

Access to Insurance Initiative - Toolkit No.2

Country Process Guidelines for Microinsurance Market Development



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About the Initiative Toolkit Series

This document was made possible with funding from the ILO and the UNCDF. It is *Toolkit II* in a series of Toolkits being developed for the Access to Insurance Initiative (Initiative). The development of practical toolkits for microinsurance development is part of the Initiative's inputs, along with the IAIS/Microinsurance Joint Working Group on Microinsurance, to the G20 Financial Inclusion Action Plan.

- *Toolkit I: Microinsurance country diagnostic studies - analytical framework and methodology* sets out the Initiative's analytical framework and methodology for market and regulatory diagnostic studies, so as to serve as a tool for conducting microinsurance diagnostics.
- *Toolkit II: Country Process Guidelines for Microinsurance Market Development* provides recommendations on the broader microinsurance development process to follow in a country, into which the diagnostic study (Toolkit I) feeds.
- A further toolkit will be developed for supervisory self-assessment of observance with the emerging IAIS guidance on regulation and supervision supporting inclusive insurance markets.

Each toolkit is a living document that will be updated from time to time as new learning emerges.

The Access to Insurance Initiative

The Access to Insurance Initiative was created jointly by the International Association of Insurance Supervisors (IAIS); the German Federal Ministry for Economic Development and Cooperation (BMZ), the Consultative Group to Assist the Poor (CGAP), the International Labour Organization (ILO) and the DFID (the United Kingdom's Department for International Development) funded FinMark Trust in 2009. The United Nations Capital Development Fund (UNCDF) joined as partner in 2010.

The Initiative is a global partnership between insurance supervisors and these founding sponsors. The Initiative also works with regional partners such as the Asian Development Bank, the Inter-American Development Bank (via its Multilateral Investment Fund) and Promoting Financial Sector Dialogue: Making Finance work for Africa Partnership (MFW4A), a partnership between BMZ and other organisations.

The Initiative supports the improvement of the policy, regulatory and supervisory frameworks and works in partnership with insurance supervisory authorities. The core fields covered by the Initiative are knowledge generation and dissemination, dialogue and learning through country diagnostic and thematic research, inputs for the development of standards and guidance, support to country implementation processes in the area of regulatory and supervisory reform, capacity development of insurance supervisors, and advocacy and participating in international platforms. The Secretariat is hosted by the German International Cooperation (GIZ) on behalf of BMZ. For further information, please visit www.access-to-insurance.org

1. Purpose of the document

What is microinsurance? Why is it important? How do microinsurance markets typically develop? What are the benefits of a deliberate strategy or process to develop microinsurance? What steps can be taken to develop the microinsurance market in a particular country? What are the issues to consider in doing so and what are the possible risks involved?

This document will consider these and other questions by drawing on country experience in microinsurance development thus far¹. It is aimed at any interested party wishing to proactively promote microinsurance development in a specific country. It is intended as a practical tool to guide the reader in unpacking the process of a microinsurance development strategy and the fundamental questions underlying it. It highlights the considerations to take into account, steps, stakeholders, issues that may arise and desired outcomes of a microinsurance development process. Finally, it provides guidance on the core, practical questions faced by stakeholders aiming to promote microinsurance market development. Essentially, it groups these questions into three categories – “why”, “what” and “how”:

- **Why** is microinsurance important enough to justify a collective effort or strategy? This will be the topic of Section 3.
- **What** is microinsurance and what should you take into account when seeking to stimulate a market in microinsurance products? Sections 2, 4 and 5 will consider this.
- **How** do you go about formulating a microinsurance strategy and what are the key issues to address? This will be the focus of Sections 6 and 7

The purpose of Sections 2 to 5, the *why* and the *what*, is to set the stage for Section 6, the *how*, where the crux of the toolkit lies.

Box 1. What is a microinsurance strategy?

Though for various reasons a government may decide to adopt an official national strategy on microinsurance development, the term “microinsurance strategy”, “country strategy” or “strategy process” as interchangeably used throughout this toolkit has a broader, less official, meaning. It denotes any collective process or effort to develop the microinsurance market, informed by domestic market and regulatory realities. Such a strategy could be based on an official policy paper issued by the Ministry of Finance, or it could simply be an action plan or a road map that the Insurance Supervisor and key industry stakeholders agree to implement, to name just two examples.

Note, furthermore, that the framework provided here is **not a one-size-fits-all solution or a template that will be applicable in all situations**. Each country has a unique context and political economy and its insurance market has developed and will develop in a unique manner. The strategic questions and process to be followed will therefore differ from country to country.

To enable the reader to more easily navigate through the toolkit, each section opens with a box that highlights the critical questions covered in that section.

¹ See Appendix 2 for a list of country studies and references. The document also builds on a number of other documents as noted in Appendix 2.

2. What is microinsurance?

STRATEGIC QUESTIONS

1. What can be considered the “low-income market” for insurance in your country?
2. What does the insurance product landscape look like in your country? Does microinsurance differ from other, traditional products?
3. What products are targeted at the low-income market and what are their typical features?

Microinsurance is insurance² for the low-income market. Though there are a multitude of definitions of microinsurance in different contexts and for different purposes, the conceptual definition adopted for this document is that of the 2007 IAIS-CGAP Working Group on Microinsurance paper titled “Issues in the regulation and supervision of microinsurance”. It defines microinsurance as “insurance that is accessed by the low-income population, provided by a variety of different entities, but run in accordance with generally accepted insurance practices (which should include the IAIS Insurance Core Principles). Importantly, this means that the risk insured under a microinsurance policy is managed based on insurance principles and funded by premiums”. By implication social welfare or social assistance schemes that are not funded by premiums and managed according to insurance principles are not considered microinsurance.

Broad conception of low-income target market. According to the conceptual definition discussed above, microinsurance targets the low-income market. “Low income” is understood differently in different countries and contexts. Hence, there is no universal definition or guideline on what it should entail. Indeed, defining the microinsurance target market as consisting only of households within a certain income band at the lower end of the income spectrum is likely to be self defeating. Markets evolve naturally from their current client base to the next-most profitable area and it is unrealistic, without substantial state subsidy, to expect insurers to jump from the top-end of the market directly to the bottom – especially where there is a large middle market not yet served by formal³ insurance.

The definition of the microinsurance target market is therefore not necessarily determined by the national or international poverty line (though it may relate to some multiple of the poverty line). Absolute poverty lines denote absolute poverty. It may not be realistic to expect people living in absolute poverty to dedicate some of their disposable income to pay insurance premiums. The microinsurance target market thus typically excludes the very poor, who will remain dependent on public social protection.

On the other end of the income spectrum, microinsurance also excludes the traditional insurance market. The traditional insurance market would include commercial clients as well as the current retail client base (typically those able to afford the insurance policies currently available on the market). In many developing countries a very small proportion, typically less than 5%, of the population is covered by formal insurance.

The bulk of the population can therefore be considered as the microinsurance target market. The following diagram provides an indicative example, plotted against the income distribution in a hypothetical country:

² An insurance policy, and thus insurance, is defined as a contract that promises to pay an agreed amount or provide a defined benefit upon the occurrence of an agreed event in exchange for the payment of an agreed premium.

³ Where “formal” denotes insurance provided by licensed providers compliant with the insurance laws of the country.

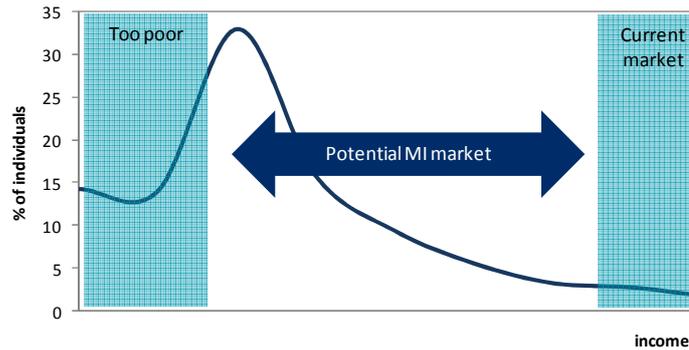


Figure 1. Illustration of microinsurance target market.

Unique product nature. Microinsurance is not traditional insurance products shrunk by a factor of 5, 10 or a 100 to fit the pockets of low-income households. Besides having lower disposable income, low-income households have needs distinctive from those of their higher income peers. Their experience and thus perception of insurance also tends to be different from traditional policyholders and is often characterised by high levels of distrust of insurance and insurers. Their living and income situation is also different from the traditional client segment. To be viable, microinsurance products must be designed to address these characteristics:

- Microinsurance policies tend to offer **low benefit values** against the payment of small premiums. Some products offer cover of a few hundred dollars or less (though microinsurance benefits can also go up to \$1,000 or more) at premiums ranging from less than \$1 to several dollars per month, depending on the type of cover.
- To be understandable to a market with lower levels of financial literacy and higher levels of distrust, products are **simpler in design, have fewer exclusions** and dispense with long and complex policy documents.
- Asset insurance is often provided on a first loss (also referred to as sum assured) basis rather than an indemnity basis.⁴

The low premium nature of microinsurance has a number of important consequences, both for the underwriting and intermediation of microinsurance products:

- *Group underwriting:* Microinsurance product pricing is usually done on a group basis rather than through individual underwriting, as individual underwriting is too expensive. As a result, insurers targeting the low-income market often assess the profile of groups rather than of individuals. Insurers' lack of experience with the microinsurance target market means that they have limited actuarial data on this market, in turn implying that it may be difficult to get pricing exactly right. Due to this uncertainty, they are generally (though not always) reluctant to commit to a whole-life/long-term price guarantee or contract, rather opting for renewable cover with a shorter contract duration. A shorter-term contract gives the insurer the option not to renew the contract when it expires or to adjust the price on each renewal in line with the risk experience of the group.

