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# 2020 ABI Health Care Program: The New Reality in Health Care

## **Consolidation: Where Do We Go From Here?**

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## The New Reality in Healthcare: *Increasing Scale, Velocity and Forms of Mergers and Acquisition Activity*

March 5, 2020

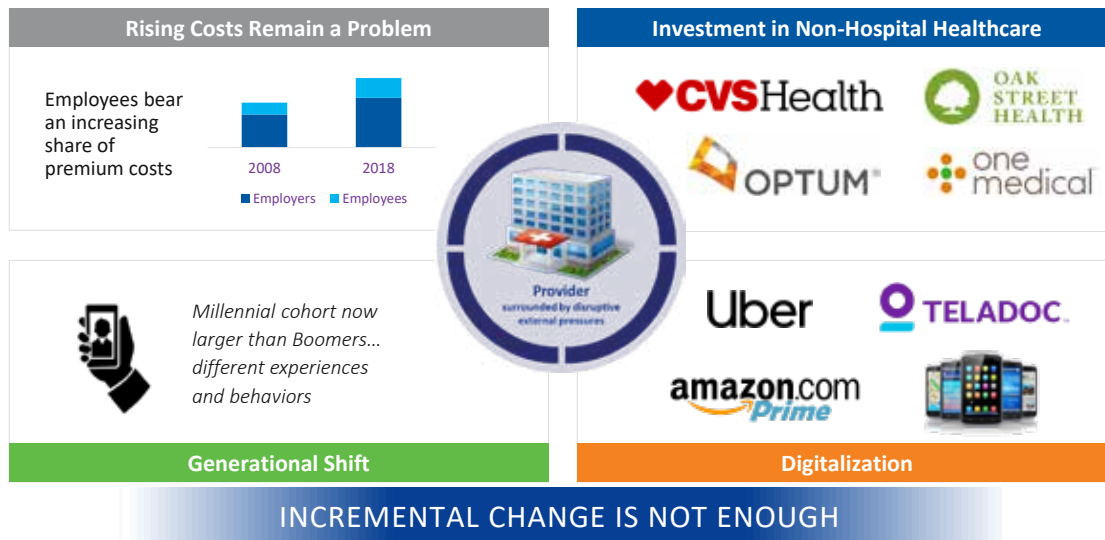
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### Legacy Healthcare Is Under Immense and Multiple Pressures

 <b>Insurers/ Risk Managers</b>	Will change the high and often inconsistent costs of legacy care models
 <b>Clinicians/ Caregivers</b>	Are likely to resist payment changes until new models are proven
 <b>Patients/ Users</b>	Losing tolerance for lack of accessible transparency about cost and quality
 <b>Disruptive Entrants</b>	Show intense cross-vertical interest in key segments of care delivery
 <b>Government Agencies</b>	Continue their regulatory scrutiny as transformation marches ahead



## The Traditional Provider Business Model Must Be Reinvented



## Industry Forces Are Reshaping the Basis of Competition

Consolidation is a given across the entire spectrum: new forms of alignment with unexpected participants and with novel structures will become the norm

The healthcare industry will continue to dis-aggregate into more distinct and specialized segments of care driven by new customer demands

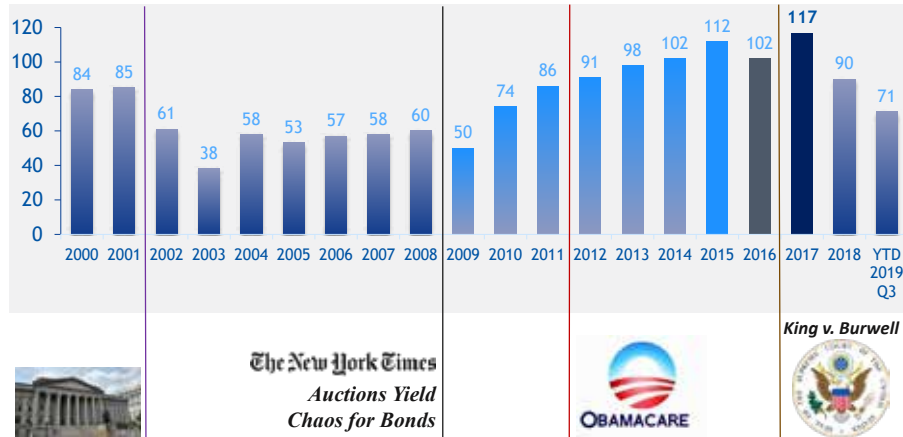
New entrants will likely focus on higher margin or easier entry services, with a more capable and effective market offering and will cede the rest to legacy providers

True value-based orientation and population health management likely will be beyond the reach of most organizations that opt to ignore collaborations and partnerships

INDUSTRY TRANSFORMATION WILL PRESENT THE BIGGEST THREAT TO ORGANIZATIONS THAT IGNORE THE FUNDAMENTAL MARKET SHIFT, AND PROVIDE OPPORTUNITIES TO THOSE THAT EMBRACE IT.

