

# Health Inequality: Role of Insurance and Technological Progress

Siddhartha Sanghi <sup>\*†</sup>

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## Abstract

The paper investigates the role of insurance and technological progress on the rising health inequality across income groups. Using large scale federal survey datasets, I document new findings which suggest the role of timing of health investments as a key channel behind increased health disparities. I then develop a dynamic stochastic life-cycle model of an economy where individuals choose insurance, timing of investment into their health capital, consumption, and savings. My estimates show that while rich and poor have comparable health investments, there are substantial differences in their timing. The estimated model is able to explain about half of the gap in life-expectancy across income/wealth groups. I show that technological innovation and insurance interacts with the timing of investments and have a first order effect on disparities. While a non-uniform increase in the productivity of the medical sector – one where there are improvements in treating early stages of cancer for example, but none for stage 4 – can lead to increase in inequality in life-expectancy, a uniform increase in the productivity leads to a reduction. Focusing on the role of insurance, I find that while Medicaid alleviates health inequality, private insurance exacerbates it by almost twice as much. Finally, I find that a policy of “Medicare-for-all” not only reduces health inequality, it could also lower existing income inequality.

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<sup>\*</sup>First Version: February 15, 2019. The views expressed herein are solely those of the authors and do not necessarily reflect those of the FRB StL, the Federal Reserve System or the U.S. Census Bureau. All results have been reviewed to ensure that no confidential information is disclosed. The statistical summaries reported in this document have been cleared by the Census Bureau’s Disclosure Review Board release authorization number CBDRB-FY22-CES004-004. I am grateful to my dissertation advisors Rody Manuelli, Bart Hamilton, George-Levi Gayle, Paco Buera, Carlos Garriga and Yongs Shin for their help and guidance on the project. Special thanks to Jahn K Hakes of the Bureau and Ray Kuntz of AHRQ. I also thank Jérôme Adda, Job Boerma, Neha Bairoliya, Michael Darden, Mariacristina De Nardi, Elisa Giannone, Donna Gilleskie, Chad Jones, Ellen McGratten, Amanda Michaud, Kevin Murphy, Adriana Lleras-Muney, Stephen Ryan, Jon Skinner, Bob Topel, and various seminar participants for helpful comments.

<sup>†</sup>Research Division, Federal Reserve Bank of St. Louis. Email: [sid.sanghi@stls.frb.org](mailto:sid.sanghi@stls.frb.org)

# 1. Introduction

There is a huge disparity in health outcomes across income groups in the US. The richest 1% are expected to live for 12.3 more years than the poorest 1% (for e.g., [Chetty et al. \(2016\)](#)). The past few decades have seen a divergent trend in health inequality where the rich gained about two and a half years in their life expectancy while the poor only gained a couple months (for e.g., [Chetty et al. \(2016\)](#)). The huge inequality in health outcomes in the US and its worsening over time is quite puzzling, given that rich and poor have comparable total health investments<sup>1</sup> in any given year (for e.g., [Ales, Hosseini, and Jones \(2012\)](#) and [Skinner and Zhou \(2004\)](#)). Further, despite spending nearly a fifth of their GDP on healthcare (17.7 %), the US shows concerning trends when compared to other countries<sup>2</sup>.

Motivated by these puzzling observations, this paper seeks to answer the following three questions: (i) Why do health outcomes differ across rich and poor, despite having comparable healthcare spending? (ii) Why do technological innovations in the healthcare sector improve the outcomes of the rich but not those of the poor? (iii) What is the impact of private insurance and Medicaid on health inequality?

In order to answer these questions, I focus on one key mechanism: timing of health-care investments. First, I provide new empirical regularities, using a merged panel dataset of health, expenditure and mortality, complemented by large scale federal datasets on mortality, which show that, when the rich visit the doctor, they are at much better health than the poor when they visit the doctor. Second, I develop a dynamic stochastic life-cycle model with incomplete markets where I explicitly model that individuals choose the timing of health investments and insurance take-up. I use my estimated model – using the merged dataset – to quantify the role of timing on healthcare investments on health outcomes. I further evaluate the role of technological progress in the healthcare sector in exacerbating existing health inequalities and the value provided by different types of technological innovations: broad-based productivity improvements in the healthcare sector vs improvements in early treatments of a disease but not for terminal illnesses. Lastly, I quantify the role of Medicaid and private insurance in alleviating or exacerbating health inequality.

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<sup>1</sup>I use investments, expenditures and spending interchangeably throughout the paper.

<sup>2</sup>such as Canada, who having spent only 10.7 % of their GDP on healthcare, have seen a convergence in inequality (for e.g., [Baker et al. \(2021\)](#)) and have better health outcomes (life expectancy of 82 years vs 79 years in the US)

I start by documenting several new stylized facts on health spending and outcomes in the US. First, heart related technological improvements are the biggest contributors to the increased life-expectancy over the past few decades – poor and rich alike have gained about 4 years in their life-expectancy due to heart related innovations. On the other hand, cancer related reduction in mortality is one of the largest contributors to the *increased* disparity in health outcomes, where the rich have gained more than a year in their life-expectancy but the poor have only gained a couple months. Second<sup>3</sup>, about 60% of poor individuals (vs 22% rich) do not have any investments in any given year. Conditional on having positive medical spending, poor individuals' spending distribution has a thicker tail compared to rich, that is, they also have very high expenditures. I also find that while the poor spend more on hospitalizations and emergency rooms, the rich spend more on outpatient visits. Third, poor individual's visit and investment decisions are very responsive to their health status, i.e. they go to the doctor when their health is considerably worse and don't go for regular checkups when their health is good. This contrasts with rich individuals who go to the doctor more in all health states and have lower responsiveness to their health status in their visit decisions. Fourth, I find that, likely due to the timing of the visit, poor individuals are less likely to transition to a better health state even when they do go to the doctor.

The empirical findings suggest the potential role played by the timing of healthcare investments. Therefore, I develop a dynamic stochastic life-cycle model with incomplete markets where I explicitly model that individuals choose the timing of health investments and insurance take-up. Individuals enter the model at age 25, with heterogeneity in their education, wealth and health. The key model ingredients are: i) Individuals face health shocks that can arrive continually. Flow utility of consumption, productivity in the labor market, disability rate and death rate is affected by how healthy they are. ii) Individuals can invest in the likelihood of transitioning to a better health state. Health production function features dynamic complementarities: if one invests in their health when it is very low, their health is less likely to improve substantially compared to those who invest when it is not very low. iii) They face a fixed cost, such as doctor co-pay or search and travel costs, associated with health investments, leading to a stopping time component where individuals decide on the timing of doctor visits. Individuals differ across many dimensions: their income (affected by education, potential experience in the labor market and health), health state, wealth, age, the intensity to go to a better

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<sup>3</sup>The second fact has been documented in the literature such as [Ozkan \(2014\)](#).)

health (affected by their previous investments), insurance status (based on their previous choices) and disability status. iv) Individuals can change their insurance once annually, in expectation, and choose between paying a fixed cost associated with Medicaid, if they are eligible, or pay the monthly premium associated with private insurance. This leads to a selection into Medicaid and private insurance where only the unhealthy or the wealthy take up private insurance. v) Markets are incomplete and individuals face borrowing constraints. This means that individuals cannot borrow against their future income or future health investments funded by public provisions (such as Medicaid and Medicare).

I use a rich panel dataset on health, spending and outcomes<sup>4</sup> along with large scale federal datasets on mortality<sup>5</sup> to estimate the model using Simulated Methods of Moments. In particular, I target choices such as doctor visits, healthcare investment, and insurance take-up; evolution such as change in health with and without visit, death rate, health over the life-cycle, average investment ratio between rich and poor of the same health, and disability rates to identify health transition, mortality and disability shocks, utility gains from health, health production function and fixed costs associated with doctor visits and Medicaid take-up.

The key findings from the estimated model, which are consistent with the data, are as follows: First, while the total health spending across income groups is similar, the timing of the spending is very different for the rich and poor. Lower wealth individuals' visit decisions are more responsive to their health state – particularly in bad health. Second, fixing health, the wealthy spend more on their health over the next year, thus transitioning to better health with a higher probability. Third, health inequality starts off low at the beginning of working-life and increases substantially by the age of 45. Fourth, when a poor uninsured individual defers getting treatment until their health deteriorates significantly, they are not able to improve their health even by spending the same amount of money, i.e. they don't get the bang for the buck. This is because of the effective complementarities in health production where investing early is better than investing later. An example to provide intuition for this: \$1,000 on doctor visit, MRI and a small surgery is likely to have better outcomes than \$5,000 in chemotherapy.

The effect of difference in timing of health investment on spending and health outcomes can be illustrated through an example of an uninsured individual in average

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<sup>4</sup>Merged National Health Interview Survey (NHIS) and Medical Expenditure Panel Survey (MEPS)

<sup>5</sup>National Longitudinal Mortality Survey (NLMS) and Mortality Differentials in American Communities (MDAC) Survey

health with low wealth and income. They face financial constraints and cannot borrow against their future income. Hit by a health shock, they face two possible scenarios: i) They wait to accumulate savings before going to the doctor, as a result of the steep out-of-pocket cost (without insurance) ii) They wait and take-up Medicaid (if eligible) or private insurance before going to the doctor. As a result of the delay their health might deteriorate further. Given the complementarities in health production, where \$1 in average health is better than \$1 in worse health, the investment at a lower health state is less likely to result in a transition to good health. It may also result in a transition into long-term-disability at a younger age after which Medicare starts paying for them. It is also important to point out that this also feeds into the income and wealth accumulation: poor health makes their labor income go down<sup>6</sup>, making wealth accumulation slower. On the other hand, a rich insured individual in average health – when faced with a health shock – would visit the doctor without any delay, invest in their health and transition to a better health state. This would result in comparable health investments but significant differences in health outcomes.

In order to understand the role of insurance, I perform three counterfactual experiments: first, shut down only Medicaid; second, shut down both Medicaid and private insurance; and third, implement a “Medicare-for-all” financed by a flat income tax. My findings are that: i) Medicaid alleviates the health inequality, and without it, the gap in life-expectancy across bottom and top quartiles would go up by about 10%. ii) Private insurance exacerbates inequality by almost twice as much. This is due to the fact that private insurance overwhelmingly is taken up by the relatively wealthy – who face a lower “effective price” of goods and consume more. iii) Medicare-for-all, with fixed costs and co-pays, can reduce the gap in life-expectancy across bottom and top quartiles by about 20%. Medicare-for-all illustrates a key tradeoff in the policy making: while the inequality in health outcomes would go down, it has to be financed by income taxes.

In order to understand the role of technological innovation on health outcomes, I consider two types of innovations. First, uniform broad-based TFP improvements in the healthcare sector and second, a non-uniform productivity increase in early treatments but not in terminal illnesses. I find that the type of technological progress and its interaction with the visit decision is one of the key determinants of increased health disparities. A uniform broad-based increase in productivity of the healthcare sector lowers

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<sup>6</sup>My model only models labor income but one can think that this comes from two channels: either due to fewer hours worked or lower wage. See for example [Hosseini et al. \(2021b\)](#)

health inequality while a non-uniform increase – one where there are improvements in early care but not in late treatments – increases the disparity. An example to build intuition for this result: suppose that two decades ago, medical technology was such that only stage 1 cancer could be treated. Now suppose that due to technological progress in cancer treatments, the medical technology today is such that cancer until stage 2 can be treated. While the rich, frequently going to see the doctor, visit the doctor and invest in their health at stage 1, the poor, having deferred the treatment, only go for their visit and health investment when the cancer is in stage 3<sup>7</sup>. Thus, the poor not only end up spending the same amount as a rich person in any given year, they are also not able to reap the benefits of the medical technological progress that we have witnessed<sup>8</sup>.

I use my model to quantify the dollar value of the two types of innovations in the healthcare sector discussed above. My findings can be summarized as follows. First, I find that society puts a large dollar value on medical innovations, ranging from \$69,000 to \$92,000 per individual (1.5-2 times average income per capita). Second, the value of innovation depends on whether it is uniform broad-based or limited to certain types. The value of a uniform broad 20% improvement in the healthcare sector that results in about a year of gains in average life-expectancy is \$92,000 per individual (2 times average income per capita in the model) compared to \$69,000 per individual (1.5 times average income per capita) from non-uniform 20% improvements that results in about 5 months of gains in average life-expectancy.

Lastly, I use my model to quantify the role played by health in exacerbating the existing income inequality. I find that private insurance exacerbates the existing income inequality by about 5% whereas Medicare-for-all reduces the income inequality by 9%.

**Related Literature** The paper belongs in the strand of literature modeling health as health capital dating back to [Grossman \(1972\)](#). It brings timing of health investments such as [Gilleskie \(1998\)](#), into life-cycle models with endogenous health and wealth accumulation. It endogenizes health evolution, largely assumed exogenous in the literature, such as [Hosseini et al. \(2021a\)](#), [Attanasio et al. \(2011\)](#), [Palumbo \(1999\)](#), [Michaud and](#)

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<sup>7</sup>See, for example, [Walker et al. \(2014\)](#) and [Niu et al. \(2013\)](#) which use Surveillance, Epidemiology, and End Results (SEER) registry data to document the differences in diagnosis stage of cancer across insurance groups providing the basis for our example here.

<sup>8</sup>It is consistent with the fact that the type of cancer for which the survival rates have converged the most for the affluent and less affluent over the past 2 decades is Hodgkin Lymphoma [Cancer Research UK, Accessed April 2021](#) for which the survival rate is relatively flat across cancer stages [Cancer Research UK](#) while the cancer for which the survival rates have diverged the most is oesophageal cancer, which has a steep one-year mortality rate across cancer stages Source: UK Cancer [Cancer Research UK Accessed: April 2021](#)

Wiczer (2018), Poterba et al. (2017), De Nardi et al. (2017), Nakajima et al. (2018), Conesa et al. (2018), Nakajima and Tuzemen (2016) and builds onto recent work with endogenous health such as De Nardi et al. (2010), Cole et al. (2016), Ozkan (2014), Scholz and Seshadri (2011), Hai and Heckman (2015) and Halliday et al. (2019).

The closest work to this is Ozkan (2014) and Hong, Pijoan-Mas, and Rios-Rull (2015). The key innovation with respect to these papers is that I explicitly model the timing of the healthcare investments, which is crucial in understanding the empirical facts I document. Further, both papers do not focus on increased health disparities over time.

This work complements the literature focusing on other aspects such as smoking (for example, Darden (2017), Adda and Cornaglia (2006), Hai and Heckman (2015), Chen et al. (2017)) or race (such as Schwandt et al. (2021)). Other forms of health investments such as type of food, time spent exercising, smoking (or lack thereof), are things not explicitly modeled in this paper. Recent literature (such as Schwandt et al. (2021)) point out the *convergence* in inequality across race, consistent with my findings across race<sup>9</sup>.

With a few exceptions, existing literature hasn't focused on the causes of increased health disparities over time. Glied and Lleras-Muney (2008) look at the role of education in increased health disparities over time. I complement their work by showing that even for individuals college and above, there is divergence in life-expectancy by family income quartiles over the last few decades, suggesting that education may not be enough to explain increased health disparities across these groups. However, their work doesn't analyze healthcare spending or its comparability across rich and poor. To the best of my knowledge, this is the first paper to look at the flatness in spending, cross sectional differences in outcomes *and* increased health disparities over time.

On the methodological side, this paper adds to the literature bringing continuous time tools in questions relating to health such as Agarwal et al. (2019) and more broadly, in questions relating to inequality such as Achdou et al. (2017).

It also contributes to the empirical literature documenting changes in life-expectancy over time, such as Cutler et al. (2006), McGinnis and Foege (1993), Becker et al. (2005), Chetty et al. (2016), Case and Deaton (2015), most recent one being, Schwandt et al. (2021). To the best of my knowledge, this is the first paper to document the change in life-expectancy over the past few decades by cause-of-death across income groups, à la Becker et al. (2005).

It also contributes to the literature on value of health and/ or healthcare innovations,

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<sup>9</sup>see A.10.



such as [Murphy and Topel \(2006\)](#), [Jones and Klenow \(2016\)](#), [Hamilton et al. \(2018\)](#), [Hall and Jones \(2007\)](#) [Chandra and Skinner \(2012\)](#), [Acemoglu and Finkelstein \(2008\)](#).

The paper also relates to the literature on health reforms and outcomes including [Miller et al. \(2021\)](#), [Finkelstein et al. \(2012\)](#), [Baicker et al. \(2013\)](#), [Sommers et al. \(2017\)](#), [Wilper et al. \(2009\)](#), [Sommers et al. \(2012\)](#), [Kolstad and Kowalski \(2012\)](#), [Ho \(2006\)](#), [Finkelstein et al. \(2018\)](#). The estimates also relates to the literature estimating marginal utility of consumption in presence of health such as, [Finkelstein et al. \(2013\)](#). The paper also contributes to the literature on health insurance such as [Handel and Kolstad \(2015\)](#), [Handel \(2013\)](#), [Einav et al. \(2013\)](#).

Lastly, it also contributes to the work quantifying role of health on income and welfare, such as [Hosseini et al. \(2021b\)](#), [Prados et al. \(2012\)](#), [Miller and Bairoliya \(2017\)](#), [De Nardi et al. \(2017\)](#), although in their setting health is assumed exogenous. I find that by endogenously investing in their health, individuals are able to partly offset the consequences of bad health shocks.

The remaining of the paper is divided as follows: section 2 provides the “new” facts. Section 3 describes the model, section 4, 5 and 6 present estimation strategy, results and policy experiments, respectively and section 7 concludes.

## 2. Data

The merged National Health Interview Survey (NHIS) and Medical Expenditure Panel Survey (MEPS) dataset, as detailed in Appendix section A.9, is a rotating panel of nationally representative dataset of health, income and wealth from 2000 to 2014. It consists of measures of health (including diagnostic and procedure codes), individual and family income, wealth, insurance, health expenditures by type of visit and source of payment for 5 interview waves over 2 years along with detailed mortality status and cause of death until 2015. I augment this data with large-scale federal survey datasets National Longitudinal Mortality Survey (NLMS) and Mortality Differentials in American Communities (MDAC) Survey including cross-sectional information merged with mortality status of over 9 Million individuals to decompose the long-term changes in life-expectancy.

Due to absence of life-cycle panels of individuals, I use family income or wealth adjusted for family size as a proxy for permanent income. Quartiles are determined by family income or wealth distribution for age decade (25-35, 35-45, and so on). Amongst these two measures, family income is consistently available across all datasets relative



to wealth and therefore, this is the measure I primarily use for analysis. I conduct robustness checks with wealth. If family income or wealth is not observed for some datasets (such as NLMS-MDAC), I use poverty percent which adjusts for family size <sup>10</sup>. Note that in order to account for the life-cycle pattern in income and wealth, the quartile cut-offs are based on age decade (25-35, 35-45, and so on). Unless otherwise stated, the bottom quartile will be referred to as poor and top quartile as rich.

## 2.1 Health outcomes and health spending: a puzzle

### Poor and rich have comparable total medical spending, but very different outcomes

The leading cause of death across the income distribution were cancer and heart conditions based on one-year crude mortality from MDAC. As shown in Figure 1, I see that across all age groups and cause of death, individuals in fourth quartile of family income distribution<sup>11</sup> have a lower aggregate and cause-specific mortality-rate compared to individuals in first quartile of family income distribution. This pattern has been well documented in the literature including Chetty et al. (2016). For those in 52-65 age group, the mortality-rate of top quartile of income is less than half of the mortality-rate of the bottom quartile of income.

