

CGAP Working Group on Microinsurance / Munich Re Foundation

2005 Microinsurance Conference: The Regulator's Dilemma

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- Independent trust formed in April 2002
- Initial funding from UK's DFID
- Mission of "*Making Financial Markets Work for the Poor*"
- Facilitating and catalysing the next generation of development around access to financial services.
- Further information available at www.finmarktrust.org.za



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The Regulators' Dilemmas

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Financial sector is one of the most heavily regulated; now regulators face new questions:

1. How to manage the trade-off between financial stability and societal stability?
2. How to allow space for innovation and experimentation, e.g. new form insurers, without undermining the system?
3. How to handle international pressures e.g. IOSCO, FATF recommendations without damaging local priorities?



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The Regulators' Dilemma

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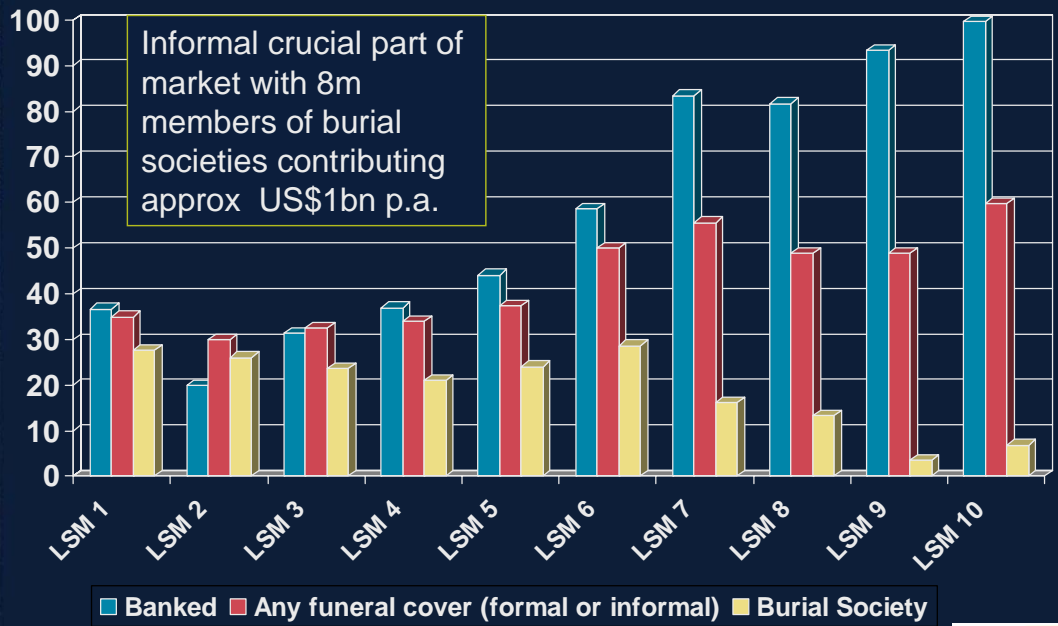
The Regulator's Solution?

Tools and suggestions



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Funeral cover is one of the most important markets in South Africa – 10m (37%) adults with some form of funeral cover vs 13m (48%) banked 5



Informal crucial part of market with 8m members of burial societies contributing approx US\$1bn p.a.

LSM = Living Standards Measure. 10 is high, 1 is low



#1) Understand demand side of the market

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Quality information is key to innovating at the 'Bottom of the Pyramid'. Demonstrated by 100% syndication of FinScope SA by year 3.

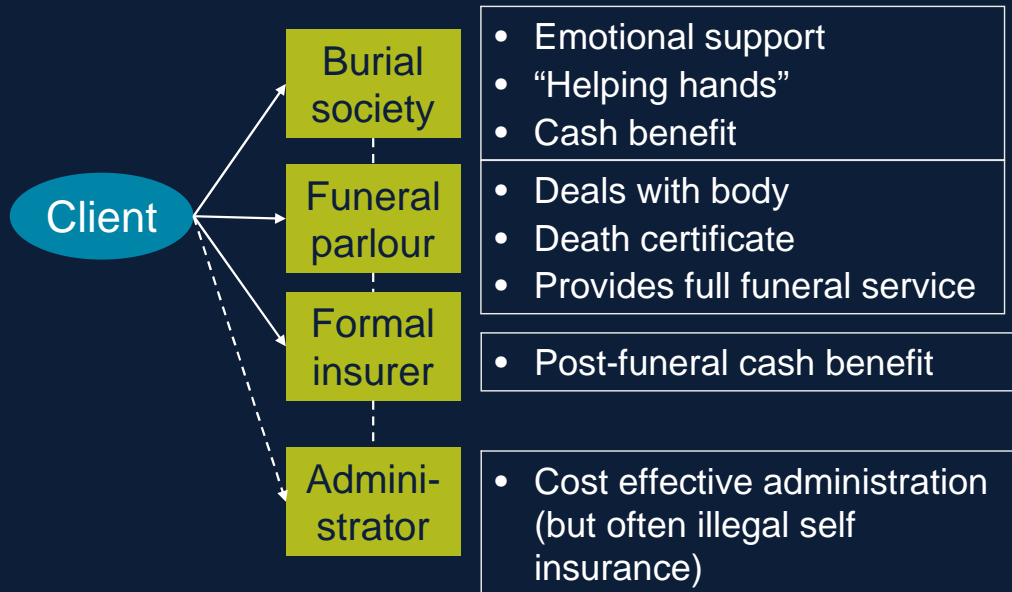


#1) Understand demand side of the market

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Multiple cover from multiple providers: each with market failures

