

# SEP\_AIN3147

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**Submission date:** 29-Apr-2023 05:41AM (UTC-0500)

**Submission ID:** 1898814507

**File name:** SEP\_AIN3147\_Final.docx (30.96K)

**Word count:** 3803

**Character count:** 21656

# **FUNDAMENTALS OF HEALTH & CARE FINANCE**

### **Executive Summary**

The report has highlighted the development of financial and regulatory changes in healthcare sectors. The report has elaborate the funding way of healthcare sectors. DU Pont analysis of BUPA Group for the year 2019 and 2020 is included in the paper using the provided data. Suggestions to company is also illustrated concern to selection of service offerings considering significant investment appraisal techniques. Process to develop financial statement is also discussed. Debt ratio of BUPA Group is also explores including presenting solvency performance of the company. Moreover, the report has incorporated the role of traditional marketing in healthcare.



## Introduction

Fundamentals in health and social care finance refer to the solid grounding of principles that finance manager's use for audit activities. In this context, the study focuses on the recent developments in the finance and regulatory environment in healthcare institutions. Moreover, the funding options of healthcare sectors are included in this study.

## Task 1

### (a) Determining the recent developments in the financial and legal/regulatory the environment of Health and social care service Delivery

#### Financial development

The recent developments in healthcare services rely on the activities of the government and private sectors on health care services. As per the discussion by Pazarbasioglu *et al.*, (2020), innovation in payments is an important development in healthcare services in terms of accessing payments at the proper time. In this context, the healthcare sectors have included the *digitisation process* in their services to collect payments from patients online. The healthcare sectors have adopted the *QR code system* for collecting payments from patients. Moreover, the inclusion of innovation is a beneficial factor for the healthcare sector in terms of gathering funds from investors online. Thus, the development of payment options provides opportunities for the healthcare system in managing transactions effectively.

Covid 19 plays a crucial role in the healthcare sector in terms of developing financial activities online. As per the findings of Evstafyeva *et al.*, (2019), the inclusion of digitisation helps in improving the financial process in healthcare workplaces. In this context, healthcare sectors are moving from traditional finance to digital finance in order to stabilise the economy more strongly. Thus, financial development through adopting digital culture can be an appropriate development for the healthcare sectors in order to improve health and social care services.

#### Legal development

The development of the "*Inflation Reduction Act*" (IRA) is an important regulatory change by the governments in terms of improving healthcare services through drug reform. As observed by Rome *et al.*, (2023), the IRA includes the drug pricing reform section for improving the Medicare programme effectively. In this context, the developed IRA states that the Medicare programme

will pay for the prescribed drugs to the patients. Therefore, it can be beneficial for the patients due to the reform of drug pricing development under the IRA.

**(b) Elaborating the usefulness of 3 alternative funding options and mentioning which is best for the health and social care sectors**

It is important to elaborate on the funding option of healthcare institutions in order to demonstrate the effective way to stabilise economic conditions. As per the study by Grilli *et al.*, (2019), there are three types of funding such as **general taxation, venture capitalists and medical insurance**. In this context, the **general taxation** funding process is an effective way for healthcare institutions in accessing funds for health and social care activities. Accordingly, the government receives the general tax from the people to allocate to different departments such as health and social care. Similarly, the health care institutions rely on the budget of the government to access the annual funds through the general taxation method. On the other hand, the decisions over the utilisation of funds from general tax are based on political processes (Campos *et al.*, 2019). The involvement of political decisions creates often challenges for healthcare institutions in accessing proper funds at a given time. Moreover, the healthcare sector is allowed to depend on the annual revenue for gathering funds from the government. The general tax rate of the UK was 223 billion US\$ dollars in 2022 (Statista, 2023). In addition, general taxation helps the healthcare institutions of the UK to access free Medicare programmes from the government. Hence, it can be said that the general taxation of the government is the primary funding option for healthcare institutions.

