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making financial sense of the future

UK Launch of the Actuarial Training Modules for Microinsurance
Microinsurance Member Interest Group
Lisa Morgan



An Introduction to Microinsurance

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An Introduction to Microinsurance

Agenda

- **What is Microinsurance?**
- Characteristics of low-income market
- Challenges and key considerations
- The role of the actuary in microinsurance

What is Microinsurance?

IAIS definition

- Not a specific product or product line
- Not limited to a specific provider type
- Provision of cover to a specific market segment
- i.e. “**low-income persons.**”
 - ~ *IAIS Issues Paper (2007)*



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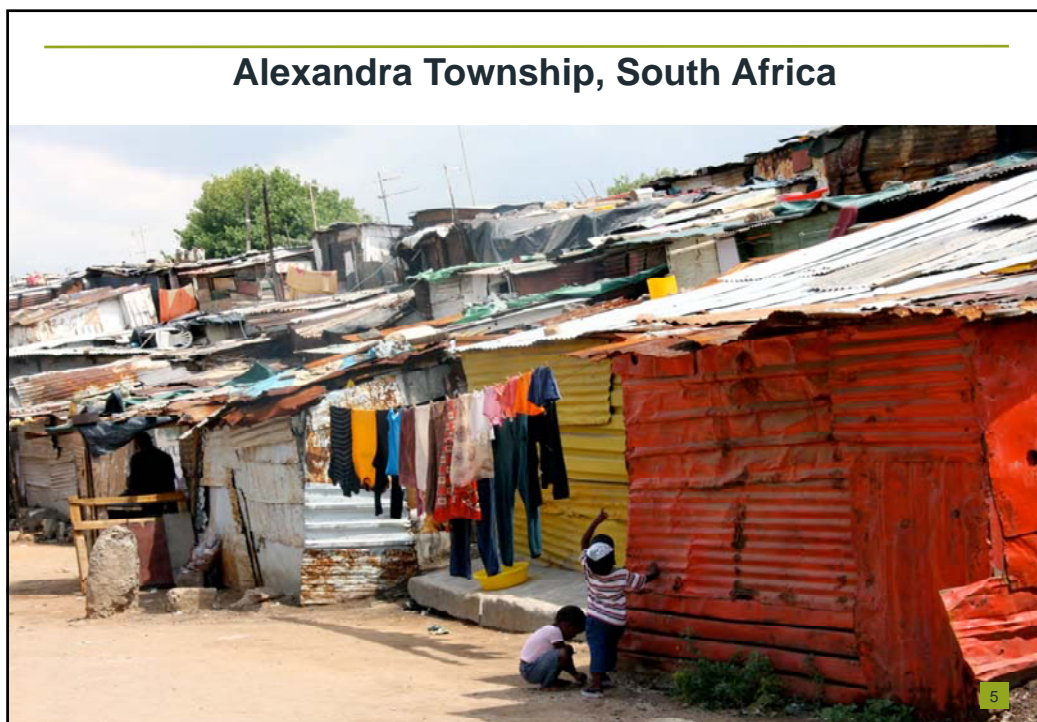
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Microinsurance Defined

- “.... ***mechanism*** to protect poor people against risk.... in exchange for....payments ***tailored to their needs, income & level of risk***”
- Aimed (primarily at ***developing***) world’s ***low income workers***, especially those in ***informal economy.... ignored by mainstream....***”

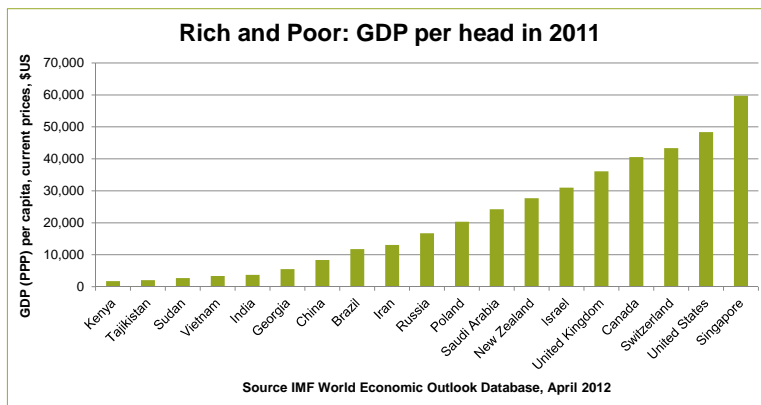
ILO, Microinsurance Innovation Facility (2010)

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GDP Per Capita, Current Prices, US\$

- But how low is “low-income”? No hard and fast rule.



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How many people are there in the world?

7 billion

Let's just assume that **LOW-INCOME**
means living on
less than US\$10 (~ £6) a day
in local purchasing power

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How many of the 7bn live on low incomes?

