A LOOK INSIDE

2020 J.P. Morgan Healthcare Investor Conference

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The following is a synthesis of the tax-exempt track at the January 2020 J.P. Morgan Healthcare Investor Conference held in San Francisco on January 13-16, 2020. **This narrative highlights common themes, organizations pushing the edge on transformation, and some thoughts on what was not discussed but should have been.** This was the 10th year of the tax-exempt track and 38th year overall for the annual conference. This write-up focuses on the tax-exempt sessions, although there were almost 450 presentations by investor-owned organizations that are also trying to change the future of healthcare.

Common Themes

There was much passion, humility and celebration of what progressive health systems are doing to better meet the needs of their communities. When watching 27 presentations by leading health systems, many common themes emerge, as we all face similar industry challenges and opportunities. Leadership teams and boards can look at the following list as another data point to test their own playbooks. While most core strategies have continued over the last several years, this write-up also comments on trending of focus compared to presentations at prior conferences.

Patient/consumer centricity and experience continue to be a commitment for all systems, with even more emphasis on putting the patient and their families at the center of care and business model redesign and strategic focus. There is growing emphasis on moving care closer to the patient through ambulatory growth and virtual means, and out of traditional inpatient settings.

Safety and quality improvements are a continued expectation for all systems, with some systems committed to being High Reliability Organizations with zero serious safety events.

Growth, scale and diversification remain top priorities for most systems, although approach, pace and value proposition vary across entities and markets. While there is still enormous value to be tapped, some systems are truly differentiating themselves at a pace not seen previously.

Affordability of healthcare is a widespread concern, with broad recognition that the current system is already unaffordable.

Efficiency and performance improvement continue to be important for most systems to offset the gap between payment rate increases and input inflation. Many systems are proud that they leverage business discipline and push for wide adoption of evidence-based practice.

Value-based care and population health received more discussion than in recent years, with many health systems describing benefits of having their own health plans, expanded Medicare Advantage participation, risk-based contracts, direct-to-employer relationships and ongoing programs to reduce PMPM costs.

Transformation, disruption and innovation are driving many health systems that believe they must accelerate transformation before others disintermediate them. While discussed in prior years, urgency and effort to push for transformation appear to be increasing.

Digital enablement, including virtual care, data analytics, AI and robotic process automation (RPA) are now uniformly discussed as essential to better serve patients and members, although healthcare still lags other industries.

Genetics and precision medicine are growing as strategic priorities, particularly for cancer care. Multiple organizations are now pursuing full genome sequencing for large numbers of individuals in their communities, and technologies such as CAR-T therapies, CRISPR and regenerative medicine have moved from research to care delivery.

Partnerships and commercialization are expanding in popularity as ways to gain access to additional capabilities and accelerate transformation. This includes partnerships with Google and Microsoft, as well as a plethora of relationships to improve care, patient experience or cost structure. Health systems are expanding efforts to commercialize their own perfected administrative capabilities and discoveries.

Social Determinants of health receive wide recognition, as health systems need to partner with other organizations and engage with individuals differently to improve health in their communities.

Unwavering Mission Commitment describes many organizations. This includes providing care for at risk populations as reflected in community benefit spending, the obligation to maximize impact on communities served, as well as investments in teaching the health professionals of tomorrow and care discovery.

Culture and commitment to employees continue as areas of focus, including diversity and inclusion, talent development, and more recently, broader commitment to caregiver well-being.

Treasury management remains important as most organizations are half bank and half operating unit based on the respective size of assets and cash flow. Balance sheets generally strengthened in 2019 as a result of robust investment gains and solid operating performance.

Common Electronic Medical Records (EMRs) play a critical part of standardizing high-quality care, but discussions about EMRs had less prominence than in prior conferences.

Organizations "pushing the edge" — presenting tax-exempt systems ranged in size from sub-$2 billion to $30 billion of revenue. They included regional and national systems, health systems with robust academic missions, integrated plan/provider systems, and specialty organizations. Some benefit from being in high growth markets, others are in stable or declining markets. All face a rapidly changing healthcare environment. Each organization had 25 minutes to succinctly share their situation, strategies and successes. A synthesis of the presentations by those moving particularly fast to transform is included in the Discussion section of this write-up.

