Tanzania Access to Insurance Diagnostic

Document 4: Insurance industry trends

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About the Tanzania Access to Insurance Diagnostic series

This is *Document 4* in a series of 8 documents that together comprise the findings of the Tanzanian Access to Insurance Diagnostic. The series consists of one headline findings summary and seven input documents, each focusing on a specific thematic area, that build up the evidence base to the headline findings:

1. **Headline findings.** This document summarises the main findings of the diagnostic study across the other documents, then concludes on market potential and opportunities, the challenges to be overcome and the strategic imperatives to unlock such potential.
2. **Context.** Document 2 outlines the macroeconomic, socio-economic, political economy and financial sector context within which the Tanzanian insurance market develops.
3. **Insurance uptake.** Document 3 estimates the current penetration of the microinsurance market as percentage of adults in Tanzania and how insurance uptake has evolved in recent years.
4. **Insurance industry trends.** Document 4 analyses recent trends in the insurance industry in terms of premium volumes, players and performance, asking what the catalyst for the next wave of growth required towards an inclusive insurance market will be.
5. **Product and distribution landscape.** Document 5 considers the current suite of products in the Tanzanian microinsurance landscape. In addition, it unpacks trends in insurance distribution.
6. **Health insurance dynamics.** Document 6 takes a closer look at the health insurance dynamics in Tanzania, given the unique features of the health insurance landscape.
7. **Regulatory framework.** Document 7 considers the role of policy, regulation and supervision in building an inclusive insurance market by unpacking the key features of the insurance regulatory framework, as well as ancillary areas of regulation.
8. **Understanding client needs.** Document 8 draws on focus group and demand-side survey research to better understand the economic realities, risk experience, coping strategies and knowledge and perceptions of insurance of the Tanzanian adult population. On this basis, it conducts a segmentation exercise whereby the target market is grouped into distinct segments and the profile of each is explored.

The series was designed so that readers can focus on the Headline Findings document, drawing on specific input documents for the evidence base and as per their area of interest.

The full series is available at: www.fsdt.or.tz and www.finmark.org.za

The series has been submitted for review by the global Access to Insurance Initiative (www.access-to-insurance.org) and, upon acceptance and subject to further refinements, will also be published under the banner of the Access to Insurance Initiative.

INSURANCE INDUSTRY TRENDS: DOCUMENT 4 SYNOPSIS

The insurance industry was liberalised in the late 1990s, heralding an initial wave of entry. Between 2008 and 2010, the number of insurers rose from 18 to 27: 20 general insurers, 2 long-term, 4 composite insurers – due to split by the end of 2012 – and one reinsurer.

Key findings

- *Strong growth off low base.* Insurance premiums grew by 24% in 2010. Traditionally, the sector has been dominated by general insurance and the long-term (life) market only recently started to develop in earnest. Long-term premiums made up only 11% of total industry premiums in 2010, but its premium growth now outstrips that of general.
- *General insurance growth driven by health insurance; long-term growth driven by embedded group life insurance.* Health insurance premiums grew 54% in 2010. Group life premiums grew 92% in 2010 – due to an initial explosion of credit life embedded in loans, followed by a trend of embedding funeral insurance in deposit accounts.
- *Early signs that strong premium growth will slow.* There is a clear trend of increasing competition in the general insurance market, witnessed in new entry, declining market shares for the top five players, as well as increasing claims ratios and commissions. Challenges that could prevent further growth include:
    - The large number of small companies, which have higher expense ratios than large ones, negatively impacts client value and raises sustainability concerns.
    - Generally high expense ratios, as well as still largely paper-based systems and limited technological infrastructure and connectivity, imply that administrative efficiency is not yet sufficient to handle large volumes of clients.
    - A lack of insurance skills in the industry, ranging from underwriting to selling skills.

Conclusion

- The *s*lowing growth should create a competitive imperative for insurers to find new market niches and innovate. Yet few insurers have made this mind shift yet. They still have a largely high-value-low-volume focus. Reasons for not prioritising retail/mass market opportunities include distribution and premium collection challenges.
- To tap into new markets, companies need to:
    - reach scale in order to be sustainable and ensure they are able to provide reasonable value for money to clients;
    - implement automated and efficient administration systems;
    - overcome the technical and sales skills deficit; and
    - address solvency concerns to ensure that a company failure does not tarnish the image of the entire industry.

Unless these factors are addressed, there is a risk that microinsurance market growth may stall and even of consumer fall-out. Should they be addressed, it will facilitate a next wave of growth needed towards an inclusive insurance market in Tanzania.

1. Introduction

This document considers the supply of insurance in Tanzania. It provides a brief context to the formal insurance sector in Section 2.1, analyses recent trends in the insurance industry in terms of premium volumes and performance in Section 2.2 and examines challenges to future growth in Section 2.3. Informal providers of insurance are considered briefly in Section 3, with Section 4 concluding on the main drivers of the supply of insurance in Tanzania and the imperatives that this creates for market development.

2. The formal insurance sector

2.1. Industry context

Insurance industry nationalised for 30 years. The Tanzanian insurance industry was nationalised in 1967, with the National Insurance Corporation (NIC) and the Zanzibar Insurance Corporation (ZIC) being the only insurance companies permitted to transact insurance business. This status quo held until liberalisation of the insurance industry in 1996.

Liberalisation led to a strong foreign influence. A number of new insurance companies have entered the market since liberalisation. The majority of new entrants are general insurance companies, as shown in Table 1. The same table shows the significant foreign ownership of Tanzanian insurers, with only 5 of the 27 registered insurance licenses in 2010 being 100% locally owned.