Up to 80%
= 5.6 billion
live on less than US\$10 a day
... *Microinsurance target market*
within this

43% of the world's population lived on less than US\$2 in 2008

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Reasons for Microinsurance

- **Humanitarian reasons** – United Nations (International Labour Organization), World Bank, Oxfam America etc. wish to alleviate global poverty using microinsurance
- **Commercial reasons** – many see the potential for profit (small margin, large volume business)
- **Organically developed** – workers unions wish to protect their members
- Penetration in 2011 – around **3%** of world's poor

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Being poor is risky

'One of the least remarked-on problems of living on two dollars a day is that you don't literally get that amount each day. The two dollars a day is just an average over time. You make more on some days, less on others, and often get no income at all.'

'How do you make sure there is something to eat and drink every day, and not just on the days you earn? If that seems hard enough, how do you deal with emergencies?'

Portfolios of the Poor, Collins et al. (2009)

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Characteristics of low-income market

- Often work in informal economy
- Irregular cash flows, not always banked
- May not have a bank account
- Manage risks through number of informal means, including social networks
- Have short-term planning horizons

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Characteristics of low-income market

- Limited familiarity with formal insurance
- Don't understand how insurance works or compares to other risk-management tools (e.g. savings)
- Often don't trust insurance companies – suspicious of motives

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Characteristics of low-income market

- May believe insurance only for rich
- Vulnerable to risks, much more so than middle/high-income earners
- May need to rely on social security, often inadequate
- Significant low-income populations in developing countries

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What risks do low-income earners face?

Risks

Death
Illness
Accidents
Loss of assets
Business
Unemployment

Economic stresses

Wedding
Ceremonies
Child birth
Education
Paying rent, utilities



Cycle of vulnerability & poverty

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Challenges of serving the low-income market

Design, Pricing & Monitoring

- Commercial insurance definitions may be n/a
e.g. definition of a household
 - Difficult to accurately set price & benefit level
 - Poor data or lack of data for pricing
- So designs need to be kept simple

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Challenges of serving the low-income market

Design, Pricing & Monitoring

- Difficulty in recording member & claims information, &
...so experience monitoring may be difficult
- Coping with huge volumes of small policies

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Challenges of serving the low-income market

Launch & Benefit Delivery - the Practical Issues

- Collecting premiums when members don't have bank accounts
- Volatile income (may default on premiums)
- Verifying and paying small claims
- Controlling Fraud (member & provider)
- Moral hazard
- Adverse selection

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Challenges of serving the low-income market

Launch & Benefit Delivery - the Practical Issues

- Distribution issues
- Potential lack of infrastructure & **expertise** in developing country context
- Overcoming scepticism/negativity
- Communication – initial & continuing – no postal system, email etc.

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Challenges of serving the low-income market

- Cost of benefits may be high...
 - so may need to negotiate significant discounts, involve aid organisations & governments...not always sustainable
- Overcoming expectations: all risks covered
- Lack of coordination & alignment of incentives of various stakeholders

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Challenges

Example: Healthcare Microinsurance

- Insufficient facilities & lack of qualified doctors, nurses etc.
 - Developing world is net exporter of medical professionals
- Often, high rates of illness & the complexities of co morbidities (e.g. HIV/AIDS, TB, malaria, etc.)
 - Expected frequency of illness high

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The microinsurance context

- The client base:
 - has limited insurance knowledge
 - has very limited financial resources
 - is untrusting of insurance
 - is reached via new distributions methods
- Products need to
 - meet the clients' unique risk needs
 - be simple and understandable
 - be affordable
 - have an easy claims process
 - be as inclusive as possible

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The microinsurance context

- Exclusions
 - Microinsurance is more inclusive – “if in doubt, pay”
 - Cost of monitoring and enforcing complex exclusions must be weighed against the claims avoided
 - Microinsurance small premiums and claim amounts cannot support large screening costs

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The microinsurance context

- Efficient operations are essential
- Requires very low operation costs
- Technology usage is limited, however advanced solutions are available

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The microinsurance context

- To be sustainable:
 - Reach a large number of clients
 - Very low premiums
 - Be efficient

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Role of the Actuary

- Review Pricing, Reserves and Product Design:
 - Well-priced product
 - Ensure there is good value for the premium being paid
 - Affordable for the clients

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Role of the Actuary

- Operations
 - Effective distribution
 - Efficient processes
 - Lowering expenses
 - Administrative procedures
 - Claims processing
 - Controls
 - Technology (MIS)

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Role of the Actuary

- Review of Financial Statements
 - Claims Analysis
 - Performance Indicators
 - Balance sheet
 - Income Statement
 - Asset/Liability Matching

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Overall, ask...

- Do potential customers understand and value insurance benefits?
- Good client value – does the product meets client needs at an affordable price?
- Good economic value – is the product returning as much premium as possible to client while remaining viable and providing good service levels? An Innovative product design is required to minimise expenses and transaction costs on a per policy basis

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Thank you!

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