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Comparingtwo Business Model In Business Expansion:Case Study Of Two Private Hospitals In Malaysia

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Abstract :*Business model describes the method or means by which a company tries to capture value from its business which may be based on many different aspects. In Malaysia, the number of private medical facilities experienced the highest growth from 50 to 209 from 1980 to 2012 and there was a limited study that had been conducted on the expansion of new private hospitals.After receiving the license to operate the inpatient services in January 2015, HospitalA started with 56 beds, increased to 82 beds in 2007 and further increased to 105 in 2009. By expanding in stages this hospital generated RM 19.5 million in 2005, increased to RM 60.8 million in 2006 and increased further to RM 66.3 million in 2007. Hospital A recorded losses of RM 5.3 million in 2005, reduced to RM 370,398 in 2006 but recorded a profit of RM 2.9 million in year 2007. Hospital B with a different business model was completed in 2005 but due to various constraints , this hospital started operation only late 2007. Revenue generated in 2008 was only RM 3.2 million with a loss of RM 111.2 million. This hospital generated an income of RM 24.1 million in 2009 with a loss of RM 192.8 million. After the third year of operation Hospital B only generated a revenue of RM 81.5 million with a loss of RM 450.6 million. The failure of Hospital B was because the company had completed 277 beds from the beginning but cannot fullyutilisedall the beds due to various constraints. The hospital is over staff and had to pay the management fee to outsource companies until the management was handed over to the local CEO in April 2011.*

Keywords *:Business model, private hospitals, expanding in stages, revenue, profit before tax*

I. Introduction

Business model describes the method or means by which a company tries to capture value from its business which may be based on many different aspects of a company, such as how it makes, distributes, prices or advertises its products. It concentrates on value creation and organisation's core strategy to generate economic value, normally in the form of revenue. The model provides the basic template for a business to compete in the market place, it provides a template on how the firm is going to make money, and how the firm will work with internal and external players .

The business model indicates how the firm will convert inputs into outputs and make a return that is greater than the opportunity cost of capital and delivers a return to its investors. It is reflected in its ability to create returns that are greater than the opportunity cost of capital, invested by its shareholders.Business models are an essential part of strategy because they provide the fundamental link between product markets, within the industry, and the markets for the factors of production such as labour and capital.

Business strategy will be depending on the targets that need to be achieved because without clear targets the organization is just like a ship without the captain. The process to set targets involve the entire organization starting from the lowers rank of staff up to the top management (Drucker, 1954). According to Selznick (1957),strategy is actions taken to meet the need of both internal elements and the external elements in the organization. The values and leadership will be the basic strength of the organizationwhich will determine the survival of the organizations without depending merely on mechanical process. The management must control and direct this social pressures to accommodate the need of the organization. When an organization acquires a distinctive identity, it becomes an institution where issues provide grounds for the process to be institutionalized. The coordination of strategy for long term purposes is needed to provide the structure and direction to the company so that it can be focussed to achieve the target and as quoted by (Chandler, 1962) there is a need to match between all elements available in any organization to become one strategy. The strategy of an organization is derived by the structureat various level of management and control is necessary for the entire management functions.Johnson and Scholes (1996), defined strategy as a long term direction of any organization which is important for the organisation to meet the demand of the market and to fulfil the requirement of the stakeholders. This can be done through a proper planning of the resources to meet any changes on the environment. It is the way a business can get from where it is today, to where it wants to be tomorrow.

