consulting | technology | outsourcing

Insight Driven Health

Europe´s hospitals: An industry operating in the red

High performance. Delivered.

Benchmarking hospital finances

How financially secure is the hospital sector in your country? Most of us consider hospitals as vital parts of communities: while we appreciate that other organizations could shut doors, it's nearly unthinkable that hospitals would actually close or limit their services. But the reality is that many hospitals today are operating in the red – putting severe financial strains on national health systems.

Accenture analysis of more than 1,500 hospitals, accounting for about 30 % of the entire hospital market across nine major European economies, highlights this observation. By categorizing hospitals into low (green), medium (yellow) and high-risk (red) classes, based on how well they would be able to meet their financial commitments if a typical commercial creditworthiness review was applied. The resulting index, Accenture's European Hospital Rating Report (EHRR) shows the relative proportion of hospitals with a low, medium or high degree of risk, in terms of their probability of default (see figure 1).[1]

Accenture's EHRR findings indicate major financial issues. First, more than one in five (22 %) hospitals can be considered high risk, in terms of their probability of default. Simply put, these hospitals are entirely reliant on their funding body to guarantee their financial continuity. Second, nearly one in four (24 %) hospitals is rated in the yellow "increased risk" class: these organizations would ordinarily face challenges in borrowing, and only be able to do so with an increased cost of capital.

The problem is even more acute in some countries. In Portugal, nearly six in ten (59 %) hospitals are rated as "high risk". This kind of financial risk is not limited to financially stressed nations, but also wealthy ones. In Norway, for example, which faces none of the public sector debt risk that Portugal does, fully 41 % of hospitals are also considered at high risk of default.

Altogether, nearly one in two (46 %) hospitals in the study are currently at risk of defaulting on their financial commitments. This is in our opinion especially risky for countries trying to curb public spending: while Norway could in practice bail out its hospitals, administrators in Portugal face a much tougher test when seeking to invest in infrastructure or maintain care quality standards.

Many hospital executives point to the unique challenges of operating a fiscally sound service – not least as they face the issues of ageing societies, rising demand for health services and pressure to curb spending. Nevertheless, the two most fiscally secure hospital systems rated in Accenture's EHRR – Germany and Switzerland – show that it may be feasible to run financially sound hospitals, whether primary state-funded, or largely an insurer-funded model.

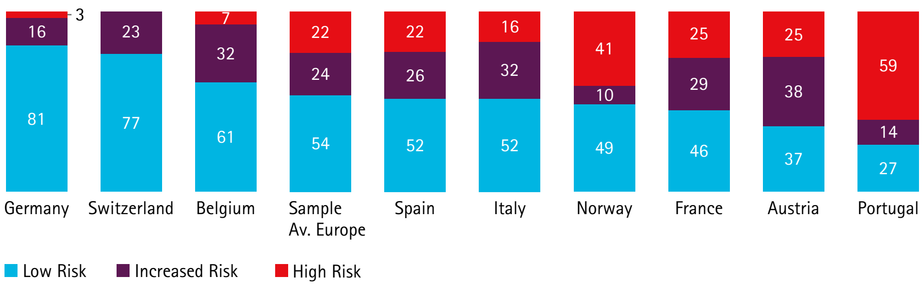
Internal finance risks

Furthermore, many hospitals simply do not balance their books: one in three (33 %) of those reviewed report an operating loss. This highlights an additional financing challenge: while hospitals with a high probability of default struggle to raise financing from external sources, such as bank loans, those with low or negative average earnings before interest, tax, depreciation and amortization (EBITDA) would be unable to finance investment through their operating cash flow.

One striking example is Austria: its operating costs as a proportion of revenue is better only than Portugal, generating average EBITDA margins of -4 % (see chart). Furthermore, just 37 % of Austrian hospitals receive a low-risk ranking in terms of their risk of default. Although the Austrian government would be unlikely to allow its hospitals to fail, the fact remains that many future investment planned by hospitals are likely to be reliant on state support.

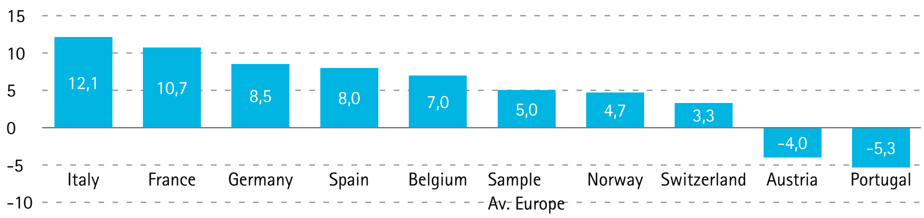
Other countries are stronger on one measure, while weaker on another. In France, for example, while average EBITDA margin is second highest of the ten countries overall, at 10.7 %, more than half of the country's hospitals are flagged up as either medium or high risk of default. It points to wider problems in these hospitals' balance sheets, with insufficient cash or equity on hand to cover deficits.

