



Federal Ministry
for Economic Cooperation
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Microinsurance as a social protection instrument



Protection from major risks for little money

The lives of the poor in developing countries are characterized by constant economic insecurity. Most of them do not have adequate financial reserves to properly cope with crises that are caused by personal and environmental risks. Every illness, every accident, every family death can push them deeper into poverty.

In most parts of the world, the extended family or village community provides a safety net in times of crisis. That safety net is based on reciprocal exchange relationships. However, this traditional form of protection often fails in the face of severe emergencies or crises that affect entire communities, for example after a natural disaster. In such instances, people are forced to go into debt by taking out more loans, to reduce the amount they spend on food, to take their children out of school or, in extreme cases, to sell their productive assets, such as animals and fields.

Formalized social protection can prevent the impoverishment of people with no or very little income. Many governments have realized that. However, social protection systems – where they exist – often only reach a small percentage of the population. In particular, informal sector workers typically have no access to such protection.

Microinsurance is one way of cushioning the impact of general risks such as illness, old age, and death. It gives people with low income an opportunity to buy appropriate insurance for small premiums and thus to provide themselves for their own futures. This makes it easier for them to cope with crises. Microinsurance is a social protection instrument that can complement existing social protection systems in a meaningful way.

By providing better protection against risks, microinsurance supports poor people's initiative to escape from poverty through their own efforts. People with low income have a chance to invest more in their productive assets and in education and health if they have protection against unpredictable risks.

Where governments actively support microinsurance programs and link them closely to existing governmental protection systems, public and private instruments can complement each other, forming an overall system of social protection. The purpose of such a strategy is to give the entire population coverage with regard to the main risks that are relevant for the poor.

A number of countries have therefore decided to actively encourage and foster the integration of private risk



Microinsurance enables poor people to hedge against risks.



Comic strips are used to educate customers about the way microinsurance works.

protection into governmental protection systems. For instance, the Indian government adopted a law for the social protection of informal sector workers, thus putting in place a legal basis for microinsurance as a social protection mechanism. Governmental institutions help build the capacity of local microinsurance providers by providing training to staff and by supporting their efforts to form networks.

Assistance in hard times: life and accident insurance

The death of a family member is always a painful experience. If that family member is also the family's breadwinner, the entire household may fall into poverty as a result. Life or accident insurance that is tailored to the needs of low-income people cannot take away families' grief, but it can help them overcome financial crises in hard times.

Cooperative endeavors between official German development agencies and the German insurance industry show how this works in practice.

Payung Keluarga ("Family Umbrella") is the name of the credit life insurance which Allianz insurance company is selling to microcredit clients in Indonesia. If, after taking out a loan, a family's breadwinner dies, Allianz pays the outstanding credit sum back to the bank and provides an additional amount to the family to see them through the difficult initial period.

Sujiyati from Jakarta lost her mother. Payung Keluarga credit life insurance not only covers the repayment of the portion of the loan that is still outstanding, it also gives her a bridging allowance equivalent to 154 euros. This makes it easier for her to cope with the loss of income caused by her mother's death. Sujiyati uses 36 euros to pay for the funeral. Her neighbors and family also chip in something. Of the remaining sum, she invests 98 euros in her small textile business. She retains 12 euros as a contingency fund. So her mother's insurance has prevented the children from going into debt for the funeral. And it helps Sujiyati to continue to feed this family of seven.

Microinsurance reduces the risk of illness resulting in poverty

For low-income groups in developing countries and emerging economies, illness is one of the biggest impoverishment factors. 1.3 billion people worldwide have no adequate or affordable access to health care. In many countries, people who get sick have to pay for medical services immediately and out of their own pocket.

If there is no insurance, entire families often go into debt when someone falls ill. On the other hand, inadequate medical treatment (or no treatment at all) may result in a person's losing their ability to work and thus, in permanent income loss. So the reimbursement of payments for basic services such as treatment, drugs and hospitalization is of crucial importance.

Illness is a particularly great risk for informal sector workers. In sub-Saharan Africa and Asia, most people work in the informal sector, which means that they have no health insurance through their jobs or from the government. Microinsurance is a social protection instrument that is able to partly close that gap.

In Africa in particular, mutuals are very common. They are community-based, non-profit systems that are often set up by municipalities, cooperatives or associations. Mutuals are typically very small and only cover a limited number of members.

Due to the small number of policyholders covered by mutual schemes, all of whom share similar risks, the pooling of risks across healthy and sick people and young and old people is often inadequate. Moreover, the low premiums collected are often only sufficient to pay for basic services, even in cases where mutuals receive subsidies. Community-based microinsurance usually

does not pay for surgery or HIV/AIDS or cancer treatment. Moreover, small, community-based microinsurance systems are often not financially viable because there is a lack of management capacity, administrative costs are very high and the system is threatened with bankruptcy as soon as many members fall ill at the same



Microinsurance gives people access to important basic health services.

time. Due to these and other illness-specific factors, illness is considered one of the risks that are the most difficult to address through microinsurance. Yet in many countries, micro health insurance is the only form of protection available as there are no public systems.