## High Levels of Consolidation Continue

Hospital and Health System M&A Transactions, 2000-2018



Sources: Kaufman Hall Transactions Data, S&P Median Credit Rating Reports, Moody's Median Credit Rating Reports, Moody's Credit Rating Changes Reports.

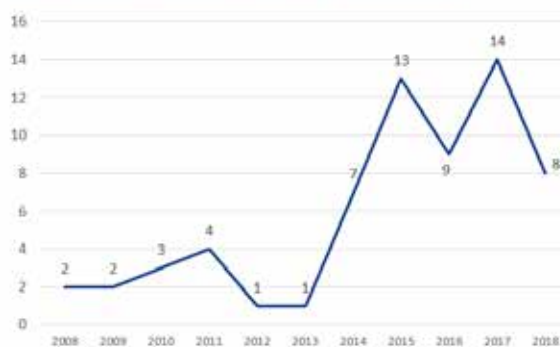


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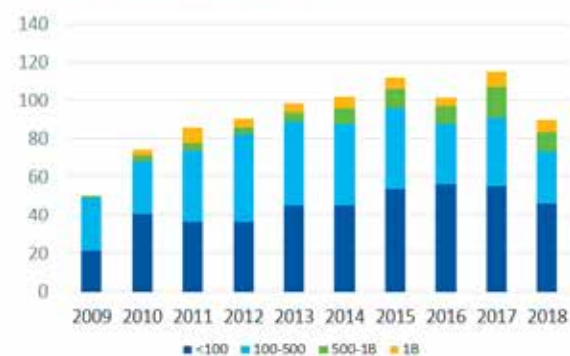
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## Higher Rated and Larger Organizations Are Participating

Number of Targets, Credit Ratings A- or Above



Transactions by Target Revenue



Sources: Kaufman Hall Transactions Data, S&P Median Credit Rating Reports, Moody's Median Credit Rating Reports, Moody's Credit Rating Changes Reports.

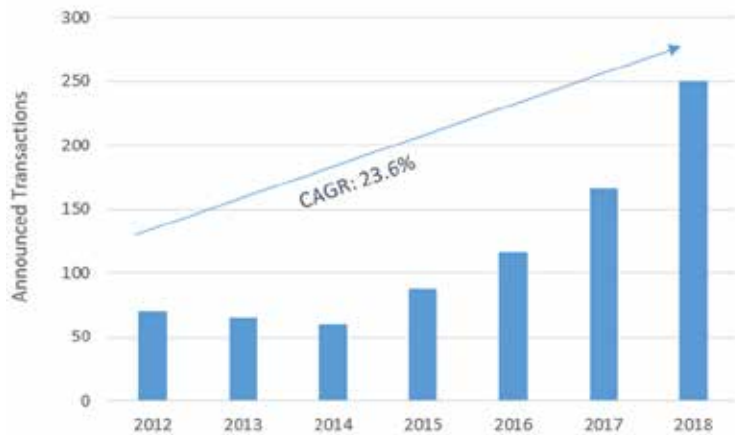


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## Transactions Involving Physician Groups Are Accelerating

U.S. Physician Group M&A Transactions by Year



Physician Group transactions have more than quadrupled in the last five years.



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## Once Distinct Industry Verticals Are Eroding



- \$194 billion company
- Rolling out 1,500 HealthHUBs over two years, putting a center within 10 miles of three-quarters of the nation's population
- Expanding into higher acuity care with launch of clinical trials for a new home dialysis device and a pilot program offering pre- and post-operative care for knee replacements



- Revenue of \$100 billion in 2018, up 11 percent over 2017
- More than 45,000 physicians, mainly through acquisition of practices, nationally
- Strong presence in 35 of its 75 target markets nationwide
- Recently announced new partnership with John Muir Health, in which Optum provides all back-office services

