

Examining the Circumstances that Allow Select Independent Hospitals to Thrive: Do you have what it takes?

The Chartis Group
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Introductions



**Sue
Anderson**

- 20+ years of healthcare management consulting experience advising hospitals, health systems, academic health systems, and physician practices
- Specializes in partnership development, strategic planning, service line strategic planning, hospital/physician alignment, and programmatic development



**Christopher
Regan**

- 35-years of experience in the healthcare field, having led over 150 engagements for provider, payer, and health sciences clients nationally.
- A Chartis founder, leader in the firm's strategy practice and national leader of its partnerships practice

Agenda & Discussion

01

Partnership / M&A Trends
Overview and Implications
for Independent Hospitals

02

Characteristics of Successful
Independent Hospitals

03

Alternative Partnership
Opportunities

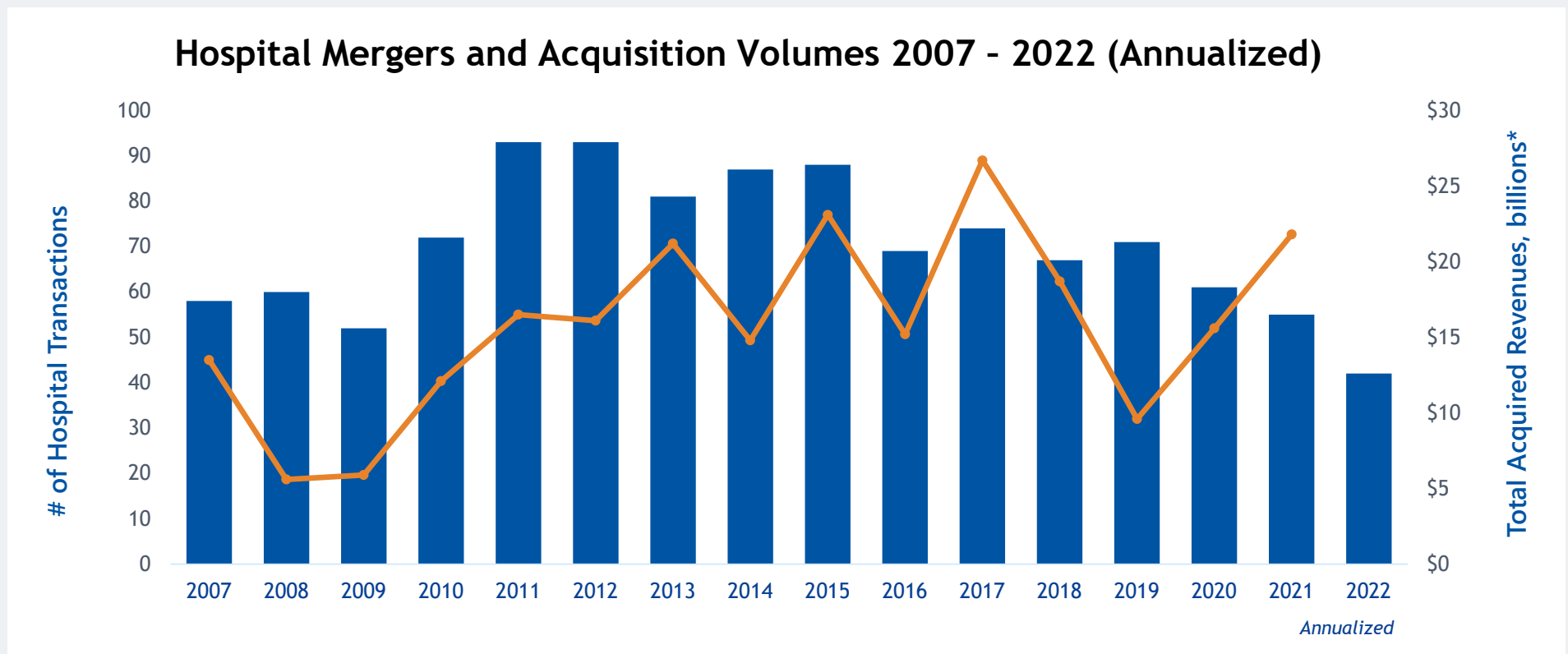
Partnership / M&A Trend Overview and Implications for Independent Hospitals



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Nationally, hospitals have been consolidating to create scale and realize strategic and financial benefits.

