



# **CAPITAL INVESTMENTS IN HEALTHCARE – EUROPEAN PERSPECTIVES AND TRENDS**

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# You need three things to win a war (and to run a hospital)



1. Money
2. Money
3. (lot of) Money





# Content



1. Capital investments
2. Capital investments in insurance sector
3. Capital investments in hospital sector
4. The role of profit in health care
5. Creating an investor friendly environment in Slovakia
6. Conclusions

# 1. Capital investment

Parameter	Public Capital	Private Capital
Goal	Declared „societal“ values	Profit and Dividends
Criteria for decisions	Lobbying Absence of alternative costs	IRR ROE
Vision	Shortterm	Longterm
Decision-making	Beaurocratic No corporate governance	Flexible Corporate governance
Risks	Ineffective allocation of scarce sources Higher costs Corruption	Needs stewardship



# Criteria for decisions

<b>Return on Equity (ROE)</b>	earnings before extraordinary items, less preferred-share dividends, divided by average common <u>shareholders' equity</u> . Shows the rate of return on the <u>investment</u> for the company's common shareholders, the only providers of <u>capital</u> who do not have a fixed return	8%-12%  Above 20% is considered as very good
<b>Internal rate of return (IRR)</b>	<u>discount rate</u> that gives a <u>net present value</u> (NPV) of zero. The NPV is calculated from an annualized <u>cash flow</u> by <u>discounting</u> all future amounts to the present.	Differs by sector  Above 30% is considered as very good

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## 2. Capital investments in insurance sector

Trends:

- 2A. Developed market in private (supplementary) health insurance
- 2B. Pioneers in the market of for-profit social health insurance

## 2A. Private (supplementary) health insurance

Country	Coverage of population in %	year
France	92,0%	2000
Japan	80,0%	2003
Canada	65,0%	2000
Belgium	57,5%	2000
Ireland	43,8%	2000
Denmark	28,0%	1998
Germany	18,2%	2000
Italy	15,6%	1999
Portugal	14,8%	2000
Spain	13,0%	2000
UK	10,0%	2000
Finland	10,0%	2000

**Source: OECD Private Health Insurance in OECD Countries, 2004**

# 2A. Supplementary insurance – as % of total health expenditures

Country	Share of supplementary Health Insurance as % of total health expenditures
Belgium Germany Israel Netherlands	< 5%
Austria	7%
France Switzerland	10 – 13%

*Source: Comité Européen des Assurances 2000; Vektis 2000; Verband der privaten Krankenversicherung e. V. 2000c; Gross 2001.*

*Source: Colombo 2001; OECD 2003*

*Source: OECD 2003*



# The market structure of supplementary PHI

Country	For-profit Insurers as % of total insurers
Belgium France Israel	Around 25%
Austria	Almost 100%
Germany Netherlands	Around 50%

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## 2B. For-Profit oriented social health insurance

Profit oriented social health insurance

Pioneers:

- 2005 – Slovakia
- 2006 – Netherlands
- 2007 – Poland (?)

## 2B. Why for-profit orientation in social health insurance



- Motivation
- Hard budgetary constraints
- Sustainability of public finances
- Solvency criteria
- Efficient purchasing (market cleaning)
- Innovations
- Lower Risk aversion
- No political pushes



# Slovakia



- For-profit oriented Health Insurance Companies
- Initial capital SKK 100.0 million (EUR 2.8 million)
- Strong supervision by Health Market Authority
- Regular reporting
- Corporate governance (standard bodies)
- Solvency criteria (3% of prescribed premiums)
- External Audit
- Transformation of current 5 HIC from public funds to joint stock companies
- Open market for investors
- After 10 years of deficits as public funds, last year all HIC in Profit



# Netherlands

- The Health insurance system will be operated by private health insurance companies
- They are allowed to make profits and pay dividends to shareholders
- HIC are regulated by Pensions and Insurance Supervisory Authority
- Both existing social health insurance funds and private insurance companies can operate health insurance policies under the Health Insurance Act
- New insurers can also enter the market



# Poland



- Decentralization of NFZ (National Health Fund)
- Into 5 independent national health funds
- Allow establishment of private health funds (permission from Health Insurance Supervision Commission and they have to be joint-stock companies)
- Initial capital PLN 15.0 million (EUR 3.8 million)

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## 3. Why for-profit oriented capital in hospital sector?

