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Microinsurance NOTE 7

Life Insurance for the Low-Income Market

Demand research among low-income people consistently finds demand for risk management tools that could help them cope with financial issues related to the death of a breadwinner. Client-responsive products with a high value for money have the potential to improve sustainability of the family and facilitate continued human capital growth into the next generation.

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For a family living on just a few dollars a day, when a breadwinner dies, the impact is rapid and harsh. In the midst of the emotional jolt from the loss, the family must then face a series of financial shocks. These financial shocks start even before the reality of the loss begins to sink in. Often the hospital and sometimes the police need to be paid for dealing with the body. There are costs for transporting the body to the burial site, for religious services, for feeding mourners, buying the casket and the cemetery plot, and transporting the mourners to the burial site. Too many times, people desperately scrape together the funds simply to get the body released from the morgue.

The *real* cost of the breadwinner's death is felt after the funeral. After the mourners go home, the family is left without the breadwinner's income, without the cash that was spent on the funeral, or the inventory or other productive assets that might have been sold to generate the funds to keep the breadwinner alive. Lenders come collecting. A desperate search for income begins. Nutrition declines. Children leave school. The family moves to cheaper and often riskier lodgings. The decline of the family, and diminished potential for the next generation has begun.

There are local informal social mechanisms that can assist the bereaved family. These are typically insufficient and usually focused on the funeral itself. Some cultures, as in Western Kenya, have traditions that take care of the family after a male breadwinner's death. The surviving spouse becomes the wife of the deceased's brother. This tends to be a problematic local risk management practice. However, in neighbouring Northern Tanzania, the family of the deceased male takes possession of all household goods leaving the widow and her children with nothing.[1] In each culture, the means of addressing surviving families is specific to that culture. However, in most cultures widows and their children feel the financial stress of a breadwinner's death most intensely. Good quality microinsurance, with a high value for money for this market, has the potential to dramatically change the predicament of families suffering the loss of a breadwinner.

Demand research among low-income people consistently finds demand for risk management tools that could help them cope with financial issues related to the death of a breadwinner. In these cases, this market is looking for (1) funds to help the remaining family carry on; (2) funds to assist with the funeral and the related ceremonies and customs; and (3) coverage for the outstanding balance of a loan, if indebted although this demand often comes from microcredit institution rather than from the clients themselves.

FAMILY INCOME ASSISTANCE

Although there may be some assistance for families at the time of a breadwinner's death, typically, extended family and friends quickly return to their own lives and concerns, leaving the deceased's family in a diminished financial position. The internal financial struggle then ensues to balance the new family income levels with priority expenditures. With the income shift there is a priority shift. Food becomes more important than schooling. Allowing children to be children becomes less important than having them generate some income. Having time to nurture the family becomes less important than working longer hours to have the money to care for them.

Several microinsurance programs have developed term products to help address these issues. For example, La Equidad, a credit union owned microinsurer in Colombia, offers a product ("Amparar") that provides funds for household needs like groceries, utilities, and school fees for one to two years after the death of the breadwinner. This product is specifically designed to provide particular benefits that allow the family to cover its basic needs while the family adjusts to the new financial situation. La Equidad offers this coverage in six different levels so that policyholders can find a level that is appropriate to their needs. The Table outlines the benefits provided with this product at levels one and six.[2]

Coverage (US$)	Plan 1 Smallest	Plan 6 Largest
Death (any cause)	1,244	8,292
Total and Permanent Disability	1,244	8,292
Food/Groceries for 12 months	25	104
Utilities for 12 months	12	62
Funeral support (lump sum)	62	332
Optional:		
Children's Educational Expenses 24 months	15	75

Note: there are six plans. Only the smallest and largest are included.

Family assistance coverage, as is offered by La Equidad, requires efficient and effective control mechanisms in order to make sure that such efforts do not simply drive up operational costs. Innovative processes are required, such as linking with a chain supermarket that caters to the low-income market in order to make one single payment on account for the family. Paying school fees to a designated school might also work effectively. However, setting up each of these relationships requires effort, and cost, on the part of the insurer. La Equidad has not yet found the right claims distribution mechanism and thus calculates these costs and provides them in a lump sum payment. In another example, at least one electric company in South America

[1] See Altemius Millinga's "Assessing Demand for Microinsurance in Tanzania" for more discussion about the husband's family taking possession of household property.

[2] Gloria Almeyda and Francisco de Paula Jaramillo. La Equidad Seguros, Case Study No. 12. Working Group on Microinsurance. September 2005, p. 26.

offers insurance to cover continued electrical usage by the surviving family. Because the company acts as the provider of the service and the delivery channel, the claims "payment" is more efficient.

