KPMG Healthcare CFO Roundtable: 6th edition

September 2022

CFO agenda

In a challenging economic environment, the healthcare sector continues to struggle with staffing shortages and supply management issues. Challenges attracting talent, particularly among nurses and other support staff, are having a significant impact on healthcare organizations' ability to accommodate fluctuating patient volumes as well as plan for needed surgical and medical supplies.

At our 6th healthcare CFO roundtable, KPMG gathered leading healthcare CFOs to discuss the scope of these challenges, review the degree to which staffing issues are being exacerbated by the current economic environment, and pose some cost takeout and operational recommendations to help health systems ensure financial solvency in these challenging times.

Kenneth Kim, senior economist from KPMG Economics, gave an in-depth presentation to the group on the economic factors contributing to supply and labor shortages. The cost-takeout discussion comprised insights from Tom Griffin, KPMG healthcare supply chain leader, as well as Jamie Sanchez-Anderson and Bill Timmins, managing directors in KPMG C&O health and government practice

Economic impact

Kenneth Kim shared his insights on the impact of inflation on the healthcare industry and beyond. He went into detail on the impact of rising costs that include a six percent increase in medical supply prices, a 14-16 percent increase in drug prices, and a 10-12 percent increase in the cost of purchased services.

His guidance for healthcare CFOs struggling to deal with elevated supply costs included considering reshoring and nearshoring in response to rising manufacturing prices in China and Southeast Asia. "For many companies, sourcing supplies nearer to home may be a viable financial decision, as well as a way to circumvent some of the current supply chain disruptions and delays."

Acknowledging the strain of a potential recession on organizations across all sectors, he highlighted that there is "another R word" that CFOs should keep top of mind. "That is rollover risk," he said. "To rollover into new debt, healthcare organizations are facing much higher financing costs. The 10-year treasury yield is 3.96 percent, which is significantly higher than in January 2021 when it was just one percent. Healthcare organizations have to factor the 4x multiple on long-term interest rates into OpEx and other major purchases."

> **Supply expenses are the most significant stressor for the healthcare industry at present.**
>
> **– Participating CFO**

Lower labor availability, higher wages

Across sectors, the workforce participation rate has not returned to pre-pandemic levels, which is "being driven to a great extent by demographics, including the retirement of Baby Boomers, which total 70 million people out of a population of 330 million in the U.S.," said Kim. "There are also 2-4 million people suffering from long COVID, which is preventing their active reengagement with the workforce. Combined, these two factors will constrict the labor force going forward, whether we go into a recession or not."

Although there are some signals that inflation will start to abate as the Fed triggers a short-term recession, "healthcare continues to face tremendous pressure on wages that won't go away any time soon," said Kim. According to the Bureau of Labor Statistics, healthcare occupations – including nurse practitioners, physical therapists, and home personal care aides -- are supposed to be the fastest growing occupations between 2020 and 2030 due to the aging of the population. "However, the disconnect is that wage rates are low for some of these professions," Kim continued. "When individuals are hired, there will be pressure on wages as healthcare will be competing with other industries for a shrinking labor pool."

There was almost unanimous consensus among participating CFOs about the need to cut costs through automation and other strategies to offset supply and wage pressures. Following are some of their comments:

- "To counteract rising labor costs, we are looking for cost-cutting methods within the revenue cycle and focusing on faster issue resolution through more automated processes."
- "Shifting everything in the corporate area to be as lean and mean as possible will allow us to free up resources for patient care."
- "Matching demand signals with patients coming in will require basic blocking and tackling activities to help blunt the impact of inflation to the organization until better times are here."

> **We are expanding our work from home policy so we can increase our catchment area and access talent from a broader base.**
>
> **– Participating CFO**

Kim concluded by cautioning CFOs about the risk of attrition if an organization's values don't align with employee's views on issues like ESG and DEI. "When it comes to staffing, you have to take more of a holistic view," he said.

Cost takeout

Kim kicked off the discussion on cost takeout methods by stressing that healthcare organizations can overcome supply and labor challenges through digital transformation, workforce transformation, upskilling, and other ways to increase productivity. Specific insights and recommendations were then provided:

Supply chain

Tom Griffin, KPMG healthcare supply chain leader, talked about how hospitals are experiencing the sharp impact of inflation without the offset of the level of revenue they enjoyed in earlier years. "The cost of capital is coming back into the conversation," he said. "For a long time, cash was cheap. You could buy inventory and keep it on the shelf. Now, it is important to decide how much cash to lock up in supplies and for how long. Clearly organizations have to balance mitigating against supply disruption with the risk of hoarding."

