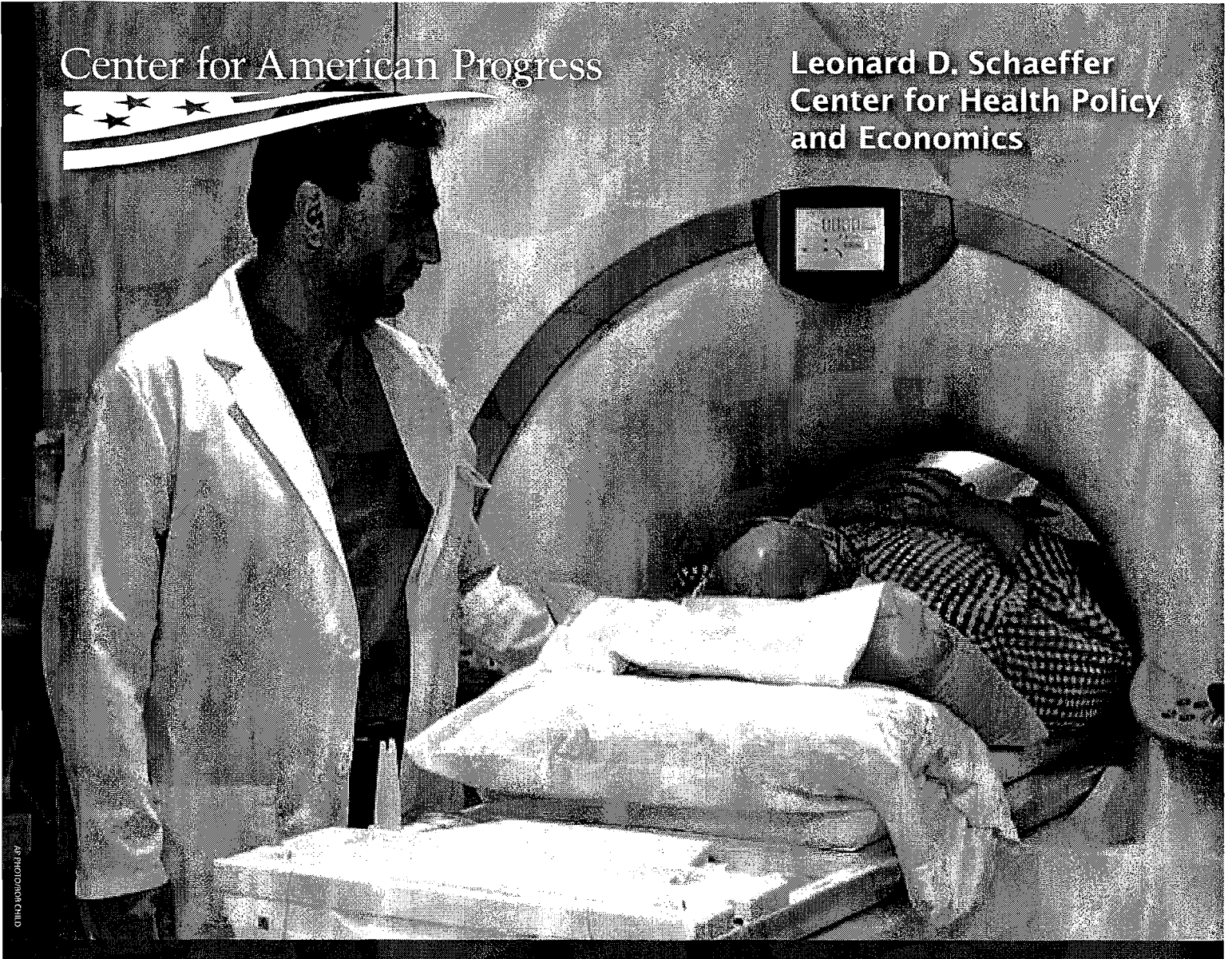


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New Jobs Through Better Health Care

Health Care Reform Could Boost Employment by 250,000 to 400,000 a Year this Decade

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Introduction and summary

One in ten Americans remains out of work today as the two-year-long Great Recession gives way at last to a slow economic recovery. Dealing with persistent unemployment is one of the top priorities of President Barack Obama and the leaders of Congress. One important way to create jobs is to slow the growth of medical spending. If health care cost increases slow down, then businesses will find it more profitable to expand employment, and workers will more readily move into those new jobs.

