



November 30, 2012

CBO's Long-Term Projections for Medicare and Medicaid Spending in the United States

Presentation to the OECD Expert Workshop on
Improving Health Expenditure Forecasting Methods

Joyce Manchester
Chief, Long-Term Analysis Unit

This presentation contains information published in *The 2012 Long-Term Budget Outlook* (June 2012) and in *The Budget and Economic Outlook: Fiscal Years 2012 to 2022* (January 2012). See www.cbo.gov/publication/43288 and www.cbo.gov/publication/42905.

The Framework for CBO's Long-Term Projections

- The Congressional Budget Office (CBO) examines the pressures facing the federal budget over the coming decades within the context of current law (EBS) or “current policies” (EAFS).
 - The budget projections over the next 10 years are based on detailed program projections that underlie CBO’s baseline.
 - Beyond 10 years, CBO relies on its long-term model (CBOLT):
 - A microsimulation model set within an actuarial framework,
 - Governed by an overarching macro model.
 - Spending on the major federal health care programs evolves within the actuarial framework.

Longer-Term Budget Projections

■ CBO's Long-Term Model

- Social Security
- Medicare and Medicaid
- All other spending, which generally is assumed to grow with GDP
- Taxes

■ Value of Long-Term Projections

- Highlight trends
- Provide baseline for policy changes

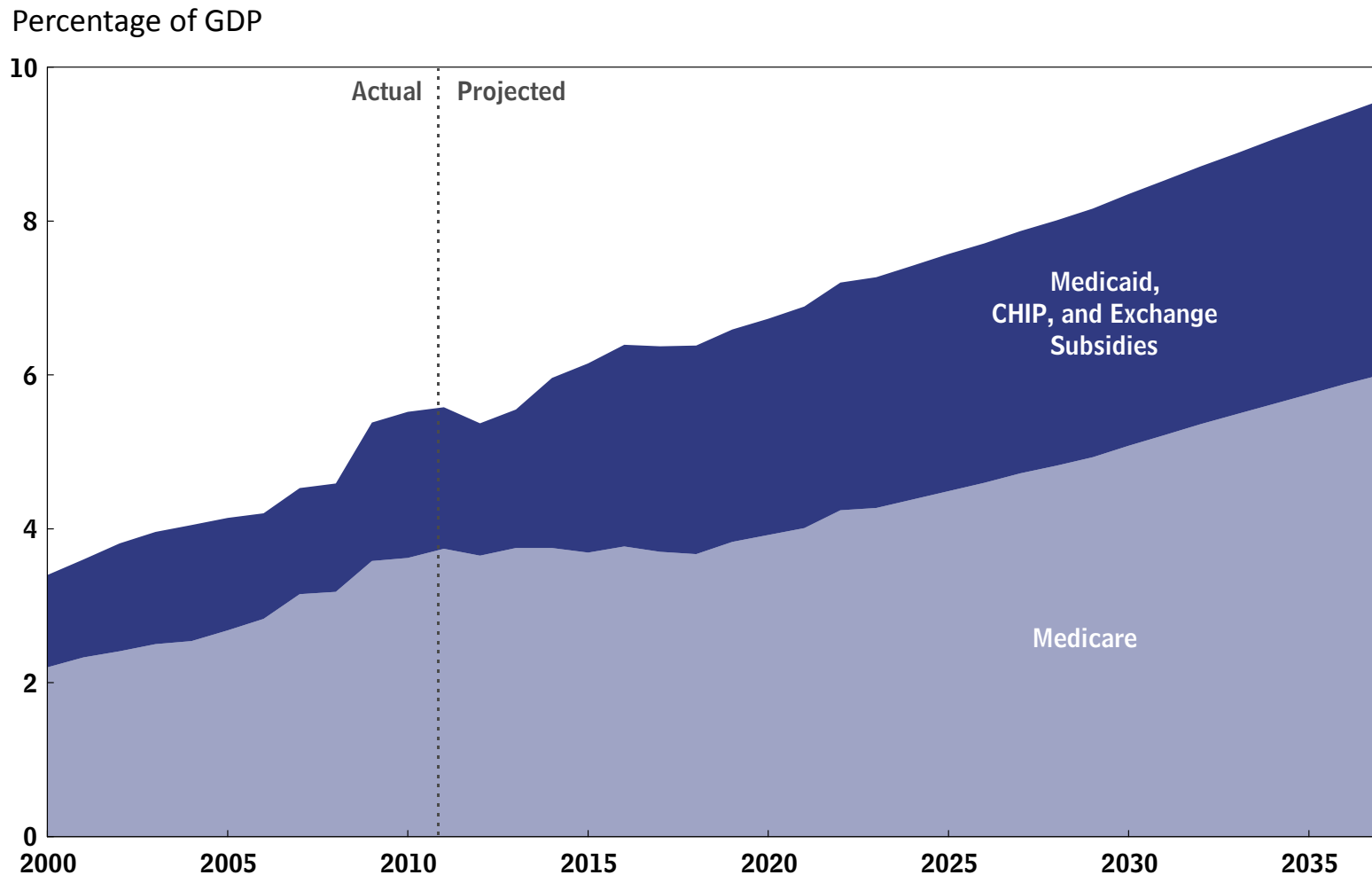
■ Limitations of Long-Term Projections

- Uncertainty, especially for health programs
- Interaction with macroeconomic conditions

Outlook for the Federal Budget

- If current laws remained in place, spending on the major federal health care programs would grow from more than 5 percent of GDP today to almost 10 percent in 2037 and would continue to increase thereafter.
- The aging of the population and the rising cost of health care would cause spending on the major health care programs and Social Security to grow from more than 10 percent of GDP today to almost 16 percent of GDP 25 years from now.
- By comparison, spending on all of the federal government's programs and activities, excluding net outlays for interest, has averaged 18.5 percent of GDP over the past 40 years.

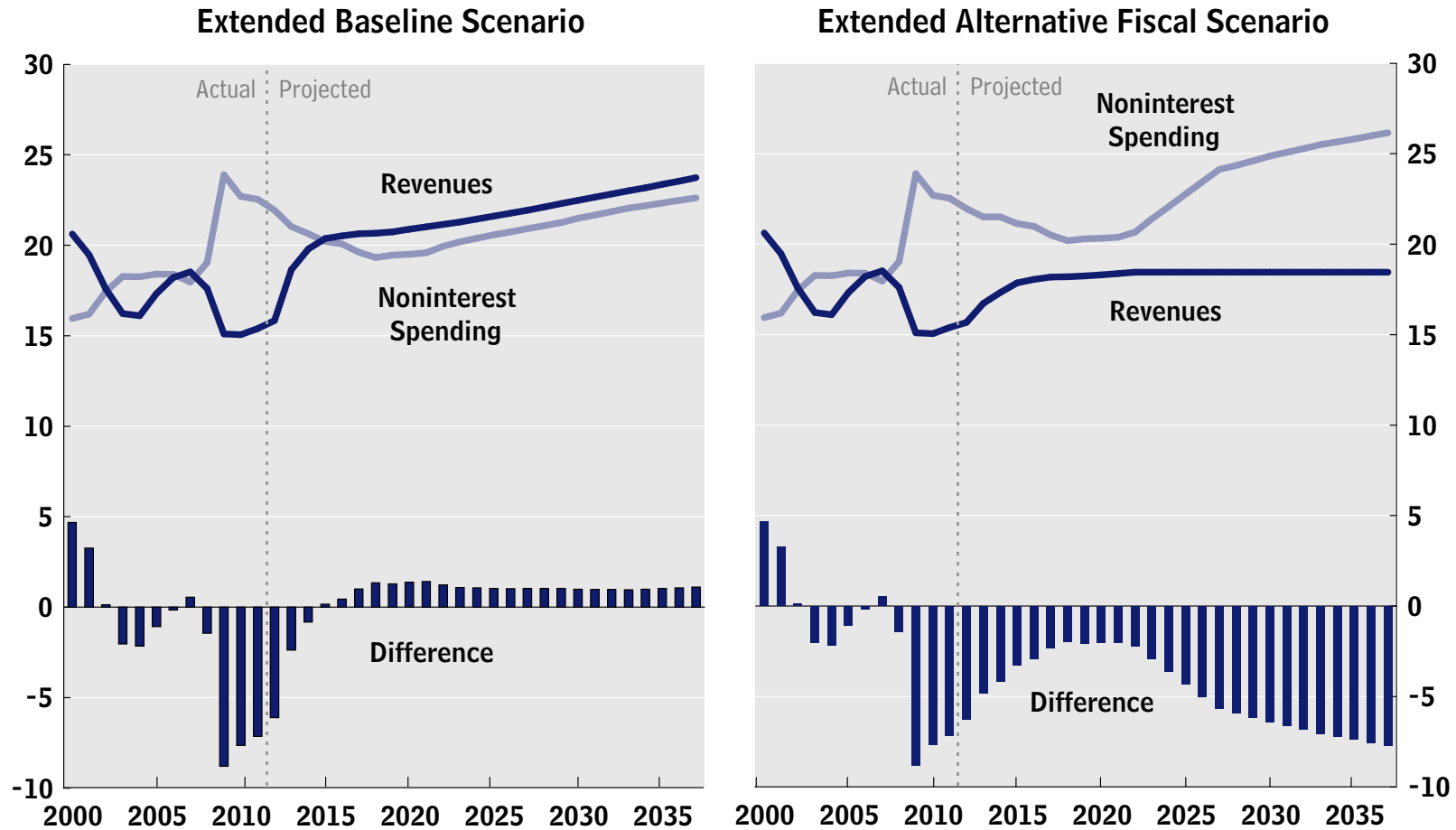
Federal Spending on Major Health Care Programs, by Category, Under CBO's Extended Baseline Scenario



