

Healthcare Reforms In The US : A Multi-Billion Opportunity For Indian Firms

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BRIEF BACKGROUND OF THE US HEALTHCARE INDUSTRY

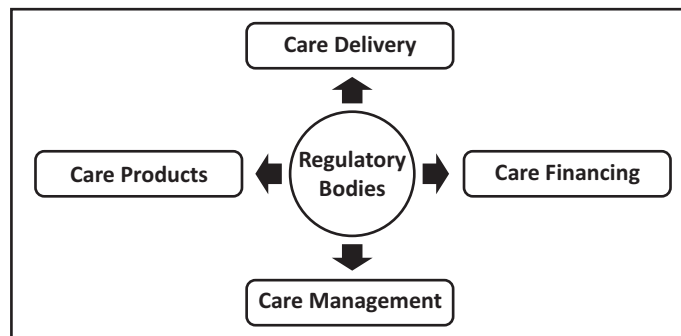
The US health care industry is a complex entity with significant contrasts. Despite its leadership position in health care spending and medical research, over 45 million of the US population continue to be uninsured and cannot afford even basic medical care. To understand this paradox, one needs to take a look at the history of health care in the US.

As early as in the 1920's, US hospitals evolved into modern scientific institutions and along with this development came the beginning of health insurance, as a prepaid hospital plan, for covering sickness. This model was quickly embraced by the large workforce based organizations such as the auto and the railroad companies and employer sponsored health insurance plans became the de facto health benefit operating model in the US.

During the 1960's, as medical research began to cover a range of illnesses, cost of medical care increased, thereby making health insurance also unaffordable to the public. To address this, the US government created the Medicare and Medicaid social programs in 1965. Medicare extended health coverage to almost all Americans aged 65 or older and Medicaid provided access to health care services for low income and poor persons and people with disabilities.

Over the last few decades (1970-2010), due to the country's stress on private capital, medical research, innovation and risk taking management approach, US became the leader in various fields of health care. Further, with constant industry consolidation, the landscape is currently being dominated by large private sector health care entities, such as health insurance firms, hospitals, pharmaceutical companies, biomedical devices and equipment companies. Due to this level of corporatization and limited competition, the sector is characterized by high costs and profit maximization. As a net result, the US is currently the world's largest and most expensive health economy with an annual spend of \$2.3 Trillion. Even when compared to other developed nations, US's health expenditure at 16% of its GDP is much higher than the OECD average of 10%. And unlike other OECD countries, majority of the health expenditure (53%) in US is borne by private which includes private insurance and member out-of-pocket funds. US healthcare today is an interlinked system of care delivery, care financing, care management and care products, controlled by health care regulatory bodies, as shown below in Figure 1.

Figure 1 : Interlinked Entities In US Healthcare



Care delivery includes all entities that deliver medical care to patients such as hospitals, care facilities, physician practices and other medical care providers. Care financing includes all entities that finance the care, includes individuals, employer groups, government agencies and insurance companies. Care management includes all entities

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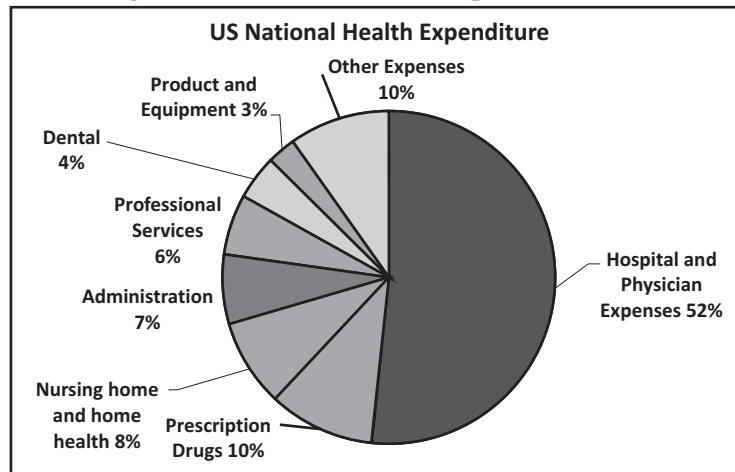
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that manage care and healthcare utilization including health insurance, care management companies and other care intermediaries and care products includes medical products such as drugs, devices and equipment. Regulatory bodies include the various agencies that regulate the healthcare process such as Food and Drug Agency (FDA), Department of Health and Human Services (DHHS), Centre for Medicaid and Medicare (CMS) etc. In terms of spending, the major of expenditure is on care delivery such as hospitals, physicians and clinical expenses (over 50%), followed by care products such as prescription drugs (10%), as shown in the Figure 2.

