Hospital Liquidity in the COVID-19 Pandemic: Early Actions Are Critical to Financial Recovery

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Vast Upheaval to an Already Fragile Ecosystem

In less than 12 weeks, COVID-19 has disrupted life, perhaps more than any event in our generation. The nation's response is remarkable for its teamwork, compassion and commitment, especially the health care community, which despite dire shortages of resources has unified to deliver its critical services to meet unprecedented demand. The U.S. Congress has passed several legislative actions to support individuals, small businesses and health care organizations.

Unfortunately, hospital management teams may have a false sense of comfort by the increased patient census resulting from COVID-19, and the balance sheet boost from stimulus funding, including Medicare advances. However, with the increased costs of temporary staff, overtime and supplemental pay, additional personal protective equipment, and many other related costs either becoming due or now past due, the current levels of stimulus funding will not indefinitely cover the lost income and fixed costs of operatio*ns.*
Many hospitals, especially community and rural hospitals, have cut their elective procedures and bought supplies only to have empty beds and higher costs. Major hospital systems across the country, such as Detroit Medical Center, UK Healthcare (Lexington, Ky.)[1] and Dallas-based Steward Health,[2] have implemented cost-cutting measures that include furloughs, salary cuts and even hospital closures — all actions indicative of the severe and abrupt impact of the pandemic, regardless of geography.

Urban Hospitals Highly Impacted

While every health care organization's resources are stretched, nowhere is more challenged than urban safety net and community hospitals that serve a high proportion of economically and socially vulnerable patients who are contracting COVID-19, getting hospitalized and dying all at a higher rate than the general population. These hospitals, more than 1,300 nationwide already with often thin or negative financial operating margins, are now facing dire challenges as they compete for resources to manage the current surge of acutely ill COVID-19 patients. Moreover, any recovery will cost hospitals 90 days of cash on hand or more, often far greater than is available to vulnerable providers and further weighing on solvency concerns.

