Balancing Growth Versus Other Agendas – The Public Option Example

DOUGLAS HOLTZ-EAKIN | DECEMBER 18, 2020

Eakinomics: Balancing Growth Versus Other Agendas – The Public Option Example

The incoming Biden Administration will face some tricky tradeoffs in constructing its policy agenda. The top priority is protecting American lives from the coronavirus, but until the vaccines provide herd immunity there is a tradeoff between social isolation and the economic activity – especially in the hard-hit leisure and hospitality sectors – that will bring full recovery from the pandemic recession. The Trump Administration has struggled with this issue; how will the next administration differ?

More generally, it is important to remember that social policies are not divorced from the economy. Indeed, since the health sector is just under one-fifth of the overall economy, health policy is economic policy. To get a feel for this, consider the recent work of AAF's Gordon Gray and Chris Holt on President-elect Joe Biden's public option. From a health policy perspective, the proposal is intended to "provide an affordable health insurance choice for Americans by limiting out-of-pocket costs, keeping premiums down, and negotiating better rates from providers and drug manufacturers."

Fine, but how would that happen? According to recent research, it is possible that this would occur by imposing Medicare (i.e., lower) reimbursement rates on providers, while charging actuarially fair premiums. Possible, but inconsistent with history, which instead suggests that reimbursements will migrate toward commercial rates, while premiums will be subsidized (by the taxpayer) well below actuarially fair premiums. If so, the public option would cost an estimated $718 billion over 10 years.

Where does the money come from? Gray and Holt estimate that "such a plan could result in a 0.7 point increase in the hospital insurance tax, a 12.4 percentage point increase on upper incomes, or perhaps some version of a wealth tax, which would cost workers $430 billion in lost wages." It is starting to sound like a serious economic issue, especially when the topline is "0.1 to 0.6 percentage point declines in gross domestic product."

The bottom line is that the public option likely carries a significant economic cost. One might choose to avoid those economic losses at the very moment when the economy is trying to recover from a downturn, especially because it is far from obvious that the public option would solve any real problem. After all, two-thirds of the uninsured are already eligible for subsidized coverage. On balance, the public option is not a good idea.

The tradeoffs presented by the public option will be repeated in broader health policy, climate and energy policy, environmental policy, labor market regulation, policy to address inequality, and beyond. How the new administration makes these decisions will be very revealing.