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Innovative Financing Frontiers: Nontraditional Investment Models and Partnerships

About the authors: *Bill Laughlin, Bill Siren, and Simon Gisby are leaders within Deloitte's Health Care Strategy practice. This editorial represents perspectives on how health care leaders can respond to increasing financial constraints via non-traditional models and partnerships to drive innovation and margin growth.*

Introduction

Historically, innovation within the U.S. health care industry has been stifled by financial constraints, particularly for not-for-profit organizations that lack access to significant equity capital. With budgets pre-allocated to standard operating needs, health care organizations are not left with much capital to invest in innovation. Yet, many health care leaders are inspired to access alternative sources of capital, investments, and partnerships to achieve margin growth and innovation goals.

Current Financial Constraints in Health Care and Rising Inflation

Labor accounts for a large percentage of a health care organization's budget. According to the AHA, labor costs, which include costs associated with recruiting and retaining employed staff, benefits, and incentives, account for more than 50% of hospitals' total expenses. Beyond labor, costs of goods have been hitting record highs due to inflation, with about 20% of hospital costs going towards medical supplies.[1] In light of these financial constraints, CSOs must partner with their CFOs and other executive leaders to leverage external financing to support their corporate strategy and innovation goals.

Strategies for Revenue Diversification

In the face of these financial challenges, it's critical that health care organizations explore new ways to stabilize their financial future. One such approach is diversifying revenue streams, which can not only enhance financial stability but also create new opportunities for innovation and growth. Strategies for revenue diversification can be understood through three broad categories – investment, innovation, and commercialization – each aimed at supplementing low core business margins with higher profits from additional services.

1) Investment

The first strategy is investment in early-stage companies with the goal of scaling and profiting from dividends or sales. For instance, several payers and retailers have entered into joint ventures or acquisitions to operate value-based primary care clinics for Medicare patients.

2) Innovation

The second strategy relies on innovation, specifically leveraging internally developed Intellectual Property (IP) and monetizing it through external partnerships. In the health care sector, innovation can involve introducing new or significantly improved solutions for increased efficiency, quality of care, or access to services.

3) Commercialization

The third category is commercialization, which involves selling core business competencies where there is excess capacity and scalability. In the health care context, commercialization could include implementing a new technology or method of treatment, often involving partnerships or capital raising to support these efforts.

Pursuing Partnerships for Revenue Diversification

Navigating the complex terrain of revenue diversification can seem daunting, yet the outcomes can be compelling. By forging strategic partnerships and alliances, health care organizations can tap into a wealth of resources and expertise, driving innovation and financial growth. It is through this lens of collaborative growth and innovation that we examine the power of partnerships in the health care sector.

Partnering with external organizations can unlock significant opportunities for revenue diversification. Such collaborations can drive substantial innovation while effectively managing associated costs and risks. The breadth of expertise needed to compete in today's health care landscape may be beyond the reach of many organizations, making alliances and partnerships a more feasible route for building capabilities.[3]

Certain capabilities, like Generative AI, may be too resource-intensive to develop from scratch. Thus, marrying patient engagement and marketplace trust with third-party capital and talent can open intriguing partnership opportunities. For instance, Microsoft's $10 billion investment in OpenAI, the creator of ChatGPT, demonstrates the potential scale of such collaborations.[2]

In addition to facilitating innovation, partnerships offer access to specialized expertise, speed and efficiency, risk mitigation, cost savings, competitive advantages, and assistance with regulatory compliance. These benefits make partnerships a compelling strategy for health care organizations seeking revenue diversification.

Continuing Innovation in the Face of Financing Challenges

While partnerships offer a compelling strategy for revenue diversification, it is important for health care organizations to continue to innovate and adapt to financing challenges to remain competitive and achieve their goals. Innovation must become a habit in an organization. It is important to start with a thesis on where to invest strategically and have the discipline to 'say no' to certain investments. For example, venture capital communities deploy rigorous investment strategies because they can effectively recognize that while capital is liquid, the right talent, use case, and application are rare. Health care organizations can learn from this practice and decide strategically where to invest, not just to gain capital returns, but because the innovation has a positive impact on the organization.

Action-Oriented Key Takeaways

Having explored the dynamics of financial constraints, the power of innovation, and the potential of strategic partnerships, we now turn our attention to actionable insights.

1. ***Diversification of Revenue***
   "To determine the optimal proportion of each revenue stream for margin improvement and mission advancement, providers and health systems must gauge the organization's appetite for strategic risk and diversification."[11] Health care organizations should consider how to leverage their existing embedded services and solutions in the marketplace to diversify margins.
2. ***Partnering with Third Parties***
   Health systems can offer their tangible and intangible resources, such as patient engagement and trust, to third-party capital and talent to fund transformation. With health systems' existing assets and notable ability to test new products, access to third-party capital and knowledge can open the door to new, creative innovations.

In tandem with diversifying revenue streams and establishing strategic alliances, health care organizations can assess their appetite for strategic risk and diversification, capitalize on existing resources, and partner with third-party talent and capital to transform financial limitations into catalysts for innovation and ultimately advance their mission in health care.

Please reach out to Bill Siren, Bill Laughlin, or Simon Gisby with any questions.

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