

Managing in a Downturn

How Do You Manage in a Global Financial Recession?

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As we write this column, global and local financial trends threaten to radically alter the world as we know it. Across the Atlantic Ocean, European countries face a debt crisis and the collapse of the euro. Here at home, the federal government amasses unsustainable federal deficits exceeding a trillion dollars per year. State budgets are severely out of balance as tax revenues decline while committed costs, including retiree pension and health benefits, continue to rise. In Massachusetts, for example, some municipal employees who retire after age 55 with at least 10 years of service are eligible for “free” healthcare benefits for life.

These trends affect your institution, and healthcare leaders must be prepared to respond. As leaders consider the right course of action, they will find it helpful to understand how the financial world reached its current state.

On a Monday morning in March 2008, we woke up to the news that the federal government, by way of the Federal Reserve Bank of New York, had arranged an emergency loan to Bear Stearns in hopes of preventing a market crash. It seemed to be an anomaly, reminiscent of the successful 1979 government bailout of Chrysler Corporation. That \$1.5 billion government loan guarantee stabilized the too-big-to-fail, Big Three automobile manufacturer. In the 1990s, the government took similar action to rescue the failing savings and loan industry.

As spring wore on, it became clear that the Bear Stearns package was not a silver bullet solution. Evidence of the problem continued to pile up, and more government bailouts followed. Fannie Mae and Freddie Mac received a weekend bailout from the Federal Reserve and the Treasury, complete with a government guarantee to cover their losses for three years, with no upper limit on the coverage. Two of the Big Three automakers hit bottom and filed for bankruptcy. The prepackaged bankruptcy of General Motors, established in 1908 and once the largest corporation in America, was a sentinel event for all who remembered the expression, “As GM goes, so goes the country.”

America had led the world into a major recession. Anyone who owned a home, a 401(k) plan, or stock was suddenly a lot poorer, at least on paper. As the freefall continued, the federal government quickly developed and deployed the massive Troubled Asset Relief Program (TARP), sending some \$700 billion in relief funds to

the financial industry. A total collapse was averted, but the effects of the financial downturn remain, with January 2010 unemployment levels at 9.7 percent, or double the 2007 rate.

In December 2008, Bernie Madoff's empire and other Ponzi schemes unraveled, devastating many foundations and charities, particularly in the Northeast. The ripple effects severely impacted recipients of their grants and commitments, including many hospitals.

With credit markets drying up, unemployment rising, consumer confidence eroding, and employee morale shaken, healthcare system executives had their hands full. The combined result of the turmoil made the old adage "cash is king" truer than ever. As consumers pulled back and individuals lost health insurance, hospitals experienced losses in volume for elective, nonemergent healthcare. Financial operating results suffered. Meanwhile, losses in investment values eliminated the safety net reserves created by nonoperating income. Many hospitals and healthcare systems were forced to consider or enact layoffs and postpone or cancel capital-intensive projects. All were required to rethink their strategic plans.

None of us had direct training or experience in leading healthcare organizations on the brink of what felt like the next Great Depression. Whether we had 30 years of experience or had graduated after 2000, none of us had navigated a storm of this magnitude. Previous crises, including the dot-com bust and Y2K fears, suddenly seemed like the good old days. The challenges facing healthcare leaders seemed analogous to the prospects for college graduating classes: significantly more difficult in 2010 than in 2000.

To meet the challenges of an unknown financial environment and to lead through a financial downturn, we needed to get back to the basics. We needed to refocus on short-term financial projections, cash flow projections, conserving cash, lots of communication to financial institution partners, and even more communication with our staff. By late 2008, seven key financial principles required attention and action (PriceWaterhouseCoopers 2009):

1. Develop and maintain a robust financial forecast.
2. Identify key forecast risks and develop appropriate responses.
3. Protect and ensure adequate sources of liquidity.
4. Drive efficiency in working capital processes.
5. Aggressively manage costs.
6. Exercise discipline in capital investments.
7. Assess and monitor credit exposures throughout the value chain.

At Froedtert & Community Health, a regional hospital system made up of an academic medical center affiliated with the Medical College of Wisconsin, two community hospitals, and a multispecialty medical group, everyone knew someone in the community who had lost his or her job. Negative rumors about companies and institutions ran rampant through the community. Nationally, the retail, manufactur-

ing, and housing industries were being devastated, while healthcare joined government and education as better, more stable industries. But it became clear that no industry was immune in this “falling tide lowers all boats” environment, as health providers around the country began to experience layoffs.

