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Post-M&A survival: lessons from success stories

Healthcare has seen accelerated consolidation activity in recent years. In 2015 alone, the number of hospital mergers and acquisitions (M&A) deals reached 102. There were 90 M&A transactions recorded last year.

A new analysis however reveals that the finances of acquired hospitals generally suffer for two years after the merger. During this post-M&A period, acquired hospitals typically experienced a decline in operating expenses but an even larger decrease in operating revenue, resulting in lower operating margins, according to the report published by the Healthcare Financial Management Association (HFMA) and Deloitte. The report authors studied the finances of organisations involved in 750 hospital M&A deals between 2008 and 2014.

“Conventional wisdom is that these transactions happen and in some cases they drive up revenue, but we found in the results that revenue per adjusted admission actually went down in the period after the transaction,” said Chad Mulvany, director of healthcare finance policy, strategy and development, for HFMA.

The short-term financial hit for acquired hospitals occurred despite elimination of redundant functions because immediate investments were needed in capital projects, additional staffing, and value-improvement initiatives, according to the HFMA-Deloitte report’s online survey of 90 financial executives and phone interviews with 13 others from hospitals involved in M&A deals in that period.

However, the negative trends in hospital margins levelled off two years after the transaction, the report says.

“There was a group of hospitals that performed better because they were much more intentional,” Mulvany noted. Their success can be attributed to a number of factors including effective leadership (i.e., having strategic vision for the combined entity), a strategy to realise revenue growth and cost-reduction opportunities, and an understanding of key enablers.

A key factor in an acquired hospital’s likelihood of meeting quality-improvement and savings goals was leadership, according to the report authors. In particular, top executives needed to develop a strong strategic vision for pursuing the transaction; determine explicit financial and nonfinancial goals; hold staff accountable, often at the vice president level, for integration efforts; and address cultural differences between the organisations.

Many of the hospital finance executives who were interviewed and involved in acquiring or merging hospitals admitted that they underestimated how cultural, competitive, and market differences of acquired organisations could limit the ability to realise post-transaction value.

A strategic focus — beyond merely looking to increase economies of scale — was an important part of what elevated successful deals, according to the executives.

It's also important to focus on a strategy of increasing market share for the combined hospitals in order to improve earnings. This is because attaining efficiencies is easier when hospitals are in the same or nearby markets, explained Thomas Hawk, a partner at King & Spalding.

“By contrast, deals where hospital A in market B buys hospital X in market Y often don’t move the needle meaningfully in terms of improved earnings, unless one of the hospitals is just mismanaged in the first place and there is low-hanging fruit to fix,” Hawk said. “Those instances are rare by now.”

Source: HFMA
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