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Competition and the American Hospital

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Hospitals Today & Yesterday

- Modern Hospital:
  - Core Provider Care:
    - Nearly 5,000 community hospitals in U.S.,
    - Almost 31% healthcare expenditures
  - However, not always so:
    - In 19th century Little clinical reason to go to Hospital
    - Primarily vendors of last resort charity patients

Questions:

- How did we get where we are today?
  - What propelled hospitals' rise and Could similar forces lead to their future decline?
  - What implications re:
    - Evolving organization industry?
    - Future of hospital competition?
  - Note number of hospitals, beds, share of spending down somewhat. (Tables 1 & 2)
    - 31% spending 2006 vs. 40% 1975,
    - BUT hospital share total GDP highest ever:
      - 4.8% GDP 2006 vs. 3.2% 1975

Conceptual Framework

- Conceptual Framework

Organization healthcare reflects:

- Uncertainty Issues: demand, evaluation needs, quality & appropriateness care (Arrow 1963)
- Economies of Scale and Scope:
  - Gains from Centralization Care
    - Complementary services per se
    - Coordination Issues, Transfer Costs and Uncertainty future needs $\longrightarrow$"*Option Demand*"

Historical Evolution Hospitals

- 19th Century:
  - Most care provided in doctors' office & patients' homes
    - Paid for out-of-pocket on fee-for-service basis- *no insurance*
  - Hospitals Charitable public & private non-profit institutions- serve those with nowhere else to turn
    - Hospital Care typically free - paid for by gifts & public subsidies
    - Medical services donated (vs. hired staff)
      - little/no price competition

Early 20th Century: Rise Modern Hospital

- Interaction Social & Technological forces
- Economies scale & scope centralizing new diagnostic & therapeutic services
- Emergence hospital as “doctor’s workshop”
  - Focus inpatient care local community
  - For first time demand by paying patients

Rise Modern Hospital (cont'd)

- Extension Fee-for-service, out-of-pocket payment to Hospital Setting
  - Fees New source revenue(~50% 1929), help fuel big expansion industry (4000+ by 1928)
  - Emergence "Patient Driven Competition"
    - \- Degree market discipline given information problems cost/quality?
  - Separate payment hospital/physician services w/MD as patient agent & issues incentive alignment
  - Opportunities for For-Profit Hospitals
    - Early role and later tilt towards Nonprofit/Public Hospitals (Table 2)

Third Party Payment

- Rising Costs & Demand for Insurance
  - Private coverage & rise employment based group coverage WWII and after
  - Public coverage, Medicare & Medicaid 1965:
    - shift from direct provision to financial access
    - indigent care cut but not eliminated
- Continued "Patient Driven Competition" but w/
  - Dilution incentives consumers to shop
  - Cost based reimbursement & lack accountability providers
- Accelerating growth costs: 3.5% GDP 1928, 4.4% 1955 vs. 8% 1975 (Table 1)

Cost Containment & Competitive Reforms

- Regulatory vs. Pro-Competitive Approaches
  - Medicare PPS & realignment provider incentives, but continued reliance on patients for shopping
  - Managed Care & "Payer Driven Competition"
    - Shift purchasing decisions towards health plans → Restrictions on Consumer Choice
      - Selective contracting & "steering" patients
      - Utilization Controls
      - Novel provider payment (e.g. Capitation)

Competitive Reforms & Realignment Incentives

- Vertical Integration
- Horizontal Integration
- Specialization
- Movement services to least cost locations:
  - Inpatient→ Hospital Outpatient→ Free Standing Center→ Doctors' office
  - Local v. Distant
- Issue Option Demand and Choices general v. specialty hospital, inpatient v. outpatient, network

Industry Trends 1980s & 1990s:

- Price effects
  - Major contraction Hospitals/Beds (Table 2)
- Geographic & Product Markets
  - Still Local
  - But New Products & Competitors
    - Diversification Hospital Product mix: Shift towards outpatient: 13% revenue 1980 v. 38% 2006
    - Growth Free standing surgery & imaging centers, Doctor's office procedures
      - 93% Outpatient Surgeries in Hospital in 1981 v. 45% in 2005 (38% centers, 17% MD offices)

