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Microinsurance NOTE 4

Product Development—Making Microinsurance Products Successful

A critical prerequisite to the success of any new product is following a systematic new product development process. The microinsurance product development process is continuous and designed to ensure that appropriate products get delivered to the market in an effective manner and are monitored for potential improvements. Every step is informed by the needs and abilities of the low-income consumers, the activities of the competition, and the capacity and objectives of the institutions offering the microinsurance product. It is imperative that the product also fit the needs of the institutions (insurers and delivery channels) that offer it.

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A critical prerequisite to the success of any new product is following a systematic new product development process.¹ This is true of microcredit and microsavings, and it is especially true of microinsurance. In almost every low-income country microinsurance starts in an environment where people either do not understand insurance or have a negative attitude towards it from seeing poor results in the past. Introduction of products into that atmosphere requires that products and processes are right for that market. A systematic new product development process helps to:

- Tailor products for wide scale offer that clearly respond to the market's needs
- Prepare institutions to effectively offer the products, and educate the market
- Minimize the potential for failure of the new product, where product problems can have a strong negative impact on intangible insurance products
- Improve potential policyholder satisfaction, which leads to greater renewals, faster market expansion, and a win-win-win-situation for policyholders, delivery channels, and insurers

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¹ Although this is true of all types of microinsurance, this paper will focus on new product development with respect to the partnership, or partner-agent model of microinsurance delivery. This model is described in detail in "Microinsurance Note #2: How is Microinsurance Delivered".

As microinsurance expands, more products are being offered through a variety of insurer models and delivery channels. Too often the approach is more product-driven—in the way microcredit was initially provided—than market driven. This often leads to disappointment on the part of policyholders and insurers. Policyholders, who finally obtain access to formal risk management tools, find the products are insufficient and / or inappropriate for them. Insurers find that product expansion is weak and become disinterested. One insurer in Sri Lanka, for example, offered a non-life microinsurance product designed without market research or testing, and sold only one policy in the first three months! This could have been averted had they followed a structured product development process.

The product development process is typically started by an MFI or other delivery channel as a means of assisting their clients with specialized risk management tools. Starting from the client perspective often results in a more effective process and ultimately a better product. In many successful cases, a product prototype is developed by the offeror and then presented to insurers, rather than relying upon insurers to define and develop the insurance product. When the insurer is selected, the process moves forward with both parties working together.

WHY FOLLOW A PRODUCT DEVELOPMENT PROCESS IN MICROINSURANCE?

Product development is a complex, resource consuming activity which is too often skipped by commercial insurers. This is because of a combination of:

- Wanting as large a risk pool as possible as quickly as possible
- Limited coverage values yielding limited risk
- Not using a structured product development process with other products since they believe they understand their traditional markets.

MFI's often skip the product development process under pressure from insurers to rollout quickly, and because they often do not understand that they are best placed to approach the insurer with a product prototype that reflects demand from their clients. It is not uncommon for an MFI or insurer to decide that a product will be good for their market and then offer it to the masses. Almost invariably this leads to difficulties. These difficulties are seen immediately with low purchase and retention rates, and the long term impact of such a “bad” product can increase the difficulty of offering “better” products in the future.

Those insurers who skip the product development process

may experience slower than average growth, become disinterested, and eventually drop the product. This can result in further reluctance to participate in the next microinsurance effort by that company and its competitors, and deters the growth of a dynamic microinsurance market despite potential high levels of demand.

When the CHaP Kenya health insurance scheme started up, for example, they experienced tremendous demand from the low-income market. It soon became clear that the organization had set the premium significantly below the likely healthcare expenses (even their prospective low-income market recognized this, which was one of the reasons for the very high demand). They quickly realized that if they did not stop offering the product, not only would the insurance product quickly fail, but also they would lose the value of many years of confidence and trust they had built within their community. Such a loss, management noted, would hinder the wide array of other activities in which they engaged the poor, seriously reducing their overall effectiveness. The damage could have been minimized had they followed an effective new product development process.

