Challenges and Prospects in Developing Microinsurance in Indonesia

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Introduction

Over the past few years, there has been intense debate and discussion over the need to develop microinsurance in Indonesia. Some are pessimistic about the move to develop microinsurance for various reasons. But others are optimistic about the prospect of microinsurance. Those who are pessimistic argue that it will take sometime for Indonesia to develop microinsurance sector given vast geographic area, low financial literacy among low income group of people, as well as the absence of adequate legal framework to support the microinsurance industry.

The low level of financial literacy is reflected in the low level of financial inclusion compared to neighboring countries. Financial inclusion is the capability of the people to have access to various financial institutions financial services. According to the central bank (Bank Indonesia) data, as of 2011, the financial inclusion index of Indonesia stood at 19.6 percent, compared to 98 percent in Singapore, 73 percent in Thailand, 66 percent in Malaysia and 35 percent in India. Financial inclusion index of Philippine was even higher than Indonesia, standing at 27 percent. This low level of financial inclusion is also supported by the number of Indonesians who have bank account. According to Bank Indonesia data, about 80 million people Indonesians or 62 percent do not have bank account.

Financial Service Authority or Otoritas Jasa Keuangan (OJK) has realized this condition. One of its tasks is to improve the financial literacy of the public at large. Financial literacy is important as it can accelerate people’s economic activities, which ultimately improves people’s welfare. Improving level of financial literacy is paramount for further lifting Indonesia’s economic development.

On the other hand there are those who are optimistic about the potentiality of microinsurance in Indonesia. True, that there has been low level of financial literacy or people’s access to financial institutions, such as banks or non-banks. True, that there has been no specific legal foundation that drive microinsurance in Indonesia. But that
does not mean that microinsurance cannot be developed and nurtured in Indonesia.

Nevertheless, we have million reasons to be optimistic. We have to look at it from different angle. The huge population base and low level of financial literacy can open doors to develop microinsurance, which ultimately improve people’s welfare. What we need is the strong determination of the industry players, regulator and all stakeholders to develop microinsurance industry in Indonesia.

So far, the financial inclusion is perceived and understood as the people’s access to banking. Financial access was even perceived as the capability of low income group and micro business to get small credits from banks or other financial institutions. Microfinance refers to a broad range of financial services such as deposits, loans, payment services and money transfers.

What is microinsurance? We can say microinsurance is an insurance policy specifically designed to meet the need of low income group of people. Thus, microinsurance offers protection for the low income group.

Microinsurance and Microfinance can be developed at the same time. The two types of services can support each other. On micro level such services has been applied by certain financial institutions or Cooperatives. Microfinance products are tied with some kind of microinsurance products.

**Microinsurance: Past, Present and Future**

Between period of 1945-1991, the insurance industry was guided by Staatsblad Year 1941 Number 101. During this period, the insurance industry was not really regulated yet. There was no formal supervisor agency that specifically governed insurance industry.

This condition encouraged the government to issue Law on Insurance [Law No. 2 Year 1992]. This Insurance Law provides legal basis for the current insurance industry.
Based on this law, the insurance industry is under the auspices of Finance Ministry, with Insurance Bureau acting as Supervisor. According to the law, the legal entities that are allowed to offer insurance products are Stock Company (or PT), Cooperatives and Mutual Company.

However, the Insurance Law does not specifically regulate microinsurance. Despite the absence of specific law or regulation on microinsurance, certain legal entities offered microinsurance products.

These entities offered microinsurance products through third parties, such as rural banks and Cooperatives or/and others. A number of insurance companies have offered microinsurance products, such as PT Asuransi Central Asia, PT Charties Insurance Indonesia (CII), PT Asuransi Allianz Life Indonesia and PT Asuransi Jiwasraya (Persero).

There are also microinsurance products offered by certain entities that serve low income group and their members, such as Koperasi Mitra Dhuafa which offers microinsurance products to hundred thousands of its members as well as Inkopdit, which also offers microinsurance products to million of its members. One of the main purposes is to serve the interest of their members.

The insurance industry players perceived microinsurance as insurance with low premium payment. With the offer of microinsurance products by these companies and entities, the insurance industry associations learnt that there is need and demand for microinsurance products.