⁴ First loss insurance refers to insurance that provides a defined benefit upon a defined event as opposed to indemnity insurance that indemnifies losses, i.e. pays benefits according to the actual value of the loss suffered..

- *Low cost distribution and administration:* Low premiums imply low margins, necessitating high levels of efficiency in the distribution and administration of microinsurance products. Similar to the experience with other bottom of the pyramid products and services, successful microinsurers have to develop new business models, especially on the distribution side, to be financially viable. The pressure of low margins combined with the requirement for active sales have driven most of the innovation in microinsurance distribution:
 - To secure scale, microinsurance is often sold to pre-existing client groups utilising third party sales forces rather than dedicated insurance brokers or agents. Examples of such third party sales forces include microfinance institutions, banks, labour unions, retail chains or community-based groups.
 - Furthermore, the distribution channel and/or an external third party may play a bigger role in administering the policy. The presence of an administrator, in turn, implies that the value chain may become longer and that distribution costs may be higher, proportionally, than for traditional insurance. Even at low absolute levels (e.g. \$0.3), intermediation costs may be high as percentage of premiums if premiums are low (e.g. 30% of a \$1 premium). Therefore claims ratios in microinsurance may also be lower than traditionally accepted levels.

Typical microinsurance products. The products with highest penetration in the low-income market in many developing countries are credit life insurance, funeral insurance and personal accident insurance:

- *Credit life* insurance, the most pervasive form of microinsurance worldwide, insures the value of the outstanding debt in the case of a policyholder's death or disability. It may include riders such as funeral insurance for the purchaser or insurance on the value of the product bought on credit if lost or damaged. The pervasive nature of credit life insurance in the low income market is due to the fact that credit providers, to protect themselves against payment default, often make the purchase of a credit life policy a compulsory precondition for the granting of a loan. At the same time, the policy protects the deceased borrower's family from having to repay the debt.
- *Funeral insurance* is term life insurance where the payout – which could be provided in cash or in kind – is intended to cover the expenses of a funeral. For most poor households, especially in cultural contexts where funerals are important events, the cost of a funeral is prohibitive. Informal risk pooling mechanisms to cover funeral, medical or other costs, such as burial societies or self-help groups are therefore often the first type of “insurance” to evolve in low-income communities.
- *Personal accident insurance* provides a payment for loss of life or disability as result of an accident. Such insurance is attractive to low-income persons exposed to high risk transportation or dangerous work environments.
- Illness is one of the highest risks for most low-income households. In some markets, *health microinsurance* is becoming increasingly available. The greatest limitations tend to be affordability and the non-availability of health services and it is often challenging to force successful partnerships with health service providers.

- Due to the high costs of individual loss assessment, as well as the fact that asset insurance is not a high priority for low income households, successful standalone⁵ *asset insurance* schemes are rare in the microinsurance space. However, the exception is Latin America, where extended warranties and different forms of home or asset insurance are operating at scale.
- *Agricultural insurance* can potentially play a very valuable role in the low-income market given the fact that so many people in developing countries depend on agriculture for their livelihoods. Traditional multi-peril agricultural insurance is however simply too expensive to be viable as microinsurance. Therefore weather index based insurance is drawing increasing attention, with an emphasis on innovative use of technology and the core role of partnerships within the agricultural value chain. Data availability remains a challenge, though, and few pilots have been successful without donor support.

Along with health insurance and most of indemnity asset insurance, agricultural insurance may therefore be a type of “second generation” of microinsurance products, as they have not yet taken off to the same extent as life, funeral and personal accident insurance. It is important to create a “product needs and landscape vision” as part of the strategy process.

3. Why develop the microinsurance market?

STRATEGIC QUESTIONS

1. What role could microinsurance play in the insurance market in your country, what public policy objectives could it achieve?
2. Is microinsurance making sufficient headway in fulfilling this role? If not, why not?
3. Will a strategy be needed to develop the microinsurance market?

This section considers the reasons for embarking on a microinsurance development strategy process.

Why microinsurance matters. Depending on country circumstances, there could be a variety of reasons why microinsurance should be promoted:

- *Core to broader insurance market development.* Because the bulk of the retail insurance market in many developing countries is effectively a microinsurance market (i.e. most of the households in the country are low-income,) microinsurance may be the best way to promote financial inclusion in insurance and for insurers to expand their business. In such a market microinsurance is not a peripheral issue and the implications of microinsurance for business models and regulation should be centre stage. The experience and efficiencies insurers gain in the microinsurance market will furthermore impact on the delivery of products to the rest of the market.
- *A coping mechanism for the poor.* Microinsurance may be a complement to social protection for poor households who are unable to cope financially with risk events. Low-income households are particularly vulnerable to risks leading to financial shocks and resort to various coping strategies when financial shocks happen. These include depleting hard-won savings, taking out a loan, calling on family and friends for

⁵ The inclusion of some kind of asset insurance is common as a rider on a different type of policy, e.g. for personal accident insurance.

contributions, selling assets or even taking children out of school. All of these mechanisms are sub-optimal and cause deterioration in the financial position of the household. Where such coping mechanisms cover costs only partially, households will sink deeper into poverty and the society as a whole will be weakened. To prevent this vicious cycle it is in the interest of the country to extend risk mitigation via the insurance mechanism as far down the income spectrum as possible to assist households to protect themselves against financial shocks.

- *Effective microinsurance supports asset formation.* By prefunding emergencies, microinsurance supports incremental asset formation in the low-income market and prevents those that have escaped poverty from falling back into it. Moreover, life insurance enables an intergenerational transfer for those who may be unable to save enough to leave a legacy, even if only to complete the education of their children. Therefore microinsurance is a vehicle for the mobilisation of funds from a macroeconomic point of view that can contribute to economic growth.
- *A tool for catalysing essential other services.* The reliable financial flows created by microinsurance can enhance the provision of essential services, such as health services, by the private sector. In some countries, the health services sector is reliant upon health financing through the insurance mechanism to be viable. Microinsurance can therefore support the provision of health services in an otherwise underserved area. The credit market is another example. Where clients have no collateral, credit markets may depend on credit life insurance to mitigate the credit provider's default risk.
- *Formal market development serves consumer protection.* The existence of informal microinsurance schemes may be widespread and pose consumer protection risks. Where the formal insurance market fails to deliver insurance to low-income households in need of risk mitigation products, the informal market often steps in, delivering microinsurance in an unregulated and/or unsupervised environment. Such informal schemes can be well managed and often are, but their informal nature makes them more vulnerable to abuse. In particular, they are seldom managed on an actuarially sound basis, which can lead to the failure of the scheme as a whole. When this occurs the damage is not limited to the members of the scheme, but can undermine the confidence, sometimes for many years, of an entire community in insurance as a product. Collective distrust, present in many countries, is more damaging for microinsurance growth than any regulatory obstacle.

But why should microinsurance market development happen by design? Why can the market not just be left to develop organically?

Markets do not always develop optimally by themselves. Appropriate formal products may indeed develop organically to serve the needs of a broad microinsurance market. In most countries, however, this is either not the case, or the formal market evolves very slowly or in ways that do not meet the risk mitigation needs of low-income households, implying that microinsurance does not yet reach its full welfare-creating potential. Why is this the case? There may be a number of contributing factors:

1. Market failure. A textbook market characterised by full efficiency and equity hardly ever exists. Microinsurance is no exception. Market failure happens when a market does not

allocate resources efficiently. Economic theory highlights four causes of market failure, two of which are particularly relevant for microinsurance (Bishop, 2004)⁶:

- *The existence of market power.* Where competition is not sufficient, the suite of products on offer, the features and the value provided will be suboptimal. There may also not be a large enough variety of players. Where there is not enough competition, existing insurers are comfortable serving the current market and have no incentive to explore new markets.
- *Information asymmetries between suppliers and clients.* Information asymmetries can relate to the insurer's knowledge about the client's profile or the client's financial literacy or awareness of insurance and understanding of the nature of the contract. In some cases, unscrupulous players may exploit clients' limited knowledge. They may not deliver on their promise of value or may provide downright bad value to customers. As insurance is a promise of future value in return for a premium, trust plays an important role. Market failure may undermine that trust.

2. *Investment hurdles.* In some cases insurers in the formal market remain reluctant to invest in microinsurance. In deciding to invest, companies weigh the risk-return ratio. Where the business case of a new market has not yet been proven or there are a number of uncertainties in the market or external environment (refer to the discussion of the microinsurance ecosystem in Section 5), as is often the case in microinsurance, it may be difficult to convince the board to invest. Where external parties share some of the risk, e.g. through co-funding of innovation, it may help overcome this investment hurdle.

