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Portfolio Analysis: Bridging the Gap between Planning and Finance
The Camden Group Continues to Expand
Top 10 Operational Concerns of Hospital CEOs
...and more!

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Given current financial pressures on hospitals and health systems, it is essential that resources be allocated effectively and with precision to achieve financial performance targets. Many hospitals have well defined financial reporting structures that measure operating performance against these targets. Sometimes missing, however, is a linkage between a hospital’s operating performance and its relative position in the market, and how these two translate into strategic performance or allocation of capital. In order to maximize results, it is critical to preserve and strengthen these linkages through consistent portfolio analysis of key business units and service lines.

Portfolio analysis is a process tool which illustrates, in multi-dimensional graphic form, the critical components of a system’s or hospital’s portfolio relative to key financial and market position metrics. This analysis communicates a clear picture of those entities with weaknesses and vulnerabilities and those with opportunities for growth and expansion. Overall bottom line results can be significantly impacted by using this process of analysis as the basis for allocating key resources for optimal leverage and return.

Health System Capital Allocation Assessment
Portfolio analysis is an effective tool for allocating capital resources. Figure 1 illustrates an example of a health system’s portfolio analysis using three key criteria to examine each hospital’s performance. The three criteria used are:

» Market opportunity
» Ten-year projected EBITDA (earnings before interest, taxes, depreciation and amortization)
» Ten-year capital requirements

The goal of the health system is to move its hospitals up the chart and to the right into the “Investment Priority” quadrant.

The matrix shown in Figure 1 (left) illustrates that Hospitals D and F both have moderate capital needs and similar levels of EBITDA. However, given the relative market opportunity of each hospital and the system’s limited capital resources, the investment should most likely be made in Hospital F rather than Hospital D in order to receive the highest return on investment. In addition, the system is now considering divesting Hospital D due to its low market opportunity and moderate need for capital investment. Prior to this analysis, these discussions rarely took place at the system level.
Hospital Level Assessment – Service Line Resource Analysis

Figure 1 illustrated an example of capital allocation based on hospital performance, required investment and relative position in the market. Portfolio analysis can also be applied to a hospital’s portfolio of service lines and the impact that each has on overall organizational financial performance.

Figure 2 (right) illustrates a hospital’s inpatient service line portfolio, showing contribution margin per case (X axis) and relative market share (Y axis). The size of the bubble represents the total number of cases. This hospital is currently doing further analysis regarding divesting psychiatric services due to its negative contribution, per case and overall. The hospital may also choose to focus on cardiology and thoracic & vascular surgery, or any other services positioned on the right hand side of the chart, due to the high contribution margin per case and potential to increase market share. This hospital performed an additional “drill-down” analysis on its psychiatric services, with particular focus on payer mix, contracted pricing, and staffing levels. The analysis concluded that there was little room to increase price, and staffing ratios were at appropriate levels.

Impact on Access to Capital

Hospitals are managed with targets, whether self-imposed or dictated by bond ratings, and must constantly balance the need for capital investment and the impact that investment will have on meeting its financial goals. Figure 3 (below) illustrates how the example hospital’s financial ratios compare to Moody’s median ratios for the hospital’s current rating (A) and Moody’s next highest rating (Aa).

In this case, the hospital is seeking to maintain and improve its current bond rating, and management must know the sensitivity of key financial and strategic variables. Portfolio analysis provides the data required to identify the variables that will have the greatest impact on operations. The example shown in Figure 2 illustrates a situation where the hospital may decide to divest psychiatric services and invest in cardiology and thoracic and vascular surgery. Two separate sensitivity analyses would be developed estimating the impact these actions would have on operations. The resulting operating performance would then be compared to the financial targets to determine if the investment in these strategies would generate the desired return.

