

HS&S Strategy OUTLOOK

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Children's Hospital Building Boom: Will the Bubble Burst?

Children's hospitals are among the hottest growth areas in health care today. A recent survey by the National Association of Children's Hospitals and Related Institutions (NACHRI) identified over 100 capital projects totaling almost \$2 billion dollars at 41 of their member hospitals from 2001 to 2004. Health Strategies & Solutions, Inc., estimates that between \$7 and \$10 billion could be spent on the major children's hospital building projects completed, underway, or announced since 2000.

At first glance, pediatrics may seem an odd investment priority since the inpatient pediatric market is small and has been declining. The inpatient utilization rate per 1,000 population age 0 to 17 is one tenth that of the 65+ population. Nationally, 6.5 million children age 0 to-17 were discharged from inpatient facilities in 2002, a modest 1.6 percent increase from 1997. However, a 500,000 increase in normal newborn discharges from 1997 to 2002 masked an almost 10 percent decline in other pediatric inpatient activity over the same period.

Other factors that make pediatric investments seem less attractive include Medicaid as 45 percent of inpatient days at children's hospitals, a deficit of pediatric subspecialists, and higher infrastructure expenses associated with caring for pediatric patients, often without higher reimbursement rates.



Select Major Children's Hospital Building Projects 2000-2010

Hospital	Amount* Millions
St. Jude Children's Research Hospital (Memphis)	\$1,000
Children's Hospital of Philadelphia (Philadelphia)	\$650
University of Pittsburgh Medical Center (Pittsburgh)	\$475
Children's Hospital (Denver)	\$460
Children's Healthcare of Atlanta (Atlanta)	\$350
Texas Children's Hospital (Houston)	\$345
Children's Hospital of Los Angeles (Los Angeles)	\$340
All Children's Hospital (Tampa)	\$270
Children's Hospital and Regional Medical Center (Seattle)	\$230
Children's Medical Center of Central Texas (Austin)	\$175
Vanderbilt Children's Hospital (Nashville)	\$170
Columbus Children's Hospital (Columbus)	\$160
University of Chicago Comer Children's Hospital (Chicago)	\$130
Morgan Stanley Children's Hospital (New York)	\$120
The Children's Hospital at Montefiore (New York)	\$120
Children's Hospital (Boston)	\$110
Phoenix Children's Hospital (Phoenix)	\$105
Carolinas Medical Center (Charlotte)	\$85
Lucile Packard Children's Hospital and Santa Clara Valley Medical Center (San Jose)	\$75

*Figures have been rounded. Some represent multiple building or expansion projects.

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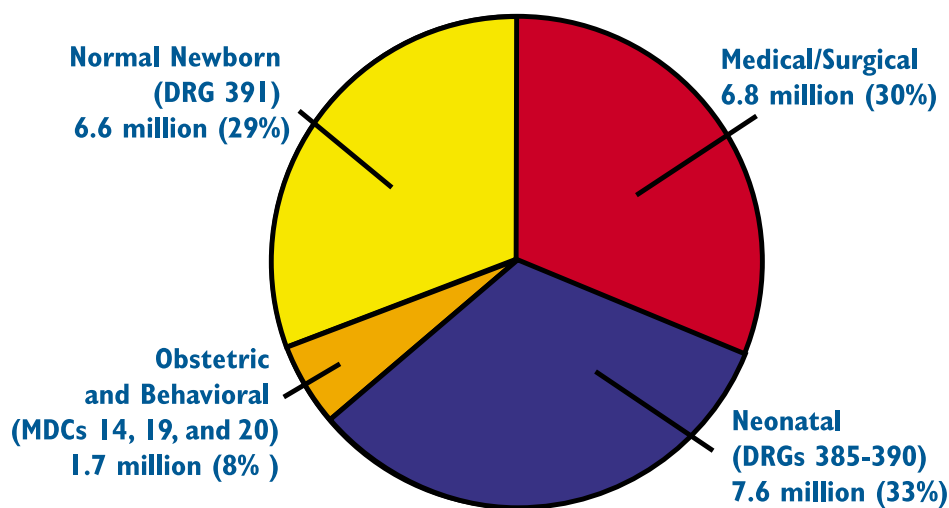
Despite a cloudy outlook, many see a silver lining. The much anticipated consolidation of the pediatric market is finally occurring. In the last decade, the 40+ freestanding general medical/surgical children's hospitals reporting data to the American Hospital Association gained over 50,000 incremental discharges. NACHRI estimates that children's hospitals (freestanding and hospitals-within-hospitals) already discharge approximately one million children annually, nearly one-third of the 3.4 million pediatric discharges nationwide (excluding normal newborns). The building boom should fuel children's hospitals' ability to capture an even larger proportion of the inpatient pediatric market.