The leader can use those strategies to look for opportunities in the future and also to overcome any challenges. In term of the strategy for the organization, the leader should formulated the gap analysis which is useful for the management to see the gap between the existing situation compared to the target. In making any standard decisions, the management in any organization will be depending on strategy, guidelines, activities and standard working manuals to solve any problems which do not require decision from the top so that it can be delegated to other staff (Ansoff,1965). However strategy decisions are different because it is related to a new conditions.In the 1980s, car manufacturers in Japan began to concentrate on low cost for production but with high quality products and was able to overcome American car producers. This concept is called lean production techniques and was later followed by many companies. The principle of this strategy is to lower costs, increase the quality of products and increase the efficiencies (Berkshirestrategic.com)

A company that is able to choose a position within an industry and combine activities in many ways will be able to create sustainable competitive advantages (Porter, 1980).This will enable that company to generate profit sustain competition. Positioning is important to shape advantages within a company where the replacement of strategy enables many firms to increase operational effectiveness but was not able to translate those improvements into values for customers.Activities chosen to deliver customer value will produce different profit compared to competitors. Leadership chooses strategy based on analysis followed by well-coordinated activities to support that strategy.Porter (2008), also quoted that strategy is what make your company different from others, values that meet your need, a clear definition and the choice on what is not required. It is related to actions that meet the need and strengthening each other. It is also a continuous strategic continuity followed by continuous improvement to achieve the strategy.

(Steward, 2008), defined business strategy as a long term planning to obtain a specific target or a set of targets or goals quoted that the word strategy originated from the Greek word stratēgos, consisting of two words: stratos (army) and ago (ancient Greek for leading). Strategy is a road map to strengthen the performance of the company and to provide guidance for the top leaders in the company with the basic principle to obtain the set targets of the organization and serve as the main role of the management.Effective strategy means to change,turn or transform a company from losses to a company that make profit (kalyan-city,2012). For a new business the aim of effective strategies is to achieve breakeven which is the point of equilibrium between a profit or a loss followed by generating profit.

In Malaysia, the number of private medical facilities experienced the highest growth from 50 to 209 from 1980 to 2012. Although the figures also include nursing and maternity homes,the bulk of these facilities were private hospitals. In 2001, private hospital beds also grew from 5.8% share of total beds to 28.4 % and the rapid grow of the sector has been fuelled primarily by the rapid rise of national income. The number of private hospital grew from 199 to 209 with an average growth rate of a mere 0.8 percent from 2006 to 2012. The number of private hospital beds grew from 11,206 in 2006 to 13,568 in 2012 with an average growth of 3.7 percent where the higher growth rate of beds is probably due to hospital expansion of existing hospitals and larger hospitals being established during the period (MOHHealth Fact 2009-2013).

For a new hospital,the gestation period to breakeven can be long unless it is already an existing known brand name, such as the KPJ group or the Pantai group of hospitals. However, this slow and steady growth will continue and a few more private hospitals are expected to come into operation by 2015.The majority of the private hospitals are owned by individuals. However the biggest players are group of corporations. In the development of the private hospital business, there are quite a number of international players beside local players. The two major international players in Malaysia are Columbia group of companies and Parkway group (Market Watch, 2012).KPJ Healthcare Berhad is a local company with the biggest change of private hospitals which currently has more than 20 hospitals in Malaysia and two in Indonesia (Annual Report KPJ, 2010). KPJ Healthcare will build five hospitals in the next three years and expand its healthcare travel business. The five hospitals are Sabah Medical Centre, PasirGudang Specialist Hospital, KPJ Klang Specialist Hospital, KPJ Pahang Specialist Hospital and DatukOnn International Specialist Hospital (The Star, 14th November 2011).

The effective strategies will help a new profit hospitalto maintain healthy cash flow to ensure the smooth running of the business. Effective strategies will facilitate the hospital to achieve faster breakeven and generate profit. A new company should determine the point in time when to expand the business and there must be a time period when to expand (Damodaran ,2009). Based on the guidelines given by Info Entrepreneurs (2013), a new company must have good cash flow because cash constraints can be the biggest factor limiting growth and wrong decision made can be fatal and making the best use of financial strength should be a key element in assessing new opportunities. If the resources is limited, expansion would mean starving the business of essential funding and every element of working capital should be carefully controlled to maximise the free cash flow. Good stock control and effective supplier management is increasingly important as business grow and the company may also consider raising financing against trade debs and for expansion plan including raising the equity from the shareholders. With this type of approach the new company is required to expand business in stages depending on the cash flow and affordability to raise funding. Fazzari, Hubbard, and Petersen (1988) propose that when firms face financing constraint, investment spending will vary with the availability of internal funds, rather than just with the availability of positive net present value project. The important of managing free cash flow is to ensure the sustainability of the business. Therefore expanding in stages can prevent the business failure. According to Jagafa and Wood (2012), business failure has been defined as an insufficient revenue or a rise in expense to such a point that the company cannot sustain business. The consequence of this will be a discontinuance of business or discontinuance of ownership (Shepherd, 2003) .Dikman et al (2010) quoted that business failure is a situation when a firm cannot pay their lenders, stock shareholders or suppliers.

