

Consumer choice and demand.

Folland *et al* Chapter 9

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Economics 317

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Chapter 9: Consumer choice and demand

Consumer choice
and demand.

Demand analysis in
a health context.

- ▶ Econ 103 consumer theory with “doctor visits” instead of “apples.”
- ▶ We will run through this quickly.

Bread or health

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a health context.

- ▶ Recall our discussion of health capital.
- ▶ Sweeping a bunch of stuff under the rug, we can use simple analysis to determine how much health the person would choose.
- ▶ (graph: health vs bread PPF)
- ▶ How does the person allocate their resources to generate that health?
- ▶ (graph: consumer's equilibrium, other goods and doctor visits)

Demand shifters

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- ▶ Recall a demand schedule in (price, quantity) space gives the quantity demanded at every price, *holding all else equal*.
- ▶ Changes in anything that affects demand other than price *shift* the demand curve. Changes in price move us along the demand curve.

Price elasticity of demand:

$$\text{Price elasticity} = \left(\frac{\Delta Q}{\Delta P} \right) \left(\frac{P}{Q} \right) \quad (1)$$

where Q is quantity and P is price.

(graph: deriving a demand curve for visits)

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Income elasticity of demand:

$$\text{Income elasticity} = \left(\frac{\Delta Q}{\Delta Y} \right) \left(\frac{Y}{Q} \right) \quad (2)$$

where Q is quantity and Y is income.
(graph: income expansion path)

Other demand shifters

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- ▶ Health status, e.g., demand more doctor visits when sick.
- ▶ Insurance: as we saw in Chapter 8, changing the price the consumer pays by changing the generosity of insurance generally changes the consumer's quantity demanded.

The role of time

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- ▶ We can simply incorporate time into the analysis by converting time costs to dollar costs.

$$\text{full price} = \text{money price} + \text{value of time} \quad (3)$$

- Notice price elasticities are larger (in magnitude) with respect to full price than to money price.

$$E_{Mp} = \frac{\Delta Q}{\Delta P} \frac{P_M}{Q} \quad (4)$$

$$E_{full} = \frac{\Delta Q}{\Delta P} \frac{P_{full}}{Q} \quad (5)$$

Empirical evidence on demand

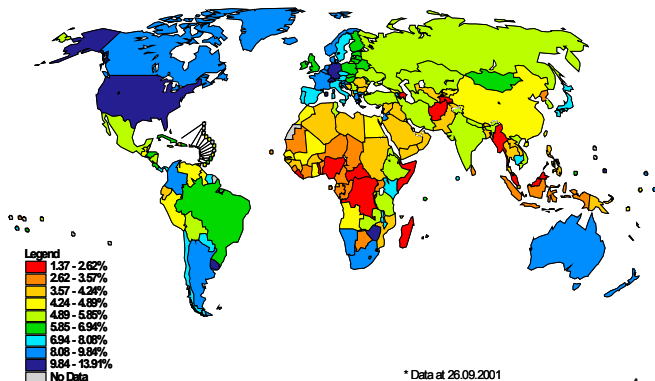
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- ▶ Measurement issues: how do we define a unit of care?
- ▶ Usual problems in statistically estimating the causal effect of price or other determinants on care.
- ▶ Demand is usually estimated to be quite inelastic, ie, changes in price of care lead to relatively small changes in quantity of care demanded.

- ▶ Across people (in the U.S.), income elasticities are quite small.
- ▶ Across countries, income elasticities are quite large: richer countries spend not just more, but a greater fraction of GDP, on health care.
- ▶ How do we reconcile these results?

Health spending around the world, 1998* (measured share in total expenditure, % of GDP)



* Data at 26.09.2001

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Global Programme on Evidence for Health Policy

