MICROINSURANCE CASE STUDY - AIG UGANDA LTD.

Microfinance Industry

Before we consider how to respond to an insurance need we must first understand the nature of the risk and the specific fundamentals which adhere to it. Knowledge of a particular environment is essential to determine acceptable product offerings, distribution mechanisms and the criteria for delivery of efficient services.

To give you a little background - in a developing country such as Uganda historically there was little in the way of financial support for those who wished to escape the clutches of poverty. The banking industry both internationally and locally showed little interest in assisting the poor in undeveloped areas. They regarded unsecured loans to those who live and operate in the informal sector as far too risky, on top of which, was the extremely high cost of administering and servicing very small short term loans. In truth large retail banks have difficulty justifying directly banking to this sector.

The poor in countries like Uganda depended on family, community or, as a last resort, loan-sharks, to meet their financial needs.

Several international Non Governmental Organisations saw the opportunity to provide a microfinance system focused on enterprise development similar to those which have proved successful elsewhere in the world. The Ugandan Government gave the project their support and several local MFI’s were set up with initial NGO’s funding to develop lending programs based on the Grameen Bank model for which Prof Yunus has been so deservedly recognised.

These programs tend to be based on either group or village lending and in Uganda it is the former system which is the norm. I am sure everyone is familiar with the concept of group responsibility and the pyramid system of management control which has made these so successful.

The MFI’s have very low default rates and loyalty amongst their borrowers.

As the business has grown and matured with a solid customer base, the local MFI’s have had to do whatever they can to increase their capital base to satisfy future demand for loans.

The NGO’s have limited resources and mainly depend on Governmental bodies and foundations for charitable donations. Many finance similar operations across the developing world from South East Asia, the Indian continent, Latin America and in other African countries so may be unable or unwilling to meet the call for additional capital.

As an alternative many MFI’s started taking deposits from borrowers and accessing capital from the formal banking sector. Some of these then move to local control reducing or severing the bond with the original NGO’s.

In Uganda like most countries there has been little or no regulation of the microfinance sector. When charitable organisations offered to lend money to people previously spurned by the banks, the authorities naturally encouraged the process and did not bind it up in red tape. However as MFI’s start acting as banks and/or insurance companies, taking deposits or carrying insurance risk then regulation must follow.

We shall hear more about that subject later.

Microinsurance in Uganda

As explained above the microfinance market in Uganda is focused on small enterprise development loans made for very short periods, mainly to groups of woman. Loans periods are generally from 3 to 6 months and are rolled over.
This is the bottom segment of the Living Standard Measurement scale as applied to the microfinance industry and most of the people are in the informal business sector either involved in curb-side trading or as traders in recognised open markets.
It is important when considering appropriate product and service that one differentiates between the various segments within microfinance. In this case we are not talking about people with regular incomes from formal employment who may own basic assets. These people do not have formal housing or means of transport. However the objective is that in time some will build up their businesses and become small formal enterprises enjoying the accompanying live style benefits.
Most borrowers initially have little basic education or business skills and the MFI's through their committee and group structure carry out training programs to encourage them to run their enterprises efficiently.
Insurance is not a high priority for this segment of people in Uganda with the exception of Funeral Insurance which is the one cover they recognise as important. The cost of distributing insurance on an individual basis would make it so expensive and premiums would literally compete with the basic necessities of life.
Like the large banks, insurers have struggled to provide product, distribution and service to the very poor. Access, continuity, overhead costs, potential fraud and the general lack of customer interest have in the past all been barriers. Many banks now seek access to this sector by proving loans to MFI's, who already possess the necessary infrastructures. Insurers can likewise make use of these same structures to overcome most of their prior concerns. This is the so called partner-agent model.
AIG Uganda picked up this opportunity to work with the MFI's in the region and develop product, distribution and service which compliments their infrastructure. For the sake of efficiency in most cases a tied insurance agent acts as an intermediary as like many other jurisdictions insurance agents in Uganda require to undergo training programs to obtain licenses. Using a tied insurance agent has many advantages for both the MFI and the insurer in that market.

The benefits include-

- A dedicated licensed resource is always available with specialised skills and a full understanding of how the microfinance institutions operate in the region.
- The agent acts as a focal point for managing, processing and servicing the business including management of claims settlements. This can be a difficult process identifying the spouse and family.
- The agent develops and acts as the training resource on insurance programs to the MFI loan officers in widely dispersed locations across the region.
- The agent provides translations of all the insurance training documentation into the numerous local languages.
- The agency is a central access point for general queries

- The agent is the representative for the microfinance industry in negotiations with the insurance company.
- Without a central dedicated agent all MFI's would need to allocate resource and have that the individual trained and licensed before they can act as an agent. It is unlikely that they will attain the same level of knowledge as a dedicated central agent can acquire.

Coverage –

When AIG started their program there was little history so, if the project was not to fail, a conservative approach was necessary. Experience has now provided a greater appreciation of the exposures and has allowed us to continually expand the coverage and improve the service.
Each MFI can customise its own individual program however product standardisation is important to obtain efficiency and exert controls. Limited options are available within each plan.
Obviously other local insurers have recognised AIG's success with microinsurance in Uganda and are keen to penetrate the sector. Normal open market forces are therefore at work to ensure that the service standards, terms and coverage which AIG offers are kept competitive.
As most of you know, AIG has a very broad global network being in over 130 countries and jurisdictions. We continually share information and knowledge so are conscious of what is being offered elsewhere in the world. We are always looking to replicate programs which have been successful in other jurisdictions or at least elements from these programs which may benefit our local business. Many of our operations in other countries have learnt a great deal from our success in Uganda.

Cover is now available as follows –

- Death of the borrower from natural causes repays the loan amount to the lender
- Permanent total disability of the borrower repays the loan amount to the lender
- An additional amount for accidental death or disability of the borrower is payable to the spouse/ family
- Accidental death of the pre-identified spouse payable to the borrower
- Accidental death of pre-identified legal children/dependants payable to the borrower
- Total loss of the physical property from catastrophe / disaster / major perils up the loan amount.
- Funeral benefits in respect of death of the borrowers, identified spouse and children.

As mentioned above, many of the larger NGO's who are behind enterprise development programs are international with headquarters in the developed world. While obviously local management have a say, building central HQ relationships is extremely important. Alongside this sits social responsibility. To give the poor a chance to become economically independent requires lots of capital and organisations such as us are called upon to make financial contributions to the NGO's.

MFI's are the principal microfinance providers at present in Uganda. It will not be long before the specialized banks become a major participant providing unsecured personal loans to individuals including loans for housing and vehicles. The microinsurance approach to this will need to be different however it will again be on a Partner-Agent relationship

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