Insurance is an intangible product—once low-income people have paid their premiums, they have only a “warm feeling of security” and the trust that the insurer will honor the insurance agreement.

Thus, the success of microinsurance in particular relies on a positive demonstration effect from the start. If people see that the insurer offers appropriate products, services them in a way that is effective for the buyers, and honors their commitments, the microinsurance business will grow. A systematic product development process can help to avert many obstacles to success. This will lead to an environment in which a strong microinsurance market can be built.

A STRUCTURED MICROINSURANCE PRODUCT DEVELOPMENT PROCESS

The microinsurance product development process is continuous and designed to ensure that appropriate products get delivered to the market in an effective manner and are monitored for potential

improvements. The diagram at the right outlines the major steps in the microinsurance product development process starting with understanding demand and supply. Note that every step is informed by the needs and abilities of the low-income consumers, the activities of the competition, and the capacity and objectives of the institutions offering the microinsurance product.

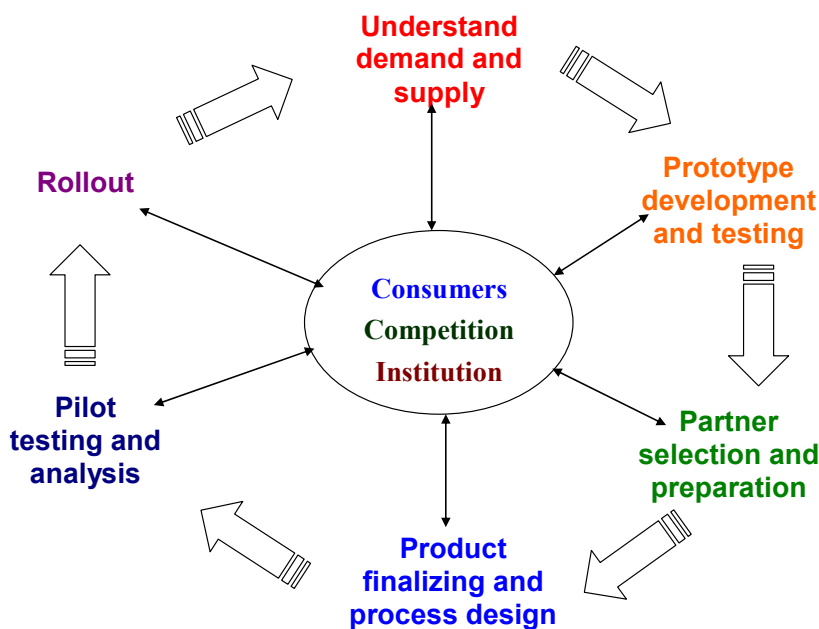
This is a process to develop demand driven microinsurance products. However, it is imperative that whatever product is eventually offered must fit the needs of the institutions (insurers and delivery channels) that offer it. Developers must also recognize that competition will have an important impact on the product. All three of these areas must be seriously addressed in this process.

Understanding Demand and Supply

If insurance products are to be purchased by the low income market, their needs must first be understood and products must address these needs in ways that potential policyholders will see as advantageous. Thus, the process starts with understanding the market. Typically the market demand research focuses on understanding three points:

1. The risks low-income people face
2. How they currently address these risks, and
3. The effectiveness of the current methods

