MILK Brief #23:
Getting better at improving client value: the case of Fonkoze's Kore W microinsurance product[1]

Microinsurance practitioners face two fundamental challenges as they work to ensure that their products provide value to clients. The first is **understanding** the relative value of those products to clients, a complex and nuanced issue that must be considered in light of the alternatives those clients have to cope with risk. The second challenge is translating these insights into practice by **improving** products and processes to ensure that microinsurance is both valuable and financially viable. The MicroInsurance Centre's Microinsurance Learning and Knowledge (MILK) Project and the ILO's Microinsurance Innovation Facility have developed tools to help meet these two challenges: Client Math and PACE.[2] In 2012, the Haitian microfinance institution Fonkoze partnered with the Facility and MILK to use these two tools to better understand how and whether its Kore W property insurance product added value in the lives of clients and how it might be modified to improve that value. The product itself was modified shortly after the study and following the devastating effects of Hurricane Sandy in October 2012. It is currently under more comprehensive review and is not being offered with new loans. This brief summarizes the results of these two studies, illustrating the complementarities between the two tools and how a deeper understanding of a product's value can translate into practical improvements that better serve clients. We find that while the Kore W product provided value to clients, there was space to improve that value within the financial and practical constraints Fonkoze faced.

Why Kore W?

Haiti has suffered more than its fair share of disaster in recent years, and each hurricane season threatens to set back the fragile progress made since the 2010 earthquake. Small-scale entrepreneurs, owning little more than a house, a stall and a small inventory to sell, risk losing their entire livelihoods each time a storm or earthquake strikes. Haiti's extreme vulnerability to natural disaster makes an important case for the need for catastrophe microinsurance.

The Kore W ("support you" in Creole) product offered by Fonkoze represented a new and innovative product that aimed to tackle one of the most complex risks facing poor Haitians today - the risk of weather-related and natural catastrophes. It was fundamentally a basis-risk policy, where the basis risk covered any claims that exceeded a parametric coverage. This structure was implemented to ensure that affected clients could benefit from insurance coverage even if the parametric reading in their area did not trigger a payment.

Most clients paid a premium equivalent to 3% of their loan upon receipt of their loan, and these premium payments covered approximately 55% of the cost of the product to Fonkoze. The product was mandatory for Fonkoze's borrowers and covered any outstanding loan balance, provided a cash payout of USD125, and pre-approved clients for a new loan. There were no comparable property microinsurance products covering weather risk in Haiti, and low-income people had few other resources to which they could turn when faced with a weather catastrophe.

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[1] The MILK brief was a combined effort of the MicroInsurance Centre's MILK project and the ILO's Microinsurance Innovation Facility and was authored by Barbara Magnoni and Emily Zimmermann of MILK and Michal Matul and José Miguel Solana of the Facility. May 2013.

[2] For a description of the methodologies, please see Magnoni et al 2011, "MILK Brief #9: What is Client Math?" (Client Math) and Matul et al 2011, "Improving Client Value from Microinsurance: Insights from India, Kenya and the Philippines" (PACE).

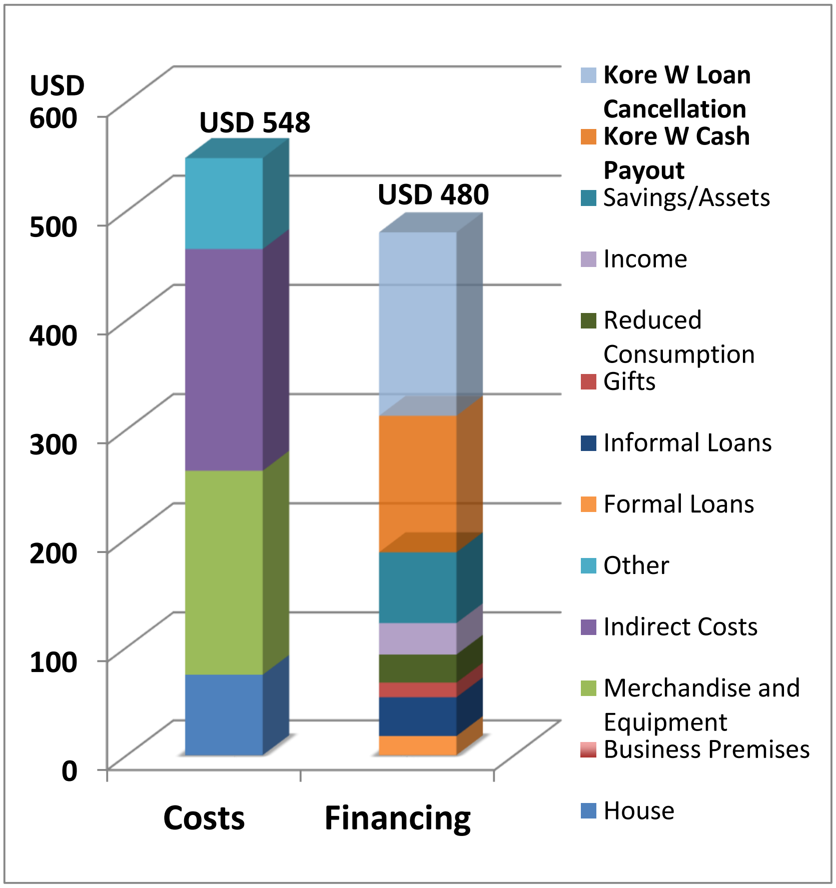
MILK's Client Math study suggests that insured clients did get value

The MILK Project completed a Client Math study which found that the product, while unable to cover all of clients' needs, helped clients avoid the most difficult strategies and bounce back from the disaster more quickly than uninsured respondents in the same area.

