strata

2024 CFO Outlook for Healthcare

Performance Management Trends and Priorities

Introduction

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2023 was a year of recovery for healthcare organizations nationwide, as many worked to rebuild financial health following a challenging 2022. While hospitals and health systems saw gains in revenues and margins, ongoing expense pressures slowed progress.

The median hospital operating margin climbed to 2.3% in December 2023, its highest level in about two years. December marked a 10th consecutive month of positive hospital operating margins after the metric fell into the red throughout 2022 and the first two months of 2023. Even with the margin improvements, hospitals saw persistent expense growth throughout the year. Non-labor expenses had the biggest increases — jumping more than 20% from 2019 to 2023 — as organizations felt the ongoing effects of inflation.

Despite continued challenges, healthcare leaders are optimistic about the year ahead. Our annual survey of finance professionals nationwide found that more than half are optimistic about their organizations' financial health and anticipate they will see further operating margin growth in 2024.

Reining in costs, including high labor costs, remains a primary aim for healthcare leaders. Survey respondents cited contract labor and employed labor as their biggest unforeseen costs of 2023. Respondents identified their top priorities for 2024 as:

- Reducing costs
- Managing strategic and performance improvement initiatives
- Managing service line financial performance

Healthcare leaders are increasingly leveraging data to address such challenges. The survey results show that more than nine in 10 organizations use benchmark data to inform organizational decisions, but nearly as many said their organizations should do more to leverage financial and operational data for effective decision-making.

This report combines findings of our annual CFO Outlook survey with year-end data from more than 1,300 hospitals and health systems and more than 135,000 physicians, including Axiom™ Comparative Analytics and Strata's All-Payer Claims and StrataSphere™ data. Drawing insights from our various datasets allows us to provide a retrospective look at 2023 and a more comprehensive view of the year ahead.

Priorities and Challenges

2023 Was a Year of Recovery for Healthcare

THE DATA

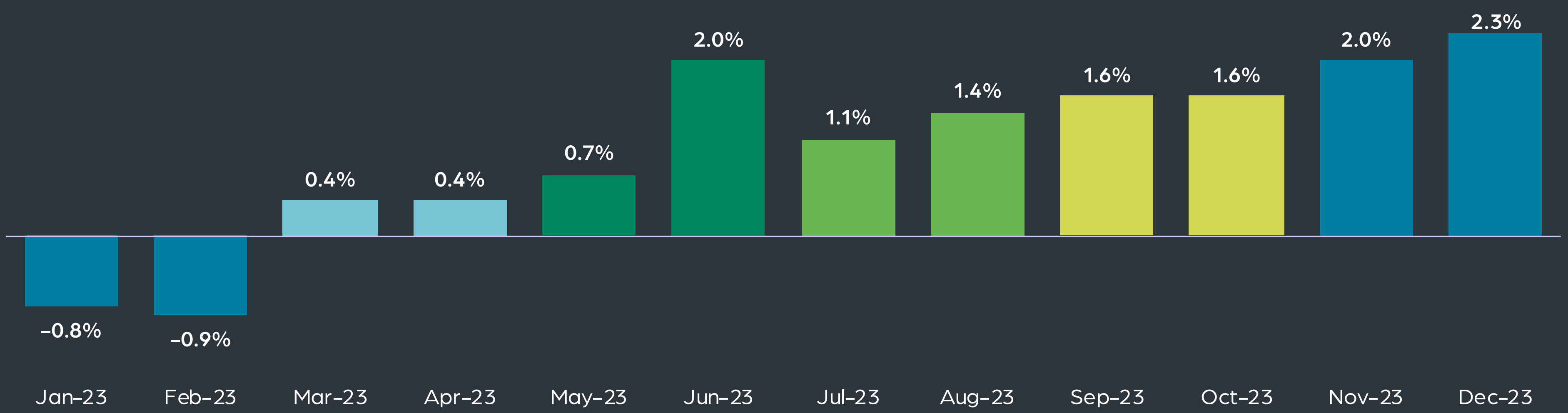
U.S. healthcare organizations moved toward more sustainable financial footing in 2023 following a perilous year of operating losses throughout 2022. Revenue gains contributed to operating margin improvements for hospitals and health systems nationwide, but those gains were hampered by relentless expense increases.

Hospital operating margins stabilized somewhat in late 2023, with the median year-to-date operating margin reaching 2.3% in December. It marked the 10th month of positive operating margins and a second consecutive month of margin increases following unsteady performance, including narrow margins throughout the year and a rocky start with margins in the red in January and February.

Margins remain narrow, but overall margin performance rose in 2023 compared to 12 months of negative margins seen in 2022. For 2023 overall, the median change in operating margin rose 2.4 percentage points versus 2022, while the median change in operating earnings before interest, taxes, depreciation, and amortization (EBITDA) margin rose 2.1 percentage points. For December 2023 versus December 2022, both median operating margin and operating EBITDA margin were up 2 percentage points.

Median Hospital Operating Margins

Nationally, Year-to-Date



Source: Axiom™ Comparative Analytics

Persistent Expense Increases Hinder Progress

THE DATA

Total hospital expenses saw persistent increases throughout 2023. The increases were particularly stark compared to before the COVID-19 pandemic in 2019.

Total expenses jumped 22% in 2023 compared to 2019. While expenses climbed across all categories, non-labor expense had the biggest increase, rising 21.5% over the four-year period due to the ongoing effects of inflation and other expense pressures.

