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In My Opinion

The Tea Parties Revisited



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AN OLD SAYING DESCRIBES INDIVIDUALS this way: There are people who make things happen, there are people who watch things happen, and there are people who wonder what happened.

On April 15th, over 300,000¹ American citizens gathered in more than 800 cities to voice opposition to what? Increasing tax rates? Increasing levels of government spending from local to federal levels? Creeping bureaucratic encroachment of personal decision making and self-determination? What?

Conservative pundits opined that these protests represented a return to an era of fiscal conservatism and limited government. Liberal pundits painted the protestors as unsophisticated hicks unworthy of participation in public debate. Both were wrong.

Making Things Happen.

Most decisions about future government size, spending and involvement in the private lives of its citizens were made in the 1930s by the New Deal; the paradigm was sealed in the 1960s by the Great Society era. Those designing and developing Social Security, Medicare and Medicaid were people who make things happen.

The programs enacted during these eras, mostly elderly, middle class entitlement and wealth transfer programs, were a quantum increase in government involvement in the private sector. They were also a massive funding vehicle for financing activist government.

Social Security and Medicare were designed with "trust funds" that were never funded. All of the involuntary contributions by workers into these funds were immediately used to buy government bonds that funded new government programs. It was a great deal; Ponzi schemes always are.

Unfortunately, the consequences of the unfunded entitlement programs are now coming due. Moving money from one section of government to another does not generate wealth. We are about to begin experiencing a massive cash flow problem in this country.

The pay-as-you-go systems that finance these entitlement programs, including government retiree medical programs, require taxpayer subsidies of shortfalls between trust fund contributions and obligation payments. There are no trust funds to draw upon. The trend in the liability is breathtaking. By 2012, we will need 1 in 10 income tax dollars for entitlement obligation payments. By 2020, 1 in 4 dollars will be required. By 2030, 1 in 2 tax dollars will be required.

Watching What is Happening.

This brings us to the Tea Parties. These protesters were everyday folks who rarely think about government other than on April 15 each year. They disgruntlingly pay their taxes and go on with their private lives, leaving the rest of the year to the professional and largely permanent political class. In the past, they have tolerated politicians enacting programs provided they were paid for using wealth redistribution and borrowed funds. These taxpaying protesters fall into the second group of people. They have observed that something very bad is happening.

What the Tea Party protesters do not appreciate is that it matters not what party is in power. The consequences of decisions made five to eight decades ago are dictating current events.

We are about to experience a perfect fiscal storm that has been foreseen since the inception of the activist government era. Exploding government spending beyond entitlements; the looming inability of the government to service its existing and increasing debt; the collapsing ability of state and local governments to support their unfunded retirement liabilities; are all conspiring to crush the economy of the United States. This economy has been the greatest wealth producing system in the history of mankind. It is now technically bankrupt when assessed by accepted public accounting standards.

The Democrats who now control policy making in Washington are entering sui generis territory. Their current and planned spending initiatives are unprecedented. The Administration and Congress are generating spending bills for bank bailouts, union-centric Detroit rescues, comprehensive health care overhauls to cover all the uninsured, education reform programs, climate-change cap-and-trade regulation and various stimulus plans increasingly recognized as "political pork."

During the first six months of this fiscal year, the federal deficit is running at \$956.8 billion, or nearly one seventh of gross domestic product - levels not seen since World War II, Federal debt alone, backed by public liability, as projected by the Congressional Budget Office, will rise from 41 percent of gross domestic product in 2008 to 51 percent in 2009 and to a peak of around 54 percent in 2011. Unless the economy rebounds sharply later this year, these projected deficits will be far greater.

For all of 2009, the administration will need to borrow approximately \$2 trillion. The Congressionally mandated debt ceiling of \$12.1 trillion will most likely be breached in the second half of this year.

Government borrowing to pay for debt servicing will displace the capital needed by the private sector to invest for competition in the evolving world economy. This lack of investment capital will destroy the engine that drives our economy. The Congressional Budget Office expects interest payments to more than quadruple in the next decade as Washington borrows and spends (\$806 billion by 2019 from \$172 billion next year).