The costs from the rain damage were high, on average ***amounting to 2.7 times respondents' monthly income.*** The largest portion of these costs were the ***indirect costs of lost profits and wages*** (see Figure 1).

Both insured and uninsured respondents struggled to recover from the damages brought on by rains, ***financing less than half of total costs they incurred***, on average. Insured clients experienced long delays in claims processing (on average 58 days, which was reduced in the second year), and 63% of them reported additional financial difficulties due to the delay.

Figure 1: Rain damage costs and financing strategies of the insured



Gifts from family and friends, often an important source of financing in other contexts, were largely unavailable to both insured and uninsured respondents in Haiti. ***Both the insured and uninsured relied relatively heavily on savings, asset sales, income, and informal loans to finance the shock.***

However, differences in the financial responses between insured and uninsured still point to substantial value in the product. While ***selling assets*** was a common financing strategy for all respondents, the ***uninsured sold substantially more assets than the insured***, depleting in-kind savings in order to stay afloat, with long-term consequences for their financial wellbeing. The insured, by contrast, were more likely to reduce consumption in the short term – a strategy with fewer long-term financial consequences – while waiting for the eventual insurance benefit.

When the insurance benefit was received, the insured saved or invested over half of the payout on average, using the rest to pay off debt and to increase consumption.

Although the product was designed to cover damage to home or business assets, ***respondents put off all but the most urgent repairs to their homes, focusing instead on regaining their ability to earn income by replacing business inventory.*** The insured were far more likely to replace inventory: at the time of the study six months after the flood, only 33% of the uninsured who lost inventory had replaced it, compared to 62% of the insured.

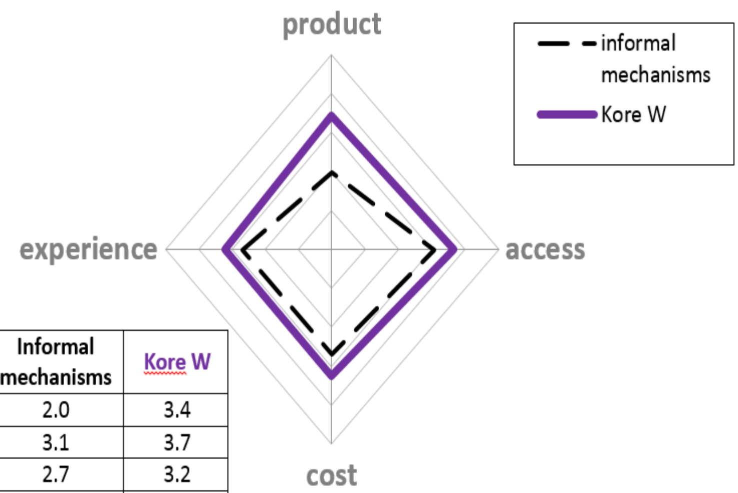
PACE Analysis shows relatively high value of Kore W vis-à-vis informal mechanisms

In light of the unavailability of comparable insurance products in Haiti, Fonkoze's product was compared only to the most prevalent informal mechanisms such as informal loans and selling assets, using inputs from the Client Math study.[3] ***The Kore W product outscored informal mechanisms in each of the four PACE dimensions*** (see Figure 2).

In the ***product*** dimension, Kore W offered a unique but simple benefit package, including some crucial elements such as loan forgiveness, pre-approval for a new loan and a cash benefit that was greater than what most family members could provide.

On the downside, the product was less flexible than informal mechanisms, which can be used to cover a broader range of needs and can potentially be accessed more frequently.

Figure 2: PACE scoring chart: Kore W vs. Informal Coping



	Informal mechanisms	Kore W
Product	2.0	3.4
Access	3.1	3.7
Cost	2.7	3.2
Experience	2.7	3.2

In the ***access*** dimension, Kore W combined a simple, straightforward enrolment process at MFI branches with sufficient education to ensure that clients understood the product and how to use it, though the lump sum, up-front deduction of the premium from the loan amount may have been a hardship for some clients. Nevertheless, Kore W outscored informal mechanisms by a small margin, even though traditional ways to manage risks are often very accessible and clearly understood.

