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Economic and Financial Considerations in Health Policy

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Section A

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

[Graph showing the tradeoff between Guns and Butter, with Guns on the Y-axis and Butter on the X-axis.]
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

[Graph showing diminishing returns with 'Input' on the x-axis and 'Output' on the y-axis.]
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
### RAND Health Insurance Overall Results

<table>
<thead>
<tr>
<th>Coinsurance</th>
<th>Probability of Medical Use</th>
<th>Expenses per Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>Free</td>
<td>87%</td>
<td>$1,019</td>
</tr>
<tr>
<td>25%</td>
<td>79%</td>
<td>$826</td>
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<tr>
<td>50%</td>
<td>74%</td>
<td>$764</td>
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<tr>
<td>95%</td>
<td>68%</td>
<td>$700</td>
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</table>
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
Section B

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

- Medicare: 14%
- Medicaid: 8%
- Social Security: 24%
- Interest: 8%
- National Defense: 20%
- Other: 26%
Maryland State Budget: Fiscal Year 2004

- Health and Medicaid: 25%
- Transportation: 14%
- All Others: 28%
- Education: 21%
- Public Safety and Corrections: 6%
- Human Resources: 7%
Corporations

- 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
Unions

- Corporations negotiate with unions over total compensation package
- Total compensation = wages + benefits
- If health benefits increase faster than total compensation than 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

- 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 costs
Section C

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)
Section D

The Eightfold Path, Part I
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

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.
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

Source: Harris Survey, 2000
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?
Section E

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