FAQ: Demand for Health Care

Question 1: What is the role of the patient regarding the demand for medical care?

Answer 1:

The patient generally has very limited information about health care supply and the associated prices. Historically, the patient has had to rely on the practitioner for all information. The physician may have somewhat of a hidden agenda as far as treatment plans are concerned. The more tests and treatments that are prescribed, the more money the particular physician will make; thereby, the less liability will be faced.

Very ill patients do not have the time or resources to go on a search to compare quality and cost among health care organizations. The average patient is limited in this respect and is intimidated by years of conditioning into respecting the physician to the point that he/she would certainly not question a prescribed treatment plan, but because of the advent of the information age, this situation may be changing.

Patients can easily do research on a focused area because of various sources (notably the Internet), and they may know more about their malady than even their own personal physician knows. Patients are now beginning to question the particulars of treatment and wanting to have a more concerted role in medical choices that are made. This situation has lately been substantiated by various patients' bills of rights that have been adopted by many organizations.

Question 2: What characteristics of the health production function are associated with demand?

Answer 2:

The first characteristic of the health production function associated with demand is that the various inputs are, to some extent, substitutable for one another. For example, there may be situations where a licensed practical nurse (LPN) may substitute for a registered nurse (RN). The costs for the organization would (theoretically) be lowered or minimized.

The second characteristic is the concept of marginal productivity of each input. In our example, if the RN is paid twice the salary of an LPN, the reasonable expectation is that the RN would be twice as productive.

A third characteristic of production functions associated with demand is the distinction between the short run and the long run. The decisions to be made are very different regarding these different time periods. Continuing with the example, in the short run, administrators may substitute LPNs for RNs. In the long run, they may
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decide to totally change the nature of the particular ward from the intensive care unit (ICU) to pediatrics.

**Question 3:** What are some assumptions of medical service production and cost functions?

**Answer 3:**
Legal restrictions may apply as far as substituting inputs are concerned. For example, a registered nurse (RN) may be quite capable of prescribing medications, but legal restrictions will usually prevent this. This is one of the constraints for health care policy decision makers.

The health cost function makes it clear that successful managers will use the least costly combination of inputs. In doing so, the relative prices of the inputs are not distorted. If the Federal Government subsidizes an input (e.g., it provides low-cost loans to assist professionals in their education), this input has been somewhat distorted because the relative price has been lowered. Economic inefficiency in producing that output may result (Feldstein, 2005).

Decision makers may have goals other than cost minimization. Decisions and policies are actually made in the political venue. Not all decisions or policies are rational ones because of this political consideration. Most want to minimize costs whenever possible, but you find that many considerations may come before those that seem to make more sense.

**Question 4:** What are two competing approaches of examining medical markets?

**Answer 4:**
The competitive organizational view of medical markets places reliance upon competitive pressures to urge the goal of economic efficiency. Free-market forces will ensure that the most efficient organizations will survive and thrive as demand for their goods and services steadily increase. With this increased demand, a competitive industry should produce a greater output at a lower price.

A totally different view places greater emphasis on regulation and centralized decision making to achieve the desirable outcomes of a competitive market. Possible restrictions on various inputs will occur as the government steps into the situation to provide more rules and regulations to govern medical services.

These two ideas (increased regulation and greater reliance on market pressures) are competing with one another. Society has generally opted to use the regulating
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approach in examining medical markets. Historically, government intervention has been the hallmark while the medical services market has pursued equilibrium in this country.

Question 5: What is the status of the supply of medical care in the United States?

Answer 5:

There is indeed a shortage of registered nurses (RNs) in the United States. One reason for this lag is that RNs are incrementally co-opting some of the chores that have previously been the domain of physicians so the demand for members of this profession has increased. This demand will continue to grow.

Many may be surprised to find that there is an excess of physicians in the United States. This oversupply is somewhat disguised by the fact that doctors create the demand for more medical services to a large degree. An examination of the situation reveals that there are areas of the country where there remain shortages of physicians. These are the rural and the inner-city areas. This is the case in spite of federal programs designed to address this need.

In the United States, as each medical facility strives to keep up with the latest development, one finds an overabundance of technical hardware. In other developed nations, another approach has been taken regarding the supply of the latest diagnostic and treatment hardware. Other developed nations have national health insurance (the two exceptions on the list of developed nations are South Africa and the United States), so there is really no sense of competition among health care organizations. Each facility does not feel the need for the latest and best technical advances for the sake of market share. The federal governments of these countries purchase these needed machines and strategically locate them to maximize accessibility and use.

