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# Microinsurance in Africa: Enabling Development through Risk Reduction

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### Introduction

This is a summary of a roundtable meeting held by the Africa Programme at Chatham House to discuss the challenges and opportunities of the emerging African microinsurance sector. The meeting heard from Aparna Dalal and Pranav Prashad, both technical officers at the International Labour Organization (ILO), and from Japh Olende, head of American International Group (AIG) in East Africa. The meeting was then opened to questions and discussion.

The meeting and the question and answers session were held on the record, and the views expressed are those of the participants. The following summary is intended to serve as an aide-memoire for those who took part, and to provide a general summary of discussions for those who did not.

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### Aparna Dalal

Dalal described the role that insurance can play in the complex financial lives of low-income households. Over the last six years, the ILO's Impact Insurance Facility has helped more than 60 partners to design insurance products that offer better access and value to low-income households. Recently the ILO commissioned work examining risk in 300 Kenyan households using a financial diaries methodology. Examples from these diaries were used to illustrate a more aggregated picture of the financial lives of low-income households.

One example is Patrick, living outside Nairobi with five sources of income (selling ice cream, making cooking grills, mending cooking pots, buying and selling scrap metals, and recycling empty bottles and cans). His cash-flow chart on any given week varied from \$0.50 to \$10, as did his expenses. Unlike the incomes of salaried workers, which are stable, the incomes of micro-entrepreneurs like Patrick fluctuate a lot and are unpredictable. The same applies to their expenses. Patrick used nine different financial instruments, both formal (such as M-Pesa) and informal (such as borrowing from creditors, friends and family), in order to plan for the future and to maintain short-term liquidity.

In Europe, most workers have regular and orderly cash flows, receiving a salary on a regular basis which is allocated to savings, mortgage payments and investment. Decisions on such allocations are made on an infrequent basis: for example, a European worker's spending portfolio may be reallocated every six months or every year. Financial analysis skills are used when making these decisions. In low-income households, by contrast, financial decisions are made continuously and are exhausting. There is a constant struggle to balance the management of risk and the maintenance of liquidity, but this is where insurance plays a role. The challenge is to educate households about insurance, because there is a general perception that insurance is an investment in the future – rather than something that can be used for immediate needs. Cash flows in low-income households are infrequent, irregular and unpredictable, and financial decisions are smaller but are made many times a day. In such resource-constrained environments, any decision can have long-term implications.

Insurance products and processes must therefore make it easy to make good decisions. Decisions can be automatic, or bundled with other financial or non-financial services. People living in resource-constrained environments experience scarcity of both time and resources, which makes it much harder to plan for the future. The challenge is how to offer insurance in a way that makes it easier to make sound financial decisions.

The role of social financing and social network financing is significant for low-income households. The evidence from the financial diaries was that loans from friends and family were the prime resource used for mitigating risks to health, life and theft. Social network financing can be very powerful because it is new money. It differs from savings and credit, which are borrowed from the future to pay for present needs (or vice versa). In addition, the pool of money available from the social network is much larger than what an individual household can procure alone. Money from a social network is not tied to specific needs, and is therefore more flexible than an insurance product.

But there are limitations, including that financing from a social network is not immediate. Additionally, not everyone has friends and relations with resources on which they can draw. Women have stronger social networks, than men and rural families have better social networks than urban families. Social network funding necessitates a very public showcasing of needs, and so may be better suited to certain risks rather than to others. One example from the financial diaries showed the limitations of the social network as an effective source of funding. Isaac's wife had a medical condition requiring surgery that would cost \$260. Because the family could not afford this, they used traditional medicines but these did not prevent her death. Social network funding provided Isaac with \$370 in cash to pay for the funeral.

Credit, savings and insurance have tended to be siloed as a result of rhetoric that maintains that savings are used for aiding consumption, credit for investment, and insurance for risk. This does not hold true for low-income households. The M-Shwari loan can be obtained through a mobile phone in Kenya, and is rated as the best way to manage risk despite being a credit product. There are also African examples of insurance being bundled with credit to boost investment. Low-income households use these tools in very creative ways.

