

A Note on the Distinction between Two Market Conditions in Japanese Health Care Market: Excess Demand vs SID *

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JEL classification: I11; L11; J44

Abstract

This article shows that the market condition can be distinguished by investigating the stability of physicians' regional distribution. Contrary to the conventional wisdom, instability of an equally distributed equilibrium means markets are not in supplier-induced demand (SID) but in excess demand.

A positive correlation between physician density and per capita utilization of medical services gave rise to the supplier-induced demand hypothesis, SID. The SID, which says physicians can create demand for their own interests, appeals to health care research because physicians are not only agents for determining the necessary care for their patients but also suppliers of medical services.

However, the positive correlation can also be explained as a result of excess demand. In contrast, SID occurs when a market is in excess supply. Two mutually exclusive hypotheses can explain the same phenomenon, but they differ in welfare implications. It is important to identify the market condition to adopt appropriate policies toward competition, cost containment and so forth. In spite of their importance, conclusions about market conditions are still controversial. There is great difficulty in distinguishing the market condition because two models with different market conditions have almost the same comparative statics results.

This article shows that the market condition can be distinguished by focusing on the stability of the regional distribution of physicians. If we only investigate suppliers' behavior in one market, it is hard to identify the underlying market condition. However, it can be distinguished by observing multiple markets at once. The market of interest in our study has fee-for-service payments with controlled prices, as in the Japanese health care system.

*The author would like to thank Ted Frech for helpful comments and UCSB for its hospitality. Financial supports from the Pfizer Health Research Foundation and KAKENHI (19530218) are gratefully acknowledged.