

KaufmanHall



Current State of Kentucky Hospital Finances

March 2023

Agenda

1. Executive Summary of Findings
2. Kentucky Hospital Margins Overview
3. Kentucky Hospital Expenses Overview
4. Kentucky Hospital Revenues Overview
5. Kentucky Hospital Volumes Overview
6. Methodology

1. Executive Summary

Kentucky Hospital Margins Negative in 2022

Since the onset of the COVID-19 pandemic in March 2020, Kentucky hospitals and health systems have taken unprecedented steps to care for their communities amid significant pressure on staff and resources.

The financial impact of the pandemic has been staggering. As hospital executives, policymakers, and other healthcare leaders assess the current landscape, key findings about the financial state of Kentucky hospitals from the beginning of the pandemic through December 2022 include:

- **Margins remained depressed relative to pre-pandemic levels.** Throughout 2022, the hospital operating margin for Kentucky remained negative, resulting in the worst financial performance since the start of the pandemic.
- **Expenses were significantly elevated from pre-pandemic levels.** Total expenses in 2022 for Kentucky hospitals were \$4.2 billion higher than pre-pandemic levels, outpacing increases in revenue. Rising expenses for labor, medical supplies, drugs, and purchased services have contributed to the increase.

- **Hospital volumes remained below pre-pandemic levels.** Hospital discharges and emergency department (ED) visits in Kentucky hospitals were all lower than pre-pandemic levels. However, a significant rise in average 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 likely prevented timely discharge of patients from the hospitals, leading to an increase in expense without a commensurate increase in revenue.
- **Hospitals experienced a profound financial toll, with no further relief in sight.** Hospitals incurred serious losses relative to pre-pandemic levels—including approximately \$329 million in 2022—increasing strain on Kentucky hospitals and need for additional support.

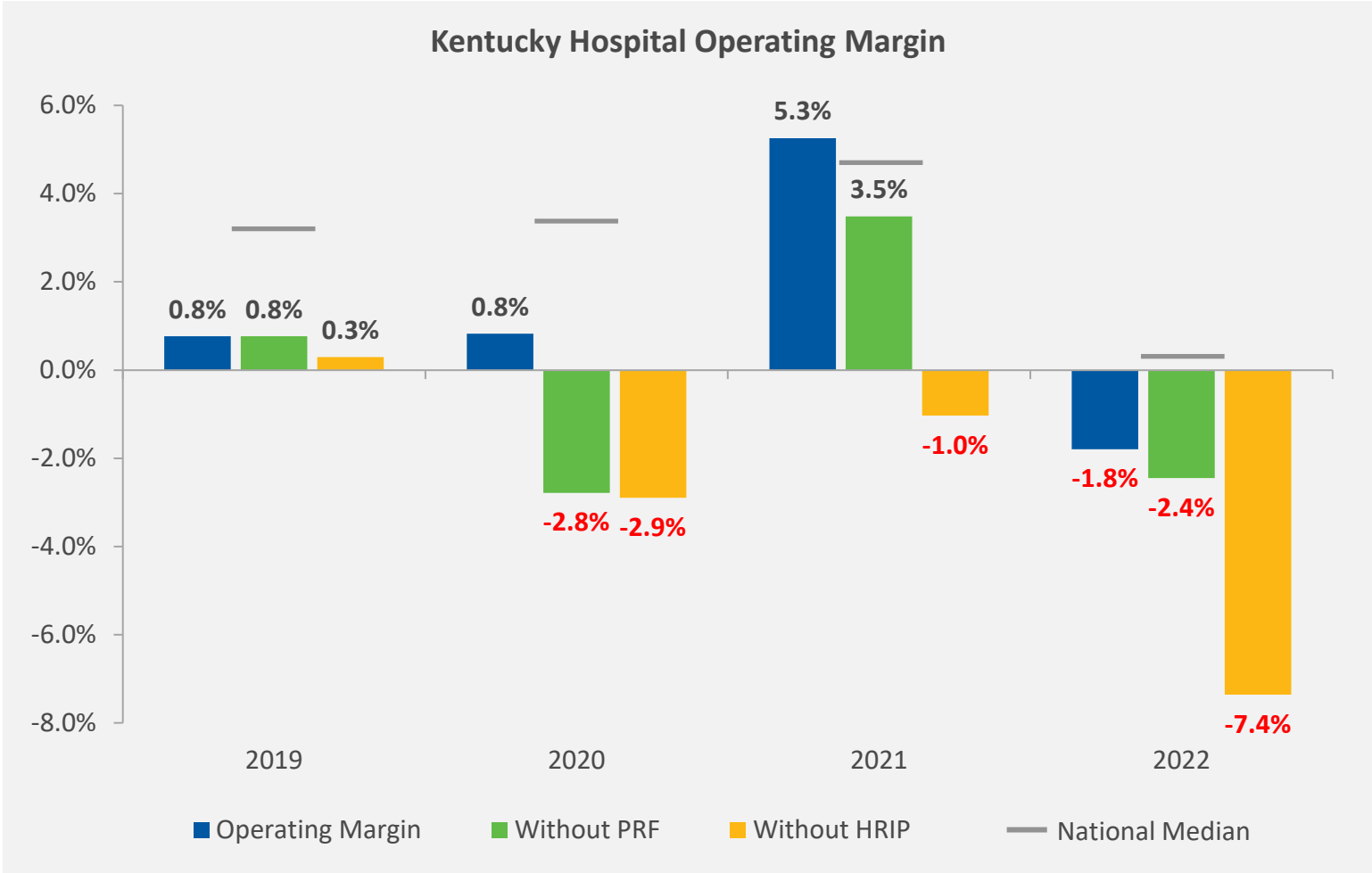
Hospitals faced a host of other related challenges, including workforce shortages and supply disruptions.

These findings underscore the existential financial and operational threats Kentucky hospitals continue to face three years after the beginning of the pandemic.

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

2. Hospital Margins

Hospital Operating Margins in 2022 Were Significantly Below Pre-Pandemic Levels

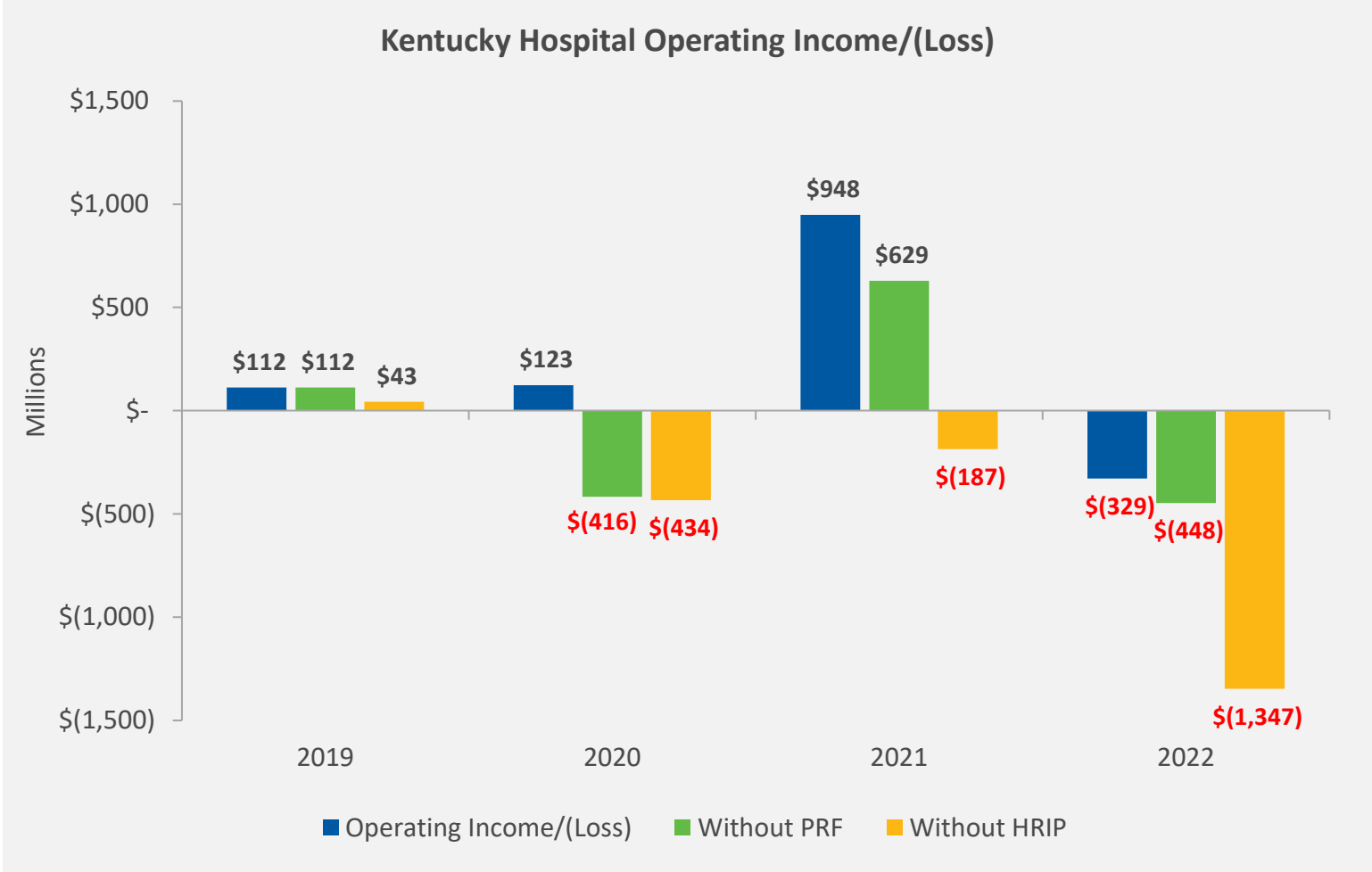


KEY TAKEAWAYS

- Total hospital operating margins for Kentucky in 2022 were significantly below pre-pandemic levels.
- Without one-time payments from the Provider Relief Fund (PRF), Kentucky operating margins fell to -2.8% in 2020 and -2.4% in 2022.
- Without the Kentucky Hospital Rate Improvement Program (HRIP) funds, Kentucky operating margins were even more depressed, falling to -2.9% in 2020 and -7.4% in 2022.
- Except for 2021 when the Kentucky HRIP funds were increased, the operating margin for the state of Kentucky was at or below the national median each year.

