8 Takeaways from Health System Q1 2024 Financials

Blake Madden <hospitalogy@workweek.com>
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To:Arvin Juan <arvin.juan@vayaworkforce.com>

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By Blake Madden, a Workweek Friend

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Happy Thursday, Hospitalogists.

Today concludes the Hospitalogy Beach Reads as I return from Florida soon. It's been a great, restful week with family and I hope you're enjoying some time off this summer as well.

Onto today's post, which is everything health systems and financial performance in Q1, including some pretty interesting graphs - a few of which you may have seen before. As mentioned, this was a **community-exclusive** post sent to my community in the past weeks, so you guys are getting a sneak peek at the type of content they usually get.

Onward!

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Well, the results are in—I partnered with some smart folks at Adonis to put together a new report that addresses all of these things at scale.

We've gathered insights from over 100 top healthcare leaders to pinpoint the pivotal trends and hurdles that will shape the industry's financial landscape for 2024 and beyond.

This comprehensive analysis doesn't just spotlight problems—it offers a roadmap for enhancing financial outcomes, boosting efficiency, and elevating patient care.

It's high time to turn challenges into opportunities with strategies that matter.

Get your copy for free and start preparing today for a more robust tomorrow in healthcare.

Access the report

Health System Q1 Analysis

Overview of Analysis

1. My takeaways and key quotes from HCA, Tenet;
2. Broad hospital performance from Kaufman Hall's Flash Report with data thru April;
3. Change in health system operating margins from Q1 2023 to Q1 2024;
4. Comparative scatterplot of the top ~20 largest health systems classified by both total revenue growth and operating margin;
5. Some graphics on total net revenues, revenue growth, operating margins, and operating margin growth including some takeaways;
6. Increased divide between higher-performing hospitals and lower-performing hospitals; and finally,
7. Health system investment priorities from McKinsey
8. Let's dive in!

NOTE: this essay was shared with Hospitalogy Board Room community members. Certain references were made to my community throughout this piece!

Blake's Q1 Takeaways and 2024 Outlook for Health

Systems

I’m characterizing 2024 as the Year of Stabilization and Reset – in demand, in labor, and in hospital operations.

Most large health systems have moved on from labor and utilization woes and are looking for incremental improvement in those areas in the back half of 2024. While patient volume trends have been abnormally good to start 2024, the percentage growth in total volumes will level off (if they haven’t already), and therefore we should see a return to normal 2-3% Inpatient / Outpatient growth moving forward into 2025.

From a price perspective, HCA and other dense networks have found success in negotiating favorable reimbursement terms with payors amid an inflationary backdrop. General acuity for most hospitals is rising. Finally, stemming from an alleviating labor market, general trends in length of stay are positive as the post-acute labor market normalizes and discharge locations free up. But expect to see struggling names like CommonSpirit, Ascension, and other ‘bloated’ nonprofits sell off certain noncore assets in an attempt to refocus on core market density and deleverage the enterprise a bit.

What else is top of mind? Lots of buzz around the Two-Midnight rule leading to inflated admissions at hospitals. Medicaid supplemental dollars (state directed payment programs) are in limbo and hard to predict. Orthopedics and Cardiology remain the top specialties of focus. Subsidies for physicians, while elevated, are stabilizing. Health system transformation is top of mind, as is investment into both capital projects and areas including AI, RCM, and patient acquisition (digital front door, urgent care, ER). ACA exchange and Medicaid disenrollments are affecting volumes. Finally, many operators are sitting on the sidelines in ‘wait and see’ mode during an election year and market turmoil in Medicare Advantage.

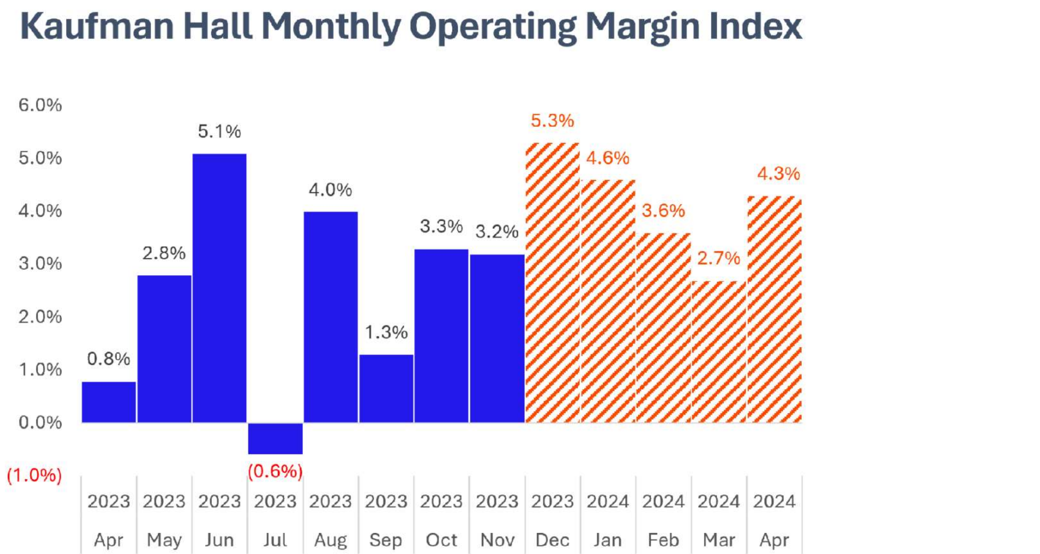
“…after a year where we grew more than twice what our typical growth rate would be, remain flat and have an opportunity to build off that floor suggests significant fundamental strength and tailwind in the demand for USPI type of services as opposed to 2023 having just been a catch-up year that was going to go away…So I think the fundamentals look good. The comps are hard through the year. We think they get a little bit better as the year goes on. But our fundamental belief is that the ability to grow off of last year is really what the first quarter affirmed as opposed to that have been just purely onetime deferred activity in '23. We view it as a good news story.”
Tenet Healthcare Q1 2024 earnings call

