

Healthcare Mergers and Acquisitions and What They Mean for the Patient

Recent trends:

In the early 2000s, it appeared that the only healthcare establishments looking to merge were those with no other alternative; it was a case of merge or go out of business. Well, the situation has changed.

Mergers and Acquisitions (M&A) activity has been gradually increasing over the past decade or so, and a spike was seen in 2017, with the number of transactions (115 in 2017 compared to 2016's 102) being the highest since the financial firm, Kaufman Hall, began monitoring it in the year 2000. Even more remarkable than the number of mergers, however, is the gain in revenue by the smaller organization in each deal. In 2016, this stood at \$31.3 billion, while in 2017 it more than doubled to \$63.2 billion. When considering the relatively small number of additional transactions, this revenue increase is substantial.

This is largely due to the fact that in recent years, more and more successful Healthcare businesses have realized that M&A can be a lucrative venture if done right, and not just a means of avoiding bankruptcy. As Anu Singh, a Kaufman Hall managing director, put it, "Organizations that very credibly could remain independent and have that option, are proactively saying, 'We think partnerships can be a better route for our organization; we think we can do more for our community through a partnership than remaining independent.'"

The trend seems to have continued into 2018 for the most part,

although there has been an unusual hiccup according to [PricewaterhouseCoopers \(PwC\)'s report](#), which showed that Q3 2018's total deal volume (261) was slightly lower than the average for the past 7 quarters (264), and the deal value took a hefty hit, decreasing by 35.8% and 10.1% when compared to the previous quarter and 2017, respectively. Regardless, Thad Kresho, US Health Services Deals Leader at PwC stated, "While overall deal value has decreased in the recent quarter, volume levels remain strong across numerous sub-sectors both in the Corporate and Private Equity arenas. We expect this momentum to carry through the remainder of 2018, and beyond, as the pool of potential acquirers continues to expand."

What all this does to the price of healthcare:

Simply put, a merger or acquisition results in diminished competition between healthcare providers, and traditionally, this is something a consumer should never want. After all, two groups in competition with each other have no choice but to bring out the best products for the cheapest prices consistently or else their customers will just go to their competitors instead. But what if there is no competition? Well, worst case scenario, you've got another Martin Shkreli-Daraprim scenario and the prices of a healthcare provider's services could increase by exorbitant amounts overnight. Fortunately, such extreme price increases are not the standard practice. Even so, there is clear evidence that shows that more competition for a particular drug's manufacture means lower prices for the patient. [One particular study](#) analyzed 1120 generic drugs and categorized them according to their manufacturers' competition levels. Drugs made in very competitive markets decreased in price by 32% on average, while manufacturers with a monopoly on their drug increased their prices by a quite significant 47%.

It's a simple concept and one might presume it would apply in most M&A deals, but here's where it gets complicated. In some cases, one might actually expect the costs of healthcare to go down. Consolidation of healthcare groups could mean reduced overhead and operating costs, for instance, or better deals on bulk orders for medical supplies. In fact, data from Centers for Medicare & Medicaid Services (CMS) showed that, on average, larger hospitals have a lower cost-per-encounter than smaller hospitals offering the same services. Having analyzed this data, the [PwC strategy& team's report](#) concluded that hospital consolidation could reduce healthcare costs by 15 to 30% without any detrimental effects on the quality of the care provided. With that said, even if this decrease in costs is achieved, there's no guarantee that the hospital would actually lower its treatment prices, so the patients themselves might not benefit from these savings at all. In truth, more often than not and regardless of the merged hospital's increased or decreased profits, the patient tends to pay more. This is according to [research](#) conducted by David Dranove, a professor of strategy at Kellogg; Christopher Ody, a research assistant professor of strategy at Kellogg; and Cory Capps of Bates White Economic Consulting, who found that, on average, healthcare costs for services provided by a physician rose by an average of 14% following mergers between 2007 and 2013. Another more recent study found that if the merging hospitals were in the same state but at least 30 minutes apart by car, the average price of care provided increased by around 7 to 10%. "The rising prices are partly due to 'mechanical elements' of how prices are set in contracts [with insurers]," says Dranove, referring to the fact that insurers can, for example, write contracts allowing hospitals to bill more for a procedure than a physician group could. This is already a known issue and groups such as Medicare are actively trying to come up with preventative measures.

Nevertheless, this doesn't mean that all known cases of M&A activity lead to price increases for the patient. A merger between [Walcheren Hospital and Oosterschelde Hospitals](#) approved in 2009 managed to do just the opposite. The likely cause for the success of this merger is that it was approved with [three remedies](#). The most significant of these, and likely the main contributing factor for the price decreases, ensured that a price ceiling was established, specifying a maximum average charge for business-sector diagnosis-treatment combinations. Since the price ceiling was based on a weighted average of prices charged by other hospitals in the country, this prevented the new 'United Hospital' from overcharging its clients, even in the absence of competitive pressures to do so.

Are the increased costs justified by superior quality of care?:

The answer to this is, "not necessarily." In [research](#) conducted on over 750 hospital acquisitions or mergers, Deloitte analysed 28 quality measures and found that 20 of these measures remained unchanged in the hospitals after the M&A activity, while only 8 improved. Deloitte also conducted a survey of 90 hospital executives, and 49 (54%) of them stated that the new hospitals did, in fact, improve their quality of care. Interestingly, most of the hospitals with successful results reported allocating more time to the planning phase of how they were going to integrate and execute the transaction when compared with the hospitals which achieved underwhelming results. However, since these improvements exist in quite unique instances (e.g. more patients provided with beta blockers, fewer readmissions following knee or hip replacements, etc.), most patients won't even benefit from them. Moreover, in spite of these apparent improvements, however small they may be, it should be noted that patient satisfaction scores following the M&A activity actually went down slightly.

Conclusions:

The effects of M&A on the costs and quality of healthcare are, unfortunately, difficult to study. The data necessary for analysis are not easily accessible and, furthermore, it's also troublesome to confirm that trends are actually due to M&A as opposed to external factors, such as inflation. Regardless, as things stand currently, and despite what many of those pushing for increased M&A activity may claim, the evidence seems to strongly suggest that, in most cases, the patient has more to lose than to gain—at least financially—following M&A.

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