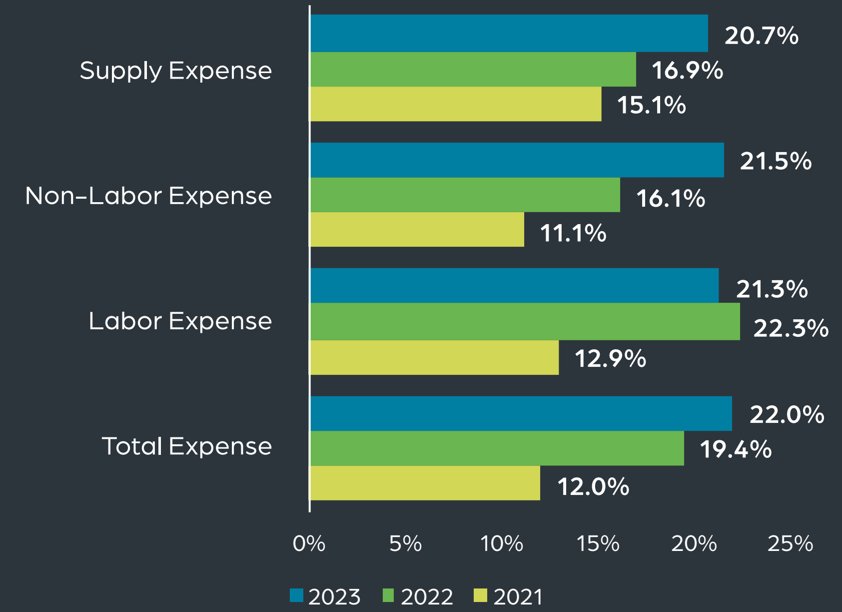
Such factors contributed to steady expense increases in recent years across non-labor categories. Supply expense, for example, rose 20.7% above 2019 levels in 2023, compared to 15.1% and 16.9% increases above 2019 levels in 2021 and 2022, respectively.

Labor expense remained elevated, up 21.3% for 2023 versus 2019. While still high, that was down slightly from the 22.3% increase from 2019 to 2022, reflecting that some hospitals were able to rein in high contract labor costs that spiked with pandemic-related demand in early 2022.

According to our StrataSphere data from 353 hospitals, contract labor costs as a share of total labor expense declined from a high of 7.4% in the second quarter of 2022 to 3.4% in the fourth quarter of 2023. While the declines are an improvement, contract labor costs remain above pre-pandemic levels, when they averaged about 1% of total labor expense.

Yearly Expense Trends vs. 2019

Hospitals Nationally



Source: Axiom™ Comparative Analytics

Contract Labor Declining as a Share of Overall Labor Expense

Source: StrataSphere data

Note: Analysis included data from 353 hospitals.

Healthcare Leaders Optimistic About Financial Performance in 2024

LEADERS' PERSPECTIVES

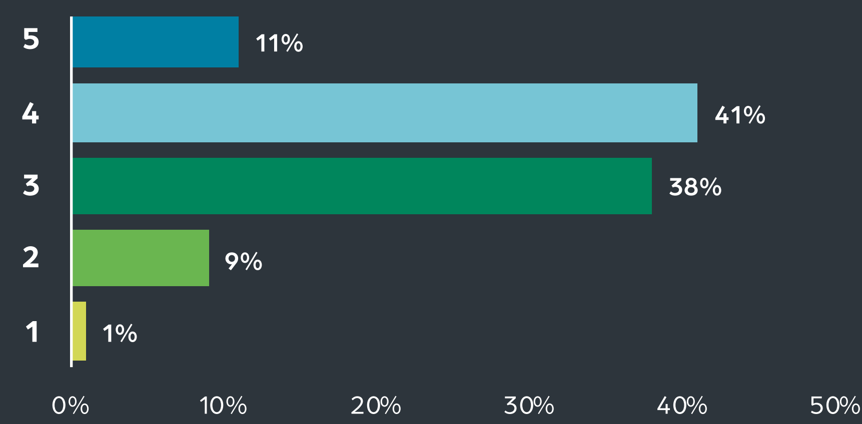
Financial improvements in 2023 contributed to increased optimism about performance in 2024. Our survey of healthcare financial professionals nationwide found that more than half (52%) said they were optimistic about their organization's financial future, ranking their optimism at 4 or 5 on a 5-point scale. Only 1% of respondents said they were not optimistic about their organization's financial performance.

Fifty-two percent of respondents also said they expect to see their organizations' operating margin improve over the next year. Fourteen percent expect to see operating margins decrease over the course of the year, while 28% said it would be about the same and 6% said they did not know.

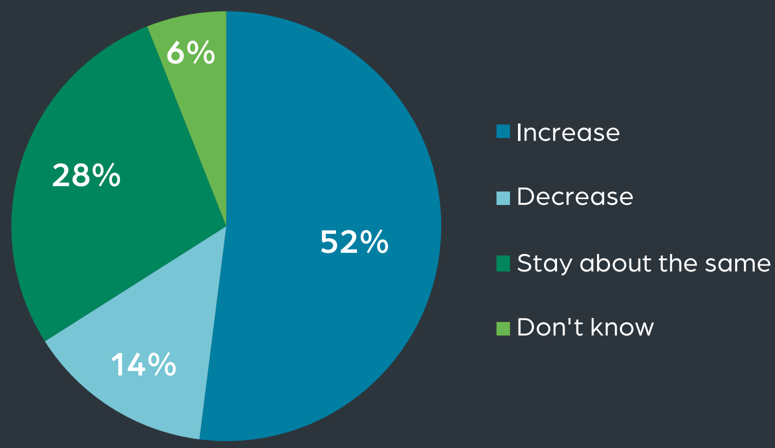
Cost improvements ranked as the area that offers the most opportunity to improve margin, while strategic growth was No. 2 and quality improvements was No. 3.

On a scale of 1 to 5, how optimistic are you about your organization's financial performance in 2024?

(1 = not optimistic, 5 = extremely optimistic)



What operating margin trends do you expect to see in 2024?



