

2016
LETTER TO
SHAREHOLDERS



FINANCIAL HIGHLIGHTS

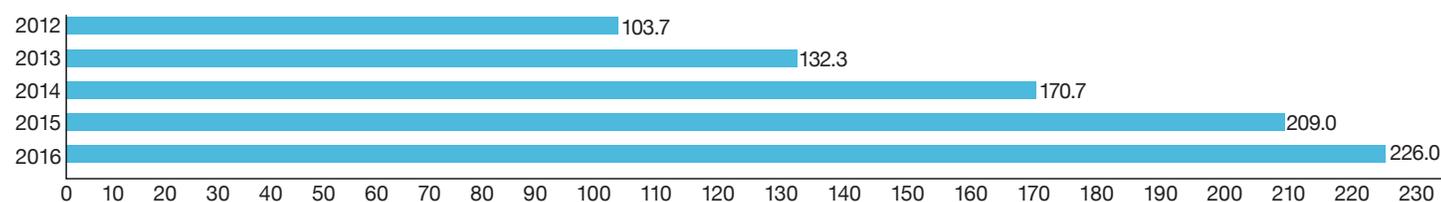
Year Ended December 31, <i>(In thousands, except per share amounts)</i>	2016	2015
Statement of Income Data:		
Revenues	\$ 225,974	\$ 209,002
Operating costs and expenses	220,407	195,445
Operating income	5,567	13,557
Other income, net	581	162
Income before income taxes	6,148	13,719
Income tax provision	2,393	5,098
Net income	\$ 3,755	\$ 8,621
Net income per share:		
Basic	\$ 0.12	\$ 0.29
Diluted	\$ 0.12	\$ 0.28
Weighted average shares of common stock outstanding:		
Basic	31,721	30,057
Diluted	32,068	30,436
Income before interest, taxes, share-based compensation, depreciation and amortization ("Adjusted EBITDA"⁽¹⁾):		
Net income	\$ 3,755	\$ 8,621
Interest, income taxes, share-based compensation, depreciation and amortization	26,096	25,162
Income before interest, income taxes, share-based compensation, depreciation and amortization	\$ 29,851	\$ 33,783

⁽¹⁾In order to better assess the Company's financial results, management believes that income before interest, income taxes, share-based compensation, depreciation and amortization ("Adjusted EBITDA") is an appropriate measure for evaluating the operating performance of the Company at this stage in its life cycle because adjusted EBITDA reflects net income adjusted for non-cash and non-operating items. Adjusted EBITDA is also used by many investors to assess the Company's results from current operations. Adjusted EBITDA is a non-GAAP financial measure and should not be considered as a measure of financial performance under generally accepted accounting principles. Because adjusted EBITDA is not a measurement determined in accordance with generally accepted accounting principles, it is susceptible to varying calculations. Accordingly, adjusted EBITDA, as presented, may not be comparable to other similarly titled measures of other companies.

Year Ended December 31, <i>(In thousands)</i>	2016	2015
Balance Sheet Data:		
Cash and cash equivalents	\$ 49,634	\$ 82,010
Investments in marketable securities	53,540	66,976
Accounts receivable, net	44,805	36,348
Goodwill and intangible assets	188,129	139,039
Working capital	82,467	120,459
Total assets	396,000	379,569
Deferred revenue – current and noncurrent	76,401	69,448
Shareholders' equity	286,108	280,320

TOTAL REVENUES

(in \$ millions)



DIRECTORS

Robert A. Frist, Jr.

*Chief Executive Officer, President, and
Chairman of the Board of Directors*
HealthStream, Inc.

Jeffrey L. McLaren

Chief Executive Officer
Medaxion, Inc.

Thompson S. Dent

Chairman and Chief Executive Officer
Urgent Team
Chairman
Re:Cognition Health

William W. Stead, M.D.

Chief Strategy Officer
Vanderbilt University Medical Center

Linda E. Rebrovick

Senior Client Partner
Morgan Samuels

Frank E. Gordon

Managing Partner
Crofton Capital

Michael D. Shmerling

Chairman
Clearbrook Holdings Corporation

Dale W. Polley

Past President and Vice Chairman
First American Corporation

C. Martin Harris, M.D.

Associate Vice President of the Health Enterprise
Chief Business Officer
Dell Medical School
The University of Texas at Austin

Deborah Taylor Tate, J.D.

