6 Conclusions

6.1 Strategies for sustainability

Craig Churchill and Denis Garand

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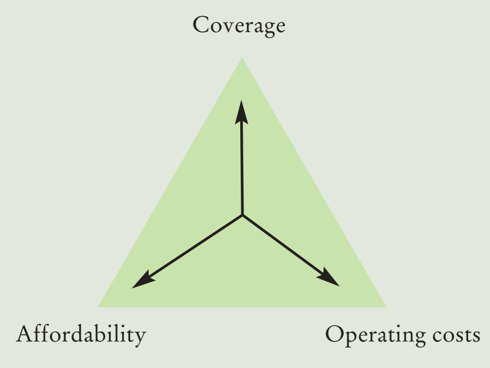
As illustrated in the preceding chapters, creating a viable microinsurance scheme is challenging. Whether the scheme covers its costs with the assistance of donors and governments, or from premium revenues and investment income, sustainability ensures permanent access to services. The sustainability dilemma boils down to a trade-off between three competing objectives *(see Figure 38)*. How do microinsurers find a balance between 1) **coverage**, meeting the needs of large volumes of low-income people, 2) **costs**, operating costs and transaction costs for the insurer, and 3) **affordability**, representing the price and transaction costs for clients?

Figure 38 **Striking a balance: The microinsurance challenge**



Based on experiences from the case studies, this chapter summarizes 12 strategies that can be used to achieve sustainability, divided into three major categories:

1. Limit benefits
2. Focus on efficiency
3. Diversify income sources

The chapter concludes with some observations on management, which underpins each strategy and can make the difference between a scheme's success and failure. As a business develops and grows, and achieves a regular flow of income, it has to balance another set of three competing interests – of **employees** to get the best compensation, of **customers** to purchase the product at the best price, and of "**shareholders**" to receive the best return on their investment, whether in financial or social terms. Success then depends on managing effectively to keep these main stakeholders satisfied.

1 Limit benefits

Starting a microinsurance programme is similar to starting a normal insurance company; however, it takes longer to reach viability. Just how long depends on the product, target market and the sustainability strategy. The first approach to achieving sustainability is to limit the benefits offered. Though not a perfect scenario since the insurer cannot provide low-income households with the range of protection they need, insurance with limited benefits can be relatively inexpensive and in any event better than no coverage at all. Basic benefits are also an appropriate starting point. As the target market develops an appreciation for the value of insurance, and as the insurer develops expertise in providing it, benefits can be gradually increased.

1.1 Start with credit life

One of the most affordable products is credit life or loan protection. Apart from providing a limited benefit, as a compulsory product tied to an existing distribution channel, its administrative cost structure should be very efficient with a reasonable spread of risk.

While it is debatable whether these advantages really help the low-income market, credit life should be thought of as a starting point. If microinsurers provide credit life cover at an appropriate rate, they can build a substantial capital base and then expand the benefit package. With appropriate technical help, they can establish a sufficient premium to pay expected claims and administrative expenses, and contribute to a surplus. The provision of credit life can also be used to establish basic insurance management skills, monitoring systems and communication strategies. Once the surplus reaches a predetermined amount and the microinsurance scheme is financially stable, the funds can be used to increase benefits for the policyholders.

For example, once Spandana had built up sufficient reserves from its credit life product, it expanded benefits to include the death of the spouse and hut insurance, while at the same time lowering premiums. MUSCCO

(Malawi) and CARD MBA (Philippines) are in a similar position to enhance benefits now that they have amassed considerable capital – in the case of CARD, perhaps excessive capital. MUSCCO has built up US$198,000, while CARD MBA has generated US$830,000 in surpluses as it has a very efficient administrative structure and the premiums charged are much higher then required.

The "credit life" strategy for sustainability is predicated on using this cash cow to lay a strong foundation, which enables the microinsurer to provide customer-friendly benefits in the future. However, this strategy is only appropriate for lending institutions wishing to get involved in insurance. A major disadvantage is that early policyholders are essentially overcharged, while those who join the scheme later benefit. In addition, because coverage is mandatory, customers may not even know that they have it. Consequently, it does not help to overcome the market's lack of understanding and its wariness of insurance. To achieve that objective, it would be more useful to start with a "credit life plus" product that provides a payout (i.e. over and above the loan amount) and covers other family members as well. It also may make sense to offer a couple of different options so that, even though it is mandatory, clients can choose between two or three levels of coverage.

Sustainability strategy 1. Start with credit life

Advantages
- Relatively simple to put into place.
- Provides target population with some benefit – at least it is better than doing nothing.
- Creates a clear management focus important for achieving efficiency and viability. Management can learn simple steps before proceeding to more complex insurance offerings.

Disadvantages
- Only covers death risk (and sometimes disability) and provides a very limited benefit.
- Main beneficiary may be the lending institution. Is this insurance really for the MFI?
- Does not help clients understand insurance, nor does it nurture an emerging insurance culture.
- Provides insurance only to debtors, and provides no service to the wider community.
- Early policyholders may be overcharged.

– It may take time to develop the broader coverage required by the target market.
– Management may get comfortable and fail to improve insurance skills or operational efficiency.

1.2 Cap benefits

Another way of limiting benefits is by putting a ceiling on the amount that will be paid out over a period of time. For example, ALMAO's funeral policy covers up to nine lives per household, but only covers two deaths per year per household. Karuna Trust pays for lost income due to hospitalization up to a maximum of 30 days per year. Life savings schemes always specify a maximum benefit; at MUSCCO, the maximum coverage is MK 100,000 (US$935), while, in Guatemala, Columna's life savings coverage goes up to Q. 50,000 (US$6,000).

This benefit-capping approach is particularly common in health insurance. TYM goes so far as to only provide a health insurance benefit once during a client's lifetime, and limits that benefit to VND 200,000 (US$13), which hardly seems sufficient to cover members' needs. While this is certainly not an ideal benefit, it is the best that this informal scheme feels it can provide given its current management capacity and the members' ability to pay.

Although not as severe, Grameen Kalyan and BRAC in Bangladesh both limit the benefit amounts for patients needing treatment from other healthcare providers. Although the vast majority of GK and BRAC policyholders have their healthcare needs addressed at the organizations' own clinics, more severe cases must be referred to hospitals and other specialist facilities. Where this arises, GK, for example, reimburses up to US$34 for hospitalization due to maternity complications and up to US$17 for hospitalization due to other complications.

Providing limited benefits reduces claims volatility and hence reduces the need to obtain reinsurance coverage. However, this approach does not solve the basic problem of helping low-income households to cope with large losses.

Sustainability strategy 2. Cap benefits

Advantages
– Capped benefits reduce the premium.
– No need for any reinsurance coverage.

Disadvantages
– The greatest need for insurance is to cover large medical bills; capping benefits defeats one of the primary objectives of health insurance, which is to prevent the poor from having to sell their assets or borrow from a moneylender to receive treatment. Insuring high claims amounts should be affordable if the incidence rate is small.

1.3 Target benefits

If the low-income market cannot afford comprehensive cover, especially for health insurance, then it is necessary to ration benefits, and make some difficult choices regarding what is and is not covered. For instance, the public schemes in Bolivia (SBS) and Peru (SMI) limited their initial benefit packages to the most relevant epidemiological problems of maternal and early childhood health. AssEF and UMSGF clearly list the treatments covered, and do not pay for any that are not. This is necessary not only to reduce claims, but also to educate the policyholders.

Benefits can also be designed to fill key gaps in the existing mechanisms for coping with risk. For example, Karuna Trust's benefits were designed to supplement services for the poor in public health facilities. These people do not need the actual healthcare coverage, but if the policyholder is hospitalized for more than 24 hours in a designated public health facility, Karuna provides Rs. 50 (US$1.10) per day as compensation for wage loss. This benefit package is very appropriate for workers in the informal economy who might otherwise not seek healthcare, not because of the cost of the care but because of the opportunity costs of not working. Other gaps addressed by the Karuna insurance coverage include pharmaceuticals and ambulance transportation.

It is best to involve the members in choosing the benefits to allow them to make the tough decisions about how much they are willing to pay and for what benefits. For instance, Microcare's customers chose not to include medication for chronic diseases in their benefit package instead of excluding chronically ill persons. This made the package more affordable while being broadly inclusive, and therefore more attractive to the clients (although the chronically ill had to find some other way to pay for their insulin, inhalers and so on).

