THE BOND BUYER

Hospitals report grim coronavirus fiscal toll for March

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Not-for-profit hospital operating margins plummeted in March as expenses mounted and revenue from elective procedures dried as facilities prepared for the onslaught of COVID-19, according to a report from Kaufman Hall.

The data from 800 hospitals offers a comprehensive national look at the initial toll of the coronavirus pandemic on hospital balance sheets.

The coronavirus pandemic has kept hospital staffs busy, but damaged the facilities' bottom lines because most have deferred lucrative elective procedures.

Bloomberg News

The report comes as Congress is poised to sign off on additional aid to nation's hospitals and some facilities begin to prepare for the resumption of elective surgeries and procedures following national guidance released over the weekend.

"Volume and revenue declines, along with flat to rising expenses, resulted in a dramatic fall in margin within a matter of weeks, plunging not-for-profit hospitals, which historically operate on thin margins, deep into the red," wrote James Blake, a managing director at the Illinois-based financial advisory firm.

Hospitals median operating earnings before interest, taxes, depreciation, and amortization fell more than 100% compared to the same period last year.

The mean EBITDA margin dropped 13percantage points relative to March 2019 from about 1% to negative 12%.

In March 2019, the year-over-year change was just 1%.

The numbers are expected to deteriorate further for April.

"For many hospitals, the volume and revenue impacts primarily hit the last two weeks of March — showing just how quickly the pandemic is upending the industry. The results will be even more dramatic in coming months, as hospitals experience the effects of COVID-19 over extended periods," Blake wrote.

March revenues were down 13% compared to the same period last year while expenses rose modestly as hospitals were partially on their own to purchase drugs, supplies, equipment and hire additional staff after some personnel were exposed to the virus.

The expense rate growth was only slightly up with total labor expense rising by 3% year-over-year and 4% month-over-month while non-labor expenses were up just 1% both year-over-year and month-over-month. But looking at the number in a comparative manner of expenses to discharge rates the percentage rose to 18% for labor and 19% for non-labor over the previous March.

The revenue losses in March stemmed from both the voluntary patient cancellation of services as fears of the virus grew and the sector-wide hold based on the federal government's recommendations to defer elective procedures and surgeries to ensure that hospitals could manage the expected surge COVID-19 cases. Nearly half of hospital beds remained empty to accommodate the surge with the median occupancy rate down to 53% from 65% the prior March.

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Bad debt and charity care rose 13% year-over-year but the report warns that that number “likely will accelerate in coming months as people lose coverage due to the economic slowdown” that has claimed jobs.

Facilities operating in the Northeast and Mid-Atlantic suffered the biggest blow with the median operating margin tumbling 167% compared to last year. The region as a whole has seen some of the highest concentrations of cases.

Hospitals, initially in triage mode, focused on liquidity, tapping or establishing new lines of credits and putting off capital expenses. Some have turned to employee furloughs and layoffs.

While the crisis is still on the rise in some regions, planning has also begun to restore elective procedures. Resuming surgeries and procedures will vary. Federal officials released guidance that paves the way for facilities less impacted by COVID-19 caseloads to begin providing some diagnostic and elective procedures and surgeries now on hold. Other facilities could also then phase in the procedures if certain precautions are followed and thresholds met.

In his press briefing Wednesday, California Gov. Gavin Newsom said the state's hospitals are now clear to resume many needed non-coronavirus procedures, such as cardiac surgeries.

Individual hospitals and systems are undertaking their own assessments and states may also have a say. A public perception hurdle remains as some patients might still avoid hospitals over fears of contracting the virus.

Planning is also recommended by sector participants on post-pandemic fiscal recovery measures that include undertaking modifications to budget forecasts, meeting demands for more timely data, strategizing on how to benefit from expected growth in telehealth and whether some procedures should lose the label of “elective.” Planning is also needed for a projected second wave of the virus.