That is why in Cameroon, Germany engaged in development cooperation to help mutuals set up a national network and gave them access to a support and reinsurance fund. In parallel, German experts helped the government draw up a legal framework for micro health insurance at the national level and to incorporate it in the national health insurance system. These endeavors succeeded in increasing the number of people covered by mutuals.

Half of Tanzania's population cannot afford visits to the doctor or to hospitals. That is why the Tanzanian government supports the development of micro health insurance. With the support of German development cooperation, policymakers and associations jointly set up Centers of Health Insurance Competence (CHICs). They offer know-how to local micro health insurance providers at low cost and also give them practical support with regard to management and administration. In this way, community-based providers of microinsurance are able to benefit from established best practice and, as a result, become more professional and efficient in their work.

Support in the face of increasing weather risks: insured against all weathers

Time and again, extreme weather events such as floods and storms threaten many people's livelihoods. Immediate effects such as damage to what little assets there are, loss of income, the cost of medical care and rising food prices are a great burden for low-income households.

That is why official German development agencies have been working together with Munich Re to develop microinsurance solutions to protect people from the consequences of extreme weather events.



Floods pose a threat to the livelihoods of many people in developing countries and emerging economies. Microinsurance helps people cope with weather risks.

In the Philippines, for example, severe typhoons regularly threaten the livelihoods of many poor people. They destroy their homes and crops as well as their productive assets. Once the basis of their livelihoods has been destroyed, people are often no longer able to repay their loans. This results in further pressure on households that have already suffered, and it constitutes a great risk for microfinance institutions as well as cooperatives: when the flow of credit repayments stops, the cooperative may suffer financial deficits or even be ruined.

An innovative microinsurance approach has been devised in response, aimed at helping both the poor households and the microfinance institutions. In the event of loss the cooperative receives a predetermined percentage of its credit volume, enabling it to continue to operate.

The insurance sum is then passed on, through an emergency fund, to those members of the cooperative who were particularly hard hit. The emergency fund can be used to support poor households in rebuilding their homes and replacing productive assets they have lost. This enables people to make a living again and protects them from impoverishment.



Microinsurance gives informal sector workers an opportunity for improved risk management, thus helping them safeguard their livelihoods.

Benefitting from the expertise of the private sector

Insurance companies have embarked on a new avenue by offering micro policies. While in the past they did not consider people with low incomes as potential clients but only as recipients of assistance, they are now increasingly developing microinsurance as a business field, working together with local and international partners. In such endeavors, all players contribute their respective strengths so as to ensure sustainable development of this business field and thus give people more security. Local partners contribute their knowledge about local structures; development agencies contribute their expertise with regard to the target groups concerned; and enterprises contribute their actuarial and business administration know-how.

The approach of German development cooperation: strengthening partners, tapping potential

In the national and international development debate, microinsurance has come to be recognized as an effective risk management tool. However, for many of the partner organizations involved in development cooperation (microfinance institutions, cooperatives, associations, labor unions, insurance companies, supervisory authorities) they are a new field of activity. This means that the relevant institutions are often not yet familiar with the relevant requirements and insurance standards. It is crucial for an institution to be competent in this regard if it wants to offer financially viable microinsurance and be accepted by the private sector as an equal partner.

Low-income groups are not familiar with the way insurance works, either. As a result, they are often skeptical both about insurance products and about insurance providers. This means that those offering microinsurance are facing great challenges – they need to educate and inform their potential clients and ensure customer protection, and they need to offer insurance products that are as simple as possible and easily understandable.

In view of these challenges, Germany's development cooperation focuses on familiarizing central players with risk management strategies and the underlying principles of insurance. This relates, for instance, to the conducting of needs assessments, which are the basis for developing products that meet target groups' needs. Another important element of our relevant development activities is the provision of training to partners in the South to pass on microinsurance-related knowledge.



Education and information about microinsurance is an important part of Germany's development cooperation.

It is also vital that the financial viability of microinsurance institutions be ensured and that such institutions be supervised in accordance with international insurance standards. After all, the development of economically viable insurance markets is an essential contribution to financial system development and stability.

Internationally, the representatives of Germany's development cooperation work closely together with the Microinsurance Network, which is an association of donors, multilateral agencies, the insurance industry, academics, and nongovernmental organizations. The

Network fosters the exchange of information and helps coordinate the development and dissemination of insurance products for low-income groups.

With a view to strengthening and further developing the microinsurance market, it is also important to tap sources of finance for the providers of microinsurance. From its development cooperation resources, Germany supports the world's first microinsurance fund, Leapfrog Investments. The fund's vision is to give 25 million uninsured people access to microinsurance. For example, Leapfrog supports an insurance company in South Africa that offers life insurance to people living with HIV.

Microinsurance is an efficient risk management instrument. However, protection for the entire population is only possible if microinsurance is combined with other social protection instruments. Therefore, Germany's development cooperation supports our partners in identifying suitable instruments for hedging against poverty-related risks, and in integrating microinsurance into existing social protection systems.



By providing better protection against risks, microinsurance supports people in overcoming crises and poverty through their own efforts.

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