

Technical Assistance for the Promotion of Microinsurance

The Experience of Opportunity International

CGAP Working Group on Microinsurance
Good and Bad Practices
Case Study No. 11

Richard Leftley – June 2005

Good and Bad Practices in Microinsurance

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1. A **series of case studies** to identify good and bad practices in microinsurance
2. A **synthesis document** of good and bad practices in microinsurance for practitioners based on an analysis of the case studies. The major lessons from the case studies will also be published in a series of **two-page briefing notes** for easy access by practitioners.
3. **Donor guidelines** for funding microinsurance.

The CGAP Working Group on Microinsurance

The CGAP Microinsurance Working Group includes donors, insurers and other interested parties. The Working Group coordinates donor activities as they pertain to the development and proliferation of insurance services to low-income households in developing countries. The main activities of the working group include:

1. Developing donor guidelines for supporting microinsurance
2. Document case studies of insurance products and delivery models
3. Commission research on key issues such as the regulatory environment for microinsurance
4. Supporting innovations that will expand the availability of appropriate microinsurance products
5. Publishing a quarterly newsletter on microinsurance
6. Managing the content of the Microinsurance Focus website:
www.microfinancegateway.org/section/resourcecenters/microinsurance

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Acronyms

| | |
|---------|--|
| ABC | Activity-based costing |
| AIDS | Acquired Immunodeficiency Syndrome |
| AIG | American International Group |
| AIMS | Automated insurance management system |
| APPEND | Association of Philippine Partners in Enterprise Development |
| ASKI | Alalay Sa Kaunlaran Sa Gitnang Luzon Inc. |
| AUSAID | Australian Agency for International Development |
| CETZAM | Christian Enterprise Trust of Zambia |
| CGAP | Consultative Group to Assist the Poorest |
| DFID | Department for International Development |
| DIF | Death insurance fund |
| FAQ | Frequently asked questions |
| FFI | Formal financial institution |
| GTZ | German Technical Assistance |
| HIV | Human Immunodeficiency Virus |
| ID | Identity |
| ILO | International Labour Organization |
| KMBI | Kabalitkat Para Sa Maunlad Na Buhay Inc. |
| MAF | Mutual aid fund |
| MBA | Mutual benefit association |
| MFI | Microfinance institution |
| MIS | Management information systems |
| MRI | Mortgage redemption insurance |
| MZM | Mozambique Meticais |
| NASFAM | National Association of Farmers (Malawi) |
| NGO | Non-governmental organisation |
| NICO | National Insurance Company |
| NSO | Network Service Organisation |
| OI | Opportunity International |
| OIBM | Opportunity International Bank Malawi |
| OM | Oportunidad Microfinanzas |
| OMB | Opportunity Microfinance Bank |
| OTI | Opportunity Transformational Investments |
| PA | Programme assistant |
| PAR | Portfolio at risk |
| PCC | Protected cell company |
| PDA | Personal digital assistant |
| PHP | Philippine Peso |
| Sida | Swedish International Development Cooperation Agency |
| SMEs | Small and medium enterprises |
| TA | Technical assistance |
| TSKI | Taytay Sa Kauswagan, Inc. |
| TSPI | Tulay Sa Pag-unlad Inc. |
| UGAFODE | Ugandan Agency for Economic Development |
| UK | United Kingdom |
| US | United States |
| USAID | United States Agency for International Development |
| Ush | Uganda Shillings |
| ZMK | Zambian Kwacha |

Executive Summary

The Opportunity International (OI) network of 39 microfinance institutions (MFIs) served over 675,000 low-income persons at the end of 2004. Wherever possible, OI's microfinance partners strive to become (or start as) regulated financial institutions so that they can provide a range of financial services to large volumes of customers. The members of the OI network strive to achieve a triple bottom line of client outreach, financial sustainability and client transformation.

The provision of microinsurance is an important component in this 3-pronged objective. Insurance can benefit large numbers of people since clients and their family members can be covered. Furthermore, when offering insurance in partnership with an insurance company, microinsurance is not capital intensive, so growth is not limited by the ability to mobilise loan capital. These partnerships also facilitate the second objective of financial sustainability, as insurance lowers loan losses while generating fee-based income for the MFI. Thirdly, insurance helps to transform clients by providing peace of mind and assistance when they need it most.

To promote microinsurance, OI has hired in-house insurance expertise that provides demand-driven technical assistance to its implementing partners. OI's insurance team implements a six-step product development process intended to produce the best insurance products for the lowest rates, usually in partnership with insurance companies. Instead of relying on insurers to manufacture the product, this process restructures the relationships in the partner-agent model by empowering the MFIs to design their own products and effectively negotiate with the insurance companies.

This paper draws largely from the experiences of five MFIs that have introduced insurance with OI's technical assistance. Each one has a different story and unique lessons, reinforcing the advantages of Opportunity's product development approach to promoting microinsurance. The organisations are:

1. **UGAFODE:** This OI partner in Uganda could not wait for the technical assistance and went ahead and partnered with AIG Uganda like most other MFIs in the country, only to realise later that AIG's product really did not meet the needs of its clients.
2. **CETZAM:** One of the microinsurance pioneers in the OI network, this Zambian organisation has experience offering different products on behalf of different insurance companies. To get its funeral insurance right, CETZAM and its insurance partner NICO have made a number of changes over the years that provide useful lessons for others.
3. **OIBM:** While the experience in Malawi is still quite new, the case of OIBM illustrates the diversity of potential insurance products that could be considered if the delivery channel is a bank instead of an NGO.
4. **TSKI:** The experience in the Philippines demonstrates the process of transitioning from an informal to a formal insurance arrangement. OI has a number of very large partners in the Philippines, and these volumes were quite attractive to potential insurance partners.

5. **Oportunidad Microfinanzas:** This new organisation in Mexico highlights some of the challenges of attracting insurance partners when the MFI does not yet have large volumes of customers, especially when operating in a conservative insurance market where one is unfamiliar with the local insurance etiquette. But perseverance pays off.

Drawing primarily on the experiences of these MFIs, this paper highlights a number of valuable microinsurance lessons in the areas of market research and marketing, product design, claims management, structuring partnerships and providing technical assistance.

Market Research and Marketing

- The first step in designing an insurance product has to be **understanding the demand** from customers or the potential target market. OI relies on a combination of quantitative and qualitative research to understand clients' needs, preferences, and their familiarity with insurance. Market research results are also an important tool to use when negotiating with insurance companies
- When assessing demand, **gather critical information** about the types of products, key product features, the clients' ability to pay, and their service standard expectations.
- When introducing an insurance product, the **marketing plan should target both clients and staff**. If field staff do not buy into the product, they will not be able (or willing) to persuade clients to buy it either.
- **To convince sceptics to buy insurance:** 1) make sure that premiums are affordable; 2) rely on the persuasive power of the group; and 3) let doubters see the results.

Product Design

- **The simpler the better.** If a product cannot be easily explained to clients in a few sentences, it probably will not succeed. But designing a simple insurance product is harder to do than one might expect, especially when partnering with an insurance company. To do so, one must:
 - Cover fewer eventualities more completely, instead of many risks partially.
 - Avoid loading policies with lots of riders and benefits that are difficult to claim.
 - Minimise the number of exclusions.
 - Avoid contestability clauses so that pre-existing conditions can be covered.
 - Negotiate with insurers so that clients do not have to answer medical questions.
 - Have one price for all ages (as long as the sums assured are small).
- **All MFIs should have credit life insurance.**
- **Credit life should cover the disbursed loan amount** (perhaps including interest as well), not the outstanding balance. After clearing off the debt, OI's partners keep any surplus (the difference between the disbursed amount and the outstanding balance) and use it to fund trainings and prevention activities.
- Negotiate **automatic extensions for credit life** insurance, so that if the borrower does not finish repaying during the loan term, insurance coverage is still in effect.
- It is better to **link term life insurance with savings** rather than credit so that clients can have coverage even when they do not have a loan.
- To offer term insurance on behalf of an insurer, an **MFI should become a licensed agent** (whereas for credit life, the MFI can just buy as a group policy).
- Ideally, **most microinsurance products should be voluntary**, but that will be difficult until credit and insurance are de-linked.

Claims Management

- Again, **the simpler the better**. It is easier to verify claims if the product is straightforward.
- **Make it easy for clients to make claims**. Be generous with claims reporting deadlines by allowing claimants to have time to collect the necessary information. If possible, convince insurers to accept verified copies of required documents.
- If at all possible, **the MFI should administer the claims itself**, ideally at the branch level, by paying out claims from collected premiums, and then passing on the net amount (along with claims documentation) to the insurer at the end of the month. To implement this amended agency agreement, MFIs have to have decent information systems, good internal controls, and staff need to know how to verify claims properly.

Structuring Partnerships

- The **partner-agent model is the usually the simplest, cheapest and quickest** way for an MFI to start offering insurance.
- To make the partner-agent model work better, an **MFI should take the initiative** to design the insurance product(s) that it wants, and then solicit price quotes from insurers. This approach requires a change of thinking in the original partner-agent model where insurers were primarily responsible for “product manufacturing.”
- If the objective is to extend microinsurance to as many low-income households as possible, then it is necessary to **consider other delivery structures besides MFIs**.

Providing Technical Assistance

- To reorient the partner-agent model so that MFIs assume greater “product manufacturing” responsibilities, the MFIs have to have sufficient expertise. Since individual organisations could probably not justify the cost of an insurance expert on their payroll, **MFIs need to access appropriate technical assistance** so that they can level the playing field with the insurance companies. By sharing the cost of two experts over 15 MFIs, the Opportunity network has made access to expertise much more economical.
- OI firmly believes that **TA must be demand-driven**. If its MFI partners are going to be committed to and have ownership over new products or policies, they must decide what they want and pay for it themselves (or take the lead in finding funding). Within OI, the experience thus far is that the demand for its insurance expertise far outstrips the supply.
- For microinsurance, the regulatory conditions and the demand vary significantly from country to country. A **standard approach to product development** provides products that are sustainable and meet the needs of clients.
- By working in many countries on the same topic, a centralised **TA facility can promote innovations**—including product design, institutional options and the use of technology—that otherwise would not likely emerge, at least not as quickly.
- To make microinsurance cost-effective, **MFIs need an insurance-specific information system**. Another advantage of a technical assistance relationship is that it pools the costs of software development among many MFIs. Opportunity’s Automated Insurance Management System (AIMS) software greatly reduces transactional costs, human errors and the possibilities for fraud, which in turn boost income and reduce the price that clients have to pay for insurance.

1. Introducing Opportunity International

Opportunity International (OI) was founded in 1971 by Al Whittaker, the former President of Bristol-Meyers International Corporation, and David Bussau, an Australian entrepreneur, as an ecumenical Christian development organisation. Over the years, Opportunity has created 39 microfinance institutions (MFIs) in 27 countries in Africa, Asia, Europe, Latin America and the Middle East. At the end of 2004, these institutions served over 675,000 low-income persons, providing a range of financial services designed to help the poor work their way out poverty.

Opportunity's core business has three related components: 1) to establish new, nationwide, poverty-focused microfinance institutions in underserved developing countries; 2) to transform its existing partners that are non-governmental organisations (NGO) into regulated formal financial institutions (FFIs) whenever feasible and desirable; and 3) to scale-up Opportunity NGOs in countries where transformation to a regulated institution is not an appropriate strategy.

To reach its target of one million clients by 2007 with a full range of micro-business products and services, Opportunity has helped convert eight of its partner NGOs to formal financial institutions, and will convert an additional three within the next two years. Central to Opportunity's conversion and growth strategy is its commitment to creating FFIs with a triple bottom line of client outreach, financial sustainability and client transformation.

At the end of 2004, the OI network provided 87% of its \$130 million loan portfolio to poor women. The average loan size was \$239, with first loans averaging \$176. Overall, the network had an operational sustainability ratio of 108% and its portfolio at risk (PAR) at 30 days was 3.9%; key indicators by region are summarised in Table 1. Fifteen partners were financially sustainable and twenty-two of the 39 partners are operationally sustainable. At the end of 2004, the largest six partners (in terms of clients) were:

- TSKI (Philippines) with over 123,000 borrowers
- TSPI (Philippines) with over 115,000 borrowers
- KMBI (Philippines) with over 80,000 borrowers
- Sinapi Aba (Ghana) with over 53,000 borrowers
- ASODENIC (Nicaragua) with over 32,000 borrowers
- OMB Bank (Philippines) with over 27,000 borrowers

Table 1. Basic Performance Indicators of OI Partners by Region (12-2004)

| Region (no. of MFIs) | No. of active borrowers | Outstanding loan portfolio | Average first loan | PAR 30 days | Operational Sustainability |
|----------------------|-------------------------|----------------------------|--------------------|-------------|----------------------------|
| Africa (6) | 87,750 | \$9,187,698 | \$128 | 4.3% | 82.5% |
| Asia (17) | 478,805 | \$27,886,068 | \$74 | 3.1% | 107.0% |
| Eastern Europe (9) | 40,336 | \$82,800,076 | \$1,676 | 3.2% | 125.6% |
| Latin America (7) | 68,687 | \$10,180,601 | \$145 | 11.9% | 94.1% |

During the last four years, through Opportunity's capital sourcing organisations in the US, UK, Canada, Australia and Germany, the organisation has raised \$51 million from the private sector and \$54 million from bi-lateral and multi-lateral donors. Opportunity has substantial experience in implementing successful large-scale projects funded by USAID, AUSAID, DFID, and by private institutional donors such as Nike, Norwest Capital, Citicorp, Union Transport, the Ford Foundation, the Charles Stewart Mott Foundation, and Chase Manhattan.

1.1 The Structure of Opportunity International

The Opportunity Network is comprised of three major elements. Firstly, the "Support Partners" are individuals and organisations that primarily raise capital from major bilateral aid organisations, private donors and social investment funds in the form of debt, equity and grants. The second element is the "Implementing Partners," which are the microfinance institutions located in developing countries. The implementing partners are a combination of NGOs, finance companies and licensed banks with varying degrees of Opportunity ownership. The "Network Services Organisation" (NSO) is the final element. The NSO provides demand-driven consultancy, training and technical assistance to Opportunity's Implementing Partners in core areas of strategic planning, management information systems (MIS), product development and organisational development.

For investments of debt and equity made by Opportunity International into its partner networks, an investment company called Opportunity Transformational Investments (OTI) has been established. There are also plans to launch a "Guarantee Fund" that will help partners to access local currency loans when they do not have collateral to secure the debt.

For the first thirty years, OI's implementing partners were established as NGOs with local boards and management teams. The network functioned as a loose federation of organisations with a shared mission and vision, but no centralised management. Since 2000, the focus has been on the creation of "national scale, transformational, formal financial organisations," which has resulted in the creation of banks and regulated financial organisations in which OI can hold a controlling equity stake and employ its chosen management team.

These organisations have taken different structures, including fully licensed banks, rural banks, thrift banks, microfinance banks and regulated finance companies depending upon local legislation. These new structures have allowed OI's partners to offer deposit products for the first time. The promotion of FFIs also allows OI to access a wider range of social debt and equity providers to fuel its significant growth.