Sustainability strategy 3. Target benefits

Advantages
– Targeted benefits mean smaller premiums.
– Provided clients' needs are well understood, the scheme can address clients' top priorities.

Disadvantages
- When an insurer limits the benefits, members always want more.
- May not cover illnesses or risks that some policyholders are most concerned about.
- Risk of drop-outs if clients are consistently not covered for risks they face, and if coverage is not clearly understood (although these disadvantages can be tempered by involving the clients in choosing the benefits).

1.4 Focus on big-ticket items

Another way of targeting benefits is to focus only on high-cost, low-probability items such as surgery, letting policyholders pay for their more mundane healthcare costs out of their own pocket. Although this approach reduces the likelihood that individual policyholders will actually benefit from their insurance policy, it also minimizes premiums while ensuring that protection is there when people need it most.

The prime example of this approach is Yeshasvini Trust. For a premium of just Rs. 120 (US$2.70) per year per adult, the insurance scheme covers more than 1,600 operations.[1] The benefit covers surgery along with nearly all associated costs, including admission fees, bed charges in a common ward, nursing, anaesthesia, the surgeon's charges, as well consumables and medicines during and after the operative period.

The underlying assumption that led to the creation of the benefit package is that poor households cannot afford surgery, which is often lifesaving. Those who pay the full costs of surgery without insurance often further impoverish themselves and their households. Since only a few illnesses require surgery, a large number of households joining together in an insurance scheme can make surgery accessible for those who need it. While this approach undoubtedly benefits policyholders, there are still many expensive treatments that are not covered by the scheme, including hospitalization without surgery.

Sustainability strategy 4. Focus on big-ticket items

Advantages
- Focuses on major expenses that would force households to sell productive assets, starting a downward spiral further into poverty.
- Provides coverage for large and infrequent risks, lowering the administration cost of dealing with many small claims.

[1] This scheme also has a maximum annual benefit of Rs. 200,000 (US$4,545), which is sufficient for two of the most expensive operations and some smaller ones.

Disadvantages
– Primary care measures have the greatest impact on reducing overall healthcare expenditure. Funding only the big-ticket items may result in increased cost over many years as the insured delay early cost-effective treatment.
– In the history of healthcare, expenditure on prevention and health-promotion measures has had a far greater impact on reducing total health expenditure and improving the overall health of the population. Some would question the wisdom of insuring big-ticket items that save a few persons, when the same amount could save more lives, for instance if it were applied to a pre- and post-natal care programme.

2 Focus on efficiency

Besides limiting the benefits, the second set of sustainability strategies focuses on minimizing costs through more efficient and effective products, systems and processes.

2.1 Provide member benefits

The member-benefit approach is perhaps the most effective way of minimizing the operating costs for the insurer and the transaction costs for the insured. As the name suggests, the idea behind member benefits is that members of a group, such as a credit union or cooperative, automatically receive specific insurance coverage, usually without directly paying any premiums. A common example is the life savings cover provided by Columna, MUSCCO, La Equidad and other insurers of SACCO networks *(see Chapter 2.3)*.

As there are no individual transactions, the operating-cost structure is minimal. For example, for its member benefits, MUSCCO's total administrative expenses were just 15 per cent of premiums (2003), while for its individual sales of a complex product in India, VimoSEWA's administrative expenses were 97 per cent of premiums (2004). In the developed insurance market, distribution costs are generally the major item in administrative expenses and therefore, by eliminating them, the member-benefits approach can make insurance much more affordable.

To offer a member benefit, the institution has to have another revenue source to pay for insurance. For example, Yeshasvini Trust collaborates with milk-producing cooperatives that pay premiums on behalf of members by deducting the amount from their monthly milk-production income.

In the case of life savings, the credit unions pay a lower interest rate on the savings to be able to pay the insurance company to provide the benefit.

This reduction in interest on deposits may make the savings product uncompetitive and cause client desertion, or it could be marketed as an attractive benefit that could cause members to increase their savings balances, since the greater the balance, the greater the benefit (up to a maximum).

Sustainability strategy 5. Provide member benefits

Advantages
– A cost-effective method of covering the whole membership.
– As long as the benefit is reasonably low, there will be little adverse selection.
– Minimizes administrative costs.
– Can be an attractive feature which may increase membership.

Disadvantages
– Only members can receive cover.
– The level of cover may not meet the needs of the target population. For example, the client may withdraw from the savings account to pay for treatment costs prior to dying, resulting in inadequate benefits.
– The insured may not be aware they have benefits. If benefits are not claimed, this will distort data and lead the organization to believe it has better claims results than in other programmes where members know they have insurance.

2.2 Use low-cost premium payment methods

Since low-income households have difficulty paying annual premiums in one lump sum, to make premium payments fit better with the cash flows of low-income households, microinsurers have had to innovate. The most common approach is to increase the frequency of premium payments so they are in smaller amounts. Unfortunately, this is likely to significantly increase transaction costs, thus making products more expensive – more affordable and yet more expensive at the same time!

As described in Chapter 3.3 and elsewhere, VimoSEWA has an alternative solution to the lump-sum payment problem that simultaneously decreases the transaction costs. It offers a fixed deposit method whereby the interest from the savings account pays the insurance premium. This arrangement has the advantage of providing semi-permanent insurance with essentially no transaction costs once the total amount has been deposited. However, the poor find it hard to save up enough to put into the account and it is difficult to get policyholders to increase their deposit amount when interest rates decline or premiums increase. Only 25 per cent of VimoSEWA's 120,000 policyholders use the fixed deposit method to pay premiums; the rest pay through an annual marketing and renewal campaign, which partly explains why the associated administrative costs are still quite high.

Another low-cost premium payment method is through automatic deductions from the policyholder's savings account. Instead of relying on physical transactions, which are expensive for the insurer and policyholder alike, electronic transactions can minimize the cost of collecting premiums. For this to be an option, however, low-income households must have access to savings accounts.

In the Philippines, G-Cash has recently been allowing financial transactions via cell phone at a cost of 1 peso each.[2] This can be a very cost-effective method of communicating premium due and collecting premiums as clients do not have to pay transportation costs and the insurer receives data quickly and efficiently. Indeed, additional innovation is required in this area to enhance efficiency further. Perhaps technology will provide new solutions.

Sustainability strategy 6. Use low-cost premium payment methods

Advantages
– Virtually eliminates transaction costs.
– Fixed deposit method provides semi-permanent coverage for the policyholder, and minimal lapses for the insurer.
– Lower costs make it possible to offer greater benefits.

Disadvantages
– Clients need to have access to savings accounts (or cell phones).
– For the fixed deposit approach, it can be difficult for the poor to amass the deposit amount, and difficult to convince policyholders to increase the amount if premiums go up.

2.3 Rely on inexpensive distribution systems

One of the major reasons why insurance companies cannot reach low-income markets is their lack of appropriate distribution systems. However, as the experience with the partner-agent model illustrates, grassroots or community organizations can be inexpensive and effective insurance distribution channels. When considering this approach, the most logical delivery agents are microfinance institutions, since they already have savings and credit transactions with the poor. Similar experiences are found in mainstream

2 The authors wish to thank John Wipf for providing the details about G-Cash.

insurance where very efficient *bancassurance* products can reach a large number of policyholders.

However, to really expand the availability of microinsurance, it is also necessary to look beyond financial institutions as possible delivery agents. Yeshasvini uses the existing cooperative network to sell health insurance, collect premiums and distribute photo ID cards. Likewise, the partnerships between insurance companies and retailers in South Africa *(see Chapter 4.6)* seem like potentially inexpensive mechanisms to extend insurance to the poor.

For microinsurance, a key aspect of inexpensive distribution is to have minimal screening and underwriting requirements. This is possible with group policies whereby everyone who is part of the group and meets the age criteria is eligible for insurance cover. Even with individual policies, it is possible to have minimal underwriting up front (perhaps just a signed declaration of good health), shifting the burden to the claims process. This back-end scrutiny is more cost-effective since it applies only to those few people who claim instead of the huge volumes of people who join the scheme.

Sustainability strategy 7. Rely on inexpensive distribution systems

Advantages
- Can use the existing distribution structure.
- Easy to implement.

Disadvantages
- Overloaded staff of existing system may not clearly explain the insurance benefits.
- The risk carrier may not acquire the necessary in-depth understanding of the target market.
- Only appropriate for basic insurance cover.

