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## Hospitals pressured as insurers pursue more vertical integration



By [Alex Kacik](#)

Hospitals that don't adapt could get squeezed out of the care continuum as insurers grow and direct more care to lower-cost settings, according to an analysis from Moody's Investors Service.

Both [not-for-profit](#) and [for-profit](#) hospitals are feeling the pressure of falling inpatient volumes and reimbursement levels from government payers along with rising drug costs and labor expenses, as well as regulatory changes to policies like the 340B drug discount program.

Those downward pressures on margins will continue if insurers' plans to vertically integrate with providers come to fruition, the ratings agency said. The Medicare Payment Advisory Commission estimated that hospital margins could sink to negative 10% in 2017, a drop from negative 7.1% in 2015. Insurers have had to get creative since [regulators blocked](#) recent attempts to grow horizontally, including the thwarted mergers between Aetna and Humana, and Anthem and Cigna Corp. They now look to align with providers through proposed combinations between [CVS Health and Aetna](#), [UnitedHealth Group's Optum and DaVita Medical Group](#), and [Humana and Kindred Healthcare](#)—partnerships designed to prevent hospital visits through regular primary-care checkups and home healthcare.

Since they don't have to carry the hefty overhead of full-service hospitals, insurers that combine with physician groups and non-acute-care service providers can offer similar preventive, outpatient and post-acute care to their members at lower costs. Scale will also give them an upper hand in rate negotiations, denting providers' bottom lines.

The proposed deals could give insurers the power to direct care rather than doctors, said Juan Morado Jr., of counsel at law firm Benesch. But limiting patient choice is a

risky proposition, he added.

As insurers grow their physician networks, they will be better able to carve out "high-cost" hospitals or certain services from contracts, which will mean lower volume and revenue for hospitals, Moody's said. Optum, which has been on a physician-acquisition binge, could funnel more care to cheaper, risk-bearing hospitals. Also, [Anthem's](#) policy to limit coverage of emergency visits in certain states will mean fewer patient visits, lower revenue and higher bad-debt rates for hospitals, the report said.

#### Optum bulks up

Select provider acquisitions

Date announced/ closed	Organization	Provider type
Jan. 2011	WellMed	Physician group
Sept. 2011	Monarch HealthCare	Physician group
April 2015	MedExpress	Walk-in urgent care
Dec. 2015	ProHealth Physicians	Physician group
Jan. 2017	Surgical Care Affiliates	Ambulatory surgery centers
April 2017	American Health Network	Physician group
May 2017*	Reliant Medical Group	Physician group
Dec. 2017*	DaVita Medical Group	Physician group

\*Date announced, not closed

Source: Moody's Investors Service

But providers taking on more risk will be able to thrive, even with more competition, said Joseph Lupica, chairman of Newpoint Healthcare Advisors.

"Vertically integrated insurers will move health systems closer to full risk," he said.

The pending vertical integrations have caused health systems to explore adding insurance arms, similar to those run by Kaiser Permanente and Geisinger Health, which have been executed with varying success. Providers have also [added access points](#) in retail locations to broaden their referral networks and get patients to the appropriate care setting.

The CVS-Aetna deal "has made them stop and think—'Are we thinking broadly enough?'" said Gurpreet Singh, health services sector leader at consulting firm PricewaterhouseCoopers.


Investors at McGuireWoods' Healthcare and Life Sciences Private Equity & Finance Conference in Chicago last week said they are steering investment away from large acute-care health systems and instead focusing on urgent care, home health, micro-hospitals and other specialty inpatient facilities.

Private equity firm Corbel Capital Partners is focusing on dental and chronic care, drug compounders, substance abuse centers and physical therapy, and trying to "stay away from consolidated sectors," Brian Yoon, a principal at Corbel, said at the conference.

Hospitals will have to form a collaborative approach with the new entities to remain relevant, Benesch's Morado said. "Smart systems will look to solidify relationships early on and work with these groups because this is all coming out of the idea of preventative care. There are just some things you can't do at a health clinic."

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