2020 Healthcare Financial Outlook:
Performance Management Trends and Priorities

By Jay Spence, David Palkoner and Kristopher Goetz
Summary of Key Findings

In Kaufman Hall’s annual survey of hospital and health system finance leaders on performance management trends and priorities, the following findings, organized within three categories of organizational need, were the most compelling:

### Identify and Manage Cost Reductions
- The need to identify and manage cost-reduction initiatives is a top priority for financial performance improvement activities.
- Finance leaders lack sufficient tools to identify cost-improvement opportunities.
- Few organizations have a cost accounting system in which leaders have a high degree of confidence.

### Become More Agile
- Many finance leaders lack confidence in their ability to adjust quickly and easily to changing business circumstances.
- Budgeting cycles continue to grow longer.
- Finance leaders show a heightened interest in improving operational budgeting and forecasting.
- Rolling forecasting is gaining in popularity as a complement to organizational budgeting cycles.

### Understand the Impact of Clinical Outcomes on Financial Performance
- Financial health and quality of care are the top core dimensions being managed by hospital and health system leaders.
- Few organizations are prepared to use clinical measures to impact financial results.
- Better analytics and reporting to support decision-making is a top priority for improvement.
Identify and Manage Costs

“The existing culture of not-for-profit healthcare tends to value incrementalism, avoid political sensitivities, and allow autonomy. The kind of radical shift in costs that will truly distinguish an organization requires a new mindset.”

The need for better cost identification and management has been a consistent theme since 2017, when we began our annual healthcare financial outlook survey. An important part of this effort is finding and realizing opportunities to **reduce** costs. More broadly, however, legacy hospital and health systems face the need to **transform** costs. Current service offerings must be delivered as efficiently as possible to preserve margins under tightening payment pressures; free up resources for investment in new technologies, sites of care and care delivery models; and address changing demand and new competition within the healthcare marketplace.

The need to identify and manage cost-reduction initiatives has been the top priority for healthcare finance leaders since the first year of our survey. However, a lack of sufficient tools – including cost accounting systems in which finance leaders have confidence – is hampering their ability to drive the transformative changes to cost structure required in today’s environment.

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https://www.kaufmanhall.com/ideas-resources/thoughts-ken-kaufman/getting-serious-about-costs
Identify and Manage Costs (cont.)

Finding: The need to identify and manage cost-reduction initiatives is a top priority for financial performance improvement activities.

87% of respondents say that identifying and managing cost-reduction initiatives is among the most important financial performance management activities for their organization.

76% say that resource constraints are affecting effective financial planning and analysis in their organization.

These two data points underline the need for cost transformation. High costs act as a drag on organizational efficiency, tying up resources that could be deployed elsewhere, including in analytical tools and costing systems that enable improved cost management. The imperative for cost reduction in existing services and operations is widely recognized. At the same time, finance leaders say that they do not have sufficient resources to effectively transform financial planning and analytical activities. Our survey results indicate that the problem of limited resources is growing: 76% cited resource constraints as an issue this year, compared to 70% in 2019 and 66% in 2018.

Top Three Priorities in 2020

1. Identifying and managing cost-reduction initiatives
2. Improved performance management and reporting to operational and C-suite leaders
3. Predicting and managing the impact of changing payment models

Our take: To counteract the impact of resource constraints, organizations must rely on technology solutions to help identify and manage cost-reduction initiatives.
Identify and Manage Costs (cont.)

Finding: Finance leaders lack sufficient tools to identify cost-improvement opportunities.

54% say they have insufficient data, benchmarking, and reporting tools to completely support efforts to lower costs without compromising the quality of care.

15% say they currently have no tools in place.