Figure 2 : National Health Expenditure (US)



Source: Centres for Medicare & Medicaid Services, USA. National Health Expenditures Data.

Over the years, the US healthcare system, despite being a pioneer in most health aspects and high spend on healthcare, has become constrained by significant challenges such as cost escalations, premium increases, uninsured population, medical fraud and waste, dominant industry cartels, physician and nurse shortages, regional variation in quality of care (poor healthcare in rural communities), lifestyle and chronic diseases such as obesity, low spending on public health and other systemic deficiencies.

CHANGES IN US HEALTHCARE - IMPACT OF TWO EPIC LEGISLATIONS

Given the challenges in the healthcare system, successive US governments have been trying to streamline the healthcare system by bringing in legislative changes. Historically, wide ranging healthcare reforms have always been opposed by political and business interests, but the current US government has exploited the subdued global business environment and has passed two epic laws, that have a major impact on the US healthcare system.

✿ **American Recovery And Reinvestment Act:** In early 2009, the US government passed the \$800 Billion US Stimulus bill, also known as the American Recovery and Reinvestment Act (ARRA) of 2009, which provides stimulus funding for various sectors, including healthcare. The HITECH Act (Health Information Technology for Economic and Clinical Health Act) is part of ARRA, and is designed in specific to increase usage of computerized medical records and also help an overall increase in computerization and automation, so as to improve the quality of healthcare while lowering its costs. Increased computerization will cut waste, eliminate red tape and reduce the need to repeat expensive medical tests and is expected to save billions of dollars and also save lives by reducing preventable medical errors. Apart from the provisions of the HITECH Act, which focuses primarily on health related computerization, the ARRA Act also has a huge outlay for funding for the Medicaid program. In total, ARRA lays out over \$130 Billion (inclusive of \$20 Billion for the HITECH funding) for various healthcare initiatives shown below in Table 1.

✿ **Healthcare Reforms Act :** Apart from the ARRA and HITECH Acts, the US government in March 2010 passed the Healthcare Reforms Bill, also known as the Patient Protection and Affordable Care Act (PPACA), after a year long debate involving all stakeholders. This Act, along with its reconciliation bill, the Health Care and Education Reconciliation Act, is expected to cost over \$900 Billion over a ten year period. The major highlights of the reforms bill are listed in Table 2.

Table 1 : Major Healthcare Aspects Of US Stimulus Bill (ARRA)

Healthcare Funding	\$ Billion
Federal aid to states for Medicaid spending.	90.0
Incentive payments to hospitals and physicians for computerized medical records systems.	17.6
National Institutes of Health Biomedical research.	9.5
Renovation and health IT purchases for community health centres.	2.0
Office of the National Coordinator for Health Information Technology .	2.0
Other initiatives (community health, nurse training, health facilities, nutrition services, comparative effectiveness research, health employment, child care etc).	8.4

Source : The Wall Street Journal.

Table 2 : Major Aspects of the Healthcare Reforms Act (PPACA)

