

MICROINSURANCE

Improving risk management for the poor

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March 2005

The Working Group on Microinsurance, initiated by CGAP and comprising of representatives from donors, multilateral agencies, NGOs, private insurance companies and other interested parties, was established in 2001 to promote the development of insurance services for the poor through increased stakeholder coordination and information sharing. Currently chaired by the International Labour Organization (ILO), the Working Group is organised into four subgroups: Operations and Donor Guidelines, Demand, Regulation and Dissemination. To share information about microinsurance initiatives, the Working Group issues this quarterly Newsletter. For more information contact Craig Churchill, churchill@ilo.org.

➤ **Operations and Donor Guidelines subgroup:** Tries to facilitate the emergence of appropriate insurance products for low-income persons, analysing current practices and improving donor practices in this field. Contact: mjmccord@bellsouth.net

➤ **Demand subgroup:** Seeks to develop tools that MFIs and other organisations can use to assess the demand for insurance and other risk-managing financial services. Contact: moniqueC@mfops.org

➤ **Regulation subgroup:** Will focus on regulatory issues that affect the development of microinsurance products for the poor. Contact: Svenja.Paulino@gtz.de

➤ **Dissemination subgroup:** Facilitate microinsurance information sharing among the industry, including MFIs, insurance companies, donors and experts. Contact: insurance@microfinance.lu

To receive the coming issues of MICROINSURANCE, please contact insurance@microfinance.lu

Concept

Some Criteria for Successful Microinsurance

The criteria presented below are the result of theoretical considerations and practical experience. No assertion is made that all of them must be present in order to be successful in microinsurance; or that other sets of criteria could not work. Criteria such as competent and honest personnel and good management are not listed as they are necessary for success in any endeavour.

- **Real, integral partnerships with "people's" organisations**

"People's" organisations include among others co-operatives, trade unions, community-based organisations (CBOs), self-help groups (SHGs), savings and credit societies. Real and integral partnerships imply truly close relationships

- **Products decided/agreed on by partner organisations**

It is important that the products really meet the genuine needs of clients, and not merely needs as assumed

by the insurer. Products have to be developed together with the partner organisation(s).

- **Trust and transparency between the partner and the insurer**

A real and integral partnership implies that the partners are open with, and trust, each other.

- **Simple products**

Products should be kept as simple as possible, given the coverage needs.

- **Group insurances**

Insurance is by its very nature a collective enterprise; there must be a (large) pool of similar lives, objects, or eventualities being insured so that the "law of large numbers", "spread of risk", and avoidance of "anti-selection" can come into play. Microinsurance implies modest coverage and low premium amounts. Individual insurances require considerable marketing

Some Criteria for Successful Microinsurance	1
Microinsurance and Social Protection	2
Case Study: TYM's Mutual Assistance Fund, Vietnam	4
Websites	5
Terms and Definitions	5
Events	5
About an insurance product	5
Latest Publications	6
News from the Working Group	6
The Working Group's Case Studies:	6

and sales efforts as well as extensive underwriting and administration; costs which are often so high as to make individual microinsurance ineffective or even unfeasible. Group insurances provide significant cost savings. Access to, and distribution of, insurance is improved and many risks that would be rejected by an insurer on an individual basis can be included within group plans. Insurance awareness and education can more readily be enhanced.

- Minimal marketing costs; avoidance of commissions

If the above criteria are met - simple group products jointly agreed in an open and trustful relationship by a people's organisation and an insurer - marketing costs can be minimized. No commissions should have to be paid.

- Risk-only coverage

Life insurance in more developed countries very often includes both risk protection and a large element of savings accumulation. The products are generally complex and expenses high. A lot of microinsurance is offered by microfinance institutions or other institutions that offer efficient savings mechanisms. Insurance can therefore be restricted to risk-only coverage (e.g., death or accidents) at much lower costs and with greater transparency.

- "Automatic" coverage linked to other activities

Much insurance can be linked automatically to other activities. For example, taking a loan in a microfinance institution often leads automatically,

and without additional cost, to group life insurance coverage on the loan. Or, joining a trade union can automatically provide insurance to its members. In India, a large fertilizer co-operative provides accident insurance on the purchaser of each bag of fertilizer.

- Aggregated premium payments

Separate payment of premiums from each insured client in microinsurance is extremely costly. A single premium paid by a people's organisation for all insured members is the most efficient method. The premium may be paid out of the organisation's revenues, or aggregated by a variety of methods; by direct debit from member accounts, as a part of membership dues, by "baking" the cost into another service, etc.

