

Uncertain Health Expenditures and Precautionary Savings: Evidence from the Health and Retirement Study

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Abstract

While it is recognized that uncertainty regarding health status and related health expenses can significantly contribute to a households' future economic circumstances, little attention has been devoted to the role played by health uncertainty and future medical expenses on savings. The theory of precautionary savings predicts that health uncertainty and expectations of future health losses should cause households to increase their savings to account for potential future health expenditures and/or fluctuations in future income due to health conditions. Past empirical evidence of the effect of uncertainty on health care expenses is limited and provides mixed evidence. The goal of this paper is to add to the empirical literature that analyzes the relationship between uncertainty household health and precautionary savings. We utilize panel data from the Health and Retirement Study (HRS) to derive a measure of uncertainty for future health care expenses. Using data from the HRS, we investigate whether household savings are positively correlated with uncertainty in future health care expenses. Accounting for the effect of a possible negative correlation between health insurance on household savings and a positive correlation between income and health care expenses, we find evidence for precautionary savings due to expected future health care expenses.

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