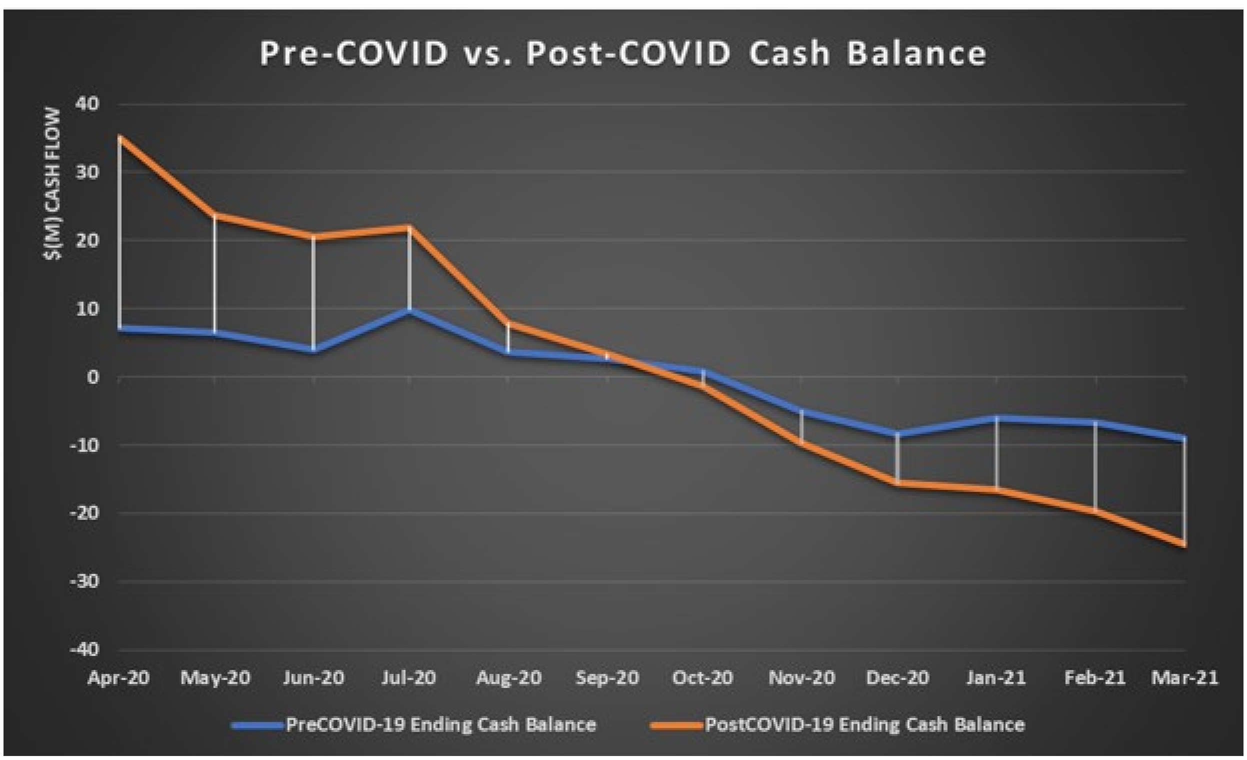
Evidence-Based Outlook

ToneyKorf Partners recently released the results of its analytical forecast on the impact of the COVID-19 pandemic, with a focus on community and urban safety-net hospitals. The Pandemic Impact Mitigation Strategy (PIMS) Model indicates that only immediate and aggressive actions, coupled with further levels of external funding or stimulus, can prevent a complete financial crisis for many health care organizations. The PIMS Model indicates that, while pre-COVID-19 financially vulnerable hospitals are now at risk of imminent insolvency, many hospitals previously considered stable will also face significant financial challenges due to the extended impact of lost elective case volume during and after this viral pandemic.

Data-Driven Approach

Utilizing predictive epidemiology to quantify the number of COVID-19 patients who will require hospital admission, coupled with indicators of future lost routine volumes, the PIMS Model forecasts the pandemic's impact on hospitals' and other providers' financial stability. Essential factors include surge capacity 'ramp up,' direct costs from COVID-19 patient care, and lost revenue from the disruption of elective health care services that converge to create, after the initial receipt of supplemental funds, a rapid decline in net cash flow absent additional government stimulus. As a result, this disruption, combined with lingering COVID-19 costs, will place many independent health care organizations on a course to insolvency, as shown in Diagram 1, unless transformation and restructuring actions begin immediately as COVID-19 hospitalizations subside.