Former Commissioner
Federal Communications Commission
Director
State of Tennessee / Administrative
Office of the Courts
Special Envoy to the International
Telecommunications Union

EXECUTIVE OFFICERS

Robert A. Frist, Jr.

*Chief Executive Officer, President, and
Chairman of the Board of Directors*

J. Edward Pearson

Chief Operating Officer and Senior Vice President

Gerard M. Hayden, Jr.

Chief Financial Officer and Senior Vice President

Jeffrey S. Doster

Chief Technology Officer and Senior Vice President

Michael J. Sousa

President, Provider Solutions and Senior Vice President

Thomas B. Schultz

Senior Vice President

LETTER TO SHAREHOLDERS

While change seems to be never-ending—particularly in the healthcare industry—one thing remains constant: every patient is important and deserves the best possible care. For this reason, healthcare providers are teaming with HealthStream to ensure a qualified workforce is hired, onboarded, assessed, trained, certified, and provided with ongoing education and skills development opportunities. At HealthStream, it is our honor and privilege to support the nation's healthcare providers in their mission to improve the quality of care their workforce delivers.

2016 was a year of solid revenue growth, which included annual revenues of \$226.0 million, up eight percent over 2015 revenues. We entered 2016 knowing that to show any growth, it would be necessary to overcome an \$18 million decrease in top-line revenue due to our extensively reported and fully anticipated decline in ICD-10 readiness product revenues. We accomplished growth despite those headwinds—particularly in our Workforce Development segment, including continued outperformance of our resuscitation portfolio, which grew in revenue by 26 percent for the year and our clinical solutions portfolio, which grew in revenue by 24 percent for the year.

During 2016, we experienced some expenses that challenged our full-year operating income growth, which was down 59 percent over 2015. Margin loss from the decline of ICD-10 revenues, deferred revenue write-downs from the last two acquisitions in our Provider Solutions segment, transaction closing costs related to our Morrisey Associates acquisition, and ramping up our implementation resources in Provider Solutions to more efficiently process our growing sales backlog all contributed to headwinds that pressured operating income growth. We anticipate returning to leveraged operating income growth for 2017—as reflected in our most recent financial guidance that included operating income increasing 50-65 percent over 2016.

We ended 2016 well capitalized with a cash and marketable securities balance of \$103.2 million and full availability of our \$50.0 million line of credit with no long-term debt. This strong capital position allows us to utilize multiple strategies for creating shareholder value, such as developing and launching new products and pursuing an active M&A pipeline.

Our target market is a workforce of approximately 8.6 million healthcare professionals, which includes approximately 5.3 million employees working in the nation's acute-care hospitals and 3.3 million employees in the post-acute care market. By combining the capabilities of our enterprise workforce development platform with leading content and superior data and analytics, HealthStream is delivering solutions that drive positive outcomes in healthcare. Every day, we help our customers meet compliance requirements, improve resuscitation outcomes, develop their clinical workforce, manage revenue cycles, improve patients' experience, and ensure that their workforce maintains all of the credentials they require.

HealthStream's enterprise workforce management solutions include a wide range of healthcare-specific applications, such as the HealthStream Learning Center™, HealthStream Performance Center™, HealthStream Competency Center™, HealthStream Recruiting Center™, HealthStream Compensation Planner™, and complementary applications like Checklist Management™ and COI-SMART™. We also offer a diverse suite of innovative applications from our provider solutions business for credentialing, privileging, and enrolling healthcare professionals—like EchoCredentialing™, MSO for the Web™, and EchoOneApp™.

At year-end 2016, our workforce platform applications were contracted by healthcare organizations for, collectively, their approximately 4.6 million healthcare employees in the U.S.

As part of its ecosystem, HealthStream has over 100 healthcare industry partners, which include highly regarded professional medical and nursing associations as well as best-in-class content providers. Increasingly, our partners are incorporating HealthStream's core technologies into their initial thinking and development plans as they consider what is now possible for their products by utilizing our powerful network, its data, and benchmarking opportunities. EBSCO Health, for example, adapted its prestigious Clinical Skills Development Program to take advantage of HealthStream's Checklist Management application, thereby reaching hundreds of thousands of healthcare professionals that subscribe and use Checklist Management in their respective healthcare organizations.