Critical issues not addressed at the conference given time constraints and general desire to tell a positive story in front of peers, prospective partners and the financial community, it is not unreasonable for leaders to focus on "the good stuff" and avoid "uncomfortable truths." Sometimes that is unfavorable financial performance, more broadly it is about industry exposures. Two industry issues not really discussed but critical to future viability are risk of major future payment reductions, and the fact that the industry remains massively subscale. Both of those topics have enormous future ramifications, and are discussed in more detail later in this write-up.

DISCUSSION
Deeper Review of Common Themes

The following provides a more robust discussion of the common themes identified above.

Patient/consumer centricity and experience — Essentially every health system declared its commitment to patient and family centricity both as a business imperative in a world of high consumer expectations, and because it is the right thing to do. There is much more focus now on building clinical processes around patient convenience and experience instead of provider convenience. This includes moving care out of acute settings into local ambulatory or home settings, leveraging digital and virtual health, radically expanding access hours, reimagining sites of care, and using new capabilities to truly personalize care.

Intermountain declared they want to serve their community as the "Amazon Prime of healthcare," a pretty bodacious goal. Patient centricity is driving radical change in philosophy and approach at all health systems, including academic health systems and specialty organizations such as orthopedics, cancer and children's hospitals. While much progress is being made, there is still consumer frustration with their inability to see a doctor or get a test quickly and conveniently, and to know prospectively how much their care will cost. If health systems don't continue to transform, they will be disintermediated by technology and niche players who better understand how to serve the consumer.

Improving safety and quality — Safety and quality continue to be a given for all health systems, with many presenters describing focus and successes relative to core measures and other metrics. Although some studies have suggested mergers actually hurt quality and safety, a number of systems documented that safety and quality were improved through integration. NYU Langone emphasized the importance of actual to expected mortality for inpatient care for all hospitals, while others celebrated system-wide dashboards and physician comparative scorecards that ensure transparency and focus on improvement. Multiple organizations talked about employee safety in addition to patient safety. While safety and quality performance has improved across the industry, the reality is that harm still does occur more often than necessary in healthcare. To address this, an increasing number of health systems have committed to becoming High Reliability Organizations with expectation of zero serious safety events.

Growth, scale and diversification — The majority of presenters discussed substantial growth over the last several years. In some cases, this reflected high compound annual growth rates (CAGR) through a megamerger or a series of rapid consolidations. Some organizations such as Baylor Scott & White and Providence are blessed with significant market penetration in favorable high-growth markets. Others in more stable or declining markets have found ways to grow through focus on Medicare Advantage, improved access, increasing "share of care," etc. While multiple presenters emphasized that they did not want to "grow for growth's sake," there was wide desire to positively touch more lives, increase market relevance, and leverage larger scale to reduce costs, improve care and gain access to capabilities.

Some systems have seen net growth in inpatient activity due to population or market-share growth, although many have seen declines due to shift to ambulatory care. There is great passion to bring care to the patient, which is accelerating this shift. Many systems continue to expand investment in employed/sponsored physicians, and most have seen growth in non-inpatient care. Virtual care, including telehealth, has continued to grow as a strategic focus area, although the economics in a fee-for-service environment are still often unclear.

There is much effort to grow diversified revenue streams, in part to offset current and anticipated decline in inpatient revenue. Part of this growth is through retention of a larger portion of services needed by existing patients, such as ProMedica that made a very large investment in post-acute facilities. Providence has defined diversification as a core strategy, and has separated acute services from other business lines. Philanthropy and commercialization were also widely discussed as important diversified alternative revenue streams.

There are a number of organizations that are leveraging unique expertise and capability to jump geographies in order to better touch more lives. For example, Mayo has 44 entities that participate in the Mayo Clinic Network. Hospital for Special Surgery has taken their orthopedic expertise to three additional states beyond New York, and noted that "scale is not just about size, but impact and knowledge." Others are monetizing administrative capabilities, such as Bon Secours investment in its Ensemble revenue cycle entity, or creating spinoffs to commercialize their research/discovery efforts.

