

Leading Through Uncertainty

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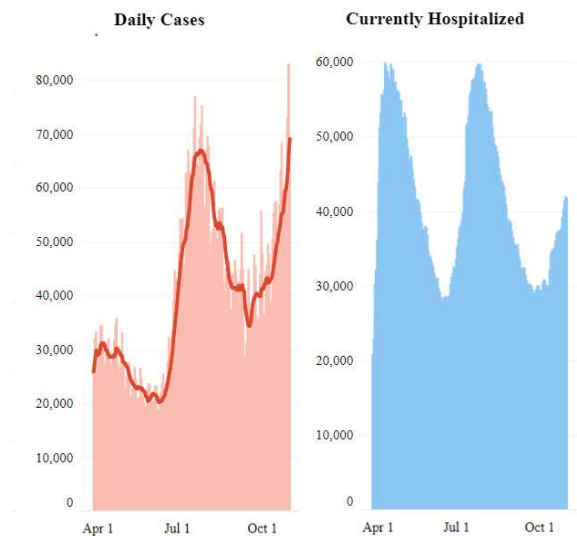
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The State of Play

- The U.S. set a new single-day record on Oct. 23 with almost 84,000 new cases
- Between September and October, we have had a 40% rise in number of people hospitalized for COVID-19
- During the week of Oct. 24, 14 states had more people hospitalized on a single day for COVID-19 than on any previous day during the pandemic

Source: The COVID Tracking Project



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Aligning Organizational Strategy With COVID's Unpredictable Path

- The virus appears to be moving from pandemic to endemic back to pandemic
- After eight months of fighting the virus, we are at the greatest level of uncertainty yet
- *Hospitals need to be ready to tackle COVID as a pandemic, an endemic, and a chronic situation*

“We will be dealing with this virus forever. We’re not going to be vaccinating our way out of this...”

—Michael Osterholm, PhD
Center of Infectious Disease
Research and Policy
University of Minnesota

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The “Organizational Thought Process” in Typical Circumstances

- In a typical planning process, health systems expect a fairly narrow range of possible financial and strategic outcomes
- Volumes, revenues, expenses, and margins tend to stay within predictable variations
- Initiatives targeting future change in areas like access, care models, cost structure, and organizational growth tend to proceed incrementally
- The competitive landscape tends to be among known entities within the local market
- This result can provide a high level of cultural comfort with business as usual

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What we are facing now is not business as usual, but disruption of uncertain intensity, duration, and effect.



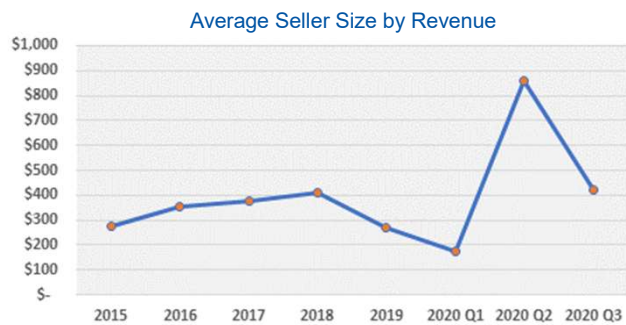
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A New Competitive Landscape: Health System Consolidation

- More than ever, scale is a priority: 2020 Q2 and Q3 saw historically high size of seller by revenue
- We are seeing signs that health systems are moving beyond their geographic tradition
- The pandemic has accelerated the need to transform care delivery models and reimagine health system configuration
- Systems are beginning to restructure their portfolios as they look for opportunities to monetize or exit underperforming assets and strengthen their financial viability
- Where do these shifts leave organizations of various sizes, levels of financial strength, and competitive positions?



Source: Kaufman Hall Q2 M&A Report

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A New Competitive Landscape: The Influence of Big Tech

- The tech sector's economic dominance has accelerated
 - Verticals with a face-to-face orientation (retail, hospitality, live entertainment) have been devastated by COVID-19
 - The more tech is winning, the more the nature of economic competition changes
 - To what extent will nature of competition in healthcare be based more on technology and less on face-to-face care delivery?
- Apple, Amazon, Google, and Facebook now account for almost 20% of the S&P 500 market cap
 - Apple's market cap is hovering at \$2 trillion
 - Amazon's revenue was up 40% in Q2 2020, and its profitability was over \$5 billion for the quarter

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The Need to Accelerate Telehealth Expertise

- Forrester Research predicts more than 1 billion virtual care visits in 2020, up from an initial estimate of 36 million
- CMS has dramatically expanded the number of covered telehealth services
- Patients report positive experiences with telehealth
- A rise in telehealth demand could mean less revenue for organizations already damaged by revenue losses from COVID-19
- If telehealth demand is sustained, hospitals may be able to rethink some facility and real estate expenses
- Providers whose telehealth services are limited in scope, capacity or functionality will have difficulty competing against more sophisticated solutions from other providers or new entrants
- The question remains: How broad and sustained will telehealth demand be?

