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Health Care's Free Market Paradox

The U.S. economy relies on the free market principle of market competition. Here, individuals, rather than government, make the majority of decisions regarding economic activities and transactions. There are, however, essential organizations — including not-for-profit hospitals like Florida Hospital — that operate in the netherworld between a free market and a command market.

Free Market Economics
In a free market economy, consumers and businesses decide what they want to produce and purchase. The government plays a limited role in the marketplace, and few or no coercive measures interfere with exchanges between buyers and sellers. Buyers are free to determine the value or utility of an item relative to the price they are willing to pay. Sellers are free to determine if they will part with goods or services at the price the buyer offers.

While there are few examples of purely free markets, the U.S. economy is heavily free market. Suppliers of goods and services — both essential and non-essential — set prices according to supply and demand, and have minimal government or other coercion.

Command Market Economics

1 Wikipedia

Our Goal: To become a global pacesetter through the delivery of pre-eminent faith-based health care.
The free market is the opposite of the command market, in which the government decides which goods and services are produced, how many are produced, and what they will cost.

**Health Care’s Mixed Market**

For half its economic activity, health care operates in a command market. The government, for both Medicare and Medicaid, sets the purchase prices for hospital and physician care. In most cases, the purchase price is less than the cost of providing the service, yet providers are more or less obligated to provide the services. Not-for-profit providers, as a condition of their tax exemptions, must participate in the Medicare and Medicaid programs. Hospitals also cannot engage in exchanges in the emergency department, where the government requires that all patients be seen regardless of ability to pay. In a free market, a rational business entity would either negotiate a better price or refuse to treat these patients.

Health care market dynamics differ in other ways. People may choose to buy a new pair of shoes or a new car, but they do not choose to get sick. When they do, their consumption of hospital resources is based not only on their condition but also on the decisions of a third party: the physician, who is free to order as many or few tests and procedures as he or she deems necessary.

The physician is an integral part of the health care sector but he/she, too, is constrained by the command market. In a free market, the supply of physicians would reflect the demand for services. This is not the case: government limits the number of physician training slots and creates artificial ceilings that limit the physician supply. Hospitals are now forced to pay scarce specialists like ENTs and neurosurgeons to cover the Emergency Department.
For the other half of its economics, health care operates in the free market. Hospitals and other providers purchase supplies and equipment from for-profit entities. They must make capital improvements and pay competitive salaries. They are subject to the same economic and market fluctuations as the rest of the country, and must remain competitive in order to survive and grow.

**Cross-Subsidies**

Because health care is a mixed-market entity, its economics rely on the concept of cross-subsidy. In this model, services that generate a profit subsidize those that lose money. For example, certain surgical procedures help offset losses from emergency departments, physician training and the like.

The largest cross-subsidies occur when businesses and people with insurance help equalize losses from charity care and government payers. This type of cross-subsidy, often called cost-shifting, adds over $1,600 to each insured person’s hospital inpatient bill.

**The Health Care Reform Debate**

The free market/controlled market paradox lies at the heart of the 2008 presidential debate about health care reform. Some candidates want more government involvement in the health care system by expanding public programs. Others believe that a free market has far more potential to decrease health and health insurance costs down while providing greater access to coverage.

These approaches could not be more different, but one thing is clear: an understanding of health care’s complex, mixed-market economics is crucial to any changes to health care economics in the 21st century.

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