



Valuation of Hospitals: Introduction

Hospitals are one of the key elements in the market for healthcare services in the U.S.,¹ both as a clinical provider and as an economic actor. Clinically, hospitals operate as one of the fundamental elements of the continuum of care, providing intensive services to patients with severe conditions, whose treatment requires a significant investment of time and resources. Economically, hospitals control a dominant portion of U.S. healthcare expenditures, with healthcare expenditures for hospital care expected to overtake healthcare expenditures for physician clinical services.²

Hospitals face multiple challenges, due to conditions in the competitive, reimbursement, regulatory, and technological environments in which these providers operate. Chief among these challenges is the rise in demand for healthcare services resulting from the aging of the Baby Boomer generation.³ Additionally, hospitals must continue to navigate increasing regulatory scrutiny in the realm of healthcare fraud and abuse. Further, the current state of the reimbursement environment for hospitals is marked by stagnant payments for inpatient services as well as the implementation of a number of programs that punish poor quality healthcare services with reduced payments (even in the wake of the COVID-19 pandemic, which decimated hospital finances), creating a setting in which hospitals must simultaneously provide high quality healthcare and control the costs associated with providing that healthcare in order to survive. Lastly, hospitals must find ways to compete with less traditional outpatient care settings (e.g., ambulatory surgery centers and urgent clinics), which patients find to be more convenient and payors find to be more cost efficient. To meet these challenges, hospitals may be able to leverage certain technological advancements in order to provide the high quality, efficient healthcare that is demanded by the modern healthcare industry.

There are various types of hospitals in the U.S.:

- Short-term acute care hospitals, which represent over half the nation's hospitals, specialize in the general, short-term treatment of patients;
- Academic medical centers (AMCs) are short-term acute care hospitals that educate healthcare providers in partnership with medical schools, with some AMCs conducting medical, academic, and human subject research, in addition to delivering a wide breadth of healthcare services;

- Specialty hospitals focus on certain medical conditions or patient population and offer a specialized subset of technology and skills. Examples of specialty hospitals include children's hospitals and psychiatric hospitals;
- Critical access hospitals (CAHs) provide healthcare services to underserved and rural communities. CAHs typically have fewer than 25 inpatient beds, a 24-hour emergency department (ED), and are located more than 35 miles away from the closest hospital;
- Rural emergency hospitals are small rural hospitals that maintain emergency outpatient hospital services in communities that may not have a CAH or other rural hospital;
- Federal hospitals are operated by government agencies, such as the Veteran's Administration (VA), Department of Defense (DOD), or the Department of Health and Human Services (HHS).⁴

Hospitals provide a variety of healthcare services, which can generally be categorized as either (1) inpatient care or (2) outpatient care. Inpatient care refers to those services that are furnished to patients who have been admitted by a physician's order to stay in the hospital, while outpatient care refers to observation services, ED services, many diagnostic services, and any other hospital services furnished to patients who have not been admitted to the hospital.⁵ In recent years, improvements in technology and medical practices have allowed many procedures that formerly required inpatient care to be performed on an outpatient basis, thus drawing attention to the distinction between inpatient and outpatient services.⁶ This distinction between inpatient and outpatient care may have a significant impact on a hospital's revenue, as hospitals typically receive higher reimbursement for inpatient care than outpatient care, even for patients with similar clinical needs.⁷

Inpatient hospital stays in the U.S. typically span 4.5 days, with average costs of over \$3,000 per day.⁸ Common services furnished during inpatient hospital stays include: (1) procedures associated with pregnancy, childbirth, and newborns; (2) orthopedic procedures; and (3) cardiovascular procedures.⁹

Outpatient hospital care is often provided in either a hospital outpatient department (HOPD) or hospital ED.

In 2021, the five most common primary outpatient diagnoses were:

- (1) Essential (primary) hypertension (3% of diagnoses);
- (2) Contact with and (suspected) exposure to COVID-19 (2.5% of diagnoses);
- (3) Other long term (current) drug therapy (1.4 % of diagnoses);
- (4) Hyperlipidemia, unspecified (1.1% of diagnoses); and
- (5) Type 2 diabetes mellitus without complications (1.0% of diagnoses).¹⁰

Comparatively, the reasons for visits (as defined by patients' own words) to hospital EDs are more varied, with the five most common reasons for ED visits accounting for less than one quarter of all visits to hospital EDs.¹¹ The top five most common reasons for visits to hospital EDs are:

- (1) Stomach and abdominal pain, cramps, and spasms (8.7% of visits);
- (2) Chest pain and related symptoms (5.3% of visits);
- (3) Fever (4.3% of visits);
- (4) Cough (3.6% of visits); and
- (5) Shortness of breath (2.9% of visits).¹²

Across all settings, elderly patients are the most frequent users of hospital services. Despite comprising approximately 18.64% of the total population,¹³

individuals age 65+ represent approximately: (1) 35.5% of inpatient stays; (2) 18% of visits to HOPDs; and, (3) 18% of visits to hospital EDs.¹⁴ For inpatient hospital stays, individuals age 65+ have the highest utilization per capita of all age groups.¹⁵ For HOPDs (as compared to ambulatory surgical centers), Medicare beneficiaries were more likely to be under age 65 or over age 85 and have higher medical acuity.¹⁶ Due to their relatively frequent use of inpatient hospital services, combined with the high cost of inpatient hospital stays, patients age 65+ may have a disproportionate impact on a hospital's revenue. As such, the aging of the Baby Boomer generation will likely have significant consequences for the hospital industry, although the ultimate impact on hospital revenue may depend on inpatient or outpatient classification trends.

In light of the current conditions of the U.S. healthcare delivery system, demand for hospital services may be driven by: (1) the number of individuals with private health insurance; (2) disposable income per capita; (3) funding for Medicare and Medicaid; and (4) the number of adults aged 65+.¹⁷ While there is significant demand for hospital services, competition from other facilities, such as ASCs, urgent care centers, and freestanding emergency departments (FSEDs), may lessen the role of hospitals going forward.¹⁸ The next installment of this five-part series will review the competitive environment in which hospitals operate.

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