

The Supply of Medical Care, The Market for Health Insurance and Market Competition

Lecture 25



Economics 157
Health Economics
Summer 2003

Announcements (1)

- **Tuesday 080503: Richard Kim on Enthoven and Managed Care**
- **Wednesday 080603: Guest Lecturer; Phyllis Weber of the N. Calif Organ Retrieval Network**
- **Thursday 080703: Guest Lecturer: Professor McCormick of UC Davis. Topic; Economics and Organ Donation**

Announcements (2)

- **Reading Assignments**
 - **Tue 080503; Alain C. Enthoven...on Manage Care (see course website)**
 - **Mon 081103; Transplant articles Section VII of Syllabus (see course website)**
 - **Tue 081203 Text Ch 18; National Health Insur.**
 - **The Pauly Herring reading is dropped**

Wrap Up on The Demand for Health Insurance

Concluding Comments on Risk Selection (Feldstein p. 140)

- Adverse selection would be limited if everyone were required to have health ins.**
- Preferred risk selection could be limited if risk adjusted premiums. Make all patients equally attractive to insurers**
- Practically: risk adjusted premiums has not been very successful. Examples....**

The Rational Economic Consumer “...Will not Want Complete Comprehensive Health Insurance” p 141

- **Without Moral Hazard: loading charges and transaction costs can be inefficient**
- **With Moral Hazard: leads to other inefficiencies such as dead weight loss**

The Effect of Deductibles on the Demand for Medical Care: Deductibles May, but Not Necessarily, Reduce Moral Hazard

