

FORTUNE FAVORS THE BOLD

COST AS AN INVESTMENT (NOT AN INCONVENIENCE)

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Cost takeout. Two dreaded words that often strike fear into the hearts of health system executives. Two words meaning the beginning of a painful exercise – one that’s time-consuming, demoralizing, and distracting – to identify wasteful spend. The continued pressure of margin compression unfortunately makes this distressing exercise necessary. Cost growth is outstripping reimbursement increases. Hospitals are quickly losing their center of gravity, as services migrate away from in-patient settings. These macro trends, along with other deleterious developments, show no sign of abating, forcing executives to take on the Sisyphean task of removing cost from their business.





Not all is doom and gloom, however. Cost, when viewed as an investment, means every choice becomes a strategic decision, rather than just another transaction. It means deciding where to put your money. When everything is on the table, you're forced to make the right trade-offs. Investments must align with the strategic direction, rather than on transaction-based efforts. A well-run health system puts its investment where its strategy is. Striking a balance between differentiating capabilities versus table stakes is critical. Even more important is deciding to discontinue investment in activities that don't add value. It's not unusual to see health systems with over 30 percent of investments in capabilities that don't add value.

We believe the imperative to take out costs represents an opportunity for health systems to sharpen their strategy and focus, and to redesign their core business processes. An effective cost takeout process does not merely improve margins; it is transformational and empowering, allowing an organization to chart its own course, instead of being pushed and pulled by broader market dynamics.

SHARPEN YOUR ORGANIZATION'S FOCUS

"FORTUNE FAVORS THE BOLD!"

"NECESSITY IS THE MOTHER OF INVENTION!"

We strongly believe all organizations should base their strategies on old proverbs. (Well, okay. Maybe don't construct strategy around old proverbs just yet, but those two are pretty good ones, right?) The point is, taking an incremental approach to cost takeout just leads to more of the same. Identifying two to five percent of spend as waste probably means you're optimizing the same processes and operating through the same business model. What if your objective was to take out 20 percent of costs? You'd then be forced to ask the tough questions of "What? Where? How? What clinical services should I focus on? Where would I deliver them? How do I redesign my business to deliver care in the most effective way?" This mindset requires you to define what differentiates your organization. Are such drastic changes necessary? No...if you are content with the status quo. The status quo, however, is unsustainable. A typical "healthy" health system has a margin of three to four percent. If reimbursement rates drop by five percent (not an unreasonable assumption), systems will quickly find themselves operating at a deficit. As a result, cost management and strategy should not be viewed as different activities. Business considerations that typically fall under the strategy umbrella, such as mergers and acquisitions, must be viewed through the lens of not only whether they support strategic imperatives but also whether they accelerate cost transformation. If not, you risk reinforcing internal processes and structures that will limit your ability to effect transformative change.

A SNAPSHOT OF CHANGE

As one example, OhioHealth, a not-for-profit health system based in Columbus, Ohio recognized hardened structural barriers were slowing its move to value. To remove meaningful cost from the system – and quickly – it partnered with ChenMed (a physician-led primary-care provider serving seniors) to run OhioHealth clinics. OhioHealth was now forced to become more

efficient by “handing over the keys” to a provider group more experienced in delivering value-based care.

“Models like ours are still somewhat unique because we are one of the few that actually get compensated for keeping people outside of the hospital and keeping them healthy,” Gaurov Dayal, MD, ChenMed’s Chief Growth Officer, said.³ “In most markets, we are working with a select group of plans. Our success is contingent on the ability to garner members with those plans. And likewise, the plans are working with them, and with us. One of their goals is to grow market share and get better outcomes and cost controls. There’s a lot of alignment on that, and we work very closely with plans in accomplishing that.”

As another example, Mount Sinai Health System is partnering with insurance startup Oscar to run the non-clinical components for one of its primary care clinics. That’s correct: A health system chose a payer to run administrative operations. Why? Mount Sinai realized new business models were necessary to drive significant, sustainable changes to its cost structure.

“We’ve had a lot of fun with Oscar, peeling back areas where we can say, ‘You know what? Just because traditionally one organization does ‘x’ or ‘y’ doesn’t mean we have to do it the same way in this arrangement,’” Niyum Gandhi, Executive Vice President and Chief Population Health Officer at Mount Sinai, said.⁴ “If we really want an outstanding experience that bridges clinical care delivery with health coverage, wellness, a yoga studio, or whatever else, let’s identify the jobs to be done and who’s best positioned to do them,” he added.

Both these examples underscore if you want a fundamentally different cost structure, you need to think differently about how you operate.