	2006	**2007**	**2008**	**2009**	**2010**
Long term assurance	2	1	1	1	2
General insurance	10	12	12	18	20
Composite	4	4	4	4	4
Reinsurer	1	1	1	1	1
Total	17	18	18	24	27
100% locally owned	3	4	4	6	5

Table 1. Number of registered insurance licenses by type

Source: TIRA annual insurance market performance reports for 2006 to 2010.

2.2. Industry growth trends

Insurance penetration in Tanzania is very low. Measured as gross premiums (general insurance and long-term assurance premiums combined) expressed as a percentage of gross domestic product (GDP), insurance penetration is very low by global and African standards. Despite an increase in penetration from 0.62% in 2006 to 0.86% in 2010[1], penetration in Tanzania is still significantly lower than the 6.9% global average for 2010 and the 3.9% African average[2]. Even when measured against the neighbouring countries of Mozambique and Kenya and against Ghana, penetration is shown to be relatively low as illustrated in Figure 1. This level of penetration clearly shows the insurance industry is performing below its potential, with significant scope for future growth. It is also safe to conclude there are

[1] Tanzania Insurance Regulatory Authority (TIRA) annual insurance market performance reports for 2006 to 2010.
[2] Swiss Re Sigma report, no 2 of 2011.

significant barriers that have historically prevented the insurance industry from realising its full potential:

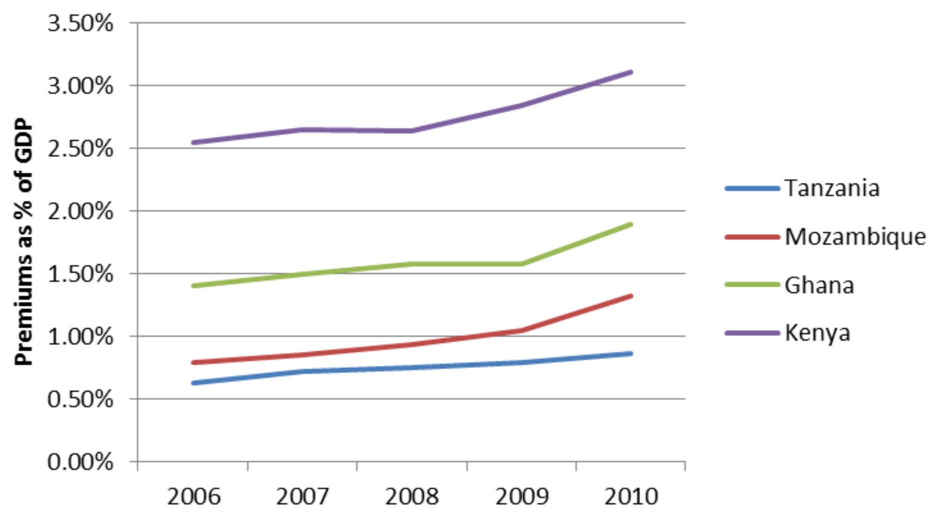

Figure 1. Insurance penetration as a percentage of GDP relative to other countries

Source: various.

Strong growth from both general insurance and long-term assurance. According to the TIRA annual insurance market performance reports for 2006 to 2010[3] (henceforth referred to as the TIRA data), the general insurance market has grown rapidly over recent years, with an average premium growth of 25% per annum between 2006 and 2010. This is markedly higher than the growth in the national nominal GDP of 16% and the finance and intermediation sector GDP of 18%[4] over the same period. The growth in long-term assurance premiums has been even more impressive at 33% per annum between 2006 and 2010, although it should be noted that this growth comes off a significantly lower base. Long-term assurance premiums made up only 11% of total industry premiums in 2010.

General insurance growth driven by health insurance. The strong growth of the general insurance market can be attributed to exceptional growth in the health insurance business class, with average premium growth of 36% between 2006 and 2010, reaching as high as 57% between 2009 and 2010[5]. The engineering business class has also shown strong growth with an average of 35% between 2006 and 2010, although its contribution to the total general insurance premium income was only 7% in 2010. Figure 2 shows the 2010 general insurance gross premiums split by class of business, dominated by motor insurance. It is interesting to note that 3rd party liability motor insurance is compulsory. However, industry consultations revealed that most of the motor insurance premiums are for comprehensive cover, indicating an appreciation for the value that insurance provides.

[3] Note: source for all statistics in this analysis, unless otherwise stated, is *TIRA annual insurance market performance reports for 2006 to 2010*.

[4] Bank of Tanzania Quarterly Economic Bulletin for the quarter ending December 2010.

[5] The premium growth between 2006 and 2010 includes premiums from the accident and other general business classes. Health only became a separate class for reporting purposes in 2009.