- Rapid increase of capital possible
  - Reconstruction
  - Green fields
  - Technology
- Sound investment schemes
- New structure of products
- Innovations
- Mergers, eating up older competitors
- Freedom over inputs (assets, wages, technology, ...)
- The function of profit is crucial for sound asset improvement



# Private capital in selected countries

Country	% private	year
Belgium	100%	2004
Denmark	100%	2004
Nederlands	90%	2003
Spain	61%	2003
Italy	39%	2003
France	35%	2004
Slovakia	32%	2006
Austria	28%	2001
Portugal	25%	2003
Ireland	20%	2001
Poland	10%	2003
Germany	8%	2001
Finland	7%	2004
UK	5%	2004

Source: World Health Organization 2004, on behalf of the European Observatory on Health Systems and Policies

Polish Private Hospitals Association



# Rise of private capital

<b>in Poland</b>	<b>1980</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>
<b>% of private hospitals</b>	2%	2%	5%	10%
<b># of private hospitals</b>	17	18	38	78

<b>in Germany</b>	<b>1990</b>	<b>2002</b>
<b>% of private hospitals</b>	3.7%	8.3%
<b>% of not-for-profit</b>	33.5%	37.7%

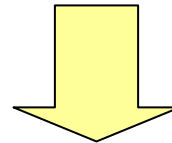
# Why in many countries the share of private capital is low (Government failures 1)

- Cost and value of capital are ignored, thus removing any incentive to manage assets efficiently.
- Generally revenue and capital funding streams are separated
- Ignored opportunity cost of capital
- Payment mechanisms do not cover ammortization
- Direct discrimination of private hospitals



# Government failures 2

- Political control
- Over-regulation
- Alibism
- ESA 95



**Hybrids**



# Hybrids

	Ownership	Public	Private
Management			
Public		Government owned and managed Public sector autonomous hospital Public not for profit hospital	Hybrid Privately owned and publicly managed hospitals (PFI)
Private		Hybrid Publically owned but privately managed hospital (PPP)	Private not for profit hospitals Privately owned and managed

