



# A Look Inside Your Customers' World

Medical Device Supply Chain Council  
November 2011



# The Harsh Realities

The future is unclear, but some things are certain:

*Healthcare costs must come down.*

*Hospitals and providers  
will be reimbursed on  
value, not volume.*

future?

*Hospitals will need to survive on Medicare  
reimbursement levels.*

# Hospital reimbursements are going down

## Influencing Factors:

- Lower payment updates
- Reduced DSH payments
- Failure to Report Quality Data
- Readmissions (above cap)
- Hospital Acquired Conditions (for bottom 25%)\*
- Failure to meet Meaningful Use

**\*Even if all hospitals improve, there will always be a bottom quartile**



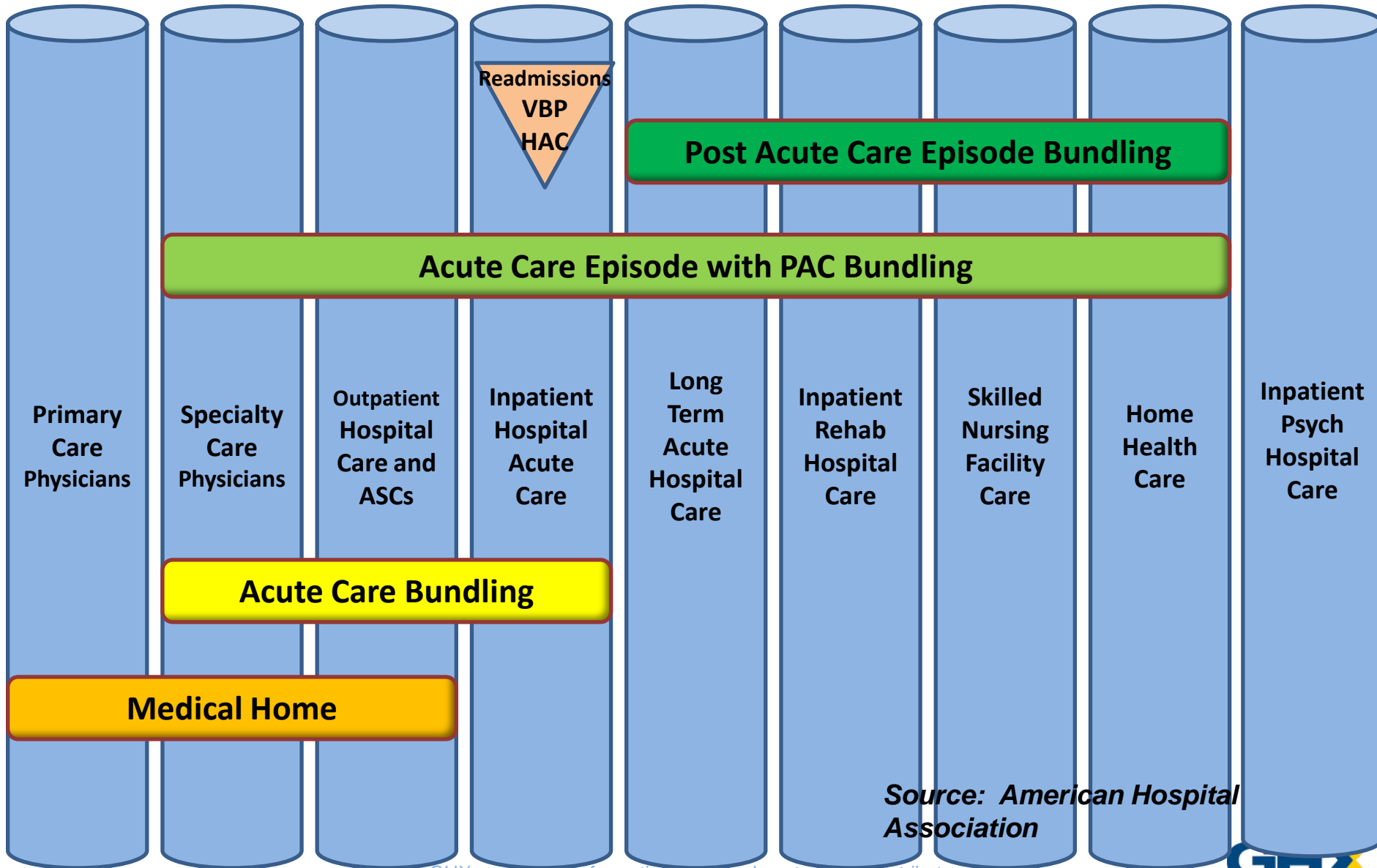
# Overlapping Policies Affecting Hospital Payment

Year-by-Year Payment Changes Affecting Annual Updates for Inpatient PPS Hospitals