**Venture capitalism** refers to the involvement of equity investors in the funding process of healthcare institutions. As per the suggestion by Sim *et al.*, (2020), the investors provide funds to the healthcare institutions for accessing greater returns in future. In this context, the healthcare institutions join the venture capitalists firms for accessing funds from equity investors to develop health and social care. The venture capitalist market of the world healthcare market was 300 billion dollars in the year 2021 (Statista, 2023). Similarly, venture capitalists provide money on some certain interest to the healthcare institutions that the institutions use for developing the healthcare process. Therefore, the venture capitalist is an essential funding option for healthcare institutions. **Medical insurance** can be taken into consideration as an important funding method for healthcare institutions. As per the evaluation by Goodyear-Smith and Ashton (2019), healthcare institutions earn a huge amount of money from the payment of medical insurance. In this context, the national

investment in medical insurance is the primary way to gather funds for health and care services which helps in covering the financial risks. Accordingly, the establishment of private and social insurance helps to gather funds for healthcare institutions. Hence, the process of private and social medical insurance is a better option for healthcare institutions in gathering funds from the user's payments and transactions.

The venture capitalist funding way is more reliable for healthcare institutions in comparison to others due to lack of fluctuation. As per the observation of Goodyear-Smith and Ashton (2019), healthcare institutions are able to gather funds from equity investors in any situation through venture capitalism. In this context, healthcare institutions face difficulties in the primary taxation process due to fluctuations in tax revenues. Besides, the venture capitalists process never fluctuates for the healthcare institutions which reflects as more reliable than the primary taxation process. Hence, it can be highlighted that healthcare institutions can use the venture capitalists' funding way to develop healthcare services.

## **Task 2:**

### **a) Reviewing BUPA Group's financial statements and evaluation of the business profitability**

#### **(i) Determine and evaluate DU Pont Analysis for 2020 and 2021**

The DU Pont Analysis signifies to as an effective tool utilises to access <sup>8</sup>the return on equity (ROE) structure of the company by segregating its components (Bhagyalakshmi and Saraswathi, 2019). Considering the provided financial information, the DU Pont Analysis components of BUPA Group for the years 2021 and 2020 are presented as follows.

#### ***For the year 2020***

Net profit margin = 2% or 0.02

Asset turnover ratio = 0.71

Equity multiplier = 1.72

<sup>1</sup>  
$$\text{ROE} = \text{Net profit margin} * \text{Asset turnover ratio} * \text{Equity multiplier} = 0.02 * 0.71 * 1.72 = 0.03 \text{ or } 3\%.$$

***For the year 2021***

Net profit margin = 3% or 0.03

Asset turnover ratio = 0.78

Equity multiplier = 1.82

<sup>1</sup>  
$$\text{ROE} = \text{Net profit margin} * \text{Asset turnover ratio} * \text{Equity multiplier} = 0.03 * 0.78 * 1.82 = 0.05 \text{ or } 5\%.$$

BUPA Group evolves with a ROA structure worth 3% in the year 2020 and 5% in the period 2021. From the structure, it can be said that the company's ROE has enhanced from the initial period highlighting that BUPA Group has been able to acquire more income from a similar equity amount (Saus-Sala et al. 2021). Moreover, the increase in ROE is subsequently attributed to the increased valuation of net profit margin, asset turnover ratio, and equity multiplier in 2021 in comparison to its initial year of 2020. Irrespective of this, comparing the ROE of BUPA Group with the industry average value of 11.6%, it can be said that the firm's performance is lower presenting an urgent requirement to enhance its efficiency in terms of utilising its equity to acquire income.

**(ii) Utilisation of DU Pont Analysis in decision-making and ensuring business viable**

Decision-makers can evaluate the effectiveness of the operations, profitability, and financial structure of a firm by utilising the DuPont analysis to pinpoint the precise divisions responsible for its ROE. For instance, the DuPont analysis can assist in determining which ROE factor (profit margin, asset turnover, or financial leverage) is the weakest and hereby needs improvement concerning the lower valuation of the company (Kasik and Snapka, 2020). The next step for decision-makers is to take action to strengthen the identified weak areas, such as raising the profit margin by boosting sales or cutting costs, or boosting asset turnover by streamlining inventory control or diversifying the company's product line.

Referring to the given case scenario, BUPA Group's business is viable in the context of enhancing ROE valuation in 2021 in comparison to its previous year. It is recognised that the net profit margin of the company increases from 2% in 2020 to 3% in 2021, highlighting that BUPA Group has been able to maintain its expenses and hereby enhance its profitability. Besides, the asset turnover ratio



of the company also enhanced from 0.71 in 2020 to that 0.78 in 2021, presenting that BUPA Group has been able to acquire more sales from its assets. Additionally, the equity multiplier of the firm also improves from 1.72 in 2020 to 1.82 in 2021 reflecting the enhanced leverage position of BUPA Group.