Source(s): 1) Kentucky hospital operating margins were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Kentucky Experienced Negative Hospital Operating Income in 2022 for the First Time Since the Beginning of the Pandemic

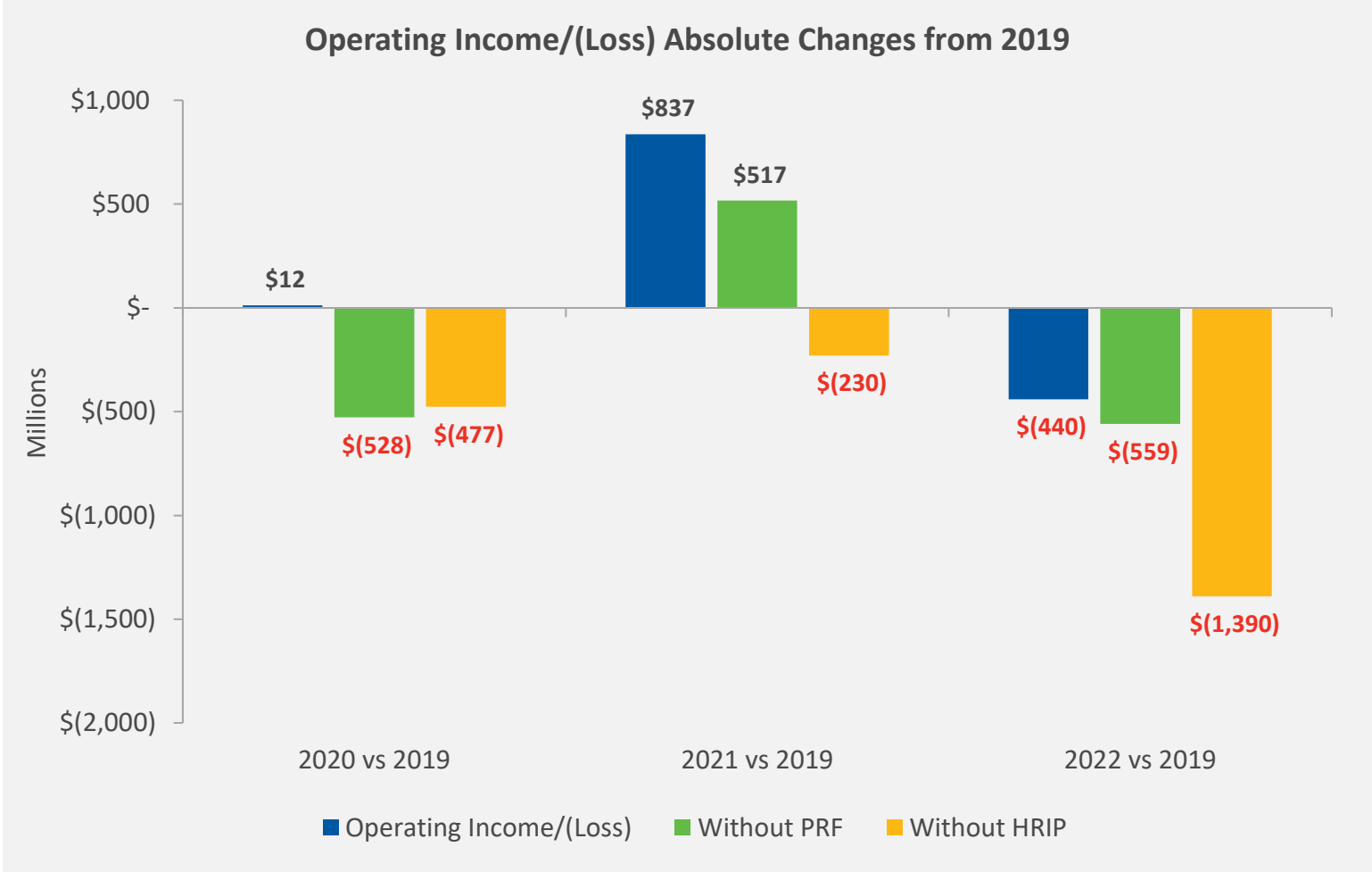


KEY TAKEAWAYS

- In 2022, Kentucky hospitals lost \$329 million, \$448 million without PRF payments, and ~\$1.3 billion without HRIP funds.
- Compared to 2020 and 2021, Kentucky hospitals received less funding from the PRF in 2022, thus resulting in negative hospital operating income for the state.
- The losses in Kentucky would have been significantly worse without HRIP funds.

Source(s): 1) Kentucky hospital operating income/(loss) was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Total Kentucky Hospital Operating Income in 2022 Was \$440 Billion Below Pre-Pandemic Levels

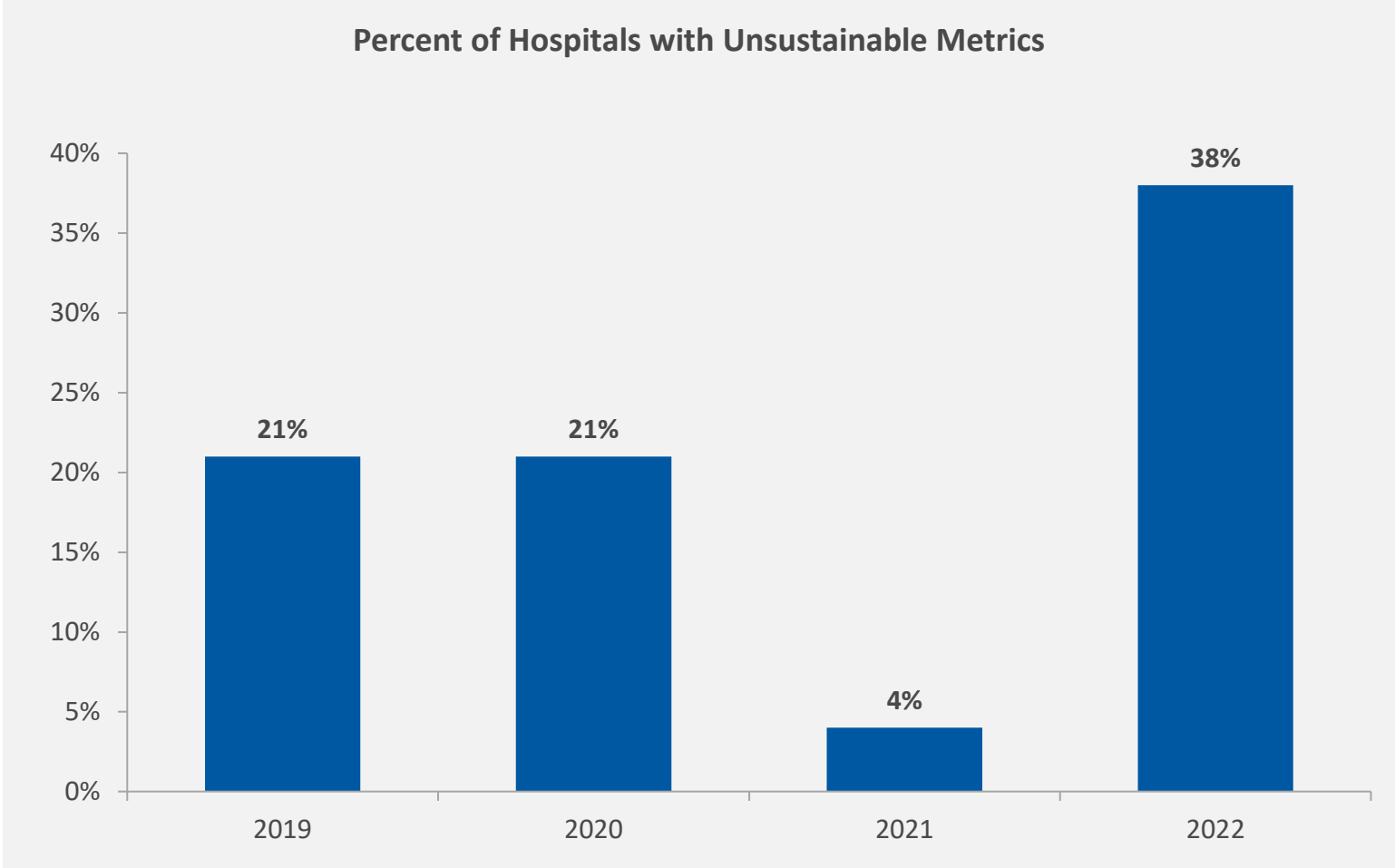


KEY TAKEAWAYS

- Kentucky hospital operating income/(loss) has still not recovered to pre-pandemic levels.
- In the three years combined following the start of the pandemic, Kentucky hospitals have lost a combined \$570 million excluding PRF payments compared to 2019 levels.

Source(s): 1) Absolute change in Kentucky hospital operating income/(loss) was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Kentucky Hospitals Are Now Facing the Highest Risk of Closure Since the Start of the Pandemic



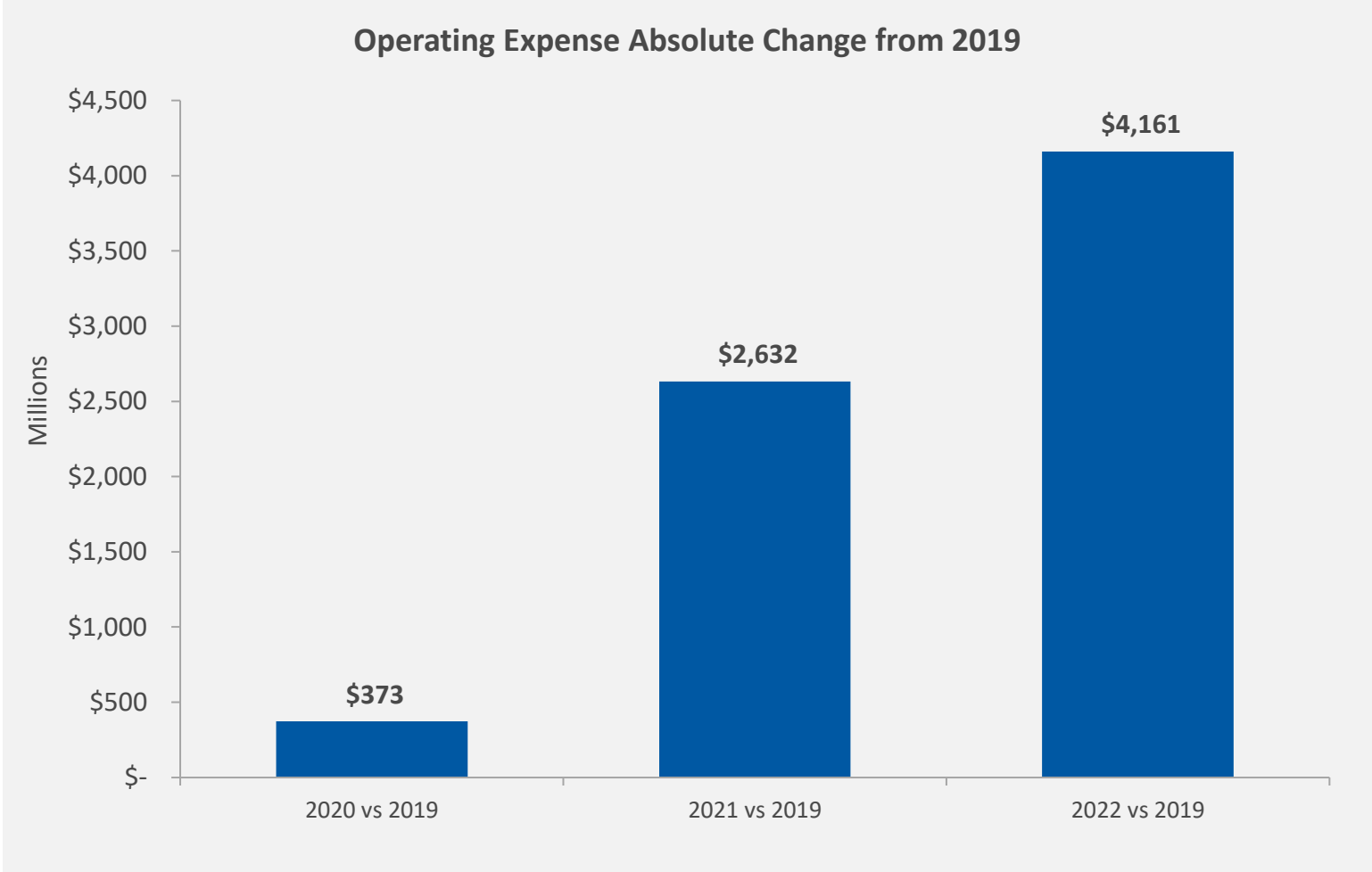
KEY TAKEAWAYS

- Kentucky Hospitals have had unfavorable trends in hospitals at risk of closure, with the exception of 2021, where slight improvement in margin and stimulus funds reduced the risk of closure.
- This risk does not reflect imminent closure, but highlights risk due to the unsustainability of operations.

