<u>Do hospitals react to increasing prices by supplying fewer services?</u>

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Medical providers often have substantial influence on treatment decisions which they can use in their own financial interest. Classical models of physician-induced demand predict that medical providers will supply fewer services if they face increasing prices. We test this prediction based on a reform of hospital financing in Germany. Uniquely, the German reform changed the overall level of reimbursement prices, with increasing prices for some hospitals and decreasing prices for other hospitals, without affecting relative prices for different types of patients. Based on administrative data, we find that hospitals indeed react to increasing prices by reducing their supply of services.

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