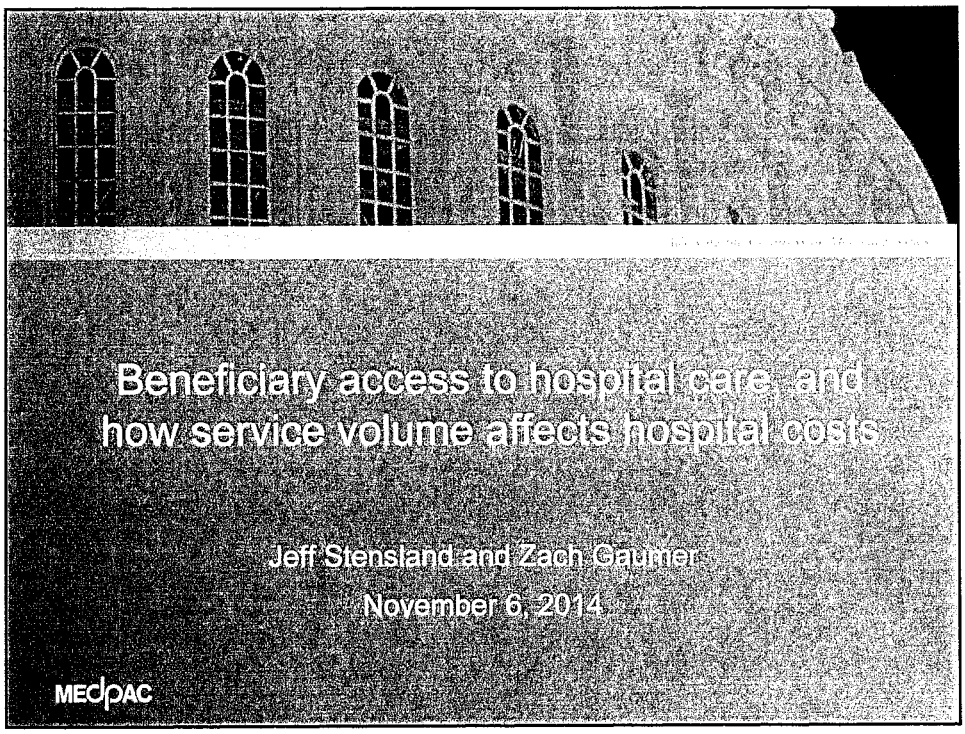
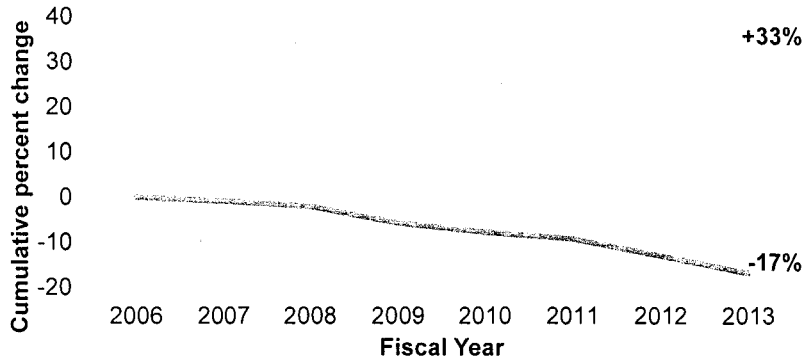


Today's topics: Beneficiary access and the relationship between volume and cost

- Beneficiary access is good
  - Inpatient use is falling, outpatient use rising
  - Occupancy is falling, creating more available beds
  - Closures are in line with changes in volume
  - Hospitals' access to capital is reasonable
  - Hospital construction focused on outpatient capacity
- Relationship between occupancy and costs suggest most hospital costs are not fixed