As documented by Ales et al. (2012), the mean total medical spending including the portion covered by private insurance, Medicaid, Medicare, and out-of-pocket looks comparable across family income distribution. For instance, for ages 35-45, individuals in bottom quartile of the family income distribution spent a little more than \$3,500 annually while those in top quartile of the distribution spend about \$ 3,100 annually as shown in figure 2. Similar pattern holds for other age groups, as shown in Appendix. A detailed discussion on charge and expenditures is provided in appendix section A.9. Breaking down the spending by source of payment reveals that very low fraction of poor individual's total medical spending comes from private insurance.

A natural question that arises from looking at the two facts documented in the literature is: why is it that while the rich and poor end up spending roughly the same amount in absolute dollars on their medical spending annually, the outcomes are so drastically different? Moreover, why is it getting worse over time?

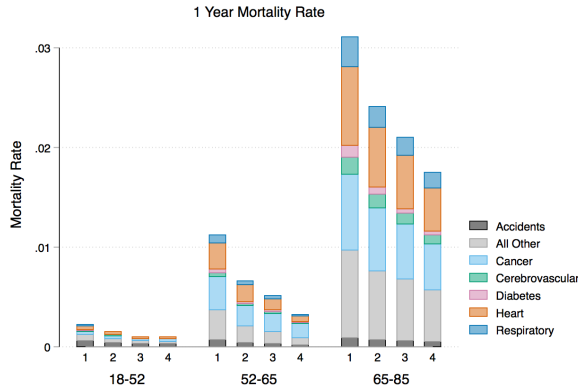
In order to understand the sources, I will now dig deeper into the data. To the best

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<sup>10</sup>Details on poverty variable here: <https://usa.ipums.org/usa-action/variables/POVERTY>

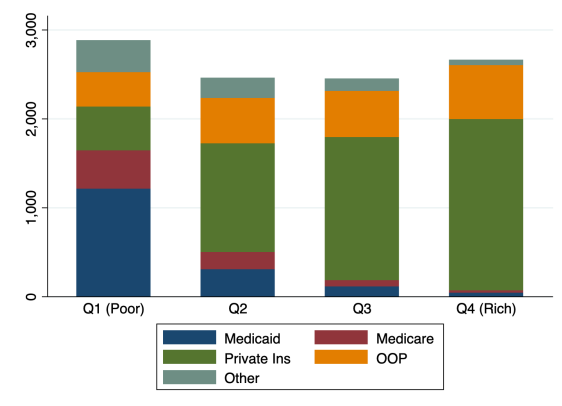
<sup>11</sup>The patterns are very similar when I define the quartiles based on wealth.

Figure 1: 1-Year Mortality Rate by Age and Inc



Source: MDAC

Figure 2: Medical Investment Age 35-45



Source: NHIS-MEPS

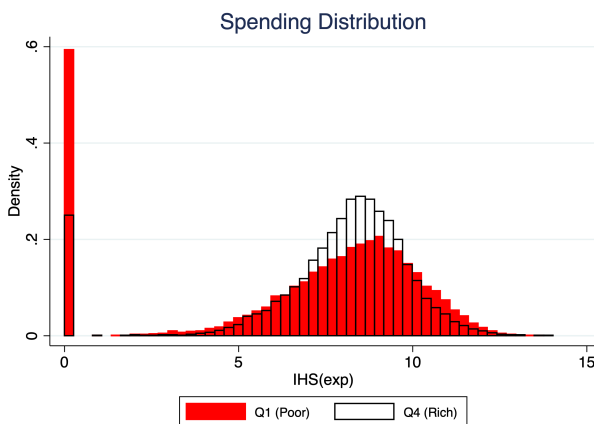
of my knowledge, the empirical facts 2-4 in the next section are relatively unexplored in the literature.

## 2.2 Facts

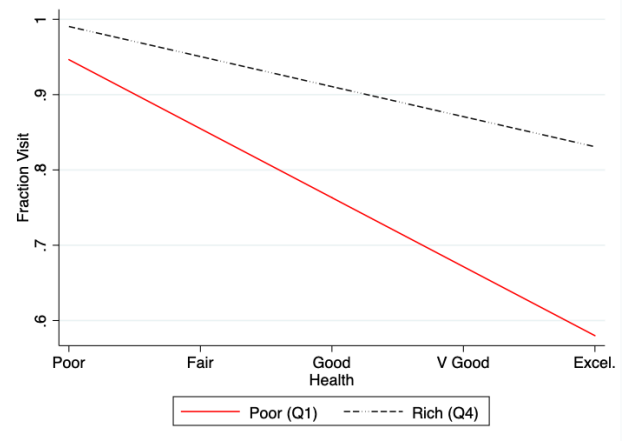
### Fact 1. Poor spend more on Hospitalizations and Emergency Rooms while rich spend more on Outpatient visits

In figure 3, I document the inverse hyperbolic sine (IHS) transformation of the distribution of medical expenditures for 1st and 4th quartile based on family income. I observe that while larger fraction of poor have zero medical spending, they also have thicker tails in expenditure distribution, which suggests that while they are less likely to go for a doctoral visit in any given year, if they do, they end up spending more than the rich who are going for doctoral visits. Those in bottom quartile of the distribution spend significantly more on hospitalizations and emergency room while those in top quartile of the distribution spend more on office based and outpatient visits, as detailed in the appendix A.10. These findings are consistent with the literature (for e.g. Ozkan (2014)). The next three findings are relatively unexplored in the literature.

Figure 3: (IHS) Medical Expenditure Age 45-55 Figure 4: Timing of Investment by Health State



Source: NHIS-MEPS



Source: NHIS-MEPS

## Fact 2. Rich individuals go to the doctor in a much healthier state

In figure 4, I document fraction who visit the doctor by health and wealth. I find that rich individuals visit the doctor more in all health states. The fraction of rich who visit the doctor ranges from close to 1 for poor health individuals to 0.83 for those in excellent health. On the other hand, poor individuals visit decision is very responsive to their health status: it goes from 0.95 in poor health to less than 0.6 for excellent health. These results suggest that compared to the rich, poor individuals wait until their health deteriorates to a much worse health state before they go to the doctor and get the treatment.

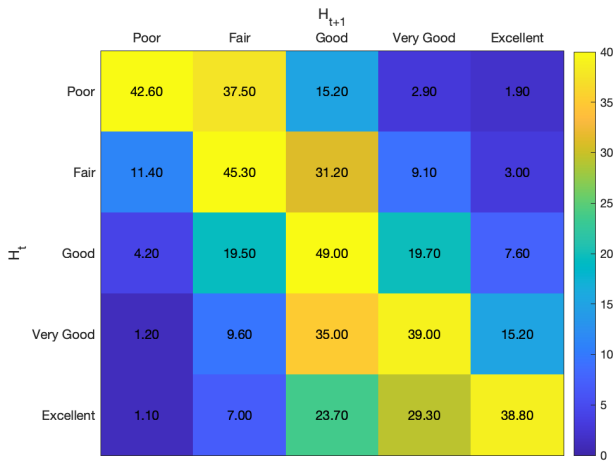
In addition, I also do a fixed effect regression<sup>12</sup> where the variation comes from the panel component where I observe an individual and its doctoral visit decision on their health status. The findings are similar and I present them in appendix A.10.

## Fact 3. Going to the doctor improves rich individuals' health more than that of poor

In Figure 5 and 6, I compare the annual transitions in health for individuals in the first quartile and fourth quartile of family income distribution conditional on medical visit for ages 35-45 years. For those in poor health in time  $t$ , 42.6% of poor remain in poor health while compared to 35.8% for rich. Similarly, more than 56% of poor in fair health

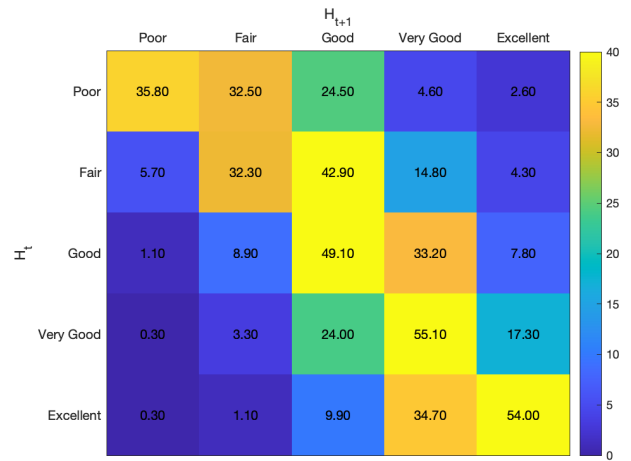
<sup>12</sup>For this analysis, I do not need the self-report status to be comparable across income groups since the coefficients are identified off of the *change* in health status

Figure 5: Transition matrix | visit: Poor aged 35-45



Source: NHIS-MEPS

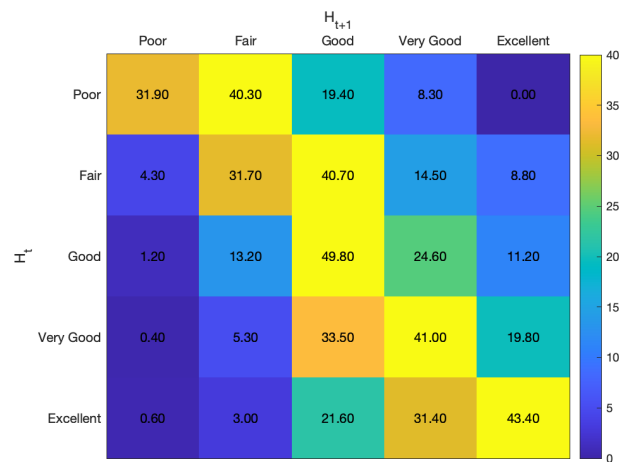
Figure 6: Transition matrix | visit: Rich aged 35-45



Source: NHIS-MEPS

Notes: Raw transition matrix from  $H_t$  to  $H_{t+1}$  on annual data

Figure 7: Transition matrix | no visit: Poor aged 35-45



Source: NHIS-MEPS

remain in poor or fair health compared to 37% for the rich. The pattern is similar across age groups, as shown in the appendix.

This is also a good place to emphasize the need to model the visit decision – if I compare the transition matrix of those who didn't go to the doctor for the poor, as shown in figure 7 with those who did in 5, I see that those who didn't go to the doctor transitioned to a better health with a higher probability. Simply put, those whose health got better were also the ones who didn't demand any healthcare, i.e. didn't need to go to the doctor. Thus, modeling visit decision is crucial to understand health outcomes.

#### **Fact 4. Cancer related innovation is a major contributor in increased health disparities**

I find that, conditional on surviving until age 20, there is a gap of about 8.5 years in life-expectancy, for the top and bottom quartile of the family income distribution. From 1983 to 2015, those in bottom quartile have gained about 2 years and 11 months, those in top quartile have gained 5 years and 5 months. This aggregate pattern of increasing life-expectancy gap is also consistent with others that have looked at the aggregate life-expectancy such as [Chetty et al. \(2016\)](#).

In order to understand the underlying components of the changes in life-expectancy, I do a decomposition by age and cause specific mortality across four family income groups adjusted for family size<sup>13</sup>, à la [Becker et al. \(2005\)](#). In appendix , I describe the exercise along with providing robustness across different thresholds, samples and an analysis by race, where we have witnessed convergence in life-expectancy.

While the improvements in heart related causes have contributed the highest gains in life-expectancy, their distributional impact have been limited. As shown in Table 1, while poor have gained 4.1 years in life-expectancy due to heart related causes, rich have gained 4.3 years in life-expectancy. It is malignant neoplasms (cancer) that have contributed significantly to the rising health inequality across rich and poor over the two decades from 1983 to 2015. An age-based decomposition of life-expectancy gains tells us that while most gains have been for ages 50-80, gains above 80 years have also contributed to the rise in health inequality across income groups<sup>14</sup>.

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<sup>13</sup>I define the groups using age adjusted poverty percent variable which adjusts for family size

<sup>14</sup>Note that drug-overuse (for e.g., [Case and Deaton \(2015\)](#)) is attributed in accidents. For aggregate trends on cause of deaths, see [CDC Report](#). Category others include Alzheimer's and other forms of dementia, whose occurrence has gone up in the recent decades.

Table 1: Gains in Life-expectancy: 1980s to 2010s

	Q1 (Poor)	Q2	Q3	Q4 (Rich)
Life-expectancy 1980s	68.9	72.5	75.7	77.4
Total Change (1980s - 2010s)	2.9	3.7	3.9	5.4
By cause of death:				
Heart	4.1	4.3	4.4	4.3
Cancer	0.3	0.5	0.7	1.1
Diabetes	-0.2	-0.1	0.0	0.0
Respiratory	-0.1	0.1	0.0	0.3
Cerebrovascular	0.7	0.6	0.6	0.8
Accidents	0.0	0.0	0.0	0.1
Alzheimer's	-0.3	-0.3	-0.4	-0.4
Suicide	-0.0	-0.0	-0.0	-0.0
Kidney Disease	-0.1	-0.1	-0.0	-0.0
All Other	-0.9	-0.9	-0.8	-0.6

Life-expectancy conditional on surviving until age 20.

1980s is computed by NLMS 6a wave 6 year average mortality rates; 2010s is computed by MDAC 2008 wave 6 year average mortality rates

The empirical findings suggest that the timing of healthcare investments might play a key role in the increased health disparities.

### 3. Model

I then develop a dynamic stochastic life-cycle model of an economy where individuals choose insurance, timing of investment into their health capital, consumption, and savings. The model brings continuous time methods, a popular tool used in macroeconomics and finance, into a problem involving individual's health related decisions<sup>15</sup>, and is set up based on our data availability.

<sup>15</sup>See for example, [Agarwal et al. \(2019\)](#) who use continuous time to model kidney exchanges

### 3.1 Setup

#### Timeline

Individuals enter the model at age 25 with initial wealth ( $w$ ), initial health ( $h$ ) and education. While wealth is continuous state variable, health is a discrete state from 1-5 with 1 being poor health and 5 being excellent health, as observed in data<sup>16</sup>. Individuals' transition from one health to another as governed by the Poisson intensities. They age when hit by age Poisson  $\eta$  and die when hit by death Poisson  $\lambda(h, a)$ . The stochastic evolution of health can be thought of as consisting five parts: a) deterioration governed by intensities  $d_h^a$  as a function of health,  $h$  and age,  $a$ , b) improvement governed by intensities  $v_h^a$ , c) sudden illnesses which could lead to long-term disability,  $\kappa_h^a$  or d) mortality governed by intensities  $\lambda_h^a$  and e) stochastic aging governed by intensity  $\eta$ <sup>17</sup>. Other than the standard consumption-saving decisions, individuals face two crucial decisions: whether or not to buy private insurance at a price based on their age or Medicaid if they are eligible and subsequently, given their insurance status and wealth, when to go for a medical visit and invest in their health.

Note that in the current version of the model, there is no information asymmetry. In particular, I assume that individuals observe their health capital with/without medical visit or in other words, health is common knowledge at all times. I leave the version in which health capital cannot be observed perfectly, for future research.

#### Evolution of health capital

An alternative way to think about the health evolution process is that it is a modified birth and death process adjusted to account for mortality, aging and endogenous Poisson intensities. The evolution of health capital follows a Poisson process with an exogenous depreciation, which is governed by  $d_h^a$ , and endogenous appreciation, which is governed by  $v_h^a$ .  $d_h^a$  is the intensity with which a person of age  $a$ , goes from state  $h$  to  $h - 1$ . Improving one's health is governed by intensity  $v_h^a$ , which is the intensity with which a person of age  $a$  goes from state  $h$  to  $h + 1$ . Individuals age at a rate  $\eta$  which is set to

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<sup>16</sup>An alternative is to use construct health indices such as [Poterba et al. \(2017\)](#) or [Hosseini et al. \(2021a\)](#). However, some of the questions literature use include questions about disease diagnosis (such as cancer and diabetes), which suffer from selection in the context of my model as they require doctoral visits. Therefore, I use the self-reported measure, which doesn't suffer from this bias.

<sup>17</sup>It is analogous to a continuous time life-cycle model with finite horizon. Stochastic aging helps us make the model stationary and reduce the computation burden, a standard practice.



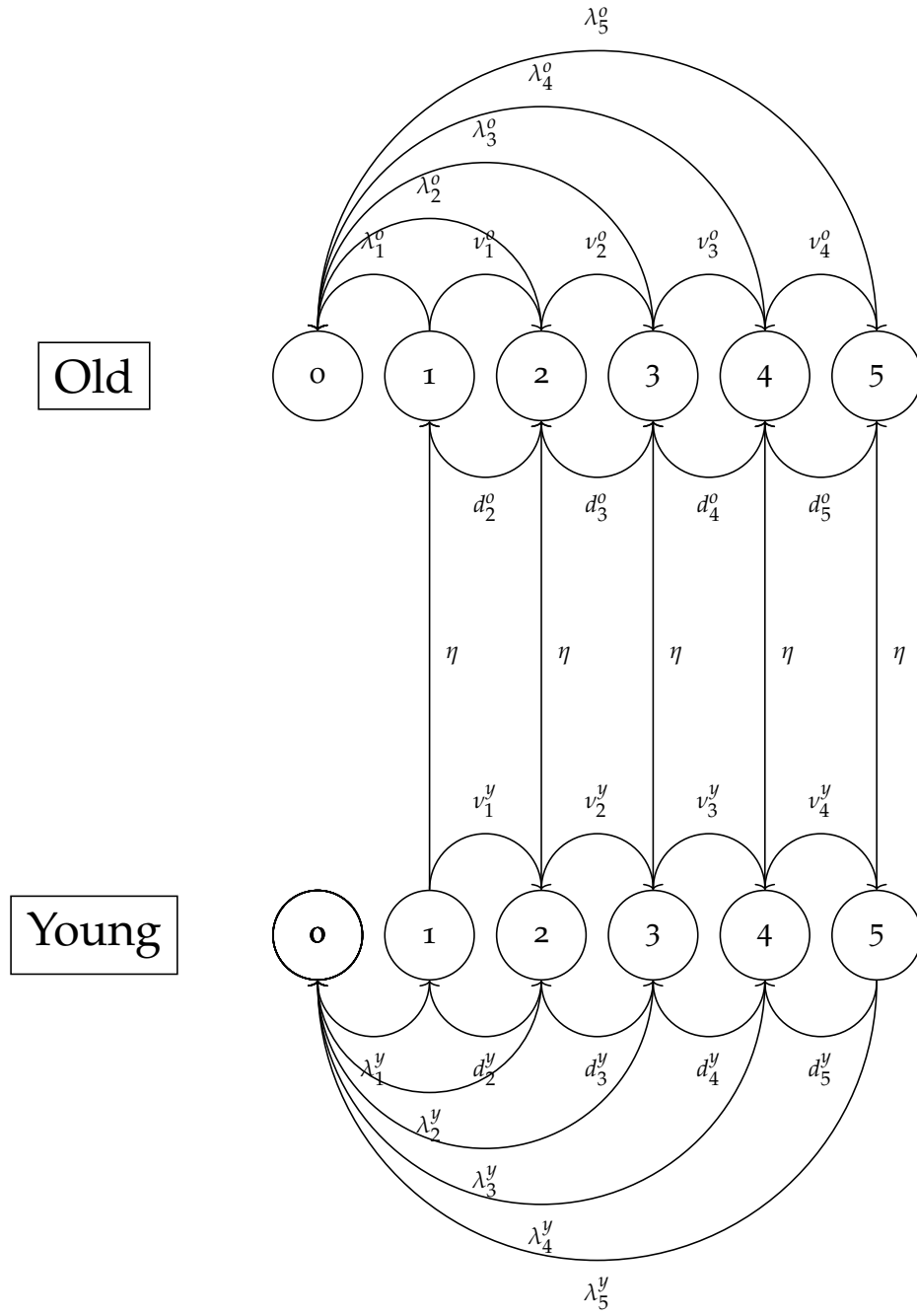


Figure 8: Illustrative health evolution with two ages

match the interval of 10 years in each age state., i.e. on average, a person stays in an age group for 10 years before aging and transitioning to the next age group. Note that upon aging, the health and wealth of the individual remains the same; as individuals age, the health depreciates at a higher intensity. Individuals in health state  $h$  and age  $a$  transition to an absorbing state of long-term disability with intensity  $\kappa_h^D$  or die and exit the model with intensity  $\lambda_h^a$ . All the intensities are allowed to vary by health,  $h$ , and age,  $a$  to allow for the fact that healthier individuals are more like to become disabled or die at a much lower rate compared to individuals in poor or bad health at the same age. Disability or long-term-disability is an absorbing state where individuals get a constant disability income and their healthcare expenses are paid for my Medicare.

