SCBF **SWISS CAPACITY BUILDING FACILITY**
Association for Income and Employment Generation

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Innovative Microinsurance Products for Rural Poor in Nepal

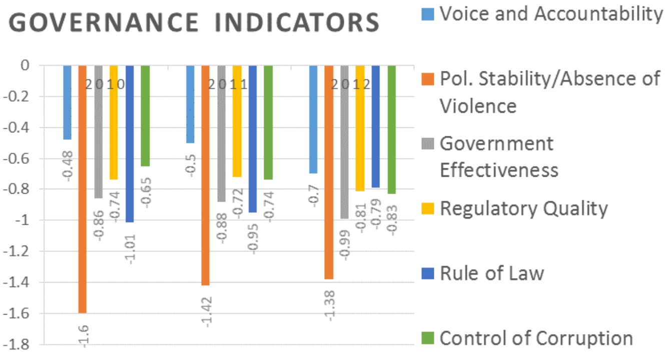
1. Development relevance

Economic and poverty context: With more than 25% of its population below the poverty line, Nepal is one of the poorest and least developed countries in the world. After the insurgency of the Maoists and a decade of armed conflict that only ended in 2006, the country has yet to recover. Real GDP grew by 4,7% on average between 2008 and 2011 which is low for Asia-Meanwhile, inflation rose by 10,5%.

Agriculture provides a livelihood for 75% of the population and accounts for a little over one-third of GDP. Industrial activity mainly involves the processing of agricultural products, like pulses, jute, sugarcane, tobacco, and grain. The trade balance remains in deficit about 25% of GDP. However, the shortfall is offset by large inflows of remittances[i] from manual labourers working mainly in the gulf and India. Official aid has been 4,7-6,6% of GDP between 2008 and 2011. Foreign direct investments are less than 0,5% of GDP.

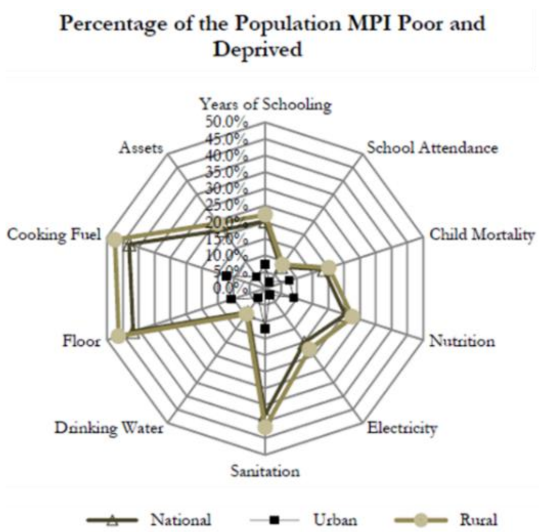
Nepal is in a constitutional crisis since 2008. Elections for a new Constituent Assembly in November 2013 have not yet overcome the political deadlock. Besides the political instability, Nepal's landlocked geographic location, civil strife and labour unrest, and its susceptibility to natural disaster impede economic development[iii]. Since 1996, Nepal's economic freedom score has been stagnant, ranking 147 out of 186 countries.

Population and economic indicators	
Population in million *(2011)*	**27,1**
GDP growth (average: *2008-2012*)	**4.8%**
Inflation (average: *2008-2012*)	**10.3%**
Trade balance (% of GDP) *(2011)*	**-27.86%**
Foreign Direct Investment (net) (% of GDP) *(2011)*	**0.49%**
Net ODA & official aid received (% of GDP) (*2011*)	**4.7%**
Workers' remittances (% of GDP) (*2011*)	**22.05%**
Economic Freedom Index[ii] (2012)	**147**



Improvements in freedom from corruption, business freedom, monetary freedom, and trade freedom have been more than offset by deterioration in other areas, particularly in investment freedom: lack of transparency, corruption, and a burdensome approval process impede much-needed private investment and production. Labour regulations are rigid and property rights are undermined by the corrupt and politically influenced judicial system. Corruption is also endemic in the legislative and executive. Public administration is inefficient[iv].