2.4 Control costs

A key strategy for controlling costs is to enhance efficiency by differentiating requirements depending on the size of the insurance policy. For example, simple microinsurance products can be handled by less expensive employees. Or if the sums insured are below a certain amount, then a more streamlined, less expensive approach can be taken. At Delta Life, if a policy is for more than US$2,000, then the applicant must undergo a medical examination; for amounts below US$2,000, only a health declaration is required. Similar adjustments can go a long way towards making the smallest policies more sustainable.

The community-based model often relies on volunteer labour of its members as a cost control strategy *(see Chapter 4.3)*. This approach has been particularly effective in making it possible for many small schemes to cover their costs in a short period of time, but it is not a long-term strategy; volunteers tend to become de-motivated resulting in high turnover.

In health insurance, minimizing claims costs is a major challenge. Organizations that manage their own healthcare providers, such as ServiPerú, BRAC and Grameen Kalyan, can exert a greater influence on healthcare costs. At ServiPerú, for example, doctors' salaries, usually a fixed cost, are rendered variable by linking remuneration to the number of consultations provided. If properly managed, such a capitation compensation system can provide a direct link between income and expenses.

In addition, regardless of who provides the healthcare, microinsurers must make sure that appropriate treatment protocols are followed, such as only prescribing pharmaceuticals that are actually needed (a challenge since consumers always want pharmaceuticals, even if they are not necessary), providing generic pharmaceuticals where possible, and not conducting unnecessary tests – BRAC's MHIB has made significant progress in this regard.

Although these approaches are relevant for conventional insurance as well, one microinsurance-specific cost-control strategy is to appeal to the members' sense of solidarity in the expectation that they will voluntarily refrain from over-usage. For example, as a cooperative, ServiPerú asks its members to avoid excessive or unnecessary use of services so that the company can keep prices low. While such an approach will undoubtedly engender a certain amount of free-riding, it will probably be less severe in a mutual or NGO than it would be in an organization driven by profit.

Another element in keeping costs down is loss prevention. Microinsurers can reduce claims costs by providing health education that encourages people to eat better and obtain treatment early, and by health promotion campaigns, for example providing insecticide-treated mosquito nets in areas of high malaria risk to and developing access to clean water supplies *(see Chapter 3.9)*.

Such prevention campaigns do not necessarily need to be conducted by the insurer. Indeed, strategic partnerships are a particularly useful way of stretching the budget. For example, several microinsurers collaborate with organizations raising awareness about HIV/AIDS or with government immunization campaigns to provide valuable services to their members at a limited (or no) cost, while striving to reduce claims.

Sustainability strategy 8. Control costs

Advantages

- Differentiated processes, with more streamlined requirements for small policies, appropriately balance costs and controls.
- With proper guidance, many healthcare providers can reduce costs without adversely affecting quality; in fact, clear treatment protocols can reduce costs, and improve the quality of healthcare and service.
- Small investments in prevention can often reap significant returns in the form of lower claims, especially if implemented through mutually beneficial strategic partnerships.
- Prevention campaigns enable policyholders who do not make claims to receive some benefit from the scheme.

Disadvantages

- Dependence on volunteer labour is not a long-term solution.
- Heavy downward pressure on the salaries of insurance and healthcare providers could result in high staff turnover and poor-quality service.
- Reliance on solidarity to minimize claims and insurance risk becomes less effective as the organization grows.

2.5 Buy benefits in bulk

Another way to keep claims costs down is for the microinsurer to negotiate with the benefit provider to get a better deal. For example, ServiPerú's cover includes a funeral benefit. The organization has negotiated a discount from associated funeral service providers in exchange for bringing in large volumes of business. Consequently, low-income households have access to a funeral of the same quality for less money by going through the insurer.

Yeshasvini followed the same strategy. Given the significant over-capacity in the local hospitals and clinics, the Trust was able to persuade its network of providers to agree to fixed prices for operations 30 per cent below the average price. The healthcare providers agreed to the lower rates because the insurer will actually pay and because they want to increase the utilization rate of their facilities and staff.

Sustainability strategy 9. Buy benefits in bulk

Advantages
– Can make benefits more affordable.
– Advantage for service providers (e.g. clinics, funeral parlours) as they receive a certain "guaranteed" clientele in exchange.

Disadvantages
– Only appropriate when benefits are provided in kind.
– Providers of in-kind benefits may deliver poorer quality services to the insured since they are being paid less.
– The strategy relies on use of excess capacity, which may not always be available.

3 Diversify income sources

One problem in providing insurance to the poor is that they may not be able to afford it, even if the benefits are small and the operating costs are kept to a minimum. The third general approach to making microinsurance sustainable is to diversify income sources so that low-income people only pay for a portion of the costs. This approach is common among the traditional financing mechanisms of social health insurance, whereby financing is based on wage-related and bipartite contributions shared between the employer and the employee, such as that used by Bienestar Magisterial in El Salvador.

However, such an approach can only work in the formal sector. For workers in the informal economy, more creative strategies are required. Some microinsurers become involved in unrelated income-generating activities. Microcare, for example, has a number of contracts for software development and teaching computer skills, which are unrelated to providing health insurance, but they help pay the rent. Yeshasvini is selling advertising on the back of its ID cards to bring in additional revenue. Other ways of diversifying income sources are discussed below.

3.1 Cross-subsidize from other products or markets

One strategy is to subsidize the premiums from other, more profitable products or market segments. Indeed, for a microinsurance scheme to be considered as constituting social protection, it should have a redistribution function from the not-so-poor to the poor.

For example, Grameen Kalyan and BRAC's health insurance schemes serve the broader communities in which they operate. They charge higher premiums for the non-poor to be able to minimize the premiums for low-income community members. Penetration of these higher-income populations is intended to help the plan achieve viability by bringing in more revenue, although the schemes are not quite there yet. In 2003, 10 per cent of BRAC's insureds and 13 per cent of GK's were non-members, providing 18 per cent and 15 per cent of premium revenue respectively. Both organizations have learned that greater effort is required to increase the participation of the non-poor and to avoid adverse selection with this market segment.

Tata-AIG intends to follow a similar strategy. Once its micro-agents have exhausted the market that they can serve easily, they will be taught how to offer more expensive products to higher-income clients. VimoSEWA adopted this approach in 2001, introducing a new benefit package with higher sums insured targeted at higher-income customers. However, sales for this product were quite slow and after two years, VimoSEWA abandoned the strategy. It realized that its existing distribution mechanism was not particularly effective in serving the non-poor, a market where SEWA's brand was not as powerful. In addition, efforts to move up market distracted management from achieving viability in the low-income market.

To extend coverage to the poorest members of the community, the MHOs promoted by UMSFG also intend to cover the destitute when the organizations are in a strong financial situation. However, a major challenge to offering sliding-scale premiums is that the distinction between those who can and cannot pay premiums is not easy to make. In the Forestry Guinea area where UMSFG operates, anybody can become destitute.

This sustainability strategy is also appropriate for commercial insurers serving the low-income market since they naturally have a range of other business lines. For these insurance providers, there is a risk that they will try to generate short-term profits from the poor. Instead, the cross-subsidizing approach can be justified, even to shareholders, if the insurers adopt a long-term view of this market and strive to cultivate customer loyalty in the expectation that these policyholders will be profitable in the future. Indeed, the primary goal today should be to develop an insurance culture in the low-income market, whereas a strategy of maximizing short-term profits is likely to undermine that objective.

TUW SKOK's approach was different because its two market segments were the credit unions and their members. The insurer initially focused on corporate policies for the credit unions, including deposit insurance, coverage for fire and robbery, and fidelity bonding. After it had saturated its corporate market, TUW SKOK turned its attention to meeting the needs of credit union members. Most importantly, the insurer only began going downmarket once it was in a financial position to do so. Although it is unclear to what extent its member policies are now subsidized by the corporate insurance, TUW SKOK's microinsurance certainly benefits from the fact that the credit unions represented a large captive market for its corporate services.

Sustainability strategy 10. Cross-subsidize from other products or markets

Advantages

– Redistribution is a core element of social protection systems.
– Market diversification increases the security of microinsurance by spreading risk and increasing volumes of insureds.
– Increased volumes should result in increased efficiency, if well managed.
– Can reach sustainability sooner.