Insurance can make four distinct contributions to low-income households:

- 1) Insurance reduces vulnerability by helping households to develop medium- and high-stress coping mechanisms.
- 2) Insurance facilitates higher investment in education and production, as it permits households to increase their productive capacity. This has been observed among farmers with access to agricultural insurance, which allows them to invest more in fertilizer and in high-risk, high-return crops.
- 3) Insurance improves efficiency by providing cover for more risks, or for multiple risks through a single product. However, ILO partners have found it very difficult to offer and administer such products. Four out of the five partners that tried composite products were not able to scale up.
- 4) Insurance provides benefits in the near term, and is not just an investment in the future. Value-added services that can be offered with insurance products could make the benefits to households more tangible.

Health insurance is one example of a value-added service. Useful services could include the provision of health tips, or access to telemedicine. The ways in which insurance products can complement such services requires further investigation. Many governments in Africa are using national health insurance schemes. The private sector could play a role within these schemes by helping governments to cover risks and by providing more cost-effective distribution of national health insurance.

There is a crucial need to understand that insurance has added value as a risk-mitigation mechanism, because it can aid increased production and can provide access to other services. There are real behavioural constraints arising from the environment of low-income households that affect both demand and use. Principles from behavioural economics could be utilized to address these constraints and prevent

obstacles to action. Such realities have real design implications for products and services, and there is a need for greater creativity in forming the right partnerships and in understanding client perspectives – a critical factor for viability and profitability.

### Pranav Prashad

A holistic viewpoint is required in order to understand the role of insurance. The protective use of insurance is much discussed, and impact studies have supported this use – finding that insurance can provide individuals with lower risk coping mechanisms. Studies of a livestock insurance programme in Kenya showed that the number of individuals responding to drought by selling their assets fell by 29 per cent. Insurance also has a productive use. In Ghana, for example, insured farmers have been found to increase fertilizer use, to plant better seeds, and to engage in riskier, more rewarding agriculture.

Lack of awareness about insurance is an issue globally, not only in Africa, but various initiatives are under way that could also improve the current status of insurance in Africa. These include community-driven mechanisms that involve combining risks, although these have shown limited ability to scale. Financial institutions play an important role in communicating what insurance can do. Microfinance institutions remain important, not only because they provide credit to the customers and are in closer contact with customers on a financial services basis, but also because they provide a local context. They therefore have huge potential to build community trust about insurance. There is a strong case for using financial services to back up insurance, because on its own insurance has challenges.

In addition, banks are increasingly important to the promotion of insurance in Africa. Kenya's Equity Bank set up an insurance agency, and has begun to distribute insurance products targeted at the agricultural community. One such focuses on pastoralists, and relies on satellites to determine grassland availability. This in turn can determine the likelihood of cattle surviving and thereby be used for claims in cases of drought.

Growth in technology has contributed to the huge impact of mobile phones on insurance. Mobile phones can be used across the entire value chain. Given the ease with which people can transact via phone, mobiles are becoming tools for distribution as well as for settling insurance claims. The Kenyan initiative Kilimo Salama is a prime example of mobiles being used for enrolment purposes, enabling a quick answer for insurance applicants. Mobile phones are also useful in financial dealings and in the payment of premiums.

Mobile technology is also useful for insured farmers seeking to access data from automated weather stations, and for insurance providers to communicate updates pertinent to the index-based products designed for agriculture-related insurance. Moreover, services providing agricultural advice, including on the best timing to sow seeds, are utilized by insurance providers to encourage farmers to renew their policies and remain insured.

Aggregation is important for improving scale and efficiencies within financial systems. Microfinance institutions have been described as a 'sell-through' mechanism for farmers, but they can also act as a 'sell-to' mechanism. Certain cotton associations in Mozambique buy insurance cover for their farmers, of which there are about 43,000, and also finance their premiums. Facilitative regulatory mechanisms could be built around aggregate organizations that would enable them to distribute insurance. In Senegal the national agricultural insurance company has supported data suppliers, meteorological organizations and insurers to create products and deal directly with farmers. After three years, the number of Senegalese farmers receiving coverage through this scheme rose from 73 to 7,000. This is a good example of a public-

private partnership where both regulatory and government bodies understand the benefit of collaboration. In Ethiopia the R4 Rural Resilience Initiative, a joint World Food Programme and Oxfam America resilience initiative, permits individuals to pay their insurance premiums through labour ('insurance for work'). The programme has now been extended to Senegal.