Labor Challenges Persisted in 2023

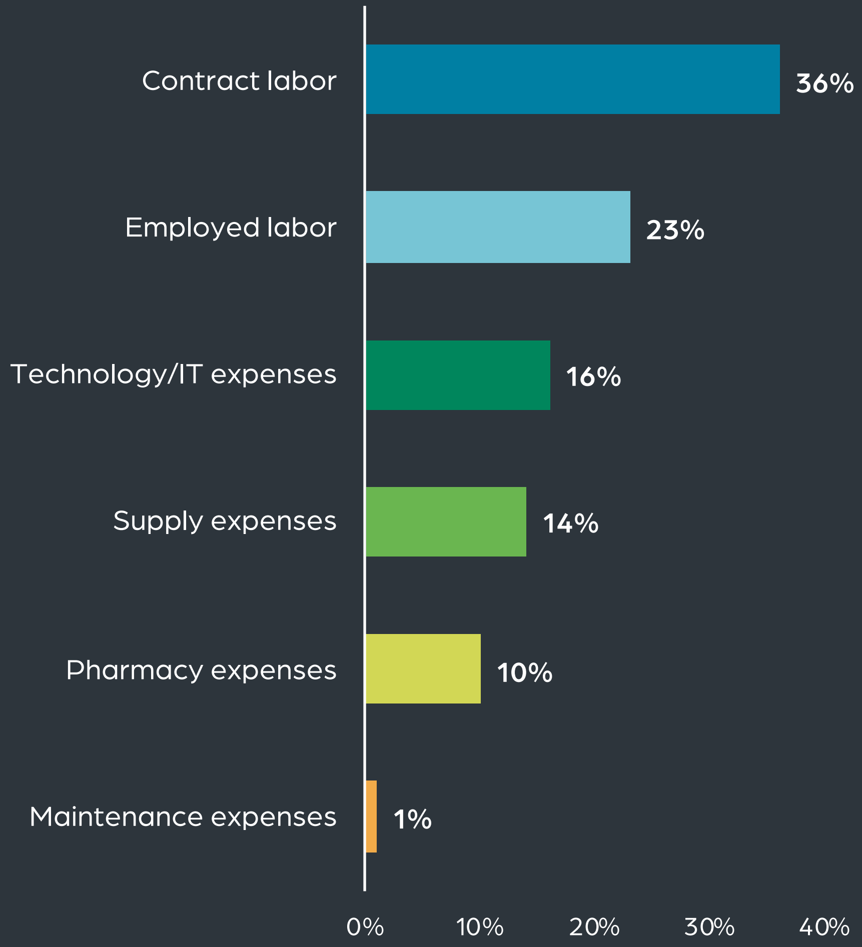
LEADERS' PERSPECTIVES

While non-labor expenses had the biggest increases, labor expenses remain hospitals' single largest expense, making up 47% of overall expenses in 2023, according to Axiom™ Comparative Analytics data.

Contract labor remains a focus for hospital finance teams even after many organizations tamped down pandemic-related spikes in contract labor costs from the previous year. Even so, more than a third (36%) of hospital finance professionals identified contract labor as their organizations' largest unforeseen cost for a second consecutive year.

Employed labor was another significant unforeseen cost in 2023, according to 23% of respondents. Other unforeseen costs included technology, supply, and pharmacy expenses.

What was your largest unforeseen cost in 2023?



Reducing Costs and Managing Improvement Initiatives Are Top Priorities for 2024

LEADERS' PERSPECTIVES

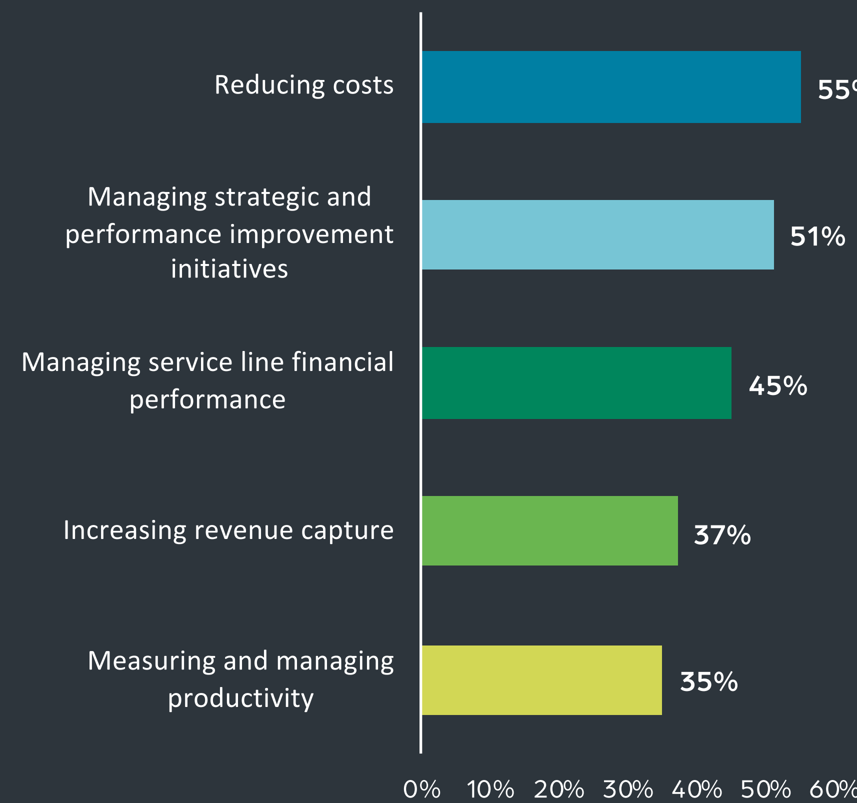
After the financial turmoil of 2022, the relative stabilizing of finances in 2023 helped healthcare leaders gain renewed confidence in their teams' ability to adapt to change.

The vast majority of survey respondents — 95% — said they are either very confident or somewhat confident in their teams' ability to adjust strategies in response to sudden market and business changes. That was up from 89% in 2023 and 92% in 2022. Of those responding to the most recent survey, 21% were very confident and 74% were somewhat confident. Only 5% were not at all confident in their organizations' ability to be agile.

