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Healthcare Post-COVID-19:

Uncertainty and Opportunity for Provider Restoration and Revitalization

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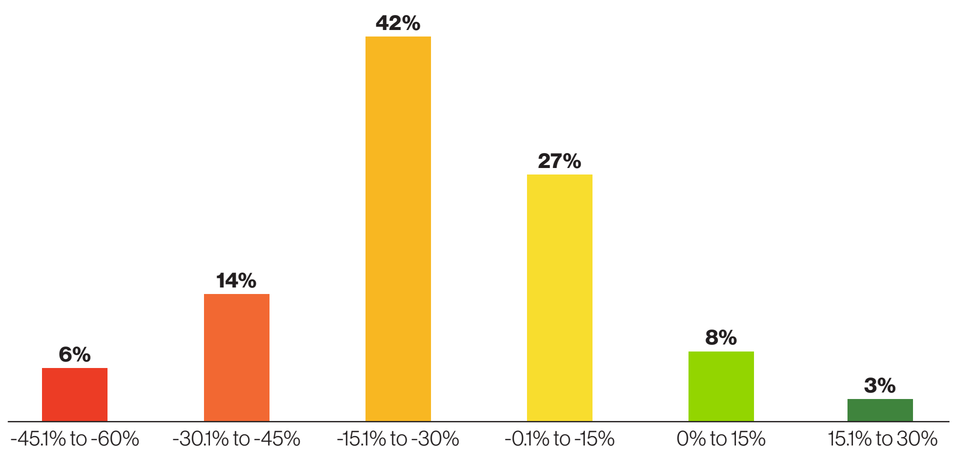
Background

As the COVID-19 pandemic unfolds, the essential role that care providers play in communities nationwide has never been more apparent. Examples of the dedication of frontline healthcare workers risking their personal health to care for coronavirus patients have become widespread. What's also coming into focus is the rapidly deteriorating financial position of the hospitals and health systems that employ the millions of doctors, nurses, and other clinicians caring for COVID-19 patients.

The American Hospital Association estimates the total COVID-19 financial impact on hospitals and health systems through June will exceed $200 billion — an average of more than $50 billion a month — with the bulk of losses stemming from canceled elective and nonelective surgeries.[1]

Looking forward, a Guidehouse/HFMA COVID survey[2] of provider executives suggests that, compared to pre-pandemic levels, 89% of respondents predict their organizations' revenues will be lower at the end of 2020. Among them, almost two-thirds project decreases of greater than 15%, while one-in-five forecast decreases of more than 30%. (Figure 1). Moreover, additional Guidehouse analysis of health systems representing ~350 hospitals nationwide found median cash on hand is projected to drop 26% from approximately 190 days to 140 days by the end of 2020, assuming hospitals must repay advanced payments from Medicare.

Figure 1: Hospital and Health System Revenue Projections, End of 2020 vs. Pre-Pandemic *Guidehouse, HFMA COVID-19 Hospital & Health System Survey*



"Median hospital cash on hand is projected to drop 26% from approximately 190 days to 140 days by the end of 2020."

A major reason for this projection: half of respondents anticipate it will take through the end of the year or longer for their organizations' elective procedure volumes to return to pre-COVID levels. While federal funding will help hospitals on the road to recovery, just 11% of all executives — and only 3% of health system respondents — believe it will be enough to cover COVID-19-related costs.

1. American Hospital Association, "New AHA Report Finds Financial Impact of COVID-19 on Hospitals and Health Systems to Be Over $200 Billion through June," May 5, 2020, https://www.aha.org/special-bulletin/2020-05-05-new-aha-report-finds-financial-impact-covid-19-hospitals-and-health.
2. Guidehouse, "COVID-19 HOSPITAL & HEALTH SYSTEM SURVEY," May 21, 2020, https://www.guidehouse.com/covidhealthcaresurvey.

Key Principles in the New Healthcare Reality

COVID-19 has created an industrywide scenario that has brought unparalleled amounts of uncertainty and volatility.

For provider executives, the main area of uncertainty is specific to the recovery of patient volumes. As local and state legislators allow organizations to conduct elective procedures, will consumers continue to avoid obtaining care, including in the emergency department, due to fear of contracting the virus? How will the economy impact consumer ability to afford and access care?

Executives have also been left asking:

- How do we meet the demand for increased telehealth and remote work?
- Despite federal funding and relief sources, how will we overcome the significant operating gaps and struggles accessing capital from the loss of patient volumes and investment income?
- How will we respond to a second COVID-19 wave or surges, should they materialize?
- How do we deal with dramatic shifts in payer mix?
- How do we create new points of access to address the needs of our patients that help them feel safe and well cared for?