To fix ideas, consider a setting with only two age groups young (y) and old (o) and no long-term-disability. Figure 8 illustrates the evolution process for two age groups - 'Young' and 'Old'. Consider a young individual born in good health state, i.e. in node 4 for the figure. He can transition to average health, i.e. node 3, with intensity  $d_4^y$ , transition to a better health state, i.e. node 5, intensity  $v_4^y$ , get hit by the aging Poisson with intensity  $\eta$  and transition to node 4 of state 'Old' or be hit by the mortality shock  $\lambda_4^y$  and exit the model.

The formulation is general enough to capture a potential increase in the depreciation of health as individuals age and a reduction in health improvement. Due to data limitations, I only allow for one step above or below in health transitions. Given that I only observe five snapshots for the two years the individual is observed in data, I do not know the exact time the individual stayed in a particular health state or the transition path of health followed. For example, I observe that an individual is in health state 4 in quarter 1 and health state 2 in quarter 2, I won't be able to see if he transitioned directly from 4 to 2 or he went from 4 to 2 via 3 or even 1 for that matter. Therefore, this is an identifying restriction that I need to impose to be able to pin down the Poisson intensities. Since I observe the exact duration of exit in our data, I allow exit from all health states. While the assumption for health transitions may sound restrictive, given that the model is in continuous time, probability of any transition in any interval is non-zero. Note that continuous time allows us to think about the evolution continually as opposed to discrete time where I typically have to put stronger restrictions on when the choices can be made.

## Health capital investment

At time  $t$ , individuals observe their health  $h_t$ , wealth  $w_t$  and the Poisson of going to a better health state  $\nu$ , their (endogenous) insurance status  $I_0$ . Individuals can invest in the likelihood of transitioning to a better health, i.e. invest in the Poisson intensity  $\nu$ . The evolution process of  $\nu$  is a function of two parts: i) an exogenous natural improvement rate  $\nu_0(a)$ , which depends on age  $a$ , to capture the feature of data that individuals transition to a better health state without doctoral visits; ii) an endogenous component  $Am^{\alpha_m}$ , which depends on  $m$  or the amount of medical spending optimally chosen by the individual to invest in their health capital, a technology with Total Factor Productivity  $A$  and a returns to scale parameter of  $\alpha_m$ . The evolution equation is as follows:

$$\nu' = \nu_0(a) + Am^{\alpha_m}$$

I assume that individuals choose medical spending but it is analogous to an altruistic physician who makes the plan of care decision for the person. Every time, an individual transitions to a better or lower health state,  $\nu$  resets to  $\nu_0$ . Absent this reset, investments in  $\nu$  would be completely persistent and individuals would simply invest once to get to a very high  $\nu$  and never invest again. This setup also captures the idea that there is some uncertainty associated with a doctoral visit. Since the individuals are investing in the probabilities or Poisson intensities, it is possible that they spend a lot of money but are not able to get to a better health state.

Investing in medical spending is a function of insurance status  $I_0$ . They face a fixed cost of going to the doctor  $k$  and a proportional out-of-pocket cost depending on their insurance status  $m q(I_0)$  where  $q(I_0)$  can be thought of as co-insurance.  $q(I_0)$  can also be thought of as the “effective price” of the healthcare service depending on the insurance status. It is important to emphasize that because of the fixed cost  $k$ , the individuals don’t invest in their health continually and it becomes a stopping time problem where individuals choose to invest in their health by visiting the doctor as a discrete choice. Thus, the wealth evolves as:

$$\underbrace{w'}_{\text{Wealth after visit}} = \underbrace{w}_{\text{Wealth before visit}} - \underbrace{k}_{\text{Fixed Cost}} - \underbrace{m(q(I_0))}_{\text{Out-of-pocket Cost}}$$

Thus, individuals optimally choose when to visit the doctor and how much to spend on medical care. There are various channels through which individuals may want a

better health: direct utility from being able to enjoy consumption more, higher labor productivity resulting in higher labor income, lower likelihood of disability or dying and getting the terminal value.

## Wealth and Income

An individual earns an income  $\theta(h)y(e, a)$  which varies by education,  $e$  and age  $a$ . I also allow for income to be scaled by labor productivity  $\theta(h)$  which is an increasing function of health  $h$ . Individual consumes  $c$  and pays an health insurance premium  $p$ , if insured (otherwise, it is set to 0 for Medicaid and uninsured). They also earn a rate of return  $r$  on wealth  $w_t$ . The budget constraint is standard and is given by:

$$dw_t = (rw_t + \theta(h)y(e, a) - c_t - p) dt$$

## Utility Function

Individuals derive utility from consumption  $c$  and their health  $h$  and the specification is as follows:

$$u(c, h) = (1 + \phi(h)) \frac{c^{1-\gamma} - 1}{1 - \gamma} \quad (1)$$

I chose a multiplicative form to allow for the possibility that individuals can derive more utility from consumption when they're at a better health state. Note, however, that I am not imposing that health and consumption are complements vs substitutes as the functional form of  $\phi(h)$  can handle either possibilities.

## Insurance take-up problem

Insurance take-up is governed by a Poisson process of intensity  $\phi$ . This implies that individuals are given the option to take up insurance at random intervals through their life cycle. When this option occurs (or at the time of Poisson realization), they are offered a premium,  $p(a)$  based on their age  $a$ . Individuals then decide whether or not to take up insurance. If they do, then the premium stays the same until another (random) realization of the Poisson. Insurance premium and risk sharing is obtained from the data.

At the time of Poisson realizations, individuals can take-up Medicaid if they are

eligible by paying a fixed cost  $f$ . This leads to selection into Medicaid take-up problem. Note that private insurance is the same as Medicare after 65 where individuals pay a highly subsidized premium, which I estimate from data.

### Long-term Disability Stage

Long-term-disability is modeled as an absorbing state, where exit rate is given by  $\lambda^D a$ , health is given by  $h^D$  and disability income is given by  $y^D$ . Given that long-term disability makes one eligible for Medicare, it can be modeled at these individuals needing  $\bar{m}$  investments continually – such as dialysis treatment for end-stage renal failure, which comes from Medicare.

Thus, the HJB becomes:

$$\begin{aligned} \rho V^D(w, h^D, a) = \max_c \{ & u(c, h^D) + V_w^D[y^D + rw - c] \} \\ & + \eta[V^D(w, h, v, a + 1) - V^D(w, h^D, a)] + \lambda^D(a)(V^T - V^D(w, h^D, a)) \end{aligned} \quad (2)$$

## 3.2 Individual's Problem

The individual's problem is composed of two branches: (1) a continuation region, where the individuals do not go to the doctor and the only decisions are consumption-savings and taking-up private insurance in case of Poisson realization; (2) a stopping region where individuals go to the doctor and invest in their health capital.

In the continuation region, the value includes the flow utility  $u(c, h)$  from consumption – augmented with the health state – and captures the idea that individuals may derive more utility from consumption in a healthier state. The value also incorporates the dynamic effects from aging, transitioning to a better  $(h + 1)$  or worse  $(h - 1)$  health, likelihood and value from dying and the change in value associated with the insurance

choice. The continuation region  $\Gamma^C$  is described as follows:

$$\begin{aligned}
\rho V(w, h, v, a, I, p) = & \max_c \{u(c, h) + V_w[\theta(h)y(a) + rw - c - p]\} \\
& \underbrace{\eta[V(w, h, v, a + 1, I, p) - V(.)]}_{\text{aging to } a+1} + \underbrace{v[V(w, h + 1, v_0, a, I, p) - V(.)]}_{\text{transition to } h+1} + \\
& \underbrace{d(h, a)[V(w, h - 1, v_0, a, I, p) - V(.)]}_{\text{transition to } h-1} + \underbrace{\lambda^T(h, a)[V^T - V(.)]}_{\text{death}} + \\
& \underbrace{\phi[\bar{V}(w, h, v, a, I', p') - V(.)]}_{\text{insurance choice}} + \underbrace{\kappa^D(h, a)[V^D - V(.)]}_{\text{disability}}
\end{aligned} \tag{3}$$

$$\text{where, } \bar{V}(w, h, v, a, I', p') = \max \left\{ \underbrace{V(w, h, v, a, 1, p(h, a))}_{\text{insurance}}, \underbrace{V(w, h, v, a, 0, 0)}_{\text{no insurance}}, \underbrace{V(w - f, h, v, a, 2, 0)}_{\text{Medicaid}} \right\}$$

On the other hand, in the stopping region, given their decision to invest in health, they choose medical expenditure  $m_t$  which increases  $v$ , i.e. lowers the expected duration of going to the better health state, according to equation (7). The cost of medical expenditure depends on the fixed cost of going to the doctor  $k$  and out-of-pocket cost  $mq(I_0)$ . The impact on wealth is given by equation (6). The stopping region  $\Gamma^S$  is described as follows:

$$V(w, h, v, a) = V^*(w', h, v', a) \tag{4}$$

$$\text{where, } V^*(w, h, v, a) = \max_m V^i(w', h, v', a) \tag{5}$$

$$w' = w - k - mq(I_0) \tag{6}$$

$$v' = v_0(a) + Am^{\alpha_m} \tag{7}$$

It is important to emphasize that because of the fixed cost  $k$ , the individuals don't invest in their health continually and it becomes a stopping time problem where individuals choose to invest in their health by visiting the doctor as a discrete choice.

Thus, under the assumptions of at most linear growth and Lipschitz continuity,<sup>18</sup> the individual's problem can be written compactly as,

<sup>18</sup>By (Øksendal and Sulem, 2005, Theorem 1.19), the solution to Levy SDEs exists

$$\begin{aligned}
& \min \left\{ \rho V(w, h, v, a, I, p) - \max_c \{ u(c, h) + V_w[\theta(h)y(a) + rw - c - p] \} \right. \\
& - \eta[V(w, h, v, a + 1, I, p) - V(\cdot)] - \nu[V(w, h + 1, v_0, a, I, p) - V(\cdot)] - \\
& d(h, a)[V(w, h - 1, v_0, a, I, p) - V(\cdot)] - \lambda^T(h, a)[V^T - V(\cdot)] - \phi[\bar{V}(w, h, v, a, I', p') - V(\cdot)] - \\
& \left. \kappa^D(h, a)[V^D - V(\cdot)], V(w, h, v, a) - V^*(w', h, v', a) \right\} = 0 \tag{8}
\end{aligned}$$

or

$$\min \left\{ \Gamma^C, \Gamma^S \right\} = 0 \tag{9}$$

*Optimal stopping would be  $\tau(w, h, v, a, I, p)$ .*

Following Theorem 3.2 in Øksendal and Sulem (2005) Integrovariational Inequality for Optimal Stopping, the maximization problem is same as solving the following HJBII in (9).

### 3.3 Policy Function: Doctoral visit

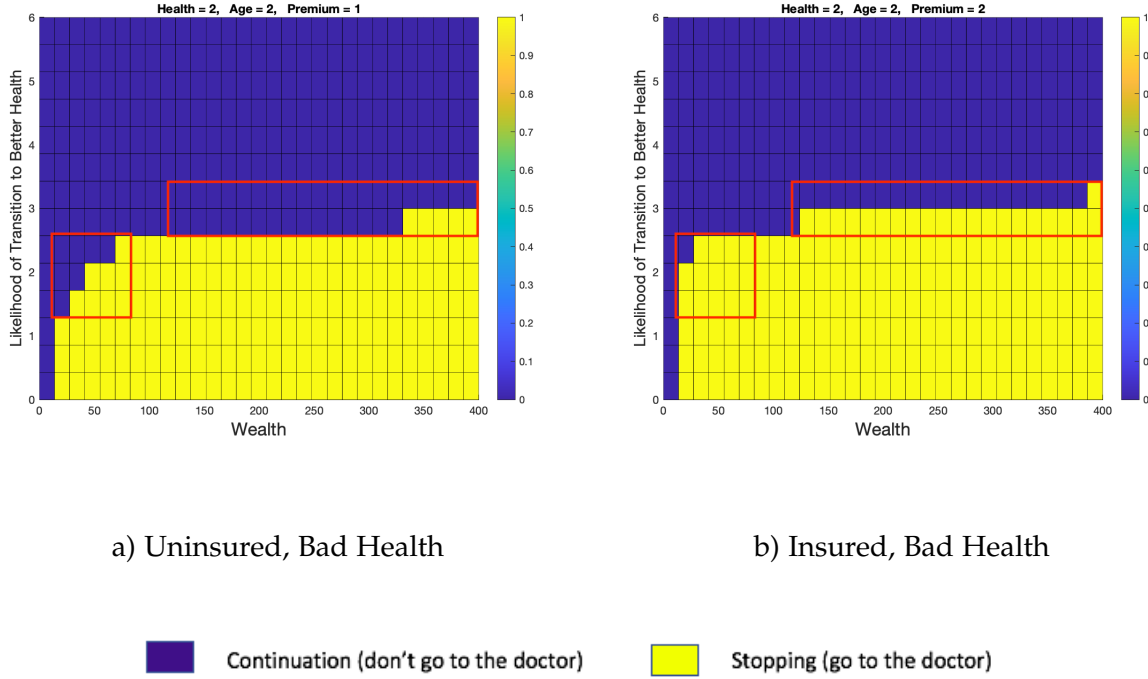
To provide a description of one of the key choices of the model, I look at the visit decision for an individual at age 35-45 in bad health<sup>19</sup> (Figure 9). I plot the decision to visit the doctor as a function of their wealth and improvement intensity, fixing age and health status. As a result of the fixed cost, there are wealth effects in the visit decision. I see that as wealth increases, more individuals go to the doctor, fixing the likelihood of going to a better health state before going to the doctor (y axis). For each level of wealth, there is cutoff in improvement intensity below which the individual goes for the doctoral visit and health investment. It is also clear that rich individuals go to the doctor much earlier (at a higher improvement intensity) as compared to those who are poor. On the other hand, comparing insured and uninsured, there are states of the world where insured individuals would go to the doctor while uninsured individuals would not.

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<sup>19</sup>The whole policy function is a multi-dimensional object, I look at some cross-sections of this multi-dimensional object.



Figure 9: Visit Decision, Age 35-45



## 4. Estimation

First, I present the functional forms I assume in the model which help in reducing the number of parameters to be estimated while still allowing for flexible parameterizations. Second, based on identification, I separate the parameters into three sets: i) a set of parameters to be calibrated outside of the model; ii) a set of parameters estimated outside of the model; iii) a set of parameters estimated within the model. Finally, I use Simulated Method of Moments to target choices (doctor visits, healthcare investment, and insurance take-up) and transitions (change in health with and without visit, death rate, health over the life-cycle), average investment ratio between rich and poor of the same health, and disability rates to identify health transition, mortality and disability shocks, utility gains from health, health production function and fixed costs associated with doctor visits and Medicaid take-up. In particular, I leave the health and spending by wealth untargeted and show an untargeted fit with respect to wealth moments in the next section.

## 4.1 Specification

I allow for 6 age groups in the model, each with a 10 year range, starting from 25 years up to 85 years. As observed in data, there are 5 health states: 1 (Poor) to 5 (Excellent). I impose certain simplifying assumptions to ensure feasibility in estimation. The exogenous depreciation of health capital  $d_h^a$  is assumed to be the same across health states for a specific age  $a$  i.e.  $d_h^a = d^a \quad \forall h = \{1, 2, 3, 4, 5\}$ .  $d^a$  is specified as a power function of age, and is given by:

$$d^a = d_0 + d_1 a + d_2 a^2 \quad (10)$$

The natural improvement component of  $v$  is also specified as power function of age, and is given by:

$$v_0(a) = n_0 + n_1 a + n_2 a^2 \quad (11)$$

For exit probabilities  $\lambda_h^a$ , I assume proportional increase of mortality rates across by age, keeping the gradient of health from  $\lambda_h^6$ . In other words, I allow for 5 factors,  $F_{25-35}$  -  $F_{65-75}$  such that:

$$\lambda_h^a = \begin{cases} \lambda_h^6 / F_{25-35} & \text{if age} \in \{25 - 35\} \\ \lambda_h^6 / F_{35-45} & \text{if age} \in \{35 - 45\} \\ \lambda_h^6 / F_{45-55} & \text{if age} \in \{45 - 55\} \\ \lambda_h^6 / F_{55-65} & \text{if age} \in \{55 - 65\} \\ \lambda_h^6 / F_{65-75} & \text{if age} \in \{65 - 75\} \end{cases} \quad (12)$$

I specify the utility cost of health  $\phi(h)$  as a power function of health:

$$\phi(h) = \phi_0 + \phi_1 h + \phi_2 h^2 \quad (13)$$

## 4.2 Parameters Outside the Model

Two set of parameters that are set outside of the model. First, I present the parameters parameters that are calibrated outside of the model in table A.8.7. Two key parameters are: i) productivity by health ( $\theta(h)$ ), which is taken from Ozkan (2014); ii) value of life or terminal value ( $V^T$ ) is assumed to be 11.5M.

Second, I present the parameters which I estimate from the data. I feed in the initial distribution of health ( $h_0(e = L, H)$ ), education  $e = L, H$  and wealth ( $\mu_L, \sigma_L, \mu_H, \sigma_H$ ) at the age 25 by education as initial conditions to the model. Income by age and education  $y(e, a)$  as well as disability income  $y^D$  is estimated from the data. The exit intensity  $\lambda_h^a$  at health  $h$  and age  $a$  comprises of two components:  $\lambda_h^6$  and the survival factors  $F_{25-35} - F_{65-75}$ . For  $\lambda_h^6$ , while I estimate the exit intensity for average health and age 75-85 within the model ( $\lambda_3^6$ ), all other exit intensities are normalized based on this estimate outside the model. Therefore, I set  $\lambda_h^6$  for  $h = 1, 2, 4, 5$  and  $\lambda_h^a$  for  $h = 1, 2, 3, 4, 5$  and  $a = 1, 2, 3, 4, 5$  by using the exit probabilities for from the data by taking 15-day exit rates. For example, my 15-day exit rates show that those in poor health at age 75-85  $\lambda_1^6$  are 11.07 times more likely to die compared to those in average health at ages 75-85  $\lambda_3^6$ . For the survival factors  $F_{25-35} - F_{65-75}$ , these are estimated from the data using aggregate age-specific instantaneous mortality.