Mergers and acquisitions have clearly continued with more organizations recognizing that they need to become part of a larger health system in order to have resources, scale and access to key capabilities. Many large organizations believe they still need to continue to grow, and to leverage innovation through partnerships with investor owned entities to accelerate speed-to-value and reduce innovation costs.

Affordability and the cost of healthcare — Multiple presenters noted that "healthcare is not becoming unaffordable; it is already unaffordable." This is true for individuals, employers, for government, and for society as a whole. Several systems noted that healthcare is the number one cause of bankruptcy. While it may be debated whether healthcare costs and hospital collection efforts are what put the most people into bankruptcy, or just contributes to financial challenges related to adverse health situations, it is clear that the cost of healthcare is catastrophic for many.

Employers are increasing copayments and deductibles for their employees to reduce cost and increase price sensitivity, which is creating pain for employees and lower collections for providers. ACA Bronze plans provide catastrophic coverage, but with unaffordable deductibles. And the elimination of the ACA mandate means more individuals will roll the dice, have major health problems, and not have coverage. In response to this, most health systems are trying to reduce their cost structures and respond to higher consumer price sensitivity.

Efficiency and performance improvement — Many organizations discussed how they improved efficiency to reduce the cost of healthcare, and a plethora of things to create value. These multiyear initiatives have allowed maintenance of margins, and in some cases improved margins. Acronyms used for performance improvement initiatives vary by entity, but the common themes are to improve productivity, increase throughput and asset utilization, redesign care processes, enhance access, streamline administrative processes, and improve revenue cycle and supply chain. Some systems have emphasized uniform adoption of evidence-based best practices. For those systems with health plans, there are also efforts to reduce per-member, per-month utilization and costs, improve HCC documentation, etc.

Many systems attributed success at being better financial stewards to strong organizational discipline. John Orsini, CFO at Northwestern noted that "budgets are a commitment, not just an aspiration." Many organizations stated that their operating company model with unified processes and associated scale absolutely improved efficiency while also enhancing quality and patient experience. This was reflected in "One Intermountain," "One Jefferson," and "One OSF," who all use similar vernacular to describe the increased effectiveness of a unified entity. Even highly complex academic health systems discussed success in driving efficiency and effectiveness. For example, NYU Langone proudly described specific examples of how they improved throughput.

Efforts have not just focused on efficiency, but also effectiveness. OSF regularly asks "how can we get better in all we do?" as an internal mantra and a challenge to the industry. Many organizations have committed to performance improvement for both operational and clinical processes. This is supported by robust system-wide scorecards, as well as transparently comparing performance between physicians. Advocate Aurora has a system-wide report card that shows current state against 2025 aspirations to help drive change.

Value based care and population health — While many health systems still rely on fee-for-service payments, many more organizations are embracing value-based care. There is much broader participation in partial- or full-risk arrangements, with some systems noting they had entered into four- or five-year contracts with payers that included risk provisions. There were multiple success stories for those participating in Medicare Shared Savings Programs (MSSP) and Next-Gen programs. Direct-to-employer contracting on a risk basis has increased, for academic health systems as well as Cancer and Children's hospitals.

A number of presenters described how they effectively leveraged their owned health plans to increase market share, improve quality and member experience, reduce cost and allow the organization to remain viable in the face of declining utilization. This "integrated care and coverage" provides maximum opportunity to manage a defined population. Geisinger discussed successful efforts to reduce PMPM costs and improved outcomes related to evolution for its Medicare Advantage membership. Many systems stated that success in value-based care requires focus on per-member, per-month utilization, supported by strong data analytics, prospective care management, improved transitions of care, expanded focus on social determinants of health, HCC coding focus, etc.

Transformation, disruption and innovation — There was wide recognition during many of the tax-exempt sessions that the pace of needed transformation is accelerating, and general consensus that tax-exempt health systems need to transform before they get intermediated by others. This includes fundamental change in mission, structure, care delivery, geography, leverage of technology, etc.

