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How much Health funding is needed in Budget 2017 to maintain current service levels?

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The health system needs more funding each year just to maintain its current services. This is to cover among other things population growth, inflation - including costs of new technology and pharmaceuticals - and salary costs. This does not take account the additional funding required to meet unmet health need.

This report summarises an analysis of what is needed in operational funding the Health vote[1] in Budget 2017 to maintain the status quo so that the public can judge whether announced funding is sufficient, whether it will allow for improvements, or whether services are likely to deteriorate. Capital expenditure requirements are not analysed.

Key points

- The Health vote's operational expenses would need to rise by an estimated $721 million (or 4.7 percent), from $15,324 million to $16,045 million, to maintain the current levels of service. The $721 million is simply to keep up with population and cost increases.
- In addition, the Government has so far announced initiatives and incurred additional costs to the current financial year with an estimated total of $375 million. That means the Health vote's operational expenses will need to rise by an estimated total of $1,096 million (or 7.2 percent) from $15,324 million to $16,420 million, to meet those new costs and maintain the current levels of service. If further new services are announced, the need will increase accordingly.
- For the Health vote to regain the spending power of the 2009/10 Health vote and pay for the initiatives and additional costs announced over that time, it would need to increase by $2.3 billion in the 2017 Budget to $17.6 billion.

[1] Note that Budget "Health packages" can include items in budget areas outside the actual Health vote itself. Usually these are relatively small compared to the Health vote and are not part of this analysis.

- The DHBs' combined budget needs to rise from $12,220 million to $12,800 million, requiring an increase of $580 million, or 4.7 percent, to maintain the current level of DHB services and cover population and cost increases. The Government has announced a number of additional initiatives and costs which require DHB funding. The $65 million which are quantifiable take the increase needed to $645 million, or a 5.3 percent increase. However there is over $300 million more in initiatives and additional costs whose impact on the DHBs is unclear at this stage. For example the cost to the 2017/18 Health vote of the TerraNova pay equity settlement is estimated at $303 million, the majority of which is likely to be a cost to the DHBs.

- The appropriations for national health services such as National Child Health Services, Disability Support Services and Mental Health Services (which are funded directly by the Ministry) will need to rise in total by $136 million, or 4.7 percent, to maintain service levels. However, as noted with respect to the DHBs, there is considerably more in initiatives and additional costs whose impact is unclear at this stage, an appreciable portion of which will be a national health service cost including part of the Terranova pay equity settlement.

- Funding for the Ministry of Health will need to rise from $196 million to $200 million to meet increased costs.

- Population pressures are projected to increase costs by 2.5 percent for the year to June 2018. This takes into account health costs of different age groups.

DHBs

For the first time we estimate the increased funding needed for each DHB. They are approximately as follows. **Please note that this does not include certain additional costs including those of the $303 million TerraNova pay equity settlement, which will be additional costs for each DHB.**

DHB	Increase required *(excluding additional costs)*	New total operational expenses required		DHB	Increase required *(excluding additional costs)*	New total operational expenses required
	$m	**$m**			**$m**	**$m**
Auckland	69	1,237		**Northland**	26	566
Bay of Plenty	36	706		**South Canterbury**	7	180
Canterbury	75	1,401		**Southern**	35	858
Capital and Coast	37	746		**Tairawhiti**	7	162
Counties-Manukau	73	1,402		**Taranaki**	16	343
Hawkes Bay	21	490		**Waikato**	59	1,156
Hutt	16	391		**Wairarapa**	6	138
Lakes	14	314		**Waitemata**	85	1,485
MidCentral	19	504		**West Coast**	5	130
Nelson-Marlborough	20	425		**Whanganui**	8	220

Our estimates are conservative on several counts, including:

- The State Services Commission reports that increases in public sector health wage rates were 4.0 percentage points behind general private sector wages measured by the Labour Cost Index (LCI) between March 2010 and June 2016 (a 12.2 percent increase for the private sector compared to an 8.2 percent increase for the public health sector).[2] The cost of living measured by the Consumer Price Index rose 9.8 percent over the same period. Poor wages, gender pay gaps and the lack of training and development in residential care were demonstrated in Kristine Bartlett's successful pay equity case for support workers in the aged residential, disability and homecare sectors. Similarly we believe our estimate for increased pay increases for 2017/18 are conservative (see below).

- The estimates do not take account of growing unmet need for health services and the additional funding that is needed to address it. New research findings published in the *New Zealand Medical Journal* in March suggest that at least 25 percent of adults are not able to get the primary health care they require and about 9 percent have an unmet need for hospital care.[3] In a recent report on mental health care, Professor Max Abbott, past president and senior consultant to the World Federation for Mental Health, referred to "increasing gaps, if not chasms, in service provision".[4] Our analysis of Ministry of Health mental health service data shows the growing need for mental health services is far exceeding the growth in resources. A summary of our findings will be included in a more detailed analysis of health funding after the Budget announcement. For example, the number of mental health clients presenting to DHBs rose by over 5 percent in the year to September 2016 according to Ministry of Health data, and we have used this as an estimate for the increase in the 2017/18 year[5].

This analysis does not take into account the findings of our previous analyses which found that each year public health services have started the new financial year worse off than they were the previous year. This shortfall will have accumulated to billions of dollars since 2010. We have estimated the cost to bring the purchasing power of the 2017 Health vote back to 2009/10 levels, including paying for the various initiatives and added costs (such as the transfer of responsibility for superannuation contributions from the State Services Commission to the DHBs), less "savings" by way of discontinued services. This would require an increase in operational expenses in the Health vote estimated at $2.3 billion, bringing it to $17.6 billion. This estimate uses actual rises in DHB full-time-equivalent employee wage costs, the rises in the Health Care and Social Assistance average

[2] State Services Commission. *Human Resources Capability in NZ State Services*, December 2016, p 7

[3] Bagshaw P, Bagshaw S, Frampton C, et al. Pilot study of methods for assessing unmet secondary health care need in New Zealand, *NZMJ*, Vol 130 N0 1452, 24 March 2017.