Individuals aged 25-65 years who are on Medicare are used to estimate the cost being paid by Medicare in long-term-disability  $m^D$ . Exit rates of disabled individuals at each age  $a$ ,  $\lambda^{Da}$ , is estimated relative exit rates of those in same age but average health  $\lambda_3^a$ , using 15-day exit rates. Similarly, while aggregate disability rate is estimated within the model  $\kappa_D$ , the gradient of disability by health is estimated outside using disability rates by health from the data.

Average annual out-of-pocket insurance premium by age is used to estimate insurance premium by age  $p(a)$ . Effective price/out of pocket healthcare spending by insurance is used for out-of-pocket co-insurance  $q(I)$ . For uninsured, I estimate this by looking at charge-to-expenditure ratio of insured individuals. Put differently, I assume that for same service, if an uninsured visits the doctor, they would pay 1.45 times the total – not just out-of-pocket – amount paid for by a person who is insured.

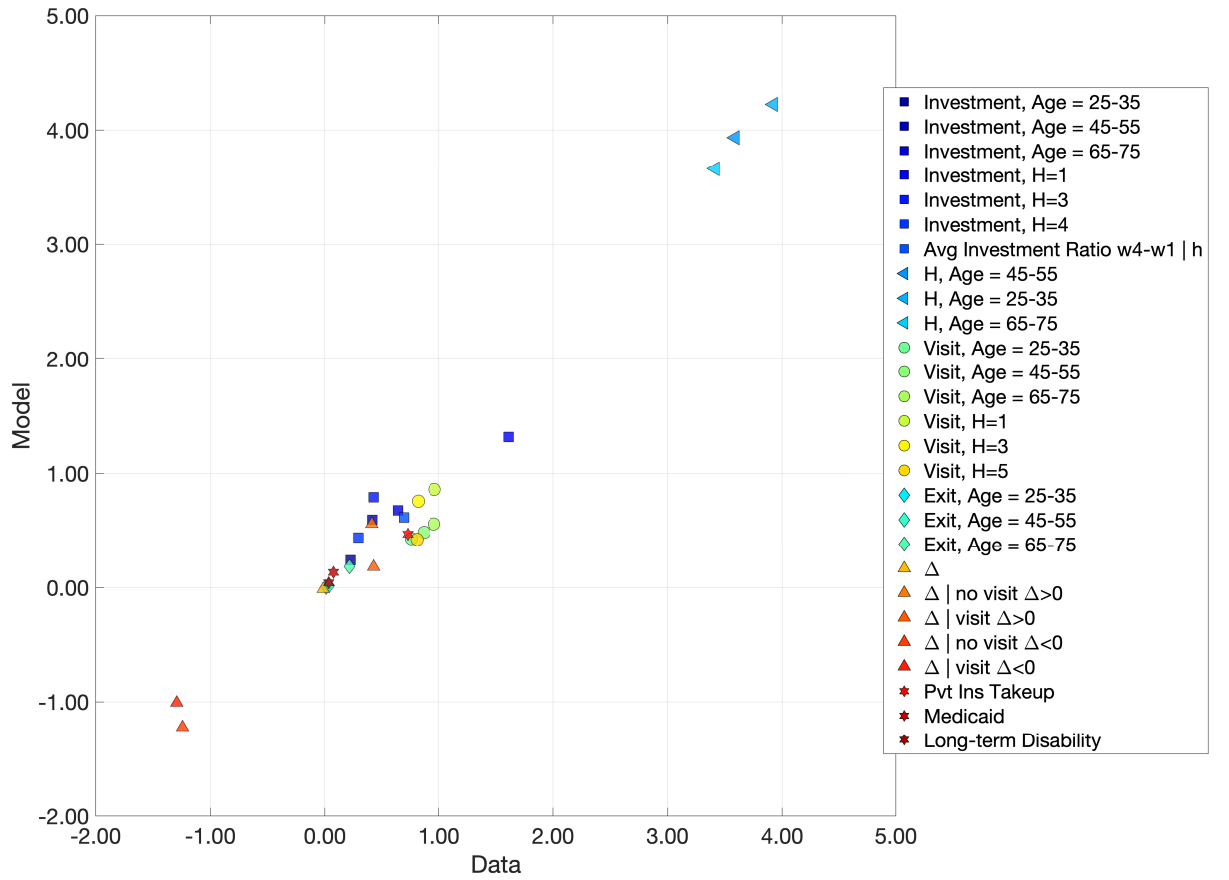
### 4.3 Identification

The remaining parameters to be estimated include health production parameters  $A$  and  $\alpha_m$ , fixed cost of doctoral visit,  $k$ , depreciation and improvement parameters  $d_0, d_1, d_2$  and  $\nu_0, \nu_1, \nu_2$ , the utility parameters  $\phi_0, \phi_1$  and  $\phi_2$ , fixed cost of Medicaid take-up  $f$ , disability rate  $\kappa^D$  and mortality rate  $\lambda^T$ .

While a lot of moments co-move with parameters, the idea behind identification is to use observable heterogeneity in the decisions such as fraction visit and spending across health and age to pin down Poisson intensities along with differences in outcomes such

as improvement and changes in health across age and health to pin down technology parameters. More specifically, rate at which an individual transitions to worse and better health with and without doctor visit is informative about age based depreciation and improvement of health. Health investment by age and health status pins down the utility gains from health. Fixing other parameters, health investment ratio by rich and poor for same health are informative about the curvature in the health production function,  $\alpha_m$ . For example, for every low  $\alpha_m$ , we would expect to see very little difference across rich and poor for same health compared to higher values of  $\alpha_m$ . The fraction of individuals who take-up Medicaid is informative about the fixed cost in acquiring Medicaid. Lastly, fraction of those individuals who visit doctor is informative about fixed cost associated with that decision.

Figure 10: Model Fit: Targeted Moments



## 4.4 Estimates

I estimate the partial equilibrium model on individuals aged 25 and above. A natural limitation is that in the policy simulations, the general equilibrium effect – via clearing the insurance prices – would be missing and I would point out scenarios in which it could play an important role. In the appendix, I write down the ways to incorporate these provisions with insurance firms' problem and the estimation with those is left for future work. I select our sample from NLMS-MDAC and NHIS-MEPS as the privately insured individuals aged 25-85 with 10-year intervals. I interpret the categorical variable of self-reported health status from Poor to Excellent Health as the measure of health in the model from 1-5.

I report the set of targeted moments and the model fit in table A.8.9 in the appendix and in the figure 10. The model does a good job of capturing health investments over the life-cycle and by health. Two place where model doesn't do a good job are: private insurance take-up for 25-65 year age (73% in data vs 47% in the model). One reason for this could be that for a lot of individuals in the US, the insurance choices available is tied to their jobs and the data isn't able to capture the employer-subsidies provided in the insurance market. Another reason could be the highly negotiated price for services by private insurance, something I try to address as well as possible with the data, as described previously.

I describe the estimates now. The estimated fixed cost is  $k = 0.0335$ , equivalent to \$335 per visit. i.e. on average individuals face \$335 per visit as equivalent monetary cost to visit the doctor. The estimates of  $d_0$ ,  $d_1$  and  $d_2$  are 0.36, 0.04 and 0.003 respectively. Converting the implied Poisson intensities to expected duration, the estimates imply that the expected duration before going to a worse health state is 2 years and 7 months for those aged 25-35 and this number goes down to 1 year and 6 months for individuals in age 65-75. Similarly, based on the estimates of  $\nu_0$ ,  $\nu_1$  and  $\nu_2$ , the natural improvement duration is 7 years to go to a better health state for those ages 25-35 while those in 65-75 group never go to a better health state naturally. Finally, the estimates imply the marginal utility of consumption at same level of consumption for average health is about 2.56 times that in poor health, showing that health and consumption are complements in the utility function. This last results is consistent with Finkelstein et al. (2013).

Table 2: Parameter Estimates

Parameter	Type	Estimate
$A$	TFP	0.98
$\alpha_m$	Elasticity w.r.t. $m$	0.10
$k$	Fixed Cost	0.0335
$d_0$	Depreciation Poission (Constant)	0.36
$d_1$	Depreciation Poission (Age)	0.04
$d_2$	Depreciation Poission (Age <sup>2</sup> )	0.003
$n_0$	Natural Improvement (Constant)	0.13
$n_1$	Natural Improvement (Age)	-0.13
$n_2$	Natural Improvement (Age <sup>2</sup> )	0
$\phi_0$	Utility Cost of Health (Constant)	1.30
$\phi_1$	Utility Cost of Health (Health)	0.99
$\phi_2$	Utility Cost of Health (Health <sup>2</sup> )	0.01
$\lambda^T$	Exit Intensity	0. 01872
$q$	Insurance Cost	0.02
$\kappa_D$	Disability Intensity	0.06

## 5. Results

With the estimated model, I now present data patterns across health, wealth and age to illustrate the model fit for the un-targeted moments and to show the mechanisms in the model.

### 5.1 Visit decision by health status

I first explore the key mechanism of the timing of health investments. To understand the responsiveness of doctoral visits on health status for rich and poor wealth, I run an individual fixed effect regression of visiting a doctor on their health status for rich and poor separately. This is done for both data (using family income) and model (using wealth). While the model is simulated monthly, I perform the regression using quarterly frequency – same as the data – for better comparison. In figure ??, I present the estimated probability of doctoral visit for those in poor health relative to those in average health for

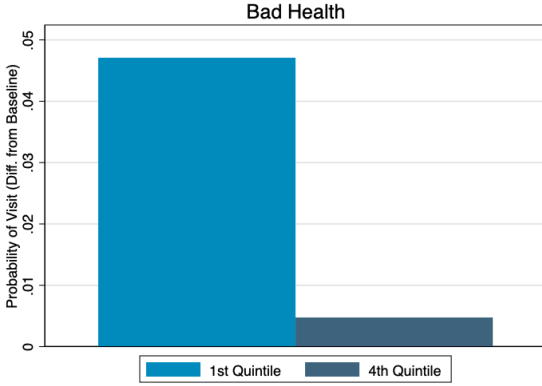


Figure 11: Visit Decision by Health Status: Model

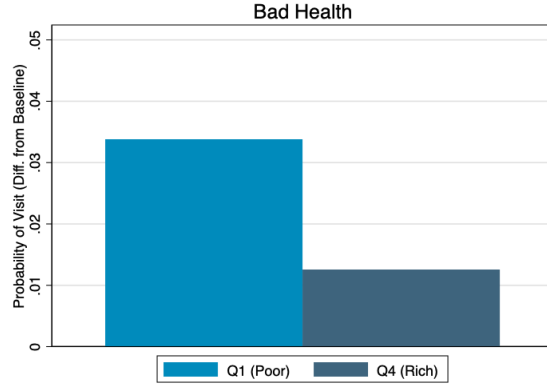


Figure 12: Visit Decision by Health Status: Data

income/ wealth rich and poor, for data and model respectively<sup>20</sup>. The results indicate that poor individuals' visit decision is highly responsive to their health state esp. for bad health shocks. An implication of this is that the poor individuals go to the doctor in a much more unhealthy state than the rich. Compared to a poor person in average health, a poor person in poor health is 4.7% points more likely to go to the doctor (vs 3.3% in data). This number is 0.5% in the model for the rich (vs 1.2% in data). Similarly, compared to a poor person in average health, a poor person in excellent health is 25% points less likely to go to the doctor.

While the responsiveness for bad health is comparable to data, the responsiveness for excellent health in the model is higher compared to data. It is not surprising since in the model, the only way in which a person in excellent health goes to the doctor is if their health depreciates. In other words, it may be an artifact of a bounded health state. A way to address this would be to allow for people to invest in lowering depreciation intensity,  $d_h^a$ , which could be thought of as preventive spending.

## 5.2 Spending across health status

After looking at the visit decision, I present the quarterly spending by health and wealth from the model and data in Table 3 and 4, respectively. Fixing health, wealthy spend more on their health over the next year, thus transitioning to a better health with a higher

<sup>20</sup>The variation for this regression comes from the panel component where I observe an individual and its doctoral visit decision on their health status



Table 3: Model: Age 35-45

	Health				
	1	2	3	4	5
Q1 (Poor)	1.29	0.31	0.31	0.19	0.09
Q2	1.06	0.57	0.44	0.20	0.10
Q3	1.24	1.01	0.69	0.34	0.19
Q4 (Rich)	1.21	1.33	0.91	0.51	0.20

Table 4: Data: Age 35-45

	Health				
	1	2	3	4	5
Q1 (Poor)	1.61	0.81	0.43	0.29	0.21
Q2	1.88	0.92	0.47	0.31	0.20
Q3	2.02	0.98	0.55	0.33	0.23
Q4 (Rich)	2.40	1.19	0.61	0.39	0.26

probability. This pattern is true across all health states<sup>21</sup>. I also show that this compares well with the medical spending data by family income adjusted for family size and age quartile<sup>22</sup>.

### 5.3 Health Transitions

Having looked at the choices of decisions and spending, I now show the outcomes, such as health transitions. I analyze the health transition of each wealth group, relative to the poor or bottom quartile. I plot the coefficient of wealth group dummy for quartile 2 to 4 as a percent of the base (quartile 1 or poor) of a regression of  $H_{t+1}$  controlling for  $H_t$  and age for individuals who visited the doctor in the past year. In figure 13, I find that after controlling for age and health in time  $t$ , those in top quartile have a health that is 20% higher than those in bottom quartile. This is a result of higher spending by the rich, due to which they transition to a better health with a higher probability in the next quarter. I conduct similar exercise albeit for family income group, which is an imperfect analogue to the model, and find similar differences across top and bottom family income quartile. One caution is that I am interpreting the categorical variable of health as an index from 1-5. For this, I perform similar analysis for a binary variable for health, as is common in the literature [De Nardi et al. \(2017\)](#), as well as a multinomial logit, and get similar results.

<sup>21</sup>It holds for all ages, however, ages 35-45 are shown here for exposition.

<sup>22</sup>Moments by wealth are pending from the data center and will be added as data release approval is received.

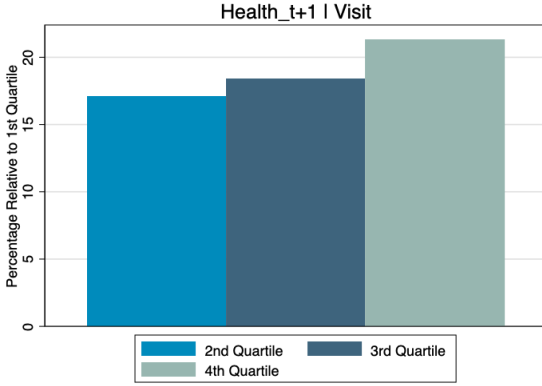


Figure 13: Model (by Wealth)

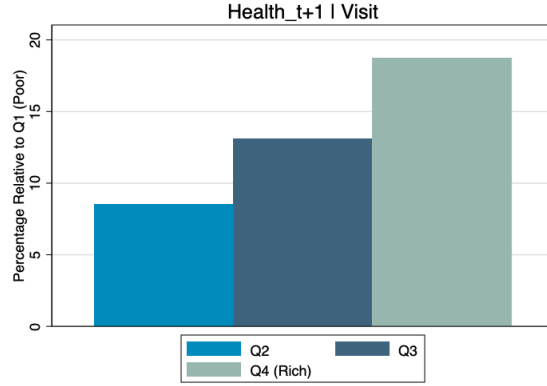


Figure 14: Data (by Family Income)

Source: NHIS-MEPS  
Notes: Regress:  $Health_{t+1}$  on  $Health_t$ , Age, Age<sup>2</sup>; base set to family income (Data) or wealth (Model) poor

## 5.4 Spending and Outcomes

A key puzzle motivating this paper is the difference in life-expectancy across rich and poor with comparable medical spending. Table 5 and 6 present the model and data moments on life-expectancy, mean spending and mortality rates where the poor or bottom quartile are normalized to 1. First, the estimated model is able to predict about half of the gap in life-expectancy between the top and the bottom quartiles. Second, the model also does a good job of capturing the flatness in medical spending across wealth groups – an untargeted moment – for the younger ages. In particular, note that the higher mortality rates for the poor relative to the rich is not driven by higher spending by the rich.

The effect of difference in timing of health investment on spending and health outcomes primarily arises as a result of the complementarities in health production, where \$1 in average health is better than \$1 in worse health. Thus, the investment at a lower health state is less likely to result in a transition to good health. Poor individuals, due to lack of insurance or financial constraints delay their visit decision until they reach their stopping time (a lower health state), which causes them not to reap the benefit of their medical spending as opposed to rich, who do not delay their visit. This results in comparable health investments but significant differences in health outcomes.

Table 5: Model

	Wealth Quartiles			
	Q1	Q2	Q3	Q4
Life-Expectancy	1.00	1.04	1.04	1.06
Mean Spending 25-35	1.00	1.06	1.47	1.15
Mean Spending 35-45	1.00	0.75	0.96	1.08
Mean Spending 45-55	1.00	0.74	0.82	1.65
Mean Spending 55-65	1.00	0.66	0.86	1.94
100 x Mortality 25-35	1.00	0.75	1.25	0.56
100 x Mortality 35-45	1.00	0.67	0.52	0.46
100 x Mortality 45-55	1.00	0.70	0.51	0.41
100 x Mortality 55-65	1.00	0.47	0.47	0.32

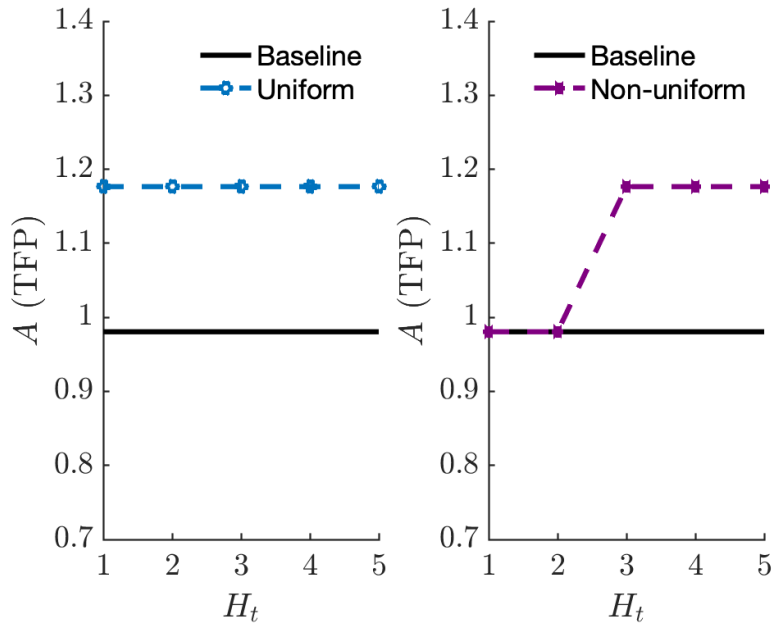
Table 6: Data

	Wealth Quartiles			
	Q1	Q2	Q3	Q4
Life-Expectancy	1.00	1.05	1.10	1.12
Mean Spending 25-35	1.00	0.90	0.99	1.07
Mean Spending 35-45	1.00	0.89	0.86	0.93
Mean Spending 45-55	1.00	0.74	0.72	0.73
Mean Spending 55-65	1.00	0.89	0.90	0.93
100 x Mortality 25-35	1.00	0.87	0.87	0.86
100 x Mortality 35-45	1.00	0.51	0.48	0.35
100 x Mortality 45-55	1.00	0.55	0.41	0.37
100 x Mortality 55-65	1.00	0.59	0.47	0.32

## 6. Quantitative Experiments

### 6.1 Technology

Figure 15: Technological Progress Type



In order to understand the role of technological innovation on the rising health inequality in the US, I consider two types of innovations. First, a uniform broad-based 20% TFP improvements in the healthcare sector (which results in about 1 year of gains in life-expectancy on average) where the medical innovation is happens across all the health spectrum and Second, a non-uniform 20% increase in technology (which results in about 5 months of gains in life-expectancy on average) which leads to improvement for early diagnosis – such as cancer stage I – but not for later stages of cancer. The experiment is shown in the picture below.

