Problem Set #2

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Problem 1 Critical review computational approach to answering research question.

Part (a). The research question of "Understanding the Advice of Commissions-motivated Agents: Evidence from Indian Life Insurance Market" is: How is the quality of advice provided by life insurance agents in India? To be more specific, the researchers studied how does features of customer interactions, insurance agents? self-understanding of the products, and commission disclosure regulation affect life insurance agents? offerings of advice on whole-life products versus term-life products to customers.

Part (b). To answer the question, the paper mainly uses the data developed by their original field experiments and follow-up surveys in India. To be more specific, the data for the empirical analysis comes from in-person audits of life insurance agents beginning in 2010, with a follow-up survey of life insurance agents occurring in 2014. More information about their dataset can be found here in their replication instructions. (Data Replication)

Part (c). In order to interpret the data, the paper reference to recent theoretical work on the provision of advice to potential customers. The paper tests two types of predictions that arise from this class of models. The first set of predictions concerns the quality of advice provided by commissions-motivated agents. These models predict that at least some consumers will receive low-quality advice encouraging a complicated product that has higher commissions but no real benefits to them (Inderst & Ottaviani, 2012c; Gabaix & Laibson, 2006). The second set of predictions relates to how regulation and customer types affect the quality of advice. A key feature of the recent theoretical models in Inderst & Ottaviani (2012c) and Gabaix & Laibson (2006) is the presence of two types of customers, with different levels of sophistication. Details of the theory and the paper's adjustment can be found in the Online Appendix. (Online Appendix.) Beside this, the paper also test the theory raised by Inderst & Ottaviani (2012c) that disclosure requirements can improve the quality of advice by essentially converting unaware customers into customers who are aware of how commissions can bias advice. The researchers studied a particular type of insurance product(ULIP) and test it using the data collected from the natural experiments mentioned in Part (b).

Part (d). Therefore, this paper is a combination of a descriptive study, an identification exercise and a numerical solution to system of equations study. First, they developed their own data sets as stated in Part (b); Second, they set up theoretical framework and built two models of a Dominated Financial Product and solved them. One is Monopolist Insurance Company and the other is Two Competing Insurance

Companies. These models and their solutions can be found in their online appendix. (Online Appendix.) (They did small adjustment and fitted the model to their data, thus, I think the paper also include numerical solutions to system of equations study) Third, they did empirical analysis based on the two types of models and use the the data developed by their natural experiment to test the theories mentioned in Part (c). Thus, I think this paper is a combination of the three.

Part (e). As stated in Part (d), to answer the research question, the paper run a series of audit studies (Computational Methods: doing experiments, adjusting and testing theoretical models. When testing models, the paper use simple statistics and simple data visualization, see appendix, along with regression methods.) to evaluate the quality of advice given by life insurance agents and find that life insurance agents provide poor quality advice: (1) they often recommend a dominated product, (2) they cater to customers' preconceptions of what the right product is even conditional on objective information about what the right product is, and (3) they compete by suggesting term insurance in addition to, as opposed to as a substitute for, whole insurance, which is a difficult decision to rationalize objectively. Besides answering the research question, the authors also find some speculative evidence: first, customers who report having received poor recommendations from another agent in an earlier visit are more likely to receive advice to buy term insurance; second, requiring disclosure of commissions on one particular product led to that product being recommended less.

Part (f). My suggestions are:
(1) The sample size of the paper's follow-up survey is too small. The authors conducted their survey only with 32 life insurance agents. It is highly possible that some of the agents responded to the survey with bias. When the sample is that small, the quality of the data is poor. So it would be better if the authors enlarge their sample.
(2) For the theory part, the paper uses the model of a Dominated Financial Product and only takes two cases into account. One is Monopolist Insurance Company and the other is Two Competing Insurance Companies. Thus the authors only examined the policies offered by the Life Insurance Corporation of India and by ICICI Pru. Actually, given the information that the price of insurance doesn't follow the one price law in India market, it would be more realistic that the authors take into account that what if the market is stratified, there is a monopolist company that offers insurance along with better service and credibility while there are serval competing companies that offer the similar life insurance. In this case, it would be better if the authors did experiments among more companies and find out whether agents in different insurance companies offer advice with different qualities.