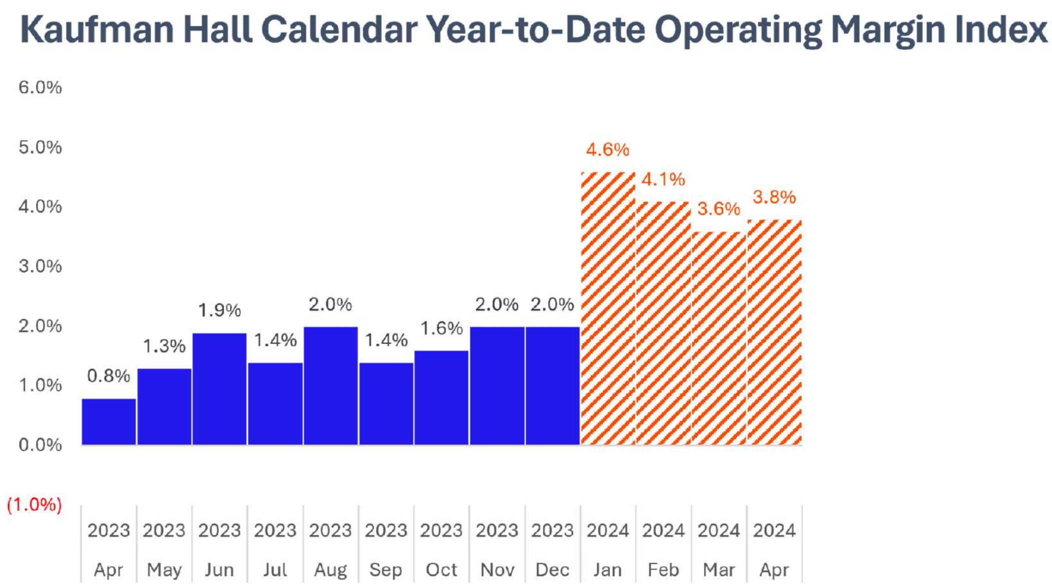
“we have made really good progress broadly across our people agenda. We still see some opportunities. It's not going to be as easy to get, if you will, as what we've achieved so far, but our belief is that a number of our initiatives should yield incremental improvements over the rest of this year. Longer term, Brian, what I'm really excited about is our workforce development initiatives, generally speaking, and we have a very robust workforce development effort in our company, investing heavily in nurse education with our Galen College of Nursing, where we will get to the point where we have 30 colleges. Each of those colleges will be connected as a front-end component of our provider systems…

“We think health care demand in the long run is going to be 1.5% to 2% on the inpatient side, at least in the markets that we serve. We also think on the outpatient side, demand is going to grow anywhere between 2% and 3%. In 2024, Brian, we guided a little bit higher because we sense that the market demand, at least in the short run, was stronger than our long-run horizon with respect to demand. And sure enough, that's played out in the latter part of 2023 and then in the first quarter of 2024. We have a 3% to 4% guide on our volume growth in 2024.”