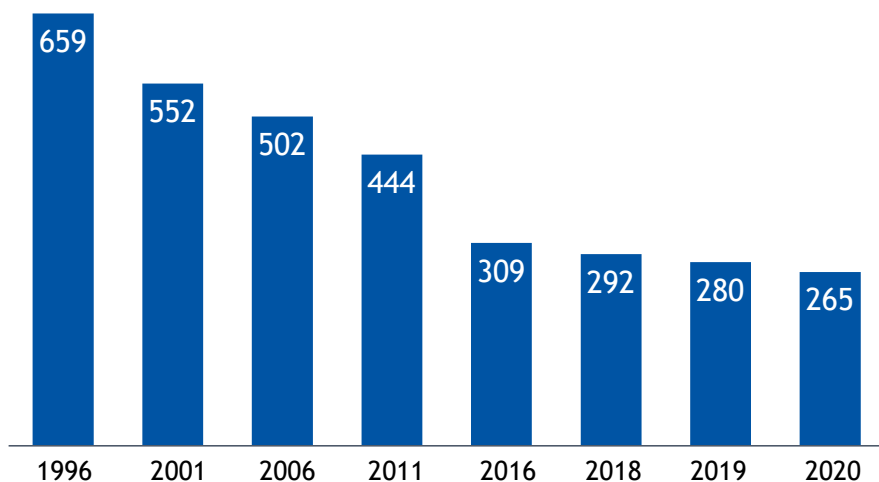


Sources: American Hospital Association (left); Irving Levin Associates, Inc., *Health Care Services Acquisition Reports* *Based on data availability: 91% of deals represented for 2007, 72% for 2012 - per Irving Levin Associates' note, \$ values are likely understated in recent years because transaction details are not publicly available for all deals. 2022 total acquired revenues not yet disclosed.

The number of independent hospitals continues to dwindle. Today, ~70% of hospitals are affiliated with a health system.

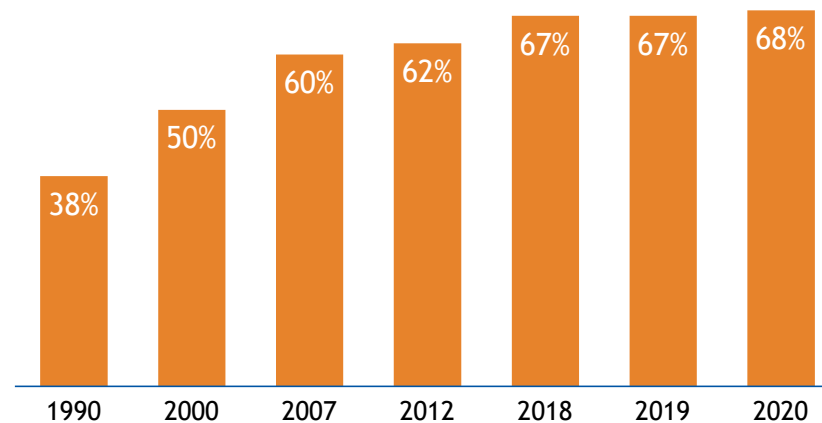
The number of independent hospitals continues to decline...

Number of Independent Hospitals with greater than 200 beds, 1996-2020



...as more hospitals increasingly affiliate with regional and national systems.