Demand for better value and price pressures on services are intensifying. Hospitals and health systems simply must find ways to improve their cost structures without compromising the quality of care or the patient experience. A healthcare organization’s ability to sustain high-value care delivery and ensure its long-term strategic financial viability increasingly depends on how effectively it can apply data analytics to inform improvement efforts.²

Data is everywhere in healthcare today, flowing in from claims systems, electronic health records, cost accounting systems, patient satisfaction surveys, wearable devices, patient portals, pharmacy refill systems, and many other sources. A lack of sufficient – or any – data, benchmarking, and reporting tools imposes a significant competitive disadvantage by restricting an organization’s ability to gain insights and inform decision-making by using the data available to it.

Our take: A lack of sufficient data, benchmarking, and reporting tools imposes a significant competitive disadvantage.

Identify and Manage Costs (cont.)

**Finding:** Few organizations have a cost accounting system in which leaders have a high degree of confidence.

Only 36% of respondents have a high degree of confidence in the accuracy of results from their existing cost accounting system.

In Kaufman Hall’s 2019 State of Healthcare Performance Improvement report, a refined and improved understanding of costs was identified as one of four key strategies hospitals and health systems should pursue.

The business case is clear. Inpatient volumes are declining. Growth is occurring outside the hospital’s walls, where legacy hospitals and health systems face the prospect of increased competition – in part on the basis of price – from new market entrants. These new competitors do not bear the burden of costs for providing acute inpatient care and have no interest in competing for inpatient business. Potential competitors such as CVS Health and Walmart have demonstrated their ability to hold down prices in competitive retail markets. Another competitive pressure comes from health plans, which are positioning themselves to be the organizers of healthcare networks and will use unit price as a key factor in selecting preferred network providers.

Effective competition in a new, retail-focused business model for the many healthcare services that are no longer delivered in an inpatient setting will depend on a more granular understanding of the actual costs required to offer a service. Health systems will need to know which services are truly margin positive and which are not as they make decisions on where they have a competitive advantage.³

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**Our take:** Effective competition in a new, retail-focused business model will depend on a more granular understanding of the actual costs required to offer a service.
Become More Agile

“As incumbents are often caught flat-footed when tech firms move into markets where nobody expected them.”

As noted in Kaufman Hall’s 2019 State of Consumerism in Healthcare Report, competition in healthcare is nothing new; however, the nature of that competition is changing. Hospitals and health systems today face new competitive threats from tech giants, industry behemoths, and innovative, targeted healthcare providers seeking to disintermediate legacy organizations from critical shares of their business. Sixty-seven percent of respondents to our consumerism survey saw UnitedHealth Group/Optum as a “strong” or “extreme” threat, and similar percentages saw the same threat level in CVS Health and Amazon.

The business climate can change abruptly when a disruptive new competitor enters a market. Agility is a critical attribute for legacy organizations that must address new competitive threats. While our survey findings show that finance leaders lack confidence in their ability to adjust quickly and easily to changing business circumstances, they also show a heightened interest in improved operational budgeting and forecasting and a growing trend toward rolling forecasting.

Perceptions of Potential Competitors

Question: Over the next five years, what degree of competitive threat do the following companies pose to hospitals and health systems?

<table>
<thead>
<tr>
<th>Company</th>
<th>Strong Threat</th>
<th>Extreme Threat</th>
</tr>
</thead>
<tbody>
<tr>
<td>UnitedHealth Group/Optum</td>
<td>26%</td>
<td></td>
</tr>
<tr>
<td>CVS Health/Aetna</td>
<td>21%</td>
<td></td>
</tr>
<tr>
<td>Amazon</td>
<td>10%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Kaufman Hall 2019 Healthcare Consumerism Survey

Become More Agile (cont.)

Finding: Many finance leaders lack confidence in their ability to adjust quickly and easily to changing business circumstances.

Only 24% of respondents are “very confident” in their team’s ability to quickly and easily make adjustments to strategies and plans if business circumstances change suddenly. This percentage has remained essentially unchanged for the past three years (23% in 2019 and 25% in 2018 were “very confident”).