Disadvantages

– Reaching a higher-income market may require a different, more costly distribution system.
– The microinsurer may not have the correct brand image to attract higher-income clients.
– The natural tendency with all insurance operations is to drift to higher-income markets over time, as they are usually more profitable. This strategy requires strong governance to maintain focus on serving the needs of the poor.
– In a competitive market, other insurers may have more efficient distribution systems for higher-income populations.
– In a mutual organization, those providing subsidies may be elected to the governing body and change this policy.

3.2 Use an endowment fund to subsidize operations

Another source of compensating revenue could be an endowment or capital fund, from which investment earnings could contribute to operating costs. For this to work, the insurer has to have a significant amount of money and investment opportunities that generate decent returns. Some investment earnings would have to be ploughed back into the fund so it could grow in line with inflation to maintain its purchasing power. It would also be important for the management of the fund to be transparent to ensure that the money is not used elsewhere.

Grameen Kalyan and VimoSEWA have both received endowment grants for this purpose. For VimoSEWA, GTZ provided a capitalization grant in the early 1990s as a strategy to defray administrative expenses. This fund served its purpose as long as the number of insureds remained at around 30,000. However, when membership grew to 90,000, the income from the invested endowment fund was no longer sufficient. Grameen Kalyan's endowment fund was provided by its parent organization to establish health microinsurance. If the scheme were expanded to serve all of the communities where the Grameen Bank operates, however, the fund would not generate sufficient income to cover operating shortfalls.

Sustainability strategy 11. Subsidize from an endowment fund

Advantages
– Increases the value of the insurance programme.
– Provides financial flexibility to target and serve the poor and destitute.
– Provides stable funding for the scheme to plan its future.

Disadvantages
– Who provides the original endowment? It would be difficult to endow many microinsurance programmes or have a large impact on the poor.
– Large endowments require good governance to ensure that they generate earnings and are not diverted to other uses.
– A growth in the covered population may result in deficits if the endowment does not grow at the same pace.
– Even with a stable population, the endowment fund has to generate returns at least at the rate of inflation to maintain its purchasing power.

3.3 Access government subsidies

Microinsurance schemes that emerge from the social protection perspective are either financed in whole or in part by government funds, or a strategy for sustainability is to gain access to these subsidies eventually. For example, the health insurance initiatives of SBS (Bolivia), SMI (Peru) and SI (Paraguay) were all started by the public sector with government funding to extend healthcare to specific high-risk market segments. Other schemes, such as UMSGF, AssEF and Karuna Trust, have benefited from indirect government subsidies. The costs of the healthcare services used by members of these organizations are kept artificially low by subsidies from the government.

A major disadvantage of this approach is that it is vulnerable to political interference. The SBS and SMI both experienced major upheaval when new governments, with different priorities, were elected. Consequently, it is hard to count on long-term or permanent subsidies from the government. When subsidies are discontinued or decreased, microinsurance operations can experience considerable problems. For example, Yeshasvini received a direct government subsidy in its first two years of operation, which was helpful in providing good benefits at a very low cost. In its third year, when the government subsidy disappeared, the premium had to be doubled, resulting in a renewal rate of only 43 per cent.

Sustainability strategy 12. Access government subsidies

Advantages
– Healthcare should be seen as a human right, and therefore it is entirely appropriate for governments to channel resources to facilitate access for those who cannot afford to pay the premiums themselves.
– Microinsurance can be a cost-effective vehicle for governments to deliver benefits to the poor.

Disadvantages
– Government bureaucracy may not provide timely payments, creating a strain on the microinsurer's cash resources.
– A change in government policy may result in an abrupt cancellation of the subsidy.
– Governments may seek to impose certain methodologies that are not in the interest of the implementing organization.

4 Good management

None of these twelve strategies for sustainability are appropriate in all circumstances, and all have drawbacks. The challenge is to find ways of combining selected strategies in an approach that makes sense for each particular microinsurance scheme. Consequently, the bottom line for success in microinsurance is the same as for any other enterprise: the most essential strategy for sustainability is good management.

Among other things, microinsurance managers must have appropriately-skilled employees in place, realistic product pricing, a sound business plan, timely and reliable management information, and possibly reinsurance if required *(Chapter 5.4)*. They also need boards that know how to manage managers effectively *(Chapter 3.8)*. As many of these elements are not in place in organizations intending to offer microinsurance, it would seem logical to start with a focused or limited insurance benefit. When appropriate skills and systems have been established, the insurance programme can be expanded.

As with other businesses, managers need a business plan that helps them stay focused on delivering high-value protection at the lowest possible cost. Before expanding benefits and enhancing protection, mangers must understand the implications. To do so, managers need tools to allow them assess the options, and to weigh the advantages and disadvantages of higher premiums, lower benefits and so on, ideally in consultation with current or prospective policyholders. Managers also need an information system to track progress towards achieving the goals in the business plan.

As mentioned above, a key aspect of this plan is to define a balance between appropriately compensating employees, giving customers the best product and ensuring that shareholders receive an appropriate return on their investment. This trade-off is simplified if the interests of the parties are aligned. For example, for insurance provided through cooperatives *(Chapter 4.1)*, the clients are the shareholders. In the community-based model *(Chapter 4.3)*, the employees are often clients and owners.

The importance of having appropriate expertise among the staff, management and board cannot be over-emphasized. Some microinsurers do not have a good grasp of what they are doing or are not paying sufficient attention to their microinsurance activities to even know whether they are succeeding. To be managed effectively, microinsurance should be seen as an independent activity – separate from credit and savings and from conventional insurance – so that management can assess its viability and potential and deploy appropriate expertise to allow it to achieve that potential. In this respect, the community-based model has the advantage of only focusing on microinsurance.

Microinsurers do not have to have all of the required expertise in house, as long as they have access to it. Community-based or mutual schemes accomplish this objective through federations, with second-tier organizations maintaining technical expertise that can benefit many smaller, primary-level organizations. Partnerships between organizations with different types of expertise are a particularly effective strategy. If there is a lack of insurance skills, technical assistance can assist in achieving sustainability. As discussed in Chapter 5.5, various international organizations provide technical assistance to microinsurance programmes, as do many independent consultants. If international expertise is too expensive or not readily available, fledgling microinsurance schemes might also consider local insurance talent.

While expertise at the head office or federation level receives most of the attention, for microinsurance schemes to be sustainable, they need to have policyholders, many policyholders. Volumes are critical to the success of microinsurance schemes. So if they want to attract and keep customers, microinsurers need to have effective sales and service functions, and a good reputation for customer service. Indeed, microinsurance providers have to build up trust among their client base by clearly providing value. In short, the frontline people need to know what they are doing and need to make a good job of it. Consequently, greater investment in training frontline personnel is often warranted.

Well-managed insurance companies usually use reinsurance to manage risk, although reinsurance is not necessary in all situations. Some of the larger insurance companies that are involved in microinsurance, such as AIG Uganda, Madison, Delta Life and La Equidad, do not purchase reinsurance for their smallest polices because they cover many people for small sums over a large geographical area. However, microinsurers without significant reserves and without portfolios diversified between traditional and microinsurance would be well-advised to explore reinsurance arrangements (or at least insurance for catastrophic losses).

Last but not least, good management means using available opportunities and confronting imminent threats effectively. It is an art and a science. Though there are some business fundamentals to keep in mind and respect (such as the solvency ratio and capital levels required to meet obligations to policyholders), survival often depends on problem-solving that calls for judgement. Judgment can be better-informed by the use of industry standards and benchmarking, which for microinsurance is just beginning to emerge *(see Chapter 3.10)*. In addition, good judgement comes from experience, and experience comes from bad judgement. It is hoped that from a review of the experiences – good and bad – of other microinsurers, throughout this book and in the case studies, current and future microinsurers will gain wisdom and avoid repeating the mistakes of others.

6.2 The future of microinsurance

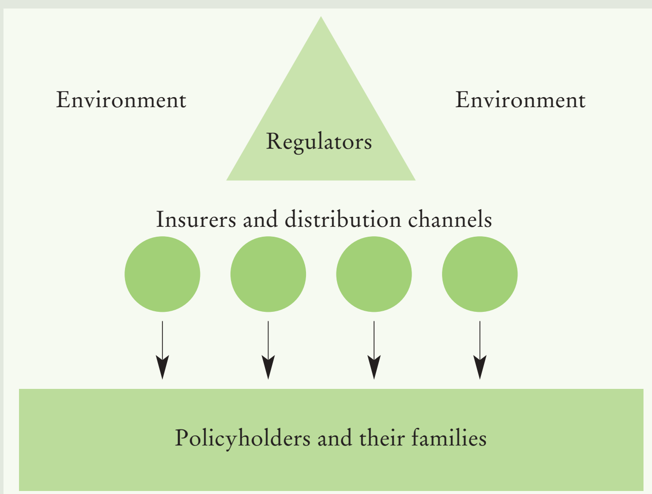
Felipe Botero, Craig Churchill, Michael J. McCord and Zahid Qureshi

The authors would like to thank August Pröbstl, Christina Hahne and Andreas Moser of Munich Re for their insights and comments on this chapter.

