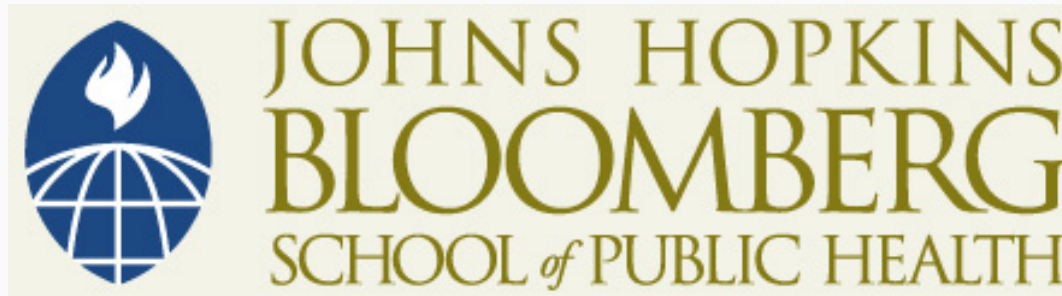


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# *Economic and Financial Considerations in Health Policy*

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Gerard F. Anderson, PhD  
Johns Hopkins University



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## *Section A*

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Introduction to Economics

# *Four Fundamental Tenets of Economics*

- Resources are scarce relative to human wants
- Resources have alternative uses
- People have different priorities
- Consumer knows best

# *Opportunity Costs*

- You have to choose because you cannot do everything at once
- You select the best alternative given budget constraints
- You must make tradeoffs

# Tradeoffs



# *Two Ideas Not Embraced by Economists Because They Ignore Tradeoffs*

- Romantic
  - We can afford it
- Technical
  - Best possible

# *Economists Versus Clinicians*

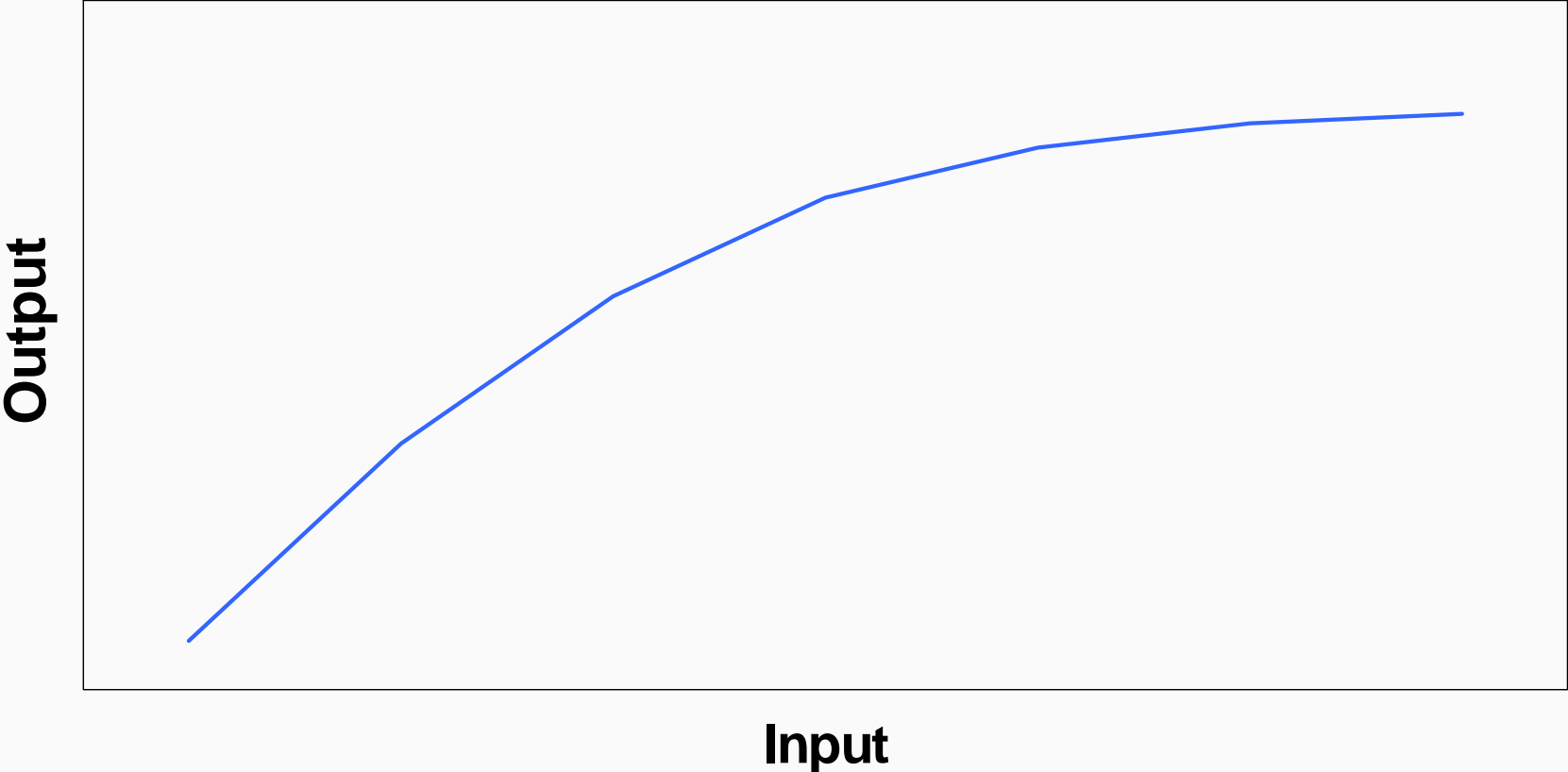
- Orientation of clinicians/public health advocates is to achieve ...
  - Highest quality of care possible
  - Health services available to meet demand
  - 100% immunization rates
  - No pollution
  - No medical errors



