settlements, if any, in excess of available insurance policy limits and our own reserves would be expensed by us.

Revenue Recognition Subordination of Fees and Uncertain Collections We provide management services to certain long term care facilities and to others we provide accounting and financial services. We generally charge 6% of net revenues for our management services and a predetermined fixed rate per bed for the accounting and financial services. Our policy is to recognize revenues associated with both management services and accounting and financial services on an accrual basis as the services are provided. However, under the terms of our management contracts, payments for our management services are subject to subordination to other expenditures of the long term care center being managed. Furthermore, there are certain of the third parties with whom we have contracted to provide services and which we have determined, based on insufficient historical collections and the lack of expected future collections, that collection is not reasonably assured and our policy is to recognize income only in the period in which the amounts are realized. We recognize the expenses related to the provision of those services in the period in which they are incurred. We may receive payment for the unpaid and unrecognized management fees in whole or in part in the future only if cash flows from the operating and investing activities of the centers are sufficient to pay the fees. There can be no assurance that such future cash flows will occur. The realization of such previously unrecognized revenue could cause our reported net income to vary significantly from period to period.

We agree to subordinate our fees to the other expenses of a managed center because we believe we know how to improve the quality of patient services and finances of a long term care center and because subordinating our fees demonstrates to the owner and employees of the managed center how confident we are of the impact we can have in making the center operations successful. We may continue to provide services to certain managed centers despite not being fully paid currently so that we may be able to collect unpaid fees in the future from improved operating results and because the incremental savings from discontinuing services to a center may be small compared to the potential benefit. Also, we may benefit from providing other ancillary services to the managed center. We may receive payment for the unrecognized management fees in whole or in part in the future only if cash flows from the operating and investment activities of the centers are sufficient to pay the fees. There can be no assurance that such future cash flows will occur.

Certain of our accounts receivable from private paying patients and certain of our notes receivable are subject to credit losses. We have attempted to reserve for expected accounts receivable credit losses based on our past experience with similar accounts receivable and believe our reserves to be adequate.

We continually monitor and evaluate the carrying amount of our notes receivable in accordance with Statement of Financial Accounting Standards No. 114, AAccounting by Creditors for Impairment of a Loan An Amendment of FASB Statements No. 5 and 15.@ It is possible, however, that the accuracy of our estimation process could be materially impacted as the composition of the receivables changes over time. We continually review and refine our estimation process to make it as reactive to these changes as possible. However, we cannot guarantee that we will be able to accurately estimate credit losses on these balances. It is possible that future events could cause us to make significant adjustments or revisions to these estimates and cause our reported net income to vary significantly from period to period.

Potential Recognition of Deferred Income - During 1988, we sold the assets of eight long-term health care centers to National Health Corporation (ANational@), our administrative general partner at the time of the sale. The resulting profit of $15,745,000 was deferred. $10,000,000 of the deferred gain and related deferred income taxes of $4,000,000 was recognized as income in December, 2007 with the collection of the $10,000,000 note from National. $3,745,000 of the deferred gain has been amortized into income on a straight-line basis over the 20-year management contract period. Additional deferred income of $2,000,000 will be reported when the Company no longer has an obligation to advance the $2,000,000 working capital loan which obligation was extended until January 20, 2018 with the extension of the management agreement with National to that date.

Guarantees We guarantee certain debt of National and the ESOP ($1,030,000). It is possible that future events could cause us to make significant adjustments to our estimates and liability under this guarantee and cause our reported net income to vary from period to period.

Uncertain Tax Positions NHC continually evaluates for uncertain tax positions. These uncertain positions may arise where tax laws may allow for alternative interpretations or where the timing of recognition of income is subject to judgment. We believe we have adequate provisions for our uncertain tax positions including related penalties and interest.

However, because of uncertainty of interpretation by various tax authorities and the possibility that there are issues that have not been recognized by management, we cannot guarantee we have accurately estimated our tax liabilities.