The Network Services Organisation has provided technical assistance to these "ownership" partners to assist in their conversion from NGOs to regulated organisations. In some cases, where an OI partner does not already exist in the country, the organisation has been established from day-one as a bank.

1.2 Opportunity International and Microinsurance

In 2001, client surveys from partners in Africa, but specifically Zambia, demonstrated an increasing demand for access to insurance from existing borrowers. This finding prompted OI to submit a proposal to DFID to develop insurance in Zambia and Malawi, which would require insurance expertise within the Network Services to deliver. In January 2002, Richard Leftley joined Opportunity from a career in reinsurance brokering with London-based Benfield Greig Limited with a remit to develop insurance products for clients in Zambia. It was soon realised by OI that there was significant demand from clients located throughout Africa, and so in 2002 technical assistance was provided in Malawi and Ghana, followed by work in Zimbabwe and Uganda in 2003. During the course of 2003, demand for insurance was identified outside of Africa, with work being conducted in India, Albania, Mexico and the Philippines.

Work also started in 2003 on the development of insurance software to reduce administration, fraud and error associated with the manual production of premium schedules and claims. The new software had to work in conjunction with the eMerge banking software used by most OI partners, and as a result a decision was taken to develop the “Automated Insurance Management System” (AIMS) in-house.

In January 2004, OI’s insurance capabilities were bolstered when Shadreck Mapfumo joined as manager for Africa. Having just finished his masters in actuarial science, and with over a decade of reinsurance underwriting experience in Southern Africa, Mapfumo’s skills opened up new possibilities for insurance within OI.

As highlighted in Table 2, Opportunity International’s Network Services has worked (and continues to work) with a number of partners on the development of insurance products. At the end of 2004, OI’s partners had nearly 700,000 active policies under management, some of which also provided coverage for family dependants.

1.3 Why is Microinsurance Important to OI?

The primary reason for Opportunity instigating its work in insurance was client demand in Africa. Market research conducted with clients served by OI partners in Africa revealed that on average 40 percent of clients can expect a death in the family within the course of a year. Furthermore, these funerals are costly, equating to approximately three months of disposable income. This combination of the cost and frequency of the funerals first motivated Opportunity to provide insurance services to its clients in Africa.

However, the “triple-bottom-line” objectives of client outreach, financial sustainability and transformation are central to the workings of Opportunity International. The development of microinsurance clearly fits within these objectives:

Table 2. Insurance Activities in the Opportunity Network

| OI Partner & Location | Products Developed | Policy Count (Q4 2004) |
|--|---|------------------------|
| Opportunity International Bank Malawi (OIBM) | <ul style="list-style-type: none"> ➤ Credit life ➤ Combined savings / life insurance product due for release in 2005. | 1,700 |
| UGAFODE, Uganda | <ul style="list-style-type: none"> ➤ Combined credit life, personal accident and property catastrophe product | 10,959 |
| CETZAM, Zambia | <ul style="list-style-type: none"> ➤ Credit life ➤ Property insurance ➤ Term life insurance | 4,674 468 4,674 |
| TSKI, TSPI, OMB, ASKI, DSPI, HSFPI & RSPI, The Philippines | <ul style="list-style-type: none"> ➤ Credit life ➤ Term life insurance | 327,931 327,931 |
| Oportunidad Microfinanzas, Mexico | <ul style="list-style-type: none"> ➤ Credit life | 513 |
| The Bridge Foundation, India | <ul style="list-style-type: none"> ➤ Endowment life | Unknown |
| PsHM, Albania | <ul style="list-style-type: none"> ➤ Considering packaged life and property product for launch in 2006 | |
| Opportunity Bank, Montenegro | <ul style="list-style-type: none"> ➤ Considering new credit life, property and term life products in 2005 | |
| Opportunity Bank, Serbia | <ul style="list-style-type: none"> ➤ Considering new credit life, property and term life products. | |
| Sinapi Aba Savings & Loan, Ghana | <ul style="list-style-type: none"> ➤ Developing credit life and funeral insurance for release in 2005. | |
| Zambuko Trust, Zimbabwe | <ul style="list-style-type: none"> ➤ Developing credit life and funeral insurance for release in 2005. | |
| Banco Oportunidade, Mozambique | <ul style="list-style-type: none"> ➤ Developing credit life and term life products in 2005. | |

- **Client outreach:** The number of clients and their family dependants that can be reached is very significant because insurance is not capital intensive. To reach a large number of clients with loans, the MFI needs access to significant capital; this is not the case with insurance when acting as an agent on behalf of an insurance company.
- **Financial sustainability:** By working as a registered agent on behalf of an insurance company, a commission can be earned on every policy sold. This commission can be calculated to ensure that it covers the administrative expense of collecting premiums and verifying claims. The insurance products are therefore financially sustainable and in some instances can return an operating profit to the MFI. These insurance products can also reduce the organisation's credit risk, either directly (e.g., credit life) or indirectly by helping borrowers to cope when they experience a crisis.
- **Transformational impact:** Insurance helps to transform the client in a number of ways. Firstly, the client is empowered because she can purchase a product that she wants but could not previously access (in many cases). Secondly, insurance provides peace of mind. For example, it replaces the uncertainty associated with the cost of a funeral with the certainty of a regular, fixed payment. Many low-income households complain that they have to use their savings and working capital to pay for a funeral; in some cases funeral costs even bankrupt the business. Helping remove this burden from families is

transformational. Finally, to process claims, field staff interact with a grieving family; in these interactions, staff can offer moral and spiritual support to the bereaved.

Opportunity International is committed to providing the poor with access to a range of financial products. Traditionally this has been limited to microcredit, but increasingly OI is able to offer deposit and insurance products to the clients that it serves with loans as well as the wider low-income market.

1.4 Insurance and the Role of Network Services

Opportunity's Network Services provides technical assistance to implementing partners in many areas, including product development and product management. At the start of 2002, OI retained the services of Richard Leftley, and later Shadreck Mapfumo, to help implementing partners to develop microinsurance products. This technical assistance is provided on a demand-driven basis; the implementing partners are free to choose OI's assistance or the services of external consultants. In nearly all cases the partners have opted to utilise the network's technical assistance, although in a few cases, especially where funding has not been forthcoming, partners have developed insurance products without assistance.

Typically, once an implementing partner has decided to investigate the possibility of introducing insurance, funding is sought from the support partners as part of the annual budgeting process and a project plan is drawn up by Network Services. In most cases, the project plan will include the following major steps:

- 1. Market research:** A quantitative market research questionnaire is developed with input from the implementing partner. The purpose of this questionnaire is to ascertain client biometrics, family income, family size and composition, current insurance knowledge, competitor analysis, capacity to pay premiums at different levels, required sum insured, risks to be covered and reasons for not buying insurance. This questionnaire is then conducted by loan officers with a sample of the clients; the results are coded and analysed by Network Services prior to the first site visit.
- 2. First site visit:** During the first visit to the partner, meetings are held with management to discuss which products might be applicable in the broadest terms. Focus groups are held with existing and potential clients to build a better understanding of the demand for insurance. Information garnered from the focus groups is used in conjunction with the questionnaire results to build a picture of key product features that are needed, especially in relation to service standards (e.g., the speed that claims need to be paid). During the site visit, meetings are held with local insurance companies to establish a working relationship and ascertain indicative rates for different classes of insurance. Meetings are also held with the insurance regulators to clarify the requirements for becoming a registered insurance agent.
- 3. Prototype design:** Based upon the client needs' analysis, the potential pricing gathered from insurers and the regulatory positioning, a prototype product is designed and presented to the implementing partner along with recommendations relating to operations and product distribution (e.g., how best to sell the product, collect premiums and pay claims). The MFI's management and board then discuss these proposals; if they are accepted then the project proceeds.

- 4. Product pricing:** Following a decision to proceed, a detailed proposal is sent to a limited number of local insurance companies. The proposal sets out the product and all the features that are required, and requests a written quotation from the insurance company. Often the product that is requested is not an existing product in the market and so the insurer needs to decide if it wishes to offer such a product; the insurers' actuaries often work with Mapfumo (who is a trained actuary) to price the product. While the insurance companies are pricing the product, Network Services works with the MFI to calculate the cost of administering the product. A work flow is developed based on how the product is expected to be used, from which an activity-based costing (ABC) exercise is carried out. By calculating the cost of administering the product, the implementing partner can determine the rate of commission required to cover costs. These two elements—the net rate required by the insurer and the MFI's administrative costs—are combined to determine the cost of the product to the client. The work flow and product pricing are presented to the MFI's management and board for a final "Go / No Go" decision.
- 5. Product build phase:** Using the work flows, an operations manual is developed along with product specifications for the MIS department. If the partner has the AIMS insurance software, then this is configured to take into account the specific product features. In those cases where the partner does not have the ability to use AIMS, spreadsheets are developed to assist the finance department to calculate the premiums due and report to the insurance company. During this phase, an agreement is signed between the implementing partner and the insurance company, and the implementing partner is registered as an insurance agent. Clients and staff are made aware that a new product is about to be launched. A marketing plan is devised and implemented.
- 6. Staff training and pilot test:** Loan officers, supervisors, branch accountants, branch managers, branch MIS, and heads of department are provided with a one-day training covering the basics of insurance, answers to frequently asked questions (FAQs), and specifics of how the new product will perform. A pilot test (between 6 to 12 months), normally using one or two branches, is initiated to ensure that the product works as envisaged and is received well by clients. Lessons from the pilot test are used to refine the product accordingly before it is launched across the organisation.

The Opportunity Network does not have standardised insurance products that it implements in different locations. Rather, it utilises a product development process as set out in the six points above. The output of the process is a unique product (or products) that fits the needs of clients, the MFI, local insurers and of course complies with local regulations. By utilising a standard process, the quality and consistency of OI's insurance products can be assured.

This paper uses the experiences of Opportunity International and its implementing partners to illustrate critical lessons about the design and delivery of microinsurance, while highlighting the importance of technical assistance. The next section of this paper introduces five OI partners that have had different microinsurance experiences. Section 3 considers the issues related to client demand, including market research, client education and marketing strategies. Product design issues for credit life, term life and, to a limited extent, property insurance are covered in Section 4. The fifth section reviews issues around claims management and Section 6 explores a range of institutional structures that could be used to deliver microinsurance. This paper concludes with some final thoughts on the role of technical assistance in promoting microinsurance.

2. Microinsurance Practitioners

This section describes the experiences of five OI partners that have introduced insurance with technical assistance from Network Services. Each one has a different story and unique lessons, reinforcing the advantages of Opportunity's product development approach to promoting microinsurance. The organisations are:

- UGAFODE in Uganda
- CETZAM in Zambia
- Opportunity International Microfinance Bank in Malawi
- TSKI in the Philippines
- Oportunidad Microfinanzas in Mexico

2.1 UGAFODE, Uganda

The Uganda Agency for Development (UGAFODE) was founded in 1994 by Opportunity International to help poor Ugandans create self-employment and generate income by providing microcredit and training in ways that will transform lives. This company limited by guarantee operates in ten districts of Uganda.

By serving more than 22,000 clients over the last five years, UGAFODE has played a significant role in fighting poverty through employment creation and income generation. At the end of 2004, UGAFODE had 10,959 active borrowers with an outstanding portfolio \$1.4 million. UGAFODE is 85.5% operationally sustainable (83% financially sustainable) and has a portfolio at risk (30 days) of 7.9%. Over 64% of UGAFODE's loans are made to women. Its small average loan size of US\$255 confirms UGAFODE's commitment to reaching the most vulnerable populations.

During the course of 2003, Opportunity International conducted a survey that revealed strong demand for insurance in Uganda. In fact, 28% of UGAFODE's clients wanted access to funeral insurance and 26% wanted access to other insurance products. This demand is perhaps not surprising considering that 23% of UGAFODE's clients have experienced a death in their family in the last year (8% experienced one death, 6% two deaths and 9% three or more deaths). Focus groups held with groups of clients in 2003 suggested that the average cost of a funeral in Kampala is approximately Ush 1,000,000 (US\$550). The client survey showed that 64% of families in Uganda reported a weekly income for the family of less than \$50. The average funeral was costing the equivalent of almost three months of income for many families; for some, the cost of funerals will be equivalent to half a year's income.

The management of UGAFODE decided in 2003 that insurance had to be made available to clients based upon the evident client demand. At that time, however, OI was unable to offer technical assistance in the development of a product in Uganda because its financial and human resources were already allocated to other projects. As a result, UGAFODE decided to

provide clients with access to the personal accident policy offered by American International Group (AIG) to Ugandan microfinance organisations since 1996.¹

The AIG personal accident policy provides a range of coverage including credit life, property losses arising from catastrophes, permanent disability and death arising from an accident. AIG is registered locally as a non-life insurance company and as a result is not licensed to sell life insurance. The non-life licence does permit the sale of the personal accident policy, which forms the basis of the product providing the following benefits to UGAFODE clients:

- **Credit life and permanent disability insurance:** If the client dies or is permanently disabled, UGAFODE receives a payout equal to the outstanding balance of the loan.
- **Funeral benefit:** This benefit only applies if the client or family members die from an accident (i.e., not from a natural cause). The benefit amount is Ush 1,200,000 (\$666) for the client, Ush 600,000 (\$333) for the client's spouse, and Ush 300,000 (\$166) for each of four family members.
- **Property:** In the event of a catastrophe that destroys a client's business (e.g., flood or fire that affects a whole market), then UGAFODE receives a payout equal to the outstanding balance of the loan.

This insurance product is compulsory for all UGAFODE borrowers; the cost is 1% of the loan principal paid in advance of the loan disbursement. AIG currently does not pay any commissions to UGAFODE to cover the costs of administering this product, and as a result it is financially unsustainable.²

During a review of the product, including focus group discussions with UGAFODE's clients, the following issues were identified with the existing product:

1. The clients were surprised that they could not claim if the death occurred as a result of natural causes. This misunderstanding stems from the use of the word "accident," which has a specific technical meaning in insurance that has not been communicated to clients. One woman stated: "If my husband dies from a heart attack – that is an accident!" When clients found out that the product only covered accidental deaths, they demanded a change in the terms to include death from all causes.
2. Clients and staff were unclear about the property elements of the coverage—most loan officers do not refer to this element because they do not understand it themselves. When it was explained to clients, they found it difficult to understand what a catastrophe was. One client explained that, as far as she was concerned, "A fire that destroys my market stall and no one else's is a catastrophe for me and the insurance should pay."
3. It was surprising that the clients were largely unaware of the coverage for permanent disability, but again this was probably because the loan officers did not understand

¹ For more details about AIG's microinsurance policy, which is currently covering more than 1.6 million lives through 26 MFIs in three countries, see McCord et al (2005), "AIG Uganda," CGAP Working Group on Microinsurance Good and Bad Practices Case Study No. 9. Geneva: International Labour Organization.

² Some of AIG's microfinance partners in Uganda charge their clients a higher premium than the MFIs pay to AIG and retain the difference to cover administrative costs. UGAFODE does not load its premium in this way.

how to define “permanently disabled”. When asked about disability, clients seemed to be unconcerned about this element of the product and several asked whether it would be possible to trade the disability cover for full life insurance.