The ability to service this debt through borrowing is showing signs of distress. America is facing increasing competition in global financial markets for its bond-based borrowing needs.

A consortium of investor nations ranging from China and Russia to most of OPEC have announced intentions to extricate themselves from dollar dependency as fast as they can.

Zhou Xiaochuan, the Chinese central bank governor, earlier this year called for a world currency modeled on the "Bancor." The Bancor was first proposed by John Maynard Keynes at Bretton Woods in 1944; his proposal called for anchoring international finance to 30 commodities.

International investors have announced that they are seeking a basket of units, similar to the Bancor that will be based upon the euro, the sterling, the dollar and the yen as well as a collection of industrial metals.

China has already begun to implement this investment strategy. China now holds the world's largest foreign reserves, believed to be mostly in dollars, along with around 800 billion dollars in US Treasury bonds.

Treasury Department data show that investors in China have sharply curtailed purchases of bonds in January and February of this year. China's State Reserves Bureau (SRB) has instead been buying copper^{2,3} and other industrial metals over recent months on a scale that appears to go beyond rebuilding of stocks for commercial reasons. Beijing appears to have made a strategic decision to stockpile metal as an alternative to U.S. Bonds.

From China's perspective, buying raw materials is a solid self-interest move. China will enjoy a rate of return for their \$1.9 trillion of reserves that exceeds by a factor of 10 what it reaps from U.S. Bonds. Of even greater significance, China can implement its stated plans to dominate industrial development for the next half-century. As an example, the next industrial revolution is going to be led by hybrid cars, and those cars need copper.

These unfolding and irreversible developments mean our ability to finance increasing debt through bond sales to foreign investors is about to end.

So the Tea Party protesters have every reason to express their concern.

What happened?

This brings us to those who wonder "what happened"? "Joe six-pack" is about to become engaged in the political process. When this segment of the population, which as a rule does not vote, finally engages things happen. Remember the car tax and the dumping of Governor Davis?

This group can best be categorized as former Louisiana Senator Russell Long, political party agnostic, populists. "Don't tax me, don't tax thee, tax that feller behind the tree!" Other than taxing the rich, the populist public will not tolerate higher taxes that are levied upon them - witness the recent defeat of all initiatives here in California to increase taxes despite the looming state deficit.

Unfortunately populism is a ruse to manipulate Joe. Taxing the rich is an artifice well understood by policy makers throughout government. The utterly disingenuous rhetoric coming from Washington presents a policy of ending tax breaks for the wealthiest 2 percent of Americans, and promising that households earning less than \$250,000 won't see their taxes increased.

At best, this is utter nonsense. Increasing taxes on the salaries, dividends and capital gains of all those making more than \$250,000 will not raise the revenue needed to fund the programs in the pipe-line and service existing debt.

What's Ahead for Health Care?

Many physicians fall into the "what happened" group. They will be shocked at what is about to happen to their practices. We make the following 10 predictions using economic trends and data rather than ideology.

We predicted the demise of health care reform here in California a year before its implosion;⁴ and we predict the same for comprehensive national health care reform. The unfolding catastrophe in Massachusetts should be instructive. The state is trying to manage the huge costs of a subsidized middle-class insurance program that is gradually swallowing the state budget. Over the next year, America will come to recognize that health care is not free. It costs far more than a \$5 co-payment. It cannot be paid for by the rich. The public will discover that federal credit card, used to pay for much of health care, is maxed out.

The only wild card in this prediction is that Washington has the ability to escape economic reality. The federal government can print money, as opposed to California and Massachusetts. Furthermore, the Democrats have the political power to pass any form of comprehensive health care reform they choose. With the defection of Senator Specter and the likely seating of Al Franken they will have a filibuster-proof Senate. They also have the backup option of passing a health plan through the "budget reconciliation" process. There is no obstacle short of economic reality to restrict their passing a comprehensive health reform measure. Elections have consequences and to the winners go the spoils.