In the face of ongoing increases in overall expenses, most respondents (55%) cited reducing costs as their No. 1 priority in 2024. Just over half (51%) of respondents also cited managing strategic and performance improvement initiatives as a top priority, while 45% indicated managing service line financial performance and 37% noted increasing revenue capture. More than a third (35%) of respondents said they are prioritizing measuring and managing productivity in 2024, down from 52% who said it was a top priority in the prior year's survey.

Are somewhat or very confident in their teams' agility

Top five priorities for 2024



High Costs, Low Reimbursements Contribute to Financial Pressures

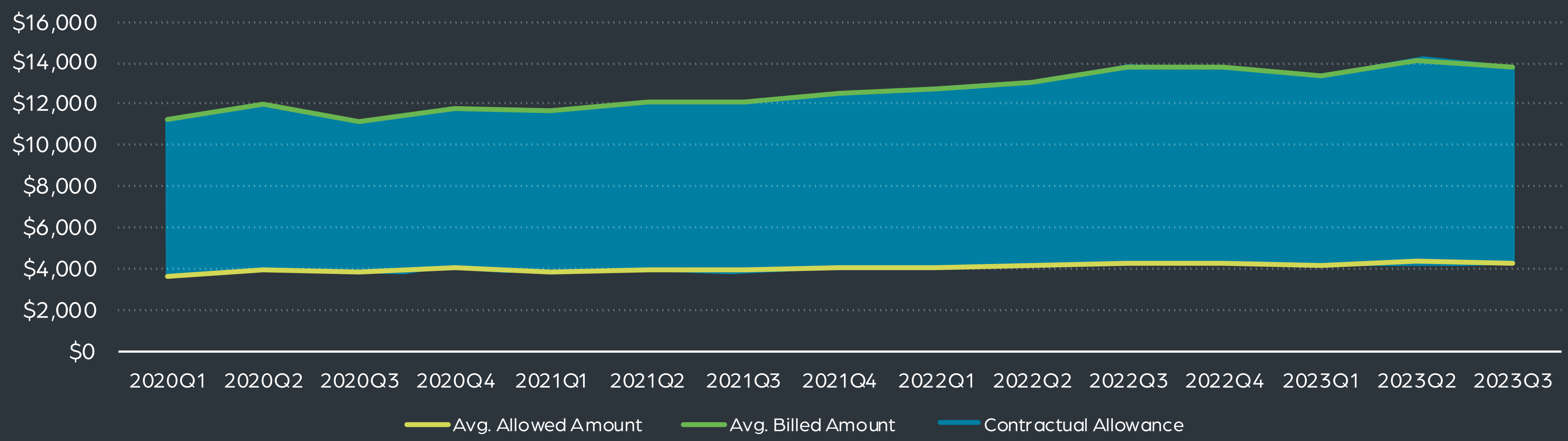
To illustrate some of the factors that contribute to sustained, narrow hospital operating margins, data from Strata's proprietary all-payer claims database (APCD) and StrataSphere show the high costs of care and the sizable gaps that persist between the amount hospitals bill for the care they provide and what healthcare payers reimburse for that care.

Looking specifically at shoulder surgeries as an example, the graph below shows how the amount paid to hospitals for such procedures — known as the allowed amount — has remained relatively flat in recent years while the amount hospitals bill has steadily increased due to rising costs. As of the third quarter of 2023, hospitals received nearly $9,600 below what they billed for shoulder surgeries. The gap between billed and allowed amounts has steadily widened, up more than 26% from $7,588 in Q1 2020.

Meanwhile, analysis of StrataSphere data shows the average cost to hospitals for shoulder surgeries increased 12% from early 2020 to the third quarter of 2023.