Considering the future of microinsurance involves looking at the whole picture, which includes 1) current and potential policyholders and their families, 2) the range of different insurance providers and their distribution channels, 3) the insurance regulators and supervisors and 4) the general environment in which all of these interact *(see Figure 39)*.

The future success of microinsurance depends on achieving prudent, profitable and continuous growth and development. What will be the development lifecycle for microinsurance? How long will it be? Some say that microinsurance is still at the conceptual stage and a good case can be made for this perspective. However, for the men and women out in the field today, whose efforts have been the raw material for this book, microinsurance is quite re al, even if it is still early days. Their hopes for the short-to-medium-term future are the focus of this chapter.

Figure 39 **Perspectives on the future**



The goal of microinsurance is to make appropriate, affordable risk-management products available to the poor, to help support their economic development and to enable them to achieve financial freedom for themselves and future generations. Microinsurance complements and enhances the effectiveness of informal coping mechanisms, and supplements statutory social protection schemes where they are available.

Chapter 1.1 summarizes the many challenges that inhibit the development and expansion of microinsurance; the subsequent pages are filled with numerous examples of how schemes are overcoming them. However, a number of further obstacles must be faced if insurance markets are to become significantly more inclusive. To massively increase the outreach of insurance services to low-income households, and to deepen penetration to reach those who are even more vulnerable, it is necessary to tackle these challenges *(highlighted in Table 52)*. This chapter summarizes some of the solutions that need to be considered to expand the availability and enhance the quality of microinsurance.

Table 52 **Continuing challenges that limit the expansion of microinsurance**

Category	*Item*
Clients	– Providing effective client education – Cultivating an insurance culture in the low-income market – Satisfying an unmet demand for new products – Reaching the most vulnerable
Providers	– Building staff capacity – Strengthening management – Enhancing efficiency – Finding the right business model and delivery channels
Regulators	– Removing regulatory obstacles – Adopting a market development agenda – Recognizing informal schemes where appropriate – Developing systematic and comprehensive approaches
Environment	– Improving healthcare facilities – Generating and using key insurance data – Strengthening financial markets – Creating stable macroeconomic conditions – Preparing for catastrophic risks

1 Microinsurance customers of the future

Microcredit has had an important impact on the ability of poor people to rise above the poverty line. Although the development of microinsurance is more recent, preliminary and anecdotal evidence suggests that it can be an important factor in enabling people to remain above the poverty line. By providing protection against certain perils, microinsurance serves as a natural complement to other financial and social services for the poor. For it to fulfil its potential, it is necessary to develop an insurance culture among the low-income market, as well as to introduce products that meet their primary needs, particularly for those who are most vulnerable.

1.1 Education and culture

Yet the demand for microinsurance requires some coaxing. The case studies noted that greater efforts need to be invested in market education so that potential policyholders understand and appreciate the value of insurance. In fact, successful insurers in developed markets continue to provide their clients and the general population with education on certain topics, leading to improved underwriting experience and customer loyalty. There is certainly a need to develop better pedagogical tools to convey the usefulness of insurance to an illiterate or uneducated market. To make a significant impact, however, client education is insufficient. Rather, stakeholders in the development of microinsurance – including providers, policymakers and donors – need to cultivate an insurance culture among the poor.

An insurance culture is a prerequisite for the success of microinsurance. In many developed countries, it took generations before people commonly turned to insurance to address their risk-management needs. Microinsurance providers will help build the culture of insurance when they serve their clients' needs in a fair and equitable way. The product is the starting-point: clients need to know that they have cover and they need to witness the regular provision of benefits.

Paying a claim – delivering on a promise – is arguably the single most important opportunity to reinforce the value of insurance, and therefore claims need to be handled efficiently and appropriately. Too often, benefits are not delivered as promised and this leads to an anti-insurance culture. Many microinsurance programmes operate in these anti-insurance cultures and struggle to counter the prevailing sentiments.

The evolution of attitudes to insurance will be affected by the ability of providers to continuously improve processes, services, benefits and costs for clients. Governments and civil society can contribute to the development of such a culture through educational programmes. This culture is reinforced when associations and employers begin offering insurance as membership or employment benefits. In developed countries, the growth of an insurance culture has been further supported by the prevalence of obligatory, government-mandated cover such as third-party liability cover for vehicles. Many people's experiences with these products have helped them to understand insurance, and in some cases encouraged them to seek out voluntary products as well.

For low-income persons in developing countries, the relevant parallel experience could come from credit life insurance provided through microfinance institutions. If MFIs can ensure that their clients have a positive experience, the poor may be more interested and willing to voluntarily purchase other insurance products. Consequently, there should be significant cause for concern when credit life is not taken seriously by MFIs (or their risk carriers) and when efforts are not made to ensure the poor have a positive experience with insurance. Every late payment or summarily rejected claim and every instance of opaque pricing or misinformation about the scope of cover, will add to the time it takes to foster an insurance culture.

To maintain a culture of insurance, providers should strive to serve customers throughout their lives rather than getting them on board and then neglecting their changing needs and circumstances. Lack of attention from the provider is a key cause of high lapse rates and gaps in coverage associated with many microinsurers. Efforts to minimize lapses and non-renewals should include using appropriate premium payment and financing mechanisms, as well as market education and marketing approaches that avoid misdirected and self-serving sales incentives. When microinsurance markets reach a stage where people really understand and appreciate what they are buying, lapses and non-renewals will become less frequent.

1.2 Product evolution

Insurance for the poor needs to develop as the demand for those services evolves. Health cover is the next priority, especially in countries where the governments cannot adequately address the healthcare needs of their citizens. Soon, there may be growing demand for long-term, retirement insurance or old-age pensions, as well as for disaster, housing, and in some areas, livestock and agricultural insurance. These are risks that cannot be managed by savings and credit alone. If microinsurance providers cannot keep up with these demands, they may stifle the development of an insurance culture as low-income persons lose confidence in risk-pooling mechanisms.

Insurance products sold through organizations that potential policyholders trust could also help develop positive attitudes. An insurance culture will emerge only when it is supported through word-of-mouth communication that promotes and spreads awareness of insurance. The combination of a trusted intermediary and word-of-mouth communication may be why many credit unions have been effective in generating an insurance culture among their members.

Microinsurance products that respond appropriately to potential policyholder needs and demands will help to generate an insurance culture. The key strategy to achieve this goal is to involve policyholders (or prospective clients) in the process of making hard choices between benefits and price. Tools that enable clients to see the trade-offs and voice their preferences will go a long way towards appropriate product design.

A long-term, multi-generational outcome is an enticing reason for insurers to enter this market, even though it is incompatible with the short-term perspective of most companies. In developing countries, millions of today's poor households will be tomorrow's middle class. Historically, the measure of success most revered among large multi-line insurance companies is the ability to build lifetime relationships with their clients, even multi-generational ones, providing products and services to cover changing needs throughout the policyholder's life. This is common knowledge to insurance sales agents who rely on referrals for their business and is evident in the multi-line companies that monitor the number of products per customer or household.

The overriding objective of microinsurance is to enable low-income people to protect wealth and achieve some level of economic security. Helping customers to achieve these goals also creates an ideal market for patient insurers; the long-term market potential is huge. Furthermore, brand loyalty is high in this market segment, which makes this argument that much more compelling.

In the long term, microinsurance policyholders will become more knowledgeable about insurance. They will recognize the potential for insurance to address some of their risk-management needs, and they will seek out such cover. They will understand the different risks and capabilities of insurance providers and will be able to make appropriate choices and decisions. Low-income consumers will push the insurance providers to offer the products they want. Microinsurers today have an obligation to help their clients become more knowledgeable, while preparing themselves to serve a more sophisticated market.