Communication became critical. Managers and staff needed straight talk to maintain perspective on the challenges and the changing environment. Solid information and two-way communication were essential to keeping managers and staff informed, focused on the work at hand, and proactive about identifying and implementing solutions. Effective messaging required an independent, empowered leadership team. At Froedtert & Community Health, the leadership team was built around these core principles (Petasnick 2008):

1. Focus on people and develop them.
2. Give your management team the latitude to make decisions.
3. Hold people accountable for results.
4. Never lose track of your core mission.
5. Do not let process get in the way of meeting your vision.

These principles positioned the team well for the task ahead. The leadership team immediately went back to the drawing board, meeting regularly to recraft our immediate strategic priorities around three core strategies:

1. Reduce exposure to complex growth strategies.
2. Focus on operational improvement to take waste out of the system and achieve operational efficiencies.
3. Strengthen our balance sheet to preserve our ability to access capital when the debt markets reopened.

Once the revised strategic framework was defined, the Froedtert & Community Health leadership team put into place a series of immediate action steps to preserve our cash, including

- imposing a freeze on all salaries;
- consolidating and strengthening our supply chain infrastructure to achieve significant economies of scale through standardization, including physician preference items;
- strengthening our operational improvement infrastructure to take advantage of Lean improvement methods to reduce variations at every level of our health system;
- actively engaging each operational entity to improve efficiency and reduce marginal programs and service lines to achieve predetermined budget targets; and
- aggressively consolidating key support functions such as HR, Finance, Supply Chain Management, and IT at the health system level.

Throughout all this our priority was on retaining our staff. Talented people provide an indisputable competitive advantage, and the best organizations focus on retention of key individuals and identification of recruitment opportunities. At a time when many organizations were reducing their training and development budgets, Froedtert & Community Health did the opposite. A unified system approach to organizational and leadership development was created to support staff mobility and enhance teamwork. Excellent staff contribute to patient satisfaction and create opportunities to capture new business.

Effective workforce planning and development continue to be critically important. Healthcare systems must develop teams made up of the right number of staff members with the right capabilities. Healthcare organizations are challenged to recruit the right talent while keeping expenses in check; both elements are critical to maintaining a healthy balance.

Perhaps the greatest challenge any health system faces today is effectively aligning their physician partners. In the current economic climate, new solutions are needed to meet this challenge. Physicians have also been dramatically affected by the downturn, personally and professionally. Practices are faced with declining reimbursement and increasing demands for significant investments in IT, EHR, and other infrastructure. These financial pressures have changed the market, making physicians more open to opportunities to sell their practices, consider direct employment, or otherwise align their practices more closely with hospitals. This dynamic creates options that can expedite the launch or implementation of strategic initiatives.

Meanwhile, hospitals and healthcare systems have fewer resources to support acquisition of physician practices and physicians' employment. Froedtert & Community Health began to explore alternatives and developed a pluralistic portfolio of strategies to provide physicians with new options. These included the development of a new independent physician association (IPA), backed with system support but led independently with a unique governance model. Other strategies sought to enhance community access and create new opportunities for specialty physicians by establishing practices in new geographies and identifying ways for system physician partners to complement and support each other. These strategies represent a start; new options will continue to develop and evolve in the changing market.

Froedtert & Community Health hopes that the pluralistic options will create an environment where physicians and hospitals align more closely, leading to a more integrated healthcare delivery system. An integrated system will be better positioned to compete in the healthcare marketplace, offer an attractive product to insurers and others, and respond to changes that are sure to accompany healthcare system reform.

Dr. Jim Mongan, the retiring CEO of Partners HealthCare in Boston, recently published a book entitled *Chaos and Organization in Health Care*. Jim and his coauthor, Dr. Thomas Lee, offer a prognosis about the daunting challenges we face in reforming today's health system. His assessment of the current situation is that the problem is chaos, the solution is organization, and the question is how to get there. This book and the ideas and writings of many other healthcare thought leaders

underscore the magnitude and urgency of the challenges healthcare leaders must address. There is no question that rising to the challenge will require the courage to address the tough issues and to lead organizations to where they need to go. Staying the course and staying put are not viable options. The times call for courage and perseverance. Again, the problem is chaos, the solution is organization, and the path to that solution is strong leadership.

The current financial situation is the new normal. Unemployment may fall to 8 percent, but 2007 levels will not return anytime soon. Since all parties are experiencing cost pressures, especially federal and state governments (the source of the majority of hospital revenues), the future looks cloudy for organizations that are not cost and quality leaders. To establish themselves as leaders, organizations will need to proactively manage their financial position, communicate with and engage an empowered staff and leadership team, recruit and retain key staff, partner effectively with physicians, and remain vigilant in the exploration of new opportunities. Perhaps most important, organizations and leaders must plan carefully without losing sight of the need to be flexible and responsive to the dynamic environment.

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For more information on the concepts in this column, please contact Mr. Goldberg at agoldberg@aboutams.com.