Technology continues to play an important role in all of these programmes. Mobile phones and the distribution networks these create play an important role. In some countries, outlets selling mobile phone chargers are being trained also to sell insurance. With such uses of technology and distribution channels, and government playing an increasing role, it seems the ground is being set for financial services to take a central role in the decision-making processes of low-income households.

### Japh Olende

In East Africa microinsurance is relatively new. Uganda was the pioneer of microinsurance in the region: insurance companies in Uganda began their involvement in 1990. The microinsurance sector in East Africa is less developed than in West Africa, or South Africa. Prominent microinsurance products in East Africa are linked to health, property, agriculture, livestock – particularly cattle – and personal accidents.

There are about 150 microfinance companies in Kenya; these work with a range of partners including mobile phone companies, banks, cooperative societies, NGOs, community-based organizations and welfare associations. Credit Bank is one of the longest-established providers of microfinance in Kenya, followed by Equity Bank. These initial microinsurance providers were intended to principally protect the credit business, which at the outset focused on low-income workers. Micro-lending propelled the two institutions to become two of the largest commercial banks in Kenya, but the microinsurance that they initiated has not grown at the same pace as the banking business.

In addition to the commercial insurance companies that largely drive the microinsurance sector in East Africa, there are notable partners such as Kenya's National Hospital Insurance Fund (NHIF). The NHIF is one of the most successful recent microinsurance initiatives in Kenya, providing composite health insurance to the formal workforce, and there are plans to extend its provision to the informal sector. Legislation was recently introduced to increase contributions to the NHIF; when implemented, this will make the NHIF one of the largest microinsurance players in the region.

The slow pace of microinsurance growth in Kenya, and in East Africa in general, is attributed to a lack of knowledge of the products among the general population. There is also a lack of trust in insurance companies, few appropriate payment platforms or appropriate IT systems to manage the business of microinsurance, and a lack of clear regulation.

Additionally, distribution channels have largely focused on using insurance to grow their core business. Across East Africa, donor-funded micro-lending organizations introduced microfinance in the region with some success. Whilst these organizations put Kenya, Tanzania and Uganda on the microinsurance map, they have continued to encounter challenges in expanding their business. Mobile phone technology has been used to sell health insurance, but with minimal success. It presents a big opportunity for profitable growth, particularly as mobile phone operators have seen similar growth in voice, data and money transfer. The operators do not, however, appreciate the value of microinsurance.

Although microinsurance growth has been slow in Kenya, it has significant potential due to the large number of low income earners in the country. There is potential to reach some 1.4 million formally

employed, low-income people, and for microfinance companies and cooperative societies to help cross-sell to about 3.9 million people.

Kenyan welfare societies have about 4 million adult members, but these societies do not provide any form of insurance. As many welfare societies are now unable to meet some costs such as funeral expenses, they are well-placed to grow microinsurance. Trade unions also have thousands of members who remain uninsured, and this presents a big opportunity for microinsurance.

Microinsurance regulation has been a primary issue in East Africa. The ILO and other development partners helped to install a policy framework in Kenya, and there is now an act that recognizes microinsurance as a line of business. The same initiative has been adopted in Uganda, and it is believed that this development will enable a growth in microinsurance, as in the past it was unclear how commercial insurance related to microinsurance.

Innovation will ensure the success of microinsurance, and will protect policyholders and their beneficiaries. In Kenya, for example, only 7 per cent of the population are insured. Innovation in microinsurance could help overcome the barriers to attracting the population.

The development of mobile phone technology and mobile money can also aid the expansion of microinsurance. In Kenya there are some 2 million mobile money users, mainly through M-Pesa. Mobile phones are being used to market products, for publicizing new products and new ideas, and to send information and documents to existing and potential customers. Mobiles are also used to make payments and claims.

