

VISION+VIABILITY

SOUND SOLUTIONS FOR HEALTH CARE ORGANIZATIONS

2007, Number 3

EMERGING STRATEGIC ISSUES FOR HOSPITALS AND HEALTH SYSTEMS

“CHANGE BRINGS OPPORTUNITIES. ON THE OTHER HAND, CHANGE CAN BE CONFUSING.”

—MICHAEL PORTER

Change is a byword in health-care. Hospitals and health systems are at once constantly on the alert for new trends, and at the same time, inured to change to the point of being blasé about emerging opportunities and threats. It is indeed confusing to sort out what truly merits strategic attention from the many small issues that nip at leadership’s heels.

DGA has identified three emerging issues that we believe demand real attention from hospitals and health systems at this time. While these do not encompass the full scope of strategic concerns, we believe these issues should be considered in strategic planning within the next few years:

ISSUE 1: CONSOLIDATION AROUND STRONG PLAYERS

The widely-discussed recent departures from the Health Alliance of Greater Cincinnati have raised the question of whether consolidation has reached its peak. We believe there are in fact new and continuing pressures for further consolidation of the hospital and health system market.

Hospital construction spending grew 15% last year, continuing the boom of the last several years. Though many believe the boom may be peaking, the resulting facilities have changed the competitive dynamics in many markets.

In some cases, new capacity has raised the stakes. Weaker players without the capital to upgrade are being squeezed out. Remaining healthcare organizations may have significant debt burdens, driving them to pursue merger and program consolidation options (among others) for filling their newly built or renovated facilities.

At the same time, payers are continuing to consolidate at a rate of approximately 30 managed care mergers or acquisitions annually.¹ This allows payers to continue to improve their negotiating leverage with health systems, and to achieve economies of scale. Providers may need to “counter-consolidate” even further to maintain a level playing field.

Another factor pushing for consolidation is the need for IT investment. Healthcare organizations are looking towards greater investment in electronic medical records and IT in general. This is driven in part by Medicare’s drive to value-based purchasing and quality reporting, which is already spreading to other payers. More sophisticated IT capabilities may be required to support evidence-based medicine and improved coordination of care. These IT costs are more easily borne by larger organizations.

As your organization looks at strategy, it will need to determine how these pressures are affecting your local market.

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1 Irving Levin Associates’ Merger and Acquisitions Data Base in Kaiser Family Foundation’s Trends and Indicators in the Changing Health Care Marketplace, 2006

PROFILE

JOHN M. HARRIS, PRINCIPAL

John Harris is a well-grounded strategist. He has founded a national healthcare information business, run facilities, and consulted to hospitals, PHOs, IPAs, and PACE programs. His clients get advice that will work.



“I want the client to achieve their vision,” says Harris. “We make sure their plans have a solid financial and market underpinning.”

John’s ability to facilitate planning retreats helps clients set new strategic directions. His financial acumen ensures that the strategies come to fruition. Whether he’s assisting with mergers, physician alignment or a new venture, John combines the touch of a facilitator with hard-nosed analytics.

Harris founded DocuBank, which has provided emergency access to advance medical directives for over 120,000 members. He has had senior operational responsibility in several health care facilities. John was a health policy fellow for the US Senate’s Finance Committee – Health Subcommittee.

Harris speaks nationally on clinical integration and IT strategies connecting physicians, hospitals and payers.

When not at work, John plays a number of sports just well enough to keep up with his three kids.

John holds a BA from Dartmouth College and an MBA in Health Care Management from The Wharton School of the University of Pennsylvania.

EMERGING STRATEGIC ISSUES*continued from front*

Do you need to take action to increase scale so that you can maintain a reasonable position vis a vis payers? If so, how can it be done in a way that will achieve other strategic goals such as access to capital, sophisticated IT, and/or improved clinical programs to fill new facilities?

ISSUE 2: THE PUSH TOWARD NEW FORMS OF PHYSICIAN-HOSPITAL INTEGRATION

Hospitals and health systems may be moving to tighten integration with physicians through greater use of an employment model and through technological integration, as well.

As we indicated in our last issue, as physicians adapt to Medicare and other reimbursement changes as well as mal-practice premium pressures, hospitals need to respond to physician adaptations (See *Vision + Viability*, 2007, no. 2). As hospitals see physicians competing for testing and treatment services, some hospitals are choosing to hire physicians who will not build competing services. Hospitals may also want more control of the care process as health care quality data holds them increasingly responsible for the quality of care resulting from physician decisions. Taken together, these forces will lead an increasing number of physicians to become hospital employees, with some markets experiencing significant changes.

Recent regulatory changes allowing hospitals to help fund EMR technology for physicians are also creating the potential for a new kind of bond between hospitals and non-employed physicians.

In developing strategy, your organization will need to consider the level of physician employment which will best meet its needs in your market context. You'll need to keep a close watch on competitors' physician strategies and

adjust your approaches in light of market changes. Any physician transactions will need to be structured and executed appropriately, with incentives to assure that physician performance meets hospital goals.

ISSUE 3: THE NEED TO RECONSIDER PRICING STRATEGY

Over the last several years, hospitals have leaned towards negotiating for higher margins on fast-growing outpatient services, and accepted minimal inpatient margins. However, new forces at work may require a re-examination of this strategy.

Until recently, health insurance coverage made consumers relatively insensitive to price. Low co-pays protected hospitals from the potential impact of price competition by physician-owned services, ambulatory surgery centers, and other low cost vendors. However, Consumer Directed Health Plans (CDHPs) and other high co-pay insurance policies could significantly increase price sensitivity in some markets. In addition, there is a general push for greater pricing transparency, with newspapers potentially comparing prices (not charges) if they are available, bringing further attention to higher hospital prices for outpatient care.

In the short term, the main impact of CDHPs and their high deductibles will be a longer payment cycle as providers must bill and collect significantly more funds directly from individual patients. In the longer term, where CDHPs achieve significant market penetration, they could open hospitals to increasing competition from lower-cost providers.

This means that for the first time in many years, pricing needs to be examined as a strategic consideration. You may need to explore the potential for negotiating margin on the inpatient side, where you face limited competition from non-hospital providers. ■

DGA NEWS

DGA has two new consultants! Aaron Dov Rosenstock, Senior Associate, joins us with experience in health-care consulting, research and financial management and an MHA from Cornell University. Molly M. Johnson, Associate, has worked in health care research management and holds an MHA from the University of Michigan.

ABOUT DGA PARTNERS

DGA Partners has been providing management consulting services to health care organizations since 1994.

Our services include:

- > Strategic and Business Planning
- > Financial Planning and Modeling
- > Facility Planning and Programming
- > Medical Staff Development and Compensation Planning
- > Care Management and Operations
- > Payer Contract Modeling and Support
- > Business Intelligence

DGA also provides expert opinion services that help hospitals and health systems handle the regulatory challenges associated with recruiting and compensating physicians. Services include physician community need assessments, physician compensation benchmarking, business valuations and litigation support.

DGA's seasoned professional team averages 20 years experience in health care consulting and operations. We have the knowledge, insight and skills to address your complex business problems.

Let's talk about how we can help your organization.

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