International Microinsurance trends and regulation

Presentation to industry stakeholders, Maputo 17 Sep 2010
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About FinMark Trust and Cenfri

- Independent trust established in 2002
- Initial funding from the UK’s Department for International Development (DFID)
- Facilitating and catalysing the next generation of development around access to financial services.
- Theme areas:
  - FinScope
  - Housing finance
  - Credit
  - Consumer financial empowerment
  - Rural and agricultural finance
  - Retail payment systems
  - Insurance
- Further information available at: www.FinMarkTrust.org.za
Finscope 2009
Key insights

• Finscope measures access to and usage of both formal (including insurance) and informal financial services.
• By virtue of this definition, the study also explores other topics related to this measurement including source of income, financial literacy usage of formal versus informal financial services etc
• This data is freely available (Central Bank)
• For more information please go to www.finscope.co.za
Finscope 2009
Key findings

- 9% of the population earns a wage or salary – some stable form of income
- Furthermore:

<table>
<thead>
<tr>
<th>Income brackets</th>
<th>% of adults</th>
<th>US Dollars per day</th>
</tr>
</thead>
<tbody>
<tr>
<td>menos de 5.000,00mt</td>
<td>42.06</td>
<td>0 to 37 cents per day</td>
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<tr>
<td>entre 5.001,00 e 25.000,00 mt</td>
<td>23.87</td>
<td>37 cents to $1.84 per day</td>
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<td>entre 25.001,00 mt e 50.000,00 mt</td>
<td>5.9</td>
<td>$1.84 to $3.68 per day</td>
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<td>entre 50.001,00 mt e 100.000,00 mt</td>
<td>1.78</td>
<td>$3.68 to $7.40 per day</td>
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<td>entre 100.001,00 mt e 200.000,00 mt</td>
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<td>$7.40 to $14.80 per day</td>
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<td>$14.80 to $22.22 per day</td>
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<tr>
<td>entre 300.001,00 mt e 500.000,00 mt</td>
<td>0.19</td>
<td>$22.22 to $37 per day</td>
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- 13% have access to the formal financial sector (**12% banked**, 1% other)
- **Savings**: 5% formal, 6% at home, 10% informal and 80% not saving
- 10% of respondents make use of informal financial services
- **Informal financial services**: 5.7% xitique, 1.3% funeral association, informal family grouping sharing a conta da familia 0.8%
- Usage of informal financial services indicative of people managing their money
5.90% of respondents have funeral cover
63% of respondents mentioned they did not have funeral cover because they did not know they could have it or were unaware of funeral cover – only 20% indicated they had no cover because they couldn’t afford it

INSURANCE
2.3% of respondents have insurance – mostly employer based or subsidised for example, employer subsidised insurance, employer
Top three: employer covered funeral insurance, employer covered accident insurance and employer subsidised medical aid.
The picture may look bleak, but potentially there are opportunities
Why regulate MI?

- **Policy objectives**
  - Stability
    - Sufficient prudential management
  - Consumer protection
    - Formalisation & enforcement
    - Intermediation regulation
  - Consumer education
  - Market development, financial inclusion
    - Creating regulatory space for outreach and formalisation
- **Changing mindset**
  - Emerging conceptual framework to understand the market
  - Microinsurance is not microbusiness – understanding the bottom line & getting to grips with innovation & implications for regulation
  - New regulatory approaches will be required
Some international MI trends

- Credit life (conditional)
- Funeral insurance (voluntary)
- Personal accident (voluntary)
- Little asset (extended warranties, cell phone, household content and structure)
- Short-term/renewable (monthly/annually)
- Often credit-led (banks, MFIs and payroll lenders)
- Mutuals/coops play a role
- Active sales required
- Large informal markets
What is MI?

- IAIS definition: insurance for low-income market
- Regulatory definition necessary?
  - Common understanding
    - Appropriate and realistic income target
    - Distinguish social welfare from insurance
  - Target subsidy
  - Define quotas
  - Carve out regulatory space
- Practical definitions:
  - Income levels (e.g. 3 min wages in Brazil – not in regulation)
  - Premium caps (e.g. $25 pm in Philippines)
  - Benefit caps (e.g. $7k in SA, $5k Mexico)
Understanding the market: MI target

Potential MI target market?

