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3 ways hospitals can strengthen their operating margins amid ACA uncertainty

By Mackenzie Bean

Hospital leaders must remain vigilant in their goal to provide high-quality, affordable care, regardless of what happens in Washington, D.C. Despite President Donald Trump's and Republicans' failed attempt to pass an ACA repeal and replacement bill March 24, it is likely Republican leaders will continue to seek changes to the ACA as it was passed and interpreted under the previous administration.

The Republican-majority Congress underscored its goal to rein in federal healthcare costs with proposed per capita caps and block grants for Medicaid funding in the recently withdrawn American Health Care Act. The pursuit of this goal, whether through broad healthcare reform or incremental amendments, will intensify the economic pressure healthcare organizations already face.

To combat these pressures, hospital and health system executives must adopt a cost-reduction mentality, said Mukesh Gangwal, president and CEO of Prism Healthcare Partners, and George Whetsell, managing partner at the firm, in a webinar hosted by Prism on March 27. Prism is a national healthcare consulting firm based in Chicago.

"The future lies in an operating environment where a relentless attention to reducing costs is actualized — not by diluting quality, but by enhancing quality and being prudent," said Mr. Gangwal. "This is the mantra of the future."

Here are three strategic mindsets hospitals must adopt to reduce costs, strengthen operating performance and increase resiliency in the face of possible changes to healthcare reform.

1. Renew emphasis on rationalizing services, programs and locations

While a broad healthcare overhaul stalled at the federal level, there are several incremental yet influential changes HHS can make to the ACA without an act of Congress, such as ceasing to enforce the individual mandate and allowing states to impose Medicaid waivers and work requirements for beneficiaries. These changes would challenge affected hospitals and health systems with lower reimbursement and higher rates of uncompensated care.

Moving forward, standalone community hospitals must refocus on improving efficiency and reducing costs by scaling back low-volume service lines, or looking for other consolidation opportunities, said Mr. Whetsell.

"Standalone community hospitals have to take a step back and assess their programs and services and ask, 'Can we maintain everything we have?'" He said divesting and closing unprofitable service lines will be necessary to offset decreased government funding and retain sustainable operating margins.

Multihospital systems face the need to rationalize services as well. Mr. Whetsell said strengthening a health system's operating margin may require eliminating competition among hospitals within the same system and combining redundant services. Many hospitals offer duplicate or triplicate services simply to have a presence, rather than thrive, in the market.

Rationalizing services comes down to examining patient capacity, overall demand, size and strength of clinical service lines, and the service line's reputation and brand in the local marketplace, the webinar presenters advised.

"Too many smaller hospitals

offer too many services," said Mr. Gangwal. "There seems to be a redundancy and overcapacity no matter which way you look. Institutions have to focus on which space they want to play in and where they want to excel, opposed to being a mediocre provider of services in a vast array of clinical areas, which does not lend itself to profitable growth."

2. Rethink system and scale coordination

The healthcare industry is in the midst of rapid provider consolidation. Healthcare is now a marketplace in which profitable mergers are more critical than ever, and leaders must ensure acquisitions add value.

Mr. Whetsell says hospitals and health systems often have ample room for improvement in achieving economies of scale. He warns against mergers or acquisitions that result in a "confederacy of individual hospitals that have the ability to veto decisions made at the corporate office." Leaders must make difficult or politically sensitive decisions when it comes to scale, otherwise acquisitions are bound to result in weakly integrated systems with duplicative services.

Mr. Gangwal agreed that hospitals and health systems must relentlessly pursue economies of scale once a deal is done, but they must also exercise caution when selecting their partner. He advises hospitals base these choices on an entity's performance history and track record, rather than optimistic expectations or the anticipated trajectory of the combined organization post-consolidation.

"When a merger is contemplated, the incentive is to project the rosiest future — but everyone is leaning toward a future of growth and profitability that is rarely realized," Mr. Gangwal said. "We see far too many cases where two weak institutions have come together and coming out of that is a weaker enterprise, not a stronger enterprise."

3. Redirect management strategies toward return on investment

Management agility — or the ability to respond to market changes — will prove integral to healthcare organizations as they prepare for reduced federal dollars and fewer insured patients.

While addressing regulations and federal policies remains an important duty for management, Mr. Gangwal says hospitals and health systems must begin to align themselves with the commercial model of other industries. "It means management agility to quickly respond to regulatory changes, investments based on return on capital, investments based on pure market share or growth, and a cost model that is sustainable," he says.

To strengthen their operating margins, hospitals and health systems must obtain a clear understanding of their cost structure, including labor costs, non-labor costs, expenses in the clinical delivery of services, length of stay and investments made in the physician network.

Specifically, Mr. Whetsell says providers must reevaluate the ROI from hefty investments, such as information technology platforms and physician networks.

"A lot of providers are going to have to take a look at how they get value from the information technology investments they've made over the last 5 to 10 years. There have been huge amounts of money put into EHRs and automated scheduling systems. It's now time to figure out how to get productivity gains out of those IT investments," Mr. Whetsell said.

The vast majority of hospitals and health systems today employ physicians, which presents a complicated economic challenge for leadership teams. "If you're employing 100, 200, 300 physicians — you've got a multi-million dollar business, and you can't afford that business to have a -1, -2 or -4 percent operating margin," said Mr. Whetsell.

To make the most of physician network investments, Mr. Whetsell underscored the need for accessibility. There is no shortage of alternative care settings or clinics that can siphon a health system's patients today by competing on access.

"Make access to the physician network easier," Mr. Whetsell said. "It needs to be easier to get an appointment and get in to see a physician. I can go online and instantly make an appointment at Walgreens a mile from my house. There are very few physician networks where I can do that. Being able to prevent that business from going somewhere else is essential."

Whatever cost-reduction model hospitals and health organizations use, they must build profitability, maximize net revenue, increase efficiency and incorporate ROI into their strategy and processes — irrespective of the ACA's future. ■