



Three Ways to Thrive in the Face of Today's Cost Constraints



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Executive summary

All around the world, today's hospitals are operating in an environment of downward cost pressures, yet are being expected to demonstrate improved outcomes – which usually entails costly innovations to improve infrastructure, staffing, and technology. This white paper explores how such investments can actually lower costs by preventing expensive complications and examines financing options that can enable such investments. It also investigates how some hospitals, even in the most financially strapped global markets, are able to be profitable by taking advantage of efficiencies and economies of scale, as well as the growing trend of medical tourism.

Introduction

The growing and aging world population, the rise in chronic diseases, a growing middle class in emerging markets, and advances in diagnosis and therapy are all driving increases in global healthcare expenditures. Faced with ever-increasing numbers of patients, hospitals are under pressure to reduce the costs of treatment.

At the same time, healthcare facilities are increasingly being expected to demonstrate that they are providing patients with the most appropriate care and the most desirable outcomes and are taking steps to avoid adverse events. Often the achievement of these goals requires costly investments in infrastructure, staffing, and technology.

A hospital's success or failure depends in large part on how well it navigates these conflicting pressures. This white paper presents three strategies that can make the difference between getting ahead and falling behind. **Which path will you choose?**

The Challenge

Healthcare systems today are struggling to succeed financially and provide high-quality care in the face of scarce resources, government budget constraints, and limited-to-nonexistent access to the capital market. In addition, a global trend towards population health management is greatly impacting processes and business models and requiring comprehensive aggregation and analysis of patient data. This is "Health 4.0," the increasing standardization and industrialization of patient care.

In response to the pressure on healthcare systems, several trends are now emerging. Alternative compensation models, public-private partnerships, and new lucrative patient flows from abroad ("medical tourism") are causing people to rethink established business models and adapt their investment strategies. "Most players will need to develop new business models to win," the consulting firm Bain & Company predicts.¹ Deloitte Consulting adds, "Many of these new models will require costly infrastructure investments."²

This white paper examines three solutions that successful hospital systems are using to triumph in the face of today's financial challenges.

1. Boost profits through better patient management

Rapid, accurate diagnoses, effective patient monitoring, and appropriate treatments can improve outcomes, prevent adverse events, and reduce unnecessary patient readmissions, significantly decreasing the costs of care.³ Readmissions alone led to \$41.3 billion in additional hospital costs in the United States in 2011, according to the Agency for Healthcare Research and Quality (AHRQ).⁴

One opportunity for better cost control is the management of sepsis, an increasingly prevalent and expensive in-hospital complication. The cost of hospital treatment of sepsis has grown by \$3.4 billion from 2011 to 2013 in the United States alone, a 19% increase. "Early recognition of the symptoms of

sepsis, combined with prompt administration of fluids and antibiotics, can make a huge difference not only in morbidity and mortality, but also in length of hospital stays and health care costs," says Dr. James O'Brien, Jr., Medical Director of the United States Sepsis Alliance.⁵

At first glance, the technological investments required to reduce complications and improve patient care may appear to present a daunting financial hurdle. But investing continuously in effective and efficient medical technology, as well as in systematic and continuous training of staff, contributes decisively to improved diagnosis and treatment. This helps hospital operators avoid expensive mistakes and high opportunity costs, and therefore substantially improve their cost structure for the long term.

"A powerful driver of value in health care is that better outcomes often go hand in hand with lower total care cycle costs. Spending more on early detection and better diagnosis of disease, for example, spares patients suffering and often leads to less complex and less expensive care later," notes the Harvard Business Review. "Reducing diagnostic and treatment delays limits deterioration of health and also lowers costs by reducing the resources required for care. Indeed, the potential to improve outcomes while driving down costs is greater in health care than in any other field we have encountered.

Harvard Business Review adds that unlocking this potential requires healthcare providers to combine an accurate cost measurement system with the systematic measurement of outcomes. "With these powerful tools in place, health care providers can utilize medical staff, equipment, facilities, and administrative resources far more efficiently, streamline the path of patients through the system, and select treatment approaches that improve outcomes while eliminating services that do not."⁶

While there is broad consensus that prudent technological investments can lead to reduced costs and improved outcomes, many healthcare providers are struggling to find ways to afford such investments in the face of systemic cost containment pressures. In particular, many hospital operators have either very limited access to capital market financing or no access at all.

