

KaufmanHall

Commissioned by



**California
Hospital
Association**

Current State of California Hospital Finances

May 2024

Agenda

1. Executive Summary of Findings
2. California Hospital Margin Overview
3. California Hospital Expense Overview
4. California Hospital Revenue Overview
5. California Hospital Volume Overview
6. Methodology

Executive Summary

California Hospital Performance Continues to Be Challenged

In recent years, California hospitals and health systems have taken unprecedented steps to care for their communities amid significant pressure on staff and resources.

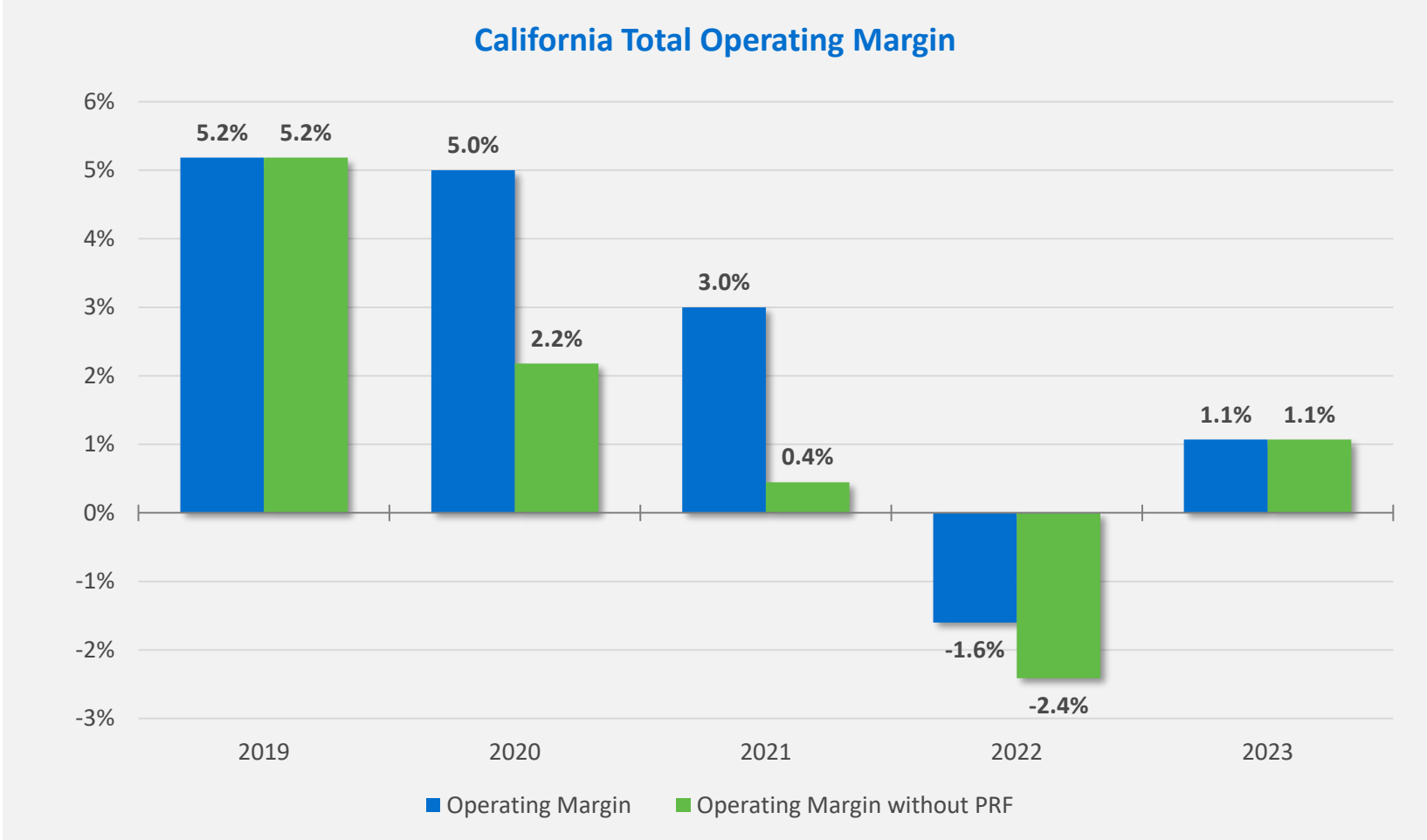
As hospital executives, policymakers, and other healthcare leaders assess the current landscape, key findings about the financial state of California hospitals through the end of 2023 include:

- **Hospital finances remain at risk.** Growing operating losses fueled by sicker patients, combined with declining cash balances and debt loads, are still placing many hospitals in unsustainable financial positions.
- **Margins remain depressed relative to pre-pandemic levels.** Throughout 2023, the hospital operating margin for California remained below its 2019 value, with 70% of hospitals experiencing low or negative operating margins.
- **Hospitals are still experiencing major financial challenges, with no further relief in sight.** Hospitals incurred serious losses relative to pre-pandemic levels—including approximately \$4.7 billion in 2023. Since 2020, hospitals have lost a combined \$25.3 billion.
- **Expenses are still significantly elevated from pre-pandemic levels.** Total expenses in 2023 for California hospitals were \$28.9 billion higher than pre-pandemic levels, outpacing increases in revenue. Rising expenses for labor, medical supplies, and purchased services have contributed to the increase.
- **Hospitals are treating patients with more severe health needs, which is driving higher expenses.** Hospital discharges, ED visits and patient days have returned to—or are slightly above—pre-pandemic levels. However, a significant rise in length of stay suggests that patients who visited hospitals had more severe health needs than prior to the pandemic. Furthermore, labor shortages in post-acute settings and prior authorization policies have prevented timely discharge of patients from the hospitals, leading to an increase in expense without a commensurate increase in revenue.

This report was prepared at the request of the California Hospital Association.

Margins

Hospital Operating Margins Remain Below Pre-Pandemic Levels

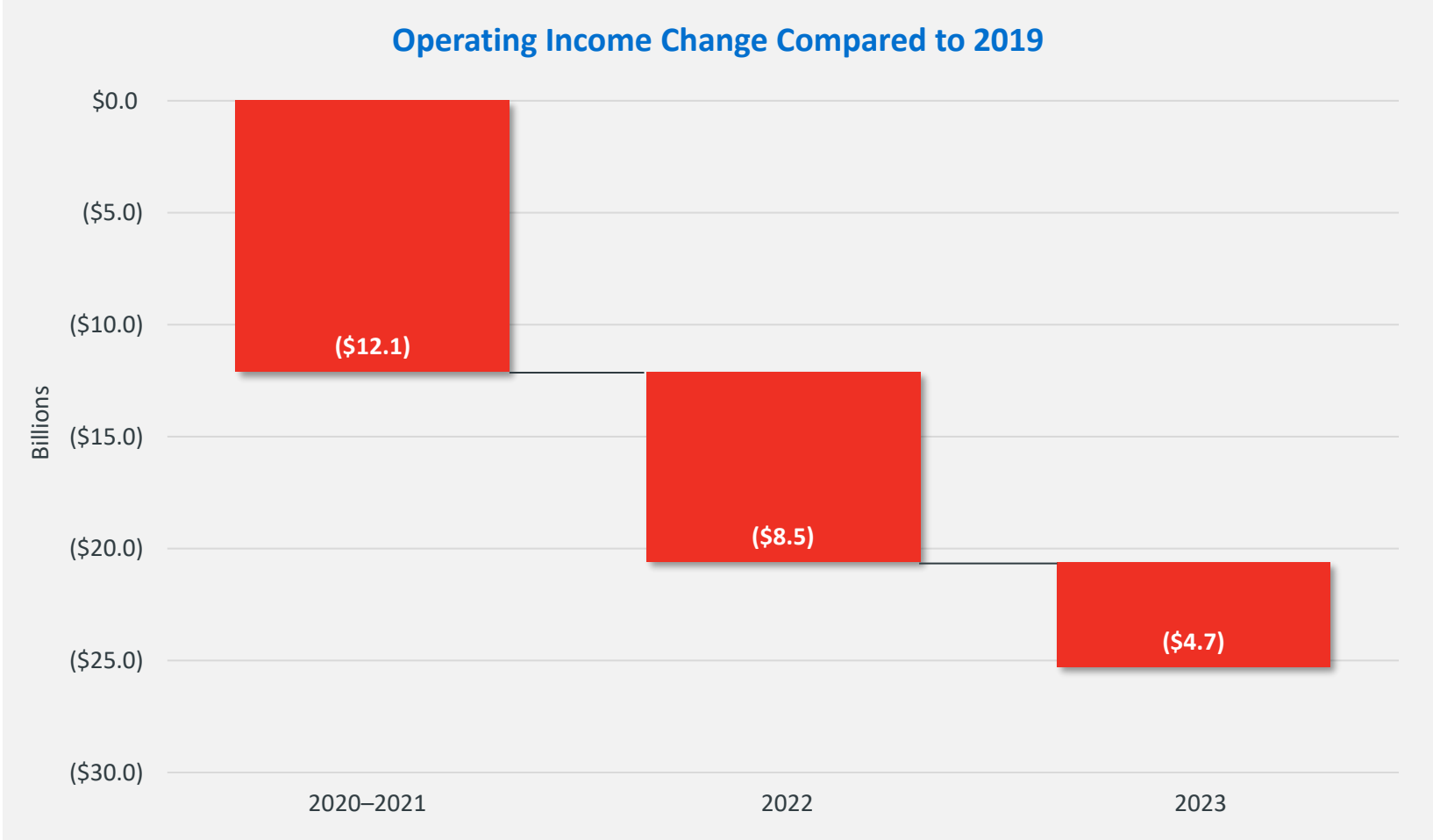


KEY TAKEAWAYS

- California hospital operating margins were approximately 1.1% in 2023.
- Operating margins remain below their 2019 values of 5.2% due to historic expense growth.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Total California Hospital Operating Income in 2023 Was \$4.7 Billion Below Pre-Pandemic Levels