> **Implants and devices that are more costly require a spend analysis to see where they are having the most acute impact on hospital margins.**
>
> **– Tom Griffin**
> KPMG healthcare supply chain leader

He stressed the benefits of looking closely at upstream partners, like manufacturers, distributors, and pharmaceutical companies. "These organizations are not experiencing margin restriction to the same degree as hospitals," Griffin said. "You have to compare margins and look at how they pull through. You'll want to share demand signals with partners to gain more visibility into when products and services are being consumed all the way to the point of care."

When conducting a spend analysis, Griffin cautions that external data sources and benchmarks may not always be relevant. When collaborating with partners, organizations should probe into how recent their data is, as well as the source. Such efforts should start as early as the contracting process.

One CFO spoke to this issue by sharing that his organization has had some protection because long-term contracts are in place. Another said that his organization is "putting pressure on vendors to be transparent on performance data," for example the numbers of backorders. "We are trying to create a competitive atmosphere, although this doesn't work with products where there are only a handful of suppliers."

On the issue of securing secondary and tertiary sources in targeted areas of the supply chain, another participating CFO said, "We've been very creative in leveraging temporary supply resources to protect us against disruption or excessive prices. But we might actually end up spending more."

Griffin concluded by saying, "For larger healthcare organizations, it may be worthwhile to have shared services capabilities through joint ventures with other health systems in the geography. But organizations should be careful to differentiate between when they need to have direct control and when a joint venture is warranted."

Patient management

Jamie Sanchez-Anderson, managing director, KPMG C&O health and government practice, continued a discussion on patient management that started at the fourth KPMG Healthcare CFO Roundtable.

She gave details of some newer innovations such as "tele-sitting" capabilities in hospital rooms that will allow nursing staff to be freed up as cameras and voice activation monitor patient health status. Another newer technique is using patient wearables to monitor vital signs while patients are moved within the hospital for testing, MRIs, and other procedures. Finally, she gave more details of the benefits of the medical home model, which can be used when capacity constraints are an issue. "This will allow organizations to focus on higher revenue-generating patients," she said.

Sanchez-Anderson continued her presentation by focusing on transformation of staffing and scheduling policies. "Current policies are driving excessive staff overtime," she said. "Organizations need to revisit their approaches by, for example, evaluating whether every staff member needs to be trained on particular technologies."

Other challenges she detailed included an aging workforce that might be interested in job sharing or shorter shifts as incentives to remain in the profession longer. "This doesn't just apply to older staff, however," she said. "The younger generations also want more flexibility. If healthcare organizations don't provide this, we expect to see fewer people choosing healthcare as a career."

How healthcare organizations place staff also requires a shift in mindset. "You need to look at seasonal fluctuations and holiday requirements and whether you are taking an equitable approach to which staff is assigned to less desirable shifts," she said. This also applies to assignments in high-pressure environments like the emergency department, trauma and burn units, and ICUs.

Regarding perennial issues like absenteeism and burnout, Sanchez-Anderson responded to CFOs' questions by recommending that, by moving from paper timecards to systems like Workday, organizations can not only better measure how often employees call in sick, but also realize up to a one to two percent cost savings.

> **Consider alternating staff shifts so responsibilities in high-stress environments are balanced by shifts in lower-pressure primary care.**
>
> **– Jamie Sanchez-Anderson**
> Managing Director, KPMG C&O health and government

Operational efficiencies

Bill Timmins, managing director, KPMG C&O health and government practice, turned the group's attention to operational transformation that can help healthcare organizations counteract rising labor and supply costs. He homed in on the depletion of pandemic relief funding, as well as the abatement of mergers and acquisitions activity among traditional healthcare organizations. These challenges fall against the backdrop of an influx of nontraditional players in healthcare, including among retail health organizations and other new entrants in primary care, including CVS's purchase of Signify Health as part of the organization's effort to move into home care.

"Organizations now need to make their margins through operational improvement," said Timmins. "One key trend is to move patients into outpatient settings, whenever possible."

Timmins echoed the plans of many of the CFOs on taking a back-to-basics approach to improving margins by, for example, managing patient throughput and associated supply costs more closely; taking advantage of economies of scale when feasible; reviewing supplier service level; and prioritizing long-term capital needs, such as those needed to deal with aging physical plants, ERP upgrades, and cutting-edge CRM systems.