- Stream-lined administration

Integrating the administration into already existing systems of a people's organisation can be most effective. Membership registers can have a simple notation if a particular insurance product covers the member. The people's organisation can, in many cases, maintain all records and only send copies of particular information to the insurer when a claim is made.

- Simple claims procedure and verification

Group term life insurance on member loans in an MFI can, for example, be administered so that the insurer keeps a minimum of records; none need to be kept about the individual members of the MFI. When a member dies or is disabled, an extract of the member's

account information, loan balance outstanding, and individual particulars are sent to the insurer. In some cases, MFI's or other peoples' organisations are authorized to process and settle smaller, uncomplicated claims without even contacting the insurer.

- Rapid delivery of benefit payments

Rapid delivery of benefit payments is vital to maintaining faith in the insurance scheme, in the insurer, and in the people's organisation itself. The aforementioned example of peoples' organisations themselves settling claims enables the most rapid delivery of benefits.

- A profit-sharing mechanism

Some type of profit-sharing arrangement between a people's organisation and an insurer is, while not a necessity, a good way to strengthen the integrated partnership as well as a way for the insurer to gain greater interest and cooperation from the people's organisation in making the insurance plans successful and profitable.

The observant reader will though note a bias toward the so-called "partnership model" as the author strongly doubts that microinsurers lacking people's organisations as integral partners can be truly successful; not only in terms of growing and making a profit, but also in providing effective and worthwhile services to the policyholders (i.e., meeting genuine needs of the policyholders and using at least 60-70% of the premiums for paying claims).

The author would be most grateful for readers' feedback - disagreements as well as suggestions for additional criteria. Ellis Wohlner, consultant to Sida, November 2004, elliswohlner@yahoo.com

Concept

Microinsurance and Social Protection

Alternative insurance structures and their complementary relationships to each other are illustrated by the insurance pyramid (figure 1). The pyramid is divided into 4 sections defining the key insurance types.

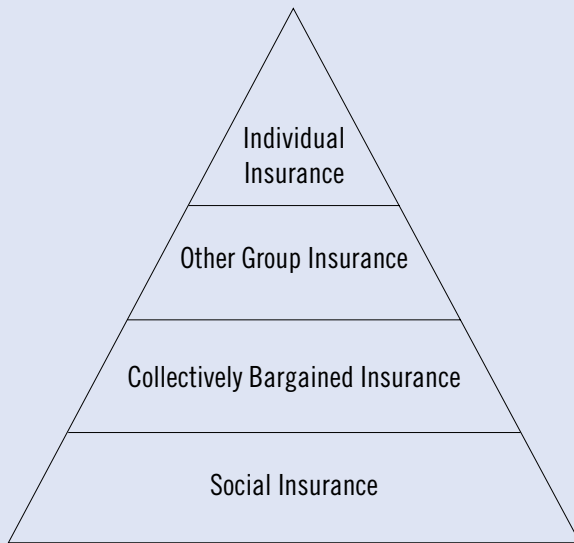
Social insurance

The bottom, broadest, section encompasses "social insurance" schemes. Definitions of social insurance vary greatly, but they generally have two necessary elements:

- that the scheme has been established through a political process, and
- that the scheme is compulsory for all concerned.

The protections provided are usually designed to give economic security to large sections of the population and are often

Figure 1: The Insurance Pyramid



regarded as social “rights” by those covered. The schemes may be financed by general tax revenues, by special taxes, levies or charges, and the schemes may be run by government institutions, special-purpose institutions or the private sector.

The most common schemes provide a degree of income replacement in case of work-place accidents, sickness, disability, retirement, unemployment, maternity (and paternity) leave, as well as income support for rehabilitation. Children’s allowances and housing allowances may also be included in the sphere of social insurance.

Social insurance is a tool of social protection, which is defined as the set of policies and programmes designed to reduce poverty and vulnerability by promoting efficient labour markets, diminishing people’s exposure to risks, and enhancing their capacity to protect themselves against hazards and interruption or loss of income. Social protection involves five major kinds of activities: labour market policies and programmes, social insurance programmes, social assistance, micro and area-based schemes, and child protection.