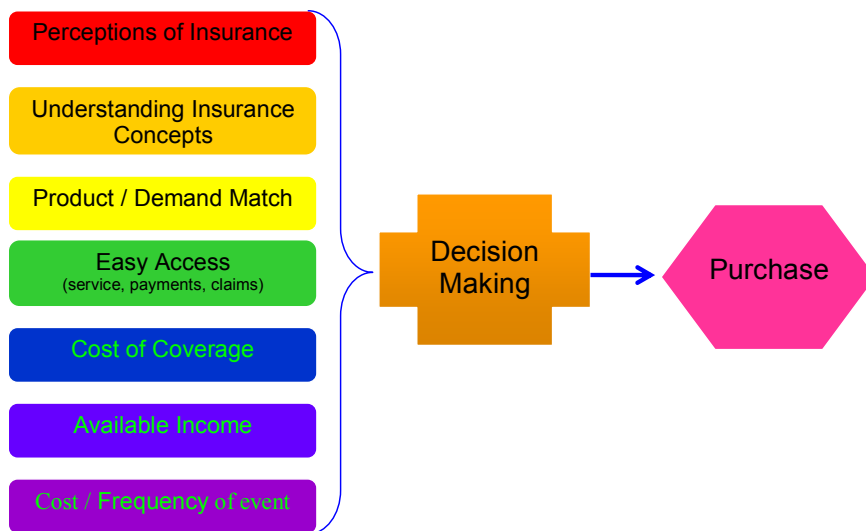
Having the answers to these three questions, helps the potential microinsurer to understand the gaps that might be filled with microinsurance products. For example, the Constanta Foundation in Georgia (with Aldagi Insurance) found, among other things, a strong financial risk in serious health issues requiring hospitalization. Traditional means of accessing funds to cover these through borrowing from family and others were insufficient. The government's efforts to offer free health care was of limited effectiveness since costs were simply transferred from official to unofficial transactions. This led Aldagi/Constanta to offer a daily cash benefit payable for each day spent in the hospital. Cash was provided to assist in the payment of those non-receipted costs which would not be



otherwise insurable (because they are not receipted).

Issues of market research for microinsurance are extensively addressed in the document [Guidelines for Market Research on the Demand for Microinsurance](#).

The ultimate purchase decision for microinsurance products has many components—not just cost. In product development, all the issues in the microinsurance purchase decision diagram at left must be considered. The first two relate to developing appreciation for insurance within the market. The rest are issues that must be addressed directly in the construction of the product.



The match of product characteristics with the demand concerns of the market is critical in any successful product. The level of ease of access will determine success or failure of a microinsurance

product. Access must be seen broadly in microinsurance as making every aspect of the product easy—from policy simplicity to clear and manageable claims procedures. Demand research provides guidance in the creation of accessible products. The cost of the premiums, available household income, and the potential policyholder’s perception of the cost and frequency, and thus their risk, of the occurrence of the insured event all must be considered in developing a balance between what the product will cover and what it will cost. All these factors are key inputs to the purchase decision, and not just the cost.

While market demand research focuses on the potential client, supply side research focuses on the delivery environment for microinsurance. Several areas are reviewed and assessed within the supply side research.

Understanding The Market

“More than any other financial service, an understanding of the market is crucial to the success of microinsurance. Estimating demand is not only about the number of potential clients or determining the appropriate insurance products but it also about understanding where microinsurance fits within the panoply of other financial products, in particular what is a low-income household’s cash flow capacity to commit to a range of long-term financial obligations, as well as other risk management options. Lastly, demand should address the key issue of building trust among low-income populations about insurance. Without a plan to build that trust the desired persistence rates will not be achieved. The people who are the most successful in this fledgling business seem to spend considerable resources on market research.” (Monique Cohen, Microfinance Opportunities)

- The regulatory structure must be reviewed to ensure that efforts to develop and deliver microinsurance are not thwarted by legal issues.
- Other insurers, including informal insurers and social protection systems, are reviewed to assess what they offer within the microinsurance market. Much can be learned from what others are offering and how they offer it. Any new product will have to find an approach to microinsurance that works well for the potential policyholders, the delivery channels, and the insurers. Understanding the products and processes of others can be a key input to developing that approach.
- Delivery channels are critical. The supply research should identify and analyze currently active and potential delivery channels.

