

THE STATE OF MICROINSURANCE

THE INSIDER'S GUIDE TO UNDERSTANDING THE SECTOR



micro
insurance
network

2015

With insights from Access to Insurance Initiative - Adamjee Life - Allianz - AM Best - Bradesco Seguros - Geneva Association - Grameen Crédit Agricole Microfinance Foundation - ILO's Impact Insurance Facility - Inclusivity Solutions - MicroEnsure - MicroInsurance Centre - Star Microinsurance - Stonestep

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Summary

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11th International Microinsurance Conference 2015

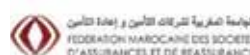
3–5 November 2015, Casablanca, Morocco

Driving growth and sustainability –
A business case for microinsurance



The 11th International Microinsurance Conference will take place in Morocco from 3–5 November 2015. Approximately 400 participants and experts from around the world will discuss and identify ways of accelerating growth and economic viability in microinsurance. The conference will be hosted by the Munich Re Foundation, FMSAR and the Microinsurance Network, supported by CIMA, the CEAR, ILO's Impact Insurance Facility and Making Finance Work for Africa.

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Editorial



Marco Antonio Rossi

President of Bradesco Seguros Group
President of the Brazilian Insurance Federation (CNseg)
President of the Inter-American Federation of Insurance Companies (FIDES)



Bradesco Seguros



FIDES
Federación Interamericana
de Empresas de Seguros

“ The Microinsurance Network is leading the sector in bringing together key figures from the microinsurance sector to facilitate open dialogue, generate and share knowledge. “

Though 263 million people are covered by microinsurance worldwide, the microinsurance sector is still nascent and we continue to test and to learn. The problems and risks facing low-income populations are vast and complex. Offering microinsurance to these segments brings with it all the complexities of their daily life which need first to be understood and then addressed by microinsurance stakeholders; education levels, household budgeting, behavioural economics, choice, priorities and inconducive infrastructure to name but a few. These barriers change from community to community, from region to region and are often vastly different to those faced by the more traditionally served clients in developed insurance markets.

These difficult and persistent barriers have necessitated innovation, particularly in the distribution of products, using alternative channels and finding new partners. Technology is playing an ever-greater role in innovative distribution, with millions of customers now accessing insurance through mobile network operators. Insurance is also available in corner shops, through utility bills or bundled with other financial services or agricultural inputs. In a move to reduce the administrative costs, technology that streamlines claims validation has pioneered the index-based insurance movement.

Because of the complexities involved, and the continuous emergence of new microinsurance programmes and products, it is of utmost importance that we in the sector exchange knowledge, sharing experiences of what has worked and what hasn't, to encourage and facilitate innovation. It is vital that we continue to learn from one another with one goal in mind: a sustainable microinsurance sector which protects low-income populations from risk. That we are given the space to interact with one another, a platform to disseminate information, to ensure that failures are in fact as useful in acquiring knowledge as successes, that there were no wasted opportunities. Innovation is not possible without understanding the environment in which you are working, and this understanding can only come from the absorption of experience-based, context-specific knowledge.

The Microinsurance Network is leading the sector in bringing together key figures from the microinsurance sector to facilitate open dialogue, generate and share knowledge, and carry out in-depth research, leveraging the expertise of members across the Network to distil key lessons learned and best practices for adoption by the microinsurance sector.

As a multi-stakeholder network, the Microinsurance Network offers a space in which seekers and providers of insurance solutions can come together around specific issues. Policy makers, regulators, insurers and brokers can interact and engage in a way that is beneficial to the sustainability of the sector. This magazine is an attempt to embody what the Network stands for: the sharing of knowledge and the facilitation of open dialogue on key issues affecting the sector to increase access to valuable insurance for low-income people.

The voices heard in this magazine belong to some of the sector's most authoritative figures on the issues they write about. Here, you will learn about the failures and innovation in MicroEnsure's distribution of microinsurance, the state of microinsurance across the globe using data from the World Map of Microinsurance programme, approaches to regulation across the globe from A2ii, the ILO's Impact Insurance Facility take on the complexity of assessing and meeting demand, and the role of microinsurance in disaster risk management strategies from the Geneva Association.

I hope you enjoy reading this first issue of the annual "State of Microinsurance" magazine, and that you continue to spread the knowledge you acquire with your peers. Only with your help will the sector continue to grow and protect ever more vulnerable people from risk.

Microinsurance: A vital tool for boosting the local and global economy



Andrea Keenan

Senior Managing Director -
Industry Relations, AM Best
Vice Chair of the Microinsurance
Network



“ Insurance promotes economic development by creating a safer environment for investment and innovation. “

Insurance is a risk financing mechanism. It allows people to protect their families, livelihoods and wider communities from the financial loss of unanticipated events. In providing a safety net, it enables calculated risk-taking and drives economic activity forward. Insurance accommodates for our natural sense of aversion to risk and promotes the forward movement of progress. The benefits are endless, and the sector contributes largely to both the national and the global economy.

Global economy

As Rudi H. Spaan, President and CEO of AIG Hong Kong, highlighted at the Asian Insurance Review's conference on "Value of Insurance for Development" last April, insurance underpins all daily economic activity across the globe. If all insurance contracts were suspended for just one day, the world of business and a good chunk of our personal lives would come to a grinding halt; planes would not fly, cargo ships would not set sail, business would stop in its tracks.

In a global economy that is increasingly inter-connected, prone to rapid social shifts and facing increasing claims from risks of climate change - induced natural catastrophes, insurance is a critical component of economic stability and growth and its value has never been higher¹.

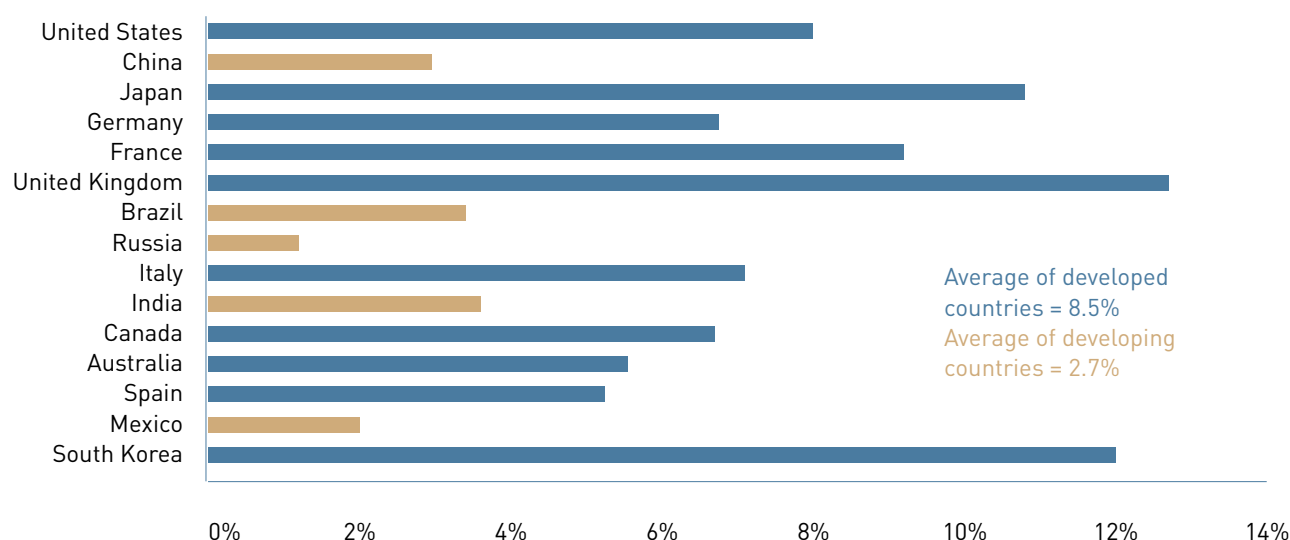
Insurance in a country's growth

Insurance provides peace of mind, enhances consumption, and fosters entrepreneurship and innovation—all of which are factors of economic growth. It enables risk management and encourages loss mitigation. As the economy grows, so do premiums written. However, in emerging markets, penetration levels are far below those of developed markets. As highlighted in the graph below, countries with more mature economies have higher insurance penetration than the emerging market economies. Thus, real maturation of an insurance industry occurs when the rate of growth or premiums exceeds that of GDP. Policymakers and industry participants in these regions struggle to find ways to improve this ratio so that the country is better protected and has a better foundation to grow.

1. CEA (2006). The Contribution of the Insurance Sector to Economic Growth and Employment in the EU. Brussels: CEA
2. Geneva Association (2012) The Value of Insurance to Society. Risk Management N° 51 / May 2012

FIGURE 1 Insurance penetration rate

Source: Swiss Re and AM Best research



From a policy standpoint, microinsurance is a strong development tool for countries looking to encourage inclusive economic growth and socio-economic development. Since regulators have, as part of their mandate, been making insurance available to low-income populations, the presence or use of insurance for different target groups in a country should be a major policy objective.

Natural disasters have been increasing in severity and frequency in recent years, with developing countries hit the hardest. A robust disaster risk management framework that strongly features microinsurance can help protect vulnerable people by ensuring money is available after a disaster, which they can then use to finance their recovery, repairing homes and restarting livelihoods. With higher insurance penetration among poorer populations, fewer people would be pushed into a cycle of poverty and thus would be more likely to be able to continue contributing to the national economy, despite the shock event.

Investment, entrepreneurship and innovation

Insurance promotes economic development by creating a safer environment for investment and innovation. Individuals and

companies are more inclined to take on risky activities with insurance in place to safeguard them. On a micro level, this may be in the form of farmers opting for riskier but ultimately more lucrative investments, safe in the knowledge that their insurance covers crop failure. For example, a farmer wishing to expand into higher yield crops might be more inclined to do so if the risk of drought were not so devastating to his future income. On a larger scale, investors are more likely to invest in risk-averse spaces, meaning the role of insurance is paramount to enabling investments.

A strong performing insurance sector allows for the efficient management of risk through nurturing a culture of risk management in firms and individual households. With a strong insurance culture, the savings of individuals and small companies can be mobilised toward productive activities and need not be diverted towards risk management in the event of a shock.

Small and medium enterprises (SMEs), often the engines of growth of emerging market economies, have limited access to capital, and more efficient use of resources would carry a multiplier effect on their ability to produce. Microinsurance can address the needs of SMEs to enable them to free up savings and look at expanding their businesses. By transferring risk to a third party,

businesses can re-allocate the funds they would have needed to save for potential future shocks, towards investment in better technologies and product innovation.² In a similar way, credit life, which has the highest microinsurance coverage globally, protects the portfolios of banks, providing security for the banks and in turn facilitating consumer access to financial services.

Insurers also have a direct impact on the overall economy, as they themselves are also a major institutional investor in the economy. In an emerging market like India, the state-owned life insurer Life Insurance Corporation of India (LIC) is the biggest domestic institutional investor in the Indian capital markets and invested about € 8 billion in the financial year 2013-14.³ The capital amassed from premiums is often re-invested in the financial market.

Insurers, in investing premium income, then make their capital available to private companies and government bonds, hence funding infrastructure and other socio-economic projects, which in turn impacts on development⁴. The consistent nature of premium payments means insurers can be a source of liquidity and can buy assets that are undervalued during downturns⁵. In this way, insurers can have a stabilising effect on financial markets and the economy.

3. Time of India 2015

4. Geneva Association (2012) *ibid*

5. Insurance Europe (2013). *Funding the future: Insurers' role as institutional investors*. Brussels: Insurance Europe/Oliver Wyman

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“ From a policy standpoint, microinsurance is a strong development tool for countries looking to encourage inclusive economic growth and socio-economic development. ”

Social protection

Insurance is complimentary to social protection and so can relieve the burden on public resources by offering coverage alongside the state, particularly for pension and health care provision. This is particularly important given that life expectancies are generally increasing, whilst birth rates are declining for some low-income countries such as Thailand, Brazil and parts of India. In OECD countries, the percentage of people aged 65 years and older is expected to reach 37% by 2040.⁶ These factors mean that many countries are ageing rapidly, the elderly have less support to rely on from their children, and the labour pool is diminishing. With this ageing population, public resources in terms of healthcare and pensions are overburdened, and diverting capital to social protection measures inevitably means cutbacks in other areas of socio-economic development. Insurers can absorb some of the risk and financial burden of the public sector by offering products on the private market or rolling out programmes on the government's behalf.

Health microinsurance

Health microinsurance can play a tremendous role in boosting the long term growth potential of an economy through production of a virtuous cycle. Those with limited or no access to healthcare are unlikely to seek help until their conditions are extremely debilitating. With access to healthcare through microinsurance, sick people can seek treatment earlier and avoid prolonged sickness, often meaning fewer sick days and stronger and more productive performance in the workforce⁷. Improved access to healthcare also means children stay in school and perform better, which in turn boosts national education levels and economic development, as high education often equates with higher income and thus more spending power.

Ultimately, a strong performing insurance sector provides peace of mind to individuals and businesses alike, offering a safer, more risk averse environment in which innovation and investment can thrive. This in turn offers huge potential for the development of the national and global economy.

⁶ Geneva Association (2012) Ibid

⁷ Nasr, J. (2015) Paving the Way Out of Poverty. Health microinsurance can keep a medical emergency from becoming a financial tragedy, NextBillion

Insurer investment in FinTech is gathering steam



Brandon Mathews

Managing Director,
Stonestep

Facilitator, Microinsurance Network's
Distribution Working Group

“Microinsurance can generate big numbers directly by reaching massive and still growing emerging consumer demographics in lightly traded markets.”

A single loan or a single auto policy is super volatile for the provider – either it will pay or else be a total loss. To consistently make money in financial services requires underwriting more than one risk; it requires a portfolio. Just as individual loans and insurance policies are individually volatile, so too individual innovation projects carry greater uncertainty – especially when compared to “business as usual”. Thus, to invest in and manage these innovations, major insurers – among them AIG, AXA, Generali, Marsh, MetLife, XL, and Zurich – have recently announced new structures with a portfolio approach to insurance innovation – and several have a specific remit for microinsurance.

Individual microinsurance projects are funkier than other projects which cross most insurance managers' desks. These projects are in new markets, with new customers, and rely on new partners, as well as new technology. Whether due to a sense of corporate responsibility or due to appreciation for reputation risk, these projects also use new measures of customer impact and societal value. That's a lot of “new” for the 300+ year old insurance industry, and “new” to any insurer means “uncertain”. In most cases, “uncertain” means no investment.