Source(s): 1) Absolute change in Kentucky hospital operating expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.
Note(s): The percent of hospitals with unsustainable metrics are based on three key factors: operating margins, debt-capitalization ratio, and days cash on hand. Hospitals are deemed unsustainable if they have unfavorable trends for all three metrics.

3. Hospital Operating Expenses

Total Kentucky Hospital Operating Expenses Rose \$4.2 Billion Above Pre-Pandemic Levels in 2022

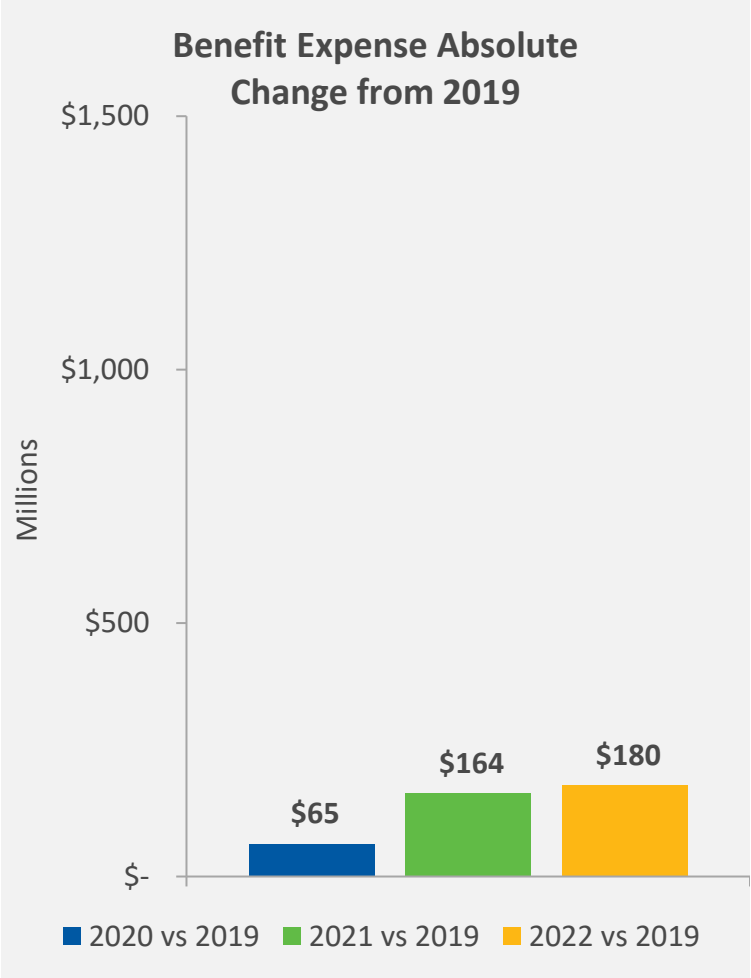
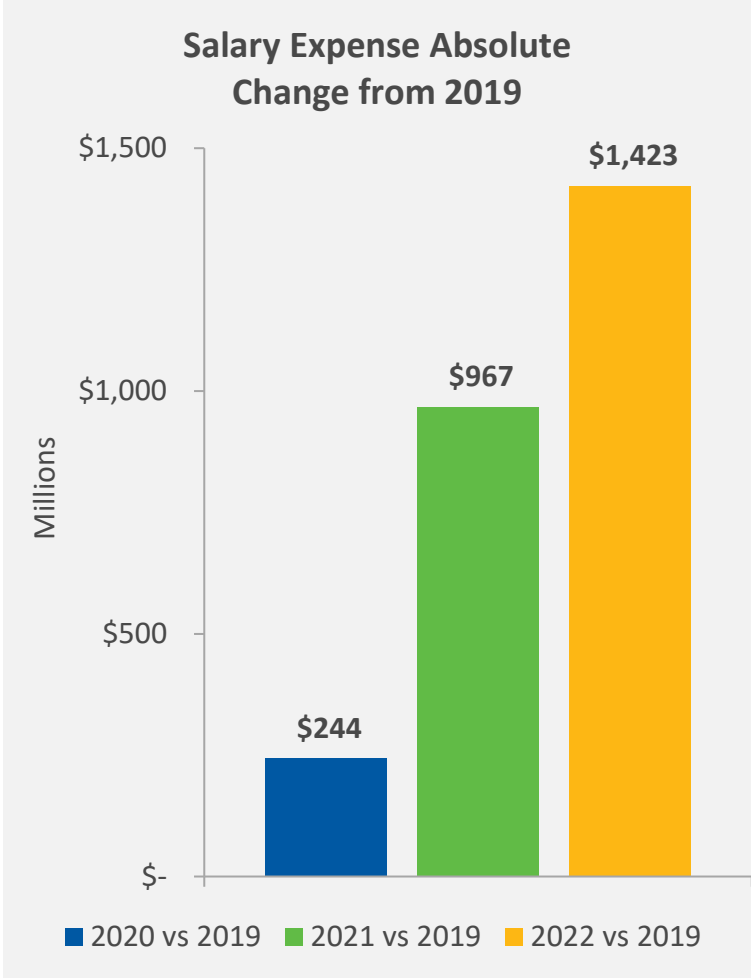


KEY TAKEAWAYS

- Total hospital operating expenses slightly increased in 2020, but then rapidly increased in 2021 and 2022.
- In the three years combined following the start of the pandemic, Kentucky hospitals saw their operating expenses increase ~\$7.2 billion.
- Rising operating expenses are generally not within a hospital’s control, and many outside factors directly impacted the increase.

Source(s): 1) Absolute change in Kentucky hospital operating expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions’ Axiom Comparative Analytics and Definitive Health.

Rising Labor Costs: \$1.4 Billion Increase in Salary Expense in 2022 Compared to 2019

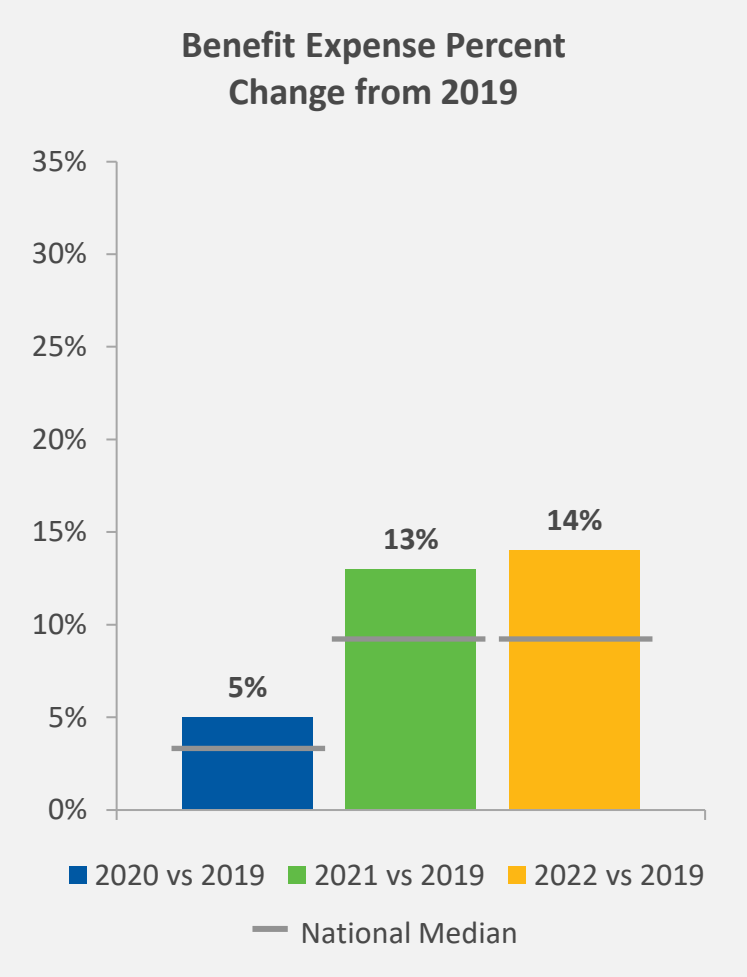
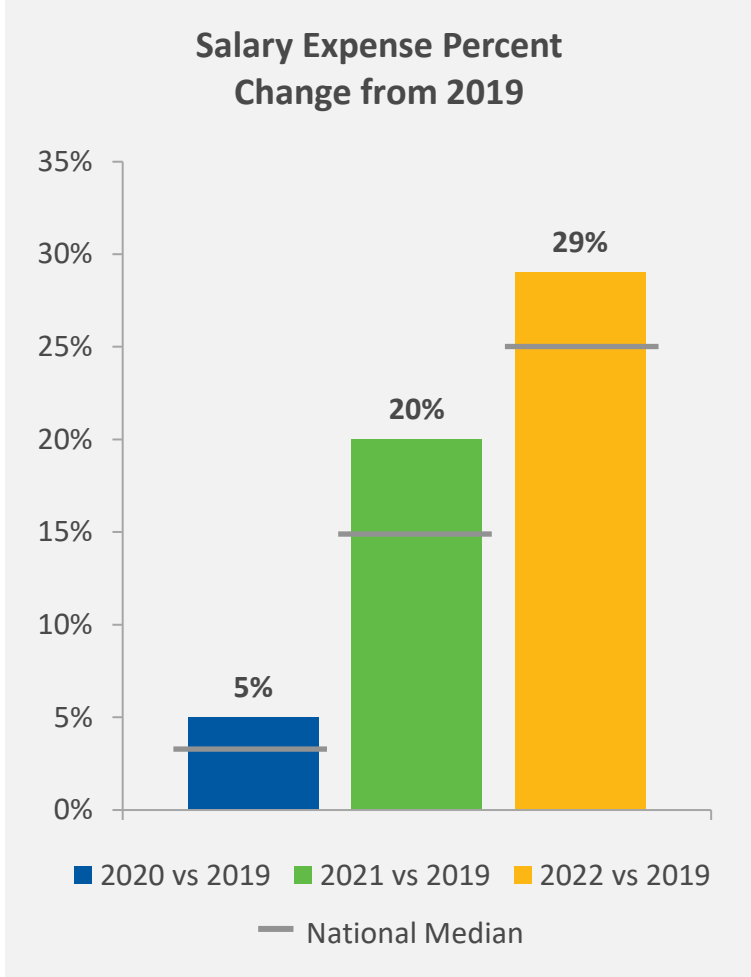


KEY TAKEAWAYS

- Salaries accounted for roughly 89% of the increase in labor expense in 2022 compared to pre-pandemic levels.
- Benefit expenses increased by only \$65 million in 2020, but then more than doubled to \$164 million in 2021 and \$180 million in 2022.
- In the three years combined following the start of the pandemic, salary expense increased ~\$2.6 billion, while benefit expense increased \$409 million.