3. *Policy and regulatory barriers.* Policy frameworks rarely include microinsurance and policymakers often lack awareness of microinsurance. Regulation furthermore imposes barriers to entry (by determining who may provide or distribute insurance and what entry requirements they must meet). Ongoing prudential and consumer protection requirements also entail compliance cost. Microinsurance business typically operates with small margins and requires scale and efficiency in distribution to be viable. Microinsurance is therefore particularly sensitive to compliance requirements that impact transaction costs. By increasing the cost of operation, regulation may inadvertently make microinsurance products unprofitable to deliver.

Policy and regulatory barriers are not only of an insurance nature, but could also lie in other areas such as financial sector or cooperatives regulation. Furthermore, in spheres such as health financing where multiple regulators or public authorities are involved, coordination failure becomes a serious danger – and one that can plague microinsurance development.

The *absence* of regulation or enforcement can also be a problem. In situations where there is limited supervisory enforcement capacity to formalise informal business, regulation offers consumers limited protection. The presence of informal players and channels may furthermore create an unlevel playing field vis-à-vis those who meet compliance costs.

Rationale for a microinsurance strategy. An active discussion and collective start – in the form of a microinsurance strategy or road map – can play an important role to overcome these barriers to catalyse or accelerate market development. It is important to note that a

⁶ The other two are: the existence of externalities and the existence of public goods.

formal microinsurance strategy will not *necessarily* be required: the market assessment may show that there is no need for an active strategy, as there are no significant barriers and/or the market is on track to develop organically. However, in many countries there are substantial obstacles to the delivery of microinsurance, implying that in most instances an active strategy is indeed needed. How ambitious and comprehensive that strategy is depends on the situation analysis and strategic objectives for that particular market.

The sum is bigger than the parts. It is important that microinsurance development efforts be coordinated, as there may be obstacles that are not within the ability of individual players to resolve. Where a number of different players each pursue their own microinsurance development objectives without alignment, the danger is that there will be no coherence in the development process, that informal markets will develop unchecked, with implications for consumer protection, and that formal market development may be suboptimal.

For microinsurance development to extend beyond individual efforts, a coordinated strategy that builds a common understanding and vision, sets common principles and defines the role of various stakeholders will therefore be important. Specific benefits include:

- (1) **Consensus building:** Microinsurance sectors in many countries are fragmented and underdeveloped. A strategy can help to reach a consensus on the role of different providers, the role of government agencies, linkages between public and private actors, and financial literacy and consumer protection work required.
- (2) **Sector coordination:** Often, there is no permanent forum for regular exchange between the public and the private sector, or other important or potentially important actors such as donors. The objective is to widen the scope of consultation by not only including explicit microfinance experts, but also all other players with an impact on the sector.
- (3) **Support institutions:** Support institutions or services for the microinsurance sector such as audit companies, rating agencies or credit reference services are not at a very advanced stage. A strategy will help to clearly establish the need for these support institutions and may help to make more funds available for their establishment. It could also assist in implementing necessary changes in the legal environment in order to facilitate the formation of additional support institutions.

4. How do microinsurance markets develop?

STRATEGIC QUESTIONS

1. Through what channels or models has microinsurance developed to date in the country?
2. What are the specific triggers that have set off market development?

Before embarking on a microinsurance strategy process, it is important to understand both the current insurance and microinsurance landscape and where it comes from. This section considers the evolution of microinsurance in a particular country. Section 5 then provides a guide for unpacking the current landscape.

Microinsurance markets do not develop in a uniform way. Each country is unique and so is its insurance market. Understanding the development path to date is an essential part of a

well informed, realistic strategy going forward. Experience to date reveals certain common drivers and even models of microinsurance market development:

1. *Credit-driven.* The growth of microcredit or the extension of credit to low-income households is probably the most common model for microinsurance development. To protect themselves against the risk of default, credit providers insist on their clients' entering into a credit life insurance policy when taking credit. The compulsory nature of this transaction means that it does not easily lead to further insurance purchases, especially where the client is not even aware that he or she is covered by insurance or where the pricing is opaque or exorbitant. However, there are also instances where credit life insurance has triggered the purchase of further policies leading to more extensive risk cover for the affected households.
2. *Prefunding of services.* Another indirect way in which low-income households enter the microinsurance market is through the pre-funding of large bulky expenses such as funerals or health services. Low-income households know that, should death or illness strike, they will face unavoidable expenses which they cannot cover from existing resources. An individual or household is therefore prepared to pay regular instalments towards covering these large expenses. Such instalment schemes are normally offered by the service provider, for example a funeral parlour, hospital or mobile phone retailer. Since the agreement between the customer and the service provider entails the provision of a defined service (for example a funeral of a particular quality, a defined medical procedure or a replacement telephone) upon the occurrence of an uncertain risk event, such instalment schemes amount to insurance. They often start informally, and then evolve into formal insurance schemes.
3. *Member benefit.* The incidence of large, bulky and unavoidable expenses referred to above can also trigger informal risk pooling schemes or member benefit schemes, for example provided by cooperatives or credit unions. In many countries, both developed and developing, the story of microinsurance starts with the formation of informal burial societies, self-help groups or community-based health schemes coming together to cover essential costs for members and their relations. These groups are driven by mutual support and solidarity. The same goes for cooperatives, credit unions or other mutual or community organisation where membership automatically entitles the member to certain insurance benefits. Most of them do not provide guaranteed benefits and simply contribute to the cost of the funeral or medical expense from whatever resources are available to the group. However, when such groups grow large and start to provide fixed or guaranteed benefits, they effectively evolve into insurance providers, requiring more rigorous risk management, with accompanying regulation and supervision. Alternatively, many mutual, cooperative or community-based groups may act as intermediation channel for formal insurance.
4. *Market extension by existing insurers.* In rare cases the main impetus for growing microinsurance comes from existing insurers. Early movers may see an opportunity in the low-income market that they are willing to invest in. In other instances traditional markets may become saturated or competition may increase due to liberalisation or the entry of foreign insurers. To maintain growth, some insurers are move into new markets, catalysing innovation, new product development and new business models, especially on the distribution side. This model tends to occur in more mature insurance markets.
5. *Added value for existing non-insurance client groups.* Institutions with large client or member groups may see insurance as an avenue to provide added value to existing

customers (and thus retain them for their main business) or members. Examples include retailer chains (notably white goods retailers), financial institutions (including microfinance institutions), labour unions, utility companies, agricultural input suppliers or various forms of cooperatives. The strength of this model is that it reduces the cost of intermediation significantly since sales, policy administration and even claims payment can be undertaken by the relevant institution and its existing staff. Moreover, product development is usually also driven by the intermediary institution, ensuring that the microinsurance products sold through this channel are appropriate for their customers or members.

6. *Financial inclusion policy initiatives.* The promotion of financial inclusion is now a key financial sector policy objective for many countries, often promoted at presidential level. A deliberate financial inclusion policy can vary from simply signalling the government's intent, to removing regulatory obstacles to extending access to financial services, to providing budget funding for financial access, to setting specific access targets for private sector firms with resulting penalties should they fail to achieve the targets. Although most financial inclusion policies primarily target banking and payment services and credit, microinsurance is increasingly finding its way into financial inclusion objectives.
7. *Direct government provision.* Publicly funded microinsurance schemes are found primarily in the health and agricultural sectors. Such schemes can be fully or partly funded by the state. To be sustainable, most contributory social health schemes are compulsory (by statute) for certain categories for citizens, notably those who are formally employed. However, they have limited coverage in countries with high levels of unemployment or informal employment. Public funding of microinsurance schemes, and the interplay that this will have with private market development, has to be factored into any microinsurance development strategy.

In embarking on a microinsurance strategy process it should be recognised that a country can follow one or a combination of these development paths, each with its own opportunities and challenges. It is important to take stock of the development path(s) in the country in question as part of the "what" underlying a microinsurance strategy, as that will help inform the specific strategy adopted. Indeed, the strategy process will be a way to systematically engage with the development path so far and the desired future channels for growth to achieve the market development vision set.

5. What does the microinsurance ecosystem look like?

STRATEGIC QUESTIONS

1. What are the different functions in the value chain and who are the players fulfilling them?
2. What other stakeholders and context factors will impact on the value chain?
3. Who are the regulatory stakeholders to bring on board or take into account?
4. At what stage of development is the market currently and how will that inform the strategy?

The preceding sections provided some background on what microinsurance is, the rationale for developing it and the channels for microinsurance market development. In designing a process or strategy for microinsurance market development, it is also key to have an understanding of the current microinsurance market in the particular country, the functions to be fulfilled, the players involved, the broader context or enabling environment within

which it operates and the stage of development that the market is currently at. This set of factors can collectively be referred to as the *microinsurance ecosystem*⁷. The analogy is drawn from the ecology field, where an ecosystem is defined as an ecological community that, together with its environment, functions as a unit⁸. The ecosystem can be illustrated as follows:



Figure 2. Illustration of the ecosystem.