Collectively bargained insurance

The next level in the pyramid comprises collectively bargained schemes. Many employee groups are covered by various insurances—for group life, supplementary accident and sickness, retirement benefits, and others—agreed on through collective bargaining between trade unions and employer associations. Workers in the informal economy usually do not have access to these services.

Other group insurance

The third level in the pyramid consists of other types of group insurance. These are plans offered through various types of affinity groups—trade unions, professional associations, cooperatives, church groups and others. Insurance coverage can range from traditional group life schemes through a variety of products, up to and including special insurance needed uniquely by members of certain trade associations (for example, commercial fish farmers).

These other group insurance schemes can vary greatly in their structures, from compulsory schemes for everyone in a particular group and with one premium paid centrally for everyone, to schemes where joining up is voluntary and where each individual covered pays the relevant premium.

Individual insurance

Finally, individual insurance is on the fourth and uppermost level of the pyramid. Offered by public and private insurance companies, individual insurance generally covers life, health, auto, and other individual needs. Insurance companies collect premiums directly from the individual.

At the bottom of the pyramid, compulsory schemes covering large segments of the population are the least expensive to administer and do not require traditional underwriting (the selection of risks and avoidance of adverse selection). The further one climbs up the pyramid, the more marketing and sales costs are incurred, the more underwriting is required, the greater the transaction costs involved, and the more costly the scheme is to operate.

In a comparison between the top three layers of the pyramid, group schemes are generally preferable to individual insurance. Group schemes are usually far less expensive since they eliminate much of the marketing, sales, enrolment and distribution costs, reduce other administrative expenses, and can even simplify claims settlement procedures. Group schemes avoid adverse selection problems (i.e., the disproportional purchase of insurance by worse than average risks), provide a larger spread of risk, and thereby allow for less restrictive underwriting standards—which means that more people can obtain access to insurance. They can also reduce or eliminate aggressive sales tactics and the distrust of insurance schemes. Group schemes are usually easier to price, give more stable financial results, and re-insurance can be easier and less costly to obtain.

Group schemes can be offered on a mandatory basis (i.e., all members of the group are automatically insured) or on a voluntary basis. The latter means higher costs and increased risks of adverse selection. In general, voluntary group schemes lie between mandatory group schemes and individual coverage in the scale of advantages and disadvantages.

Chapter The Relationship with Social Protection from the Preliminary Donor Guidelines for Supporting Microinsurance (CGAP Working Group on Microinsurance, October 2003)

More info: http://www.microfinancegateway.org/files/13836_Draft_Donor_Guidelines.pdf

Case Study

TYM's Mutual Assistance Fund, Vietnam

The TYM Fund or Compassionate Fund (TYM stands for Tao Yeu May which literally translates to "I love you") is a Grameen replication project that was formally launched in 1993. The fund is managed by the Vietnam Women's Union (VWU), a mass-based national organisation to promote the welfare of Vietnamese women. TYM works predominantly in rural agriculture-based communities in the northern provinces of Vietnam, targeting the poorest districts in these provinces. TYM's members are women living in poor households usually earning less than VND 100,000 (\$6.50) a month.

In 1996, TYM launched the Mutual Assistance Fund (MAF) to protect against the death of a client or family member. The premium is a flat rate rather than a rate based on the size of the loan or the number of family members covered. With a weekly contribution of VND 200 (\$1 cent), upon the client's death, her outstanding loan balance would be written off and her family would receive VND 400,000 (\$26) to cover funeral expenses. Likewise, a member would receive a payout upon the death of her spouse or child less than 18 years of age. In July 2001, a health benefit of VND 200,000 (\$13) was introduced and the death benefit was also revised upwards to VND 500,000 (\$32).

The target market for the MAF is the same as that for TYM's loan products. The MAF enables the client's family to better cope with expenses incurred from the member's death and also relieves the family from the burden of repaying her outstanding debt. At the institutional level, the MAF enables TYM to have an additional level of reserve for its loan portfolio without having to increase its provision expenses and reduce its net profit.

TYM's Mutual Assistance Fund is not a full-fledged microinsurance product. From the beginning, MAF was touted as community-based financial support rather than a financial product aimed at mitigating key risks faced by poor households. At the end of March 2004, the MAF insured 68,157 lives. This figure includes 18,951 members, 16,372 spouses and 32,834 children. The assistance fund balance stood at VND 469 million (\$30,300).

Breakthroughs

- Appropriate product design for low-income rural households:

The simple premium structure of the MAF—where everyone pays the same level regardless of age, number of dependents, and marital status—ensures a broad participation by all members. The premium is also set at an affordable level for poor households.