These insights into clients’ understanding of the personal accident product highlight the need for client and staff training. Initially, when UGAFODE launched the product, AIG agreed to provide training to loan officers. However, this was at most an hour long overview of the product, not in-depth technical training on the basics of insurance. Certainly there was no opportunity to develop techniques to answer the difficult questions that clients regularly ask. AIG provided no training to the clients themselves, and since it does not pay a commission to the MFI, UGAFODE does not have the financial resources to train its clients on insurance.

AIG’s product is relatively complex, with multiple coverages combined into a single package. This complexity means that it is essential that loan officers fully understand the product and its exclusions. When the loan officers are unsure about a product, they tend to shy away from explaining it to the clients less their lack of knowledge is exposed. Consequently, the clients do not understand the product and are inevitably disappointed when a claim is declined or the product fails to perform as they expect.

This product also demonstrates the danger of using technical terminology, such as “accident” when dealing with low-income households. It would seem a better approach to have a simpler product that covered fewer eventualities more fully, rather than many eventualities only partially. In focus groups with UGAFODE clients, there was strong evidence that clients wanted access to credit life and funeral coverage for death arising from any cause. To maintain the price at the same level, clients were willing to forgo the property and disability elements of the current product. On this basis, OI and UGAFODE have approached AIG and other local insurance providers to see if a workable solution can be found.

2.2 Christian Enterprise Trust Zambia (CETZAM)

CETZAM is a non-governmental organisation founded in 1995 by a group of Zambian business leaders committed to fighting poverty through microenterprise development. In 1996, Opportunity and CETZAM formed a partnership with the aim of CETZAM becoming a sustainable, formal, regulated financial institution providing microfinance to the economically disadvantaged of Zambia.

In 1997, CETZAM received a grant for £ 2,290,000 from DFID for the establishment of the Northern Zambia Micro Enterprise Development Project. At the end of 2004, CETZAM had 4,674 active borrowers with an outstanding loan portfolio of \$552,255, an average loan size of \$180 and operational sustainability of 35.4%. Its PAR (30 days) was 5.4%. At the end of 2002 and into 2003, CETZAM’s portfolio and management underwent a significant change; branches were closed and the portfolio was realigned, which meant that client numbers reduced from a high of over 20,000 active borrowers to around 3,000 by the end of 2003. CETZAM is a classic case of an MFI that outgrew its capacity and suffered the consequences. Yet despite these difficulties, CETZAM has been one of OI’s microinsurance pioneers, learning valuable lessons along the way.

Funeral Insurance

During 2000, CETZAM conducted research into the needs of its borrowers and discovered a strong demand for access to life insurance mainly driven by the increasing cost and frequency of funerals. The management of CETZAM approached NICO Insurance Company in Lusaka and the “Ntula” funeral insurance product (see Table 3) was pilot tested in Kitwe, Northern Zambia in the fourth quarter of 2000.

Initially, Ntula was provided via a local insurance agent, but in May 2002 CETZAM registered as an agent on behalf of NICO and now receives a 20% commission on the premiums. In addition, following the slow payment of some early claims, an agreement was reached to amend the agency agreement to allow CETZAM to settle claims on behalf of NICO and to submit premiums net of claims paid at the end of each calendar month. This facilitated the payment of claims within two weeks of the death being reported. The Ntula product—which means “to carry someone’s burden”—was expanded to all 20,000 clients throughout Zambia during the summer of 2002.

Table 3. Product Details for Ntula by NICO Insurance

| Product Feature | Comments |
|------------------------|---|
| Premium | Fixed ZMK 1,125 (\$0.25) per week of the loan, irrespective of the age of the borrower. Premium deducted from disbursed loan. |
| Coverage | Death arising from any cause, including HIV, for client plus an additional five family members chosen by the client during the loan application. |
| Claim value | Fixed at ZMK 500,000 (\$108) for an adult and ZMK 250,000 (\$54) for a child. A child is less than 14 years old. |
| Period | Insurance active from date of loan disbursement until expected date of maturity (normally 16 weeks for group loans) plus an additional two weeks of “free cover” after the loan has matured to cover the loan application process for a subsequent loan. |
| Exclusions | <ol style="list-style-type: none"> 1. If the claim is not reported within 14 days of the death. 2. If the deceased was not a listed family member on the application 3. If the client (or the client’s group) is more than 14 days in arrears with its loan repayments the insurance is invalidated until the arrears are cleared. |

In September 2002, market research was conducted with CETZAM clients to gauge their reaction to the new Ntula product. The research demonstrated that 81% of CETZAM’s clients thought that Ntula helped them in a time of stress and helped to protect their businesses. The research also highlighted the reason for the demand for insurance: 41% of clients reported a death in their family over the previous year. Interestingly, 15% of CETZAM’s clients were opposed to the introduction of Ntula and nearly all of these were located in Livingstone, a town in southern Zambia.

CETZAM’s head office and the majority of its 20,000 clients were based in the northern towns of the Copperbelt. It was common for clients to travel between these towns. As a common language was spoken, clients in other northern towns heard about the Ntula pilot that was being conducted in Kitwe via the community radio stations. By the time that Ntula

was rolled out to the other Copperbelt towns, clients were already asking their loan officers for the product and as a result, its introduction was enthusiastically received.

By contrast, Livingstone in the south was a day's drive from Kitwe with a different local dialect and culture. The clients and staff in Livingstone had not been informed about Ntula and so its introduction was met with resistance and suspicion. It was later revealed that at the time of Ntula's introduction, two factors conspired to convince local clients that it was a bad product. Firstly, problems with the loan tracking MIS had meant that loan disbursements were being delayed, which led clients to become concerned about CETZAM's financial health. The introduction of the insurance product, which was compulsory and involved a deduction from the loan amount, struck clients as being a desperate measure to ensure the survival of the organisation. They did not consider that Ntula would ever pay any claims, and rather saw it was a levy on the loan to keep CETZAM running. Secondly, at the time of its introduction, a local newspaper was exposing incidents of "black magic" in the town. Clients linked Ntula, a product covering the death of the client plus five family members (six people in all), as being somehow demonic. It took several weeks of street theatre by a local organisation to change public perception of Ntula in Livingstone.

In July 2004, Opportunity International conducted a review of the Ntula operations to reduce administration costs and ensure that clients' needs were being met. The main findings of the review were as follows:

1. **Compulsory or voluntary:** Focus group discussions revealed that clients would prefer that the product remained compulsory for borrowers. The "trust bank" groups use a mutual guarantee and if one member of the group is unable to pay, then the other group members are responsible for the loan repayment. Clients felt that a death in the family of a group member would result in difficulty in repaying the loan, whereas Ntula helped ensure that group members continued to service their loans.
2. **Confusion over "next of kin":** The focus groups revealed confusion among clients about whether the next of kin was covered under Ntula. This resulted in re-training of the loan officers to ensure that the next of kin was also listed as an insured family member on the application form.
3. **Increase in the number of dependants:** Feedback from clients revealed that Ntula should cover six (rather than five) family members besides the client. Negotiations with NICO on this point proved fruitful and an agreement was reached to increase the number of family members covered for the same premium.
4. **De-link Ntula from loan arrears:** The link between the Ntula product and loan repayment is unpopular with clients because it is possible for an individual to be on-time, but the group to be delinquent. In these circumstances, in the event of a family member dying, the claim would be declined. In addition, it is usual for a client that falls sick to have difficulty repaying the loan; in the event that the sick client then dies, no claim is paid. In this situation, the person that needs Ntula the most is actually excluded from its benefits. It has been a recommendation for some time that Ntula and the loan repayment be de-linked. If this recommendation is followed, however, NICO's loss ratio will worsen, placing pressure on the product's pricing.

5. **“Free cover” between loans:** While the two weeks of free cover at the end of each loan cycle is popular with clients and loan officers, it is proving difficult to administer. It is easy to determine whether someone has an active loan, but at the branch level it is hard to calculate whether the death occurred during a two week period at the end of the loan. CETZAM also faces a potential difficulty when it installs an MIS to reduce the cost of administering Ntula (for example the AIMS software) as “free cover” is not a standard concept in insurance and so it is unlikely to be compatible with the software. Eradicating the free cover would have a positive effect on NICO’s loss ratio and perhaps counter the effect of de-linking the product from loan repayment.
6. **Increase in claim reporting period:** Clients complained that it can be difficult to get all documentation to CETZAM within 14 days of the death. This is especially true if the death occurs in a rural location (it is common for those suffering with HIV and other illness to be sent from urban areas to family in the rural areas). With approval from NICO, this reporting window has been extended to 30 days.
7. **Premium payment options:** Clients were split over the best way to pay premiums. Those in Livingstone were happy with the premium being deducted from the loan at disbursement, while those in the Copperbelt wanted to pay the premium in instalments along with the loan repayments. The difficulty with spreading the premium over the loan term is that NICO must be paid in advance, so CETZAM would be funding the client’s premium. In the event that the client defaulted on the loan, CETZAM would not only have to write off the loan, but also the outstanding premiums. Allowing premiums to be paid with weekly loan repayments would also require an MIS to divide payments into the loan and insurance general ledgers.
8. **Speed of claims payment:** Clients complained that claims had started to take up to three weeks to be settled. This is probably a result of rationalisation of the staff at head office causing a temporary shift in focus. As a result, CETZAM has handed claims administration back to NICO, which has undertaken to settle claims within 24 hours of receiving documentation.

CETZAM’s Other Insurance Experiences

Since its inception in 1995, CETZAM had offered all its borrowers a simple credit life product that it called the “Death Insurance Fund” (DIF). The DIF was an in-house fund which required each borrower to pay a fixed sum of ZMK 1,000 (\$0.22) into the fund upon joining CETZAM. The fund was used to pay off any outstanding loans in the event of a client’s death. However, the contributions were not based upon any actuarial estimation of potential claims volumes and the fund soon became depleted.

In September 2002 a new branch was opened in Lusaka to offer loans to individuals rather than groups. At this time a decision was made to introduce credit life insurance provided by Madison Life Insurance Company.³ Credit life was purchased on a flat balance basis with coverage fixed at the value of the disbursed principal rather than on a declining balance. The

³ For more details, see Manje (2005), “Madison Insurance, Zambia,” CGAP Working Group on Microinsurance Good and Bad Practices Case Study No. 10. Geneva: International Labour Organization.

cost of the credit life insurance was factored into the interest rate charged for the individual loan with monthly reporting to the insurance company from CETZAM. The effect on the interest rate of including credit life was an increase of 0.5% on a flat basis per month. At the end of 2004, credit life was extended to include all group loans and the Death Insurance Fund was closed.

The new individual loan product required collateral in the form of either buildings or contents, and CETZAM realised that most of its clients did not insure their belongings. The fact that the collateral could be damaged, destroyed or stolen was a concern to management and a decision was made to implement property insurance to protect the collateral. A fixed rate for building and contents was negotiated with Madison and the cost of the insurance was loaded into the interest rate of the individual loan. The effect on the interest rate charged was an increase of 0.25% flat per month. CETZAM submits a schedule of collateral covered under this binding agreement at the end of each calendar month.

2.3 Opportunity International Bank Malawi (OIBM)

Opportunity International Bank of Malawi Ltd. (OIBM) was granted a full commercial banking license by the Central Bank on March 21, 2002 and its doors opened to the public in May 2003. OIBM's mission is to provide access to a range of financial services to low-income and un-served sections of Malawi's society. Specific focus has been placed on the savings aspect of the business, with loans, insurance and foreign exchange also being offered.

Realising the potential dangers of operating in the world's fourth poorest country, and aware of the effect that HIV was having in Malawi, management sought assistance from OI in the development of suitable insurance products. Together OI's Network Service and OIBM management explored a range of insurance products including: credit life insurance, unemployment insurance for salary-backed loans, property insurance to cover collateral, life savings insurance, livestock insurance, and drought insurance through rainfall indexing. Not all of the products have been launched, but the process of developing them has been quite educational. In addition, OIBM was the test location for the AIMS software developed by Opportunity to work as a module of the eMerge banking software.

Few of OIBM's clients have birth certificates, passports or driver's licences, and few could afford to get them. Without identification, commercial banks are not willing to provide services. OIBM has overcome this problem with the use of biometric fingerprint technology to identify clients who have opened an account. The fingerprint data are stored on their 'Malswitch' Cards and they are only able to access their accounts by having their fingerprints scanned.

At the end of 2004, after just 19 months in operation, OIBM had mobilised \$2,784,050 in deposits from 19,715 savers, most of whom had never previously held a savings account. The outstanding loan portfolio was \$1,369,784 with 1,700 active borrowers, of which 80% were women. The PAR at 30 days was 3.6% and the overall operational sustainability was 45.1%.

Perhaps understandably the initial focus was on the development of **credit life** insurance to protect the bank. Amazingly, credit life was a new product in Malawi's tiny insurance market and none of the existing commercial banks purchased credit life (it is possible that banks with

head offices in South Africa are covered under regional binders). With support from Network Services, OIBM arranged for credit life cover with NICO Insurance at a cost of 0.35% per month of the loan term on a flat balance basis (i.e., the loan was insured for the disbursed principal for the full term of the loan, regardless of what was paid back by the borrower). Certainly CETZAM's relationship with NICO in Zambia assisted in developing a relationship with NICO Malawi.

Initially OIBM introduced credit life for its entry level group loans on a pilot test basis with the cost of the credit life incorporated into the interest rate charged to the clients. Credit life was reviewed a year later in mid-2004 and the decision was made to extend the product to include all group and individual microloans. At the start of 2005, OI's negotiations with NICO resulted in credit life being offered to OIBM's small and medium enterprise (SME) borrowers at a lower rate of 0.2% per month.

After its opening in 2003, OIBM began considering a range of savings, credit and insurance products that may be required by the target market. One of these products was a consumer loan for low-income individuals in full-time employment. The loan would be repaid through the payroll, but OIBM would be exposed if the individual was fired from the company. Opportunity International worked with a local insurance company on a new '**unemployment**' insurance product to reduce this risk. Following negotiation, it was agreed that the insurer would be liable for a maximum of three monthly loan repayments (the proposed loan term was six months) and in return would receive a premium equivalent to 1.25% of the loan principal. The only exclusions were if the borrower retired, resigned, or was dismissed for gross misconduct. OIBM later decided not to launch the consumer loan, at least not yet, but it remains of interest that unemployment insurance would have been available.

Also in 2003, investigations were made into the pricing of **property insurance** that would be applied to any loan secured with collateral. Negotiations with local property insurers demonstrated that buildings could be covered for a rate 0.2% of their sum insured and contents for 2% of sum insured subject to a minimum premium. The minimum premium ratios had to be negotiated down as they originally would have applied to most of OIBM's clients. Claims would be subject to a deductible of 10% of the claim. It was projected that the cost to the client for property insurance would equate to 0.35% per month for an individual microloan and 0.5% per year for an SME borrower. However, OIBM later decided to require loans to be secured by a personal guarantor as well as collateral, and this guarantor replaced the need for property insurance.

Market research during the summer of 2003 revealed that there was demand for life insurance among the target market, most probably as a result of the high frequency and relative severity of the costs of funerals. It was also identified that the target clients had little or no experience with insurance and were unfamiliar with how insurance works. There was concern that insurance would be purchased for the short term and then lapse due to the instability of clients' incomes.

