Knowledge Problem

July 8, 2009

Health care policy, individual consumption portfolios, and liberty

Filed under: Economics, Liberty — Tags: Economics, health care, Liberty — lkiesling @ 10:27 am

Lynne Kiesling

Two posts I've read this morning about health care resonate for me in combination. The first was Russ Roberts' discussion of his conversation with a new Walmart employee about wages and benefits, where he notes that

> I didn't get to ask her if she had health care coverage at either job. But the conversation reminds me that people prefer different mixes of cash, retirement, health care and so on.
>
> Which is why the political pressure and the threat of coercion that lead to this kind of result [Walmart's support of an employer health care mandate -ed.] is so dangerous and harmful to human beings and other living things.

Diverse, heterogeneous individuals with their own private, subjective preferences over their consumption, saving, investment portfolio mixes.

On a related note, Doug Bandow writes at Cato @ Liberty about Uwe Reinhardt on health care. Commenting on criticisms of government-provided health care's rationing of services, Reinhardt points out that rationing is a fundamental function of markets too. He's technically correct, from a static neoclassical perspective — given a set of resources and unlimited wants, our budget constraints necessitate rationing, and in markets price signals interact with our subjective individual preferences to enable us to allocate our resources optimally.

But Doug makes a deeper point that often gets lost in the technocracy of health care policy:

> But Reinhardt leaves liberty out of the equation. The health care system is a mess, largely because of perverse government incentives through its big health care programs, Medicare and Medicaid, and its tax break for employer-provided insurance.   As a result, we now have a third party payment-dominated system which simultaneously encourages excessive

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> spending and pushes insurers and providers to decide how to "ration" (i.e., limit) care.
>
> What people need is a medical system that allows them to make the basic rationing decisions: what kind of insurance to buy, what kind of coverage to choose, what kind of trade-offs to make between spending on medicine and spending on other goods and services.
>
> Such decisions are complex and people with little means will need assistance. But the specific "rationing" decisions–i.e., the inevitable trade-offs–vary dramatically by individual and family preference and circumstance. Even today's system allows many people some choice between plans and providers. The rise in consumer-directed care is a positive development which is expanding the choices available to Americans.

Put another way, and from a Hayekian perspective, who is doing the rationing matters. With government mandates, bureaucrats do the rationing. With a market for health insurance and health care services, individuals do the rationing. Apply the knowledge problem here as Hayek did to the failure of central planning, and you see the analogy that I think is apt.

Just as individual planning generates superior static and dynamic outcomes relative to central planning, individual rationing generates superior static and dynamic outcomes relative to central rationing, because of the knowledge problem and heterogenous agents with diverse preferences and private knowledge of their own preferences. It also honors the precepts of individual liberty.

UPDATED to add the link to Russ' original post, sorry about that!

UDPATE2: This excellent Ron Bailey post at Reason's Hit & Run complements my above argument, and includes a link to Shikha Dalmia's thorough exposure of the fallacies in the current health care policy debate.

Comments (4)

4 Comments »

1. Excellent post, Lynne.

   Comment by Brian — July 8, 2009 @ 10:41 am

2. Thanks Brian!

   Comment by lkiesling — July 8, 2009 @ 11:11 am

3. I agree in principle, but I suppose there must be

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some sort of market failure in American health market, because the percentage of GDP per capita is much higher that in Europe, and the results aren't any better. So, which way?

Comment by Carlos Ferreira — July 9, 2009 @ 1:04 pm

4. Your comments and the Cato article are in dire need of a reality check. The mess that we have today actually was developed by the private market. Blue Cross and Blue Shieled were hospital and doctor association "prepay" creations to ensure individuals could pay for uncertain expensive treatments. The associations prevented non business groups from forming. The result is that we do not have health insurance institutions(e.g., like term life insurance taken out when outcomes are uncertain), and healthcare is fragmented lacking market coordination. In a multi-provder market generally one entity acts as prime contractor ensuring service and collecting revenues, and others act as subcontractors. This cooedination has not happened in healthcare.

   The market solution is not to quote your free market ideology which in healthcare has failed so miserably, but rather focus on minimum interventions that could make a market solution work better than the clearly superior public solutions adopted in other countries.

   Comment by gnat — July 10, 2009 @ 8:20 am

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