The more the target market understands insurance, the more aware they will be of the limitations of market-based solutions. This recognition will also help empower low-income communities to demand publicly-provided social protection services – after all, social security is a human right. Plus, there will always be a market segment that contributory insurance schemes cannot reach – the chronic or hard-core poor – which must be covered by government programmes. The ongoing challenge in the development of microinsurance is to determine where that frontier lies. How far can the envelope be pushed? What segments of the market could ultimately be reached through continued improvement in delivery mechanisms and efficiency? Similarly, how can microinsurance distribution mechanisms enhance access to government-provided social protection schemes?

2 Microinsurance providers of the future

The second set of challenges that need to be addressed involves the providers themselves. These issues fall into three categories: 1) building the capacity of management and staff, 2) enhancing efficiency, including the use of technology and 3) finding a business model that works for all stakeholders and balances short-term viability with long-term growth.

2.1 Building capacity

Since microinsurance is a relatively new endeavour, it is not surprising that there is a need to build up the capacity of providers. While the case studies indicate that some effort should be channelled to improve existing providers, to fill the enormous access chasm, investments also need to be made in new delivery channels and perhaps in creating new insurers.

The capacity challenges exist on two levels: field staff and management. In general, the field staff associated with the distribution channel – the agents selling and servicing the policies, or the managers of mutual schemes – require additional expertise in sales skills, insurance basics, adult education techniques and customer service. Just as important as the skills, however, is creating a work environment that allows schemes to retain qualified personnel. Currently, many microinsurers and their distribution channels experience high turnover of frontline personnel. Consequently, there is a great need to consider the compensation, incentives and career development of those who have the expertise of selling and servicing insurance for the poor.

As discussed in the previous chapter, building the capacity of management remains a significant challenge. The requirements for managers of informal schemes that may one day become formal, however, are quite different from those for managers in regulated insurance companies considering the low-income market opportunity. The latter need a crash course in understanding the needs of the poor, recognizing that microinsurance has some unique characteristics that require more than just smaller premiums and sums insured. The experiences of AIG Uganda and Madison Insurance illustrate that corporate insurers have been reactive, responding to requests from their distribution channels. Tata-AIG's approach of proactively designing specific measures for the low-income market could be a more appropriate tactic for corporate insurers.

In contrast to formal insurers, the managers of informal schemes have a much greater appreciation of the needs of the target market and are more receptive to adopting unconventional approaches since they are not rooted in mainstream insurance practices. However, they tend to have limited education and experience and therefore require more assistance with basic management and insurance skills. To assist these managers, and to support the dramatic expansion of microinsurance products, there is a great need for basic management tools, suitable information systems and software for business planning and modelling. Investors and donors must be careful, though, in their attempts to assist management of informal schemes. Insurance is a business of numbers and any "insurer" should be aiming for a large and diverse client base. It is important that investments be made in organizations that can achieve scale.

As illustrated in Box 107, some of these tools are under development or already in use and the challenge will be to make them more widely available.

Box 107

Management tools for microinsurance

A key strategy to strengthen the capacity of microinsurance managers is to ensure that they have access to, and know how to use, appropriate management tools. A number of recent tools have been developed that might enhance future performance, or inspire the development of future tools.

The HMI **health insurance software**, developed by the ILO-STEP, was designed to help the managers to record, verify and monitor enrolments, premium payments and claims. Through HMI, AssEF monitors 11 key indicators including enrolments, premium recovery, entitlement to benefits, frequency of utilization and average cost of services, as well as average expenses (claims and operating costs) per beneficiary. It also includes an accounting module to calculate annual technical results. The software allows managers to react quickly to anomalies.

The ILO-STEP programme has also developed a **feasibility study guide** for setting up health microinsurance schemes. It provides practical information for managers on everything from premium calculation to contracts with providers.

For its affiliated MFIs that work in partnership with insurance companies, Opportunity International has developed AIMS, **insurance software** that can be merged with OI's preferred banking software to eliminate duplicate record-keeping.

ICMIF has a **business-simulation tool**, Morotania, which explores the key issues in setting up and running a new insurance company. The simulation creates an enjoyable but challenging learning environment, which allows managers to sharpen decision-making and managements skills and learn first-hand about the reinsurance risks.

RIMANSI has developed an **actuarial modelling and business planning tool** for life, health and savings products which produces prospective income statements and balance sheets complete with actuarial reserves and expected claims. Managers use this tool to adjust the product pricing and benefits on an iterative basis until they can project a solvency ratio of 80 per cent by Year 4 and a targeted IRR of around 8 per cent.

Besides tools for managers, it is also necessary to strengthen support organizations and technical assistance providers, such as networks or federations of microinsurance schemes. If local TA providers and networks have the right tools and expertise, they can have a powerful multiplier effect.

Investment in developing actuarial expertise is also necessary. Miscalculations of risks and premiums can have drastic effects on microinsurance programmes as demonstrated by CARD's initial experience. Actuarial expertise can be secured either by employing in-house experts or, perhaps more realistically, outsourcing needs to consulting actuaries. Yet few actuaries understand the *micro* aspect of microinsurance. To achieve significant expansion and innovation, a new breed of actuary is needed which can use its spreadsheets to meet the needs of the poor in a sustainable manner.

2.2 Enhancing efficiency

One of the great imperatives for the expansion of microinsurance is to significantly reduce operating expenses relative to premiums. More efficient operations should result in lower premiums and/or additional benefits for policyholders – both would be welcome outcomes. More efficient operations might also mean that microinsurers could pay their employees better, resulting in improved staff retention and better customer service. Great expectations are placed on the potential of technology to enhance efficiency.

Nothing can make up for badly-managed companies. However, technology is a fundamental driver and has become a great equalizer. Throughout history, those that possessed more advanced technology dominated – politically, militarily and economically. That was true during the industrial revolution and has not changed in the information age. What has changed is technological development's pace and accessibility. The microprocessor has enabled the masses to reap the fruits of automation. The birth of the Internet has provided connectivity to every corner of the globe, making information available to all.

Insurance is an information-processing business. The raw materials are customer data, product information, transaction details, investment records and so on. Even before the birth of the computer, large insurance companies drove the development of sorting, tabulating and calculating machines to improve efficiency. Today these capabilities are available to small insurers as well. Microinsurers big and small must take advantage of ways of improving efficiency if they are to be honest stewards of microinsurance premiums.

Implementing technology is a risky proposition and thus there is a natural reluctance by cost-conscious microinsurance practitioners to go down this route. The low start-up costs of manual processes are attractive; however, this approach does not establish a sustainable and scalable foundation for the massive expansion of microinsurance as it does not provide the ability to optimize processes and build economies of scale. An insurer unable to reach large numbers places itself in a precarious position.

In the developed world, major insurance companies invest on average 3 to 6 per cent of annual gross revenue in technology. The new technology architectures based on the Internet and wireless communications will prove to be a good growth catalyst for microinsurance. Similarly, using open-source software would be an inexpensive way for microinsurers and grassroots organizations to benefit from technology.

The key to success in this area is to align the technology solutions with business problems. Management information systems should be designed to support the business strategy, not the other way around. This link between technology and strategy is illustrated by the fact that several insurance companies, including TUW SKOK and La Equidad, have provided their delivery channels with software to help them sell and service microinsurance, and help the insurer manage its relationship with its distribution channels.

Technology applications are a critical success factor in enhancing the efficiency of the insurance business. Automation has been introduced in almost every operational area. As illustrated in Table 53, automation could play a significant part in improving the efficiency of microinsurance, not to mention enhancing customer service, strengthening management and training staff.

Table 53 **Process automation transforms insurance operations**

Business process	*Automation opportunity*
Policy issue and enrolment	– Agents can submit applications or enrolment requests via the Internet – Automated underwriting and policy issuance – Document printing and record retention via imaging – Automated risk-pooling better reflecting risk levels in premiums
Premium collections	– Automated billing for group clients – Premium posting and automatic lapse processing
Claims	– On-line claim submission – Tracking available on the Web – Fast claim processing and payment via local banks or ATMs – Effective records for processing and claims-experience studies
Actuarial studies and pricing	– Mortality and morbidity studies – Pricing analysis – Data sourcing and aggregation on a national level
Education and training	– Staff education and training via Internet-based services – Effective client-education techniques

Some microinsurers have already begun to automate. For example, Microcare (Uganda) and Opportunity Bank (Malawi) both issue smartcards to their policyholders. This enables them to easily verify that the premium is up to date and determine the level of coverage that the client has. In the absence of national identification systems, smartcards also confirm that the person trying to access benefits is actually covered under the policy.