- Easy start-up and management: Management of the MAF was fully integrated into TYM's existing operational structure. The simple product design did not necessitate the hiring of staff with insurance expertise and required minimal staff training.

- Streamlined claims procedures: The benefits are predetermined, which simplifies the processing of claims and facilitating timely payouts. Instances of fraud are rare due to the existence of proper procedures that provide clear guidance as to the kinds of supporting documentation to be submitted.

- Customer satisfaction and impact on community: Clients consider the MAF as good value for the money. The MAF helps to support group and community solidarity since members can rely on the Fund to help defray costs related to death and illness.

Challenges

- Long-term sustainability of current pricing structure: The premium of VND 200 has not changed since the launch of the product and will need to be adjusted to reflect the larger volume of claims being submitted and the higher loan amounts. The change to a tiered pricing structure would enable TYM to set its premium more accurately but would also imply a substantive change in the operating procedures for the MAF.

- Coverage that responds to clients' needs yet remains affordable: TYM's decision in 2001 to offer sickness benefits under the MAF appears to respond to clients' real needs. However, the benefit level of VND 200,000 represents a small percentage of actual medical expenses; clients could only receive the illness benefit one time; and the types of illnesses and medical procedures covered were not defined clearly and were subject to differing interpretation by branch managers.

- Staff training and client sensitisation:

TYM's technical officers make a general presentation to new members on the different types of products offered, including the MAF, but provide no follow-up discussion to reinforce this training. There was also some confusion among members about the difference between TYM's savings products and the MAF.

Lessons Learned

- Periodic adjustment of premiums and benefits: An insurance product needs to be tweaked periodically to reflect the client's changing risk profile over time. In TYM's case for example, members are growing older which means they would be more susceptible to illness. The increasing number of clients taking on the special loan of VND 15 million (\$1000) means that should they die, the burden on the MAF would be substantial. An institution should review the type of benefits covered, but changes should be made following a systematic process that includes careful market research, actuarial analysis and careful business planning.

- Customer service: The MAF is highly appreciated by TYM members primarily because of the personalised service provided by TYM staff. Members do not have to travel far to make their contribution, the technical officers come to them. Likewise, the delivery of claims by the branch head and technical officer adds a personal touch and generates good word of mouth publicity. The staff also make frequent house visits to members, which strengthen client relations and help to prevent potential fraudulent claims.

- Clients' willingness to pay: Interviews with TYM members showed that clients are willing to pay higher premiums for additional benefits. Clients view the MAF as a valuable tool not only for their own household but also for the larger community since it strengthens solidarity among the members. This willingness to pay is also related to the fact that TYM is the only programme that provides this type of product for poor households.

More Info: Nhu-An Tran and Tan See Yun. TYM's Mutual Assistance Fund in Vietnam. Good and Bad Practices in Microinsurance, Case Study No. 3. The Working Group on Microinsurance. Info: <http://micro-financegateway.org/content/article/detail/22460>

More Info

Websites

The just launched **French** localisation of the Microfinancegateway, www.lamicro-finance.org, includes a **Highlight on microinsurance**. The French adaptation of the MicroInsurance Focus will be available in April. Info: <http://www.lamicrofinance.org/content/article/detail/15372>

ILO launched a **new website** on microfinance with a **microinsurance category** as part of their Work Themes. Here you can find working papers, case studies and information about their Microinsurance Capacity Building project in India. Go to <http://www.ilo.org/public/english/employment/finance/vulnerab/micro/index.htm>

Terms and Definitions

Partner-agent model: The least risky approach for an MFI to provide microinsurance. The MFI acts as an insurance agent, selling and servicing policies. The insurance company, or partner, manufactures the insurance product.

Source: Making Insurance Work for Microfinance Institutions, ILO, 2003

Selected Info

About an insurance product

CEMK, Mutuelle Santé SOFAC, RD Congo

The cooperative "La mutuelle de santé Solidarité et Fraternité dans l'Action (SOFAC)", Goma, RD Congo, started in 2000 the Caisse d'Entraide Mutuelle de Katindo (CEMK).

Being aware of the difficult conditions in this region, the promoters set about to solve the problem caused by limited access to medical services, and the common issue of non-assisted dying. Although there are health committees at each medical centre, the community participation in primary health treatments is negligible. The promoters also wanted to make use of the concept of solidarity with regards to sharing costs; a concept very important in Congo. This solution presents several advantages: it is participative, shows solidarity with regards to cost and risk sharing, empowering and self-promoting.

