Health Expenditures, Longevity and Growth

by

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Executive summary

Since human capital is the main driver of productivity and growth in knowledge-based economies, health should also matter for economic outcomes. In the context of rapid population ageing, the contribution of health for human capital and hence for growth potential could therefore be expected to become increasingly important. This paper tackles this issue by offering an integrated view of the relationships between, health spending, medical innovation and adoption, health status, growth and welfare. The starting observation is that longevity has increased steadily in developed countries. Providing labour market and pension reforms offer the right environment, we show that these longevity gains could be used to smooth the negative effects of baby-boom bust on labour force, notably in Europe. A key condition, however, is the existence of a virtuous cycle between longevity and health status ("healthy ageing"). Despite the uncertainties on whether healthy ageing could continue in the future, improved health status can be (and has been) achieved to a significant extent through improved health care. But health care is costly and developed societies are spending an increasing share of their income in health services and products, with already strained public budgets paying most of the bill. This rising expenditure trend has little relation to demography, but it is rather driven by consumers' preferences for longer lives and the diffusion of technological progress. We provide empirical evidence that health expenditures tend to grow in line with incomes (unitary elasticity) and, on the top of this income effect, it is the change in medical practices

[*] The views expressed are those of the authors and do not reflect those of the OECD, the WHO or its Member countries.

that explains most of the drift of health expenditures per capita. The structure of health insurance, as well as the regulation of health care supply might also encourage some costly innovations with a small benefit in terms of social welfare. Given the various determinants of health expenditures, we carried out several projection exercises leading to the conclusion that the expected increase in the resources directed to health care by 2050 is substantial (ranging from 4 percentage points in a conservative scenario to above 12 percentage points of GDP). The question then arises what could be the likely impact of these developments on economic growth, and what could be the impact, if longevity was "better managed"? In particular, would there be a role for investing in health to act as a driver of the European catching up with the US in terms of GDP per capita? Despite convincing theoretical arguments, there is weak empirical evidence showing that health and health spending play a significant positive role in economic growth in rich countries. Probably, the positive impact of improved health on the economy has been hindered by a fixed and too low retirement age. Once institutional incentives for early retirement are lifted and the effective retirement age increases, through labour market participation of the elderly, the health status could have a more important role on growth. Given the role of preferences and the demographic transition, the global market for health services and products is huge. Satisfying this demand offers a potential for growth, but the EU is lagging behind the US in terms of health-related R&D and innovation. This is partly due to differences in regulation and market structure, which would require appropriate product market reforms. Health policies are connected and are often complementary with other areas (e.g. public budgets, labour market, pensions, etc.), so reforms need to be broad-based.