



Unit 5: Are hospitals a business like any other ?



4. Mergers and acquisitions in the hospital sector

- ➔ Hi! I'm Daniel Herrera. I am currently doing a postdoc in Hospinnomics so I research subjects like industrial organization, health and the environment usually looking at the interaction between these different topics. The objective of this video is to provide you with some insights about the different forms of cooperation that can occur between hospitals as well as to evaluate the potential impacts they may have.
- ➔ What different forms of cooperation can occur between hospitals? There are several ways that one or more hospitals can collaborate. Firstly, a collaboration can be verbal or non-verbal. This might correspond, for example, to an agreement between doctors when they use their professional networks to refer patients to another particular hospital. It could also be a hospital-to-hospital agreement. This is the case with maternity wards in France where, for example, in the event of a complication a patient will be transferred from a level-one maternity ward which handles pregnancies with a particular risk factor – rather, no risk factor – to a level-three maternity ward which is better suited to that specific patient. An alternative method of cooperation is technical cooperation. This mechanism seeks to develop or improve a hospital's performance. This type of cooperation can improve administrative, logistical, technical and even research activities. For example a group of hospitals purchasing and sharing expensive medical devices is a group of hospitals using this type of mechanism. In addition, this allows the movement of human capital between cooperating hospitals. Another strong form of cooperation is mergers and acquisitions. On the one hand, acquisitions can occur when a company assumes all the assets and liabilities of another company. The acquiring company retains its identity while the acquired company ceases to exist. On the other hand, mergers can occur when two companies agree to become a single entity. All the assets and liabilities of both are surrendered and will be transferred to this new entity in their place. So why do companies like to merge? Two companies will be involved in a merger or acquisition procedure if they hope to gain something. Usually this is monetary but it does not have to be. The most common reason is market power where the merger increases the market power of the non-merger companies by reducing competition. It could also be more efficient. Mergers can increase efficiency by realizing economies of scope which means producing several units at one single site or by realizing economies of scale which means producing one single unit in greater quantities. Other examples might be to avoid bankruptcy or even to diversify different sources of profits. So what are the different forms of mergers? The first is horizontal mergers defined as the union of two companies in the same market. An example is a merger between two hospitals or between two pharmaceutical companies. Horizontal mergers can benefit from both economies of scale and economies of scope but can often create negative effects through the elimination of competition in that specific market. It will give market power to all the companies that are left in the market. The second form of merger is vertical mergers or upstream-downstream integrations. This often involves a manufacturer and retailer merging into a single, silo-shaped entity. A vertical merger internalizes transactions between manufacturer and retailer so that the potential effects between the two of them are turned into a partnership. Unlike with a horizontal merger the number of competitors will not change. However, the behavior of the industry may change because the acquired company will stop dealing with other companies – it will only deal with its acquiring company. This raises concerns that vertical mergers may actually foreclose competitors by limiting access to either supply sources or patients.





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- ➔ What are the benefits and problems that arise from an acquisition? What are the benefits and problems that can arise from an acquisition in the hospital sector? On the one hand the benefits may be providing higher quality. Studies show a clear relationship between volumes and outcomes of surgical procedures. A merger may increase the volume of specialized services and this will improve their quality. Large hospitals may also be able to spread out the financial burden of high-cost investments such as electronic medical records. A merger may also contribute to cost savings. Care provision may be more efficient if one organization simply coordinates for all the other organizations in the chain of care for different patients. This is the rationale of Accountable Care Organizations in the US and the Territorial Hospital Groups developed in France in 2016. Mergers and acquisitions may be theoretically appealing but it's challenging to find clear empirical evidence. Some studies show that mergers lead to lower costs but this may require the integration of very large hospital systems which usually does not occur. Now, on the cost side, in systems where prices are negotiated, mergers may actually lead to price increases. Clearly, in a situation where a merger is in a large system the options of the pair are reduced and they will be unable to properly negotiate prices. In addition, mergers might also lead to less innovation due to lower competition. For example, there will be no investment in new protocols for post-surgical care because there are no alternatives for the patients. Or they will simply adopt new technologies that are similar to current ones. To conclude, when you consider any type of cooperation, both problems and benefits may arise. Care must therefore be taken when assessing the effects of cooperation in the hospital sector. Thank you very much for watching this video. I hope you liked it!