The above listing is not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles, with no need for management=s judgment in their application. There are also areas in which management=s judgment in selecting any available alternative would not produce a materially different result. See our audited consolidated financial statements and notes thereto which contain accounting policies and other disclosures required by generally accepted accounting principles.

Government Program Financial Changes

Cost containment will continue to be a priority for Federal and State governments for health care services, including the types of services we provide. Government reimbursement programs such as Medicare and Medicaid prescribe, by law, the billing methods and amounts that health care providers may charge and be reimbursed to care for patients covered by these programs. Congress has passed a number of laws that have effected major changes in the Medicare and Medicaid programs. The Balanced Budget Act of 1997, or the Budget Act, sought to achieve a balanced federal budget by, among other things, reducing federal spending on Medicare and Medicaid to various providers. In February 2006, Congress enacted the Deficit Reduction Act, or DRA, which reduced net Medicare and Medicaid spending, and in December 2006, Congress passed the Tax Relief and Health Care Act of 2006, which also affects payments under the Medicare and Medicaid programs. In the Tax Relief and Health Care Act of 2006, Congress reduced the limit on Medicaid provider taxes for the period January 1, 2008 through September 30, 2011 from the 6 percent set by CMS regulations to a 5.5 percent limit set by statute.

Medicare

Effective October 1, 2007, our PPS rates were increased by 5.5% due to inflation update (3.3%) and Care Based Statistical Area (CBSA) designations. We estimate that the positive revenue effect of the Centers for Medicare and Medicaid Services (CMS) final rule was $2,535,000 for the first six months of 2008. The inflation update (or market basket increase) was 3.1% in 2006 and 3.3% in 2007.

For the first six months of 2008 our average Medicare per diem increased by 3.62% over the same period of 2007. No assurances can be given as to whether Congress will increase or decrease reimbursement in the future, the timing of any action or the form of relief, if any, that may be enacted.

Medicaid

Tennessee annual Medicaid rate increases were implemented effective July 1, 2007. The increase in revenue was approximately $533,000 per quarter. Minimum wage pass through impact was $318,000 per quarter.

Missouri Medicaid funded a global rate increase for all providers of $3.00 per day effective for February 1, 2007 through June 30, 2007. Effective July 1, 2007, an additional $6.00 per day increase was funded. The combined effect of the eleven months in rate increases was approximately $1,275,000 in 2007. The first six months of 2008 effect was approximately $695,000.

South Carolina Medicaid annual per diem rate increases that were implemented on October 1, 2007 have resulted in additional revenues of approximately $251,000 per quarter.

For the first six months of 2008 our average Medicaid per diem increased by 3.96% over the same period in 2007. We face challenges with respect to states Medicaid payments, because many currently do not cover the total costs incurred in providing care to those patients. States will continue to control Medicaid expenditures but also look for adequate funding sources, including provider assessments. The DRA includes several provisions designed to reduce

Medicaid spending. These provisions include, among others, provisions strengthening the Medicaid asset transfer restrictions for persons seeking to qualify for Medicaid long-term care coverage, which could, due to the timing of the penalty period, increase facilities exposure to uncompensated care. Other provisions could increase state funding for home and community-based services, potentially having an impact on funding for nursing facilities. There is no assurance that the funding for our services will increase or decrease in the future.

Results of Operations

Three Months Ended June 30, 2008 Compared to Three Months Ended June 30, 2007.

Results for the three month period ended June 30, 2008 include a 7.1% increase in net revenues and a 16.0% increase in net income compared to the same period in 2007 after removing the after tax effect of the recovery of the note receivable occurring in the 2007 period.

Net patient revenues increased $9,132,000 or 6.8% compared to the same period last year. Medicare, Medicaid and private pay per diem rates increased 4.0%, 3.2% and 6.7%, respectively, compared to the quarter a year ago. Additionally, the January 2, 2008 acquisition of a 109-bed skilled nursing and rehabilitation facility located in Knoxville, Tennessee added approximately $1,824,000 in net patient revenues.