As Janice Nevin MD, CEO of ChristianaCare noted, "healthcare systems need to transition from providing healthcare to improving the health of their communities." This was a common theme at the conference and reflects a fundamental shift from a focus on addressing acute health needs to a focus on improving health. This requires leaving the four walls of hospitals, providing services and engaging with communities and individuals in different ways. This has led to modifications in mission statements and substantial changes in assets. Much effort is concentrated on moving care out of inpatient settings and moving as close to the patient as possible, including in the home. Providence noted that they believe 52% of inpatient DRGs will move to an ambulatory setting or be handled by drug therapy instead.

There was wide recognition that many others, especially those with deep pockets, want to move into spaces historically occupied by health systems. This was clear in many of the investor-owned presentations elsewhere at the conference. Amazon has moved aggressively into retail pharmacy and believes they can do many things better than traditional providers. Google wants to change the face of healthcare, with aspirations to provide healthcare to billions. Google Ventures has made many investments in transformational medicine, such as gene therapy for adults. Oscar and Livongo appear to have vastly superior platforms for health plan member/patient engagement and activation. Niche companies with superior approaches abound to serve a broad array of patient/consumer needs. As Joe Impicciche (the new CEO of Ascension) noted, "technology companies are getting healthcare faster than healthcare is getting technology." That imbalance is very dangerous for incumbent health systems.

In addition to business-model and competitive-landscape changes, medical knowledge, technology and treatments are quickly changing healthcare. Immunotherapy, genetic and gnomonically-driven treatments are coming to market quickly. This will change and save lives, but further increase the cost of healthcare and create additional pressures on the system.

Digital enablement, including virtual care, data analytics, AI and robotic process automation (RPA) — Every presenting organization commented on digital enablement and virtual care, although healthcare lags other industries. Many health systems are effectively leveraging telehealth and remote patient monitoring to provide care wherever the patient is. While care continues to be shifted from inpatient to ambulatory settings, some are leapfrogging this transition to move care into the home.

Every healthcare organization now has a digital app. Baylor Scott and White said they have the highest-rated app in the country, one that is fully integrated for plan and provider. Others implicitly challenged that boast. Alexa is now heavily into healthcare, and many want to leverage voice as a critical interface to improve the patient/member experience, reduce burnout of providers, and enhance administrative efficiencies, care and community health. Health systems with unique expertise, such as Mayo Clinic, Mass General Brigham (new brand for Partners), Children's and Cancer hospitals, all expect to use digital technology to allow them to touch patients over broader geographies.

Large-scale data analytics, machine learning and RPA are in use more extensively now in a variety of ways: identifying patients for treatment, recommending the best treatment for a particular individual, supporting basic and applied research, and improving administrative processes.

Partnerships and commercialization — Recognizing the changing environment, competitive threats and new opportunities, most health systems are building relationships with others who can help bring scale to newly required core competencies. Some are partnering with Google or Microsoft to help with large-scale data analytics, artificial intelligence and other opportunities. Providence described in some detail its relationship with Microsoft to create large data sets with the assurance that Microsoft will not have access to underlying data to ensure privacy.

More organizations are expanding their efforts to monetize their perfected processes, clinical discoveries or other intellectual property. Ascension is now opening their fifth fund, investing in firms that can bring value-based capabilities to the organization while also providing strong investment returns. Most academic health systems such as Mayo Clinic and Mass General Brigham have traditionally had commercialization functions, although focus on commercializing discovery is increasing as both a revenue source and an opportunity to scale impact to help more people.

Genetics and precision medicine — Many health system leaders said that CRISPR gene editing, CAR-T therapy and even regenerative medicine are no longer just research tools, but are used by their organizations to change the lives of patients. It is now common for precision medicine to be used to target better cancer therapy. Full-genome sequencing of large populations is being sponsored by multiple health systems to better identify disease and advance knowledge. While these techniques can be costly, their use will continue to expand and become more mainstream. Organizations that do not leverage such tools will be providing inferior care.