Inpatient Prospective Payment System (IPPS) Policy	Fiscal Year									
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Market Basket (MB) Cuts for Productivity Adjustment (P) <sup>1</sup> and Medicare Savings	MB - 0.25	MB - 0.25	MB - (P + 0.1)	MB - (P + 0.1)	MB - (P + 0.3)	MB - (P + 0.2)	MB - (P + 0.2)	MB - (P + 0.75)	MB - (P + 0.75)	MB - (P + 0.75)
Reporting Hospital Quality Data for the Annual Payment Update <sup>2</sup> (Pay for reporting)	MB - 2.0 If Failure to Report	MB - 2.0 If Failure to Report	MB - 2.0 If Failure to Report	MB - 2.0 If Failure to Report	MB - 2.0 If Failure to Report	MB - ¼ of MB If Failure to Report	MB - ¼ of MB If Failure to Report	MB - ¼ of MB If Failure to Report	MB - ¼ of MB If Failure to Report	MB - ¼ of MB If Failure to Report
Hospital Value-Based Purchasing <sup>3</sup>				MB - 1.0 Potential for Earn Back	MB - 1.25 Potential for Earn Back	MB - 1.5 Potential for Earn Back	MB - 1.75 Potential for Earn Back	MB - 2.0 Potential for Earn Back	MB - 2.0 Potential for Earn Back	MB - 2.0 Potential for Earn Back
Readmissions <sup>4</sup>				MB - Hosp-specific amount capped at 1.0	MB - Hosp-specific amount capped at 2.0	MB - Hosp-specific amount capped at 3.0	MB - Hosp-specific amount capped at 3.0	MB - Hosp-specific amount capped at 3.0	MB - Hosp-specific amount capped at 3.0	MB - Hosp-specific amount capped at 3.0
Hospital Acquired Conditions						MB - 1.0 For Bottom Quartile Hospitals	MB - 1.0 For Bottom Quartile Hospitals	MB - 1.0 For Bottom Quartile Hospitals	MB - 1.0 For Bottom Quartile Hospitals	MB - 1.0 For Bottom Quartile Hospitals
Health Information Technology Meaningful Use <sup>5</sup> (MU)						MB - ¼ of MB If Failure to Meet MU	MB - ½ of MB If Failure to Meet MU	MB - ¼ of MB If Failure to Meet MU	MB - ¼ of MB If Failure to Meet MU	MB - ¼ of MB If Failure to Meet MU

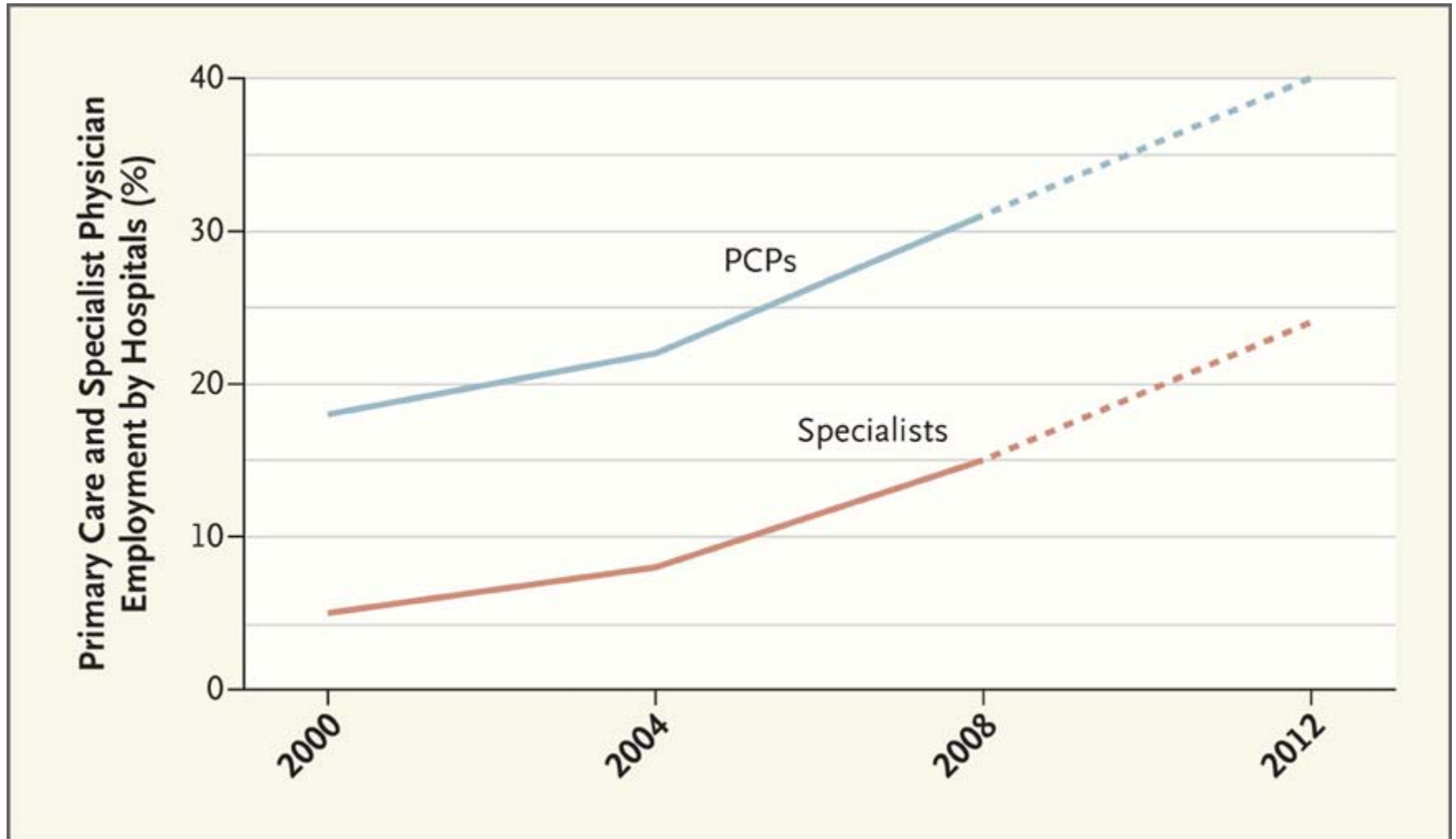
Note: all numeric reductions represent a percentage point reduction from the market basket rate. For example if the market basket is projected to be 3% and the reduction is 2 percentage points, then the remaining amount for the update is 1%.