When it comes to expense reduction, Timmins recommended that organizations focus on using enterprise asset management to track equipment lifecycles and spend. He also delved into analyzing workflows to minimize lease costs, leveraging automation for repeatable tasks, and exploring joint ventures and commercialization of capabilities, such as turning cost centers like the print shop or laundry into profit centers by selling those capabilities to other providers.

> **Tracking equipment lifecycles with enterprise asset management can result in the elimination of millions of dollars in costs.**
>
> **– Bill Timmins**
> Managing director, C&O health and government

Regarding joint ventures, one CFO in Texas shared the following: "In a hospital-dense geography like Texas, it made sense for us to create a new shared services physical plant where we can use cost allocation to help spread operating costs around."

Another CFO said his organization was focused on "length-of-stay management and introducing robotic process automation. "As a nonprofit, we are not a big fan of layoffs. However, we are using digital automation strategically to reduce the need for non-clinical labor. And, when it comes down to it, we are using organic attrition and turnover to right size the organization."

Procedure volumes and associated supplies

As mentioned earlier, many healthcare organizations have been struggling with managing volumes of elective procedures, many of which were put on hold at the height of the pandemic.

One midwestern CFO shared: "Our expense pressures are well understood, but there has been a lot of noise on the volume side. Historically, we have seen a strong secular growth trend. However, inherent demand is changing as one percent of the adult population in our county died of COVID. Although our pediatric hospital is overflowing, we no longer see the same growth in ambulatory services and downstream from there. The market is much softer, so we've had to look at RPA, offshoring of IT, transforming the revenue cycle, and other cost-cutting measures."

In contrast, a CFO from a hospital in a rapidly growing area of the South said that their "health systems are still recovering but are getting close to pre-COVID levels. We also see an influx of patients due to the demographics of our region."

Sanchez-Anderson spoke to this contrast by stressing that some organizations' utilization capacity is "through the roof" and that others are seeing growth in urgent care use, which often has capacity constraints. On the other hand, "organizations in other geographies are seeing depressed volumes, especially with elective procedures. In capacity constrained areas, many systems are pushing for longer patients stays and steering more people toward in-patient care." She cautioned, however, that

organizations "need to be careful about putting people in a level of care that isn't warranted because they will be turned down by health insurers."

One CFO in the Northeast shared that her systems' strategy for dealing with patient volumes is focused on optimizing physical space. "Our academic medical centers have more capacity challenges, while our community hospitals have more space," she said. "When appropriate, we are trying to transfer patients between centers to better optimize what we have."

Sanchez-Anderson spoke to this issue by suggesting that some organizations should consider putting centralized resource centers in place to help stabilize the patient transfer process. "In some cases, you may not have to use case managers or social workers for discharge," she said. "You can look at using lower-margin resources."

Real estate footprints

The peer exchange wrapped up with a discussion about health systems' real estate footprints, led by Ash Shehata, KPMG's national sector leader for healthcare and life sciences.

Several of the CFOs in attendance said they are considering downsizing their footprints and/or shifting to a sell/lease-back model. One CFO shared that "although his organization is creating a new cancer center, we had a developer build it because they thought they could do it for less than our facilities teams." He continued, "Since so many people are working remotely now, we are moving away from the ownership model, and we now lease 11 of our buildings. We are shedding as much physical space as possible and converting what we do have to clinical uses."

Another CFO said that his organization is "building an asset-allocation model due to their understanding of what is likely to happen over the long term. We may have to slow some things down. This isn't the first time we've been through a downturn like this."

Regarding the short- and longer-term stability of the markets, KPMG senior economist Kenneth Kim concluded the discussion by saying, "The early part of next year is when we expect the Fed to get to its terminal fund rate. Despite remaining challenges in the global economy, healthcare organizations should see some stabilization in the markets."

Topics for future sessions

The CFOs in attendance at the roundtable expressed interest in the following topics for future sessions:

- **Margin improvement**: As inflation and a potential recession remain in play, more sophisticated margin improvement strategies will be needed across the healthcare sector.
- **Volume management**: As we approach the third year of the pandemic and potential new COVID variants, the need to balance COVID care and elective procedures will likely persist.
- **Talent recruitment**: Health systems are interested in exploring recruitment strategies to help attract talent from outside of their geographic areas, including internationally.
- **Midterm elections**: By the time the next healthcare CFO peer exchange takes place in early 2023, the impact of changes in Congress on the markets and healthcare-related policies will likely require discussion.

> **In the current environment, developers may have excess capacity due to a slowing in commercial activity.**
>
> **– Ash Shehata**
> National Sector Leader,
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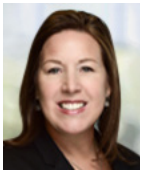

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