Should economic reality prevail, a likely Democratic back-up plan will be to expand Medicare to cover individuals down to age 55. With the expansion of the State Children's Health Insurance Program (SHIP) eligibility up to 35 years earlier this year, this would leave only a 20 year gap in full coverage under single-payer.

With either comprehensive reform or expansion of SHIP, the government will far exceed its current 50 percent level of funding for health care in the United States. Controlling health care spending will become a priority for government at all levels. Spending is driven by two variables: the cost per unit of services delivered and the number of units delivered. Americans receive more medical services than do other peoples, and they pay more for them.

Controlling the cost per unit of service will require substantial reductions in the cost of labor in health care. Labor costs now consume more than 70 percent of every unit of health care delivered across the U.S. The U.S. labor costs are double those seen in our most comparable system, Canada. By leveraging its monopolistic payer position the government will dictate rather than negotiate unit pricing. With the demise of private health plans, reimbursement for services will initially decline to Medicare allowable rates. Ultimately, as was the plan under the rejected Clinton plan over a decade ago, reimbursement levels will drop to Medicaid levels for doctors and hospitals.

No current health care unit's business model will withstand this level of funding reduction. No American hospital, no staff model health plan and no medical group will have a viable business model. We will likely see the return of the old county hospital system with attached medical groups. The only difference from the past will be that now everyone will get their care from these facilities, not just the indigent. If you like the DMV, you are going to love this delivery system.

Reducing the number of units of service will also be necessary. Every single-payer system around the world limits access to high-tech diagnostic and therapeutic modalities by limiting supply. Waiting time will grow to those commonly seen in Canada or the European continent.

In addition to limiting supply, we are likely to see age-based overt rationing of goods and services in health care over the next few years. Many are now speculating that the patient data collected by the Administration's national electronic health record (EMR) initiative will be mined to assess the cost effectiveness of different treatments. This analysis could then be used to determine return-on-investment and cost-benefit-ratios. Thereafter, guidelines will be set using these calculations. These guidelines will be used to dictate which drugs and devices doctors can provide to their patients while the EMR monitors conformance to those standards.

As the above restrictions take hold, the elderly, the terminally ill, the infirm and the disabled will see significant reductions in their ability to access health care services. One of the announced goals for health care reform under the current administration was articulated by Tom Daschle in his book, "Critical: What We Can Do About the Health-Care Crisis." Daschle called for a Federal Health Board (FHB) for the health care industry that would resemble our current Federal Reserve Board for the banking industry. One of the primary assignments of the FHB would be to set cost effectiveness and return on investment values for each medical procedure. It should not be a surprise if hip replacements or coronary stents and bypass procedures for elderly patients would not pass muster with this cost-benefit methodology.

Innovation in the development of new pharmaceuticals, diagnostic and therapeutic technology will be driven offshore. With the FHB having a stranglehold on access to these new products and modalities, no company will be able to justify the R & D costs associated with development. Furthermore, no hospital receiving Medicaid levels of reimbursement will have the ability to purchase new technology.

As access to health care is limited by technology supply and cost considerations, those with the ability to pay for their own care will migrate to the international markets for needed procedures and cutting edge technology. The inevitable result - America will no longer be the leader in effective health care delivery.

So, the Tea Party protesters are right. Something bad is happening to them and their families. Unfortunately, almost all of the government activist and redistribution programs are now in place. There is little a typical political protest will do to change the inevitable.

Only a real rebellion by Joe Six-pack will fundamentally change the definition and direction of government.

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1. <http://www.fivethirtyeight.com/2009/04/tea-party-nonpartisan-attendance.html>
2. This explains why copper prices have surged 49-percent this year to \$4,925 a ton despite estimates that world demand will fall 15 to 20-percent this year as construction demand declines.
3. Chinese imports reached a record 329,000 tons in February, and a further 375,000 tons in March of this year.
4. <http://www.sacbee.com/static/weblogs/crossroads/healthcare/archives/005138.html#more>