

Industrial Evolution

CAN MICHIGAN'S VITAL HEALTH-CARE INDUSTRY LIVE UP TO ITS PROMISE?

As our state pines and prays for economic turnaround and salvation, few industries hold more of the "Holy Grail" promise than health care. No industry offers more of what it takes to enrich firms and their participating workers. So, at a time when auto companies are spinning off skilled workers by the tens of thousands, we'd naturally expect one of Michigan's growth industries to re-employ many of them with open arms. Indeed, if the business climate were inviting, this would be a slam dunk.

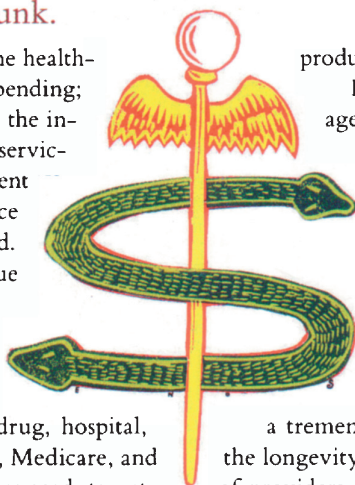
What are the prosperity-assuring factors in the health-care industry? They include: rapid growth in spending; dynamic investment in technology related to the industry; addictive qualities of the products and services being marketed; and guaranteed replacement demand. Let's see what Detroit could experience if the past is prologue in the health-care field.

Spending on health care will continue trending dramatically upward because population and discretionary personal incomes are rising, and the population is aging. Moreover, governments are redistributing ever-greater sums of tax revenues toward drug, hospital, and general care programs such as Medicaid, Medicare, and welfare. Even larger allocations are being proposed, targeting children, noninsured (voluntary and nonvoluntary), and immigrants (legal and illegal).

For example, in Detroit, notwithstanding government workers, health care already constitutes the largest private-sector job provider. Health care exceeds the auto industry statewide in private employment, with nearly half a million workers. More than a quarter million work in the nine-county southeast Michigan corridor.

Senior citizens, the wealthiest segment of the U.S. population, are the largest consumer of health-care services. In fact, per person, Americans 75 years of age and older spend 75 percent more on health care than do the next age cohort: those 65 to 74. Moreover, they spend nearly 300 percent more than the overall average.

And guess which way the aging baby boomers will take these numbers? Just 25 years ago, those over age 65 constituted less than seven percent of the population (30 million). Twenty-five years from now, their share of the population will reach 18 percent (75 million citizens). This is why health care already absorbs 16 percent of gross domestic product and will account for a quarter of the economy by 2030. Proportions for Michigan's gross state product and Detroit's gross regional



product do not vary materially from these estimates.

In fact, in 2006, total health-care outlays averaged \$19,000 per household, of which \$11,000 (58 percent) was government subsidized.* Thus, when it comes to spending on health care, demographics, rising incomes, and government intrusion all assure growth.

Technology also favors rising prosperity in the health-care industry. From medical devices to pharmaceuticals and bio-tech industries, the United States holds a keen comparative advantage. Technology is at once a tremendous export industry and a factor improving the longevity of patients and the efficiencies (bottom lines) of providers. Improved drugs and drug therapies encourage specialization among hospitals, as well as growth in home care and rehab-regional centers.

Addiction is associated with unhealthy products like tobacco and alcohol. But addiction sustained their phenomenal sales. Ironically, "addiction to healthy lifestyles" now sells well. Schools promote more healthful eating, insurance companies and workplaces advertise regular checkups, and public-service announcements urge preventive medicine. To the extent these behaviors are instilled in the citizenry, there will be an "addiction" to health routines that augments the industry while lowering the proportion of catastrophic-care cases, thereby improving economic productivity.

Last but not least, profitable industries have a built-in replacement demand. Rapid aging of our population — from a median age of 27.8 in 1967 to 36.8 now and to 38.5 by 2030 — assures greater demand for medical care. Repeat protocols, from replacement and transplant surgeries to drug upgrades, are part and parcel of this replacement (or after-) market. And some hospital groups are already experimenting with "90-day warranties" on operations to encourage better care.

In the 14-county corner of southeast Michigan alone, there are 50 major hospitals, with approximately 14,000 beds.

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Together, with physicians, pharmacies, and other health-care providers, they account for some \$36 billion of Michigan's total gross state product. Direct spending on health care sets off a ripple effect of expenditures for products and services in ancillary industries, such as real estate, construction, finance, and retail. The overall economic impact is closer to \$72 billion, or roughly 20 percent of the state economy.

That's today's good news. Looking ahead, there's promise and peril facing Michigan's health-care industry. First, according to SEC (regulator) filings, General Motors Corp., has \$68 billion in post-retirement, hourly employee health-care obligations; Ford Motor Co., \$31 billion; Chrysler Group, \$19 billion. Auto-supplier firms add tens of billions to these largely unfunded liabilities. These numbers are national in scope, yet the consequence of unfunded obligations is profound on local firms that are downsizing.

As local firms cut payrolls and health costs, medical providers will also be obliged to merge or downsize. Likewise, as public-sector health-care contracts get the scalpel, double-digit projections in annual health-care premiums will be trimmed.

Second, facilities catering to indigent patients must rationalize their location and delivery systems. As with banks, retailers, or realtors, failure to make profits or gain proximity to paying clients means bankruptcy.

Third, Michigan has installed myriad disincentives to growth in health care. For example, a) Lansing blacklists pharmaceuticals that fail to adhere to its formulary (which is a price control on drugs); b) municipalities make it difficult to get building permits; c) "prevailing wage" statutes drive up construction costs, compressing profit margins; and d) Lansing mandates nonessential Medicaid treatments.

With a normally operating regional economy, displaced workers from Detroit's automotive industry would be re-absorbed by the rapidly expanding health-care sector. But for our health-care industry to reach its stride, Michigan's overall business climate must improve first. **db**

* SOURCE: Eugene Steuerle, "Is Health Spending Out of Control?" National Center For Policy Analysis, Brief Analysis No.586, May 17, 2007



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