Objective	Key reform mechanisms	Expected Benefits
Cover more lives under insurance	- Residents to obtain minimum health coverage. - Employers to offer coverage options. - Expand coverage through government programs such as Medicaid. - Tax credits and subsidies for individuals and employers. - Create state level health exchanges through which individuals and small businesses can purchase qualified coverage.	32 Million uninsured will be covered under health insurance.
Regulation of Private Insurance Firms	- Coverage of pre-existing medical conditions. - Requirement to report the proportion of premium dollars spent on clinical services. - Prohibit individual and group health plans from placing lifetime limits. - Increased consumer protection.	Make insurance firms more accountable and transparent.
Cost Containment	- Streamline Medicare and Medicaid programs. - Encourage use of generic drugs. - New initiatives to control waste and fraud.	Reduce the federal deficit by more than \$1.2 trillion by 2030.
Improving Quality Of Care	- Streamline care delivery and reduce regional disparities in quality of care and more transparency in medical costs. - Accountability from hospitals serving Medicare and Medicaid patients.	Standardize and improve care quality.
Prevention and quality	- Preventive care services. - Wellness and nutrition initiatives.	Disease prevention and promote wellness.
Long term care	- Initiatives for community living assistance services. - Streamline skilled nursing facilities.	Improved care for the aged and chronic diseases.
Improved medical infrastructure	- Improve workforce training and development to address medical workforce shortages. - Improved community health centres and school based health centres. - Strengthen emergency department and trauma centre capacity. - Improved public health and disaster preparedness.	Significant improvements in public health medical infrastructure.
Patient centred initiatives	- Patient oriented outcome research authorized. - Changes to tax structures for health related accounts. - New patient care models to be created.	Improve individual care delivery and financing models.

Source: Kaiser Family Foundation

EXPECTED CHANGES

As these two laws come into operation, the healthcare entities will need to revise their strategies to cope with these

changes. The following paragraphs describe some of the significant changes affecting the various entities in the US healthcare system.

1) The biggest impact of these reforms are on hospitals and physicians who will now be incentivized with \$20 billion funding, to procure and use electronic health records (EHR), which is mandatory if they want to do business with government, as part of Medicare and Medicaid. The hospitals and physicians also need to gear up to address the healthcare needs of an additional 32 million patients, who will now be covered by insurance. Along with this increase in patient population, the government has also included \$150 billion reimbursement cuts, which will reduce the payments doctors will receive for treating Medicare patients. These new rules will result in hospitals and physician groups implementing EHR systems in an accelerated manner and evaluate all solutions that help them to rationalize their operating costs. The additional 32 million patients will also trigger enhanced demand for medical professionals such as doctors, nurses, pharmacists and other related skills.

2) The other major impact is on health insurers, who will now get a government subsidized additional 32 million members but will face controls on how much they can show as profits. The rules now mandate that insurers have to spend eighty-five cents of all premium dollars on medical costs. In other words, they have to run their business on the balance fifteen cents of the premium dollar. The new rules also deny them the freedom to turn down insurance on the basis of pre-existing conditions and also imposes a \$74 billion additional taxes and fees over the next ten years. These changes are going to force insurers to streamline and cut costs in their operations along with pressure on forcing the hospitals to reduce their medical claim amounts.

3) There is lesser impact on other major entities such as the pharmaceutical firms and medical device firms, who will see increased business because of the additional 32 million insured members and pharmaceutical firms in specific will also will see an increased demand for generics, as part of the new rules. The vendors will also face an estimated \$110 billion of additional taxes and fees over the next ten years.

OPPORTUNITY FOR INDIAN FIRMS

The combined \$ 1 trillion impact of the two US healthcare laws will have a significant effect on various aspects of global economy and more so on India, which has a long association with US healthcare entities. The long term effect of the healthcare laws will be seen in the following areas and will give rise to significant opportunities that can be exploited by Indian firms.

✿ **Healthcare IT Firms:** The single biggest opportunity is for IT firms, which can leverage the \$20 billion funding for computerized EHRs along with the other IT initiatives announced as part of the HITECH Act. IT firms with experience in electronic medical records and knowledge of US healthcare environment will be in a position to quickly benefit from the increased spending on computerized medical records. Additionally, the medical home and patient centric care models listed will throw up huge opportunities for IT firms in the area of telemedicine and remote monitoring and diagnostics solutions and services. Finally, the relentless pressure to control costs will ensure there is increased IT outsourcing as all health entities try to streamline their operating costs.

✿ **Healthcare BPO Firms:** With an additional 32 Million Americans coming under the health insurance schemes, this offers a huge administrative burden on the existing infrastructure. At \$12 per member per month in administrative expenses, this adds an additional \$4 Billion to the existing costs. Healthcare BPO firms need to position themselves to benefit from the possible outsourcing opportunities that this will entail such as enrolment processing, customer service, claims processing, billing and medical coding services etc.