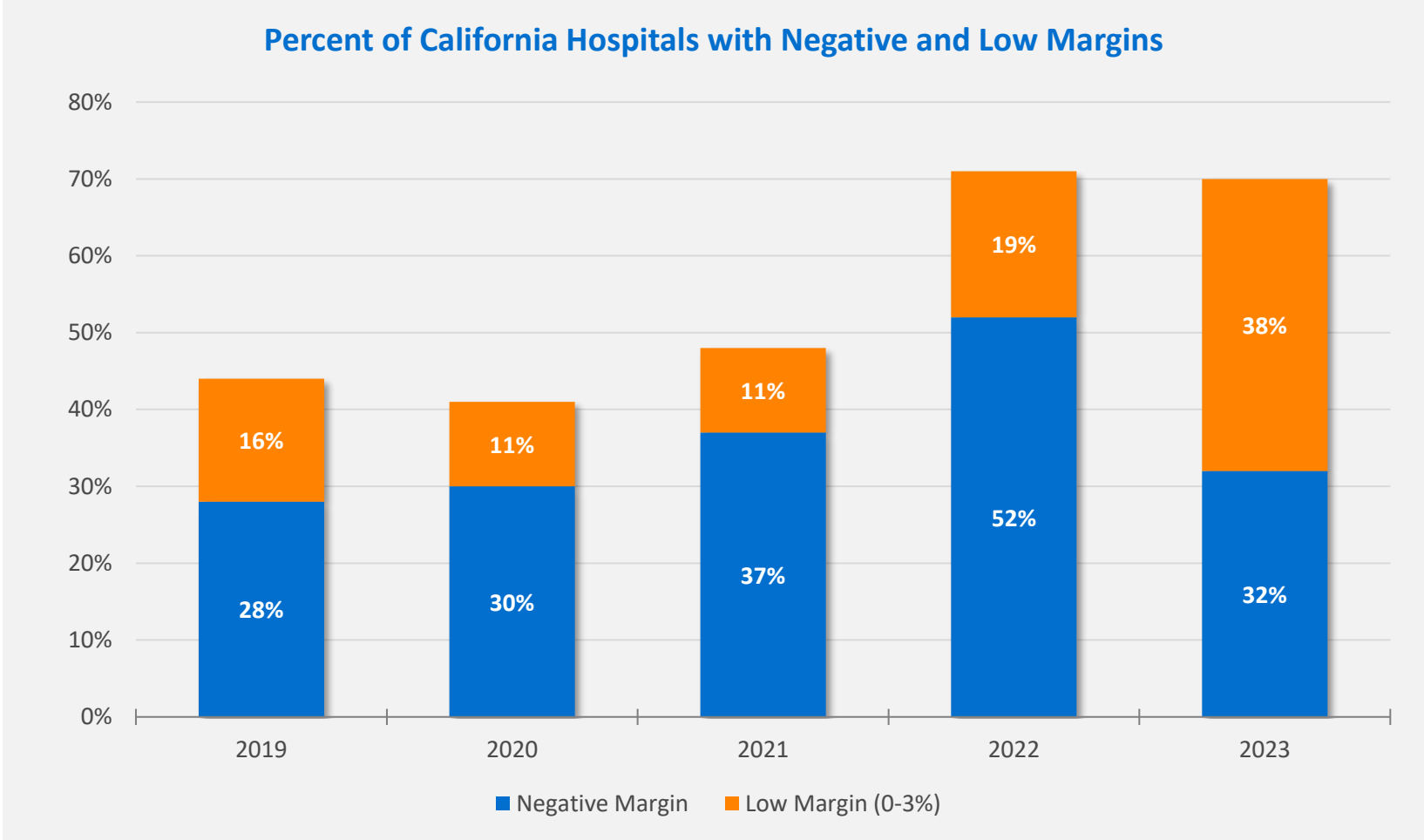


KEY TAKEAWAYS

- California hospitals lost \$4.7 billion in 2023 compared to 2019 operating income.
- Since 2020, California hospitals have a combined total of \$25.3 billion in operating income losses.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

70% of California Hospitals Have Unsustainably Low Margins

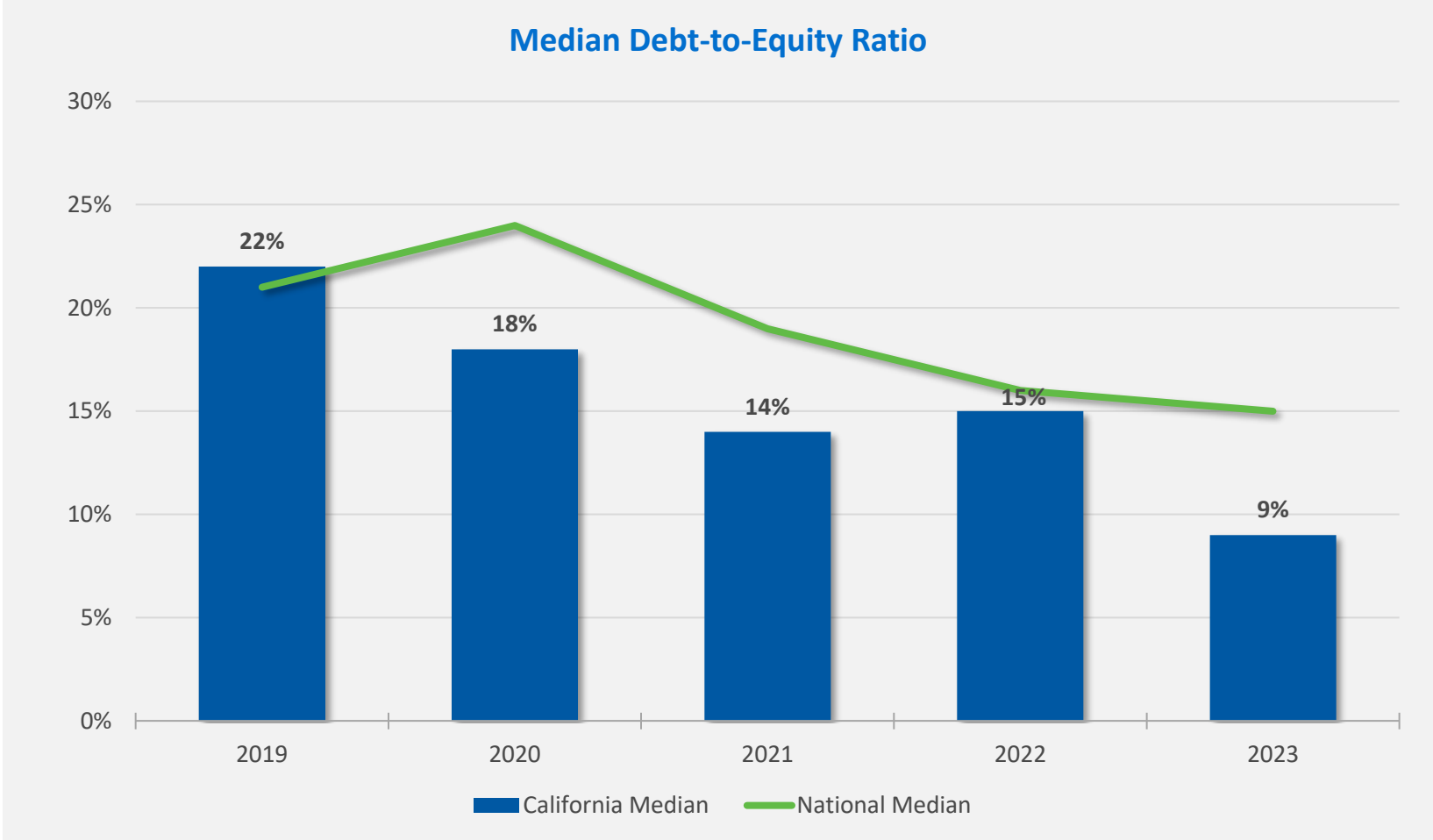


KEY TAKEAWAYS

- The percentage of low margin California hospitals is still far above pre-pandemic levels.
- Seventy percent of hospitals currently have margins at or below 3%, a measure of unsustainably low margins, the cash flow generated is usually insufficient to fully support capital needs, strategic investment, and grow reserves.
- The total proportion of hospitals with unsustainably low margins has not significantly changed since 2022.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solution, now part of Strata, and Definitive Health.

