

# COVID-19 and a New Financial Perspective for Hospitals

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The COVID-19 pandemic has significantly disrupted the operational and financial landscape of hospitals and health systems nationwide. Historically, most hospitals have relied on a flow of elective, non-urgent procedures reimbursed by commercial payers to maintain financial health, as margins for medical patients and from government payers are either narrow or negative.

The COVID-19 pandemic has shown what happens when this lifeblood of hospitals' financial health goes away for a significant time. As a consequence of the pandemic, many healthcare organizations have decreased or stopped elective, non-urgent procedures for extended periods. The central financial planning challenge for hospitals now is to deal with any continued immediate threats to their financial viability, and to adapt for the new revenue, cost, and operational picture of a recessionary, post-COVID environment.

Organizations have faced serious revenue erosion and expense increases in recent months. Many have had to make hard decisions to contain costs, including reducing hours, scaling back benefits, and cutting staff. In the midst of the surge, executives shifted all focus to ensure they had the capacity, staff, and equipment to test and treat COVID-19 patients. For the most part, organizations found that the virus hit them more quickly than they ever could have imagined, and the impact

was more profound than they ever could have envisioned.

Boards and senior leaders must work together to continue to address the major financial consequences of this imbalance of revenue and expenses. Doing so requires ensuring their organizations have a clear and full picture of the pandemic's impacts—both since its start and moving forward. **Exhibit 1** lists key metrics that senior leaders and directors should be monitoring to inform their current financial position, and to help them prepare for immediate and longer-term next steps.

## Adapting for a New World

Hospitals will find themselves in a very different recessionary and post-recessionary world. The rebound in elective and non-elective procedures is proving unpredictable.

Organizations typically fit into two broad categories in how they think about the immediate and longer-term financial implications. One category comprises organizations that, before the virus, were operating with marginal profitability and relatively weak balance sheets. For these hospitals, the immediate concern is how to continue to navigate the virus and recessionary pressures in the short term. They need an understanding of exactly what financial damage has been done and is expected in the coming months in

## Key Board Takeaways

As COVID-19 continues to disrupt the traditional foundations of U.S. hospitals and health systems, boards and senior leaders must be diligent in monitoring the pandemic's continued repercussions, and in planning to close financial gaps. Questions to ask include:

- What is the organization's payer mix and how has it changed due to COVID-19?
- How is management addressing continued COVID-related demands and costs?
- What performance metrics is the organization tracking to assess the impacts of the pandemic?
- What type of budgeting processes are senior leaders using to ensure flexibility?
- What steps is management taking to plan for the new revenue, cost, and operational picture of a post-COVID environment?

Continuing to navigate the pandemic's short- and long-term impacts requires timely data, sophisticated analysis, and flexible forecasting and budgeting methodologies for an unpredictable future.

order to make precise financial decisions that will best serve the hospitals and their communities in the short and long run.

If they have not already, this group needs to start as quickly as possible to determine changes to their cost structures in order to weather a potential longer-term decrease in volumes. For some independent organizations, partnership options may need to be assessed.

Organizations that are stronger financially, many of which are larger systems, have a somewhat different financial planning perspective. For these organizations, the longer-term financial issues have to do with how to remain financially sound when the major source of margin is dramatically reduced for a significant period of time. Such organizations need to look at costs through a new lens. They may look for substantial capital budget reductions, cancel certain large initiatives, and take a hard look at their hospital portfolios, overhead costs, and labor. The level of cost reduction is likely to be meaningful in every respect, and the cultural and political adjustments could be significant.

In general, larger organizations need to continue to plan for unexpected

**Exhibit 1: Key Metrics for Tracking the Impacts of COVID-19**

Volume and Revenue	Expenses	Balance Sheet and Cash Flow
<ul style="list-style-type: none"> <li>• Elective volumes</li> <li>• COVID-19 volumes</li> <li>• ED visits</li> <li>• Service mix</li> <li>• Payer mix</li> <li>• Intensive care</li> <li>• Bad debt</li> <li>• Physician visits</li> <li>• Telehealth</li> <li>• Governmental support</li> <li>• Philanthropy</li> </ul>	<ul style="list-style-type: none"> <li>• Workforce</li> <li>• Supply chain</li> <li>• Physician productivity and compensation</li> <li>• Emergency preparedness</li> <li>• Capacity implications</li> <li>• Interest expense</li> </ul>	<ul style="list-style-type: none"> <li>• Collections of receivables</li> <li>• Accounts payable management</li> <li>• Invested asset portfolio/ investment income</li> <li>• Near-term liquidity requirements and capital access</li> <li>• Capital structure disruption</li> <li>• Pension funding</li> <li>• Debt capacity</li> <li>• Swap collateral posting requirements</li> </ul>

Source: Kaufman, Hall & Associates, LLC

stresses on credit ratings, weakened balance sheets, and profitability. Boards must be well educated about the situation and the new state of hospital economics. Executives will have some opportunities; for example, new competitive positions and partnership options might exist compared with the pre-COVID environment. In general, however, these organizations will need to develop a new mental model accompanied by a new and more sophisticated financial plan.

Boards will need to stay in close communication with their executive teams about the nature and degree of the financial impact of COVID, the gap that impact creates between current and budgeted performance levels, near-term actions to address the gap, and longer-term effects on strategic and capital plans. This information will need to be updated regularly, due to the

unpredictable nature of the current and future environments.

### **A New Hospital Economy and New Planning Paradigm**

The financial instability of the nation's healthcare system has been apparent for some time. For hospitals, a critical element of that instability has been reliance on commercial insurers and surgical procedures to maintain margins. The COVID-19 pandemic has revealed that vulnerability in the starkest terms. Lost revenue and higher expenses remain a major problem for many.

The COVID-19 virus has challenged hospitals not just to plan for short-term financial hits, but for a new healthcare economy. This new planning paradigm has exposed the inadequacies of traditional annual operating budget processes.

Annual budgeting by itself simply does not provide the frequency or

flexibility to meet the demands of the current planning environment. Hospitals require a process such as rolling forecasting for efficient and timely updates that enable management to assess changes frequently, and adjust quickly to a volatile environment.

Whether tracking for the immediate, continuing needs of the crisis or forecasting for the post-COVID-19 world, healthcare leaders face new demands for timely data, sophisticated analysis, and forecasting and budgeting methodologies suitable for a highly unpredictable future.

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