- Other microinsurance support structures also must be identified and assessed. Microinsurance pricing will require relevant risk data.² Possibly independent insurance adjusters would be required, or if present, might have some important lessons to offer. Brokers can also be an important component in improving access to microinsurance. Researchers with microinsurance demand assessment skills, as well as microinsurance marketing specialists can help facilitate the product development process.
- Insurance associations are also important to assess since they generally oversee insurance training and, promote insurance throughout the market. They can be helpful in identifying training resources and assisting with the integration of microinsurance into their promotional work.

² Risk data is often found in mortality and morbidity tables. These tables are used by actuaries to calculate the potential financial risk of insurable events. Most developing countries do not have tables reflecting their specific risk structures, and even if they do, the data is typically woefully outdated. Finally, even if there is data, however, outdated, this data is sourced from hospitals and other official sources. However, low-income people frequently suffer without access to such formal structures and often die without death certificates or any inclusion into the official records. Thus, the risks of low-income people are typically not included in the actuarial data.

A clear view of these supply side issues, matched with the lessons and information from the demand side provides a critical base from which to build a microinsurance product. Based on work done in this first step of microinsurance product development, Allianz in Indonesia, for example, has developed a life microinsurance product that they are testing.³

Prototype Development And Testing

Once the market research is complete, the key information for prototype development is available. The developer, most appropriately the MFI or other delivery channel, is able to create the outlines of a product that clearly define what would be offered, how it will be offered, and how it will be serviced. This is also an opportunity to develop premium ranges. Once the general prototype structure is developed, it is appropriate to return to the market for further research, essentially asking, “Did we get this right?”

While the initial market demand research is conducted using qualitative research methodologies—to gather information from people that explains the “what” and “why”—prototype testing is done using quantitative methodologies. Quantitative

³ The MicroInsurance Centre, with partners, has conducted several microinsurance demand and supply studies, including the Allianz study and others in Albania, Georgia, and Romania.

research is more appropriate for prototype testing to provide direct information on product interest, as well as generating information on premium acceptance and willingness to pay through sensitivity analyses. Thus, when this stage is complete, the developer has a product that should respond to the demands of the market. The developer will also have an understanding of the range of prices that people are willing to pay for the product.

Once the institution, or delivery channel, has a reasonably clear idea about the product that its market is interested in, it is then time to attract an insurer to analyze the product develop further if necessary, and take on the risk. In this sense, the MFI or bank is representing its clients' interests in the way an insurance broker represents its clients. The approach of developing the basics of a product and then approaching insurers to offer it has been found significantly more effective than simply requesting “life insurance” or “health insurance” from an insurer. By going to the insurer with a good idea of what the product should look like, there is much greater chance of product success.

Partner Selection and Preparation

Although partner selection may come earlier in the process, upon completion of prototype testing all parties must be identified and committed. Together, the insurer and the delivery channel must determine

if they have the capacity to offer and service the product, and that the product meets their institutional needs as well as the needs of the potential clients.

Selection works best when the partner or agent shows concrete evidence of their commitment to the product and the process. Thus, a form of tender offer to attract either the insurer or the delivery channel(s) can be very effective. In Ghana, CARE International used the tender offer method effectively in their search for an insurer to underwrite and market what became the “Anidaso” (“hope after grieving”) life microinsurance product. Of the twelve insurers in Ghana at the time, eight responded to the tender offer. Ultimately, Gemini Life Insurance Company (GLICO) won the tender and aggressively moved forward with Anidaso. On the distribution channel side of this program, a similar selection process was followed. In order to gauge the seriousness of the rural bank respondents, CARE required that the banks obtain a computer to post insurance information and communicate the insurance sales. In some cases, this resulted in board members actually reaching into their pockets to provide the funds to equip their institutions.

This phase also requires at least the start of planning for communications processes between the entities. Ability to transact efficiently is critical. As an example, transactional efficiency was the reason CARE

required at least one computer at each rural bank before the relationships were solidified. This is important for data communications, but funds transfer is also important. Gemini Life insurance quickly realized that there were difficulties in managing the physical long-term savings of their new microinsurance clients. This difficulty was not just because it is expensive to move cash in rural Ghana, but also because the rural banks did not want to give up those deposits. These issues need to be addressed early in the product development process.