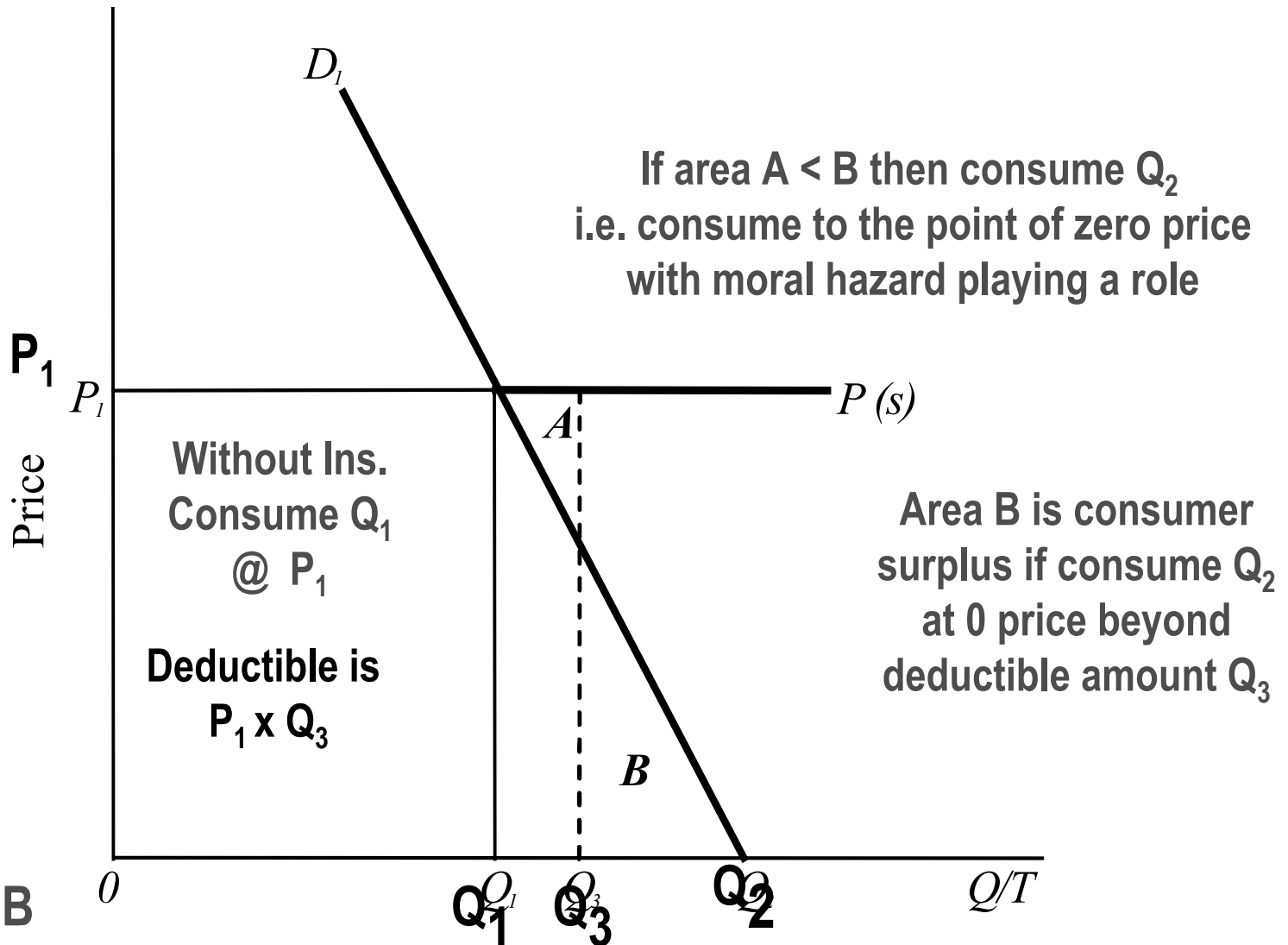


Figure 6.7B

Feldstein's Conclusions on the Demand for Health Insurance p 145-146

- **Insurance coverage for 100 % comprehensive services for all persons is not warranted;**
 - **Why?**
- **With different demands and transaction costs, no single insurance policy is best for everyone**
- **Moral hazard only reinforces the social desirability of choice and variety in health insurance**

(1) Summary of the Demand for Health Insurance pgs. 146-149

- **Very good and very long**
- **Note: Justification for Fig. 6.8 (pg.148)**
- **Indemnity Insurance: keeps relative prices intact and leads to cost minimization**

(2) Summary of the Demand for Health Insurance pgs. 146-149

- **Capitation (prospective) payments also maintain relative prices and cost minimization**
- **Method of provider reimbursement has historically been shown to be important e.g. cost reimbursement leads to inefficiencies**

