



## Practice Management and Economics: Defining the Healthcare Market — A Critical Precursor to Your Strategic Plan

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*"My views are fluid, and are subject to change as circumstances change."*

*Winston Churchill*

Most hospitals undertake an annual strategic planning process. Medical practices also plan, but less frequently. In fact, sometimes medical practices erroneously depend on a hospital market analysis for their planning. This paper serves as an opportunity to review key concepts in developing an analysis of a "market".

Often a market analysis is a key component of the strategic plan. A detailed market analysis assists in identifying utilization rates, projecting future volume, assessing competitive position, developing an actual marketing plan, and is a vital component when researching potential new services/locations. While considerable time, thought, and effort goes into the analysis of various data components, one key component of the market analysis is often overlooked — defining the actual market.

**The Hospital Service Area.** The grouping of counties or zip codes into areas or "markets" is vital in market analysis. Such groupings enable advanced analysis on a rolled up basis. Often hospitals define

primary, secondary, and (sometimes) tertiary service areas for use in market analysis. Such areas are often defined based on patient origin (the percentage of discharges a hospital received from a particular area in relation to the hospital's overall discharges), market share (the percentage of discharges a hospital receives from a particular area in relation to the overall discharges generated in the area), or a combination of both factors. However, is a service area really a market? If you walked up to the average person on the street and asked them where they live, would they respond "in the primary service area for hospital X"?

In general, hospital service areas have nothing in common with the way people identify themselves as a community or "market" (an especially important point for clinical practices to remember). Consider a map displaying a primary and secondary service area for a particular hospital. The service areas will usually look like a "bulls eye" with the primary service area being at the center and subsequent service areas radiating out in rings. The secondary market area is often 50+ miles across with a large hole in the middle (the primary service area). Look at the area on a map and ask yourself what do the people on one end of this service area have in common with those on the other end? Often the age mix of the population, household income, and travel patterns will be quite different. More importantly, if competitor hospitals are displayed on the map, you will note that often the hospitals in the area make no sense as a grouping. While this would not seem like a large problem, think of the purpose of creating an area or market. It allows you to examine data such as population, household income, market share, and utilization (inpatient days and discharges per 1,000) on a rolled up basis. Take marketshare as an example, if you examined a hospital on the edge of the secondary service area and then split the area in half you would probably find that the hospital's market share on the half of the "donut" is relatively high while their marketshare on the other side of the donut is rather low. This is because your service area is specific to your hospital. However, in

general, it will not be a good grouping to analyze competing hospital's marketshare. If your competitor has a 75% marketshare on one side of the "donut" and a 25% marketshare on the other side, is it accurate to roll everything up and look at an overall marketshare of 50%?

In general, the use of service area definitions for market analysis purposes is only useful in limited circumstances, mainly for rural independent hospitals with little or no competition. Interestingly enough, these are the same circumstances where a detailed market analysis is of limited usefulness since competition and outreach are in many cases irrelevant. When one or more of the following conditions apply, an alternative to service area definitions is suggested:

- 1) The hospital or practice is located in a metropolitan area;
- 2) The hospital or practice is part of a system or network with multiple hospitals in the same area;
- 3) The hospital or practice faces significant competition (3 or more major competitors);
- 4) Service areas would cross state lines and the availability of data differs;
- 5) There are extreme differences in demographics and/or travel patterns of residents within the service area(s).

**What Is A Market?** In most instances, the development of market definitions for use in the market analysis is preferred to a service area approach. Markets are also defined by grouping zip codes or counties but unlike service areas they are NOT dependent on the patient origin or marketshare of any one particular hospital. Rather, a healthcare market can be defined by consumer behavior/preferences, demographics, use rates, natural and manmade barriers, and travel patterns.

**Defining The Market.** The most important part of defining the market is to constantly look at things from a consumer/patient perspective, not from hospital perspective.