The total census at owned and leased centers for the quarter averaged 92.8% compared to an average of 92.7% for the same quarter a year ago.

Other revenues increased $1,484,000 or 9.3% in the three month 2008 period to $17,399,000 from $15,915,000 in the 2007 three month period. Increases in other revenues include increased collections of management and accounting services fees ($253,000), increased dividends and other realized gains on securities due both to higher dividend rates and greater numbers of securities owned ($79,000), greater earnings from our equity in unconsolidated investments (primarily from Caris HealthCare L.P., $531,000), and increased rental income ($2,410,000). The increased rental income is due primarily to (1) rental revenues from nine Florida facilities received on October 31, 2007 in the merger with NHR ($1,836,000) and (2) rental revenues from the real estate of a 544 bed long term care center and 66 unit assisted living center located in Chattanooga, Tennessee acquired on November 1, 2007 ($600,000).

Increases in other revenues in the 2008 period over the 2007 period were offset in part due to decreases in interest revenue ($1,559,000) and in advisory fees ($125,000). Interest revenue decreased in 2008 compared to 2007 due primarily to decreased investments caused by the expenditure by NHC of approximately $89,600,000 in cash to complete the merger with NHR effective on October 31, 2007. Further, interest income decreased in 2008 compared to 2007 due to the collection of notes receivable of $13,571,000 occurring in the second, ($6,195,000) and fourth ($7,376,000) quarters of 2007. The advisory fee income from NHR was terminated with completion of the NHR merger with NHC on October 31, 2007.

Total costs and expenses for the 2008 second quarter compared to the 2007 second quarter increased $14,136,000 or 10.8% to $145,021,000 from $130,885,000. Salaries, wages and benefits, the largest operating costs of this service company, increased $4,773,000 or 5.9% to $86,312,000 from $81,539,000. Other operating expenses increased $3,706,000 or 9.1% to $44,639,000 for the 2008 period compared to $40,933,000 in the 2007 period. Rent expense decreased $2,610,000 to $7,876,000 compared to $10,486,000 in the 2007 period. Depreciation and amortization increased $2,196,000 or 57.4% to $6,024,000 from $3,828,000. Interest costs decreased $124,000 to $170,000. Costs and expenses for the 2007 second quarter include a $6,195,000 recovery of a note receivable which had previously been written off.

Increases in salaries, wages and benefits are due to increased staffing due to the acquisition of a 109-bed skilled health care facility ($971,000), increased costs for therapist services ($831,000), increases in the provision for workers compensation and health insurance claims accrued ($1,084,000) and inflationary wage increases. Increases in other operating costs are due to costs associated with the acquisition of a 109-skilled health care facility ($889,000) and inflationary increases offset in part due to decreases in workers compensation ($960,000).

Rent expense in the first quarter of 2008 declined by approximately $2,829,000 compared to the same quarter last year because NHC is no longer paying rent to NHR after the October 31, 2007 merger between the two companies. This decline in rent expense is offset in part due to increased percentage rent to NHI ($141,000). Percentage rent to NHI is equal to 4% of the increase in facility revenues over the 2007 base year revenues.

Depreciation expense increased primarily due to the acquisition of assets during the last year. The merger with NHR completed on October 31, 2007 added depreciable real property of $247,649,000 and the net increase in depreciation in the quarter ended June 30, 2008 was $2,196,000.

The income tax provision for the three months ended June 30, 2008 is $6,055,000 (an effective tax rate of 39.0%), which is in line with management s expectations. The income tax provision for the three months ended June 30, 2007 was $7,169,000 (an effective tax rate of 37.6%). The 1.4% increase in the effective tax rate in 2008 is due to permanent differences including a reduction in the tax exempt income.

Six Months Ended June 30, 2008 Compared to Six Months Ended June 30, 2007.

Results for the six month period ended June 30, 2008 include an 8.2% increase in net revenues and a 16.1% increase in net income compared to the same period in 2007 after removing the after tax effect of the recovery of the note receivable occurring in the 2007 period.