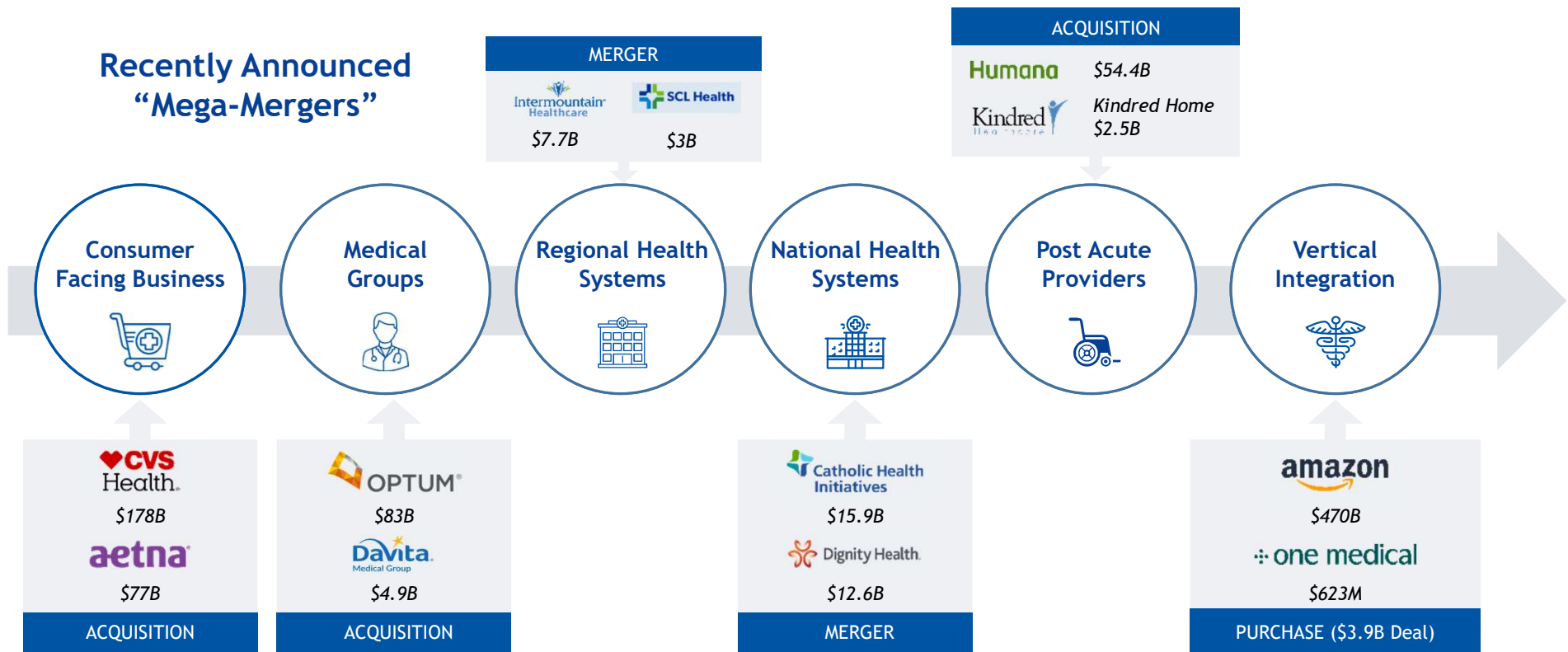
% of Hospitals Affiliated with Systems 1990-2020



Notes: *Free-standing hospitals, single-state and multistate healthcare systems.

Source: AHA Hospital Statistics 1998 – 2022 Report and Fast-Facts (2022 survey data reports on 2020 actuals)

2021 was coined “Year of the Mega Merger.” The value of the average transaction exceeded that of prior years. The trend continues in 2022.



COVID and increased scrutiny from the FTC have had a dampening affect on the number of transactions.