At the same time, the prize for cracking the code is huge. Microinsurance can generate big numbers directly by reaching massive and still growing emerging consumer demographics in lightly traded markets. It also aims to create measurable societal benefit, which in turn can bring sexy back to insurance.

During the first 90 days of 2015, no fewer than nine major insurance industry companies announced participation in three new structures which take portfolio approaches toward insurance innovation. Two of these mention an explicit mandate for microinsurance. This activity puts an industry exclamation point behind what Network members such as MicroEnsure, LeapFrog,

GreenOaks, and Stonestep have been doing in recent years: building portfolios of new ventures to expand the microinsurance space.

The new structures take two distinct approaches: single company funds with focus on Financial Technology (FinTech) or a consortium of multiple companies working as an incubator solely for microinsurance. The FinTech funds announced by AXA and XL Group open with offices in the technology hub of Silicon Valley whereas the consortium starts in insurance-friendly Bermuda. Each brings a distinct approach to managing a portfolio of innovations.

The first of these three structures, an industry consortium, was announced in January during the World Economic Forum in Davos. There, eight major industry companies jointly announced the formation of an industry-owned consortium which pledges to launch ten microinsurance ventures within ten years, and to stand the first one up in 2015.

The consortium benefits from an exceptionally impressive list of supporters. It is backed by a veritable who's who of the industry including: Alex Moczarski (CEO Guy Carpenter), Dan Glaser (CEO Marsh &

McLennan), Mike McGavick (CEO XL Group), Mike Kerner (CEO General Insurance Zurich), Kevin Hogan (CEO AIG Consumer Insurance), Mario Vitale (CEO Aspen), Paul Jardine (COO Catlin), Michael Sapnar (CEO Transatlantic Re), and Brian Duperreault (CEO Hamilton Insurance). In a recent podcast with the Microinsurance Network's Véronique Faber, Joan Lamm-Tennant who leads the consortium explained that a name for the consortium is in the works using methods which underscore the commitment to "collaborative innovation".

Just weeks after Davos, AXA Strategic Ventures was announced with the aim to invest "in companies with the potential to shape the future of the financial industry". The fund has one limited partner, AXA Group, and is launched with EUR 200 million. The fund's focus areas include "alternative business models, big data, climate change, financial inclusion, and health". It is led by Francois Robinet, previously CEO of two AXA companies and Chief Risk Officer for AXA Group, together with other senior AXA executives. It offers access to insurance expertise from AXA together with investment. In a video explaining AXA's vision for the fund as regards customer experience, Robinet said, "the insurance industry is not known for great consumer experience, which is in contrast with the societal purpose of insurance. We believe that innovation and technology will allow us to bridge the gap."

On April 1, XL Group announced its fund, XL Innovate, to be led by a leading insurance industry innovator and prior member of XL Group's Board, Tom Hutton. In announcing the new structure, XL Group CEO, Mike McGavick commented "We are very excited to launch this new initiative, which will extend XL's capabilities in existing markets and give us new opportunities to address some of the most pressing and complex risk problems in the global economy. XL Innovate is an important step as we continue to drive our focus on innovation forward and secure the relevance of XL and the

industry well into the future." The launch of XL Innovate comes at the heels of XL Group's USD 4.1 billion acquisition of Catlin Insurance and adds another new dimension to the company. Mr. Hutton adds in the fund's announcement that "we look forward to being a unique partner to entrepreneurs with the vision and ambition to address new risks with new solutions, unconstrained by geography, scale, or traditional thinking".

In May 2015, Generali announced its approach to FinTech, committing EUR 1.25 billion through six venture capital funds. These new structures each bring a portfolio investment incubation approach to insurance innovation. The portfolio approach allows each to explore new options while operating with a reasonable expectation for good risk-adjusted returns. These 2015 announcements follow close on the heels of MetLife Asia's November 2014 announcement of its futureLab in Singapore, another single-company innovation effort with the aim of launching "disruptive new business models and capabilities". Zia Zaman, MetLife Asia's newly appointed Chief Innovation Officer and founder of futureLab explains that "futureLab will harness disruptive innovation principles and the start-up philosophy of Silicon Valley, together with the strong creative talent pool available in Singapore, to develop solutions that meet the needs and aspirations of tomorrow's consumers".

These efforts from leading insurance companies are welcome news, particularly considering the 2014 CGAP Funders Survey's recent insight into who finances financial inclusion. The study, released in April, shows that while the total funding for financial inclusion increased by ~15% during the period 2011-2013, growth was fueled by public funders whilst private investors trimmed back slightly. The recently announced structures are all backed by private institutions and thus this portfolio of portfolios represent a positive trend for insurance innovation and financial inclusion in 2015 and beyond.

“ During the first 90 days of 2015, no fewer than nine major insurance industry companies announced participation in three new structures which take portfolio approaches toward insurance innovation. “

Lessons in distributing microinsurance: The MicroEnsure experience



Richard Leftley

CEO, MicroEnsure
Board Member,
Microinsurance Network



“ Whilst only 150 million families have a microfinance loan, an estimated four billion people need insurance, meaning many providers have had to look for additional distributors. ”

The microinsurance market is young and is continuously evolving. As distributors, we must constantly find ways to access new markets and devise innovative business models to distribute products through a range of partners to best suit the needs and demands of local communities.

The importance of innovative distribution approaches to microinsurance cannot be underestimated. As my colleagues discuss elsewhere in this magazine, consumer education efforts are wasted if customers do not have an easy, simple and accessible point of sale, through which they can also see the value proposition. Finding a one-size-fits-all approach to distribution is no mean feat given underlying infrastructural discrepancies between markets, as well as different cultural constraints. A lack of infrastructure is a major challenge for distributors and often incurs high administrative and human resource costs. Finding ways to reduce these costs from signing up to settling claims is therefore of fundamental importance to the sustainability of microinsurance programmes.

MicroEnsure

Over the last 12 years, MicroEnsure has focused a great deal on developing innovative strategies to distribute microinsurance through an array of partners, with the aim of massively increasing uptake of microinsurance products in developing countries. From our experience, whilst other areas of microinsurance product development are important, often not enough attention is paid to how the products will ultimately be

distributed, and this is a common reason for the failure of microinsurance programmes. It is important that we learn from our successes and failures, so here we take a look at what worked in distributing microinsurance – and what didn't.

We have developed distribution partnerships with more than 90 microfinance companies, 20 banks and 12 mobile network providers. In our experience, a successful distributor of microinsurance needs to have three key attributes;

- **Strong brand:** The company distributing microinsurance needs to be trusted by the community, and the client needs to trust that the product will work. Interestingly, there is a strong correlation between the frequency of transactions and levels of trust, which is why mobile networks are a great brand to sell through.
- **Accessible points of sale:** Points of sale (POS) can be a loan officer or a handset, but the best POS is one that reaches out into the community rather than requiring a client to come to the company.
- **Ability to transact payments:** The collection of premiums and disbursement of claims must be cheap and simple, which is best done when embedded into



another transaction, such as a loan repayment, savings deposit or purchase of airtime. Covering the cost of the transaction as a stand-alone item can often present major issues in terms of overall sustainability.

Taking into account the three requirements listed above, let's take a look at the major types of distributors that have worked for us and how they performed.

Microfinance companies

Most people working in microinsurance started by working in partnership with MFIs, which typically have a strong and trusted brand in the communities they serve, as they give out loans that require frequent repayments. The loan officers are already in the community making loans and receiving repayments, and it's easy to embed the premiums into the loan disbursement with claims distributed by the loan officers.

Though MFIs successfully distribute microinsurance, they do have limitations. Firstly, some MFIs focus on products that benefit the MFI more than the client, which explains the ubiquity of credit life. The client does benefit from not having to repay the loan after a shock event; however, the primary beneficiary is the MFI. Over the years, credit life has expanded to provide coverage for a wider range of risks including accident,

property damage, additional family members, funeral cover, hospitalisation and even political risk. But the balancing act is always what the product will cost (and hence how competitive the loan is), versus how much risk of default the lender can lay off through the product.

MFIs can also be unwilling to offer insurance outside of the loan period, which leaves the client with gaps in coverage, as most clients do not borrow back-to-back. Even those that do can experience delays in loan disbursements which leave them uncovered.

MFIs are further constrained by their outreach. Whilst only 150 million families have a microfinance loan, an estimated four billion people need insurance¹, meaning many providers have had to look for additional distributors. The available market is simply larger than the distribution afforded by MFIs.

Anglican Church

Some years ago, MicroEnsure tried to use churches as a distributor. Research showed that the Anglican Church was trusted in low-income communities, with tens of millions of members in Africa, a long-term presence in the communities and senior leadership which appeared committed. Interestingly, our research showed that the church was

trusted even by those who followed a different or no religion. We launched products in Tanzania in 2010 that would be sold at the church with premiums collected weekly, but we soon hit problems!

Our mystery shopping revealed that there was a significant tension between the parish priest and the product, as the priest relied on money provided during the service to pay for his basic needs. So when the money was diverted to pay for insurance, the priest would struggle to collect enough money to buy food or educate his children. The priest therefore had reasons to discourage his community from purchasing insurance.

Large multinational NGOs

Over the years, we have been approached to work with a number of large NGOs. The attraction of these partners in the distribution of insurance is their sheer scale in terms of the countries they operate in and the number of people they serve. With years of experience, they are clearly well-integrated and trusted by the communities they work in, although it is important to note that they are seen as a donor to the community, rather than a place to purchase a product such as insurance. These partners also have a fantastic spread of potential POS. However, field workers are not trained to sell financial products, and communities are often conditioned over many years not to pay money to NGO field workers in order to avoid corruption. Minimal competency in selling insurance and collecting premiums means these organisations are often weak distributors of insurance.

Mobile wallets

When MicroEnsure first approached mobile network operators, we were steered toward their mobile wallet service; outside of Kenya and the success of MPesa, many telcos are struggling to get users to sign up for and use their mobile wallets. The telcos were interested in seeing whether adding additional products such as insurance would incentivise users to use their mobile wallets. Like many others, we spent time making our products available via the mobile wallet and hoped that, by making sign up easier

1. Swiss Re "Microinsurance – Risk Protection for 4 billion people", June 2010



through the use of a phone-based USSD menu and simpler to pay small premium instalments, we would somehow tap into demand for the products. The reality was of course different and like most others we learnt that access does not equal demand!

Most people do not wake up wanting to buy insurance and low or middle-income people have numerous concerns to prioritise over insurance. Making it easier to sign up and pay via the mobile did not affect demand and as a result did not work.

Mobile airtime

Having discovered that providing improved access via the mobile wallet was insufficient, we started to focus on educating consumers about the value of insurance, which we hoped would allow us to create a market. The end goal was to sell insurance over the mobile wallet, but it was clear we needed a way to “prime the pump”.

Most mobile phone users in emerging countries are pre-paid customers, topping up small amounts of airtime as needed and using multiple SIM cards which they swap depending on who they are calling or which network is offering a promotion. Our idea was to leverage this lack of loyalty alongside the fact that customers worry about the risks they face, to provide insurance in return for increased loyalty. In essence, the idea was that the mobile network would pay

the premium for those clients that spent USD 2 or more in a month on airtime. The more they topped up in a month, the more free insurance they received next month. This encouraged consumers to stick with the network and spend more of their top-ups with the telco running the free insurance offer.

It worked. MicroEnsure signed up 1 million clients a month in 2014 through this distribution channel. Now the next step is to encourage clients to start paying for their insurance in return for greater levels of cover or to insure additional family members.

Savings accounts

After seeing that insurance could alter consumer behaviour in the mobile networks, we noticed that many of our MFI partners had started to take deposits, but that the majority of their bank accounts had very little money deposited in them. Our research showed that clients just did not value the interest they received for the deposits, favouring instead to save money through other methods such as buying jewellery or livestock.

Our questions was; if a bank offered free insurance to those depositors that maintained a deposit of say USD 50 or more, would this motivate people to use the savings account? We trialled this idea with Women’s World Banking in Ghana and deposits increased

by more than 200% in just a few months. We have since deployed these products with many MFIs and banks including Barclay’s in Africa. Again – trusted brand, easy POS and the ability to transact all come as second nature to the deposit taker.

Distributors of the future

MicroEnsure is always looking for new ways to work with partners in distributing insurance to the mass market. As the loyalty model has worked so well with mobile network operators and banks, it could also be applied to other distributors in order to fix a specific consumer loyalty issue. We are already working with utility companies, money transfer companies and branchless banking providers to see if insurance can alter consumer behaviour.

But the real challenge of providing insurance on a direct basis still looms large for the industry. Nearly all of our activity is done on a group basis with products embedded into a loan, savings account or airtime purchase. The cost of selling and servicing a direct sale model has always been a huge hurdle, but with increasing penetration of low-cost smartphones and the advent of 3G networks, it will not be long before reaching the middle and low income consumer via the internet becomes a reality. When that happens I think we will see a whole new array of potential distribution models flourish.

The complexity of increasing demand and what we can do about it



Michal Matul

Chief Project Manager,
ILO's Impact Insurance Facility



“ 63% of respondents in Kenyan financial diaries who experienced crop failure reported no impact on their household, as they didn't register the value of the loss of harvest, input costs, or labour. ”

Vulnerability to risk, a constant in the lives of the poor, is a cause of persistent poverty. Microinsurance offers one solution to mitigate risk, yet demand remains disappointingly low. This article looks at lessons learned and selective recommendations for increasing demand, based on academic studies¹ and the experiences of over 60 innovation partners of the ILO's Impact Insurance Facility.

Addressing the low demand for microinsurance is complex. To increase scale, practitioners must first understand the factors influencing a household's decision to buy microinsurance, before developing strategies to overcome barriers. Determinants of demand include personal characteristics, understanding of insurance, trust, value proposition and perception of the product, ability to pay, use of other risk-coping mechanisms, and behavioural factors that prevent even those who want to buy microinsurance from doing so.

A review of studies revealed trust, liquidity constraints, quality of the client value proposition and behavioural constraints as the most important determinants of demand for first sales (see Table 1). The data on renewals, though limited, suggests that increasing understanding, improving the client value proposition and overcoming behavioural constraints could significantly boost renewals and lower client acquisition costs.