Despite some progress in poverty reduction in recent years, Nepal remains the 157th poorest out of 186 countries in the world (Human Development Index of 0,463)[v]. 25% of Nepalese live below the poverty line at less than USD 12 a month[vi] and 45% of the people in remote hilly areas where about 80% live. They depend on subsistence farming and household food insecurity and poor nutrition – notably undernourishment of young children – are widespread. Most rural households have little or no access to primary health care, education, sanitation or other basic services. Social discrimination and marginalisation on grounds of ethnicity and caste is also a major reason for inequality and poverty[vii]. Unemployment is high with 46% and rural youth work increasingly abroad in manual labour. Remittances are mainly used for daily consumption (78,9%) and only 2,9% are used for capital formation[vi].



The government of Nepal has adopted the policy of prioritizing access to finance in hills and mountains. Access to financial services such as savings, credit and insurance benefit especially women as most Nepalese foreign workers are rural men while women mostly stay back and look after the household.

Poverty indicators	
GDP per capita (2011, current USD)	477,93
Gini Index (2010)	32,82
Multidimensional Poverty Index (2011)	0,217
National/international poverty rates (2010)	25,2%

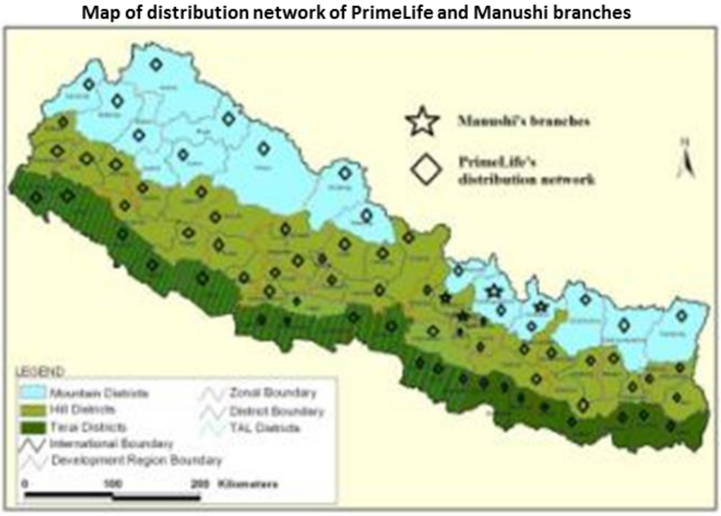
Financial and insurance sector: The financial sector remains fragmented with a relatively small microfinance sector and few significant players accounting for 2,2% of the overall loan portfolio. Over the past 20 years, the Nepali financial system has grown substantially in terms of numbers of institutions, resource mobilization, functional reach and financial viability. In 2011, there have been 31 commercial banks, 87 development banks, 79 finance companies, 21 microfinance development banks, 16 licensed savings & credit co-operatives and 38 licensed financial intermediary NGOs[1]. There are also some very small NGOs/societies and savings & credit co-operatives which are not regulated. The financial system remains dominated by the public sector[2] that accounts for 19% of loans outstanding and 22% of deposits[viii]. While commercial banks, development banks and finance companies compete in urban markets, microfinance development banks, FINGOs and co-operatives compete for savings, credit and insurance services among the poor. In 2010, the market penetration of savings and loans were estimated at 29,3% and 21,2% of the population respectively. Low-income people have access to formal financial services in the Terai region along the border with India and along the country's main highways but limited or no access in remote regions.

Therefore, the government has prioritized hilly and mountainous areas for access to finance through the National Microfinance Policy 2007 offering low cost refinancing options for rural expansion of MFIs. The policy also aims at motivating the poor to mobilize savings. A microfinance credit bureau, which would be an expansion of the existing Credit Information Bureau[3], was expected to be established in 2012/13. The establishment of a separate Micro Finance Authority got stuck in parliament. However, sector participants note that the Nepalese Central Bank treats MFIs increasingly like commercial banks. Customer protection principles are still very poorly developed[ix] but some ongoing initiatives push this agenda forward.

Insurance services are at an infant stage with about 9% penetration rate of life insurance. This rate drops below 2%, if the mandatory term life insurance for migrant workers going abroad is excluded[x]. Only 2,2% of people engaged in agriculture have purchased agriculture insurance in 2011. Some MFIs have started to offer credit life and cattle insurance. Most MFIs offer in-house insurance products to their clients that protect them from financial risks, such as death of the client and his/her spouse, maternity, natural disasters. These products are not providing full-fledged protection from covered risks; monetary coverage is rather modest compared to actual damage or loss. MFIs collect small premiums from their clients, either annually or during each loan disbursement, which feed into the in-house insurance fund of the MFIs. However, the MFIs offer these insurance products without proper market study and actuarial calculations. This makes them vulnerable with regard to large-scale incidences of covered events. MFI clients value such insurance products and may change their MFI for the search of better insurance products.

