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Medicare at Age 50: Unlikely to Make It to 100

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When President Johnson signed the Medicare program into law on July 30, 1965, no one expected the program to grow at the rate it has. In 2014, the Medicare program spent $613 billion to cover just under 54 million beneficiaries. Seniors do not qualify for Medicare until age 65, and back in 1965 many died before reaching that age.

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Americans born in 1900 and earlier were eligible for Medicare at its inception in 1965, but life expectancy for men and women born in 1900 was under 50 years of age. The few men who lived to see their 65th birthdays around the time Medicare began could only expect to live another dozen years or so — and women could only expect a few years more than men.

Longer Life Expectancy. Life expectancy has increased dramatically over the past half-century. As a result:

- About percent 70 of Americans born in 1950 are still alive and now reaching Medicare eligibility at age 65.
- Indeed, one-in-five Americans born in 1950 will live to see their 85th birthday.
- Men born in 1950 and turning 65 today can expect to live another 17 years, while women can expect another 20 years of life.

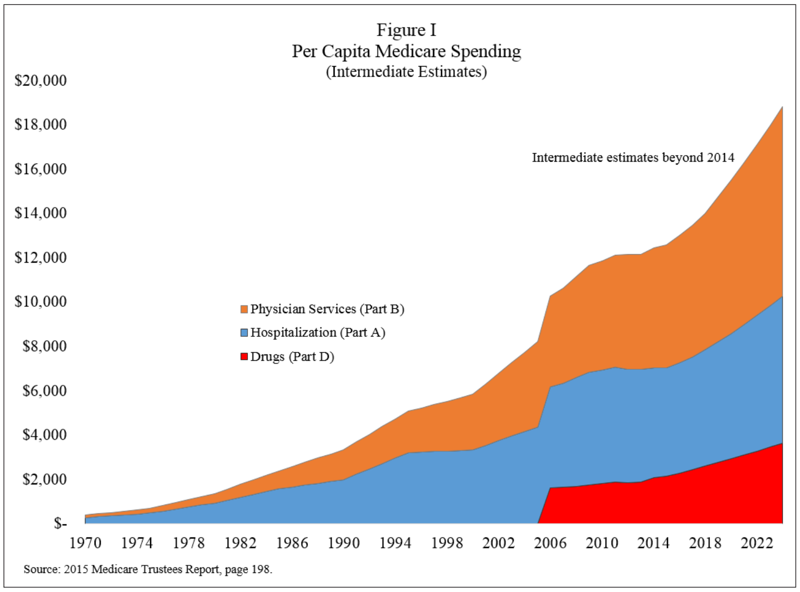
Some scientists even believe advances in medical science could extend longevity by decades before the dawn of the next century.

Higher Spending Per Capita. It is not just the proportion of Americans reaching Medicare eligibility that is driving up the program's cost, nor is it the number of years they remain on Medicare. Per capita spending on Medicare beneficiaries has also skyrocketed:

- In 1970, annual per capita Medicare spending was only $385.
- Today it is $12,430, and it is projected to approach $19,000 a decade from now.
- Of the $12,430 spent per beneficiary in 2014, $5,400 was spent on physician care while $4,900 was spent on hospital care.
- About $2,100 was spent on drug therapy.

Spending on Medicare beneficiaries is on course to grow another 58 percent in the coming nine years. [See Figure I.]

Medicare's Fiscal Health 50 Years On. In July 2015, the Medicare trustees released their 2014 report on the financial solvency of the program. The news was hailed as comparatively good. For instance, per beneficiary spending was only 2 percent higher than the previous year, and Medicare is expected to remain solvent until 2030 — unchanged from 2013. Medical spending growth is projected to moderate and grow at a slower rate around mid-century.



Yet, upon closer inspection, the report is not very reassuring. Medicare spending as a percentage of gross domestic product (GDP) was 1.3 percent in 1980 and 2.2 percent in 2000, and is now about 3.5 percent of GDP. It is expected to surpass 4 percent of GDP by 2022, but projected to only approach 6 percent by 2089.

The problem is that these projections assume conditions under "current law." The Medicare actuaries also look at spending under conditions they believe are more likely to occur in their Illustrative Alternative scenario. Under this more likely projection, Medicare spending could reach 9.1 percent of GDP in 2089 — about 50 percent higher than current law projections. [See Figure II.]

For instance, current law projections assume the Independent Payment Advisory Board (an Obamacare mechanism to control costs) will remain in place, and planned reductions in physician fees will take place, as will other Medicare fee reductions. Thus, the trustees assume reforms will be implemented to reduce the rate of growth in Medicare spending to no more than the rate of economic growth. This would shrink the projected deficit in Medicare spending to manageable proportions, but it is unlikely these provisions will be implemented.

Drug Costs Rising. There are other reasons to worry about Medicare's financial future. In 2014, Medicare spending on drugs was 0.48 percent of GDP. This proportion will nearly triple over the next 75 years as specialty drugs displace spending on cheap generics. Specialty drugs are a new generation of high cost treatments and biological agents that can cost $15,000 per year and sometimes much more. About 20 years ago, only about 10 specialty drugs were available; today there are more than 300. Specialty drugs accounted for one-third of drug spending in 2014 despite comprising only 1 percent of drugs prescribed. By the end of the decade, half of drug spending will be on specialty drugs.

In the coming years, taxpayers' burden for Medicare spending will undoubtedly rise. In 1970, payroll taxes and premiums paid for virtually all Medicare spending. Today, general revenues are needed to pay about 43 percent of Medicare costs — comprising about 1.5 percent of GDP. Only two decades from now, general revenues will be needed to cover more than half of the program's costs. That is scary enough; taxpayers will be on the hook for Medicare spending equal to 3.2 percent of GDP.

Of course, that assumes the provisions under current law are actually followed. Under the Illustrative Alternative scenario, Medicare spending could reach 9.1 percent of GDP — nearly three times today's 3.5 percent of GDP. Under this more likely scenario, taxpayers could find their burden quadrupling from its current level of 1.5 percent of GDP to 6.1 percent.

One Final Thought. The Trust Fund itself is little more than a filing cabinet full of IOUs that are claims on future taxpayers. There really is no Trust Fund in the traditional sense of one that represents assets that can be sold to alleviate the burden on taxpayers.

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