OIBM's clients are so poor that they often live from day-to-day, which causes them to have a short-term perspective on their finances. Insurance with its promise to payout at some undisclosed point in the future was simply not attractive to many. They also could not

understand why their contributions could not be refunded if they did not suffer a death. At the same time, OIBM wanted to increase the average balance of its savings accounts.

The combination of these factors led OI to the idea of combining **savings with life insurance**. This new savings account would have a higher minimum balance and lower rate of interest than the standard account, and in return the saver would receive free life insurance. The life insurance element of the new product was negotiated with NICO Insurance. It is essentially a monthly term life product with a fixed price regardless of age, with minimal administration and exclusions. The insurance has a waiting period of one month to reduce moral hazard and as a result the insurance benefit is retrospective. Therefore if a saver opens the account and deposits the minimum balance on the 1st of January, she will not receive life insurance until 1st February and if she has maintained the balance above the minimum for the whole of February then she receives insurance in March and so on. This product is really only feasible due to the AIMS software that completes all back office reporting and accounting functions automatically.

The new savings account, named “Zonse” (“Everything”), has proved to be popular with the target audience in field research. Originally, the new account was planned for launch at the end of 2004, but overruns of other projects has pushed its launch into the first quarter 2005.

During the course of 2004, OIBM also started to develop strategic alliances with the Land O’Lakes NGO that supports local dairy farmers. OIBM considered offering loans to the dairy farmers, with the dairy herd acting as collateral for the loan. However, the risk of agricultural lending remained a concern for management, and OI was asked to look into **livestock insurance**. The Malawian insurance market is small and undeveloped; no local provider was willing to offer terms since underwriters had no experience in this line of business. Discussions with contacts in South Africa found that Munich Re would be willing to provide coverage at a fixed rate of 5% of the animal’s value. A fronting arrangement was agreed with a local insurance company in Lilongwe to set up the facility with Munich Re in South Africa.

Opportunity International has also been retained by the World Bank to help develop **agricultural insurance** in Malawi, and work started at the end of 2004. The proposal is for a range of commercial banks, including OIBM, to offer loans to small-scale farmers that are members of the NASFAM Union to purchase seed and fertilisers. Loan repayments will be adjusted based on a rainfall index, with lower interest charged (and hence lower repayments) in years with below average rainfall. The shortfall in the interest rate will be covered by an index-linked insurance, which is currently being negotiated by Opportunity International with insurers in Malawi.

2.4 Taytay Sa Kauswagan, Inc. (TSKI), The Philippines

Established in September 1986, Taytay Sa Kauswagan, or “bridge to progress,” is registered with the Securities and Exchange Commission in the Philippines as a non-stock, non-profit Christian development organisation based in Iloilo City. TSKI is part of a local network of microfinance institutions called APPEND (Association of Philippine Partners in Enterprise Development), which includes TSPI, KMBI, ASKI, and Opportunity Microfinance Bank (OMB). At the end of 2004, APPEND’s members were serving 419,511 active borrowers

with an outstanding loan portfolio over \$25 million, and portfolio at risk (30 days) of 2.5%. The average loan size was \$112 and operational sustainability was 111%.

APPEND members tend to share resources and methodologies, both locally and internationally. The trust bank lending methodology, which is now the core product for OI, originated at KMBI and other Philippines partners. Also commonly used by members of APPEND is the “Mutual Aid Fund” (MAF or sometimes “Pondong Damayan”).

The MAF is probably best described as a compulsory savings product that provides a death benefit to members. All borrowers deposit PHP200 (\$3.60) into a fund held at the branch level. If a member dies, then each client associated with the same branch has PHP20 (\$0.36) deducted from their MAF savings, and the accumulated sum is given to the family of the deceased minus any outstanding loan. If a spouse or child (or parent for single clients) die, then the member would receive PHP5 (\$0.09) from each branch member. Clients top-up their MAF savings to PHP200 (\$3.60) at the start of each loan cycle or if the balance reaches PHP50 (\$0.90) during a loan cycle. The MAF pays out benefits to the MFI’s members regardless of whether they have an active loan.

Market research showed that the MAF was one of the most popular products at TSKI. However, as TSKI and other APPEND members grew, they realised that MAF was rapidly becoming a burden for the organisation for a number of reasons:

1. The larger the organisations grew, the more administration was required to deduct individual sums from clients’ accounts. This administration was not only costly but the chance of human error or fraud occurring was becoming unacceptable.
2. The product was becoming unsustainable as it was not earning income from commissions and the cost of administering the product was increasing.
3. In the event of a natural disaster or disease outbreak, it was highly likely that the MAF would be exhausted and TSKI would have to decide to leave clients claims unpaid or use loan funds and income to pay for claims that exceeded the MAF.
4. To attract the debt and equity needed to continue growing, the NGOs would probably need to become formal financial institutions, which would not be allowed to carry the risk associated with MAF on their balance sheet.

In 2004, several APPEND members asked Opportunity International to work on a suitable alternative to the MAF; the study was to include all options, including becoming an insurance agent and establishing a Mutual Benefits Association (MBA). After a careful review, OI recommended that they become insurance agents, with the expectation that once a product had been established and rolled out, institutional alternatives such as the MBA could be considered. In the short term, the quickest and most cost-effective way to launch a product and gain experience was by working as an agent on behalf of an established insurer.

To design the new product, quantitative and qualitative market research with 782 clients from APPEND partners was conducted during June 2004. The main findings were as follows:

- The average family size was five, usually two parents and three children.
- Almost all respondents wanted life insurance for the whole family.

- Analysis of income demonstrated that most respondents were living on or below the “poverty line” defined as \$1 (PHP55) per day per person.
- Half of the respondents estimated that the cost of a funeral was less than PHP35,000 (\$636).
- Fifteen percent of respondents indicated that they had experienced a death in the family in the past year.
- Respondents wanted a death benefit of PHP100,000 (\$1,818) for themselves; PHP60,000 (\$1,090) for their spouse and PHP50,000 (\$909) for a child.
- Forty-one percent of respondents were willing to pay between PHP50 to 75 (\$0.90 to \$1.36) per month for funeral insurance; 59% were willing to pay more.

This research was used to design a prototype product that was presented to five local insurance companies with a request for indicative quotations. The product was a term life product, although some APPEND members planned to deduct any outstanding loan from the claim should the client die. At the same time, a competitor analysis demonstrated that 16% of the 782 clients questioned already purchased insurance from either an insurance company or an informal provider. The average rate charged was 0.48% of the sum insured.

By mid-July quotations had been received from the insurance companies and it was clear that Cocolife Insurance Company was offering not only the best price, but was also willing to negotiate on terms and conditions to simplify the product to meet the needs of APPEND’s members. The details of the product that was accepted by TSKI, OMB and KMBI are summarised in Table 4.

Table 4. Product Details for Microinsurance by Cocolife

| Product Feature | Comments |
|-----------------------------|--|
| Coverage | Losses arising from death only. Covers client, spouse and maximum of three children (or parents if client is single). Compulsory for borrowers. |
| Term | Insurance term linked to the loan term, being six months. |
| Benefit | PHP 100,000 (\$1,818) paid upon death of client, minus any outstanding loan; PHP 50,000 (\$909) upon death of spouse and PHP 25,000 (\$454) for death of child or parent |
| Age / health limitations | Client 18-65; Parents less than 65; child 6 months to 21 years but must be living at home. All must be “in good health and performing normal duties”, but no medical check or questionnaires. |
| Premiums | Calculated as PHP 1.06 per PHP 1000 of the total sum insured for six months paid to Insurance Company and PHP 90 administration fee paid to MFI per loan cycle regardless of number of people covered. |
| Contestability | No claim contestability for existing illnesses, but a one-year contestability for suicide. |
| Documents required to claim | Death certificate, birth or baptismal certificate and claim form. |

It is common practice for existing illnesses to be excluded from insurance products in the Philippines; it is often referred to as claims contestability for existing illness. In some instances, the existing illness is excluded for a set period (e.g., one year) and if the client dies after this period the existing illness is covered. Opportunity sought coverage that included

existing illnesses because clients often lack formal medical records and efforts to enforce the contestability clause would significantly increase administrative costs.

During negotiations with the insurers, it emerged that it is common practice to increase the rate significantly if a commission is paid to the intermediary. For example, if a 20% commission is required then it is common for the net rate without commission to be increased by over 100%. Based upon this observation, it was agreed that APPEND members would pay the net rate to insurers and receive 0% commission, but would instead load the rate charged to the clients with an administration fee. This resulted in a cheaper end solution for the organisations' clients. In fact, for this product, over 90% of clients were paying less than they were willing to pay and receiving higher levels of benefits than they had requested. The cost of the insurance for a family of five is approximately PHP55 (\$1) per month, which is approximately half of the cost that clients were paying to competitors for the same sum insured. This rate was achievable based on the large number of borrowers served by the APPEND members—the volume of clients was a significant incentive to insurance companies during the negotiation.

Staff at TSKI received training in the new product during December 2004 and the product was implemented in January 2005. It is the intention that OMB and KMBI will also launch the new insurance product in 2005 after receiving training from Opportunity International.

The MAF will be phased out with all new or subsequent loans having microinsurance. Any monies remaining in the MAF will be refunded to clients as their existing loans mature. The new product is being presented as a replacement for MAF and many clients actually refer to it as “MAF 3” even though it has different terms and conditions and is being provided by an insurance company; this seems to indicate that the social solidarity that comes from helping one another remains for APPEND clients.

2.5 Oportunidad Microfinanzas, Mexico

In the spring of 2002, after extensive research and numerous visits to Mexico by OI staff members, the OI Network decided to create a microfinance institution in Guadalajara, Jalisco, Mexico. By February 2003, Oportunidad Microfinanzas, S.A. de C.V. (OM) was incorporated under Mexican law, with majority ownership by Opportunity Transformation Investments. The new MFI focused on the poorest entrepreneurs using the trust bank methodology to foster maximum transformation in their lives. While Guadalajara has a large target market, it proved harder to mobilise groups than anticipated. As a result, OM has started to expand to towns and villages in increasingly rural locations within the Jalisco, which have provided more significant growth.

At the end of 2004, OM was serving 513 borrowers with a loan portfolio of \$53,633, an average loan size of \$185 and operational sustainability of 4.7%. By the end of 2007, OM is projected to have more than 7,000 active clients, with an outstanding loan portfolio of more than 20 million pesos (about US\$1,750,000). The projections indicate that operational sustainability will be achieved in the latter part of 2006, at which point OM can begin the process to transform into a regulated MFI.

In March 2003, OI was invited to assist Oportunidad Microfinanzas with the implementation of credit life. While credit life is widely available in Mexico, it was always provided on the declining balance. Declining balance coverage has a serious limitation for a microfinance lender. In the event that borrowers are sick, they normally fall behind with loan payments. If the ill client then dies, credit life on a declining balance basis will only pay the outstanding loan according to the repayment schedule, and as a result the MFI will be left with an unpaid balance. This position is compounded if late fees are charged on the loan, which cannot be charged to the insurer. Declining balance is favoured by commercial banks because the loans tend to be much larger than microcredit, and as a result the lower cost of declining balance is attractive. For commercial lenders making larger loans over longer terms, the portfolio at risk is not significantly affected by an illness that leads to a death as the illness is a short period relative to the overall term. As a result the effective underpayment by the insurance company is minimal in comparison to the claim. Whereas for microfinance, with small loans over short periods, an illness of several weeks can lead to an underpayment by the insurance company that is a significant percentage of the original loan.

Consequently, Opportunity International (and in this instance Oportunidad Microfinanzas) normally seeks to purchase credit life on the disbursed loan amount (plus interest if required) for the full loan term. For example, if a loan of \$2,000 is disbursed with interest payable of \$500, the loan can be insured for \$2,500 for the full term. If the client dies mid-term, having paid back half the loan and interest, then the MFI will still receive \$2,500 from the insurance company. If the client dies on the first day of the loan, the insurer covers the full outstanding loan, but if the client dies later in the loan the MFI receives more from the insurance company than is outstanding on the loan.

Oportunidad Microfinanzas (OM) started to seek quotations from a range of local insurance companies in March 2003, but from the start it was clear that securing even the most basic of products would not be easy. The insurance market in Mexico is extremely traditional and there was resistance from the outset to any alterations to the standard credit life offering. In meetings, the insurance companies stated that they understood the reasons for OM's requests to purchase credit life on a flat balance basis, but they would only provide a quotation on the declining balance basis. Eventually it transpired that the insurance companies were uncomfortable with the direct approach from OM and so a local agent was recruited to act as an intermediary. Eventually, after much negotiation, Principal Insurance Company offered terms to OM and in April 2004, after 13 months of trying, OM finally secured credit life insurance coverage (see Table 5). After one year, OM had not yet made any claims.

Table 5. Product Details for credit life by Principal Insurance Company

| Product Feature | Comments |
|-----------------|---|
| Coverage | Losses arising from death of a borrower during the loan term. |
| Sum insured | Disbursed loan principal plus the interest payable on the loan on a flat balance basis. |
| Age restriction | All clients must be less than 75 years old |
| Medicals | Clients are not required to undergo medicals or complete questionnaires as long as the loans are less than \$11,119 |
| Exclusions | Death arising from suicide or attempted suicide is excluded. |
| Premium | Premium = $((0.0039 \times \text{sum insured}) / 52) \times \text{loan term in weeks}$. Paid by OM. |

The experience of trying to secure even a basic insurance product for OM provided Opportunity International with the following lessons:

1. Sometimes relatively developed insurance markets can be less willing to innovate than those insurance markets that are relatively immature. Mexican insurers were unwilling to be flexible, whereas in African countries, with much less sophisticated insurance markets, local insurers are willing to innovate to meet new needs.
2. In some markets there are rules of etiquette that must be followed to secure coverage. Insurers in Mexico were not used to being contacted directly by a company and preferred to deal via an intermediary even though the product was simple and the margins secured by the insurer would be less for having used the agent.
3. It is possible to access a product, even when the insurers' initial reaction is to resist change. However, one must be willing and able to make the case technically and explain the reasons for one's needs. A significant dose of patience is also necessary!

3. Understanding and Cultivating Demand

A major challenge in microinsurance provision is ensuring that the product is designed to meet the needs and preferences of the target market. Then, since many low-income persons are unfamiliar with insurance, one must educate clients about how insurance works and how they can benefit from it. This section reviews issues related to market research, marketing, client education and convincing sceptics that insurance is for them.

3.1 Market Research

Client need is central to the process that Opportunity uses when designing any new product. The first step of the process described in Section 1.4 is market research. Opportunity recognises that microentrepreneurs increasingly have a choice of which MFI to use, so understanding client demand is essential if OI is going to be competitive in the future. However, client demand is more important than simply competition. OI strives to empower clients; as a result, understanding demand is necessary even where competition is absent.

While insurance is often linked to the loan (and are hence compulsory for borrowers), one must still understand client needs. If a compulsory insurance product does not meet clients' needs, then they will become dissatisfied and loans will start to fall into arrears.