Source(s): 1) Absolute change in Kentucky hospital salary and benefit expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Rising Labor Costs: 29% Increase in Salary Expense in 2022 Compared to 2019

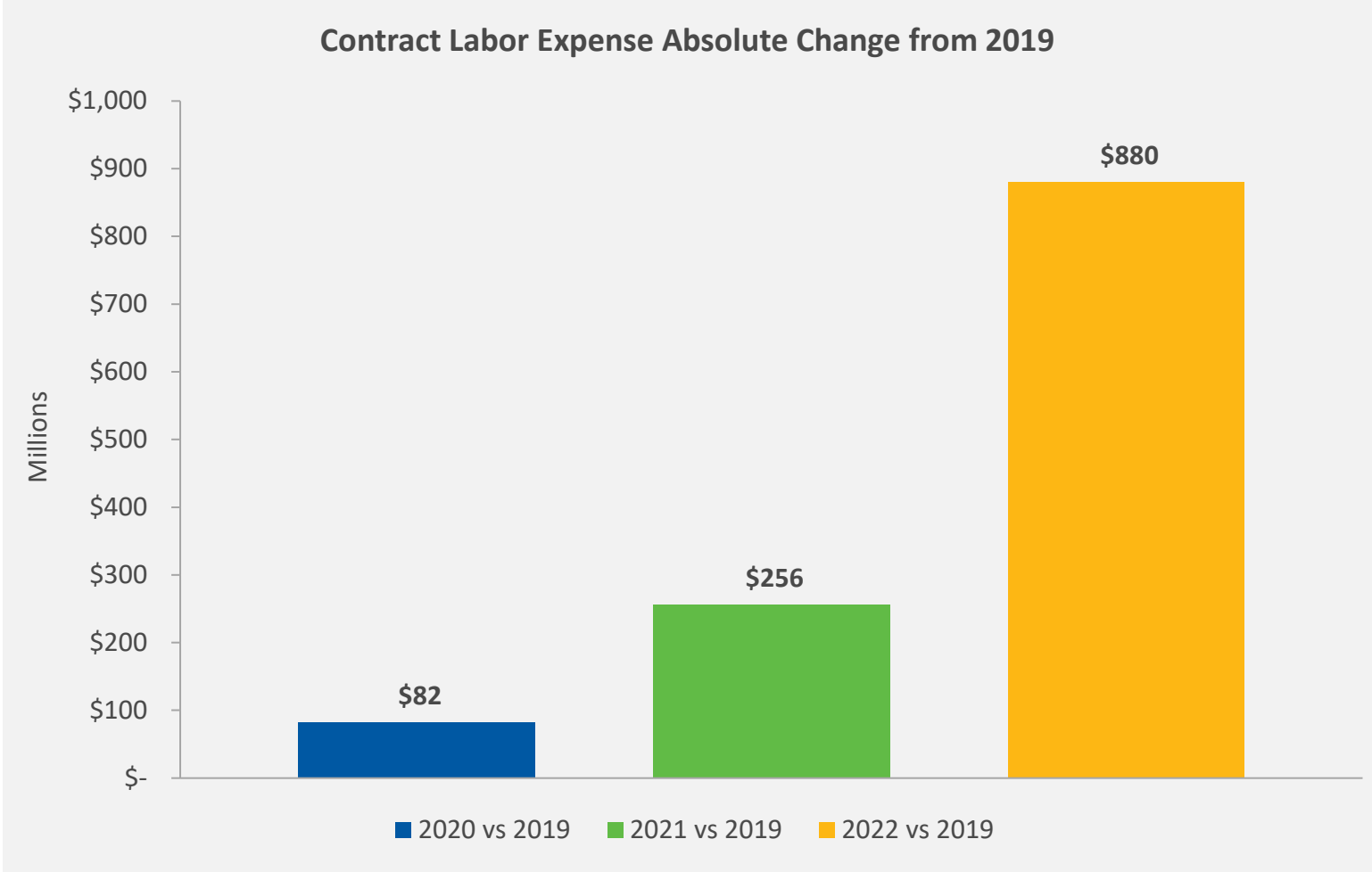


KEY TAKEAWAYS

- Growth in both salaries and benefits for Kentucky outpaced the national median for each year.

Source(s): 1) Percent change in Kentucky hospital salary and benefit expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Growing Dependence on Contract Labor: \$880 Million Increase in 2022 Compared to 2019

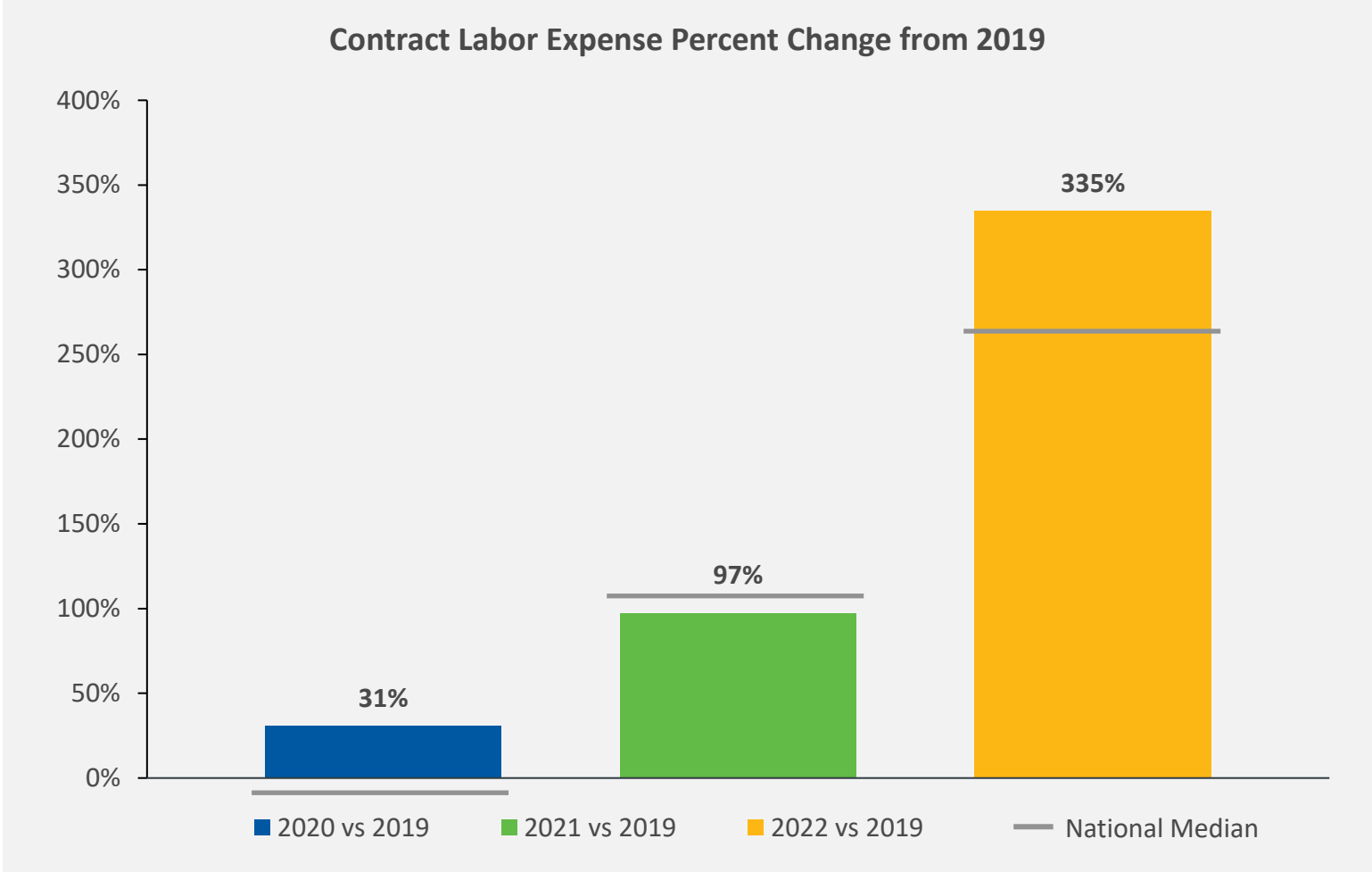


KEY TAKEAWAYS

- Compared to pre-pandemic levels, contract labor expenses for Kentucky rose dramatically due to increased reliance on more expensive contract labor.
- In the three years combined following the start of the pandemic, Kentucky hospitals have collectively spent ~\$1.2 billion more on contract labor compared to 2019 levels.

Source(s): 1) Absolute change in Kentucky hospital contract labor expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Growing Dependence on Contract Labor: 335% Increase in 2022 Compared to 2019

