

## The COVID-19 Impact on Healthcare M&A

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The COVID-19 pandemic has upended our nation and our healthcare delivery system. The extreme pressure being put on hospitals during this crisis will permanently change the way healthcare is sought and provided. In addition to the sweeping changes we can expect in clinical standards and care delivery models, we will also see changes in how hospitals approach partnerships. Following are seven observations on the impact the pandemic will have on the healthcare merger and acquisition market:

- **We are entering a buyers' market.** Hospitals and health systems are experiencing financial strain during the pandemic. The loss of revenue from non-urgent procedures along with the increase in supply and workforce costs is dramatic. The burden is being felt most acutely by hospitals that were near or in financial distress pre-pandemic. Stressed hospitals are already seeking infusions of cash and other support to keep their doors open. In the aggregate, there will be more sellers than buyers in the market post-pandemic. As a result, sellers will need to be more flexible as the composition of transaction consideration will change. Hospitals that seek relationships with academic medical centers should also be aware of the anticipated

### Key Board Takeaways

- Hospitals' need for financial support and scale have been heightened as a result of the pandemic. Boards should evaluate partnership opportunities post-pandemic based on how well they would preserve their organization's sustainability and meet their new strategic imperatives. This is particularly germane given the expectation that employment levels in healthcare will continue to decline during the recovery.
- Certain and emerging competitors are experiencing growth and success in this crisis. Widespread adoption of telehealth and new reimbursement policies are here to stay and will further diminish utilization of hospital-based services. Hospitals should evaluate services that are at-risk for disruption by competitors and develop strategies to blunt their impact in order to remain relevant to their communities.
- The ability of hospitals and health systems to resume elective procedures is paramount to demonstrating organizational acumen. Providers that can get back up and running safely and quickly will be the most attractive partners. Organizations should consider employing multidisciplinary teams to develop and monitor recovery plans to ensure success.

consolidation in higher education, including medicine and the allied sciences, as partnerships are developed.

- **Priorities are shifting.** Hospitals that manage to maintain some degree of solvency may also have an increased appetite to pursue growth strategies. The pandemic response has underscored the need for the access to capital, supplies and equipment, and operational expertise that is often afforded to hospitals in health systems. As part of a system, a hospital may find itself better positioned to respond to their community's needs and more

resilient in a deep recession.

After experiencing a global pandemic, hospital boards may choose to prioritize operational and clinical effectiveness over independence, trading some of their "nimbleness" for stability.

- **Disruptors are taking center stage.** While hospitals are consumed by COVID response, existing and emerging competitors are growing rapidly. Private equity groups are investing heavily. Policies are being amended to incentivize telemedicine and the provision of complex procedures in ambulatory settings. When they emerge from the pandemic,

hospitals will be challenged by a more competitive environment. However, they may also find new opportunities to partner with disruptors.

- **In-market collaborations are permitted—for now.** Health systems are capitalizing on their scale by transferring patients, staff, and supplies between their hospitals. They are sharing institutional know-how amongst facilities to optimize care. Independent hospitals are coordinating with their in-market peers to achieve similar benefits; the FTC is not obstructing such relationships during the crisis. However, there is no indication that restrictions regarding business combinations involving the exchange of ownership will be similarly loosened. Hospitals that wish to continue relationships that were developed during the pandemic should carefully evaluate whether these would hold up under FTC scrutiny after the crisis.
- **Recovery planning is important.** Well-capitalized providers and new field hospitals are attracting frontline caregivers away from

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community facilities with above-market compensation. Retaining staff has proven difficult due to recruitment competition and burnout. It has also been exacerbated by the need of some hospitals to furlough staff. Taken together with the financial losses caused by the pandemic, resuming “business as usual” will be challenging. Buyers and sellers that are able to demonstrate the ability to ramp-up clinical services as soon as permissible will be attractive M&A partners.

- **Transactions are moving forward.** Transaction counsel and advisors have been able to support their hospital clients in advancing announced transactions during this time. While some health systems have hit pause on strategic initiatives during the pandemic response, business combinations are

expected to close as planned once recovery begins.

- **Strategic discussions are ongoing.** Development teams at large non-profit and investor-owned health systems are continuing to look for opportunities. Some prudent health system leaders are laying the necessary groundwork now to consider exploring partnerships when the pandemic ebbs.

Boards of directors should be preparing for the likelihood that the financial shocks hitting hospitals and physician practices could lead to a wave of consolidation. Amongst the many governance implications of the pandemic, the following bear particular consideration:

- *Timing* is likely to become critical in considering the initiation of partnerships. There are likely to be more “sellers” than “buyers” post-crisis. As a result, boards should consider strategies that contemplate approaching potential partners sooner rather than later.
- *Tactical approaches* to partnerships, similarly, might need to change. It is likely that traditional bilateral discussions will need to rapidly evolve to more overt and well-designed processes.
- *Board goals* strongly favoring independence should be reconsidered in light of financial exigencies and heightened need for clinical and operational effectiveness.
- *Structures* being utilized for increased relationship-building between hospitals during the crisis may not be sufficiently stable to survive the coming

### Considerations for Public Hospitals

Local government budgets are being stressed by the pandemic with less tax revenue coming in and growing response expenditures. Counties and other government entities may be faced with difficult decisions regarding budget cuts. As a result, public hospitals may not be able to rely on the same level of financial support from local governments in the next fiscal year. In preparation, public hospital leaders should outline an alternative budget that does not contemplate public funds.

Either because of financial need or prudent foresight, government officials may find the pandemic recovery period an opportune time to explore the transition of a public hospital to an independent non-profit entity. Public hospitals with a dual-board model should encourage hospital directors and elected officials to cooperate with a single vision on any initiatives that would affect the governance structure or ownership of the hospital. Alternatively, for those public hospitals that operate most efficiently, the pandemic may present an opportunity to grow by absorbing struggling private hospitals into their systems.

recession in healthcare. These phenomena need to be reconsidered. Deliberation should be given to alternative structures for many of these interim affiliations.

Hospital executives and boards of directors are not alone in grappling with the ramifications that the pandemic will have on their organization's future. These challenges cross industries and geopolitical borders. The dynamics of our nation's health system have changed indelibly. The coming months will provide even more clarity on how hospitals will emerge from this crisis and what partnerships are established as a result.

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