Social Determinants of Health — Most presenters noted that they believed it is important to address negative social determinants of health to improve the overall health of communities they serve as well as individual health. There is significant disparity in care driven by caregiver bias and, more significatly, by social conditions and needs that are not adequately met. While health systems cannot independently solve underlying issues such as lack of food security, housing, education, employment, transportation etc. that lead to adverse health status, they can and generally are working harder to partner with others to address these issues. While hospitals still complete their annual 990 Community Benefit Reporting and mandated Community Health Needs Assessment and Workplan, the rigor of assessment and planning, and level of partnership and focused resource commitment has grown.

Unwavering Mission Commitment — As seen in the past, most tax-exempt health systems started their presentations with a review of their mission statement, and many discussed their Community Benefit expenditures. It was clear that these organizations do not exist as simple business enterprises, but to truly address the needs of the communities they serve as effectively as possible. The traditional distinction between health systems focused on delivering exceptional care and the tripartite mission of academic health systems (care delivery, education and discovery) has blurred. While organizations remain committed to effectively serving those in their geography, digital has allowed organizations to morph from touching individuals in contiguous markets, to massively scale their ability to positively touch people across the country and around the world.

Culture and commitment to employees — Many organizations continue to emphasize the importance of culture in success of the organization. This is true for existing organizations but also critical in the context of mergers where alignment of premerger cultures is important, as well as sensitivity and deliberateness during integrations. The importance of employees was also emphasized, with many celebrating their Gallup engagement scores, talent management efforts, frontline engagement, etc. Employed physicians were recognized as part of this. Multiple presenters described concern around clinician burnout and caregiver health, and their efforts to address. The traditional Triple Aim has been revised by many to be the Quadruple Aim, where the fourth element (in addition to Experience, Quality, PMPM Cost) is Caregiver Well Being. As in the past, a number of speakers noted the importance of good governance as well.

Treasury Management — Effectively managing financial assets and liabilities remains very important as most tax-exempt health systems are "half bank and half operating unit." Over time, a typical health system will earn about as much in return on financial assets as operating cash flow earnings on operating assets. However, there is generally much more volatility in investment returns, so deliberate integrated asset liability analysis and investment/debt structure is essential to organizational financial viability. Balance sheets generally strengthened in 2019 as a result of robust investment gains and solid operating performance.

Common Electronic Medical Records — EMRs continued to be referenced by some systems as a critical part of standardizing high-quality care but took less prominence than in prior conferences. A number of systems noted they had completed major EMR implementations without disrupting income, reflecting more product maturity and good implementation practices.

Some of the Most Dramatic Transformational Stories

The pace of transformation in tax-exempt healthcare has clearly accelerated, and all presenters showed great passion and commitment to create value for the communities they serve.

The following list highlights some examples of rapid transformation and efforts to change the face of healthcare, in alpha order.

Ascension — Historically the largest Catholic system, Ascension has accelerated their efforts to take advantage of their size and scale to drive transformation. The largely-new leadership team is continuing to leverage partnerships, including with Google, with expanded focus on digital technology to move care into the home and improve clinical process reliability. Best practice sharing and continuous improvement efforts receive further emphasis.

Bon Secours Mercy — After quickly integrating two modestly-sized Catholic health systems, subsequent mergers have grown the organization into a $10 billion international health system in two years. Effective growth and scale are the result of very nimble decision making, strong business discipline, mission commitment, and strategic investments such as in Ensemble Health Partners. CEO John Starcher noted they are "still not at scale at $10 billion."

Children's Hospital of Philadelphia (CHOP) — This system continues to advance healthcare for children through innovative genomics, data analytics and cell therapies. In addition to scientific breakthroughs, they are addressing social determinants of health, including a significant investment in housing in the community. At CHOP they are also reducing costs leveraging efforts such as a "financial stewardship blog" and *Nursing-Led Savings* (a book written by their nursing staff.)