This paper will demonstrate the potential impact of health care reform on employment growth in the new decade, examining two recent studies and then combining their estimates of potential employment growth. The first study, by health economists Neeraj Sood at the Leonard D. Schaeffer Center for Health Policy and Economics and School of Pharmacy at the University of Southern California, and Arkadipta Ghosh and José Escarce at Mathematica and University of California Los Angeles, shows the significant negative impact of rising health care costs on employment as firms struggle with health costs that they cannot pass along fully to workers or consumers.¹ The second study, by health economists David Cutler of Harvard University and Karen Davis and Kristof Stremikis of the Commonwealth Fund, estimates that health care reform will slow the growth of health care costs and health insurance premiums.²

In the analysis that follows, we combine these two studies to show that health care reform could increase the number of jobs in the United States by about 250,000 to 400,000 per year over the coming decade.

The impact of health care costs on employment

Rising health care costs affect employment in two basic ways. On the employer side, employer-paid health premiums are a cost of business, just as wages and salaries are. Reducing the growth of health insurance premiums would therefore enable employers to hire more workers, according to economic theory, holding wages and other benefits constant. On the worker side, most workers are willing to give up wage and salary payments in order to receive employer-paid health insurance. When health insurance premiums rise, therefore, workers who value health insurance as part of the job are often willing to accept lower wages in exchange for the higher benefits.³ Conversely, when costs fall, a large part of the impact will be on higher wage and salary payments. A major effect of health care reform that lowers employer premium growth will therefore be to raise middle-class wages.

But the wage offset is not dollar-for-dollar for all workers. Firms have little ability to reduce wages for workers at or near the minimum wage or for workers with fixed employment contracts. Rising health insurance premiums will thus lead to more job losses among these types of workers while falling premiums will increase employment. Similarly, not all workers value employer-provided health insurance at its cost—either because their overall income is low or because they have health insurance from another source (perhaps a spouse). For these workers, the lower wages that rising health insurance premiums necessitate induce them to leave the labor force or move into part-time jobs (with no health benefits). Reducing the growth of health insurance premiums would allow employers with full-time positions to pay higher wages and allow such workers to return to jobs they would prefer.

A recent study, “Employer-Sponsored Insurance, Health Care Cost Growth, and the Economic Performance of U.S. Industries,” by University of Southern California economist Neeraj Sood and his colleagues Arkadipta Ghosh and Jose Escarce, estimates how the growth of health care costs that exceed the growth in gross domestic product—called “excess cost growth” in economic parlance—affects three important economic outcomes in U.S. industries:

- Employment.
- Gross output (the total value of sales in the industry).
- Value added to gross domestic product (sales net of factor inputs).

They analyze these relations using data from 38 industries over the 19-year period—1987-2005.

The study posited that the effect of excess cost growth on economic outcomes depends on the percentage of workers with employer-provided insurance. The growth in health insurance premiums should have a greater effect on employment in industries that have a larger percentage of workers with employer-provided insurance because the increase in labor costs is greater in those industries. The study looked at this by relating employment in the industry to the share of workers with employer-provided insurance and that share interacted with medical spending as a percentage of GDP. To control for other factors influencing employment, the study controlled for unionization, labor productivity, and sector-specific trends in employment.

The study by Sood and his colleagues demonstrated a clear negative relation between the share of workers with employer-provided health insurance and industry growth in the United States. Over the period 1987 to 2005, for example, the workforce in the amusement and recreation industry—where about 29 percent of workers have insurance through their jobs—grew by about 2.1 percent. In contrast, in the hotel industry—where 54 percent of workers have employer-provided insurance—the workforce grew about 1 percent. And in the paper industry—where about 85 percent of workers have insurance—the workforce shrank by 1.9 percent.

