On the Efficiency of a Public Insurance Monopoly: The Case of Natural Hazard Insurance in Switzerland

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1 Introduction

Privatisation of Public Enterprises: Telecom, Railways, etc., but:

- **Different success**
- **Public Resistance: Privatisation of a Waste Incinerator, Basel-Landschaft, 1995**

Housing Insurance in Switzerland against Fire and Elementary Damages:

- **Private insurance companies in 7 cantons and Liechtenstein Institutions (Switzerland)**
- **Public monopolies in 19 Cantons**
- **Strong claims for privatisation**

4 Arguments in favour and against privatisation (2)

Experiences in Germany

- **Public monopolies existed in several states (Baden-Württemberg, Hamburg)**
- **Abolishing of these monopolies due to a decision of the Commission of the EU in 1991**
- **Strong increase of the insurance premia after the privatisation**

Canton Zürich (1998/99)

- **Parliamentary initiative to privatise the cantonal insurance company**
- **120 out of 129 local communities voted for keeping the cantonal monopoly**
- **77.4 percent of the people voted for keeping the cantonal monopoly**

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2 The empirical evidence

Table 1: Premium Rates

ct / 1000 CHS insurance value, ten-years average 1984 – 1993

	Public Monopolies		Private Insurers	
	absolute	relative (in percent)	absolute	relative (in percent)
Damages	**32.8 ct**	**51.3**	**55.1 ct**	**50.6**
Administration	**6.0 ct**	**9.4**	**14.1 ct**	**12.9**
Acquisition	**—**	**0.0**	**16.9 ct**	**15.5**
Prevention	**13.4 ct**	**21.0**	**6.0 ct**	**5.5**
Reserves	**11.7 ct**	**18.3**	**16.9 ct**	**15.5**
Total Premia	**63.9 ct**	**100.0**	**109.0 ct**	**100.0**

Source: TH. V. UNGERN-STERNBERG (1995)

2 The empirical evidence (2)

$$\ln(PR) = \underset{(5.56)}{0.382} + \underset{(7.89)}{0.555}\ln(DR) - \underset{(3.42)}{0.196}\,DVCM + \hat{u},$$