Figure 1: Accenture's European Hospital Rating Report: Proportion of hospitals potentially at risk



Source: Accenture European Hospital Rating Report, 2014

Figure 2: Internal finance risks: Average earnings margin per country (%)



Note: Earnings are shown as earnings before interest, tax, depreciation and amortization (EBITDA)
Source: Accenture European Hospital Rating Report, 2014

1 See appendix for full methodology of this index.

The gap widens: An urgent call for action

This research tries to highlight gaps not only across countries but also within them – between hospitals that are potentially financially secure, with all investment options open to them, and those that are financially fragile. Each country has clusters of these stronger hospitals, along with clusters of those that are at risk. Categorizing the top 25% and bottom 25% of all hospitals shows striking differences in performance: the top-performers face a negligible 0.2% probability of default, with average EBITDA margins of 8.4%. By contrast, the weakest 25% have a probability of default of 6.8%, with EBITDA margins of just 0.9%. Furthermore, the trend from 2008 to 2011 reveals that financially strong hospitals further strengthened their internal and external financing capabilities whereas the situation for financially fragile hospitals further aggravated revealing a widening gap between stable and fragile hospitals.

Figure 3: Internal vs external strength: Finance capability across the group

Internal Financing Capability

Internal Financing Capability	External Financing Capability –	External Financing Capability +
+	Reliant on cash flow: Hospitals in this group will likely have challenges raising loans, and thus are reliant on internal cash flow for investment. If margins were not sustained, it would be reliant on the national funding body.	Financially secure, all options available: Hospitals in this group will not have problems securing loans or raising money from cash flow for investment.
–	Financially fragile, state dependent: Hospitals here are highly dependent on their funding body – only able to survive, or invest, as long as the funding body or state provides financial aid.	Reliant on loans: Hospitals here will not have problems securing loans, but they are reliant on external finance for any planned investments (eg, improving efficiency).

External Financing Capability

Source: Accenture European Hospital Rating Report, 2014

If these discrepancies are not addressed, citizens within the same countries may face different standards of care over time—or risk losing nearby access to local hospitals. What is needed is a more robust, public debate about the right business models for operating hospitals, to set them on a more secure financial footing for the future.

Study methodology – Accenture European Hospital Rating Report

Accenture's European Hospital Rating Report (EHRR) draws on 2011 data of 1,522 financial statements from hospitals and trusts across nine countries, extracted from ORBIS database provided by Bureau van Dijk.

The analysis conducted by Accenture in collaboration with RWI (Rheinisch-Westfaelisches Institut für Wirtschafts-forschung) covers approximately 30% of the entire hospital market of the target countries reviewed in this study, including Austria, Belgium, France, Germany, Italy, Norway, Portugal, Spain and Switzerland. The sample comprises public and privately owned hospitals, yet does not claim to be representative for the two sectors. Please note that for Spain only private hospitals were considered, as P&L data for public hospitals is unavailable.

An Accenture classification model, adapted from the modeFinance MORE rating classes, provides an assessment of creditworthiness of these hospitals. This determines how well they can meet their financial commitments, based on a balance sheet and profit and loss analysis.

The analysis details two key measures: PD (Probability of Default), which implies the probability of an organization to default within a year; and EBITDA (Earnings Before Interest, Tax, Depreciation and Amortization) margin is used to approximate the organization's cash flow. PD gives a measure of the organization's ability to secure funding externally, while EBITDA margin shows its ability to reinvest and secure financing internally.

Insight Driven Health

Insight driven health is the foundation of more effective, efficient and affordable healthcare. That's why the world's leading healthcare providers and health plans choose Accenture for a wide range of insight driven health services that help them use knowledge in new ways—from the back office to the doctor's office. Our committed professionals combine real-world experience, business and clinical insights and innovative technologies to deliver the power of insight driven health.

For more information, visit:
www.accenture.com/insightdrivenhealth.

About Accenture

Accenture is a global management consulting, technology services and outsourcing company, with approximately 289,000 people serving clients in more than 120 countries. Combining unparalleled experience, comprehensive capabilities across all industries and business functions, and extensive research on the world's most successful companies, Accenture collaborates with clients to help them become high-performance businesses and governments. The company generated net revenues of US$28.6 billion for the fiscal year ended Aug. 31, 2013. Its home page is www.accenture.com.

For more information, please contact:
Dr. Sebastian Krolop
Managing Director,
Accenture Health Germany
sebastian.krolop@accenture.com