Source: *The 2012 Long-Term Budget Outlook*

Noninterest Spending and Revenues Under CBO's Long-Term Budget Scenarios

Percentage of GDP



Source: *The 2012 Long-Term Budget Outlook*

CBO's Methodology for Projecting Federal Health Care Spending

- Spending from 2012 to 2022 follows CBO's March 2012 baseline.
- Projections beyond the 10-year budget window are based on historical trends in health care cost growth, population growth and economic growth.
- Assumptions about trends in health care cost growth are central to CBO's long-term spending projections for health care.

Excess Cost Growth

- The concept of excess cost growth (ECG) helps define the underlying path of the cost of health care.
 - ECG is the increase in health care spending per person relative to the growth of potential GDP per person after removing the effects of demographic changes on health care spending.
- CBO calculated historical rates of ECG as a weighted average of annual rates relative to potential GDP, placing twice as much weight on the latest year as on the earliest year.
 - The resulting growth rate is 1.6 percentage points per year.

Excess Cost Growth in Spending for Health Care

Percentage Points

	Medicare	Medicaid	Other	Overall
1975 to 2010	2.1	1.8	2.0	2.0
1980 to 2010	1.8	1.4	1.9	1.8
1985 to 2010	1.5	0.9	1.7	1.6
1990 to 2010	1.4	0.3	1.4	1.3

Source: *The 2012 Long-Term Budget Outlook*

Declining Path for Excess Cost Growth

- Using the historical average for ECG for all years results in a projection of federal health care spending that is very large.
- Continued growth in health care spending will create mounting pressure to slow growth of costs, even if federal law is unchanged.
- CBO assumes that ECG will slow over time, and the starting point is the historical weighted average rate of 1.6 percentage points.

Assumptions About Excess Cost Growth in Spending for Medicare over the Long Term

- The underlying rate of ECG for Medicare will decline from 1.6 percentage points to 1.0 percentage point over 75 years.
- From 2023 to 2029 under current law, excess cost growth for Medicare is equal to the average recent historical cost growth of 0.6 percentage points; thereafter, ECG follows the underlying path.
- Starting in 2023 under “current policies,” ECG follows the underlying path.

Assumptions About Excess Cost Growth in Spending for Medicaid over the Long Term

- The underlying rate of ECG will decline from 1.6 percentage points in the first year to zero in the final year of the 75-year projection period.
- Under both current law and current policies, ECG for Medicaid follows the underlying rates beyond 2022.

Projecting Population and GDP

- CBO projects the population using estimates of births, deaths, and immigration.
 - CBO uses a cell-based approach to estimate the population annually by single year of age (0-119) and sex.
 - For Medicare only, the population matrix is further extended by three “time until death” categories (0-12 months, 13-24 months, and survivor).
 - Projections of mortality and fertility come from the actuaries at the Social Security Administration.
 - CBO projects immigration levels.
- CBO projects GDP using a macro growth model.

Putting It All Together

$$M(t) = M(t - 1) * \frac{N(t)}{N(t-1)} * \frac{y(t)}{y(t-1)} * (1 + ECG(t))$$

where M is Medicare spending in t, N is the number of beneficiaries, y is GDP per capita, and ECG is excess cost growth

Strengths of CBO's Approach

- The long-term projections jump off the detailed 10-year forecast from the Medicare analysts at CBO.
- The approach is based on historical excess cost growth in health care spending:
 - Adjusted for age, sex, and time until death (in Medicare).
- The long-term projections for health care spending are designed to be consistent with CBO's overall long-term budget projections.
- The projections provide a baseline for policy changes.