VimoSEWA in India is testing a barcode system to manage client information. When clients subscribe, they receive barcode stickers. When they want to file a claim, illiterate clients stick a barcode onto a pre-addressed envelope and send it to the microinsurer. VimoSEWA's barcode scanner indicates which client needs assistance and the appropriate fieldworker is dispatched. Also in India, Tata-AIG is training its micro-agents to use an Internet portal to retrieve and submit customer account information, such as premiums due and collected.

Technology is not just the realm of the insurers; today, customers too want to benefit from its use in product delivery. Even the low-income market has increasing access to technology, such as cell phones and the Internet, which could be used to streamline operations. According to Prahalad (2003), "the proliferation of wireless devices among the poor is universal, from

Grameen Phone in Bangladesh to Telefonica in Brazil. Further, the availability of PCs in kiosks at a very low price per hour and the opportunity to videoconference using PCs are adding to the intensity of connectivity among those at the BOP (bottom of the pyramid)." Indeed, banking services are actively using technology to extend outreach to the poor *(see Box 108)*. Insurance is likely to follow suit as long as the market education measures can be expanded to include the use of technology.

Box 108 **Technological advances in banking services for the poor**

Microfinance institutions have adopted a variety of technologies to supply services to the poor. Some of the most promising technologies might also be relevant for the expansion of microinsurance, including personal digital assistants (PDAs), smart cards and mobile-phone banking.

The use of **PDAs** by field staff provide advantages in the areas of transaction efficiency, error reduction and fraud prevention. In Bangladesh, the use of PDAs by SafeSave's door-to-door collectors has eliminated three to four hours per day of data processing, and reduced the number of mistakes in recording transactions by 90 per cent compared to paper-based systems. The technology also made it possible to cut loan processing time in half (from two days to one), and increased adherence to product rules by preventing policy-violating transactions.

Similarly, **smart card technology**, such as at that used by Prodem FFP in Bolivia, is expected to reduce the operating costs of serving rural areas. The cards have client identification information, including three fingerprint templates and financial data from Prodem's MIS. With smart card and fingerprint readers at its 54 branches, Prodem FFP offers clients a quick means of conducting financial transactions. Prodem FFP has realized a number of benefits from implementing smart cards. Waiting lines for tellers have dropped dramatically since many cardholders who wanted to check their balances may now do so without assistance. The adoption of technology has given the MFI a competitive advantage and attracted depositors who appreciate the system's speed and convenience.

Mobile-phone banking is another innovative product with great potential. To capitalize on this potential, Vodafone, with its local Kenyan affiliate, collaborated with a bank to provide services to clients of Faulu, a Kenyan MFI. This multilingual mobile-phone banking service allowed clients to transfer money, withdraw and deposit cash at registered local outlets and make loan repayments, all from their phones.

Source: Adapted from Churchill and Frankiewicz, 2006.

Technology cannot overcome every obstacle that microinsurance operations face. However, it can help optimize the return on investment and bridge operational gaps by enabling the communications and cooperation of stakeholders around the world. For example, a global data clearinghouse for actuarial studies, pricing and reinsurance could contribute significantly to expanded outreach, better products and the sustainability of providers.

2.3 Business model

The third challenge for microinsurance providers as they move forward is developing an effective business model. As illustrated in Part 4, all of the models currently in use have advantages and disadvantages. Obviously, one model will not be appropriate in all circumstances, and therefore the real challenge is to improve the existing approaches, exploiting their strengths and overcoming their shortcomings.

The criteria for success are business models that work for both the clients and other stakeholders, balancing short-term sustainability and long-term growth. Since the target market for microinsurance is relatively new, insurers need to adopt a market development approach whereby profitability is founded on volumes and long-term relationships.

Any insurance business model must acknowledge the need for reserves and reinsurance. Indeed, reinsurers are actively trying to identify a role for themselves in microinsurance. The reinsurer's role should focus on catastrophic risks, which are often excluded in microinsurance products. If catastrophic risks are excluded, insurance is not there to help people when they need it most; by covering these risks, reinsurance can play an important part in fortifying an emerging insurance culture.

A reinsurance-like approach could also help professionalize the activities of community-based and local microinsurance programmes. Although these schemes would still act as the first line of protection for their members, a local regulated insurer could "reinsure" these programmes. The regulated insurer could provide the financial back-up for certain risks and also technical input that may be lacking in community-based schemes. This would represent a new hybrid of the community-based and partner-agent models, while offering a greater variety of products to low-income members with greater professionalism.

The emergence of new models and delivery channels will be an important development for the future expansion of microinsurance. The distribution channel is the face of microinsurance for the customer, both for sales and servicing. The development of microinsurance depends largely on the quality and quantity of the delivery channels. The primary channel used today, microfinance institutions, has limitations. While they certainly will have an ongoing role in extending insurance to the poor, to expand the outreach dramatically it will be necessary to engage new distribution channels. In particular, there is a need to organize the unorganized to offer group insurance. Involving social organizations, such as cooperatives, workers' associations and the like, in organizing the poor will greatly facilitate their access to insurance.

To involve new distribution channels in microinsurance, there will be a clear role for intermediaries, such as insurance brokers, which can serve as translators between grassroots distributors and corporate risk carriers. By understanding the priorities, needs and language of both parties, the intermediary can help improve the quality of the products and the relationship between the partners.

In the long term, the face of insurance will change and adapt to this market. Thanks to the massive expansion of Internet access, low-income people will be able to buy insurance on-line from insurers and their agents. Delivery channels will expand far beyond financial service providers like MFIs and will become omnipresent in retail shops, post offices, hospitals and doctors' surgeries – anywhere that a link can be made with risk-management needs. Even the products themselves will be transformed to respond more accurately to the direct needs of potential policyholders. Insurers will be able to offer such products because improved distribution will allow them to serve very large volumes of policyholders.

3 The regulatory landscape

The basis for providing risk-management services to the poor is a sound regulatory and corruption-free political foundation. Without this, it is impossible for microinsurance to develop in a sustainable way.

Insurance is and needs to be a highly regulated industry. Building a risk-management culture is difficult enough – it only takes one or two company failures to destroy it. Insurance supervisors are primarily responsible for consumer protection, which comes in two main forms: 1) protecting policyholders in general against insurance company failure and 2) protecting individual policyholders (or potential policyholders) against unscrupulous sales and unfair policy documents. As described in Chapter 5.2, there is also a third type of consumer protection – concern for the protection of those who cannot access insurance – which represents a market development function for insurance regulators. The extent to which regulators are willing and able to embrace this development function will have a significant influence on the future scope of microinsurance in their jurisdictions.

A significant share of the microinsurance market is currently covered by organizations outside the reach of supervisors. While it is not appropriate for supervisors to look the other way, the costs and benefits of supervising informal microinsurance need to be considered: is it better to have no access to insurance or to have access to unregulated insurance? Some countries have legal structures that take greater account of different types of ownership structures and regulatory requirements. For example, in the Philippines, CARD has created a mutual benefit association for its members. This MBA has professional management, reserves, limited products and markets, and a link to the regulatory system. Similarly in Senegal, health mutuals have been incorporated into the legal framework. Such regulatory flexibility will be necessary in the move to a massive expansion of microinsurance.

Efforts to offer alternative business structures for microinsurance are limited by the ability of the regulatory structures to manage the system and fulfil their consumer protection role. The reduced capital requirements advocated by some have significant potential for abuse. Generally, regulators use minimum capital requirements in two ways: (1) to ensure that an insurance company has sufficient capital to meet future obligations to policyholders and (2) to maintain efficiency in the insurance system to prevent it being overrun by inefficient operators that they cannot properly supervise.

The balance between prudence and entry barriers is a tenuous one. A hybrid approach linking informal schemes to regulated insurers may help to create a higher level of supervision in the system while opening up opportunities for greater microinsurance provision. In addition, self-regulated schemes of cooperative and mutual organizations need to be seriously considered as a means of extending insurance to the poor without overwhelming the insurance supervisors.

It is advantageous to have a certain level of consistency across regions and on a global basis for multinationals to enter this market, so that they can implement their processes on a global scale. Although regulations on a global or regional basis are a noble but improbable goal, it is realistic to envisage a certain level of collaboration among regulators that would eventually result in improvements and standards for all nations. Through the International Association of Insurance Supervisors (IAIS), for example, it may be possible to design and promote model microinsurance regulations. This association could act as a standard-setting body, recommending appropriate reserve levels, solvency limits, etc. for microinsurance.