Industry Trends 1980s & 1990s (Cont'd)

- Vertical Integration (Or Not)
- Horizontal Integration (Up!)
  - HHI 2323 in 2003 v. 1597 in 1990
- Consumer "Backlash" & Reduced Restrictions Consumer Choice
  - Reductions UR, Net Work expansion, shift plan types (Table 4)
- Emergence Quality Issues

Hospital Competition & the Marketplace: Some Current Issues

- Survival Hospital:
  - Shift to Out-of-hospital Care
    - Potential Countervailing Forces:
      - Limits Outpatient Care
      - Option demand & economies scope
      - New Technology and Hospital as First Mover
    - Persistence (so far) (Table 1)

Vertical Integration

- Current Fragmented Payment System:
  - Hospitals & Physicians
    - Hospitalists
    - Purchases PCPs, potentially other specialists
  - Physicians & Outpatient Services/Specialty Hospitals
    - MD ownership
    - Tension around affiliations, right hospitals to exclude MDs from privileges

Horizontal Integration

- Continued Overall Consolidation
  - Decline activity since late 1990s, but recent uptick
  - Potential impact of financial crisis?

Geographic Market

- Local Service Markets
  - Option Demand and Market Analysis
    - Hospital v. Network level effects
- Extension Market Boundaries
  - Telemedicine, Image Reading etc.
  - Regionalization, Medical Tourism
    - Can they constrain local behavior?

Benefits Design:

- Crisis Managed Care
  - Glass half empty or half full?

- Moving Shopping back to Patients:
  - Consumer Directed Health Plans: What impact? (~8% Pvt. Group market)
    - Empowerment with price/quality information
    - Low dollar v. catastrophic care
    - Relation Managed Care: substitute v. complement?

Health Information Technology (HIT)

- Early Stage Implementation
  - Potential Impact Competitive Conditions via Effects on:
    - Transactions Cost Coordination
    - Predictability Care Needs
- Issues Introduction:
  - Public Good Aspects & Alignment Incentives
  - Open v. Proprietary HIT Platforms & Role Hospital

Quality

- Increased Availability Quality Information:
  - Will greater transparency drive increased quality competition?
- Pay-for-Performance:
  - Major potential restructuring hospital finances, possibly driving shake out?
  - Potential incentives to increase vertical integration hospitals and physicians?

Health Reform:

- Covering the Uninsured
  - Bad debt reduction
    - New opportunities for-profits?

- Payment Reform:
  - Focus disease management, prevention, wellness
  - Possible bundling/ global fees
    - Implications for integration?

Table 1: Spending on Hospital Care 1929-2006: All Hospitals

Year	National Health Expenditures (Billions)	National Health Expenditures as Percentage of Gross Domestic Product	Hospital Expenditures (Billions)	Hospital Expenditures as Percentage of National Health Care Expenditures	Hospital Expenditures as Percentage of Gross Domestic Product
1929	3.6	3.5	0.7	19.4	0.7
1948	10.6	4.1	3.2	30.2	1.2
1955	17.7	4.4	5.9	33.3	1.5
1965	41.1	5.7	14.0	34.1	1.9
1975	130.7	8.0	52.6	40.2	3.2
1985	428.7	10.3	168.3	39.3	4.0
1995	1,020.4	13.3	340.7	33.4	4.4
2000	1,353.3	13.8	417.0	30.8	4.3
2006	2,105.5	16.0	648.2	30.8	4.9

Sources: 1929-1955: U.S. Bureau of the Census, Historical Statistics of the United States, Colonial Times to 1970, Bicentennial Edition, Part 1 (Washington, D.C.: 1975); 1965-1996:
National Center for Health Statistics (1998) Health, United States 1998, (DHHS Publication No. (PHS) 98-1232). Health, United States 2006, (DHHS Publication No. 2006-1232).Catlin A et al. "National Health Spending In 2006: A Year of Change for Prescription Drugs" *Health Affairs*, January/February (2008) 27:1 14-29.

