Chapter 5

The Economics of Health: An Overview of the American Healthcare System

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ABSTRACT

The American healthcare system is vast and complex. An overview of the United States’ healthcare system provides a view into the interrelated dynamics between three categories of factors: consumers, intermediaries, and providers. Consumers demand health inputs in order to produce health status that allows them to live productive lives. Intermediaries, such as insurance companies and government programs, reduce the direct cost of healthcare for consumers. Providers, such as hospitals and physicians, amongst others, have historically exhibited a degree of monopolistic power in the healthcare market. The modern trend towards managed care organizations, firms that vertically integrate multiple aspects of the healthcare market, aims to reduce costs imposed by such providers.
INTRODUCTION

Why does the United States spend so much money on healthcare? This is a popular question in modern socioeconomic discourse, as the United States spends more on healthcare than any other country in the world by a large margin (OECD 2019). This disparity attracts a lot of attention from researchers looking to design reform measures. However, this leads to additional questions, such as; how does the market for healthcare function in the United States? And, is it efficient in allocating resources? In order to answer these questions, the various facets of the American healthcare system must be examined in detail in order to untangle their interdependence and highlight inefficiencies.

Healthcare is a fundamentally essential factor in modern societies. The individual incentive to prolong one’s life and alleviate discomfort means that healthcare is universally demanded by consumers. Even healthy individuals will likely face medical adversity at some point that requires professional treatment. Moreover, the extension of life expectancy across the population through advances in healthcare has led to increased economic output over time. Economically, the healthcare industry makes up a large portion of both capital and labor in the United States. Due to the importance of healthcare in modern society, the system faces a high degree of public scrutiny and criticism. Such criticism is warranted as the United States’ healthcare system contains many inefficiencies that are uncovered through an economic examination; from disproportionate spending and cost increases, to problems in information transmission and distorted market dynamics.

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Consumers

The first category of components involved in the American healthcare system are consumers. This category looks at the demand side of the healthcare market by including consumption behavior, the prices paid by consumers, and the demand of healthcare products and services in the market.
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