ChristianaCare — This $2 billion organization has proven that including "Love" in its strategies has been transformational. The system has implemented a broad array of initiatives to improve health and shift care out of the hospital, benefiting from capabilities gained through many partnerships. Leaders believe that "anything that can be digital will be digital," and they worked to reimagine urgent care, behavior health, etc.

Geisinger — They continue to be a leader focused on "total health of the population," leveraging plan and provider assets. Geisinger continues pioneering efforts to conduct full genome sequencing for many in their communities, an approach other systems are now replicating to more proactively identify and treat disease. Ongoing care model redesign for Medicare Advantage populations continues to create better outcomes and lower costs. In 2019 Geisinger added "Proven Recovery" to their prior list of "Proven" best practice commitments. Surprisingly, this historically financially stable organization had a first quarter operating loss.

Hospital for Special Surgery — As the nation's leading orthopedic hospital for over 10 years (US News), HSS has now expanded into four states by leveraging its high-quality, cost-effective protocols and leading patient satisfaction. HSS has aggressively embraced ambulatory and virtual care, invested heavily in musculoskeletal research, and is building a "Musculoskeletal Eco System." Of the people who went to HSS for a second surgical opinion, HSS redirected 32% to nonsurgical alternatives. If HSS continues to expand geographically, it will substantially raise the bar and create strong competition in more communities.

Intermountain — CEO Marc Harrison M.D. shared his personal perspective 66 days after receiving a bone marrow transplant for multiple myeloma, a blood cancer. Intermountain continues its legacy of evidence-based "best care" and its commitment to being a model healthcare system. It is aggressively pursuing scale in capabilities through partnerships, and plans to complete full genome sequencing for 500k people in their community. To address affordability, they reduced prices on 60 "shoppable" procedures, decreasing margins by $100 million over 2 years, and committed to limiting rate increases for its health plan to 2%/yr.

Jefferson Health — An "academic health system that thinks like a start-up" has grown three-fold in six years through five mergers leveraging "currency of governance." CEO Stephen Klasko, M.D., believes that healthcare will look dramatically different by 2030, and is pushing Jefferson to become "healthcare with no address." Jefferson is using technology aggressively to move care out of the hospital, acting on its passion to bring all care to the patient.

Mayo Clinic — At almost $13 billion of revenue and $900 million of annual research, Mayo continues to grow as a leading academic health system. In addition to being a destination center, Mayo is providing specialty expertise more widely across the country and the world. This expansion has happened through the Mayo Clinic Network, which has 44 participating organizations across the country. But expansion will increasingly be through robust digital platforms. Mayo has a major partnership with Google, as well as many other strategic partnerships, since leaders believe "we cannot do it alone." It also has a major commercialization capability, and spun off 12 start-ups in 2019.

NYU Langone — An academic health system that has significantly raised its academic rankings, research spending and revenues through organic and inorganic growth, NYU Langone has proven that consolidation can in fact improve quality. The system has aggressively focused on throughput to reduce hospital costs and improve quality, while achieving excellent observed-to-expected mortality. Leaders believe the system has the highest researcher productivity in the nation.

Northwestern Medicine — With an aspiration to be at least top ten nationally in everything they do, Northwestern has continued its programs that drive "clinical integration at the speed of trust." The system leverages technology, best practices from outside healthcare and 24/7 optimization of its assets. Through its partnership with Google, Northwestern Medicine has cut false negatives for mammograms in half.

Providence – With a newly-abbreviated name, $24 billion of revenue and strong market position in many fast-growing markets, Providence wants to be the "intercept of innovation and compassion." This historically well-run Catholic system is aggressively working to "stay relevant, lead transformation and grow." They have recruited many leaders from outside healthcare and believe they need to diversify their revenue stream substantially. Although Providence is large and does have many internal capabilities, they are partnering with Microsoft and many others to leverage digital transformation.