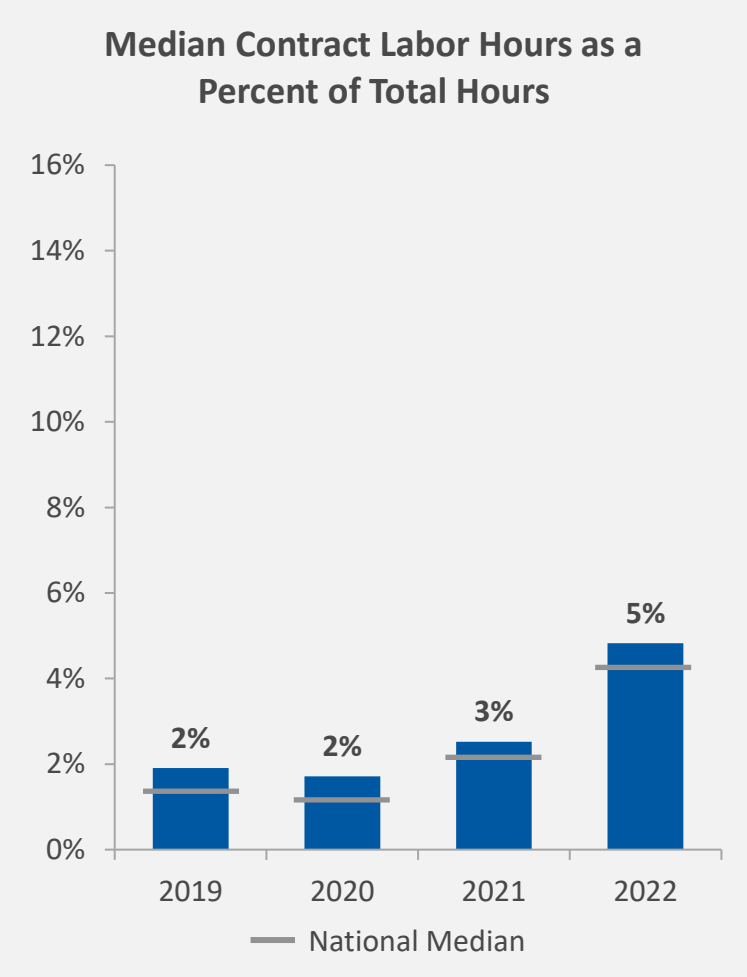
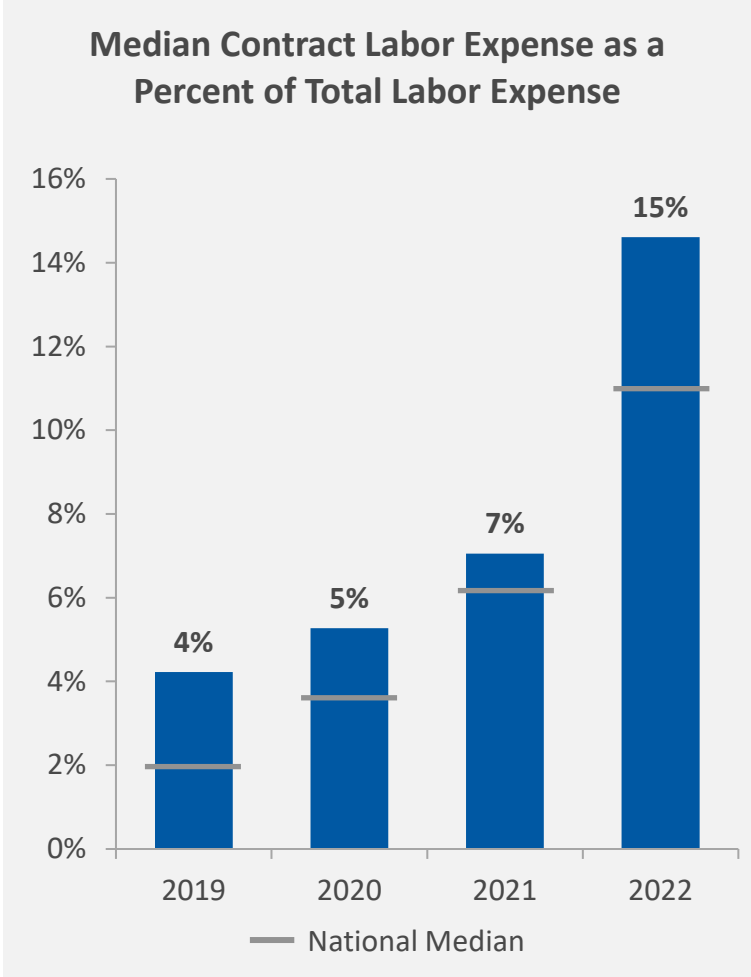


KEY TAKEAWAYS

- Contract labor expense growth in Kentucky was higher than the national median in both 2020 and 2022.

Source(s): 1) Percent change in Kentucky hospital contract labor expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Kentucky Hospital Contract Labor Expense Makes Up a Growing Percent of Total Labor Expense

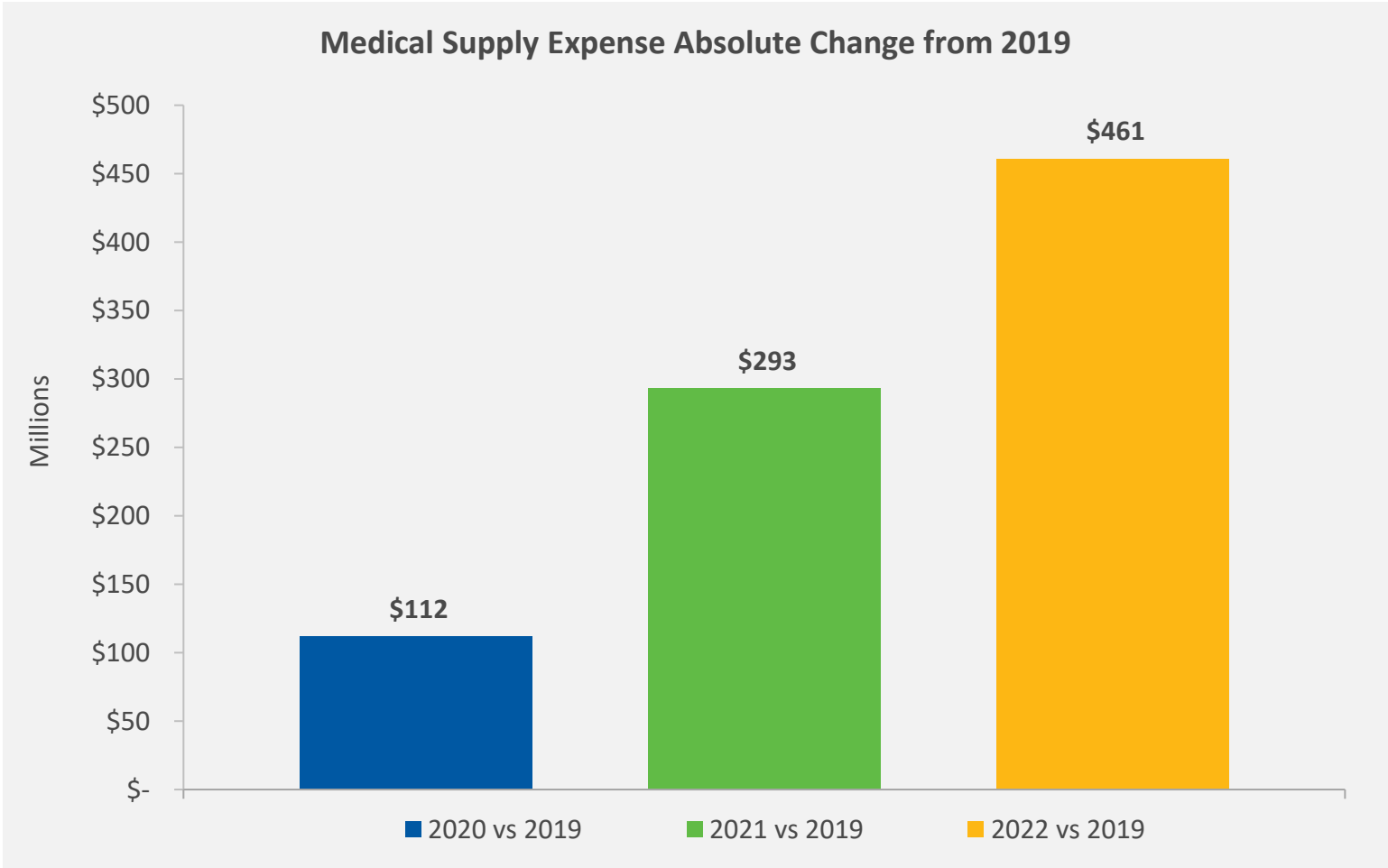


KEY TAKEAWAYS

- Median contract labor expense as a percent of total labor expense increased to 15% in 2022, while median contract labor hours as a percent of total hours only increased to 5%. Both metrics were above the national median each year.
- The larger increase in contract labor expense as a percent of total expense can be attributed to an increase in the median contract labor wage rate, which exceeded \$139 per hour in 2022.

Source(s): 1) Median percent changes were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics.

Medical Supply Expenses Were \$461 Million Higher Than Pre-Pandemic Levels in 2022

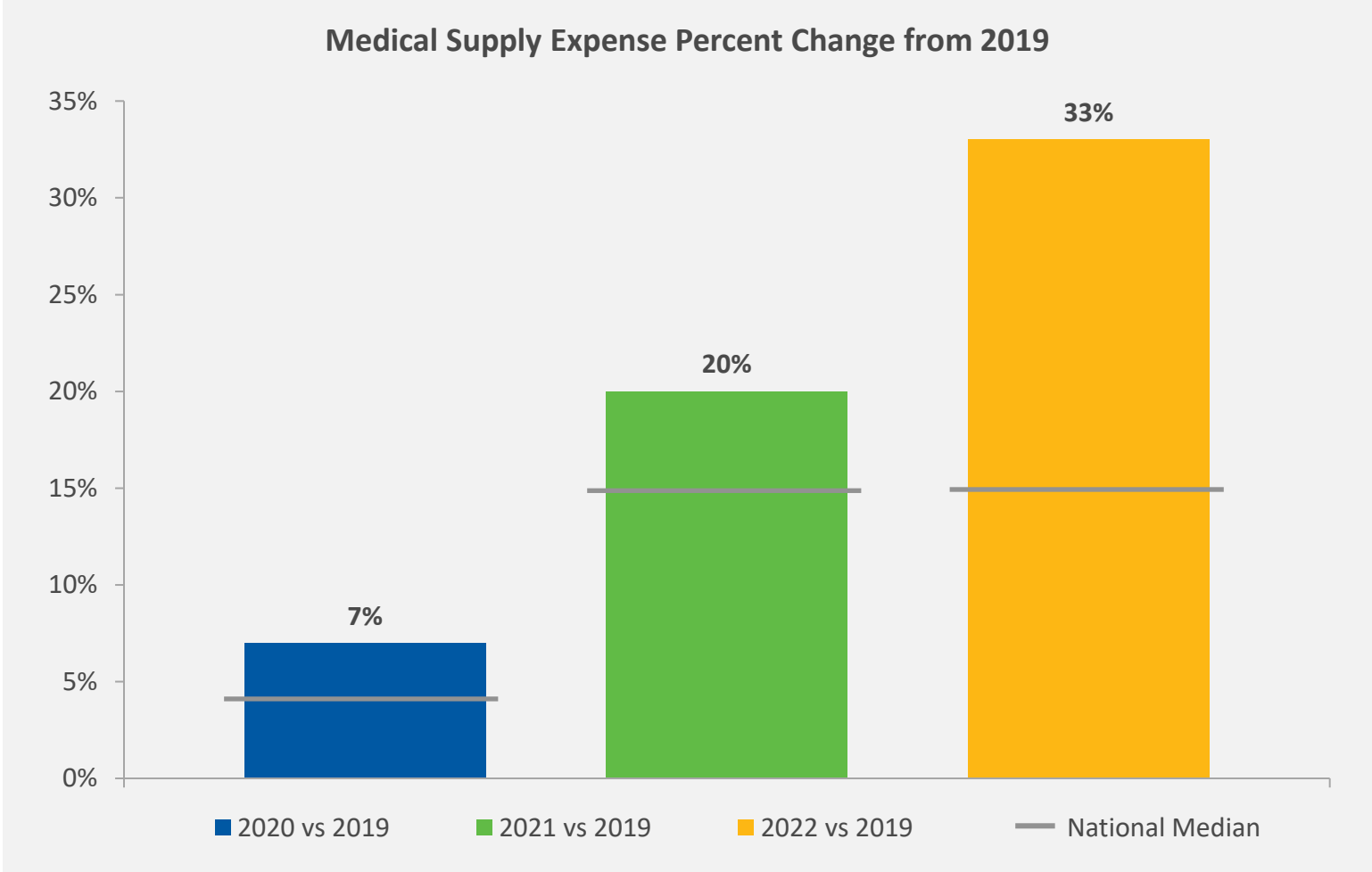


KEY TAKEAWAYS

- Kentucky hospital medical supply expenses increased by \$461 million in 2022 compared to pre-pandemic levels.
- In the three years combined following the start of the pandemic, Kentucky hospitals have collectively spent \$866 million more on medical supplies.

Source(s): 1) Absolute change in Kentucky hospital medical supply expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.
Note(s): Percentages represent the percent change compared to 2019.

