



Peter Burgess LinkedIn Blogs

Cost and Price in US Healthcare

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There is a lot of commentary about the state of US healthcare, but for me, this conversation is rarely clear about cost and price. There is a difference between the cost of healthcare, and the price of healthcare, and this difference is important. What the user of the healthcare system pays for health services is the result of prices. What the deliverer of the healthcare pays for everything are costs.

Over time there have been big changes in the costs, and because of great technology many aspects of healthcare have much reduced cost. For example the advent of antibiotics reduced the cost of disease control substantially. The cost of aspirin therapy is very very low.

The cost of running the healthcare system should have gone down significantly with the advent of IT, but it is not at all clear that the power of IT delivered much in the way of cost reduction. There has to be a reason!

The cost of training for positions in the medical field has increased over time, just as education in general has increased in cost over time. Why is this? A big part of this answer may be that the shortage of medical staff has enabled the price (wages) of medical staff to increase so that the cost of education did not matter very much. Innovations in the way medical staff get trained and certified could have changed significantly, but has not.

For most people receiving medical care, the price of medical staff is not a direct concern, because this price is being paid by some third party payer. The receiver of medical care usually pays into some sort of a pool with very little negotiated other than in the broadest possible terms. Third part intermediaries try to match costs with prices in a way that best serves their stakeholders. In for profit intermediaries, investors are an important stakeholder, yet it is not at all clear whether their investment brings any significant benefit into the healthcare space.

Some of the technology being used in the healthcare sector is amazing. Companies like GE and Siemens have put a price on this equipment that is very high, and these business segments are very profitable for the respective companies. In other words, the cost of this equipment is significantly lower than the price. Maybe the profit is reasonable, maybe not.

The differential between cost and price in the pharmaceutical segment of the healthcare industry is a matter of interest. Research and development is a real cost in this part of the healthcare industry ... but it can also be said that keeping investors happy with more and more profit is also a very real cost in this industry. Whether or not the pharmaceutical industry has optimized its performance with respect to health outcomes has not been as important as optimizing performance with respect to stock price metrics.

Some of the actors in the healthcare sector understand the difference between cost and price, and the way profits and premiums are earned. I am reminded of the very active lobbying efforts of the American Medical Association (AMA) at the recent past political conventions. It seems that the AMA are very protective of the status quo and the reason for this is that there is a very large profit or premium differential between the cost of healthcare and the price of healthcare. To what extent the shortage of staff in the health sector is a function of reality or is some artificial creation that has the result of being a big benefit to insiders at the expense of everyone else.

Thinking about everything that is going on in the healthcare sector through the lens of both cost and price gets very interesting. A simple conclusion is that in large part the US healthcare industry has been run for its own benefit rather for the benefit of society as a whole. I argue that this should come as no surprise because the basic business model of the industry has been to make anything that approaches a 'market solution' end up being of benefit to the industry. In my view many of rules and regulations have been 'gamed' so that in the end the rules ended up being another way that there is more benefit to the industry.

Thinking more clearly about cost and price is a first step in getting to understand better what is going on in the industry ... and then, perhaps, getting some reforms so that price more reasonably relates to cost. It is only a step ... the industry is very complex with a very large number of actors and stakeholders ... but one has to start somewhere.

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