Product Finalizing and Process Design

The prototype has been developed and tested. The parties are all assembled. It is now time to “finalize” the product design and formalize the processes to deliver it.

Formal pricing is done in this phase. Ideally, this is done with appropriate actuarial tables and professional actuaries. This process is outlined in Chapter 7 of the technical guide [Making Insurance Work for Microfinance](#).

The new product must work for all concerned. If the formal pricing falls above the price ranges that people are willing to pay (based on the prototype testing), the product must be adjusted to reduce the premium while retaining as much as possible of the product coverage demanded from the market. It is important at this

point to focus on cost savings through efficient processes. In the end, the product will not be successful if the price is lower than the insurer’s cost, or the product is not what the market wants.

Formalizing the processes, including writing procedures documents, will identify wasted process costs. Delta Life Insurance in Bangladesh, for example, recognized a process problem of requiring too many signatures to approve a claim. This wasted management time, had little control value, and delayed settlement to the beneficiary. Adjusting this process would help them reduce their costs, and make beneficiaries happier. Making processes as efficient as possible is a critical exercise that offers positive results in keeping premiums down.

It is in this phase that staff incentives are developed and mathematically tested to obtain an idea of the likely impact that the incentives might generate. Often there is a need for a combination of group, individual, and non-financial incentives. Such a mélange is necessary because typically a front line staff person is unable to generate enough business with low margin microinsurance products to make individual incentives effective.

Pilot Testing and Analysis

Pilot testing is a critical but oft overlooked step in the microinsurance product

development process. Insurers want as large a risk pool as they can manage as fast as possible. However, this can lead to market dissatisfaction that lingers long after a poorly designed product is withdrawn, making future interventions difficult.

Pilot tests should be designed to test three areas: (1) market acceptance of the product, (2) the systems and processes that make up the product infrastructure, and (3) the people who deliver and service the product.

(1) Market Acceptance

Market acceptance is observed through initial growth and growth trends. However, almost universally, microinsurance products initially grow slowly as the first movers, unfortunately often those with a greater need for insurance, purchase the products. Most others watch to see how the insurer will respond when an insured event occurs. Once the demonstration effect proves that the insurer honors the insurance commitment, many others will apply. The example of VimoSEWA's insurance product growth in the early years exemplifies this trend. Note in the graph below that in the first two years the product was mandatory, while in the third it became voluntary.

The key indicators of market acceptance are growth in covered lives coupled with high levels of renewals. Initially, insurance is sold, not bought.

But voluntary renewals show that people have experienced the product and still want to continue. This is why at least in theory, a pilot test should continue until it provides time enough to test renewals. Many insurers are averse to such a delay, but a true understanding of how a product performs in the market requires an understanding of how likely people are to re-purchase the microinsurance product.

Mandatory products like the VimoSEWA product in its first two years help to quickly build a large risk pool. However, there is no indication of customer satisfaction in such a product. The graph shows that in the transition from mandatory to voluntary, 80 percent of the insured base did not renew. Much of the reason for this decline is that with a mandatory product, delivery channels typically are very poor at conveying information about the