A few insurance companies have partnered with mobile phone operators in social health and accident insurance, but with limited success. Insurance providers need to better engage with mobile phone companies to provide incentives that build the mobile phone companies' appreciation of microinsurance's ability to expand their business among the poorer population, while also providing them with the opportunity to engage in corporate social responsibility. Not only does mobile phone technology make it easy to reach large numbers of low-income earners, but it can also be useful for education, marketing and other forms of payments.

Risk management is an area of innovation that can make businesses more attractive to investors. For example, index insurance products can manage risk associated with climate change. Product diversification is also in need of innovation, as many products on the East African market do not adequately address the needs of customers. There is a need for improved microinsurance-specific systems that help to reduce the cost of doing business, provide efficient processes and improve the delivery of microinsurance products, especially through non-traditional channels.

Microinsurance can inform business development strategies. Research shows that microinsurance has big potential, with the sector expected to grow at a rate of 10 per cent annually. In Africa there are potentially some 700 million microinsurance customers, with only around 15 million currently insured. Returns from microinsurance have been modest, but by overcoming some of the challenges outlined microinsurance could form a significant part of the overall premiums of the insurance industry.

Microinsurance has both profit and welfare motives which are important for any country's economic development plan. There has been increased investment by both insurance companies and development partners in the area of microinsurance. For example, some of the big international insurance firms have partnered to develop a company called Microinsurance Incubator. This is a major investment that will

attract funds, resources and technology for innovation in microinsurance, demonstrating how microinsurance can be a big player in the overall expansion of the insurance industry.

Microinsurance has provided insurance firms with the opportunity to develop innovative new policies which in turn help them build their brands. The potential of today's low-income earners to be the middle class of tomorrow will drive growth in the insurance business, and makes microinsurance even more attractive. Microinsurance stops families from eroding their assets in the event of a calamity, thereby aiding economic development. Microinsurance is also important for agriculture, as it helps rural populations feed their families.

Insurance forms part of Kenya's development plan, Vision 2030, and microinsurance has been incorporated into this plan. The government, industry and development partners can all play a role in promoting microinsurance. Governments should develop policies and enhance insurance and banking regulations to facilitate the development of microinsurance. The insurance industry can be an important ally in promoting access to vital services and making communities more resilient to climate change. Development partners and industry should also provide technical input and share their experience in order to ensure that the right policies for microinsurance are introduced. Understanding the interest of delivery channels, and aligning them to other stakeholders to create scale, is a very important aspect of any policy to grow microinsurance.

Capacity-building by development partners is key. The World Bank, the Bill & Melinda Gates Foundation and the ILO have led such efforts. Governments can enact laws that enhance the performance of health facilities by encouraging businesses to provide room for the growth of health insurance as a product of microinsurance. Governments should introduce policies that reduce the cost of agricultural input, thereby easing access to markets which could then provide an opportunity to develop microinsurance in rural areas.

Governments, development partners and the insurance industry play an important role in promoting the growth of microinsurance. Governments have a vital role, as they can enact laws to promote education on microinsurance. Governments could even develop curriculums specific to microinsurance that could be taught in primary and secondary schools. The insurance industry should share its experience, and highlight the challenges in microinsurance to help shape policy formation in the development of microinsurance. Policy-makers, regulators and supervisors can achieve policy objectives by drawing on the experience of private insurers, including situations where they have failed or succeeded, and where they see potential.

## Summary of Questions and Answers

### Questions

Is price elasticity in direct conflict with the bundling of insurance with other products? Institutions that are able to bundle also seek to maximize their existing profitability. How can insurance premiums fit into that framework?

Challenges to microinsurance include buy-in, trust and knowledge of the products. It is yet to be identified how to maintain clients' understanding of insurance products while using mobile operators to achieve scale. Additionally challenging is getting mobile money operators to explain products so that clients' trust expands and they feel secure in repurchasing insurance.