It's not just education

Low demand is often attributed to a lack of understanding of microinsurance; however, better awareness and knowledge of insurance does not always translate into higher demand. Interestingly, consumer education seems to stimulate demand for index insurance but has no effect on health microinsurance, which highlights distinctions in purchase decisions for different products. For health microinsurance, the product's scope of benefits and the quality of healthcare services might be more important triggers of demand.

Households tend to underestimate impacts of shocks that are not in the form of new cash outlays, which is the case for most agriculture risks. 63% of respondents in Kenyan financial diaries² who experienced crop failure reported no impact on their household, as they didn't register the value of the loss of harvest, input costs, or labour. Only for death of a breadwinner and temporary and permanent disabilities

1. Matul et al [2013]. Why people do not buy microinsurance and what can we do about it. Geneva: ILO's Impact Insurance Facility.

2. Zollman, J. (2015). Two steps back: How low income Kenyans think about and experience risk in their pursuit of prosperity. Geneva: The ILO's Impact Insurance Facility.

TABLE 1 The effects of determinants on first sales and renewals³

Determinant	Evidence available	Effect on first sales	Effect on renewals
Trust	😊😊😊	↗ High	↗ Medium
Liquidity constraints	😊😊😊	↗ High	↗ Medium
Value proposition (and its perception)	😊	↗ Medium-high	↗ High
Behavioural factors	😊	↗ Medium-high	↗ High
Understanding insurance	😊😊	↗ Low-medium	↗ Medium-high
Access to other coping mechanisms	😊	↗ Medium	↗ Medium

did respondents report any lost income. Underestimating losses may make them easier to face, but it also makes it difficult to communicate the value of protection. The way people conceptualise losses shapes how they manage them, and by not acknowledging the full cost of risks, they are unlikely to adequately prepare for them.

Consumer education does have an important impact on renewals, as clients might test a product but won't renew it if the product is confusing. Providers need to embrace consumer education as an on-going activity, focusing on key issues such as scope of coverage, how to claim and how to request for more information.

Leverage savings to increase uptake

Faced with the tough balance between ensuring day-to-day liquidity and investing in the future, there is a preference for low-income people to save for investment and rely heavily on informal borrowing for liquidity. By taking small loans from friends and family or taking goods on credit from local shops, people navigate through some small-scale disruptions. The flip side is that people are very cautious about borrowing for investments.

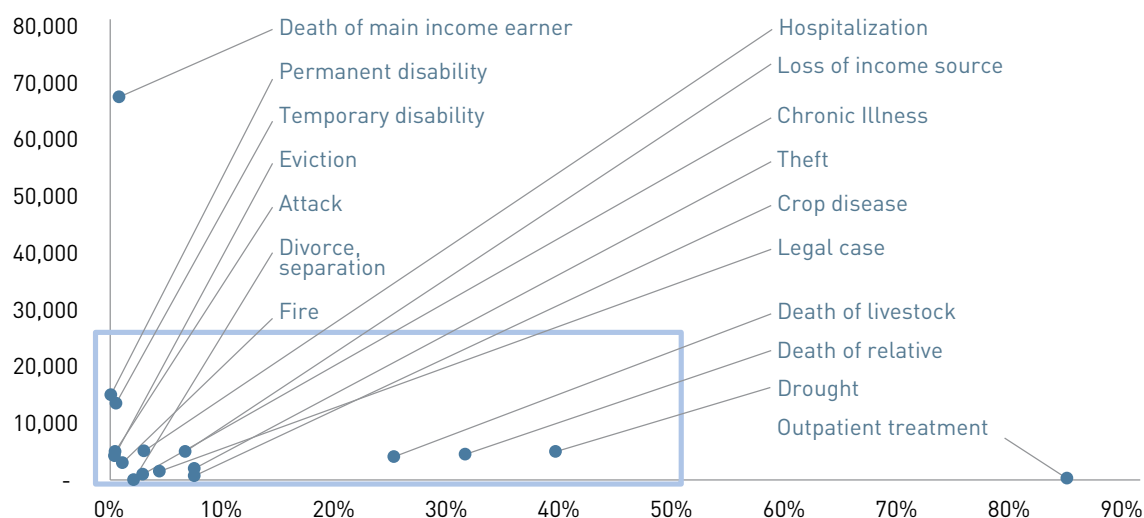
It seems that better balance between investment and risk-management would benefit low-income households, and would allow insurers to tap into part of the savings to collect premiums. Money can be saved throughout the year when it is available, and then used to pay an insurance premium when it is due. In Kenya, Safaricom, Britam and Changamka have eased clients' liquidity constraints by offering a savings-linked composite health product using mobile technology to facilitate premium collection. When clients save half of the premium, the insurance kicks in with half of the benefits. 40% of clients used this option successfully.

Bundling insurance with other financial products could increase the demand for both products if they are seen as complementary solutions. Evidence from MicroEnsure in Ghana shows that bundling savings and insurance can increase insurance penetration and stimulate savings. Depositors with a minimum balance of USD 60 each month were entitled to free life insurance with benefits of up to USD 180. Five months after the launch, deposits in the bank increased by 19% and deposits from clients with balances below USD 60 increased by 207%. This suggests that a change in savings behaviour as a result of the free insurance cover.

“ Providers need to embrace consumer education as an on-going activity, focusing on key issues such as scope of coverage, how to claim and how to request for more information. ”

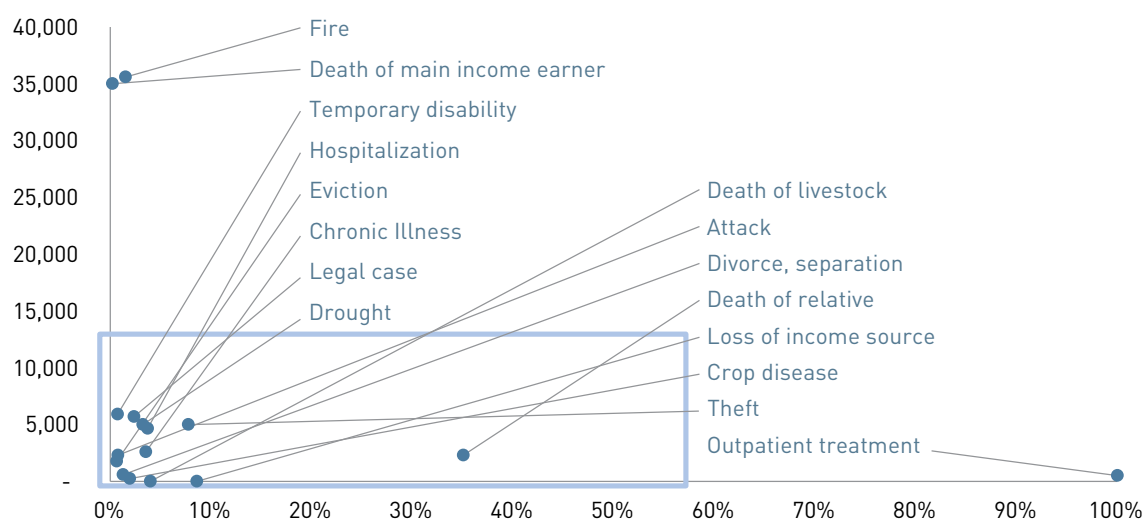
3. Matul et al (2013) ibid

FIGURE 1 Shock frequency and severity⁴



Rural Incidence and Severity

Probability of Population at Risk Experiencing Event in One Year (%)
by Median Cost of One Event (KSh)



Urban Incidence and Severity

Probability of Population at Risk Experiencing Event in One Year (%)
by Median Cost of One Event (KSh)

4. Zollman, J. (2015) ibid

Start simple but consider covering multiple risks

Often low-income households face a very large number of moderate probability, and moderate severity risks (Figure 1).

The large number of moderate risks seem ill-suited to single-purpose insurance products. Low-income clients need more flexible risk-management solutions. Composite products that cover several critical risks have the potential to improve the ability of low-income households to manage risk. Multi-risk products provide good value when (a) the insurance market is developed enough for clients to understand benefits and (b) insurers have the experience and capacity to deliver quality. After experience with single-risk products since 1992, in 2001 VimoSEWA started to offer a composite health, life, accident and asset product. This basket of benefits was again unbundled in 2010 because of difficulties in managing the mix of claims from different types of cover. Five other Facility partners have tried composite products in India, Kenya and Brazil. All these attempts failed as providers struggled to explain products to the market, achieve scale and administer multi-risk cover. Further problems were fuelled by partnership challenges between life and non-life sister companies⁵.

Since composite products may be too expensive and difficult to administer, one solution would be a combined savings/insurance composite product that provided a clear lump sum upon the occurrence of a verifiable trigger event. This fund can be something like a “start-over” fund to boost existing savings and help a family navigate through a hard time⁶.

Make it tangible

While it is relatively easy to test a savings product, it is harder for clients to test insurance since they may never file a claim. Nevertheless, free insurance products from trusted brands such as mobile network op-

erators⁷ or savings banks are giving many clients a first taste of its potential benefits. Some providers go one step further to create an experience. Econet gave new clients one dollar to transfer to a friend or relative, in total giving away USD 100,000. This allowed clients to experiment with the service for free, gaining their trust and creating a buzz⁸.

Bundling insurance with value-added services⁹, such as free health check-ups or SMS weather alerts provide a positive experience, even for those who never make a claim, which can have a substantial effect on renewals.

Remove obstacles

Barriers to action greatly influence demand. Even people who are convinced about insurance do not buy it because of a failure to convert intentions into action. People are influenced, sometimes disproportionately, by seemingly inconsequential behavioural constraints that prevent enrolment, such as requiring clients to submit the enrolment form at the insurer's office without them knowing the location of the office. Researchers in Nicaragua found that when they allowed market vendors to enrol directly at their market stall, uptake was 30 percentage points higher.

A study in China¹⁰ revealed renewals were higher when clients had to opt-out, rather than stay in insurance. Such a default option, however, needs to be clearly communicated to clients, as an undesired renewal can easily lead to distrust in the scheme.

Don't forget about demand even if you go mandatory or cover portfolios

It's important to consider demand issues also for mandatory products or solutions that cover credit or agriculture portfolios aggregated at regional or organisational level rather than individuals. SKS, India's

largest MFI, found that when bundling health microinsurance with its loans, clients who were offered the bundled product were 23% less likely to renew their loan within one year. Even though the insurance covered hospitalisation and maternity expenses at a fair price, a new study by researchers at Harvard and MIT found that many clients prefer to give up loans rather than pay higher interest rates for insurance. Though the households faced frequent serious health shocks, demand was low as very few people were able to claim the insurance benefit, largely because clients were never provided with the documents and cards needed to do so.

A positive experience of claims drives satisfaction and renewals. This is evident in the experiences of Fonkoze (Haiti) and Microfund for Women (Jordan), who experienced steady renewal rates after the introduction of bundled insurance. In both cases, the MFIs paid special attention to claim procedures¹¹, investing in simplification, standardisation, decentralisation and efficiency, such as establishing procedures allowing the MFI to quickly authorise small claims on behalf of the insurer.

Failure to ensure great experience has implications for the insurer, distributor and, most importantly, clients. In the case of SKS, the majority of clients who dropped out lost access to microloans altogether, hurting their businesses and livelihoods.

Demand is a complex issue, with trust, liquidity constraints, quality of the client value proposition and behavioural constraints emerging as the most important determinants of demand. Practitioners need to understand the demand puzzle in their context, identify the most important determinants and design specific products, pricing, promotion and distribution strategies to best address the needs and appeal to their clientbase.

5. Matul, M., Dalal, A. (2014) Creating client value: Ten blueprints for microinsurance providers. Geneva: The ILO's Impact Insurance Facility

6. Zollman, J. (2015). Two steps back: How low income Kenyans think about and experience risk in their pursuit of prosperity. Geneva: The ILO's Impact Insurance Facility

7. Prashas, P. et al (2014). Mobile phones and microinsurance. Geneva: The ILO's Impact Insurance Facility

8. <http://www.ilo.org/public/english/employment/mifacility/download/repaper8.pdf>

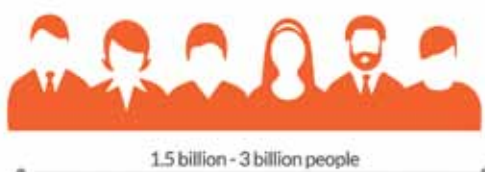
9. Pott, J., Holtz, J. (2013). Value-added services in health microinsurance. Geneva: The ILO's Impact Insurance Facility

10. Cai, J. (2011). Social Networks and Insurance Take-up: Evidence from a Randomized Experiment in China. Geneva: The ILO's Impact Insurance Facility

11. <http://www.impactinsurance.org/emerging-insights/ei47>

Digital insurance in emerging markets

Estimated market potential



Penetration in emerging markets



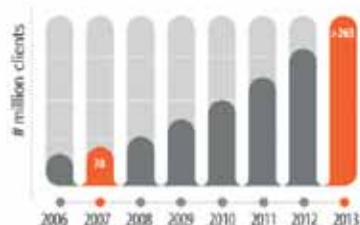
Estimated time to insure 1 million lives



Annual growth rates



Microinsurance growth



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The global landscape of microinsurance



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Katie Biese

Project Manager,
MicroInsurance Centre

Microinsurance is proving an important component of the insurance business in Latin America and the Caribbean (LAC), bringing in almost USD 830 million in premiums, covering nearly 50 million people, and resulting in estimated pre-tax profits of about USD 230 million across the region in 2013. Growing significantly faster than the traditional insurance market in LAC (Figure 1)¹, though from a lower base, microinsurance will expand in importance in the coming years, not only in this region but across the globe.

The lower-income market offers tremendous potential for the expansion of insurance services, and more and more insurers are recognizing this opportunity. Some are still just starting to experiment with a product offering or two, while others have already found successful business models. As the microinsurance industry develops and more attention is focused on lower-income consumers, it is critical to have good market data and information to support positive growth. The landscape studies are intended as tools for those companies that want to succeed in microinsurance. Without understanding the environment in which we do business, we will fail. The landscape studies (the published documents and the interactive World Map of Microinsurance) are thus designed to show what is happening in the microinsurance markets in LAC, Africa and Asia, so that insurers gain a perspective of products and profitability, premiums and people insured.