# *Economists Versus Clinicians*

- Orientation of economist
  - Social optimum
  - Value of additional increment of health = cost of resources to provide it

# *Diminishing Returns*



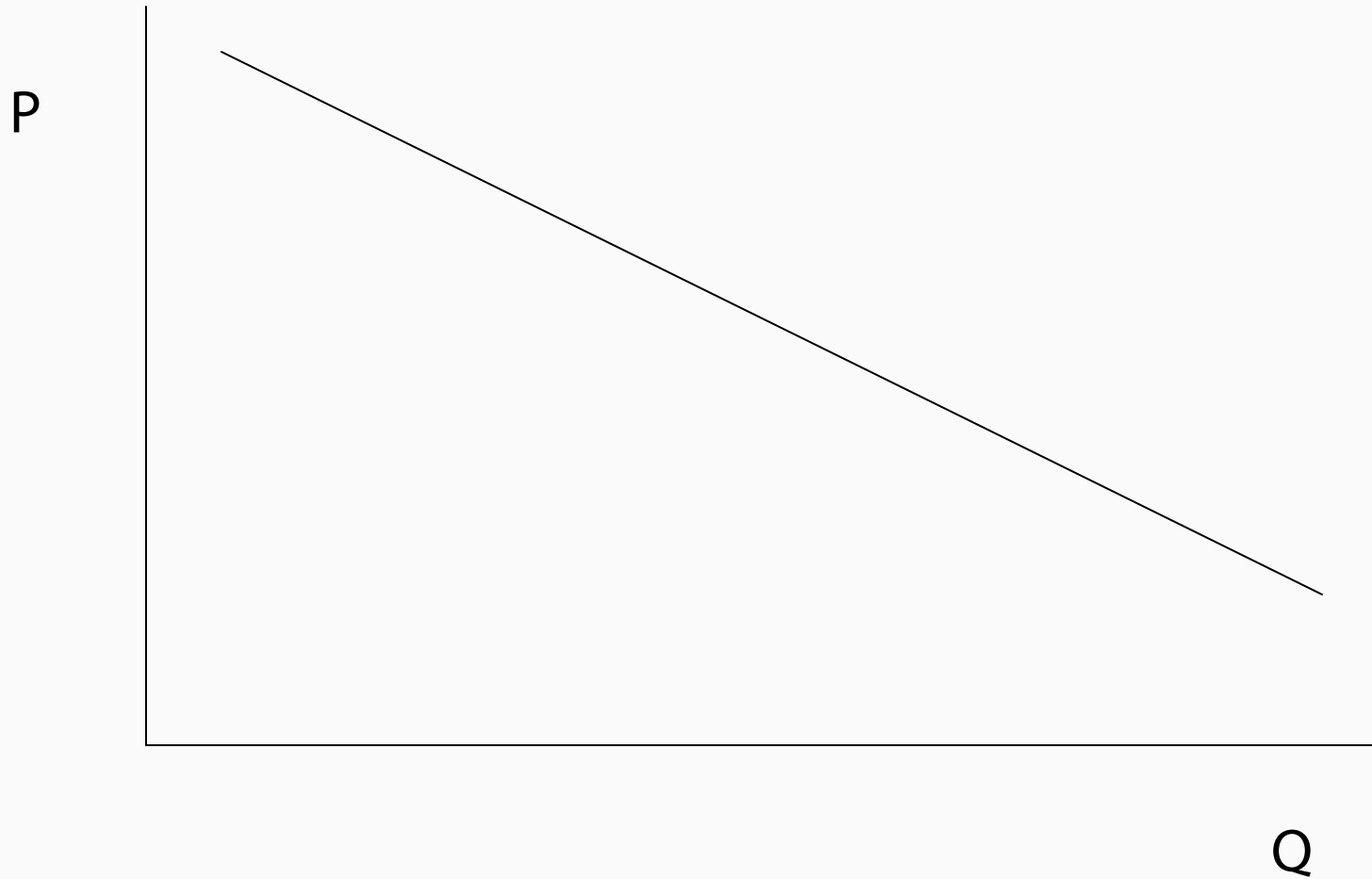
## *Marginal Benefit = Marginal Cost*

- What is the benefit someone receives from the last dollar invested in health?
- Could the same dollar be better spent on something else and the person would receive more benefit?