Large vulnerable market



Rational but not optimal

Sources: Genesis 2004

#2) Analyse market structure & identify market failures



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Q: What is the objective of financial regulation?

A: To create and sustain healthy financial markets for the benefit of the economy and society.

- “Classic” objectives
 1. Maintain **stability**
 2. Improve market **efficiency** by correcting market imperfections
 3. **Protect** consumers from abuse
- “New generation” objectives?
 4. Facilitate **development** of markets
 5. “Other **strategic policy**”

But may be tensions and trade offs between objectives eg AML/CFT legislation in Swaziland reduces access to banking from 83% to 25% of population

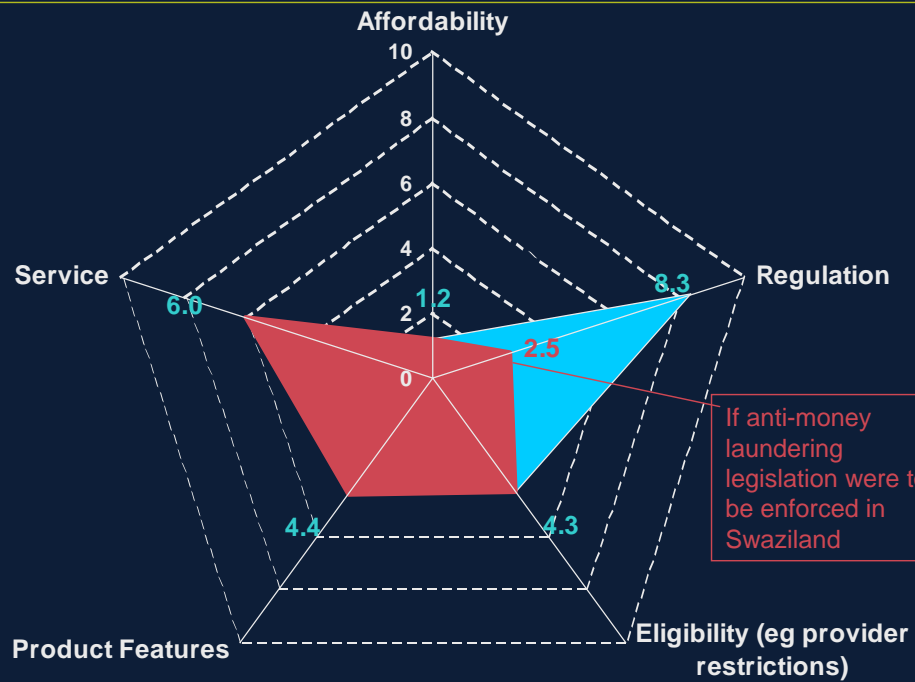
Sources: Genesis 2005

#3) Clarify objectives of the regulator



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Towards a toolkit on access: starting with banking



Sources: G:genesis 2004, Finscope 2003

#4) Analyze the impact on access



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Inefficient and burdensome regulation?

Great North Burial Society

- Registered friendly society with 15,000 to 20,000 members
- Structure: primary, secondary and apex
- Until 2000:
 - Managed risk under Friendly Societies Act
 - Contractually guaranteed benefits
 - Employed own actuary
- 2000 evaluation report suggested that risk pool was insufficient
- Advised to obtain underwriting from formal insurer
- Underwriting from New Era in 2000 did not match
 - Different premium revision frequencies
 - Lapses treated differently (FS Act > 6m)
- Result: substantial losses to GNB and uncertain regulatory position

Case study: Great North Burial Society



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Capacity and competence of regulators



The new environment changes regulators' roles from focusing on :

- Regulation and supervision only

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- Leadership, coordination, facilitation, supervision

This requires training and support



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The new role for regulators

Financial Architecture



- Needs a coherent overall strategy
- Identify real trade-offs
 - Cost of not doing > cost of doing
- Define societal risk parameters and accept parameters
 - State as ultimate risk manager
- Understand functioning of broader (formal and informal) market through improved market information.
- Role of special windows (tiering) and exemptions in creating space



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Resolving the dilemmas



The dilemmas are tough but resolvable

Like the innovator's solution,
the regulator's solution is not easy but
requires starting with the right questions
and wrestling through to the answers.

Donors can support through enabling
improved market analysis (demand and
supply side) and supporting use of tools
to assess trade offs



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Conclusion



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