The results with the additional controls clearly show that excess growth in health insurance premiums has adverse effects on employment, output and value added to GDP, and that the effects are greater in industries where high percentages of workers have employer-provided insurance. The study by Sood and his colleagues finds that every 10 percent reduction in excess health care cost growth—a decrease in cost growth from 2.2 percentage points above GDP to 1.98 percentage points—leads to about 120,000 more jobs.

To further rule out the possibility that these economic effects reflected some industry-wide factor rather than the true effect of rising health insurance costs, the study compared U.S. industries with their Canadian counterparts. Since Canada has publicly-financed universal health care, employment growth trends in its industries are not influenced by health insurance costs. Conversely, industry-level changes such as product innovation or labor outsourcing would affect Canadian and U.S. employers in the same way.

In contrast to the results in the United States, there is no significant relationship between industries with more employer-provided health insurance in the United States and employment changes in Canadian industries. The lack of a relationship confirms the evidence that health care cost and premium increases have an adverse effect on employment growth.

When employment declines in one industry, some workers move out of the workforce entirely, while others take jobs in other industries where health insurance is less prevalent. The analysis in the first study combines both of these effects, but for the purposes of estimating overall job growth associated with health care reform we need to separate out

the two. Greater entry of workers into the labor force as a whole would affect total employment, while movement of workers from one industry to another would not (though it would have other benefits).

To estimate the labor force effect of changes in health care costs, we adjusted the estimates from the study done by Sood and his co-authors using results from displaced workers. The data from the Bureau of Labor Statistics' 2002 Displaced Worker Supplement of the Current Population Survey show that among displaced workers who cannot find employment in the same industry, about 26 percent leave the labor force and the remaining 74 percent obtain employment in other industries or are unemployed but actively seeking work.⁴ We thus multiplied the employment response to health care premiums by 26 percent to obtain the labor force impact of rising health care premiums. The results of this analysis will be combined with the results of the second study examined in the next section to calculate the potential effects of health care reform on employment.

The impact of health care reform on health insurance premiums

National health care reform now being considered in Congress will help modernize American health care and will affect employer-provided health insurance premiums in several ways. To gauge the consequences, we employ the estimates from David Cutler of Harvard University and Karen Davis and Kristof Stremikis of the Commonwealth Fund in the second study examined in this paper, “Health System Impacts of Health Reform Proposals.”⁵

An initial impact of reform is savings associated with lower administrative expenses in insurance, especially for small- and medium-sized firms. Administrative costs range from 5 percent for the largest firms to 30 percent or more for small firms. The higher costs for these businesses are associated with the marketing, underwriting, and brokers’ fees charged by health insurance companies. Creating health insurance exchanges is forecast to lead to significant reductions in these administrative expenses. Selective marketing and individual underwriting will not be permitted in exchanges, and brokers’ fees should decline with greater competition. Cutler and his co-authors estimate that insurance exchanges should lower average employer-paid premiums by about 2 percent.

The second impact of reform is to change the incentives in current payment systems, and thus encourage higher quality, lower cost care. Estimates show that large savings are possible in a number of areas of medicine, among them:

- Reducing the number and cost of high-cost illnesses through better coordination of care (for example, fewer people needing to be re-hospitalized after an initial hospitalization).
- Lowering unit prices of health care services that are more expensive in the United States than in other developed countries (for example, operating rooms and scanners that are run at less than full capacity).
- Streamlining excessive administrative costs that neither improve quality nor patient satisfaction.

Aspects of the health reform legislation now before Congress that would promote more efficient care include bundling payments for different health care providers to encourage practice of more coordinated care, increased use of pay-for-performance systems for providers rather than the pay-per-visit system used by most insurers, and greater funding

to support health care transitions, such as between hospitals and outpatient care, and for so-called medical homes, a primary care model that emphasizes coordinated care for the patient. These reforms would initially be implemented within the Medicare program, but are expected to extend to privately insured patients as reforms take hold, as has happened in the past.⁶

Cutler and his co-author estimate cost reductions from these initiatives of about 0.75 percentage points annually after a phase-in period, or 6 percent by 2019. Other work suggests savings as high as 1.5 percentage points annually are feasible.⁷ These cost reductions will enable employers who gain from these increased efficiencies to hire more workers and enable employees to seek higher wages as rising health care costs slow down.