**b) Accessing investment options and ensuring suggestions with justification**

<sup>6</sup> Net present value (NPV) and Internal rate of return (IRR) are two major approaches for accessing the investment opportunities of BUPA Group. To determine the NPV and IRR for each of BUPA's two service offerings, they are required to discount back the cash flow to their present value considering the 10% rate as shown here.

***Premium cash flows***

$$\text{NPV} = -£ 650,000 + (£ 175,000 / 1.1) + (£ 178,000 / 1.1^2) + (£ 150,000 / 1.1^3) + (£ 190,000 / 1.1^4) + (£ 192,000 / 1.1^5) + (£ 50,000 / 1.1^5) = £ 32,510.31$$

$$\text{IRR} = 15.19\%$$

***Basics cash flows***

$$\text{NPV} = -£ 515,000 + (£ 125,000 / 1.1) + (£ 130,000 / 1.1^2) + (£ 140,000 / 1.1^3) + (£ 150,000 / 1.1^4) + (£ 160,000 / 1.1^5) + (£ 40,000 / 1.1^5) = £ 70,798.79$$

$$\text{IRR} = 19.22\%$$

BUPA Group must select the Basics service offering for investment with higher NPV and IRR in comparison to the Premium service offering. This is because Basics Offering identifies more financially attractive to BUPA as it intends to acquire higher investment returns and develop more valuation for the firm (Gardi et al. 2021).

### **Task 3:**

#### **(a) Process to develop financial statement**

Financial statements are referred to as crucial instruments that offer insightful information about the financial health of the business corporation. As opined by Fridson and Alvarez (2022), they are mainly prepared in terms to discuss the financial performance of the firm over a certain period. Business owners, investors, creditors, and other stakeholders can make effective decisions with the help of financial statements. The three major financial statements that companies specifically develop include the income statement, the cash flow statement, and the balance sheet. Evolving with these ideologies, the process of preparing each of the mentioned financial statements is illustrated below.

##### ***Income Statement***

As referred by Arya and Nagar (2021), an income statement displays a company's earnings and outlays for a given time frame. The steps listed below are specifically used to prepare the income statement:

- Assemble all of the income earned during the time, and record it.
- Keep track of every expense the company made during that time.
- To calculate the net income or loss of the business, expenses are subtracted from that of the business's revenue structure.

##### ***Balance Sheet***

As considered by Jeenas (2019), a balance sheet is a statement that lists a company's assets, liabilities, and equity at a certain time. The steps listed below are used to prepare the balance sheet:

- List each of the company's assets along with their corresponding values.
- List each of the company's debt obligations or liabilities along with their relative values.
- Subtract the entire liabilities from the total assets to determine the company's equity structure.

##### ***Cash Flow Statement***

As understood by Setiany (2021), an organisation's both inflow and outflow structure of cash over a given period are displayed on a cash flow statement. The steps listed below are used to prepare the cash flow statement:

- Recording every monetary inflow of the business within a particular period.
- Recording all cash outflows of the business during the specific year.
- Subtract the cash outflows from the cash inflows to determine the net cash flow.

Once the primary financial statements are created, they should be reviewed for consistency and accuracy purposes. A comparison of the financial statements to earlier periods should be done, and any major differences or discrepancies should be looked into. As indicated by Alijonovich and Akhmadjonovich (2022), financial statements should also follow all regulations and standards governing accounting. To enable stakeholders to make effective judgments, the financial accounts must be presented clearly and straightforwardly.

Hence, it can be ultimately said that creating financial statements is implied as a crucial duty for any firm. Furthermore, financial data must be gathered, precisely recorded, and presented clearly and straightforwardly to create relevant financial statements for the firm.

#### **(b) Calculation of debt ratio and comprise company's solvency position statement**

A debt ratio implies the financial indicator considers assessing how much of an organisation's assets are financed by its debt structure. As highlighted by Husna and Satria (2019), by dividing the total debt of the business by its total assets, the debt ratio is determined. The resulting ratio shows how much a business depends on debt financing to finance its operations. Referring to the provided case circumstance and data associated with financial statements, the debt ratio of BUPA Group for the years 2020 and 2021 is calculated as follows.