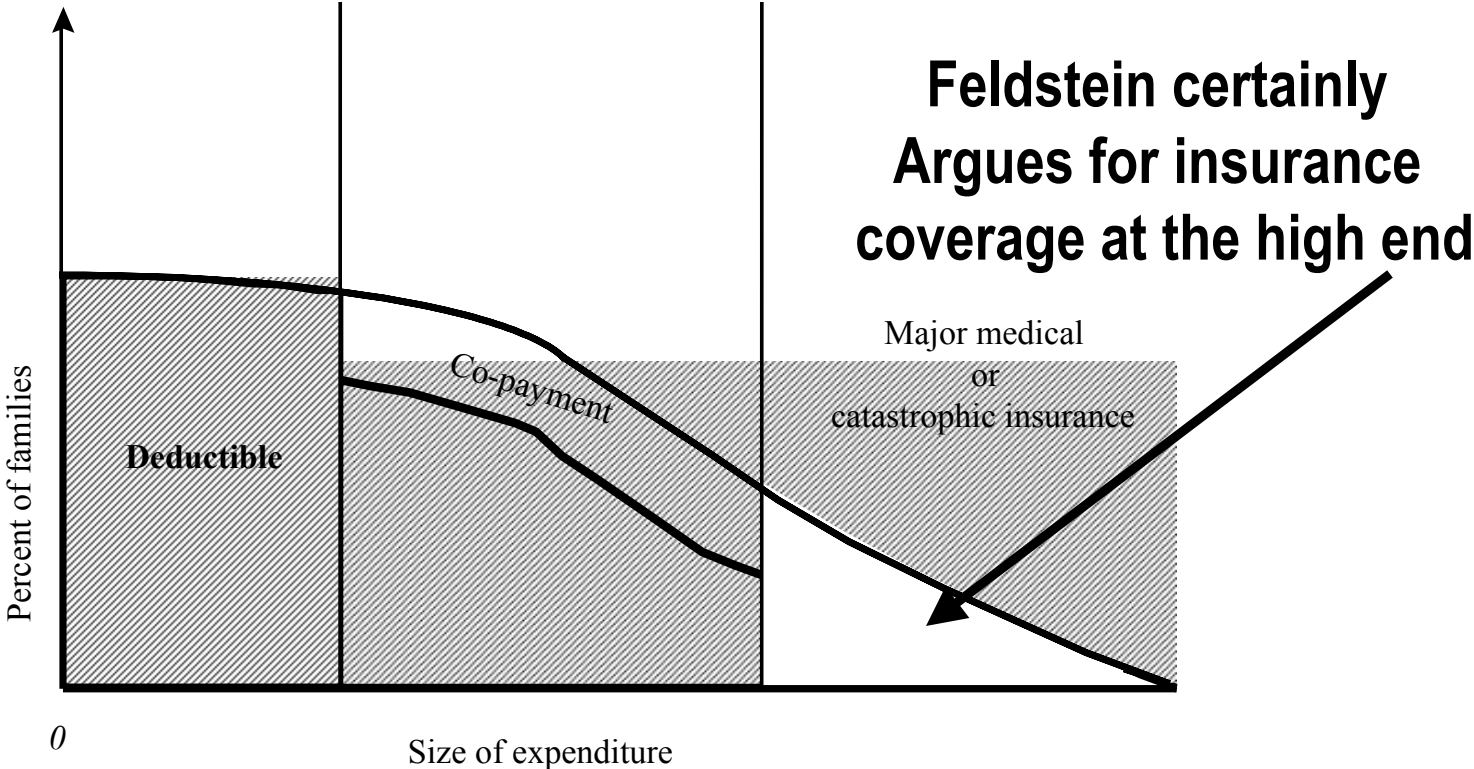
When is the Quantity & Quality of Medical Care Consumed Optimal?

- **When the price of care equals the cost of that care produced in a competitive system and which**

Equals

- **The marginal benefit of that care**

Fig. 6-8 (Feldstein) The effect of health insurance on the expected distribution of medical expenses among families



The Supply of Medical Services

Fig. 7-1 The effect of different supply elasticities on the price, quality, and cost of national health insurance.

