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FEATURE ARTICLES

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Now that the benefits of financial services for the poor are more universally recognized and accepted, and microcredit is becoming a common tool in the infrastructure of developing countries, it is a good time to look at another beneficial tool for the building of sustainable infrastructure in the developing world. Like microcredit, microinsurance has the potential to significantly aid the lives of the world's poorest people and positively impact the development of the world's poorest countries.

"Microinsurance is simply the protection of low-income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of the risk involved. This definition is essentially the same as one might use for traditional insurance except for the clearly prescribed target market: low-income people. However, those three words make a big difference."¹

A Brief History

Microinsurance, as a distinct field of development practice, is a relatively new phenomenon, though its roots go back for more than a century. In the early 1900's, selling industrial insurance at factory gates on payday made the Metropolitan Life Insurance Company not just the largest insurance company, but the largest company of any kind in the world at the time. This "industrial insurance" was an important step in building an insurance culture and had a significant role in building a sustainable infrastructure for economic development. Simply put, people who had insurance against risks have proven more likely to engage in higher return activities and are thus more likely to end the cycle of poverty.

Industrial insurance was the forerunner to today's partnership model that is a feature of commercial insurance. The transition from collecting premiums at the factory gates to group policies significantly

enhanced the cost-effectiveness of the insurance coverage. As a delivery chain, employers found a benefit in bundling premiums for insurers not only by being able to develop a consistent and sustainable workforce through an employee benefit but also by mitigating some of their own risk, thus being able to engage in newer technologies and benefiting from participating in activities with the potential for higher yields. The practice of bundling premiums has not just made civilized life possible but also made it affordable.

Why Microinsurance?

Because their resources are so limited, low-income people can experience great financial disruption when unexpected events befall them. Due to the same limited resources, low-income people have limited capacity to prepare for the eventual but inevitable events. If the breadwinner is injured or falls ill there is not only the loss of work and income but also the prospect of not even being able to seek treatment without payment up front. That leaves the family with three choices: seek a loan from a friend or family member, forego treatment, or deplete family resources, including selling productive assets. If they seek a quick loan they risk unreasonable payment demands and costs that could still leave their assets in jeopardy.

No matter what decision they make, the breadwinner could still die. Then not only would there be funeral expenses to be paid but also the continued up-keep for the family. A low-income family's property may be limited to just a few animals or crops and a modest shelter but the loss of any of these can be devastating to a family's economy.

Low-income families will often be forced to execute strategies that will even further jeopardize their ability to be productive. These strategies can include harsh choices such as reducing food consumption, withdrawing children from school or selling productive assets. Thus, the cycle of poverty is perpetuated onto the next generation.

¹ Protecting the Poor: A Microinsurance Compendium. Craig Churchill, ed. ILO, 2006

In developing countries, even a small amount of insurance can prevent a household from falling further into poverty. Yet in developing countries there are very few insurance products that appropriately respond to the needs and real risks of low-income families.

From the point of view of insurers, however, small sums insured mean small premiums and low profit margins. Thus microinsurance has to be well administered, cost-efficient, and delivered on a large scale if it is to benefit the poor, and those who provide the microinsurance.

The study upon which this paper is based was conducted to understand what microinsurance is available to low-income people in the world's 100 poorest countries.

The Microinsurance Supply Chain

As with microcredit and savings, microinsurance does not occur in a vacuum. When looking at the landscape of microinsurance, it is thus important to recognize the roles and activities of the participants in the supply chain. The microinsurance supply chain is made up of five components:

- Reinsurers—provide insurance to insurers for catastrophic risks
- Insurers—carry the insurance risk
- Delivery channels—sell the insurance policy and provide basic servicing
- Policy holders—buy the product (can be individuals or groups)
- Covered lives—those who benefit from the cover (normally family members, or group members for group policies)

All of this is underpinned by regulation and supervision, as well as support in part by donors.

Reinsurance does not yet play a big role in microinsurance. Microinsurance tasks are essentially shared between the insurer and the delivery channel. It is crucial to understand the distinction between insurer and delivery channel. The *insurer* is the one who carries the risk, finalizes the premium and product design, and ultimately pays claims. The *delivery channel* sells the product and provides after-

