Outline

- What drives cost growth
- Implications of cost growth
- Cost containment options
Definitional issues matter

Focus on expenditures at the national (or population) level

Not:
  – Cost per service
  – Cost per patient treated
  – Cost per disease
Cost Drivers
Could obesity be driving spending

- Probably contributes to cost growth, but not a main driver.
- Costs were growing faster than real GDP for EVERY 10 year period since WWII
  - Even before obesity epidemic
- If the only change between 1987 and 2001 were BMI related then real, per capita spending would have risen ~ 1%
Long run cost drivers

- Medical technology
  - New knowledge (and associated stuff)

- Less important factors
  - Prices
  - Aging
  - Rising incomes
  - More generous coverage
  - Inefficiency
  - Inappropriate use
  - Liability
Evidence

- Several literature reviews document the role of technology
  - Chernew et al. (1998)
  - Smith et al. (2000)

- Different methodological approaches
  - Residual approach
  - Affirmative

- 81% of economist cite technology as main cost driver (Fuchs, 1996)

- Estimates suggest 50% of cost growth related to ‘technology’ (Cutler, 1995)
Types of technology changes

1951 - 1971: little ticket items
- lab tests
- X-Rays

1971 - 1981: big ticket items
- CABG
- C-section
  - radiation & chemotherapy for breast cancer

Early and Mid 1990s
- Pharmaceuticals
Implications of Cost Growth
### Incremental spending on health care

#### 1% gap

<table>
<thead>
<tr>
<th></th>
<th>1999-2010</th>
<th>2010-2050</th>
<th>2050-2075</th>
<th>1999-2075</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual % increase in per capita non-health care expenditures</td>
<td>1.0%</td>
<td>.8%</td>
<td>.6%</td>
<td>.8%</td>
</tr>
<tr>
<td>% of real increase in per capita income devoted to health care</td>
<td>30.9%</td>
<td>45.5%</td>
<td>66.3%</td>
<td>54.8%</td>
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Cost growth deters coverage

Despite the best economy in generations, the rate of health insurance coverage fell over the 1990s.

The coverage decline is associated with rising health insurance premiums.


Over half of the coverage decline in the 1990s attributable to premium growth

Cost growth complicates coverage expansions

– Greater subsidies needed to maintain impact
Cost Containment
Level vs Trajectory

Costs vs Time

- High cost
- Low cost
Options

- Managed care/ competition
- Lower provider prices
- Higher consumer cost sharing
Managed care

- Manage care lowers costs
- Possibly some modest reduction in rate of cost growth
  - Concentrated in areas with considerable provider competition
  - Cost growth still exceeds income growth
  - Hard to maintain impact
Lower provider payments

- Can reduce spending
  - Utilization effects as well
- Concerns about access
- Conceptually could affect growth as well as level
  - Scant evidence
  - What are the thresholds?
Patient cost sharing

- Can lower costs
- In theory can control cost growth
- Concern about quality
  - Patients do not ration well
Value Based Insurance Design

- Reduce (or keep low) copays for high value services
  - For high value patients
- Recognize heterogeneity in value
  - By service
  - By patient
- Recognize that for high value services, higher copays lead to under-consumption
Summary

- Cost growth is driven by new technology

- Continued cost growth will:
  - Consume a large share of income growth
  - Contribute to coverage declines

- No magic cost containment options
  - level vs trajectory
  - Cost containment vs quality/ access