Over the Course of the Pandemic, the Debt-to-Equity Ratio of California Hospitals Fell Below National Levels



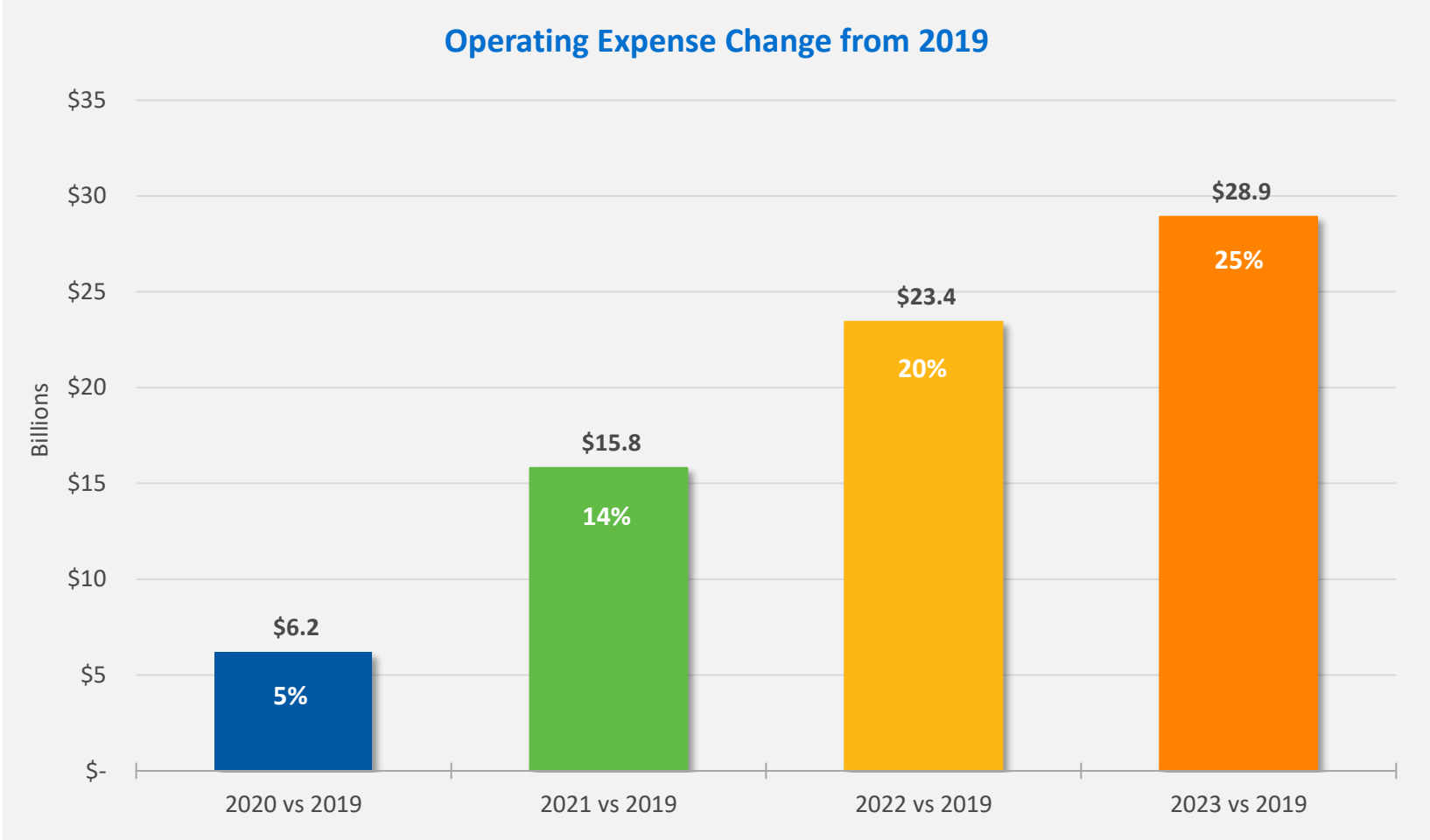
KEY TAKEAWAYS

- In 2023, the median debt-to-equity ratio of California hospitals was 9% as compared to a national median of 15%.
- While the debt-to-equity ratio of California hospitals was slightly above the national median in 2019, they have consistently outperformed the national median since 2020, indicating a lower reliance on debt to continue operations than seen nationally.

Source(s): Findings sourced from Definitive Health.

Expenses

In 2023, Operating Expenses Were \$28.9 Billion Above Pre-Pandemic Levels

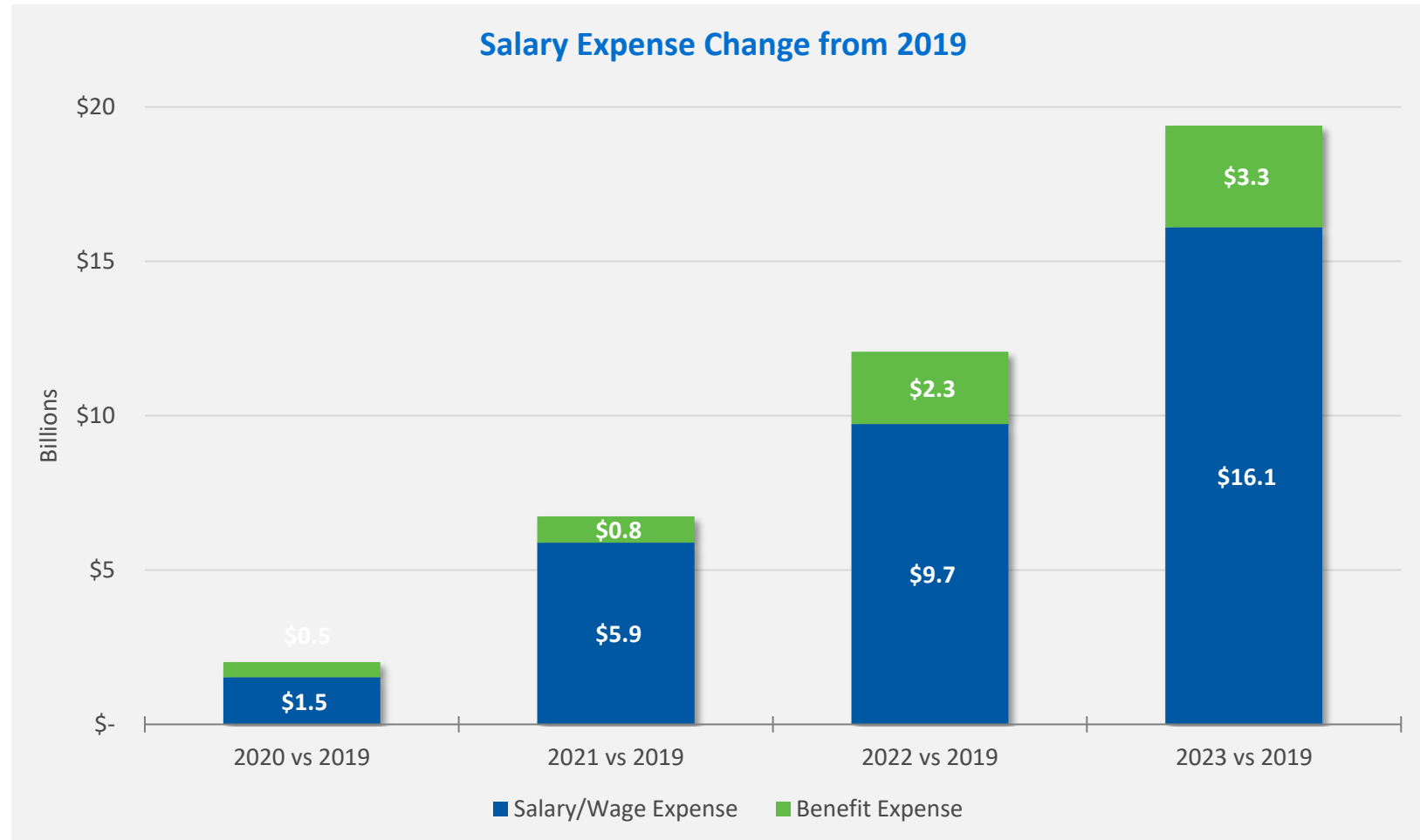


KEY TAKEAWAYS

- Total hospital operating expenses have climbed significantly since the start of the pandemic, reaching \$28.9 billion above 2019 levels in 2023.
- Rising operating expenses are driven by multiple factors, many of which are outside of hospitals' immediate direct control, including costs for labor, supplies, drugs and purchased services.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Rising Labor Costs: A \$19 Billion Increase in Salary and Benefit Expense in 2023 Compared to 2019