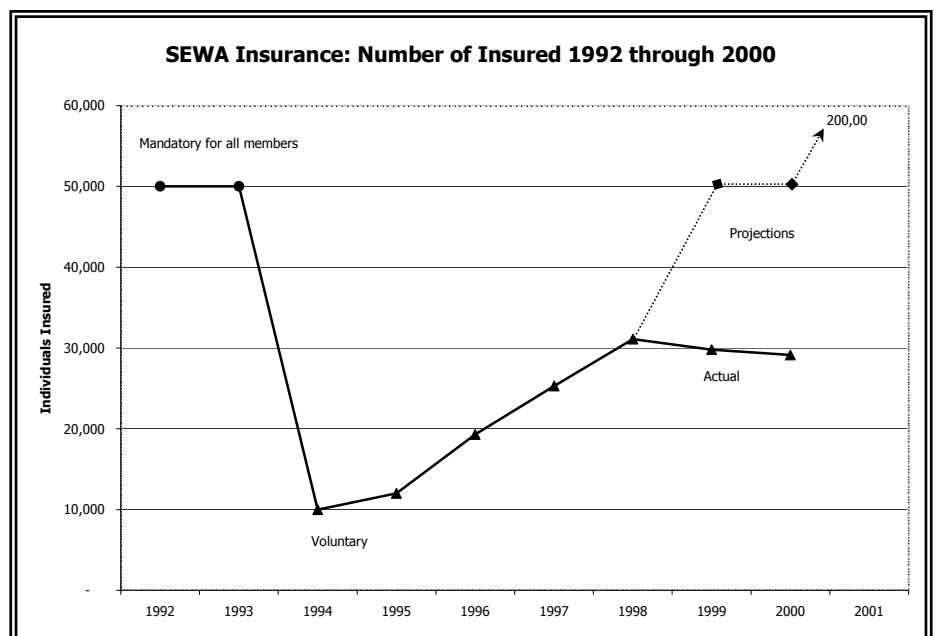
The Demonstration Effect in Nepal

In the Kalaiya area of Nepal, after providing benefits to the families of two deceased persons within a short time, there was a rapid increase in the number of clients showing interest in purchasing the microinsurance product. (CMF Nepal, Pilot Testing of a Micro Life Insurance Product, Results and Lessons Learned)

product. "People have to buy it, so why waste time explaining it" seems to be the attitude of front line staff, for example. For this reason, offering the product on a voluntary basis for the pilot test is advisable. This forces front line staff to convey an appreciation of the product to clients, and allows for a better gauge of product interest.

(2) Systems and Processes

Systems and processes failures with an intangible product such as microinsurance can have a dramatic negative impact on product growth. Insurance is a business of trust and trust is



The Need for A Clear Understanding From Clients

PSHM was working with an agricultural training organisation to provide loans to rural communities in Albania for the purchase of livestock. Management decided to offer these clients insurance to protect them against the possibility of the cows dying whilst the loan was outstanding. During the market research this product received positive feedback from potential clients and so a product was designed. However, when it was offered to clients the product proved to be extremely unpopular and eventually the product was recalled.

Later, focus groups were conducted with these rural clients. The research indicated that the clients were in favour of the product, its terms and pricing but the clients were unable to pay the premiums in advance as required by the insurance company. Subsequent negotiation with the insurance industry in Albania has demonstrated that companies are now willing to consider providing insurance with premiums collectable on a monthly basis.

Source: An overview of insurance product development within the Opportunity International network.

damaged when people see systems fail. Unfortunately, system and process failures are common! For this reason, it is critical that systems and processes be tested and proven on a small pilot test group rather than on a huge population spread over a large geographic area. Problems are easy to fix in a pilot test, and the negative impact is controlled when it occurs on a small scale.

(3) People

Front line staff who sell microinsurance require significant training to understand and appreciate the benefits of the product they are selling. This training needs to be tested and refined through observation of front line sales people and their approach to marketing, as well as their effectiveness in processing information and transactions. It is critical that these issues be tested and confirmed before training the rest of the staff or rolling out a major marketing program.

Any test requires analysis to determine success or failure. In

addition to tracking growth against a business plan, a number of other tracking indicators are important in microinsurance. Among these include understanding:

- The costs involved in selling and servicing the microinsurance products
- The promptness of claims settlements and the level of claims rejections, and
- The level of claims compared to premiums

Tracking this information is critical to fully understanding the results of the pilot test, and refining the product and/or processes.⁴

New microinsurance products are generally watched carefully for failure at the beginning, especially by a skeptical low-income market and even by the staff of the delivery channel. Pilot testing to ensure that

potential policyholders actually will put their hands in their pockets and pay, and repay, for insurance; that the systems work without error and in the most efficient manner; and that the staff are well trained, appreciate the product, and have marketing support that works on this market, can save significant staff time, management time, and other costs in the long-term.