Source: web image

The ecosystem analogy provides an appropriate lens for considering the microinsurance market since it encompasses both the value chain (the ecological community) and the environment (all the other contextual factors) within which all the players that participate in the value chain operate. Seeing the one without the other will produce a partial picture at best and lead to a flawed strategy for market development. The nature of the ecosystem will determine who it is that you need to bring on board in the strategy process and what particular aspects to cover or elements to take into account.

5.1. Insurance functions and value chain

Core to the microinsurance ecosystem is the value chain – the various entities that each fulfils one or more functions in the insurance market. In order to better understand how the value chain is constituted and what the implications thereof may be for the microinsurance strategy, it is important to first understand what the different functions are to be fulfilled in the microinsurance value chain.

Insurance functions

The insurance market comprises a number of functions:

- **Underwriting.** Insurance entails risk management. The insurer underwrites a policy by determining what risk it is prepared to assume for what premium. Across an entire portfolio of policies, risk management requires a thorough understanding of the nature and degree of the various risks present in the policies. The risks must be quantified (a task normally performed by an actuary) and the quantification must be used to

⁷ Note that, in the logic of the Initiative and its partners, the *financial system framework* is most often used to describe the microinsurance market. It consists of the **macro** level (enabling environment, regulatory framework), **meso** level (support organisations and infrastructure) and **micro** level (players in the value chain). For the sake of illustration, the ecosystem analogy is used here, but in a way that is consistent with the logic of the financial system framework.

⁸ <http://www.answers.com/topic/ecosystems-1>

determine the actuarial reserves and capital required to ensure the long-term sustainability of a microinsurance operation⁹.

- *Investment*. The investment function requires the placement of premium and other income in a portfolio of assets to optimize the value of the investment earnings while maintaining appropriate liquidity and asset security to meet policy obligations as they arise¹⁰.
- *Reinsurance*. Reinsurance is a form of insurance that insurance companies buy for their own protection and whereby one or more insurance companies assume all or part of the risk undertaken by another insurance company¹¹. In this way the risk is pooled broader than just the insurer's own book – which is for example important for catastrophic risks. Reinsurance can play a vital role in ensuring the insurability of some types of risk for the low-income population.
- *Product development*. Product development entails conceptualising a product need, conducting market research, determining the features of the product and piloting to test the viability of the project and on the basis of which product features can be tweaked. It requires market intelligence as well as knowledge of insurance principles.
- *Intermediation*. Intermediation refers to all activities that happen “in between” the insurer and the client. It will include sales, premium collection, claims settlement and management, policy administration and client aggregation¹². More formally¹³, intermediation can be defined as any action that results in a client entering into a transaction with a product supplier, or any act with a view to buying, selling or otherwise dealing in, managing, administering, keeping in safe custody, maintaining or servicing a financial product purchased from a product provider.

Microinsurance value chain

The functions described above are fulfilled by various entities that together comprise the insurance value chain. Traditionally, underwriting, financial management, product development and much of policy administration are all conducted by insurers, with reinsurers conducting reinsurance and in many instances also being a source of risk management expertise, for example by providing pricing inputs. Most intermediation and some administration functions would traditionally be fulfilled by brokers and agents. In such a scenario, there are only three entities in the value chain.

The microinsurance market has however evolved to a situation where there is often a longer value chain, with more entities involved. The microinsurance value chain can be represented as follows:

⁹ See Garand, D and Wipf, J, *Risk and Financial Management*. In: C. Churchill (ed), 2006., *Protecting the Poor: a Microinsurance Compendium*, p254.

¹⁰ See Garand and Wipf (ibid): 265-267.

¹¹ Definition taken from the Microinsurance Network lexicon, www.microinsurancenet.org.

¹² Aggregation can also be termed “client mobilisation”; it refers to the formation of client group to which insurance can be sold, or to an existing grouping being used for insurance distribution purposes

¹³ As defined for example in the South African Financial Advisory and Intermediary Services Act.

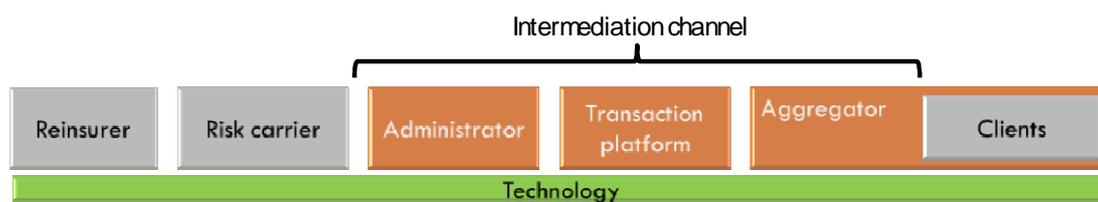


Figure 3. The microinsurance value chain

Source: adapted by the authors from Leach (2005)

Between the reinsurer and risk carrier/insurer (who is responsible for underwriting, financial management and some product development) on the one hand and the client on the other hand, the following entities can be found:

- a professional *administrator* (who could also be a brokerage firm) that does, or contributes to, product development and conducts back-office functions related to policy administration;
- a payment system provider that provides the *transaction platform* for premium collection and claims payments; and, in many cases
- a client aggregator (e.g. an MFI, a retailer or a community association) that aggregates individuals into a client group and does marketing and selling of policies (fulfils the front-office functions). The aggregator may or may not be involved in administration and may also provide the transaction platform.
- In some cases, the value chain can become even longer, for example to also incorporate a broker to facilitate the relationship between the aggregator and the insurer, or individual agents who sell the policy.

Underlying all of the entities in the value chain will be the technology and systems that enable all the various functions.

It is therefore apparent that quite a number of entities need to be considered when building an understanding of the microinsurance market. Likewise, there can be costs and bottlenecks to development – or opportunities – at different levels. In devising a microinsurance strategy, as will be discussed in Section 6, all potential value chain players should be considered and involved as stakeholders.

5.2. The enabling environment

The ecosystem consists not only of the functions and stakeholders inside it; it is also impacted by its external environment, namely the regulatory framework and the context within which it operates, as well as the infrastructure underlying it.

There are a number of environmental factors that impact on the microinsurance value chain. Among the most important are:

The policy, regulatory and supervisory framework. Government policy towards financial sector development in general and financial inclusion and insurance sector development in particular, will strongly influence microinsurance development. The policy considerations are numerous, but generally a policy position that supports the growth of financial inclusion in all financial services, not only insurance, will facilitate microinsurance. In the insurance sector, the higher the regulatory burden on insurance and its distribution, the more it will

inhibit microinsurance development, while a lower regulatory burden, or even a second tier of insurance license, will facilitate moves down market¹⁴.

Other policy fields and accompanying regulation may also impact microinsurance. These include, amongst others:

- *taxation*: for example where value added tax is levied on insurance premiums;
- *health regulation*: since health financing and the availability of public and private health services will determine the viability of health microinsurance, the nature of health regulation may have a bearing on the microinsurance strategy;
- *cooperatives regulation*: the strength of cooperatives regulation and supervision will affect the viability of mutual insurers;
- *social protection*: the extent of government provision in risk mitigation will determine where the private sector can play a complementary role; and
- *agricultural regulation*: agricultural regulation in general or regulation relating to agricultural cooperatives may be relevant for agricultural insurance or the distribution of other types of insurance to farmers and others in the agricultural sector.

All of these fields – and others that are relevant in the domestic context – will have to be considered as part of the strategy process and each of the responsible regulators may be a potential stakeholder to take into account.

The capacity and orientation of the insurance supervisor. While policy is generally made by the Ministry of Finance, detailed insurance regulation as well as supervision often falls to the national insurance supervisor. The approach of the supervisor, as well as its capacity to supervise, will therefore play a critical role in the evolution of the microinsurance market. For example, a supervisor with a restricted budget or small team may be reticent to permit a number of small microinsurers to be licensed simply because it does not have the resources to oversee many small entities. Likewise, the supervisor may find it difficult to implement the required adjustments to the supervisory system implied by microinsurance, for example separate reporting for microinsurance or different modalities for on-site supervision.

Economic, demographic and social context. A country where the bulk of the population is poor will face different consumer education, product design and delivery challenges than an upper-middle-income country. If most of the population live in rural areas, innovative distribution strategies will be needed to reach them. If most of the population are financially illiterate, this will likewise shape market development strategies. Furthermore, if the country experienced a financial crisis or hyperinflation in the past that eroded life insurance value, building trust among the target market may be a particular challenge. Culture can also be a determinant of the need for insurance as well as of the structure of the market. For example: in some countries the cultural need for a dignified funeral drives demand for life insurance and leads to a proliferation of informal players, whereas in others an aversion to talk about death may cause an avoidance of life insurance.

¹⁴ See the 2007 IAIS-CGAP Joint Working Group on Microinsurance Issues Paper on the Regulation and Supervision of Microinsurance, as well as the 2008 document titled “Making insurance markets work for the poor: microinsurance policy, regulation and supervision (full references in Appendix 2) for more guidance.