WSJ Wall Street Journal

Biden Competition Order Targets Hospital Mergers, Surprise Medical Bills

AHA among groups arguing stricter merger laws may cause lasting damage

Alia Paavola - 17 hours ago Print | Email

New Hampshire Bulletin
Dartmouth Health, GraniteOne Health abandon merger plans following objections from AG

BY: ANNMARIE TIMMINS - MAY 13, 2022 12:49 PM



FEDERAL TRADE COMMISSION
PROTECTING AMERICA'S CONSUMERS
FTC and Commonwealth of Pennsylvania Challenge Proposed Merger of Two Major Philadelphia-area Hospital Systems

HEALTHCARE FINANCE

JUN 03 | MORE ON MERGERS & ACQUISITIONS

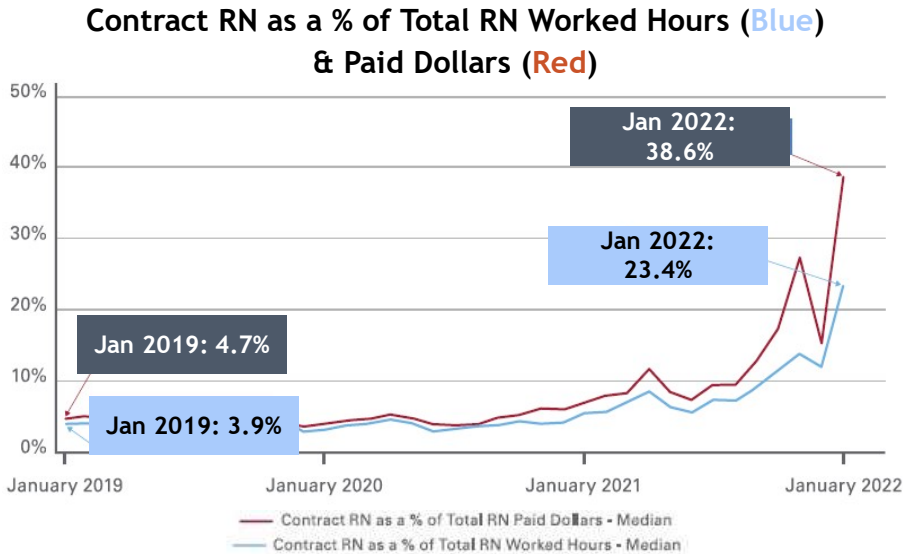
FTC sues to block merger between RWJBarnabas Health and Saint Peter's Healthcare System



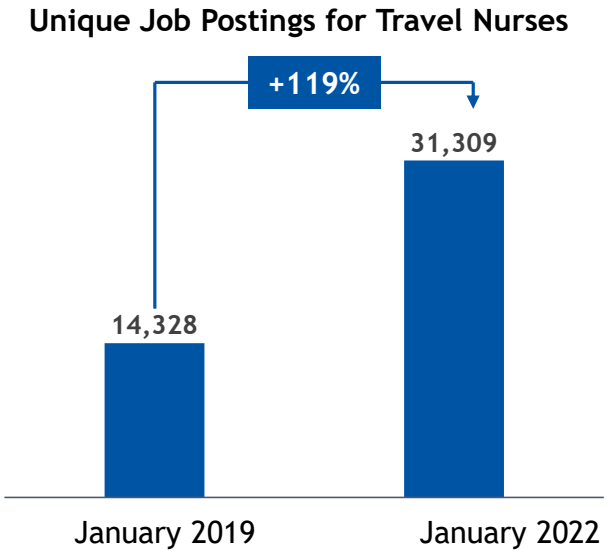
FEDERAL TRADE COMMISSION
PROTECTING AMERICA'S CONSUMERS
FTC Challenges Hackensack Meridian Health, Inc.'s Proposed Acquisition of Competitor Englewood Healthcare Foundation

Today's healthcare workforce is highly volatile; hospitals are using increased contract labor and raising salaries to retain top talent.

Additional measures are necessary to support remaining staff, and ensure they have adequate resources for their daily jobs and mental health.