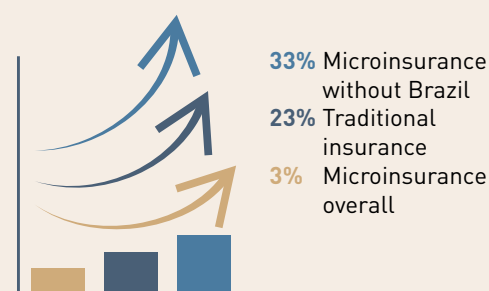


FIGURE 1 Comparable growth in gross written premium, LAC 2011 - 2013

Premiums

The three most recent regional landscape studies identified a combined USD 2.2 billion in gross written premiums (GWP) for microinsurance products (see map pg. 22-23). In LAC, the USD 828 million GWP in 2013 represents about 0.5% of total industry GWP; however, in individual countries mi-

1. Comparable rates are calculated based on 2013 USD, including only those companies that reported data in both periods, plus new market entrants. Comparative data is not available for Africa or Asia.

“Efficient claims payment is key to expanding the market and building an insurance culture.”

“Without understanding the environment in which we do business, we will fail.”

croinsurance represented as much as 4.7% of total GWP. Microinsurance is increasing in its significance and, with a coverage ratio of just 8%, there is clearly substantial untapped potential and plenty of room for growth. The opportunity is even greater in Africa and Asia, where coverage rates are 4.4% and 4.3% of the total populations, respectively.

In LAC, 2013 GWP per covered life is about USD 17.0, while that for Asia and Africa are USD 4.9 and USD 12.3, in 2012 and 2011, respectively. As these predominantly reflect the results of life and accident policies, the difference reflects a generally “wealthier” market in LAC, as well as the extremely low premiums of many products in Asia. Low premiums are characteristic of microinsurance products, yet the landscape studies and other research efforts are finding clear evidence that many insurers are finding a way to stretch these premiums into a business case.

Claims

Regionally, we see big differences in claims ratios. With a weighted average claims ratio of 79%, Asian insurers are paying out a higher relative proportion to clients than insurers in Africa and LAC (Figure 2), largely due to the lower average annual premiums throughout Asia. Insurers in LAC are at the other end of the spectrum, with a weighted average of 26% claims to premiums. The low claims ratios in LAC suggest that insurers still are not confident in their un-

derstanding of the risk of microinsurance products, leading to substantial loading of premiums, coupled with a market segment that is better able to pay these higher premiums. Greater competition should have the effect of increasing the claims ratios to more traditional levels; however, with a clear move towards mass insurance – which tends to experience even lower claims ratios and much higher commissions – it is possible they will remain low.

Claims ratios that are too low can be counterproductive in building an insurance market. Across LAC, Africa, and Asia, and across time (since the first study in 2005), about 80% of insurers have indicated that clients’ lack of insurance knowledge is a significant barrier to offering microinsurance. There is limited evidence of improved perceptions over time, with the vast majority of insurers reporting that market education is one of the biggest needs for development of the sector. The best form of market education, however, is a good product, with claims paid efficiently. The same can be said today as was said in the 2005 landscape study: “Poor people’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... and commercial insurers need to overcome their stereotypes of the low-income market and...recognize that the market is both profitable and reliable.”

Efficient claims payment is key to expanding the market and building an insurance culture. There is much potential with the microinsurance products now reaching millions in several countries, as long as the service is good and people know they are covered. In some countries, like the Philippines, a substantial percentage of people are covered (21%²) by microinsurance, and many insurers compete based on service, with several focused on showing people that insurance works.

Administrative costs

Generally, the microinsurance business case is most significantly driven by ad-

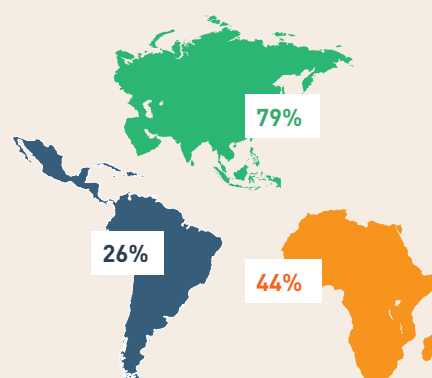


FIGURE 2 Average claim ratio by region

2. The Asia landscape study, based on 2012 information, found 21% of the population covered. The Philippine Insurance Commission has estimated this to have increased to 28% as of 2014. http://www.microsave.net/files/pdf/The_Landscape_of_microinsurance_in_Asia_and_Oceania_2013.pdf

ministrative costs and less so by claims. Business profitability combined with value for clients necessitates low administrative costs. Though still difficult for insurers to assess, data on administrative expenses (excluding commissions) is now available for the LAC region, where they account for about 25% of premiums on a weighted average basis. Technology is becoming increasingly necessary to improve the cost efficiencies at both the front and back office of the business. In an effort to increase efficiency and get costs down, insurers in LAC have focused on call centres as an approach to core microinsurance activities, while in Africa insurers have focused more on mobile technology.

Although front office technology like mobile phones is appealing, the more critical element is back office technology to efficiently process transactions and link into distributor systems, minimising or eliminating the need for costly manual activities. In LAC, one-third of insurers report using specialised software for managing their back office operations in microinsurance.

Most insurers do not actively track their administrative costs by product. This offers much room for business risk in insurance, as administrative costs are often the most significant component of costs for microinsurance. To get true understanding of profitability, insurers really must track their costs by product.

Distribution

Without a doubt, distribution is a lynchpin in terms of the advancement of microinsurance. Across the globe, microinsurance is increasingly becoming a hunt for distribution channels that reach greater numbers of people. The fundamental need of insurers for large numbers to generate profits from relatively small premiums, coupled with the need for efficiency to keep acquisition and administrative costs low, pushes insurers towards a broadening array of distribution channels.

In 2005, retail channels accounted for just 2% of the market, and mobile was merely a blip. In contrast, in the 2013 LAC study, retailers, utilities, and other mass chan-

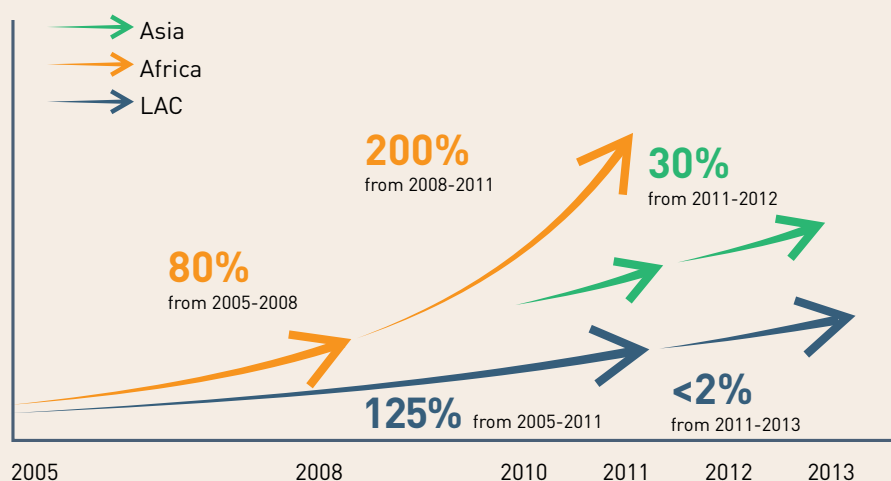


FIGURE 3 Growth rates (lives insured), 2005-2013

nels accounted for almost a third of the market (almost 15 million people), and are largely responsible for the growth seen in the 2005 – 2011 period. In Africa, mobile network operators (MNOs) largely contributed to the 200% growth between 2008 and 2011 (Figure 3), and the use of MNOs as a distribution channel in Africa and Asia currently is undoubtedly even larger, as evidenced by intermediaries such as MicroEnsure, with 1 million new clients per month in 2014 through this channel.³

In LAC, microinsurance is quickly morphing into “mass” insurance – low premiums, typically linked insurance cover – that is not designed particularly for the low-income market, but can provide some value to any economic level. This expands the market for insurance more substantially into the middle economic ranges, which have also commonly had little or no access to insurance. While these mass products might be covering a broader range of clients, they do seem to be including low-income people, as shown by the Bima e-insurance programmes.

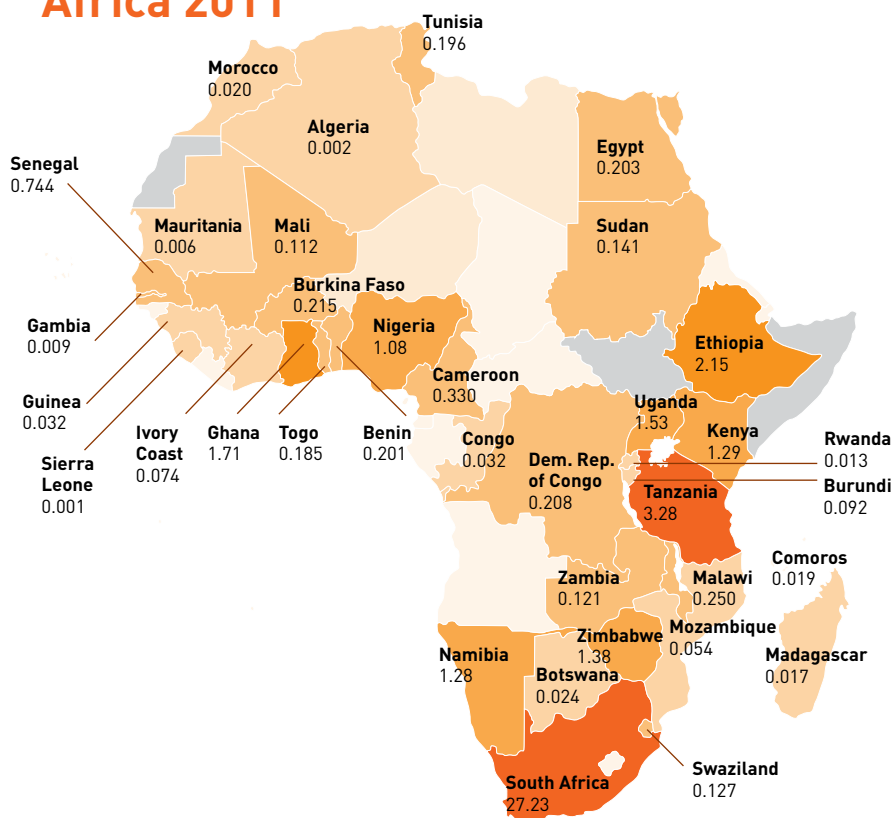
Commissions

With access to distribution channels a key constraint reported by many insurers, high commissions have become a reality. In LAC, commissions as high as 61% were reported,

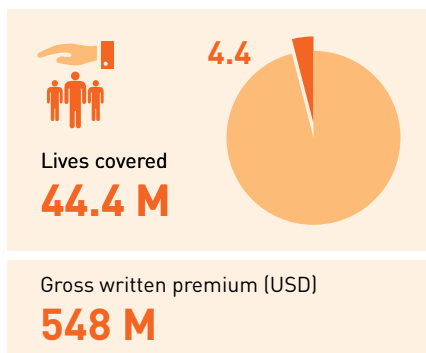
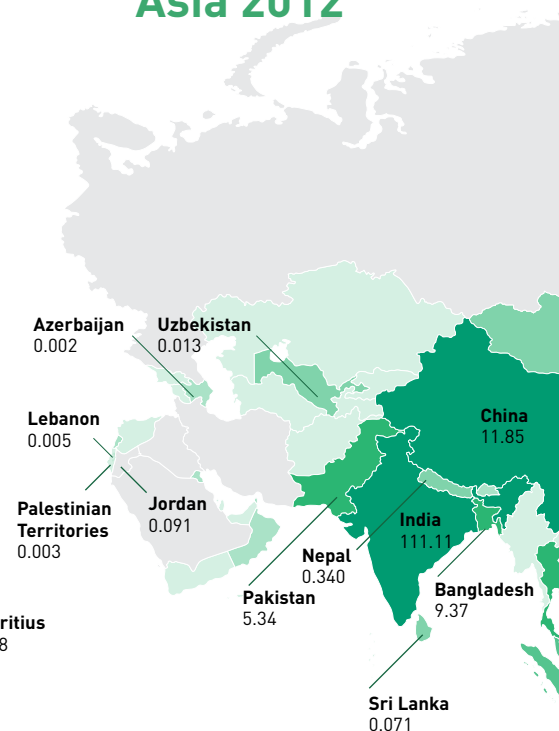
“ Mass and microinsurance together have dramatically expanded access both to those who could not access insurance and to insurers who could not access a wider market. ”

3. See Richard Leftley's article on distribution on page 11

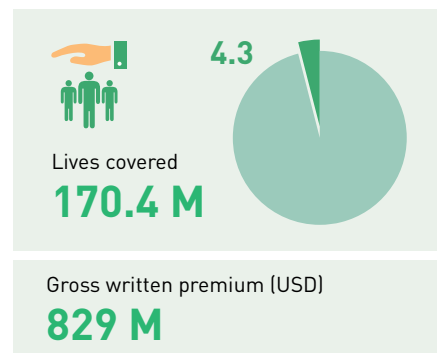
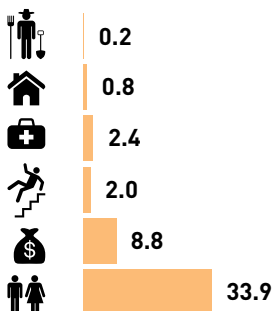
Africa 2011



Asia 2012

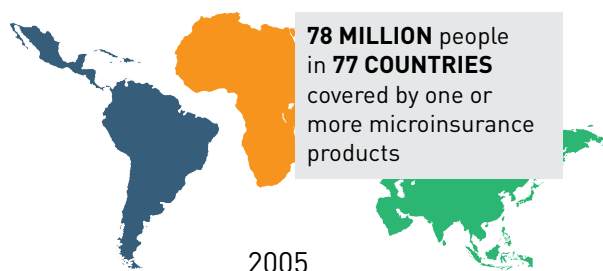


Types of products offered (millions of lives covered, including secondary covers)*

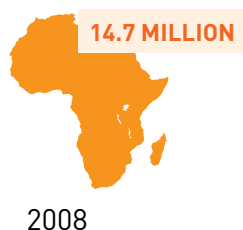


* see legend on page 42

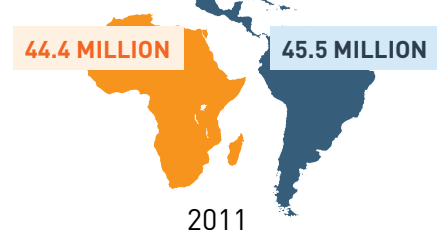
1st global microinsurance study Landscape of Microinsurance in the World's 100 poorest Countries



