

## The Healthcare, Unions and the Next Bull Market

By Robert Huebscher

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Ten years ago, MRIs and Lasik eye surgery each cost approximately \$3,000. Today, an MRI costs \$3,500, but the price of Lasik surgery has dropped to about \$500.



The difference? MRIs are covered by insurance, but Lasik is not. As a result, Lasik customers shop carefully, and competitive forces operating in a free market have driven down costs without diminishing the quality of services.

In order to reduce health care costs, consumers must be empowered to shop for and select health care services in a competitive environment, according to Jack Ablin.

Ablin is an executive vice president and the chief investment officer of Harris Private Bank. He was the keynote speaker at the Boston Security Analysts Society's annual market forecast dinner last week.

Reduced health care costs are a critical need of new and small businesses that can spark renewed economic growth and higher employment, Ablin told his audience.

His talk focused on the tradeoff individuals make between short-term gains and long-term benefits, as in the decision to diet for the sake of better overall health. While individuals are often able to choose the more appropriate path for the longer term, groups of people and society as a whole tend to cater to short-term needs when making decisions. The failure of health care reform to date, Ablin said, can be explained by a lack of broad-based support.

Anti-smoking legislation is one area where society has succeeded in making prudent long-term policy, Ablin said, as the smoking rate has shrunk from approximately 55% to 24% over the last several decades, a decline catalyzed initially by Surgeon General C. Everett Koop's war on smoking. Legislation to establish clean air and water standards are other examples of long-term policy successes.

Those successes came when the policy had broad public buy-in. For example, at the time of Koop's reforms, 96% of Americans perceived smoking was hazardous to one's health.



Broad buy-in for fiscal policies is less likely, Ablin said – 46% of Americans do not pay income tax – and this underlies the difficulty of enacting health care reform.

Ablin said it has been rare for Congress to act in a proactive manner for the long term, except when it has been faced with a broadly perceived crisis, in part due to two-year Congressional terms. Presidents who have been willing to cross party lines, though, have on occasion been able to overcome that short-term mindset.

Obama, Ablin said, has the opportunity to bridge party divisions through his support of nuclear energy, which has been embraced by Republicans to a greater degree than by Democrats.

“I believe that health care is the key” to fostering economic growth, Ablin said – universal health care must be “taken off the table” to convince entrepreneurs to grow businesses.

Economic growth depends on small businesses, and government’s role should be to insulate them from the threat of ending up in “debtor’s prison” if they fail, Ablin said.

During the last three economic recoveries, companies with fewer than 20 employees accounted for 3.6 million new jobs, while companies with more than 500 employees accounted for more than 500,000 in job losses.

“That is what large companies do,” Ablin said. “As they grow and productivity slows down, all they can really do is shrink their number of employees.”

How does health care fit into this? Affordable health care removes an important risk from those facing entrepreneurs.

Although Obama is on the right track in his efforts to reform health care, he is “putting the cart before the horse,” Ablin said. By establishing universal coverage without fostering a free market for health care services, Obama’s plan will not achieve the key goal of reducing the cost of those services.

When Obama says that Americans should assume that they can keep their existing coverage, he is doing them a disservice, Ablin said. “It is just unsustainable,” he said, adding that, unless checked, health care costs, including Medicare, will bankrupt the government.



Ablin's main point is that we have too much insurance. Broadly speaking, there are only two buyers of health care: Medicare and private insurers. Since the typical American can get a \$3,500 MRI without cost, they do not in any meaningful sense buy health care.

There is no free market for health care, he said, which results in a skewed and non-free market. A simple aspirin that might cost a few dollars at a drug store can cost many times more at the hospital across the street.

The current health care system, Ablin believes, is analogous to splitting the check for a dinner. He tested this hypothesis at a restaurant where he frequently dined. Over a three-year period he found that dinners where the bill was split were 20% higher than those where diners paid individually for what they ate.

Ablin's solution is to couple high-deductible insurance plans with health savings accounts as the primary type of health care coverage. Employers will save a lot of money by offering plans with higher deductibles, and they could use the savings to increase salaries for their workers.

Employees, who would pay for most of their health care through their health savings accounts, would become rational buyers of health care services, creating a free market with competitive forces that would drive prices down.

Americans collectively spend approximately \$2.25 trillion on health care, Ablin said. Reducing those costs by 10% – half the savings achieved when diners pay their checks individually – would be a big step toward deficit reduction.

Ablin offered another, more radical way to lower health care costs. Drug companies spend significant amounts of money to develop new products, which are then protected by patents. Inefficiency arises because multiple companies compete to develop the same or similar products, and consumers ultimately pay those costs industry-wide through high drug prices.

A better solution, he argued, is for the government to pay for the research and development of new pharmaceutical products and fund this activity through research grants. The intellectual property for new products would be in the public domain, and pharmaceutical companies would serve primarily as drug manufacturers.

While the bulk of Ablin's remarks focused on health care, he identified a second opportunity to spur economic growth.



Problems at the United States Postal Service may force it to cut back to a five-day delivery schedule and trim its workforce. More importantly, though, Ablin said it is considering trimming retirement and union benefits.

“If this turns out to be successful, and if we can ultimately get the stranglehold of unions off the public sector, this could be a key catalyst for a multi-year secular bull market,” he said.

He likened the current opportunity to Reagan’s de-unionization of air traffic controllers in 1981. As a result of that action, which was highly controversial at the time, the cost of providing air traffic control services was dramatically lowered. It was another 10 years before staffing levels among controllers returned to their pre-1981 level, despite substantial growth in air traffic.

At a macro level, Ablin and his team look at a range of indicators to forecast the economy and the market in a secular framework. All of them concern whether capital is being efficiently deployed in the private sector. War is the most critical, he said, because it draws capital away from the private sector, but regulation, trade, energy prices, taxes, are also among those that play important roles.

All of those indicators are still negative, and market analysts are increasingly focused on those things that could go wrong. According to Ablin, however, health care reform and labor reform in the public sector are two areas where things can go right – and catalyze entrepreneurship and economic growth.

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