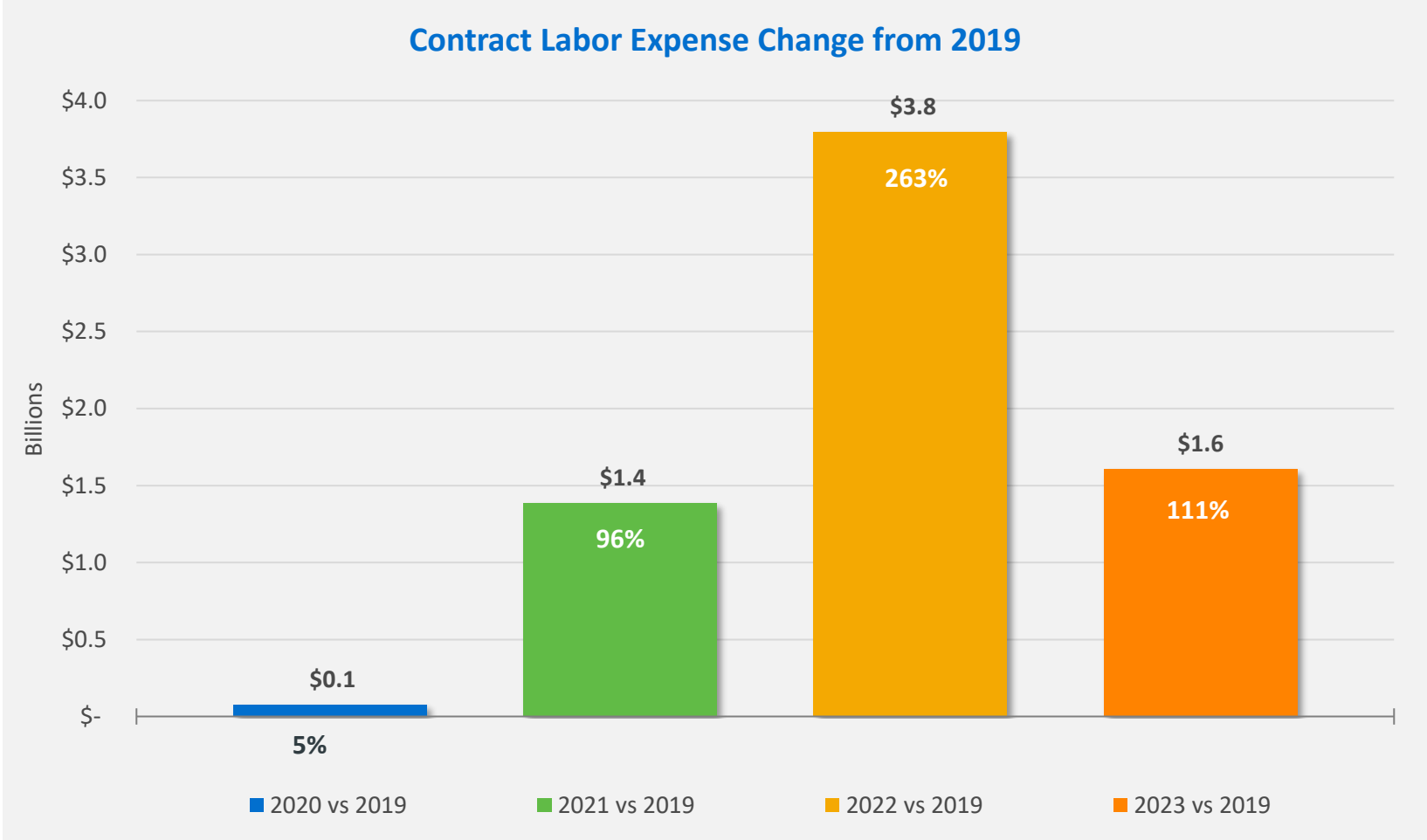


KEY TAKEAWAYS

- Salaries accounted for roughly 85% of the increase in labor expense in 2023 compared to pre-pandemic levels.
- After more modest increases in previous years, salary expense increases rose more than 34% above pre-pandemic levels in 2023, while benefit expense rose more than 28%.
- Employee turnover reached 36% in 2023 from 25% in 2019, fueling increases in salaries and benefits as well as contract labor expenses.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Contract Labor Costs Are Still More Than Double Pre-Pandemic Levels

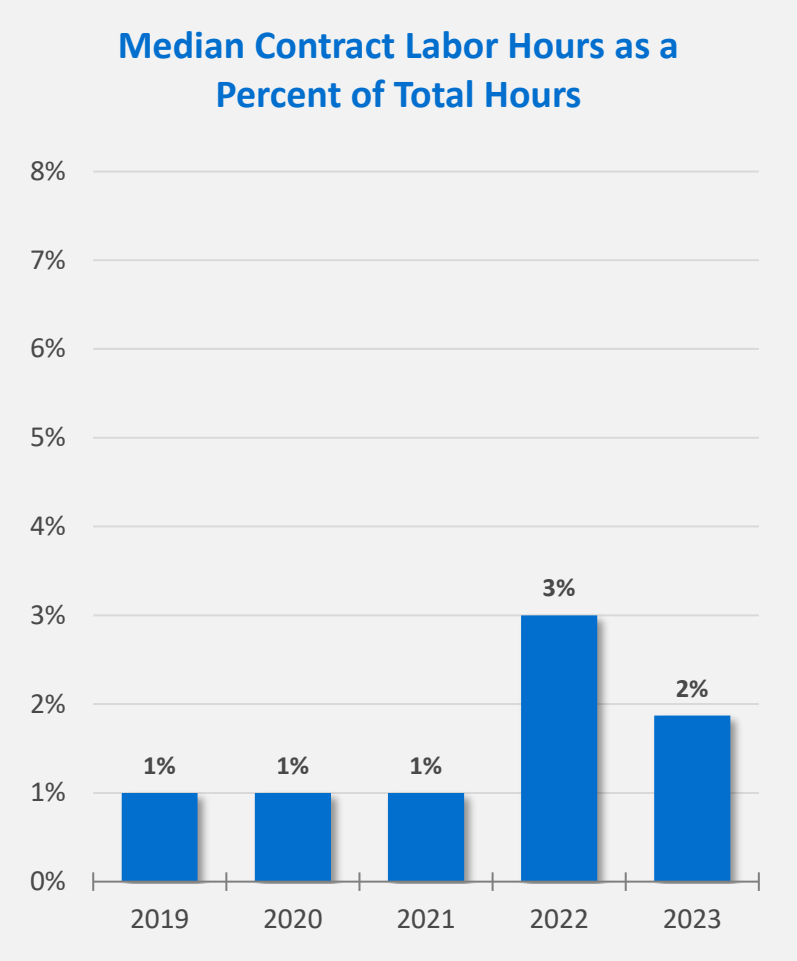
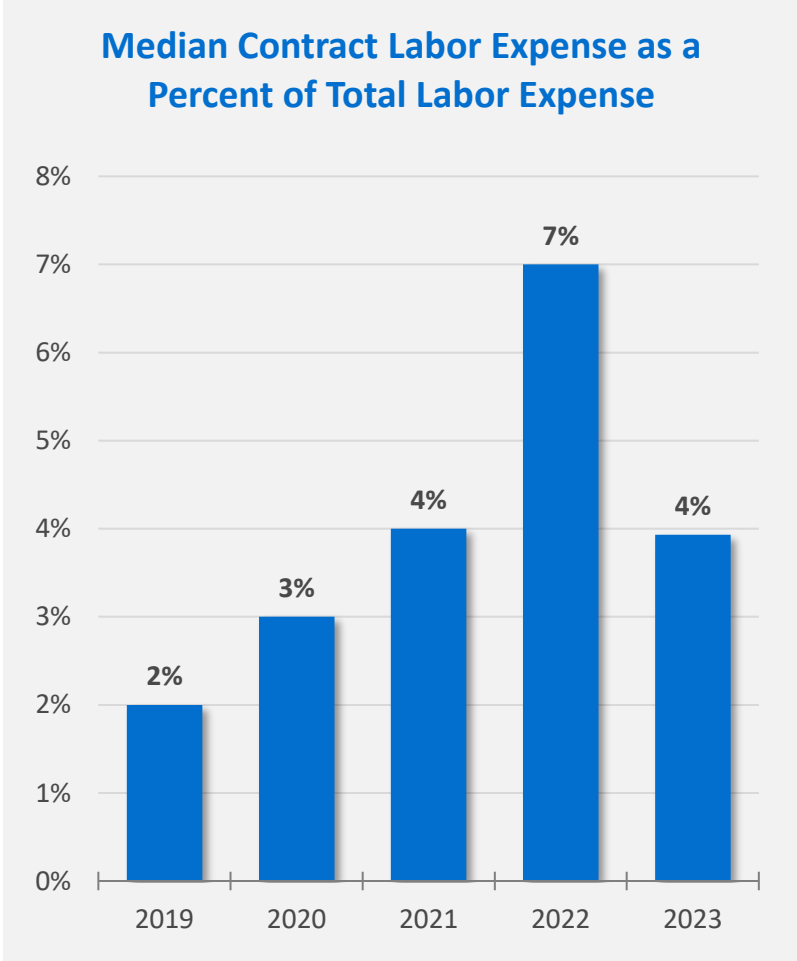


KEY TAKEAWAYS

- Contract labor expenses for California hospitals remain significantly above pre-pandemic levels. In 2023, spending for contract labor was \$1.6 billion higher than in 2019.
- In the four years since the start of the pandemic, California hospitals have collectively spent more than \$6.9 billion more in contract labor compared to 2019 levels.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Contract Labor Expenses Remain Highly Elevated