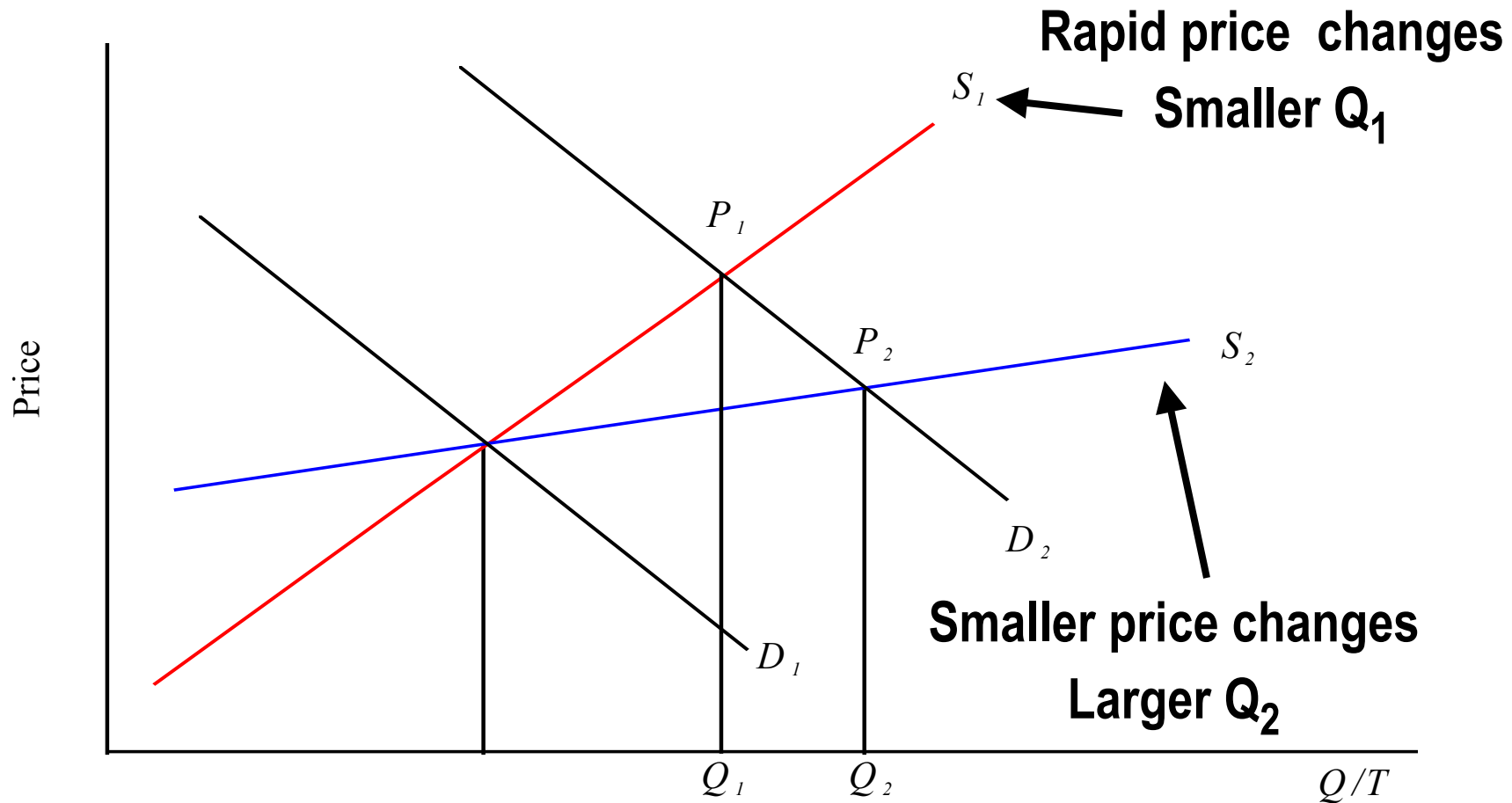
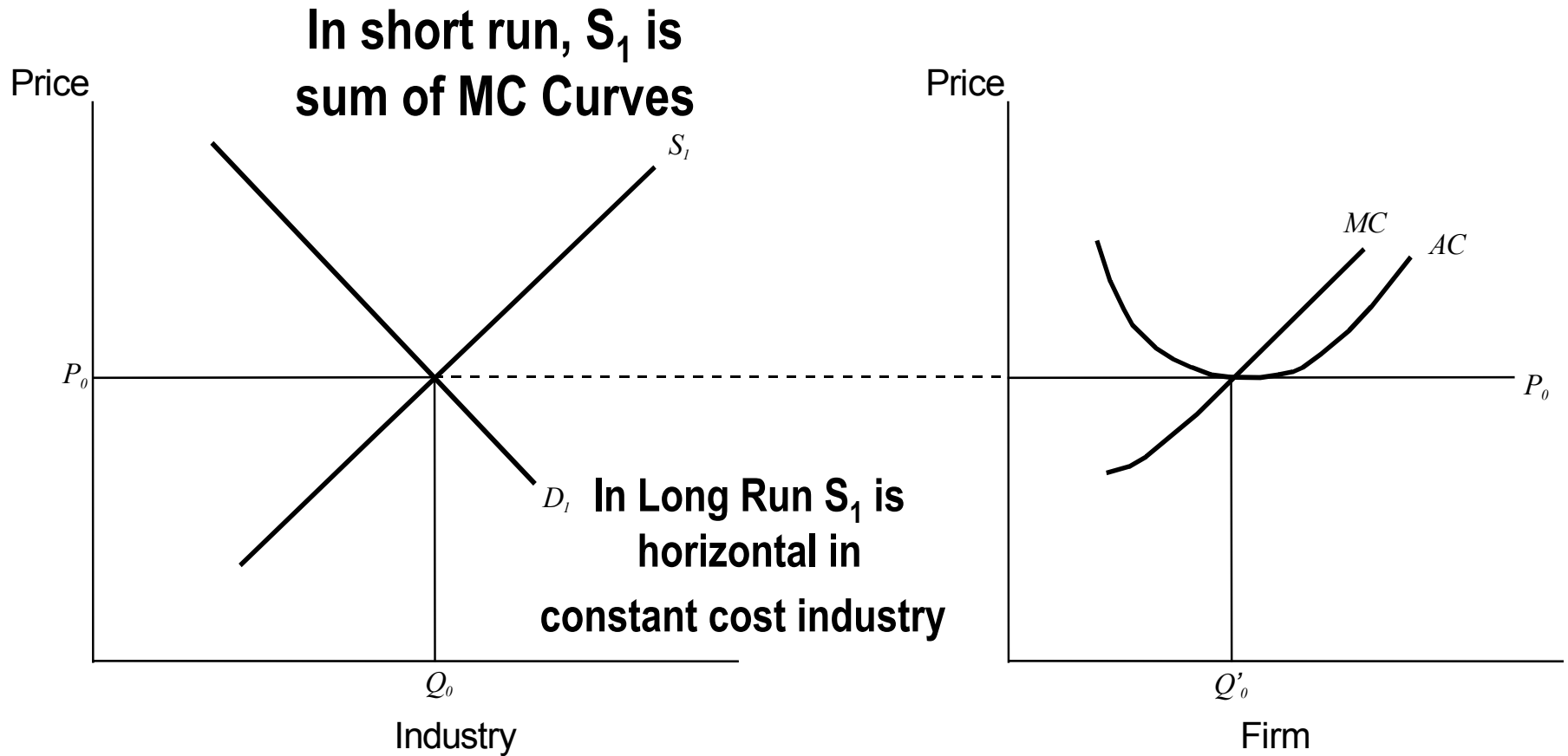