Payments and telecommunications infrastructure. The technology platform and payment system necessary to manage information, collect premiums and pay claims underlie the value chain. A basic level of financial and payment system infrastructure can in many cases be regarded as a prerequisite for large-scale microinsurance take-off. The introduction of cost-reducing technologies to communicate with clients, collect premiums and make pay-outs makes low-premium policies viable that were previously unviable. It also connects insurers to new clients. Likewise, the physical and telecommunications infrastructure will drive the value chain and its development. A country with well developed infrastructure will face fewer challenges than others. Payment system and infrastructure providers will therefore need to be considered as stakeholders in the insurance development process.

5.3. Market development stage

The last step in understanding the microinsurance ecosystem is to determine the current level of market development, as that is the point of departure for the strategy. Countries where the insurance sector is small and underdeveloped, with a limited product suite, will face a different set of development challenges than those where there is a well-developed sector with broad-based competition and a variety of products already on the market. In the same vein the current balance between formal and informal markets will impact on what strategy is required.

Markets tend to develop through distinct stages. As Figure 4 illustrates:

1. Some markets will be at the **pioneer stage**, i.e. just setting off, with limited microinsurance activity. The environment will not necessarily be favourable for development yet. Generally, relative macroeconomic stability, a basic level of industry development and the existence of a basic insurance regulatory framework will be conditions to a market development strategy taking off.

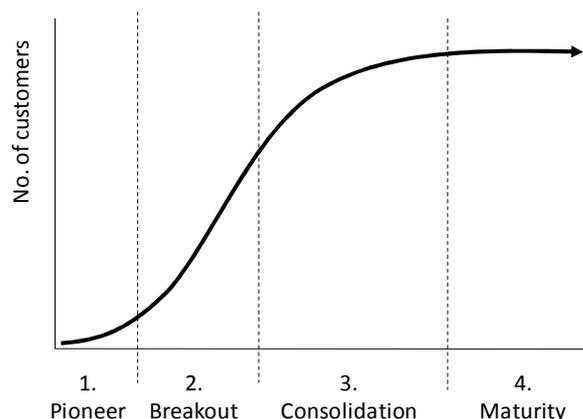


Figure 4. Market development stages

Source: Bankable Frontier Associates

2. Some markets will be at the **breakout stage**, where a few models have demonstrated success and others are following suit. The breakout stage may also be the stage during which microinsurance regulation is put in place or the regulatory framework is adapted to accommodate microinsurance.
3. During the **consolidation phase** there will already be a critical mass of activity. Further growth takes place as the industry consolidates and outstanding issues in the regulatory framework are resolved based on the learning from the initial experience.
4. Finally, some markets will have reached **maturity**, with limited scope for further growth.

With a few exceptions, microinsurance markets tend to be at stage 1 or 2. An organised approach that incorporates all stakeholders can play an important role in progressing market development.

6. Designing a microinsurance strategy

The preceding sections provided a guide for answering the “why” and the “what” underlying a microinsurance development strategy. They outlined the rationale for a deliberate, coordinated effort across a variety of stakeholders to develop the microinsurance market, as well as the importance of taking stock of the meaning and importance of microinsurance in the local context, the evolution path of the domestic market, and the functions, stakeholders and environment that form the microinsurance ecosystem. But how do you devise and implement an effective strategy? This section considers the “how” of a microinsurance strategy by unpacking some of the questions that arise when embarking on the process.

The issues and recommendations set out below are intended as practical guidance for those wishing to catalyse and support market development, rather than as a prescriptive checklist or sequence of events. Local buy-in and tailoring the strategy to the domestic context will be very important. The strategy itself is not the major output, but should rather be seen as a guide towards the desired outcomes.

STRATEGIC QUESTIONS

1. Where are you heading?
2. How do you define microinsurance for the purpose of the strategy?
3. How do you develop a microinsurance strategy?
4. Who can support the process?
5. Who takes the lead and who pays?
6. How long will it take?
7. What pitfalls to avoid?

6.1. Where are you heading?

When devising a microinsurance development strategy, it is worth having some vision of the desired end-state or ultimate market position you want to achieve. Generally, the aim is to work towards a well-functioning insurance market that serves the largest possible number of customers and that will exhibit the following features:

- General awareness amongst the target market of the value and purpose of insurance and how to use it.
- Efficient policy, regulation and supervisory systems that do not impose unnecessary costs and facilitate innovation and the introduction of new products, efficient services and administration and delivery, while ensuring stability and consumer protection as well as easy access to recourse for consumers
- A variety of insurance providers and intermediaries, staffed by an appropriately skilled workforce, that profitably and sustainably serve the needs of the widest possible target market, thereby achieving scale, high outreach and value-for-money products.
- Sufficient transparency and competition to ensure good prices and value, as well as ongoing innovation, a variety of products and a variety of intermediary models

The specific goals, strategic objectives or end-state vision will differ from country to country. Determining the strategic objectives is the first task of a microinsurance strategy. The second task is to determine what microinsurance is for the purpose of the strategy and who it should reach.

6.2. What definition to include in the strategy?

Conceptual definition linked to the target market. Who do you want to reach through the strategy? Is the target market all those who are not currently reached by the insurance market, or is the objective to reach specifically the poor or rural population? The answer will determine what microinsurance will mean, conceptually, in the country. As discussed in Section 2, the market segment targeted by the strategy will be informed by the understanding of what microinsurance is in the specific market, as well as the strategic objectives or desired-end state to be achieved.

Do you need a formal definition? Once there is clarity on who the target market is, the next question is whether a formal definition will be required to ensure that microinsurance is effectively targeted. Section 2 gave an overview of the conceptual definition and shared features of microinsurance products. But how do you *practically* define microinsurance for strategy and regulatory purposes? Why formally define it in the first place?

Whether a formal definition will be necessary will depend on the country context and whether or not a dedicated microinsurance regulatory framework is pursued. Even where a regulatory definition is not required, a formal definition of microinsurance may still be regarded as useful by other stakeholders, in which case it may for example be adopted by an industry association. The benefits of formally defining microinsurance include:

- *Industry dialogue and alignment.* Microinsurance is a new field for both market players and regulators. A shared definition will ensure a common understanding of the nature of the products that could help them to work together in building the market.
- *Delineating a microinsurance space in regulation.* A definition may be used to limit microinsurance to lower-risk products by setting certain product parameters (for example by relating to the contract term or the benefit level) that all microinsurance products have to meet. The setting of product parameters would allow regulation to be tailored to the risk profile of the product category by removing or relaxing certain regulatory barriers. Tailored regulation, in turn, could facilitate market development.
- *Delineating the target market.* A definition may also be required in instances where government wishes to target subsidies or tax concessions specifically to microinsurance, or where it wants to enforce a quota or target on industry for reaching a certain segment. Likewise, industry may want to define its target market through a definition.
- *Facilitate supporting initiatives.* By pegging the parameters of the market, a definition could also promote consumer education, protection and recourse measures that will be appropriate to the target market.
- *Government coordination.* A further advantage could be that an official definition (whether in regulation or not) will support the coordination of different levels of government in developing the market, as well as reassure potential industry players in cases where regulatory frameworks may not yet exist.

If any of these rings true in the specific context, a formal definition of microinsurance is called for. Once the decision to adopt a formal definition has been made, the next step is to decide what that definition will be.

Parameter-based definition. A definition that will be applied in regulation and business practice needs to be specific and practical. Different countries have followed different approaches based on their unique country contexts. The approach has however consistently been to use a combination of product parameters to delineate microinsurance from other insurance products. Definitions can do one or more of the following:

- define a maximum (and sometimes minimum) renewable contract duration to limit the underwriting risk
- set maximum benefit values to ensure that the products will target mostly the poor (some countries prefer to set maximum premiums, others relate the limits to multiples of the minimum wage rather than to a monetary level)
- define the target market (e.g. those earning below a certain multiple of the minimum wage) and require insurers to design the product parameters in such a way that the products will mostly be used by this target market
- set simplicity requirements or require that policy documents be available in the vernacular
- limit the types of risk events that can be covered, e.g. excluding a savings component
- limit the deductibles and exclusions that are allowed on the policy
- stipulate whether it should be group or individual policies
- stipulate what distribution channels may be used and/or who the risk carriers/underwriters may be
- stipulate that premium payments should be flexible or tailored to the income realities of the target market

The specific definition to adopt cannot be prescribed in any toolkit. The decision to adopt a formal definition and the parameters to use must be determined in the local context and in a coordinated way between different stakeholders.

6.3. The process to develop and implement a microinsurance strategy

With the groundwork in place, namely the strategic objectives and the definition, the strategy can kick off in earnest. What will be the steps in the process? It is worth reiterating that markets develop in different ways. The country context and strategic objectives determine what the process in each country will look like, as will the political economy and domestic policy priorities. Nevertheless, it is handy to have some roadmap of potential steps that interested parties can use to navigate through the strategy development process.