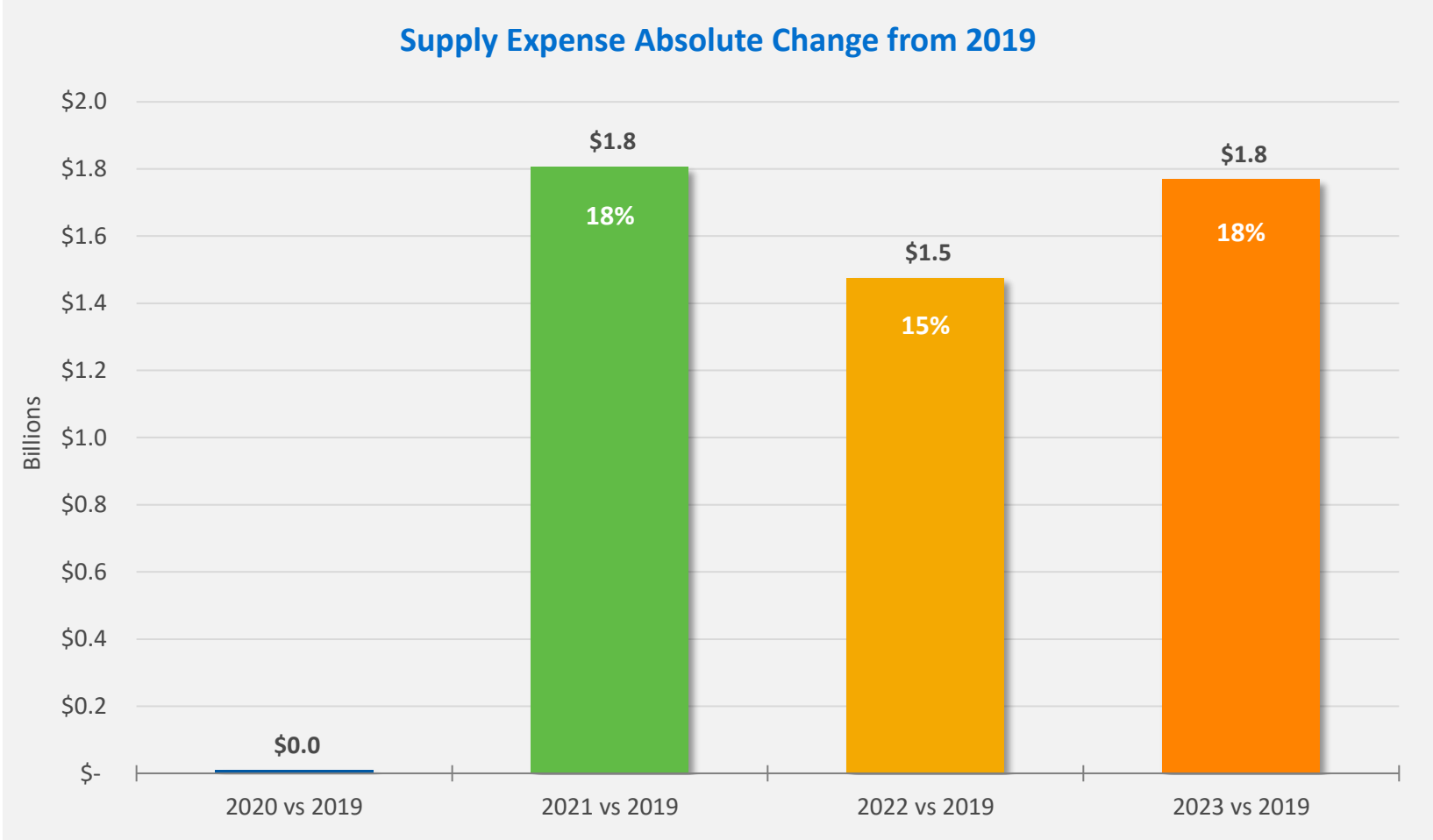


KEY TAKEAWAYS

- Median contract labor expense as a percent of total labor expense in California was 4% in 2023, while median contract labor hours as a percent of total hours was 2%.
- The median contract labor wage rate in California has decreased to \$116 from its high of \$132 per hour in 2022, but still greatly exceeds the 2019 rate of \$81.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata.

In 2023, Supply Expenses Were \$1.8 Billion Above 2019 Levels

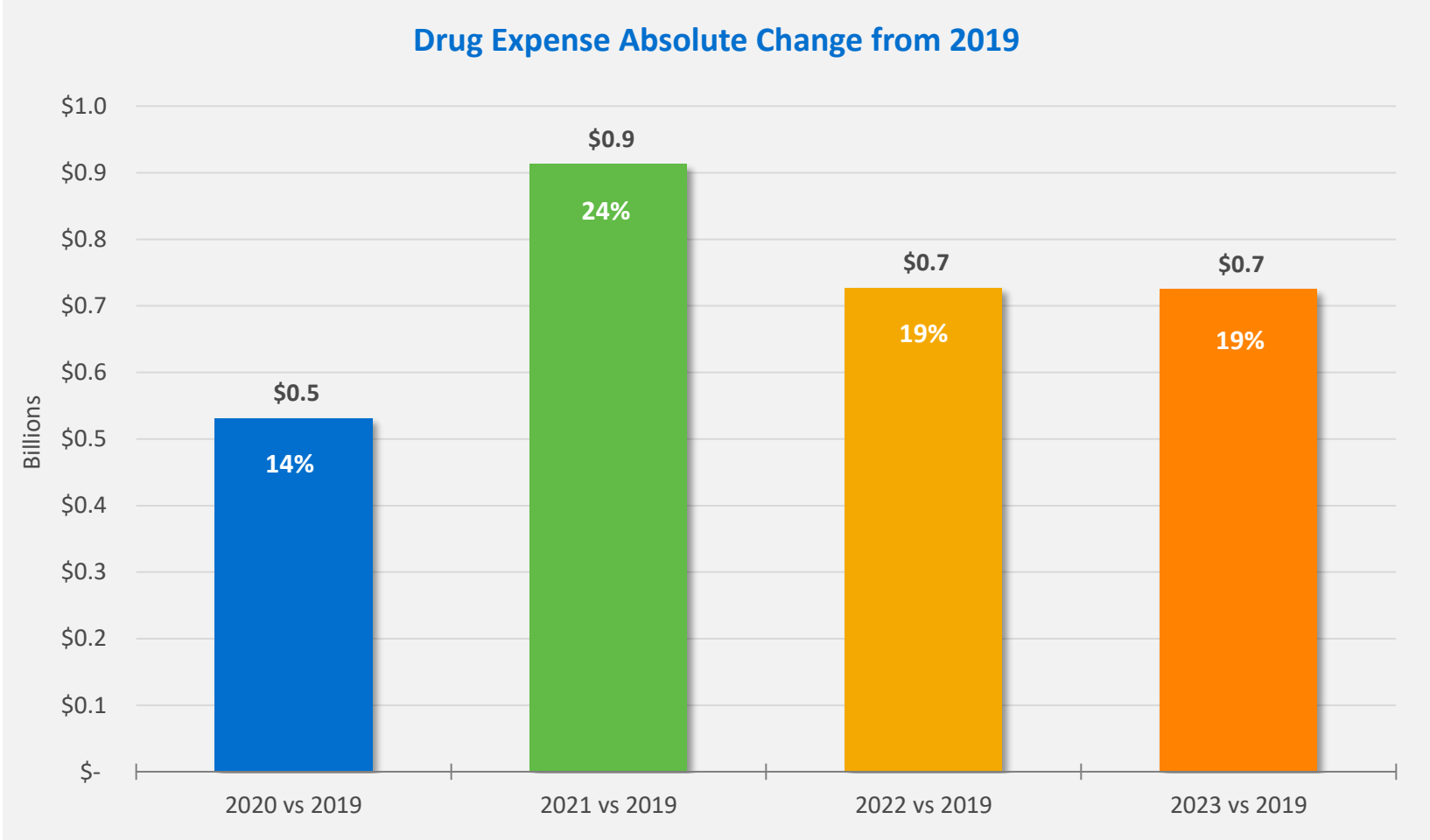


KEY TAKEAWAYS

- California hospital supply expenses increased by nearly \$1.8 billion in 2023, or 18%, compared to 2019.
- Since 2020, California hospitals have collectively spent \$5.1 billion more on supplies compared to 2019 levels.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.
Note(s): Percentages represent the percent change compared to 2019.

