

Wednesday June 9, 2010

## Prospect News Distressed Debt Daily

EVERY TRADING DAY, THIS NEWSLETTER BRINGS YOU:

- \* COMPREHENSIVE MARKET COVERAGE, WITH THE DAY'S EVENTS AND MAJOR MOVERS, ALL BACKED WITH PLENTY OF MARKET COLOR.
- \* DISTRESSED DEBT NEWS STORIES.
- \* COVERAGE OF COURT AND SEC FILINGS.
- \* DIP FACILITIES.
- \* CALENDAR OF BANKRUPTCY COURT EVENTS.
- \* TENDERS AND EXCHANGES.
- \* RATING ACTIONS.

### FOR MORE DETAILS

VISIT  
[www.prospectnews.com](http://www.prospectnews.com),

EMAIL  
[service@prospectnews.com](mailto:service@prospectnews.com)

OR CALL  
212 374 2800

## Prospect News

© Copyright 2010 by Prospect News Inc. Electronic redistribution, photocopying and any other electronic or mechanical reproduction is strictly prohibited without prior written approval by Prospect News. Information contained herein is provided by sources believed to be accurate and reliable, however, Prospect News makes no warranty, and each such source makes no warranty, either express or implied, as to any matter whatsoever, including but not limited to those of merchantability or fitness for a particular purpose.

# Health-care providers struggle to make ends meet, but solutions exist, experts say

By *Stephanie N. Rotondo*

Portland, Ore., June 8 – In these troubled times, players in the health-care arena – specifically, health-care providers, not insurance or medical device companies – are struggling as revenues and cash flows decline.

Hospitals and other providers of health-care services have seen reimbursements decline as state and local governments see wider deficits. With that, federal spending also gets cut, adding more pressure to the sector.

Additionally, leadership problems and business models are playing a role in distressed situations.

“The health-care provider industry is going through a period of unparalleled difficulty,” said Martin G. Bunin, a bankruptcy partner at Alston & Bird LLP and moderator of Turnaround Management Association’s webinar “The Health-Care Industry: Financial Distress, Solutions, Trends” held on Tuesday.

Bunin noted several statistics regarding distress in the health-care arena, such as that nine out of 10 providers have made cutbacks due to financial concerns and that seven out of 10 hospitals are seeing a decline in overall financial health.

“The level of financial distress is evident by the fact that it takes three slides to list the causes of today’s health-care distress,” Bunin remarked wryly.

But regardless of cause, there is some relief to be found for providers and investors alike.

### Declining reimbursements

One of the main factors contributing

to the distress of the health-care sector is revenue – that is, a lack of or decline in. This is compounded by a decline in government reimbursements, a key source of revenue for most providers.

“It’s no secret to many that the key sources of revenue come from two sources primarily: government and private payers,” said David Rock of Carl Marks Advisory Group LLC.

But as “states are essentially broke,” reimbursements from programs like Medicare and Medicaid are “continuing to show alarming decreases,” he said.

“Because of their dependency on [government reimbursement programs], health-care providers have fixed cash inflows that can be changed at any time by the government,” added Suzanne Koenig of SAK Management Services LLC. Every day, she said, you hear about hospitals getting their subsidies cut. “No other business has to rely so much on the government than health care,” she said, adding that U.S. health care is “more regulated than nuclear power.”

And, if a provider loses state funding, Koenig said, “they automatically lose a lot of federal-matched funds.”

As a result of this loss of revenue, “what we are seeing is hospitals making difficult choices in regards to cash flow,” Rock said. “Funding is focusing more on 13-week cash flows, that’s how tight it is.”

And in the bigger picture, declining revenues and cash flows will create big gaps in the coming years due to an aging baby boomer population.

“We know what is going to happen is 76 million baby boomers will begin to turn 65 beginning in 2011,” Rock said. “We will see a tremendous strain on the system,”

*Continued on page 2*

*Health-care providers struggle to make ends meet, but solutions exist, experts say**Continued from page 1*

given that those “65 and older tend to use health-care services three times more.”

### For-profit vs. not-for-profit

Still, losing government subsidies and revenues is something for-profit systems have been dealing with since the beginning. While for-profits nonetheless will suffer, it's not-for-profit systems that are really feeling the burn.

Not-for-profits, Koenig said, have historically had what she deemed “big war chests,” mostly from charitable contributions, that could be used for investments or capital expenditures. That excess cash typically resulted in “excess spending ... to fulfill a mission.

“[For-profits] don't have that excess cash, so they are more used to doing without,” she said.

In her view, not-for-profits “feel they can wait [to make important decisions] until the next meeting. There is not a lot of motivation to make immediate decisions.”

Given the current state of the economy, this lack of motivation is detrimental and could bring “a lot of restructurings and a lot of bankruptcies,” she said.

“It will be interesting to see if there is a change in the for-profit model,” Rock opined. “They may expand their role into what has traditionally been a not-for-profit area.”

### Management must focus

Whether for-profit or not-for-profit, leadership is also key in creating – or responding to – a distressed situation.

“The board either has to be focused on fundraising or on being a good corporate board,” said Andrew Turnbull of Houlihan Lokey.

Turnbull also noted that he believes both models can survive and turn around. However, if leadership on either side is “resting on their laurels,” then “that is a recipe for disaster.”

“Whether for-profit or not-for-profit, management/board seems to be a very key issue,” said Bunin. “One of the takeaways that I'm getting from this panel is that whatever the structure, management needs to get nimbler.”

### No single fix

In the end, “there is never a single strategy to turn around a distressed hospital,” Rock said.

Still, there are some avenues available to such businesses – and to investors looking to capitalize on the changes in the industry.

Health-care providers should first develop a strategic plan, Rock explained. That plan should then be amended and updated consistently to keep up with the changing environment, whether it be changes in demographics or changes in economics. For example, if the demographic of a community is largely made up of people in the later years in their lives, funding should be focused on care related mainly to that population. That means that services such as pediatrics and obstetrics can be cut, as there is not as much demand.

Other cuts should be looked at, but only in relation to quality of care. Supply costs – the most burdensome of the industry – is an area to look at, as are labor costs. As Rock pointed out, “unions are willing to make changes” to contracts, but they “want to know what the end game is.”

Rock also noted that any cuts – whether it be to staffing, supply or otherwise – could be temporary if a provider was able to turn itself around.

Consolidation and outsourcing are additional ways to create a more efficient cost structure. Turnbull pointed out that the sector is currently seeing a trend of outsourcing IT, billing and housekeeping, among other areas.

But what, then, does this mean for investors?

In essence, it means that investors should be looking at ways to capitalize on demographic changes. The baby boomer generation is an example of how to do this, as many of them are getting ready to hit retirement age within the next year, Turnbull suggested. Add to that the trend of increasing life expectancy, and areas like nursing-home providers and similar businesses could be a boon for investors.