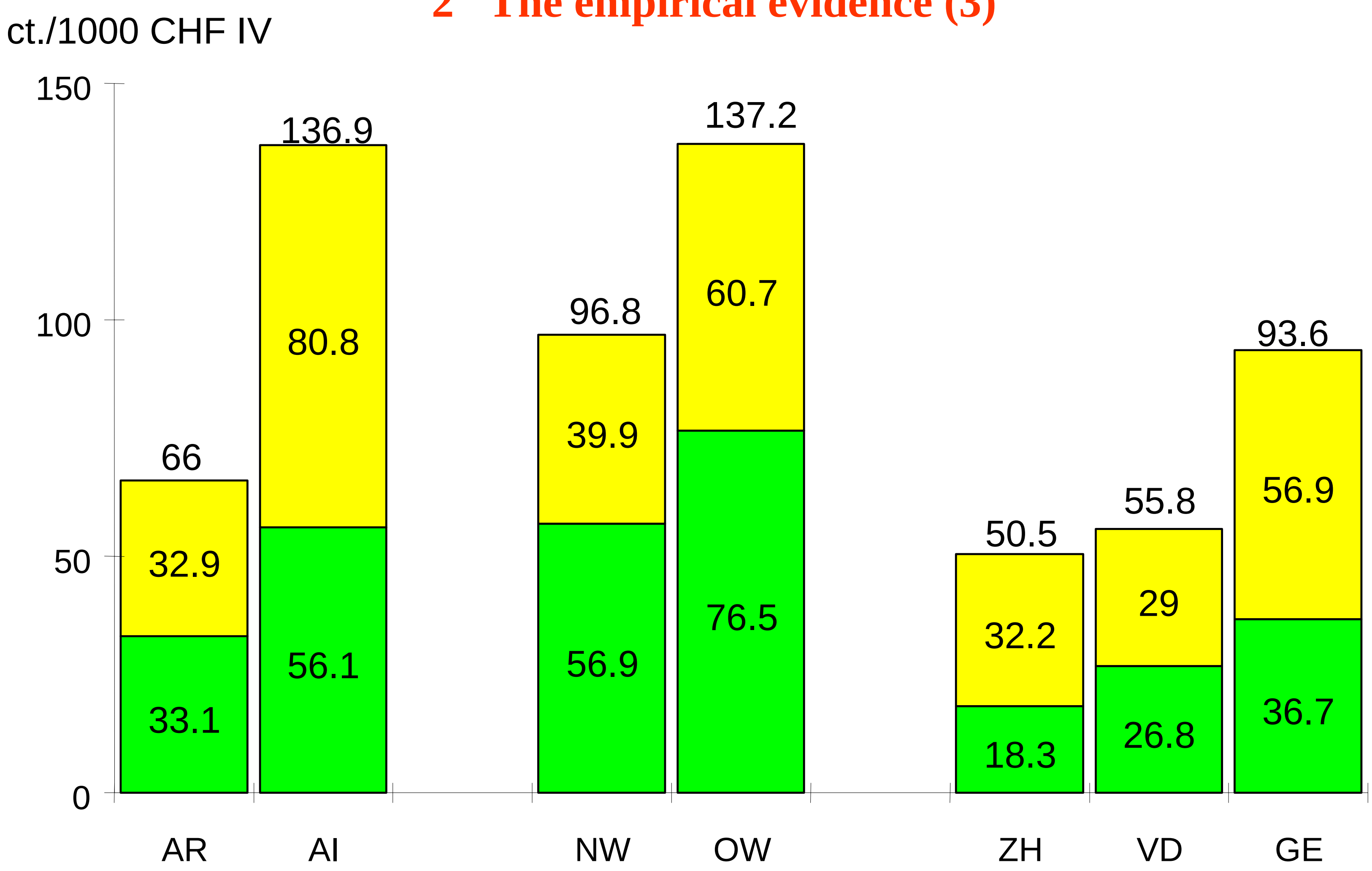
$$\bar{R}^2 = 0.662, \; SER = 0.183, \; J.\text{-}B. = 0.579, \; DF = 23,$$

with

PR	**Premium Rate (ct./ 1000 CHF insurance value)**
DR	**Damage Rate (ct./ 1000 CHF insurance value)**
DVCM	**Dummy Variable: DMC = 1.0: Public Monopoly** **0.0: Private Insurer**

⇒ **Public monopolies are – ceteris paribus – about 20 percent cheaper than the private insurers.**

2 The empirical evidence (3)



Damage costs, mark-ups, and total premium rate in selected cantons

3 Why are the public monopolies cheaper?

3 Main reasons:

(i) No acquisition costs $\Rightarrow$ lower administrative costs

- **Public Monopolies: 6.0 ct. / 1000 CHF insurance value: 9.4 percent of total premium**
- **Private Insurers: 31.0 ct. / 1000 CHF insurance value: 28.4 percent of total premium**

(ii) Stricter fire prevention due to higher prevention expenditure

- **Prevention as a public good for private insurers**

(iii) Less moral hazard

- **Higher damages in cantons with private insurance**

  Reasons: a) Private insurers are primarily working in mountain cantons

  b) Private insurer agents are more generous

4 Why privatise?

(i) Static Efficiency

but: **No acquisition costs in a monopoly**
Problem of regulating a private monopoly

(ii) Dynamic Efficiency

– **Private firms more innovative,**
but: no technical progress

(iii) Risk based premia

– **Cantonal monopolies: Unitary premia,**
i.e. the same rates for all buildings (e.g. Zürich)
but: higher rates for most clients

4 Why privatise (2)

(iv) Covering Cantonal Debt (Luzern)

(v) Compatibility with EU norms

(vi) Liberal economic order

Only those activities should be performed by public enterprises which cannot be performed by private firms, independent which firms are more efficient.

5 Concluding remarks

Conclusions:

(i) Public monopolies are more efficient

(ii) Precondition: Yardstick competition between cantons

(iii) Other areas of insurance, e.g. health?

Tank you very much for your attention.