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A three-pronged approach for health systems to achieve financial resiliency

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To position health systems for long-term financial and operational success, we propose a collective focus on strategy-driven financial resiliency, using a combination of traditional performance improvement and strategic planning. Further, we outline how to initiate regional planning for health resources in collaboration with state health agencies.

Background

Health systems were hit hard by the COVID-19 pandemic, and many have been unable to recover from major financial losses. While government institutions provided billions in COVID-19 relief subsidies and grants,[1] many hospitals have struggled to stay afloat as various expenses, such as clinical staffing, medical supplies, health IT, etc., have seen double-digit increases from pre-pandemic levels.

An AHA report[2] detailing the extraordinary financial pressures faced by health care systems noted:

- Hospital expenses increased by 17.5% between 2019 and 2022. This outpaced Medicare reimbursement, which increased just 7.5% during the same time period.
- Labor costs, which, on average, account for one-third to one-half of a hospital's budget, increased 20.8% between 2019 and 2022.
- Supply expenses per patient increased 18.5% between 2019 and 2022, outpacing inflation by nearly 30%.

As a result of these mounting pressures, there is a renewed focus on cost reduction. Several health systems have already iterated through more than one round of cost optimization. There is now a real fear that quality of care may be affected if further cost cutting is not conducted with prudence.

Go-forward plan

We propose a three-pronged go-forward plan:

01. Some traditional margin improvement efforts to harvest any remaining low-hanging fruit;

02. A keen evaluation of strategic positioning to help balance cost cutting and strategic investments in growth services; and

03. In some circumstances, a more holistic and strategic regional planning effort (involving collaboration with state agency leaders) to optimize the regional health care delivery ecosystem.

Step 1

Pursue traditional performance improvement initiatives while upholding quality

Step 2

Develop and launch a strategic resiliency plan informed by macro and regional strategic positioning

Step 3

Engage with state agencies to configure and fine-tune the regional health care delivery ecosystem

Step 1. Pursue traditional performance improvement initiatives while upholding quality

This first step is typically based on a function-by-function assessment of performance often informed by industry benchmark analyses. The sum-total savings of individual initiatives becomes the anchor financial target that the organization rallies around and launches its business transformation efforts.

Examples of traditional margin improvement:

- *Optimize supply chain.* Improve sourcing efficiency. Evaluate options for group purchasing (GPO). Reduce the number of stock keeping units (SKUs). Streamline physician preference cards. Narrow down the pharmacy formulary.
- *Conduct IT review.* Streamline IT application and vendor portfolio. Contract for additional technology support, if needed. Seek efficient environments such as cloud.
- *Enhance staff productivity.* Benchmark productivity levels, simplify workflows, and identify ways that IT and artificial intelligence (AI) may enable efficiencies.
- *Clinical throughput.* Enhance patient progression. Evaluate Models of Care. Optimize OR utilization. Shorten emergency room door-to-discharge time.
- *Revenue cycle.* Clean up documentation and billing. Automate prior authorization process. Chip away at denials.

The challenge is that in this traditional performance improvement approach, each function is evaluated as a stand-alone opportunity. Little or no consideration is given to interdependencies and/or which areas are critical for future sustainability and growth. For example, if medical oncology is identified as a near-term growth area, it would be important to maintain pharmacy and lab staff, even if they are above benchmark today.

Step 2. Develop and launch a strategic resiliency plan informed by macro and regional strategic positioning

The fallacy in Step 1 is to assume that the current mix of services and the existing care delivery configuration are adequate to serve current and future demand. Under that premise, the primary objective is to drive efficiency in the current asset base: "Do more of the same, just do it more efficiently!" In contrast, our point of view is that a balanced approach between efficiency/cost reduction, growth/revenue enhancement, and capital reallocation is needed to achieve sustainability.

We propose that health systems consider a holistic approach to resiliency planning. Consideration might be given to items such as local market dynamics, evolving reimbursement models, workforce transformations, care model innovations, and emerging medical and health IT technologies. Collectively, the macro trends may suggest that a different mix of services and asset configuration may be needed (i.e., certain services may need to be enhanced and others discontinued). In addition to rethinking the asset mix, the ownership structure could also be reconsidered through partnerships and joint ventures as less capital-intensive options. In other instances, strategic capital investments that enable efficiency or yield revenue enhancement may be justified to meet specific growth opportunities.