Table 6. Market Research Parameters

| |
|--|
| Biometrics |
| <ul style="list-style-type: none"> • Family size: what is the average family size and composition? • Client age range: important if clients are outside the age ranges normally covered by insurers (e.g. 65 years plus) • Marital Status: important if a family package policy is to be sold • Premium affordability: what sum is “affordable” to a client from disposable income? • Home ownership, title deed availability, construction materials of the home • Value of home and contents – required for property insurance |
| Product feature preferences |
| <ul style="list-style-type: none"> • Interval for premiums (monthly, weekly, yearly) • Should the insurance be loan-linked or independent? • Would the client pay more (interest) for a loan with credit life? • Sum insured: what benefit is required upon death of client / spouse / child / parent • Speed of claims payment |
| Competition analysis/purchasing habits |
| <ul style="list-style-type: none"> • What informal mechanisms are used in the community to pay for funerals? • What formal mechanisms will be our competition? • Current insurance purchasing habits • Reasons for NOT purchasing insurance (is trust a major issue?) • Should the MFI offer insurance? |

OI's product development process utilises both quantitative and qualitative techniques. Typically a market research questionnaire is used with a sample of clients prior to the first TA site visit (see Appendix 1 for a sample). This questionnaire considers client biometrics and purchasing habits, and explores the potential demand for "insurance" (although this term is rarely used as clients have little experience with insurance). The quantitative data gathered from these questionnaires is used to build a preliminary picture of client demand. This snapshot is then reviewed in focus groups to build a better understanding of the key design features for the new product. In many cases it transpires that service (e.g., claims payment speed) is more critical than price. The parameters investigated by these market research techniques are summarised in Table 6.

By conducting this research in different parts of the world, one can see a variety of outcomes from different countries on the same questions. For example, Table 7 shows significant variations in the preferred sum insured amounts and acceptable claims payment speeds between the Philippines, Zambia, Montenegro and Mozambique. These results reinforce the utility of OI's process-oriented approach rather than a cookie cutter replication of products in different countries.

Table 7. Comparison of Market Research Results in Different Countries

| <i>Country</i> | Affordable premium | Sum insured upon death | Acceptable claims payment |
|-----------------|--|---|----------------------------------|
| The Philippines | 50% said more than PHP 75 (\$1.36) per month | Client PHP 100,000 (1,818) Spouse PHP 60,000 (\$1,090) Child PHP 50,000 (\$909) | Within a week |
| Zambia | ZMK 1,125 (\$0.28) per week | Adult ZMK 500,000 (\$109) Child ZMK 250,000 (\$54) | Within two weeks |
| Montenegro | €20 to €50 per month | €35,000 (\$42,000) | Within two days |
| Mozambique | MZM 50,000 (\$2.50) per month | Adult MZM 7,500,000 (\$375) Child MZM 3,750,000 (\$188) | |

The output from the market research will heavily influence the product design. So for instance, if the market research shows that clients want to receive \$1,000 upon death, then this becomes the product's sum insured. While it is critical to design the product around the identified client need, it is also important to take into account additional factors such as the MFI's operational capabilities, available supply from insurers, and regulatory requirements.

There are inevitably times when demand cannot be met because of a restriction in one of these areas. For example, clients may want a sum insured of \$1,000 and they can afford \$1 per month, but from discussions with insurers it is evident that for \$1 per month, the maximum sum insured available is \$750. In these instances, it is important to use focus groups to work through whether clients will be happier paying \$1.25 to secure the \$1,000 sum insured or whether the premium of \$1 is more important and the sum insured of \$750 is acceptable. In some cases, client demand will not mesh with available supply, operational reality or regulatory requirements so that an insurance product is not feasible; although these instances are rare.

It is perhaps easiest to meet client demand in relation to product features, such as sum insured, number of people covered and even premiums; it can be harder to meet expected

service standards as this often impacts upon product distribution. Product distribution will depend on the MFI's operational reality (e.g., MIS, staff capacity, etc.), the willingness of insurers to consider alternative arrangements, and the provisions of local regulation. The most common example is the speed of claims payment. Some clients expect claims to be paid within 24 hours of the death because the funeral often needs to occur quickly. The reality is that the MFI needs time to validate and process the claim. Even if the MFI can act fast, it is unlikely that the insurance company can pay the claim within 24 hours. In the Philippines, Malawi and Zambia (although this was later reversed), the inability of insurers to meet the required service standard led OI to negotiate a revised agency agreement whereby the MFI has the authority to verify and pay claims (see Section 5 for more details).

3.2 The Need for a Marketing Plan and Client Education

Marketing is often overlooked by microfinance organisations; but experience has demonstrated that it is a critical part of any product launch. Marketing is often restricted to the clients, whereas a marketing plan should also target staff because they are just as likely to be resistant to change. If loan officers do not endorse a new product, it will not succeed.

This lesson was learned the hard way when CETZAM launched the Ntula product. The geography of the branch locations meant that staff and clients in the north were aware of the pilot product and were very happy when it was rolled-out. By comparison the branches in the south were unaware of the new product and it was met with hostility when it was introduced. With hindsight, the most damaging mistake was a failure to inform staff of the impending change. When clients started to question the new product, staff were not willing or able to defend the company's policy and as a result the clients lost faith not only in the new product, but also in the institution. It is essential to warn staff several weeks before a new product is introduced so that they can start to discuss it among themselves and get used to the new ideas. They also can then start informing clients that a change is about to occur, so when the change is implemented it does not come as a shock.

In CETZAM's southern branches, the only way to restore confidence in the institution and the product was to allow the insurance product to be voluntary. Staff trainings were held that allowed them to air their grievances. At the same time, street theatre was arranged with a local troop of actors who sensitised the clients to the need for insurance. The use of street theatre has proved successful within OI as a means for educating clients on a new product such as insurance.

The main method of educating clients, however, remains the loan officers as they have weekly contact with the clients. In recognition of this fact, each loan officer is provided with a full day of training on insurance and the specifics of the new product, as well as an operations manual that contains FAQs (see Appendix 2 for a sample of FAQs for staff). Questions such as "if I don't claim, why can't I have my money back" are common from clients that have never used insurance before. If loan officers do not feel equipped to answer these difficult questions, then clients will lose faith and assume the worst about the new product. Often a product can be designed taking into account client demand, but if loan officers are unable to explain how the product works, then clients will be dissatisfied with it. Client education is therefore critical to a successful product launch.

3.3 Convincing the Sceptics

Calculating client demand through the use of market research will always result in the “average” client’s view. It is to be expected that within any client base there will always be those who disagree with the majority. Convincing clients to part with their hard-earned cash in return for an unfamiliar product presents a unique challenge. The following insights from OI’s experience may be useful:

1. **Invest in market research**, which will ensure that the product is correct for the majority, leaving only the minority to convince. Being able to show doubters that the product is based on popular demand is often a compelling argument within societies with strong social group ties (i.e., do it for the community).
2. **Make sure that the premiums are affordable** for the poorest clients. The easiest way to define affordable is to work out what cash a client will have spare on an average day. Clients are unlikely to always save for a premium payment, so a monthly premium needs to equate to the cost of a non-essential item, such as a packet of cigarettes.
3. **Invest in staff training**: If the staff believe, then the clients are more likely to follow. You have no hope of convincing clients if you cannot convince your staff. It is always a bad idea to force staff to believe!
4. **Encourage the power of the group**: An individual who is hostile to a new product often experiences a change of heart when the idea is discussed in a group. This is particularly true with group lending methodologies as clients realise that the product will help group members who would otherwise struggle to repay the loan when their household experiences a death.
5. **Let the doubters see results**: The best way to convince sceptics is to inform them of how many claims have been paid. Once clients start to see claims being paid, often the mood toward the new product shifts significantly.

4. Product Design

Table 8. Premiums and Benefits across Countries

| Country | Premium | Benefits |
|---------------------|---|---|
| OIBM, Malawi | 0.35% of loan principal per month of the loan term | Upon death the disbursed principal will be paid to OIBM. |
| UGAFODE, Uganda | 1% of the disbursed principal | Credit life – loan cleared upon death of the client from any cause Funeral Benefit – Ush 1,200,000 (\$666) for client, Ush 600,000 (\$333) for spouse and Ush 300,000 (\$166) for child upon death from accident only. Property – loan cleared if business destroyed by a catastrophe (e.g. market fire). |
| CETZAM, Zambia | ZMK 1,125 (\$0.25%) for every week of the loan period | Upon death of the client and up to six family members a benefit of ZMK 500,000 (\$108) for an adult and ZMK 250,000 (\$54) for a child. |
| APPEND, Philippines | PHP 1.06 (\$0.019) per PHP 1,000 (\$18.18) of the sum insured plus a PHP 90 (\$1.63) administration fee | Death of client: PHP100,000 (\$1,818) Death of spouse: PHP50,000 (\$909) Death of child: PHP25,000 (\$454) |
| OM, Mexico | $((0.0039 \times \text{loan principal} / 52) \times \text{loan term in weeks})$ | Upon death the disbursed principal will be paid to OM. |

Opportunity International’s approach to insurance product design can be summed up as “make it as simple as possible.” Experience has demonstrated that if a product cannot be easily explained in just a few sentences, then low-income clients will not understand it and the product will not be well received.

Making an insurance product simple is actually harder than it sounds, especially within the partner-agent model where the insurance company has influence over a product’s terms and conditions. OI spends a significant amount of time working through with an insurance provider how to simplify the process, terms and conditions. By simplifying the coverage from the “standard” off-the-shelf product, it is often also possible to reduce the cost to the client. For example, many insurers offer disability coverage as part of a life policy, but is this coverage important to the clients? And can the client realistically make a claim under the disability cover? Many clients cannot claim for disability because they are unable to demonstrate that it was not an existing condition as they have no formal medical records. Trying to explain to clients that they get 50% of the sum insured for one arm, and 25% for an eye, and so on, is also complicated and off-putting for a newcomer to insurance.

4.1 Product Design Lessons

This section summarises the lessons that OI has learned about the design of credit life, term life and property insurance.

Credit Life

While credit life is perhaps the simplest and most common product offered by MFIs, it still can be designed badly. When designing a credit life product, consider the following issues:

1. **All MFIs should have credit life insurance:** New and mature MFIs, those offering big and small loans—if an MFI is concerned about what to do when a client dies, then it needs credit life.
2. **Flat or declining balance?** Credit life can be purchased either on a flat or declining balance basis. OI's experience suggests that the flat balance—providing coverage for the disbursed loan amount for the full term of the loan—works best for a microfinance portfolio. While coverage for the disbursed amount is slightly more expensive, the lender is guaranteed to cover the full outstanding loan regardless of whether the loan is in arrears on the date of death. The other attraction of purchasing credit life on a flat basis is that interest can be easily covered (whether the interest is calculated on a flat or declining basis).
3. **What to do with the surplus?** By arranging cover on a flat balance basis, there will normally be a surplus. For example, if a client with a \$100 loan dies with \$20 still outstanding, then the MFI receives \$100 from the insurance company and is left with a surplus of \$80, which can be used to repay any accrued interest and late fees. When OI's partners first introduced this product, they would refund any surplus to the bereaved family. However, there were instances within a group when one client died early in the loan term, so the family received a small payout, and one client died at the end of the term and the family received a larger benefit. Such “discriminatory” behaviour in the eyes of the community was unacceptable as it appeared that the MFI was placing a differential value on the clients' lives. The unexpected payout to the family was also seen as “charity” and the MFIs were besieged with relatives seeking a hand-out. A decision was taken to retain any claims surplus in a fund and to use the fund to run periodic trainings within the community on a range of issues from HIV/AIDS to book-keeping classes.
4. **What risks to cover under credit life?** In some countries, insurance companies will offer a range of coverage within a standard credit life policy. These include disability as well as terminal illness. Experience has shown that these add-ons are often difficult to claim (see Box 1). It is easier and cheaper to just purchase cover for death.

Box 1. Illness Cover in a Credit Life Policy?

When CETZAM first introduced credit life, the product covered sickness. If the client was ill for a prolonged period, then Madison would pay up to three monthly loan instalments. Experience showed that it was hard for clients to claim under this provision because they could not get formal medical records as required by Madison. As a result, CETZAM negotiated to have the credit life just cover death at a reduced premium.

5. **How to collect premiums?** Premiums can be collected in a variety of ways, but the favoured approach for credit life is to load the cost into the interest rate on the loan. The advantage of this approach is that the client can be told of the benefit of the product, rather than explaining that insurance was purchase by the lender on the client's life (which is often daunting for a borrower). The disadvantages of loading the interest rate are: 1) it can make the loan less competitive; and 2) the MFI must finance the premium as the insurance company often wants to be paid upfront, and by collecting through the interest rate the MFI is exposed to non-payment via loan default. The alternative is to seek an up-front fee from the client for credit life, but clients inevitably take the fee from the disbursed loan, leaving them with less working capital, which could reduce their ability to repay the loan.
6. **Extensions:** It is worth negotiating with the insurance provider to allow automatic extensions to the credit life policy in the event that the borrower is in arrears and the loan remains active past the maturity date. If the client dies after the maturity date, then the MFI is not covered normally. By arranging an automatic extension clause, an additional premium can be paid for the remaining period (i.e., until write off).
7. **Medical questionnaires:** Most insurers have a coverage limit under which medical examinations are not required. However, a lot of insurers still insist upon a medical questionnaire to be completed by each client. This can be burdensome for an MFI and it is worth negotiating with the insurance company to remove this requirement.
8. **Regulations:** There is normally no need for an MFI to become an agent to introduce credit life insurance. The reason being that the MFI is purchasing the cover for its own asset (the outstanding loan) and the MFI does not normally receive a commission for credit life.

Term Life

Within the OI network, this product is often referred to as funeral benefit insurance, but in essence it is a simple term life contract. In designing term life cover, consider the following issues:

1. **Demand is critical:** If the product is designed with client needs in mind, then it will most likely succeed. Premium affordability, sum insured, and the number of dependants covered are all critical factors to ascertain from research.
2. **Distribution:** In microinsurance, the most common way of making term life available is by linking it to an MFI's loan term and using the loan as the mechanism for collecting premiums. The disadvantage of this is that the insurance is only available while the client has a loan and often clients want insurance even when they do not have a loan. Opportunity has started to use the savings account as a method of distribution, which allows the client to pay premiums incrementally over a month with a debt being made from the savings account at month end. This approach is being used in preliminary product designs in Montenegro, Mozambique and Malawi.
3. **Make premiums affordable:** The best way to make premiums affordable is to collect them regularly. Within OI this has typically been on a monthly basis. While this adds transaction costs for the MFI, the burden can be reduced by using the loan or the savings account as a conduit for premium collection.