Drug Expenses Are Also Elevated From 2019 Levels

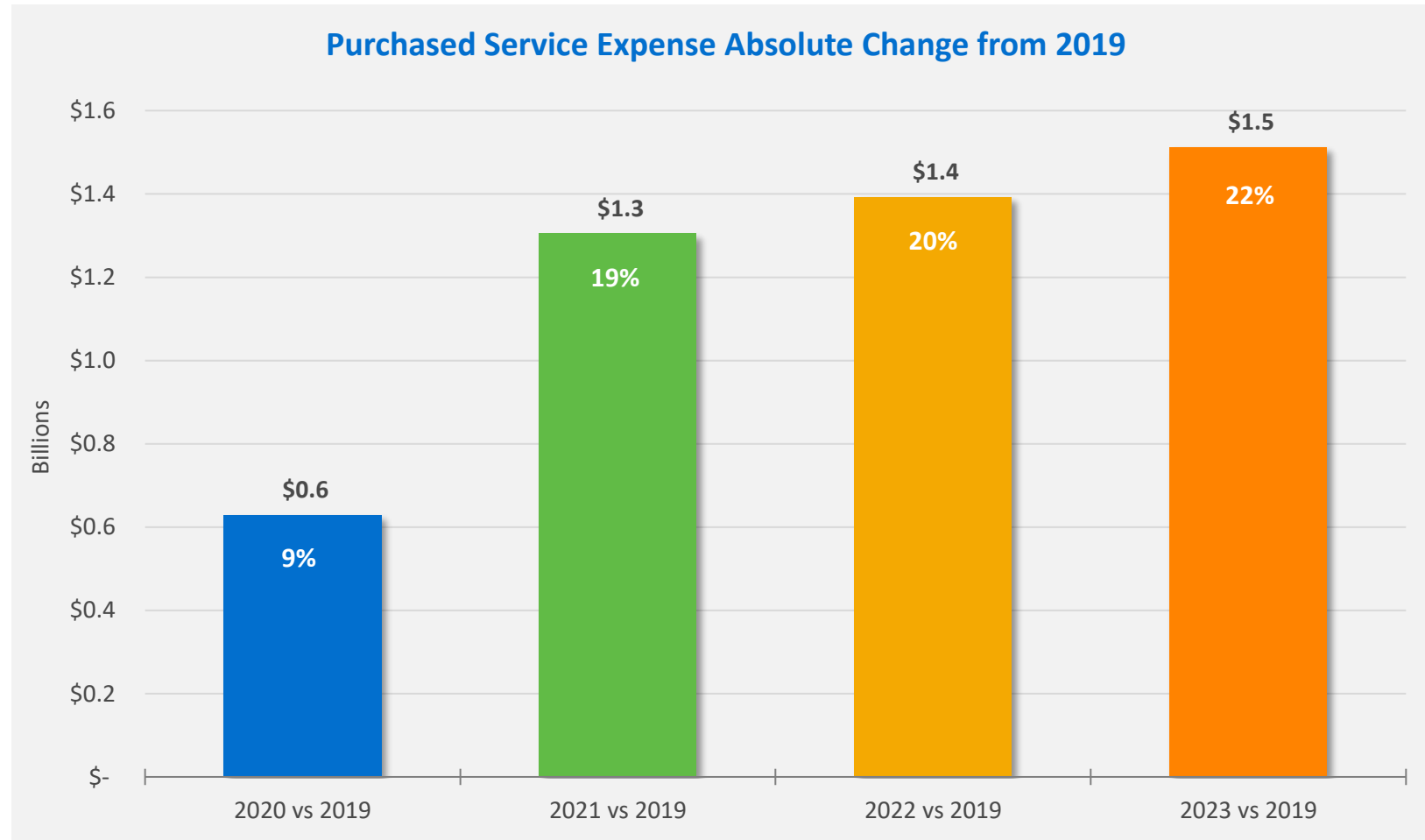


KEY TAKEAWAYS

- Drug expenses for California hospitals in 2023 were \$725 million above pre-pandemic levels.
- California drug expenses increased by 19% compared to 2019 levels in 2023.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.
 Note(s): Percentages represent the percent change compared to 2019.

Purchased Service Expenses Also Remain Above 2019 Levels



Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

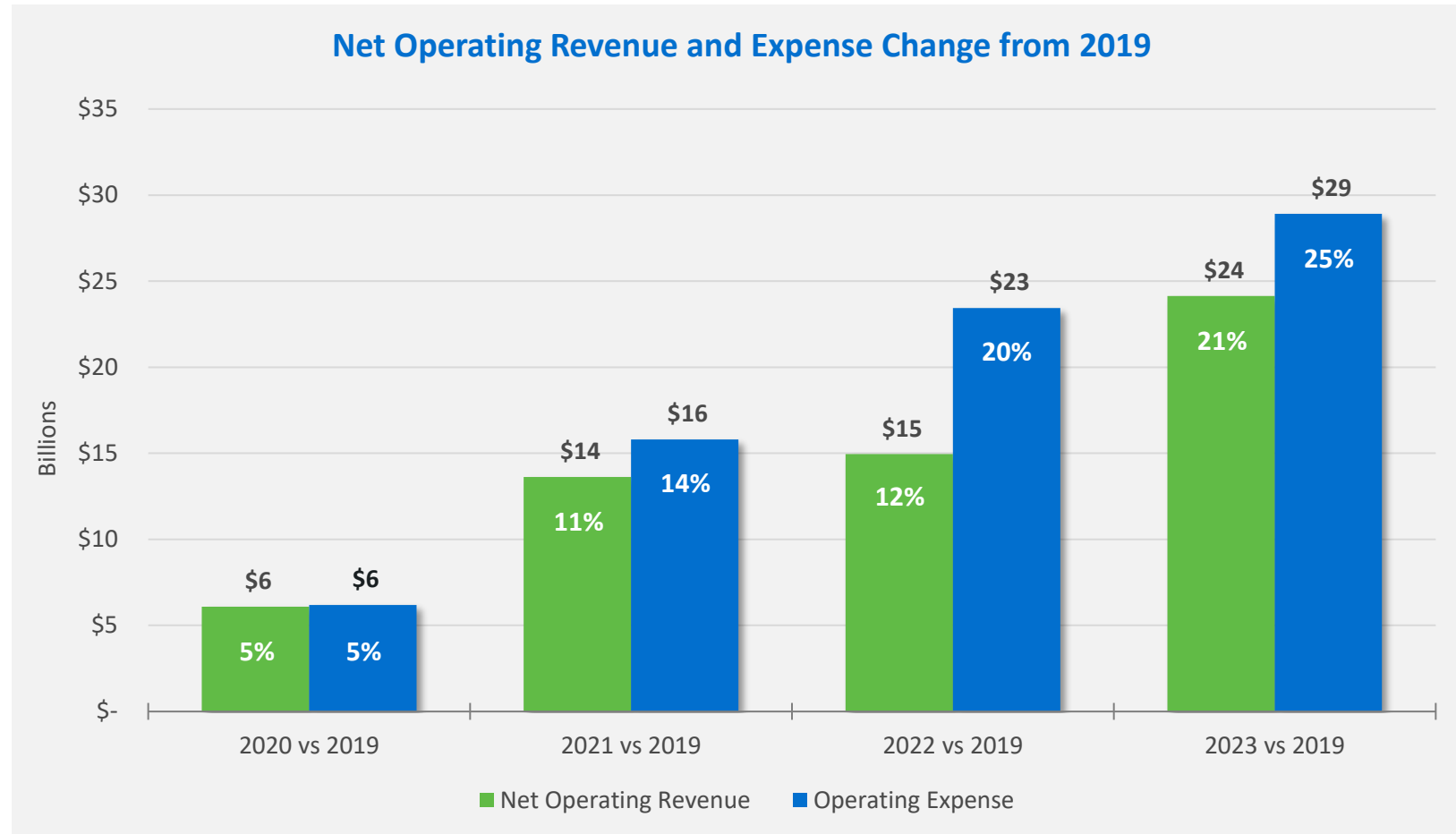
Note(s): Percentages represent the percent change compared to 2019.

KEY TAKEAWAYS

- California purchased service expenses increased by 22% in 2023 compared to 2019 levels, continuing a trend of exceeding national medians throughout the pandemic.
- Purchased services include vendor expenses that support operations including software, marketing, recruitment, laundry, management fees, and maintenance.
- Since 2020, cumulative increases in purchased service expenses relative to 2019 levels amount to \$4.8 billion.

