Private Equity Value Creation 2.0 Requires a Revised Approach to Healthcare IT Due Diligence

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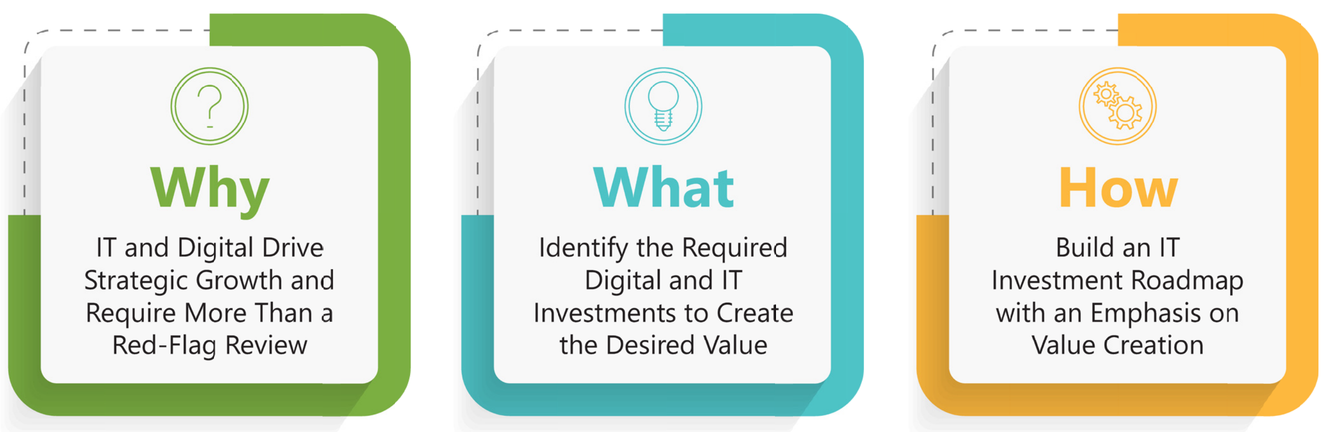
Fast, accurate, and actionable investment intelligence on information technology (IT) and digital is critical to private equity (PE) firms and their investment partners in deploying capital strategically, scaling efficiently, mitigating risk, delivering economic returns, and spurring and spreading innovation to fundamentally improve healthcare for all.

With nearly $2.3 trillion in undeployed capital, we expect a robust year of PE transactions.[1] Value creation is front and center as competitive and regulatory pressures continue to emerge. With deals under greater scrutiny and valuation multiples at all-time highs, demonstrating deal value is of utmost importance—yet it is becoming harder and harder to realize. Traditional approaches to value creation, such as optimization in revenue cycle, IT, and platform integration are and always will be relevant. But new tools and approaches are necessary for success in today's market. These "Value Creation 2.0" initiatives are characterized by multi-disciplinary solutions and often accelerate an organization's move into value-based care. IT and digital capabilities are more important than ever—as enablers and, in some cases, as contributors to value. They should be strategically implemented across the PE investment lifecycle to optimize returns.

> "I'm tired of IT guys speaking hard-core tech language and not telling me how the technology will position our healthcare investment for the future."
>
> —PE investment firm executive

Going into the investment with eyes wide open is increasingly critical to achieve the desired value creation. PE firms and their investment partners need to understand the **why**, **what**, and **how** for IT and digital capabilities from the outset of the due diligence process.



Why

IT and Digital Drive Strategic Growth and Require More Than a Red-Flag Review

We are seeing a shift in IT and operations deal due diligence from a brief, transaction-based process to an important catalyst for value creation efforts. The criticality of IT and digital capabilities has heightened the importance of gaining visibility into how the technology capabilities of an organization might pose risk or strategic opportunities for realizing the deal's true potential. IT should be viewed as a driver of the business and must be examined closely during diligence to ensure it is effectively and efficiently enabling operations and strategic growth. If it is not, the due diligence process should determine what additional investment is needed—and just how much that investment would need to be. Assessing IT risks, capabilities, and maturity during diligence must go beyond the typical "red-flag" diligence process focused on "checking the box."