I find that a uniform increase in the productivity of the healthcare sector reduces the inequality in life expectancy by more than half a year. Both poor and rich alike benefit from the progress and have higher life-expectancy but the poor – starting from a lower initial life-expectancy – gain more than the rich, leading to an overall reduction in the gap.

Figure 16: Role of Technological Progress

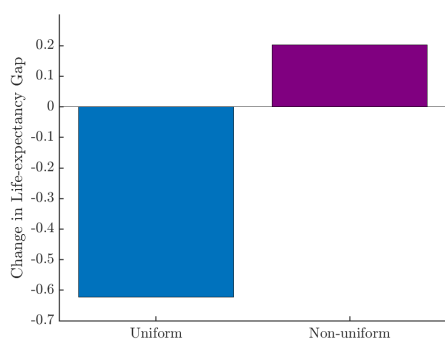
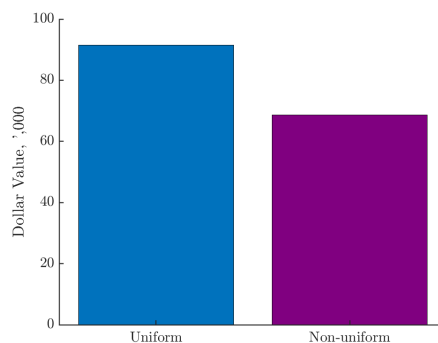


Figure 17: Value of Technological Progress



On the other hand, a non-uniform increase in TFP – one where the medical system gets better at treating early illnesses but not at treating terminal cancer, disproportionately improves the life-expectancy for the rich and not for the poor. Thus, the timing of the health investment interacts with the technological progress to worsen the inequalities. An example to build intuition for this result: suppose that two decades ago, medical technology was such that only stage 1 cancer could be treated. Now suppose that due to technological progress in cancer treatments, the medical technology today is such that cancer until stage 2 can be treated. While the rich, frequently going to see the doctor, visit the doctor and invest in their health at stage 1, the poor, having deferred the treat-

ment, only go for their visit and health investment when the cancer is in stage 3.<sup>23</sup> Thus, the poor not only end up spending the same amount as a rich person in any given year, they are also not able to reap the benefits of the medical technological progress that we have witnessed<sup>24</sup>.

I use my model to quantify the dollar value of the two types of innovations in the healthcare sector discussed above. My findings can be summarized as follows. First, I find that society puts a large dollar value on medical innovations, ranging from \$69,000 to \$92,000 per individual (1.5-2 times income per capita in the model). Second, the value of innovation depends on whether it is uniform broad-based or limited to certain types. The value of a uniform broad 20% improvement in the healthcare sector that results in about a year of gains in average life-expectancy is \$92,000 per individual (2 times income per capita in the model) compared to \$69,000 per individual (1.5 times income per capita in the model) from non-uniform 20% improvements that results in about 5 months of gains in average life-expectancy.

## 6.2 Insurance

In order to understand the role of insurance on health inequality, I perform three experiments. First, I shut down Medicaid. Second, I shut down Medicaid and private insurance together. Third, give everyone a public health insurance, aka “Medicare-for-all” financed by a flat 16% income tax along with 30% cost sharing. Figure 18 presents the results.

I find that Medicaid would lead to the inequality in health outcomes going up by 10% (6.2 years vs 5.5 years baseline). On the other hand, shutting down private Insurance exacerbates in inequality by almost twice as much. This is due to the fact that private insurance overwhelmingly is taken up by relatively wealthy – who face a lower “effective price” of goods and consume more. The role of private insurance on the inequality is ambiguous, ex ante. On one hand, an option to buy private insurance may increase

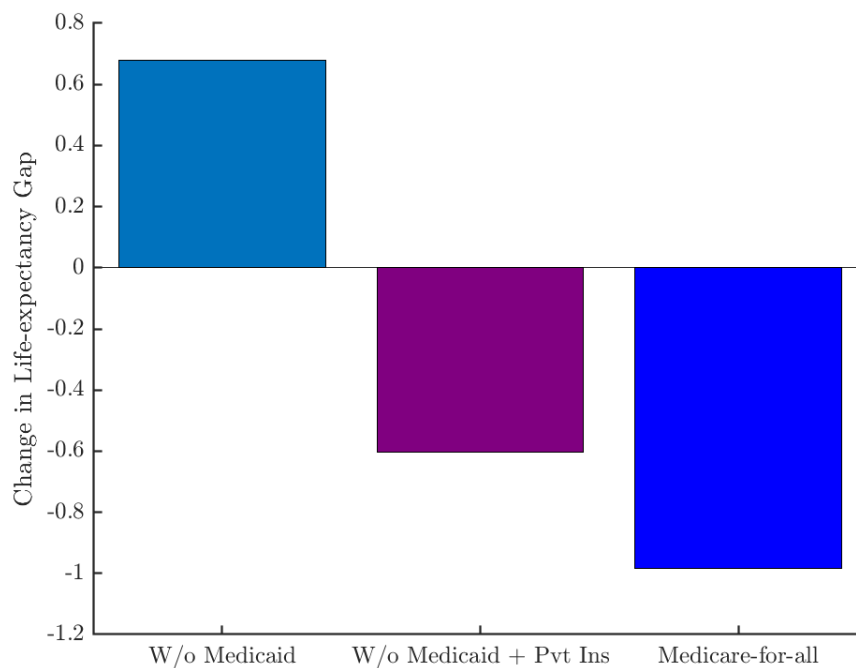
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<sup>23</sup>See, for example, [Walker et al. \(2014\)](#) and [Niu et al. \(2013\)](#) which use Surveillance, Epidemiology, and End Results (SEER) registry data to document the differences in diagnosis stage of cancer across insurance groups providing the basis for our example here.

<sup>24</sup>It is consistent with the fact that the type of cancer for which the survival rates have converged the most for the affluent and less affluent over the past 2 decades is Hodgkin Lymphoma [Cancer Research UK, Accessed April 2021](#) for which the survival rate is relatively flat across cancer stages [Cancer Research UK](#) while the cancer for which the survival rates have diverged the most is oesophageal cancer, which has a steep one-year mortality rate across cancer stages Source: UK Cancer [Cancer Research UK Accessed: April 2021](#)

disparities since only the rich would be willing to pay the premium and buy insurance to diversify their health risks and smoothen out their consumption. On the other hand, unhealthy individuals would be the ones selecting into health insurance due to the well documented adverse selection in the insurance markets. This can be clearly seen in the insurance take-up problem in Figure 19 and 20. While for those in excellent health, only the wealthy take up private insurance, for those in good health, there is a selection of people whose expected duration of going to a better health is low or in other words, those who anticipate going for a doctoral visit, take up private insurance. The threshold below which people take-up private insurance is increasing in wealth. The same selection applied to Medicaid below the eligibility threshold. On net, I find that the wealth effect dominates and the effect of removing private insurance and Medicaid would lead to a modest increase in life-expectancy inequality.

Figure 18: Role of Insurance



Medicare-for-all, with fixed cost and co-pays, can reduce the inequality by about 20%. Medicare-for-all illustrates a key tradeoff in the policy making: while the inequality in health outcomes would go down, it has to be financed by income taxes, esp. if Medicare-

Figure 19: Good Health

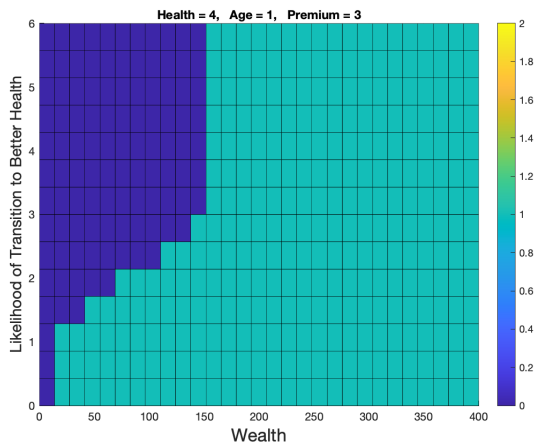
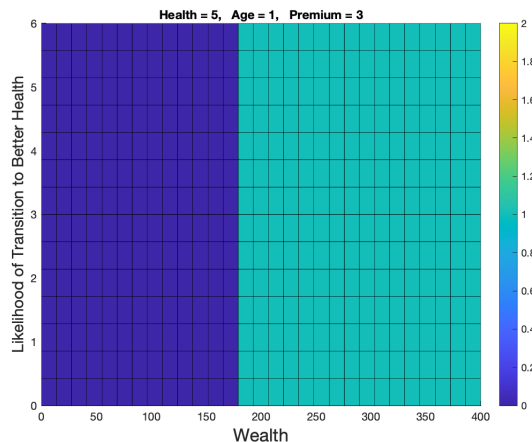


Figure 20: Excellent Health



for-all offers a lower out-of-pocket costs. Therefore, Medicare-for-all with out-of-pocket same as private insurance can be financed at a lower tax but an blunt the effects of the policy.

I should emphasize here that the policy experiments involving private insurance and “Medicare-for-all” insurance maybe missing general equilibrium effects through the insurance firms’ problem.

### 6.3 Role of Health in Income Inequality

I use my model to quantify the role played by health in exacerbating the existing income inequality. To end this, I look at three experiments: i) No feedback of health into productivity ii) Shutting down private insurance and Medicaid iii) Implementing Medicare-for-all policy.

I find that if there was no feedback of health into productivity, income inequality, as measured by 90-10 ratio, would go down by about 15% (3.44 v 3.65 in baseline). This is lower than the recent findings by [Hosseini et al. \(2021b\)](#), likely due to the fact that they do not incorporate the endogenous responses to reduced incentives to invest in health. Individuals lower their medical investments over the life-cycle by 20% as a result of a reduced incentive to invest in their health via productivity channel as shown in figure 22.



Figure 21: Income Inequality

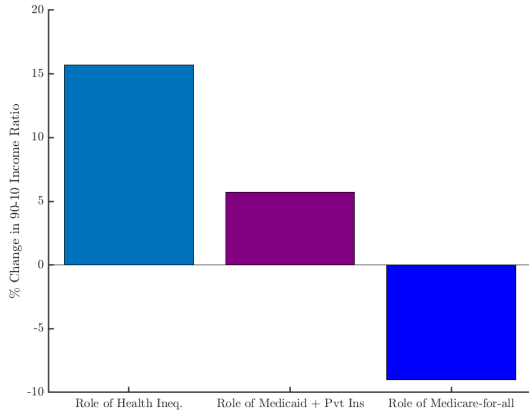
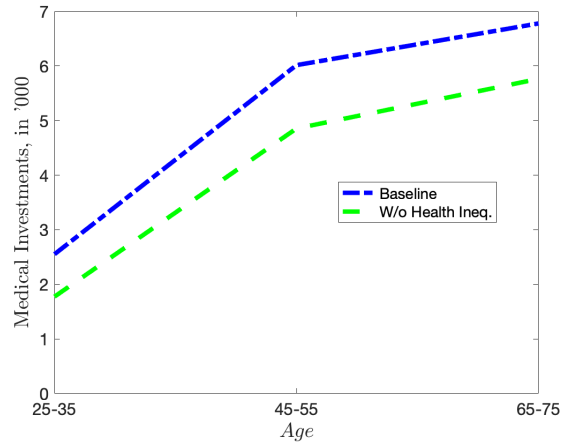


Figure 22: Health Investments: Shutting down Health-Income Channel



Interestingly, I find that private insurance exacerbates the existing income inequality by about 5% whereas Medicare-for-all reduces income inequality by 9%, as shown in figure 21. This is largely driven by the productivity channel of health wherein improvements in health for the low income individuals leads to higher labor income through higher productivity and subsequently, lower income inequality.

## 7. Conclusion

The large inequality in health outcomes and its worsening over time is puzzling, especially given that the rich and poor have comparable total health investments in any given year. This paper explores the role of insurance and technological progress on rising health inequality across income groups. I focus on key mechanism: timing of healthcare investments.

First, using a merged panel dataset of health, expenditures and mortality along with a large scale federal survey data, I document new facts on health spending and outcomes. i) While heart related improvements are the biggest contributors to increased life-expectancy equally across income groups, cancer related improvements are the largest drivers of increased disparity in health outcomes. ii) Poor individuals' timing of investment is very responsive to their health status, i.e. poor delay their investments till they are in worse health relative to rich and thus are less likely to transition to a better health

state even when they visit the doctor.

I then develop a dynamic stochastic life-cycle model with incomplete markets where I explicitly model that individuals choose the timing of health investments and insurance take-up. A key feature of the model is that health production features complementarities between health and health investment, i.e. the return on each \$ spent depends on the health status when they visit the doctor. I estimate the model using the merged dataset using Simulated Methods of Moments. The key finds are: i) lower wealth individuals' visit decisions are more responsive to their health state – particularly in bad health; ii) flatness in spending is generated as a result of the complementarities in health and health investment, in presence of borrowing constraints and fixed costs associated with visit decision.

I show that different types of technological innovation interacts with the timing of the investment and has a first order effect on disparities. On one hand, a non-uniform increase in the productivity of the medical sector – one where there are improvements in treating early stages of cancer for example, but none for stage 4 – can lead to increase in inequality in life-expectancy. In contrast, a uniform increase in the productivity of the healthcare sector, leads to a reduction in disparities. Focusing on the role of insurance, I find that while Medicaid alleviates the health inequality, private insurance exacerbates inequality by almost twice as much. Finally, I find that a policy of “Medicare-for-all” not only reduces the health inequality, it could also lower existing income inequality.

In future work, extending the model to incorporate the general equilibrium effects of the health insurance markets would allow us to think about an optimal health insurance policy. Technological access and diffusion across geographies (counties and across countries) is another aspect to be explored in future work. Incorporating other types of healthcare investments (such as smoking and exercising) which can be complementary to healthcare spending or in health production function is something I leave for future work.

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## A.8. Tables Appendix

Table A.8.7: Set Outside of the Model

Parameter	Meaning	Value
$\rho$	Discount rate	0.06
$r$	Interest Rate	0.05
$\gamma$	Risk Aversion	1.5
$T$	Exit Age	85
$s$	Initial Age	25
$V^T$	Terminal Value	11.5M
$\theta(h)$	Productivity by Health	11% per h (Ozkan (2014))
$\bar{w}$	Medicaid Cutoff	20 % ptile wealth
$h^D$	Disability health (utility function)	1
$\eta$	Aging Poisson, all ages	$\frac{1}{10}$
$\phi$	Insurance Intensity	1/12

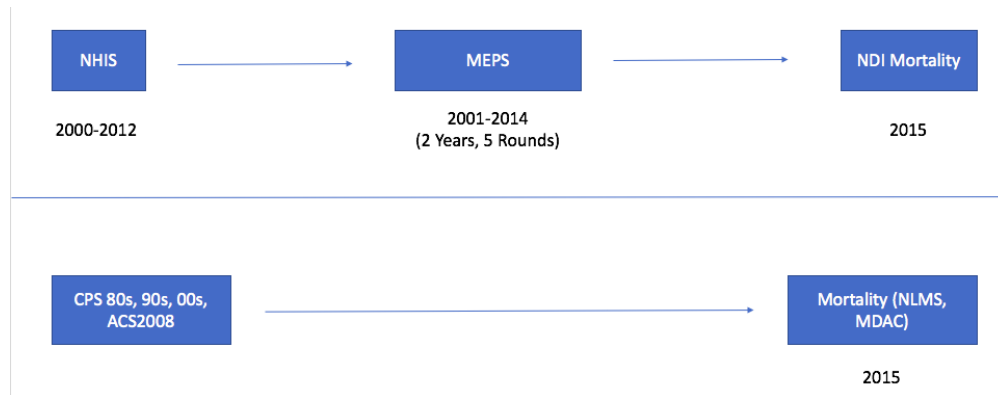
Table A.8.8: Estimated Outside of the Model

Meaning	Parameter	Value
Mortality Rate, Age 75-85	$\lambda_1^6, \lambda_2^6, \lambda_3^6, \lambda_4^6, \lambda_5^6$	$(11.07, 1.82, 1, 0.45, 0.07)\lambda^T$
Survival Factor by age	$F_{75-85}, F_{65-75}, F_{55-65}, F_{45-55}, F_{35-45}, F_{25-35}$	1, 2.05, 4.53, 12.43, 26.56, 41.78
Disability Exit relative to Avg Health, by age	$\frac{\lambda^{Da}}{\lambda_3^a}$	3.10, 6.75, 6.48, 5.96, 5.96, 5.96
Income by Education and Age (\$10,000)	$y(e = L, a)$	2.49, 3.23, 3.55, 3.34, 2.66, 2.23 ACS (2013)
Income by Education and Age (\$10,000)	$y(e = H, a)$	4.73, 7.41, 8.35, 7.68, 6.27, 5.15 ACS (2013)
Initial wealth distribution by education	$\mu_L, \sigma_L, \mu_H, \sigma_H$	0.94, 3.52, 1.73, 2.88
Disability Income (\$10,000)	$y^D$	1.53 ACS (2013)
Insurance Premium by Age	$p(a)$	0.25, 0.31, 0.33, 0.35, 0.25, 0.25 OOP Premium (NHIS)
OOP Rate Pvt Ins, Medicaid, Uninsured	$q(I)$	0.33, 0.15, 1.45 (MEPS)
Annual Spending, Long-term Disability (\$10,000)	$m^D$	1.48 (MEPS)
Initial health distribution (%), e = L	$h_0(e = L)$	1.10, 5.03, 24.12, 34.86, 34.89 (MEPS)
Initial health distribution (%), e = H	$h_0(e = H)$	0.27, 1.54, 11.66, 34.82, 51.71 (MEPS)
Initial education distribution (%)	$e = L, H$	69.49 30.51 (ACS2013)
Disability factor by h	$\kappa^D(h)$	$(0.34, 0.16, 0.06, 0.03, 0.0) \kappa^D$

Table A.8.9: Model Fit

Moment	Data	Model
Investment, Age = 25-35	0.22	0.24
Investment, Age = 45-55	0.41	0.60
Investment, Age = 65-75	0.64	0.68
Investment, H=1	1.61	1.32
Investment, H=3	0.43	0.79
Investment, H=4	0.29	0.44
Avg Investment Ratio $w_4-w_1 \mid h$	0.69	0.62
H, Age = 45-55	3.59	3.93
H, Age = 25-35	1.09	1.07
H, Age = 65-75	0.95	0.93
Visit, Age = 25-35	0.76	0.43
Visit, Age = 45-55	0.87	0.49
Visit, Age = 65-75	0.96	0.56
Visit, H=1	0.96	0.86
Visit, H=3	0.82	0.76
Visit, H=5	0.81	0.42
Exit, Age = 25-35	0.01	0.00
Exit, Age = 45-55	0.04	0.02
Exit, Age = 65-75	0.21	0.18
$\Delta$	-0.01	-0.01
$\Delta \mid \text{no visit } \Delta > 0$	0.41	0.56
$\Delta \mid \text{visit } \Delta > 0$	0.43	0.18
$\Delta \mid \text{no visit } \Delta < 0$	-1.24	-1.22
$\Delta \mid \text{visit } \Delta < 0$	-1.29	-1.01
Private Insurance Takeup	0.73	0.47
Medicaid	0.08	0.13
Long-term Disability	0.03	0.04

Figure A.9.23: Data Chart



## A.9. Data Appendix

The dataset is constructed from four main sources, namely, Merged National Health Interview Survey (NHIS)-Medical Expenditure Panel Survey (MEPS) and National Longitudinal Mortality Survey (NLMS) and Mortality Differentials Across Communities (MDAC). MEPS is a rolling panel and provides us with 5 snapshots over two years, its sample is drawn from the cross sectional NHIS. A merged dataset thus allows us to track individuals for 3 years in 6 snapshots from the start in year 2000 - 2015 along with ex-post mortality status until 2015 irrespective of the sample year. We provide a brief description of the datasets here.

