

Ounces of Prevention and Pounds of Cure

by Robert Gibbons

Did America become rich because of the wealth of natural resources the continent contained, or the extent of its fertile soil, or the continual infusion of new streams into the population, or the unique American character? Explanations of economic growth usually focus on visible factors, especially big ones like factories and dams. Also important, however, are invisible factors like business practices and social expectations. There is a crucial difference among the peoples of the world in their level of economic security. More than just the difference in income, their vulnerability to unanticipated events frustrates progress in poorer countries.

Thus America has no better examples of success stories that can help developing countries than its insurance companies. On March 25 the Philadelphia Contributionship for the Insurance of Houses from Loss by Fire celebrates its 250th anniversary. Benjamin Franklin was among the founders of this new company, and he vigorously promoted it because—like the Library Company, the University of Pennsylvania, Pennsylvania Hospital, street paving, street lighting, and many similar civic improvements—it served “the good of mankind.” Never satisfied with things as they were, Franklin advocated new practices such as smallpox inoculations and lightning rods because they made life healthier and more secure. Insurance was yet another application of useful knowledge to a serious problem.

In 18th century cities fire was perhaps the greatest peril, and Franklin obviously recognized the danger. Poor Richard's Almanac noted regarding September 2 that on that date in 1666 “began the fire of London, which reduc'd to ashes 13,200 houses and 89 churches: Near ten times as much building as Philadelphia.” Franklin's famous saying, “An ounce of prevention is worth a pound of cure,” first appeared in a newspaper editorial “On the Protection of Towns from Fire.” According to Franklin's *Autobiography*, the prevention of fires was a regular subject of discussion in his circle of friends. Each month they considered new ideas, such as improving the night watch so that fires might be discovered more quickly.

In 1750 the Union Fire Company, a volunteer fire-fighting unit and social society Franklin had organized in 1736, proposed establishing a fund “to make up the damage that may arise by fire among this company.” This proposal led to the formation of the Contributionship, modeled after London's Hand-in-Hand society.

The earliest known fire insurer in America, organized in Charleston, South Carolina, in 1735, folded as a result of a fire on November 18, 1740, that destroyed three hundred houses, over half the town of Charleston. The Contributionship avoided the same fate because Franklin's knowledge of fires improved the management of risk in Philadelphia.

Although wooden houses were accepted at first, after 1769 the Contributionship insured only brick houses within ten miles of Philadelphia, and then for no more than 500 pounds. Each property was inspected and individually rated. The Contributionship accepted no sugar houses, brew houses, bake houses, coopers shops, or shops conducting hazardous trades such as apothecaries, chemists, ship-chandlers, tallow chandlers, or stable keepers. Also ineligible were buildings used to store hemp, flax, tallow, pitch, tar, turpentine, hay, straw, and fodder. The Contributionship's underwriting standards and loss prevention measures made it a successful insurer.

Franklin's concern for the danger of fire continued even in the midst of his travels to London and Paris. Everywhere he went, he spread his ideas for preventing fires by building houses with masonry chimneys, copper roofs, and nearby water supplies. As he wrote to his daughter in 1771, “If I were to build again, I would contrive my House so as to be incapable of burning, which I think very possible and practicable.”

Franklin recognized fire's threat to civic well-being. His practical approach was to prevent fires when possible, and when not, to help the victims recover. We now celebrate the 250th anniversary of both the lightning rod [a loss control device] and the insurance company [a loss financing device] because Franklin's experiments with electricity were motivated by his desire to understand lightning and alleviate it as a cause of fire.

Robert Gibbons is Executive Director and President of the International Insurance Foundation. He presented these remarks at the Benjamin Franklin Birthday Celebration in Philadelphia on January 17, 2002.

For developing countries today the gravest perils are natural disasters rather than fires, but the same principles apply. In the aftermath of hurricanes, floods, and earthquakes, relief agencies have marshaled tons of assistance, or at least pounds of cure to help the victims. So far, however, the world has seen fit to offer few ounces of prevention. The combination of civic cooperation and individual freedom that enabled 18th century Philadelphians to find the most efficient solutions to their exposures to accidental loss can help everywhere. Robust, private insurance markets can make an enormous difference in lifting billions of people out of poverty. Insurance, banking, and capital markets are integral parts of the healthy financial sector all economies need to facilitate economic progress.

Insurance firms help to channel funds to productive investments, but far more important is their value in analyzing risks, revealing the costs, and helping people make better decisions. Price signals from the insurance market lead to more efficient allocation of resources. Seat belts save lives. Smoke detectors save lives. Factories are safer places to work when there are guards on the cutting tools. It is thanks to the insurance industry that we know these things, and it is thanks to the insurance industry that people have economic incentives to adopt safety measures. This analysis of risk is the insurance industry's main contribution to American economic growth.

Americans now spend close to nine percent of gross domestic product on insurance products that help them recover from accidental losses and premature deaths. They invest in techniques that reduce their insurance premiums, but also reduce losses in the aggregate and leave more resources for productive purposes. As insurance has grown, the country has become safer and more prosperous. Accidents and natural disasters still happen, but they rarely disrupt the American economy as much as in developing countries.

Two recent natural disasters illustrate this economic security gap. When Hurricane Andrew destroyed thousands of buildings in 1992, insurance financed the rebuilding and Florida's economy was soon humming again. In 1998 Hurricane Mitch, a storm of similar force and extent, set Honduras's economic development back 25 years because funds intended for schools and public works were diverted to rebuilding.

Ten countries, where only twenty-two percent of the world's people live, have nearly ninety-percent of the world's insurance. The rest of the world has little defense against the vicissitudes of nature. Ninety-five percent of all deaths from natural disasters occur in developing countries. Total losses from natural disasters relative to GDP are twenty times greater in developing countries. For these countries, the problem is not just that they are poor; it is that they have more difficulty overcoming poverty because they are so vulnerable to unanticipated events.

So when American insurance experts ask, as Franklin did, "What good can I do this day?," the answer is clear: Let us help developing countries create the institutions of a free insurance market. Ounces of prevention for sound risk management of natural disasters will do far more good than the pounds of cure sent for post-loss relief.

Benjamin Franklin would agree. Following Cook's first voyage to the South Pacific, Franklin proposed a new voyage

to visit a distant people on the other side of the globe, not to cheat them, not to rob them, not to seize their lands or enslave their persons, but merely to do them good and make them, as far as in our power lies, to live as comfortably as ourselves.

For Franklin this dissemination of useful knowledge was not so much an act of charity, but of utility. As he pointed out,

a commercial nation particularly should wish for a general civilization of mankind, since trade is always carried on to much greater extent with people who have the arts and conveniences of life....We may therefore hope in this undertaking to be of some service to our country, as well as to those poor people who, however distant from us, are in truth related to us, and whose interests do, in some degree, concern every one.

For the American insurance community, backed by 250 years of experience, what could be more useful than to share our knowledge of risk and how to manage it with those whose lives would become safer, more stable, and more prosperous as result.