**Example Hospital**

<table>
<thead>
<tr>
<th>Current Financial Performance Compared to Moody’s Median Ratios*</th>
<th>Baseline</th>
<th>Aa-Rated</th>
<th>A-Rated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating cash flow margin (%)</td>
<td>10.2</td>
<td>10.9</td>
<td>10.1</td>
</tr>
<tr>
<td>Max annual debt service coverage (x)</td>
<td>4.65</td>
<td>5.81</td>
<td>4.5</td>
</tr>
<tr>
<td>Cash on hand (days)</td>
<td>190.2</td>
<td>245.73</td>
<td>181.37</td>
</tr>
<tr>
<td>Cash-to-debt (%)</td>
<td>135.3</td>
<td>166.8</td>
<td>126.1</td>
</tr>
<tr>
<td>Debt-to-cash flow (x)</td>
<td>3.2</td>
<td>2.67</td>
<td>3.22</td>
</tr>
</tbody>
</table>

* Based on Moody’s most recent available health care median ratios.
Figure 4 (below) summarizes the output from this sensitivity analysis and the impact on the hospital’s financial ratios.

Health systems and hospitals seeking to improve operating performance as well as access to capital will benefit from the discipline of examining relative performance using portfolio analysis criteria for organizations and service lines. Using objective, transparent evaluative criteria and data that display results in a clear, graphic form, decisions can be made based on an overall perspective of performance, rather than on an incremental, project-by-project basis. This is critical to assure that the appropriate trade-offs are made and investments yield required results.

Further information about portfolio analysis and how this process can be implemented in your organization, please contact Linda Perry at lperry@thecamdengroup.com or Bill Wachs at wwachs@thecamdengroup.com.

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### Top 10 Operational Concerns of Hospital CEOs

1. Labor shortages and wage escalation
2. Patient throughput
3. Efficient and effective use of resources in the OR
4. Lack of education and experience at middle management level
5. Efficient and effective use of resources in the Emergency Department
6. Managing continuous cost increases
7. Identifying new and less costly strategies for providing Emergency Department call-panels
8. Management of the gap in work redesign between the prior work processes and the installation of new technology
9. Recruitment and retention of Medical Staff members
10. A lack of available capital

To access the details, or any past Top 10, visit our website at www.thecamdengroup.com. While there, sign-up to receive the monthly Top 10 via e-mail.
what we’re up to...

At this time you will find Camden team members in the following states:

- Arizona
- California
- Florida
- Idaho
- Illinois
- Indiana
- Kansas
- Massachusetts
- Michigan
- New York
- North Carolina
- Ohio
- Oregon
- Pennsylvania
- Tennessee
- Texas
- Virginia
- Washington

We are currently assisting our clients with the following types of projects:

- Strategic, business, market and facility master plans
- Medical staff, bed, service line and specialty hospital need assessments
- Hospital-physician alignment strategies and compensation plans
- Hospital-physician joint ventures
- Mergers, acquisitions, due diligence, valuations and fairness opinions
- Patient throughput and education implementation
- Hospital department assessments
- Health plan development
- Hospitalist and intensivist program development and implementation
- Patient access improvement
- Interim hospital management (CEO, COO, CFO)
- Retreat planning and facilitation
- Hospital business advisory

have you heard the news?

The Camden Group has opened a Chicago office, headed by vice president, William W. Wachs. Mr. Wachs has nearly two decades of financial advisory experience within the health care industry.

With our new location and Mr. Wachs’ leadership, The Camden Group is better positioned to provide integrated strategic and financial business advisory services to our clients throughout the country.

New office information:
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fax: (312) 474-6071
wwachs@thecamdengroup.com

Also, please join us in welcoming the following Camden team members:

Tamara Austin, senior consultant
Specializing in strategic and business planning, and operations improvement

Barbara Letts, senior consultant
Specializing in analysis, finance and planning.

Jason Dee, consultant
Specializing in need and market share analysis, and medical staff development plans.

Yun Zhao, consultant
Specializing in strategic and business planning, and utilization and resource need analysis.
Since 1970, The Camden Group has been providing management and consulting services to the health care industry exclusively. We have supported more than 1,000 medical groups, hospitals and health systems located in 43 states throughout the nation.

Our wide range of capabilities and a commitment to our clients’ vision and goals has made us a respected industry leader. With four specialized divisions, we are able to provide the support required to identify and develop solutions to the challenges our clients face, and are differentiated by our national industry perspective, innovative approaches, proven methodologies, analytic rigor and objectivity, and trusted relationships.