1st regional study in Africa Landscape of Microinsurance in Africa



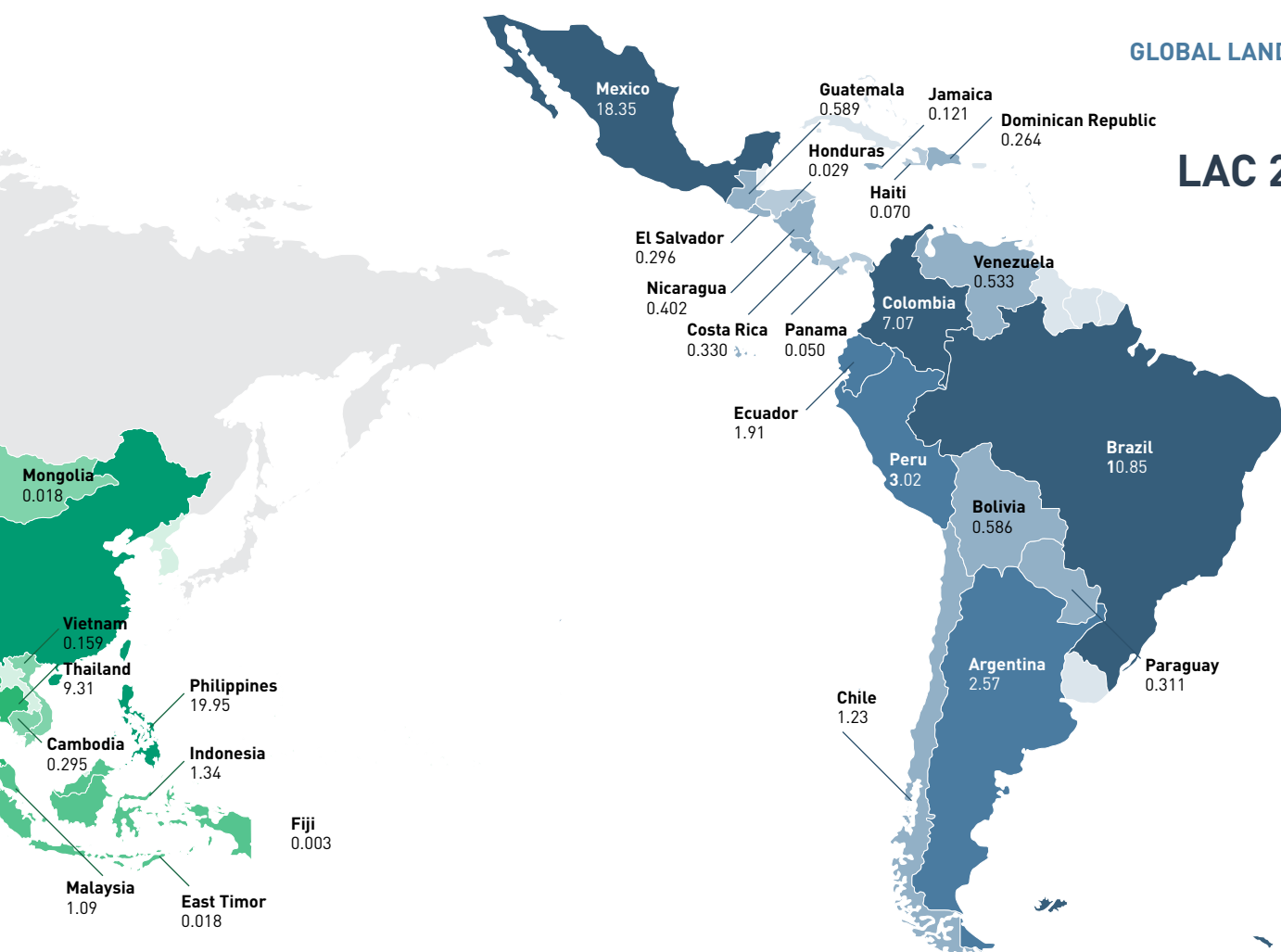
2nd regional study in Africa Landscape of Microinsurance in Africa 2012



1st regional study in LAC Landscape of Microinsurance in Latin America and the Caribbean

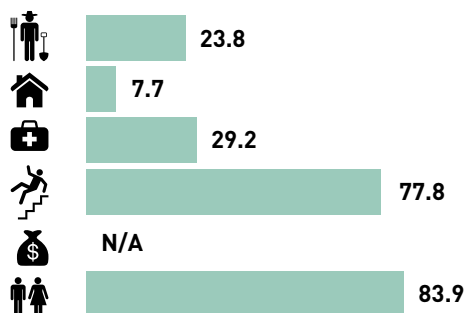


LAC 2013



Types of products offered

(millions of lives covered, including secondary covers)*



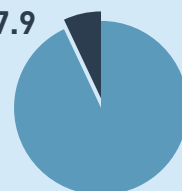
Lives covered

48.6 M

Gross written premium (USD)

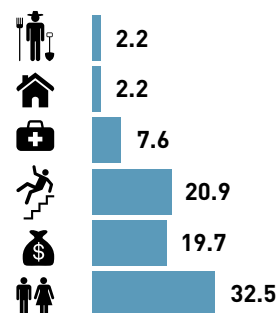
828 M

7.9



Types of products offered

(millions of lives covered, including secondary covers)*

1st regional study in Asia

Landscape of Microinsurance in Asia and Oceania 2013

170.4 MILLION



2012

2nd regional study in LAC

Landscape of Microinsurance in Latin America and the Caribbean 2014

48.6 MILLION



2013

3rd regional study in Africa

Landscape of Microinsurance in Africa 2015

IN PROGRESS



2014

2nd regional study in Asia

Landscape of Microinsurance in Asia and Oceania 2016

PLANNED



2015

with a regional weighted average of 21%. The average commission for the 5 products with the highest number of insureds was 36%, indicating that access to volume comes with a cost. As intermediaries take on more of the costs, such as marketing and facilitating transactions including claims, higher commissions can be justified – but only if this does in fact reduce the work and administrative costs for the insurer.

Distribution channels have the potential to reduce costs and provide access to new volumes of people, but there is also the potential for increased costs. Anecdotally, as insurers will not “officially” report this, additional commissions can take the form of “exclusivity” or “access” fees, particularly when distribution channels don’t see the opportunities that insurance can bring to them or their clients. This was commented on numerous times in the key mass insurance markets of Mexico, Colombia, and Brazil. Such fees are often paid before a single policy is sold, and are said to occasionally amount to more than a million USD. Although this is not often seen in Africa and Asia, it is likely to become more evident as microinsurance aims for greater distribution potential and as insurers move more into the “mass” market.

Profits

When the first landscape study was conducted a decade ago, the profitability of microinsurance was considered by per-

ception only. Most insurers were optimistic – profitability was less of a concern than affordability for clients (though the two are of course linked!). The 2008 Africa regional landscape study concluded, “Profitability is a key challenge for microinsurance... in order to convince players to actively enter this new area, the profitability of the sector must be proven.”

The 2013 LAC landscape, with data provided for administrative and commissions expenses in addition to claims, allows for the first significant set of data on combined ratios – and thus a big step closer to offering proof of profitability. And the evidence is clear: only a handful of insurers experienced combined ratios over 100%, and most had more than ample room for profits, with a weighted average of 64%. The data is particularly clear for life and accident products, due to the relative volume of products offered, but there are many examples of health and property products that also showed clear business viability. As more health and property products are offered, the business case should emerge there as well.

The products offered tend to be limited to life and accident, where profits are often higher and there is often government provision of healthcare and other social security programmes. The outreach numbers show little evolution over time in terms of health, property and agricultural covers. The 2008 Africa study found such covers to be a mere fraction of life insurance cov-

erage, despite being much needed by the low-income market. Figure 4 shows the relative coverage of health, property, and agriculture coverage from the landscape studies; across regions, health and property covers are minimal compared to life and accident covers. Only in Asia are a significant portion of insureds receiving coverage for agriculture-related risk, largely the result of government support.

However, what we do see is a shift in the types of coverage offered, and many products are poised to scale up. Instead of comprehensive or primary healthcare programmes with limited growth potential, we see ‘component’ covers offering a smaller ‘slice’ of coverage – such as hospital cash or dread disease covers, often sold as secondary covers. These simpler products, which can fill gaps in public healthcare, are easier to offer and can be sold through mass channels. In LAC, 33% of the new products launched in the past two years contained a health cover, though the effect hasn’t yet been seen in terms of volume of insureds or premium.

Growth

While Asia and Africa seem to be experiencing continued growth in terms of numbers of insureds, the recent LAC landscape has shown that it has continued its growth, outside of Brazil. As insurers learn more about the market, some are exiting (in LAC 11 companies exited microinsurance activi-

FIGURE 4 Proportion of total identified insureds with coverage for health, property or agriculture

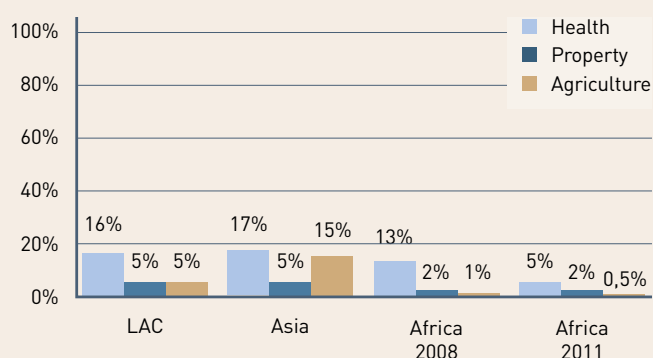
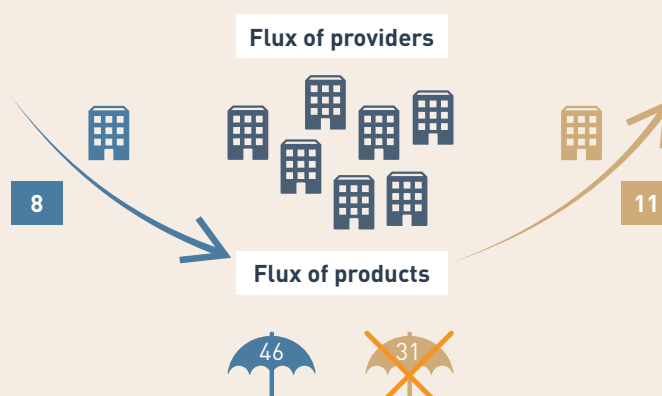


FIGURE 5 Flux of providers and products in LAC



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To get SUAVE (simple, understood, accessible, valuable, and efficient) microinsurance products in the hands of 3 billion people across the globe

PRODUCT EVOLUTION

MAGICAL BALANCE

LOCAL CAPACITY

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ties between 2011 and 2013) while others saw opportunity in this market and entered. This sorting out among the insurers reflects the new-found reality of the market. For some, they simply could not improve their efficiencies. Others found the market more effort than anticipated. Still others were not able to satisfy profit expectations. Over the same time period, 31 products were removed from the market while 46 were newly introduced. In discussions with insurers, this was clearly in response to lessons learned from other products and insurers, and reflects an effort to improve the potential for success of their market interventions.

Continued growth at very high levels over a long period, as seen with the most recent Africa and Asia studies, is also unlikely as the business grows. However, given the limited coverage ratios across regions there is still much potential for growth. The key to growth is centered on distribution; where very large and effective distribution channels are motivated by microinsurance for the markets, microinsurance will continue to grow rapidly. For example, the MNO channels have become massive growth engines for microinsurance in Africa and Asia and will certainly continue to push growth in those regions, and also

likely LAC in the near future. Although the MNO channels bring in very large numbers of policyholders, the related revenue per policy is quite small, even relative to "typical" microinsurance products. For example, in Ghana in 2014, MNOs accounted for 57% of individuals covered by microinsurance, but only 8% of premiums and 4% of claims when considering all products including insurance-linked savings components, or 58%, 39%, and 44% if insurance-linked savings are excluded.⁴

Conclusion

Microinsurance is becoming an important component of the insurance market. In LAC in 2013, it was responsible for bringing in over USD 800 million in premiums with over USD 200 million in pre-tax profits spread around the region. This is significant! The market as a whole, as exemplified in LAC, is expanding to cover more of those traditionally without access to insurance. In LAC, mass market products are expanding, rapidly covering middle and some lower-income markets. Microinsurance products, particularly life and accident, are also substantially expanding through the low income markets of LAC. The mass market spread is likely to now be seen strongly in

Africa through mobile insurance, and later in Asia. Mass and microinsurance together have dramatically expanded access both to those who could not access insurance and to insurers who could not access a wider market.

Products remain centered on the easier, and often more profitable, life and accident covers, though expansion beyond these is slowly evolving as insurers gain confidence in the market and distributors push for greater comparative advantages. Distributors are increasingly showing their dominance in microinsurance, and the large ones are providing greater challenges with their very large commissions, as insurers work to both provide value to clients and retain some profits.

Overall, the state of microinsurance is healthy. Some growth, some contraction. Lessons are being learned and apparently applied. Premiums are growing and distributors are expanding. The market – middle and low income – is gaining improved access to insurance, and continuation is likely with more of a merging of micro and mass insurance. Insurers are doing better at finding their way, and the adolescent microinsurance is moving into adulthood.

4. Authors' calculations from unpublished data generated during a specific Landscape of Microinsurance in Ghana.

How are regulators and supervisors supporting inclusive insurance markets across the globe?

A2ii Secretariat Team¹



Considerations in creating a regulatory framework for inclusive insurance

The creation of a regulatory framework should be based on a thorough assessment of jurisdiction-specific challenges, involve industry dialogue and awareness sessions, and factor in coordination with other authorities.

Important aspects to be considered when creating a specific regulatory framework for inclusive insurance include:

- Implications for the industry: the associated compliance burden created by product registration; actuarial, reporting and consumer protection requirements.
- Implications for the supervisory authority: the supervisory systems and supervisory capacity; adjustments required to supervisory practices, staff training and organisational structures; potential overlaps with insurance regulations and other jurisdictions, such as the banking or cooperative authority.