Avg. Billed vs. Allowed Amount for Shoulder Surgery

Facility-based Claims Occurring in a Hospital or ASC Setting



Source: Strata All-Payer Claims Data — 835 Remit National Dataset

Strategies and Opportunities

Hospitals See Mixed Volume Results, with Some Moderate Increases

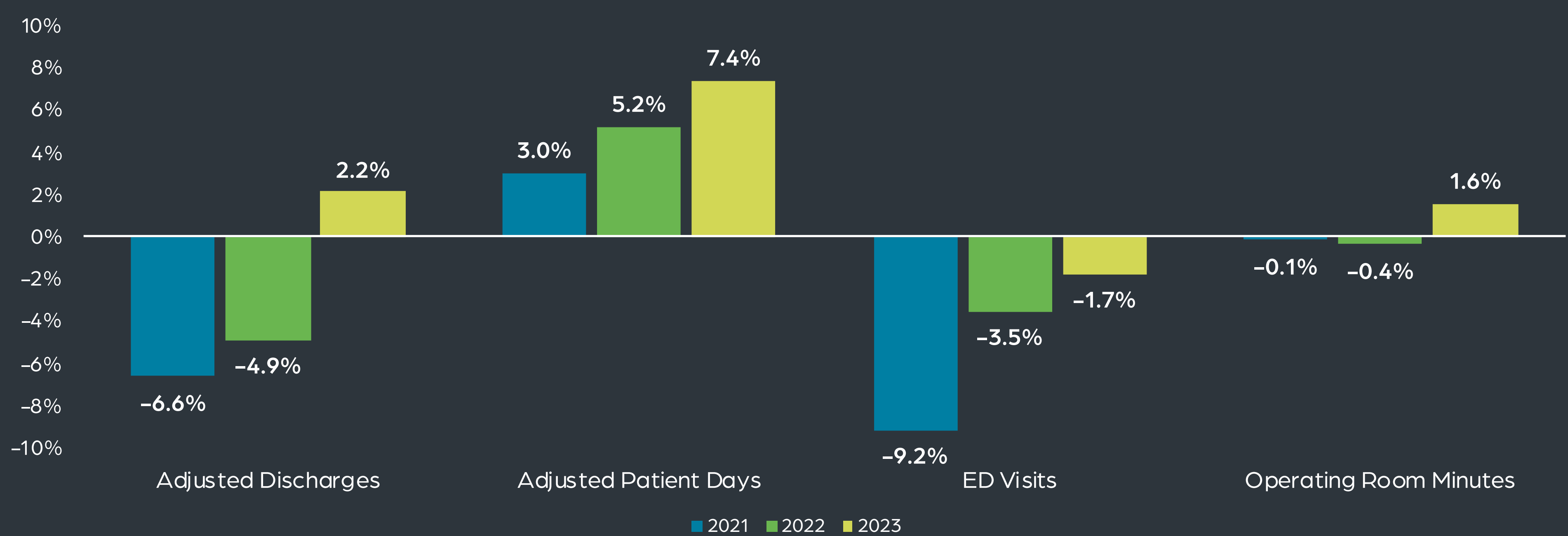
THE DATA

U.S. hospitals and health systems had some volume gains in 2023. Both adjusted discharges and surgery volumes rose above pre-pandemic 2019 levels for the first time in recent years. Adjusted discharges increased 2.2% from 2019 to 2023, after falling 6.6% and 4.9% below 2019 levels in 2021 and 2022, respectively.

Operating room minutes inched 1.6% above 2019 levels in 2023, after holding at less than 1% below 2019 performance the previous two years. Emergency department (ED) volumes, however, remain below pre-pandemic levels. ED visits were 1.7% below 2019 volumes in 2023. While low, the metric was up compared to 9.2% and 3.5% below 2019 levels in 2021 and 2022, respectively.

Yearly Volume Trends vs. 2019

Hospitals Nationally



Source: Axiom™ Comparative Analytics

Outpatient Volume, Revenue Increases Reflect Growing Demand

THE DATA

Outpatient volumes remain significantly higher than inpatient volumes as patients continue to demand more convenient outpatient options, and as healthcare payers adapt their coverage accordingly. StrataSphere data from 426 U.S. hospitals show there were approximately 17.9 million outpatient visits compared to just under 1 million inpatient visits in Q4 2023.

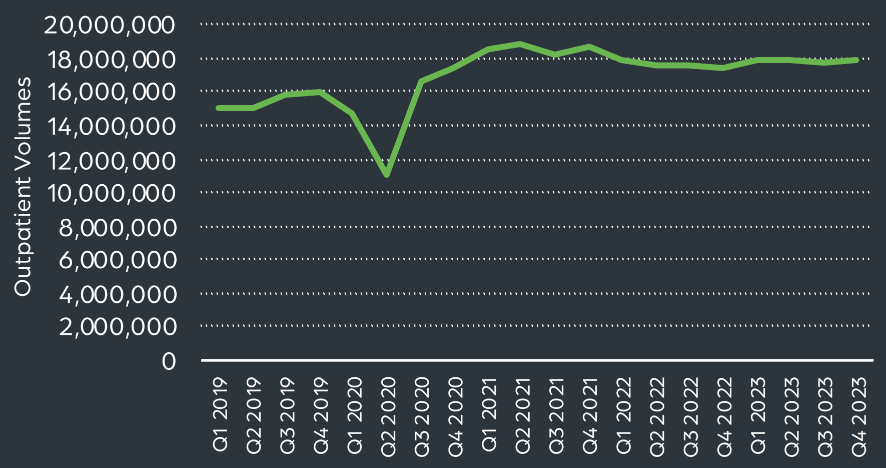
Looking at quarterly data over the past three years, outpatient volumes were above 15 million before the pandemic in 2019 and dipped down to a low of 11 million in Q2 2020, but have held above 17 million since late 2020. On an annual basis, overall outpatient volumes were up 14% in 2023 compared to before the pandemic in 2019.

Revenue increases in 2023 — especially outpatient revenue growth — contributed to finance leaders' optimism about how their organizations will fare financially in 2024.

Gross outpatient revenue climbed 32% in 2023 compared to levels seen before the pandemic in 2019. The metric has seen persistent increases in recent years, rising 11.4% in 2021 and 19.7% in 2022 versus 2019.

While gross inpatient revenues rose over the same period, the pace of increases was lower. Compared to 2019, inpatient revenue increased 11.1% in 2021, 10.7% in 2022, and 14.1% in 2023.

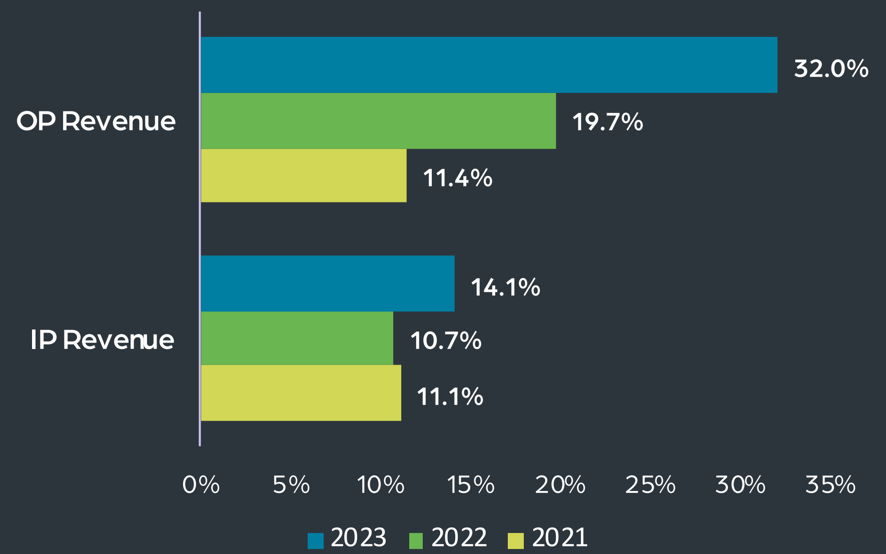
Demand for Outpatient Care Remains High



Source: StrataSphere data
Note: Analysis included data from 426 hospitals.