Net patient revenues increased $19,617,000 or 7.3% compared to the same period last year. Medicare, Medicaid and private pay per diem rates increased 3.6%, 4.0% and 6.3% compared to the six month period last year. Additionally, the January 2, 2008 acquisition of a 109-bed skilled nursing and rehabilitation facility located in Knoxville, Tennessee added approximately $3,507,000 in net patient revenues.

The total census at owned and leased centers for the six months averaged 92.9% compared to an average of 92.5% for the same six months a year ago.

Other revenues increased $4,636,000 or 16.0% in the six month 2008 period to $33,575,000 from $28,939,000 in the 2007 six month period. Increases in other revenues include increased premiums from insurance services ($172,000), increased collections of management and accounting services fees ($990,000), increased dividends and other realized gains on securities due both to higher dividend rates and greater numbers of securities owned ($352,000), greater earnings from our equity in unconsolidated investments (primarily from Caris HealthCare L.P., $895,000), and increased rental income ($5,436,000). The increased rental income is due primarily to (1) rental revenues from nine Florida facilities received on October 31, 2007 in the merger with NHR ($3,306,000) and (2) rental revenues from the real estate of a 544 bed long term care center and 66 unit assisted living center located in Chattanooga, Tennessee acquired on November 1, 2007 ($1,200,000).

Increases in other revenues in the 2008 period over the 2007 period were offset in part due to decreases in interest revenue ($2,906,000) and in advisory fees ($250,000). Interest revenue decreased in 2008 compared to 2007 due primarily to decreased investments caused by the expenditure by NHC of approximately $89,600,000 in cash to complete the merger with NHR effective on October 31, 2007. Further, interest income decreased in 2008 compared to 2007 due to the collection of notes receivable of $13,571,000 occurring in the second, ($6,195,000) and fourth ($7,376,000) quarters of 2007. The advisory fee income from NHR was terminated with completion of the NHR merger with NHC on October 31, 2007.

Total costs and expenses for the 2008 six months compared to the 2007 six months increased $25,568,000 or 9.6% to $292,010,000 from $266,442,000. Salaries, wages and benefits, the largest operating costs of this service company, increased $13,140,000 or 8.2% to $173,853,000 from $160,713,000. Other operating expenses increased $7,192,000 or 8.7% to $89,953,000 for the 2008 period compared to $82,761,000 in the 2007 period. Rent expense decreased $5,215,000 to $15,794,000 compared to $21,009,000 in the 2007 period. Depreciation and amortization increased $4,437,000 or 58.5% to $12,021,000 from $7,584,000. Interest costs decreased $181,000 to $389,000.

Costs and expenses for the 2007 six months included a $6,195,000 recovery of a note receivable which had previously been written off.

Increases in salaries, wages and benefits are due to increased staffing due to the acquisition of a 109-bed skilled health care facility ($1,803,000), increased costs for therapist services ($2,363,000), increases in the provision for workers compensation and health insurance claims accrued ($1,703,000) and inflationary wage increases. Increases in other operating costs are due to costs associated with the acquisition of a 109-skilled health care facility ($1,966,000) and inflationary increases offset in part due to decreases in workers compensation ($960,000).

Rent expense in the 2008 period declined by approximately $5,215,000 compared to the same period last year because NHC is no longer paying rent to NHR after the October 31, 2007 merger between the two companies. This decline in rent expense is offset in part due to increased percentage rent to NHI ($327,000). Percentage rent to NHI is equal to 4% of the increase in facility revenues over the 2007 base year revenues.

Depreciation expense increased primarily due to the acquisition of assets in the last year. The merger with NHR completed on October 31, 2007 added depreciable real property of $247,649,000 and the net increase in depreciation in the six months ended June 30, 2008 was $4,437,000.

The income tax provision for the six months ended June 30, 2008 is $11,035,000 (an effective tax rate of 38.5%), which is in line with management s expectations. The income tax provision for the six months ended June 30, 2007 was $11,076,000 (an effective tax rate of 36.9%). The 1.6% increase in the effective tax rate in 2008 is due to permanent differences including a reduction in the tax exempt income.