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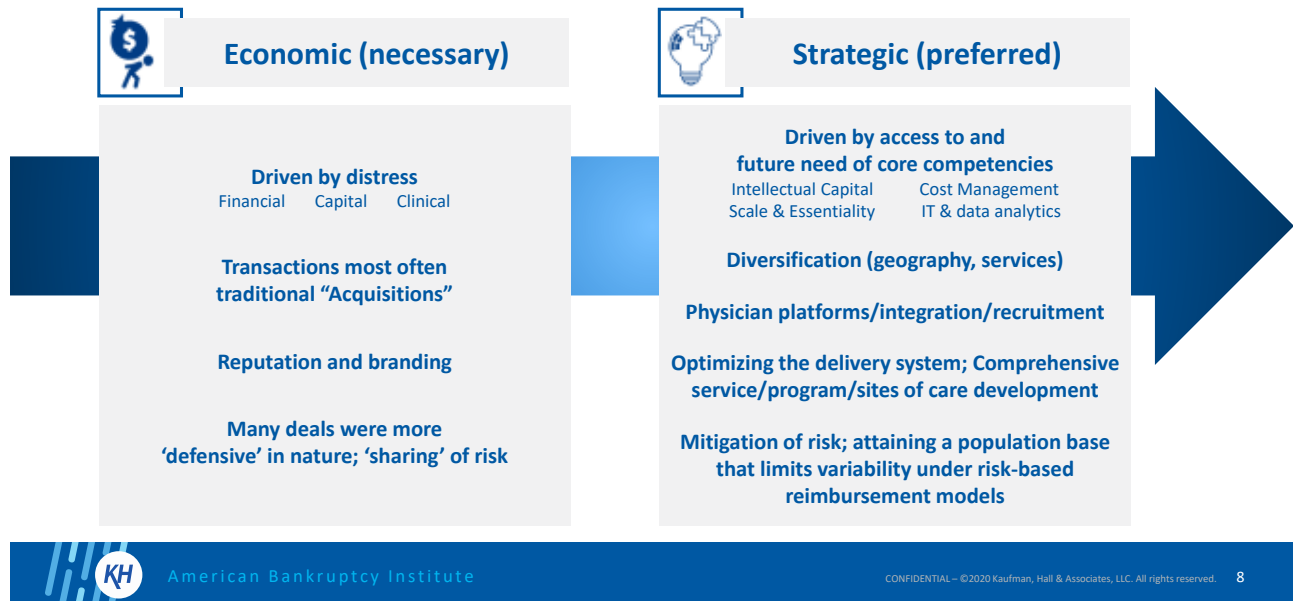
Sources: CVS Health: "CVS Health Reports Fourth Quarter and Full Year Results." Feb. 20, 2019; LaVito, A.: "CVS to Open 1,500 HealthHUB Stores Over Next Two Years." CNBC, June 4, 2019; Mathews, A.W.: "CVS Begins Clinical Trial for Home-Dialysis Device." *The Wall Street Journal*, July 17, 2019; Pifer, R.: "CVS to Test Knee Replacement Program for Aetna Beneficiaries." *HealthcareDIVE*, July 23, 2019; UnitedHealth Group: "UnitedHealth Group Reports 2018 Results." Jan. 15, 2019; Bailey Southwell & Co.: "Chasing the Leader: Healthcare Vertical Integration Follows Optum Model." Oct. 3, 2018; Japsen, B.: "UnitedHealth's Optum Now in Half of 75 Targeted Provider Markets." *Forbes*, Jan. 17, 2018; Japsen, B.: "UnitedHealth's Optum: We'll Lure More Providers to New Partnership Model." *Forbes*, July 19, 2019.



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## Industry Transformation Is Driving a Different Approach to Partnerships



## The FTC's Influence on the Industry Is Noteworthy

- The FTC historically has:
  - Viewed provider consolidation through the lens of pricing of **historically observed inpatient volumes**
  - Expressed its desire to limit concentration of area providers within **fairly tight geographic parameters**
- The rationale is that this would reduce competition and **give hospitals inappropriate pricing power**
- Limited market definitions and single measurement criteria are leading to blocked mergers that **pale in comparison** to the scale of corporations in other industries



## Key Issues for Healthcare Organizations Experiencing Financial Distress

Strategic Position	<ul style="list-style-type: none"> <li>• Erosion of long-term viability</li> <li>• Illustrative markers of distress</li> <li>• Market essentiality and payor mix dynamics</li> </ul>	<p><b>For many health care providers and organizations, the zone of insolvency will require careful consideration of fiduciary duties that influence creditors as well as community stakeholders, like patients, care givers and others.</b></p>
Governance	<ul style="list-style-type: none"> <li>• Fiduciary duties: Duties of care, loyalty; solvent vs. insolvent</li> <li>• Ownership and sponsorship issues</li> <li>• Governmental and Attorney General</li> </ul>	
Operating Performance	<ul style="list-style-type: none"> <li>• Revenue quality decline and negative cash flows</li> <li>• Working capital buildups become severe</li> <li>• What cost structure is required to produce positive cash flows?</li> </ul>	
Balance Sheet	<ul style="list-style-type: none"> <li>• “Softer” and contingent liabilities can add to overall leverage</li> <li>• Key triggers include defaults, renewals, changes in funding</li> <li>• What resources exist to execute a turnaround?</li> </ul>	
Restructuring Options	<ul style="list-style-type: none"> <li>• What is the core underlying business? Do non-core assets have value?</li> <li>• Options outside and inside bankruptcy may inform decisions</li> <li>• Communication to other stakeholders is critical</li> </ul>	



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