HCA Healthcare, Jefferies Global Healthcare Conference

1. Broader Hospital Financial Performance indicates continued recovery in Q1 and start of Q2:





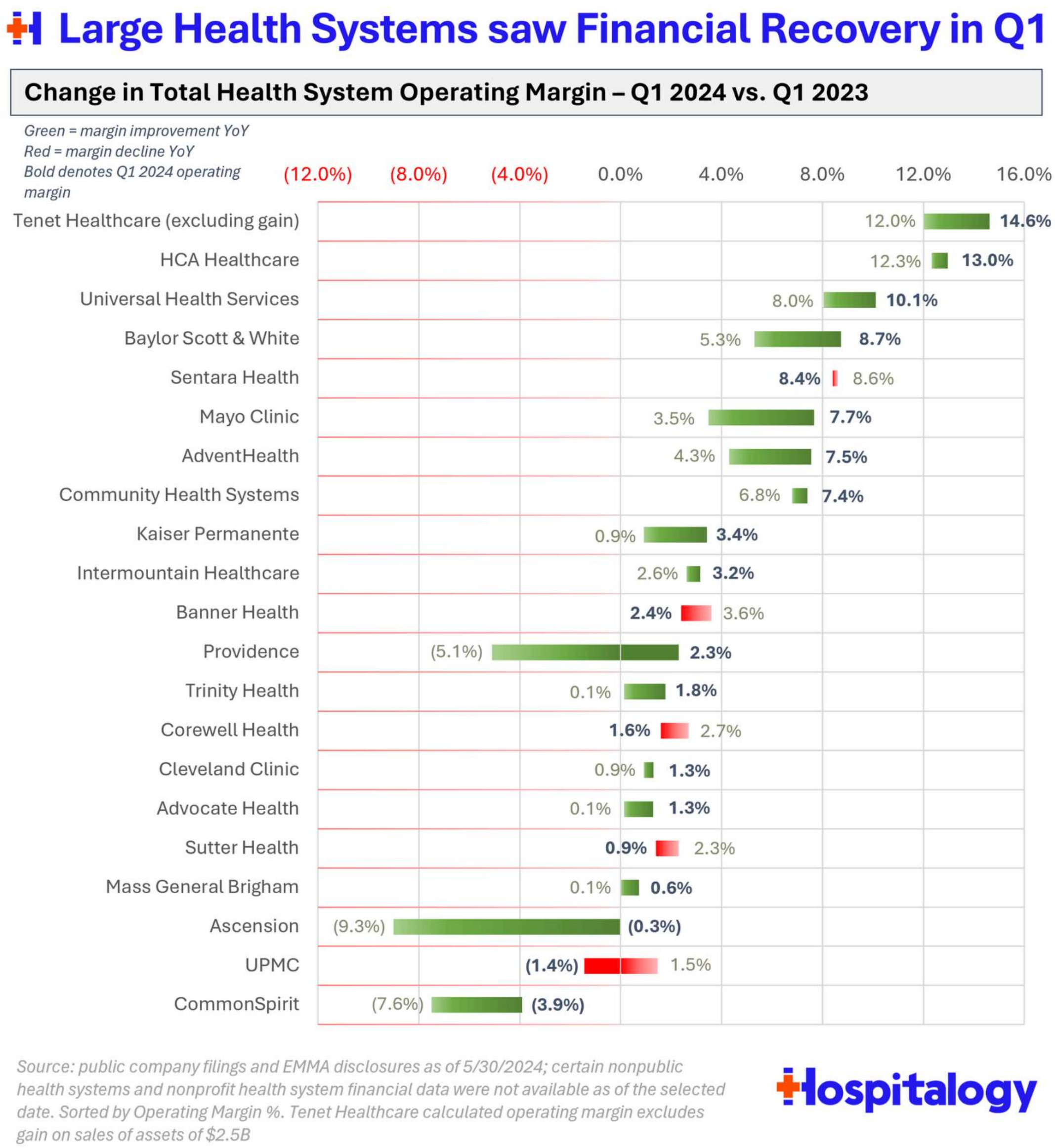
Driven by increased volumes and decreased length of stay, hospitals are well in the black based on Kaufman Hall's Hospital Flash Report through April. You should expect to see margins hover around this level as utilization isn't expected to elevate further based on payor commentary I've seen.

2. Large Health Systems Saw Financial Recovery in Q1 2024:

The below graphic is Hospitalogy original analysis and it’s sorted by operating margin % profitability. I've posted it around a few times already, but it's relevant for this analysis. Any green bar means the system performed better in 2024. Any red bar signifies worse performance than a year ago.

Several players – including Tenet, Baylor, Mayo, AdventHealth, Providence, and Ascension – saw significant improvement in operating margins between the two periods. Baylor sitting at 8.7% in Q1 is incredible. The Dallas-based nonprofit is benefiting from strong Texas markets and strong strategic decision-making within.

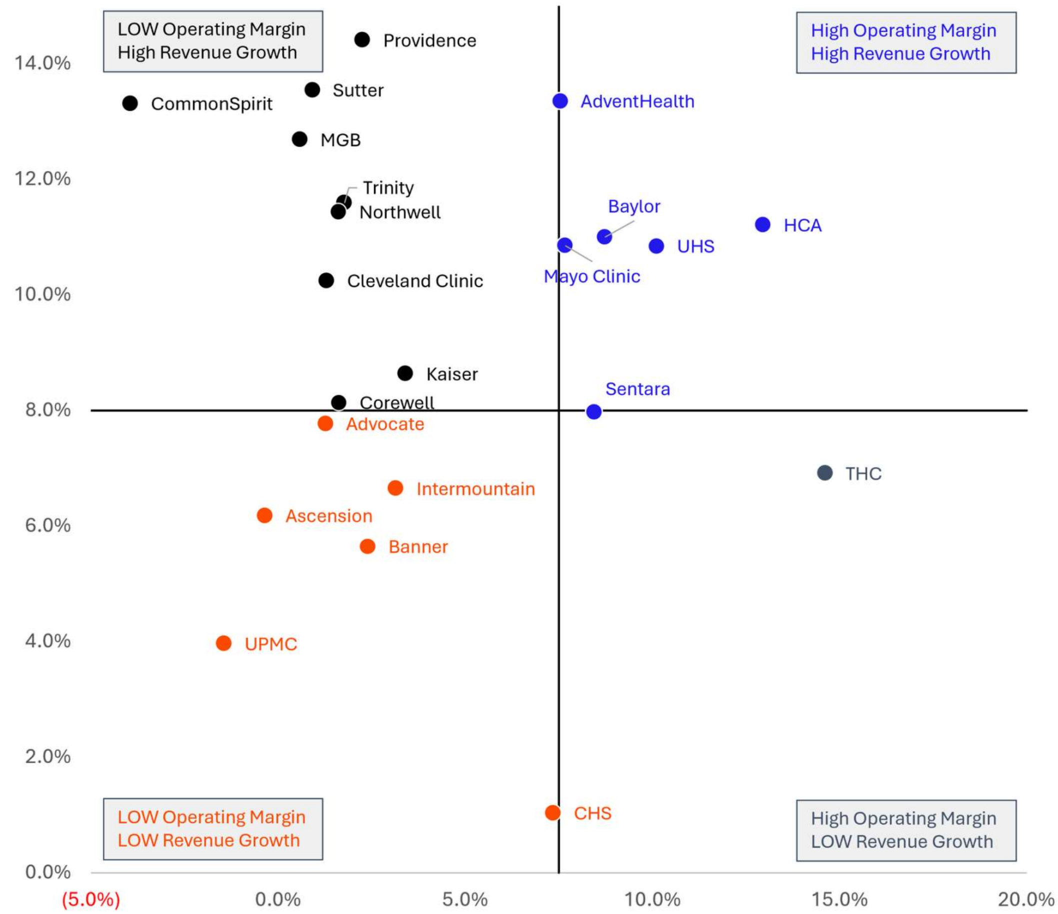
75% of health systems analyzed saw operating margin improvement from a year ago, signaling a strong market for healthcare services.



