

# Hospitals to Boost Spending, A Move That May Hurt Profits

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Hospitals plan to boost capital spending by 14% annually over the next five years, a new survey shows, a move that could squeeze many hospital systems' already thin profits.

Roughly three-quarters of the 460 U.S. hospitals surveyed said they expected to increase capital investment over the next several years. The big spending plans mark a turnaround from austere times: Hit by money-borrowing troubles in the late 1990s, hospitals increased capital spending by just 1% a year between 1997 and 2001.

After years of little or no capital investment increases, hospitals say they have no choice but to spend more now on buying new technologies, such as computerized physician order-entry systems, and expanding emergency and operating room space. Nearly half of the hospital chief financial officers surveyed said their facilities are deteriorating and depreciating faster than they can make improvements. Large teaching hospitals in particular say they need to spend more to keep and recruit top-flight physicians.

The survey was conducted by the Health Financial Management Association, an association of health-care financial executives, with GE Healthcare Financial Services, a unit of General Electric Co. that provides financing for medical investments.

The pressure to increase capital investment may divide hospitals more sharply between those that can and can't access enough capital to make the improvements. Hospitals with strong balance sheets will be able to tap the capital markets with bond issues to finance their investments. Those that don't will have to seek philanthropic or other resources, or face pressure on profits. The median profit margin in hospitals is about 2.6%, according to the Health Financial Management Association.

"A significant number of hospitals don't have access to traditional sources of financing and have to be creative," said Randy Fuller, a manager with GE Healthcare Financial Services.

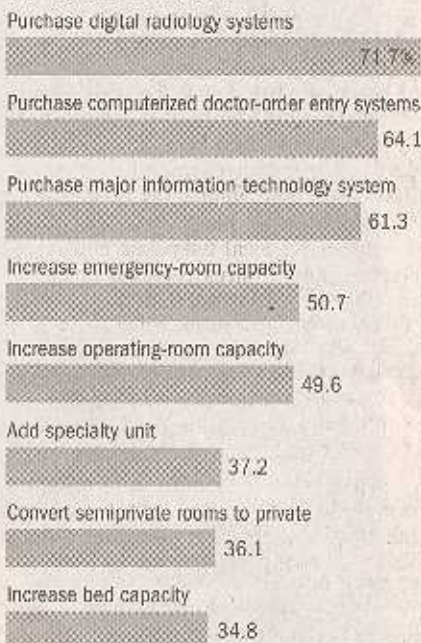
Some hospitals with market clout also have been able to negotiate price increases with health insurers and improve their finances in recent years, though not all hospitals have benefited and the trend may have leveled off recently.

Pressure to expand is being felt by hospitals in states with swelling elderly populations, including Florida, California and Colorado. The number of uninsured is putting additional pressure on hospitals.

But if hospitals fulfill their spending plans, that might trigger a short-term surplus of medical services in some mar-

## Money to Spend

Hospitals surveyed said they will invest capital over the next five years to...



Sources: GE Healthcare Financial Services; Healthcare Financial Management Association.

kets. When that happens, hospitals often try to drive more utilization, which can result in sometimes unnecessary tests or procedures, contributing to higher health-care spending.

"There could be a period of overcapacity until there is a more acute ramp-up in demand," said Maryanne Hennessey, hospital analyst at Criterion Research Group.

Some hospital executives say the new spending plans are a rebound from the managed-care era of the 1990s. During that time, new health plans helped create a shift to more outpatient services, and so hospitals were faced with a glut of beds. That shift leveled off "just as we were seeing the effect of the graying of America," said Roy Santarella, chief financial officer of Stanford Hospital and Clinics in Palo Alto, Calif.

Stanford, which spent only about \$20 million in capital improvements during the last few years, will boost its spending to between \$50 million and \$60 million a year between 2005 and 2007, Mr. Santarella said. This year it is spending even more after opening a \$187 million cancer center earlier this week.

New technology is the biggest area where hospitals see a need to invest. More than 60% of hospitals said they planned to buy computerized physician order-entry systems. Nearly three-quarters of hospitals say they also plan to buy costly digital radiology systems, which store, retrieve and display medical images in digital format.