✿ **Nurse Facilitation:** US has a perennial nursing shortage which will be further accentuated by the additional 32 Million insured. Moreover, the community living assistance provisions in the reforms bill addressing the aging and retiree population, will increase the demand for nurses and care givers. The current shortage of 100,000 nurses is expected to go up to over 200,000 over the next ten years. Typically, this translates to a \$2 Billion opportunity in nurse staffing services. Currently, India is the fourth largest supplier of nursing professionals to the US after Philippines, Canada and Korea. Nursing education institutes and medical agencies in India and travel facilitators will need to work with The US government and hospitals to evolve a mechanism to ensure India can provide a significant number of these requirements without affecting India's internal health requirements.

✿ **Medical Tourism:** Two aspects of the US healthcare laws will trigger an increase in medical tourism. One is the increase of 32 Million patients, which is likely to cause waiting times for medical treatment and two is the tight control mandated by the government on medical expense ratio for health insurers. Because insurers have to spend minimum 85% of premium on medical expenses, they will look to areas to control medical expenses. Given that treatment costs in India are almost a third of the costs in US, there is a significant incentive for health insurers to encourage medical tourism as a means to ensure medical expenses are kept under control.

✿ **Pharmaceuticals And Generics :** The US healthcare laws have offered increased drug coverage to its citizens and also stressed on the use of generics (as a cost containment strategy). As seen in figure 1, drug costs contribute to 10% of US healthcare costs, which makes the US drug market of over \$230 billion and which will grow further. Given India's proven track record in generics, there will be increased demand for Indian generics, from US markets. India drug firms should aim to supply at least 10% of the US market, which will throw open a huge potential of over \$20 billion. In addition, we will see increased M&A activities in the generics market place as US firms try and take control of leading Indian manufacturers. The most recent was Abbott Labs acquisition of Piramal Healthcare's India business for \$3.72 Billion. Earlier to this, Hospira acquired Orchid Chemical's generic injectables business for \$400 Million, Daiichi Sankyo acquired Ranbaxy Laboratories for \$4.6 billion and Sanofi-Aventis AG acquired Shantha Biotechnics. In addition to acquisitions, various MNC firms have signed up for partnerships with Indian firms. Pfizer, GSK and AstraZeneca, meanwhile, have tied up with several Indian firms to sell branded generics in emerging markets.

✿ **Clinical Trials And Medical Research Firms:** The new rules which mandate generics over branded drugs will pressurize drug firms to further optimize their processes, triggering increasing demand for offshored clinical trials from cost and speed to market reasons. This market already estimated at over \$1 Billion will grow further on the back of these new US rules. Additionally, the rules also provide for over \$9 billion of funding for various types of medical research initiatives. Indian research firms can partner with US entities to jointly work on such research programs.

✿ In addition to the above major areas, there are several other areas where Indian firms can play a major role, such as health facility infrastructure services, health related training services, funding program oversight and financial management and other related areas where demand will be triggered by the new laws.

✿ A quick conservative summation shows that innovative Indian firms with the right skills and experience can stand to tap an addressable market of over \$50 billion (over ₹ 2 Lakh crores) over the next ten years, which will be thrown up as a result of the US healthcare reforms bills. This is a substantial once in a decade opportunity, which if exploited intelligently, will catapult Indian firms to market leadership status in an accelerated timeframe.

CONCLUSION

US healthcare sector at \$2.3 trillion is the single largest healthcare market in the world. With the passage of the two new health related reform laws, the US has proposed significant additional funding for various health initiatives and enforced strict cost control and related rules on the various health entities. The two new laws have a combined \$1 trillion effect over the next ten years and will generate significant new opportunities in various health entities.

Even though US healthcare is a highly regulated market, the new laws and the concomitant changes will provide a \$50 billion opportunity for firms which show the foresight to move rapidly and exploit these opportunities. In specific, Indian firms, who already have exposure to US healthcare markets, are in a prime position to benefit from this opportunity. These and other firms have to take a deeper look at the impact of these new regulations and identify core areas where they can quickly scale up and provide the necessary products and services, to support the implementation of the new US healthcare regulations. This win-win approach for both US healthcare industry and Indian firms can be a model for further strengthening the relationships between US and Indian business entities.

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