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The Necessity of a New Cost Structure

- Basic math provides the impetus: each hospital's new cost structure will depend on the slope of its revenue recovery curve
- Hospitals will need to make major changes to operations in order to adjust to a loss of revenue whose exact level remains unknown
- What will the resulting healthcare delivery system need to look like? What are its core functions? What is its most effective structure? What is the optimal workforce? What technology support is needed? What facilities are needed?
- At this point, executives have only a hazy idea of what their new cost structure will need to be

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Historic Racial Inequity

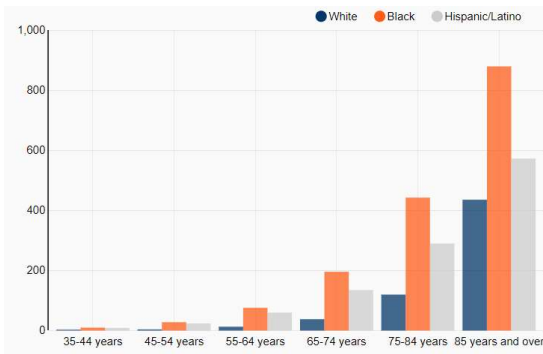
- We have known for years that a person's zip code has more to do with life expectancy than any other factor
- For example, in Chicago's largely white Streeterville neighborhood, life expectancy is 90 years, while 10 miles away in the largely Black Englewood neighborhood, life expectancy is 60 years
- Racial disparities have long existed in healthcare: disparities in quality of care and in rates of cancers, heart disease, maternal and child health

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Ending Racial Disparities

- COVID-19 has put a harsh spotlight on racial inequity in healthcare
- Three times more Blacks and Latinos than Whites have been diagnosed with COVID-19
- Blacks have died from COVID at more than twice the rate as Whites among ages 75 and older
- And now the Black Lives Matter movement has put an even brighter light on racism and racial inequity
- Hospitals must make racial equity part of their DNA

COVID-19 Death Rates by Ages and Race

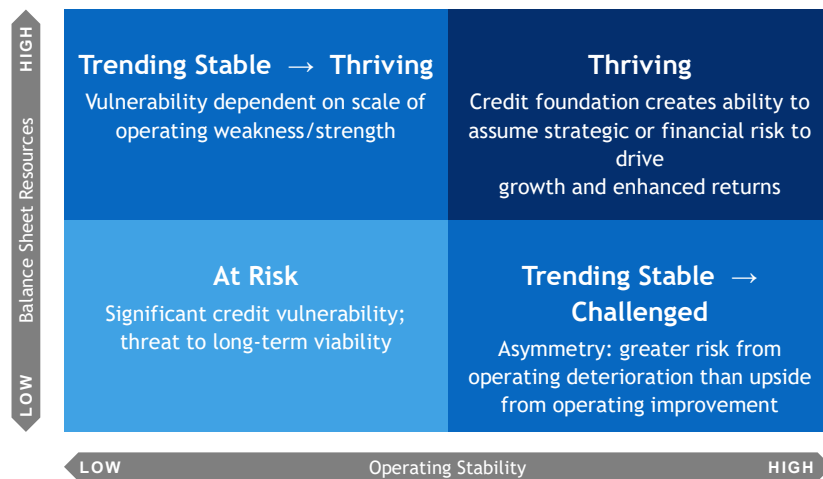


Source: CDC data from 2/1/20-6/6/20 and 2018 U.S. Census population estimates; Brookings

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Risk vs. Resiliency

- Balance sheets will be an anchor
- Operations will be a credit variable



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Conditions of Risk

- Two kinds of risk:
 1. **Operating risk:** Risk internal to the organization
 2. **Event risk:** Risk external to the organization
- Economic rule of thumb: When event risk is high, reduce operating risk
- To state the obvious, event risk has never been higher

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Building Operating Risk Could Collide with Event Risk

Operating Risk

- Accumulation of short-term liquidity
 - Lines of credit plus CARES Act money
- Permanent reduction in volume
- Payer mix deterioration
 - Greater dependence on Medicaid
- Overall reduction in patient service revenue

Event Risk

- The endless pandemic
- Long-term economic dislocation
- State and federal financial deterioration
- Capital markets dislocation

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Active Risk Mitigation

1. Convert short-term financing (lines of credit) to permanent financing. Do this now while capital markets are operating within a normal range.
2. Scrub the operating model for accumulated assets that have increased operating risk but are not positively contributing to operating performance.

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At this point, we have more questions than answers. However, there are some observations that encourage a positive strategic outcome.



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What We Know – Three Very Important Things

- Organizations with strength are in the best position to lead
 - A strong balance sheet, scale, and revenue diversification help weather uncertainty
- Math has never been more important
 - Highly sophisticated monitoring, predictive modeling, and analysis are more necessary than ever to understand current position and future scenarios
- Multi-taskers will have the broadest options
 - The ability to simultaneously:
 - Take on COVID as a chronic condition
 - Recover financial stability
 - Reimagine strategic position

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Four Principles from Jim Collins

- I was fortunate to talk with Jim Collins at the relative beginning of the pandemic
- Jim is perhaps the best mind in leadership and management today
- He offered four principles about how organizations make their way through unprecedented uncertainty



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Principle One: Readiness

“What organizations do before the storm affects how they perform during the storm.”

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Principle Two: Discipline

“Organizations that are not disciplined when times are good find that discipline is critical when the crisis hits.”

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Principle Three: Competitive Separation

“In times like these, the separation between organizations tends to be permanent, and those that are weaker tend to fall further behind.”

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Principle Four: Durability

“As individuals and as organizations, we can orient ourselves around transactions or around relationships. Especially during a crisis, the most durable business orientation is around relationships.”

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For more than forty years, Ken Kaufman has been one of the leading thinkers on the future of healthcare. He is the Chair of Kaufman Hall, a management consulting and software firm that he founded in 1985. Ken has helped healthcare organizations of all sizes with their most critical strategic challenges. He is also the author of seven books and hundreds of articles, and he has delivered more than 400 speeches, most recently focusing on healthcare disruption. In 2019, he received the Richard L. Clarke Board of Directors Award from the Healthcare Financial Management Association for lifetime contribution to healthcare.

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