Rollout

Once the pilot test has proven market acceptance of the product, the consistent and efficient implementation of systems and processes, and the ability of the people to sell and service the product effectively, it is time for rollout. At this point all activities go into high gear to ensure successful product expansion throughout market areas and clientele. Key areas to consider in this phase are education, systems, and marketing.

Expanding microinsurance education throughout the delivery channel staff is critical. The same appreciation that was built among select staff in the

⁴ The CGAP Working Group on Microinsurance and ADA have recently published "Performance Indicators for Microinsurance Practitioners." This workshop paper is helpful for understanding key ratios to monitor for microinsurance products.

pilot test phase must be conveyed to other staff. Even if the product is going to be mandatory, appreciation and knowledge must be built throughout the organization.

Educating the market is a critical activity especially in the rollout phase. There should be an active effort to educate the broad potential microinsurance market about the importance of microinsurance, how it fits with current household financial structures, and how it can benefit low-income families. Success in this effort will make sales much easier.

In several microinsurance partnerships witnessed so far, the insurer typically is responsible for preparing the promotional materials. This has turned out to be a critical juncture in the evolution of an insurer to a microinsurer. In each case, the insurer has tried to introduce marketing strategies and materials that have succeeded in their traditional upper income market, but are not effective for the low-income market. In these cases, the insurers have been pushed to test their strategies and materials on focus groups of likely microinsurance clients. Each time, this has had a dramatic impact on the insurer as they realize that they need to shift their understanding to be effective in this market. This process often starts in the pilot testing phase.

Systems must be able to manage the volumes of rollout. In the pilot phase a good

understanding of the system demands should have been developed. It is important to make sure that systems will manage the expanded volumes of rollout and that there is sufficient staff capacity to operate the systems.⁵

CONCLUSIONS

Following a structured product development process can be time consuming and require significant effort. However, the benefits generated include:

- Faster acceptance by potential clients because:
 - The product was designed to meet the real needs of potential policyholders
 - The product education and marketing campaign is appropriate for the low-income market
 - The sales people have been well trained and appreciate the benefits of the product they are selling
- Better renewal rates because service provision was tested and perfected on a small group
- Limited chance of systems or process failure because these were fully tested

⁵ Of course, one method that is commonly employed in microinsurance is to work with group policies. This way many lives can be covered while the insurer only manages a relatively small number of policies. A classic example of this is AIG Uganda with 26 policies covering over 1.6 million lives.

Insufficient Systems

In 2005, an insurer in Azerbaijan issued 50,000 compulsory motor third party policies. In 2006, they issued 6,000. Why? After the major effort to sell policies in 2005, the company realized that their system was unable to manage such a volume of business. They had no choice in 2006 but to send their policyholders elsewhere while the insurer addresses its systems problems. The impact is that they have lost business in 2006 (premiums of USD 5.5 million in 2005 versus approximately 0.7 million in 2006) and the client base they invested in will require reinvestment to get them to return. When systems do not have the capacity to manage volumes this can be very expensive.

(Source: Michael J. McCord, Microinsurance Pre-Feasibility Study—Azerbaijan, forthcoming)

- Increased trust and confidence from a skeptical market because systems and processes work
- Increased client loyalty to the institution

All this adds up to a relatively small investment with very large returns to low-income policyholders, the delivery channels that get product to them, and the insurers that take on the microinsurance risk.

Some key sites that provide good information on microinsurance and/or microfinance product development: MicroInsurance Centre, CGAP Working Group on Microinsurance, MicroSave, Microfinance Opportunities, and Accion

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