The cooperative offers its members medical consultations, laboratory exams, treatments, medicine and hospitalisation. The illnesses for which the cooperative agrees to cover (60%) are evolutive and critical illnesses, meaning that if they would be left untreated or badly treated, they would be lethal. For example: Malaria, respiratory infections, worm infections, diarrhoea, cholera, meningitis, measles, skin diseases, etc. Furthermore, accidents are covered as well.

Access to primary health care is almost hypothetical for the people of the North Kivu region, deeply affected by armed conflicts. The health cooperative has been perceived by its promoters to favour inter-ethnic alliances and create social cohesion.

More information: mutusantesofac@yahoo.fr

Events

Conference on Securitization, Microinsurance and Technology, hosted by KfW, on June 23-24, 2005 in Frankfurt/Main, **Germany**. A panel discussion on microinsurance will be introduced by Michael McCord, and will have Monique Cohen as a guest. Contact Martin Hagen at martin.hagen@kfw.de

KfW together with the **Microinsurance Center and the Insurance State Supervision Service of Georgia** holds a **Regional Workshop on Microinsurance on May 9-10, 2005** in Tbilisi, **Georgia**. The seminar is aimed at participants (MFIs, insurers, insurance supervision) from the Caucasus and Central Asia. Contact Michael McCord at mjmccord@bellsouth.net for place availability.

MFC holds its **8th Annual Conference** entitled **Success of Microfinance: How do We Use this Success to Maximize Benefits for Clients?** on **May 26- 28, 2005** in Bucharest, **Romania**. Workshops and a panel discussion on microinsurance with Michael McCord, Monique Cohen and Craig Churchill are part of the agenda. Visit <http://pg.mfc.org.pl/conference/main.htm>

Latest Publications

Lessons Learnt the Hard Way, case study on “worst practises” in microinsurance. (CGAP Working Group on Microinsurance, Good and Bad Practices Case Study No. 6, January 2005). Download at <http://www.ilo.org/public/english/employment/finance/download/worst.pdf>

Eyes in the Sky Aid Crop Insurers, article on the use of satellite surveys for crop insurance (ICMIF World no. 51, January 2005 by Erich Kasten). Download at http://www.eomd.esa.int/files/docs/131-176-149-30_2005124141630.pdf

Qu'est-ce que la micro-assurance ?, (What is Micro-Insurance?), article with questions and answers on microinsurance (Lettre du MBA, January 2005 by Marc Nabeth). Contact mnabeth@planetfinance.org

Microinsurance and Disasters: Steps to Take to Mitigate Risk Next Time, article on the urgency for microinsurance for risk management (Microfinance Matters, Issue 9, February 2005, Michael McChord and Monique Cohen). Download at http://www.unctf.org/english/microfinance/newsletter/pages/2005_02/news_insurance.php

News from the Working Group

Demand Subgroup

The **Demand Subgroup** has gathered a wide range of materials which will be reviewed for the preparation of the guidelines for undertaking market research for microinsurance. Jennefer Sebstad, who is an expert on client assessment and market research and several years ago developed impact assessment guidelines, will work with Microfinance Opportunities on the preparation of these Guidelines. A draft version of the guidelines should be available in late Spring/early summer and will be sent to Working Groups members for review. For more information contact Sarah Pearlman, who is working with Microfinance Opportunities on this task, Pearlman@econ.umd.edu

Operations Subgroup

Institution	Country	Products
1. ServiPeru	Peru	Health and funeral insurance
2. TUW SKOK	Poland	Accidental death and disability, property, savings completion, deposit insurance
3. Delta Life	Bangladesh	Endowment (long-term savings plus life insurance)
4. Columna	Guatemala	Loan protection, life savings and term life
5. TYM	Vietnam	Loan protection, funeral, hospitalisation
6. MUSCCO	Malawi	Loan protection, life savings
7. CARD Mutual Benefit Association	Philippines	Loan protection, term life, provident fund
8. AIG	East Africa	Group personal accident
9. Lessons Learnt the Hard Way	Global	Various

These case studies are part of the **Good and Bad Practices in Microinsurance** project, managed by the Working Group. Further case studies will be available soon. More information: <http://www.microfinancegateway.com/section/resourcecenters/microinsurance>