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Private capital transformed health care—outside NY

While the city's health industry undergoes a transformation that brings consolidation and bankruptcy, health care executives argued at Crain's health care conference Thursday that private capital could strengthen the city's health system.

BY IRINA IVANOVA

Adam Blumenthal's work in health care started with a laundry service.

In 2008, the founder and managing partner of Blue Wolf Capital Partners bought two failing laundries from Chicago hospitals. Three years later, Blue Wolf was able to sell the resulting company, Healthcare Laundry Services, to a national operator, after increasing its volume by 70%, while union employment grew by half and prices dropped 5%.

Mr. Blumenthal used the laundry story, part of his keynote address at a Crain's health care conference Thursday morning, as an example of the potential private capital can have to transform the industry.

"Taking things over from hospitals and doing them in a simpler way creates the potential for savings," he said.

Private equity capital has long been off-limits for hospitals in New York, where the law prohibits corporations from owning hospitals. This year, Gov. Andrew Cuomo proposed a pilot program to allowed private equity investment in hospitals, but it failed to get traction in the Assembly.

But some hospitals are finding a way to work with private capital. Blue Wolf Capital Partners formed a partnership with the Brooklyn Hospital Center to bid for Long Island College Hospital. Though they didn't win the bid, the partnership will continue.

"The underlying economics, the microeconomics in Brooklyn and the macroeconomics in the [health care] industry continue to demand capital," said Mr. Blumenthal. "New York's hospital infrastructure is weak."

His solution is to move to a network of outpatient care sites—the model Blue Wolf and Brooklyn Hospital proposed in their bid for LICH. He touted models like CityMD, an urgent care chain backed by private equity that "does an extraordinary job."

Dan Moen, chairman of Plano, Texas-based LHM Hospital Group, offered a similar model of privately-financed health care. LHM is owned by CCMP Capital Advisors and finances not-for-profit hospitals exclusively. It runs 36 hospitals nationwide, including in Hackensack, N.J.

Mr. Moen's solution for a failing hospital, and the number-one user for LHM's capital, is to connect it to a regional health care network, Mr. Moen said. LHM also makes sure the partner has at least a 20% stake in the venture—enough "skin in the game" to be make sound decisions and be invested in the outcome.

And while New York's struggling hospitals often face an unfavorable payer mix, treating many patients who are uninsured or on Medicaid, which pays less than private insurers for care, there's still money to be made by treating the poor and disadvantaged, said Eric Klein, a partner at the law firm Sheppard Mullin Richter & Hampton.

"If you redesign your hospital for Medicaid patients, you can be very profitable," he said, citing three hospitals that, after restructuring, earned $70 million in before-tax earnings in three years.

In the meantime, hospitals will need to look to the state for financing. The recently passed budget includes a $1.2 billion capital financing program, said Paul Williams, chief executive of the Dormitory Authority of the State of New York, which provides bond financing for schools and health care systems. DASNY could help speed up the state Department of Health approval process, he said—saving millions in construction costs.

But continued state financing for hospitals isn't permanent, said Al Aboud, chief financial officer for East Orange General Hospital in New Jersey.

"State coffers are virtually empty, especially in the northeast," Mr. Aboud said. "We have to run the hospital like a business. If we say, 'Oh gee, making money is a bad thing,' we'll get to the point where we cannot continue."