Only 14% believe their current financial planning processes and tools make them “very prepared” to manage the financial impact of evolving payment and delivery models, again essentially unchanged since 2019 (13%) and 2018 (15%).

At a time when healthcare leaders warn of a “Category 5 disruption” headed for the U.S. healthcare system, the lack of confidence among healthcare finance professionals to adapt to changed business circumstances or new payment and delivery models gives cause for concern.

Our take: Healthcare finance professionals must have confidence in their ability to adapt to changed business circumstances in the face of industry disruption.

Become More Agile (cont.)

Finding: Budgeting cycles continue to grow longer.

50% of respondents report budgeting cycles lasting six months or more from initial roll-out to board presentation. This is up from 37% in 2019 and 27% in 2018.

Several factors could be attributed to the lengthening of budgeting cycles. As noted in last year’s report, management teams may be making new and tougher decisions that require more extensive analysis. This year’s survey drew a higher percentage of responses from large health systems (those with 10 or more hospitals) than prior surveys, and budgeting processes may take longer in more complex organizations. It is also possible that growth at the very high end of responses, with 16% reporting budgeting cycles of 12 months or more, reflects a “continual budget cycle” phenomenon: Organizations spend so much time preparing the budget that assumptions are outdated by the time the fiscal year begins, and the budget requires regular updates throughout the fiscal year.

Long annual budget cycles pose a problem for several reasons:

• Budget development is a highly time- and resource-intensive process.
• Initial assumptions will often be outdated by the time budgets are published.
• Budgets produce rigid and highly detailed plans that are not easily adapted to changing market conditions.
• Budgets drive management reporting in a retrospective direction, with a focus on variance explanation.

Despite evidence of lengthening budget cycles, however, there are several promising indicators in the survey findings, as described on the following pages.

Our take: Organizations should avoid spending so much time preparing the budget that assumptions are outdated by the time the fiscal year begins.

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Become More Agile (cont.)

**Finding:** Finance leaders show a heightened interest in improving operational budgeting and forecasting.

63% of respondents seek to improve operational budgeting and forecasting in 2020. This is up from 53% in 2019.

41% report using cloud-based applications for performance management, budgeting, and planning, up from 31% in 2019.

Plans to improve operational budgeting and forecasting were second only to plans to improve reporting and analysis to support decision-making (cited by 69% of respondents). This finding is a welcome counterweight to the finding of increased length in budgeting cycles, indicating recognition of the need to make budgeting and forecasting processes both more efficient and more valuable to the organization.

Also promising is the significant increase in the percentage of respondents who report using cloud-based applications for performance management, budgeting, and planning. Although some organizations are still relying primarily on spreadsheets (18% of this year’s respondents), cloud-based applications offer several advantages in terms of efficiency, security, reduced need for on-site IT support, and standardization to provide a single source of truth across the organization.

**Our take:** Improving operational budgeting and forecasting are positive counterweights to increased length in budgeting cycles.
Become More Agile (cont.)

Finding: Rolling forecasting is gaining in popularity as a complement to organizational budgeting cycles.

49% of respondents now use rolling forecasts as a complement to the annual budgeting process, up from 38% in 2019. Another 7% are using rolling forecasting as a replacement to the annual budgeting process.

Rolling forecasts are a key component in more agile planning processes. They enable organizations to:

- Identify and adjust to changes in the market
- Improve the timely allocation of resources
- Focus on a forward-looking view of organizational performance
- Have the visibility needed to improve and adjust strategy formulation and execution

Most organizations are using rolling forecasting as a complement to their annual budgeting process. This enables organizations to retain the value of target setting at the department and account levels, while adding the most current information to future-period projections. Organizations that have replaced their annual budgeting process with rolling forecasting can expect the need for fewer staff hours (rolling forecasting typically takes just two to three weeks per quarter) and longer-range visibility, extending three years or more (annual budgets forecast for the next 12 months only). In either case, rolling forecasting can be an effective approach to financial modeling and is flexible enough to meet varied organizational structures.7

Our take: Rolling forecasting is a flexible alternative to meet varied organizational structures as either a complement to or replacement of an annual budgeting process.