Indeed, the expansion of microinsurance would receive a big boost if insurance authorities believed they had an active role to play in enhancing the inclusiveness of the insurance markets. How involved should regulators become in promoting microinsurance? Their approach will depend on whether they see the low-income market as a threat to the financial stability of the insurance industry, or as a market opportunity that could potentially strengthen insurance companies. Some countries may follow India's approach and require commercial insurers to serve the low-income market, while others will explore less prescriptive means of making their insurance markets more inclusive. Either way, microinsurance promotion by regulatory authorities should help expand the product range and delivery channels insurers use to gain access to the poor, while opening up opportunities for alternative types of insurers.

Long the poor relation of the banking sector which has benefited from significant aid in the last ten years, the insurance sector in some countries is now beginning to receive some development assistance. This will result in much greater capacity at insurance regulators and will in turn allow for a greater variety of insurance provision models, but this will take time.

4 The environment for microinsurance

Many factors determine whether microinsurance can be made available, what products might be offered, how they will be offered, and the costs and benefits. The environment in which microinsurance operates is as important to consider as the policyholders, providers and regulations.

4.1 Healthcare quality

Health insurance has little value if there is no access to good-quality healthcare providers. Outside urban areas, such healthcare is often not available. Government and donor inputs have most frequently been invested in the cities, leaving the rural poor with low-quality medical practitioners and frequently no doctors. In some countries, the government healthcare systems advertise themselves as being free to all, yet the poor who need to access these facilities are quite aware of the value of the "gift" that must be provided even for the least assistance.

Governments and civil society must create healthcare systems guaranteeing quality, equality and transparency. The involvement of patients in the process of managing or governing local healthcare providers is one way to ensure that they are responsive to the needs of their market, which is a key advantage of the community-based health insurance schemes. If they are supported by a strong apex body, MHOs can open the systems to effective health insurance products, improve care of those in need and allow governments to focus more on the people who are truly destitute and can only be covered by social protection.

4.2 Data for risk management

The limitations of healthcare monitoring systems in the developing world also have a great impact on the ability of insurance companies to understand the risk of the low-income market, and thus to calculate premiums appropriately. Where they exist, morbidity and mortality data that filter into the national databases generally reflect the wealthier segments of the market because these are the people who can pay for healthcare and access systems that are able to record critical risk information accurately. The illnesses and deaths of the poor may not make it to the national databases, for example when they rely on informal medical care or return to their rural home to die. This leads to severe loadings on microinsurance products, or overly optimistic risk premiums – neither of which aids microinsurance outreach.

Better data will result from better healthcare, improved government record management and requirements by insurance regulators, many of whom review premium calculations prior to product approval. This will improve the foundation upon which risk calculations are made.

A particular data-management challenge in some developing countries is the fact that there is no national identification system. This dramatically increases the potential for insurance fraud – a dead person mis-identified as a policyholder, a hospital patient being covered under someone else's policy, and numerous other ways in which the non-insured might be covered as an insured. The significant cost of such fraud is reflected in premiums. This problem is not limited to insurance and as countries move towards introducing reliable national identification systems, the financial sector in general will improve.

4.3 Macroeconomic conditions and the development of financial markets

Weak economies with periodic bouts of hyperinflation and currency devaluation create strong deterrents to long-term investment and thus undermine the life insurance business. Weak banking infrastructures make it difficult to manage financial assets efficiently. Effective and diverse microinsurance depends on strong economies with efficient financial markets and infrastructures. Well-conceived efforts in this area by governments will have a positive impact on the expansion of insurance products.

One aspect of microinsurance that is often overlooked is the potential for microinsurers to accumulate large amounts of capital and reserves. The accumulation of any investment capital is highly desirable in the developing world. However, unlike other industries, insurers tend to build long-term capital, which fosters the growth of long-term investment markets, creating an ideal situation for the development of physical infrastructure. Most insurance companies have investment strategies based on an asset-liability matching model and since the liabilities can fall due in 15 or 30 years, the appropriate investment opportunities are usually found in government bonds, transportation projects and housing construction. It is not a total coincidence that countries where the insurance and pension sectors are fully developed also have vibrant long-term investment markets and a substantial physical infrastructure.

4.4 Catastrophic risks

The catastrophic risks of climate change, HIV/AIDS, avian influenza and others still to come will have an important and dramatic impact on the provision of all insurance, and especially on microinsurance. Low-income people are typically the front-line losers in catastrophic events. Since their incomes are low, they live in high-risk areas where others will not live. They must take risks that make them more susceptible to diseases, and have less ability to cope when catastrophes do occur. Insurers and reinsurers need to recognize the effect of catastrophic risks on the low-income market and work to develop efficient mechanisms to help the poor prepare for these risks and recover after they occur.

Due to a lack of care for the environment across the globe, weather is becoming more unpredictable. The resulting natural disasters hit agricultural communities the hardest. Governments and the insurance industry are hard-pressed to protect against these losses; notwithstanding that, only 20 per cent of worldwide agricultural production – crop and livestock – is insured today (Kasten, 2004). An innovative approach to extending financial protection to small farmers, herders and producers is index-based insurance. Simply put, it moves away from individual farm insurance towards coverage for a farming area. This would make collective care for the environment in the insured community relevant and essential to help mitigate losses.

The health issues of HIV/AIDS, new mutated flu strains, malnutrition and other diseases will be exacerbated in the future. Although microinsurance cannot solve these issues single-handedly, it can be a valuable tool in the battle against these scourges if microinsurance prepares and adapts. For example, the role of insurers in building appropriate infrastructure such as preventive healthcare will become more prominent as appropriate risk-management products are offered in these markets.

5 Embracing the future

If the future were known with absolute certainty, futurists would be redundant. They consider historical and current developments and expectations of the future to identify emerging trends. Actuaries are the futurists of insurance – they look at past experience and forecast the future using mathematical and statistical models of mortality and morbidity. Among the authors and readers of this book's chapters are consulting actuaries who have been advising microinsurance practitioners. What future do they see for microinsurance as they gaze into their crystal ball?

- Expanded technology where even low-income people have easy access to insurance products through computers, cell phones and smartcards. For insurers this will dramatically improve access to the market.
- Improved awareness of the benefits of insurance within the low-income market. People will appreciate the usefulness of insurance and their greater expectations will make for a more discerning market.
- A better distinction between what government social protection systems will do and what other insurance mechanisms will cover. This will help to clarify which risk-management solutions will be appropriate for which sections of the population.
- The spectre of global climate change, emerging diseases and other potential catastrophic events will hang over all long-term plans.

In the short run, in some countries, microinsurance, though desperately needed, will not spread massively; nor will it offer the variety of products and services that could help low-income people. These countries are simply not moving towards an environment which would allow successful microinsurance markets. Where conditions are improving – with stable economies, the development of financial markets, improving healthcare quality, insurance supervisors with a market development agenda, etc. – microinsurance will flourish. Such a change is likely to take time without a concerted push by policymakers, donors and the international community. Indeed, improved risk protection for the poor is not just a local issue, as epidemics and disasters can have ripple effects across the globe, justifying a greater role for international agencies and multinational corporations.

To insure the poor, customers, regulators, policymakers, insurers and social organizations must work together with a common purpose and unrelenting spirit:

- **Insurers** must strive to understand the customer's changing needs and adapt their products and services accordingly, continually improving the cost-benefit ratio for clients.
- **Regulators** must promote a development agenda for inclusive insurance markets, finding the right balance between protecting consumers and expanding access.
- **Policymakers** need to create an enabling environment that includes the necessary infrastructure for providing microinsurance.
- **Social organizations**, including employers' and workers' organizations, cooperatives, NGOs and other associations can play a critical role in organizing workers in the informal economy who lack access to social protection or other types of microinsurance.
- Lastly, the **billions of poor people** who do not have a formal way of coping with risk must respond positively to the efforts of providers and regulators in accepting a culture of insurance and its capability to provide financial freedom, security and well-being.

By itself, microinsurance will not put a major dent in poverty. However, if risk protection is effectively coupled with efforts to enhance productivity, together they can make great strides towards alleviating poverty and achieving the MDGs. Microinsurance will have succeeded when it is no longer needed. As the former Chair of Delta Life, Monzurur Rahman, said, "We want to see the day when there is no more microinsurance, just insurance."