“Volume and revenue declines, along with flat to rising expenses, resulted in a dramatic fall in margin within a matter of weeks," wrote Kaufman Hall's James Blake.

Hospitals received $100 billion in relief from the Coronavirus, Aid, and Economic Security ACT enacted March 27. Hospitals can also bolster liquidity through a measure that allows for the acceleration of six months worth of expected Medicare reimbursements.

Another $75 billion is earmarked to reimburse hospitals, systems, and providers for expenses and lost revenues in the new $500 billion relief package passed by the Senate Tuesday and expected to pass the House Thursday.

Hospitals with fewer than 500 employees should also be able to benefit from the $310 billion of forgivable loans included in the new legislation for the Paycheck Protection Program.

Ratings

The rating agencies hold a negative overview on the sector and some hospitals have already received credit warnings.

S&P Global Ratings this week moved the outlook to negative from stable on 39 lower rated hospitals “due to the heightened risks associated with the financial toll” of the pandemic and related recession and the view that the organizations have “less flexibility and are more susceptible to financial stress” that could drive a downgrade over the next year.

The rating agency moved another three ratings to stable from positive.

The health care organizations affected include those with speculative-grade ratings of BB-plus and lower or those entities whose unrestricted reserves are approximately 100 days cash on hand or less.

S&P excluded from the action not-for-profit health care issuers with speculative-grade ratings or limited unrestricted reserves that already had non-stable outlooks. That includes two organizations on CreditWatch with negative implications, 13 that already carry a negative outlook, and one on developing outlook with the upside tied solely to merger and acquisition activity.

S&P said as of Dec. 31, 14% of its rated stand-alone hospitals and 7% of rated health care systems carried negative outlooks while 7% and 3% of rated stand-alone hospitals and health care systems, respectively, carried positive outlooks.

“Most March financial statements are not available at this time, but we expect that the health care providers we rate will face an unprecedented level of operating stress and tightened liquidity, which will worsen the longer and deeper the pandemic endures,” S&P noted.

Moody’s earlier this month warned that the existing federal relief may be extraordinary but “it is unlikely to fully cover the material revenue decline facing hospitals as a result of the pandemic, and cash flow will likely be materially lower for the next several months. As such, our outlook for the sector remains negative.”

Moody’s has not yet weighed in on the impact of the pending package as the vote is not yet final.

Postponed services will likely reduce hospital revenue by 25%-40% per month on average and strain cash flow significantly, according to early anecdotal information and smaller hospitals are expected to struggle most acutely due to liquidity challenges compared to larger hospitals and systems with greater access to capital and credit, Moody's said.

Merger deferred

For two Midwest systems, the pandemic will delay their planned union. Michigan-based Beaumont Health and Ohio-based Summa Health announced their intent to form a $6.1 billion system in January.

Under the terms of the agreement, Summa's assets were to be combined with Beaumont's at the time of closing. Both systems are big players in their respective markets.

Beaumont is among Michigan's largest healthcare systems and includes eight hospitals and a total annual net patient revenue of $4.7 billion. It operates eight hospitals and has nearly 5,000 affiliated physicians, 38,000 employees and 3,500 volunteers. It carries single A level ratings on its $1.5 billion of debt.

Summa Health, which has total annual revenues of $1.4 billion and employs about 7,000 people, includes a network of four hospitals, community health centers, a health plan, a physician-hospital organization, and a multi-specialty physician organization. Summa's $350 million of debt carries a rating in the triple-B category.

Beaumont announced it was deferring the acquisition Tuesday along with plans to temporarily lay off 2,475 employees and permanently cut more than 400 positions due to COVID-19 driven strains.

Beaumont president and chief executive officer John Fox couldn't say how long the delay would last. The two systems decided it was an "unnecessary distraction" given their primary focus on the crisis.

"It's kind of like you had a plan to do something but the house is on fire so we are going to deal with the fire," Fox said during a virtual news conference.