



Health Care Spending Growth: Utilization and Drug Prices Driving Recent Increases

Over the past several years, health care spending growth has been at historic lows, but in the first half of 2015, growth accelerated. It is important to understand the factors driving this trend.

Factors Driving Growth: Health care spending is a function of the amount of health care services provided, the price paid for those services, and the mix of those services. The amount of health care services reflects the population's demand for health care. It can be influenced by economic conditions, coverage levels, health status and other factors. Researchers attribute the recent historical low growth to a number of factors, including the economic slowdown, as well as structural changes in the health care system as providers begin to transition to value-based care and insurers implement new plan designs (e.g., high-deductible plans) that encourage consumers to reduce their consumption of care.

Utilization: Utilization of health care services grew at a rate of 4.5 percent for the period ending in June of 2015, nearly double that of the same period in 2013. There are a number of reasons why this may be occurring. First, since 2013, there has been a net increase of 15.8 million people with health insurance. That is an increase of 5.8 percent in the number of people with coverage. That alone could be driving the increase in utilization seen in 2015. Hospitals, particularly in states that expanded Medicaid, are reporting increased admissions and emergency department visits in 2015. Second, the economy is improving. When the economy is performing poorly people tend to put off elective procedures. As things improve, the pent up demand is released, leading to higher utilization. Hospitals are adding staff to meet this demand for care.

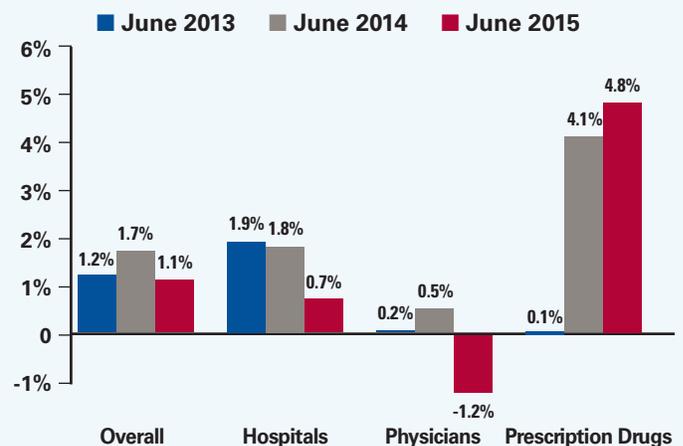
Mix: The mix of services provided may change because of advances in medicine or changes in the population. For example, as the Baby Boomers age, many are living longer with more chronic conditions. New technology, especially specialty drugs, also is changing the mix of services provided and driving up health care spending. The PwC Health Research Institute estimates that the new hepatitis C drug Sovaldi, at a cost of \$84,000 for a course of treatment, pushed up employer health spending by half a percentage point in 2014 and will push it up another one-fifth percentage point in 2015. New cancer drugs are having a similar impact on spending trends. Payer mix also plays a role, with the uninsured paying little or nothing and public payers such as Medicare and Medicaid paying less than the cost of providing services for their beneficiaries. For example, in 2013, underpayment by Medicare and Medicaid to U.S. hospitals was \$51 billion. Medicare reimbursed 88 cents and Medicaid reimbursed 90 cents for every dollar hospitals spent caring for these patients. Payer mix is changing as more people gain coverage. Hospitals are seeing a significant drop in uncompensated care especially in expansion states. This trend also is leading to increased health care spending.

Price: Price reflects the cost to provide services plus an additional margin used to support underfunded services and for reinvestment in new technology and an organization's physical facilities. The most current data show that price growth for hospital and physician services is not a factor in the recent acceleration in health care spending, with hospital prices increasing by less than 1 percent and physician prices decreasing (see chart below). Price growth for prescription drugs, however, is much higher at 4.8 percent, and significantly higher than what it had been in the prior year. Drug shortages and manufacturer consolidation are driving up prices for generic drugs in particular. For example, the price for a 500 mg capsule of tetracycline, a common antibiotic, has gone from \$0.05 to \$8.59 per pill.*

*Retail Generic Drug Inflation Reaches New Heights. Drug Channels. August 12, 2014. <http://www.drugchannels.net/2014/08/retail-generic-drug-inflation-reaches.html>

Price growth for prescription drugs is outpacing that of hospital and physician services.

12-Month Growth Rates in Health Care Prices for Periods Ending June 2013, 2014 and 2015



Source: Altarum Institute, Insights from Monthly National Health Spending Data through June 2015, Price Brief, August 13, 2015