Estimate of the Situation

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Paradigm Shift!

"We don't see things as they are, we see things as we are." - Anais Niin

On July 30, 1965, President Lyndon Baines Johnson signed Medicare into being and everything changed.

Virtually everyone now working in the health care field grew up (professionally speaking) in the world that Medicare created. Most have no memory of what hospitals were like in the days before Medicare nearly half a century ago. The changes Medicare wrought were great—and not only in health care.

Today we find ourselves in the midst of another paradigm shift, one possibly more profound than that brought about by Medicare. As was the case in 1965, the shift is partially brought about by changes in the way that health care is paid for (although other forces are also at work). In the case of Medicare, there was some certainty. Although the "experts"—including the program's architects--missed badly on estimating program costs, everyone knew that a very large amount of new money would be diverted to health care. In the case of the Affordable Care Act, the ultimate financial effects on health care and the general economy are far less clear.

The United States of today and the United States of 1965 are not the same nation in many important ways.

1. Economically: The American service-based economy of 2014 bears little resemblance to the manufacturing and agriculture-based economy of 1965. Government consumed far less of the GDP prior to the implementation of "Great Society" programs. International trade has assumed immense importance.

2. Demographically: The United States has become an older, more ethnically diverse, more urban, and more obese nation that consumes health and other social service resources at a far greater rate than was the case in 1965.

3. Technologically: The last half century has seen the introduction of personal computers, the Internet, fiber optic networks, cellular and satellite communications, GPS, advances in microelectronics, digital imaging and other diagnostic and treatment technology, all of which permit smaller, leaner, more efficient organizations to outperform large, traditional organizations in terms of service quality, turn around time, and cost.

Hospital governing bodies and management teams find themselves confronted with the need to make unprecedented decisions in a very tough operating environment. It is difficult for some stakeholders to distinguish between the current new and urgent need to act strategically and the decades-old urgings of financially-oriented decision makers to reduce costs. Among those who recognize the imperatives of the new environment and see the need for swift and decisive action the risks are both obvious and plentiful. The temptation is great to use tried and true methods. These include the securing and expansion of market share through acquisition and the reliance on building organizational mass to realize economy of scale benefits.

The market share acquisition model is potentially dangerous for both the acquiring hospital and the entity being acquired or, at least, the community served by the entity being acquired. The acquiring institution needs to assure itself that it is not primarily purchasing rapidly obsolescing and very expensive buildings. Given the apparent elasticity in primary care demand, this is especially important for community hospitals and systems made up of community hospitals. The community served by the entity being acquired must consider not only the impact of losing control of local health care but also the potential financial implications of that loss.

Potential economy of scale benefits should also be examined with a good deal of healthy skepticism. Large organizations of necessity spend more time on organizational maintenance than do smaller organizations. Resources required to maintain an organization are not available to do the work of the organization. Increasingly, due to regulatory pressures and other considerations, administrative and bureaucratic overhead costs are growing exponentially and the growth curve is not encouraging. Caution is advised.

In previous editions of this newsletter, we have observed that two competing models of American health care are developing.

- One model relies upon large centrally administered and financed bureaucratic delivery organizations that provide standardized treatments from an approved list and control utilization through regulation.
- The other is composed of decentralized, horizontally distributed, entrepreneurially managed, privately financed networks or associations of service delivery units that may be owned or contracted employing completely transparent market-based pricing with utilization controlled by consuming patients.

Interesting times lie just ahead.

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