1. Merged National Health Interview Survey (NHIS) - Medical Expenditure Panel Survey (MEPS): We use harmonized Integrated Public Use Microdata Series (IPUMS)-NHIS data from 1996-2015 and augment it with variables from Medical Expenditure Panel Survey (MEPS) including the recently available harmonized IPUMS-MEPS. We use the restricted link-file to merge individuals across the two datasets. Variables from NHIS include (not an exhaustive list):
  - Demographic and Socio-Economic Variables: Education, Income, Age, Sex, Occupation, Family Income, Hours worked, Health Insurance: type and coverage
  - Health Care Utilization: Number of shots , Number of visits to doctor in the past 12 months, time since physical breast exam, blood stool test, genetic test, mammogram, skin cancer exam, CT scan

- Health Outcomes: Body Mass Index, Bed Disability Days, lost days of work, history of diseases requiring diagnosis including asthma, cancer, coronary heart disease, diabetes, emphysema, heart attack, etc., date and detailed cause of death

Variables from MEPS include (not an exhaustive list):

- Demographic and Socio-Economic Variables: Education, Income, Age, Sex, Occupation, Family Income, County and State of Residence
  - Medical Conditions: life-threatening including cancer, diabetes, high cholesterol, hypertension, heart disease, and stroke; chronic conditions including arthritis, asthma
  - Event-level Medical Visit, ICD-9 Diagnosis and Procedure Code, Expenditure and Charge: Detailed event-level visit and expenditure variables; Expenditure by visit type such as outpatient, hospitalization, emergency; Expenditure by payment source such as private insurance, Medicaid and out of pocket
  - Health Insurance: type and nature of coverage under each plan; duration of coverage; payment source of policy premium; employer and non-employer related coverage
  - Preventive Care: Mammogram, Pap test, breast exam, PSA test, physical exam, blood pressure reading, and flu shot
2. National Longitudinal Mortality Survey (NLMS) and Mortality Differentials Across Communities (MDAC): Besides the demographic and socio-economic variables described earlier, NLMS includes detailed date and cause of death across multiple CPS waves from 1980- 2008. In particular, we get three normalized waves for 1983, 1993, 2003 where they track the cause of death for 6 years starting the date of interview or one 1990 wave where they track the cause of death for 11 years. Some waves include additional information on tobacco use. Similar to NLMS, MDAC covers individuals interviewed in ACS 2008 and their matched mortality details until 2015. Together, NLMS and MDAC would provide us with about 9 million records in various waves from 1980 to 2015 and merged mortality information from death certificate until 2015 (upto 35 years of mortality tracking). Detailed zip codes and longitudes, latitudes of residence are also available in this dataset.

## A.10. Facts Appendix

### Expenditure and Charge

It is also important to understand how the spending or expenditure is reported. Spending or expenditure is anything for which the provider was compensated for and thus it does not include uncompensated care<sup>25</sup>, which would likely increase poor's spending. Note that the expenditure/ spending is the amount that finally gets paid, i.e. the negotiated amount after the discounts and is lower than the charge. There are certain limitations to this spending data. First, prices are not known. Therefore, if the insurance providers negotiate a better price for the same quantity, the poor get a lower quantity of medical goods even after spending the same amount. It is also worth noting that public provisions such as Medicaid, which is available for the poor subject to income and asset criteria pays for more than a third of poor's medical spending and Medicare, which consists of about 10% of the expenditure for the poor as in figure 3 for those in 45-55 ages, are one of the most efficient negotiators and negotiate some of the lowest prices for the medical services (see for example, Clemens and Gottlieb (2017)).

Second, another potential concern is that the same service is being provided to the poor, at a higher price, simply because they visit the ER while rich visit outpatient. To address these concerns to the extent I can based on the available data, I look at the average, charge-to-expenditure ratio over the working ages. For the rich charge-to-expenditure ratio goes from 1.4 early in the life-cycle to 1.5 after 65 while it goes from 4.7 early in the life-cycle to 1.5 for later ages for the poor. This suggests that, if anything, the services being provided to poor are negotiated intensely as opposed to rich. For the visits for which I expect similar service – such as ambulatory optometrist or ambulatory dentist – the charge-to-expenditure ratio is comparable all across the income spectrum with rich (1.2) only slightly lower than poor (1.4). This can be further done at the service level, such as Magnetic Resonance Imaging, MRI or an X-Ray, something that will be added in the later versions due to data limitations.

### Decomposition of changes in life-expectancy across income groups

Let  $S_k$  be the survival rate implied by a cause of death,  $k$ . If there are  $K$  competing causes of death, assumed independent, survival rate is given by  $S = \prod_{k=1}^K S(k)$ . As is standard,

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<sup>25</sup>Uncompensated costs were about \$41 Billion or 1% of the total medical expenditure. Source: <https://www.aha.org/fact-sheets/2020-01-06-fact-sheet-uncompensated-hospital-care-cost>



survival function directly maps into life-expectancy<sup>26</sup>.

With time, the survival rate changes and is now given by  $S'$ . Now, if I were to compute the survival rate if only the cause of death  $i \in \{1, 2, \dots, K\}$  had changed from  $S_i$  to  $S'_i$ . The counterfactual survival rate is given by,  $S_{ci} = \prod_{k \neq i} S(k)S'_i$ . Thus, the life-expectancy implied by the survival rate  $S_{ci}$  would be counterfactual life-expectancy, if only cause-of-death  $i$  were to change. A direct implication of this is that the change in life-expectancy implied by the survival rate  $S_{ci}$  and  $S$  would be the change in life-expectancy if there were changes in cause-of-death  $i$ .

Similarly, I can extend this to age and cause specific survival where  $S_{k,a}$  be the survival rate implied by a cause of death,  $k$  for age,  $a$ . The counterfactual survival rate if only the cause of death  $i \in \{1, 2, \dots, K\}$  for age  $a$  had changed from  $S_{i,a}$  to  $S'_{i,a}$  is given by,  $S_{c,i,a} = \prod_{k \neq i} S_{k,a}S'_{i,a}$ . I implement the above decomposition by considering 8 major cause of death groupings defined by NCHS and age groups 20-50, 50-80 and 80+. I take the groupings as in [Becker et al. \(2005\)](#), but add the category 80+ to understand the gains at the end-of-life cycle separately. I use the geometric average of the 6-year mortality rates from 1983 using NLMS wave a and define it as an average mortality rate in 1980s while use wave c for the average mortality rate in 2000s. This is done to increase the sample size by exploiting whole person-year observation, given the age and mortality specific decomposition I are interested in.

One limitation of this analysis is that I use poverty percentiles to define income groups instead of wealth or permanent income. This is due to the fact that I only have cross section information and mortality follow-up in NLMS-MDAC and thus, are unable to do such decomposition by other classification. Another limitation of this decomposition is that it since it uses population mortality/ survival rates, it treats large reduction in mortality rates for small fraction of population similar to small reduction in mortality rates for large fraction of population. I perform robustness checks for this pattern across finer age bin and the results are similar.

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<sup>26</sup>I use period life-expectancy which is commonly used by the US Social Security Administration in its projects. It tries to obtain the expected duration a person of a given age at time  $t$  is going to live if he/ she were subject to the same mortality rate as experienced by the whole population in period  $t$ . More details can be found [here](#)

Table A.10.10: (Robustness) Gains in Life-expectancy, Age3: 1983 to 2003

	Q1 (Poor)	Q2	Q3	Q4 (Rich)
Life-expectancy 1983	70.7	74.2	77.4	79.2
Total Change (1983 - 2003)	2.4	2.7	3.1	4.7
By cause of death:				
Accident	0.1	0.1	0.2	0.2
Other	-1.1	-0.6	-0.6	-0.2
Malignant neoplasms	0.3	0.3	0.7	1.2
Cerebrovascular	0.4	0.2	0.2	0.4
Diabetes	-0.2	-0.1	-0.0	-0.1
Heart	2.8	2.6	2.8	2.9
Respiratory	-0.0	0.1	-0.1	0.2
Unknown	-0.0	-0.0	-0.0	0.0
By age group:				
20-50	-0.1	0.3	0.0	0.5
50-80	2.2	1.7	2.4	3.3
80+	0.2	0.7	0.7	0.9

Life-expectancy conditional on surviving until age 20.

Table A.10.11: Gains in Life-expectancy, by Race:  
1983 to 2003

	Whites	Blacks
Total Change (1980s - 2000s)	3.2	4.9
By cause of death:		
Heart	3.3	3.2
Cancer	0.5	1.0
Diabetes	-0.1	-0.2
Respiratory	0.0	-0.1
Cerebrovascular	0.4	0.5
Accidents	0.0	0.6
Alzheimer's	-0.3	-0.2
Suicide	0.0	0.0
Kidney Disease	-0.1	0.1
All Other	-0.6	-0.2

Life-expectancy conditional on surviving until age 20.

Table A.10.12: Gains in Life-expectancy, by Income (Some College and Above): 1983 to 2003

	Q1 (Poor)	Q2	Q3	Q4 (Rich)
Total Change (1980s - 2000s)	-2.63	-2.99	1.23	2.99
By cause of death:				
Heart	1.69	0.90	1.48	2.09
Cancer	-1.14	-0.68	0.04	0.75
Diabetes	-0.39	-0.57	-0.09	-0.18
Respiratory	-0.62	-0.65	0.13	0.24
Cerebrovascular	0.58	0.45	0.01	0.44
Accidents	-0.48	-0.34	0.01	-0.09
Alzheimer's	-0.31	-0.35	-0.34	-0.14
Suicide	0.05	-0.11	0.02	0.06
Kidney Disease	-0.16	-0.10	-0.08	0.29
All Other	-1.59	-1.42	-0.16	-0.42

Life-expectancy conditional on surviving until age 20.

Note that education attainment have changed dramatically over this time, college graduates ending up in the lower bin features selection that has changed over these decades.

Table A.10.13: (Robustness) Gains in Life-expectancy, Age4: 1983 to 2003

	0-25%	25-50%	50-75%	75-100%
Life-expectancy 1983	71.5	74.4	76.4	77.9
Total Change (1983 - 2003)	2.6	3.0	2.8	3.8
By cause of death:				
Accident	0.2	0.1	0.1	0.2
Other	-0.5	-0.3	-0.2	0.1
Malignant neoplasms	0.5	0.6	0.6	0.9
Cerebrovascular	0.3	0.3	0.2	0.3
Diabetes	-0.2	-0.1	-0.1	-0.1
Heart	2.2	2.4	2.2	2.2
Respiratory	0.0	0.0	-0.1	0.1
Unknown	-0.0	-0.0	-0.0	0.0
By age group:				
20-40	0.0	0.0	-0.0	0.1
40-60	1.5	1.4	1.4	1.5
60-80	1.0	1.1	1.1	1.7
80+	0.1	0.5	0.3	0.5

Life-expectancy conditional on surviving until age 20.

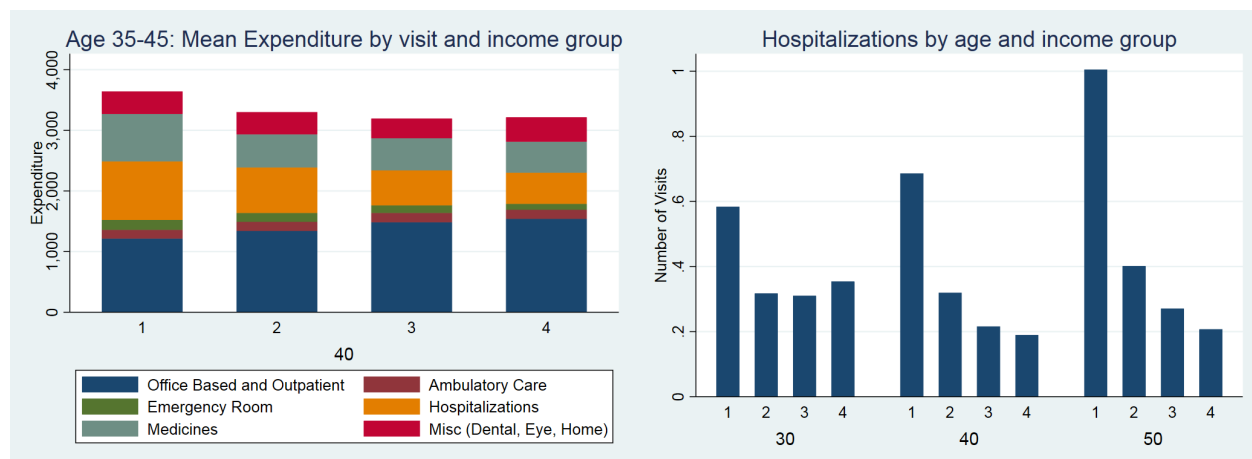
Table A.10.14: (Robustness) Gains in Life-expectancy, Age8: 1983 to 2003

	0-25%	25-50%	50-75%	75-100%
Life-expectancy 1983	71.2	74.0	75.2	76.4
Total Change (1983 - 2003)	2.4	2.7	2.7	3.0
By cause of death:				
Accident	0.3	0.1	0.2	0.2
Other	-0.3	0.0	0.1	0.1
Malignant neoplasms	0.4	0.5	0.5	0.8
Cerebrovascular	0.3	0.2	0.2	0.2
Diabetes	-0.1	-0.1	-0.0	-0.0
Heart	1.8	1.9	1.8	1.6
Respiratory	0.0	0.1	0.0	0.1
Unknown	-0.0	-0.0	-0.0	-0.0
By age group:				
20-30	0.1	0.0	0.0	-0.0
30-40	0.0	0.0	0.1	0.1
40-50	0.3	0.3	0.2	0.5
50-60	0.7	0.9	0.8	0.8
60-70	0.9	0.9	0.9	0.9
70-80	0.2	0.4	0.5	0.6
80-90	0.0	0.1	0.2	0.2

Life-expectancy conditional on surviving until age 20.

## Poor spend more on Hospitalizations and Emergency Rooms while rich spend more on Outpatient visits

Figure A.10.24: Mean Expenditure by Visit, Age 35-45  
 Figure A.10.25: Number of Hospitalizations by Age and Income

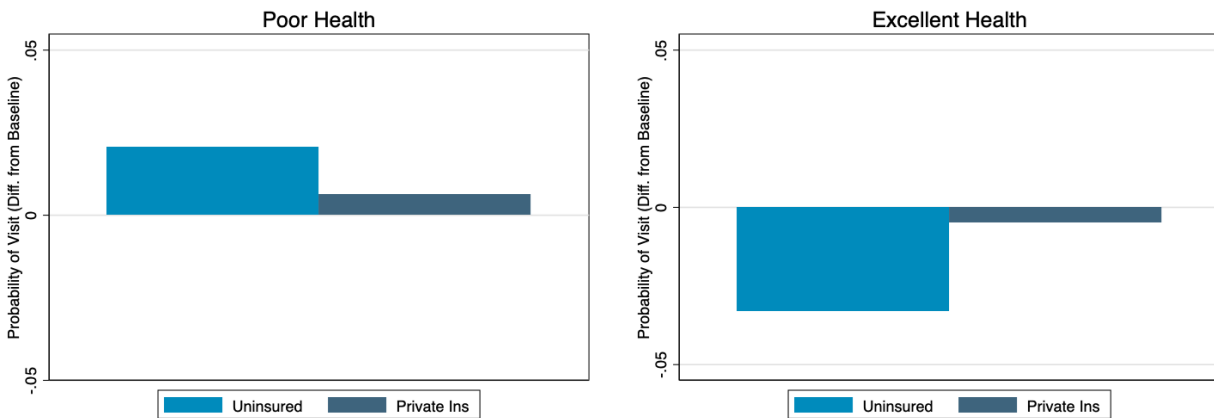


Source: NHIS-MEPS

Source: NHIS-MEPS

While the rich and poor, defined based on family income quartiles, spend comparable amounts in total medical expenditures, those in bottom quartile of the distribution spend significantly more on hospitalizations (\$1000 for first quartile vs \$500 for the top quartile for ages 35-45) and emergency room while those in top quartile of the distribution spend more on office based and outpatient visits (\$1100 for the first quartile vs \$1500 for the top quartile for ages 35-45, Figure A.10.24). This is also evident from the number of hospitalizations in Figure A.10.25. Individuals in top income quartile had less than a third of hospitalizations than bottom income quartile for age 35-45.

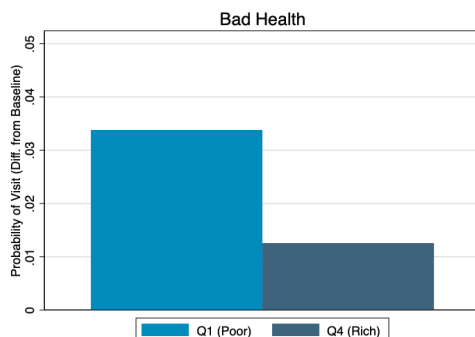
Figure A.10.28: Timing of Visit by Insurance



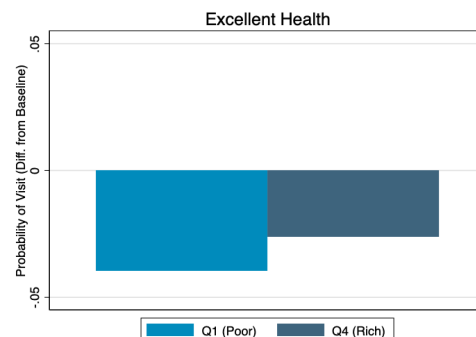
Notes: Includes individual fixed effect; base set to average health in each income group regression

## Rich individuals go to the doctor in a much healthier state

Figure A.10.26: Responsiveness to Health State: Poor vs Rich



Source: NHIS-MEPS



Source: NHIS-MEPS

Notes: Includes individual fixed effect regression of doctoral visit from  $t$  to  $t + 1$  on health in time  $t$ , run separately by income groups. Base set to average health in each income group regression.