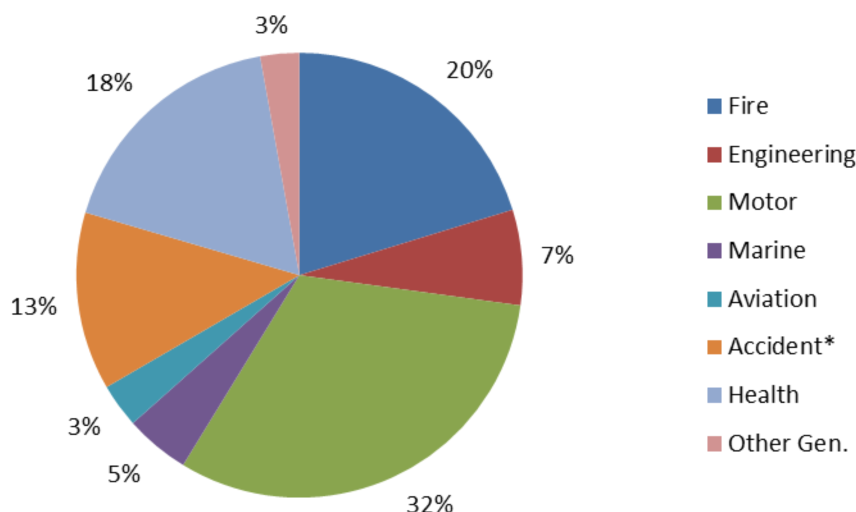

Figure 2. General insurance premiums written for 2010 split by class of business

Source: TIRA annual insurance market performance report for 2010

Long-term assurance growth driven by embedded products. The group life business class has grown at a phenomenal 92% between 2009 and 2010[6]. This exceptional growth has been due to an initial explosion of credit life offerings embedded in the loans provided by commercial banks as well as MFIs and SACCOs. This was subsequently followed by a trend of embedding funeral products in commercial banks' deposit accounts.

Box 1. Example: embedded funeral product

The National Microfinance Bank (NMB) has partnered with African Life to provide its clients with a funeral insurance product. The insurance cover is automatically attached to, or "embedded" in, all NMB's Personal Accounts, estimated to be more than one million in number. The product provides funeral cover of TZS600,000 ($386)[7] on the account holder's life as well as his / her spouse's life and is offered for free. However, an account must be active in order to qualify for cover. The cover is subject to a 3-month waiting period from the date on which the account is opened.

The product is effectively a loyalty programme with NMB expecting the benefits from providing the funeral cover at no additional cost to account holders to be outweighed by the benefit derived from increased loyalty in the form of more active accounts (an account must be active in order to qualify for the cover).

Source: industry consultations.

As the uptake figures in *Document 3* show, the embedding of insurance products in retail banking products has given insurers access to a significantly bigger market than was previously the case.

General insurance retention levels are low. As discussed in *Document 7*, the regulatory framework imposes some compulsory reinsurance cessions on all insurers. Actual cession levels significantly exceed the compulsory levels. General insurance retention levels have

[6] Data prior to 2009 is unfortunately not available.

[7] All instances of exchange rate conversion draw on the three-month average USD/TZS exchange rate up to 12 September 2011 obtained from www.oanda.com

consistently remained just below 50% from 2006 to 2010, as shown in Figure 3. A 50% retention level for general insurance is relatively low when compared against some other developing insurance markets elsewhere in Africa (72% for Mozambique, 71% for Ghana and 78% for Kenya). A possible reason for the relatively low retentions could be a lack of underwriting skills, which is explored further in Section 2.3. Long-term retention levels have reduced from 94% in 2006 to 87% in 2010, but are on par with the other African countries considered (90% for Mozambique, 98% for Ghana and 94% for Kenya)[8].

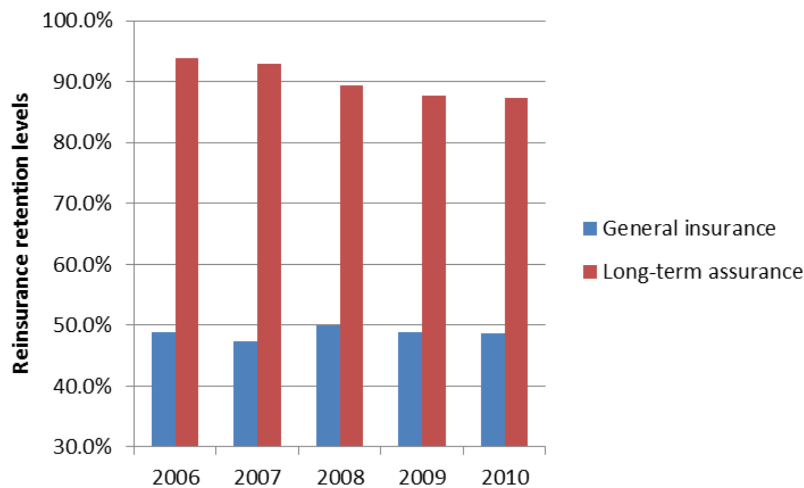

Figure 3. Reinsurance retention levels as a percentage of gross premiums written

Source: TIRA annual insurance market performance reports for 2006 to 2010

There are early signs that the strong premium growth will slow. If one looks beyond the very strong recent growth picture that has been painted above, there are indications from both hard data and industry consultation that this rate of growth is likely to slow in the near future, on a number of fronts:

- For the long-term assurance market, the exceptional growth in embedded products suggests there is fairly limited scope to grow premium income outside of the natural growth in credit and deposit accounts from commercial banks[9]. The growth in the number of commercial bank accounts is outside the control of the insurance companies, who would do well to start considering alternative growth markets.
- There is furthermore a clear trend of increasing competition in the general insurance market. TIRA data indicate that the number of general insurance licenses, excluding composite licenses, has doubled from 10 in 2006 to 20 in 2010, which will translate directly into increased competition in the traditional markets. The increasing competition is further evidenced by the steadily reducing market share of the top five insurers by premiums written. The decreasing market share of the top five insurance companies is clearly illustrated in Figure 4, which shows that each of the top five

[8] Insurance regulators' reports for 2010 (Ghana and Kenya) and 2009 (Mozambique).

