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Brown and Goolsbee (2002)

This paper would like to examine whether the internet made the markets more competitive by using the life insurance industry as a case study. When internet comparison sites for insurance started in 1996, they focused data on term life insurance while the sites of whole life policies did not provide comparison quotes. The study used hedonic type regression methods by using panel data. They obtained insurance data from LIMRA and gathered data of internet users including insurance search from Forrester. The dependent variables included log of annual premium per $1,000 of face value insurance, age dummies, non-smoking dummy, gender dummy, material status dummies, policy rated dummy, state dummies, occupation dummies, own agent dummies, participating policy dummies, length dummies, amount dummies and year dummies. The result indicated that the price of term insurances declined dramatically which was around 8-15 percent from 1995 to 1997 while the price of whole policies remained constant or even rose slightly. It meant that the price would decrease when Internet insurance comparison price sites came online. One important thing was using more internet tended to increase price dispersion first but after the usage has already spread the dispersion will decrease. This result shows that the internet has the ability to reduce search cost and significantly impact on market power. Moreover, it can create huge consumer welfare gains.

I do think the question in this paper is very interesting because it makes me know more about the power of the internet that can create a huge impact on both producer and consumer side. As a consumer, this can help us to get maximum benefit with minimum cost when we invest all purchase any products or services. The economic theory used in this paper was the “Stahl model” which aimed to analyze the impact of search costs and differential information on market price distribution. Further to the Starhl model, they used transaction prices rather than offering prices which showed that customers may have more bargaining power to get the lower prices.

As I mentioned above that this paper used hedonic type regression as a method to answer the question, I think the method is appropriate because hedonic regression is widely used to evaluate the impact of factors on the price. The variables in this regression are appropriate. However it would be better if they include more variables such as family health history and alcohol drinking habit. In summary I think the results are very convincing because they can explain clearly how the rise of the internet during 1995 to 1997 helped make insurance markets more competitive by reducing the price of term life insurances by 8 to 15 percent and lead to enormous gain in consumer welfare.