Transforming Cancer Care — While reduction in smoking rates translates into fewer cancer cases, obesity-related cancer rates are growing dramatically. And as average age of the population increases, so does the incidence of cancer. Precision medicine, immunotherapies and other developments are radically transforming cancer treatment. While most health systems view cancer care as a key service line, some organizations are trying to improve diagnosis and treatment through broader collaboration. As an example, the University of California has a vision to integrate their five NCI-designated cancer centers to leverage protocols and collective access to clinical trials. The Seattle Cancer Care Alliance discussed similar strategies to improve access to the best diagnosis and care. City of Hope is trying to "democratize their capabilities" to allow others to access their expertise from across the country. Direct-to-employer contracting is redirecting care to these advanced centers.

Next steps after major mergers — Advocate Aurora, Baylor Scott & White and CommonSpirit all gave updates on their strategies and successes after their recent large-scale mergers. All have aspirations to grow further to leverage their scale and touch more lives. Like others, they all have robust playbooks to drive transformation.

What Wasn't Discussed That Should Have Been

While healthcare investor conferences provide an opportunity to see critical thinking by major health systems, it is also revealing to note what was not adequately discussed. The following are two such issues to consider more deeply.

Future financial exposures: Presenters described the need to transform to become more affordable, be more patient centric, to better serve communities, and to grow. All have focused on cost management and performance improvement, but most have achieved only modest financial improvement during a time of positive rate increases. At the conference two years ago, there was considerable discussion about "winter coming," but this year no speaker emphasized the need to proactively prepare for future, large-scale, payment rate cuts. Although Moody's recently improved its industry outlook from negative to stable, the reality is that over the medium term the tax-exempt healthcare industry will need to be ready for large economic headwinds. Every health system needs to assess their potential risks, ensure they have a long-range financial plan that anticipates those risks, and proactively accelerate performance improvement. Here are six major potential economic shocks that were not referenced at the conference:

- **"Medicare for more" —** Whether from potential healthcare reform or simply from the aging of the population, more patients will move from high-margin insured coverage to negative-margin Medicare coverage, significantly reducing operating income. "Break even on Medicare" will need to become a strategy again as systems will be less able to leverage the "hidden tax" of cross-subsidization from employer-paid care.

- **Legal disruption of ACA or retrenchment in Medicaid coverage —** At best there is uncertainty relative to court or legislative impact on the ACA, and some states are increasing work requirements or otherwise reducing Medicaid coverage. This will increase uncompensated care in many markets.

- **Reductions in Disproportionate Share payments, site-neutral payment changes, provider assessment reductions and 340b changes —** While pending changes have generally been delayed, and these issues affect organizations differently, ultimately there will likely be significant negative impacts on many healthcare systems.

- **Enormous federal budget deficits will ultimately get addressed in part through healthcare payment cuts.** Budget deficits of $1 trillion per year, at a time of low unemployment and low treasury bond rates, will ultimately be unsustainable.

Recent elimination of the ACA Health Insurance Tax, Cadillac Tax and Device taxes create relief in the short term, but ultimately a federal budget crisis will drive material cuts in Medicare and Medicaid payment.

- **Financial market correction —** After a 10-year upward market there will be a market correction sometime within the next 5 years. The last time that happened many healthcare organizations had to "stop the cranes" on major projects.
- **Softening economy —** Similarly, at some point the economy will soften. While this traditionally helps nurse recruitment, it also on balance hurts healthcare system financial performance.

The tax-exempt healthcare Industry is still massively subscale: While healthcare systems are running hard to increase their scale and market relevance, in reality it is still a cottage industry where the largest health systems each serve less than 3% of the US population. That contrasts with high consolidation in the insurance market, and almost every other domestic industry. Many health systems have achieved market relevance in their geographies, but limited aggregate consolidation is a barrier to true scale. Some thoughts:

- **The lack of scale is increasing the cost of healthcare.** Common playbooks mean much duplicative effort. A good example is independent investment by almost every health system in the creation of their own digital apps. Parallel innovation can lead to superior solutions, but duplicative spending is widespread, meaning higher cost.
- **Large, investor-owned enterprises have far greater scale and resources.** United Healthcare has a market capitalization of $277 billion, Google and Amazon have market caps of $1 trillion, and Microsoft and Apple are currently both at $1.4 trillion. They have almost infinite ability to invest in technology, services and consumer experience compared to even the largest health systems. The largest provider sponsored health plans other than Kaiser have about a million members, a small fraction of national plans. Centene noted that they serve one in every five Americans. It is unrealistic to believe that most individual tax-exempt health plans can achieve the cost efficiencies, consumer-centric engagement, data analytics or care management capabilities that the large national plans are building on.
- **Small systems are even more challenged than large systems in leveraging scale.** There is a demonstrative difference between a $20 billion health system and a small system regarding their abilities to systematically develop or partner for key competencies. Large systems can spread costs and develop necessary infrastructure faster.
- **Limited examples of industry-wide collective scale —** While there are collective advocacy groups such as the American Hospital Association and organizations like Premier and Vizient that have wide industry membership, there are few examples of true industry-wide scale initiatives. The one discussed at the Conference is Civica Rx, a game-changing collective effort. Over 45 health systems participate to create a scaled competitive manufacturing, purchasing and distribution model, with the goal of addressing the high cost of pharmaceuticals.
- **Lack of venues to rapidly share best practices across the industry —** Many investor-owned entities and some tax-exempt health systems spoke about accelerating cycle time. A historical value proposition for health systems has been the identification and rapid adoption of best practices. For example, Kaiser Permanente historically saw a reduction in cost and increase in quality whenever they adopted a care management bundle across the organization. However, the reality is that process and cultural change take a very long time in tax-exempt healthcare, and the industry does not have robust, systematic sharing of best practices across organizations.
- **Boards and CEOs don't always do the right thing.** Mergers of tax-exempt healthcare organizations to create scale requires boards and CEOs to make hard choices. To ensure their communities are best served in the long term, they might have to sacrifice independence, and things like continued inpatient service in a town. Hesitancy around these decisions can extend to leadership and governance of even small- and mid-sized health systems that believe they can be effective on their own, instead of recognizing that they can be better stewards by joining a larger system.

The subscale nature of the industry is not easily addressed. Like with most challenges, it can start with realization and acceptance of the current state. As tax-exempt organizations and often as faith-based entities, we exist to serve our communities as effectively as possible. Opportunities to do that include:

- Accelerated M&A through both full-asset and virtual models;
- Instead of building it ourselves, leverage external scaled capability through investor-owned entities or ventures created by other tax-exempt health systems;
- Expand collaborative efforts between tax-exempt healthcare organization to create more efficient regional models and to ensure access to national expertise and best practices;
- Scale tax-exempt service-line-specific organizations on a national basis to ensure access to best-in-class care, everywhere; and
- Create more industry utilities like Civica Rx.

Final Words

Although overly verbose, hopefully this write-up provides useful perspective as we collectively work to "change the face of healthcare" to better serve our communities and nation. **If you'd like to discuss your impressions of the common themes and how they're affecting the health systems you work with, please reach out to the author at edward.chadwick@ihfstrategies.com** or www.linkedin.com/in/edward-chadwick.

About the Author

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Presenting Tax-Exempt Healthcare Systems

Advocate Aurora Health
Ascension
Baylor Scott & White Health
Bon Secours Mercy
Children's Hospital of Philadelphia (CHOP)
ChristianaCare
City of Hope
CommonSpirit Health
Cottage Health
Geisinger Health
Henry Ford Health System
Hospital for Special Surgery
Intermountain Healthcare
Jefferson Healthcare
Mass General Brigham (FKA Partners Health)
Mayo Clinic
NorthShore University Health System
Northwestern Memorial HealthCare
NYU Langone
Oregon Health & Sciences University
OSF
ProMedica
Providence (FKA Providence St Joseph)
Seattle Cancer Care Alliance
Seattle Children's
SSMHealth
UC Health – University of California

In Remembrance

In remembrance of Bernard Tyson – This was the first healthcare investor conference following the death of Bernard Tyson, the CEO of Kaiser Permanente, the largest tax-exempt health plan/provider in the country. Mr. Tyson was widely regarded as a passionate and articulate advocate for positive change in healthcare and for those we serve. He will be greatly missed by all in the industry and beyond.

Bernard Tyson