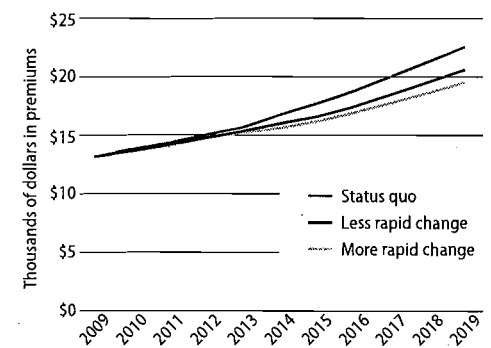
Other aspects of reform will affect premiums by influencing the generosity of benefits. Some small firms will pay more for insurance because the quality of the coverage they offer will increase. Most firms, however, offer relatively generous benefits and thus would not be greatly affected. The Congressional Budget Office estimates that health care reform will increase premiums at small firms by zero to 3 percent.⁸

The reform legislation also includes an excise tax on employer-sponsored health plans offering more generous benefits, so-called “Cadillac” plans. CBO estimates that this excise tax will reduce premiums for small and large employers by 9 percent to 12 percent. Overall, these changes in benefit generosity will reduce premiums for employers. In this report, however, we focus on the modernization aspects of the reform and do not include the employment effects of reform that stem from changes in benefit generosity.

Figure 1 shows the potential effects of reform on premium growth. We assume that health care reforms do not affect premiums until 2012 and that health insurance exchanges are created in 2013. In Figure 1 we consider two alternatives: one where health system modernization reduces premiums by 0.75 percentage points annually, and, alternatively, one where modernization reduces premiums by 1.5 percentage points annually. In the first scenario, premiums in 2019 are lower by 8.4 percent. In the second scenario, premiums are lower by 12.3 percent. If Congress fails to pass health care reform and the status quo remains, premiums would increase by 71 percent—or nearly \$10,000—by the end of 2019.

FIGURE 1
The consequences of health care reform on premium growth

Estimated change in employer-based health insurance premiums due to health care reform



Source: Based on the calculations in David Cutler, Karen Davis, and Kristof Stremikis, “Health System Impacts of Health Reform Proposals” (New York and Washington: The Commonwealth Fund and the Center for American Progress Action Fund, December 2009).

Impact of health care reform on number of jobs

The premium changes estimated by Cutler and his co-authors can be used to predict employment changes using the results in the first study by Sood and his colleagues. We focus on private sector wage and salary jobs in this analysis. We exclude public-sector jobs from the analysis as public employers' response to rising health care costs might differ from that of private employers.

Figure 2 shows the impact of slowing premium growth on employment in 2016 in different industries. We estimate more than 200,000 new jobs in manufacturing and nearly 900,000 jobs in services.

Two additional aspects of reform will affect employment. First, employment in the health care industry will be affected by the amount spent on medicine. Reductions in administrative expenses will reduce the need for clerical workers, and better health care delivery could shift workers from inpatient to more appropriate outpatient settings. We assume that the effect of health care spending on the need for health care workers is proportional to total dollars spent, that is, a 1 percent decline in health care costs or premiums results in a 1 percent decline in employment in the health care industry.⁹ The total change in health spending and premiums we model is from the second study by Cutler and his co-authors. They estimate that overall medical costs will decline by about 4 percent and premiums will decline by 8.4 percent in 2019.