OUTLOOK FOR 2010+

The price of entry for the children's hospital market increases with each new ambitious project announced, but the opportunity for incremental pediatric business remains. New hospital and major expansion projects announced to date should add 25 to 35 percent to children's hospital inpatient capacity nationwide. If these organizations can fully staff the incremental capacity, they should have little trouble filling the beds. Assuming consolidation continues to the point where 50 percent or more of pediatric discharges (excluding normal newborns) occur in the children's hospital setting, there may be room for an additional 10 to 20 percent increase in inpatient pediatric capacity nationwide.

U.S. Pediatric Inpatient Days, 2002



Source: Healthcare Cost and Utilization Project Agency for Healthcare Research and Quality, 2004

“.. There's a new brood of children's hospitals being built,..” (Modern Healthcare July 2004)

The outlook for a particular organization attempting to capitalize on a pediatric market share growth opportunity is mixed. Big winners and big losers among pediatric providers will emerge in the next decade.

Factors Fueling the Children's Hospital Building Boom

- Capacity constraints caused by volume growth
- Philanthropic opportunities and access to capital (excellent bond ratings)
- Community hospitals exiting the pediatric market
- Concentration of limited pediatric subspecialty care resources
- Systems with sufficient critical mass to get in the game
- Design considerations (safety and security, family-centered facilities)

• **Market Leaders:** Today's market leaders are in for the long haul. They will continue to invest and become even more dominant, limiting growth potential for competitors in nearby communities.

• **Serious Investors:** Those willing to risk a big investment in the next few years could be successful consolidators by pulling market share from struggling pediatric programs across their region. Exceptions include markets with insufficient population base and locations with clearly dominant market leaders already present.

• **Fence Sitters:** Those who adopt a wait and see posture will watch their business erode to market leaders and serious investors. Even worse, those who try to be in the business half-way will end up watching their subsidy of pediatric services mushroom out of control. Pediatrics is not a business for dabblers.

“Children’s Hospitals Maintain Credit Strength During Growth Spurt” (Moody’s Investor Services September 2004)

If the children’s hospital building boom continues at the current pace for much longer, the risk of overbuilding intensifies. There is definitely room for some new serious investors, especially in mid-sized metropolitan areas without a full-fledged children’s hospital and in larger metropolitan areas with a children’s hospital that is recognized as good, but not outstanding. Growing areas such as Denver, Phoenix, and their outlying suburbs are also emerging as vast opportunities for pediatric providers; however, the window of opportunity is narrowing. It is time to decide — invest or watch as others take advantage of opportunities.