3. HCA, UHS, Tenet, Baylor Shine among 'Peer' Group

HCA, UHS, Tenet, Baylor Lead the Way

Health System Classifications and Comparative Analysis based on Q1 2024 Revenue Growth and Operating Margin: Q1 2024



Source: public company filings and EMMA disclosures as of 5/30/2024; certain nonpublic health systems and nonprofit health system financial data were not available as of the selected date. Sorted by Operating Margin %. Tenet Healthcare calculated operating margin excludes gain on sales of assets of $2.5B

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Turning next to this scatterplot of health system performance, revenue growth is plotted on the Y axis while operating margin performance is on the X axis. I've arbitrarily classified the studied health systems based on comparative performance. The main thing you need to know is that health systems WANT to be in the top right quadrant, and the bottom left quadrant (low operating margin combined with low revenue growth) is less than desirable.

A Board Room member pointed out to me while I was putting this analysis together that revenue growth might not be the best metric to study here given there's some noise in total revenue numbers. For that reason I'll probably shift to doing operating cash flow generation analyzed against net margin (potentially backing out investment income) or operating margins, or look at pure patient revenues instead!

Back to the analysis - you can see top performers here pretty clearly from Q1 (and most quarters).

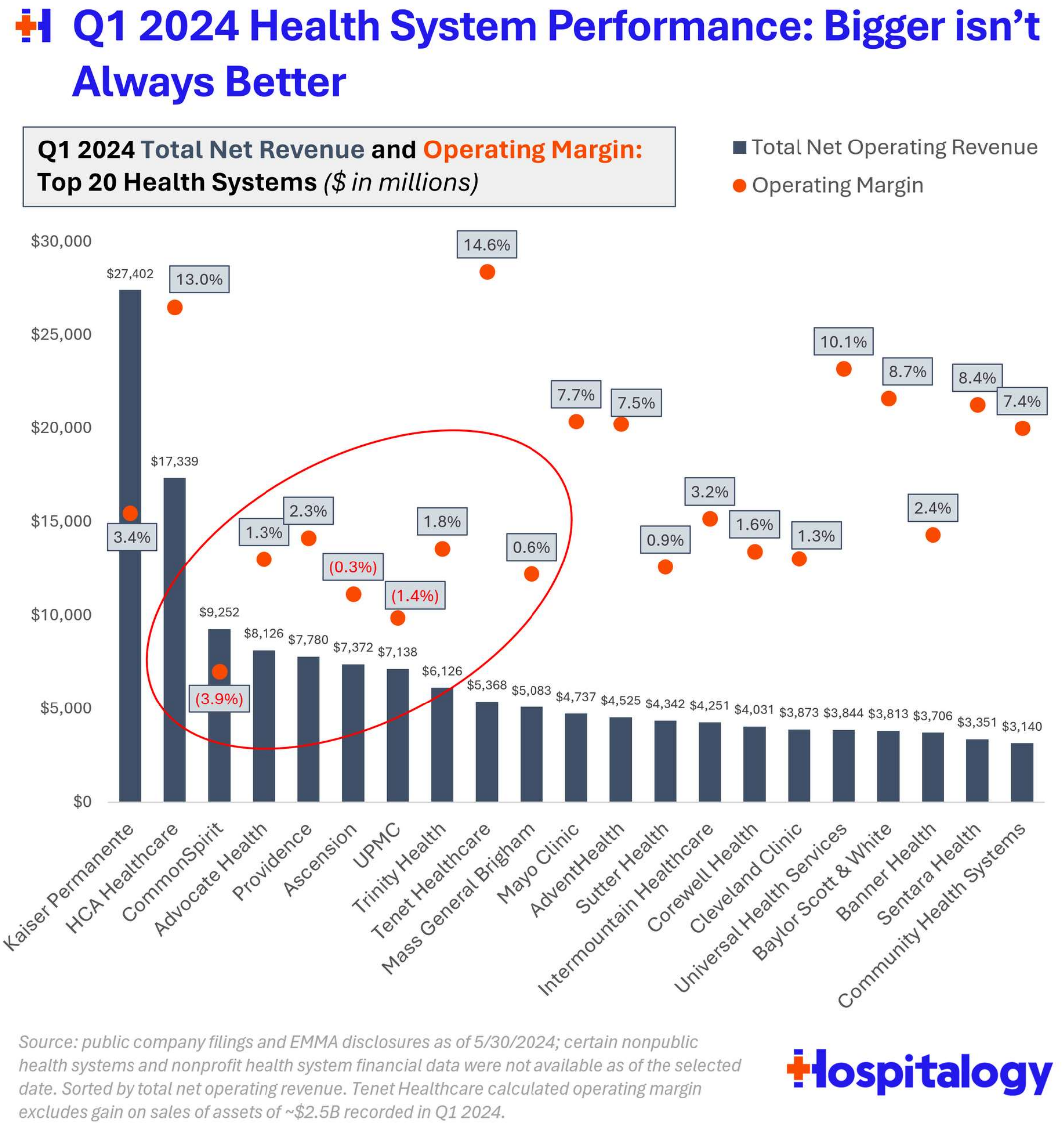
HCA, UHS, Baylor, AdventHealth, Sentara, Mayo all make the cut, and Tenet really should've made the cut too (revenue didn't grow as quickly due to hospital divestitures) so you can throw them up there too.