Diagram 1: COVID-19 Impact on Hospital Financial Stability



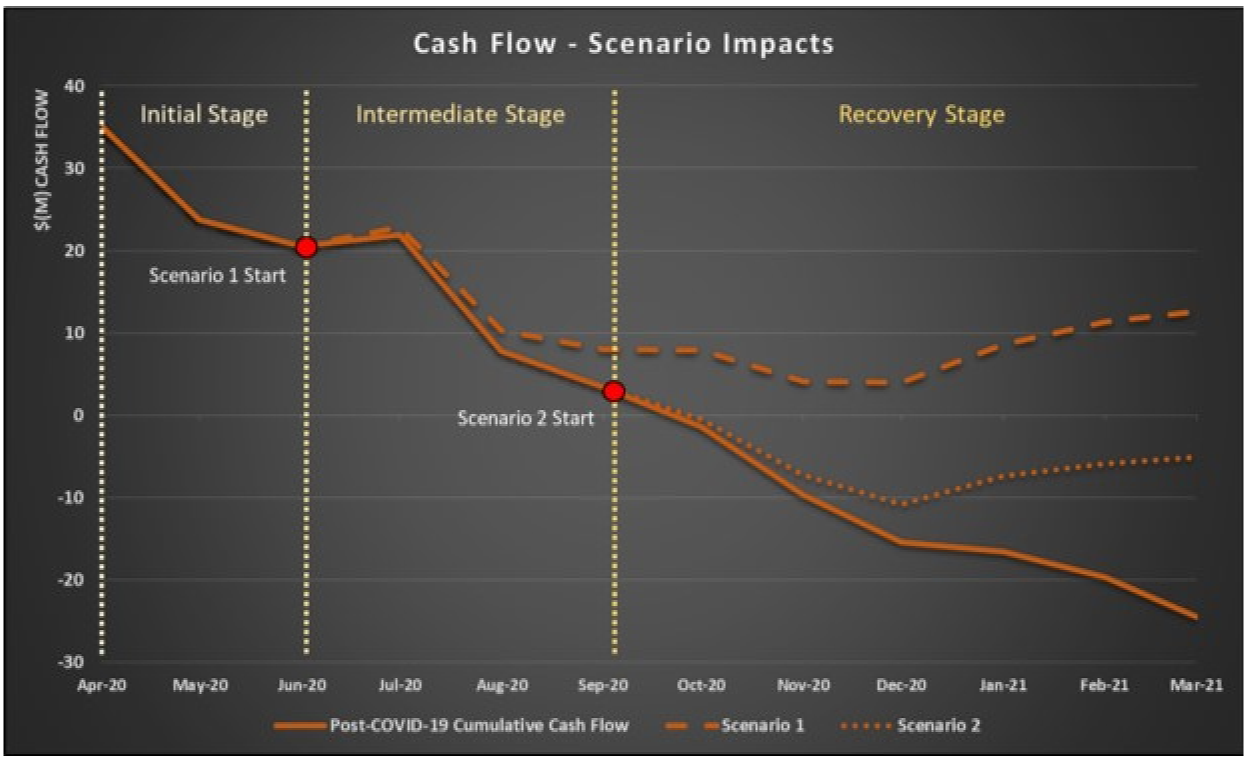
Key Stages of Impact

The PIMS Model identifies three distinct stages of financial impact:

1. **Initial Stage (Months 1-3),** beginning with the first COVID-19 infected patient in a community;
2. **Intermediate Stage (Months 3-5),** beginning when COVID-19 hospitalizations decline; and
3. **Recovery Stage (Month 6 and beyond),** beginning when COVID-19 hospitalizations are less than 10% of the average daily census (ADC).

Based on these stages, Diagram 2 demonstrates that specific, early actions taken during the Intermediate Stage (Scenario 1) may vastly improve the solvency outlook, whereas delayed actions, insufficient supplemental funding or a COVID-19 resurgence (Scenario 2) will gravely threaten the financial stability for many hospitals.

Diagram 2: Impact of Early Recovery Actions During COVID-19 Pandemic



Healthy or Distressed Facilities Are Both Highly Impacted by COVID-19

Regardless of the pre-COVID financial position of hospitals or health systems, the compounded losses from the extended course and net impact of this illness, including a potential COVID-19 resurgence later in 2020, will affect the financial stability of most providers. Stimulus funding to date, including Medicare advances that currently require repayment, are insufficient to make up for the likely post-COVID-19 inpatient and outpatient case volume lag and related revenue shortfalls as our PIMS Model predicts in the Intermediate Stage.

Key Takeaway

After the COVID-19 surge subsides, health care systems will need to pivot quickly toward meeting new variable patient demands for clinical services through a combination of alternative delivery, partnerships and capital structures better suited to a dramatically different economic and care-delivery environment. Regardless of the payer mix, every health care system will need to take dramatic and aggressive action to ensure ongoing viability. This pandemic will force changes to health care delivery: Some changes are needed and long overdue, some are painful but revitalizing to organizations, and some that we don't even know about today will be essential for future viability. All of these organizations must quickly 'up their games,' or face absolute failure.

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[1] Alia Paavola, "253 hospitals furloughing workers in response to COVID-19," Becker's Hospital CFO Report, April 7, 2020.

[2] "Easton Hospital owner to 'proceed immediately' on closure without state takeover by midnight," March 27, 2020, *available at* https://www.lehighvalleylive.com/coronavirus/2020/03/easton-hospital-own....