Policy, regulation and supervision are critical for enhancing access to insurance: they affect how trust is developed between insurance providers and low-income consumers, determine who can operate in the market and at what cost, and can enforce the provision of certain types of insurance. The insurance supervisor plays a crucial role in safe-guarding quality insurance that provides value, as well as in motivating the industry to serve the un-served by removing barriers to access while ensuring a well-supervised industry. Increasingly, supervisors in emerging markets are aware of the need to strike a healthy balance between regulation, enhancing access to insurance and protecting policyholders.

This article gives an overview² of the current status of microinsurance regulation, highlighting recent trends in inclusive insurance markets and providing an outlook on their regulatory implications and potential challenges.

Microinsurance regulation across the globe

Striving to make their insurance markets more inclusive, at least 15 jurisdictions have already adopted a microinsurance-specific regulatory framework, though some are yet to be implemented. In addition, at least 18 countries³ have proposed some form of microinsurance-specific regulation. The creation of an enabling regulatory environment for inclusive insurance has been

approached by different jurisdictions in a variety of ways. There are also significant differences in the maturity levels of the adopted regulations, with some having been in place for around 10 years, whilst others have only recently been adopted.

The table below gives an overview of the existing regulatory frameworks and year of adoption, and summarises some major aspects of the respective jurisdiction's approach to regulation. Most jurisdictions have followed a functional approach, allowing insurers to offer microinsurance as a special business line. This usually involves the adjustment of conduct of business regulations to the type of products and consumers accessing microinsurance, including creating new rules for distribution. The depth of these regulations varies

1. The team includes Onur Azcan, Teresa Pelanda, Hannah Grant, Martina Wiedmaier-Pfister, Janina Voss

2. The authors of this article endeavor to make their best effort to provide updated information on the status of adopted microinsurance regulations around the world, but highlight that the overview provided is not claimed to be exhaustive.

3. For example Colombia, Jamaica, Bolivia, Nigeria, Uganda, Kenya and Bangladesh.

considerably, from a few clauses added to other regulations, to comprehensive and continuously adapted microinsurance frameworks based on a variety of regulatory instruments.

Some jurisdictions followed the institutional approach, creating the option to obtain a dedicated microinsurance license, which means the commission introduced a new type of insurer for this business. Some

regulators are taking an active role in promoting inclusive insurance by making it mandatory for providers to offer it to rural and economically disadvantaged sectors, as is the case in India and Nepal.

Country	Year: Main regulatory documents	Business line approach: examples of topics covered	Microinsurance license
BRAZIL	2011 [Circular 244]: Microinsurance, microinsurance brokers and microinsurance correspondents 2012 [Circular 439]: Microinsurance Company 2012 [Circular 440]: Mandatory parameters for microinsurance plans	Distribution (specific type of microinsurance agent, alternative distribution channels, relationship between distribution partners) Product features Disclosure to the customer Premium values Separate reporting on microinsurance premium values Coverage limits per product Criteria for target public	Microinsurance license for microinsurance company (2012)
CAMBODIA	2011: Circular on Issuance of Temporary License for Microinsurance	Claims settlement Alternate dispute resolution	For commercial microinsurers and community-based health insurers
CHINA	2008: Rule on supervising China Rural Microinsurance on Life & Personal Accident Insurance 2008: Rule and Notice of Related Matters on the Implementation of Systematic Management on the Qualification of Rural Insurance Agents 2009: Circular on Further Expanding the Pilots of Small-amount Life Insurance in Rural Areas 2012: Rule on concept for Comprehensive Roll out of Micro Personal Insurance	Stimulation of pilot projects in rural areas, first restricted to a limited number of regions before allowing for broader roll-out Distribution (encouragement of innovative distribution technologies, microinsurance/rural insurance agents) Simplified policies	No
CIMA (Conférence Interafricaine des marchés d'assurances) ⁴	2012: Regulation of microinsurance operations in CIMA member countries	Distribution/intermediaries (innovative distribution channels, e.g. mobile network operators, community based associations) Risk types covered by microinsurance policies Product types (e.g. group insurance, agricultural insurance, index insurance) Minimum capital requirements	Microinsurance enterprises (stock company or mutual)
GHANA	2013: Market Conduct (microinsurance) Rules	Microinsurance contract Disclosure to customer Rating of microinsurance products Claims handling	No

4. Benin, Burkina Faso, Cameroon, Central African Republic, Congo, Comoros, Ivory Coast, Gabon, Guinea, Equatorial Guinea, Mali, Niger, Senegal, Chad and Togo.

Country	Year: Main regulatory documents	Business line approach: examples of topics covered	Dedicated microinsurance license
INDIA	2001: Obligations of Insurers to Rural and Social Sectors 2005: Microinsurance regulations 2004/2011: Reserve Bank of India directives 2013: IRDA circular 2015: (Micro Insurance) Regulations	Mandatory provision of insurance to rural and social sectors Microinsurance-supporting quota fulfilment Products and definitions Reference to Code of Conduct for Microinsurance Composite products Commission caps between 10% and 20% Reduced training requirements for microinsurance agents Expanded range of intermediaries	No
MEXICO	2008 (Circular CNSF S-8.1): Product registration 2008 (Circular CNSF S-2.1): Distribution	Distribution (special intermediaries and their training requirements) Product features Disclosure to customer	No
MOZAMBIQUE	2011: Regulation of the Conditions of Access to and Exercise of Insurance Activity and its Intermediary Activities	Licensing Intermediaries Solvency margins	No
NEPAL	2014: Micro Insurance Directives, 2071	Microinsurance business mandatory for all insurers Distribution (microinsurance agents) Claims settlement Dispute resolution	No
PAKISTAN	2014: Securities and Exchange Commission (Microinsurance) Rules	Distribution (microinsurance agent and their functions) Key features of microinsurance products Consumer protection and disclosure: transparency, fair prices, privacy, recourse, code of conduct for microinsurance agents	No
PERU	2007 (SBS 215/07): Microinsurance resolution 2009 (resolution SBS 14283/09): Revised Microinsurance resolution	Distribution (intermediaries) Product features: limited exclusions Disclosure to customers Specific reporting requirements	No
PHILIPPINES	2006 (Circular 9-2006): Microinsurance Regulation and Declaration of Policy Objectives 2010 to 2014 ff: over 20 regulatory provisions ⁵	Product-related and contract rules such as standard contract, bundling of life and non-life allowed with separate underwriting, Specific logo for microinsurance Agent licensing and training, and the role banks can play Alternative dispute resolution Separate performance standards Reduced capital requirement for those having 50 % of their portfolio in microinsurance Formalisation requirements to stop informal insurance provision	Microinsurance license for Microinsurance Mutual Benefit Organisations
SOUTH AFRICA	2015: Insurance Bill (giving effect to the National Treasury's Micro-insurance Policy Document)	Distribution (intermediary requirements) Product standards and benefit limits Supervision and enforcement Code of Conduct Consumer recourse	Microinsurance license (including a transition path for informal providers)
TAIWAN	2009: Directions for Insurance Enterprises Engaging in Micro-Insurance Business	Product design: simple (standard clauses), one year term, covering only one peril Obligation to establish a microinsurance customer service unit Separate reporting	No
TANZANIA	2013: The Insurance Act (CAP.394) "Regulations" (Made under sections 167): The Micro-Insurance Regulations	Distribution (registration of a microinsurance agent) Products Policies Training of insurance officers Settlement of claims Handling of complaints	No

5. The Insurance Commission Philippines has issued a comprehensive regulatory framework for microinsurance: Insurance Law, at least 16 IC regulations including the one of 2006; two joint circulars of the Insurance Commission with the Securities and Exchange Commission and the Cooperative Development Authority; three Central Bank Circulars on insurance intermediation by Rural Banks; and an Order of the Department of Finance on reduced capital requirements.

Non-traditional distribution channels are adding complexity to microinsurance supervision

Over the last few years, new business models have sparked major changes in inclusive insurance markets. The increase of non-traditional mass channels, along with the advent of digital finance, have introduced new entities to the value chain, changed the mode of interaction between insurers and customers, and facilitated the development of innovative products. In a number of areas traditional regulatory constructs no longer apply, which has resulted in a need for a paradigm shift for insurance supervisors.

For example, the assumption that the licensed insurer is the strongest party in the value chain is no longer guaranteed. Mass distribution channels, such as mobile network operators in Africa or retailers in Latin America, entering the insurance space often wield considerably more power than the insurer and can hold them to ransom to extract higher rents for access to the channel. This creates new consumer protection challenges for supervisors. At the same time, many of these mass distribution channels sit outside of insurance supervisors' regulatory authority, thereby limiting their ability to act. Hence, there is an increased need for supervisors to coordinate with other financial and non-financial regulators and supervisors; however, little information is currently available on how supervisors should go about doing this in the most efficient and effective manner.

The scale and pace of growth of coverage in some developing markets from the massive expansion of non-traditional distribution is also worth noting. This is a positive development, with insurance increasingly available to low-income people living in remote or urban areas. It has also helped stimulate private sector interest as new opportunities arise from economies of scale. However, the speed and scale of growth challenges the low-risk assumptions previously associated with inclusive insurance markets, meaning supervisors must look at proportionality in different ways, and enhanced supervision potentially being required to protect consumers and avoid systemic shocks.

The development of innovative and more complex insurance products such as mobile insurance and index insurance is also introducing additional challenges for insurance supervisors. Supervisors need to be able to keep up with market innovations and ensure they have a good understanding of new types of products being developed, as well as the right tools to supervise them.

Overall, the key theme uniting the challenges mentioned above is the need for enhanced supervisory capacity building to ensure supervisors are equipped to deal with changes occurring in their markets. Supervisors need to be able to strike a careful balance between ensuring consumers remain adequately protected and trust is maintained whilst not stifling market innovation.

“ Supervisors need to keep up with market innovations and ensure they have a good understanding of new types of products as well as the right tools to supervise them. “

“ The assumption that the licensed insurer is the strongest party in the value chain is no longer guaranteed. “

Important lessons from the last 10 years of microinsurance regulation

The following lessons are emerging from drafting and implementing microinsurance regulatory frameworks enabling inclusion:

- Other rules that may be issued later, for example on mass distribution, can over-rule the microinsurance rule and create a regulatory conflict.
- Insurers may not register products under the microinsurance framework if they see an increased compliance burden.
- Regulations may have unintended consequences, such as the industry fulfilling quotas but not developing a sound business approach.
- A regulatory framework can be best implemented under constant performance monitoring and continuous adjustment of the provisions as needed.
- A regulatory framework alone is not sufficient to grow inclusion; complementary efforts in the field of financial education and industry training are also required.
- Performance monitoring of the microinsurance business line through separate reporting on microinsurance allows supervisors to observe growth and quality of products and services.
- Regulations not taken up by the industry may not have the right mix of obligations and incentives to establish a dedicated microinsurer or engage in this business line.
- A test and learn approach by the supervisor is required to respond to fast-developing market practices, for example in mobile insurance and digital distribution.

Regulatory Challenges in West and Central Africa



Luc Noubissi

Senior Insurance Specialist, CIMA



“ There is a need to address the lack of understanding of the new international standards and how they can be applied in a manner which is consistent with the nature of insurance markets in the region. ”

Despite notably establishing a regional cooperation agreement regarding insurance supervision, and considerable commonality in banking and currency, the CIMA's markets (covering central and western Africa) remain nascent with insurance penetration at just one percent of GDP. Growth over the past five years has been positive, however, and the market continues to show signs of being well-placed to develop further. New regulatory developments, growth in the complexity of the insurance business and the need for greater consumer confidence put the regulator covering these countries under increasing pressure to deliver better supervision.

CIMA

Insurance in West and Central Africa operates in the regional group known as the *Conférence Interafricaine des Marchés d'Assurances* (CIMA). The region currently encompasses 14 countries, mostly former French colonies, scattered into two sub-regions (UEMOA and CEMAC) with their respective central banks (BCEAO and BEAC). There is transferability between the two monetary zones and France guarantees the convertibility of the local currency with Euro¹.

With 146 million inhabitants, the region represents roughly 2% of the world population. Two-thirds of the population lives on less than USD 2 per day. Agriculture, which weights around 30% of GDP, is the backbone of the economy.

The mandate of the supranational regulator

The initial regulatory body, CICA, was created in 1962 and based in Paris. Following many reforms, the Treaty signed in 1992 instituted CIMA as the supranational regulatory body with a unique insurance code in force across the region. The mandate of CIMA includes creating or strengthening synergies between countries in order to reinforce technical and financial capabilities of local actors, and ensure the financial soundness of institutions and integrity of insurance markets. The mission of CIMA is to assist national authorities in serving the public interest and effectively achieving insurance regulatory goals, consistent with the wishes of State members. CIMA has been created as an effective catalyst for financial inclusion, stability and development of African economies. Although the achievements so far are appreciable, there is still much room for improvement.

1. 1 euro = 655.957 XOF - XAF

Low insurance penetration

Insurance penetration is a measure of the level of development of insurance markets and depends on consumer confidence; consumers generally won't purchase insurance products unless they are confident that insurers will pay legitimate claims. Effective insurance regulation and supervision builds confidence in the insurance sector by protecting consumers from the risk that an insurer will have insufficient resources to pay claims or will treat them unfairly. Increasing confidence is also a precondition for building greater financial inclusion, which can broaden and increase insurance markets.

In CIMA countries, the penetration rate (the ratio of premiums written to GDP) is extremely low, ranging from 0.34% to 1.89%. Table 2 illustrates that all CIMA countries are in the bottom half of 184 countries assessed in a recent global survey, with insurance penetration for the region averaging 0.9% of GDP. If insurance penetration were raised to levels seen in greater Europe², there would be an approximate increase in premiums written of USD 8.7 billion per year.

The current state of the industry is defined by limited products, mostly credit life offered through MFIs. Only a few insurers target the low-income segment or rural populations which constitute the vast majority of the population, and products are complex and expensive for this demographic. Lack of local expertise could explain the current state of the market, as most of the member States are underdeveloped countries with very limited actuarial experience. According to the figures, the microinsurance market in CIMA is still nascent and there are reasons to expect exponential growth in the upcoming years, should the needs and expectations of the population be met.

