

Volume 9 - Issue 2, 2009 - Cover Story: The Impact of the Recession on Medical Imaging

The Economic Crisis: The Outlook for Healthcare & Radiology

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The Outlook for Healthcare & Radiology

The worldwide financial crisis has not spared the healthcare and medical communities. Until the credit markets fell into a black hole in September 2008, healthcare was seen as a growth industry with a variety of “fail safe” debt instruments available to borrowers. With the onslaught of the financial crisis, things changed dramatically.

From mid-September to the end of December 2008, there were almost no healthcare financings brought to the capital markets. Financings that were closed were private placements or previously committed deals. The availability of capital for healthcare continued to be stunted well into the first quarter of the 2009 calendar year. However, the good news is that healthcare versus other sectors, such as municipalities, or schools, is more stable and still viewed positively. There have been very few defaults, and as the turmoil calms, it is expected that healthcare will be considered a rather “safe haven” for investment.

Impact for Hospitals

Nevertheless, the worldwide economic crisis has significant impact on hospitals. The American Hospital Association has released a study that shows 39% of hospitals are considering reductions in information technology capital investments and 45% are considering reductions in clinical technology. The report documents that patients are less likely to access hospitals for care and less likely to be able to pay for services.

Hospitals are having a much harder time paying off their debt and have less access to capital. 33% of hospitals are reporting increased interest expenses for variable rate bonds, with interest rates in the most recent quarter up 15% over the same period last year. More than half of the hospitals surveyed reported that they are also considering reductions in administrative costs and staff, as other financial pressures come to bear. Hospitals' total margins were down significantly in the third quarter of 2007 from plus 6.1% to minus 1.6%.

The margin pressures include:

- Non-operating revenue is down significantly due to investment losses, which are causing 31% of hospitals to increase funding in their pension plans;
- 38% of hospitals are reporting a moderate or significant decline in admissions and 31% are seeing a moderate or significant decline in elective procedures;
- Unemployment is increasing. Each 1% increase in national unemployment takes 2.5 million people off of employer health plans;
- Uncompensated care rose 8% compared to the same quarter last year;
- Medicaid expenditures are growing with increasing enrollment, but the state Medicaid funding gap is also increasing as the states confront their own budget deficits, and
- Hospital payment shortfalls for Medicare and Medicaid are increasing.

According to Millennium Research Group's (MRG's) 'US Markets for Diagnostic Imaging Systems 2009' report and its US Imaging Markettrack™ service, a combination of factors involving the current state of the US economy, excess installed capacity, and regulatory initiatives aimed at managing healthcare costs will have a negative effect on sales of computed tomography (CT) systems, magnetic resonance imaging (MRI) systems, and nuclear medicine scanners over the next five years.

The effect of the US economic downturn in the diagnostic imaging market was evident in MRG's US Imaging Markettrack™ findings. Compared to Q2 2008, respondents in Q3 reported a decrease in facility financial health and a notable decrease in diagnostic imaging purchase intentions.

"In addition to the current credit crunch, which has made raising capital for new purchases more difficult and expensive for many facilities," says David Plow, Manager of MRG's Diagnostic Imaging division, "there are already over 8,000 MRI scanners installed in the US, meaning the market has reached saturation. Compounding these restrictions, most MRI facilities are operating below capacity and, as a result, do not intend to purchase additional scanners."

Government cost-cutting initiatives are further dampening revenues. The implementation of the Deficit Reduction Act (DRA) has constrained the market for diagnostic imaging systems. Reduced reimbursements enforced by the DRA have made investment in additional scanners more difficult for non-hospital facilities. Furthermore, proposed initiatives from Centers for Medicare and Medicaid Services (CMS) designed to regulate contrast-enhanced procedures performed in physicians' offices to restrict self-referral will also hinder scanner sales.