There was a limited study that had been conducted on the expansion of new private hospitals. In 2012 ,a focus research was conducted by LautandhanaSecurindo in Indonesia related to the expansion of Omni hospital in Jakarta. This hospital started business in September 1972 as non-profit hospital by providing psychiatric diagnosis and therapy to general public. However in 1988, it was transformed into a general hospital and later in 2007, the new Omni hospital was equipped with modern facilities to attract various categories of customers. The total number of premium beds was only 58 in 2010 but increased to 77 beds in year 2011and further expended to 95 beds in 2013. With this expansion, the revenue also increased accordingly and this hospital managed to breakeven and generate profit in year 2012.Another business expansion study was conducted by (Sharif,2010) related to the expansion of KPJ Healthcare Berhad from year 2004 to year 2008. The number of hospitals had grown from 13 in 2004 to 19 in year 2008. With this expansion, the turnover generated had grown from RM 583,397,000 in 2004 to RM 1,267,305,000 in year 2008. The assets had grown from RM 291,248,000 in 2004 to RM 470,797,000 in year 2008. In line with the expansion the profit also grew from RM 40,646,000 in year 2004 to RM 114,052,000 in year 2008.

II. Objectives

1. To compare two business model for hospital expansion
2. To compare the outcome of the two business model

III. Methodology

Case study method was chosen to conduct the study. In this study two new private hospitals in Malaysia namely Hospital A and Hospital B were chosen as samples. Data were collected related to the business expansion plan and the financial performance of the two hospitals. For Hospital A, data were collected from the Finance Manager and Suruhanjaya Syarikat Malaysia(SSM) whereas for Hospital B, data were collected from the Senior Manager, Suruhanjaya Syarikat Malaysia (SSM) and newspaper. Data for Hospital A were collected from 2005 to 2008 whereas data for Hospital B, data were collected from 2005 to 2011. Data were collected through the following process:

1. Initial contact with the organization through phone calls and conduct interview via telephone
2. Draft and submit the official letter using email
3. Received the required data from the two hospitals
4. Purchased the official report from Suruhanjaya Syarikat Malaysia (SSM)
5. Data from newspaper for Hospital B

After all data were received, they were sorted out in each category and tabulated accordingly.

IV. Results

Table 1 : Total revenue and PBT of Hospital A from 2004 to 2007

	2004	2005	2006	2007
Revenue	RM 4,095,540	RM 19,531,453	RM 60,831,245	RM 66,342,165
Profit before tax (PBT)	(RM 933,242)	(RM 5,324,145)	(RM 370,398)	RM 2,865,130

Table 2 : Summary of key ratio for Hospital A

	2005	2006	variance	2007	variance
Revenue	RM 19,531,453	RM 60,831,245	212%	RM 66,342,165	9%
PBT	(RM 5,324,145)	(RM 370,398)	93%	RM 2,865,130	873%
No. of beds	56	82	56%	105	28%
Return of investment	-	-	-	3.5%	-
Net profit margin	-	-	-	4.3%	-

Table 3 :Total revenue and PBT of Hospital B from 2008 to 2010

	2008	2009	2010
Revenue	RM 3,236,375	RM 24,116,992	RM 81,535,414
Profit before tax (PBT)	(RM 111,171,001)	(RM 192,794,384)	(RM 450,578,215)