In addition, some firms will be affected by the “pay-or-play” requirements for employers. These requirements mandate that firms with 50 or more employees that do not offer insurance coverage—and in the case of the Senate bill have people who

FIGURE 2
The consequences of declining health insurance premiums

Estimated impact of a 6 percent decline in U.S. health insurance premiums on employment by industry

Industry	Percent of workers with employer-sponsored insurance ¹	Change in employment, 2016 ²
Agriculture, mining, and construction		
Agriculture, forestry, fishing, and hunting	20%	6,026
Mining	68%	10,738
Construction	37%	76,339
Manufacturing	65%	202,109
Trade		
Wholesale trade	57%	87,750
Retail trade	39%	154,557
Transportation and communication		
Transportation and warehousing	55%	66,689
Utilities	80%	10,219
Services		
Information	63%	48,606
Financial activities	66%	141,480
Professional and business services	44%	231,262
Educational services	61%	55,808
Leisure and hospitality	25%	89,638
Other services	48%	304,537

¹ Author calculations based on 2008 Current Population Survey.

² Author calculations as outlined in the issue brief.

receive a subsidy in the exchange—pay fines ranging from \$750 to \$3,000 per worker. We estimate that these requirements will reduce the number of jobs by about 80,000.¹⁰ Yet most of this reduction in employment would be offset by an increase in spending associated with providing coverage to the 30 plus million currently uninsured Americans who would become insured by the legislation.

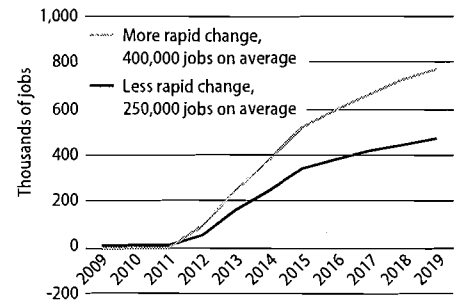
Figure 3 shows the forecast of total job creation under two scenarios—less rapid change versus more rapid change in insurance premiums. Relative to baseline employment forecasts from the Employment Projections Program at the U.S. Department of Labor, we estimate that moderate medical savings from health care modernization as envisioned under the legislation now before Congress would lead to an average of 250,000 additional jobs created annually. Under the larger assumption about savings due to health care reform, 400,000 new jobs a year would be created on average.

We show the employment increase continuing over a decade, although changes in the out years are more speculative. At some point, higher labor demand exhausts labor supply, and wages will adjust—even for low-wage workers and workers who do not value health insurance on the job. The point at which this will set in is not easy to predict, however.

FIGURE 3

Health care reform results in job creation

We estimate that reform will create between 250,000 and 400,000 jobs annually on average over the next decade.



Source: Authors' calculations based on results above.

Conclusion

We estimate that health care reform that reduces premium growth will add between 250,000 and 400,000 jobs annually over the next decade.

Our estimates of net job creation compare favorably with other estimates by other economists, which are generally based on less complete data. Katherine Baicker and Amitabh Chandra of Harvard University, for example, use data on malpractice premiums across areas to estimate the impact of rising health insurance premiums on employment.¹¹ They estimate that a 10 percent reduction in premiums would increase employment by 1.6 percentage points, very similar to the estimate by Neeraj Sood, Arkadipta Ghosh, and Jose Escarce that we highlight.

In earlier work by one of the authors of this report, Cutler, along with Brad DeLong of University of California, Berkeley and Ann Marie Marciarille of McGeorge School of Law, the authors estimate that cost savings of the type considered here would increase employment among low-wage workers by 90,000.¹² Additional employment effects for workers above the lowest wages would add to the total. Finally, President Obama's Council of Economic Advisors recently estimated that health care reform would create 320,000 additional jobs for some period of time.¹³ Thus, a number of studies with very different methodologies reach a similar conclusion about the labor market implications of major health care reform.

Clearly, health care reform that reduces premium growth is economic policy as well as health policy. The reform goals of a healthier America are well understood. In this paper, however, we demonstrate a less emphasized point about the health care reform legislation currently before Congress—if successful, its provisions can lower the costs of business and increase both the number of jobs by 250,000 to 400,000 annually over the next decade and increase wage growth.

Health care reform that includes even more robust measures to contain health care costs could further enhance job creation. In an economy that has lost 5 million jobs in the past year and where wages have stagnated for many years, this is a strong reason to pass health care reform that contains growth in health care costs and modernizes the U.S. health care system.

