

Competition and incentives: scientific and societal challenges

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Introduction

- Very broad topic: I will only be able to make some very general points.
- I will first mention some broad societal challenges and then sketch what I consider to be the most urgent (and fascinating) scientific challenge.

Societal challenges

1. *The availability of more and better genetic information:*
 - increased focus on prevention (and individual responsibility?).
 - difficult challenge for markets:
 - EITHER increasing problem of asymmetric information.
 - OR increasing danger of risk selection.
2. *The increasingly unclear boundary between long term care and health care.*
 - will “markets” be able to steer the coordination between health care and care (including the necessary shift from hospital treatment to ambulatory care)?

Societal challenges

3. *Increasing cultural diversity* (preference heterogeneity) and *increasing education level of consumers/patients*: makes markets more relevant!

Yet, position of society towards “markets” and “competition” in health care remains ambiguous (to say the least). This is to some extent due to:

- (a) the sometimes primitive positions taken by economists.
- (b) the neglect of crucial factors in the standard economic analysis.

A realistic view on markets

- Effects of choice hard to predict, when there are many dimensions:
 - Price regulated/fixed: positive effects on quality to be expected IF patients are informed.
 - Price and quality competition: effects will depend on availability of information and on the strength of consumer reactions.
- *Introducing choice can only work:*
 - *if consumers have the necessary information.*
 - *if consumers take “rational” decisions, reflecting their own well-considered preferences.*

Preference heterogeneity

- If preferences are homogeneous, it is sufficient that there is an active and well-informed subgroup of consumers at the margin.
- However, with heterogeneous preferences, there is an issue of sorting consumers in what is the best health plan for them – and poorly informed (or “irrational”) consumers will then end up in suboptimal situations.

Illustration: choice on insurance markets

- Cost awareness: is taking distance the best setting to decide about the trade-off between price and quality? In fact, evidence that consumers focus (too strongly?) on costs. Moreover, it is difficult for consumers what would be their preferences when they need care.
- Choice between different insurance policies is very difficult:
 - Multiple attributes, complex policies.
 - Human beings (including medical doctors and economists) are not good in evaluating probabilities.
 - Time preferences and time inconsistency: pay now, get (perhaps) reimbursed later.

A striking (exemplary) case

- Choices of 23.849 (relatively highly educated) workers in an American firm offering an insurance menu with 48 different options (copayments, stop-loss, deductible).
- Some of these options were clearly dominated. It was in almost all cases advantageous to choose the option with the highest deductible.
- Analysis: Bhargava et al., Quarterly Journal of Economics, 2017.