Table 4 : Summary of key ratio for hospital B

	2008	2009	variance	2010	variance
Revenue	RM 3,236,375	RM 24,116,992	645.2%	RM 81,535,414	238.1%
PBT	(RM 111,171,001)	(RM 192,794,384)	-273.4%	RM (450,578,215)	-333.8%
No. of beds available	277	277	0	277	0
No. of beds in operation	16	65	306.2 %	113	73.8%
Return of investment	-	-	-	-	-
Net profit margin	-	-	-	-	-

V. Discussion

Hospital A, constructed at the total cost of RM 48 million, started business in November 2004 by operating the Emergency services. After receiving the license to operate the inpatient services in January 2015, this hospital started with 20 beds consisting of 18 general beds and 2 Intensive care Unit. The bed was increased to 58 in June 2005 with 56 normal beds and 2 ICU beds. 18 medical consultants had joined the hospital in year 2015. After completing the renovation of the new ward at the total cost of RM 2.6 million, the bed was increased to 82 in 2006. With the additional beds the revenue increased by 122% compared to the previous year and the hospital also started a new dialysis services with 3 machines. The revenue for 2005 had increased by more than RM 15 million compared to 2004 because the hospital had operated 58 beds for inpatients. However due the costs incurred the hospital had recorded a loss of RM 5.3 million in year 2005 which was RM 4,390,903 bigger than 2004.

In 2006 the number of beds increased by 24 and additional 2 Intensive Care Unit. In line with the expansion program the revenue for 2006 had also increased to RM 60.8 million and lossbeforetax had been reduced to RM 370,398. With the new injection of RM 10 million paid up capital in 2007, the hospital had expended the ICU from 2 beds to 4 beds and the normal beds was increased to 105 after the completion of new ward . Further expansion of services was done by starting a catheterization laboratory (Cathlab) and also converting the third Operation Theatre to Cardiac OT. By expanding the services in stages the revenue of the hospital increased from RM 4,095million in year 2004 to RM 19.5 million in year 2005. The revenue further grew to RM 60.8 million in year 2006 and further increased to RM 66.3 million in year 2007. The hospital started with a loss before tax of RM 933,242 for year 2004 and increased to RM 5.3 million in year 2005. However, the loss was reduced to only RM 370,398 in year 2006 and generated a profit of RM 2.8 million in year 2007. Hospital B did not expand business in stages but instead the management had open the whole hospital one go with full capacity of 277 beds and fully equipped .Total cost of construction for the hospital was RM 544 (TheStar.com) .The hospital was incorporated in year 2005 and the Company entered into an agreement with VS Services SdnBhd and MU University for the supply of medical, administrative and technical packages for the operation of the Company and subsequently to manage and operate the hospital (Annual Report, 31 March 2010).Since opening in year 2006, the hospital had been equipped with full capacity of 277 beds of single room only which is against the norm in Malaysia where other private hospitals will have a few types of room consisting of single room, two bedded room, four bedded room and in some hospital 6 bedded room. By having only single rooms, it will make it difficult to sell the room due to the high charges for single room and this hospital also failed to secure partnership with insurance companies which require various types of rooms.Even though 277 beds were ready for use, due to shortage of doctors, only 100 beds were licensed by Ministry of Health. Therefore 177 beds were left unused and the management had to include financial cost and cost of depreciation into the Profit and Loss account. There was no revenue generated for year 2005 and 2006. Total number of staff ending 31 March 2005 was only 2 with staff costs of RM 67,144. However by 31 March 2006 the number had increased to 73 with staff costs of RM 564,939 and the hospital had to pay operator's management fees of RM 7,350,000.As at 31 March 2007 (Annual Report as at 31 March 2007) ,there was still no revenue generated because the hospital is not yet in operation. However the hospital had recruited 230 staff with the staff cost of RM 8,547,577. This hospital is continuously depending on the support from its ultimate holding company with a total amount due to the immediate holding company of RM 776,780,566 . The hospital had to pay the operators management fees of RM 11,028,150,consultation's fees of RM 6,988,203 and administration expenses of RM 9,428,823. Therefore for the financial year ended 31 March 2007, loss before taxation was RM 35,654,378. The Company commenced operation on 1 October 2007(Annual Report as at 31 March 2008). Even though 277 beds were available , due to various constraints , the hospital only operated 16 beds, 2 Intensive Care Unit and 2 Operation Theatre, supported by 23 Medical Consultants. As at 31 March 2008(Annual Report as at 31 March 2008) the hospital had a total of 618 staff with staff costs of RM 22,655, 347. The revenue generated for the current year was only RM 3,236,375 whereas the hospital had to pay RM 11,472,000 for Operator's management fees, RM 8,719,753 for consultation fees and RM 6,714,934 as guaranteed minimum income for consultants (medical specialists). Therefore, loss before taxation was RM