Figure 5 gives an example of what such a process could look like. These steps can be implemented in different ways and combinations: some of them will happen sequentially; some will happen simultaneously; sometimes not all of them will be required; sometimes additional steps will arise that are not reflected here. *The process and elements provided below should therefore be regarded as indicative only:*

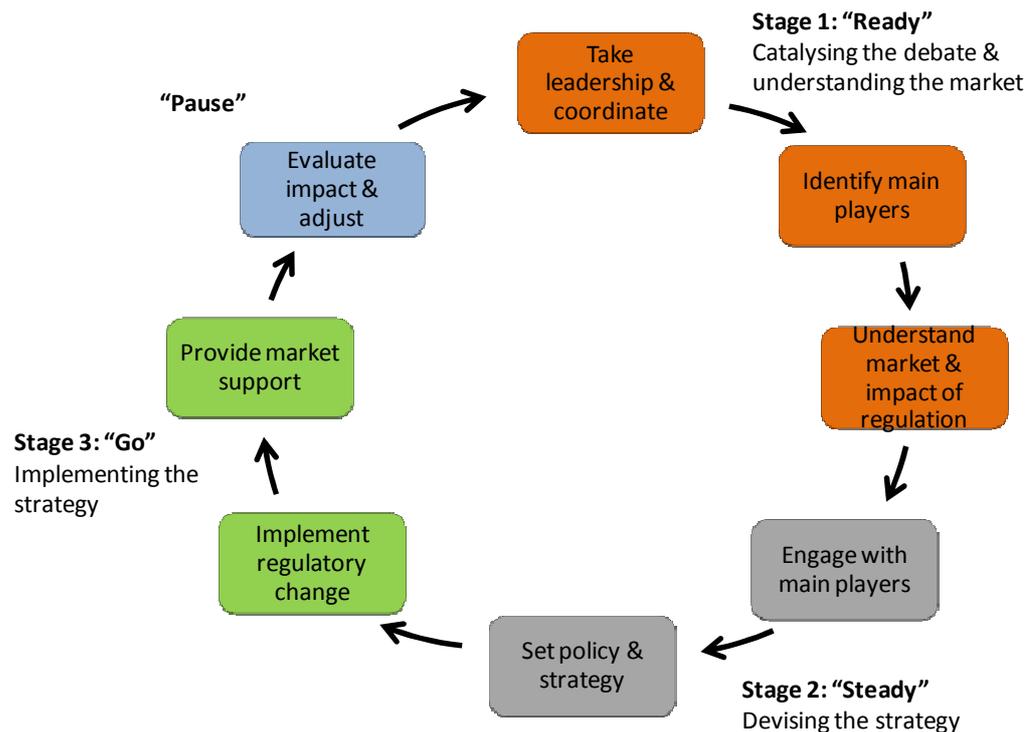


Figure 5. Steps to develop a microinsurance market

Source: authors

The **decision to support microinsurance development** (as discussed in Section 3) is the starting point. A particular trigger or a number of factors may combine to lead to such a decision and it can be made by one or a combination of stakeholders. Once the decision has been made, the process to design and implement the strategy can commence:

Stage 1: "ready"

1. Take leadership and coordinate. If coordinated action is required to move the microinsurance market forward, someone must take the lead. There is no specific recipe for who should take the lead. Different entities may lead different aspects or at different points in time. However, if substantial changes in the policy or regulatory environment are essential for market development, it will be very difficult to move forward without the active participation, if not leadership, of the relevant public entities and office bearers, particularly the insurance supervisor. Country experience reveals a number of possible leadership variations:

- *Policy-maker-led:* Sometimes the policymaker, through a financial sector development plan, broad microfinance strategy or financial inclusion policy, will be the leading player. When there is a financial inclusion policy in place, for example, it may be the source for a broad-based strategy to achieve financial inclusion in the insurance sphere.
- *Supervisor-led:* government and specifically the insurance supervisor has an important role in initiating a regulatory review process or by playing a core role in the strategy process and bringing other stakeholders on board. The supervisor could also use moral suasion to encourage the industry to go down-market. The Initiative is specifically focused on empowering policymakers, regulators and supervisors to be champions of

change. Even if the supervisor does not initiate the strategy process, it is important that it plays a proactive role and that full buy-in is achieved by the policymaker, regulator and supervisor.

- *Industry-led.* Industry can also take the lead in the strategy process, for example through a strong industry association, or if one particularly innovative leader champions microinsurance development and brings other players on board. In some instances industry players will realise that cooperation with government is essential to create an enabling environment for microinsurance development. They will then proactively involve the supervisor and/or policymaker. Such a situation is facilitated where there is already an “open door” spirit of cooperation between the supervisor and industry.
- *Third party-led.* Sometimes the discussion is initiated or led by a neutral catalyst or third party, for example a donor or other organisation that commissions research to inform the development process, that organises a stakeholder workshop to discuss the issues or that provides technical assistance to support capacity-building. Where such involvement is used to create local buy-in or ownership, the lead may then be taken over by the policymaker, supervisor or industry.

The need for coordination. There will be limitations on what the lead institution can do by itself. For example, it is possible for the state to initiate the process and provide a facilitative regulatory environment but it will be problematic for the state to push specific products or market development outside of state-owned insurers. Furthermore, different players in the ecosystem will have different agendas and there may be intricate politics involved. The insurance regulator may for example be concerned with what the features of the regulatory framework should be, how it should go about protecting consumers, or how to formalise the informal market. Other government departments may have other objectives, for example small business, cooperative or rural development. The market, on the other hand, would amongst others want to determine how to design and market microinsurance products and who their potential distribution partners could be, and would be want regulators to create a level playing field to avoid unfair competition from unregulated players.

A coordinated partnership between different stakeholders will be a vehicle to narrow down the key issues and to provide each group a platform through which to voice and address their own core concerns, while working towards the common goal.

Bringing all parties together in a loose partnership, establishing a means of regular communication between them, and securing their commitment to the wider process, even if not to any particular outcomes, will start to generate the flow of information and ideas without which the strategy process cannot progress. Maintaining the information flows throughout the strategy process will greatly enhance the chances of success.

It may make sense to form an action-orientated working group or committee to which all relevant stakeholders are invited and under which further activities can be pursued. It will form a neutral platform for engagement and debate among stakeholders and will ensure that the ultimate goals and strategy remain on the table in a coordinated way. In some instances, an independent coordinator will be needed on a full or part-time basis to steer the process, provide secretariat functions and coordinate activities. In other cases a specific

entity, e.g. a unit in government, an industry association or a private sector player will be tasked with coordination.

2. Identify the main players. Since successful strategy is coordinated strategy, an essential step of the strategy process is to identify the stakeholders, both public and private, to involve and who buy-in will be essential. Section 5 above provides guidance on who these players are likely to be, from among the value chain and enabling environment. Among the stakeholders there will be a few with particular vision and commitment. It is therefore important to determine where the energy and drive is concentrated and to involve such individuals in government and industry to champion the development of microinsurance in their specific spheres and to take part in the collective strategy process – even if they do not lead the process. Such champions are ultimately the ones that will ensure that strategy leads to action.

3. Understand the market and the impact of regulation. As sections 4 and 5 indicated, a strategy that is not based on market realities – a thorough understanding of the country context, the insurance industry and wider financial sector, the realities and needs of the target market, the current microinsurance activities, and the regulatory framework – is sure to fail. One way of completing the picture is to commission or conduct as comprehensive as possible a diagnostic exercise to gather accurate and reliable market information. Generally, a diagnostic investigation should consider the context, the market (supply and demand) as well as the impact of the current regulatory framework. The proposed methodology for country diagnostic studies is contained in a separate document¹⁵.

The diagnostic will form the basis for identifying the drivers of market development – related to context, the value chain and the regulatory framework. Understanding the drivers and features of the market will enable the identification of the opportunities for market development and the barriers or challenges to overcome in the various spheres of the ecosystem that will, in turn, form the basis for engagement with stakeholders and for the strategy that will emerge.

Stage 2: “steady”

4. Engage with main players. An important part of the strategy is to establish an engagement process to secure the buy-in of all key stakeholders – and then to keep them on board throughout the process. The aim of the strategy process is to trigger a set of actions by different actors that will jointly contribute to the growth of the market. These stakeholders make their decisions independent from one another based on the information available to them. The most important part of the strategy process is thus often the sharing of the findings of the market and regulatory diagnostic with all the stakeholders. Not only will the stakeholders provide feedback and recommendations for further action, but they will start to adjust their own practices based on what they perceive to be the opportunities. To be most effective, such engagement should happen at both a collective level, e.g. via a stakeholder workshop, as well as with individual parties when issues of confidentiality or private policy comes into play.

5. Set policy and strategy. Having considered the market dynamics and drivers and engaged with the spectrum of stakeholders, the government should declare its policy intent regarding

¹⁵ See Appendix 2.

the development of microinsurance. A clear public policy statement, assuming that regulatory change will take some time to effect, will already go a long way to stimulating a market response, since it serves to provide certainty regarding proposed government actions in the microinsurance space. A microinsurance strategy is, however, more than just a policy statement. It is likely to require multiple actions from public, private and other players. Securing agreement to such a strategy, or at least the key strategic objectives to be pursued and the main activities to be implemented, and involving the main players in such an agreement, will orientate much of the future development of the market.

