

GETTING THE CHEMISTRY RIGHT

CATALYTIC DONOR STRATEGIES FOR THE MICROINSURANCE INDUSTRY

In chemistry, where the term has its origins, catalysts are substances that, in very small amounts, enable and speed up reactions. Donor funding can have the same effect – speeding up a funded project's success so that others can leverage its lessons to the benefit of the whole industry.

A good example from the microfinance industry is Compartamos in Mexico, founded in 1990 with donor support, as a non-profit NGO. By 2007 Compartamos was a fully licensed bank and had gone public. The Consultative Group to Assist the Poor (CGAP) estimates that Compartamos' initial \$6.3 million in grants have catalyzed over \$130 million in commercial resources. In 2007 The Economist wrote "Compartamos may not be the biggest bank in Mexico, but it could be the most important."

This was a turning point for microfinance. In the early days, few had expected that an NGO could become a powerful commercial bank with influence right across the financial sector. Such industry-wide catalysis breaks the ice for self-sustaining growth.

THE CASE FOR CATALYTIC STRATEGIES

The huge potential market. Low-income people have a huge unmet need for better risk management solutions. In 2010 Swiss Re Sigma estimated the potential worldwide market in microinsurance to be 4 billion people paying USD40 billion in annual premiums. The current market is less than 5% of this.

Donors who are socially motivated are in microinsurance primarily because it protects the economic growth of low income families. Donors are thus willing to "invest" in high potential programs that will generate information and lessons to help push others. Governments also can catalyse industry evolution through targeted development strategies. The Indian IRDA, for example, has led the way in this respect with a quota system requiring insurance sales to the rural and social sectors.

Private sector drivers need successes and know-how. Despite microinsurance growth of 10% and more in some countries, and some products that appear profitable, a clear business case for microinsurance has not yet been made. Even value to clients is an open question. Thus the supply side remains understandably cautious. Potential market entrants need to see more examples of viable microinsurance businesses, and many need expertise and support to bring down the costs and risks of market entry. Thus a key element of catalytic donor strategies is to effectively communicate how and under what conditions microinsurance is successful for its various stakeholders.

WHAT IS A CATALYTIC SUCCESS?

Catalytic strategies are focused and limited interventions that yield long-term impacts on whole markets. If a donor supports an insurer in developing a health-microinsurance product that addresses client needs and is viable, this is a success. However it is only a catalytic success if other insurers learn from it and introduce newer or improved products to a wider market.

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One of the earliest microinsurance ventures that could be called catalytic was at AIG Uganda (today known as Chartis). In 1997, this insurer partnered up with an MFI to distribute microinsurance products, a venture which grew into a rather profitable business. This catalysed replication in various ways: locally, as further microinsurance suppliers entered the market in Uganda, and globally, as AIG's traditional insurance offices in other countries became interested and started developing and offering microinsurance products. The AIG Uganda case had a worldwide influence, encouraging others to get involved with microinsurance activities.

Another example of a donor initiative with (inadvertent) catalytic effect comes from the field of information technology. One Laptop per Child (OLPC) is an initiative to provide low cost computers as learning tools for children, primarily in developing countries. Despite initial problems and controversy about the benefits, OLPC soon it had a catalytic effect on the whole sector. The mere idea of a USD 100 laptop triggered innovations for purely commercial reasons, and these led to the abundant supply of miniature low-cost laptops that we see today in mainstream markets.

HOW DOES A CATALYTIC DONOR STRATEGY WORK?

Imagine a simplified scenario: a national insurance market that shows signs of demand for microinsurance, with a number of potential microinsurance suppliers (or supply partnerships). A donor identifies a first-mover who has a strong interest, but lacks capacity. By providing support, the donor facilitates the pioneer to enter the

market, or improve their products or processes with manageable costs and risks.

Capital is rarely the limitation to massive growth in microinsurance. What is most needed from donors at the first-mover stage is technical assistance to understand the paradigm shift needed for success in the microinsurance markets. Such assistance includes market studies, product design, market education, microinsurance training for staff, and process improvements. As in most industries, pioneers usually experience a barren spell before a venture becomes profitable. If they can get through this phase, however, first-movers occupy the choicest segments of the market and may benefit from higher profits – at least until competition sets in.

First-mover success inspires other market entrants. While these second-movers have to compete with the pioneer and with each other, they can also learn from the first-mover's products, marketing, client reactions and other operational lessons. The ensuing competition increases product diversity and service quality and brings down prices. This is all to the benefit of clients as well as insurers and intermediaries, and furthers the objective of a catalytic strategy. For donors, therefore, the key is to identify a potential market maker and then leverage their success or failure, in order to facilitate others.