Medical Supply Expenses Were 33% Higher Than Pre-Pandemic Levels in 2022

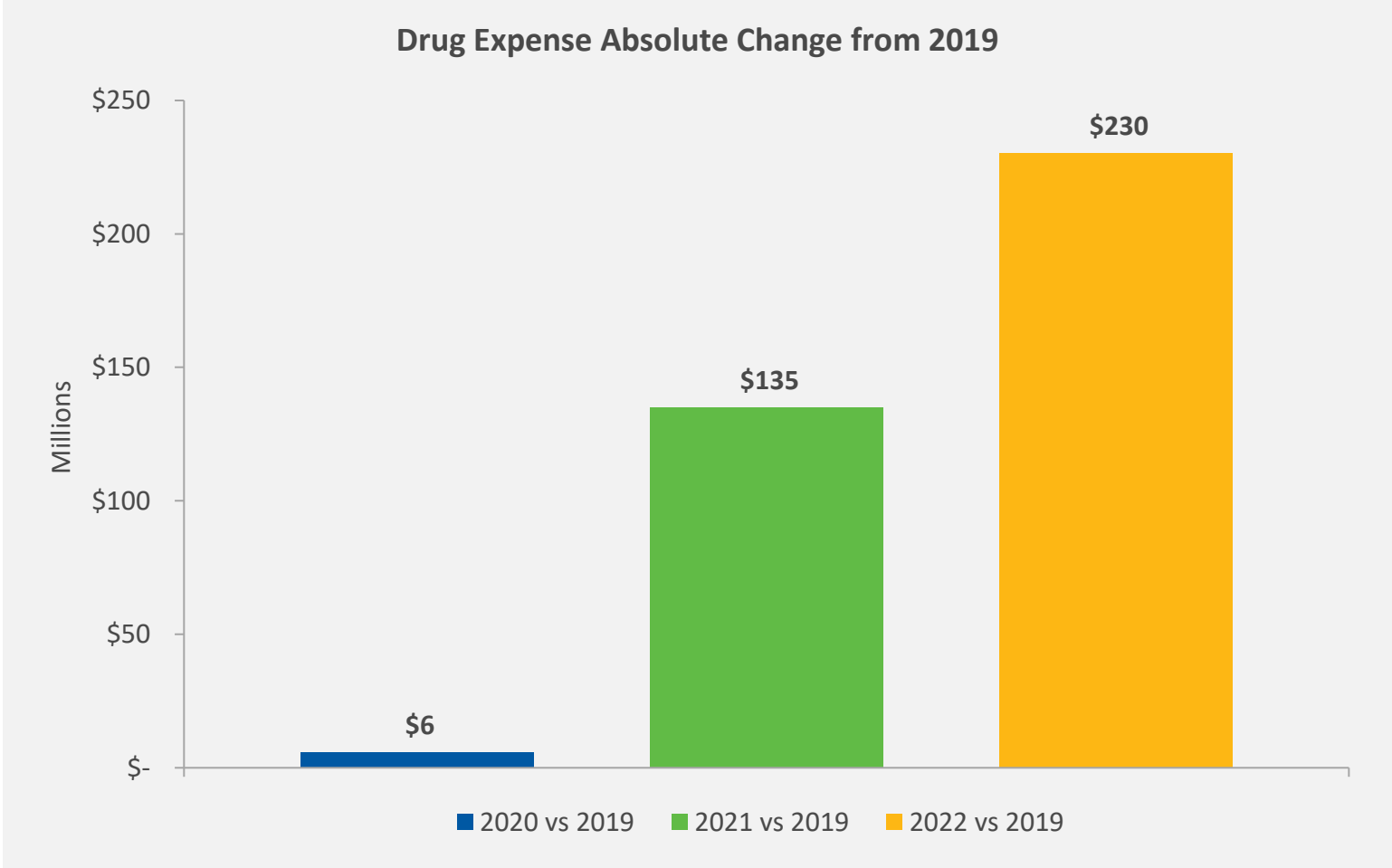


KEY TAKEAWAYS

- Kentucky hospital medical supply expenses increased by 33% in 2022 compared to pre-pandemic levels.
- Medical supply expense growth for Kentucky was above the national median each year.
- Medical expense growth for Kentucky in 2022 was more than two times the national median.

Source(s): 1) Percent change in Kentucky hospital medical supply expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

Drug Expenses Surge: \$230 Million Increase in 2022 Compared to Pre-Pandemic Levels

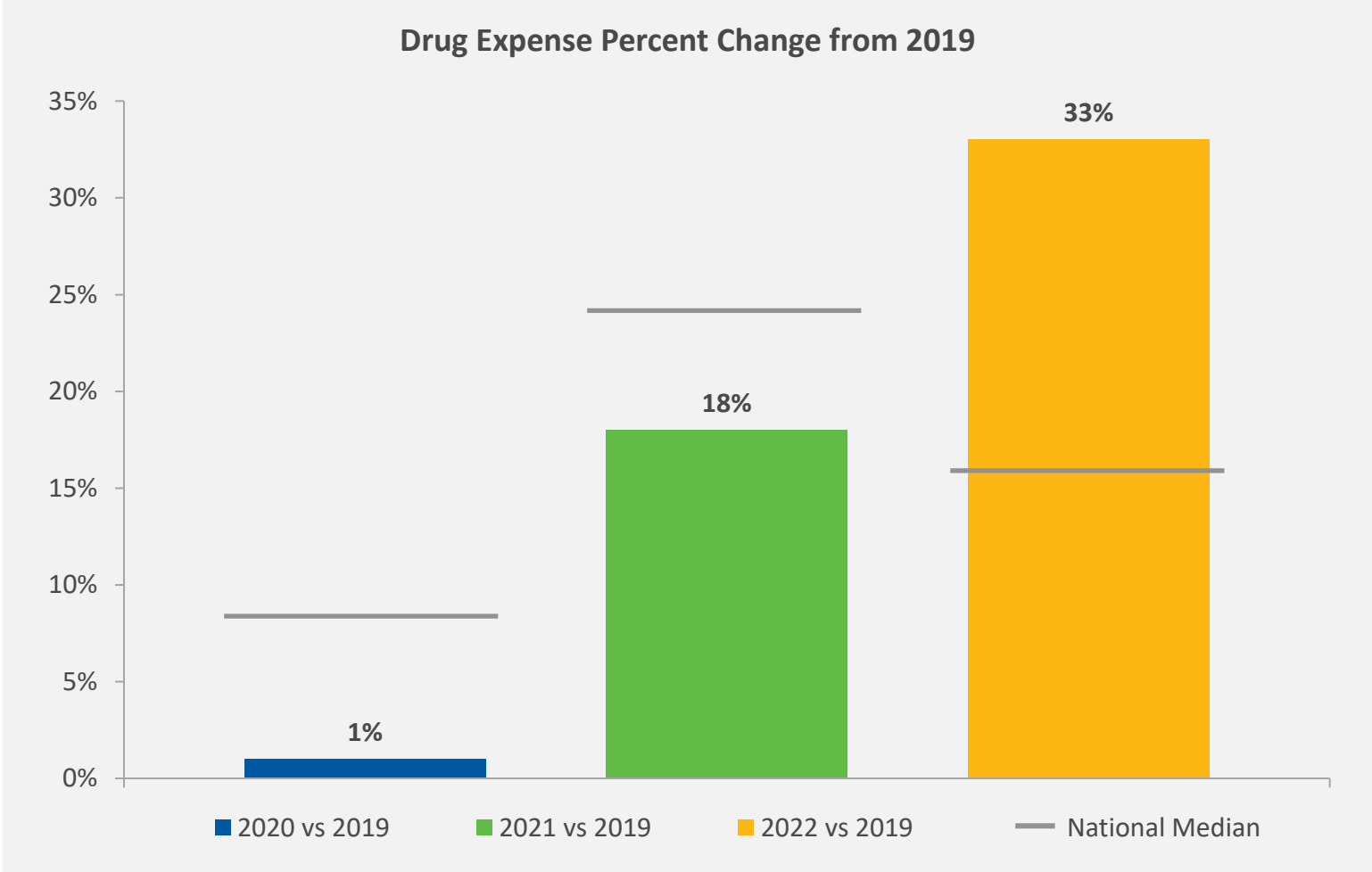


Source(s): 1) Absolute change in Kentucky hospital drug expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.
Note(s): Percentages represent the percent change compared to 2019.

KEY TAKEAWAYS

- Drug expenses have grown significantly for Kentucky hospitals since the start of the pandemic.
- In the three years combined following the start of the pandemic, Kentucky hospitals have collectively spent \$371 million more on drugs.

Drug Expenses Surge: 33% Increase in 2022 Compared to Pre-Pandemic Levels



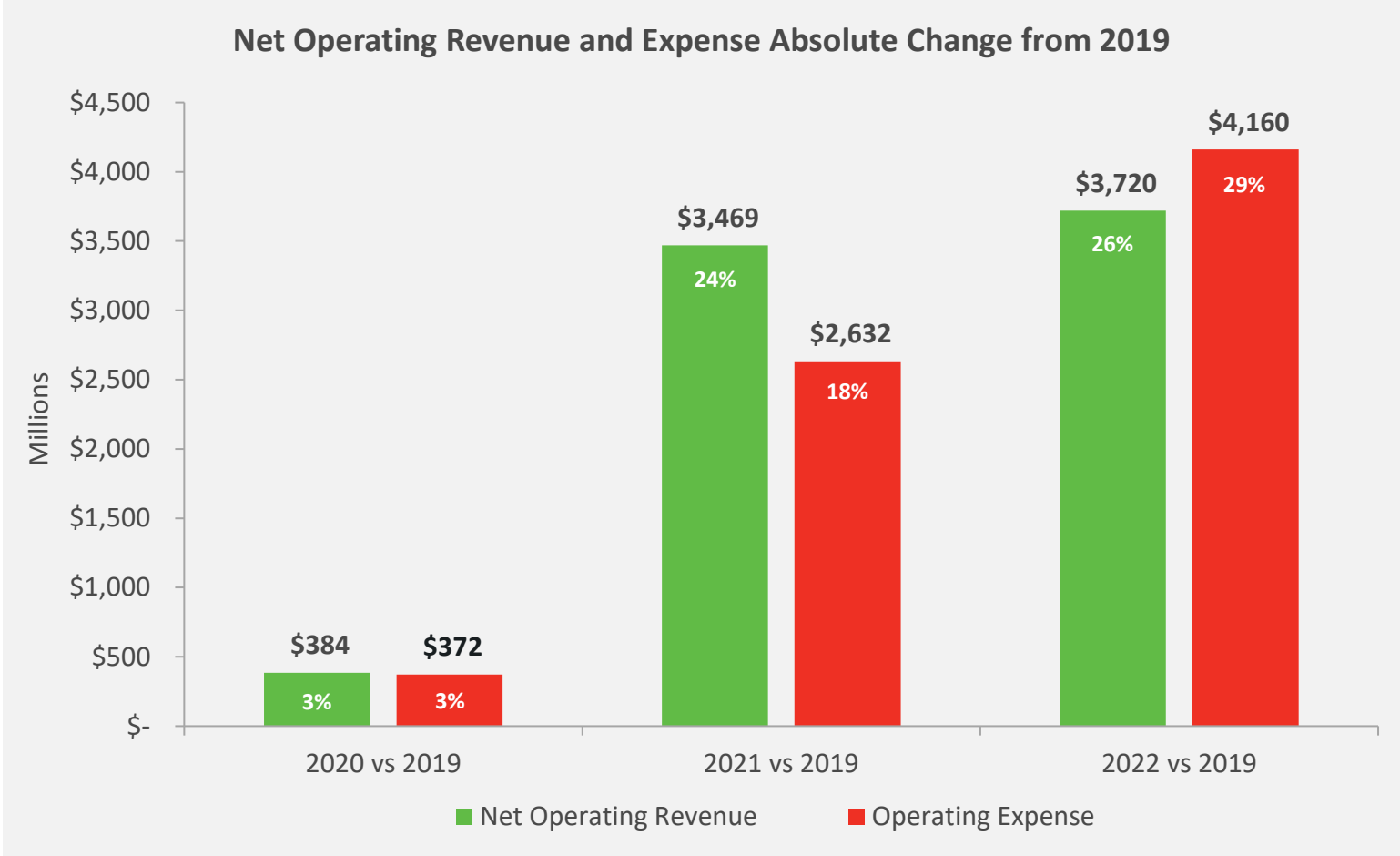
KEY TAKEAWAYS

- Drug expense growth for Kentucky was below the national median in 2020 and 2021 but was twice the national median in 2022.