Alignment with international standards and best practices

Improving insurance regulation and supervision in the region is vital to building confidence in insurance markets, facili-

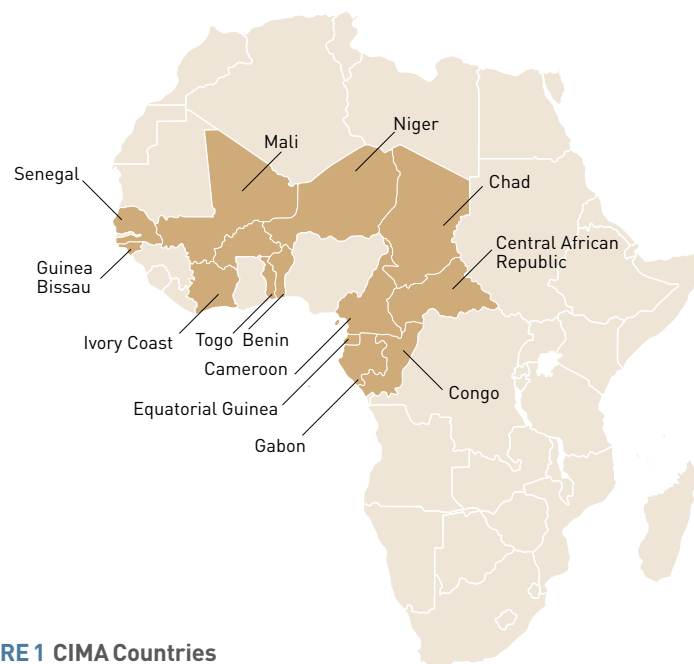


FIGURE 1 CIMA Countries

tating insurance market development and increasing potential for greater financial inclusion.

In recent years, CIMA embarked on a vast project to improve the regulatory and supervision frameworks through a multi-year strategic plan. With the support of international partners, the insurance code was modified in 2012 to include microinsurance. This new regulation introduces index insurance and enlarges distribution to include new players such as mobile network operators and community-based associations.

This microinsurance regulation is the first step of the plan and needs to be improved with specific elements on premium and benefit limits and index insurance, among others. The next steps of this microinsurance development plan include a coordinated partnership among stakeholders in order to significantly improve financial inclusion and boost business growth, encompassing aspects of product development, technology, research, communication and capacity building.

The legal, regulatory and supervisory frameworks do not fully comply with the International Association of Insurance Supervisors (IAIS) Insurance Core Principles

(ICPs) which were strengthened substantially in 2011 and 2012 in response to issues raised by the global financial crisis. In many CIMA countries, there is a lack of knowledge about the ICPs and how to improve capacity in a manner that is consistent with them. On the other hand, only partial assessments of the application of ICPs have been undertaken through the IAIS Thematic Peer Review Processes. Completing a comprehensive assessment would likely require amendment to several regulations to formally implement the proposed new reporting regime before filling the gaps identified. More specifically, there is a need to address the lack of understanding of the new international standards and how they can be applied in a manner which is consistent with the nature of insurance markets in the region. There is also a need to improve insurance supervisory capacity for off-site financial review of insurers.

Need for formalisation

Although there is general consensus that "whatever is informal is illegal", there are reasons to believe that most insurance business is likely to happen informally at the low-income end of the market, including through small community-based mu-

2. 6.8% in 2013 [Source: SWISS RE – SIGMA]

Country	Population	GDP (current billions \$)	GDP per capita (current USD)	Poverty headcount ratio at USD 2 a day (% of population)	Agriculture, value added (% of GDP)
BENIN	10.050.702	7,6	751,92	75,32	32
BURKINA FASO	16.460.141	10,7	650,06	72,56	35
CAMEROON	21.699.631	25,3	1.165,92	30,36	22
CENTRAL AFRICAN REPUBLIC	4.525.209	2,2	486,17	80,09	52
CHAD	12.448.175	12,9	1.036,30	46,7	56
CONGO (REPUBLIC OF THE)	4.337.051	13,7	3.158,83	74,4	3
EQUATORIAL GUINEA	736.296	17,7	24.039,25	76,8	10
GABON	1.632.572	18,4	11.270,56	19,59	4
GUINEA-BISSAU	1.663.558	0,8	480,90	69,3	59
IVORY COAST	19.839.750	24,7	1.244,98	46,34	24
MALI	14.853.572	10,4	700,17	78,66	42
NIGER	17.157.042	6,8	396,34	75,23	38
SENEGAL	13.726.021	14,0	1.019,96	55,22	17
TOGO	6.642.928	3,8	572,04	52,65	31
TOTAL CIMA	145.772.648	169,0	1.159,05	58,77	30
Sub-Saharan Africa	912.212.311	1.485	1.628		14
World	7.043.902.890	72.682	10.318		3

TABLE 1 Socio-economic indicators³

tual entities. A challenge for the regulator is to identify the extent of informality and recognise the nature of abuse among those that choose to remain “outside of the radar screen”. Understanding the nature and extent of this market and consumer protection risks is a key need. Once the final microinsurance framework is adopted, a suitable transition period will be allowed for all players to comply with the new regulations.

The microinsurance development plan

Above the adoption of specific microinsurance regulation, the Supervisor of CIMA intends to play a key role in developing microinsurance across the region. A plan adopted in 2014 by the ministries in charge of insurance aims to achieve significant business volumes, while ensuring consumer protection and a real added value to the economy. It is based on a harmonised partnership among stakeholders (regulator, insurers, NGO, international

organisations etc.) to conduct studies, capacity building and product development. It also seeks to facilitate the availability of information on microinsurance business, promote consumer education and instill an insurance culture in low-income households. Microinsurance Learning Sessions, held in September 2014 in Douala, were a milestone in the development of microinsurance in the region. With almost 350 participants from 24 countries, the event offered experts a forum to discuss opportunities and challenges of targeting low-income groups.

3. Source Axco Insurance Products - Rankings are based on 184 countries surveyed. - Currency denomination in USD.

Country	Written premiums (\$mn)	Insurance penetration (%)	Premiums per capita (\$)	GDP per capita	GDP (\$mn)	Population (% of GDP)	World penetration ranking (#)
BENIN	66.93	0.90	6.66	736.58	7,403.13	10.05	134
BURKINA FASO	83.17	0.78	5.05	651.65	10,726.33	16.46	139
CAMEROON	287.84	1.11	13.26	1,196.69	25,967.67	21.70	124
CENTRAL AFRICAN REPUBLIC	8.02	0.37	1.75	472.91	2,164.04	4.58	167
CHAD	19.85	0.18	1.59	885.11	11,018.02	12.45	174
CONGO (REPUBLIC OF THE)	109.44	0.95	25.23	2,656.69	11,522.21	4.34	159
EQUATORIAL GUINEA	25.09	0.11	34.84	32,038.87	23,067.98	0.72	176
GABON	192.65	1.05	118.01	11,256.52	18,377.08	1.63	126
GUINEA-BISSAU	NA	NA	NA	NA	NA	NA	NA
IVORY COAST	391.22	1.59	18.97	1,196.91	24,680.37	20.62	103
MALI	55.98	0.56	3.77	677.87	10,068.82	14.85	154
NIGER	42.90	0.61	2.50	407.28	6,987.71	17.16	150
SENEGAL	187.46	1.24	13.30	1,075.22	15,149.80	14.09	116
TOGO	73.39	1.89	11.05	584.39	3,882.13	6.64	94

TABLE 2 Insurance penetration in CIMA

In its market development mandate, the supervisor is committed to adapting regulations to support the evolution of inclusive insurance. The supervisor ensures that the activities of all microinsurance stakeholders (providers, intermediaries and other partners) comply with laws and regulations. In order to avoid any regulatory burden which can weaken growth, it is important to apply a proportionate approach in supervision while creating incentives for low-income segments. The CIMA microinsurance plan provides the basis for support from all partners, and any technical assistance in achieving its objectives is more than welcome. With the support of multilateral organisations⁴, some projects have already been engaged in terms of feasibility study, principles and standards assessments, development of index insurance, mobile insurance.

Looking forward

The creation of a unique regulatory body between CIMA countries is based on the idea that a large single insurance market with common regulations and regulatory authority will result in more effective insurance supervision. The 1992 CIMA treaty is committed to improving insurance regulation and moving towards adherence with international standards for insurance regulation and supervision. The recent adoption of microinsurance regulation and development plan indicate the dynamism and determination of the supranational regulator to fully play its role in building strong insurance markets and help people break out of cyclical poverty.

“ Although there is general consensus that “whatever is informal is illegal”, there are reasons to believe that most insurance business is likely to happen informally at the low-income end of the market . “

4. The World Bank, FIRST Initiative, Agence Francaise de Development, GIZ, among others.

The role of microinsurance in disaster risk management



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Over the past 20 years, natural disaster losses have been steadily climbing, exacerbated by growing urbanisation, environmental degradation and increases in the frequency of hydro-meteorological events. Developing countries are particularly vulnerable as their financial and regulatory systems often cannot keep pace with the rapidly growing asset bases at risk and do not have adequate resources to dedicate to reducing exposure or to responding effectively to an emergency.

Many governments and other stakeholders are increasingly recognising the important role of microinsurance. Microinsurance offers low-income households, farmers and businesses access to post-disaster funding, safeguarding their livelihoods and providing for rebuilding¹. In addition, microinsurance can help to provide economic incentives for loss-prevention activities by offering lower premiums as a reward for risk-reducing behaviour. It can promote and increase risk aversion, leading to a change in behaviours or more active risk management. In that way, microinsurance is much more effective than post-disaster relief, and a more dignified means of coping with disasters where such means are often inadequate, as this support can be ad hoc, poorly targeted and slow in being disbursed.

The last decade has witnessed strong growth in microinsurance, reaching more than 260 million people worldwide². Overall, however, market penetration remains relatively small. Micro disaster insurance can cover natural catastrophe events such as earthquakes, floods,

cyclones, and droughts. Traditional insurance programmes have consisted of indemnity insurance, which pays claims based on actual losses and requires an extensive effort and resources to assess individual losses following an event. More recently, parametric insurance has emerged, which is a type of insurance that does not indemnify the pure loss, but ex ante agrees to make a payment upon the occurrence of a triggering event, usually in the form of an index related to the intensity of the catastrophic natural event. Parametric insurance reduces the transaction costs involved in writing and administering insurance policies because there is less need for actual loss assessment for payment of claims.

So which factors impact the development of microinsurance as a tool for disaster risk management?

Demand for microinsurance

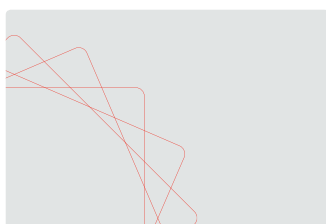
On the demand side, the development of microinsurance is first and foremost explained by a big protection gap in the face of many

1. Mechler, R., Linnerooth-Bayer, J., Pepiatt, D. (2006). "Disaster insurance for the poor? A review of microinsurance for natural disaster risks in developing countries", ProVentum Consortium and IIASA, Geneva Switzerland and Laxenburg, Austria.
2. Microinsurance Network (2014). "Exploring new frontiers: The potential of impact investments in microinsurance", Microinsurance Network: Luxembourg.



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risks low-income families and individuals are confronted with. To date, the demand for microinsurance has been relatively low due to the mix of several conditions, including economic and social factors, trust, financial literacy, and the existence of informal risk-sharing networks amongst individuals in low-income countries³.

Economic factors such as the price of insurance and the level of personal wealth have been shown to influence the demand for microinsurance. Estimates of the price sensitivity of microinsurance demand are usually high⁴, hence, the low demand could be due to the fact that households perceive the level of premiums to be too high. The effect of wealth on microinsurance purchase also seems positive on the grounds that wealth provides a higher level of liquidity and potential access to credit and, therefore, facilitates the purchase of bundled insurance. The wealth effect of microinsurance is distinct from the effect in traditional insurance, where it translates into a higher level of potential loss, and therefore increases the needs for insurance.

Social and cultural factors also drive the demand for microinsurance. Surprisingly, many works have shown that more risk-averse households are less likely to purchase microinsurance. One explanation could be that households view insurance as risky or that they do not fully understand the product. The presence of basis risk in the case of parametric insurance, which refers to the situation where insurance benefits are not perfectly correlated with underlying losses, could also explain this result. Policy-holders would perceive basis risk as an increase in uncertainty⁵.

Besides risk aversion, trust in insurance contracts can also be a significant barrier to participation. This is especially relevant in environments with weak legal systems for enforcing payment of valid claims. Low-income individuals are unsure about paying in advance for a service that they may or may not receive in the future from an institution that they do not know, or worse, do not even trust. Hence, low financial literacy and a lack of awareness of insurance explain the low insurance demand in developing countries.

Risk exposures also affects microinsurance participation⁶. Having experienced personal loss generates demand for microinsurance. It also seems that personal losses are more strongly associated with enhanced demand than observations of losses incurred by other people nearby, even though such observation of loss by others enhances the demand for flood insurance as well. Yet, depending on the nature of the shocks, such shocks might affect people's ability to cope with loss by reducing the availability of wealth to pay for the premium.

“ Both insurers and governments have an important role to play in making microinsurance a successful tool to help low-income people in coping with increasing disaster risk. “

3. Eling, M., Pradhan, S., Schmit, J. T. (2014), “The determinants of microinsurance demand”, The Geneva Papers on Risk and Insurance – Issues and Practice, 39, 224-263.

4. Cole, S. et al., (2013), “Barriers to household risk management: evidence from India”, American Economic Journal: Applied Economics, 5(1), 104-135.

5. Eling et al., (2014) Ibid.

6. Turner, G., Said F., Afzal, U. (2014), “Microinsurance demand after a rare flood event: evidence from a field experiment in Pakistan”, The Geneva Papers on Risk and Insurance – Issues and Practice, 39, 201-223.

Finally, informal risk-sharing networks, which are largely developed to cope with risk in developing countries, could deter the demand for microinsurance, since they are seen as substitutes. On the other hand, such networks could play an important role in extending insurance knowledge to the wider community, affecting positively the demand for insurance.

Supply of microinsurance

The issue of the supply of microinsurance is intrinsically related to the concept of insurability, i.e. the conditions by which insurers will in principle offer cover for a particular risk. According to Berliner⁷, to be insurable in actuarial terms, risks must be independent and estimated reliably so that the law of large numbers must apply, i.e. the larger the number of mutually independent risks, the higher the ability to predict the average loss. In addition, the maximum loss per event must be manageable in terms of insurer solvency, and the premium must also be affordable.