111,171,001. For this year number of consultants were 30, number of beds 65, ICU/CCU 8 and Operation Theatre 7.

For the financial year ended 31 March 2009(Annual Report 2009), the hospital incurred a loss of RM 192,794,384 and the company had to continuously depending upon the continuing financial support from its ultimate holding company. As at 31 March 2009, RM 697,499,980 of these advances were capitalised as share capital. The remaining RM 516,296,258 were refinanced with the ultimate holding company and bear an interest rate of 4.5% , are unsecured and repayable in year 2012. Revenue generated was only RM 24,116,992 which is not sufficient to pay for all the expenses. Staff costs was RM 39,635,146 (801 staff), operator's management fees was RM 9,396,000, consultation fees RM 9,041,551, guaranteed minimum income for consultants RM 11,310,960 and repair and maintenance expenses was RM 19,210,505. After taking into account all expenses, loss before taxation was RM 203,249,484. .For this year the hospital had 38 Medical Consultants, 113 beds, 12 ICU/CCU and 7 OT .

The company still incurred a loss of RM 450,578,215 as at 31 March 2010 and is still depending on the continual financial support from its ultimate holding company. The revenue generated was RM 81,535, 414 which is still not sufficient to cover all costs. RM 8,877,180 was paid as Operator's management fees, RM 3,564,301 as consultants' fees and RM 54,610,092 as staff costs (1,015 staff) .Guaranteed income for consultants was RM 11,844,135 followed by RM 17,981,538 for repair and maintenance. In year 2010 the hospital had 186 beds, 7 OT, 33 ICU/CCU/Neurological ICU and 38 Medical Consultants. Due to long unutilised assets, in this year, RM 158,000,000 was taken into the financial statement as impairment on property, plant and equipment. As a result Loss before taxation ended at RM 450,578,215 for year 2010.

Due to the poor performance of the hospital, on 22 June 2010, three key members of the management staff, the Chief Executive Officer, Chief Medical Officer and Legal Adviser were told to go on leave pending outcome of an audit review. In July the Chief Executive Officer of VHS SdnBhd was appointed as the interim CEO of this hospital. However effective December 1, 2011, VHS SdnBhd and MUV have ceased to be the operators of this hospital although the initial contract was believed to be until March 2014 (Ganesan,V.2011). Further to this, the owner had appointed a Malaysian CEO to head the hospital.

VI. Conclusion

Hospital A was successful to turnaround the business and generated a profit in the third year. This hospital was only constructed at the total cost of RM 48 million compared to Hospital B at the total cost of RM 544 million. Hospital A was managed by local CEO whereas for Hospital B it was outsourced to foreign consultants with high management fees. Hospital A started with 56 beds, expanded to 82 beds in the second year and 105 beds in the third year whereas Hospital B was fully equipped with 277 beds from beginning. The building for Hospital B was completed in 2005 but the business can only started in October 2007. There was a gap for two years which had incurred high accumulated cost to the company. Even though 277 beds were able, but due to various constraints, the management of Hospital B only able to operate 16 beds in 2008, 65 beds in 2009 and 113 beds in 2010. The failure of Hospital B was because the company had completed 277 beds from the beginning but cannot fullyutilisedall the beds due to various constraints. The hospital is over staff and had to pay the management fee to outsource companies until the management was handed over to the local CEO in April 2011.

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