The first step is to determine the outer boundaries of the total area to be examined, or the "overall market area". For a local multi-hospital system or large independent

provider a good start is to examine the entire MSA (Metropolitan Statistical Area) in which the provider is located. While it may be that your hospital(s) or practice does not currently pull from across the entire MSA it is usually the case that with the appropriate strategies, relationships (including medical staff and affiliate hospitals), and marketing in place, patients within the MSA will travel to your hospital or practice.

After a draft of the entire market area has been established, basic analysis should take place to verify the appropriateness of the selection. Out migration, should be at a minimum for services provided within the market area (10% or less out migration is a good rule of thumb for metropolitan areas). Next examine the overall patient origin for the hospitals within the market area. In general the overall market should represent 80% or more of the discharges for hospitals within the area. If this is not the case, further analysis should ensue to identify additional areas to include. Often "feeder" areas along a highway outside the MSA may be the source of immigration. If so, these area(s) may also be appropriate to include in the overall market. (Note: it may not be reasonable to consider extremely large regional providers or specialty providers, e.g. pediatric providers, when applying the 80% patient origin guideline. These providers typically pull patients from a multi state or even national basis. In these cases it is best to define the local market for these providers even if it only represents 50–70% of their patient base. Very large referral markets can be defined to analyze outreach efforts.) Finally, examine the marketshare of hospitals within the overall market. While there may be one or two large regional centers or specialty providers outside the market area that have a significant marketshare, if there are multiple general acute care facilities outside the market area that have a marketshare presence, the overall market definition should be reconsidered.

It is usually the case that an overall MSA or large group of counties within a metropolitan area will be too large to analyze as a single area. Once the overall market has been defined, individual markets or "sub markets" within the area should be

identified. If you talk to people who have lived in the area for any significant amount of time, they should be able to provide guidance in the grouping of zip codes or counties based on demographics, travel patterns, and a sense of "community". Most cities have a vague definition for what people think of as "the north side" or "south city" or "mid county". Once these areas have been identified each area should go through a verification process. First, map the market(s) and let as many people as possible examine the map to see if it "feels right". Next examine the demographics, while some swing in income levels and age demographics can be expected, large differences on a zip code or county basis should not be apparent. Finally examine the patient origin and marketshare of the groupings of hospitals within the market area(s). Do the groupings of competitors within the markets make sense? While the competitors may draw patients from other markets (and potentially different) markets outside of the market in which they are located, the basic grouping should seem right.

**Conclusion.** A market analysis using appropriate market definitions can assist in the development of a targeted strategic plan. The benefits of defining the market(s) based on consumer preferences and characteristics rather than the traditional patient origin based service area(s) include:

- 1) New opportunities may emerge once previously unexamined areas are analyzed;
- 2) Market definitions enable strategic planning from a community/consumer basis;
- 3) Analysis will support targeted marketing strategies;
- 4) Once developed, market definitions rarely (if ever) need to be adjusted, providing for consistency in analysis (service areas can change quite a bit from year to year);
- 5) Market definitions can be used by multiple hospitals or practices within a network, in essence only one overall market analysis will be necessary to suit all the hospitals' needs;
- 6) Market definitions provide a consistent approach for analysis across product lines and departments (planning and finance

analysis is easily integrated);  
7) Markets “make sense”, people identify with them, they work how people think.

Importantly, in today’s environment, a healthcare organization can ill afford not to know its market. This admonition applies to a variety of healthcare organizations — from hospitals, to information companies, to individual physician practices. Indeed, one needs to develop a set of sources and resources by which leaders in those organizations can obtain information about the external environment that impacts the organization and day-to-day operations. Key questions are posed to any organization undertaking strategy:

- What type of decisions are we being called upon to make? What data/information supports those decisions?
  - What trends are occurring locally/nationally that impact the organization?
  - What type of market information do we get on a regular basis? What do we need? How frequently do we need it?
  - How does the organization measure its impact on the marketplace? What measures make sense?
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