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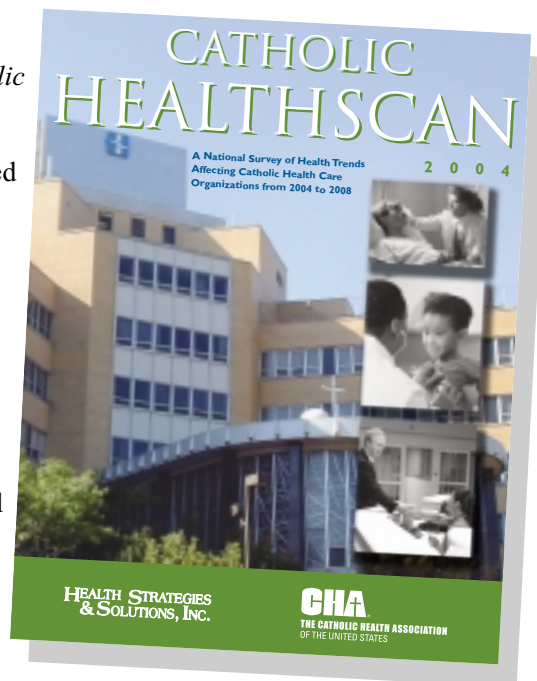


HS&S and The Catholic Health Association Publish Report on Trends Affecting Catholic Providers

Catholic Healthscan 2004: A National Survey of Health Trends Affecting Catholic Health Care Organizations from 2004-2008 is a new report copublished by the Catholic Health Association of the United States (CHA) and Health Strategies & Solutions. In January 2004, the two organizations conducted a survey that was sent to each CHA member hospital and system to identify the most important issues affecting Catholic hospitals in the United States.

The report presents the survey results and analysis for key issues in five general categories: economic/financial, legislative/regulatory, physician/staffing, capital needs/growth, and Catholic specific. Financial challenges top the list of concerns among survey respondents, followed by the close second concern of physician relations and competition from physicians. Other topics discussed in the report include workforce shortages, mission commitments, and ethical issues.

The report concludes that the next five years will be pivotal for Catholic providers, with closures and consolidations inevitable as hospitals and systems adapt to the financial realities. Issues such as the medical liability crisis, the growing uninsured population, quality and safety standards, physician-



hospital relationships, and ethical developments will need to be addressed by Catholic providers.

To order a copy of *Catholic Healthscan*, call 314-253-3458 or visit www.chausa.org/resources. The reports are \$10 each for CHA members and \$20 each for nonmembers. For additional information about trends affecting Catholic providers, please contact Alan Zuckerman at 215-636-3500, ext. 106 or azuckerman@hss-inc.com.

Off the Press

Recent Articles



“Progress Review: Essential to Keeping Your Plan on Track,” by Alan Zuckerman, October issue of *Healthcare Financial Management*

“Minimizing Costly Medical Staff Subsidies,” by Jennifer Jones Etkin and Alan Zuckerman, October issue of *Managing the Margin*

“Effective Demand Forecasting,” by Hugo Finarelli and Tracy Johnson, November issue of *Healthcare Financial Management*

“To Divest or Not Divest? That is (sometimes) the Question,” by Alan Zuckerman, December issue of *Healthcare Financial Management*

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On the Dais

Upcoming Presentations



American College of Healthcare Executives

Alan Zuckerman: "Strategic Planning: From Formulation to Action," December 16-17 in Orlando and January 24-25 in Breckenridge, CO

Healthcare Council, National Capital Area

Keith Pryor: "The Governance Committee," December 8 in Washington, D.C.

Major Catholic Health Alliance

Alan Zuckerman: "Catholic Healthscan 2004," January 14 in Sanibel Island, FL.

Connecticut Hospital Association Health Care Leadership Summit

Alan Zuckerman: "Competing on Excellence: Healthcare Strategies for a Consumer-Driven Market," January 21 in Wallingford, CT.



Above l to r: Robert Hill, Christine Markham, Keith Pryor, Tracy Johnson, Craig Holm, Alan Zuckerman and Hugo Finarelli

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Health Strategies & Solutions, Inc., is a national management consulting firm dedicated to helping organizations discover innovative strategies and

solutions for today's complex health care challenges. Our staff has enabled hundreds of health care organizations across the country to address complex issues, make decisions that achieve lasting results, and set courses for success.

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