# *Demand*

- Term used in economics
- Measures what people are willing to pay for

# *Demand Curve*



# RAND Health Insurance Overall Results

Coinsurance	Probability of Medical Use	Expenses per Person
Free	87%	\$1,019
25%	79%	\$826
50%	74%	\$764
95%	68%	\$700

# *Some of the Factors that Influence Demand for Health Care*

- Illness level
- Age and gender
- Beliefs about medical care
- Advice from providers
- Income
- Education
- Regulations
- Insurance coverage
- Quality
- Access



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## *Section B*

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Tradeoffs as Viewed by Economists



## *Better Health or Other Goals?*

- One in five Americans smokes
- People working in coal mines understand the danger
  - Have few other options besides working in the mines

- Cancer prevention vs. cancer treatment

# *Which Medical Care Provider Is Most Effective?*

- What is the best (most cost effective) way to produce health?
  - Physician or nurse practitioner
  - Nurse practitioner or social worker
  - Social worker or community health worker
  - Community health worker or nurse's aide

# *Equity/Disparities*

- How does income/race impact access to care/health status?
- What are the most effective ways to reduce disparities and promote equity?

# *Today or Tomorrow*

- Investment in improved health status vs. consumption of medical resources
- Dollars spent today versus dollars spent tomorrow
- Dollars saved today versus dollars spent today