Question 6: How have the advantages of economy of scale been addressed by the health care industry?

Answer 6:

Historically, it has been one of the most basic economic axioms that the greater the economy of scale, the lower operating expenses can be driven. Hospitals and other health care facilities generally have a poor track record when it comes to concentrating on this issue as a tactical approach to lowering their break-even points. It is very important for these organizations to lower break-even points for several reasons. When the break-even point is pushed back, more return of investment can be anticipated. More markets are opened when this occurs.
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From an operation’s standpoint, there are two approaches that are useful when considering the question of how to reduce the break-even point further. One goal of operations management is the total elimination of any waste from the value-added chain. Waste may be thought of as anything (activity or material) that does not add value to the services provided. Another tactic in this respect is total quality management (continuous improvement of goods and services). As the quality of services improves, the demand will increase. When demand increases, return on investment increases, and the break-even point drops.

Progressive health care organizations are reevaluating their purchasing procedures and have changed their purchasing paradigm. Many are evolving this paradigm to the contract buyer mode. In this arrangement, several organizations will band together and will accomplish purchasing through a centralized buyer. This buyer will represent several organizations that have previously done their purchasing individually. With such a paradigm, the economy of scale can be realized because the contract buyer has the advantage of large lot purchases to demand constantly the lowest prices available.

Question 7: What is the history of supply provision and the outsourcing of services?

Answer 7:

In the health care industry, purchasing and outsourcing has gone through four stages. Together, these stages could be considered a transition toward partnership (Knod & Schonberger, 2001):

1. **Confrontation with the supplier**: The emphasis of this stage is the emphasis on price (as opposed to quality) and constantly arguing over contracts and compliance and lawsuits.

2. **An arm's length relationship**: The attitudes of all parties are adversarial, but gradually give way to a cautious, tentative working relationship.

3. **A congruence of mutual goals, a coming together**: Both parties can only benefit from higher levels of quality.

4. **A full-blown partnership**: Business plans and data are freely exchanged for mutual benefit.

Question 8: What do patients want, and what do they demand?

Answer 8:
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Patients basically want six things when they receive health care services. First, they want quality and a high degree of excellence in the things health care professionals do. Patients want a high level of customer service orientation, and they want a high degree of flexibility. Generally, this is a point that health care organizations have missed. Patients want to feel that they are more important than the policies and procedures of the organization. Health care professionals should be willing to bend (but not break) the rules where safety issues are not at stake.

Patients want fast response times. They want to be able to expect that health care professionals will do what they say they will do in a reasonable period of time. They want a low amount of variability. Humans are creatures of habit; they want service that will be what they have come to expect. Patients want low costs (Knod & Schonberger, 2001). If health care managers are doing their job of eliminating waste from the operation, they will be able to push prices lower and lower.

In short, patients want exactly what health care professionals want when they are customers themselves. They want respect and the best service possible. To thrive in an ultracompetitive market, health care professionals must be willing to do what it takes to assure that this happens.

**Question 9:** How can you best choose who will supply your organization's needs?

**Answer 9:**

Knod and Schonberger (2001) offer six selection criteria appropriate for choosing who will supply your organization's needs:

- **Financial/Economic:** What is the overall financial health of the prospective supplier relative to the pricing and cost structures of the health care industry?

- **Marketing:** What is the knowledge level and competency of the company’s key personnel? How accessible are they?

- **Operations:** Can their operation give the customer what he/she wants and demands?

- **Information/Data flow:** Is there compatibility of their information system with the customer’s? What are the data sharing and security issues?

- **Competitive factors:** Are there any ethical issues or constraints regarding their other clients or their own suppliers?
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- **Cultural/Ethical factors:** What is the supplier’s track record regarding environmental protection and human resource issues? Is there a strong level of trust?

**Question 10:** What are the advantages to suppliers regarding the idea of partnering?

**Answer 10:**

There are several advantages to your suppliers when they become actual partners with you in the supply chain. One of these is that they can expect stable, high-volume contracts from their customers. They will not be placed in the situation of constantly investing time and energy in sales and in the continuous job of filling the empty spots in the capacity of their operations. Instead, their efforts can be concentrated on increasing the efficiency of their plants and in building better quality.

When vendors become our partners with their customers, new opportunities for economies of scale will open for them. High-volume contracts with your own organizations become springboards for other opportunities through centralized contract purchasers.

Partnering with suppliers will persuade them to improve and do their best while the idea of vendor as business partner matures and takes root. Along with the sharing of business data and business plans will come the inclusive feeling of working together for the common good. When customers partner with their suppliers, everyone will win.

**References**