Based on the outcome of step 3, a strategic action plan should be drawn up to articulate the barriers, opportunities and strategic objectives to achieve and the interventions or actions needed to achieve those objectives. The action plan will serve as a consensus document to ensure that all stakeholders are on the same page and strive towards a common goal. To make the action plan concrete, it should clearly specify the roles of the various stakeholders, the timeline for the implementation of the necessary activities as well as the monitoring arrangements that need to be in place. It is of fundamental importance that the action plan should be realistic about what can practically be implemented, rather than being overly ambitious.

There is no single template for what such an action plan should look like, but it is important to make the strategy concrete and to be systematic in the way that the actions, responsibilities, milestones and timeline are set out. An example of the format that an action plan can take is included in Appendix 1.

Stage 3: “go”

From strategy to action. The final step in the process is to implement the strategy. It is important to include clear, realistic milestones to measure progress so as to ensure that momentum is not lost. While it is laudable to be ambitious, an over-ambitious agenda will not be fully implementable and will undermine the credibility of the strategy. The strategy should identify a few key actions that can be effectively implemented. The two central components of the strategy will be:

6. Implement regulatory change Regulation will be one of the core areas that the stakeholders will consider. If the finding is that regulatory change needs to happen (this is not a foregone conclusion), the required change may be statutory in nature, i.e. a law to be passed by the Parliament or Congress or a change to subordinate legislation, or the regulator may simply issue guidance. Whatever the change, it will be speeded up and facilitated by a prior policy statement as described in point 5 above. It may also require detailed technical, including actuarial, work to be undertaken. Such processes are often aided by exchanges with other regulators who have undertaken similar processes.

Example actions to support the regulatory process may include:

- specific actions to overcome identified barriers, or, where needed, supporting the drafting of a dedicated microinsurance regulatory framework;
- developing an enforcement strategy for the microinsurance space, including actions to promote formalisation where this is a strategic objective and to protect consumers where this is a concern;

- facilitating industry-supervisor dialogue to build mutual understanding regarding regulatory objectives as well as the trade-offs and realities facing the market in complying with regulation; or
- taking part in the international debate and forums on microinsurance development.

Note that regulatory change does not necessarily need to happen before market change (point 7 below). The two processes can be initiated in parallel, or the strategy partners may feel that the market should develop first, providing an opportunity to evaluate impact and determine what regulatory response is required.

7. Provide market support. The strategy will also aim to trigger or support a market response. Section 3 above sets out some of the market failures and obstacles that require specific intervention to smooth the provision of microinsurance. Support to the market may take a variety of forms, for example:

- support for innovation and risk sharing for new business models (for example by providing open competition seed grants where funding is available);
- bringing on board potential distribution partners or aggregators in the discussion so as to facilitate partnerships;
- assessment of capacity gaps in developing and rolling out of microinsurance and products and in forging distribution partnerships;
- capacity building support, for example through technical assistance or training workshops for staff on product development, marketing, partnership management, or other relevant topics;
- generating information and data that can assist with market analysis;
- conducting feasibility studies; or
- developing industry codes and standards on for example product simplification.

Consumer education will be an important element in providing market support. The regulator and the market – in cooperation or separately – can take action to build insurance awareness. The strategy process plays an important role to identify what consumer education and awareness campaigns will bear most fruit and who could take responsibility for which aspects.

Further example activities are provided in Appendix 1.

“Pause”

8. Evaluate impact and adjust. The strategy will not be static. As the ecosystem – including the political economy, the market structure and economic environment – changes and evolves, the strategy will have to adapt to the new realities. It may also be that initial learning shows that some strategic actions are not worthwhile or that other priorities may arise. The strategy should therefore be designed to be flexible. Part of the strategic plan should be to incorporate “pause” moments where the course and impact of the strategy can be evaluated, along with market and environment developments in order to tweak the strategic plan going forward. It may even be that a complete change of course is required.

During this step you will ask:

- **Is it working?** What aspects of the strategy have encountered challenges? What elements are lagging behind in implementation? Why?
- **Has the ecosystem changed?** In what way? What does this imply for the outcomes we want to achieve?
- **What changes** should we make to the strategy?

Should the resources be available, it is advised to incorporate a formal, independent impact evaluation exercise at defined intervals to measure the outcome of the strategy against the desired end-state. Alternatively, this can be assessed internally. Either way, it is necessary to set a simple list of indicators upfront that can be monitored over time.

The Initiative has adopted the following performance indicators for which a baseline can be established and progress tracked over time¹⁶:

- The **number of microinsurance providers**: commercial and community-based, recently formalised;
- The **distribution channels used** for microinsurance intermediation: number of entities, role, size of channel as percentage of total market where available, number of insurers using each channel;
- The **number and appropriateness of microinsurance products** offered: total and by category (as per definition of microinsurance adopted). An “appropriateness index” can be compiled based on (1) *affordability* in line with income level and regularity realities of target market, (2) *accessibility* for buying the product, (3) premium payment conditions, (4) claims procedures and (5) *features vis-à-vis* the target market’s realities and needs.
- The **number of people taking up microinsurance** and the geographic and demographic composition of take-up, subject to availability of data;
- The **value offered by microinsurance products**: primarily measured through the claims ratio (claims paid as percentage of total premiums), as well as the incurred expense ratio (management, admin and distribution costs as percentage of premium) and the net income ratio (net income over net premium) of the industry. A key strategic impact will be to ensure that the necessary data is reported and tracked.
- The **appropriateness of policy, regulation and supervision** of insurance when assessed against the guidelines for the regulation and supervision of microinsurance markets (as per the forthcoming IAIS-Microinsurance Network Guidance Paper on the Regulation and Supervision of Inclusive Insurance Markets).

6.4. Who can support the process?

A non-aligned party may play an important role to facilitate conversation between different stakeholders so as to holistically support microinsurance development. Likewise, various entities can provide inputs or support to microinsurance development without being direct

¹⁶ The exact indicators and sub-indicators and how they can be measured should be defined at country level. At the international level, the Microinsurance Network has an ongoing project to develop specific performance indicators for microinsurance. For more information, see: <http://www.microinsurancenetowork.org/workinggroup/Performance-Indicators/9.php>

players in the value chain. A number of entities outside of the value chain may play such a role:

- *NGOs.* In many developing countries, NGOs play an important support role – be it directly in the financial sector or indirectly through activities such as consumer education.
- *Industry, trade and community associations.* A variety of associations representing different constituencies, ranging from business or SME associations, to labour unions, to community representatives, may be stakeholders in the microinsurance development process. They allow particular components of the target market to be represented in the dialogue.
- *Donors and multilateral organisations.* Multilateral or bilateral donors or private foundations may support financial sector development more broadly, or insurance development specifically, depending on their remit. In some instances donors who do not directly target the insurance market but focus on agriculture or other industries where insurance is of relevance will also play a role. The same goes for donors with an interest in social security and poverty relief.
- *Technical assistance or research organisations* can likewise play an important role in supporting microinsurance development. This category may include market survey companies, academic institutions and consultants.

6.5. Who provides the resources?

Any strategy will need funding for its activities. One of the incentives of a collective effort will be to syndicate funding. Funding may stem from various sources and the primary funder may or may not be the lead player. It may also take the form of in-kind contributions by all participating in the process. Coordination between funders is essential. There are typically three sources of funding for microinsurance development:

- *Government funding:* Governments tend to dedicate resources to drafting of regulation, as well as to supervision and enforcement. Government may also make staff resources available to the microinsurance strategy process, for example in the form of a dedicated team inside the supervisor to work on microinsurance.
- *Industry funding:* Industry will fund product design, piloting of new products and new distribution channels. Industry members can also pay for capacity building and other support provided to them as part of the strategy process. In this way, private sector funds can feed into the overall development strategy. At an industry level, through their association, the private sector can also contribute to the overall pot of funds for microinsurance development, or can for example fund consumer awareness or financial education campaigns.
- *External funding:* external funding (such as by a multilateral or bilateral agency) is sometimes used to support the microinsurance development process. External support could play a role as catalyst of the process, then stepping away once stakeholders become engaged. Alternatively, an external funder can stay involved throughout the process: in a “light-touch” way to facilitate or coordinate the domestic process, as core or co-funder, or as technical assistance provider to the process.

6.6. How long does it take?

To ensure realistic expectations amongst the stakeholders, it is important to take into account that the development process may take quite a long time to deliver results. The need for a longer time horizon should be understood by government (which typically expects the private sector to deliver results quite quickly), private sector (which typically expects government to change regulation quickly) and external parties such as donors (which typically want measurable outputs within programme lifetimes¹⁷). While short-term gains may certainly be possible, much of the development is likely to take longer.

The timelines will always be unpredictable and will depend on the conditions of each country. Nevertheless, it is useful to think through the possible stages of the development process and the time that each could take. A timeline scenario is presented in Figure 6. As with the other sections, please note that the suggested timeline is indicative only and will vary according to the domestic context and role players.



Figure 6. Indicative timeline across the microinsurance strategy stages

Source: authors, based on country experience

1. *Catalysing the debate and understanding the market.* The first stage will comprise the decision to support microinsurance development as well as the first three steps in the strategy process as discussed in Section 6.2. Generally, depending on the complexity of the market, at least six months should be allowed for initial research to scope the market and regulatory landscape. Then another six or so months are required for stakeholder discussions and debate. Part of this could overlap with the research process so that the combined process takes six to nine months, but it can also extend beyond that in more complex environments. Realistically, at least twelve months should therefore be allowed.

