

FEATURES

Do Market Opportunities Remain in Outpatient Imaging?

BY RICH PAULK AND M. SHANE FOREMAN

Attractive opportunities remain in outpatient imaging, but they are highly market specific

In the post-Deficit Reduction Act (DRA) era, many current and would-be imaging providers are left with the same fundamental and related questions: Do market opportunities remain in outpatient imaging? If so, how do we assess and capture these opportunities? The answers to these questions tend to be market specific and require an in-depth understanding of your local market's dynamics.

In recent years, imaging utilization has increased dramatically, driven by new technology, new applications of existing technology, demographic shifts (such as the graying of the baby-boom generation), and new market entrants seeking a historically strong return on investment for imaging services.

To meet this demand and capitalize on perceived opportunities, market participants have responded in a number of ways, from the advent of entrepreneur-owned, single-modality, freestanding imaging centers to the introduction of physician-practice-based advanced imaging services to the creation of hospital-owned and/or specialist-owned multimodality imaging centers. Payor responses to this increasing demand and the associated escalating costs are also contributing to volatility in this market space.

At 10% of the total health care dollar, imaging costs have officially captured the attention of both governmental and commercial payors. The DRA eliminated the long-standing favorable Medicare reimbursement for freestanding imaging centers (versus provider-based centers), especially for MRI services.

Commercial payors have responded to rising imaging costs through increased use of radiology benefit management companies and a stronger focus on network management. Moreover, the DRA has had a negative downstream impact on commercial contracts that were reimbursed at a percentage of Medicare rates.





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—Rich Paulk

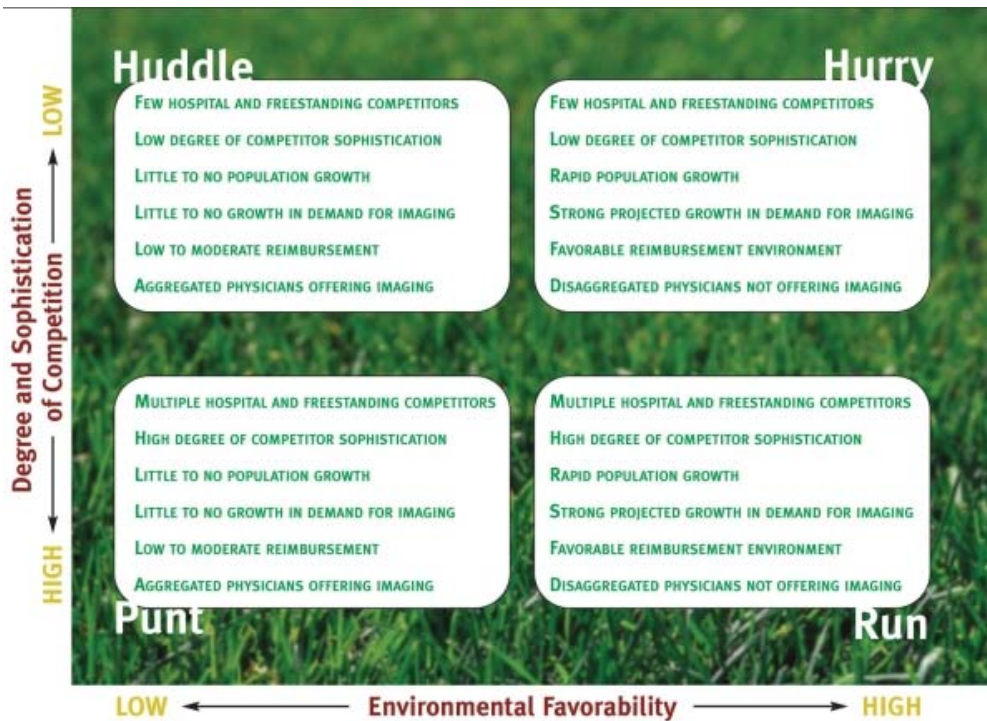
The collision of ever-increasing demand for imaging (and its concomitant costs) with payor actions to stem this tide has caused chaos in most local markets. The degree to which payor reactions have affected providers varies by type of facility. The DRA and recent commercial payors' actions primarily have been directed against IDTFs.

Many historically strong freestanding imaging providers have found themselves in real economic distress as a result. In contrast, provider-based (hospital-owned) facilities were left virtually unscathed by the DRA. Further, many hospitals have the market clout to extend their hospital-based reimbursement rates to their off-campus imaging facilities.

Pregame Strategy

Against this backdrop, you may be wondering what, if any, imaging opportunities exist in your local market and what strategies you should pursue as you attempt to capture them. To help you sort through the relevant issues, identifying the kind of market in which you live and operate is a useful first step. For the purposes of this discussion, a football analogy is useful.

The current outpatient imaging center environment can be divided into four categories based on environmental favorability and the degree and sophistication of the competition. Two critical dimensions to consider when identifying your market type are the favorability of the local environment and the degree and sophistication of the competition in the market. The figure identifies four market types: punt, huddle, hurry, and run.



Using a football analogy, the current outpatient imaging center environment can be divided into four categories based on environmental favorability and the degree of sophistication of the competition.

The punt market type in the lower left quadrant is characterized by low overall population growth and demand for imaging, a high degree and sophistication of hospital and freestanding competition, and a tight reimbursement environment. Physicians within this market type typically are well organized and are working in groups of sufficient size to enable them to offer high-end imaging services (MRI, CT, and PET/CT) within their practices.