Similarly, the American Academy of Pediatrics (AAP) chose HealthStream for an exclusive partnership where our technology provides the customized platform infrastructure for the credentialing and testing services for their 15,000 certified instructors and corresponding delivery of over a half-million tests. We provide an integrated suite of services for AAP that includes delivery and management of testing, contracting, billing, and customer service—a bundle of services not available as a comprehensive solution outside of HealthStream.

Our partner, nThrive (formerly known as “Precyse”), has utilized HealthStream's extensive storehouse of performance data by building custom performance benchmarks into their innovative DNA product, a revenue cycle management solution. These powerful benchmarks—integrated into DNA—attract customers with capabilities not available elsewhere in the marketplace. nThrive's decision to build DNA on HealthStream's control center technology, which inherently leverages our powerful network, has given them a strong competitive advantage.

The power of HealthStream's network to efficiently and quickly provide solutions for the healthcare workforce was well demonstrated by the deadline-driven mandate to adopt the ICD-10 clinical coding system, which had a CMS-imposed deadline of October 2015. HealthStream's comprehensive training solution to prepare the healthcare workforce for this transition became the most adopted solution in the U.S., earning, cumulatively, over

\$78 million from sales of this solution over an approximately four-year period where our highest quarterly revenue reached \$7.4 million in the fourth quarter of 2014. Subsequently tapering down each quarter—as expected and announced—we anticipate revenues from the ICD-10 readiness solution to be approximately \$1 million for full-year 2017. Having moved well past this deadline, we expect 2017 to be the final year that previous subscription-based sales of this solution will impact the Company.

HealthStream's Patient Experience (PX) Solutions complement our workforce development offerings by linking together the patient experience survey results we collect to evidence-based education and development resources from partners and our own research to improve patient experience outcomes. In 2016, we invested in further modernizing our data collection methodologies and creating PX courseware that links specific content to the workforce behaviors that drive mandated CAHPS survey performance across the acute and ambulatory care markets. These development efforts have evolved our value proposition from data collection, analysis, and benchmarking to leading the industry in patient experience competency assessment and development.

For full-year 2016, we completed approximately 2.6 million total surveys on behalf of our customers, which represented a 12 percent increase compared to 2015. While CMS still requires at this time that HCAHPS-submitted data be solicited exclusively from phone-based or mail-based (i.e. hard copy) surveys, healthcare organizations are demanding that their patients' feedback be collected faster, in higher volumes, and at lower cost. Specifically, our customers are increasingly requesting a greater number of online and text-message-based patient surveys compared to phone-based surveys. For full-year 2016, for example, HealthStream's volume of phone-based patient surveys declined 9 percent while online patient surveys increased by 47 percent. Though online surveys have a lower price point than phone surveys, they are more profitable, higher margin products. We have taken steps to adjust our operations to better align with this trend—as we stated on March 1, 2017 when we announced the consolidation of our Patient Interview Operations in our Maryland office to our state-of-the-art facilities in Tennessee, which will reduce our overall costs for interview center operations.

In August 2016, HealthStream announced its acquisition of Chicago-based Morrisey Associates, which expanded our Provider Solutions segment with market-leading products for credentialing and privileging healthcare professionals, adding to our Echo line of solutions. Coupled with our acquisition of HealthLine Systems in 2015, we believe we are well positioned to build off of the synergies gained in this business segment for further innovation and new product development for our customers.

Many new products were introduced in 2016 as we continue to innovate new solutions for the healthcare workforce. Launched from across our three business segments—these new products

are expected to start as small contributors to full-year growth in 2017, as we just recently introduced them to the market. Most of our new products, however, yield higher-than-average gross margins for the Company.

From HealthStream's Workforce Solutions segment, EBSCO Health's **Clinical Skills Development Program** was launched in August 2016, which delivers award-winning, innovative clinical competency solutions that meet a wide range of clinical staff development needs. We also launched the **OB Risk Curriculum**, which was co-developed with our strategic partner, MedStar/Sitel. This new product is focused on reducing risks by providing clinical staff with key knowledge and skills to identify early warning signs of maternal and infant distress.