Liquidity, Capital Resources, and Financial Condition

Sources and Uses of Funds - Our primary sources of cash include revenues from the healthcare and senior living facilities we operate, insurance services, management services and accounting services. Our primary uses of cash include salaries, wages and other operating costs of our home office and the facilities we operate, the cost of additions to and acquisitions of real property, rent expenses, debt service payments (including principal and interest) and dividend distributions. These sources and uses of cash are reflected in our Consolidated Statements of Cash Flows and are discussed in further detail below. The following is a summary of our sources and uses of cash flows (dollars in thousands):

	Three Months Ended June 30		Three Month Change		Six Months Ended June 30		Six Month Change	
	2008	2007	$	%	2008	2007	$	%
Cash and Cash equivalents at beginning of period	$ 17,288	$ 57,246	$ (39,958)	(69.8)%	$ 2,379	$ 50,678	$ (48,299)	(95.3)%
Cash provided from (used in) operating activities	19,553	16,195	3,358	20.7%	28,027	21,514	6,513	130.3%
Cash provided from (used in) investing activities	(2,804)	(3,195)	391	12.2%	7,968	484	7,484	1,546.3%
Cash provided from (used in) financing activities	(4,246)	(2,544)	(1,702)	(66.9)%	(8,583)	(4,974)	(3,609)	(72.6)%
Cash and cash equivalents at end of period	$ 29,791	$ 67,702	$ (37,911)	(56.0)%	$ 29,791	$ 67,702	$ (37,911)	(56.0)%

Operating Activities - Net cash provided by operating activities for the six months ended June 30, 2008, was $28,027,000 as compared to $21,514,000 provided in the same period last year. Cash provided by operating activities for the current period benefited from increases in various accrued current liabilities including accrued risk reserves and decreases in deferred income, and accounts receivable. The increases were offset by increases in the equity in earnings of unconsolidated investments and decreases in accrued payroll. Increases in restricted cash totaled $14,254,000 compared to a $7,150,000 increase in the prior period. The decrease in accounts receivable is due to collections and timing differences.

The increase in restricted cash in the current period is due primarily to the increase in cash reserved for our accrued risk reserves, including professional liability claims and workers compensation insurance claims, due to cash paid out for those claims.

The increase in other current liabilities and accrued risks reserves accounted for $11,440,000 in 2008 and $9,628,000 in 2007 of the cash provided by operating activities. If the risks materialize as expected, which may not be finally known for several years, they will require the use of our restricted cash.

Investing Activities - Cash provided from investing activities totaled $7,968,000 for the six months ended June 30, 2008, as compared to $484,000 provided from investing activities for the six months ended June 30, 2007. Cash used for property and equipment additions was $14,612,000 for the six months ended June 30, 2008 and $8,422,000 in the comparable period in 2007. Investments in notes receivable totaled $2,746,000 in 2008 compared to $0 in 2007. Cash provided by net collections of notes receivable was $4,450,000 in 2008 compared to $6,509,000 in 2007. Collections of our investment in the enhanced cash fund balance totaled $17,258,000 in the first six months of 2008 compared to $-0- in 2007.

Construction costs included in additions to property and equipment includes $3,319,000 incurred toward the construction of a 60 bed addition to an existing facility located in North Augusta, South Carolina. The majority of the investments in notes receivable was a working capital loan to a leased facility.

Net cash used in financing activities totaled $8,583,000 in the six months ended June 30, 2008 compared to $4,974,000 for the same period in 2007. Cash used for payments of debt totaled $7,432,000 and dividend payments to common and preferred shareholders totaled $9,355,000. In the prior year, cash used for payments of debt totaled $1,117,000, dividend payments to common shareholders totaled $4,503,000. Tax benefits from exercise of stock options provided cash of $314,000 in 2008 and $195,000 in 2007. In the current period, $7,500,000 cash was provided by borrowing against our revolving credit facility compared to -0- borrowings in the same period in 2007.

