

## **Center for Equitable Growth Continuing Student Fellowship**

Project Title : Demand and Supply-Side Behavior in Comprehensive Health Insurance: Evidence from Chile

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With Medicare Part D and the Affordable Care Act, an increasing share of the US population is expected to choose and buy their health coverage amongst a host of private insurance options. Moreover, an increasing tendency towards privatization of Medicaid is expected to substantially increase the proportion of its patients enrolled in private plans. This tendency raises several policy questions and concerns about equitable growth as to what are the long-run consequences of this shift for the currently uninsured, poor and old.

In this project I study the health insurance market of Chile, to answer several questions related to the provision of health insurance by private insurance companies. Chile is an ideal case of study since almost 20 percent of the population buys comprehensive health insurance plans in the private market. I study both individual's choices and firm's pricing strategy in a static and dynamic way.

My preliminary findings show that individuals exhibit substantial search costs, of on average 30% of the premium. Also, I find that coverage choices are inconsistent with future plan utilization. In particular, individuals tend to over-insure, which is consistent with previous evidence from the home insurance markets (Sydnor, 2010). Finally, I provide evidence of little switching over time, especially among individuals that face negative health shocks.

I argue that health insurance companies respond to the three features of the demand outlined above. Consistent with search costs, I show substantial price dispersion. Also, more generous plans are priced at a premium that cannot be explained with utilization or moral hazard. Finally, I show evidence that the evolution of prices and introduction of new plans is consistent with insurance companies risk-rating their plans dynamically. Using claims data I can test the hypothesis of risk-rating over alternative interpretations of the observed dynamic pricing strategy, like invest-then-harvest pricing (Farrell and Klemperer, 2007, Ericson, 2012).

This features of the demand and supply are likely to substantially decrease the ability of individuals to effectively insure against negative health shocks. The goal of this paper is to quantify this welfare loss, and investigate the welfare impact of potential policy reforms.

Besides its relevance for understanding the future of health care in the US, studying

the Chilean market is interesting in its own right. A currently debated health reform in Chile would require private companies to introduce a homogeneous plan covering most of diseases and abolishing pricing on preexisting conditions. This counterfactual situation would effectively eliminate sources of optimization frictions, like search and switching costs, and the ability of firms to risk-rate their plans. I expect that this paper will shed light on the overall desirability of such reform, taking into account endogenous supply-side reactions that are expected to occur.

## References

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