Modern Healthcare

A Dignity-CHI Deal Could Create National System with Scale and Savvy

October 25, 2016

If talks between Dignity Health and Catholic Health Initiatives bring them together, the union would deliver complementary geography and potential cost savings. And it could tap Dignity's knack for savvy joint ventures to tackle some of CHI's challenges.

Dignity's 39 hospitals are concentrated in California, with a handful in Arizona and Nevada. Catholic Health Initiatives, meantime, has a strong presence in the center of the country, including Arkansas, Colorado, Kansas, Minnesota and Nebraska.

"They have almost no overlap," said Gregory Hagood, senior managing director and head of investment banking at SOLIC Capital.

That geographic diversity should make for smooth sailing if an agreement triggers antitrust review, which recently has tripped up several regional systems looking to consolidate.

Dignity, which is based in San Francisco, also owns U.S. HealthWorks, a network of more than 200 urgent-care centers and occupational health sites in 20 states. The subsidiary delivered $477 million in revenue in the 12 months ended Sept. 30, 2015, according to an investor presentation in January.

The national scale of a combined system, Hagood said, could help with insurance negotiations and the costs of supplies and critical information technology.

Englewood, Colo.-based CHI, though its debt has surged to 110% of equity, is the nation's third-largest not-for-profit hospital company with annual revenue of about $15.2 billion. It operates 103 hospitals. Dignity, the nation's sixth-largest not-for-profit hospital company, would add $12.4 billion of revenue to the mix.

Together, CHI and Dignity would surpass Ascension ($20.5 billion in revenue) as the largest not-for-profit hospital company and trail only Kaiser Permanente, which generates an outsize portion of its industry-leading $60.7 billion in revenue through its managed-care plan.

Under a merger, they would have an opportunity to reduce management duplication at the highest levels in administration, finance and human resources. The cost savings would be substantial, Hagood said.

And Dignity's fresh set of eyes on some of CHI's stickier operating challenges, especially in Kentucky and Texas, might help improve results, Hagood said.

In July, Fitch Rating said losses in those markets contributed to its decision to lower CHI's credit rating by three notches to BBB+ from A+ with a negative outlook. CHI also is looking to unwind and sell off health plans after losing nearly $100 million on the venture.

Overall, CHI posted a net loss of $568.1 million in the first nine months of its fiscal 2016, which began July 1, 2015.

Dignity also has been innovative with its use of joint ventures to expand its footprint and continuum of care in its markets. The system has opened more than two dozen ambulatory surgery centers in joint ventures with United Surgical Partners International, sharing the capital risk and profits for the facilities. USPI is now majority-owned by Tenet Healthcare Corp., an investor-owned hospital chain based in Dallas.

Dignity is also a joint-venture partner with Tenet and Ascension in three-hospital Carondelet Health Network in Tucson, Ariz. Its other joint ventures include partnerships with private equity-backed GoHealth Urgent Care and Emerus, a for-profit developer of so-called micro-hospitals.

Dignity also has launched a precision medicine initiative with CHI and owns a revenue-cycle-management company with UnitedHealth Group subsidiary Optum called Optum360. CHI, meanwhile, owns a minority stake in Tenet's revenue-cycle-management company, Conifer Health Solutions.

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