### **Aparna Dalal**

Using a 'low-touch' mechanism such as a mobile phone to sell insurance is a challenge. Companies have been starting with simpler products, such as a life product or a hospital cash product, which is easier for clients to understand. The idea is to have very few nuances in the product and to emphasize those as part of the marketing strategy. For example, the ILO is working with a partner in Ghana on a product that offers life, personal accident and hospital cash. To qualify for payout under the hospital cash component, a client must spend at least three days in hospital, and this is driven by the pricing of the product. However issues have arisen in communicating the three-day stipulation to clients, and this experience demonstrates how crucial it is to address potential areas of confusion. It is also very difficult for people to test insurance to see if it works, while a mobile money transaction, for example, can be tested. Claims processes must be made clear, and payouts should be based on stipulated time frames that are adhered to. This is important in building trust.

### **Pranav Prashad**

With insurance, users have to lose before they gain. This makes the issue of client communication extremely important, especially when technology is used in remote places. One product introduced in Ghana utilized mobile network operators and their distribution channels. It included mobile network operators' agents who were trained to explain insurance products to customers; 89 per cent of clients claimed to understand the product, and 94 per cent of them were first time users of insurance. Conversely, U Mobile sold exactly the same product in Kenya, but information about it was communicated entirely over the phone, with users even registering by phone. In this case, 46 per cent of the clients in Kenya failed to complete the registration process, and 67 per cent did not understand the product.

There have been experiments where all aspects of mobile technology have been tested for the benefits they may bring. For example, in India entire training programmes have been made available through mobile phones, based on posing simple questions to test clients' understanding of an insurance product. If clients answer incorrectly, they must restart the enrolment process.

There are several ways of bundling insurance with other financial services. Customers often buy insurance alongside a loan. A financial institution could pay for the premium, but this raises concerns about how much value is being transferred to the client. Until customers pay, they often do not know they have an insurance product because it has been bundled. This continues to be a challenge, but it can be overcome if products are priced to cover the most likely risks so that customers begin to understand how insurance works.

A number of studies have found that people are willing to pay despite their income level. In focus group discussions, about 80 per cent of people said that if an insurance product were available to them, then they would buy it. Insurance can be bundled with financial services for a small price addition, or with non-financial services such as annual weather forecasts. However, elasticity remains an issue, and there is little consensus over how to value the life of an individual or the effort deployed in agriculture. If insurance can be bundled with services, education and awareness, it can be sold more effectively.

### **Japh Olende**

The cost of using mobiles for microinsurance in East Africa has been a challenge, because mobile data is a competitive market for phone companies and they do not always want to add insurance that could make

them uncompetitive. For a long time, companies did not work on bundling insurance products for this reason, but phone companies are beginning to become more receptive to provision of insurance. Because mobile companies are established brands, this addresses the issue of trust. People will buy insurance products if they are bundled properly, and so establishing the right product is essential.

### Questions

Are there opportunities for UK-based diaspora communities to buy microinsurance cover for their families in Africa?

What challenges arise from US and UK legislation that might prevent a large international insurance company from partnering with an East African one? How can microinsurance provide for the millions of Africans who remain excluded from official financial systems?

Why is microinsurance better than microfinance?

### Japh Olende

In Kenya there has been significant focus on the diaspora. The diaspora needs some form of insurance to cover the events that they usually pay for – including healthcare and funerals. There is not yet an insurance product catering to this diaspora, but two insurance companies have made advances in developing one. Insurance companies face difficulty in bundling savings with insurance for funerals and healthcare. The size and power of diaspora communities in a number of African and Asian countries means that an innovative insurance product catering to this market would have huge potential in promoting microinsurance.

Recent pushes for insurance companies to gather more information about their clients, known as ‘know your customer’ regulations, are a result of international legislation.

### Pranav Prashad

Companies on the ground run a balancing act while trying to ensure that they follow ‘know your customer’ regulations. There has been more innovation in microinsurance claims than in enrolment to microinsurance initiatives. For example, to issue micro-life insurance claims in remote areas where there are no facilities to carry out post-mortem reports, a certificate from the village head is considered valid.