There is one thing providers can be certain of: Their business models will not return to what they were before COVID-19. Healthcare delivery, operations, and competitive dynamics are poised to undergo rapid and fundamental transformation in response to the pandemic.

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Following is a series of principles regarding what the future holds for providers in the new healthcare reality.

1. A significant decline in reimbursement cross-subsidization opportunities

The pandemic is a painful reminder for health systems that most of their margins have been driven by commercial elective services. The majority of payers are reporting strong earnings, and while some are offering premium returns in anticipation of low medical loss ratios, there remains an uneven playing field across local payer/provider relationships.

As the U.S. economy labors post-pandemic, insured patients will struggle to shoulder greater cost sharing through their high-deductible health plans and commercial enrollees will decline as unemployment rates increase to levels unseen since the Great Depression. For providers, this means a deterioration in their payer mix and fewer opportunities for reimbursement cross-subsidization.

2. Advanced digital solutions will be a necessity, not a luxury

A comprehensive consumer- and caregiver-centric digital strategy is a foundational requirement in the post-COVID world.

Consumer

When it comes to providing a seamless, integrated digital experience for consumers, hospitals are known to lag healthcare disruptors and payers[3] that are already offering digital health solutions across the U.S., some of which may be favored consumers. Those providers that can leverage technology to make access to care easier, more personal, and timelier will be better equipped to win back consumer confidence and offset disruptor advancement.

An essential place to start is the use of telehealth, which has dramatically increased through the pandemic, and it's here to stay. Suspension of regulatory barriers, more beneficial reimbursement models, increased start-up funding, and rapid shifts in access have all accelerated telehealth adoption. Similarly, consumers will be more willing to engage in telehealth visits than previously, permanently altering physical appointment volumes.

For most providers, there is work to be done. While 67% of COVID survey respondents predict their organizations will be using telehealth at least five times more than they did prepandemic, only one-third of them believe their organizations have all the needed telehealth capabilities.

Furthermore, healthcare call centers have traditionally focused on metrics like dropped calls and call wait times. As the pandemic evolves, providers must implement contact center platforms and applications that go beyond simply answering the phone, to include speech recognition and customer information on pop-up screens.

3. Danielle Dyer and Subra Sripada, Guidehouse, "Healthcare Consumer Digital Experience Analysis," February 2020, https://guidehouse.com/insights/healthcare/2020/health-digital-analysis.

Caregiver

From a caregiver standpoint, most providers successfully installed electronic health record (EHR) systems over the past decade, initially motivated by billions in "meaningful use" dollars. While it was anticipated that EHRs would be the main driver of broad performance improvement, providers have instead experienced clinical and operational frustrations, including clinician burnout and an increase in expenses.

The reality with the EHR movement is healthcare did a great job of putting modern technology on old processes. Moving forward, providers must use technology to enable critical workflows, such as patient placement and referrals, in a post-COVID world. Implementing advanced IT to enhance system automation, such as shifting hardware and physical assets to the cloud and use of robotic process automation, has proven to be successful in improving operations in other industries. Providers must follow suit.

3. Greater market turbulence and competition from outside healthcare

Large Employer Disruption in Healthcare

amazon

Amazon continues to grow heavily across a number of healthcare channels, including: Amazon Care (employee health clinic); Cerner partnership with Amazon Web Services, AI, and health compliance for current tools (e.g., Alexa and HIPAA); integration across distribution channels (e.g., PillPack); and continued development of Haven, the co-venture with JPMorgan and Berkshire Hathaway.

Walmart

Walmart, the U.S.'s largest employer by a wide margin, now offers both payer and care services, including pharmacy and retail clinics, and it recently opened its first Walmart Health Centers for basic healthcare services.

With historical payer-provider disruption unable to sufficiently "move the needle" on healthcare spending, some of the nation's largest private organizations and employers have begun to reimagine a scenario that more tightly controls spending across consumers, payers, and providers.

The pandemic has opened the door wider than ever before for these organizations, which have much deeper expertise in providing an integrated, digitally enabled experience for consumers, to dig into the provider side of healthcare. Such a scenario poses a major threat to providers, raising the question: Could these models be prototypes for the future of commercial insurance and a new class of competition for traditional providers?

4. A marked move from a fixed to a variable cost structure

The COVID-19 pandemic has taught American industry – and healthcare in particular – the importance of being nimbler to right-size operations. Moving from a fixed to a variable cost structure will be key to doing so. Care delivery and its supporting physical footprint will be reimagined in a post-COVID world, with an enhanced focus on greater standardization and more effective corporate functionality and caregiver engagement. As such, executives are preparing for significant changes to their organizations' working arrangements.