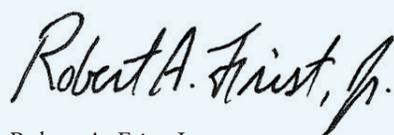
From HealthStream's Provider Solutions segment, we launched the **Privileging Content and Criteria Builder** product. This is a robust privileging library that we gained with our acquisition of Morrisey Associates. It enables healthcare organizations to create and customize their own privilege forms, using the researched content and criteria in order to meet their unique needs.

From HealthStream's Patient Experience segment, we launched **DevelopRx**, which is a 62-course library of evidence-based learning that links survey questions to best practices and competency training courses available in the HealthStream Learning Center. This product is a good example of the leverage our platform provides to the members of our network, as it allows those members to utilize insights from Patient Experience surveys, then take action on such insights with specifically targeted workforce development training and education.

Looking forward, we intend to continue growing HealthStream organically by increasing our customer base and expanding the number of solutions provided to existing accounts. We may also pursue Company growth by utilizing a portion of our cash position and/or common stock to acquire or invest in opportunities arising from our M&A pipeline while we, at the same time, continue to invest in the integration and enhancement of new products and capabilities for our customers.

In closing, I want to thank you, our shareholders, for your continued commitment and support of HealthStream. I, along with the rest of the management team, firmly believe that HealthStream is achieving its vision to improve the quality of healthcare by assessing and developing the people that deliver care. We will continue to put forth our best efforts to the task of producing superior results for you.

Sincerely,



Robert A. Frist, Jr.
Chairman and Chief Executive Officer

CORPORATE DATA

Annual Meeting

The annual meeting of shareholders will be held on May 25, 2017, at 2:00 p.m. (CDT) at HealthStream, Inc., 209 10th Avenue South, Suite 450, Nashville, Tennessee 37203.

Independent Registered Public Accounting Firm

Ernst & Young LLP
Nashville, Tennessee

Transfer Agent

Computershare
211 Quality Circle, Suite 210
College Station, TX 77845
(800) 962-4284
Investor Centre™ portal: www.computershare.com/investor

Legal Counsel

Bass, Berry & Sims PLC
Nashville, Tennessee

Corporate Headquarters

HealthStream, Inc.
209 10th Avenue South, Suite 450
Nashville, Tennessee 37203

Form 10-K

A copy of the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, is being mailed with this letter. Additional copies of the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, are available without exhibits, free of charge, to its shareholders. Requests should be addressed to Mollie Condra, Investor Relations Department, HealthStream, Inc., 209 10th Avenue South, Suite 450, Nashville, Tennessee 37203.

Corporate Stock

HealthStream, Inc.'s common stock is traded on the NASDAQ Stock Market under the symbol HSTM. The following table shows the quarterly range of high and low closing sales prices of the common stock from 2014.

	HIGH	LOW
2014		
First Quarter	\$ 34.43	\$ 26.49
Second Quarter	\$ 27.10	\$ 21.02
Third Quarter	\$ 27.14	\$ 21.80
Fourth Quarter	\$ 31.95	\$ 23.38
2015		
First Quarter	\$ 30.36	\$ 24.63
Second Quarter	\$ 31.91	\$ 25.15
Third Quarter	\$ 32.14	\$ 21.60
Fourth Quarter	\$ 25.63	\$ 21.31
2016		
First Quarter	\$ 22.35	\$ 18.20
Second Quarter	\$ 26.58	\$ 21.17
Third Quarter	\$ 27.65	\$ 23.73
Fourth Quarter	\$ 28.39	\$ 22.36

As of February 13, 2017, HealthStream, Inc. had approximately 9,547 shareholders, including 593 shareholders of record and 8,954 persons or entities holding common stock in nominee name.

The Company has never declared or paid any cash dividends on its common stock and does not anticipate paying cash dividends in the foreseeable future. HealthStream intends to retain earnings to finance the expansion of its operations.

Cautionary Note Regarding Forward-Looking Statements

This report contains forward-looking statements (all statements other than those made solely with respect to historical fact) within the meaning of Section 21E of the Securities and Exchange Act of 1934 and Section 27A of the Securities Act of 1933. These forward-looking statements are subject to known and unknown risks and uncertainties (some of which are beyond the Company's control) that could cause actual results to differ materially and adversely from those anticipated in the forward-looking statements. See the Company's 10-K filing for more detailed disclosure regarding forward-looking statements and associated risks and uncertainties.