Dominated options

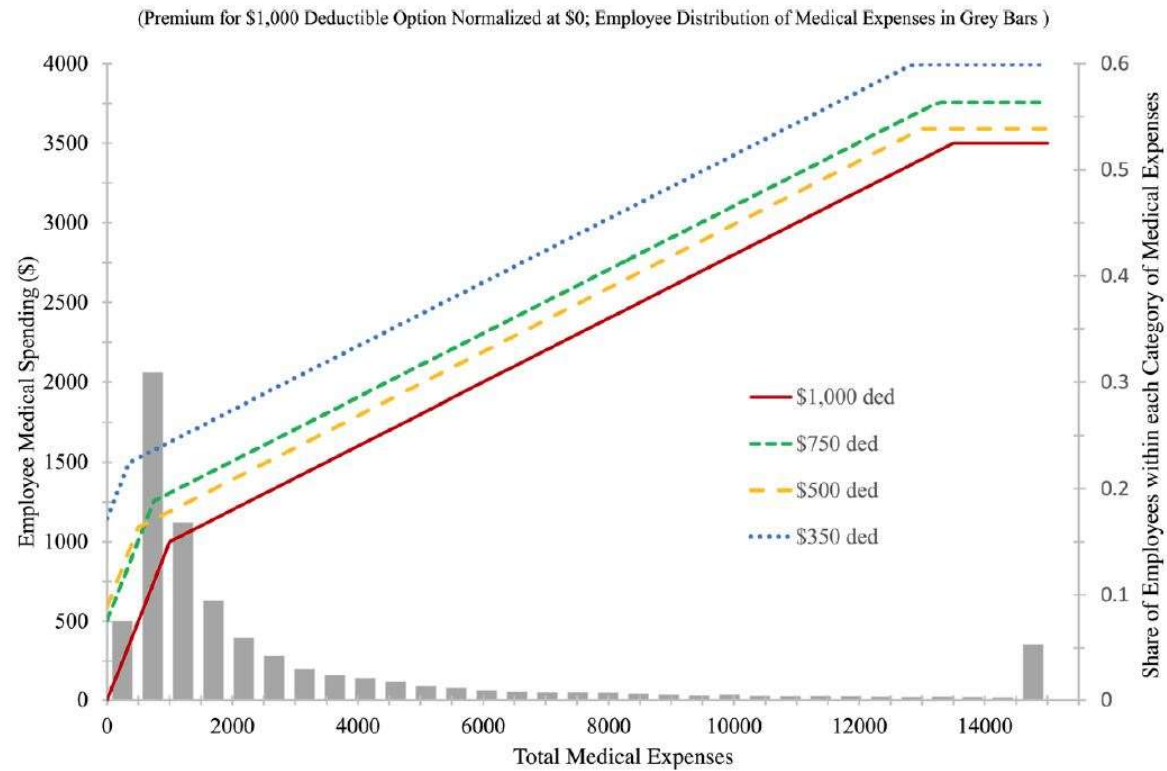
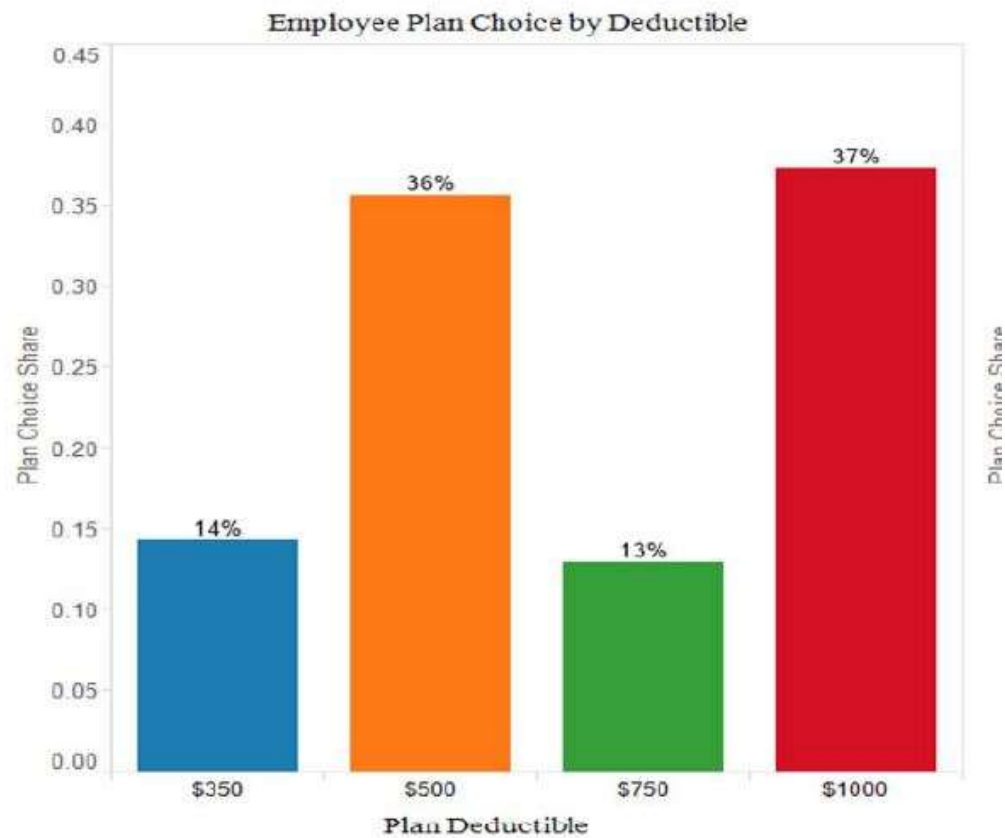


FIGURE I
Employee Spending by Total Medical Expenses

Actual choices



Interindividual differences



The scientific challenge: a research program

- (a) How do consumers use information? Are there significant biases in their decision-making?
- (b) How do non-material incentives for providers interact with monetary incentives?
- *intrinsic motivation*. Most providers want to improve their performance and comparisons with peers give them useful information.
 - *naming and shaming*. Like all human beings, providers care for their reputation.

Market design

Given these insights, the interesting issue becomes one of market design: how should we design markets so as to lead to the “best possible” results?

- *What information should be given to consumers and how?*
- *Should we spread all the information about provider performance?*
- *Should we restrict choice or leave choice completely free?*
- *Would it be optimal to have a default-option?*