Particulars	2021 (£ M)	2020 (£ M)
Total debt	9139	9862
(/): Total assets	16597	17010
<b>Debt ratio</b>	<b>0.55</b>	<b>0.58</b>

<sup>5</sup>  
**Analysis:** From the above-provided calculation, it can be appropriately said that the debt-to-equity ratio of BUPA Group in 2021 is explored as 0.55, which indicates that debt accounts for 55% of the company's assets. As considered by Ayoush et al. (2021), this shows that the company has lessened its reliance on debt financing over the previous year as it is somewhat lower than the company's debt ratio of 0.58 in 2020. Irrespective of this, the structure of the company is recognised as still much higher than the 35% industry average for the healthcare sector, indicating that the company faces greater financial risk than its competitors.

Irrespective of this, it can be referred to that BUPA Group poses a total debt structure worth £ 9,862 in 2020 and £ 9,139 in 2021. Besides, the company also acquires total asset valuation amounts to £ 17,010 in 2020 and 16,597 in 2021. Over the years, it is identified that the company deteriorates both its debt and assets structure in 2021 in comparison to its previous year of 2020. However, it is important to keep in mind that a high debt ratio can raise the financial risk of BUPA Group and even result in insolvency if it is unable to produce enough cash flows to pay its debts (Fang, 2021). Concerning this, investors and stakeholders should actively monitor the BUPA Group's capacity to generate cash flows and also to satisfy its debt commitments to maintain the company's solvency condition in the upcoming years also.

### **(c) Appraising the role of the traditional finance function in healthcare Organisations**

Traditional finance refers to the process of managing finance and assets through paper-based solutions. As per the view of Haralayya (2021), traditional finance helps investors in accessing financial information from banks and institutions. The paper-based process of traditional finance provides insight into the transactions and all alliances to the investors. In this context, the traditional finance process relies on the fact that the market and people are rational. Accordingly, investors are able to access huge data and information regarding the financial expenses of the banks through reports and spreadsheets. Similarly, healthcare institutions use the traditional finance method to manage financial assets and liabilities. On the other hand, the traditional finance process helps healthcare institutions minimise financial risks through cost measurement activities (Noy *et al.*, 2020). In turn, the cash management programme of healthcare institutions is dependent on the traditional finance process due to its paper-based solution. Moreover, the audit members of the healthcare institutions can gather information on all the financial expenses due to the paper-based solution of traditional finance (Laroiya *et al.*, 2020). In addition, healthcare institutions are

able to disclose their financial reporting through the traditional financial process. Therefore, it can be said that the role of traditional finance is prominent in order to manage the cash measurement and management activities in healthcare institutions.

Traditional finance helps healthcare institutions in making their annual budget by analysing the expenses and potential risks. As per the findings of Chang *et al.*, (2019), traditional finance provides insight into the previous risk and coverage's through the paper-based solution. In this context, the paper-based solution of traditional finance is effective to store financial records for healthcare institutions in terms of making budgets. Accordingly, the allocation of financial resources based on the budget can be possible through the traditional finance programme that helps the healthcare institutions in managing the resource allocation to the employees. On a contradictory note, healthcare institutions make sheets of employee salaries through the traditional finance process (AlHamad *et al.*, 2022). In turn, the paper-based solution process helps the health sectors to recognise the risk coverage and health benefits of the employees through traditional finance methods. Moreover, healthcare institutions use traditional finance for interpreting historical and projected economic data to manage financial risk coverage's effectively. The paper-based solution of traditional finance helps financial sectors in dealing with legal matters properly. However, the audit team of healthcare institutions need to make the papers and sheets effectively to manage the risks in the traditional finance process. Thus, the utilisation of traditional finance programmes is an important factor for healthcare services. it helps in making financial reports and statements properly.

## **Conclusion**

On a concluding note, it can be said that the healthcare sector needs to use regulatory and financial changes effectively in healthcare services. The audit team of healthcare institutions needs to manage the traditional finance system effectively. Therefore, it can be concluded that the financial process is prominent for health and social care institutions in terms of developing economic conditions.

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