New Health Economics Publications from HERO

Health Economics Research programme at the University of Oslo has published four working papers in the HERO Publications and On-line Working Paper Series. In this HEROletter we will present these papers with a short abstract for each. Those who are interested can read the reports at WWW, or download PDF files in full text versions, from internet adress http://www.sv.uio.no/hero/publications.htm

2001: 1  "Health Insurance: Treatment vs. Compensation"
Asheim, G., Emblem, A.W., & T. Nilssen, The Department of Economics, Frisch Centre, & Agder College
Like most types of insurance, health insurance offers compensation to the insured if the insured-against event occurs. Unlike most insurance, however, the compensation may take two distinctly different forms: The health insurance policy may either provide for coverage of medical expenditures (in part or in whole), or it may provide for a cash compensation of income loss caused by illness. This aspect of health insurance has interesting implications. Asheim, Emblem and Nilssen view in this paper health insurance as a combined hedge against the two consequences of falling ill: treatment expenditures and loss in income. They discuss how an individual’s ability when healthy affects her decision on whether to buy health insurance with treatment to full recovery if ill or with partial treatment combined with cash compensation for the resulting loss in income. The results show that a high-ability individual demands full recovery and is fully insured, while a low-ability individual demands partial treatment and cash compensation and is only partly insured.

2001: 2  "Politicians and soft budget constraints"
Dalén, D.M., Moen, E.R., & C. Riis, Norwegian School of Management, & Frisch Centre
From the perspective of political economics the authors study the use of soft budget constraints. What happens if a partly partisan government confronts a budget crisis in a politically important sector, e.g. like the health care sector?. To what extent wants the government to make additional grants to the sector depends on economic conditions and on the preferences of the government, both unknown to the electorate. Thus, the government’s budget response gives a signal of its preferences, and may thereby influence the probability that the government is re-elected. As a result, the handling of a budget crisis becomes inefficient even from an ex post point of view, in the sense that it does not react adequately to changing economic conditions.

2001: 3  "Designing Competition in Health Care Markets"
Dalén, D.M., Moen, E.R., & C. Riis, Norwegian School of Management, & Frisch Centre
How to set prices in the health care market?. The authors propose a simple, market based mechanism, namely a system where the patients are auctioned out to the hospitals. The aim is to characterize principles as to how such an auction should be designed. In the case of elective treatment, health authorities thus organize a competition between hospitals. The hospital with the lowest price signs a contracts with authority (or the insurer) that commits him to treat a given number of patients within a predetermined period.
However, this is not a simple mechanism that identifies the hospital with the lowest treatment cost. Due to potentially rapid and unpredictable shifts in demand, treatment capacity may be hard to know in advance. There is always a risk that treatment must be canceled due to arrival of patients that require acute treatment. This calls for a market design that accounts for the risk of default.

The main result in the study is that the expected cost for the government is reduced if the government chooses to "subsidize" default. This could be thought of as a system in which the government buys treatment in the spot market in the case of default, and let the hospital pay a default fee that is lower than the spot price. The reason why this reduces expected costs for the government is that the effect on the bids is asymmetric: The second lowest bid is on average reduced more than the winning bid. Hence, the winner’s profit tends to shrink. This is due to what we characterize an endogenous correlation. Since the cost of treatment increases in the default risk (as the hospital must pay a penalty if it defaults), high cost hospitals typically have larger default risks than low costs hospitals.

Grepperud, S., & P.A. Pedersen, Centre for Health Administration, Bodø Graduate School of Business & Department of Economics, Canterbury

Should an principal rely completely on agents’ intrinsic motivation rather than employing incentive payments? Grepperud and Pedersen analyses optimal contracts in a principal-agent model where the agent is intrinsically motivated at the outset and there is an endogenous relationship between the structure of incentive payments and intrinsic motivation (crowding effects).

The analysis shows that crowding effects have implications for the optimal contract and that under some conditions the principal can do better without implementing any economic incentives. Furthermore, it is shown that when high-powered incentives diminish intrinsic motivation (crowding-out) the first-best solution in a principal-agent framework is unattainable.

We do have a limited number of the reports in paper format, which you can order from hero@hero.uio.no. Most of the reports can be downloaded in PDF-format from WWW: http://www.sv.uio.no/hero/publications.htm

If you want information about new releases in our English HERO Publications and On-line Working Paper Series in health economics please send an e-mail to hero@hero.uio.no.

Previously released HERO publications (In English):

2000: 5  "Why do people demand health?”, Kverndokk, S., Frisch Centre
2000: 9  "Private health care as a supplement to a public health system with waiting time for treatment”, Hoel, M. & E.M. Sæther, The Department of Economics, UiO & Frisch Centre
1999: 1  "Impact of the public/private mix of health insurance on genetic testing”  Hoel, M. & T. Iversen, The Department of Economics, UiO & Center for Health Administration
1999: 2  "The interaction between patient shortage and patients waiting time”  Iversen. T. & H. Lurås, Center for Health Administration & Frisch Centre
1999: 3  "The importance of micro-data for revaeling income motivated behaviour among GPs”. Iversen, T. & H. Lurås, Center for Health Administration & Frisch Centre