# Accountable Care Organizations



Source: American Hospital Association

# Trend Toward Employed Physicians



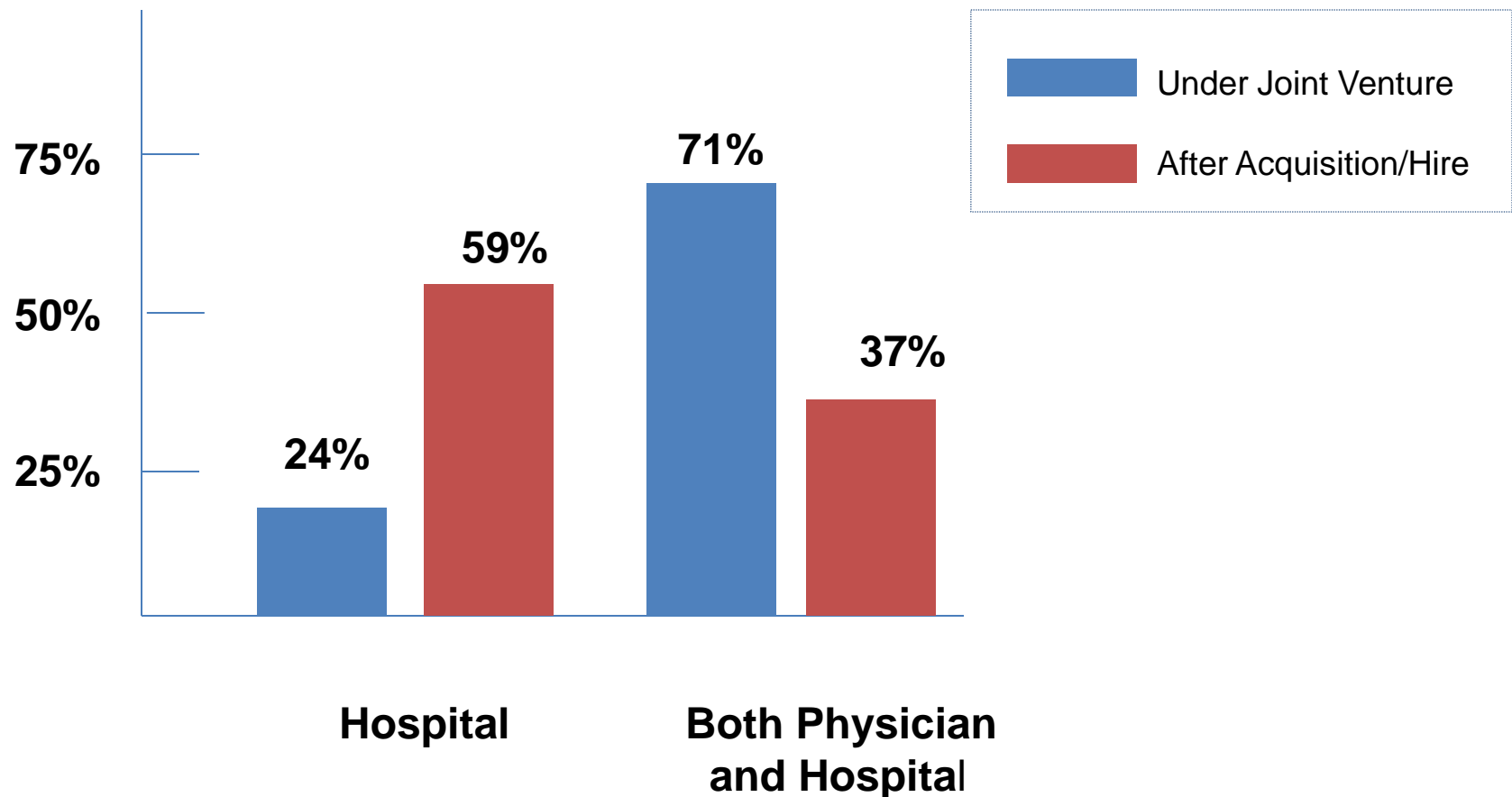
Source: Kocher, Robert, MD and Nikhil, Sahn, R., BS., "The New England Journal of Medicine, May 12, 2011 (Internet)