# *Discount Rate*

- Lives saved today vs. lives saved next year
- Important for prevention

# *Identifiable vs. Statistical Lives*

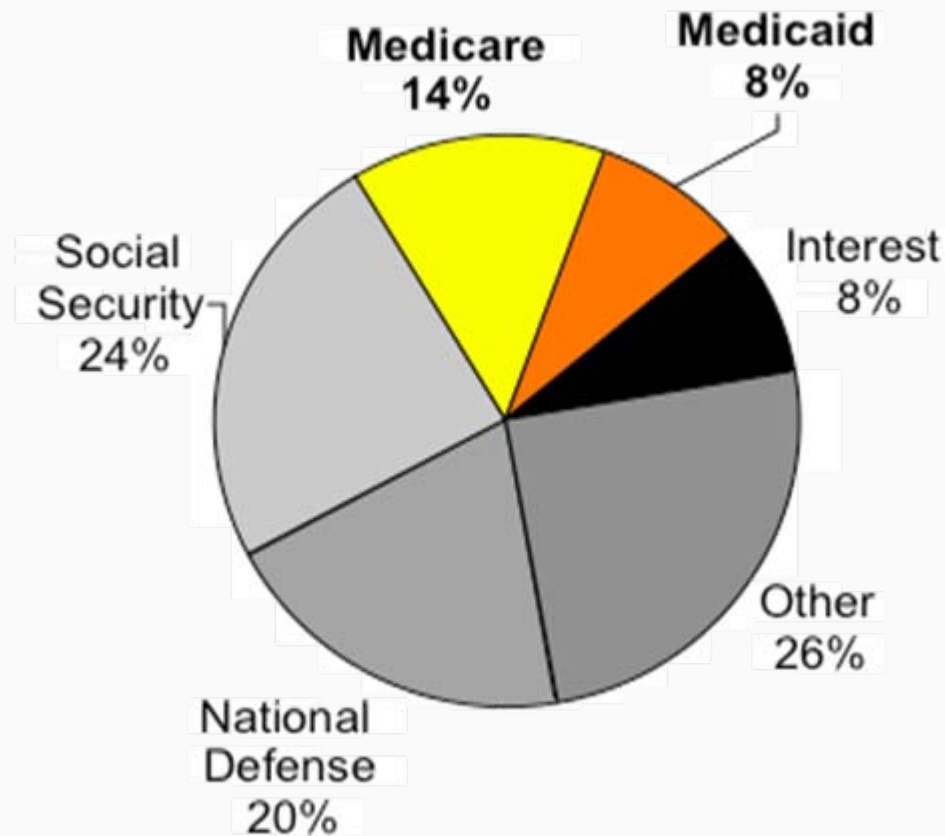
- Known person vs. statistical person

# *Spending Tradeoffs and Health Policy*

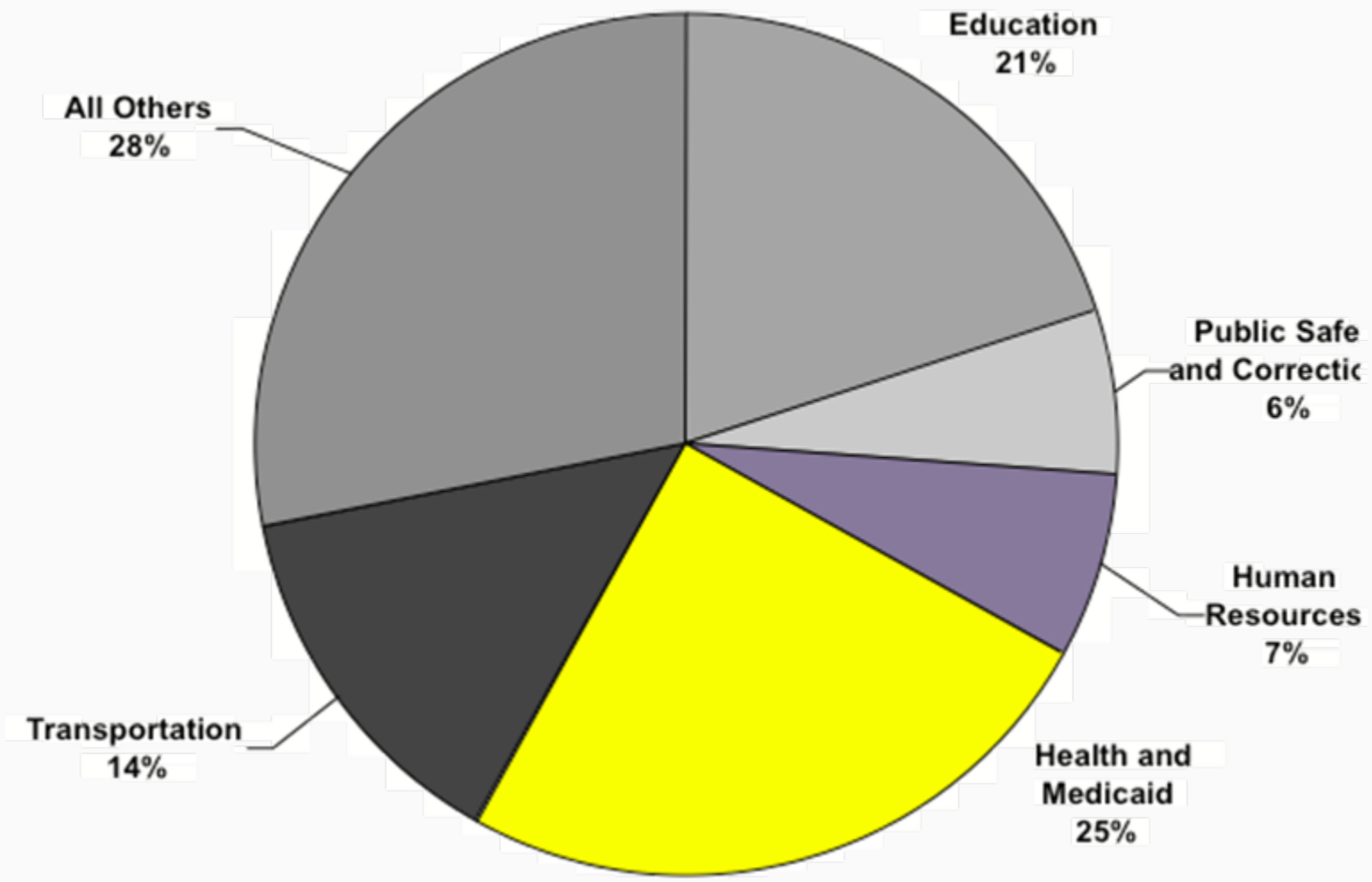
- Federal government
- State government
- Corporations
- Unions



# Medicare and Medicaid as Percentages of the Projected Federal Budget, 2004



# Maryland State Budget: Fiscal Year 2004



- The concern is competition in international markets
  - Approximately \$2,000 of the price of U.S. automobiles is for health benefits to American workers
  - Approximately \$1,000 of the price of European or Japanese automobiles is for health benefits to workers

- Corporations negotiate with unions over total compensation package
- Total compensation = wages + benefits
- If health benefits increase faster than total compensation then less money is available for wages
  - Many employees do not acknowledge this tradeoff
  - Bitter union negotiations over the last few years have focused on benefits

- Cost
- Effective
- Benefit
- Cost Effective
- Cost Benefit

# *How Do You Measure Cost?*

- Direct costs
- Indirect costs

# *Costs from Whose Perspective?*

- Person
- Insurer
- Clinician/provider
- Society

# *An Individual Person Goes to an MD —What Are the Direct Costs?*

- Person—out of pocket
- Insurer—benefits paid
- Clinician—cost of providing treatment (payment)
- Society—resources used



## *An Individual Person Goes to an MD —What Are the Indirect Costs?*

- Person—time and travel
- Insurer—administrative costs
- Clinician/provider—none
- Society—time, travel, and administrative



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## *Section C*

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### Cost-Effectiveness Analysis

## *When You Calculate Costs ...*

- From whose perspective should the calculation be done?
- What costs should be considered?

# *How Do You Measure Effectiveness?*

- Clinically
- Quality of life
- Functional level
- Quality adjusted life years
- Disability adjusted life years

# *How Do You Measure Benefit?*

- In dollar terms
- What is a life worth?
- What is an eye worth?

# *Cost Benefit*

- Both in dollar terms
- Benefits in dollar terms—value of a life

# *Cost Effective*

- Cost in dollar terms
- Effectiveness measured in some type of output (e.g., life saved)



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## *Section D*

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### The Eightfold Path, Part I



# *1. Define the Problem—Financing and Delivery System*

- The current health care system uses an acute-care financing and delivery system to treat chronic conditions; therefore people with chronic conditions suffer

# 1. *Define the Problem—Health Insurance*

- Health insurance is oriented to covering acute—not chronic—conditions; therefore people with chronic conditions suffer

## *1. Define the Problem—Medicare Orientation*

- The Medicare program is oriented to covering acute, not chronic, conditions; therefore Medicare beneficiaries suffer

