FGS Chapter 6 Demand for Health Capital

Health – Consumption – Production all linked

Health versus Health Care

Key insight of Grossman (1972) Health is a stock.

Health care is a flow of services received

Two inputs to Health: time and health care services

Suppose that all of your time can only be allocated between time working and time getting health care (Ignore leisure for now)

Time working

Income

Consumption
Goods

Health care

Health Stock

Your health stock may affect your time available to work, and may also affect your utility of consumption goods.

Empirical work:

There is an endogeneity problem with income causing health
health causing income

A great deal of empirical work fails to account for this.
Relationship between health care and health stock introduces new complexity

Labor Leisure Choice from Labor Economics

$T_L = \text{illness days}$
$T_W = \text{work days}$

Assume for now that $T_L$ is already determined by health stock $H$
Wages rate per day is constant at $w$

$365 - T_L$ days left to allocate between work and leisure

Y income

Effects of improved health => $T_L$ decreases

$T^2_L < T^1_L$
Health is produced using time and health services

\[ H_t = f(H_{t-1}, T_{Ht}, M_t) \]

\( M_t \) = Health services this period

Health production function: *Ceteris Paribus*, \( H_{t-1} \) and \( M_t \)

Health

Time spent getting health care

\( T_{Mt} \) Time spent getting health care

Health production function: *Ceteris Paribus*, \( H_{t-1} \) and \( T_{Mt} \)

Health

Health care Services
Implications for Production Possibility Frontier for Goods

Health Care Goods

All Other Consumption Goods

Higher health stock => higher productivity => higher PPF

Diminishing returns to investments in health

For some purposes it is important to divide health goods into Health Consumption Goods and Health Investment Goods

Can you give some examples of each?