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Hospital margins trend higher, but looming disruption demands strategic decisions

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The Buzz This Week

This month, Moody's credit rating agency released its annual not-for-profit and public healthcare median financial report for 2024, showing that overall hospital performance continues to improve. The median operating margin increased from 0.5% in 2023 to 1.5% in 2024.

Stronger patient volume drove improved revenues, along with one-time 340B settlements and higher state-directed payments. Median revenue growth reached 9.3%, outpacing growth in expenses for the first time since 2021 when pandemic relief funds buoyed hospitals' bottom lines. Performance improvements were the strongest among the 50 smallest hospitals in the Moody's report (which had a median of 260 maintained beds) as they managed expenses and drove operational improvements year over year.

Yet hospitals have not yet returned to pre-pandemic norms, despite ongoing improvements. This is largely a result of wage increases and supply cost inflation, including pharmaceuticals. While the median operating cash flow (OCF) margin improved from 5.3% in 2023 to 6.3%, many hospitals continue to fall short of the 8%–9% pre-pandemic OCF margin norms. Median expense growth of 7.3% was flat over 2023, but the rate was high compared with long-term averages.

The strongest utilization gains came from inpatient admissions. At 4.8% growth, this represented the highest increase since the pandemic. Outpatient care also increased, but at a lower rate. The growth rate in emergency department visits remained steady at 4%. Growth of outpatient surgeries at 2.7% was the lowest since 2020.

Academic medical centers (AMCs) saw stronger patient demand and higher acuity care compared to non-AMCs. Combined admissions and observation stays for AMCs grew by 16% from 2020 to 2024, compared with 2% for non-AMCs. This likely reflects AMCs' research capabilities, specialized and complex services, and demand for care by patients from outside their primary market areas.

While the median OCF margin rose in all regions, the South saw the largest increase—from 5.7% in 2023 to 7.8%. The South also led in revenue and patient volume increases, primarily from population growth and new supplemental funding programs, including state-directed payments.

OCF margins remained below the US median of 6.3% for hospitals in the West and Northeast, which have been impacted by labor challenges in recent years. Midwest hospitals tracked closest to the US median, with an OCF margin of 6.1%.

Why It Matters

Continued financial recovery following the COVID-19 pandemic comes at a time when hospitals face enormous operating pressures and their financial outlook is set to worsen from impacts of the One Big Beautiful Bill Act (OBBBA) and other policy changes.

Labor costs, which make up the largest portion of hospital and health system expenses at approximately 60%, have continued to increase. Salaries for registered nurses have risen 27% faster than the inflation rate in the past 4 years. While contract labor levels have declined from 2022 peaks, continued workforce shortages still necessitate significantly higher levels of contract labor than pre-pandemic.

Supply chain costs, including pharmaceuticals, are another major driver of hospital expenses. Drug expenses increased by 12% from March 2024 to March 2025, while supply expenses grew by 11%, and purchased services rose by 10%. Supply chain costs may grow further as the result of tariffs the Trump Administration enacted this month.

Meanwhile, an additional 14 million people could become uninsured by 2034, as a result of provisions in the OBBBA and expiration of the Affordable Care Act enhanced premium tax credits if Congress doesn't extend them past this year. Hospitals should start preparing for these coverage losses, for which preliminary estimates showed an increase in uncompensated care costs by more than \$280 billion over a 10-year period.

AMCs, which account for 29% of Medicaid inpatient days and 33% of uncompensated care costs, are facing unique challenges as they manage impacts from the OBBBA and respond to new challenges to research dollars, including the termination of more than 1,100 NIH grants to hospitals and medical schools.

Further compounding matters is a projected shortage of hospital beds as early as 2032. A confluence of factors will contribute to this shortage, including sustained high levels of patient volume since the pandemic, an aging population with complex medical needs, labor shortages, and hospital closures. Mitigating the potential crisis will require hospitals to forge even tighter operations or invest in new capacity during a time of reduced federal dollars.

While 2024 was a stronger year for financial performance, the coming economic headwinds mean that hospitals must begin preparing now to maintain positive margins. Immediate actions may involve identifying essential services, programs, education, and research on which to focus.

Executive teams will also want to consider opportunities for improvement, including leveraging technology such as generative artificial intelligence (AI), diversifying and augmenting revenue streams, and aligning through partnership for mutual benefit.

Despite continued financial recovery in 2024, maintaining positive margins in the coming years will demand forward-thinking strategies, adaptive leadership, and a focus on sustainable growth and resilience amid rapid change.

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