Many factors therefore affect insurability in microinsurance including risk assessment, correlated risks and transaction costs⁸.

In terms of risk assessment, a number of issues arise from the independence of risks and the quantification of loss probabilities, such as a lack of data, non-independence of risks and increasing variability in loss frequency and intensity. Many studies point out that the provision of coverage against risks due to climate change is limited due to scarce information on the underlying risk⁹.

“ Many works have shown that more risk-averse households are less likely to purchase microinsurance. “

In addition, the risks of natural catastrophes affect large areas at the same time. They affect large portions of the population or risk pool simultaneously, violating the assumption of statistical independence that makes the law of large numbers applicable. Microinsurance is not able to disseminate risks easily across members of the scheme. Related to this, a small risk pool is also an important issue, which makes microinsurance highly vulnerable to losses from low-frequency, high-severity events. This raises the question of insufficient financial capacity in the case of natural catastrophe losses, which may lead to a significant risk to insurers' solvency, especially for small and local schemes. This high insurers' insolvency in the face of such risks requires further diversification of risks.

Transaction costs are also one of the major reasons for the failure of insurance markets in covering disaster risks as these costs, along with high loading factors, make premium unaffordable. These high loadings result also from violations of insurability criteria due to limited historical data and non-independent risks¹⁰.

How to reach scale

Insurability of risk events for low-income people is challenged by various issues, and overcoming these issues is a crucial step forward to increase coverage. A first issue relates to increasing capacity of microinsurance schemes. This could be done by means of risk transfer or risk financing, such as reinsurance, index-based reinsurance, derivatives. Various works or experiences have shown the usefulness of providing reinsurance for microinsurance schemes¹¹. Another important way to increase insurability is to make the risk pool larger. This would allow sharing risks amongst a higher number of households or individuals and making the microinsurance

schemes, as well as their members, less vulnerable to high consequence catastrophes. Yet, this would necessitate expanding the organisation of the scheme to a higher level than the local level.

Ways to increase the demand for microinsurance is to build trust in insurance contracts and providers, whether through reinsurance participation and through a better understanding of how insurance works. Increased knowledge in insurance and trust in claims payments is definitely a way to increase demand. Institutionalising financial literacy in insurance is part of such a strategy. Reducing the cost of microinsurance, for instance through subsidy or tax incentives, is also likely to increase demand.

Both insurers and governments have an important role to play in making microinsurance a successful tool to help low-income people in coping with increasing disaster risk. Developing such products will not only benefit the insurance industry itself but also society in general.

“ A small risk pool is also an important issue, which makes microinsurance highly vulnerable to losses from low-frequency high-severity event. “

7. Berliner, B. (1982). Limits of insurability of risks, Englewood Cliffs.

8. Biener, C., Eling, M. (2012), "Insurability in microinsurance markets: an analysis of problems and potential solutions", The Geneva Papers on Risk and Insurance – Issues and Practice, 37, 77-107.

9. Dlugolecki, A. (2008), "Climate change and the insurance sector", The Geneva Papers on Risk and Insurance – Issues and Practice, 33, 71-90.

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Agricultural insurance fever – a development fad or here to stay?



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Agricultural insurance is having a bit of a moment. It is increasingly acknowledged by the international development community and by insurers as an important financial inclusion and risk management tool, with a spate of new initiatives launched, backed by funds and policy discussions. However, capitalising on this momentum is proving easier said than done, as emerging economies continue to falter on commitment to agricultural insurance programmes, and with questions of scale and government subsidies looming large. Further, the emphasis placed on making agricultural microinsurance financially viable risks eclipsing concerns over the protection of smallholders.

As it gains recognition and finds its place in development and financial inclusion discourse, we take a look at the state of agricultural insurance today and reflect on the critical questions dividing stakeholders in this innovative sector to ask: is agricultural microinsurance a development fad or is it here to stay?

A continuous growth fuelled by public support and innovation

The variety and volume of agricultural insurance solutions has expanded considerably in the last 50 years¹. In developed economies, premium volumes have risen under the impulse of favourable public policies, whether in the form of premium subsidies or public reinsurance provision. The global volume of agricultural premiums increased

dramatically between 2004 and 2007, rising from USD 8 billion to approximately USD 15 billion.

This spectacular growth is partially due to the increase of agricultural commodity prices, and therefore of the sums insured. It is also the consequence of rapid market development in emerging countries such as Brazil, India, and China which is now the second largest market in the world². In these three countries, government support has been critical for the market to reach scale.

India offers a very good illustration of public support leading to product innovation and social inclusion. India's crop insurance programme started in 1999, and covered more than 25 million farmers by 2012³. India has succeeded like no other country in offering insurance for smallholder farmers, thanks

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 2. Mahul, O., & Stutley, C. J. (2010). *Government support to agricultural insurance: challenges and options for developing countries*. World Bank Publications.
 3. Mahul, O., Verma, N., & Clarke, D. (2012). Improving farmers' access to agricultural insurance in India. *World Bank Policy Research Working Paper, 15987*.



“ Should an admission of the need for government support be taken as a failure, when we consider that the three largest agricultural insurance sectors, which are found in the USA, China and Spain, are subsidised to the tune of 80%? “

to a continuous effort of innovation and financial support to the sector to make policies more affordable.

India was also one of the first countries to offer index-based insurance. Unlike traditional insurance, index-based insurance relies on a proxy to evaluate the loss incurred, rather than on an in-the-field loss adjustment. A trigger for indemnification is established. For example, under a certain amount of rainfall, insured farmers would receive a pay-out. Index insurance can be based on various data sources, like area-yield indices, rainfall, temperature, livestock mortality or vegetation indices estimated through satellite imagery. This technological shift from traditional insurance holds significant potential to reduce costs and make agricultural insurance available even for smallholder farmers. However, basis risk, which arises when losses are not perfectly correlated with the index, is an issue. Other challenges to improve agricultural insurance's access include affordability, lack of financial education, appropriate legal framework, distribution issues or reinsurance capacity.

Reaching scale or reaching smallholders?

Agriculture insurance matters because 2 billion people's livelihoods depend on smallholder farms. As a relief instrument, agricultural insurance covers farmers against catastrophic losses. As a means for development, it protects their investments and can improve their revenues.

As the Millennium Development Goals come up for evaluation with the 2015 deadline, it seems that the agricultural microinsurance sector is reaching a critical juncture. Experimentation through agricultural insurance pilots worldwide has grown impressively, with many heads turned in the international development donor community, and to some degree in the insurance and reinsurance sectors. The spurt of recent initiatives, backed by funds in the case of the Global Index Insurance Facility (GIIF) and by policy discussions in the case of the Global Action Network, is testament to this, as is the interest shown by AXA and Swiss Re, to name but a few. At the same time, emerging and developing economy



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governments have been somewhat more impassive, dithering over the importance of agricultural insurance in the context of their economies and their rural constituencies. It is this dissonance that makes the next phase so interesting and also so crucial.

Outside the cases of countries where government support is significant – India, Mexico, Senegal etc. – agricultural insurance has demonstrated proof of concept and is now the subject of long debates on technical or quasi-technical questions, from basis risk to distribution, to product design to marketing. However, creeping in almost in opposition to any triumphalist statements is the question of scale, which has largely been elusive where the state has not stepped in. Of course, there are success stories such as Kilimo Salama's transformation into the limited company ACRE, the sole dedicated agricultural microinsurance initiative known to us to have secured outside investment.

Other pilots are showing promising figures, with GIIF-funded pilots alone totalling 750,000 cumulative clients by 2015.⁴ Yet from the perspective of a social investor like the Grameen Crédit Agricole Foundation, there appear to be few, if any, investable opportunities on the horizon; a fact which translates loosely as few pilots ready to be taken to scale.

What does the future hold for agricultural insurance?

This realisation should not put a dampener on the promise of the sector. Rather, it should invite all concerned to take stock of where we are and consider some crucial questions. Can scale be reached without government support? Should an admission of the need for government support be taken as a failure, when we consider that the three largest agricultural insurance sectors, which are found in the USA, China and Spain, are subsidised to the tune of 80%? If subsidised funding is needed either to help developing country insurance sectors work towards scale, and possibly even maintain it, how can this be done over the long term? And amidst all the talk of scale, and portfolio and macro-level approaches designed to bring it closer, how can we make sure that smallholder farmers don't become an afterthought?

Answering these questions is incumbent on all stakeholders in the sector, and the probability of getting the recipe right will be higher if market development activities in the next phase are approached collectively rather than in a spirit of competition. Bundling insurance with credit or farm inputs is deservedly often presented as a solution to low demand. This is indeed a very promising path, as long as bundling brings more value to smallholder farmers.

Stocktaking should veer away from navel gazing and turning over the same stones. As we admire what has been achieved, the recent momentum should be exploited to place agricultural insurance and agricultural finance at the centre of post-MDG discussions around development, taking the topic outside the usual discussion fora. The angles of attack are myriad. Indeed, agricultural insurance can be couched in terms of food security, market development, capital market resilience, climate change, disaster management and livelihoods. As transversal a topic as it is, it needs to be placed on the political agenda at the highest level. Agriculture is a public good just as much as it is a market, and should be treated as such as efforts are made to capitalise on its market potential by developing agricultural finance. The world's 450 million smallholder farmers deserve as much.

“Agriculture is a public good just as much as it is a market, and should be treated as such as efforts are made to capitalise on its market potential by developing agricultural finance.”

4. <https://www.indexinsuranceforum.org/overview-global-index-insurance-facility>

Microinsurance: What does the future hold?

Martin Hintz

Head of
Microinsurance
Allianz SE
Asia, Africa and
Latin America



**“ It is time we take
customers to the next
level. “**

What are the major upcoming opportunities in microinsurance?

I would like to focus on one of many opportunities: the deepening of the customer relationship. There is ample scope to provide more and better insurance to the micro-insurance customers of today. If products have the right fit and are well explained, we see great interest from customers in buying more insurance. Because let's face it: although hundreds of millions of customers have come into the fold of insurance over recent years, most are still severely under-insured. It is time we take customers to the next level.

This would generate more economic returns for companies and more social benefit for customers.

What are the key challenges?

Here I would focus on what stands in the way of deepening customer relationships – as insurers we need to get closer to customers. In our emerging consumers target segment, there is almost always a distributor or administrator between us and the customer. That makes it difficult to position our brand directly to customers and create customer stickiness. Because priorities of insurers and distributors don't always align, it is also a challenge to roll-out cost efficient insurance education measures that can address a lack of general insurance awareness among the target segment.

Still I am optimistic that these challenges can be overcome. There are emerging direct approaches around mobile, and distributors start to see the social and economic value of insurance deepening.

Muhammad Khalid Qureshi

Manager Channel
Development
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What are the major upcoming opportunities in microinsurance?

The most attractive and relevant opportunity for microinsurance is the expansion of the branchless banking network. These networks have retail presence all across the operating countries, thus enabling mass level penetration. Making small-ticket insurance products available through this channel would not only achieve the objective of availability of the product, but the middle man would help in tackling the challenge of customer awareness.

However, dealing with distribution partnerships poses its own set of challenges where the distribution partner holds the bargaining power because of high customer affinity, and can pit insurance companies against one another in a price war. A way out for insurers is to set up these networks on their own, rather than relying on distribution partners.

Development of the microfinance market also provides a good customer base to cross sell insurance products. Other opportunities include embedding insurance in lieu

“ Commercially, insurers are still practicing personal selling which does not generate the pull required to achieve scale in microinsurance. ”

of usage of GSM and branchless banking services. With the advent of smartphones and its mass level penetration in under-developed and developing countries, smart applications can assist in providing the customer with detailed information and enable a smooth and easy subscription process.

What are the key challenges?

The key challenges can be classified into three major categories: challenges related to the target market, challenges associated with commercial distribution, and regulatory challenges.

Customer awareness and literacy form the primary challenge as the majority of the population is unaware of the need for insurance. Commercially, insurers are still practicing personal selling which does not generate the pull required to achieve scale

in microinsurance. Where a particular segment is aware of its insurance needs, customer outreach poses an enormous challenge due to limited access to and of insurance companies.

Product design is also a major area to be worked on, as the majority of products on offer are conventional ones which are tagged with financial services intended for the low-income market. Reinsurers are also taking a cautious approach towards such portfolios because of the lack of proper infrastructure and regulatory support.

Dependency of insurers on distribution partners is yet another commercial angle that should be addressed by the insurers collectively. For regulatory purposes, microinsurance should have a standard definition as there is no tool in place to gauge the income level of the insured which forms the basis of the definition of microinsurance.

Afua Boahemaa Donkor

Executive Director
Star Microinsurance,
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STAR MICROINSURANCE SERVICES LIMITED.



What are the major upcoming opportunities in microinsurance?

For the past seven years, I have witnessed the evolution of microinsurance distribution, from bundling with credit products to the recent distribution through mobile network operators.

Microinsurance products are going to see an explosion in its mode of distribution. More untraditional distribution channels are going to identify microinsurance as a useful product in retaining clients, increasing their clientele base and, most importantly perhaps, increasing their income stream. This will lead to microinsurance providers having to become more creative in product designs and bundling these products to make them suit these distribution channels. The microinsurance evolution has also witnessed regulators becoming more open and flexible to the needs of these products hence giving the providers with the free hand to be innovative.

What are the key upcoming challenges?

In the past few years, microinsurance has attracted a lot of attention. This attention can be positive or negative and with it has come the rapid evolution of products and distribution channels which shows promise for ensuring that microinsurance is readily available.

However, will microinsurance really be available to the low-income earners we are supposed to serve, given the introduction of so many mass marketing channels and products? This challenge is real and one we as providers will have to start thinking seriously about.

We providers are faced with the fact that competition will drive us more into mass marketing/distribution channels, which might eventually mean we do not provide our microinsurance products to the target we set out to serve.

Regulators will realise that with these developments, they will have to act quickly and provide the right legal framework to encourage players in the market to not forget about the real targets that need serving most.

“ The microinsurance evolution has witnessed regulators becoming more open and flexible to the needs of these products hence providing the providers with the free hand to be innovative. ”

What are your predictions for the sector?

Let us know on Facebook, Twitter or LinkedIn

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About the Microinsurance Network

The Microinsurance Network is a global network of microinsurance experts dedicated to promoting access to valuable microinsurance low-income populations.

Find out more : www.microinsurancenetwork.org
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