Partner financial institutions: Manushi works for economic empowerment and socio-economic development of poor Nepalese women by providing loans and savings services to them for self-employment through micro-enterprises. Manushi is a not for profit Financial Intermediary NGO licensed by the central bank of Nepal. It largely operates in rural hilly districts (Kathmandu, Nuwakot, Sindhupalchowk and Dolakha) and has reached nearly 16'000 women through 3'083 groups from 10 branches. About 52% of clients (2011) live in rural areas and about 80% were living below the national poverty line. Manushi offers savings and loan products (according to group lending methodology of Garmeen Bank) and is committed to introduce insurance products in addition to its in-house insurance product – the Social Protection Fund (SPF). Before the project intervention, the SPF offered an insurance package covering death of client, death of client's spouse, maternity and natural disasters and was accessible to all Manushi clients. Today, monetary coverage is higher and the SPF includes a health insurance component but is only available to borrowers. Manushi has

Map of distribution network of PrimeLife and Manushi branches



[1] Financial intermediary NGOs and microfinance development banks can take deposits from their members. FINGOs also have a limited banking license that allows them to borrow from commercial banks for client-lending purposes.
[2] Two government owned commercial banks, Nepal Bank Limited and Rastriya Banijya Bank, and the commercial branches of the Agricultural Development Bank of Nepal
[3] The CIB monitors commercial banks, development banks and finance companies but not microfinance development banks.

performed well between 2008 and 2012: ROA of 5%, ROE of 56%, operational self-sufficiency of 125% in average and a portfolio at risk below 1% (2010)[xi].

Manushi	2008	2011	2012
Total clients	11'000	15'500	15'637
Number of borrowers	7'536	10'429	10'740
Number of depositors	11'000	15'500	15'637
Total staff	41	63	64
Total branches	6	10	10
Total deposits (USD)	0,31m	0,65m	0,91m
Total loan portfolio (USD)	0,62m	1,39m	1,53m
Total assets (USD)	0,66m	1,48m	1,94m
Compound annual growth rate of revenue	96,5%	29,1%	46,2%
Client retention	18%	26%	31%

PrimeLife	2008[4]	2011	2012
BOP clients	0	88	88
Staff	20	214	260
Branches	1	20	21
Premium collected (USD)	15'158	6,70m	9,40m
Net profit (USD)	8'321	1,14m	0,56m
Annual growth rate	n/a	32,15%	54,44%

PrimeLife is one of the leading life insurance companies in Nepal. The company is jointly owned by private business groups and the general public of Nepal with a paid up capital of Rs. 360 million (USD 3,6 million) and is regulated by the Insurance Board. PrimeLife is one of the few insurance companies in Nepal to have a dedicated microinsurance cell since it entered into microinsurance in 2010. PrimeLife has total assets of USD 9,33 million which has grown at a compound annual rate of 39% over the last 5 years. In the same period, its total revenue has grown at a compound annual rate of 12%. The company has sales points in all 75 districts of Nepal. The company issued 866'847 life insurance policies (endowment and term life) till end of 2013. PrimeLife seeks to reach out into the BoP segment through partnerships with MFIs such as Manushi.

2. Intervention approach and additionality

Manushi partnered with PrimeLife Insurance in April 2011 to offer a microlife insurance (endowment) product among its clients. This was a scaled down version of PrimeLife's regular insurance product and failed to perform well as it was not adapted to the needs of rural, low-income clients. Rural clients have limited capacity to pay for premiums. Therefore, the insurance product needed to be appropriately adapted with regard to the premium structure, flexibility in premium payments and complementarities with saving products. The institutions faced following key constraints:

- Lack of an appropriate Management Information System (MIS) on an IT-basis that enables the MFI to manage client data and transactions more accurately and cost-effectively.
- A lack of understanding, experience and expertise of microfinance on the side of the insurer as well as the MFI that partially affected the ability to design and deliver effective pro-poor insurance products.
- Weak delivery mechanism that led to cash management problems at Manushi, delay in premium availability at PrimeLife and late payment receipts for clients. All these led to high transaction cost and low client satisfaction

