

Brown and Goolsbee (2002)**Does the Internet Make Markets More Competitive? Evidence from the Life Insurance Industry**

In this research paper, it raises the question that the internet usage may significantly reduce search costs by enabling price comparisons online. So to conclude the hypothesis, they take individual policy-level microdata from LIMRA international on the prices of insurance policy as well as various owners and policy characteristics to match them to microdata on the growth of the internet usage and on-line insurance research from Forrester by the same owner characteristics. In theory, the hedonic regressions for the price of life insurance on characteristics of the policies and the individuals and then include a measure of how likely the individual is to have used the internet over time or to have researched insurance online. The exposition most relevant for our empirical work is that of “Stahl model”.

In this regression will attempt to explain the price paid for term policies. The dependent variable is the log of the annual premium per \$1000 of face value of insurance. As for their controls, they do not have a direct calculation of the survival probability for the individual, so they include standard variables to proxy for it including age dummies, a nonsmoking dummy, a gender dummy, marital status dummies and a dummy for whether the policy is “rated,” meaning that the individual belongs to a special risk class because of some personal behavior. They also include state dummies and occupation dummies to account for differences in health or demographic characteristics across groups that are correlated with life expectancy as well as dummies for whether the policy was purchased from an own agent and whether it was a participating policy. They also include policy length dummies and several terms for the value of the policy in real dollars (these are the log of the real amount, the real amount, and the real amount squared as well as dummies equal to one if the reported value was censored at the maximum value in the year).

According to the result, it can be concluded that at least for some financial products, the ability of the Internet to reduce search costs can have a significant impact on market power. When it does so, it may lead to large consumer welfare gains, potentially at the expense of supplier profits. The implications for the market value of online and offline companies are highly significant.

Reflection on the paper

By looking through this research paper, I find the topic of interest is very interesting and induce me to read more of this paper which it can be because the topic is something that we all have encountered in our daily life and by reading more in this paper would be useful to us. This paper can help us get a better understanding about the market for term life insurance and the correlation of internet price comparison sites that have made the market become significantly more competitive. This research used the Stahl model which has three basic results stated in the Stahl Model that have direct predictions for empirical work. First, when there are asymmetric search costs across customers, firms will draw equilibrium prices randomly from an equilibrium distribution rather than all of them charging a single market price. We should expect to see price dispersion in equilibrium. Second, as the share of customers with complete information (m) increases, the price distribution shifts downward monotonically. Therefore, as the

share of consumers with no search costs increases, average prices should fall and the lastly, the share using the Internet to compare prices on-line rises from zero, price dispersion should first rise and then fall. With these results, we can say that the method adopted to answer research question is appropriate.