Figures A.10.26 and A.10.27 document the responsiveness of doctoral visit w.r.to self-reported health status for rich and poor. To this end, I run two individual fixed effect regressions for each income groups with base set as average health state. The variation for this regression comes from the panel component where I observe an individual and

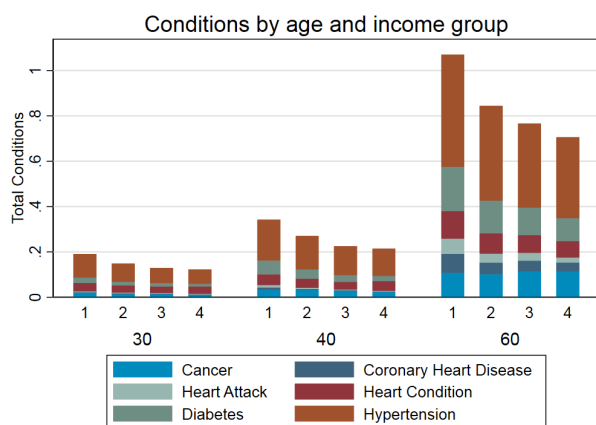


its doctoral visit decision on his/ her health status. I plot the regression coefficient associated with the health status dummy with values poor health and excellent health for each income group regression.

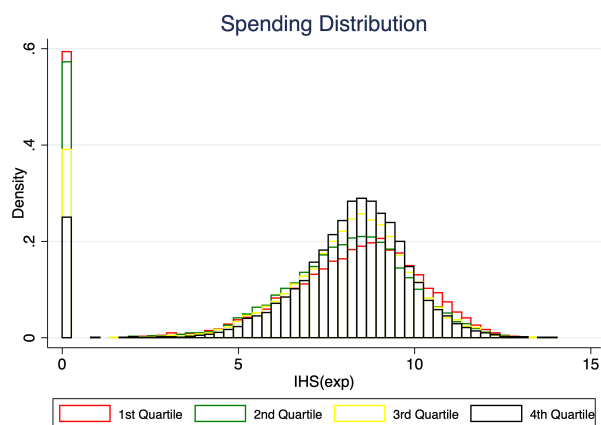
The results indicate that poor individuals visit decision is highly responsiveness to their health state. Compared to a poor person in average health, a poor person in poor health is 4% points more likely to go to the doctor. This number is only 1% points for the rich. Similarly, compared to a poor person in average health, a poor person in excellent health is 4% points less likely to go to the doctor. This indicates that while rich go to the doctor all the time, poor only go to the doctor in poor health. These results suggest that compared to the rich, poor individuals wait until their health deteriorates to a much worse health state before they go to the doctor and get the treatment. Note that for this analysis, I do not need the self-report status to be comparable across income groups since the coefficients are identified off of the *change* in health status.

## Health Conditions by Age and Income

Figure A.10.29: Mean Medical Investment: Age 25-35  
Figure A.10.30: Mean Medical Investment: Age 45-55



Source: NLMS-MDAC



Source: NHIS-MEPS

This inequality in health outcomes isn't limited to mortality as documented in Figure ?? . Across the age-distribution, individuals in bottom quartile of family income distribution report having more medical conditions such as hypertension and diabetes, compared to

Table A.10.15: Expenditure by Income: Age 35-45

	p1	p25	p50	p75	p99
1st Quintile	0	0	261	1663	40771
2nd Quintile	0	0	409	1662	30136
3rd Quintile	0	104	602	2091	27274
4th Quintile	0	195	768	2263	26763

Source: NHIS-MEPS

Table A.10.16: w/o o by Income: Age 35-45

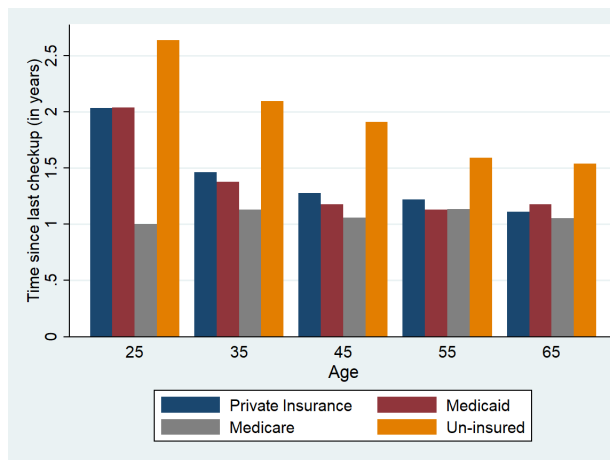
	p1	p25	p50	p75	p99
1st Quintile	10	239	838	3158	51506
2nd Quintile	13	284	855	2520	36688
3rd Quintile	24	328	958	2714	29267
4th Quintile	26	373	1035	2741	28800

Source: NHIS-MEPS

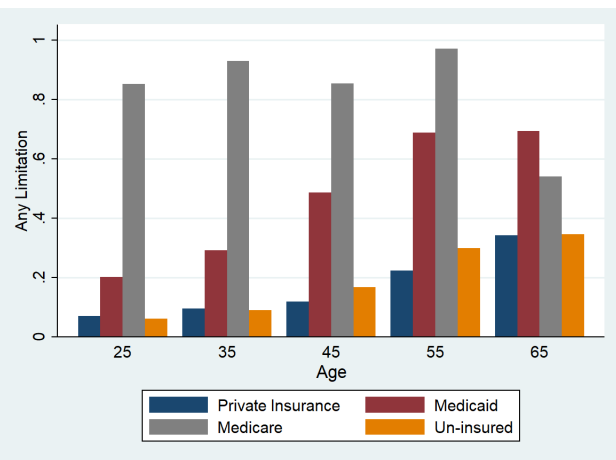
their rich counterparts. For individuals in age group 55-65, average number of conditions in a person in bottom quartile is more than one, which is about 50% higher than average number of medical conditions in a person in the top family income quartile.

While the rich and poor, defined based on family income quartiles, spend comparable amounts in total medical expenditures, those in bottom quartile of the distribution spend significantly more on hospitalizations (\$1000 for first quartile vs \$500 for the top quartile for ages 35-45) and emergency room while those in top quartile of the distribution spend more on office based and outpatient visits (\$1100 for the first quartile vs \$1500 for the top quartile for ages 35-45, Figure A.10.24). This is also evident from the number of hospitalizations in Figure A.10.25. Individuals in top income quartile had less than a third of hospitalizations than bottom income quartile for age 35-45.

Figure A.10.31: Time Since Cholesterol Checkup (with pre-existing condition)Figure A.10.32: Any Limitation by Age and Insurance Status



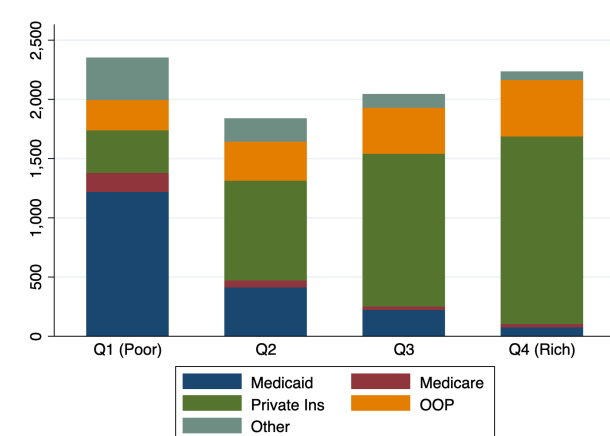
Source: NHIS-MEPS



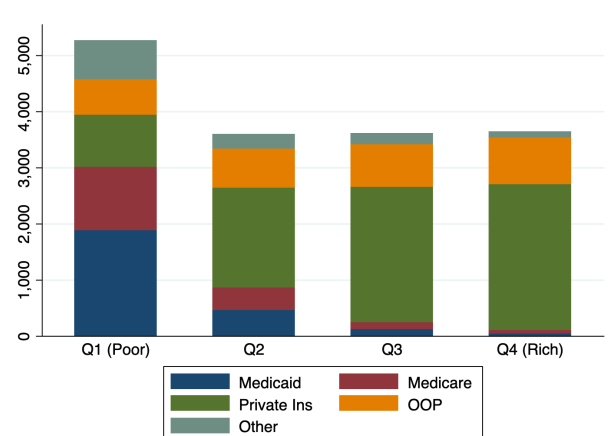
Source: NHIS-MEPS

## Health investments by Age and Income

Figure A.10.33: Mean Medical Investment: Age 25-35Figure A.10.34: Mean Medical Investment: Age 45-55

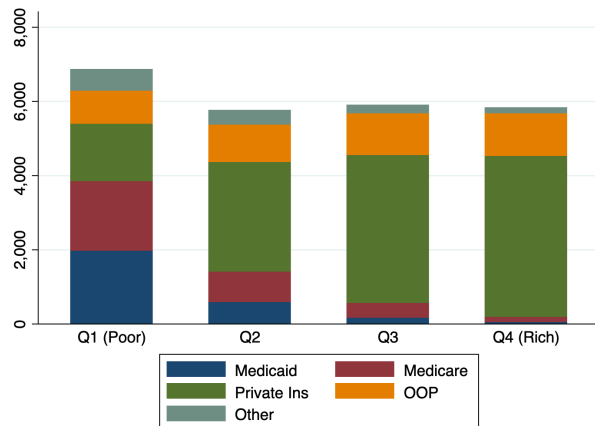


Source: NHIS-MEPS



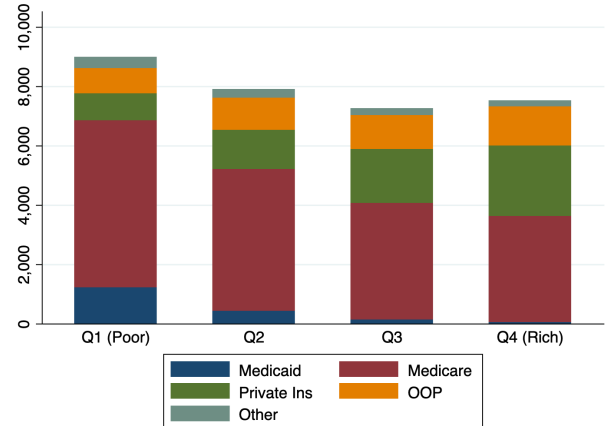
Source: NHIS-MEPS

Figure A.10.35: Mean Medical Investment: Age 55-65



Source: NHIS-MEPS

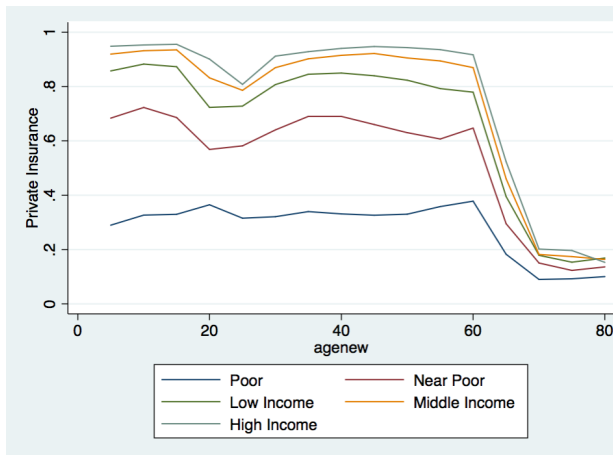
Figure A.10.36: Mean Medical Investment: Age 65-75



Source: NHIS-MEPS

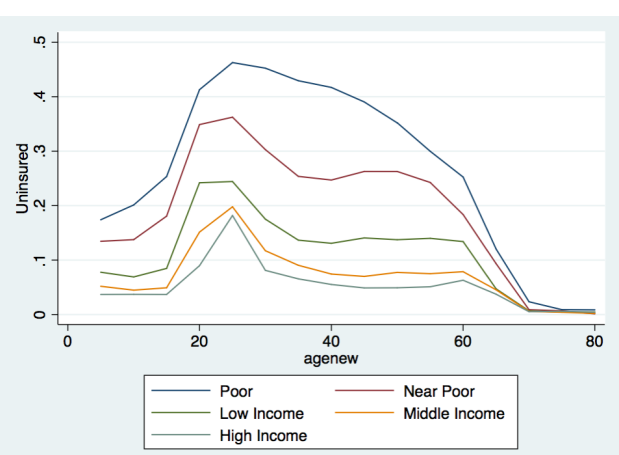
## Health Insurance by Age and Income

Figure A.10.37: Fraction with Private Insurance by Income and Age



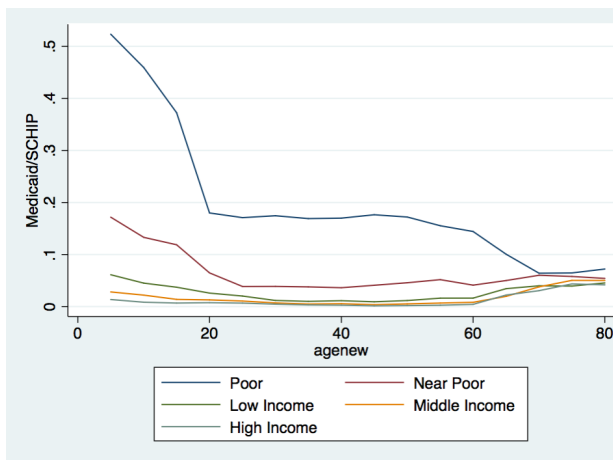
Source: Author's Calculation based on NLMS Data (early 2000s Wave)

Figure A.10.38: Fraction Uninsured by Income and Age



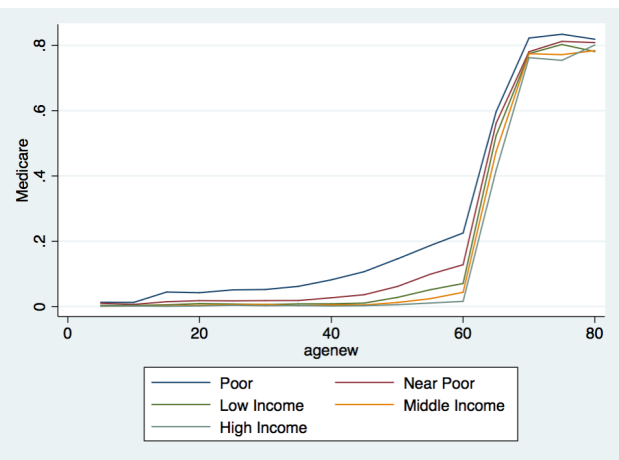
Source: NLMS-MDAC

Figure A.10.39: Fraction with Medicaid and SCHIP by Income and Age



Source: Author's Calculation based on NLMS Data (early 2000s Wave)

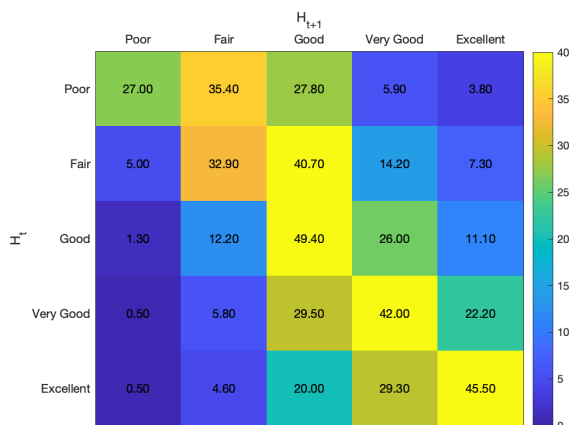
Figure A.10.40: Fraction with Medicare by Income



Source: Author's Calculation based on NLMS Data (early 2000s Wave)