Source(s): 1) Percent change in Kentucky hospital drug expense was produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

4. Hospital Operating Revenues

Total Kentucky Hospital Net Operating Revenue is Being Outpaced by Expense Growth

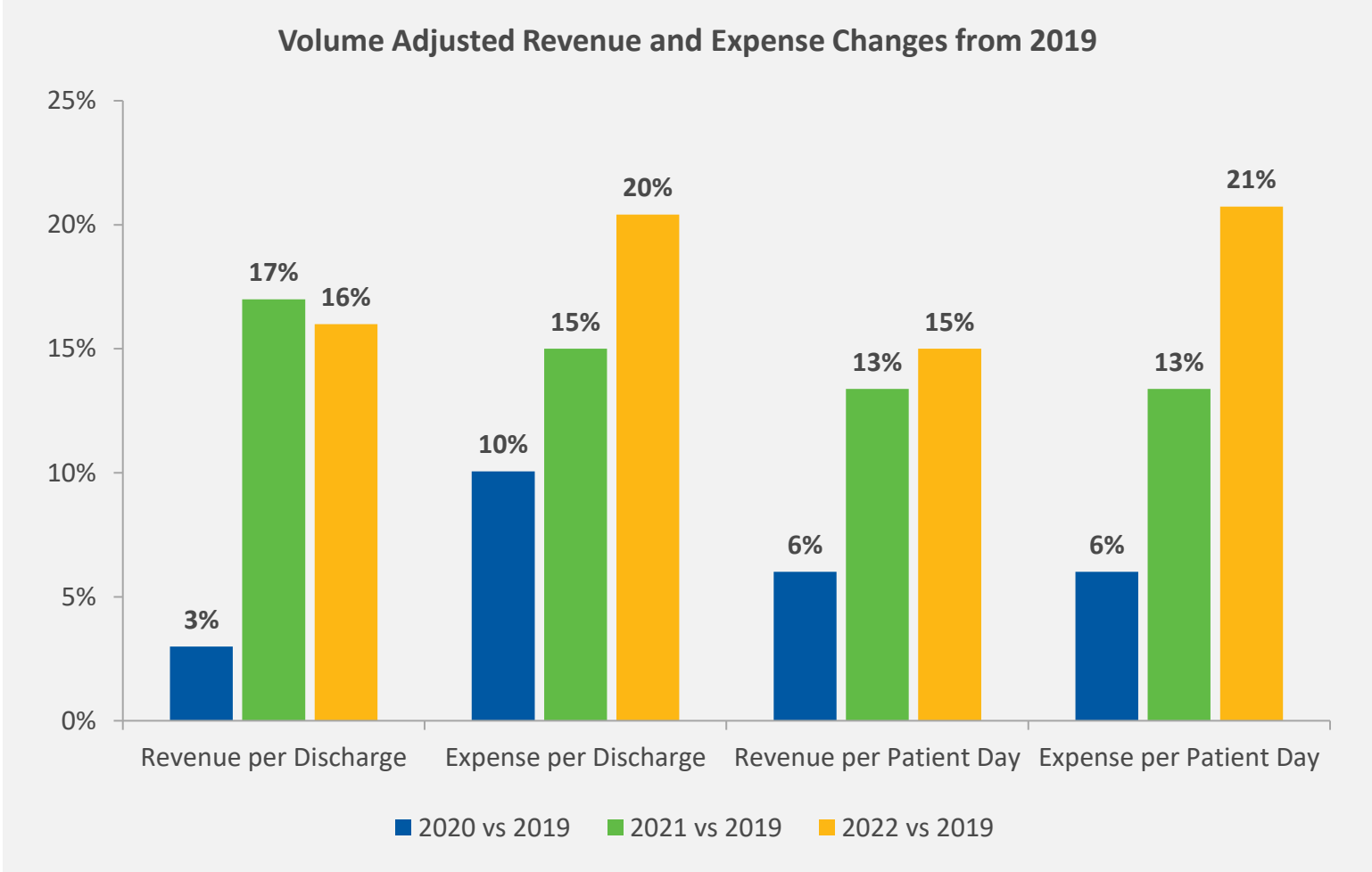


KEY TAKEAWAYS

- While Kentucky hospital net operating revenues have grown since the start of the pandemic, the rate of growth has significantly lagged the rate of growth in expenses.
- Payments made to Kentucky hospitals in 2020 and 2021 from the PRF and the Kentucky HRIP contributed to the increase in hospital net operating revenues and helped hospitals cover their increasing operating expenses.

Source(s): 1) Absolute change in Kentucky hospital net operating revenue and expense were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics 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.

Hospital Expenses Rose More Than Revenues in 2022 on a Volume Adjusted Basis



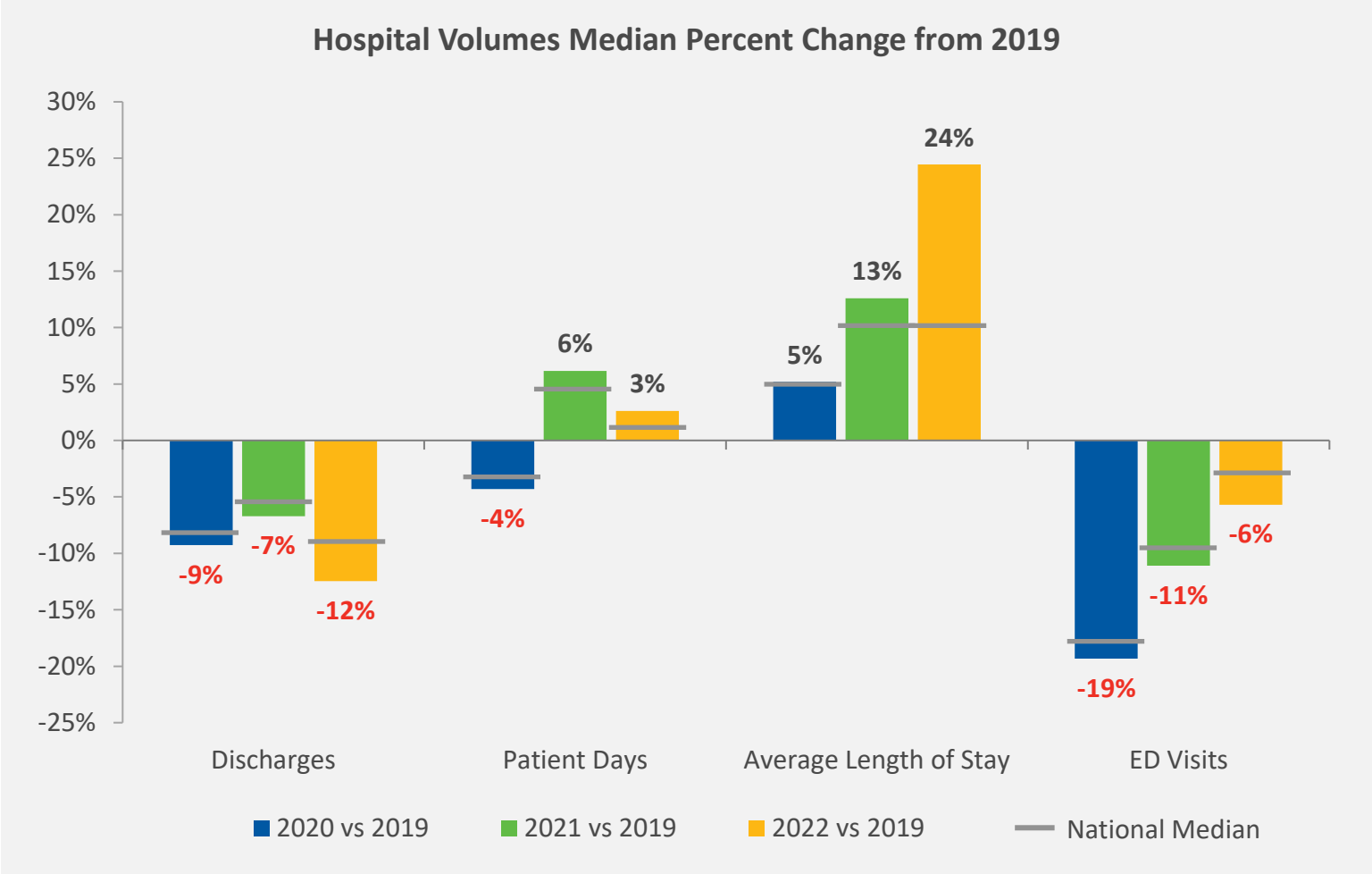
KEY TAKEAWAYS

- While revenues and expenses have increased relative to pre-pandemic levels, expenses in 2022 rose more than revenues, leading to the decline in operating performance.
- Expense per discharge and expense per patient day both outpaced revenue growth due to sicker patients and longer lengths of stay caused by post-acute care labor shortages.

Source(s): 1) Kentucky revenue/expense per discharge/patient day were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics and Definitive Health.

5. Hospital Volumes

Hospital Volumes Have Not Fully Recovered to Pre-Pandemic Levels, While Average Length of Stay Has Increased



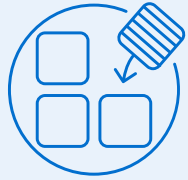
KEY TAKEAWAYS

- As care continues to shift out of the hospital, discharges and ED visits were lower than pre-pandemic levels in 2022.
- Growth in patient days continued to outpace the growth in discharges, leading in an increase in average length of stay and further stressing hospital finances. Because hospitals are paid on a per-case basis, the increase in length of stay results in higher costs per patient without realizing a comparable increase in revenue.

Source(s): 1) Median change in Kentucky hospital volumes were produced by Kaufman Hall using data sourced from Syntellis Performance Solutions' Axiom Comparative Analytics.