A majority of the nonprofits sit in the top left quadrant, meaning these players saw a decent level of revenue growth but still operate near breakeven. This dynamic seems pretty typical for most nonprofits.

A notable outlier in the worst quadrant is UPMC, with poor revenue growth (4.0%) and negative operating margins (1.4%). While outwardly UPMC is perceived and hailed as a well-run system, lately UPMC seems to be struggling as the entire state of Pennsylvania seems to want to consolidate further (see my most recent post here about Pennsylvania health system mergers.

As of this writing, UPMC just announced plans to acquire Washington Health System.

4. Q1 2024 Performance: Bigger isn't Always Better

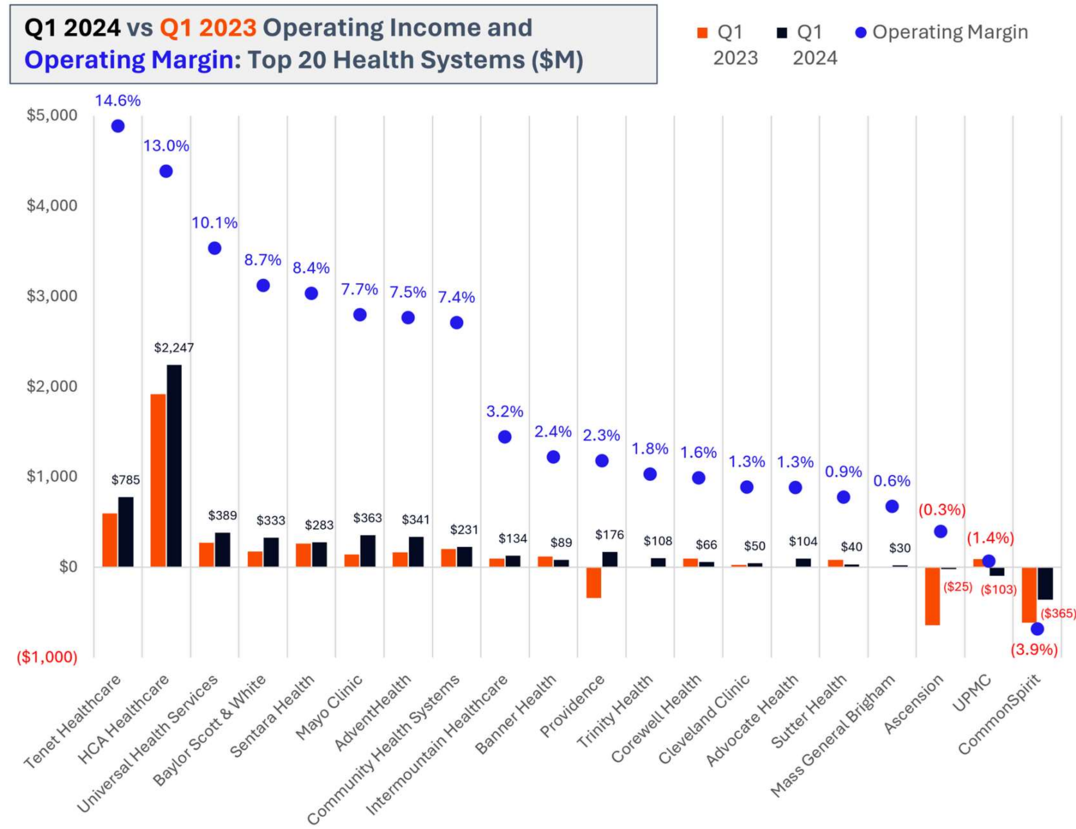


Turning to total revenue and operating margin performance - some of the largest health systems in the game are struggling on a margin basis. What gives?
As it turns out, and as I'm often reminded, market performance matters.

It doesn't matter that you're just big and can absorb a vast swath of overhead. As a health system, the way you throw your weight around in markets is more important than ever. It's the concept of density I brought up in the recent Board Room healthcare industry update, and HCA details the strategy at length in its investor day.