Understand the Impact of Clinical Outcomes on Financial Performance

“...[I]n an era of healthcare when no dimension of performance is more onerous than high cost, when many hospitals and clinicians complain that they are losing money ... as much as $800 billion in waste (give or take a few hundred billion) sits untapped as a reservoir for relief. Why?”  

These comments from Dr. Donald Berwick relate to a recent study updating estimates on the cost of waste in the U.S. healthcare system. Approximately $300 billion of this annual waste is attributed to failure of care delivery, failure of care coordination, and overtreatment. Yet even as healthcare finance leaders consistently acknowledge the potential for cost savings from reducing unwarranted clinical variations and making other changes to improve the efficiency of care processes, few acknowledge success in tackling this issue.

As the findings that follow describe, respondents to our survey are managing quality of care and clinical outcomes as core dimensions of performance. Yet few organizations are prepared to use clinical measures to impact financial performance. This inability to connect clinical and financial performance is leaving real dollars on the table, affecting not only the cost structure of hospitals and health systems but also the costs borne by those who pay for the care they provide.

Understand the Impact of Clinical Outcomes on Financial Performance (cont.)

**Finding:** Financial health and quality of care are the top core dimensions being managed by hospital and health system leaders.

85% of respondents are managing financial health and 80% are managing quality of care and clinical outcomes as core dimensions of organizational performance. These were the two most highly ranked options, followed closely by patient experience (76%) and operational efficiency (75%).

The tight cluster of top-ranked core dimensions – including financial health, quality of care, patient experience, and operational efficiency – indicates that most organizations understand the need to manage performance across multiple dimensions; ideally, the percentage of respondents who manage these dimensions should approach 100%. Quality of care and the patient experience will be increasingly important differentiators in a more consumer-focused, retail-oriented business model, and operational efficiency will be needed as legacy hospitals and health systems work to reduce costs and compete on price. Financial health is critical to maintain credit ratings, access capital, and have the resources necessary to invest in new strategic initiatives.

While the survey indicates that most organizations are appropriately focused on these critical core dimensions, less clear is the extent to which organizations are able to monitor performance across dimensions or have the right tools to gather insights for informed decision-making in these areas.

**Top Dimensions Managed for Organizational Performance**

<table>
<thead>
<tr>
<th>Dimension</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Financial health</td>
<td>85%</td>
</tr>
<tr>
<td>Quality of care/clinical outcomes</td>
<td>80%</td>
</tr>
<tr>
<td>Patient experience</td>
<td>76%</td>
</tr>
<tr>
<td>Operational efficiency</td>
<td>75%</td>
</tr>
<tr>
<td>Strategic growth</td>
<td>63%</td>
</tr>
<tr>
<td>Employee growth/retention</td>
<td>51%</td>
</tr>
</tbody>
</table>

Note: Respondents were asked to choose all that apply.

**Our take:** Organizations must manage performance across multiple dimensions, including financial health, quality of care, patient experience, and operational efficiency.
Finding: Few organizations are prepared to use clinical measures to impact financial results.

Only 14% of respondents are “very prepared” to use clinical measures to impact financial results.

This finding is consistent with the findings of Kaufman Hall’s 2019 State of Healthcare Performance Improvement report. While respondents to that report’s survey identified unwarranted clinical variation as an area of significant potential for their organization’s cost transformation efforts, only 14% said that their clinicians have access to actionable information that helps them address unwarranted clinical variation and other cost-related quality concerns. One of the report’s four recommendations for strategic focus was better engagement of clinicians with accurate and actionable data on quality and costs. As the report noted, “transformative change within a health system is simply not possible without clinicians engaged in the effort to enhance quality and lower costs.”