[9] It is difficult to make a firm estimate of the proportion of bank accounts that already have an embedded insurance product. However, we are aware of approximately 1.7 million accounts (savings and loan accounts) that have an embedded product. Comparing this to the number of banked Tanzanians (15% of the adult population – see *Document 2* for more detail on the banked population) gives a penetration ratio that will, in practice, exceed 50%. The 1.7m accounts that include an embedded product will not include all such accounts and the definition of "banked" includes all formal banking products, not all of which are conducive for embedding an insurance product.

companies have lost market share with the market share of other companies (outside the top five in 2006 and new entrants) increasing from 18% in 2006 to 55% in 2010:

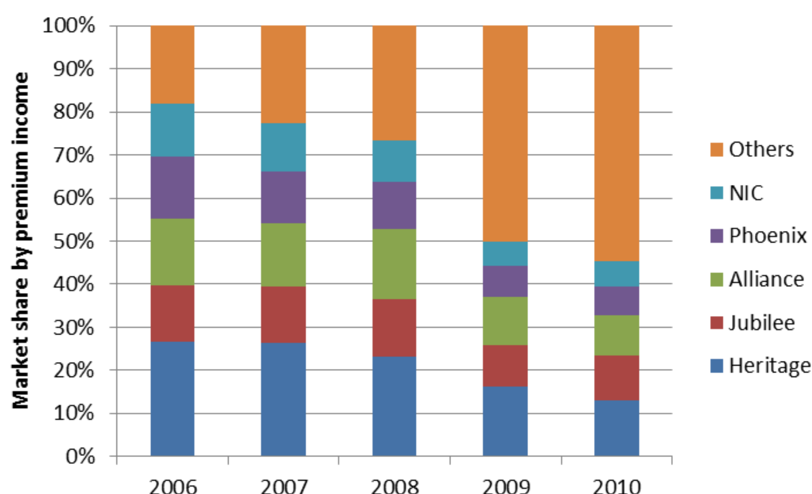

Figure 4. Market share of top five general insurers against the rest of the market

Source: TIRA annual insurance market performance reports for 2006 to 2010

- According to the TIRA data, general insurance loss ratios show a clear increasing trend from 50% in 2006 to 59% in 2010. This is in part caused by the increase in health insurance business which has higher than average loss ratios (77% in 2010 as opposed to 59% for the entire general insurance industry), but is also an indication that competition is increasing in traditional markets with premium rates being cut to ensure business is retained or won over from the incumbent underwriter.
- The data show a similar increasing trend in the ratio of commission paid to gross premiums written – from 6% in 2006 to 11% in 2010. This once again indicates there is increasing competition amongst insurers for access to the existing insurance markets, with insurers willing to pay higher levels of commission to retain existing business and win new business. This is particularly relevant in a market that is dominated by brokers, such as the Tanzanian market where in 2010 65% of general insurance premiums were intermediated by brokers.

The combination of current growth drivers nearly reaching the maximum potential market and clear indications of increasing commission in the traditional markets, particularly in the general insurance industry, can only mean that growth is likely to slow unless insurers start looking to new markets. This view is supported by the responses from a number of insurers interviewed, who indicated that their biggest future growth potential would come on the back of economic growth (i.e. from organic growth in the traditional markets). If insurers were to depend only on economic growth to grow their businesses, they would be constrained to a growth rate similar to that of the economy. Alternatively, if insurers were to actively seek out new markets, the industry could maintain and maybe even improve upon its strong recent growth rates, which exceed recent economic growth.

The expected slow-down in growth raises two questions: firstly, what are the potential catalysts for the next wave of growth, and secondly, what major challenges could possibly restrict future growth? Future growth opportunities are covered in *Document 5*, while potential challenges to growth are covered in Section 2.3.

2.3. Challenges that could prevent further growth

The fact that insurance penetration is very low implies there are significant barriers in the Tanzanian insurance industry that have historically restricted growth. Recent growth has been strong, showing that some of the barriers are being overcome. However, significant barriers still remain and are detailed in this section.

A large number of small companies. There has been rapid growth in the number of general insurance licenses from 10 in 2006 to 20 in 2010. This is a high number of licenses in what is still a very small market and naturally leads to a number of very small companies. The life assurance industry has significantly fewer licenses (5 in 2010 if composite licenses are included and if Alliance Life and Alliance, the composite license, are considered a single license) but is also a much smaller market (11% of the total insurance market by premium income in 2010), which results in a number of small companies.

Table 2 provides a comparison of the average size of insurance companies, indicated by gross premium income in US dollars per insurance license, in Tanzania against that for Mozambique, Kenya and Ghana[10]. The average Tanzanian (and Ghanaian) insurance company is significantly smaller than those in Mozambique and Kenya:

	Tanzania	Mozambique	Kenya	Ghana
Number of licenses	27	8	46	40
Gross premium income (USD million)	186	126	988	237
Average gross premium per license	6.9	15.8	21.5	5.9

Table 2. Coss country comparison of the average size of insurance companies

Source: Country insurance regulators' reports for 2010 and authors' calculations

The large number of small insurance companies gives rise to two concerns:

- *Sustainability*. The first concern is around the long-term viability of many companies, particularly the smaller ones. All insurance companies have an element of fixed overhead costs, the impact of which is more significant the smaller the company. If the smaller companies do not grow rapidly, they are likely to have difficulty covering future fixed overhead costs which will eventually put pressure on their solvency.
- *Client value for money*. The fixed overheads costs of small companies will also ultimately impact negatively on the ability of the smaller companies to offer value for money to their clients because of the lack of economies of scale. An analysis of the largest 15 general insurance companies (by premium income in 2010) shows a strong negative correlation between a company's market share and its expense ratio – the larger the company's market share, the lower its expense ratio. This means larger companies are generally in a better position to provide value for money products. The negative correlation between market share and expense ratios are shown in Figure 5:

[10] Kenya and Mozambique were selected for their relevance in East Africa, Kenya being a more developed market and Mozambique being an undeveloped market. Ghana was selected as one of the up and coming insurance industries in West Africa.