5. More charts and visuals around health system revenue and profitability:

Baylor, Sentara lead the way in Operating Margin among nonprofits



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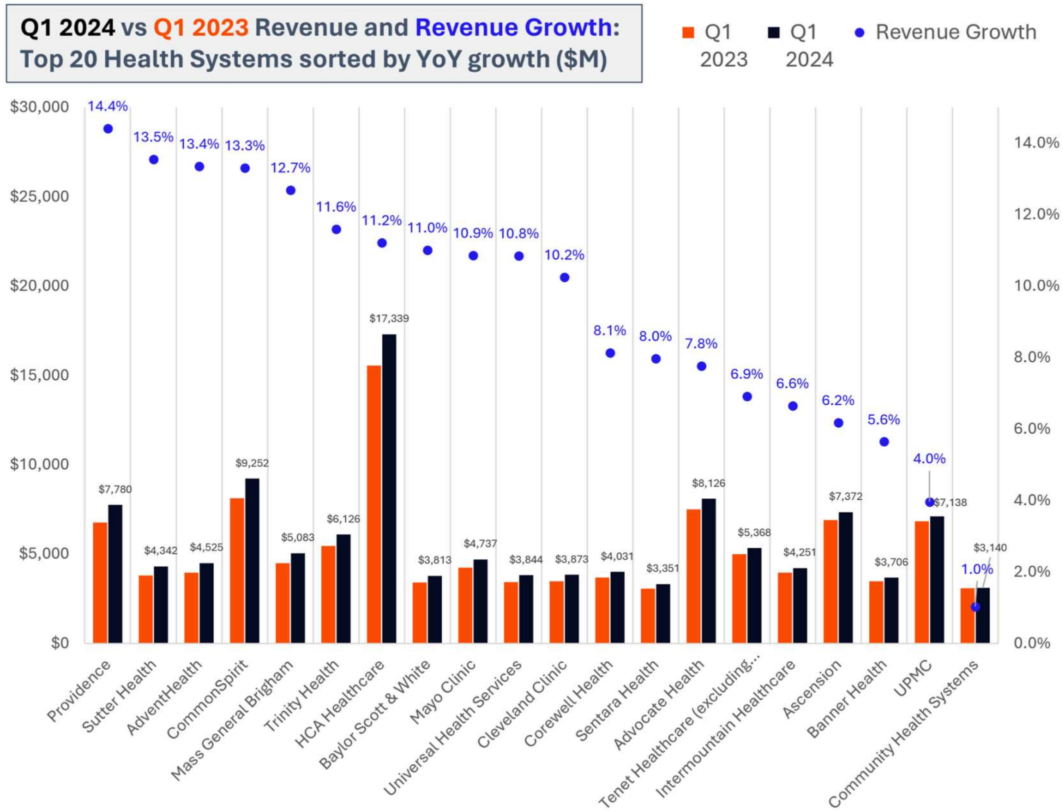
Providence, Sutter, AdventHealth, CommonSpirit see Significant Revenue Bumps Year-over-Year



Source: public company filings and EMMA disclosures as of 5/30/2024; certain nonpublic health systems and nonprofit health system financial data were not available as of the selected date. Sorted by year-over-year Revenue Growth. Tenet Healthcare calculated operating margin excludes gain on sales of assets of $2.5B; Kaiser Permanente excluded for comparability purposes

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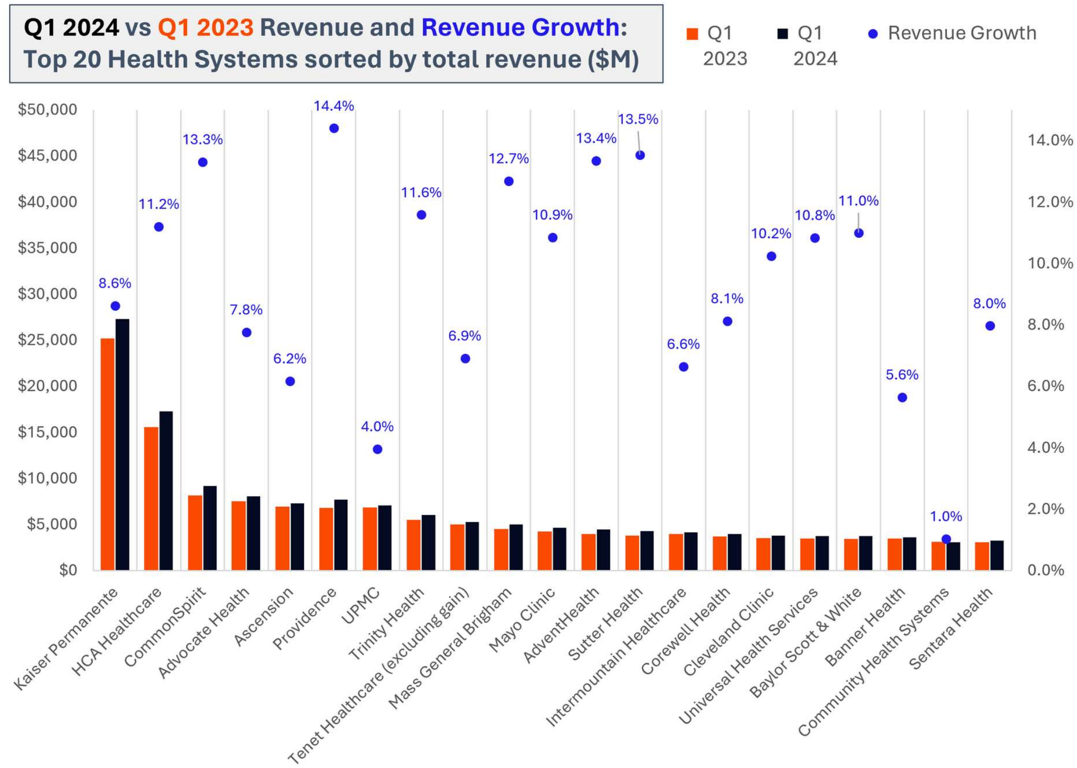
Median revenue growth in Q1: 10.5%



Source: public company filings and EMMA disclosures as of 5/30/2024; certain nonpublic health systems and nonprofit health system financial data were not available as of the selected date. Sorted by total net operating revenue in Q1 2024.