6. Methodology

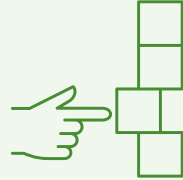
Methodology



1

Generated the Kaufman Hall Sample

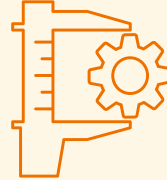
More than 31 Kentucky hospitals were sampled from data provided by Syntellis Performance Solutions.



2

Normalized the Kaufman Hall Sample

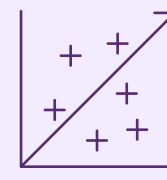
Based on hospital bed sizes, the Kaufman Hall sample was bootstrapped so that the distribution of hospitals within various bed-size bins matched that for the entire state of Kentucky.



3

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 Kentucky were calculated for 2019.



4

Calculated Median Percent Change

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

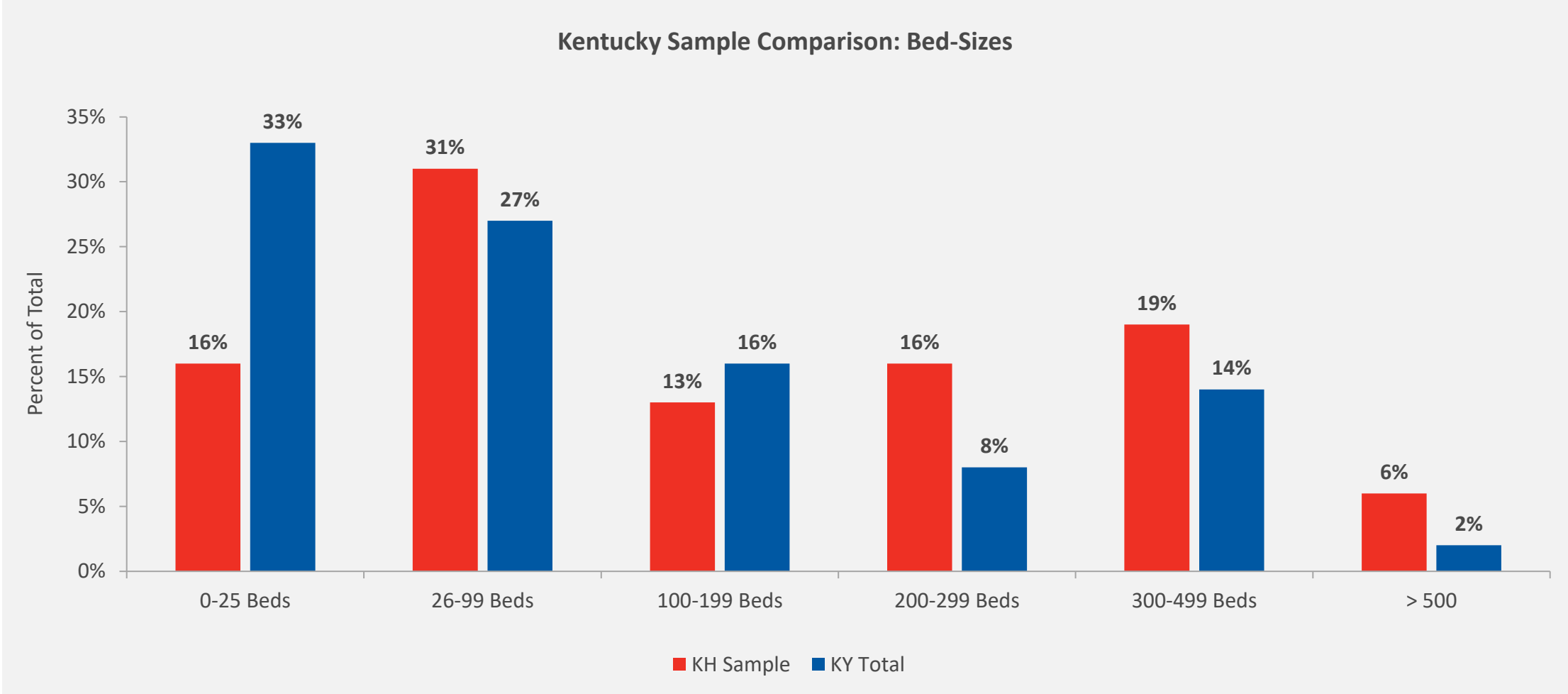


5

Extrapolated the 2020–2022 Absolute Values

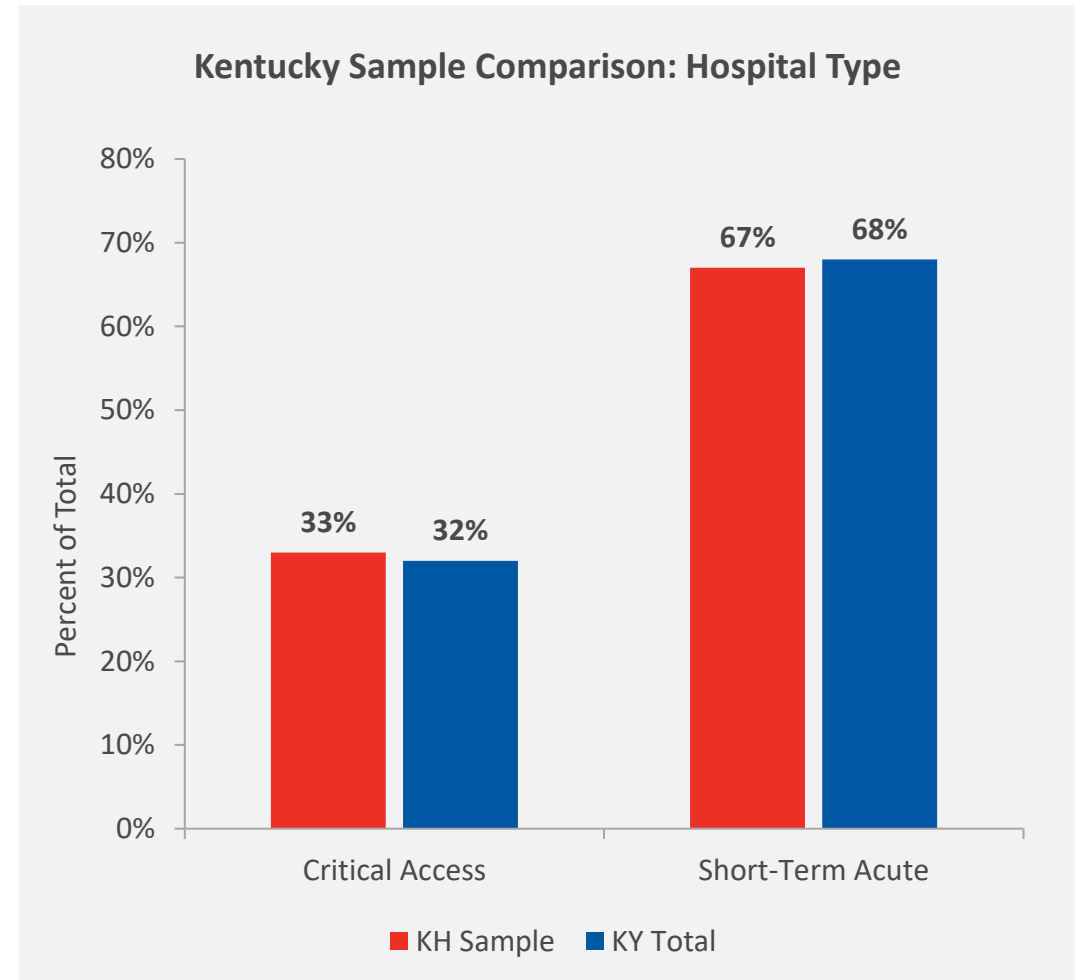
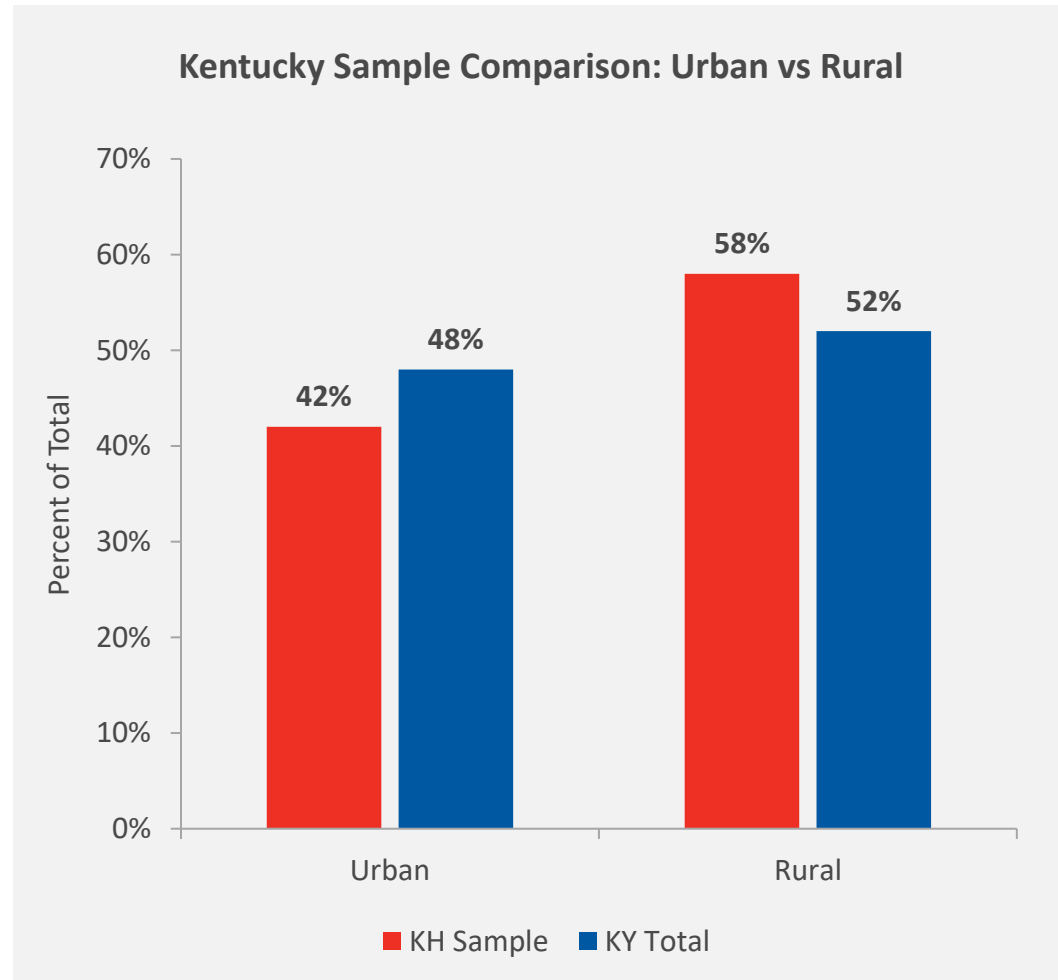
Extrapolated absolute change figures for 2020-2022 were calculated by applying the median year-over-year percent changes from the Kaufman Hall sample to the 2019 baseline metrics.

Kentucky Sample Characteristics: Bed-Size



Source(s): 1) Hospital counts for the “Kentucky Total” were pulled from Definitive Health.

Kentucky Sample Characteristics *(continued)*



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

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