NAVIGANT
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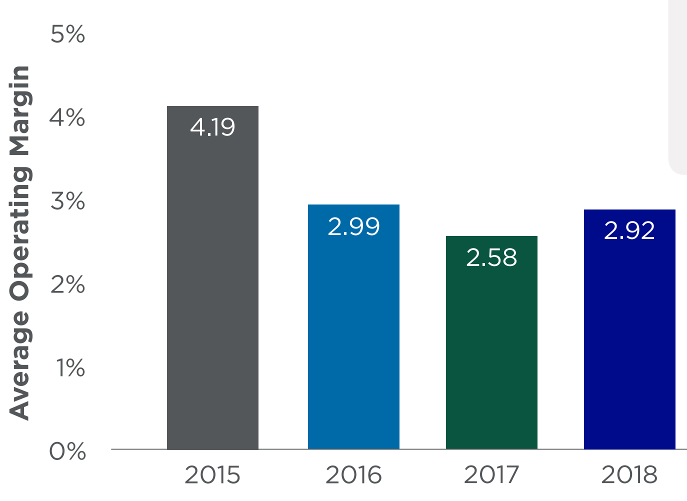
2019 Health System Financial Analysis

OCTOBER 2019

According to a Navigant analysis of four years (2015-2018) of operating measures for 103 major U.S. health systems that own 44% of the country's hospitals:

Operating Margins Rebound, Still Trail 2015 Levels

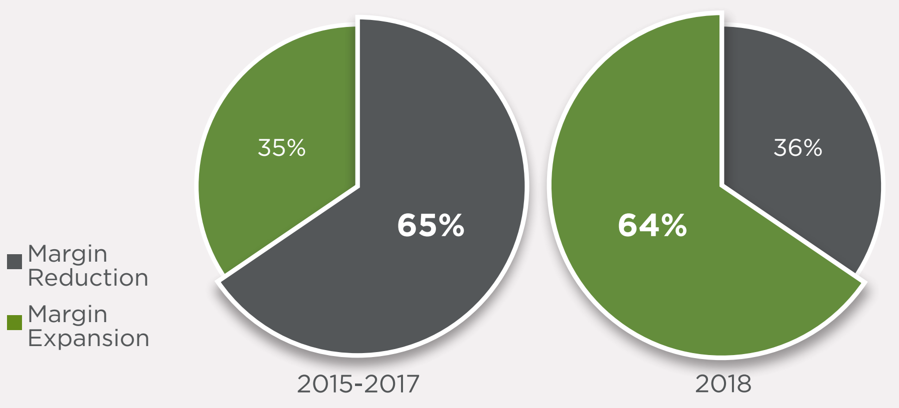


Average health system operating margins
rose 13% in 2018 after a
38%+ decline from 2015 to 2017

More than **50%** of the sample remain **~30% below** 2015 levels

Operating Income Improves for Majority – Not All – Health Systems

Change in Operating Margins from 2017 to 2018



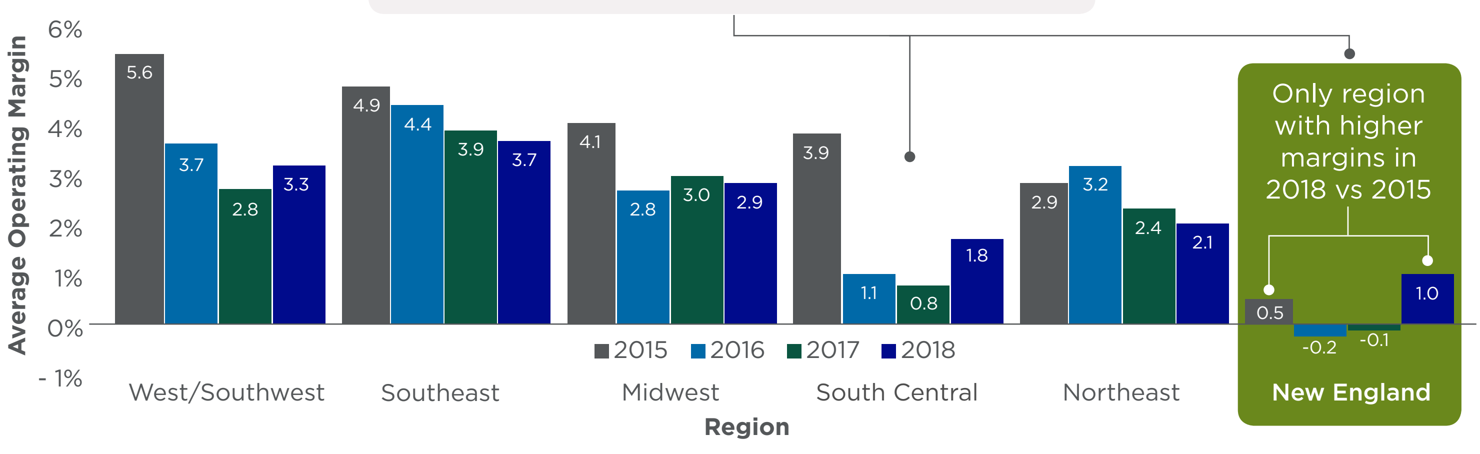
64% of systems improved margins in 2018, a marked contrast to 2015-2017 when two-thirds experienced margin deterioration