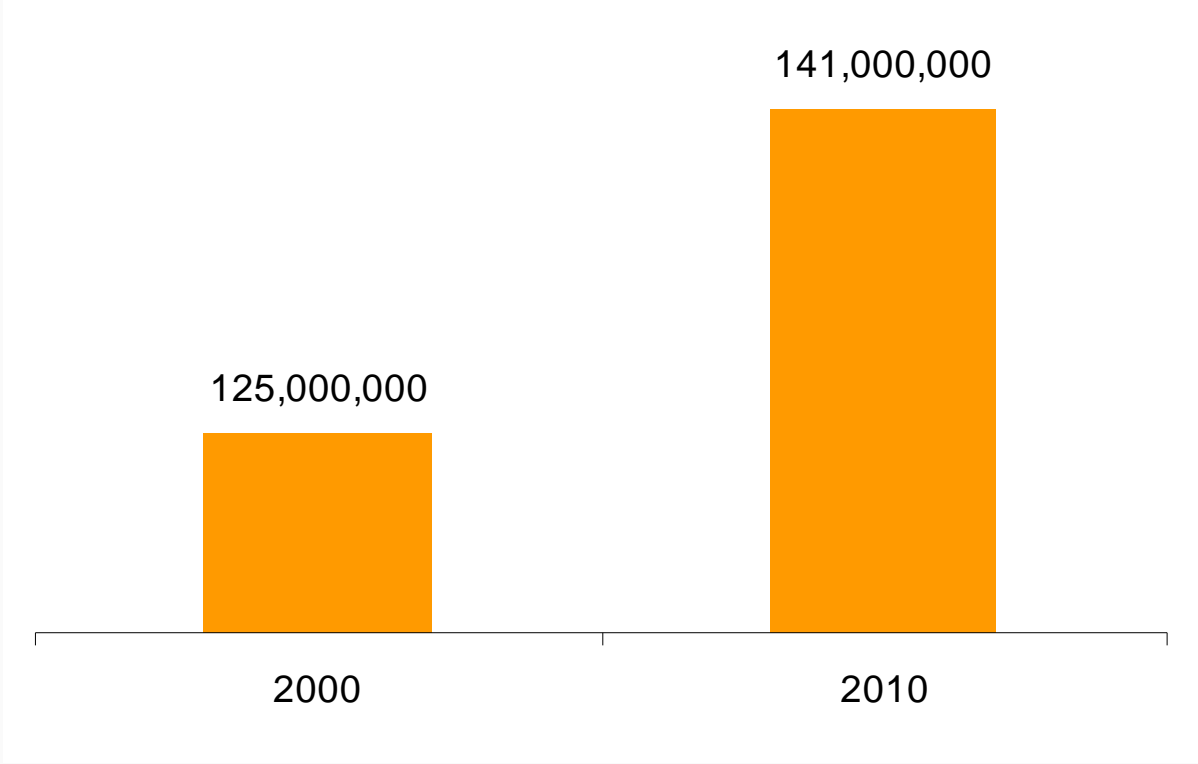
## 2. *Assemble Some Evidence*

- What are the problems?

# *Changing Needs*

- 1900–1950
  - Infectious diseases
- 1950–2000
  - Episodic care
- 2000–2050
  - Chronic care