4. **Consider the term as a month:** If the insurance term is not linked to the loan, then some clients will want to purchase insurance for the shortest possible period. If premiums are collected monthly, then the product should be viewed as a monthly renewable term contract; if the client pays at the start of the month, then they have coverage for that month and so on.
5. **Anti-selection:** Opportunity's partners have used two approaches to reducing anti-selection. Firstly, the product can be made compulsory for all borrowers, although this is only advisable if the product is only offered to borrowers. Secondly, a short waiting period can be introduced, typically one month. The waiting period can also discourage lapses as clients should be informed that if they miss a payment they will have to undergo the waiting period when they start paying premiums again. It is critical that the waiting period is long enough to discourage those that seek to abuse the product, but short enough to not be seen as prohibitive.
6. **Make it easy to make a claim:** The best way to drive up administrative costs and ensure that clients are dissatisfied is to have an elaborate claims process. Negotiate with the insurance company to ensure that the required documentation will be accessible for the client base. If an insurance company wants a copy of the birth certificate, but low-income clients do not have the documents, then they will not be able to claim and they will focus their dissatisfaction on the MFI, not the insurer. By making the products simple (i.e., if you are dead, then we pay) and reducing the scope of coverage (it is hard for a loan officer to assess if someone is sick, but easy for them to see that someone is dead), then the costs will be lower and satisfaction will be higher.
7. **Avoid contestability for existing illnesses:** Some insurers require that deaths arising from an existing illness are subject to a contestability period that can be up to a year. In reality, this stipulation is difficult to explain this to clients and loan officers, and it is impossible to implement because clients often do not have formal medical records.
8. **Minimise the number of exclusions:** Find out which exclusions the insurance company cannot delete and negotiate to remove any which do not apply. A long list of exclusions are difficult (and time consuming) for staff to explain and hard for clients to understand.
9. **One price for all ages:** It is standard practice for insurance companies to apply differential rates for life insurance to people of different ages and sex. However, this can be very difficult for staff and clients to understand. By presenting the insurance company with an accurate age distribution for the client base, most insurers are willing to provide a single rate for all ages. A single rate will mean that young people are penalised, but the sums insured and premiums are so small that the differences are insignificant. In the Philippines, for example, Cocolife initially presented its rating table listing the price per age, but after negotiations it agreed a fixed rate for all ages. This approach, however, will only work when the sum insured is small. For high value policies, the MFI will have to accept a rating table from the insurance company.

Property Insurance

To date the use of property insurance within the OI network has been restricted to insuring items used as collateral for an individual loan.

1. **Ownership:** It is critical to establish what proportion of clients actually own the building (home or business premise) that is to be insured. It is difficult to cover the building if the client does not own it. Title deeds will also be required; check what percentage of owners has these documents.
2. **Building material:** Insurers will normally only cover buildings constructed from brick or concrete with a roof that is NOT thatched.⁴ Research should be conducted to see if this is applicable to the client base.
3. **Group policy:** While it is often difficult to purchase cover for contents only, the likelihood of it being offered increases if the premium volume on the policy is maximised by a group policy. CETZAM has been able to secure contents-only cover using this approach.
4. **Reduce costs by reporting monthly:** Agree with the insurance company that a schedule of items will be submitted at the end of each month along with a single premium payment.

4.2 The Voluntary versus Compulsory Dilemma

While the eventual aim must be to offer most insurance products⁵ to clients voluntarily, there are a number of reasons why they are being offered on a compulsory basis. The main driver to insurance being compulsory is an underdeveloped distribution model. For operational reasons (e.g., lack of MIS, need for staff to focus on loan collection), most MFIs cannot offer insurance unless the loan is used as a mechanism to collect the premiums. Although this means that insurance is usually compulsory, this linkage keeps administrative costs down, which in turn reduces the cost to the client. In addition, anti-selection with a voluntary product drives up premium costs. In CETZAM, for example, the Livingston branch offers the Ntula product on a voluntary basis and the loss ratio is 400% worse than for the rest of the organisation where Ntula is compulsory.

Since microinsurance is primarily loan-linked, the number of clients that the MFI can serve is restricted to its borrowers, which by insurance standards is a relatively small number. If the product was voluntary, the number of clients participating in the scheme would be even smaller and as a result statistical equilibrium is difficult to achieve. Without sufficient volumes, the insurance company would have to inflate the premium to reflect the unstable loss ratios. Consequently, the only feasible way to offer insurance to MFI clients if the potential client base is to be restricted to its borrowers is to make the product compulsory.

Once a suitable distribution model has been developed to sell insurance to low-income persons who are not borrowing, then the number of clients can rise to a level where loss ratios, and hence pricing, are predictable. At that point, insurance products can be offered on a voluntary basis (with additional measures to control adverse selection). Toward that end, OI is working on developing a new distribution methodology for microinsurance, which is described in Section 6.

⁴ This exclusion has not been the case in India, where insurers will cover thatched roofs in a “hut insurance” rider, but the policyholder pays more if the roof is thatched.

⁵ Credit life insurance would be a notable exception.

5. Claims Management

As with product design, the claims process must also be simple to minimise the need for staff training and ensure that clients feel as if they are being treated fairly. Typically, life insurance claims require a copy of the death certificate or police report along with a completed claim form as a minimum; some insurers will also require a combination of birth certificates, marriage certificates or a copy of an ID card. Some areas that require attention are as follows:

- **Simple product requires a simple claims process:** If one succeeds in designing a simple product, then the claims settlement process will also be simple. If the product covers many eventualities and has lots of exclusions, then the claims process will require more checks. These not only add to the cost of administering the product, but will also slow down the speed with which claims can be paid, leading to client dissatisfaction.
- **Be generous with claims reporting:** While it is important to place a time limit on claims reporting, the limit should be set taking into account local customs.
- **If possible administer claims:** If clients want claims to be paid quickly (e.g., less than a week), then an MFI should verify and pay the claims itself. If the product is simple and has few exclusions, then it will be easy for loan officers to verify that a claim is payable. For the MFI to pay out the claims itself, it needs to negotiate an amended agency agreement (see Box 2).
- **Control for fraud:** Operational procedures are put in place to ensure that the branch manager or accountant verifies that the claim is payable to reduce the chance of client and/or loan officer fraud. With an amended agency agreement, any fraudulent claims will have to be paid by the MFI, so it is only advisable to verify claims for simple products.

Box 2. The Revised Agency Agreement

In those instances where the MFI and insurance company agree that it will be difficult to pay claims within the period expected by clients, then an amendment to the insurance agreement is sought. In the event of a claim, the MFI takes steps to verify that the claim is payable; typically this will include checking that: 1) the deceased was covered, 2) the death occurred during the period of insurance, and 3) the cause of death was not excluded. If the product is very simple, then this task can reliably be conducted by field staff.

If the MFI is satisfied that the claim is payable, then it pays the claim using the float of premiums collected but not yet submitted to the insurance company. At the end of the month, the MFI submits the net premium schedule showing the total premium collected and the total claims paid. All supporting documentation for the claims is attached to the premium schedule and the insurance company is able to check that the claims have been handled to their satisfaction.

In the event that the insurance company queries a claim that turns out to have been paid in error, then the MFI is responsible for refunding the erroneous claim to the insurance company. If this approach is to be used, the MFI must be sure that it has in place operational procedures to minimise the possibility of paying erroneous claims. To date, no claims have been refuted by insurance companies partnering with Opportunity International partners using this approach.

By keeping coverage and exclusions simple, clients and staff will understand the product better and be more satisfied with it. Experience has demonstrated that client understanding and satisfaction are directly linked; even when a claim is perfectly administered, clients can feel dissatisfied because they either did not know what to expect or they had false expectations. The best way to counter dissatisfaction is to ensure that clients (and staff) understand the policies and procedures. As most MFIs do not incorporate insurance in remuneration and bonus arrangements, loan officers have little or no motivation to explain the product to clients or administer claims speedily; the only solution therefore is simplicity.

5.1 The Claims Settlement Process

Any claims settlement process must seek to balance the cost of administration with a desire to place a significant barrier in the way of fraudulent claims. In addition, when partnering with an insurance company, its needs will also have to be reflected in the process. For a typical life insurance product, the claims settlement process would contain the following steps:

1. **Client reports death:** Upon being notified of the death, the loan officer advises the bereaved who can make the claim (e.g., next of kin) and what documents are required.
2. **Group verifies the death:** Normally the leadership of the trust bank is required to submit a letter confirming the death of a borrower or a family member. This reduces the chances of fraud.
3. **Client submits documents:** When a claimant submits the required (original) documents, before that person leaves the office, branch staff should ensure that the paperwork appears to be valid, relates to a person listed as insured, and that the policy is in force. If necessary, certified copies are made of the original documents.
4. **Branch verifies the documents:** Field staff validate the documents and the claim, which can include checking internal records as well as attending the funeral or seeking confirmation from the hospital or doctor that issued the death certificate. More than one staff member should be involved in verifying the documents to reduce the chances of fraud.
5. **If the claim is not valid,** then the claimant should be advised as soon as possible. The longer this takes, the greater the level of dissatisfaction on behalf of the client. Every day that passes after the documents have been accepted by the branch will increase the client's expectation for the payout.
6. **Branch escalates to head office:** In some instances, the branch manager has authority to pay the claim, but usually the finance manager at head office must authorise payments. As a result, the branch must submit the claim and supporting documents to the head office.
7. **Claim is authorised:** Once the claim is authorised, the payment should be made to the claimant as soon as possible. This is normally done by the branch manager.
8. **Reimbursement sought from the insurer:** Typically the documents to support the claim would then be submitted to the insurance company along with the premium schedule at the end of the calendar month. A revised agency agreement empowers the MFI to deduct claims paid from the premiums.

5.2 Common Reasons for Claims Delays

While service standards are often highlighted in focus group discussions as being more important than price, it seems that many MFIs do not make an optimum effort in servicing clients. With insurance, clients want to access claims payments rapidly, although this means different things in different countries. In countries where informal burial societies are common (such as Zimbabwe for example), poor people are used to receiving money for a funeral within a day or even within hours. In other countries, it is acceptable for a claim to be paid within two weeks, but the claim should not exceed two weeks.

Clients do not measure payment speed from the time the claim is reported to the MFI; instead they measure the claim process from the date of death, which can often be days before the MFI is informed. So in promoting their service standards, MFIs must make it very clear what time period is actually being measured.

There are many reasons for claims to be delayed; some of the most common reasons are as follows:

1. **Delays in claim reporting:** In some sub-Saharan African countries, it is common for the sick to be transferred from the urban area to the family home in a rural location. When the individual dies, it can then prove difficult to get a death certificate because often the person died outside a hospital. When documentation does exist, it can take time for documents to arrive back in the urban setting to be presented to the MFI. There are also often delays in the hospital providing a death certificate or, in the case of a road accident, the police providing their report. These delays in obtaining official documentation can lead to significant time elapsing between the death and the claim being paid.
2. **Need for original documents:** Insurance companies often demand that the supporting documentation be the originals. Relatives are often reluctant to let the original death certificate go because it is needed to close bank accounts and for tax authorities. It is important to work with the insurance companies to educate them about clients' needs and negotiate for the use of verified copies (verified by a staff member).
3. **Delays in checking documentation:** Following a spate of fraud in the early days of CETZAM's Ntula product, a policy was introduced whereby the loan officer had to physically visit the hospital and check with the doctor who signed the death certificate. While this reduced fraud, it also led to delays in claim payment.
4. **Lack of suitable MIS:** Claims are often reported for individuals that are not listed as family members or for loans that are no longer active. As many MFIs use paper records, the claims are often accepted for processing by the branch staff and the fact that the claim is not payable does not emerge until after the bereaved has left the building. There is then often a delay in tracking down the claimant and reporting the reasons for non-payment. These delays are seen negatively by claimants who believe that their claim was accepted when they submitted the supporting documentation. If the MFI had a suitable MIS, then the branch staff would have been able to see if the deceased was covered and if the policy was active on the date of death while the claimant was in the branch. This would significantly reduce misunderstandings and client dissatisfaction with insurance products.

5. **Lack of client understanding:** Because clients (and in some cases staff) have a poor understanding of what is covered and excluded, many claims are reported that are clearly not payable. It is common for a former borrower to report a claim many years after they had repaid their last loan. The client believed that the coverage extended indefinitely. The only remedy to this is, of course, client (and staff) education.
6. **Lack of remuneration for handling insurance:** Loan officers are rewarded for the number of loans and quality of their loan portfolio. As they receive no bonus for the sale of insurance or the quick processing of claims, they do not spend time educating clients about the insurance products and are not motivated to process claims quickly.
7. **Claim contestability:** In some instances, insurers demand that an existing illness be excluded for a set period from the start of the insurance contract. This is commonly used to reduce anti-selection as insurers do not want to pay for those that were sick when they joined the programme. Experience has shown that this condition can be hard to enforce as many clients do not have medical records or receive regular treatment from licensed physicians. As a result, trying to ascertain if the client died from an existing illness delays claims processing. Opportunity International tries to negotiate with insurers to remove contestability clauses, offering instead to pay a higher premium, which is often inconsequential in relation to the reduced administrative costs.
8. **Delays at head office:** Claims that have to be authorised by a senior manager (e.g., head of finance) can be delayed due to the severe work load of senior management. The work flow needs to be constructed to minimise the potential for bottlenecks.
9. **Delays caused by insurers:** While some insurance companies can process claims quickly, many take several weeks. It is recommended to negotiate an amended agency agreement as described above.

Within the OI network, it typically takes two weeks from the date of death for a claim to be paid to the bereaved family. In some cases claims payments have taken four or even six weeks, but this is normally as a result of a poor internal processing which is a temporary issue. While many will argue that two weeks is too long, it is OI's experience that is difficult to process claims much faster, although an appropriate MIS and an amended agency agreement make important contributions to achieving service standards.

6. Organisational Structures

Before 2002, many of OI's implementing partners operated informal (unregulated) self-insurance funds for a number of risks, including credit life. Since 2002, there has been a move away from self-insuring risks that has been instigated by an increased awareness of the potential pitfalls of such an approach and the incompatibility of carrying risk on the balance sheet of a regulated financial organisation. The result has been a move into a wider use of the partner-agent model, whereby the MFI partners with a licensed insurance company.

This section begins by describing how to make the partner-agent model work better, and then it considers alternative arrangements including a protected cell company, a mutual benefit association, and a stand-alone agency. It concludes with a discussion about insurance-specific software designed to enhance the efficiency and effectiveness of microinsurance.

6.1 The Benefits of the Partner-agent Model

While self-insuring risk allows the MFI to set the terms and conditions of the product, and in some cases offer a product that an insurance company could not provide, self-insuring also has significant pitfalls. It is hard to price the product because most MFIs have a relatively small number of clients; as a result there is no statistical equilibrium and the loss ratio varies erratically month by month. The result is that most MFIs overprice the product to compensate for the uncertain results and clients end up paying more than if the product was outsourced to an insurance company.

In a number of cases, MFIs have reduced the cost of credit life by 50% by moving from an internal fund to an arrangement with a local insurance company. For example, members of APPEND in the Philippines had charged their clients a 1% levy on the loan principal to cover the risk of the client dying. This has been replaced in the last few years with credit life through Cocolife Insurance, which is charged at 0.5% of the loan amount.

Most MFIs cannot resist cashing in any reserve at the end of the year and as a result there is no provision for natural disasters or epidemics. Since insurance funds are priced to cover the "average" year, by transferring any reserve to the loan portfolio at year-end, there is no way to safeguard the organisation's bottom line when a disaster occurs.

For MFIs that are regulated financial institutions or planning to convert into one, self-insurance is simply not an option as banking regulation will not allow for such risks to be carried on the balance sheet. Table 9 summarises the main advantages and disadvantages of working as an insurance agent.