The markets for magnetic resonance imaging (MRI) and computed tomography (CT) have been affected more than other industries by the economic crisis, because they represent the most expensive and highly advanced equipment. The regions most affected by the global economic crisis are the US and Europe. A lot of companies are on the brink of a tumble or about to move to other countries. Radiology prices are still very high, and because of company failures, insurance coverage is lost, and though medical expenses are needed, they are necessarily kept low. According to consolidated estimates cited by industry sources, revenues from CT shipments to US sites in the first half of 2008 fell to 580 million dollars, down from 755 million dollars over the same period a year earlier. This financial carnage came on the heels of a double-digit drop in 2007 compared with 2006, during which total revenues fell from 1.75 billion dollars to 1.4 billion dollars. MR shipments dropped 16% in the first half of 2008 compared with the same period from the previous year. This decline to about 530 million dollars versus 630 million dollars for the first half of 2007 was foreshadowed by very slow order activity in 2007. In the first half of 2008, revenue from the shipment of integrated PET/CT systems to US customers plummeted to from 155 billion dollars in the year prior to 110 million dollars. By comparison, revenues in the first half of 2006 amounted to about 178 million dollars.

There were some bright spots, typically markets for equipment requiring the least capital investment. Ultrasound, for example, weathered the storm well in the first half of 2008. Consolidated industry estimates indicate that radiology revenues and the number of delivered new units each rose by about 3% compared to the previous six months. Ob/gyn revenue rose by about 2%, but substantially fewer units shipped.

The industry estimates pegged new unit deliveries at about 18% below the previous six month period, indicating a trend toward the purchase of expensive, high-performance products. Mammography was a star performer, as vendors shipped 1,200 full field digital systems to US customers in the first half of the year. This compared with 765 in the first half of the previous year.

Nevertheless, there is no reason for healthcare providers not to move forward with capital plans. The following points are fundamental, however:

1. Solid business plans and strategic justification for projects.
2. Specific assumptions regarding operating performance, market dynamics, and return on investment.
3. Careful construction planning with realistic budgeting that aligns with debt capacity.
4. Appropriate equity contributions, guarantees, and operating/ financial covenants.

Credit is certain to be tighter and more closely linked to operating performance, but capital will be available for prudent borrowers with strong financial performance. The amount of debt (leverage) an organisation is able to take on will likely be less than in the past – no more 100% financings. Also, for projects involving physician investors, expect to see requirements for upfront personal guarantees and stricter requirements for bonuses (i.e., no bonus payout unless approved by the lender).

Checklist for Renovation/Expansion Projects:

- Look First for Operational and Non-Facility Solutions

Not every facility problem requires a new building. Adaptive reuse of existing space and cosmetic upgrades can often lead to improved patient experience, community awareness, and operational efficiencies.

- Conduct a Rigorous Analysis of the Market

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Good business planning demands an understanding of the market and its competitive dynamics before becoming dazzled by architectural renderings of future facilities. A typical market analysis will look at population demographics, volume analysis, and utilisation of current services in terms of the organisation as well as its competitors.

- Consider Department Relocation and Redesign

From both an efficiency and a cost standpoint examine whether or not existing spaces are appropriately located before reaching the conclusion that new facilities are needed. Good examples of this are the relocation/co-location of EDs and surgical areas to improve operational efficiency and increase outpatient revenue streams. A volume optimisation and efficiency analysis is an important first step in this area.

- Design New Spaces with Flexibility in Mind

Technology will continue to be a huge driver of how space is used in healthcare institutions. It is important to design space so that it can be adapted to new purposes and to create new opportunities for patient care and revenue generation as space needs and uses change.

EU Hopes Social Policies Will Mitigate Impact on Healthcare

The 2009 'Joint Report on Social Protection and Social Inclusion' focuses on the contribution of social policies in responding to the crisis. This year's report looks at the role of social policies in an economic downturn. The report highlights the following areas relevant to healthcare:

- Comprehensive strategies for 'active inclusion' – that combine inclusive labour markets, access to quality services and adequate minimum income – need to be implemented.
- Continued efforts are needed to reach the Lisbon target of a 50% employment rate for older workers to ensure long-term adequacy and sustainability of pension systems.
- Member States need to step up their efforts to improve value for money in the provision of healthcare and to reduce health inequalities, notably through increased attention to primary care, prevention, health promotion, better coordination and rational use of resources.
- Member States should continue to strive to establish and strengthen systems for quality long-term care, by creating a solid financing basis, improving care coordination and ensuring sufficient human resources as well as support for informal carers. The report is available at:

http://ec.europa.eu/employment_social/spsi/joint_reports_en.htm

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