Government involvement and donor support follow similar patterns. Once a first-mover breaks the ice by showing that a business is viable, second-movers are likely to follow. This is true in countless markets outside of insurance, whether they be malaria drugs, solar energy, or agricultural productivity.



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The case for catalytic donor strategies looks robust. The experience and research of the microinsurance sector, though expanding, is still thin and fragmented. Nevertheless, some guiding principles for donor-catalysts are emerging.

What are the best conditions for a catalytic strategy? The optimal environment is a market with a number of potential suppliers on the insurer side, awareness of insurance or insurance-like products on the demand side, and government policies that are conducive to microinsurance. Ideally, there would also be several potential delivery channels, insurance skills available on the labour market, and a competitive business culture in which the upper (traditional insurance) market is effectively saturated. However the reality is that conditions in low-income countries are far away from this ideal. In many cases donors must work to build up the various components in the value chain for microinsurance. For example, the Access to Insurance Initiative (A2II) is designed to support countries wishing to do this. It helps countries draft their own national microinsurance strategy, which may include capacity building, market research, client education, and improving regulation.

What first-mover to pick? Any microinsurance market leader worth backing must have a strong interest in, and commitment to, developing microinsurance. A social mission to serve the poor is important, but the main driver of an insurer's strategy should be to reach large numbers of clients on a profitable basis. The partner must recognize that some first-mover advantages will have to be given up in exchange for donor support. For instance, the insurer would have to agree to share lessons, because if the first-mover lessons are not made available to others, the potential catalytic effect could be lost.

A catalyst needs visibility. The catalyst approach needs to publicize both good and bad news of target programs, in national markets and globally. Donors traditionally support publications, conferences, and advocacy, but catalytic processes need to go further, with more diverse and focused communication. Blogs, tweets and similar communications will become important means of publicizing catalytic interventions. As microinsurance is significantly structured around a base of commercial insurers, incentivising those insurers to share information is a significant challenge.



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What do second-movers need? Catalytic strategies can only be called successful when successes of first-movers are expanded and enhanced by followers. Donors can facilitate this by presenting convincing showcases and practical lessons. Even if commercial suppliers are reluctant to share blueprints of their hard-learned lessons, catalyst-donors should compile and analyze experiences where they can, and bring insights and practical knowledge efficiently into the public domain.

Academic papers and books alone will not likely lead to a catalytic result. What is necessary is leveraging knowledge aimed at practical learning, adaptation and implementation, and in a diversity of formats. The technical assistance, grants and research geared towards an array of dissemination formats provided by the ILO's Microinsurance Innovation Facility are good examples of this approach.

Looking at the fundamental questions: Implementing a catalytic strategy also requires stepping back, looking at the core questions and testing assumptions. Microcredit as an industry

has found itself in difficulties due to a number of factors which prominently include promotion of excessive expectations. Microinsurance promoters can learn from this. Promoting achievements only and omitting challenges (or worse, promoting failures as achievements) will not prove effective in the long term. While we cannot expect insurers to broadcast their failures, we can expect donors, researchers and others to honestly and realistically try to understand whether (and if so, when) microinsurance really is valuable to the low income market, and if and when there really is a business case for insurers and intermediaries. Understanding the answers to these questions will be pivotal to catalyst interventions. The MicroInsurance Centre's Microinsurance Learning and Knowledge (MILK) Project, working closely with the ILO's Facility, is looking intently at these questions.

BY WAY OF A CONCLUSION

We cannot know what the microinsurance sector will look like in 20 years, but we do know that there is a market need for valuable risk management strategies from billions of people at the bottom of the pyramid. In light of this, it makes sense for donors to focus on interventions that enhance their effectiveness, and devise strategies to maximize industry-wide impacts. An explicitly catalytic strategy can present a dilemma to donors who have to explain to their constituents why money earmarked for helping the poor is spent on supporting a profitable insurer to explore further potentially profitable markets. Clearly a long-term perspective, a flair for the private sector, and an appetite for learning and risk is needed. As the Bill & Melinda Gates Foundation states in its Guiding Principles: "We take risks, make big bets, and move with urgency. We are in it for the long haul." ■

This paper was prepared by Michael J. McCord, Oliver Zenklusen and Roland Steinmann as a means of prompting further discussion about donors as microinsurance catalysts.

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