Opportunity has not experienced difficulty in finding locally registered insurance companies that are willing to partner, except in the case of Mexico where there was initial reluctance due to the small size of the loan portfolio. Typically, locally-owned insurance companies show more interest in the lower-end market than international insurers; the exception has been AIG that has partnered with OI partners (and other MFIs) in Uganda and India.

Table 9. Advantages and Disadvantages of Partnering with an Insurance Company

| Advantage | Disadvantage |
|---|---|
| <ol style="list-style-type: none"> 1. Often the simplest, cheapest and quickest way to start offering insurance 2. Lowest financial and reputation risk 3. Guaranteed income from commissions, no chance of making a loss 4. No capitalisation requirements 5. Lower regulatory requirements 6. No need for expensive specialist managers & staff | <ol style="list-style-type: none"> 1. Need to negotiate with a third party for a product that meets clients' / MFI's needs 2. Income restricted to commissions; low risk, but also relatively low reward 3. Reliant on the insurance company which could change its view of your products 4. Service standards in the hands of a third party 5. Strict reporting requirements to insurer |

The default position of insurance companies is to offer an “off the shelf” product that was originally designed for a higher segment of the market. While the sum insured and corresponding premiums can be reduced to fall in line with the needs of poor people, it is often the case that the product is unsuitable for use by the poor. Experience has shown that if the insurance company can be presented with compelling market research and an argument based on a sound understanding of insurance (and in some cases reinsurance), then a specialised product will be designed.

For example in the Philippines, APPEND had approached a range of insurance providers during the course of 2002 and 2003 and had been offered an off-the-shelf term life product with a high sum insured and premium. Frustrated and unable to understand the motivations of the insurance company, they asked Opportunity International to conduct market research and design a suitable product. The outcome is the product described in Section 2.4. By using the market research, a strong case could be made to insurance providers.

Most insurance companies in developing countries have portfolios dominated by commercial or industrial lines of insurance, with a few personal lines comprised of high value individual policies and corporate group policies. The portfolio of a typical MFI offers an insurance company an opening for a new line of business comprised of a (relatively) large number of low sum insured policies with virtually no acquisition costs. A progressive insurance company will recognise that today's poor are tomorrow's middle class. As a result, offering simple products to this market presents a significant marketing opportunity. These facts mean that the portfolio of clients being served by an MFI can be positioned as an attractive proposition to a forward looking insurance company.

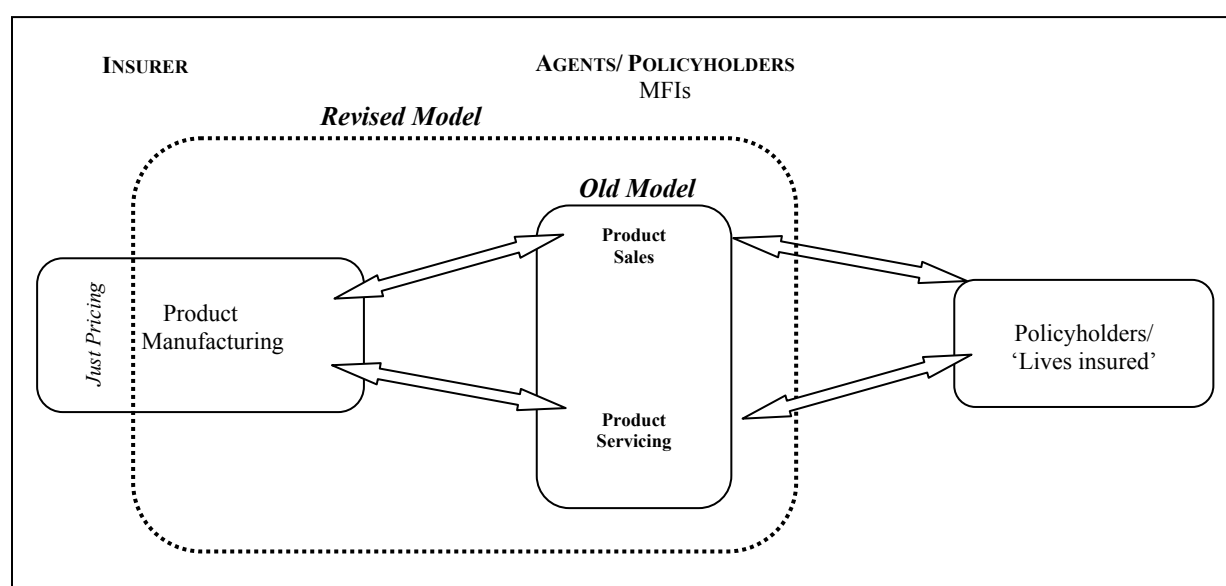
While price will always be a factor, the flexibility of an insurance company to alter its standard requirements remains the key driver in choosing a suitable provider. An example of the required flexibility is demonstrated by the medical reporting stipulations. While in most cases the sum insured sought by poor people is below the insurer's “free underwriting” limit, so no medical examination should be required, in some cases an insurance company will include questions about the applicant's health in the policy application. These forms can be difficult for the client to complete; the questions can be complicated. The poor often lack medical records, so even if they have an existing illness, the clients may not know what it is called. Asking clients to complete medical questionnaires yields little useful information to

the insurer, increases the stress placed on a client, and increases the administrative costs for the MFI.

By explaining the lending methodology to the insurance company, most have been convinced that the group lending methodology is self-selecting. The group members would not permit a client with a history of serious illness to be included because they are aware that the client could struggle to repay the loan, leaving the rest of the group to pay the loan under the mutual guarantee. The self-selecting nature of the group lending methodology is more compelling than the information that could be gathered from a medical questionnaire.

The best outcome when negotiating with an insurance company can be achieved by presenting the insurance company with a proposal setting out, in as much detail as possible, how the product would work. Such an approach requires a change in thinking from the traditional partner-agent model, as shown in Figure 1. Instead of relying on the insurer to do the “product manufacturing,” the MFI takes the lead by telling the insurer (or insurers) exactly what it wants. Then the insurer determines whether it can provide the product, and if so, at what price.

Figure 1. The Revised Partner-Agent Model



The proposal should be based on a good understanding of client demand as well as a thorough understanding of what will be legal in the local context, and what the insurer is likely to want to offer following initial discussions. The alternative to this is to provide the insurance company with the outputs from the market research and let the insurance company design the product. Experience shows that the best result for poor people is achieved when the insurance company is removed from the design process and is simply asked for the price. Clearly many MFIs will not have this option as they will not have sufficient insurance experience; this is part of the value added of belonging to a global network with a centralised pool of expertise.

The product must also be well conceived operationally before it is presented to the insurance company. How the MFI will administer the product will of course alter how the product is designed, and it is important to present to the insurer the best outcome for the MFI, rather than let the insurer mould the product to its own internal requirements, which will inevitably lead to cost escalation at the MFI.

It is also important to differentiate between products, such as credit life and property insurance on loan collateral, which are purchased by the lending institution, and insurance products that are sold to clients, such as funeral benefits or term life. With products such as credit life, normally the MFI would just buy them from the insurer as a group policy with the MFI as the beneficiary. Whereas for products that are “sold” to clients, and for which a commission is received, it is normally a requirement that the MFI registers as an agent on behalf of the insurance company.

While there is a diversity of regulation relating to becoming an insurance agent, it is rarely onerous. Typically, an MFI would need to complete the following steps:

1. Choose an insurance provider and negotiate a product that both the MFI and insurance company are willing to provide. Contracts should be signed.
2. The insurance company will typically approach the Commissioner of Insurance to seek a licence for the MFI to act as an agent on its behalf.
3. The MFI identifies the point person for insurance so that the Commissioner’s office knows who to contact. This person should be a national and have sufficient insurance knowledge. Often this means that Opportunity International provides basic insurance training to this individual prior to training all operational staff. In some cases, the individual has to take a brief and simple examination.
4. The MFI must pay an annual fee for its licence, but this rarely exceeds a few hundred US Dollars; in many cases, the insurance company arranges to pay the fee.

There are exceptions however. In Opportunity International’s experience, Serbia has proved to be the most difficult place to establish an insurance agency, where one must set up a separate limited liability company with a minimum capitalisation of €12,000.

6.2 Protected Cell Company

While the partner-agent model has been widely utilised by OI partners, other structures have been considered, including Protected Cell Companies (PCC) in Zimbabwe.

Opportunity International’s partner in Zimbabwe, Zambuko Trust, is in the process of developing a credit life and funeral benefits policy. Market research demonstrated a high demand for insurance and client focus groups revealed that the speed of claims payment would be critical to the success for the funeral product. Over half of Zambuko’s clients had contributed to an informal burial society. These burial societies are organised by a member of the community who collects small regular contributions from a relatively small number of members. These contributions are saved in a bank (or sometimes in a tin) and in the event of a death of a member or a family member, the burial society pays a sum from the saved

contributions. Due to the small number of people that are included in each burial society and the limited geographical scope, the claims are often paid within hours of the death. These burial societies have been common in Zimbabwe and the best run societies, such as Doves and Moonlight, are now registered insurance companies. In recent years, the popularity of the informal, unregulated societies has waned as inflation, poverty and theft have eroded their appeal. However, most Zimbabweans remain familiar with the concept of funeral insurance and expect claims to be paid within 24 hours.

This expectation places a huge strain on an MFI seeking to provide its members with formal funeral insurance; many insurance companies would struggle to pay claims within a week, let alone a day. Zambuko was faced with a decision to either fund claims by paying them from income while awaiting reimbursement from the insurance company, or find an alternative means of providing insurance in which the claims payment speed could be controlled. Seeking to establish an insurance carrier was not an acceptable option to Zambuko, but investigations with the local insurance companies revealed that one company would consider providing Zambuko with a PCC.

A Protected Cell transacts insurance using the host insurance company's capital and regulatory status; policies are issued in the name of the host. A management contract is drawn up between the host and the cell whereby a management fee is paid to the insurance company in recognition of the cost of capital and as a "rental" for the licence to transact insurance. The cell company is entitled to determine the terms and conditions of its products, and can therefore determine the pricing as well as the service standard. The cell transacts its own products and at the end of the year any profit or loss is the responsibility of the cell; if the products are incorrectly priced, then Zambuko could end up having to fund a loss from its loan portfolio. In most cases, the insurance company would help the cell to purchase stop-loss reinsurance so as to limit the financial downside of any underwriting loss in a given year. The establishment of a PCC requires a strong relationship between the host insurer and the cell captive; in Zimbabwe both Shadreck Mapfumo and Richard Leftley had these relationships due to work conducted earlier in their careers.

Ultimately, however, the potential for a loss arising from under pricing in an inflationary economic environment was sufficient to convince the board of Zambuko that this option was not currently viable. Zambuko will seek to launch a funeral insurance product working as an agent on behalf of a locally registered company.

6.3 Mutual Benefits Association

In the Philippines, Opportunity International serves nine MFI partners, all of which are also part of the APPEND network. As described in Section 2.4, the members of APPEND requested Opportunity International to find a suitable alternative to the "mutual aid fund", which in essence was an assisted savings scheme that paid benefits to clients upon death. As part of the product development process, corporate structures were to be addressed. At the start of the process APPEND and its members favoured creating a Mutual Benefit Association. The advantages and disadvantages of such an approach were not really fully understood, but a preliminary survey had been conducted by a local actuary into the feasibility of an MBA.

Regulations in the Philippines provide an environment where it is relatively easy to establish an MBA with reduced capitalisation requirements and favourable tax treatment. CARD has established such an MBA.⁶

Much of APPEND's enthusiasm for an MBA was grounded in the attraction of retaining the premiums generated from a large number of clients to use as a loan fund—APPEND's members currently serve over 400,000 active borrowers. In reality of course, the premiums collected from clients are required to pay for claims, as well as the cost of running the MBA operation, provisioning for reserves, and in profit sharing with all contributing members. In meetings held with APPEND and its members, these issues were discussed and in the end a decision was made to partner with a local insurance company. This arrangement would result in lower costs to clients, provide for a faster product development cycle, reduce the financial risk, and ultimately be a better outcome for APPEND. In working with a local insurance company, the details of distributing the product to clients could be worked out, and in the future the insurance carrier could be altered in line with the needs of APPEND; the future development of an MBA has therefore not been discounted.

6.4 A Stand-alone Insurance Agency

A fourth option, currently in the design stage at OI, is a stand-alone insurance agency that explores other delivery channels besides MFIs. Microfinance institutions typically focus on providing poor people with access to credit. As a result, their operational structures have evolved to become efficient at issuing loans and seeking repayment, but generally there is no mechanism for collecting money from low-income persons that are not (currently) borrowing.

For MFIs that cannot collect voluntary savings from clients, the only realistic way to collect premiums is to utilise the loan officer and hence the loan. Some MFIs load the premiums paid during the loan to offer insurance in-between loans, but this in itself brings issues because the loan resting period is seldom a uniform length of time.

By integrating insurance and credit delivery, the MFI restricts the number of clients that can be offered insurance. The scale at which an MFI can expand is limited to its branch network and access to capital to on-lend, which limits the number of loans that can be granted and hence the number of people that can access insurance. Yet demand research often reveals that many more people would like access to insurance than would want a loan.

A secondary effect of restricting insurance to those clients with an active loan is that the insurance tends to be compulsory. One way to counter this is to draw a larger number of policyholders from a much larger pool of potential clients, and the only way to do this is to expand beyond the MFI's traditional borrowing client base.

During the course of 2004, Opportunity International started work on a business model that would allow insurance to be sold to large numbers of poor people on a voluntary basis. Given the limitations of credit-led organisations for providing insurance, OI has started designing an institution that only provides microinsurance. The business plan is currently being considered

⁶ For more details about CARD MBA see McCord and Buczkowski, 2005, "CARD MBA, The Philippines," CGAP Working Group on Microinsurance Good and Bad Practices Case Study No. 4. Geneva: ILO.

by the board of Opportunity Network and if approved the new insurance agency will start to be created in the fourth quarter 2005. The new insurance agency would seek to distribute insurance via three main channels:

1. **A range of microfinance institutions:** To obtain a large volume of clients, relationships with several existing large MFIs, rural banks and co-operatives would be established to provide existing members with insurance. The MFI would be paid a commission to cover administrative costs of selling the insurance and the product development; access to AIMS software would be provided by the agency.
2. **Via other generic groups:** Flower growing unions, expatriate domestic workers, church goers and other existing groups would be targeted to sell insurance to the low-income market.
3. **Bonded sub-agents:** By bonding self-employed agents to act as a distribution channel, a large number of people that are not part of any one group can be accessed. The key to this arrangement is a cashless system possibly using premium stamps.

Such a stand-alone insurance agency could leverage Opportunity International's experience in developing insurance products as well as its existing AIMS software package to bring insurance to a large number of people. The business plan assumes that in excess of 350,000 active policies in one country would be sold within the first two years covering in excess of 2 million lives, which would allow the business to break even.

6.5 The Role of Insurance-specific Software

Regardless of the institutional arrangement, microinsurance is unlikely to succeed without an effective information system. To support its partners in their efforts to offer insurance, Opportunity has developed insurance-specific software that can be integrated with eMerge, a derivative of the Globus banking software, which is becoming the most common software platform in the OI network. Opportunity maintains a team of consultants trained in the configuration and installation of eMerge, and due to the depth and breadth of their collective experience the software vendor often seeks technical assistance from the OI-MIS team.