REDESIGN YOUR BUSINESS

Once you’ve made strategic decisions – in other words, clarified your organization’s identity and its points of differentiation – you must change how you work to sustainably take out cost and meaningfully impact your operating margin. This entails bringing health systems into a more modern era of business operations. It isn’t just about installing new information technology systems as a means to an end. Instead, it’s about realizing the full potential of “digital” – the set of process transformations enabled by a new era of big data, connectivity, and advanced analytics, like:

- **Simplifying and standardizing business processes.** Wholly eliminate activities once believed to be critical; evaluate the trade-off between standardization and customization.
- **Novel data and analytics to drive better decision making.** Provide recommendations for real-time decision making, built from integrated data sets.
- **New tools to engage constituents differently.** Skyrocket engagement and behavioral change with external and internal stakeholders.

BUT IT'S ALWAYS BEEN DONE THIS WAY...UNTIL NOW

Rejecting “business as usual” means embracing a new attitude about cost as a strategic investment, not as an inconvenience. Redesigning core processes requires a culture and talent model that supports your new focus. Some have compared large business organizations to tanker ships: slow to turn. Sure, it takes a long time to turn the wheel and change direction, but not just because of computers systems that don’t talk to each other and operating rooms that need updating. It’s also because of the people behind the wheel.

Unfortunately, businesses often realize the importance of people in driving change only after the fact, once outcomes have fallen short of expectations. What’s the secret to engaging people to accelerate change instead of stonewalling it? Well, there’s no single answer to that question. There have been thousands of frameworks and books written about behavior change. In our view – and experience – there are many approaches to making change possible and making it stick. But regardless of the approach, effective change boils down to aligning efforts against core processes, leaders’ conduct, rank-and-file behavior, and organizational incentives. Governance and change management – not organizational or hierarchical design – sparks change.

POSITIONED FOR IMPACT

Impact starts from the top down. The chief executive officer and senior management must be aligned on the path forward to successfully activate change across the organization. Providers are responsible for 80 cents of each dollar of US healthcare spend. This outsized impact underscores the opportunity facing the industry today. Again, do not disconnect cost management with strategy. Our perspective is that sustainability comes from transforming your business and doing things differently, so cost becomes an outcome versus an objective. When you evaluate merger and acquisition opportunities, ask yourself how it will help you achieve your strategic objectives and organization’s focus, and how it can help you redesign your business processes and operating model, and re-invigorate your culture. When you evaluate an innovative direct-to-employer product, or potential partnership with a plan, ask yourself these same questions.

May the odds be ever in your favor! (Oops, wrong proverb.) ... Fortune favors the bold!

KEY TAKEAWAYS

- Cost is an opportunity for every choice to become a strategic decision, not just another transaction.
- The imperative to remove costs will help health systems sharpen their strategies and focuses.
- Leaders must align efforts against core processes, conduct, rank-and-file behavior, and incentives.

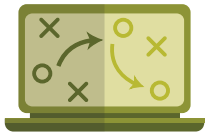
EXHIBIT 1. FOUR QUESTIONS TO SHIFT YOUR COST TAKEOUT MINDSET

**What's your organization's current cost reduction target?**

Have a number in mind? Great. Now triple it. Figure out what it would take to realize three times your current cost reduction goal. Gather together a diverse set of internal stakeholders to chart what needs to get done next to achieve "the impossible." When thoughtfully organized, this session isn't your typical throwaway brainstorm. It can transform your business.

**What benchmarks should you add... and take away?**

Benchmarks can be more of a hindrance than a help, as they often enforce the current way of doing business. In some cases, benchmarks mean striving towards mediocrity at best. Instead, consider what benchmarks you want to add – even if they seem only aspirational – from other industries. For example, consider the number of data scientists you employ. Or, the number of meetings and participants required when making a decision.

**Do you have a digital strategy?**

Digital strategy is no longer the concern of technology and marketing companies only. Every organization needs to think about how it can adopt digital tools and adapt to an ever-evolving digital landscape that maximizes impact and minimizes (unnecessary) internal disruption. Yep, you need an information technology strategy. And yep, you need a digital strategy. Some organizations (such as CVS, Walgreens, and others) have explicitly outlined digital strategies to create seamless consumer experiences across their online and physical stores. Companies like these are arguably better positioned to stand at healthcare's "new front door."

**Who's the "Chief Architect" of realizing your vision?**

Trick question! It should be everyone. It's essential leaders and managers collectively assume the role of "chief architect" and bring a vision to life. The activity flow that changes the organization is important and should be concurrent, always at work, and supported by as many people as possible throughout the organization. Empowering people across an organization to become "chief architects" depends on our prior three questions. Without clear, unambiguous benchmarks and a "North Star" to your digital strategy, people don't know where to go. As a result, change is slowed.