# Growing Prevalence of Chronic Conditions

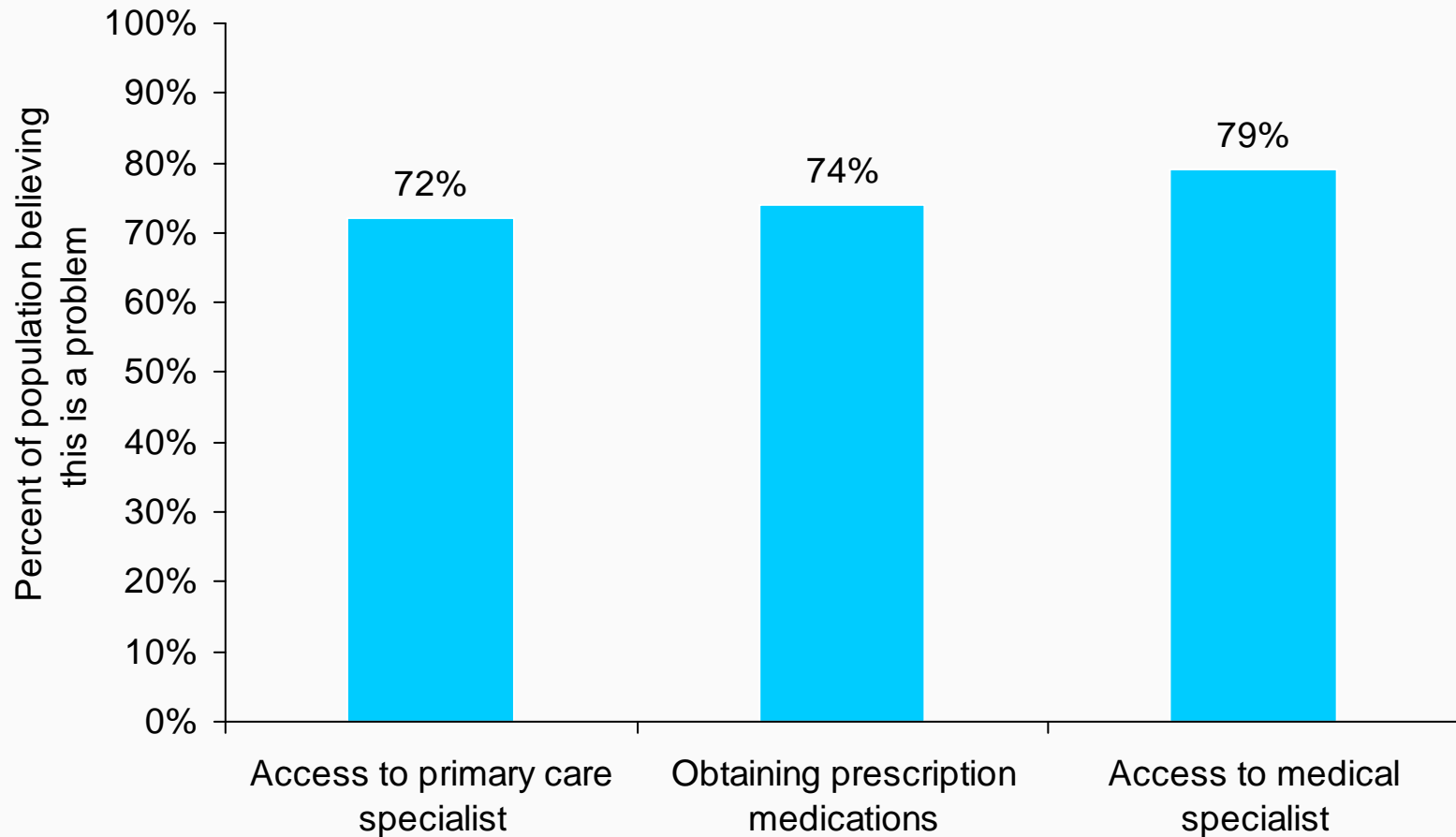


Data Source: Wu, Shin-Yi, and Green, Anthony. *Projection of Chronic Illness Prevalence and Cost Inflation*. RAND Corporation, October 2000.

# *Medical Care Spending*

- Sixty percent of medical care spending is by people with multiple chronic conditions

# Three-quarters of Americans Believe That Access to Care Is a Problem for People with Chronic Conditions



Data Source: random nationwide surveys conducted by Harris Interactive and Gallup for Partnership Solutions  
Note: three-fourths said that access to medical services is a problem; nine-tenths said that getting adequate health insurance is a problem