Many back-office corporate functions have moved to a virtual environment as a result of the pandemic, leaving provider executives wondering whether they need as much real estate. According to the Guidehouse/HFMA COVID survey, just one-in-five executives expect their organizations will return to the primarily onsite work arrangements they had before the pandemic. Not surprisingly, capital expenditures, including new and existing construction, is the top area respondents say they'll target for intermediate and long-term cost reductions.

5. Capital will be much more difficult to secure, increasing the need to unload extraneous assets

Many health systems have depended on the strong investment income they attained through the longest period of uninterrupted economic growth in American history to maintain modest margin growth. But that economic run has ended, and investment income can no longer be relied upon to sustain organizations or even buy a little time.

Health system strategies were not built for reacting to and surviving a pandemic. While previous economic disruptions spawned only marginal change, the unprecedented turbulence the industry and economy are facing will require leadership to make some uncomfortable decisions. As the need for a quicker return on investments increases, providers must focus on the new realities of their markets and their financial situations. It's likely that a period of short-cycle strategies will emerge, with many executives avoiding the traditional approach of creating long-term strategies driven by consensus building.

6. A marked increase in thoughtful provider consolidation

While provider consolidation has led to much criticism, COVID-19 has created an opportunity to devise a more thoughtful — and necessary — approach to M&A.

The pandemic magnifies the difference between "haves" and "have-nots." Leading providers will have the opportunity to leverage their strong balance sheets to shape their local markets, as smaller players struggle to maintain cash flow through the crisis. The impact will be enough to require some providers to search for organizations to acquire them. And acquirers are out there, looking for opportunities to improve their operating models and growth profitably, with the means to do so.

Emergence of a Strategic Growth Framework

The window of opportunity that will determine provider success or failure is limited in a post-COVID reality. Competition will be fierce as hospitals and health systems work to restore their organizations by addressing near-term cash pressures and liquidity concerns. Unlike the industry norm, historic pricing power and scale alone will not define providers that grow. Instead, organizations will need to respond to the impact of COVID-19 by reassessing their competitive positions and demonstrating the ability to pivot nimbly, both strategically and operationally.

Based on a Guidehouse analysis of 350 hospitals nationwide, we believe organizations will fall into one of four situations, based on their projected local market growth and competitive position, including the degree to which their consumer base has been resized and reshaped (Figure 2).

For providers, the playbook will be focused on rebuilding patient volume, reducing operating expenses, and addressing new payment mechanisms based on market forces. Sizing, prioritizing, and the pace of required change will differ for each provider, depending upon their current competitive position and the expected growth in their market.

Figure 2: Market Positioning and Opportunities Determine the Path Forward

Market Growth (Population)		
	Positioned to Grow: Position as low cost provider with differentiable, new value proposition to defend against stronger players getting stronger. Characteristics: A growing market – Provider has a strong market share and competitive financial position. Strategy: Differentiate based on ease of access and targeted growth segments. Requirement: Achieve minimum of 4%+ operating margin to profitably grow.	**Positioned to Shape:** Leverage strong market position and sizable balance sheet to reshape the market while redesigning operating model. Characteristics: A growing market – Provider has leading market share and financial strength. Strategy: Shape the market and innovate delivery and portfolio to continue to grow share. Requirement: Achieve 6%-8%+ operating margin to invest in a new business model.
	Positioned to Survive: What's the path to financial and operational viability, given role in stagnant market? Characteristics: A stagnant market – Provider has lagging market share and declining financial position. Strategy: Maintain independence or pursue consolidation partner. Requirement: Rapid action to return to breakeven.	**Positioned to Defend:** Focus on ease of access and innovation to reduce costs, and targeted market expansion. Characteristics: A flat market – Provider has strong market share and financial position. Strategy: Win the market by gaining share of wallet. Requirement: Build on 4%+ operating margin to win the market.

Competitive Position (Market Share)

Healthcare has largely been insulated from previous economic disruptions, with capital spending more acutely affected than operations. But the COVID-19 pandemic will very likely be different, since the crisis started with a one-time significant impact on operations that is not fully covered by federal funding. Through the pandemic, providers are facing a long-term decrease in commercial payment, coupled with a need to boost caregiver- and consumer-facing engagement, all during a significant economic downturn.

For organizations in some markets, it may seem like business as usual. For many others, these issues and greater competition will demand more significant, material change. While situations may differ by market, it's clear that the prepandemic status quo won't work for any hospital or health system. Winners and losers will quickly emerge, and resilient providers that can execute against the above principles will have the opportunity to grow organically or through acquisition. But with this opportunity comes responsibility to evaluate each situation closely to ensure they can bring their winning formula to additional communities.

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