Annual Gross Inpatient and Outpatient Revenue Trends vs. 2019

Hospitals Nationally



Source: Axiom™ Comparative Analytics

Healthcare Leaders See a Need to Do More With Data

LEADERS' PERSPECTIVES

Most healthcare organizations leverage benchmarks to guide financial and operational improvements, but healthcare finance leaders acknowledge they are not using them to their full potential.

More than nine in 10 healthcare finance professionals (92%) surveyed said their organizations should do more to leverage financial and operational data to inform strategic decisions. Only 8% said they did not need to do more.

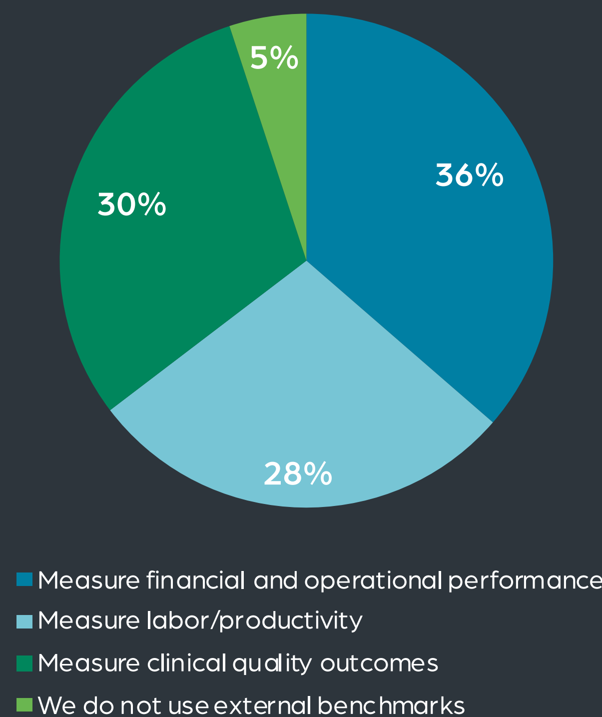
Ninety-five percent of healthcare organizations use external financial and operational performance benchmarks. More than a third (36%) use them to measure their financial and operational performance against other organizations, and 30% measure clinical quality outcomes against other organizations. Just over a quarter (28%) said they measure labor and productivity against departments at other organizations.

The survey results indicate good coordination between finance and strategy departments at many organizations. Asked to rank how familiar their finance team is with metrics used by the organization's strategy team, 62% ranked as either familiar or extremely familiar, at 4 or 5 on a scale of 1–5.

95% use benchmarks

92% should do more to leverage data

How does your organization use external financial and operational benchmark data?



Most Organizations Leverage Data from a Variety of Sources

LEADERS' PERSPECTIVES

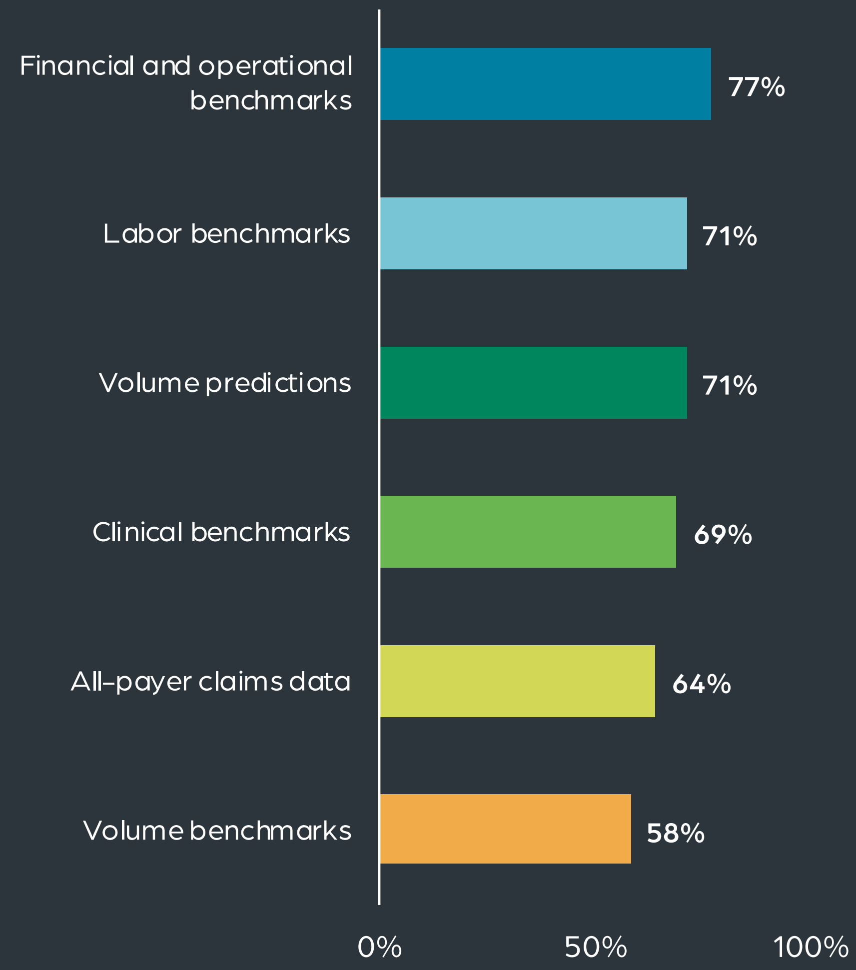
To drill in deeper on data usage at healthcare organizations, the survey asked about the types of data used to steer strategic and financial decisions. The results show more than half of organizations tap data from a variety of sources.

More than three-quarters of survey respondents (77%) said they use financial and operational benchmarks, while 71% use labor benchmarks and 71% use volume projections.

Many organizations also use a variety of data to drive strategic growth decisions, including:

- Procedure volumes (28%)
- Reimbursement rates (26%)
- Market data (26%)
- Claims data (21%)

What data sources does your organization use?



