

PREFACE

All those who wish to develop a deeper understanding of health economics—including undergraduate and graduate students in economics, business, public health, or public policy—should find *Health Economics*, Third Edition, helpful. It is written to serve a variety of users, and the content should be accessible to any student who has successfully completed an intermediate undergraduate economics course. The text presumes a working knowledge of the basic concepts of utility theory (utility functions and indifference curves), demand curves, cost curves, consumer surplus, and the like. Students who feel rusty in these areas would probably make better use of this text by undertaking parallel refresher work in microeconomics. However, a brief survey of this material appears in the end-of-book appendix to serve at least as a refresher for those who have had intermediate microeconomics previously, or as a *very* brief introduction to the material for those who wish to tackle this book without the previous course work. *Caveat emptor*: entire textbooks normally cover the material contained in this brief appendix!

As one surveys the field of health economics, one of the first major articles on medical care in economics journals (by Kenneth J. Arrow, who later received a Nobel Prize in economics) emphasized the importance of uncertainty, and I hope that *Health Economics*, Third Edition, will carry forward and extend that tradition. This text stresses the effects of uncertainty and incomplete information, both on the market for medical care and on the sustenance of health. The importance of uncertainty in generating the demand for health insurance is obvious, and every analyst of the medical care and insurance markets has encountered this uncertainty.

As this text repeatedly emphasizes, uncertainty appears in many other important ways in the study of health economics. We understand intuitively that medical treatments do not always produce the desired results, and hence that the production of health itself contains substantial uncertainty. As numerous studies have demonstrated, the medical profession as a whole harbors considerable uncertainty about the average and incremental effectiveness and desirability of using many medical interventions, ranging from coronary bypass surgery to the hospitalization of a child for a middle-ear infection. Recently, questions of information have become more prominent, particularly when asymmetric information exists—in other words, when the patient and the health care provider, or the insurance company, the doctor, and the patient have differing amounts of pertinent information.

Uncertainty also pervades the structure of health insurance, the contractual arrangements that exist between patients and doctors, and the relationships between doctors and hospitals, doctors and insurers, and hospitals and insurers. In addition, a wide range of regulatory interventions in the health market (e.g., licensure and new drug testing) is directly linked to uncertainty, and the presence of other regulations (e.g., laws limiting hospital construction or cost-control regulations) can be indirectly linked to uncertainty as a social response to the “side effects” of health insurance. *Health Economics*, Third Edition, examines all of these topics in detail. Even the newest forms of organizing the delivery of health care—the so-called “integrated delivery systems”—arise in an important way to deal with information about patients that is otherwise unobtainable in a more fragmented delivery system.

As far as the organization of the text goes, wherever I introduce concepts that might not have been covered thoroughly in preceding economics courses (or where the student might benefit from a conceptual review), I include boxed material to elaborate on the ideas. Examples of these “boxes” include review of the concepts of elasticity of demand, monopoly pricing, and statistical concepts such as mean, standard deviation, and regression analysis. Chapters dealing mostly with theoretical concepts are followed immediately by companion chapters that develop applications of those concepts (e.g., concepts of demand for medical care are followed by evidence about the importance of various factors as they affect demand). Later chapters build on the conceptual and basic empirical material in earlier chapters.

The text avoids the use of calculus, but I have included in appendixes to several chapters additional material that depends in part on calculus and statistics. I have also included optional topics that lie beyond the scope of some courses for which this text might be appropriate. The chapter on international comparisons of health care systems, for example, might prove particularly useful to students of international health or to students seeking to examine U.S. health care spending in a comparative context.

The referenced readings are intended to expand students’ understanding of the text material. Any student contemplating further study in health economics should become accustomed to dealing with original source materials such as journal articles and reports. Empirical studies in this field are burgeoning so rapidly that the only way to “keep up” is to read original sources. This edition has added dozens of new references to important material published since the second edition came out six years ago, and—obviously to any scholar in the field—even that addition of new material barely scratches the surface of the amount of new knowledge being produced. In the field of health economics, alas, the adept scholar must keep abreast of a wide variety of sources. Important material appears in some “main line” economics journals, and several specialty journals in the field now exist, most prominently

including the *Journal of Health Economics* and *Health Economics* (a journal sharing the same name as this textbook, but otherwise not connected in any formal way). A series of journals in the realm of “health services research” often produce valuable studies for the scholar of health economics, including *Medical Care*, *Inquiry*, *The American Journal of Public Health*, *Health Service Research*, *Health Care Financing Review*, and *Health Affairs*. Many very important studies appear in prominent medical journals, including *The New England Journal of Medicine*, *JAMA*, and specialty journals such as *Annals of Internal Medicine*, *Pediatrics*, and the like. This is a wide literature with which one must “keep up,” but electronic journal search capabilities, particularly MEDLINE in the realm of medical journals, can keep the problem within manageable dimensions.

Two excellent resources are now available for students of health economics. First, a set of “classic” readings, many of which are discussed in this book, appear in a two-volume set edited by A. J. Culyer, entitled *Economics of Health* (Hants, England: Edward Elgar Publishing Company, 1991). Most recently, a two-volume set of new writings by leaders from around the world in the field of health economics has appeared, *Handbook of Health Economics*, edited by A. J. Culyer and J. P. Newhouse (Amsterdam: North Holland Press, 2000). Perhaps more than any other written material, this two-volume set will be a considerable asset to anybody wishing to extend their understanding of the field of health economics. Where appropriate, I have included references to individual chapters from this new *Handbook* throughout this book and highlighted at the end of each chapter here the relevant chapters from the *Handbook*.

Data describing basic facts about the U.S. health care system are now readily available on the Internet. By far the most useful single source of descriptive data for the United States is an annual report entitled *Health, United States*, published by the National Center for Health Statistics (online at <http://www.cdc.gov/nchs/hs.htm>). This publication provides an extremely valuable resource for the student of health economics, and typically represents the most current available data of its type.

This text is accompanied by a website that provides students access to many online resources used by health care professionals and economists. An online Instructor’s Manual is also available on this website, featuring teaching tips, sample essay questions, additional project ideas, and more. To access this site go to <http://www.aw.com/phelps>.

Finally, the sets of problems and questions at the end of each chapter are designed to help students assimilate text material and to stimulate further thinking about some of the ideas presented. I have provided prototype answers to about half of these questions at the back of the book.

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