It is important to foster cooperation, not competition, between microinsurance and microfinance –both of which are necessary to improve the livelihoods of rural communities. A study in Bangladesh found that 34 per cent of people who were helped to emerge from poverty through microcredit schemes fell back into poverty because of health and economic shocks. Grameen Bank has begun to sell microinsurance products because of an appreciation that microinsurance has a complementary part to play alongside microcredit.

### Aparna Dalal

Remittance-linked insurance cover is a tremendous opportunity, but is faced with significant challenges. Insurers would have to identify whether the product covers those receiving the remittance, and whether therefore it could be sold to the diaspora. It would be difficult to do if, for example, a Haitian company aimed to sell a remittance microinsurance product to the Haitian diaspora in the US. In addition, the

product would be very difficult to sell if it was not part of a bundle with remittance transfer services. The selling model for such microinsurance would pose a problem.

The positive effects of microinsurance are understated, but the microinsurance industry can implement innovations faster than has been the case for the microcredit industry. Microcredit had to create supply-side innovation through group lending, which has become popular in a number of countries. As a result of operational challenges, microinsurance has not taken off at the same level. Impact assessments are being conducted where microinsurance has been rolled out, with insurers aiming to prove its effectiveness while also improving operations. The dynamic in the microinsurance industry is different, meaning that the focus has been placed on client satisfaction more centrally than within the microcredit industry.

### **Question**

What role does the diaspora play in buying microinsurance products?

### **Aparna Dalal**

The diaspora has a higher willingness and means to pay for microinsurance, because they take risk in transferring money. However, operational challenges to microinsurance for the diaspora remain.

### **Questions**

What role could microinsurance play in assisting those whose agricultural livelihoods have been damaged by Ebola, and in building faith in healthcare systems of West African countries during their initial post-Ebola recovery?

What would give companies the confidence to invest in microinsurance in Liberia, Sierra Leone and Guinea?

Will microinsurance become internalized within existing insurance and microfinance institutions, or will a specific microinsurance sector emerge?

### **Aparna Dalal**

Clients do not see a separation between the healthcare they receive and the insurance product they have bought. If healthcare is poor, the clients are unlikely to buy the insurance again, regardless of its price or whether the insurance company paid the claim on time. Insurance is unlikely to improve trust in a healthcare system.

It would be positive to see innovations continuing both within the insurance sector and in a separate microinsurance sector. Insurers will likely play a much more substantial role in microinsurance than traditional banks did in microfinance. This is because of the specialized expertise needed for insurance, and also because the profitability horizons for insurance products are much longer and require the involvement of companies that can commit to low profits for up to 10 years.

### **Pranav Prashad**

Governments face a dilemma over whether to improve healthcare or financial services first. Healthcare systems need to be strong enough to be supported by other financial services, but this requires time. In a few cases, insurance has provided some partial relief to agricultural livelihoods.

It is likely that commercial insurance companies will engage in microinsurance as part of their existing business, but this is not corporate social responsibility. In India the largest agricultural/rural microinsurance initiative is run by the country's largest insurance company. In this example, a private insurance company launched an index insurance product that was later taken over by the government. It has now evolved into a programme involving over 25 million customers.

### **Japh Olende**

As microinsurance is still a form of insurance, the capital behind it will always be provided by commercial insurance companies.

### **Question**

Is there enough in-depth understanding of insurance in Africa?

### **Japh Olende**

Insurance is less understood in Africa, and therefore governments and development partners need to play a role. Because of the gap in the general public's understanding, insurance companies are seeking out anchor brands, such as established microfinance companies, to reach the population. Governments can invest more in education and make the best use of mobile phones for this end. Development partners should also help with this.

### **Question**

Do insurance companies only provide communication about their products in English?

### **Japh Olende**

In most countries in Africa and Asia insurance for the general population has been translated into local languages. In Kenya information on insurance is provided in Kiswahili, but not in the other 42 languages and dialects spoken in the country.

### **Pranav Prashad**

Insurance companies are also working harder to hire sales teams from local communities, in order to get those most familiar with particular areas to sell to the local population.