Organizations Use Service Line Planning to Target the Root Causes of Challenges

LEADERS' PERSPECTIVES

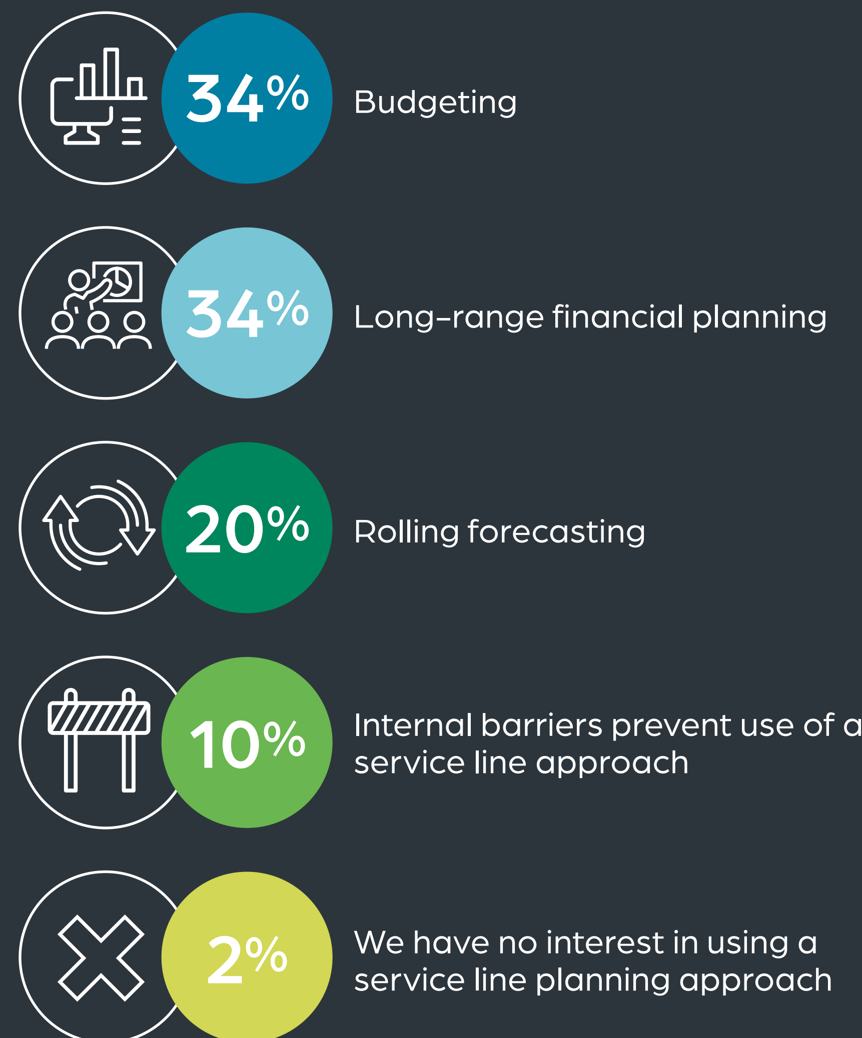
Integrating service line data into routine processes is a priority for many healthcare finance leaders as they seek to better pinpoint and address operational or cost challenges at their source. Forty-two percent of respondents said they currently use service line benchmarks, and 44% plan to implement them within the next 12 to 18 months. Forty-four percent said they currently use data on service line predictions, while 40% plan to implement them within the next 12 to 18 months.

How organizations use service line benchmarks and predictions also is increasing. More than a third of survey respondents (34%) said they incorporate a service line approach into both budgeting and long-range financial planning. Nearly 20% also integrate service line considerations in their rolling forecasting.

Of those who do not use any form of service line planning, more than 80% said they would be interested in implementing one if they could overcome internal barriers. Common barriers to service line planning noted by respondents include the effort involved in maintaining such an approach, an incompatible general ledger structure, and difficulty defining service lines.

Only 2% of healthcare finance leaders said they have no interest in pursuing a service line approach at their organizations.

What planning processes at your organization incorporate a service line approach?



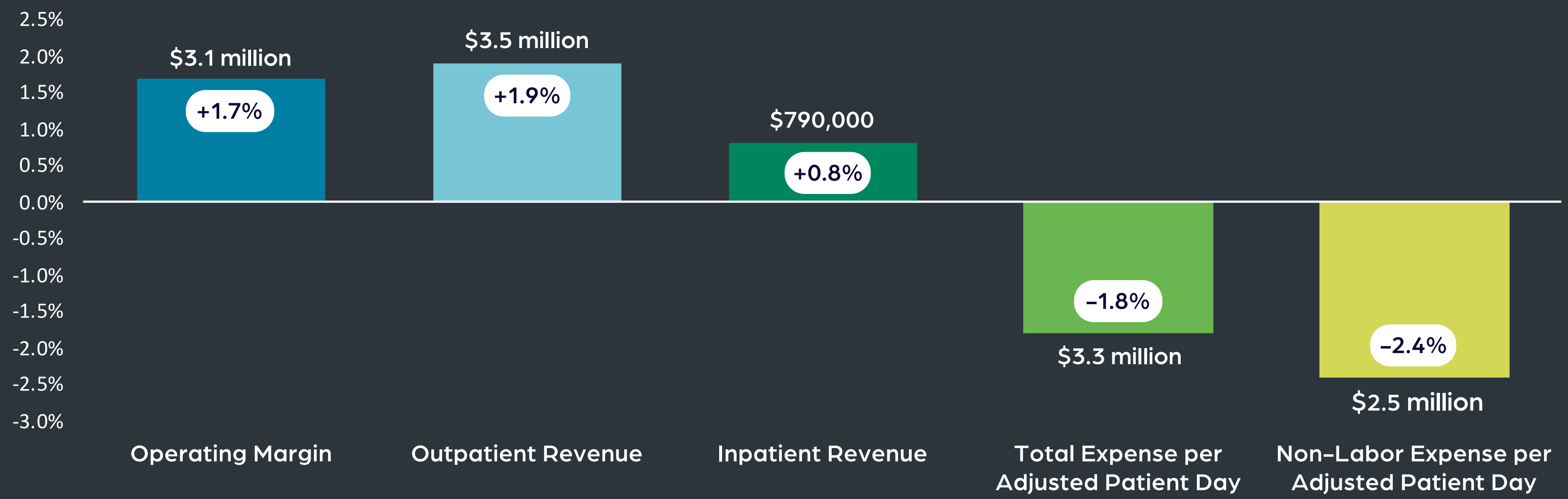
The Benefits of Optimizing Data for Your Organization