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# Trend Toward Employed Physicians

*Who will control purchasing decisions in 3-5 years?*



Adapted from HIDA/Marwood Physician-Hospital Integration Cross-Market Study 2011  
HIDA "Physician Market Report 2011"

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# View from the Street

## ***Annual Sector Outlook for Not-For-Profit Healthcare for 2010*** **Moody's Investor Service**

The primary effects of a weaker economy on hospitals include:

- **Lower patient volumes** as patients defer elective healthcare services
- **Rising charity care and bad debt expense** due to a high level of unemployment and the loss of - or reduction in - health insurance
- **Budget pressure on federal and state levels** forcing intensifying reviews of Medicare and Medicaid reimbursement rates
- **Unfavorable changes in payer mix** away from commercial due to rising unemployment and the expiration of COBRA benefits
- Financial pressures and lower membership at healthcare insurers, contributing to **lower commercial rate increases** for hospitals

From Moody's Investor Service January 2010 Annual Sector Outlook for Not-For-Profit Healthcare for 2010



# Supply Chain: The Bottom Line

40-45%	Total hospital operating expenses represented by supply chain
2022	Year supply chain costs could supersede labor costs at a leading IDN
50-80%	Contribution of some orthopedic and cardiac implants to procedural costs
\$1,000	Additional revenue needed to have same impact as \$1 in OPEX reduction
5-15%	Potential supply chain cost reduction with better supply chain management
2-4%	Better operating cost ratios for those that invest in back office automation

**Supply Chain can play an important role in delivering greater value**

**Value = Cost + Quality**

# New Customer Models

## Accountable Care Can Work



- ***Saved \$20 Million in Costs, First Year***
- ***Reduced Surgeries 13% Last Year***

Look for more integrated models like Kaiser Permanente and Geisinger

# Customer Models are Changing

## Highmark to invest \$475 million in West Penn deal Capital infusion to stave off closure of West Penn hospital

Tuesday, June 28, 2011

By Bill Toland and Steve Twedt, Pittsburgh Post-Gazette

Now you *really* are dealing with  
the people who **PAY** the bill!



## Cerberus to Buy Caritas Christi in \$830 Million Deal

*By Charles Stein*

March 25 (Bloomberg) -- Cerberus Capital Management LP agreed to acquire Caritas Christi Health Care, a hospital operator affiliated with the Archdiocese of Boston, in a private-equity deal valued at \$830 million.

# Market Consolidation

## *Chicago Market in the Past Year*

- Resurrection sells two hospitals to Vanguard
  - Resurrection merges with Provena Health
  - Ascension Health Buys Alexian Brothers Health System
  - Advocate Health Care Merges with Condell Medical Center
  - Northwestern Memorial Aligns with Lake Forest Hospital
  - Central DuPage Hospital and Delnor Community Hospital Merge
  - Trinity Health Acquires Loyola University Medical Center
- 



***Mergers and acquisitions up 20% Q3 of 2010 versus Q3 of 2009***

# Some Takeaways, Topics to Explore

**Hospitals need to make changes now, despite the ongoing political and legal debate**

**Healthcare is a SYSTEM. Hospitals cannot successfully implement change in a vacuum; All parties must be involved.**

Collaboration is critical, across functions, across the continuum of care and among trading partners.

**Healthcare reform increases COVERAGE, not necessarily ACCESS.**

**Hospitals must live in a fee for service world, while preparing for new programs, e.g., bundled payments, ACOs and value-based purchasing**

# Thank You



*Questions, please contact:*

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BLOG: <http://www.thehealthcarehub.com>