- Consider policy objectives: MMW vs poverty relief
- Define MI within limits of commercial viability
- Very low insurance penetration: Insurance sector development
Understanding the market: the insurance decision

What will make low-income people buy insurance?

Perceived value
- Discount rate, tangible and “in life” benefits
- Probability: underestimate risk
- Trust: Likelihood of successful claim
- Perceptions – awareness and financial education, active sales, demonstration

Perceived opportunity cost
- Less disposable income means higher opportunity cost
- Product design: cost and frequency of premiums, product-demand match

- Encourage innovation to address these issues
- Facilitate active sales
- Build trust
- Encourage product simplification
Understanding the market: The bottom line

- Minimise costs
- Ensure value
- Flexible cost structure

<table>
<thead>
<tr>
<th></th>
<th>Traditional insurance</th>
<th>Microinsurance</th>
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<tbody>
<tr>
<td>Surplus</td>
<td>$50</td>
<td>$2.5</td>
</tr>
<tr>
<td>Net claims</td>
<td>$35</td>
<td>$2.25</td>
</tr>
<tr>
<td>Mgmt expenses</td>
<td>$7.5</td>
<td>$2.25</td>
</tr>
<tr>
<td>Sales</td>
<td>$2.5</td>
<td>$1</td>
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- Low premiums require scale and very efficient administration
- Different distribution of costs
- Sales expenses may be proportionally higher than traditional
- Profit margins will be thin and regulatory costs will have big impact on viability
- Claims ratios will be lower: Need to ensure that value is paid to clients in the form of claims
Customer value: Brazilian example

- Increasing client coverage, premium growth
- But decreasing value to consumer: claims ratios dropping and/or very low
- Sales expenses increasing and very high on credit life and extended warranties (bundled products)
Innovation across the MI value chain

Typology of MI models

- Retailer-based
  - Bill payments / Airtime
    - Mapfre Casas Bahia (Brazil)
    - Seguros Azteca (Mexico)
    - Colseguros Carrefour (Colombia)
      - Hollard Take it Eezi (SA)
      - Cover2Go Wiredloop (SA)
    - Safari Bima (Kenya)
      - Cover2Go cell phone accidental death (SA)
      - Philam/ AKSIText (Philippines)
  - Cell phone
    - Bima ya Jamii (Kenya)
    - Sanlam Sky ZCC (SA)
    - Hollard Kaizer Chiefs (SA)
  - Affinity group
    - Mapfre CODENSA (Colombia)
      - AON QBE (Brazil)
      - SINAF (Brazil)
      - Sanlam Sky (SA)
      - Clientele (SA)
  - Database/utility
    - Traditional agents
Your new agency force?
Cross-cutting intermediation themes

**Need to rethink nature of intermediation**
- Spread across several entities not traditionally regulated by insurance supervisor (impact of other regulation)
- Definitions of brokers and agents vs direct sales vs outsourcing (avoidance of intermediation)
- Importance of face-to-face active sales (e.g. telesales experience)
- Structure and level of remuneration, sharing in revenue

**Aggregators lead interaction and incentivised to act in clients interest**
- Brand Trust and reputational risk
- Control price increases and ensure claims payment (e.g. Pep)
- Research to develop better products (e.g. CODENSA, Pep)
- Yet insurance regulation tends to be biased towards insurers and traditional intermediaries

**Group underwriting and contractual relationships**
- Underwrite on group basis even though may be individually sold
- Open voluntary groups, master policies

**Technology important facilitator but is not always cheap**
- Communication (Pep), data (Take it Eezi), payments (Safari Bima): not always lower cost
- Claims management (Jet/Hollard claims runner)

**Product innovation**
- Casas Bahia: Life (food hamper) + personal accident + income replacement + medical discounts + lottery
- CODENSA and Jet: Household structure and content (rental market, technology enabled claims management, sum assured)
- CIC: Public health insurance + PA + funeral
Drivers of regulatory design

**Market realities**
- Low overall insurance penetration and income levels: sector development
- Product-specific dynamics (Compulsory credit life, funeral, etc)
- Types of providers (e.g. mutuals) and value chain
- Limited infrastructure
- Credit-led BUT new channels opening up
- Bottom line and value proposition