Revenues

Expense Growth Continues to Outpace Revenue Growth



KEY TAKEAWAYS

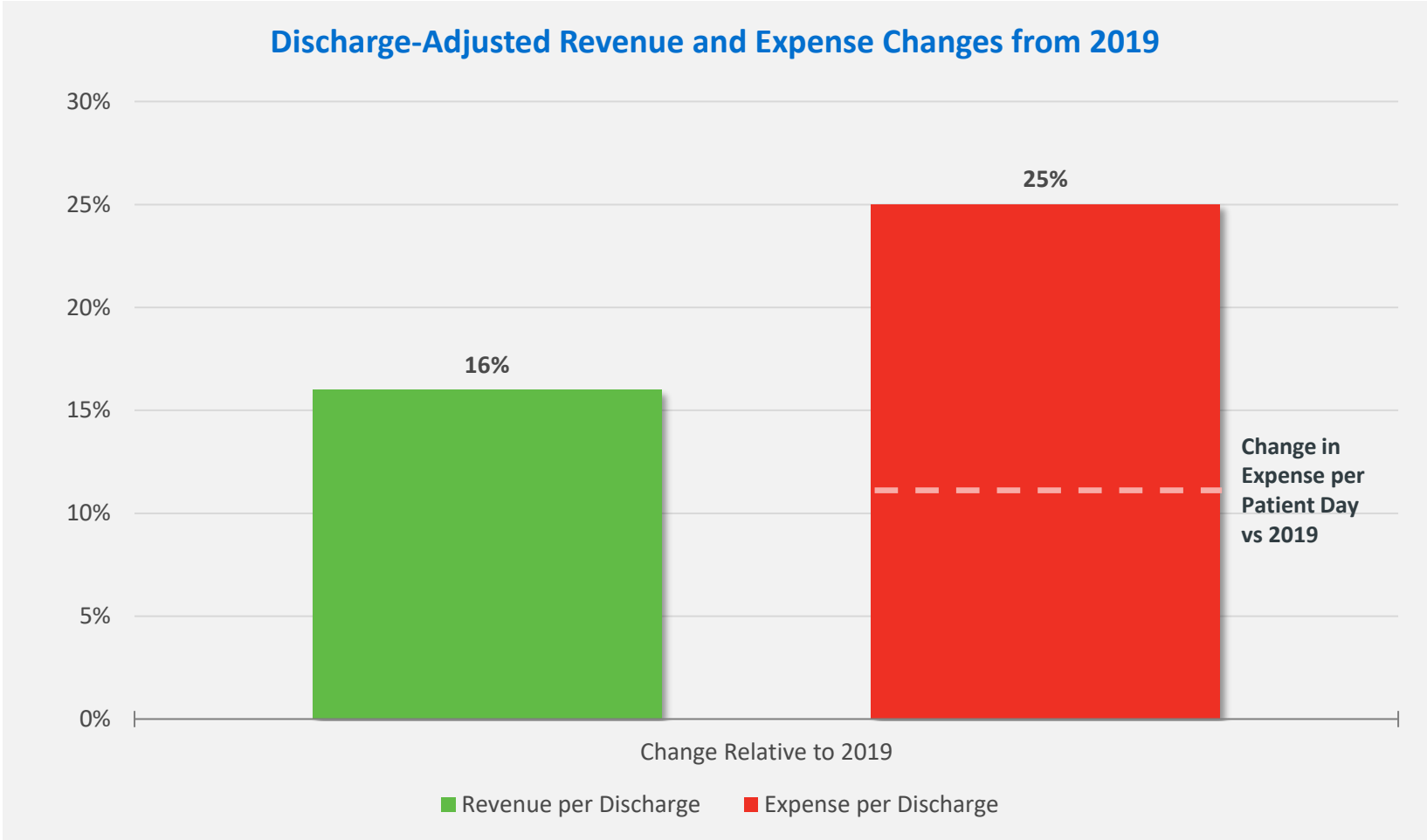
- While California hospital net operating revenues have grown since 2020, the increase in expenses outpaced the increase in revenues.
- Payments made to California hospitals in 2020 and 2021 from the Provider Relief Fund (PRF) contributed to the increase in hospital net operating revenues and helped hospitals cover their increasing operating expenses.

Source(s): 1) Absolute change in California hospital net operating revenue and expense were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Note(s): 1) Net operating revenue is calculated by taking the gross operating revenue less any deductions.

2) Percentages represent the percent change compared to 2019.

Volume-Adjusted Expenses Outpaced Revenues in 2023



KEY TAKEAWAYS

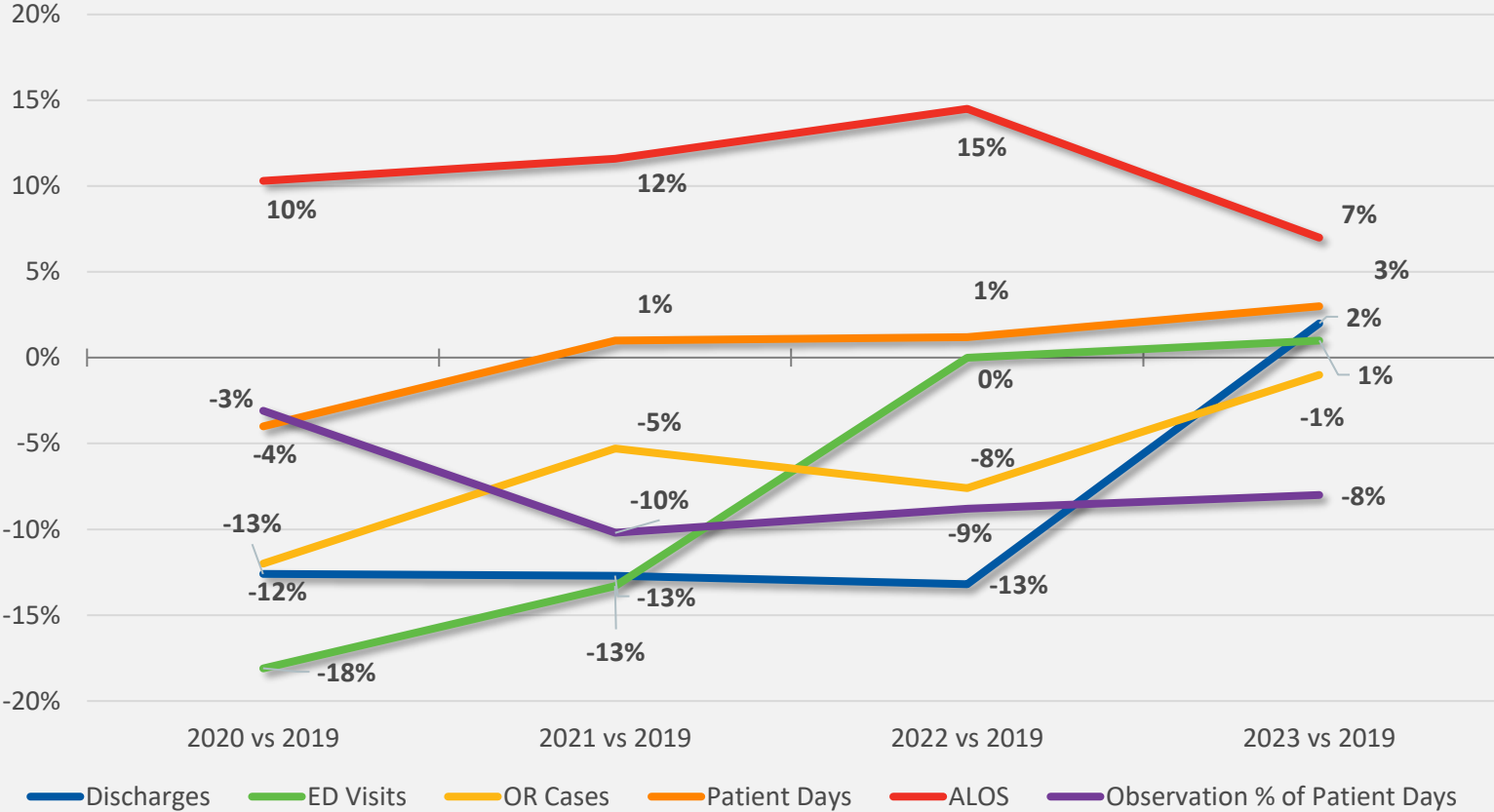
- While revenues and expenses have increased relative to pre-pandemic levels, expenses in 2023 rose more than revenues, leading to the decline in operating margin.
- The increase in expense per discharge reflects not only a 12% increase in expense per patient day, but also increased lengths of stay relative to 2019.
- Increased lengths of stay signify sicker patients, a change not reflected in payments to hospitals.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Volumes

Patient Days Grew Faster Than Discharges, Stressing Hospital Finances

Hospital Volumes Median Percent Change from 2019



KEY TAKEAWAYS

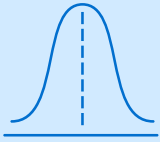
- As care continues to shift out of the hospital, operating room cases remained lower than pre-pandemic levels in 2023.
- The faster growth in patient days as compared to discharges has led to increased length of stays, as patients with more severe health needs are admitted.

Source(s): Findings produced by Kaufman Hall using data sourced from Syntellis Performance Solutions, now part of Strata, and Definitive Health.

Methodology

Methodology

1



Generated the Kaufman Hall Sample

50 California hospitals were sampled from data provided by Syntellis Performance Solutions, now part of Strata, and financial survey data from the California Hospital Association.

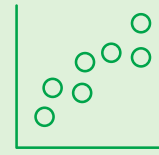
2



Computed the 2019 Baseline

Using data from Definitive Health, the total net operating revenue and operating expense for all critical access, acute care, and children's hospitals within the state of California were calculated for 2019.

3



Calculated Median Percent Change

The median year-over-year percent change was calculated from the Kaufman Hall sample for each metric.