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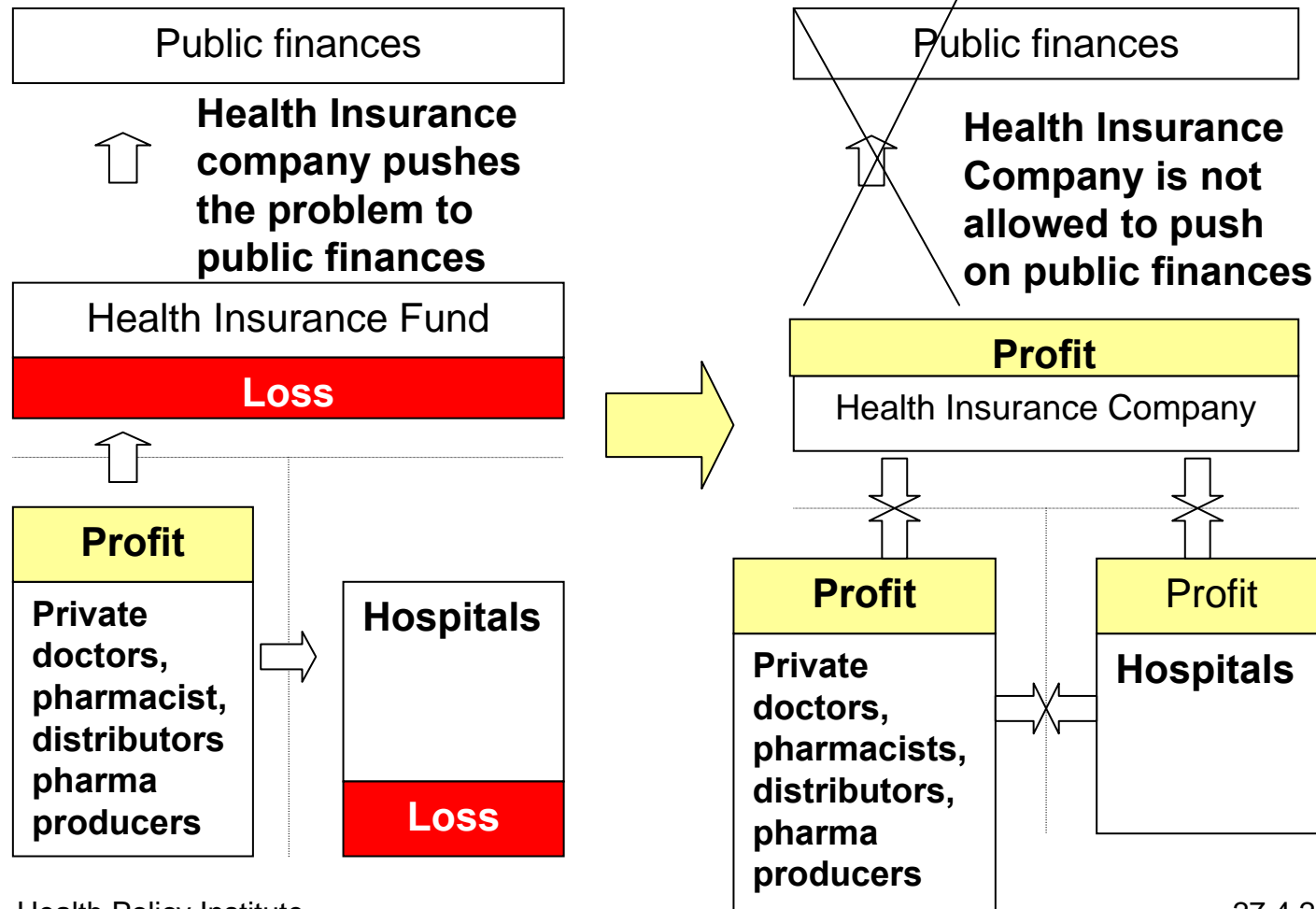
## 4. The role of profit

- Profit guarantees improvement of assets, otherwise assets deteriorate
- When the profit is not allowed by law, parafinancial mechanisms occur
  - Corruption
  - Hiding of the profit – into costs (no benchmarking possible)
- Balancing the motivations