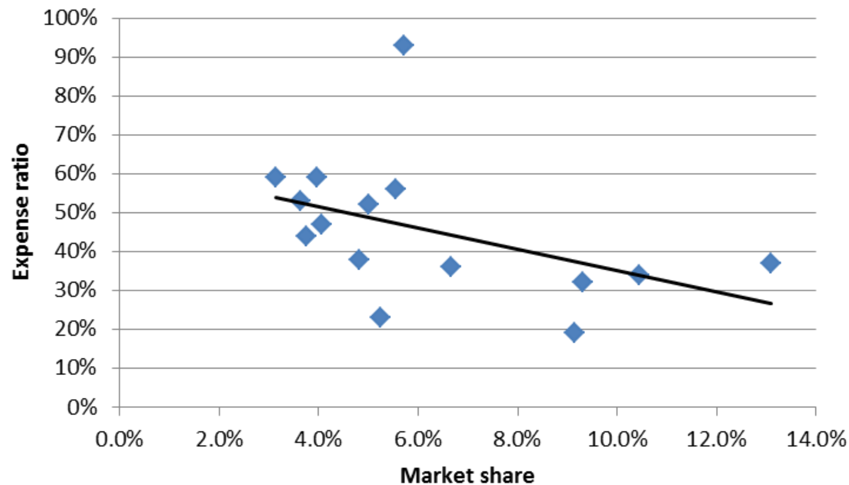

Figure 5. Correlation between size of insurer and expense ratio

Source: TIRA annual insurance market performance report for 2010 and authors' calculations

Administration systems not yet scalable. Industry interviews have revealed that a number of insurers have only recently begun moving away from manual, paper-based administrative processes to automated electronic administration systems. This is a critical transition that must be completed before the industry will be able to effectively gain scale in the retail market for a number of reasons:

- Manual processes are simply not efficient enough to enable administration of large volumes of business, particularly retail business, in a cost effective manner. The ability to administer high volumes at a low cost is essential when entering low income markets to ensure that products are affordable to the target market.
- The ability of insurers to provide adequate levels of service to clients is seriously compromised, resulting in disillusioned clients.

Manual processes depend upon significant human intervention and all people will make mistakes from time-to-time. This requires many manual checks and balances to be put into place. Besides introducing additional cost, manual process also lead to increased operational risks.

The issue of inefficient administration processes impacting clients service was highlighted in focus group discussions. The impact is even greater when the poor service relates to the claiming process. One focus group participant linked the unsuccessful claims to a poorly functioning filing system within insurance companies and made the following suggestion:

> "Also I think they evolve with the changing world. Let them keep their data in computers. This is no longer the age of using the physical filing system, that's why a lot of documents are lost, which in turn brings trouble to the customers when they come to stake their claims." (Group 2: voluntarily insured men, Dar es Salaam)

High expense ratios imply that the industry is not yet geared for the level of administrative efficiencies that will be required in the future. The general insurance industry has pleasingly

shown a reducing trend in its expense ratio (the ratio of management expenses plus net commissions paid to net earned premiums) from 49% in 2006 to 43% in 2010[11]. The management ratio (the ratio of management expenses to gross premiums written) for the long-term assurance industry was 28% in both 2009 and 2010[12]. These ratios should reduce as technology is used to increase administrative efficiencies.

Limited technological infrastructure also constrains the ability of insurers to reach minimum efficiency levels. For example, branch offices are often not yet connected in real-time to the company's head office, which significantly reduces the ability of the branches to provide an efficient service to clients. Consequently, it will be very difficult in the modern world for insurers to expand outside of Dar es Salaam without branch connectivity. In fact, industry consultations revealed that where insurers have branches outside of Dar es Salaam, they are restricted to the larger cities such as Arusha, Mbeya and Mwanza. The exception is the NIC which has the largest branch infrastructure (24 branches providing representation in all regions of Tanzania).

Signs that industry is constrained by a lack of skills. A number of insurance companies interviewed indicated that their ability to grow rapidly was seriously constrained by a dearth of skills that are critical to the insurance industry, ranging from underwriting skills to selling skills. This observation is supported by the fact that most of those companies that are driving growth in both the general insurance and the long-term assurance markets have strong foreign links and are therefore able to draw on international lessons and innovations. The areas where the lack of skills is most evident are:

- *Underwriting skills*. The lack of underwriting skills in particular could have a serious impact on the profitability of the insurance industry and ultimately on its sustainability. Tanzania Re raised this as a serious concern and indicated they have begun facilitating training session for their clients' underwriters with the training provided by foreign experts. Further reinforcing the lack of underwriting skills, one of the large international reinsurers withdrew from the Tanzanian market in 2010 citing the lack of local underwriting skills as the main reason, which had resulted in unsatisfactory market practices. The reinsurer indicated they would only consider returning once skills had improved. The low general insurance retentions relative to some of the other developing insurance markets in Africa lends further support to the lack of underwriting skills as insurers rather transfer risks to insurers instead of retaining poorly underwritten risks.

  As noted previously, there are indications that competition is increasing, which makes it even more important for the industry to address the lack of underwriting skills as more and more downward pressure will be placed on profit margins through the increased competition. Anecdotal evidence suggests that the lack of underwriting skills is already coming into play in the motor insurance class where some insurers are under-cutting rates in order to grow their premium income without regard to the level of risk being underwritten. However, there is not yet any industry-level evidence of under-cutting in TIRA's database (e.g. increasing claims ratios for motor insurance).