At June 30, 2008, our ratio of long term debt to total capitalization (total debt plus deferred income plus shareholders equity) is 2.3%.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

Table of Contractual Cash Obligations

Our contractual cash obligations for periods subsequent to June 30, 2008 are as follows (in thousands):

	Total	Less than 1 year	2-3 Years	4-5 Years	After 5 Years
Long-term debt principal	$ 17,503	$ 7,503	$	$	$ 10,000
Long-term debt - interest	4,524	485	850	850	2,339
Obligations to complete construction	235	235			
Obligation to purchase senior secured notes from financial institutions	1,030	1,030			
Operating leases	443,072	28,948	60,272	67,400	286,452
Total Contractual Cash Obligations	$ 466,364	$ 38,201	$ 61,122	$ 68,250	$ 298,791

We have guaranteed debt obligations of certain other entities totaling approximately $1,030,000. These guarantees are included in the table above; however, we do not anticipate material obligations under these commitments.

Income taxes payable for uncertain tax positions under FIN 48 of $4,595,000, attributable to permanent differences, at June 30, 2008 has not been included in the above table because of the inability to estimate the period in which it is expected to occur. See Note 2 of the Consolidated Financial Statements for a discussion on income taxes.

Our current cash on hand, marketable securities, short term notes receivable, operating cash flows, and as needed, our borrowing capacity are expected to be adequate to meet these contractual obligations and to finance our operating requirements, growth and development plans.

We started paying quarterly dividends in the second quarter of 2004 and anticipate the continuation of dividend payments as approved quarterly by the Board of Directors.

Guarantees and Contingencies

Debt Guarantees

In addition to our primary debt obligations, which are included in our consolidated financial statements, we have guaranteed certain of the debt obligations of National and the ESOP. This guarantee, which is not included as debt obligations in our consolidated financial statements, totals $1,030,000 at June 30, 2008.

The $1,030,000 of guarantees of debt of National and the ESOP relates to senior secured notes held by financial institutions. The total outstanding balance of National and the ESOP s obligations under these senior secured notes is $1,030,000. None of this obligation has been included in our debt obligations because we are not a direct obligor on this indebtedness. The $1,030,000, which is not included in our debt obligations because we are not a direct obligor, is due from NHI to National and the ESOP.

The $1,030,000 guarantee described above has cross-default provisions with other debt of National and the ESOP. We currently believe that National and the ESOP are in compliance with the terms of their debt agreements.

As of June 30, 2008, our maximum potential loss related to debt guarantees and financial guarantees is $1,030,000.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

New Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements . This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. The new FASB rule does not supersede all applications of fair value in other pronouncements, but creates a fair value hierarchy and prioritizes the inputs to valuation techniques for use in most pronouncements. It requires companies to assess the significance of an input to the fair value measurement in its entirety. Statement 157 also requires companies to disclose information to enable users of financial statements to assess the inputs used to develop the fair value measurements. SFAS 157 is effective for fiscal periods beginning after November 15, 2007 and interim periods within those fiscal years, with the following exception. FASB Staff Position (FSP) FAS 157-2, Effective Date of FASB Statement No. 157, defers the effective date to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years, for all nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The implementation of FAS 157 for financial assets and financial liabilities did not have a material impact on the Company s consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115 . This Statement amends FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities , with respect to accounting for a transfer to the trading category for all entities with available-for-sale and trading securities electing the fair value option. This statement allows companies to elect fair value accounting for many financial instruments and other items that currently are not required to be accounted as such, allows different applications for electing the option for a single item or groups of items, and requires disclosures to facilitate comparisons of similar assets and liabilities that are accounted for differently in relation to the fair value option. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The implementation of FAS 159 did not have a material impact on the Company s consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations* which replaces SFAS No. 141, *Business Combinations*. This Statement establishes principles and requirements for how the acquirer (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. This Statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company will adopt this standard at the beginning of the Company s fiscal year ending December 31, 2009 for all prospective business acquisitions. The Company has not determined the effect that the adoption of SFAS 141(R) will have on its consolidated financial statements, but the impact will be limited to any future acquisitions beginning in fiscal year 2009.