**Regulatory objectives**
- Balancing stability and development
- Challenge of protecting and including the poor: Trigger take-up of appropriate products
- Improve value proposition: Large part of MI still offers limited value to the poor
- Facilitating outreach and formalisation
- Dealing with informality
- **Regulatory capacity and resources**

**Regulatory design**
- Tailor to domestic environment
- Regulatory approach: Encourage, facilitate, coerce
- MI definition
- Tiered space required and appropriate?
- Degree of consumer protection and market conduct?
- Coordination/collaboration with other regulators
- Enforcement and recourse
Country examples

Mexico
Colombia
Peru
Brazil
South Africa
Kenya
India
Philippines
Ghana
Uganda
Zambia
Cambodia
Egypt
Mongolia
China
Venezuela
Bolivia
Brazil
Kenya
Zambia
South Africa

Country examples map.
Country examples

Colombia

- Market led development possible due to low overall regulatory burden
- Support from financial policies in banking sector: “Opportunity banking programme”
- Liberalisation and foreign entry as driver to go down-market
- Mutuals play a big role but are regulated in same way as formal insurers
- Regulatory loopholes have allowed Funeral parlours to offer in-kind benefits outside of regulatory framework
Country examples

- Liberalisation as key driver of development
- MI regulation in place since 2002
- Constrained regulatory capacity
- Focuses only on intermediation but cuts out key intermediaries
- Rural and social quotas have catalysed some interest but have generally not been successful
- Government plays direct role to establish MI programmes
- Dominance of endowment products despite poor value
Country examples

- Initial regulatory attempts to develop MI product failed: not in line with demand and not commercially viable
- Collective effort by industry and government to develop MI market
- 30-40m MI policies (half informal)
- Drivers of sales: active sales, “in-life benefits” and lottery
- MI target market defined as < 3 min wages (85% of population)
- High level MI Bill in process
- Conceptual definition of MI and allow for product parameters (policy term, benefit caps, claims payment deadline, simple documentation, underwriting)
- Create option of dedicated microinsurer
- Creates microinsurance broker and correspondent
- Proposes tax exemption
Country examples

- Significant economic and infrastructure constraints: large informal market
- Limited financial sector penetration overall. Banks and payroll lending lead.
- Mostly compulsory credit life with some experiments
- Limited retail experience: Recent introduction of agent distribution
- FSDP: well-developed inclusion policy
- Regulatory barriers undermine bancassurance
- Paper-based administration: Insurance value proposition still limited by high admin ratios, low claims ratios
- Domestic strategy process to develop MI
Country examples

- High traditional insurance penetration
- Advanced financial sector and payment system (banking sector penetration)
- Large informal and unregulated component of low-income funeral insurance market
- Charter incentivises innovation
- Consumer protection focus: Impact of market conduct regulation on inclusion
- Proposed new regulatory framework for MI
Proposed new SA MI regulatory framework

Market realities
- Concerns over abuse
- Large informal market
- Formal funeral insurance
- Compulsory credit life
- Innovation
- Strict market conduct reg

Objectives:
- Facilitate inclusion
- Facilitate entry and innovation
- Deal with the informal market
- Protect consumers & ensure value proposition
- Move beyond funeral

Implications for regulation:
- Specific MI definition
- Minimise regulatory costs – especially on intermediation
- Create space for 2nd tier of insurers and intermediaries
- Set product & other parameters to ensure value & protection (create space for non-funeral)
Proposed new SA MI regulatory framework

1. Limit risk through definition
2. Create space for underwriters
3. Create space for intermediaries
4. Enforcement and recourse
Guidelines to consider

**Guideline 1:** Take active steps to develop a microinsurance market

**Guideline 2:** Adopt a policy on microinsurance as part of the broader goal of financial inclusion

**Guideline 3:** Define a microinsurance product category

**Guideline 4:** Tailor regulation to the risk character of microinsurance

**Guideline 5:** Allow microinsurance underwriting by multiple entities

**Guideline 6:** Provide a path for formalisation

**Guideline 7:** Create a flexible regime for the distribution of microinsurance

**Guideline 8:** Facilitate the active selling of microinsurance

**Guideline 9:** Monitor market developments and respond

**Guideline 10:** Utilise market capacity to support supervision in low-risk areas
Thank you

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Sources