As noted above, hospitals and health systems must develop the capability to monitor performance across the multiple dimensions they manage. One of the most critical intersections is between clinical performance and financial performance. Organizations need a solution that offers robust analytics on quality metrics, combined with financial reporting capabilities that provide leaders with clear visibility into the bottom-line impacts of clinical variations and outcomes. They also need a solution that can serve as a single source of trusted information for clinicians and finance leaders alike.

69% of respondents are looking to improve reporting and analysis to support decision-making in 2020, the highest ranked option.

76% say healthcare expertise and best practices built into software is an important criterion when evaluating financial planning software, up from 60% last year and now the most highly ranked option (up from the fourth highest ranked option last year).

Finance leaders at most hospitals and health systems would readily admit that they are not taking full advantage of the data available to them. Consistent with prior years of this survey, 96% of this year’s respondents believe their organization should be doing more to leverage financial and operational data to inform strategic decisions. There is a significant gap, however, between the 96% who believe their organizations should be doing more and the 69% who are looking to improve reporting and analysis to support decision-making. Organizations that are not doing enough to leverage their data and are not seeking to improve their reporting and analytical capabilities to support decision-making risk limiting the insights available to their decision-makers and missing significant improvement opportunities.

Finding: Better analytics and reporting to support decision-making is a top priority for improvement.

A promising sign is the growing number of respondents who recognize the importance of software with built-in healthcare expertise and best practices. Healthcare is famous for its complexity. Finance leaders must have confidence that their software investment results in analytics informed by a deep knowledge of the healthcare industry, backed by implementation specialists and consultants with experience at top-tier hospitals and health systems.

Our take: Finance leaders must have confidence that their software investment results in analytics informed by a deep knowledge of the healthcare industry.

Top Priorities for Financial Planning and Analysis Improvement in 2020

1. Reporting and analysis to support decision-making
2. Operational budgeting and forecasting
3. Cost management and efficiency
Closing Observations

Healthcare finance leaders still lack confidence in their organization’s ability to adapt to a rapidly evolving business environment. Growing resource constraints are also a cause for concern, potentially hampering the ability of legacy hospitals and health systems to make the investments needed to compete effectively as the healthcare business model changes.

At the same time, significant improvements in several areas indicate an intent to make progress in performance management efforts. Interest in improving operational budgeting and forecasting is growing, as is adoption of rolling forecasting as a complement to annual budgeting cycles. Healthcare finance leaders are placing a higher priority on investing in software solutions with built-in healthcare expertise and best practices, recognizing the need for solutions that help navigate the complexities of the healthcare system.

The insights that come from improved data and analytics across the full breadth of dimensions that must be managed for effective performance improvement will be a critical component as healthcare finance leaders seek to help their organizations thrive in the years ahead.

Our take: Insights from improved data and analytics across multiple dimensions will be critical for successful performance improvement in the years ahead.
About the Report

The 2020 Healthcare Financial Outlook: Performance Management Trends and Priorities report presents results of an online survey completed in September and October 2019 by healthcare finance leaders at the nation’s hospitals, health systems, and other healthcare organizations. The goal of the survey is to identify the level of industry progress with performance management by gathering the insights of healthcare finance leaders responsible for this function. More than 120 individuals participated in this year’s survey.
About the Authors

Jay Spence is Vice President, Healthcare Performance Management Solutions, with Kaufman Hall Axiom Software. In that role, he focuses on shaping and executing the firm’s software strategy and product roadmap ensuring Kaufman Hall Axiom Software solutions for Budgeting, Rolling Forecasting, Performance Reporting, Capital Planning and Tracking, and Financial Planning continue to evolve to address the changing needs of healthcare organizations.

Mr. Spence has more than 25 years of experience working in the healthcare industry helping organizations leverage technology to improve their financial management capabilities. He joined Kaufman Hall in 2014 with the firm’s acquisition of Axiom EPM, where he served as Vice President of Healthcare Solutions since 2010.