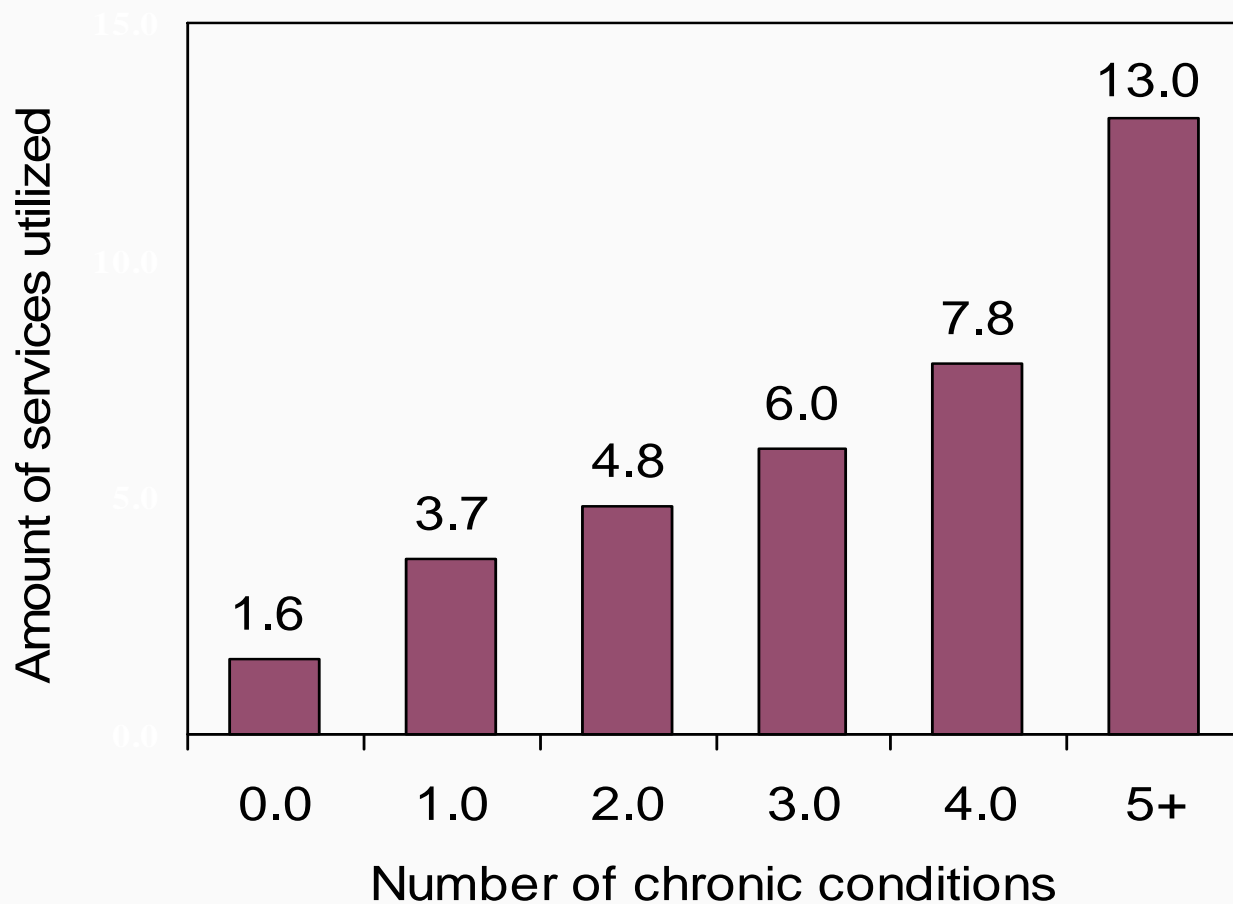
# *Insurance Coverage*

- Eighty-one percent of all physicians reported that health insurance coverage was “not sufficient to cover all the types of care” patients with chronic conditions need
- Eighty-nine percent of people report difficulty getting adequate health insurance coverage for chronic conditions

# Chronic Conditions and Health Care Confusion

- Percentages of people with chronic conditions who answered **“sometimes”** or **“often”** when asked how often the following happened in the past 12 months
  - Been told about a possibly harmful drug-drug interaction—54 percent
  - Been sent for duplicate tests or procedures—54 percent
  - Received different diagnoses from different clinicians—52 percent
  - Received contradictory medical information—45 percent

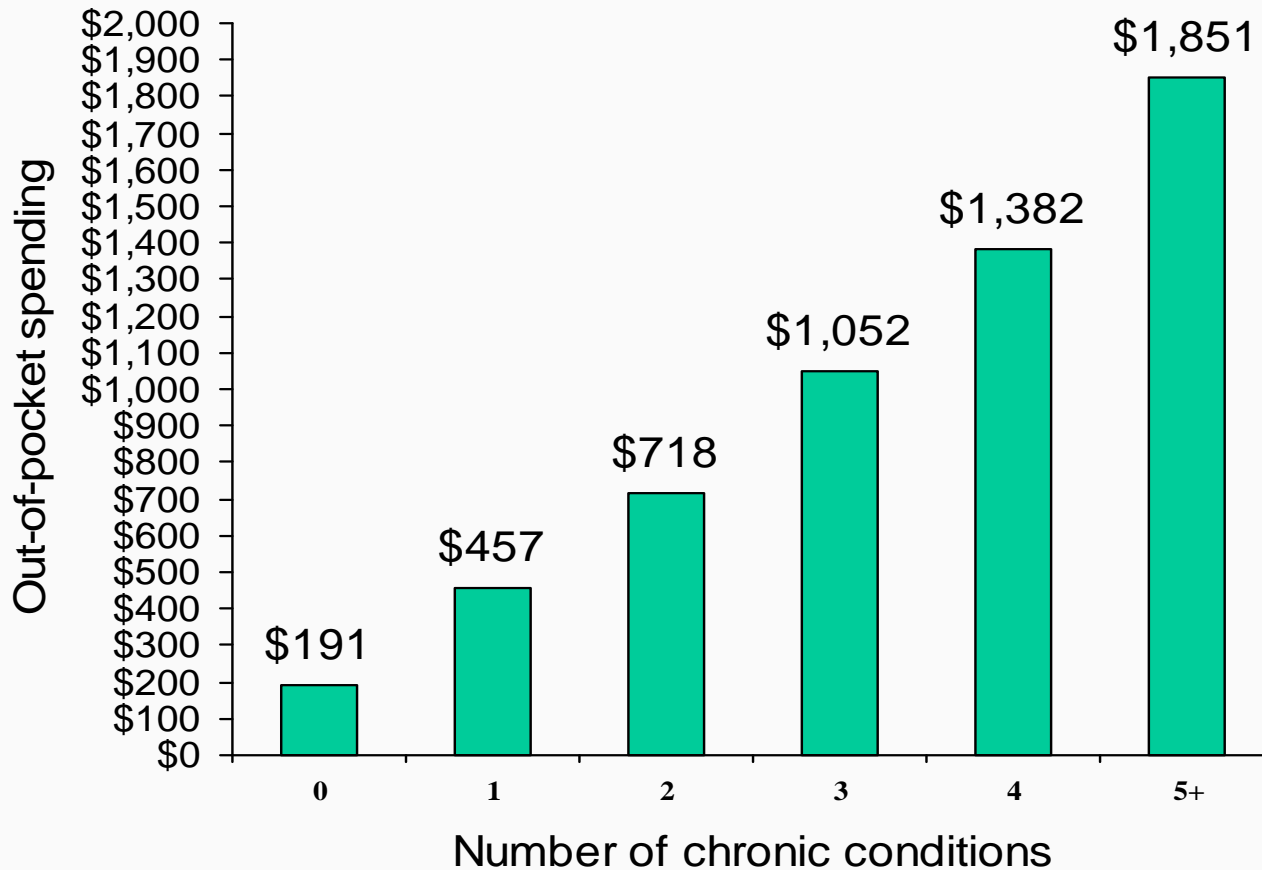
# *The Number of Unique Doctors Increases with Number of Chronic Conditions*