2. *Developing the strategy.* The second stage comprises steps 4, 5 and 6 of the strategy process, namely to reach agreement on the strategic goals and actions and to consider the required engagement process and coordination platform around that. At least another six to twelve months will be needed for this stage. If the research covered all the relevant issues, developing a strategy could be simpler and quicker as it will largely entail agreeing on specific activities to address issues identified in the research. Ultimately, the timeline depends on how inclusive and collaborative the process needs to be. While it may secure buy-in, a process that incorporates all relevant stakeholders may also take longer. Therefore a careful balance needs to be struck. The timeframe furthermore depends on whether there is a secretariat or coordinator to push and facilitate the discussion process. Without such support the process risks getting stuck due to the day-to-day priorities of the stakeholders.

¹⁷ Care should therefore be taken not to push for short-term developments to meet output requirements under a donor programme without considering the longer-term implementation process and requirements.

3. *Implementation.* Implementing the strategy (steps 6 and 7) will be the longest stage:

- **Regulatory changes.** In some cases, the process from when government first becomes aware of microinsurance to when regulation is actually implemented may take several years. If legislative changes are required that need to be submitted to the congress or parliament, the process from developing a policy position to congressional or parliamentary approval may take two years or longer, depending on the scale of changes proposed. Smaller changes or changes at the level of subordinate legislation may be much quicker but are still likely to take at least 6 to 12 months. It is also possible to facilitate market development through the use of circulars, guidance notes/memoranda or directives while the legislation or regulation is being developed. Again, the timeline will depend on the scale of changes proposed. Where directives relate to isolated issues, and if the proposed reforms are uncontroversial and receive the dedicated attention of the regulator, they may be finalised in 3 to 6 months.
- **Market changes/private sector response** will likewise take time. Typically, insurers will take some time to become convinced of the business case presented by microinsurance (that is: for market development managers to convince their boards to invest in microinsurance). Once the decision has been made, time will be needed to develop and pilot products. Piloting may require market research and capacity building, all of which will be time consuming. Insurers in most countries are unfamiliar with this market and familiarisation can take time.

All in all, it is likely to take a year or more for a new product or channel to get to pilot phase if it is supported by management, if the company has the skills required and if it receives dedicated attention. If, however, insurers' skills are limited and partnerships with foreign or other experts are required it may delay the process: not only because such partnerships need to be forged but also because management will be more hesitant to commit if they do not fully understand the outcomes. Another complicating factor may be the need to partner with groups or third party aggregators. It may take time to identify and assess suitable partners and negotiate a partnership that works.

Innovation will typically only happen where there are no regulatory uncertainties that may undermine the investment made in a particular product or channel. Hence it will be difficult to push the business side of development if regulatory uncertainties have not yet been resolved. If the opportunity is big and obvious enough, companies may be willing to take the risk, but with microinsurance this is rarely the case¹⁸.

All things considered, the implementation phase can therefore take anything from two to several years.

7. Ensuring success

In the microfinance field, national strategies do not have a particularly good track record in reaching the desired impact¹⁹. It is therefore important, from the outset, to deliberately avoid pitfalls experienced elsewhere. The following guidelines are aimed at avoiding pitfalls related to the process and the outcomes, respectively:

¹⁸ Conversely, it may be hard for regulators to know what changes are needed until insurers have some experience in the low-income market. The danger is that this will result in a deadlock. The strategy process is a key tool in preventing such a situation.

¹⁹ See the CGAP Brief on National Strategies, June 2008. The pitfalls to avoid listed here draw directly on this source.

Process

- *Start with a sound diagnostic.* In order to form an adequate basis for strategic action, diagnostic studies must have sufficient breadth and depth. This will ensure that the strategy does not miss important actions or prioritise others that may not be necessary. *Toolkit 1* provides a standard methodology for microinsurance country diagnostics to ensure that they provide the necessary depth and breadth of analysis.
- *Integrate with broader environment and political economy.* Where strategies do not properly take into account or link to the broader financial sector and environment, they may miss opportunities or embark on actions that will be undermined by environmental factors. It is essential to keep sight of the political economy and the need for political will to secure regulatory changes.
- *Ensure local ownership.* Strategies must caution against being donor-driven. Strategies that achieve impact have local ownership, with all key parties buying into the need for the strategy and its implementation. It is furthermore important that the buy-in from stakeholders is real and that all remain committed.
- *Ensure adequate government leadership and capacity.* Though a strategy needs to involve a broad stakeholder base, the commitment and role of government, specifically the insurance supervisor, is fundamental. If responsibility for the strategy is placed with a department or authority with inadequate capacity or that lacks political power, it may delay or even undermine the outcomes.
- *Adopt a realistic action plan.* Action plans that set unrealistic targets or are merely based on a template from another country without real tailoring to the local context will not succeed. Expectations that are not met will lead to disillusionment. Therefore rather take on less, especially where resources are limited, but make sure that you'll achieve it.
- *Remain flexible:* All things change all the time. The insurance sector and the broader financial sector is no exception. It is therefore critical for the stakeholders involved in microinsurance development to continue adjusting their strategies and approaches to changing conditions and as they learn from experience.

Outcomes

- *Keep the momentum.* Make sure that the momentum of the strategy is not lost after a while as the initial enthusiasm among stakeholders wanes. A specific and not overambitious action plan, with clear milestones, will help to maintain the momentum. It is also important to source enough funding to ensure that all aspects of the action plan are seen through.
- *Ensure impact.* The final and most fundamental pitfall to avoid will be that the actions simply do not lead to impact. In choosing which actions to pursue, the likely effect of such actions on usage of insurance among the target market should be the ultimate criterion.

If all of the above is considered from the outset, those embarking on a microinsurance country strategy process can have confidence that a realistic, context-specific, well thought through and coordinated microinsurance development effort will arise that will take us one step further, country by country, in achieving the goal of improving ordinary people's welfare by helping them to effectively manage their risks.

In conclusion: The Insurance Initiative works with policymakers, regulators and supervisors at the country level to catalyse market development and promote access friendly reforms. This document illustrates the role of a deliberate microinsurance development strategy incorporating a range of public and private stakeholders. It sets out the rationale for such a strategy and highlights the need for an understanding of the various components of the domestic landscape or ecosystem. On this basis, it provides tools for understanding the steps in and prerequisites for a successful microinsurance development process.

Appendix 1: Action plan template example

Goal:

-

Current state of the market:

-

	Strategic objectives:	Action steps:	Responsibility:	Milestones & timeline:
Key opportunities: • •				
Key challenges: Regulatory: • • Market: • • Context: • •				
Information gaps: • •				

Figure 7. Hypothetical example of an action plan template

Source: authors, based on country experience

Example activities that could be included in the action plan include:

Trigger or support an inclusive regulatory process	<ul style="list-style-type: none"> • Support for policy statement • Research to overcome identified barriers • Enforcement/consumer protection concern • Facilitating industry-supervisor dialogue • Taking part in the international debate and forums • Supporting further research, capacity building
Trigger or support a market response	<ul style="list-style-type: none"> • Developing industry codes and standards • Exploring business model options • Capacity building, workshops • Seed funding for innovative pilots • Generating quality information
Create insurance awareness	<ul style="list-style-type: none"> • Design & implement cons education campaigns • Developing common industry terminology • Creating a call centre

Figure 8. Example microinsurance action plan items

Source: authors, based on country experience

Appendix 2 : Relevant other Access to Insurance Initiative documents to consult

1. Access to Insurance Initiative Toolkit I: Microinsurance country diagnostic studies - analytical framework and methodology. Available at: www.access-to-insurance.org
2. IAIS-CGAP Working Group on Microinsurance, 2007. Issues in Regulation and Supervision of Microinsurance. Available at: www.iaisweb.org
3. IAIS/Microinsurance Network Joint Working Group on Microinsurance, 2010. Issues Paper on the Regulation and Supervision of Mutuals, Cooperatives and other Community-based organisations in increasing access to insurance markets. Available at: www.iaisweb.org
4. IAIS-CGAP Working Group on Microinsurance, 2008. Making insurance markets work for the poor: microinsurance policy, regulation and supervision. Cross-country synthesis report authored by H. Bester, D. Chamberlain and C. Hougaard, based on five input country studies. Available at: www.access-to-insurance.org
5. IAIS-CGAP Working Group on Microinsurance, 2008. Making insurance markets work for the poor: microinsurance policy, regulation and supervision. Five country studies: Colombia (authored by Fedesarrollo), India (authored by M-Cril), the Philippines (authored by Rimansi), South Africa (authored by Genesis Analytics) and Uganda (authored by Genesis Analytics). Individual country reports available at: www.access-to-insurance.org/country-experience.html
6. Bester, H, Chamberlain, D & Hougaard, C, 2009. Making insurance markets work for the poor: microinsurance policy regulation and supervision. Series of 12 thematic focus notes prepared based on the country case studies and cross-country synthesis. Available in English, French, Portuguese and Spanish. Available at: http://www.cenfri.org/index.php?option=com_content&view=article&id=84&Itemid=84



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