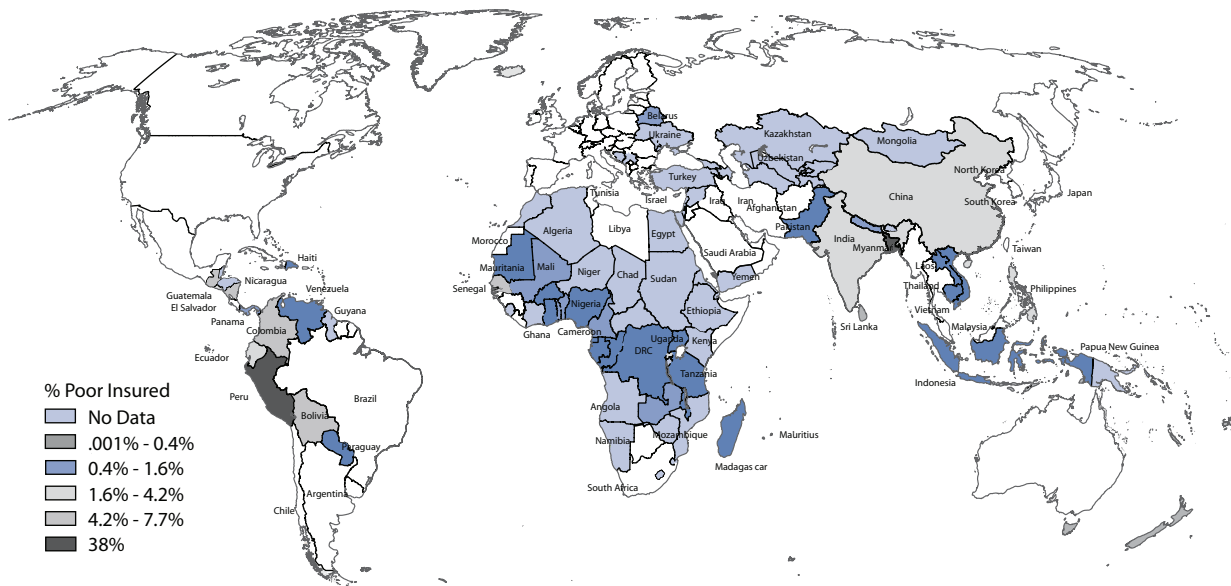
sales service. Insurers can range from multinational or domestic commercial insurers, to member-owned mutuals, non-governmental organizations (NGOs) or community-based organizations (CBOs), or even informal groups. Delivery channels are those who are in contact with the policyholder. These work best when they are organizations close to poor people—such as churches, trade unions, microfinance institutions, retailers, NGOs, or CBOs. It is possible for one entity, whether an insurance company, NGO or CBO, to be both the insurer and the delivery channel, but the distinction between these two functions still remains. In practice, however, CBOs tend to be good delivery channels but poor insurers, because they do not have professional insurance staff.

The Landscape Survey

The study gathered primary and secondary information from almost 600 sources and identified almost 360 individual microinsurance products, plus 116 social security schemes, being offered through 246 microinsurers, and covering the lives of over 78 million people. Some organizations refused to provide information, and certainly there are others that were unknown to the team even after extensive searching.

Several tendencies stand out in the landscape data. These include:

- The dramatic effect of insurance regulation introduced in India in 2001, which has pushed microinsurance out into the rural areas and towards the poor. Over 30 million low-income people are covered by over 130 products in India. However, as one might expect from regulation-enforced targeting, not all these products actually benefit the poor.
- A noticeable lack of microinsurance in North Africa and the Middle East. In no other region is the absence of microinsurance as evident.
- Weak delivery channels hinder the advancement of microinsurance. Though retail models are beginning to be implemented, only 1.8 million (2%) of the people covered by microinsurance are covered by products delivered through retail intermediaries. Broker activity in microinsurance is almost non-existent.
- Considering that microinsurance products and services were found to cover 78 million lives, donor activity has been miniscule. The



gross value of donor investment per covered life works out to be about US\$ 0.12 for the few who are covered.

- Most microinsurance programs identified were found to be very small measured by numbers of policyholders.

Microinsurance Landscape Map

That microinsurance for the world’s poor is expanding rapidly clearly emerges from the landscape survey. Most of this recent growth comes from the private sector. The microinsurers surveyed were positive about the future, predicting at least 10% growth over the following year and 100% growth over five years. It could be argued that this is relatively easy, given the low volume base of microinsurance currently, but it does also mean that microinsurers are realistically optimistic about the prospects of growth in a huge un-served market.

It is critical to remember that these volumes of microinsurance products and schemes neither reflect product quality, nor the value for money (or lack thereof) that these products offer.

Microinsurance Products — Opportunities and Barriers

The landscape survey found that the highest demand from poor people was for health products and life products, followed by property insurance and accidental death and disability (AD&D) cover. The

research team found that covered lives for these products were 6.8 million for health, 35.3m for life, 12.6m for AD&D and 7.8m for property.² The potential market is much larger, up to 30 times larger for all products.