Changes in Medicare hospital inpatient and outpatient utilization



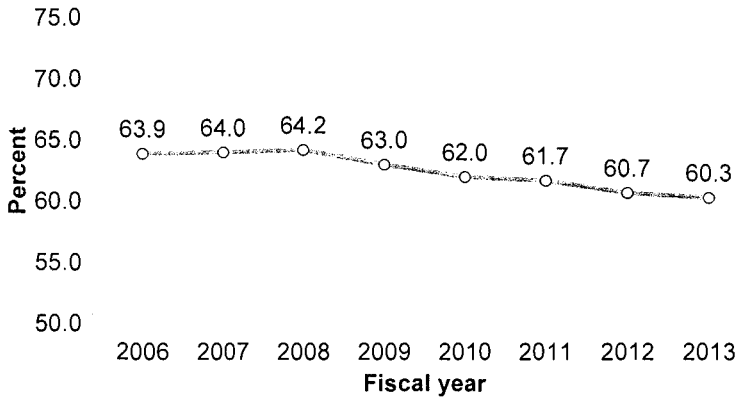
Source: Medicare claims

MEDPAC

Data are preliminary and subject to change

3

Hospital occupancy rates suggest excess inpatient bed capacity



Source: CMS hospital cost reports

MEDPAC

Data are preliminary and subject to change

4

Hospital closures exceeded openings in 2013 in midst of growing excess capacity

- Net impact: 9 fewer hospitals and 1,100 fewer beds
- 27 hospitals closed
  - Small hospitals (average number of beds = 68)
  - Occupancy rates low (32 percent) relative to the nearest hospital (51 percent)
  - All-payer margins low (-5.7 percent) relative to all-hospital average (+6.5 percent)
- 18 hospitals opened
  - Very small hospitals (average number of beds = 38)
  - Limited set of services offered

Rural hospital occupancy and closures

- Occupancy rates declined 47 to 41 percent (2006 to 2013)
- Few closures annually from 2006 to 2012
- 13 rural hospitals closed in 2013
- Rural hospitals accounted for 48 percent of all hospitals and 48 percent of closures in 2013
- Some closed hospitals become outpatient facilities

Hospital industry indicators of accessing capital

- Capital availability maintained
  - For-profit hospitals: Equity markets see them as attractive investments – rapid increase in share prices in 2014
  - Non-profit hospitals:
    - Most have access to capital at low interest rates
    - Some struggling with volume declines face rating downgrades
- Mergers and acquisitions
  - 16 percent increase from 2012 to 2013 (283 hospitals)
  - Large acquisitions drove much of the deal-making
- Employment: Stable growth in last 18 months (+0.4 percent)

Hospitals focused on outpatient capacity growth

- Hospital construction spending continued:
  - $27-$28 billion per year (2011 - 2012)
  - $23-$26 billion per year (2013 - 2014)
- Outpatient capacity the focus of hospital industry
- Other trends in the health care facilities marketplace:
  - Urgent care centers
  - Freestanding emergency departments

How do hospital costs change with volume?

- Common perception: most costs are fixed
- We find: most costs are not fixed
  - Hospital cost per discharge should not grow materially due to small reductions in occupancy
  - We should expect modest (not large) savings from hospital closures
- Hospital-based ACOs do have a financial incentive to reduce unnecessary admissions

Occupancy and cost per discharge

	Four categories of occupancy (2012)			
	<40%	40 to 49%	50 to 64%	65+%
Number of hospitals	424	416	787	560
Average occupancy	33%	45%	57%	73%
Std. Medicare cost per discharge	$12,000	$12,030	$11,840	$11,560

Note: costs are standardized for input prices, case mix, teaching status and outliers.
Data are preliminary and subject to change

Changes in volume and changes in cost per discharge

	Change in all payer discharges 2011 to 2012		
	Reduction of over 10%	-10% to +10%	Increase of over 10%
Number of hospitals	137	1,783	111
Change in discharges	-16%	-1%	20%
Change in cost per discharge	4.3%	1.9%	0.7%

Note: costs are standardized for input prices, case mix, teaching status and outliers.

Data are preliminary and subject to change

Summary

- Excess capacity (declining inpatient volume)
- Beneficiary access is good
- Access to capital is maintained
- Most costs are not fixed. Hospitals can adjust most costs to lower volumes
- In December we will present margin data and discuss hospitals' ability to reduce costs when under fiscal pressure