Table 2: Community Hospital Characteristics 1928-2005

Hospital Characteristics:	**Year: 1928**	**1946**	**1955**	**1965**	**1975**	**1985**	**1995**	**2000**	**2005**
Number Community Hospitals:									
Nonprofit	1,889	2,584	3,097	3,426	3,339	3,349	3,092	3,003	2,958
Government	540	785	1,120	1,453	1,761	1,578	1,350	1,163	1,110
Investor Owned	1,877	1,076	1,020	857	775	805	752	749	868
Total	4,306	4,444	5,237	5,736	5,875	5,732	5,194	4,915	4,936
Number Community Hospital Beds: (1000s)									
Nonprofit	197	301	389	515	658	707	610	583	561
Government	81	133	142	179	210	189	157	131	128
Investor Owned	58	39	37	47	73	104	105	110	113
Total	336	473	568	741	942	1,001	872	824	802
Average Beds per Hospital									
Nonprofit	104	117	126	150	197	211	197	194	190
Government	150	169	127	123	119	120	116	112	115
Investor Owned	31	36	36	55	95	129	141	147	131
Total	78	106	109	129	160	175	168	165	163

Sources: 1928-1965: William D. White (1982) "The American hospital industry since 1900: A short history."in R. Scheffler and L. Rossiter (eds), *Advances in Health Services Research*, Vol. 3 (Greenwich CT: JAI Press). 1975-1996: National Center for Health Statistics (1998) Health, United States 1998, (DHHS Publication number (PHS) 98-1232). National Center for Health Statistics (NCHS) 2007. *Health, United States 2007*. DHHS Publication (PHS) 2007-1232.

Table 3: Sources of Hospital Revenues 1965-2005
All Hospital Care

	Year: 1965	**1970**	**1975**	**1980**	**1985**	**1990**	**1995**	**2000**	**2005**
Total Expenditures (billions)	14.0	28.0	52.6	102.7	168.3	256.4	340.7	417.0	611.6
Percent Distribution:									
Out-of-Pocket Payments	19.6	9.0	8.3	5.2	5.2	4.0	3.1	3.3	3.3
Private Health Insurance	40.9	32.4	32.9	35.5	35.0	36.9	32.5	34.4	35.5
Other Private Funds	1.9	3.2	2.7	4.9	4.9	4.2	4.3	5.2	4.5
Government:									
Medicaid*	--	9.5	10.0	10.3	9.3	11.5	16.7	17.0	17.3
Medicare	--	19.2	22.0	25.7	29.1	27.3	31.4	30.1	29.5
Total Government All Sources*	37.6	55.4	56.0	54.4	54.8	56.6	60.2	57.1	56.8

Source: National Center for Health Statistics (1998) Health, United States 1998, (DHHS Publication number (PHS) 98-1232). Health, United States 2007 (DHHS Publication No. 2007-1232).

*Medicaid category excludes Medicaid SCHIP Expansions and SCHIP
** Includes all local, state and federal government expenditures including Medicaid SCHIP Expansions and SCHIP and care funded by the Department of Veterans Affairs

Table 4: Health Plan Enrollment: Covered Workers by Plan Type 1988-2008

Health Plan Type	**Year:**							
	1988	**1993**	**1996**	**1999**	**2002**	**2005**	**2006**	**2008**
Conventional Indemnity Insurance	73%	46%	27%	14%	4%	3%	3%	2%
HMO	16%	21%	31%	27%	27%	21%	20%	20%
PPO	11%	26%	28%	35%	52%	61%	60%	58%
POS	*	7%	14%	24%	18%	15%	12%	12%
High Deductible Health Plan With Savings Option	*	*		*	*	*	4%	8%

Source: Kaiser Family Foundation and Health Research & Educational Trust, *Employer Health Benefits 2006 Annual Survey,* Kaiser Family Foundation Publication #7315 (2006), Kaiser Family Foundation and Health Research & Educational Trust, *Employer Health Benefits 2008 Annual Survey,* Kaiser Family Foundation Publication #7790 (2008)

*Data category not collected