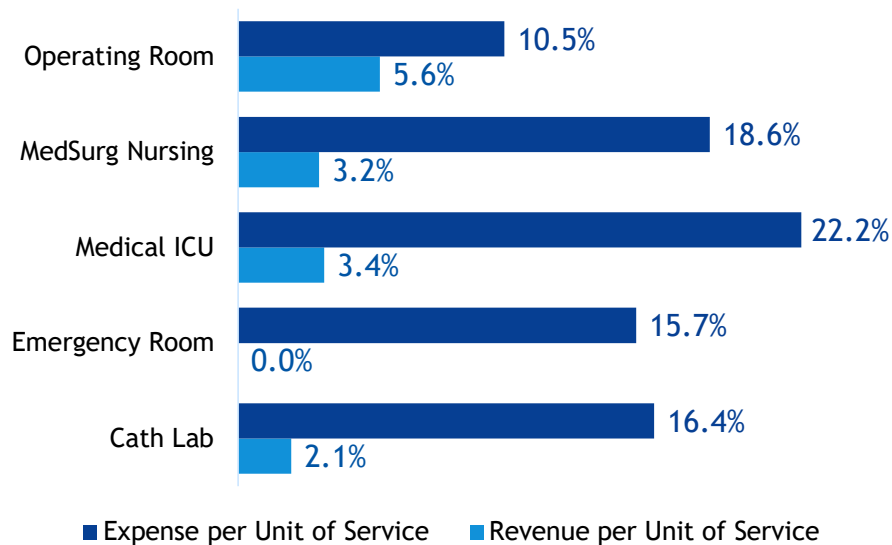


As turnover increases, remaining staff face added stress and greater workloads, intensifying existing exhaustion from managing through the pandemic.

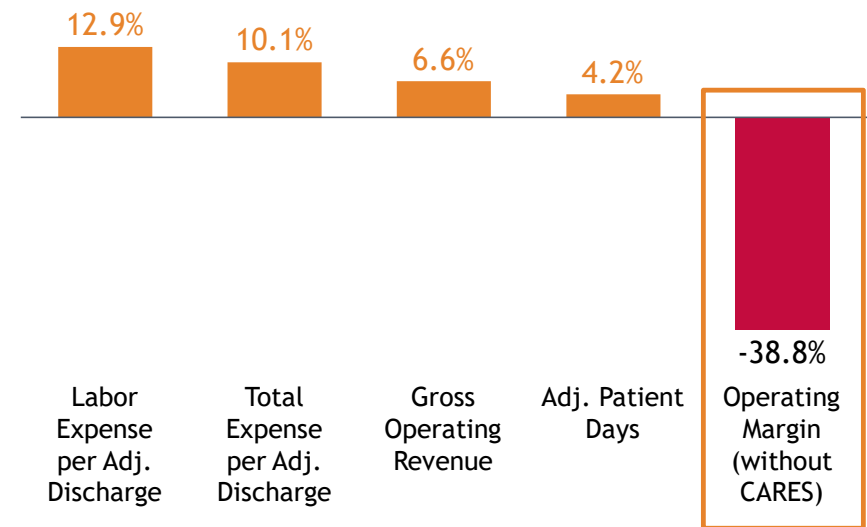


Inflation remains a major threat to healthcare financials; hospitals are experiencing a surge in expenses for items such as labor, drugs, and supplies.

Per-unit Expense and Revenue Growth
March 2021 vs. March 2022



Year-over-year March 2022 Financial KPIs
for U.S. Hospitals and Health Systems



Market conditions will remain challenging for the rest of 2022, as labor pressures and high inflation compress margins for most providers.



“The bumpy ride not-for-profit hospitals have been on will continue, with sector medians showing significant credit strength when looking backwards, but the forward look much more concerning...Fitch sees a deteriorating outlook for the rest of 2022 and into 2023, with a period of elevated downgrades and negative outlook pressure.”