- *Selling skills* were also highlighted as lacking by a number of insurers that were interviewed. Besides constraining the industry's ability to grow premium income, it also increases the risk of miss-selling, particularly for voluntary products in lower income

[11] TIRA annual insurance market performance reports for 2006 to 2010.
[12] TIRA annual insurance market performance report for 2010.

markets whose consumers tend to be less financially aware. There are a number of education institutions that provide courses covering insurance related topics (e.g. the Institute of Finance and Management). However, the insurance industry seems to have a common opinion that the standard of education provided by local institutions needs to be significantly improved to provide graduates with the standards of knowledge it requires. A number of insurers interviewed indicated they need to provide internal training to graduates before they become productive. It is therefore critical that local education institutions improve the quality of insurance courses provided.

On the other hand, insurers themselves must take a large portion of the responsibility to ensure their sales people are sufficiently skilled (the same goes for all employees). However, where insurers are taking it upon themselves and investing substantial sums of money to provide the necessary in-house training, the newly trained employees are recruited by another insurer, leaving the insurer with the training cost burden. This problem is exacerbated by the scarce skills environment.

- *Reinsurance innovation*. Related to the lack of skills in the Tanzanian industry is the role that Tanzania Re plays in the market as the only locally registered reinsurance company. Reinsurance companies are in the unique position of being exposed to the entire insurance industry and can therefore identify industry trends before insurance companies. This places reinsurers in the ideal position to be leading innovators in an industry. However, Tanzania Re does not play such a role mainly due to a lack of skills and in fact does not lead on any reinsurance treaties. Thus the Tanzanian industry is not benefitting from the catalytic role that a fully skilled reinsurance company could play.
- *Expatriate staff quotas*. During the consultations, insurers claimed the limit placed on the number of expatriate staff that a foreign company is allowed to appoint[13] was a significant constraint given the dearth of technical skills in the country, as well as the perceived poor quality of recent graduates. However, the limit of five expatriates is adequate to fill key leadership and managerial positions and should therefore not have a significant negative impact on the industry's growth potential. Furthermore, expatriate staff is generally very expensive. One of the insurers interviewed pointed out that many of the companies that are involved in the perceived rate undercutting in the motor insurance industry actually employ expatriates. If this were the case, it would appear that expatriates skills are not a guarantee to proper risk management and underwriting.

Insurance industry appears profitable, *but some solvency concerns*. The net income ratio (see Box 2 below for more detail on the net income ratio) is a measure of how viable or profitable the insurance industry is. Figure 6 shows that the ratio for 2010 is within the acceptable range of 0% to 10% for both the general insurance and long-term assurance industries, despite the reduction from 2009[14].

[13] The Tanzania Investment Act of 1997, Section 24.-(1) states that: "Every business enterprise granted a certificate of incentives under this Act, shall be entitled to an initial automatic immigrant quota of up to five persons during the start-up period. These requirements would apply to all foreign investors. (2) Subject to subsection (1), any application for an extra person within an immigrant quota shall be submitted to the Centre which shall, in consultation with the Immigration Department, authorise any additional person which it shall deem necessary taking into consideration the availability of qualified Tanzanians, complexity of the technology employed by the business enterprise and agreements reached with the investors."

[14] TIRA data is not in the format that allows for calculation of the net income ratio prior to 2009.

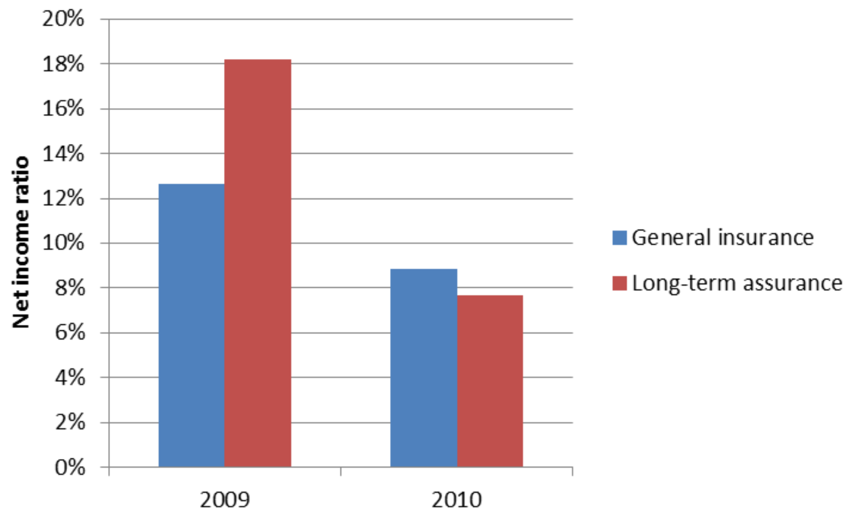

Figure 6. Net income ratios for general insurance and long-term assurance industries

Source: TIRA annual insurance market performance report for 2010

However, the solvency position for both the general insurance and long-term assurance industries appears weak. Figure 7 shows that the general insurance solvency ratio (see Box 2 for more detail on the solvency ratio) has increased from significantly below 100% in 2009 to 105% in 2010, while that for the long-term assurance industry has reduced to just below 100%. The solvency ratio indicates the financial strength of the industry and, as a general rule, should be 120% or higher. A solvency ratio of less than 100% indicates insolvency.