Kore W's ***cost*** to clients was slightly lower than for the informal mechanisms. The MILK Client Math Study helped inform the analysis by showing that alternative mechanisms can have high costs as well. The value for money (premium-to-benefit ratio) was better than loans from moneylenders and asset sales, for example. Depleting savings and selling assets can weaken a household's financial stability and reduce their ability to fully recover, and loans from moneylenders come at high interest rates. Gifts from family and friends are not available in large amounts, especially in the wake of a natural disaster. Loans from family and friends are also limited; when available, they may be cheap but can lead to social strain.

The product's progressive premium structure, which offered a more beneficial premium-to-income ratio to poorer clients, helped to ensure that the product remained affordable for all clients. In addition, to make the product more affordable, Fonkoze directly subsidized the final premium paid by clients.

Finally, from an ***experience*** perspective, the Kore W product showed greater transparency and ease at the time of subscription, when clients were offered simple policy documents in clear language with transparent and clear information about the policy and claims process. A call center offered additional support.

[3] Using 16 metrics PACE assesses the product's client value proposition in four main dimensions: Product (appropriateness of coverage, benefits, eligibility criteria and availability of value-added services); Access (accessibility and simplicity by investigating choice, enrolment, information, education, premium payment method and proximity); Cost (affordability and value for money, and look at additional ways of keeping down overall delivery costs); Experience (responsiveness and simplicity by looking at claims procedures, processing time, policy administration, product tangibility and customer care. Each of the four dimensions is given a score out of 5, relative to the score assigned to alternatives. Poulton (2013) describes the PACE methodology applied in the Fonkoze study in more detail, as well as the full findings of this PACE analysis.

Kore-W's main weakness stemmed from trade-offs with other product dimensions. Long delays in payment of claims were largely a result of the time-consuming verification process, which was required by the product's design. By contrast, some informal mechanisms are often available immediately after the shock and as a result can act as a valuable complement to insurance coverage.

A simpler index-based product might have reduced the claims payment time, but would have introduced basis risk,[4] thus leading to a product that would ultimately have been less equitable and less responsive to clients' needs in the wake of a shock. An alternative option was to develop faster and more flexible systems for verifying claims; these systems have since been developed and have led to improvements in claims speed.

Translating insights into an improved value proposition

The combined lessons of Client Math and PACE can inform efforts to improve Kore W, in the context of available alternatives and amidst all constraints Fonkoze faces.

Insurance and informal mechanisms are largely complementary, where insurance appears to help clients avoid using high-stress informal risk-management mechanisms. The Client Math study points to evidence that Kore W may have helped clients avoid some undesirable informal mechanisms that are far more costly than insurance, such as asset sales. While waiting for the eventual insurance payout, clients preferred to reduce consumption in the short term; the uninsured reduced consumption less and sold more assets, knowing that they had no other relief. For this behavior to take place, clients have to understand what is covered and trust that the insurer will pay. Although understanding and trust are already relatively strong among Kore W clients, improvements in these areas may further enhance the role of insurance in creating positive incentives when a shock occurs.

The current Kore W coverage is insufficient to cover the full cost of the shock, but it cannot cover more and be financially viable. Indeed, given the product's very high subsidy level, Fonkoze will need to reduce coverage to make it more financially viable. Likewise, informal mechanisms are often insufficient, even when combined with the insurance benefit. For this reason, it is crucial for insurance and those other mechanisms to complement one another to the greatest extent possible, in terms of timing, covered risks and availability. Paying claims more quickly can help reduce the need to seek other less efficient strategies and help clients get back on their feet more quickly without needing to increase the benefit amount.

The loan forgiveness was a key component of clients' value in the Kore W product, but slow processing of claims hampered recovery. Fonkoze noted that after Hurricane Isaac, its IT system was unable to quickly assign loan forgiveness benefits and allow for relending. When possible, clients turned to informal loans as "bridges" instead. The Client Math study suggests that these bridges were more common among the insured, perhaps because they used their pending cash claim payment as a form of collateral for informal borrowing.

Speed of payouts should be improved, but insurance is unlikely to ever be the best resource for meeting clients' most immediate needs. After our study, Fonkoze made significant progress in reducing the long delays experienced by clients by revising damage evaluation forms, using 3G wireless devices to send damage evaluations direct from the field, and giving center chiefs more authority to determine final payouts after major disasters (with random audits to prevent fraud). Despite these improvements, claims processing took on average 42 days in 2012, and clients had many needs in the short term for which they turned to other financing mechanisms. Advising clients about the expected date of payment, and exploring new technologies that can speed the process could improve both the effectiveness of the product in meeting clients' needs and client satisfaction.

[4] Basis risk is the difference between the loss experienced by the client and the payout triggered. It could result in a farmer experiencing yield loss, but not receiving a payout, or in a payout being triggered without any loss being experienced. (IFAD 2011)

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This paper combines research from the ILO's Microinsurance Innovation Facility and the MicroInsurance Centre's Microinsurance Learning and Knowledge MILK project.

The Facility offers an array of knowledge documents and other helpful information at: www.ilo.org/microinsurance

The MILK Project provides focused information on the business case and client value at: www.microinsurancecentre.org/milk-project.html