KEVIN HOLLORAN
Senior Director
Fitch Ratings

Fitch Mid-Year Outlook Not-For-Profit Hospitals and Health Systems

Hospital Operating Margins Pressured Significantly YTD 2022

Operating Margin



Source: Fitch Ratings.

Characteristics of Successful Independent Hospitals



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Key Characteristics of Successful Independent Hospitals

8

COMMON CHARACTERISTICS OF STAND-ALONE HOSPITALS That Continue to Operate as Successful, Independent Institutions

8 Sole or leading community provider



7 Located in an attractive, stable-to-growing market with a favorable payer mix



6 Of sufficient size to achieve efficient care delivery and cost management



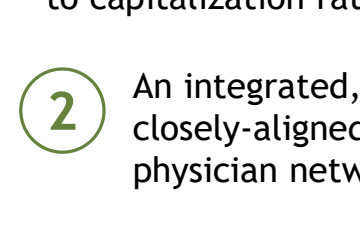
5 A wide array of profitable specialty care services and a high case mix index



1 Strong balance sheet, including >200 days cash on hand and a favorable debt to capitalization ratio



2 An integrated, closely-aligned physician network



3 Benefits from strong community support, including philanthropy



4 Recognized as a critical community health access point





1 Strong, Healthy Balance Sheet

Strong, Healthy Balance Sheets

Result from consistently strong margins;
generates strong access to capital on its own.

Characteristics

- >200 days cash on hand
 - Favorable debt-to-capitalization ratio
-

Benefits

A strong financial position can be leveraged to invest in internal organizational needs and capitalize on growth opportunities.





2 Integrated, Closely-Aligned Physician Network

Integrated, Closely-Aligned Physician Network

Loyal primary care physicians and specialists who share the goals of the independent hospital.

Characteristics

- Meeting growth agendas
 - Well-distributed across the service area
-

Benefits

High alignment gives hospitals the ability to deliver high reliability care, improve consumer access, and enter VBC arrangements.



3 Strong Community Support, Including Philanthropy

Strong Community Support

Engaged community that aligns with and supports the achievement of the independent hospital's strategic goals and success.

Characteristics

Support translates into philanthropic donors

Benefits

Philanthropic streams aid in formation of strategic capital, positioning the hospital to grow and support critical services.



4 Critical Community Health Access Point

Critical Community Health Access Point

Central provider in the payer network enabling access to care within the community.

Characteristics

- Key network component for leading payers in the market
- Providers critical access to services within reasonable drive-times

Benefits

Protections and “buffers” from renegotiation risks; ability to explore VBC and other innovative contracting arrangements.

5 Profitable Specialty Care Services and a High Case Mix Index

Profitable Specialty Care Services

Wide array of profitable specialty services and high patient acuity.

Characteristics

- Specialty service lines (e.g., cardiac services, neurosciences, orthopedics, and cancer care)
 - High percentage of surgical cases
 - Robust elective admissions
-

Benefits

Abundance of profitable specialty care services and high case mix yield higher margins that fortify the independent hospital's financial position.