One solution is to use financing instruments such as leasing, lease-purchase, or mezzanine financing to enable the utilization of new technologies without purchasing them – and remain financially healthy at the same time. These options have the added advantage of allowing hospitals to more easily replace obsolete equipment with new, more effective technology as it becomes available.⁷

Additional possibilities include cooperative ventures with other healthcare providers or industrial enterprises. Cooperative hospital service organizations (CHSOs) may represent one such solution. In the United States, if their terms of use meet the country's strict regulatory requirements, CHSOs can provide both tax exemption and Anti-Kickback Statute Safe Harbor protection for such joint ventures. CHSOs may provide certain services on a centralized basis, including clinical (e.g., radiology), industrial engineering (including the installation, maintenance, and repair of biomedical equipment), laboratory services, printing, communications, and more.⁸

2. Pursue economies of scale

In the search for innovative business approaches, it is worth taking a look at the Far East. In countries like China and India, low per-capita income, a rapidly growing population, uncertain economic prospects, and a shortage of beds and doctors – especially in rural regions – make efficient and affordable care provision a special challenge. For example, in India, the out-of-pocket spending rate is the highest in the world, at about 70 percent. At the same time, India is one of the world's poorest nations.

Narayana Health (NH), one of the world's lowest-cost and most rapidly expanding hospital companies, was established in precisely this challenging environment. Since its founding in 2001, NH has grown from a small cardiology clinic into an internationally renowned major medical company with approximately 6,500 beds in 30 hospitals. Its success is mainly based on a systematic low-cost strategy. This includes the efficient use of modern technology and optimized surgery capacity. In 2014, the Boston Consulting Group named NH as one of the 50 most successful companies in the emerging markets.

"India's Narayana Health has revolutionized the health care industry by providing high-quality care at low cost. By handling greater volumes, Narayana Health is able to sharpen the skills of its surgeons, negotiate better terms with vendors, and improve capacity utilization. The hospital chain offers heart surgeries at half the cost of other Indian providers and about 10 percent of the cost of the procedures in Europe and the U.S."⁹

"For us, looking at a profit and loss account at the end of the month is like reading a post-mortem report. You cannot do anything about it. Whereas if you monitor it on a daily basis, it works as a diagnostic tool. You can take remedial measures. While charity is not scalable, good business principles can be scaled up and can be taken to any level."

Devi Shetty, Chairman and Founder, Narayana Health

3. Take advantage of the medical tourism trend

Many of NH's patients come from abroad, so NH is participating in the worldwide trend of global "medical tourism." Many successful hospital operators secure lucrative patient flows from abroad with excellent low-cost services, a good international reputation, and a focus on foreign target groups,

especially on wealthy private patients. Experts estimate that medical tourism has a market size of \$38.5-\$55 billion globally, based on approximately 11 million cross-border patients worldwide spending an average of \$3,500-\$5,000 per visit.¹⁰

A huge market for medical tourism is emerging. It is estimated that 750,000-1.2 million U.S. residents travel abroad for care each year.¹¹ In Germany, according to investigation by Bonn-Rhein-Sieg University of Applied Sciences, almost 250,000 foreign patients (including 97,000 stationary patients) are already earning German healthcare facilities 1.2 billion euros a year in the hospital sector alone.¹²

Medical tourists are fueled by a variety of motives. Many patients travel in order to obtain quality treatment at a lower cost. For instance, the cost of heart surgery at NH averages less than 1,700 euros; in the U.K. it is seven to ten times higher.¹³ Other particularly low-cost countries include Malaysia, Mexico, Thailand, and Turkey.

By the same token, wealthy patients from places like the Middle East or Eastern Europe often seek better medical care abroad than they can access at home. This is a tendency that can be exploited by hospitals in Western Europe and the U.S., where care is typically more expensive but also often more advanced.

Three ways to thrive in the face of today's cost constraints:

Thriving in the face of today's cost-constrained healthcare environment is a challenge, but some hospitals are managing to do so very successfully. Here are three strategies that can improve a hospital's bottom line:

1. Increase profitability through better patient care.

Investing in state-of-the-art technology and staff training may be expensive, but pays off in more accurate diagnoses, better treatments, and the avoidance of costly adverse events and readmissions. Hospitals struggling to afford such investments may find that leasing, lease-purchase, mezzanine financing, or cooperative ventures are the solution.

2. Pursue economies of scale.

Some hospital systems are doing very well, even in the most economically challenged parts of the world, by ensuring efficient processes and by focusing their efforts on certain key clinical practice areas where they can consistently excel.

3. Take advantage of the medical tourism trend.

Some patients travel in pursuit of less expensive care; others do so to obtain care of better quality. Hospitals should market their services in an effort to exploit this trend, whenever possible.

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