PlaNet Finance, with the support of SCBF funding, provided technical assistance to overcome these problems. Following activities and outputs were planned for the period from February 2012 to December 2013:

1. Review of the existing microlife product through interviews and focus groups among clients and redesigning of the product. Target of the redesigned microlife product: 4500 new clients within three years of project implementation (100% female clients; 2'300 new clients from hilly regions and 2'200 new clients from Kathmandu)
2. Development of one new microinsurance product based on comprehensive market research and interactions with clients
3. Up-grade of Manushi's MIS system to a fully automated system; selection of an appropriate software and integration of the new MIS
4. Integration of the premium collection into the accounting system and recommendation of appropriate internal control processes
5. Training to enhance the capacity for effective product up-scaling of both Manushi and PrimeLife (30 staff members of Manushi and 4 of PrimeLife)
6. Organisation of a workshop with insurance and microfinance stakeholders to present results and share lessons learnt

3. Results achieved

3.1. Client level

Manushi's in-house insurance product – the SPF was redesigned and successfully piloted by the project. Key elements of the redesign included increasing coverage for death of client's spouse, increasing coverage for natural disasters and introduction of a health insurance component. Cost of redesigned SPF remained the same. Actuarial calculations based accurate pricing of the SPF was a key component of SPF's redesign.

[4] Year 2008 was the first business year of PrimeLife insurance company.

The evaluation survey for the SPF pilot found that all respondents were aware of the changes to the SPF and 95% could name at least 2 changes regarding the microinsurance product. The targets for these two indicators were 80%. The average rating for each of the three changes in SPF features was at least 4.5 out of a maximum score of 5. Clients have better knowledge of insurance now and they hope for continuation in improvements in the health insurance component of SPF. Protection from financial shocks due to critical illnesses covering clients and their family members was one of the biggest benefits for clients from the redesigned SPF. The SPF did not have a health insurance component before the project's intervention and its introduction was very well received by the clients. A respondent from Manushi's Balaju branch during the survey – *"Expenses on health can have big impact on our lives. So we are very happy to get medical insurance facility for us and our family from Manushi. We hope this initiative grows bigger and better."* During the three month pilot (mid September - mid December 2013), the project achieved 38.59% of its total target for 2014, 25% of its final year target for rural clients and 8.95% of its target for urban clients. We believe this is a strong indication that the SPF microinsurance product will meet its targets until 2015.

Target new SPF clients for Y2 (2014)	**2000**
Achievement during the pilot (09/2013-12/2013)	772 clients (=38.59% of Y2 target)
Expected % of women clients	100%
Status after the pilot	100% women clients with coverage for spouse and children ⇒ on track
Target total new SPF clients from rural areas after Y3 (2015)	**2300**
Achievement during the pilot (09/2013-12/2013)	575 clients (=25% of Y3 target)
Target total new SPF clients from urban areas after Y3	**2200**
Achievement during the pilot (09/2013-12/2013)	197 clients (=8.95% of Y3 target)

Prior to the project, Manushi did not keep a managed record of SPF data. Hence, figures before 2012 are not available. Today, Manushi has better data management capabilities for the SPF after the project developed web-based software to manage the SPF.

Outreach for the redesigned SPF	**2012**	**2015/16**
Number of policy holders	772	
% female policy holders	100%	
% rural	74.48%	
% first time insurance buyer (est.)	733 (95%)	
% longer term contingent savings (x>1yr)	0%	
% property coverage	100%	
% health or short-term well-being cover (x<1yr)	100%	
% retention or renewal	N/A	
Average sum insured / limit of liability	Rs. 6,700 (USD 67)	
Expected total claims frequency (<5%, 5%-10%, >10%)	< 5%	
Claim aging data (submitted to paid)	n/a	

