

# The New Rules of Healthcare Demand

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**H**ealthcare is an industry in which demand is growing, but the nature of that demand is rapidly changing. Hospitals and health systems face new forces that are reshaping the rules of healthcare demand, including:

- Medical and technological advancements that are pushing more care to non-hospital settings
- Consumer demand for the same level of access and convenience they encounter elsewhere
- Concerted efforts by payers to lower costs
- New competitors that seek to peel services away from legacy organizations, unburdened by the costs of providing inpatient care

Movement toward lower-cost, more convenient, high-quality care is a common denominator and forms the basis of the new rules of healthcare demand. Legacy providers need to acknowledge—and adapt to—these new rules. Hospital and health system executives and directors should focus on broadening their view of healthcare to establish a role for their organizations within an even more diversified future delivery system.

## Movement Away from Hospitals

Total healthcare expenditures are projected to continue a rapid upward trajectory, growing 55 percent over the next eight years, from \$3.68 trillion in 2018 to an estimated \$5.7 trillion by 2026.<sup>1</sup> Most healthcare sectors have a positive outlook, including non-hospital outpatient care, ambulatory surgery centers, physician services, home care, and virtual care. The outlooks for acute inpatient and hospital-based outpatient care, however, are not so optimistic.

Not surprisingly, acute inpatient care is projected to continue to decline as technology and care delivery advances shift more care to outpatient and home-based services. Continued pressure from payers, employers, and

consumers to provide care in lower-cost settings is another accelerating factor.

Hospital-based outpatient care is projected to fall with the rise of numerous competitors, including retail chains, physician groups, insurers, and other for-profit ventures. Payers are aggressively redirecting enrollees to non-hospital settings. Anthem BlueCross BlueShield, for example, no longer pays for ambulatory MRIs and CT scans performed in hospitals without preauthorization,<sup>2</sup> and the Centers for Medicare and Medicaid Services reduced payments for outpatient services in hospitals and off-campus hospital outpatient departments.<sup>3</sup>

How care is paid for also is shifting, as individuals and government payers assume an increasing share of healthcare costs. Private employer-based plans make up 46 percent of health plan enrollments, down from 48 percent in 2008. Conversely, Medicare and Medicaid increased from 24 to 31 percent of total enrollments over the last decade. High-deductible health plan enrollments rose from 16 percent in 2008 to 43 percent in 2017.<sup>4</sup>

These shifts contribute to new consumer attitudes about healthcare access, experience, and costs. Eighty-one percent of consumers are unhappy with their healthcare experience.<sup>5</sup> Consumers' dissatisfaction and the emergence of new competitors mean that hospitals and health systems risk losing out on rising demand if they do not adapt.

## New Competition for Rising Demand

Despite declining demand for hospitals, overall demand for healthcare services is robust due to a growing population and associated healthcare spending increases. The U.S. population is projected to grow 3.4 percent to 339

## Key Board Takeaways

Demand for hospital-based services is declining, but overall healthcare demand is robust. Hospitals and health systems risk losing out if they do not adapt to the new rules of healthcare demand. To compete, legacy organizations need:

- A consumer-focused platform
- A compelling brand and value proposition
- Culture and governance that supports innovation
- Broad market presence
- Capital and resources for innovation
- Ability to attract, develop, and retain top talent
- Ability to attract essential partners, and maximize partnerships

million within the next five years and surpass 388 million by 2050.<sup>6</sup>

Younger adults ages 19–44 make up the largest segment at approximately 35 percent. Ages 45–64 is the next largest at 26 percent, and 65 and over is 16 percent. Those percentages run inverse to total health expenditures. Just 21 percent of healthcare expenditures are attributed to individuals ages 19–44, while ages 45–64 comprise 33 percent, and ages 65 and older make up 36 percent.<sup>7</sup>

Individuals ages 65 and older will continue to generate the most healthcare demand, but legacy hospitals and health systems can ill afford to lose younger generations, as they will be the base from which future demand will grow. Even with high spending among seniors, adults ages 19–64 constitute 54 percent of healthcare expenditures. This represents significant opportunity. The loyalty of these groups is the primary target of new competitors looking to reshape healthcare delivery with low-cost, digitally enabled services.

Many competitors are combining across sectors to combat legacy organizations, bringing a new level of scale to the industry. CVS Health and Aetna, for

1 Centers for Medicare and Medicaid Services, *National Health Expenditures Projections 2017–2026*.

2 Anthem Blue Cross and Blue Shield, "Imaging Program Expands to Include Level of Care Reviews: FAQs" (Press Release), 2017.

3 Virgil Dickson, "CMS Dials Back Plan to Slash Payment for Off-Campus Services by Half," *Modern Healthcare*, November 2, 2017.

4 Robin A. Cohen and Emily P. Zammitti, "High-Deductible Health Plan Enrollment Among Adults Aged 18–64 with Employment-Based Insurance Coverage," Centers for Disease Control and Prevention, August 2018.

5 GE Healthcare Camden Group, *The Current State of the Patient Experience*, 2018.

6 U.S. Census Bureau, "Projected Population Size and Births, Deaths, and Migration, 2017–2060," Last revised September 2018.

7 Centers for Medicare and Medicaid Services, *National Health Expenditures Projections 2017–2026*.

example, closed their \$69 billion merger in November 2018. The two companies had combined revenues of \$240 billion in 2017, more than five times that of HCA, and more than eight times as much as Dignity Health and Catholic Health Initiatives' (i.e., CommonSpirit Health's) combined revenues.

With more than 1,100 clinics and retail stores within 10 miles of half of Americans, Larry Merlo, CEO of CVS Health, said the combined organization will "create an innovative, new healthcare platform that will be easier to use, less expensive for consumers, and integrated broadly within the marketplace to deliver superior, coordinated care."<sup>8</sup>

Initial plans include targeting chronic disease management, improving care transitions, and managing high-risk patients through retail clinics, home-based services, virtual care, and data and advanced analytics. Merlo estimates the company will see an additional \$500

million in operating margin for every 50-basis-point reduction it contributes to the medical cost trend.<sup>9</sup>

Faced with such competitors, hospital and health system leaders must rethink traditional care delivery. The industry imperative is shifting from a focus on providers to a focus on consumers.

To be successful in the future, legacy healthcare organizations need:

- A consumer-focused platform that emphasizes convenience and access through both digital and physical care sites
- A distinct and compelling brand and value proposition
- A culture and governance structure that supports innovation and change
- Market presence across a sufficiently broad geography
- Capital and resources for innovation, research, and development
- Ability to attract, develop, and retain top talent at all levels

- Ability to attract essential partners, and strategies to maximize those partnerships

Yes, overall healthcare demand is strong, but there is no shortage of competitors seeking to draw upon that demand and disrupt legacy providers. Hospital and health system leaders must broaden their focus to appeal to all generations. They cannot endure by serving only older, sicker patients. As famed business professor and author Peter Drucker put it: "The greatest danger in turbulent times is not the turbulence, but to act with yesterday's logic." ●

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<sup>8</sup> Larry Merlo, *First Quarter 2018 Earnings Presentation*, CVS Health, May 2018.

<sup>9</sup> Tomi Kilgore, "CVS Health Looks to Cut Health-Care Costs and Boost Profit with New-Look Stores," *MarketWatch*, January 9, 2019.