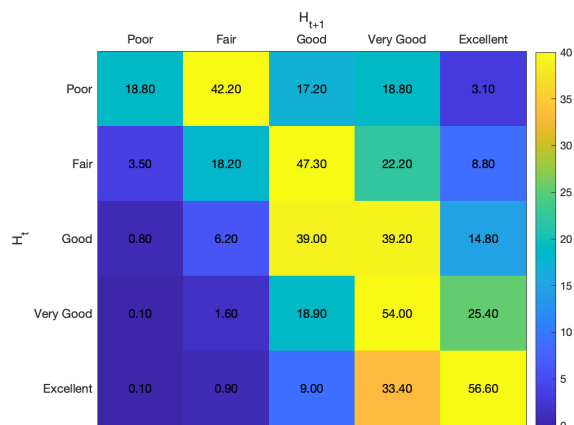
## Transition Matrix by Age and Income

Figure A.10.41: Transition matrix | visit: Poor age 25-35



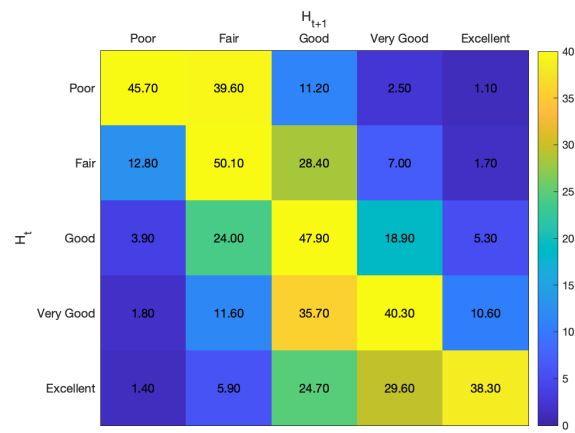
Source: NHIS-MEPS

Figure A.10.42: Transition matrix | visit: Rich aged 25-35



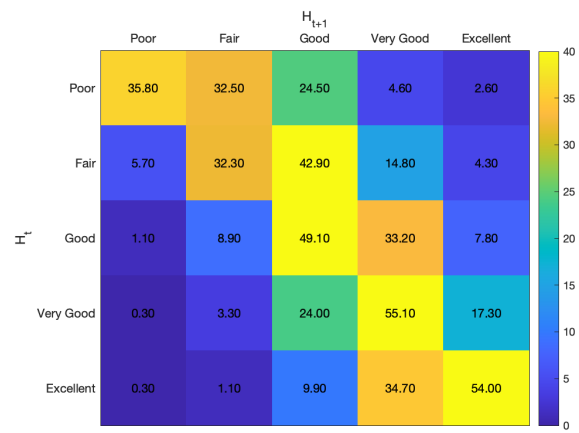
Source: NHIS-MEPS

Figure A.10.43: Transition matrix | visit: Poor age 45-55



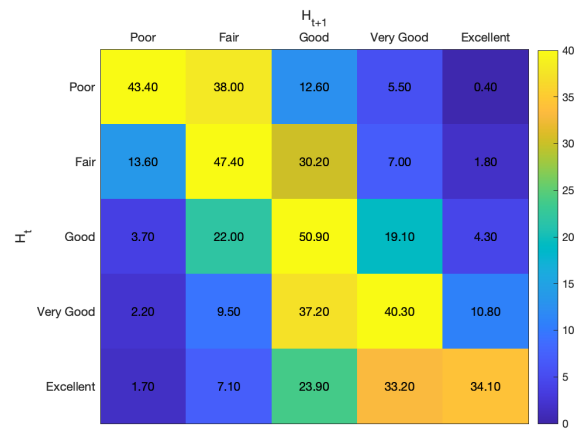
Source: NHIS-MEPS

Figure A.10.44: Transition matrix | visit: Rich aged 45-55



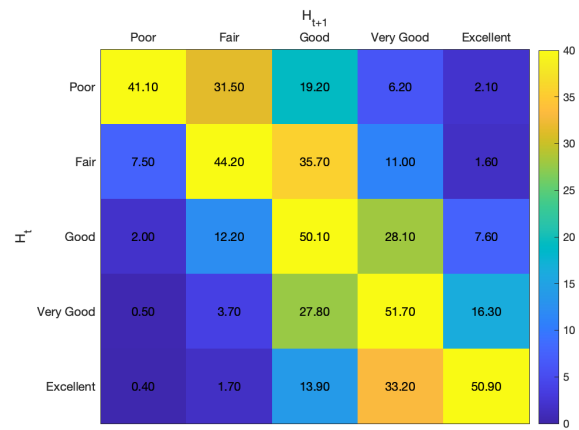
Source: NHIS-MEPS

Figure A.10.45: Transition matrix | visit: Poor age 55-65



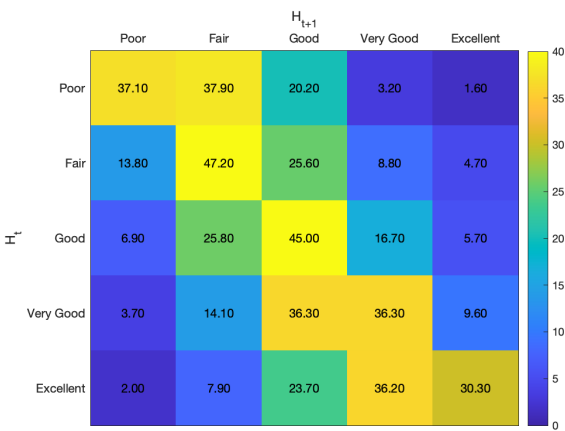
Source: NHIS-MEPS

Figure A.10.46: Transition matrix | visit: Rich aged 55-65



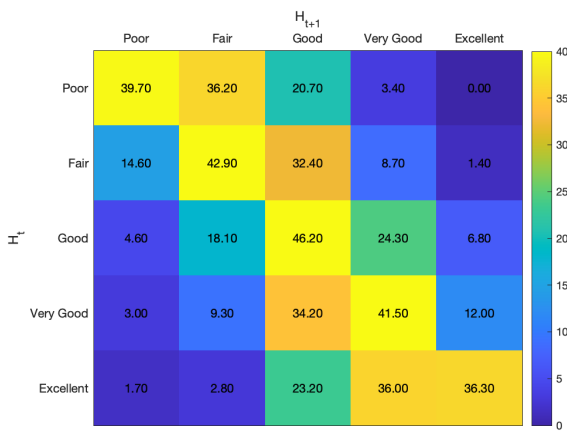
Source: NHIS-MEPS

Figure A.10.47: Transition matrix | visit: Poor  
age 65-75



Source: NHIS-MEPS

Figure A.10.48: Transition matrix | visit: Rich  
aged 65-75



Source: NHIS-MEPS

## A.10.1 External validation: Insurance and Mortality

### Effect of Medicaid on Mortality

NLMS data provides us with three cross sectional waves of initial survey which includes demographic and socio-economic status and the only “panel” component is whether an individual died at the end of 6 years or not along with the cause of death, if any. An ideal survey would have been the one with panel data along with cause of death data mapped from death certificate. Due to unavailability of such a data which is also publicly available, we make the assumption that socio-economic status, insurance status and type of insurance remain the same for the next six years. This could be problematic because of Medicaid access to poor children, thus we exclude children aged 0-18 years. Since Medicare is available, in principle, to almost everyone above the age of 65, we also exclude elderly people with age > 65 from our sample. Note that while federal government mandated minimum poverty level cutoff, states had flexibility in deciding their own eligibility criteria.

We exploit the variation in state-wide eligibility cutoff in year 2000 to estimate the effect of Medicaid on mortality. Let’s describe the ideal discontinuity design setting. Suppose a state has Medicaid cutoff as 75% of federal poverty line (FPL). We would see a discontinuity in the fraction having Medicaid at this cutoff and can look at individuals in that state with 74% of FPL and 76% of FPL. Since fine income bins are missing in the public use NLMS data, we compare the individuals in 50-75% of FPL in states where they were eligible for Medicaid and others in which they weren’t. We obtain the state-wide eligibility cutoff in 2000 from [Broaddus et al. \(2002\)](#) and follow [Blundell and Dias \(2009\)](#) to estimate the Local Average Treatment Effect (LATE) defined as:

$$\alpha^{RD}(z^*) = \frac{P(Y_{t+6} = 1|z = 2) - P(Y_{t+6} = 1|z = 1)}{P(\text{Medicaid} = 1|z = 2) - P(\text{Medicaid} = 1|z = 1)} \quad (14)$$

Where  $z$  is a categorical variable when  $z = 1$  for states for which 50-75% FPL were ineligible for Medicaid and  $z = 2$  for states in which they were. After controlling for income, education, age, sex, average education and income in the state the (local average treatment) effect of Medicaid is 9.5% points less likely to die compared to the ones who don’t have Medicaid (Table [A.10.17](#)).



Table A.10.17: Effect of Insurance on Mortality

	Logit6a	PSM_6a	Logit6b	PSM_6b	Logit6c	PSM_6c	RD6c
1 if Medicaid	0.0141*** [0.0013]		0.0135*** [0.0011]		0.0139*** [0.0008]		-0.0952*** [0.0253]
1 if Private Insurance	-0.0052*** [0.0008]	-0.0054*** [0.0012]	-0.0026*** [0.0007]	-0.0035*** [0.0010]	-0.0016*** [0.0006]	-0.0018*** [0.0007]	
Adjusted Income	-0.0005*** [0.0002]		-0.0008*** [0.0001]		-0.0007*** [0.0001]		
Age	0.0040*** [0.0002]		0.0033*** [0.0002]		0.0020*** [0.0002]		
Female	-0.0132*** [0.0005]		-0.0107*** [0.0005]		-0.0062*** [0.0004]		
1 if Medicare	0.0121*** [0.0010]		0.0133*** [0.0009]		0.0145*** [0.0007]		
Observations	301327	282423	365109	335939	443521	407441	39642
Baseline		0.0231*** [0.0007]		0.0157*** [0.0002]		0.0121*** [0.0002]	

\* p < 0.1, \*\* p < 0.05, \*\*\* p < 0.01

Standard Errors are in brackets.

Note: Outcome variable is mortality in the next 6 years across all columns. Marginal effects are tabulated. PSMxx stands for nearest neighbor Propensity Score Matching, RDxx stands for Regression Discontinuity, Logitxx shows the marginals of a simple logistic regression of whether or not an individual dies at the end of 6 years on insurance status, education, age, age sq, income, income square and sex (some of which have been suppressed from the table). xx denotes the corresponding wave number of NLMS, where 6a represents early 1980s, 6b represents early 1990s and 6c represents early 2000s.

## Effect of Private Insurance on Mortality

We first estimate a logit regression of mortality on insurance, age, education and income. The exact specification is described in table A.10.17 column 1, 3 and 5 for three waves of NLMS. Our reduced form regression specification in table suffers from potential selection problem. In particular, the decision to take up health insurance may not be random and there could be idiosyncratic gains from treatment. In order to get around the selection problem, we use the propensity score matching estimator a la Heckman et al. (1998)<sup>27</sup>. Following Caliendo and Kopeinig (2008), our parameter of interest is the average treatment on the treated  $\alpha^{ATT} = E[Y(1)|D = 1] - E[Y(0)|D = 1]$ , where D is a dummy for insurance and Y is the probability of dying in the next 6 years<sup>28</sup>. We make the following identifying assumptions:

Assumption 1 (Conditional Independence Assumption):  $Y(0), Y(1) \perp D|P(X)$

Assumption 2 (Common Support Assumption):  $0 < P(D = 1|X) < 1$

The estimator can be written as:

$$\alpha_{PSM}^{ATT} = E_{P(X)|D=1} \{E[P(Y_{t+6} = 1)|D = 1, P(X)] - E[P(Y_{t+6} = 0)|D = 0, P(X)]\} \quad (15)$$

We use nearest-neighbor matching and check for common support assumption in figure A.10.49, A.10.50 and A.10.51 and leave out the bins without overlap to ensure that common support assumption is not violated. Our propensity score specification is the following:

$$P(D = 1|age, sex, income) = \beta_0 + \beta_1 \times age + \beta_2 \times sex + \beta_3 \times income + \beta_4 \times education \quad (16)$$

Standard errors were calculating following Abadie and Imbens (2016) work on propensity score matching. Note that our matching estimate could still have some selection problem. In particular, we can only match based on observables. However, the selection could also be happening because of unobservables. As described in table A.10.17, having private insurance reduces the probability of dying in the next 6 years by about 15-25% of the baseline (uninsured individuals) in the age group 18-65 for different waves.

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<sup>27</sup>See Heckman et al. (1998), Todd (1999) and Blundell and Dias (2009) for a detailed overview of the alternative approaches.

<sup>28</sup>NLMS matches the mortality status only for 6 years after the interview

Figure A.10.49: Support for Propensity Score Matching, Wave 6a

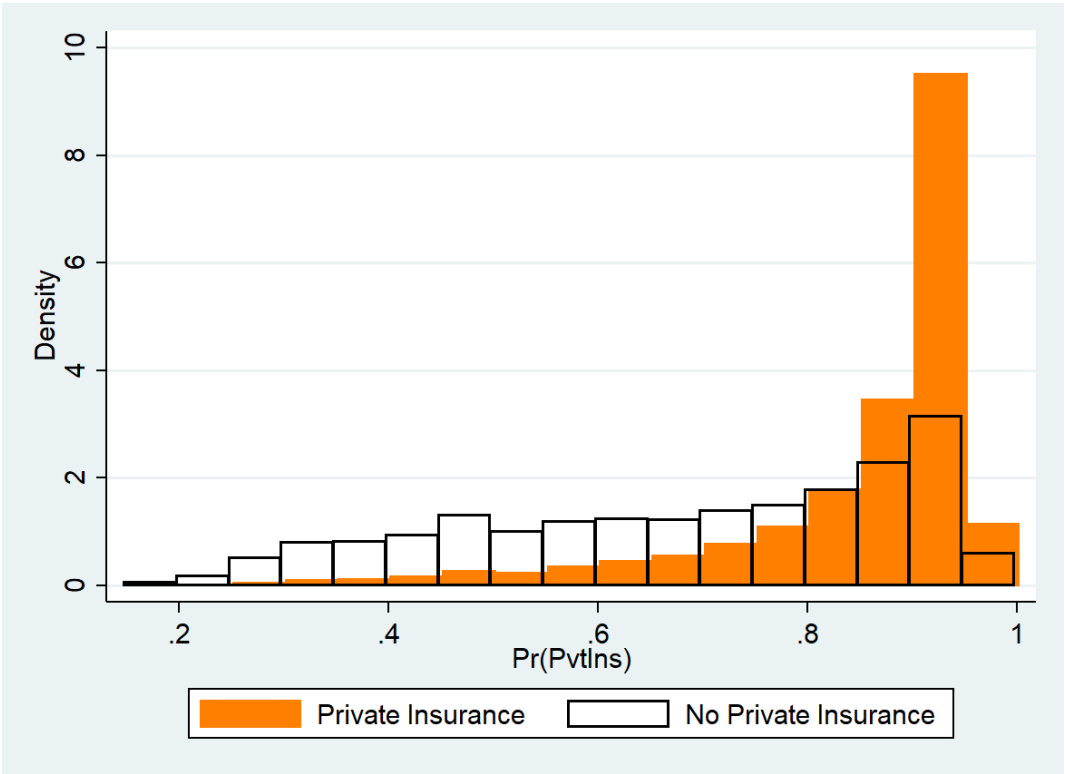
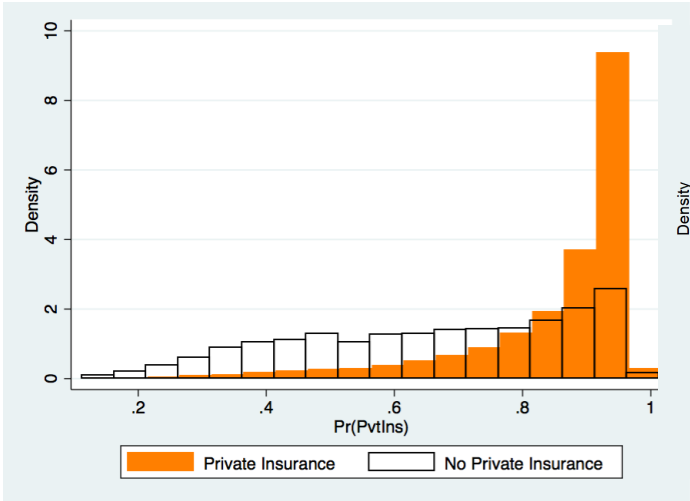
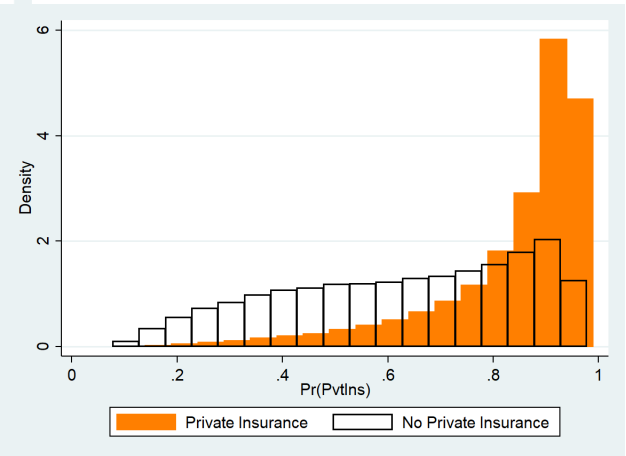


Figure A.10.50: Support for Propensity Score Matching, Wave 6b



Source: NLMS-MDAC

Figure A.10.51: Support for Propensity Score Matching, Wave 6c



Source: NHIS-MEPS

## A.11. Extensions

### A.11.1 COVID-19 Shock

I use my model to quantify the role of COVID-19 on life-expectancy, health inequality and dollar equivalent of value lost. I calibrate a COVID-like shock by increasing annual mortality by 15%, based on the empirical estimates from the first year of COVID-19. I compute the life-cycle trajectories under normal times and under COVID-19. I find that life-expectancy goes down by 1.6 years. COVID-19 exacerbates existing health inequalities due to higher mortality rate for those in poor health than rich, leading to the inequality in life-expectancy going up by 19%, as shown in figure A.11.52. This is due to the fact that poor individuals are relatively unhealthy and have more pre-existing conditions than the rich, consistent with the findings by Eichenbaum et al. (2021). Due to higher death rates in those with poorer health during the COVID-19 pandemic, the inequality in life-expectancy rises substantially. Third, the dollar value lost due to COVID-19 per person is about \$22,000 on average. Lastly, I find that faced with higher mortality rates, individuals increase their medical spending over the life-cycle by about 4%, largely concentrated towards the elderly., as documented in figure A.11.53.

Figure A.11.52: COVID-19 and Health Inequality

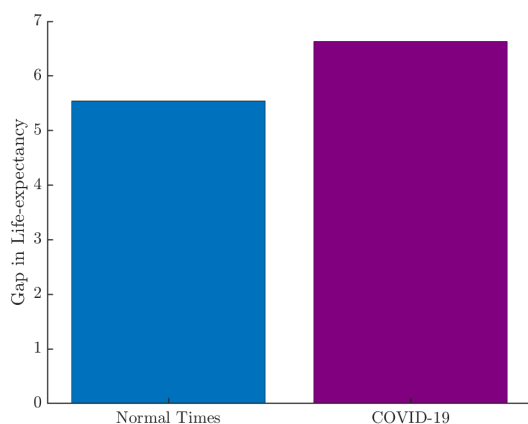
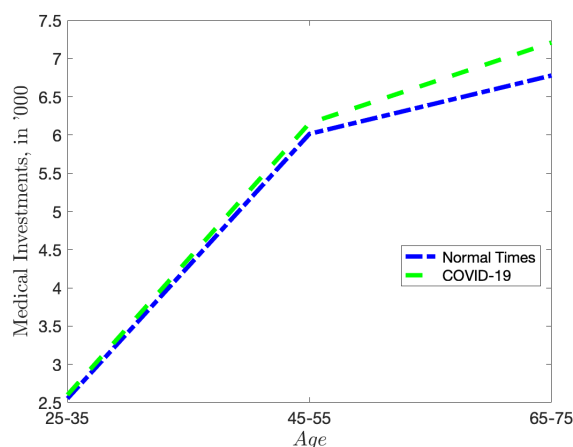


Figure A.11.53: COVID-19 and Investments



The model can be easily extended to incorporate various interesting mechanisms we discussed in the results section, something we leave for future work.

## Insurance Firm's Problem

Insurance provider is a risk neutral agent who sets the actuary fair premium in the presence of a (exogenous) stopping time determined by the individuals opting for insurance.

$$\begin{aligned}
 \rho F(w, h, v, a, I, p_0) = & p_0 + \underbrace{\eta[F(w, h, v, a + 1, I, p) - F(.)]}_{\text{aging to } a+1} + \\
 & \underbrace{\nu[F(w, h + 1, v_0, a, I, p) - F(.)]}_{\text{transition to } h+1} + \underbrace{d(h, a)[F(w, h - 1, v_0, a, I, p) - F(.)]}_{\text{transition to } h-1} + \\
 & \underbrace{\lambda^T(h, a)[0 - F(.)]}_{\text{death}} + \underbrace{\phi[\bar{F}(w, h, v, a, I', p') - F(.)]}_{\text{insurance choice from individual's problem}} \\
 \bar{F}(w, h, v, a, I', p') = & \begin{cases} 0, & \text{if } I^* = 0 \\ F(w, h, v, a, I, p(h, a)) & \text{if } I^* = 1 \end{cases}
 \end{aligned}$$

$F(w, h, v, a, I, p_0)$  is the value of the insurance firm who is in contract with an individual for insurance premium  $p_0$ , whose wealth is  $w$ , health is  $h$  and so on. Value matching condition at exogenous stopping time for the firm is:

$$\lim_{\tau \rightarrow 1} F(.) = -mq(I) + F(w', h, v', a, I, p) \quad (17)$$

$$w' = w - k(I_0) - m(1 - q(I_0)) \quad (18)$$

$$v' = v_0(a) + Am^{\alpha_m}$$

Free entry condition determines  $p_0$ . Insurance firms can offer health insurance in alternative premium contracts: a) where insurance premium can depend on the health status and b) under ACA where insurance premium cannot depend on health status.