Manushi Chautara branch: microfinance center

3.2. Partner financial institution/s level

Both Manushi and PrimeLife have benefitted from the redesigned microlife endowment product which was adapted to needs of the poor and has processes with lower transaction costs now. Some of the key pro-poor features introduced into the microlife endowment product includes waiver of medical clearance requirements for policy uptake, increase in grace period covering two centre meetings as well as reduction in sum assured and premium to make the microlife product more affordable to a wider range of the BOP segment. Furthermore, transfer of information, insurance policy documents and collected premiums between Manushi and PrimeLife using existing channels and involving a bank for premium transfers has increased efficient service delivery and further reduced costs. The support of the SCBF funded microinsurance project has helped PrimeLife as well as Manushi to enhance their understanding of the BoP segment and effective pro-poor insurance products. Unfortunately, the redesigned microlife pilot could not commence yet due to a delay in product approval by the insurance sector regulator. In order to adapt the project delay, PlaNet Finance prepared all the required material for the partners and provided relevant trainings, in order to enable the partners to proceed with the pilot once the approval is received (expected for Q2 2014). Once the Insurance Board approves the microlife product, it is expected to be fully institutionalized 6 months after the pilot and minor modifications resulting from observations during the pilot.

All other outputs have been successfully achieved. The pilot of the second microinsurance product (SPF) developed for Manushi's clients, has been a success as indicated by the results from pilot monitoring and pilot evaluation survey. The redesigned product is now fully rolled out among Manushi's clients. Health insurance component introduced into the redesigned SPF is a key element that distinguishes Manushi's SPF from other MFIs' SPF. Furthermore, the project resulted in another unexpected positive output – the development of a microinsurance software for the SPF. This software is another key element that differentiates Manushi from its competitors. The web based software is the first of its kind in Nepal and drew a lot of interest among the industry during the project's microinsurance workshop in December 2013. Manushi is now one of the few MFIs in Nepal to use web-based software. Manushi is committed to expand the software in all of its branches on its own. It will also bear microinsurance software licensing fees on its own after the pilot.

Key performance indicator for redesigned SPF	2008	2012	2015/16
Duration of claims settlement	>1 month	≤1 month	
Percentage of insured with claims	n/a	2.17%	
Claims rejection ratio	n/a	0%	
Client satisfaction from changes in SPF after the redesign	n/a	4.67 (out of 5)	

The claims settlement process for the SPF has been simplified through the delivery process map. This has led to claims being settled within 1 month, coherent to Manushi's policy. The percentage of insured that filed a claim during the pilot period stood at 2.17%. Claims rejection ratio for SPF was found to be zero during the pilot period. Other measures such as renewal ratio take more time than the three months pilot period to unfold. However, we can estimate client satisfaction from the SPF pilot evaluation survey which found that average client rating for the redesigned SPF stood at 4.67/5.

Manushi has improved its microinsurance product management, shifting from a paper based to a software based MIS. The software is currently being piloted at Manushi's Kalimati branch and is expected to be fully rolled out by beginning of next Nepalese fiscal year mid July 2014. Manushi's CEO, two IT staff and two branch managers have been trained in the use of the software so that they are able to enter SPF transactions and generate key reports on their own now.

The project also trained Manushi's 7 board members on good governance and 20 loan officers on client protection. 10 branch managers were also given Training-of-Trainers on financial education of poor clients. Some of the key visible impacts of the training include introduction of cash flow analysis based loan approval by Manushi which is expected to reduce over-borrowing among clients and introduction of financial education sessions among clients during centre meetings.

3.3. Financial sector level

The microlife endowment product redesigned by this project is based on the model favored by the regulator. Therefore, it is expected to have a high replication potential post approval. SPF, the project's second microinsurance product has an even greater replication potential as similar products are offered by most Nepalese MFIs to their clients. The project's SPF software is also available for use by other MFIs and judging by the interest shown by MFIs during the workshop, the software is set to benefit the Nepalese microfinance industry in near future. In addition, the MIS manual for MFIs drafted by PlaNet Finance based on the MIS experiences at Manushi will greatly benefit other MFIs that are looking to automate their operations.

4. Lessons learnt and further challenges

Good field performance of the SPF reconfirmed that good microinsurance products are developed ground-up through market research. Data migration at Manushi involved a lot of challenges; hence, it is important to have good plan for data migration. It was also realized that new products have to go hand in hand with financial education, especially for insurance products.

Obtaining approval of the Insurance Board for the project's microlife endowment product became a big challenge. After major delays, the process has been restarted with dialogues with the regulator. PlaNet Finance has facilitated PrimeLife in meeting all requirements recently established by the regulator, whereupon the redesigned microlife product was resubmitted to the regulator for approval. Piloting the microlife product will be another challenge and will require persistent assistance of the Technical Assistance Provider.

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