⑥ Organization is of a Sufficient Scale To Achieve Efficiency

Sufficiently Sized and Scaled Organization

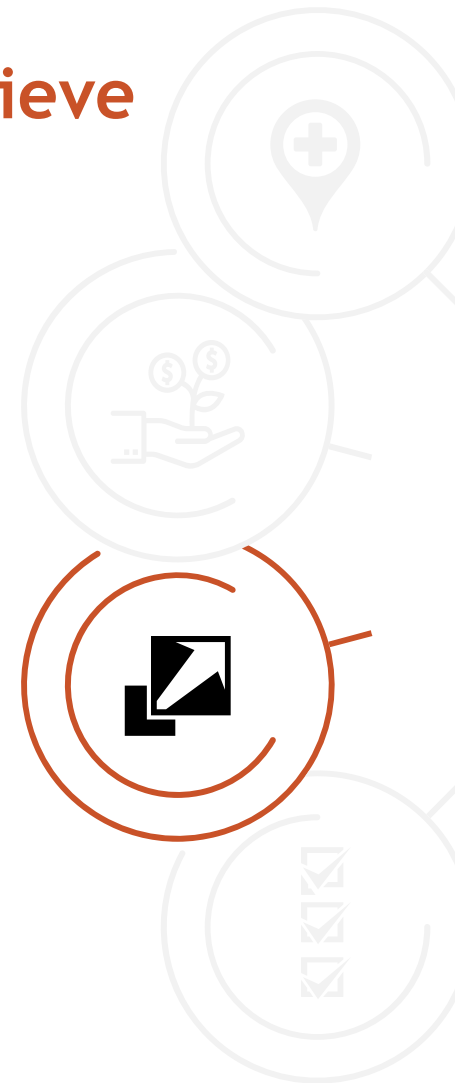
Providers with sufficient volume, supporting network, and optimized operational infrastructure.

Characteristics

- ~20,000-25,000 admissions
 - Large, well-distributed outpatient network
-

Benefits

Sustainability of profitable specialty and surgical services, better management of costs, and the ability to reinvest in strategic initiatives.



7 Favorable Market Conditions

Favorable Market Conditions

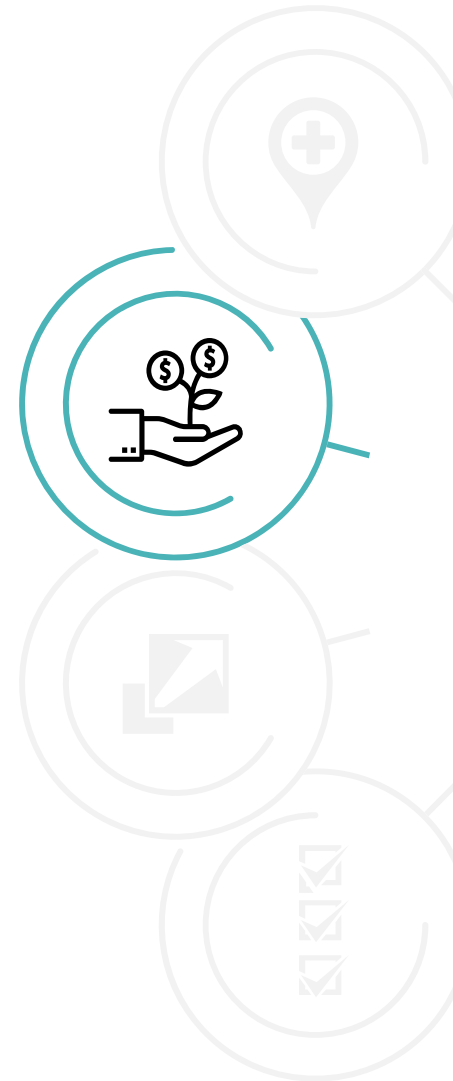
The population demographics, regulatory environment, and economic climate are attractive.

Characteristics

- Growing population base
 - Stable economic conditions
 - Favorable payer mix
-

Benefits

Provide financial resources to support clinical program expansion and produce business development opportunities.



8 Sole or Market-leading Community Provider

Sole Community Provider

The hospital is the sole or market-leading provider in the market served.

Characteristics

- Sole / leading provider in the market
 - Geographic or other market characteristics that serves as barriers to competitor entry
 - Potentially state regulations limiting new entrants (e.g., CON laws)
-

Benefits

Limited resource requirements and capital outlays to compete with a local competitor can preserve resources for other priorities.



Poll Question:

Which of these 8 categories represents the greatest threat to your ability to remain independent?