Before microinsurance can be made available on a vast scale, a number of barriers have to be overcome. Some barriers are external constraints and delivery barriers, some are shortcomings of existing products, some are related to people’s perceptions about insurance in general, and finally others are related to insurance regulations or their absence. For example:

- *Health microinsurance:* the poor physical and administrative condition of many health care facilities in the world’s poorest countries makes the quality of health care and the management of health insurance schemes very difficult. Certainly health insurance is a very risky business in any market. This fact holds back many insurers from offering such covers. However, there are emerging examples of health microinsurance that can be successful for low-income households as well as insurers and delivery channels.

² These values, as well as the tables Health and Life Insurance by Sub-Type, exclude 28.3 million lives covered by the All China Federation of Trade Unions. These people have limited cover under all four general insurance types. They are excluded here because of the distortional impact from this one program. Additionally, several organizations offer composite products that include a combination of the four microinsurance products identified here. Therefore the product use totals are greater than the basic number of covered lives.

Health insurance by sub-type		
Product sub-type	Number of Products	Covered Lives (millions)
Comprehensive	38	0.79
Health (Other)	8	1.80
Hospitalization	66	3.34
Primary	79	3.48
Targeted Benefits	40	0.79
Total	231	10.20

- *Life microinsurance*: most existing products are of poor quality, and most are linked to credit schemes (credit life insurance) and are designed to protect the lender should the borrower die. Commonly, policyholders of these products note that credit life insurance is not for them, but for the institution. Better quality products, which meet the demands of the low-income market with a positive value proposition, are needed. Products which truly assist the family with continuing coverage after the death of the breadwinner were cited as primary needs of low-income families.

Life insurance sub-category		
Product sub-type	Number of Products	Covered Lives (millions)
Credit Life	103	23.19
Credit Life Plus	11	0.03
Endowment	16	1.23
Funeral	18	3.05
Investments	1	0.07
Pensions	14	0.03
Term	19	1.49
Continuing Family benefits	2	n/a
Total	184	29.09

- *Property microinsurance*: it is difficult, especially given the tight margins, to control policyholder fraud and moral hazard (the tendency to be less careful with insured property). This is commonly cited as a reason for limited property covers.
- *Delivery channels*: these are probably the biggest single constraint to massive microinsurance expansion. Existing delivery channels often do not see the opportunities in microinsurance or recognize the secondary benefits (for example, microinsurance

Delivery channels by type and covered lives	
Delivery Channel Type	Covered Lives (millions)
Agents - microinsurance or other	7.57
Brokers - microinsurance or other	0.29
CBOs, NGOs and other groups	25.64
Employer groups	0.18
Government and Parastatals	11.82
Mutuals	13.80
Other financial services (e.g. MFIs)	17.00
Retailers of other service providers including funeral parlors	1.76
Not specified	0.44
Total	78.50

would make their clients more stable financially). They tend rather to focus only on how insurance benefits their institution (for example, commissions and portfolio protection). Few delivery channels acted as "brokers" for their clients, but those that did offered an array of client driven products and services, potentially providing the foundation for extensive growth.

- The study attempted to draw a correlation between microinsurance and microfinance provision. There was no direct correlation between the two. Although MFIs could make very appropriate delivery channels, their impact on microinsurance is still limited. Growth and expansion, thus far, appear to have been related to regulatory issues (such as in India), prompting by donors (such as the large number of community based health insurance programs in West Africa) or by individuals within delivery channels or insurance companies themselves that had the vision to push for insurance products for this market.
- *Market barriers*: Low-income household's lack of access to insurance is something of a vicious circle, as it leads to limited understanding or negative attitudes. More effort needs to be made to improve the image of insurance in general, and commercial insurers need to overcome their stereotypes of the low-income market and, as has been done with microcredit, recognize that the market is both profitable and reliable. Significant market education will be needed to prepare the markets for good quality value for money products.

- *Regulatory barriers:* Insurance regulators can be a constraint to microinsurance because they do not address specific microinsurance needs – for example simplicity in language of policies and documents. It is dangerous for consumers to be insured with unregulated insurers who hold insurance risk without reserves or reinsurance. Too frequently this has led to poor people not only losing their premiums but experiencing the full consequences of catastrophe – for health insurance, being refused treatment and possibly dying; for property insurance, losing their homes; and for life insurance, the family being left destitute. However, microinsurance in low-income markets of developing countries remains a relatively new phenomenon. Best practices have not been identified because it is still too early. The key task for supervisors will be to balance their primary role as consumer protectors against the need to allow flexibility in products and processes in order for the market to develop. Too much restriction will simply lead to a regulated lack of access to microinsurance.