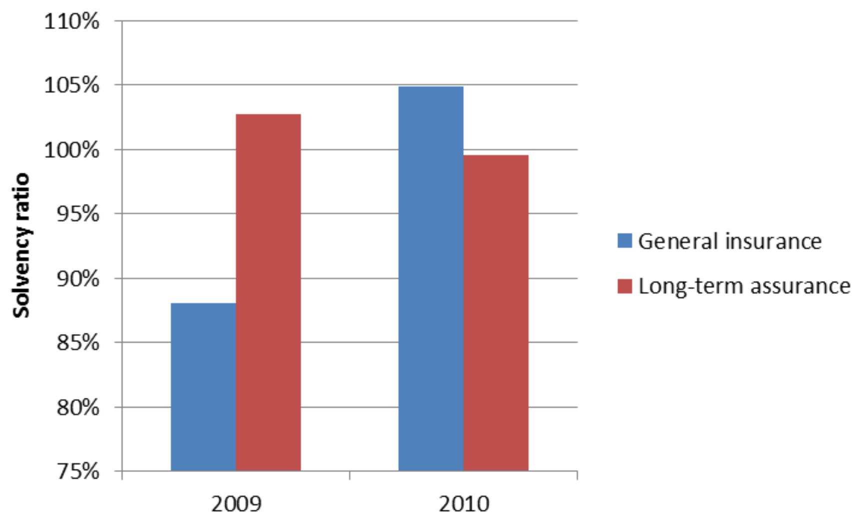

Figure 7. Solvency ratios for general insurance and long-term assurance industries

Source: TIRA annual insurance market performance report for 2010

The above solvency ratios have been calculated to exclude receivables (e.g. premiums due from brokers and reinsurance claims due), but includes all accrued liabilities (e.g. reinsurance premiums not yet paid) as per the definition provided in Box 2. The TIRA data indicate that receivables make up a substantial proportion of total assets, particularly for general insurance (30% in 2009 and 22% in 2010). If receivables are included, the solvency ratios for 2010 increase to 154% for the general insurance industry and 115% for the long-

term assurance industry. Thus, industry solvency is very dependent upon the ability of insurers to collect their short-term receivables, such as outstanding premiums.

Box 2. Explanation of net income and solvency ratios[15]

Performance indicators, in the form of key ratios, are a very useful and important tool to assess the performance of a microinsurance programme. This box provides an explanation of the two ratios that have been discussed above. However, there are a number of additional performance indicators that should be analysed when considering the performance of microinsurance. Additional information on the performance indicators can be found in the Performance Indicators for Microinsurance Handbook (2nd edition), available at: www.microfact.org.

The net income ratio is defined as the net income for a period divided by earned premium in the same period. The period can be a fiscal year or any other accounting period. It is calculated as:

Net income ratio = Net income / Earned premium

The net income ratio measures how viable or profitable a programme is and is probably the most important indicator since it reflects a summary of all activities in the period reviewed.

The **solvency ratio** is defined as the ratio of admitted assets to liabilities and is calculated as:

Solvency ratio =Admitted assets / Liabilities

The overall solvency ratio indicates the financial strength of the microinsurance programme (or company) and its ability to pay its obligations now and in the future. The microinsurer must ensure that the solvency ratio is adequate - as a general rule, the level of the solvency ratio should be 120% or higher. Insurers with higher risk products and smaller insurers should aim for a much higher solvency ratio.

Insolvencies could destroy trust in the industry. The sustainability concerns raised by a large number of small players, as well as the solvency situation in the industry at large, raise concerns that an insurer may fail. Should this happen, it will have serious repercussions on consumer trust in insurance. The position of the NIC is cause for special concern:

Since liberalisation, the NIC has lost substantial market share through increased competition, resulting in a substantially weakened financial position. Following failed attempts to sell the NIC, the government started a programme to restructure the company with some initial signs of success. However, the NIC continues to be plagued by historic claims that have not yet been settled. This history of unsettled claims has had a large negative impact on trust in NIC's ability to pay valid claims. The following focus group quote would suggest that the NIC's claims track record has in some cases not only led to distrust in the NIC, but also in the insurance industry in general:

> "Well, when I started working in those years back I was a member of national insurance. But this insurance collapsed and they never paid me a cent, so from that day I haven't been very good friends with insurance […]." (Group 12: compulsory insured men, urban Kilimanjaro – Moshi)

It is noted that NIC's failure to settle claims was partly a result of low levels of liquidity, as the company had invested heavily in real estate properties. Recently, the company obtained the necessary approval from the government (its sole shareholder) to dispose some of its real estate properties in order to realise funds that are required to settle outstanding claims.

[15] Source: Performance Indicators for Microinsurance, A Handbook for Microinsurance Practitioners (end Edition).

Trust in NIC is now beginning to return as the company begins settling the outstanding claims.

However, the poor financial position of the NIC places the returning trust in jeopardy. The NIC's general insurance business has shown a combined ratio of 118% for 2010 compared to the industry wide combined ratio of 102%. The combined ratio consists of a 25% loss ratio (industry wide loss ratio: 59%) and an expense ratio of 93% (industry wide expense ratio: 43%). This position is clearly not sustainable, considering that as outstanding claims are settled the loss ratio will increase to a level that is closer to the industry average.

The financial position of the NIC's long-term assurance business is equally weak. The NIC's solvency ratio, calculated as the ratio of investment assets to insurance liabilities, was 104% in 2010, indicating a marginally solvent position. The comparative solvency ratio for the rest of the long-term assurance industry was 218% - a substantially stronger solvency position. Similarly, the NIC's ratio of capital to insurance liabilities, which is an indication of a company's ability to withstand adverse shock events, is significantly lower than the rest of the long-term assurance industry (17% for the NIC versus 87% for the rest of the industry). Add to these low ratios the fact that a substantial proportion of the NIC's investment assets are invested in fixed property (68% of investment assets) and that the NIC has not undergone an actuarial valuation for the last five years (implying the insurance liabilities are probably undervalued), then it is clear the NIC is in a poor financial position. This highlights the importance of the on-going restructuring programme to return the NIC to a financially sound footing, as well as for an actuarial valuation of the life book to be performed to establish its true financial position.