- 1 A strong balance sheet, including over 200 days cash on hand and a favorable debt-to-capitalization ratio
- 2 An integrated, closely-aligned, loyal physician network
- 3 Benefits from strong community support, including philanthropy
- 4 Serves as a critical community health access point
- 5 Offers a wide array of profitable specialty care services and a high case mix index
- 6 Of a size sufficient to promote efficient care delivery and cost management
- 7 Located within an attractive, stable or growing market with a favorable payer mix
- 8 Sole or predominant community provider

CLOSING DISCUSSION



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“No Regrets” Strategies for Creating a Sustainable Position

- Focus on the **patient experience**, including superior customer service, exceptional quality and easy access to services
- Build a **strong provider network**, consisting of both system-employed and aligned, independent physicians
- Create a **rewarding work environment** for caregivers and staff, with a focus on professional development
- Differentiate services by making **outsize investments in 2 to 3 marquee clinical programs**
- **Create a portfolio of partnerships** to complement and expand current service offerings
- **Maintain focus on margins** to generate capital to support growth



The decision to remain independent should be **periodically reviewed**, taking into account the changing market and internal dynamics.

This assessment should involve a thorough Board and executive team evaluation process that considers the following types of questions:



Does our institution fit the profile of a strong, independent hospital?



Is it realistic to think we can independently close gaps in our positioning and operational performance?



How should we involve the Board in an objective, periodic evaluation process?

Questions?



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Appendix: Alternative Partnership Opportunities



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There is an expanding rationale and broader approach to provider partnerships.

Future Health System is a “Portfolio” of Partnerships

Be “Payer-like”

- Population health management
- Network formation
- Care management
- Patient segmentation, risk assessment and pricing
- Product development

Adopt Digital and Consumer Capabilities

- Meet the expectations of a growing population of “digital native” consumers
- Tie your organization’s digital efforts to its broader business strategy



Increase Geographic Reach

Support larger populations to achieve scale and be a “must have” network in insurance products

Expand Clinical Continuum (Depth and Breadth / % of PMPM)








Provide full range of clinical services to maximize integration, scale and thus value and own higher percent of PMPM

There are a wide range of partnership models available, stopping short of integration.

Focused Partnerships	Program-Based	Professional Service Agreements	Contract for a partner to provide distinct clinical services at the independent hospital through professional service agreements (PSA) or similar arrangements
		Program-Specific Clinical Joint Ventures	Legal structure through which parties can jointly offer clinical services and share related investments, benefits, and risks
		Value-based Care Arrangements	Structures and/or contracts (e.g., Clinically Integrated Network) to work with payers to negotiate and implement value-based contracts
		Joint Ambulatory Network Development	Development of large-scale, joint-ventured ambulatory centers located in growth regions for the independent hospital and partner of choice
Integrated Models	Asset-Based	Minority Ownership	One party takes minority financial & governance interest while original owner continues to operate assets; usually tied to major program development efforts
		Joint Operating Agreement	Contractual joint venture company formed to operate as a unified organization while assets remain under legacy ownership
		Merger / Full Integration	Typically accomplished through a member substitution or other legal mechanism



There are a wide range of partnership models available, stopping short of integration.

Focused Partnerships	Program-Based	Professional Service Agreements	Numerous examples; can include large provider groups even, such as Optum	
		Program-Specific Clinical Joint Ventures	UCSF & John Muir Cancer JV; MD Anderson clinical programs, numerous pediatric health JVs	
		Value-based Care Arrangements	Accountable Health Partners at U of Rochester; Canopy Health in northern CA	
		Joint Ambulatory Network Development	Johns Hopkins and Anne Arundel ambulatory care JV	
Integrated Models	Asset-Based	Minority Ownership	Michigan Medicine acquisition of a minority interest in Mid-Michigan Health	
		Joint Operating Agreement	Several successful (THR/UTSW; Baycare/Trinity) and unsuccessful (KentuckyOne/UofL) examples	
		Merger / Full Integration	Numerous examples; member substitution with all assets and liabilities consolidated most common model	

Academic / Research Affiliations

Discussion



What do you see as the gaps in your current capabilities that a partnership could fill?



Have you recently evaluated existing partnerships that have been in place for some time?