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Portfolio Optimization Strategies to Build Resiliency

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This article is the third in a series on resiliency through our regular collaboration with Kaufman Hall.

The COVID-19 pandemic may prove to be an inflection point for many hospitals and health systems. The pandemic has again demonstrated how essential healthcare organizations are to the communities they serve, but it has also highlighted the vulnerabilities of these organizations to sudden shifts in demand, volume-driven payment models, and a weakened economy.

Building resiliency positions an organization to weather the three stages of dislocation: the shock of initial crisis, the fight for stabilization, and the transition to normalization. Most hospitals and health systems are still in the fight for stabilization and will be until the pandemic is brought under control. These organizations must maintain a laser focus on building the framework needed to assemble, organize, and guide the coordinated deployment of all available resources.

Resiliency is not automatic; it is created through disciplined and strategic resource allocation, which focuses on the accumulation and deployment of resources in accordance with an enterprise-appropriate balance between three competing priorities:

1. Advancing the long-term mission and strategy of the enterprise
2. Addressing potential threats to enterprise operating or strategic viability
3. Pursuing financial return

In an environment where there are so many constraints on precious little bandwidth, these priorities can help clarify the organization's core business functions—both in the current environment and in the organization's forward-looking strategy—and how the resources devoted to non-core services and initiatives might be better utilized in support of the core business. It is important to note that "non-core" does not mean that services are not critical to the delivery of care, but rather that the health system may not be best suited to own or operate these services. Valuable time and resources should be focused on the health system's areas of expertise and areas critical to its mission.

As detailed below, the process of portfolio assessment and optimization requires governance and leadership to consider both vertical and horizontal perspectives on service line performance, organizational stability, mission, and strategic alignment. It also presents a range of possible actions—from monetization to partnership to additional investment—for portfolio optimization. Most of all, this process requires a thoughtful assessment and careful alignment of an organization's capabilities, market environment, and possibilities for future growth with its portfolio of services and initiatives.

→ Key Board Takeaways
Portfolio Assessment Questions for Governance and Leadership

Organizational leaders will want to refine the basic framework for portfolio assessment shown in **Exhibit 1** and determine priorities for action by asking additional questions specific to their capabilities and market position. Examples include:

- What do we do well and what do we not do so well?
- Are there services where we underperform but that are nonetheless critical to our mission as a not-for-profit healthcare organization?
- Are any of the services we offer becoming commoditized, limiting our ability to distinguish ourselves from other competitors?
- Do we want to completely exit a low-performing service line or maintain some level of ownership interest in anticipation of future growth or for other governance reasons?
- To what extent do low-performing services represent areas of "trapped capital" that could be better deployed elsewhere in the organization?
- How do various service areas create ongoing performance risk, capital claims, or other types of drag on available enterprise resources?

Assessing the Portfolio

A focus on resiliency requires blending vertical and horizontal perspectives on components of the organization's portfolio of clinical services and strategic initiatives. At the most basic level, a vertical perspective assesses performance: Is the service or initiative producing or expected to produce a high level of returns? A horizonal perspective brings other considerations into play in order to understand how the service or initiative contributes to or uses enterprise risk capacity: Does the service or initiative support other critical components of the portfolio? Could it provide revenue diversification opportunities to offset potential decline in other legacy services? Is its core performance material and variable and does it require significant capital investment?

As shown in **Exhibit 1**, a blended portfolio assessment that looks at both current and expected future performance (vertical perspective) and alignment with other

Exhibit 1: A Blended Portfolio Assessment

Source: Kaufman, Hall & Associates, LLC

organizational strategies (horizontal perspective) can help categorize portfolio components into potential actions. These include monetizing or exiting a service line, enhancing a high-performing service line's growth potential, repositioning an underperforming service to capture future growth, or maintaining the status quo in still successful legacy services.

Portfolio assessment should be treated as a dynamic process, revisited on an annual basis to determine whether service lines have moved within the assessment framework. For example, legacy services that perform well currently and in the near term should be monitored for signs of deteriorating performance, which might trigger a decision to exit or reduce investment in the business, while lower-performing service lines with strong strategic relevance should be monitored for signs that growth is taking off, or is not emerging as planned.

Determining the Best Course of Action for Portfolio Optimization

Most organizational leaders will find that the most difficult decisions on a course of action lie at the dividing line between "monetize or exit" and "reposition." A decision to sell or exit a service line can mean the loss of already invested resources and of future growth potential; at the same time, keeping a lower-performing line running exposes the organization to the opportunity cost of trapped capital or poorly utilized risk capacity, especially against what ultimately may prove to be a failed venture.

Home health and hospice care service lines are good examples of an area that is being assessed for potential partnership by an increasing number of hospitals and health systems. These services are strategically important to the continuum of care, but many health systems struggle with the cost structure of this business unit and compete against experienced, specialized providers that have often proved more adept at managing performance and costs in an area that is their core competency.

Recent transactions in this area reflect a range of possible approaches:

- **Monetize or exit:** An academic medical center, for example, may determine that home health and hospice services are outside its core focus on specialty acute-care services and sell its services to a specialized home health or hospice provider. For example, in 2019, Northwestern Memorial HealthCare sold its home health and hospice services to JourneyCare.[1]

- **Reposition:** Community hospitals may determine that home care services are central to their mission to serve their communities, and to future growth, but also realize that they lack the expertise to offer these services competitively. In these cases, a joint venture with a skilled operator that also enables the hospital to retain ownership control and realize future growth opportunities might be the best course of action. Examples include the almost 400 joint ventures LHC Group has formed with community hospitals.[2]
- **Enhance position:** An integrated delivery system that offers a high-performing Medicare Advantage plan may find that investment in a new partnership venture to provide an expanded suite of senior-focused services further expands enrollment and provides an effective means of managing the health and associated healthcare costs of its covered population. An example is Intermountain Health's creation of Homespire, a holistic home care joint venture with Lifesprk.[3]

These examples demonstrate how specific capabilities, strategic focus, and market environment will inform decision-making processes. In all cases, decisions should also be made within the context of the organization's enterprise-wide resource needs. For example, could the resources dedicated to an underperforming business line be better allocated within the enterprise, whether to support another business line, strengthen the organization's balance sheet and credit position, or add to the funds available for higher-return investments? Would an exit from certain services impair the performance of any remaining services or the long-term position of the organization in its market? Could "trapped" capital be better deployed to other areas? This connection to a well-defined resource allocation construct closes the loop and supports resiliency.

1 Jim Parker, "JourneyCare Acquires Northwestern Memorial Home Health & Hospice Assets," *Hospice News*, June 3, 2019.
2 Robert Holly, "LHC Group, Christus Health Expand Joint Venture Partnership," *Home Health Care News*, October 15, 2020.
3 Maria Castellucci, "Intermountain Partners with Lifesprk to Improve Senior Care," *Modern Healthcare*, May 8, 2018.

By balancing the perspectives derived both from current performance of individual service lines and from the mission, strategic vision, and resource needs of the organization as a whole, governance and leadership can help ensure that the decisions they make are building a resilient organization and fulfilling their fiduciary duty to the organization and community they serve.

The Governance Institute thanks Courtney Midanek, a Managing Director at Kaufman, Hall & Associates, LLC, for contributing this article. She can be reached at cmidanek@kaufmanhall.com.