A typical punt market contains multiple hospitals and freestanding centers. Hospitals own and operate freestanding centers; elective outpatient volume is not generally mingled with inpatient and emergency patient volume. The number of imaging centers per 100,000 of population is above 1.7 (the national median). Existing providers within the market have proven operational models, and annual population growth is below 1% per year, with annual projected growth in demand for imaging in the low single digits. Average imaging reimbursement is below 180% of Medicare rates. Multiple physician offices are offering MRI and/or CT.

The huddle market type in the upper left quadrant is also characterized by lower overall population growth and demand for imaging, but has a lower degree of imaging provider competition and sophistication with low to moderate reimbursement. Physicians within this market type may be well organized and working in groups of sufficient size to enable them to offer high-end imaging services within their practices.

The huddle market includes a limited number of hospitals and freestanding centers, and hospital competitors do not own and operate freestanding centers. There are fewer than 1.7 imaging centers per 100,000 of population; existing providers within the market have less-than-ideal operational models. The annual population-growth rate is less than 1% per year, with annual projected growth in demand for imaging in the low single digits. Average imaging reimbursement is less than 180% of Medicare reimbursement, and multiple physician offices offer MRI and/or CT.

Hurry markets are the most attractive (or, at least, provide the prospect of the largest returns) and are typified by strong overall population growth and growth in demand for imaging, a low degree and sophistication of hospital and freestanding competition, and favorable reimbursement. Ideally, physicians within this market type are disaggregated and are not working in groups of sufficient size to make offering high-end imaging services within their practices economically feasible.

The typical hurry market contains a limited number of hospitals and freestanding centers. Hospital competitors do not own and operate freestanding centers, and there are fewer than 1.7 imaging centers per 100,000 people. Existing providers within the market have suboptimal operational models. Annual population growth is more than 1% per year, and the annual projected growth in demand for imaging is in the high single digits or low double digits. The average imaging reimbursement is more than 180% of the Medicare rate, and there are no physician offices offering MRI and/or CT.

Run markets, with strong overall population growth and increasing demand for imaging, a high degree and sophistication of hospital and freestanding competition, and favorable reimbursement, are attractive, but there is little margin for error. Physicians in this market type may be disaggregated and are, therefore, economically prevented from offering high-end imaging services within their practices.

Run markets have multiple hospitals and freestanding centers. Hospitals own and operate freestanding centers, and elective outpatient volume is not generally mingled with inpatient and emergency patient volume. There are more than 1.7 imaging centers per 100,000 people, and existing providers have proven operational models. Annual population growth is above 1% per year. Annual projected growth in demand for imaging is in the high single digits or low double digits, and average imaging reimbursement is above 180% of Medicare rates. Few physician offices offer MRI and/or CT.

Strategic Options

Once you have determined the type of market in which you live and operate, the next step is to determine the range of strategic options available to you. The range of options varies based on whether you are an existing provider or a new market entrant and whether your facility is freestanding or provider based.

As the name suggests, there are likely to be very limited opportunities for capturing profitable, incremental imaging market share in the punt market. For existing providers, the appropriate course of action is to forego investment in incremental imaging capacity. Any market-share gains are likely to yield marginal profits and have to come at an existing provider's expense, and changing historic referral patterns in order to capture these volumes can be very tough.

If an existing hospital provider has access to preferred reimbursement, it might make sense to purchase an existing freestanding facility and convert it to a provider-based center. Existing freestanding centers must focus on maintaining their imaging volumes and, to the extent that they intend to grow their businesses, on capturing competitors' volume. They should also be mindful of the need to have a ready exit strategy, should environmental or competitive factors worsen. For new market entrants, staying clear of the punt market is likely to be the best strategy.

In the huddle market, cannibalization of existing imaging volumes and duplication of imaging investments are the primary concerns of existing providers considering opening new imaging centers. To the extent that an existing provider wants to increase its market presence—perhaps at the periphery of its service area, to mitigate cannibalization and duplication concerns—it probably makes sense to huddle (or partner) with existing providers in any new service offering, potentially including bringing in physicians as capital partners. The new market entrants best positioned to launch an imaging venture in this type of market are well-organized physicians with a group large enough to support a new venture.



The hurry market presents an opportunity to grow market share meaningfully for the fleet and nimble provider.

— M. Shane Foreman

The hurry market presents an opportunity to grow market share meaningfully for the fleet and nimble provider. In these markets, providers, whether established or new, have the most freedom relative to how to go to market, whether alone or in partnership with others. Moving quickly, however, is of paramount importance. Others will probably perceive the same opportunities, and this market type can become saturated quickly.

Existing providers in the run market can advance their franchises by keeping pace with the growing market. For these existing providers, the challenge, at a minimum, is to maintain market share. For both established providers and new market entrants, paying especially close attention to execution—such as providing excellent customer service to both patients and referring physicians, staying current with technology investments, and maintaining and upgrading the physical plant—can provide an opportunity to grow or establish the business, with volume increasing at a rate greater than the rate of growth in the market.

In summary, potential outpatient imaging opportunities still exist and largely hinge on the type of market you operate in and how well positioned you are as an organization. Existing providers, particularly those with access to provider-based reimbursement, have a real advantage in the short to medium term. New market entrants still have opportunities in some markets, but will need to be diligent in pursuing those strategies. The question for you is who will attempt to capture these opportunities in your market. We hope that the answer is that you will.

Rich Paulk is a principal of 3d Health Inc, Chicago, a company specializing in outpatient strategy, development, and management. M. Shane Foreman is a principal and founder of the company.