# *Disease Management Rationale*

- Only 50 percent of practice guidelines are followed

# Out-of-Pocket Spending Increases with Numbers of Chronic Conditions



Data Source: Medical Expenditure Survey (2000)

# *Medical Necessity*

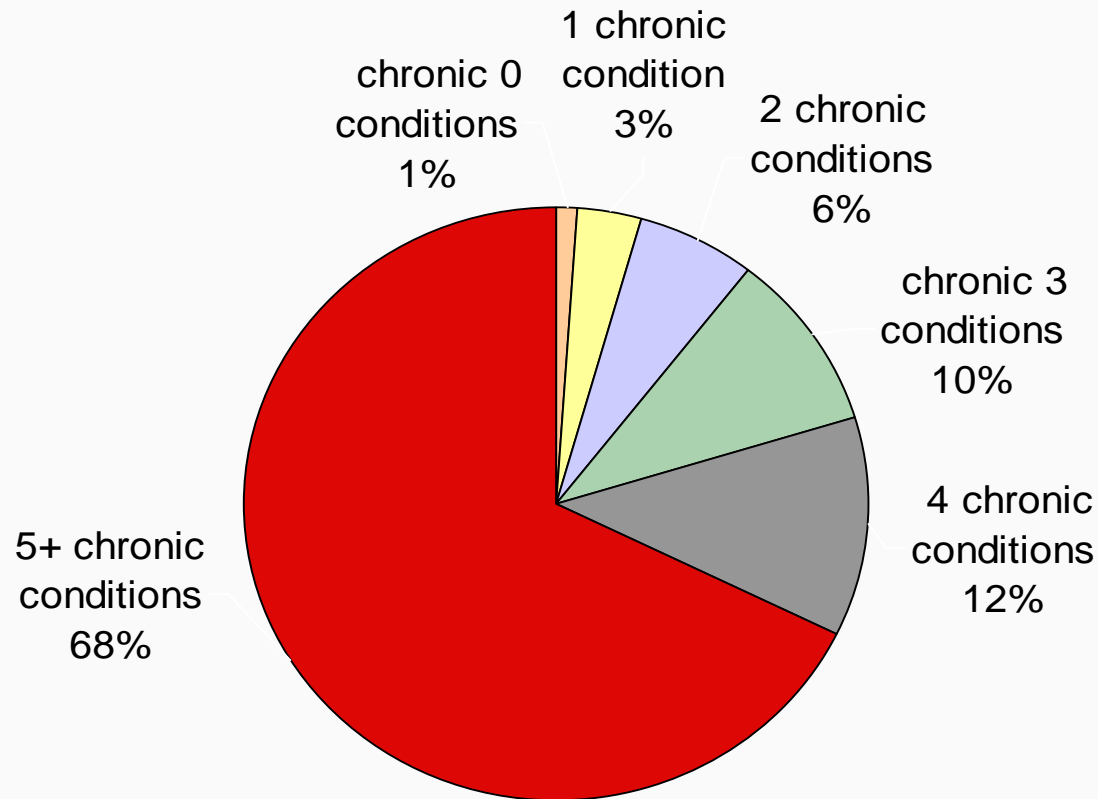
- Services may be covered but denied using medical necessity criterion
- Standard should be maintaining level of functioning, not improvement

# *Medicare Does Not Know It Is a Program for People...*

- With multiple chronic conditions

# Beneficiaries with Five or More Chronic Conditions

## Account for Two-thirds of Medicare Spending



Source: Medicare (2001) 5 percent sample



## 2. *Assemble Some Evidence*

- What are the problems?



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## *Section E*

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The Eightfold Path, Part II

### *3. Construct the Alternatives*

- More research
- New demonstrations
- New legislation
- Revise regulations

## 4. *Select Evaluation Criterion*

- Health status of Medicare beneficiaries
- Aggregate Medicare spending
- Out-of-pocket spending by Medicare beneficiaries
- Satisfaction of Medicare beneficiaries

## *5. Project the Outcomes—Research, Demonstrations*

- Research and demonstrations
  - Clearer understanding of problem and solutions

## 5. *Project the Outcomes—Legislation*

- Legislation
  - What is legislatively possible?
  - What is most important change?
  - How will change impact lives of Medicare beneficiaries?

## 5. *Project the Outcomes—Regulations*

- Regulations
  - What changes can be done using regulation?
  - What are the most important changes?
  - How will the regulatory changes impact the lives of Medicare beneficiaries?

## 6. *Confront the Trade-offs*

- What is most important and likely to succeed?



## 7. *Decide—Research*

- Research
  - Medicare will conduct research on chronic conditions

## 7. *Decide—Demonstrations*

- Demonstrations
  - Medicare will conduct demonstration to provide better care for people with chronic illness

## 7. *Decide—Legislation*

- Legislation
  - Large population groups will be given instruction on better care of chronic conditions

## 7. *Decide—Regulations*

- Regulations
  - Medicare will revise its definition of medical necessity

## 8. *Tell Your Story*

- Medicare is a program for people with chronic conditions...  
but does not know it