Every opportunity should be pursued to dig deeper:

- Truly understand the investment thesis and strategic plans for the organization, along with the technology capabilities required to enable them.
- Get a complete picture of the operational workflows and interdependencies before jumping to conclusions.
- Take a hard look at the role IT plays in supporting overall platform objectives for growth, efficiency, quality, and outcomes to drive value creation.
- Understand the real costs associated with future IT and digital investment needs.

What

Identify the Required Digital and IT Investments to Create the Desired Value

A comprehensive investment analysis must go beyond a cursory vendor scan, which will not clearly delineate where industry vendors can play a role and where homegrown systems, for example, may hold a competitive advantage. A diligence partner must have deep insights and direct operational and IT experience with core vendor platforms, understanding what their capabilities and gaps are. That partner must also have similar knowledge and experience of niche and third-party solutions, and leading practices to overcome the expensive gotchas that can often curtail implementation.

Assessments of functionality, maintainability, scalability, cybersecurity risks, and regulatory compliance are table stakes, yet they are foundational to traditional diligence. Additional factors are required during pre-transaction analysis to support overall platform objectives for growth, efficiency, quality, and outcomes.

These factors include:

- What strategies for value creation are planned post-acquisition (e.g., value-based care, patient activation and experience, and clinical outcomes and reliability)? How can technology enable them?
- What digital and analytics capabilities exist to propel growth and patient acquisition?
- What are the core operational workflows of the business? How do technology and analytics support them?

Obtaining accurate and complete answers to these and other questions will help lead to an informed investment. For example, if a strategic goal is to improve the patient's experience pre-arrival, it will be essential from a diligence standpoint to understand the stability of the target's core platform. If that platform needs remediation, platform investments will be required before making any investments in digital capabilities that will improve the pre-arrival experience.

How

Build an IT Investment Roadmap with an Emphasis on Value Creation

A final—yet often overlooked (or rushed)—step during diligence is the investment roadmap. Traditionally, it will be an incredibly high-level plan with no thought given beyond the technical changes. Instead, a roadmap built with an emphasis on value creation will include strategic goals and dependencies, operational refinements, and a level of detail from a technical perspective to articulate key factors well beyond transaction.

Examples of key success factors to consider when creating the roadmap include:

1. **Articulate the true cost and timing for major technology investments.** Accurately determining the integration-related costs requires real-world experience to correctly estimate investments. There is much more than software and maintenance costs to consider when replacing a core vendor platform (e.g., conversions, staffing, third-party solutions, and data archival). Taking these complexities into consideration will avoid the risk of unexpected costs and an unsuccessful implementation.
2. **Engage operations and IT throughout the process.** Having close collaboration between IT and operations in the roadmap development is critical to develop a holistic view of the workflows and supporting technology, as well as the implications of workflow interdependencies and impacts to ensure seamless integration.
3. **Incorporate organizational readiness and change management into the plan.** Investing in technology and implementing a new scalable system will bring much change and disruption to the organization. Planning for a robust organizational readiness and change management effort—including communications and education/training strategies—will be key to mitigate risks and maximize adoption.
4. **Define relevant success criteria and the measurements to achieve benefits outcomes.** Identify initial benefits from the investment, and outline a plan to confirm the clinical, operational, and financial benefits that are most important to drive value creation.
5. **Estimate staffing that is comprised of cross-domain experts accordingly.** Account for existing and supplemental cross-domain experts in change management, IT, clinical, enterprise resource planning (ERP), revenue cycle, and executive/advisory expertise to be successful.

IT Due Diligence Must Outline Risks and Investments Needed for Value Creation

Being cost efficient isn't enough anymore. Decisions need to be made in the context of broader strategic growth opportunities, and technology is a significant factor in that equation. Much more than calling out "red-flags," comprehensive IT and operational diligence must provide actionable insights that educate investment leaders of the potential to scale, address potential risks, realize efficiencies, and deliver differentiated outcomes and Value Creation 2.0.

Sources

1. Steven. A. Cohen, et al, “Private Equity: 2021 Year in Review and 2022 Outlook,” Harvard Law School Forum on Corporate Governance, February 9, 2022, https://corpgov.law.harvard.edu/2022/02/09/private-equity-2021-year-in-review-and-2022-outlook/

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