Since eMerge, like most other banking software, provided no functionality to administer insurance products, a team was formed to consider the various options. A detailed product specification was created that covered all aspects of the functionality required from an insurance software, and this formed the basis for a RFA that was sent to over 50 software vendors that had been pre-selected due to their existing insurance software capability. Three companies responded with quotations to build software mainly based on adjusting an existing product. Analysis of the quotations revealed that Opportunity International would be able to programme a suitable system that was compatible with eMerge for less money. The result is the "Automated Insurance Management System."

Because AIMS is integrated with eMerge, it uses the same customer information files, eliminating the need for double keying of data that applies to both the loan and the insurance policy. AIMS can be configured so that when a loan is disbursed, a record is automatically logged on the monthly report submitted to the insurance company. AIMS can also be configured to collect premiums in different ways, including automatic debit from a savings

account or deduction from a loan repayment. This has meant that the insurance premiums can be loaded into the interest rate charged on the loan. When the loan repayment is made, eMerge and AIMS work out which portion of the payment is assigned to the loan and insurance general ledgers; this all happens automatically minimising human errors. Similarly, if insurance products are packaged with different insurance companies providing different aspects of the cover (i.e., a package covering life and property with two different insurers); then AIMS calculates what percentage of the single premium is paid to each insurance company automatically and the money is moved into the correct account by the system.

At the end of the month the premium schedule can be automatically printed or emailed to the insurance company and the premium due to the insurance company can be transferred to the insurance company's account without any need for human intervention. AIMS is easily configured to include new products, terms, conditions or reporting requirements.

In the event of a claim, AIMS provides the user with the information that is required to validate if the claim. It also provides a checklist structure with increasing levels of security clearance to allow the user to determine which steps have been completed and what actions are required to process the claim.

Since many MFIs experience difficulty having branches working on-line, at the start of 2004 OI had designed a new branch utility module called eMbu, which allows branches to work off-line and be synchronised with the head office server on a regular basis by packaging and emailing the required data. The eMbu module has also facilitated the use of "Personal Data Assistants" (PDAs), whereby a loan officer can collect client information in the field and later update the on-line system. This capability was developed with assistance from the Vodafone Foundation and has wide reaching implications for microinsurance sales.

By interfacing with eMerge, insurance administration is significantly reduced, leading to cost reductions for the MFI that are essential in serving the low-income market. By automating the premium schedules, the chance for human error is eliminated and the MFI can be sure that all eligible clients have been included and the correct premiums submitted. By automating the premium collection—either by deducting from loan repayments or clients savings—the possibility for fraud is reduced since field staff do not need to handle cash.

7. Conclusions

Opportunity International's experience in offering centralised insurance expertise to a network of MFIs provides valuable lessons for the promotion of microinsurance. With access to this expertise, OI's implementing partners have developed insurance at a significant rate and in ways that would not have been possible if the MFIs were operating on their own. Insurance is specialist field, and the expertise is not widely available in the microfinance industry. By utilising this expertise, OI's partners have generally been able to access better products, better prices, and better delivery arrangements.

The OI model for providing technical assistance appears to generate significant value in the following ways:

- **Access to technical expertise:** A single MFI could probably not justify the cost of an insurance expert on its payroll. By sharing the cost of two experts over 15 MFIs, the Opportunity network has made access to expertise much more economical. Having an actuary on hand is a unique position. Insurance has its own regulations and best practices; designing products without access to expertise leads to unsustainable products that can easily breach regulations.
- **Demand-driven technical assistance:** While not specific to microinsurance, OI firmly believes that TA must be demand-driven. If its MFI partners are going to be committed to and have ownership over new products or policies, they must decide what they want and pay for it themselves (or take the lead in finding funding). Within OI, the experience thus far is that the demand for its insurance expertise far outstrips the supply.
- **A robust product development approach:** For microinsurance, the regulatory conditions and the demand vary significantly from country to country. As a result, it is not effective to promote standardised, cookie cutter products. However, a standard approach to product development provides products that are sustainable and meet the needs of the clients. OI's product development and product management process ensures that the microinsurance products are of a consistent quality.
- **Promote innovations:** By working in many countries on the same topic, a centralised TA facility can promote innovations that otherwise would not likely emerge, at least not as quickly. For example, OI is working on a number of new microinsurance products, exploring alternative institutional structures, and using new technologies to extend better insurance to more low-income households.
- **Increased negotiation capability:** Many MFIs complain that they do not speak the same language as the insurance companies. With technical assistance, MFIs can design and price their own insurance products, and level the playing field with the insurance companies. As a result, they are better placed to negotiate products that meet the needs of their clients and themselves, rather than simply generate profits for the insurers.
- **Leverage with insurers and reinsurers:** The insurance industry has its own set of networks and connections. By bringing someone from the insurance world into microfinance, he or she can leverage previous relationships and convince sceptical

insurance companies to offer products to markets that they would normally be reluctant to serve.

- **Access to insurance software:** The cost of designing and programming specific microinsurance software would be prohibitive for all but the largest MFIs. By pooling the cost of the development among many MFIs that need and are willing to pay for the development, Opportunity International has been able to design the world's first microinsurance MIS. The AIMS software greatly reduces transaction costs, human error and the possibilities for fraud, which in turn boost income and reduce the price that clients have to pay for insurance.
- **The provision of staff training:** Under the standard “partner-agent” model, the insurance company is responsible for training the MFI's operational staff. In reality, little effort is invested by the insurance company as the training is viewed as a cost (as UGAFODE's experience with AIG Uganda has demonstrated). If the MFI's employees do not understand insurance and the new insurance product, they will not be confident in selling it to clients. Staff training is a critical step in the development of insurance. Without technical assistance, this crucial step is often skipped or not given enough attention.
- **Access to industry best practice:** Few MFIs have the time to keep fully abreast with insurance best practice. Having centralised expertise that is active in the industry enables Opportunity International's MFIs to benefit from the lessons learnt from the wider industry. For example, OI's participation in the CGAP Working Group on Microinsurance has provided access to a much wider knowledge base.
- **Easier to raise funding:** Although individual MFIs may not be huge, the OI network as whole serves a sufficient volume of low-income clients that it can attract and leverage funding from both private individuals, corporations and government agencies, some of which support its efforts to promote microinsurance.

Appendix 1. Sample Market Research Questionnaire

Market Research Questionnaire

June 2005

1. What sex is the client *(please tick one box)*

Male Female

2. Describe the location of the client

Urban Rural

3. How old is the client? *(please tick one box)*

18-25 26-35 36-45 46-55 56-65 Older than 65

4. What is the value of the last loan that this client received?

LEK.....

5. How many loans has this client had from PSHM?

1 or 2 3 or 4 5 or more

6. What is the marital status of the client? *(please tick one box)*

Legally Married Commonlaw partner Widowed Divorced Seperated Single

7. Does the client have any children living at home? *(please put number in box below)*

Pre-school Junior School Senior School College

8. Does the client have other family members living at home *(please put number in box below)*

Spouse Brother / Sisters Uncles / Aunts Grand parents Parents / In-laws

9. How much money do you save for a tough day?

Less than USD 5 USD 5 USD 10 USD 10 USD 25 USD 25 USD 75 USD 75 USD 150 USD 150 More than USD 150

10. Do you currently buy any voluntary insurance? *(please tick as many boxes as apply)*

Life Property Kasko Private Pension Private Health Other.....

11. If you do not buy insurance, please indicate which of the following reason for your decision *(please tick as many boxes as apply)*

Too Expensive Too many forms Don't trust the insurer Not important to me I do not know

12. If you did buy life insurance, who should be covered? *(please tick one box)*

Just you You plus spouse You, spouse & children

13. If you had life insurance, how much should it pay upon death of the following people? *(please write a sum)*

| | | |
|--------------------------|-------------------------------------|--------------------------------|
| Upon your death LEK..... | Upon death of your spouse LEK | Upon death of a child LEK..... |
|--------------------------|-------------------------------------|--------------------------------|

14. Do you own your own your home? *(please tick one box)*

Yes, it is my house No, it belongs to me and my spouse No it belongs to my spouse No, its my parents No, I rent my house

15. If you or your spouse own the house, do you have title deeds for the house and land? *(please tick one box)*

Yes No Not sure

16. Please could you estimate the value of the belongings inside your home (furniture, TV, Cooker etc)

LEK

17. Do you own the building that you use for your business? *(please tick one box)*

Yes, I own the building I own the building with my business partner No, I rent my business location

18. If you or your spouse own your business location, do you have the title deeds?

Yes No Not sure

19. Please could you estimate the value of your business equipment (machines, computers, tools etc)

LEK

20. How much is "AFFORDABLE" for you to pay in monthly installments for insurance? *(please tick one box)*

Less than USD 2.5 USD 2.5- USD 5 USD 5 USD 10 USD10 USD15 USD 15 USD 20 More than USD20

21. Do you think that PSHM should offer insurance to its clients? *(please tick one box)*

Yes PSHM should No PSHM should not I do not mind

Thank you for your help!

Appendix 2: Sample FAQs for Staff

Adapted from “Life insurance operations manual, TSKI”

When will microinsurance start?

During a meeting held with area managers, department heads and the ED it was decided that microinsurance would start on the 1st February 2005 as this will provide staff with sufficient time to advise all clients about the new products features. Therefore, from the 1st February 2005 all loans that are released will have microinsurance and any MAF balance outstanding will be refunded to the centre on the day that the loan is released following 1st February 2005.

For those loans that are still active on the 1st February 2005, clients will remain with MAF until the loans reach the maturity date and then microinsurance will be introduced to the next loan. This means that by 31st July, MAF will no longer exist, as all loans that have MAF will have matured by the end of July 2005. Between 1st February 2005 and 31st July 2005 the number of clients participating in MAF will reduce as clients come to the end of their loans and take new loans with microinsurance instead of MAF. As a result, the MAF benefits will also reduce and in light of this it is recommended that any loan that is being made toward the end of January be delayed until February so that the clients can avail of microinsurance (only in consultation with the centre).

For new centres that are currently being formed and are getting ready to receive their first loan in January, the microinsurance will be available from the 1st January 2005. For these new centres, microinsurance will be applied to all loans from 1st January 2005.

What about individual loan clients?

The microinsurance product will ONLY apply to those clients with a group loan and it will NOT apply to those clients with an individual loan.

What about the use of marriage certificates?

Clients are no longer required to submit copies of their marriage certificates during the loan application process, as Cocolife does not require them. However, if clients wish to include their spouse on the insurance application form, then TSKI requires that clients present the marriage certificate to the programme assistant (PA) during the loan application process.

It is TSKI’s policy that clients will not be able to register their “live-in partners” for benefits under the new microinsurance product. For a client to register the spouse, they must be legally married. A copy of the marriage certificate should NOT be submitted with the application for—it is sufficient for the PA to see the copy in the field.

What about missing persons?

If someone is missing and assumed to be dead (but no death certificate can be issued), then the claimant should try and get a police report concerning the known facts. The claim should then be referred to Cocolife for a decision regarding payment. If Cocolife agree to pay the

claim, then the claimant can be paid, but the decision to pay or decline the claim should not be taken by TSKI.

What about “surrogate parents”?

Some staff asked if a client could cover their Surrogate Parents (i.e., their adopted non-biological parents). After checking with Cocolife it has been confirmed that non-biological parents can ONLY be included under the microinsurance if they legally adopted the client and they can prove this with necessary documentation.

Can clients cover more than three children?

Some staff suggested that some clients would be interested in including more than the maximum of three children, and in return would pay additional premium. It has been decided that TSKI will start by restricting clients to a MAXIMUM of three children and if in the future there proves to be demand from clients to increase this number of children then a change may be considered.

Therefore please educate clients and staff that the maximum number of children that can be included is limited to THREE ONLY.

Single clients – parents or children included?

If a client has any children, then she must cover the eligible children (up to a maximum of three). She cannot choose to cover her parents instead of her children. The ONLY clients that are allowed to cover their parents are single clients that do not have children.

Can staff have microinsurance?

Some staff members have asked if they are allowed to purchase microinsurance. It has been decided that staff will NOT be allowed to purchase microinsurance because if they are allowed too, then all members of staff will have to purchase insurance. The staff MAF will continue to operate for all members of staff.

Can illegitimate clients be included?

Children that are born outside of legal marriage (i.e., they are illegitimate) can be included under microinsurance as long as they share the same family name as the client of TSKI. Illegitimate children that have a different family name from the TSKI client cannot be included under microinsurance.

What about children from previous marriages?

Sometimes a TSKI client may have children from two marriages. For example, a client has a child from an earlier marriage with a different family name from her other children. These children with different family names can be included under the microinsurance as long as there is documentation that will prove the children are biological children of the client.

What are the benefits of microinsurance over MAF?

During the training, some PAs asked for clarification of the benefits of the microinsurance over the existing MAF product. They asked this question, as they were concerned that their clients would ask this difficult question. It is important to recognise that any change to the products offered by TSKI would be questioned as people always resist change. It is very likely that clients will resist the change from MAF to microinsurance in the first few months

until they become used to the new product. It is true that some features of microinsurance are better and some are worse than the MAF product. However, overall microinsurance is an improvement over the MAF that it replaces and it is important to highlight its benefits over MAF to clients and staff. The benefits are as follows:

1. The value of the claims paid to clients under microinsurance is much higher than for MAF.
2. Unlike MAF, microinsurance claims are for a fixed amount and so clients know the benefits they will receive before a death occurs.
3. Microinsurance will require less administration. Clients will not have to supply birth certificates and other documents unless someone dies.
4. Due to the reduced administration involved in making a claim, it should prove to be possible to pay benefits to clients more quickly than experienced with MAF.
5. Unlike MAF, microinsurance does not have contestability for existing illness. This is a significant benefit to clients with existing illness.
6. Microinsurance benefits are paid even when a client is in arrears. This means that when a sick client that has become delinquent dies, her claim will be paid.
7. Claims arising from suicide in the second year and beyond will also be paid by microinsurance, which is a benefit to those clients that have family members that die from suicide.
8. Microinsurance will pay significant benefits to clients following disasters where more than one family member is affected.
9. Finally, TSKI needs to make this change to ensure its long-term health and those clients that have a long-term interest in TSKI should support this change.

How is the premium calculated?

Please find below the possible premium combinations for the TSKI microinsurance product. Please have PAs use this matrix in the field to assist in the calculation of premium due from clients. PAs should NOT provide clients with the premium calculation equations.

| Client | Spouse | Children | Parents | Sum insured | Premium Due |
|--------|--------|----------|---------|-------------|-------------|
| 1 | | | | P100,000 | P196 |
| 1 | | | 1 | P125,000 | P223 |
| 1 | | | 2 | P150,000 | P249 |
| 1 | | 1 | | P125,000 | P223 |
| 1 | | 2 | | P150,000 | P249 |
| 1 | | 3 | | P175,000 | P276 |
| 1 | 1 | 1 | | P175,000 | P276 |
| 1 | 1 | 2 | | P200,000 | P303 |
| 1 | 1 | 3 | | P225,000 | P329 |