About the authors

David Cutler is Otto Eckstein Professor of Applied Economics at Harvard University and Senior Fellow at the Center for American Progress.

Neeraj Sood is Associate Professor at the Leonard D. Schaeffer Center for Health Policy and Economics and School of Pharmacy at the University of Southern California.

Acknowledgements

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Endnotes

- 1 Neeraj Sood, Arkadipita Ghosh, and José Escarce, "Employer-Sponsored Insurance, Health Care Cost Growth, and the Economic Performance of U.S. Industries," *Health Services Research*, 44(5) (October 2009): 1449-1464.
- 2 David Cutler, Karen Davis, and Kristof Stremikis, "Health System Impacts of Health Reform Proposals" (New York and Washington: The Commonwealth Fund and the Center for American Progress Action Fund, December 2009).
- 3 Lawrence Summers, "Some Simple Economics of Mandated Benefits," *American Economic Association Papers and Proceedings*, 79(2) (May 1989): 177-183; Jonathan Gruber, "The Incidence of Mandated Maternity Benefits," *American Economic Review*, 84(3) (June 1994): 622-641.
- 4 Ryan Helwig, "Worker Displacement in 1999-2000," *Monthly Labor Review* (June 2004): 54 - 68.
- 5 In addition to the factors we discuss, other aspects of reform will influence government or out-of-pocket spending. We do not consider these factors.
- 6 Two cases in point: Prospective Payment for hospitals, which was implemented in Medicare in the early 1980s and adopted by the private sector in subsequent years, and the Resource Based Relative Value Scale for physicians, which followed the same path a decade later.
- 7 Melinda Beeuwkes-Buntin and David Cutler, "The Two Trillion Dollar Solution: Saving Money by Modernizing the Health Care System" (Washington: Center for American Progress, June 2009).
- 8 Letter to the Honorable Evan Bayh, Congressional Budget Office, November 30, 2009.
- 9 Empirically, this overstates the degree to which employment in health care tracks spending growth. Between 1999 and 2008, for example, medical spending increased by 88 percent but employment increased by only 27 percent.
- 10 Health care reform might impose a fee of \$750 to \$3000 per employee for firms that do not offer insurance coverage. We estimate that such fee might increase labor costs by up to 8 percent. Based on estimates of labor demand elasticity from prior studies we estimate that this will reduce employment among workers in affected firms by about 3.6 percent. Health Data from the 2008 Medical Expenditure Panel Survey show that 97.4 percent of employees in firms with 50 or more workers have employer sponsored insurance and these firms represent 73 percent of the workforce. This implies that about 1.9 percent or about 2.4 million workers work in firms with 50 or more employees that do not offer insurance. Given that about 2.4 million workers will be affected, a 3.6 percent reduction in jobs translates to about 80,000 jobs.
- 11 Katherine Baicker and Amitabh Chandra, "The Labor Market Effects of Rising Health Insurance Premiums," *Journal of Labor Economics*, 24(3) (July 2006): 609-634.
- 12 David Cutler, Brad DeLong, and Ann Marie Marciarille, "Why Obama's Health Plan is Better," *Wall Street Journal*, September 16, 2008, p. A25.
- 13 Executive Office of the President, "The Economic Case for Health Care Reform" (Council of Economic Advisers June 2009); Executive Office of the President, "The Economic Case for Health Care Reform: Update" (Council of Economic Advisers, December 2009).

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 2. Improving insurance design.
 3. Understanding how public policy affects medical innovation.
 4. Identifying the macroeconomic consequences of U.S. health care costs.
 5. Improving comparative effectiveness and outcomes research.
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Center for American Progress
1333 H Street, NW, 10th Floor
Washington, DC 20005
Tel: 202.682.1611 • Fax: 202.682.1867
www.americanprogress.org

Leonard D. Schaeffer Center for Health Policy and Economics

The Schaeffer Center
Anna Cearley, USC Media Relations
cearley@usc.edu
Tel: 213.740.7895
<http://healthpolicy.usc.edu>