In December 2007, the FASB issued SFAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51.* This Statement requires all entities to report noncontrolling interests in subsidiaries as equity in the consolidated financial statements. This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. The Company will adopt this Statement effective January 1, 2009. The Company has not determined the effect that the adoption of SFAS No. 160 will have on its consolidated results of operations or financial position.

In May 2008, the FASB issued Statement of Financial Accounting Standards No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS No. 162). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP in the United States (the GAAP hierarchy). The current GAAP hierarchy is set forth in the AICPA Statement on Auditing Standards No. 69, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles (SAS No. 69). The FASB believes the GAAP hierarchy should be directed to entities because it is the entity (not its auditor) that is responsible for selecting accounting principles for financial statements that are presented in conformity with GAAP. Accordingly, the FASB concluded that the GAAP hierarchy should reside in the accounting literature established by the FASB and has issued SFAS No. 162 to achieve that result. SFAS No. 162 is effective 60 days following the SEC s approval of the Public Accounting Oversight Board amendments to SAS No. 69. We do not expect the adoption of SFAS No. 162 to have an impact on our consolidated financial position, results of operations, or cash flows.

Forward Looking Statements

References throughout this document to the Company include National HealthCare Corporation and its wholly owned subsidiaries. In accordance with the Securities and Exchange Commission=s APlain English@ guidelines, this Quarterly Report on Form 10 Q has been written in the first person. In this document, the words Awe@, Aour@, Aours@ and Aus@ refer only to National HealthCare Corporation and its wholly owned subsidiaries and not any other person.

This Quarterly Report on Form 10 Q and other information we provide from time to time, contains certain Aforward looking@ statements as that term is defined by the Private Securities Litigation Reform Act of 1995. All statements regarding our expected future financial position, results of operations or cash flows, continued performance improvements, ability to service and refinance our debt obligations, ability to finance growth opportunities, ability to control our patient care liability costs, ability to respond to changes in government regulations, ability to execute our three year strategic plan, and similar statements including, without limitations, those containing words such as Abelieves@, Aanticipates@, Aexpects@, Aintends@, Aestimates@, Aplans@, and other similar expressions are forward looking statements.

Forward looking statements involve known and unknown risks and uncertainties that may cause our actual results in future periods to differ materially from those projected or contemplated in the forward looking statements as a result of, but not limited to, the following factors:

C

national and local economic conditions, including their effect on the availability and cost of labor, utilities and materials;

C

the effect of government regulations and changes in regulations governing the healthcare industry, including our compliance with such regulations;

C

changes in Medicare and Medicaid payment levels and methodologies and the application of such methodologies by the government and its fiscal intermediaries;

C

liabilities and other claims asserted against us, including patient care liabilities, as well as the resolution of current litigation (see Note 7: Guarantees and Contingencies);

C

the ability of third parties for whom we have guaranteed debt to refinance certain short term debt obligations;

C

the ability to attract and retain qualified personnel;

C

the availability and terms of capital to fund acquisitions and capital improvements;

C

the competitive environment in which we operate;

C

the ability to maintain and increase census levels; and

C

demographic changes.

See the notes to the quarterly financial statements, and AItem 1. Business@ as is found in our 2007 Annual Report on Form 10 K for a discussion of various governmental regulations and other operating factors relating to the healthcare industry and the risk factors inherent in them. This may be found on our web side at www.nhccare.com. You should carefully consider these risks before making any investment in the Company. These risks and uncertainties are not the only ones facing us. There may be additional risks that we do not presently know of or that we currently deem immaterial. If any of the risks actually occur, our business, financial condition or results of operations could be materially adversely affected. In that case, the trading price of our shares of stock could decline, and you may lose all or part of your investment. Given these risks and uncertainties, we can give no assurances that these forward looking statements will, in fact, transpire and, therefore, caution investors not to place undue reliance on them.