In traditional insurance, long-term products, as a means of helping to protect one's family are common. They often provide important benefits whether the policyholder dies or not. These products require a periodic premium payment, which actually encompasses two components—an insurance premium and an investment. In this way, people have an opportunity to invest to protect their future and if they die along the way, the insurance will provide benefits to the family as well as a return of the investment with earnings.

Some of these products are objective based. In these cases, people save for a particular future need, and if the policyholder dies during the savings period, the insurance will complete the expected payments. Thus, if a breadwinner has such a policy to save for her child's education and dies in the second year of the fifteen year period, the insurer will complete the expected savings.

Long-term microinsurance coupled with an investment component can be an effective mechanism for providing for low-income family financial stability after a breadwinner's death. Such products can promote objective-based savings as well as providing insurance benefits for the family. Women in Jordan, for example, have a strong demand to save for their children's education. Families in India often want to save for a dowry. Still others want to save for a lump sum at retirement. Many local, informal, insurers in Indonesia, called "Arisans", for example, provide a savings and insurance linked product to generate a purposive amount of money.

These long-term policies, "endowments" typically, create a means for promoting regular savings. The insurance provides back up support in case the policyholder dies during the savings period. In such a case, the insurance policy would finish the payments. Programs like Delta Life in Bangladesh offer their Gono and Grameen Bima products to help people save as little as USD 300 over ten years.

For many years, credit unions have typically provided a basic savings life product that pays a multiple (usually two or three) of a client's savings to the beneficiaries on death. Tuw Skok in Poland has found that its parent credit unions, like many MFIs, do not want to pass on the savings of their clients to an insurer, yet still want to maintain a link to life insurance. In order to satisfy these demands, Tuw Skok has developed a product that allows policyholders to save with the credit union towards a financial objective, while Tuw Skok offers a term life policy to cover the potential death of policyholders / savers.

Caution is important with long-term savings in developing countries. Too often the ebb and flow of the economies of these countries leaves long term savers with no real value due to hyperinflation or currency devaluations. Additionally, the long-term saver relies on the profitability and ethical nature of the insurer in which they invest their funds. Discussions have taken place in Georgia for example to develop an insurance custodian to act as a control on long-term funds paid to insurers. The intention was to improve market confidence in these insurers and protect the policyholder over the long-term.

FUNERAL COVER

Funeral cover is a relatively common informal insurance type. From Ghana to South Africa, and Bangladesh to Brazil, local communities have gathered funds and other contributions for generations to support the requirements of funerals. These funds are generally helpful to the bereaved family both financially and socially; however, in many cases such groups are more focused on the social than the financial. This often leaves a funding gap for families of the deceased to meet. The funding requirement can be quite significant, as in Uganda where the body and the mourners must travel to the birthplace of the deceased for burial, or in India where the celebrations of birth, marriage, and death must receive the same level of ceremony.

To fill the funding gaps, insurance companies have entered the funeral insurance business reaching to the low income market. Companies like Madison Insurance in Zambia and Sanasa ALMAO in Sri Lanka have a major focus on funeral policies. The credit union related Aseguradora Solidaria de Colombia covers over 2.5 million lives with its funeral cover delivered through its credit union members and funeral parlours.

In South Africa, funeral policies are almost a social requirement and are so popular that most commercial insurers and even funeral parlours have been selling burial policies in the low-income markets for many years. FinMark Trust, having done significant market research in Southern Africa on microinsurance, estimates that there are between 80,000 and 100,000 burial societies in South Africa with aggregate premium contributions of about USD 1 billion per year.[3] Most of these insurance programs offer either cash or in-kind benefits. For the in-kind benefits, insurers provide the key requirements for the funerals, including: the casket, transport, tents, chairs, and other funeral requirements. This relieves the family of having to deal with all these issues, and can provide better goods and services and potentially a reduction in premium costs because of the purchasing power of the insurers. In-kind benefits can be important for the bereaved family and also acts as an advantage for some insurers to this highly competitive market.

Funeral policies will remain an important piece of the microinsurance puzzle. Microinsurance managers must recognize that success in this area will require:

- Rapid claims payments
- Innovative approaches to controls (allowing the rapid claims)
- Improved claims infrastructures (such as the in-kind claims settlement in South Africa)
- Development of innovative ways of maximizing the value of the claims payments to the bereaved family

CREDIT LIFE

Credit life insurance tends to be very profitable for microinsurers, and is very popular with MFIs. Indeed the MicroInsurance Centre's Landscape Study of Microinsurance in the World's Poorest 100 Countries found credit life to be the most popular type of microinsurance offered, with 103 different credit life products identified, covering over 23 million people, almost entirely on a compulsory basis.