15 systems had 4-year declines of **$100 million+** each

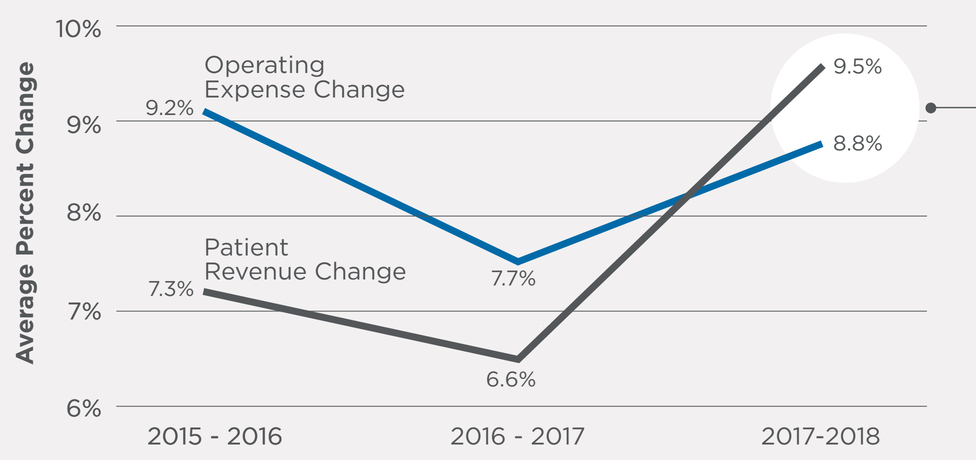
4 systems had 4-year declines of **$300 million+** each

Regional Variation in Operating Margin Performance

Most significant 2018 margin improvements in **New England** and **South Central** regions



Expense Control Vigilance, Revenue Turnaround Drives Margin Improvement



2018 revenue growth exceeded expense growth for the first time in three years, with **revenues growing at more than double expenses** from 2017 - 2018

Main reasons for revenue increases:

MERGER & ACQUISITION ACTIVITY

ENHANCED REVENUE CYCLE MANAGEMENT AND EHR OPTIMIZATION

IMPROVED COMMERCIAL REVENUE YIELD

While 2018 was a turnaround year for health systems, achieving sustainable margins over the longer term will require renewed focus on operational efficiency. Doing so necessitates not only better revenue analytics but active management and rebalancing of systems' revenue portfolios.

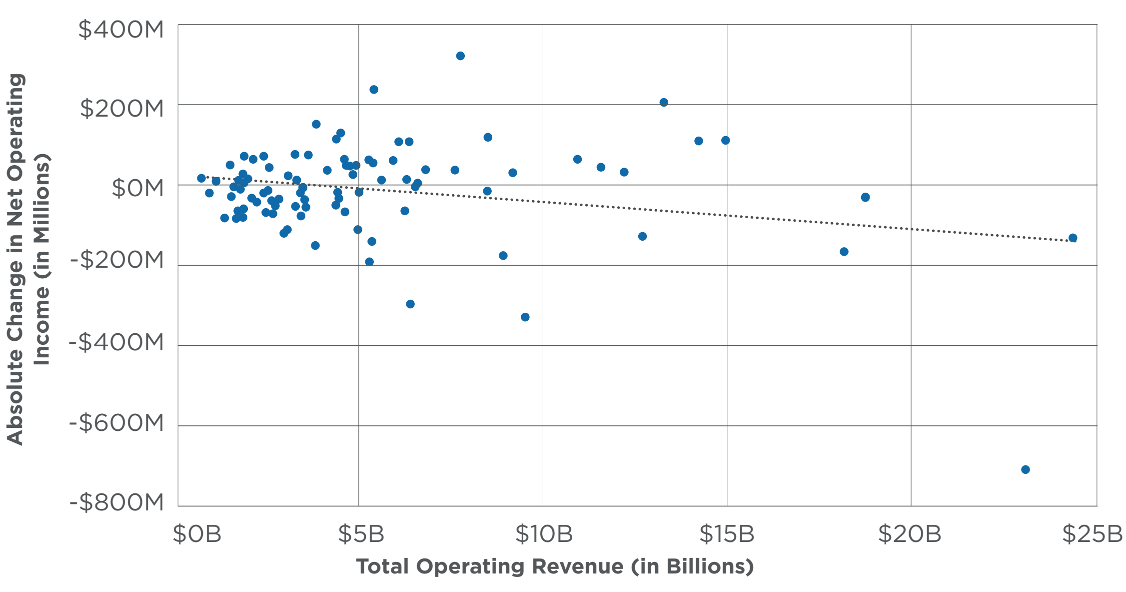
JOHN WIEST
Managing Director, Navigant

Scale Negatively Related to Financial Performance, 2015-2018

Health system scale based on 2018 total patient revenue
found to be a negative predictor of operating performance

Smaller health systems had better financial performance
as measured by change in operating profit compared to larger organizations

Change in Net Operating Income (2015-2018) vs. Total Operating Revenue 2018



These findings highlight obvious challenges for systems that have grown through mergers and acquisitions to actually realize the operational synergies they identified in their premerger planning. It is taking larger systems longer to achieve claimed synergies from mergers than perhaps their managements realized.

JEFF GOLDSMITH, PHD
National Advisor, Navigant

What Health Systems Should Do to Maintain Operational Improvements

- Better control labor and supply costs, corporate overhead, and contracted services.
- Use data analytics to reduce clinical variation, achieve ROI on physician employment and clinical IT.
- Service line rationalization to reduce programmatic duplication in neighboring facilities, eliminate programs with marginal volumes and/or substandard quality.
- Active surveillance and management of revenue portfolios, and the willingness to make continual corrections in expense trends if revenue problems materialize.
- Leverage capabilities to compete with non-traditional providers (e.g., retail clinics, eHealth providers) vying for ambulatory market share.

Our analysis reinforces our belief that rigorous control over staffing, improved clinical effectiveness, and better resource use are vitally important to the short- and long-term financial health of hospitals and health systems.

ALEX HUNTER
Managing Director, Navigant

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