LEADERS' PERSPECTIVES

Leveraging data to guide strategic and financial decision-making provides tangible benefits. The following analysis solidifies this point. It found hospitals that used a comprehensive analytics and benchmarking system — Axiom™ Comparative Analytics — had better 2023 results across multiple key performance indicators relative to non-users. For example, Comparative Analytics users had 1.7% higher operating margins compared to non-users, which equated to $3.1 million more in margins for those organizations. Higher revenues contributed to the margin gains, with users seeing 1.9% or $3.5 million more in outpatient revenue and 0.8% or $790,000 more in inpatient revenue for the average hospital in 2023.

Comparative Analytics users also had lower expenses compared to non-users. Total expense per adjusted patient day was 1.8% lower while non-labor expense per adjusted patient day was 2.4% lower, which equated to savings of $3.3 million and $2.5 million for the average hospital, respectively.

2023 Performance for Comparative Analytics Users vs. Non-Users and Average Hospital Financial Impact



Source: Axiom™ Comparative Analytics

Note: Dollar values are based on an average 100-199 bed hospital.

Imperatives for 2024

Three Imperatives for 2024

As they look to the year ahead and beyond, healthcare leaders should think strategically about how their organizations can build on recent gains and navigate current and future challenges. Three imperatives drawn from the latest data and survey results include:

Manage margins with continuous monitoring. While many hospitals have seen margin improvements in recent months, healthcare leaders must remain diligent to help their organizations maintain the momentum. This requires rigorous and routine monitoring of the many factors that can influence margin performance, such as ongoing expense increases and shifts in patient demand. By tracking performance relative to internal and external financial and operational benchmarks, organizations can measure their performance relative to peers, proactively identify opportunities for improvement, and implement strategies to improve margins.

Leverage a service line approach. Integrating service line analytics into broader strategic and financial initiatives is becoming a business imperative for healthcare organizations. Leaders benefit from having insights into performance trends across clinical service lines to help inform both tactical and strategic planning decisions, including budgeting and long-range planning. By establishing cross-functional teams to interpret service line analytics, organizations are better equipped to identify which service lines are doing well and which are not, and evaluate the potential clinical and financial impacts associated with specific service line initiatives.

Improve reimbursements. Information is key to closing the gap between what healthcare organizations are reimbursed for care and the actual costs associated with providing that care. Rather than walking into payer negotiations blind, healthcare leaders need to come equipped with insights. Market-specific claims data can help them better prepare for critical contract negotiations by understanding where they stand relative to peers, including how their negotiated rates compare to other organizations in the same service area, and the broader healthcare market.

About the Data

This 2024 CFO Outlook for Healthcare report includes four sources of data:

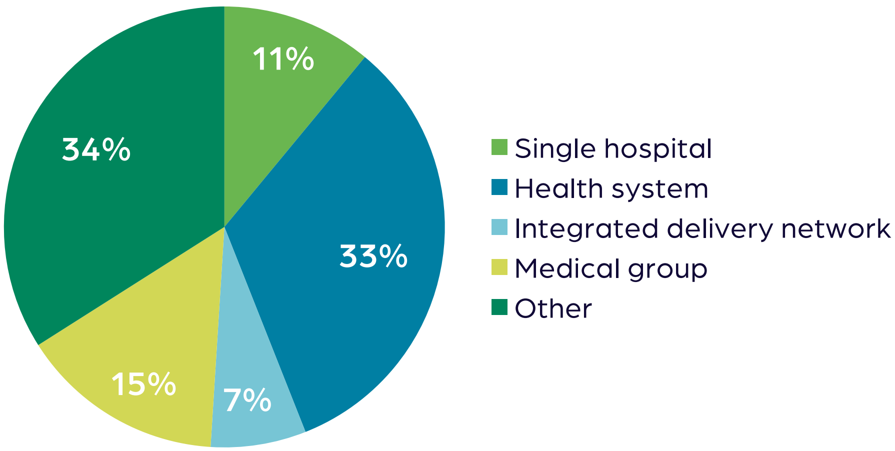
Our annual CFO Outlook survey of more than 100 U.S. healthcare finance professionals aimed at identifying trends, challenges, priorities, and process and technology changes occurring across the industry. Survey respondents represent a variety of healthcare organizations, including hospitals, health systems, integrated delivery networks, home health agencies, skilled nursing facilities, and others.

Axiom™ Comparative Analytics, which offers access to near real-time data drawn from more than 135,000 physicians from over 10,000 practices and 139 specialty categories, and from 500+ unique departments across more than 1,300 hospitals. Axiom Comparative Analytics also provides data and comparisons specific to a single organization for visibility into how their market is evolving. Read our *Monthly Healthcare Industry Financial Benchmarks* report for the latest information on hospital and physician performance data and trends.

Our StrataSphere® data draws from more than 115 health systems nationwide that have StrataJazz Decision Support. StrataSphere uses machine learning to leverage trillions of data points, providing accurate, actionable, and timely comparisons of key volume metrics. Read the monthly StrataSphere *National Patient and Procedure Volume Tracker™* for current volume data.

Strata's proprietary All-Payer Claims Database (APCD) encompasses more than 2 billion claims per year updated monthly from all sites of care, including hospitals, ambulatory surgery centers, physician offices, and urgent care centers. The APCD draws data from several claims clearinghouses to help healthcare leaders gain deeper insight to their market dynamics and better understand the continuum of care, including physician referrals and patient out-migration.

Survey respondents' type of organization



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