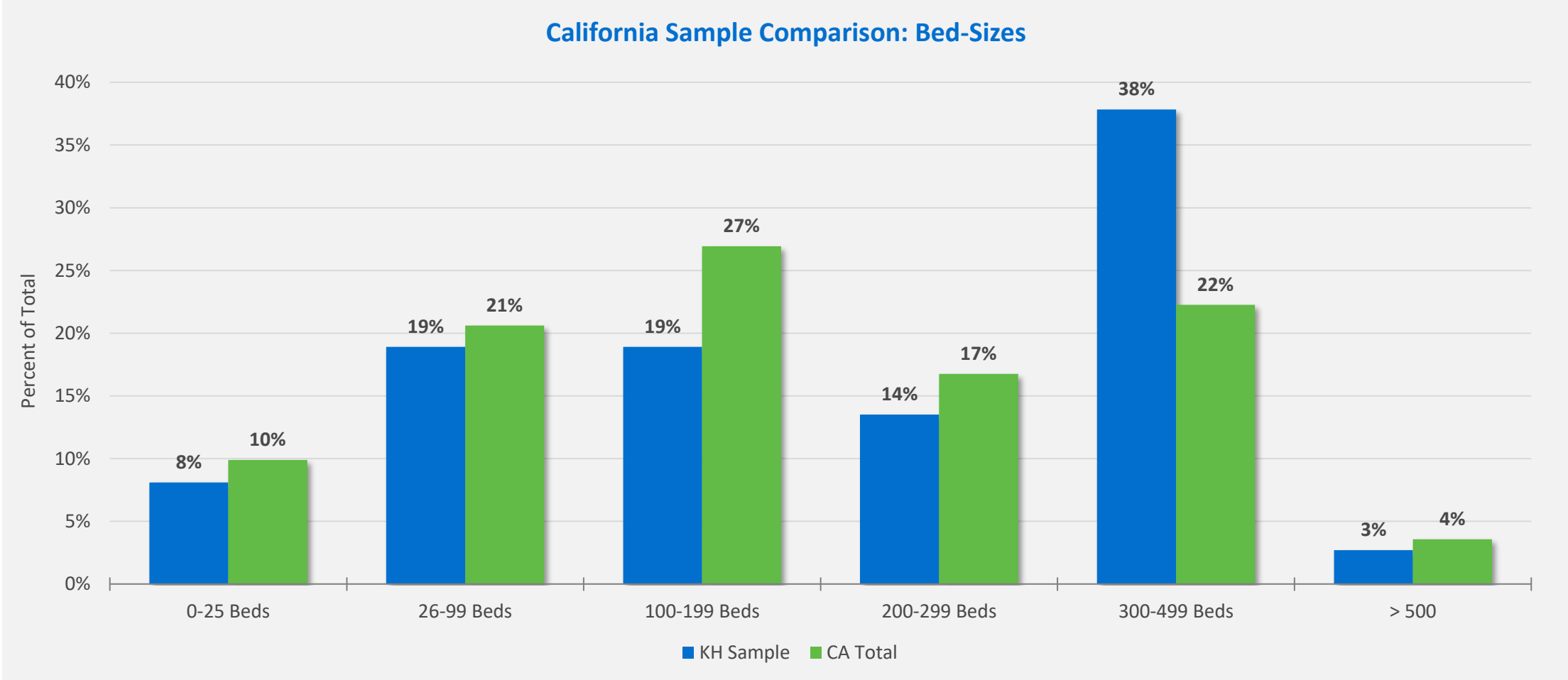
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Extrapolated the 2020 – 2023 Absolute Values

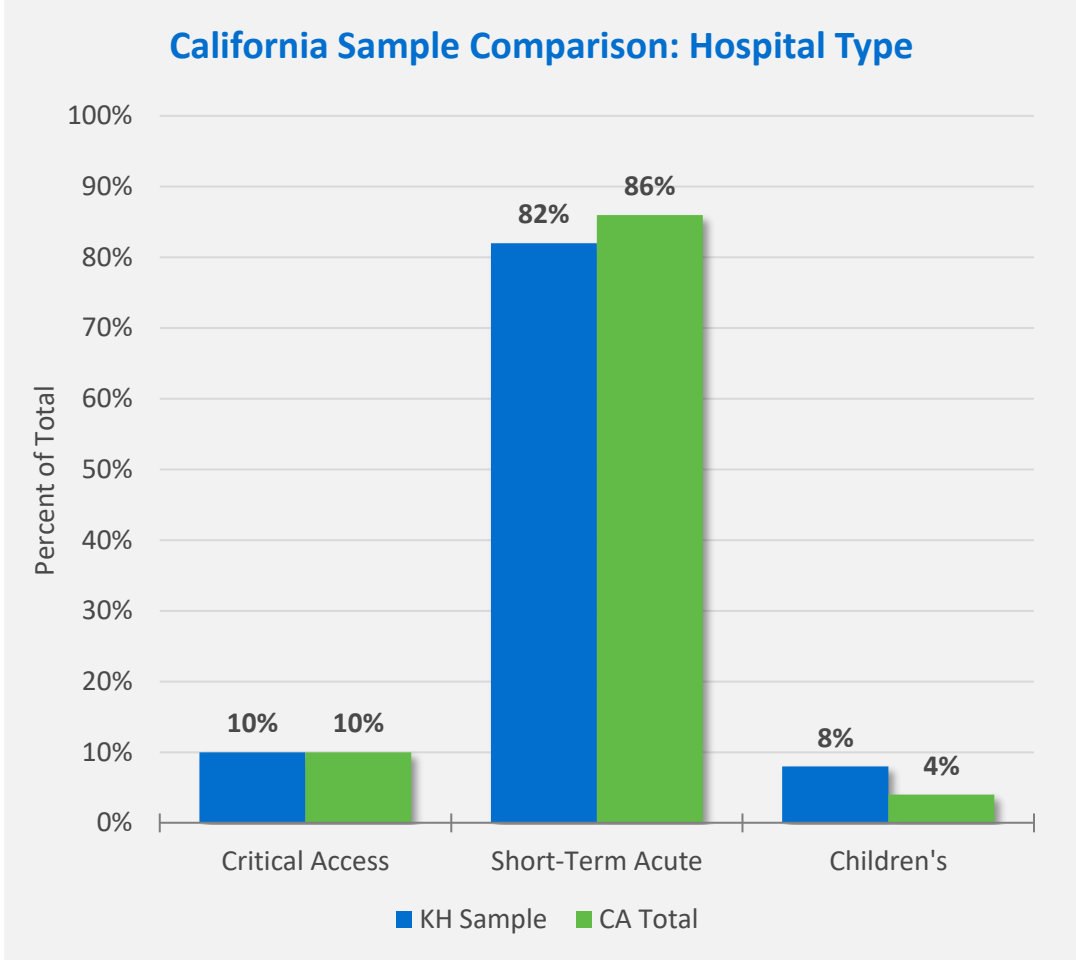
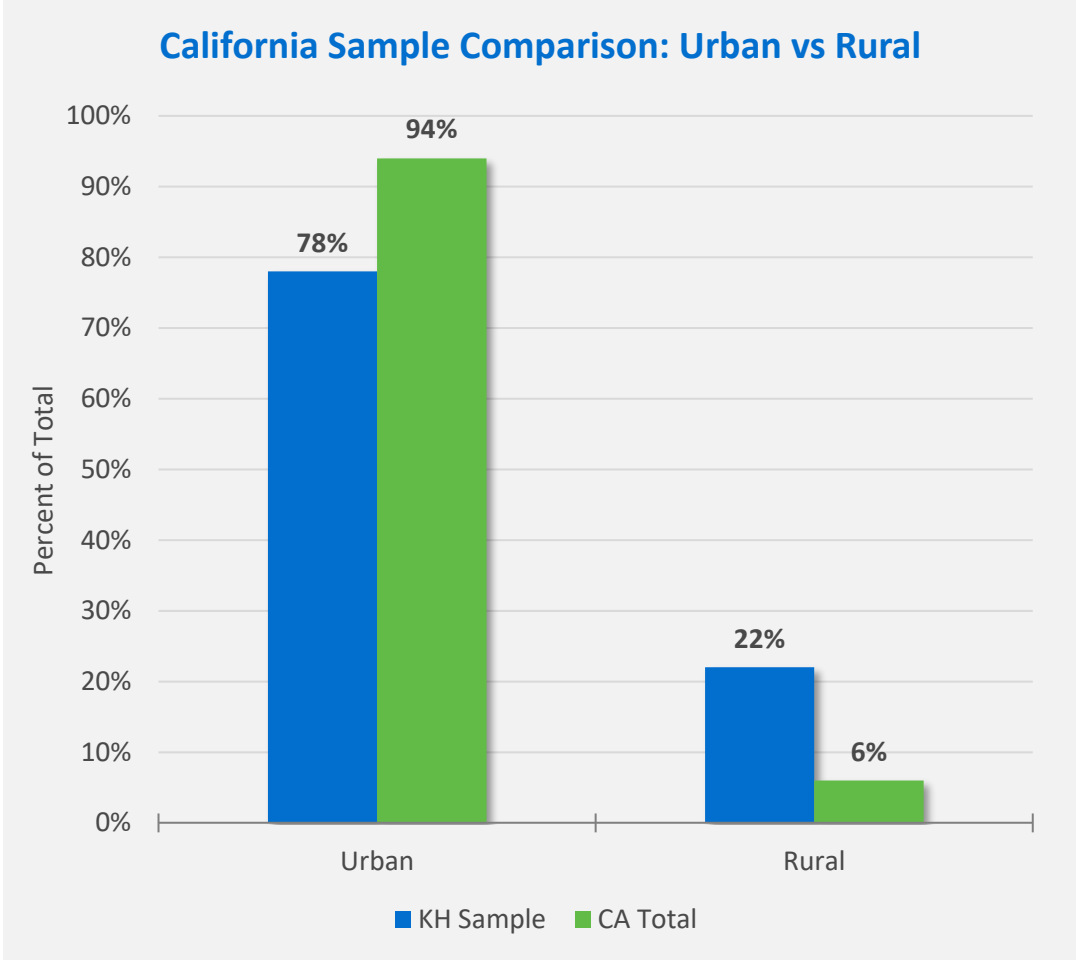
Extrapolated absolute change figures for 2020-2023 were calculated by applying the median year-over-year percent changes from the Kaufman Hall sample to the 2019 baseline metrics.

California Sample Characteristics: Bed-Size



Source(s): 1) Hospital counts for the "California Total" were pulled from Definitive Health.

California Sample Characteristics *(continued)*



Source(s): 1) Hospital counts for the "California Total" were pulled from Definitive Health.

Qualifications, Assumptions and Limiting Conditions (01.30.24):

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