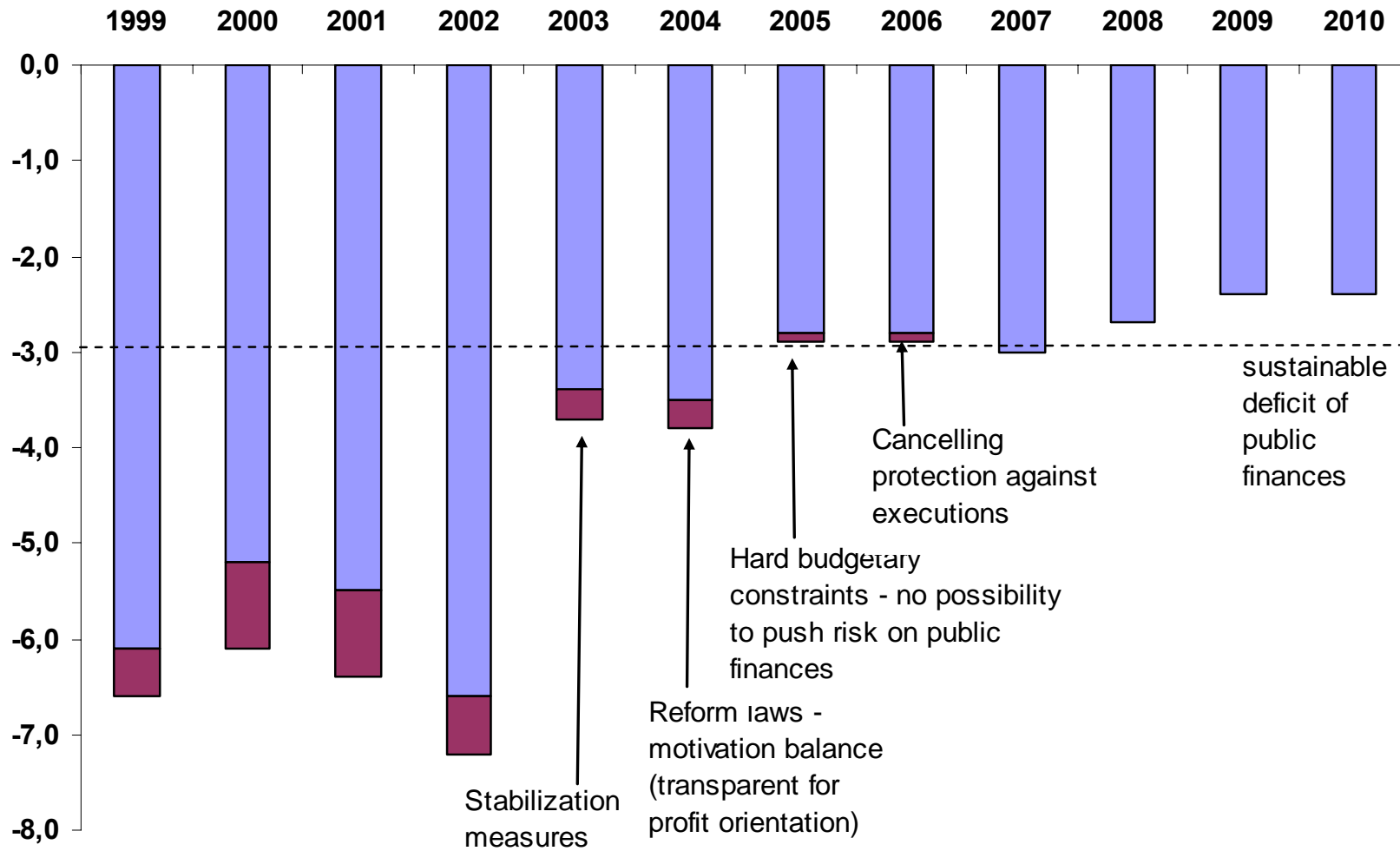
# 5. Slovakia - creating an investor friendly environment

1994 - 2004

2005 -



# Health reform stabilizes public finances





## 6. Conclusions

- Governments tend to:
  - Have political control over healthcare
  - Over-regulate healthcare
  - Be very alibistic
  - Like investing and hiding deficits





# Market friendly health policy should



- Abolish double streaming
- Include amortization into the payment mechanisms
- Minimize political „alibism“ and allow private investors operate on the market
- Allow profit function in the whole health-care sector
- Prefer clear and transparent ownership and legal subjectivity
- Minimalize the creations of hybrids
- Prefer corporate governance also in publicly owned hospitals
- Create free market entry and standard economic environment
- Act as a **wise** regulator, not as an insurer or producer



# Outlook

- More market friendly environments across Europe
- Recession phase – elimination of ineffective investments (infrastructure, technology)
- International private for-profit hospital chains across countries
- Local vertical integration within one country (Private hospital chain establishes a private insurance company and enacts supply chain)
- International vertical integration



# Thank you for your kind attention



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