

COPYRIGHT NOTICE:

David Dranove: The Economic Evolution of American Health Care

is published by Princeton University Press and copyrighted, © 2000, by Princeton University Press. All rights reserved. No part of this book may be reproduced in any form by any electronic or mechanical means (including photocopying, recording, or information storage and retrieval) without permission in writing from the publisher, except for reading and browsing via the World Wide Web. Users are not permitted to mount this file on any network servers.

For COURSE PACK and other PERMISSIONS, refer to entry on previous page. For more information, send e-mail to permissions@pupress.princeton.edu

Introduction

FOR THE PAST two decades, I have researched the role of market forces in health care. As a graduate student, I was privileged to study under Alain Enthoven, one of the leading architects of the managed care revolution. Since then, I have been on the faculty of two outstanding business schools. I have always been a big believer in the benefits of competition.

In this book I use an economic lens to examine the historical development of managed care. The starting point for this analysis is the “shopping problem.” Economists have long recognized that it is very difficult for patients to shop for medical care. Patients have poor information about what care is needed and where to buy it and also have muted incentives to shop for the best price. The result is that patients are unlikely to be cost-effective medical decision makers. The evolution of the health economy, from the traditional system centered on autonomous physicians, through government planning efforts to today’s managed care organizations, represents an ongoing effort to help patients solve the shopping problem.

When I started to write this book, I fully expected it to be a sweeping endorsement of managed care. Indeed, I find a lot of evidence that managed care is working. By one credible estimate, managed care is saving patients over \$300 billion annually. At the same time, there is no systematic evidence that managed care has harmed quality. Finally, managed care has clearly won the market test, with the vast majority of privately insured patients enrolled in some type of managed care plan. But managed care has utterly failed to win the trust of American patients and is a favorite target of politicians on both sides of the political spectrum. Piece by piece, politicians may legislate managed care out of existence.

Patients do not trust managed care because they see it as an unnecessary intrusion into the traditional physician-patient relationship. One of my goals in writing this book has been to detail the strengths and weaknesses of the traditional relationship. Another is to refocus the public debate about managed care. The current, simplistic view is that managed care is a cost containment mechanism run amok. The simplistic solution is regulation. I believe that the market forces unleashed by managed care offer opportunities to vastly improve upon the traditional health economy by simultaneously improving quality and containing cost.

In the eighteen months since I began this book, my optimistic view of managed care’s potential has wavered. I accept the possibility that managed care will never fulfill its promise. But the problems with managed care come mainly from the outside. I have no doubt that market forces can

4 INTRODUCTION

enable patients to obtain the highest quality care at low prices, while encouraging providers to be efficient and innovative. But I see several hurdles, largely beyond the control of managed care organizations, that must be overcome before we reach this state of health care nirvana:

- Markets have to remain competitive, free of the power struggles emerging between large buyers and providers. This will require vigorous enforcement of antitrust laws.
- There will need to be substantial improvements in health care data. We need better outcomes measures and must be able to link patient-level medical records across providers. This may necessitate government intervention, both to coordinate the collection of data and to establish a confidential patient “identifier.”
- Providers must accept that quality varies and must actively engage in quality measurement. Quality measurement is imperfect and unfair to many providers, but providers should rally behind the quality movement because patients stand to benefit.
- Patients must become consumers, willing to shop around for the best managed care plans and the best providers. Patients have much to gain by doing so, perhaps their very lives.

It seems to me that these are all necessary conditions for managed care to be successful. If even one hurdle remains standing, patients will fail to realize the full potential of a truly competitive health economy.

While this seems like a lot to overcome, I remain cautiously optimistic. Despite ongoing merger activity on both the provider and the buyer sides of the market, most urban health care markets remain competitive, and antitrust agencies continue to fight against blatantly anticompetitive combinations. There are massive public and private sector efforts to create sophisticated health care data systems. Providers are gradually getting used to quality evaluation, and patients are increasingly using quality data. We can expect to see more and better data in the future.

My optimism is tempered by the knowledge that improving data and changing attitudes will not happen overnight. In the meantime, patients are growing impatient with organizations that seem to do a better job of managing costs than managing care. Seeking to appeal to angry voters, legislators will enact laws that undo the potential of managed care.