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6. A Comparative Analysis of Public, For-Profit Hospital Operators

Q1 2024 Hospital Analysis

In Millions of Dollars

	HCA Healthcare Q1 2023	HCA Healthcare Q1 2024	HCA Healthcare % Change	Tenet Health Q1 2023	Tenet Health Q1 2024	Tenet Health % Change	UHS Q1 2023	UHS Q1 2024	UHS % Change	CHS Q1 2023	CHS Q1 2024	CHS % Change
Net Operating Revenue	15,591	17,339	11.2%	5,021	5,368	6.9%	3,468	3,844	10.8%	3,108	3,140	1.0%
Operating Income	1,922	2,247	16.9%	603	3,285	444.8%	279	389	39.5%	210	231	10.0%
Adjusted EBITDA	3,172	3,353	5.7%	832	1,024	23.1%	421	526	24.9%	335	378	12.8%
Net Income (Excluding NCI)	1,363	1,591	16.7%	143	2,151	1404.2%	163	266	63.0%	(51)	(41)	-19.6%
Operating Margin	12.3%	13.0%	5.1%	12.0%	61.2%	409.6%	8.0%	10.1%	25.8%	6.8%	7.4%	8.9%
Adjusted EBITDA Margin	20.3%	19.3%	-5.0%	16.6%	19.1%	15.1%	12.1%	13.7%	12.7%	10.8%	12.0%	11.7%
Net Income Margin	8.7%	9.2%	5.0%	2.8%	40.1%	1307.0%	4.7%	6.9%	47.0%	-1.6%	-1.3%	-20.4%
Key Operating Metrics (Same-Facility)												
Admissions	523,458	555,681	6.2%	119,714	124,750	4.2%	79,063	83,581	5.7%	103,172	107,055	3.8%
Adjusted Admissions	913,434	960,772	5.2%	219,914	223,912	1.8%				231,625	236,113	1.9%
Patient Days	2,637,903	2,781,596	5.4%	629,060	649,086	3.2%	397,998	415,327	4.4%	479,168	493,824	3.1%
ER Visits	2,238,063	2,400,190	7.2%	474,116	492,912	4.0%						
OP Surgeries	253,023	247,721	-2.1%	46,476	43,785	-5.8%						
IP Surgeries	130,010	132,274	1.7%	30,458	31,607	3.8%						
USPI Same-Facility Surgical Cases				400,747	393,538	-1.8%						

Every for-profit public operator saw operating margin improvement in Q1. I wrote about HCA and Tenet in the broader Hospitalogy newsletter, which you can read below.

My HCA analysis: Apart from some troubles at Mission, HCA's operations continue as a unicorn (strong volumes, inpatient market share growth, case mix acuity upward trend over several years, good demographics in markets) despite some expense headwinds from professional service fees and its recent acquisition of Valesco.

My Tenet breakdown: As Tenet makes divestitures in the acute care space, its USPI portfolio is outperforming. In a pre-announced earnings release, Tenet noted that strong surgical growth in USPI resulted in higher-than-expected profitability – above the high end of its adjusted EBITDA guidance for '23. This trend has continued in Q1.

Main takeaways from the above include HCA's decision to be a hospital-centric health system while Tenet is doubling down on USPI and ambulatory growth, selling noncore assets in noncore markets in the process.

7. Health System Bifurcation Dynamics: What's the end game?

https://www.kaufmanhall.com/insights/research-report/national-hospital-flash-report-april-2024

As a quick excerpt from my industry update published to my community a few weeks ago, pay attention to the bifurcation we're seeing among hospitals and health systems.