[4] Elliott M. *People's Mental Health Report*, ActionStation Aotearoa, April 2017.

[5] See Performance Measures: PP6: Improving the health status of people with severe mental illness through improved access at http://nsfl.health.govt.nz/accountability/performance-and-monitoring/baseline-data-quarterly-reports-and-reporting/mental

wage or minimum wage for other employees, and CPI for other cost increases. Net additional initiatives and costs are added.

Assumptions

Our analysis includes additional expenditures announced or known for the 2017/18 financial year at time of writing. These are as follows:

Additional costs identified for 2017/18	Funded from	$m	Notes
Equal Pay settlement	Unclear	$277.00	$303m less $26m estimate of pay increases had settlement not occurred.
Increased capital charges for DHBs	DHBs	$52.40	Estimate (net of interest saved). Result of government decision to convert debt to equity.
Quality Initiative in Mental Health	DHBs	$1.50	Announced by Minister ($7.5m over 5 years).
Ambulance doubled crewing; air ambulance and ambulance communication services	Unclear	$13.05	Announced by Minister ($52.2m over 4 years from Vote Health plus $82m from ACC).
Pharmac	National	$20.00	Announced by Minister.
Pharmac	DHBs	$11.00	Announced by Minister.
Total		$374.95	

In addition, there is further funding needed for the In Between Travel settlement which began the regularisation of the work of home and community support carers including payment by wages and for the time travelling between clients, guaranteeing hours of work, recognising qualifications and encouraging further training. Some of this has been explicitly funded in previous Budgets, though is time-limited pending a review, and some is covered by the TerraNova pay equity settlement, but significant further costs in the order of tens of millions of dollars per year remain. We are unable to quantify this so do not include it in the above table.

We assume a rise in the CPI of 2.0 percent in the year to June 2018 (the Budget period). This is Treasury's forecast in HYEFU 2016 for the year to June 2018. CPI is the standard price index used for costs in the Health vote. We note that the 2.2 percent increase in CPI in the year to March 2017 took most forecasters, including Treasury and the Reserve Bank by surprise: they had forecast 1.5 percent. A difference of 1 percentage point in the estimated CPI increase costs or saves $104 million.

We assume that, the TerraNova pay equity settlement aside, the pay of all employees other than those close to or at the minimum wage (which rose by 3.3 percent from 1 April 2017) will increase on average by 2.2 percent, Treasury's forecast for the increase in the average wage for the year to June 2018. We believe this is conservative. For example the Resident Doctors Association settlement over working hours has been estimated to be equivalent to a cost increase of 3 percent. There have been several years of low increases as noted above. Pay equity cases may have direct and indirect effects. A difference of 1 percentage point in the estimated pay increase costs or saves $84 million.

These pay increases do not include the effect of the equal pay settlement which benefits 55,000 low paid carers. The settlement affects people working for services funded by both DHBs and the Ministry out of its Disability Support Services appropriation. In total this will cost the Health vote $303 million in the year to June 2018 (other costs come from ACC and increased user charges to

some people in private care). However, it is not yet clear how the Health vote costs will be divided between DHBs and Disability Support Services.

Population growth is a significant driver of health costs. We assume an increase of 2.51 percent during the year, including both an increase in the population (1.81 percent) and the increased expenditure requirements due to the ageing of the population. The actual increase varies between DHB districts, ranging from 1.4 percent in West Coast and Whanganui DHB districts to 3.4 percent in Waitemata DHB's district. These were calculated using Ministry of Health demographic projections and age, sex, ethnicity and deprivation cost weights.

How reliable are our estimates of funding needs?

The results of our Vote Health analyses have been presented each year to a meeting of senior DHB and Ministry of Health officials, Treasury officials with responsibility for Vote Health, and senior health union representatives. Our methodology has never been disputed; on the contrary it has been accepted as sound.

Our estimates of funding needs are consistent with estimates made by the Ministry of Health and Treasury prior to Budget-setting in previous years, where they have been published. On average our post-Budget estimates of funding shortfalls for the full Vote, based on our pre-Budget estimates, are very close to those of the Ministry, but for the part that refers to DHBs they are consistently lower than the Ministry's. It is possible we are underestimating the pressure on DHBs because of transfers of responsibility ('devolution') from central services to DHB which are not well documented, and because some of the national services are carried out by DHBs but not fully funded.

A Treasury response to our analyses released earlier this month[6] again does not question our methodology but differs on some matters of interpretation. It claims health spending has "increased in real (CPI adjusted) terms and real per capita terms in most years, albeit at a lower rate and with occasional reductions". However, it acknowledges "There are other measures of health inflation [than CPI] that may be higher", and its figures do not include demographic factors such as ageing, "that could tend to increase costs per capita". Ministry of Health data shows that the effect of these factors is significant. It also concedes:

Ministry of Health figures (based on historical cost weights by age, ethnicity and deprivation) generally suggest that health spending growth has kept pace with demographic cost pressures, but has only made a contribution to other cost pressures, although this analysis does not include funding for new initiatives.

In other words, the Ministry's figures indicate health funding has not kept up with total costs, including the increasing costs of technology, growing health need and, to some extent, personnel costs, let alone total costs plus new initiatives. On this interpretation, new initiatives have in effect not been funded.

An Excel spreadsheet showing the calculations and assumptions is available from http://union.org.nz/health-working-papers.

[6] NZ Treasury. District Health Board Financial Performance to 2016 and 2017 Plans, February 2017.