Consider the following in assessing the strategic positioning:

Strategic value to community:

- What clinical services are provided today, and what services do peer organizations provide?
- Which services are essential to provide equitable access to care in the region and should be enhanced? What services should be curtailed because they are duplicative to peers?
- Can partnerships help with consolidation of services and potentially enhance geographic and population reach?
- How do you account for shifting business models in health care (e.g., adopting more value-based programs)?

Asset reconfiguration:

- What macro trends are driving shifts in site of care (e.g., from inpatient to outpatient and home-based care)? What is the implication for the organization's required facility configuration?
- What trends are driving new care delivery models? What investments in health IT and other technology are needed to optimize productivity and sustainability under this new care model?
- Where are the growth opportunities, and what capital investments are needed to pursue them?

Strategic path forward:

- Given the strategic goals, which performance improvement opportunities from Step 1 should be prioritized? Where should investments be made versus cuts?
- What are the implications for sequencing opportunities and investments? How can the strategy compass inform the roadmap?
- What uncertainties should be accounted for, and what are your contingency plans?

Considerations like these are the basis of informed scenario planning, which weaves strategy, finance operations, and capital investments harmoniously across functions for a collective objective.

> ***Example:*** *Hospitals should green-light projects aligned to a larger strategic plan (e.g., expand a given service line) and, in tandem, prioritize corresponding performance improvement initiatives (e.g., optimizing remaining service lines, etc.). This strategic approach will not only help improve current positioning but also enable hospitals to provide services tailored to the needs of their unique patient populations while increasing their financial resiliency.*

Step 3. Engage with state agencies to configure and fine-tune the regional health care delivery ecosystem

We observe that regulatory bodies and legislatures are providing increasing levels of financial support to health systems in the form of subsidies and grants such as Disproportionate Share Hospital template (federal), Vital Access Provider (New York State), 1115 waiver funds (federal used widely by states), and more.[3] Such funds have the opportunity to be put to maximum use to improve access and enhance the quality of care. Absent coordination at the regional level, there is a potential risk that these funds might promote duplication of resources or even bolster undue competition. To help prevent this, state leaders can assume an active role in facilitating regional health care delivery planning.

Many jurisdictions employ the Certificate of Need process to provide a demand-based coordination of resources. Such provisions and frameworks may be useful but not always sufficient for regional planning since they only regulate a subset of clinical services.

We propose that health systems look beyond individual planning efforts and engage in broader regional planning in collaboration with state health agencies.

Health systems may look to the following areas of coordination and collaboration:

Access to clinical services

- Where is access to services limited for particularly vulnerable populations such as Medicaid beneficiaries?
- In each region, how, where, and by which health care organization should such services be provided? How can health systems strategically coordinate and share in the provision of a patient's care across primary care, acute care, and post-acute care?

Grants and investments in assets

- Contingent on responses to the above questions, what services are vital, and which provider organizations need to be made whole for providing those services?
- Which regionally important facilities need to be modernized? Are there opportunities for state agencies to facilitate access to strategic capital to improve regional care delivery?

Policy and procedure updates

- Where are current regulatory policies advancing the goals of the state in health care, and in which areas might policies be hindering these goals?
- What processes and mechanisms can improve collaboration between regulatory bodies and public health delivery organizations?

Regional coordination may (a) create a more efficient and optimized regional health care ecosystem by judiciously directing funds in a way that avoids duplication, and (b) improve the resiliency of individual health care organizations through targeted financial support for vital services.

Through closer collaboration with health care delivery organizations, state regulatory agencies may participate in shaping the regional care landscape. For example, agencies can access aggregate data and analytical tools that would be unavailable to individual organizations. Additionally, senior staff members can insert perspectives from multiple angles without breaching competitive lines.

Engaging in such collaboration requires building trust among parties while acknowledging the common objective of promoting healthy communities. Collaboration between health care organizations and regulators may seem unconventional, but we have seen it done successfully.

Acknowledgments

David Betts, Keara Klinepeter, Stephanie Serafino
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Endnotes

1. Yang Wang, Ge Bai, and Gerard Anderson, "U.S. hospitals' administrative expenses increased sharply during COVID-19," Journal of General Internal Medicine 38, no. 8 (June 2023): pp. 1887–93
2. New AHA report finds financial challenges mount for hospitals & health systems putting access to care at risk,
3. Examples of subsidies: Disproportionate Share Hospital (DSH) payments, Directed Payment Templates (DPTs), construction capital grants, IT modernization grants, etc.

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