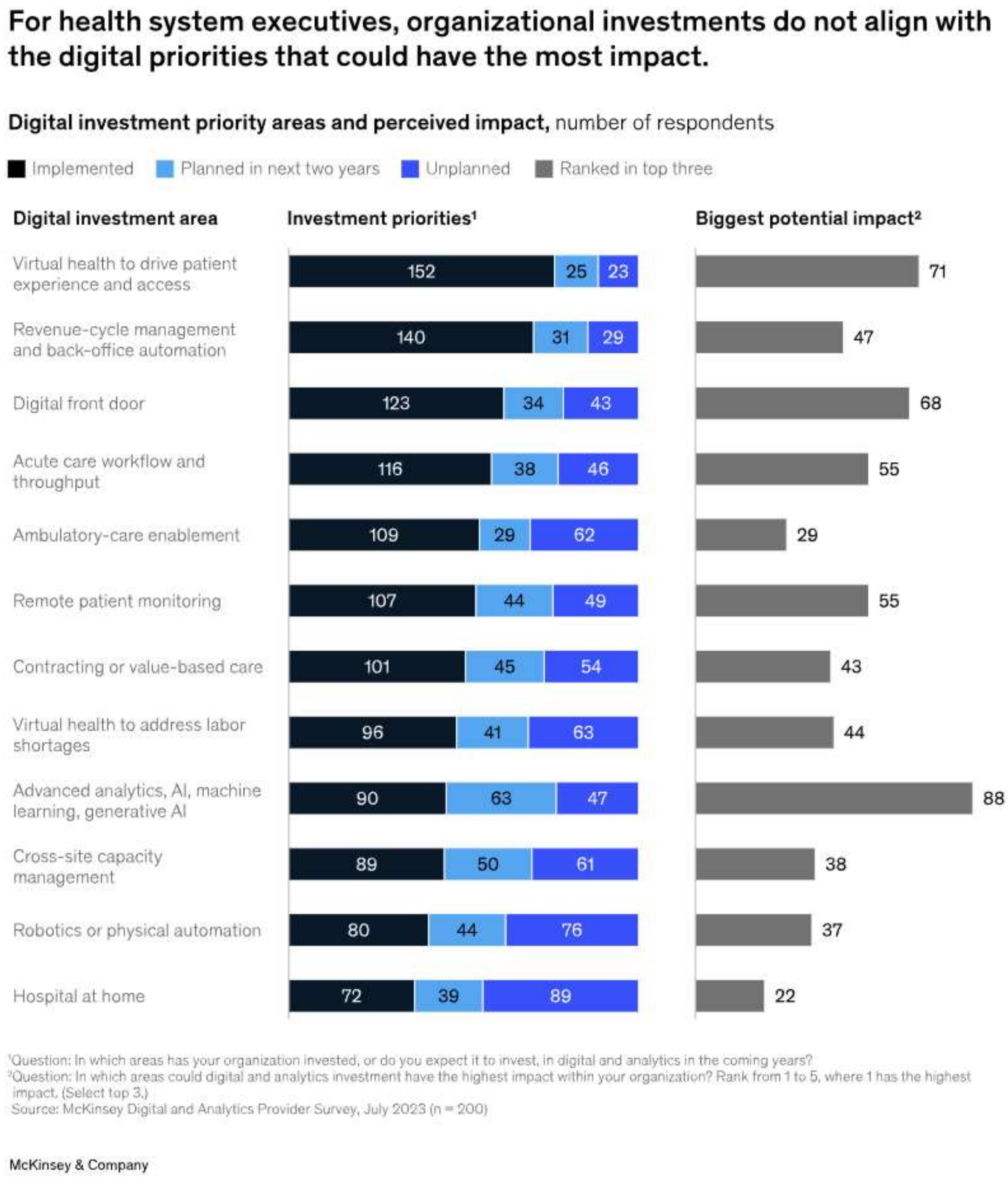
Larger integrated health systems with appropriate market density are outperforming, and these players are pulling away from the pack (many names included within this write-up).

These are the price ‘makers’ in markets - whereas price ‘takers’ are still struggling, and the state of many hospitals continues to be dire - ~40% of hospitals are underwater financially per the latest tally.

Hospitals and health systems unable to reinvest capital into new projects and expansion are falling behind quickly as labor, inflation, local market realities, and other operating headwinds apply significant pressure.

Kaufman Hall noted this health system bifurcation dynamic as an ‘inverted bell curve’ which is quite alarming and should only fuel consolidation and service line closures for the have-nots. Ken Kaufman’s post on these dynamics are must-read for any provider organization leader.

8. Health System Transformation Initiatives: Where are Leaders Investing, and What's the Perceived Impact?



https://www.mckinsey.com/industries/healthcare/our-insights/digital-transformation-health-systems-investment-priorities

Final graph, I promise!

This one was a great look at health system investment priorities as of mid 2023.

Note the glaringly obvious hole here post-Change Healthcare - no cybersecurity investments are included on the list. I'd bet it makes the list in an updated survey. But you can see the primary focus for health systems in transformation land sits squarely on telehealth / virtual care capabilities, RCM and back-office automation, and digital front door investments.

That's it for this week! Feel free to post any thoughts on the community forum, or get in touch with me for any feedback.

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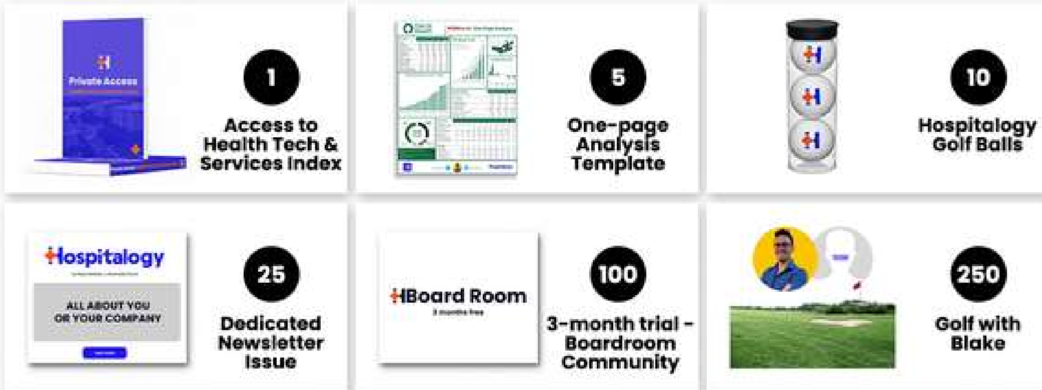
It's all about turning challenges into opportunities.

Grab the report below and let's shape your financial strategies for 2024 and beyond.

Download the report for free

Thanks for the read! Let me know what you thought by replying back to this email.

— Blake



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