Prior to Axiom EPM, Mr. Spence was a Senior Director for Healthcare Business Analytics at SAP Business Objects, supporting development of business intelligence, planning, and cost accounting solutions for healthcare organizations. He also previously provided consulting and implementation direction for decision support systems and served as Director in Finance at the Queen’s Medical Center in Honolulu.

Mr. Spence holds an M.B.A. from Hawaii Pacific University and a B.A. in Accounting from Babson College.

David Palkoner is Vice President for Kaufman Hall’s Healthcare Performance Improvement solutions. He is responsible for setting the product vision, strategy, and roadmap for the firm’s Cost Accounting, Decision Support, Contract Management, Strategy Management, Clinical Analytics, and Comparative Analytics solutions. Mr. Palkoner and his team also are responsible for product execution, working closely with development, operations, and support to create and implement market-leading solutions.

Mr. Palkoner has held leadership roles in healthcare IT product management for more than 22 years. Most recently, he was Vice President of Product Management at SA Ignite, creating Merit-Based Incentive Payment System (MIPS), Medicare Access and CHIP Reauthorization Act (MACRA), and value-based care contract optimization software. Mr. Palkoner previously was Vice President of Product Management at Aetna, where he set the vision, strategy, and product roadmaps for an entire portfolio of software and data solutions focused on electronic medical record interoperability and data exchange, physician workflow, referrals, orders and results, longitudinal patient records, and HL7 analytics.

His experience also includes serving as Director of Product Management at Truven Health Analytics, where he was responsible for the company’s healthcare strategic planning, customer relationship management marketing, and operational improvement solutions. During his tenure at Truven, Mr. Palkoner spent three years in Zurich, Switzerland, as a part of a Thomson Reuters Corporate program focused on the healthcare business. He began his career in hospital administration, working in Pediatrics at the Medical College of Virginia Hospitals in Richmond, and Baptist Medical Center in Jacksonville, Florida.

Mr. Palkoner received his M.H.A. from the Medical College of Virginia at Virginia Commonwealth University, and his B.S. in Media and Communications from the University of Illinois Urbana-Champaign.
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Kristopher Goetz is a Senior Vice President in Kaufman Hall’s Strategic and Financial Planning practice, concentrating on Performance Improvement. With significant expertise in hospital operations and financial management, he advises clients nationwide, including regional health systems, academic medical centers, community hospitals, and other healthcare providers.

Mr. Goetz’s experience includes leading hospitals through major cost-reduction initiatives while ensuring exceptional patient outcomes. With a particular focus on labor costs, he advises hospitals on the best way to improve efficiencies, reduce waste, and eliminate redundancies.

Prior to joining Kaufman Hall, Mr. Goetz held numerous leadership positions at Northwestern Memorial Hospital in Chicago, including Director of Operations, Manager of Performance and Innovation, and Process Improvement Leader. He also served as Interim Director of both the Emergency Department and the Neonatal Intensive Care Unit.

Mr. Goetz holds an M.A. in Clinical Psychology and a B.A. in Psychology from Eastern Illinois University.

About Kaufman Hall

Kaufman Hall provides a unique combination of software, management consulting, and data solutions to help society’s foundational institutions realize sustained success amid changing market conditions. Since 1985, Kaufman Hall has been a trusted advisor to boards and executive management teams, helping them incorporate proven methods, rigorous analytics, and industry-leading solutions into their strategic planning and financial management processes, with a focus on achieving their most challenging goals.

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Kaufman Hall software includes the Axiom Software Suite, providing sophisticated, flexible performance management solutions that empower finance professionals to analyze results, model the future, and optimize organizational decision-making. Solutions for long-range planning, budgeting and forecasting, performance reporting, capital planning, and cost accounting deliver decision support, reporting, and analytics within an integrated software platform. Kaufman Hall’s Clinical Analytics empower healthcare organizations with clinical benchmarks, data, and analytics to provide a higher quality of care for optimized performance and improved patient outcomes. www.kaufmanhall.com