Poor claims service can also undermine trust. To ensure that clients value insurance, efficient and effective claims payments are very important. The focus group discussions revealed a number of positive word of mouth experiences relating to successful claims, which emphasises the benefits to the insurance industry of a positive claims experience. However, there are also negative experiences. People emphasised the need to be persistent to receive their claim payment, with documentation requirements being one of the biggest problems faced. They often need money to pay for costs such as a medical certificate, to obtain the services of a lawyer or simply for travel costs to follow up. Low-income clients simply cannot afford to spend much money to ensure a claim is paid.

3. The informal sector

Informal insurance provision likely to be limited. The nature of informality implies that we will never be able to measure it fully. Industry consultations suggest that there are some organisations carrying risk in-house in the form of informal risk pooling schemes (i.e. risk pools that are not underwritten by a registered underwriter):

- *SACCO and MFI sector*: Little evidence was encountered during the interviews of informal insurance schemes amongst SACCOs and MFIs. Examples of such informal schemes are: (1) the Savings and Credit Cooperatives Union League of Tanzania (SCCULT) which runs an in-house scheme to cover the risk against borrower default due to death. According to information provided by SCCULT, this scheme currently covers 39,489 members; and (2) Fanikiwa, an MFI with a portfolio of 3,000 loan clients which are

covered for death via an in-house scheme at a premium of 1% of the loan value. The focus group discussions also did not reveal much informal insurance provision by MFIs.

Rather than running in-house insurance schemes, many MFIs and SACCOs are underwritten by formal insurance companies. African Life, Alliance Life and Jubilee all indicated that they underwrite credit life products for MFIs and SACCOs. It is quite possible, as one of the interviewed MFIs suggested, that insurance companies generally underwrite the MFIs that have large client bases, leaving the smaller MFIs to run informal insurance schemes.

- *Benefit and friendly societies*: the Insurance Act of 2009 exempts benefit and friendly societies from insurance regulation as long as they serve members only and provide only death and disability benefits that do not exceed TZS 10 million (about $6,430). See *Document 7* for more details. The focus groups revealed only very limited burial society activity among the formally employed, who tend to have more expensive funerals.
- *In-house funeral cover by funeral service providers*: it is a common phenomenon in a number of countries for funeral undertakers to provide in-house insurance schemes to clients without underwriting by a registered insurer. The consultations did not flag this as prevalent in Tanzania (indeed, the funeral undertaker industry itself is small compared to some other sub-Saharan African countries). The focus group discussions confirmed that informal insurance schemes run by funeral parlours are non-existent. Low-income people are generally not concerned about funeral expenses as they obtain contributions from the community to fund funerals.
- *ROSCAs*[16] *(called Kibati)*: These informal schemes can be used as implicit risk management tools in that a member can request fellow members for contributions, request a loan or call on their savings if an unexpected risk event occurs. However, focus group discussions revealed that Kibati are not seen as very trustworthy. Generally, people feel that their incomes are too low and irregular to make this type of rotating savings association work. They also do not pool risk in a similar way to that of an insurance mechanism.
- *Community-based health insurance funds*: these funds (of which there are private and state-administered varieties) have an agreement with health service providers to provide services to members, usually on a capitation[17] basis, but are not underwritten by insurers. These funds are discussed in more detail in *Document 6.*

Thus, although there is some evidence of informal insurance provision, there is fairly limited informal activity besides community-based health insurance funds. FinScope 2009 estimated that approximately 400,000 lives belong to informal insurance pools, which is substantially lower than the estimated formal uptake discussed in *Document 3* and unlikely to have grown as rapidly since 2009 as formal insurance.

4. Conclusions

Low insurance penetration, but strong growth. Insurance penetration is low, even by African standards. However, the insurance industry is growing rapidly, with premium growth

[16] Rotating Savings and Credit Association is a group of individuals who agree to meet for a defined period in order to save and borrow together.

[17] A health financing arrangement whereby service providers are paid a specified monthly or annual sum based on the number of clients in the area that may use their services, rather than actual services rendered. There is therefore no reimbursement of actual costs.

outstripping GDP growth, albeit off a low base. The growth is driven mostly by health insurance on the general insurance side and group life insurance on the long-term assurance side, particularly embedded credit life and funeral products.

Signs that rapid growth will slow creates imperative to search for new markets. The analysis provided substantial evidence that the current rapid premium growth is likely to slow. In order for insurers to maintain the strong premium growth, they will need to move beyond the current traditional corporate markets and look for new markets in the retail space. This will require a move down market where there is clearly a large uninsured market given the current low level of insurance penetration highlighted in *Document 3*. Those insurers that are best able to identify high growth market segments, develop appropriate products and distribution channels to meet the needs of those market segments and provide efficiently client servicing, while applying good risk management, will become the market leaders.

Some industry challenges must be overcome. There are a number of challenges that will need to be overcome by insurers that attempt to tap into new markets:

- Companies need to reach scale in order to be sustainable and ensure they are able to provide reasonable value for money to clients. There are currently too many sub-scale insurers.
- Administration systems need to become automated and more efficient to deliver cost effective administration of high policy volumes.
- The technical and sales skills deficit must be addressed by improving the standard of insurance education provided by formal educational institutions and by appropriate in-house training.
- Solvency concerns must be addressed to ensure that a company failure does not tarnish the image of the entire industry.

Formal industry to increase insurance access. Informal provision of insurance is fairly limited and there is no reason to think this will change soon. The onus therefore lies with the formal insurance industry to increase access to insurance for the uninsured. Current market dynamics are likely to force insurers in this direction.