Types of Microinsurers

The landscape survey identified four main types of microinsurers:

- *Commercial insurers* (38.0m covered lives identified). These are specialist insurers already operating in the broader insurance markets. They are professionally managed and registered under insurance regulations. Being regulated, they maintain reserves and have access to reinsurance, and their consumers are better protected. Commercial insurers are showing a rapidly growing interest in microinsurance, seeing it as both profitable and contributing to corporate social responsibility objectives. Commercial insurers prefer to partner with outside delivery channels in the low-income market but are hampered by a lack of potential partners.
- *NGOs* (9.8m covered lives identified). Non-governmental organizations include development organizations, trade unions, federations of groups, and microfinance institutions. They are close to poor people and therefore close to the market for microinsurance. They are unregulated and less professionally skilled than commercial

insurers. They are potentially very effective delivery channels.

- *Mutual insurers* (2.5m covered lives identified). Mutuals are professionally-managed, regulated member-owned insurers, sometimes owned by credit unions or cooperatives. They have the advantage of operating close to poor people, and are experienced in financial activities, disbursements, and confirmation of events.
- *CBOs* (0.7m covered lives identified). Community-based organizations are member-owned and member-managed, and very close to low-income people, who may often be their members. Their closeness to the market makes them good delivery channels. Their great disadvantage is that they are unregulated and lack the professional insurance management experience to be stable and effective insurers.

Insurance Regulation

Insurance regulators in all countries play a vital role in the industry, as their ultimate objective is consumer protection. Supervisors ensure that each insurance company complies with the country's insurance laws and policies, and that each insurer maintains adequate reserves and reinsurance to satisfy any claim. The presence of effective supervisors can boost consumer confidence. Regulation and regulators are not, however, geared to microinsurance in a number of ways:

- *Agents.* Regulations usually require all those who sell insurance to be licensed in their individual capacities. This means classes, examinations, and fees. Once licensed, an agent has an incentive to focus on the more profitable upper-end of the market. Institutions such as NGOs would not be allowed under most current regulations to act as agents because they are not individuals, yet it is difficult to expect such institutions to license each of their field staff as insurance agents to sell simple microinsurance products.
- *Supervisor capacity.* In developing countries, insurance supervisors are often under-funded and under-skilled. Converting currently unregulated CBOs and NGOs to regulated bodies will be difficult for supervisory

authorities to manage, even if special microinsurance regulations are introduced with lower supervision and reporting requirements.

- *Policy documents and language.* Policy documents are often required to contain “fine print” that low-income people do not understand. Simpler policies would help improve policyholder confidence, and improve efficiency.
- *Minimum capital requirements.* Regulators typically require insurance companies to hold a minimum capital of over US\$1 million. This level of initial capital would be onerous for CBOs and NGOs wishing to convert to regulated insurers, or for other insurers focusing specifically on microinsurance.

The research team did find that some initiatives were attempting to address regulation issues. The International Association of Insurance Supervisors is working with the CGAP Working Group on Microinsurance to address microinsurance issues within their Insurance Core Principles. A document prepared by the IAIS-CGAP working group entitled “Issues in the Regulation and Supervision of Microinsurance” was approved by the IAIS in June 2007. This will assist individual jurisdictions in assessing their own regulatory and supervisory status as it relates to microinsurance.

Three countries – India, Peru, and the Philippines – have passed microinsurance regulations. Several other countries including Mexico and South Africa are working towards microinsurance regulations.

Conclusions

Though insurance for low-income populations goes back to the earliest days of the insurance business, microinsurance for the low-income markets in developing countries is clearly in its nascent stages. This study has identified over 78 million low-income

people microinsured in the 100 poorest countries of the world. It has also shown that most of these products show limited quality for the low-income market. The most prolific microinsurance type identified was credit life being offered by credit granting institutions. Although credit life satisfies basic demands of the credit institutions (profits and portfolio protection), and the insurers (profits), low-income policyholders typically scoff at such products as self-serving by the creditor. These do not likely build an insurance culture and is often antagonistic to such a culture as the products are commonly compulsory and are seen as an additional cost of obtaining credit.

The study showed an important mismatch between what is being supplied – credit life – and what low-income people say they need – hospitalization and cover beyond the funeral in the case of the death of a breadwinner.

Although pricing information was frequently not provided to the researchers, it was also clear that in many cases microinsurance premiums were inflated to levels that provide continuing excessive profits to insurers and delivery channels, with limited value to low-income households. This is partly the result of the limited amount of risk information, prompting significant loading of premiums, the lack of delivery channels that would normally push for better products and premiums for their clients, and a lack of market competition. Several institutions, especially some of the larger MFIs in areas where there is market competition among insurers, have successfully improved the value for money proposition for their clients, and in several other countries competition is beginning to result in better products and premiums.

At least 78 million people are covered by some form of microinsurance. The market is at least a billion and maybe as much as 2.5 billion. We have just begun to touch the potential of microinsurance. Ideally, as we look forward, we will see masses of low-income people covered by insurance products that truly help them to manage their risk and secure their futures.