There are various types of microinsurance products, such as personal accidents, savings, fire insurance and life insurance credit. Microinsurance can also be offered in the form of shariah microinsurance. This provides options for customers to own microinsurance policies in line with their needs.
Microinsurance is unique and therefore requires specific approach. The products cannot be offered like commercial insurance products. Therefore, specific regulation is needed. The regulator, in this case, Financial Service Authority, known as OJK, is now preparing Grand Design of Microinsurance in collaboration with industry practitioners. We expect that the presence of the microinsurance regulation (either in the form ministerial regulation, ministerial decree) will provide legal basis and promote the growth of microinsurance industry.

**The Importance of Microinsurance**

Microinsurance provides protection to low-income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of the risk involved.

Microinsurance helps low income group to recover from various perils and prevent them from falling into poorer condition. The target of microinsurance products are those who are living in rural areas, working in informal sector, farmers, fisherman, low earner workers, on so on.

From consumers’ point of view, microinsurance products can help improve the welfare of the low income group. Although they have limited financial capability, they have the access to protect themselves through holding microinsurance products. Microinsurance can protect them in the event of perils that they may encounter in their life.

From industry perspective, micro insurance can help grow their business. Although the premium is low, however, the potential volume is large. Therefore microinsurance can help boost the insurance industry’s growth. The growth of microinsurance can also increase the number of insurance policies, which ultimately increase the insurance penetration rate in Indonesia, which currently stands at around 2 percent of GDP.

From the government’s perspective, the microinsurance industry can help the government’s drive to eliminate poverty in this country. The greater chance for the low income group to get financial access and services the greater chance from them to
It is clear that microinsurance product is important, not only for consumers, industry but also for national economy in general.

**Characteristics of Microinsurance**

Microinsurance has unique characteristics compared to commercial insurance. Micro Insurance should have the following pre-requisites: Firstly, simplicity. It does not require complicated and detailed requirements as required under commercial insurance such as having had medical records. The products are designed in simple way and simple to understand. Simplicity can also mean that the product can be purchased quickly and the claim process is also quick. Secondly, affordable. The premium payment must be affordable to low income group. Thirdly, easy access or convenience, meaning that customers find it easier to get microinsurance products and easy to request claim payment. They don’t have to go far away to get the products.

**Challenges of Microinsurance**

It is important to provide legal basis (legal framework) for the development of microinsurance in Indonesia. So far, there has no specific regulations to govern microinsurance in the country. The presence of legal basis will provide certainty for players as well as customers, in this case people with limited financial capability, to purchase microinsurance policy. Legal basis will protect the interest of both the issuers and customers a like.

Microinsurance requires technology breakthrough to serve massive customer base whose locations spread out in rural areas across the country. The other way to reach out customers is through third parties.

The other challenge in developing microinsurance industry is lack of awareness about microinsurance. One way to improve the awareness is through embarking on capacity building programs, not only to customers, insurance players, but also other stakeholders.
For regulator, the main challenge would be preparing and issuing regulations to govern the microinsurance industry. Regulations can also be designed to help stimulate the growth of microinsurance industry. The regulations refer to the Grand Design of Microinsurance in Indonesia which is being drafted by the regulator, industry players, industry associations and other stakeholders.

The main challenge for the insurance companies and other legal entities would be how to market microinsurance products. To a certain extent, micro insurance is not too attractive for insurance companies because it is expensive from administrative point of view. It requires extensive human resources and information technology support. Technology is expensive, while revenue from microinsurance may not be sufficient to cover the expenses to develop the technology support. This opposes with the characteristic of microinsurance that is low administrative cost.

One way to resolve this problem is using multiple channels in making the products available to the end consumer. Microinsurance could be offered via third party entities, as we have mentioned earlier, such as Rural Banks (Bank Perkreditan Rakyat), Pawnshop (PT Pegadaian), Post Office (PT Pos Indonesia), Bank Rakyat Indonesia (BRI), Cooperatives, or other legal entities that have wider access to low income group of people.

**Conclusion**

Microinsurance is a neglected and hidden potential given huge market and growing income, however it is undeveloped yet. But the need and demand is there. Low income people need insurance products to cover risks they face, such as serious illness, poor harvest, death in the family and social obligations or need to cover education of children. Microinsurance policy could be vital to cover unforeseen events.

Microinsurance products, in particular, provide benefits to consumers. However, it also benefits the industry and the national economic development. Last but not least, our job,
i.e. as regulator, industry players and other stakeholders, working together to develop this microinsurance industry. (*)