Item 3.

Quantitative and Qualitative Disclosure About Market Risk.

Interest Rate Risk

Our cash and cash equivalents consist of highly liquid investments with an original maturity of less than three months. As a result of the short term nature of our cash instruments, a hypothetical 10% change in interest rates would have no material impact on our future earnings and cash flows related to these instruments. Approximately $13.8 million of our notes receivable bear interest at fixed interest rates. As the interest rates on these notes receivable are fixed, a hypothetical 10% change in interest rates would have no impact on our future earnings and cash flows related to these instruments. Approximately $7.7 million of our notes receivable bear interest at variable rates (generally at prime plus 2%). Because the interest rates of these instruments are variable, a hypothetical 10% change in interest rates would result in a related increase or decrease in annual interest income of approximately $52,000. As of June 30, 2008, all of our long term debt bears interest at variable interest rates. Because the interest rates of these instruments are variable, a hypothetical 10% change in interest rates would result in a related increase or decrease in annual interest expense of approximately $68,000.

Equity Price Risk

We consider our investments in marketable securities as Aavailable for sale@ securities and unrealized gains and losses, net of applicable income taxes, are recorded in stockholders= equity in accordance with Statement of Financial Accounting Standards No. 115. The investments in marketable securities are recorded at their fair market value based on quoted market prices. Thus, there is exposure to equity price risk, which is the potential change in fair value due to a change in quoted market price. Hypothetically, a 10% change in quoted market prices would result in a related 10% change in the fair value of our investments in marketable securities.

Investment in Enhanced Cash Fund

Please see *Note 5 Investment in Enhanced Cash Fund* and *Application of Critical Accounting Policies* regarding market risk related to our investment in an enhanced cash fund.

Item 4. Controls and Procedures.

As of June 30, 2008, an evaluation was performed under the supervision and with the participation of the Company=s management, including the Chief Executive Officer (ACEO@) and Principal Accounting Officer (APAO@), of the effectiveness of the design and operation of the Company=s disclosure controls and procedures. Based on that evaluation, the Company=s management, including the CEO and PAO, concluded that the Company=s disclosure controls and procedures were effective as of June 30, 2008. There have been no changes in the Company=s internal control over financial reporting during the quarter ended June 30, 2008 that have materially affected, or are reasonably likely to materially affect, the Company=s internal control over financial reporting.

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

PART II. OTHER INFORMATION

Item 1.

Legal Proceedings.

For a discussion of prior, current and pending litigation of material significance to NHC, please see Note 6 of this Form 10 Q.

Item 1A.

Risk Factors.

During the six months ended June 30, 2008, there were no material changes to the risk factors that were disclosed in Item 1A of National HealthCare Corporation=s Annual Report on Form 10 K for the year ended December 31, 2007.

Item 2.

Unregistered Sales of Equity Securities and Use of Proceeds. Not applicable

Item 3.

Defaults Upon Senior Securities. None

Item 4.

Submission of Matters to Vote of Security Holders. None.

Item 5.

Other Information. None

Item 6.

Exhibits.

(a)

List of exhibits

Exhibit No.	Description
31.1	Rule 13a 14(a)/15d 14(a) Certification of Chief Executive Officer
31.2	Rule 13a 14(a)/15d 14(a) Certification of Principal Financial Officer
32	Certification pursuant to 18 U.S.C. Section 906 by Chief Executive Officer and Principal Financial Officer

NATIONAL HEALTHCARE CORPORATION

June 30, 2008

(unaudited)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NATIONAL HEALTHCARE CORPORATION
(Registrant)

Date August 6, 2008	/s/ Robert G. Adams
	Robert G. Adams
	President
	Chief Executive Officer
Date August 6, 2008	/s/ Donald K. Daniel
	Donald K. Daniel
	Senior Vice President and Controller
	(Principal Financial Officer)