Typically credit life products simply cover the loan principal and interest outstanding at the time of the borrower's death. Some policies cover the fixed amount borrowed and the balance after paying the loan principal and interest is provided to the beneficiaries. Others, such as Allianz Indonesia's "Payung Keluarga", provide credit life as the product base, and then add additional benefits. In several instances, these policies come with permanent and temporary disability benefits to cover the loan payments in the case of borrower disability

Though credit life products are popular with insurers and MFIs, low-income borrowers typically see basic credit life as a product that is not for them, but for the lender. Certainly, "savvier borrowers question the value of a product that appears to protect the MFI more than the clients."[4]

While credit life insurance mitigates some risk to the lender, its value to the dependants of the client is minimal. Mortality rates are typically very low among MFI clients compared to default rates, so from the institution's perspective, the insurance is only marginally better than provisioning. Indeed, simply writing off loans unpaid due to death is not likely to significantly impact on the costs of doing business. As the author, with others, have argued, ("Making Insurance Work for

[3] FinMark Trust and Genesis. The Great North Burial Society (GNBS): the growth of an informal insurer. Powerpoint presentation to the Munich Re Microinsurance Conference 22 November 2006 in Cape Town, South Africa.

[4] Monique Cohen and Pamela Young. "Using Microinsurance and Financial Education to Protect and Accumulate Assets, p. 18. Sourced 2 July 2007 at http://www.microfinanceopportunities.org/docs/Using%20Microinsurance%20and%20Financial%20Education.pdf

Microfinance" Churchill *et al*, 2003) provisioning is actually a better way for an MFI to approach credit life insurance in all but a few cases. The incremental value to dependants is minimal if the loan would have been written off anyway due to their inability to pay. At worst, credit life is just a public relations enabler, allowing the MFI to avoid the bad publicity of extracting money from widows and orphans.

Many MFIs actually abuse credit life insurance as a means of improving the fee income portion of their operating statements. They charge a fee as high as 3 percent of the loan principle as 'insurance', account for this amount directly to fee income, and simply write off losses through their Reserve for Possible Loan Losses accounts. Significant overcharging of this nature makes potential policyholders even more skeptical of insurance and damages the credibility of more appropriate insurance products.

If microinsurance is going to be successful beyond those products that low-income people are required to purchase, such as credit life, there is a need to advance beyond these very basic self-serving products into areas that respond more accurately to the needs that this market expresses. Credit life may be an appropriate place to start to gain an understanding of low-income people's risks, but there is a need to move ahead with more complex products that offer the win-win-win solutions for policyholders, delivery channels, and insurers that credit life does not, at least for the policyholder.

DELIVERING LIFE MICROINSURANCE

Because most life microinsurance products are relatively simply structured, this facilitates marketing and sales by a wide variety of distribution channels in very cost effective ways. Credit life can be distributed by any lender as part of the loan or lease. Premiums are included with loan payments and transaction costs are almost nothing. Funeral microinsurance is also relatively easy to market and sell especially in areas where culture promotes such protection. In South Africa funeral parlours sell funeral covers. MFIs and other formal and informal groups of low income people are common policyholders and delivery channels for such products. ICICI Prudential in India sells life microinsurance policies through computer kiosks deep in villages. Ceylinco Insurance in Sri Lanka sells small denomination "One and Only" life policies through swipe cards in supermarkets. Cell phone sales are likely, if not in existence already. These various delivery mechanisms help to reduce the delivery costs and expand the market access to these products.

Long-term investment linked insurance is more difficult to sell and to manage. The delivery and servicing of these products needs to be done in a way that protects the investment of policyholder while also allowing easy consolidation of the funds in order for the insurer to adequately manage them. Additionally, there is a need for controls and appropriate oversight of the insurer to protect the policyholder funds. There are many issues with long-term insurance linked products and such products should be approached with caution.

CONCLUSIONS

Of all insurance types, life cover is, relatively speaking, the least difficult to provide, because:

- It is one of the most demanded forms of cover.
- It is relatively easy to price compared to other types of insurance.
- It is mostly resistant to problems of fraud and moral hazard.
- It is not dependent, unlike many types of health insurance, on the existence and efficient functioning of other infrastructure like clinics or hospitals.
- It can easily be linked (at least with short-term life insurance) to other microfinance savings and loan products.
- The insured event is a clearly defined and almost always easy to verify

What low-income families need is a greater focus on the products that have the potential to help them the most. Funeral policies are likely to be popular in many places beyond the current markets. Certainly there is a great demand for insurance products that assist the family after the death of a breadwinner, and after the family and friends have gone home from the funeral. Client-responsive products with a high value for money have the potential to improve sustainability of the family and facilitate continued human capital growth into the next generation.