

Hospitals' profit margin hits 6-year high in 2004

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USA TODAY

January 5, 2006

The nation's hospitals, boosted by a slowdown in expense growth and continued ability to drive a hard bargain with insurers, posted profit margins that reached a six-year high in 2004 — and indications are that 2005 was just as good.

The hospital industry is in the midst of its biggest construction boom in 50 years, spending nearly \$100 billion in inflation-adjusted dollars in the past five years for new and expanded facilities nationwide, often in rapidly growing suburban areas.

That spending comes as conditions have been good for both borrowing and spending. Hospitals reported an average 5.2% profit margin in 2004, the last full year of data available from the American Hospital Association.

In addition to strong bargaining power and slowing expenses, profits were also driven by investment income from an improving stock market, says the association's Rick Wade.

Even so, Wade says the good times are not shared by all.

"About 25% of hospitals are in the red," Wade says, down from about a third in the past few years.

The ongoing construction boom has not affected profits, Wade says, though once new facilities come on line, overall revenue might increase for the industry.

Similar results were reported by credit-tracking agency Moody's Investors Service, which follows more than 500 hospital systems.

Median operating margins, which don't include investment income, were 2% in 2004, according to Lisa Goldstein, a senior vice president at Moody's in New York. The median overall margin for the same year was 4.5%.

Those margins were the best she has seen since hospital profits stumbled after Congress passed the Balanced Budget Act of 1997, which reduced Medicare payment rates. Some of those Medicare cuts have since been restored.

Goldstein says hospital profits remained strong in 2005.

"We have about 100 audits in house for fiscal 2005," says Goldstein, "and the numbers are looking better: Margins are above 2004 levels."ns are

orthopedics and neurosurgery.

- Strong outpatient revenue.

- Costs for pension, malpractice insurance and other expenses coming under control.

The American Hospital Association reported that expenses increased 6.9% in 2004, compared with 8.1% in 2003.

Wade agreed that Medicare and private insurer payments were healthy during the past couple of years. But he has a less rosy outlook for 2005 and 2006.

State Medicaid payments are being cut, he says. That, coupled with natural disasters affecting hospitals in the South, "will have a dramatic effect on national margins."

Wade fears that Medicare payments in future years will also be affected as Congress faces growing deficits related to the war in Iraq, Hurricane Katrina and other issues.

"There will have to be a move for some kind of deficit reduction," says Wade. "We've been telling members that Balanced Budget Act 2 could be just around the corner."