Figure 7-3 The industry and the firm under long-run competitive equilibrium.



The rate of output in a competitive industry is optimal since price reflects marginal benefit & is equal to marginal cost (with no externalities) pg 167

Notes

- **Can skim production and cost functions pgs 169-172**
- **Recommend problems 2 & 10 on p. 174**

The Efficiency and Equity Aspects of Community Rating

- **Compared to experience rating;**
 - **All pay the same; e.g. no adj for age**
- **Long history of Blue Cross Power**
- **Effect is subsidy to some (e.g. elderly) funded by a regressive tax (e.g. on young)**
- **Is inefficient to redistribute ms & has contrary redistributive effects (poor support the rich)**

Other Conclusions

- **Monopolies are bad; e.g. Blue Cross p 199**
 - Another version of the benefits of competition
- **National Health Insurance: do not build big power centers; rather many competitors; good histories (innovations and pricing)**

(1) Benefits of Competition in the Market for Health Insurance p. 200

- Forces insurers to minimize admin cost**
- Forces more choice in policies & cost minimization behavior**
- Work against community rating**
- These findings are true for profit and non-profit institutions. examples**

(2) Benefits of Competition in the Market for Health Insurance p. 200

- **Some regulations and laws are pushing in wrong directions with adverse outcomes:**
 - **Shorter waiting periods for preexisting condition**
 - **Community rating (regressive tax)**
 - **State mandates; higher cost of ins. decreasing the demand for health insurance**

In conclusion...(p. 235)

- **Neither a market approach nor regulation alone will solve all the problems**
- **Redistribution of medical services requires government intervention**
- **Government intervention need not be direct**
- **Government intervention can be through the market mechanism such as vouchers**