Microfinance Opportunities
"Putting Clients First"

THE DEMAND FOR MICROINSURANCE IN PAKISTAN

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GLOSSARY[2]

Benefit	The amount payable by the insurer to a claimant or beneficiary upon the occurrence of the insured event. The benefit amount should be consistent with the insurable interest. Allowing coverage above the insurable interest creates fraud and moral hazard risks.
Claim	A request for payment under the terms of an insurance contract when an insured event occurs.
Claims processing	The system and procedures that links the occurrence of an insured event with a payout. It is extremely important that microinsurers minimize the time spent in processing claims so that payouts can be made as quickly as possible.
Committee	An informal community savings group similar to a ROSCA.
Cover or coverage	The scope of protection provided under an insurance contract.
Credit life	Insurance coverage that repays the outstanding balance of a loan if a borrower dies.
Economic Stressor	A predictable event that puts pressure on household cash flow such as a marriage or school fees.
Endowment Insurance	Similar to a term insurance except that if the insured survives the term, they receive a lump sum payment representing the cash value of accumulated premiums plus interest. Also called cash value policies. Premiums are more expensive than for term insurance.
Health insurance	Protection from the costs of illness, accidents and other health-related risks.
Insurance	A system under which individuals, businesses and other entities, in exchange for a monetary payment (a premium), are guaranteed compensation for losses resulting from certain perils under specified conditions.
Insured	The policyholder, the person or entity protected in case of a loss or claim.
Insured event	The trigger event that leads to the submission of a claim (e.g., death of the policyholder).

[2] Sources: Churchill, Craig F., Dominic Liber, Michael J. McCord, and James Roth. Making Insurance Work for Microfinance Institutions: A Technical Guide to Developing and Delivering Microinsurance. (ILO: Geneva, 2003). Brown, Warren and Craig Churchill. Providing Insurance to Low-Income Households. Part I: Primer on Insurance Principles and Products. (USAID: Washington, DC, 1999).

Life insurance	Coverage providing for payment of a specified amount on the insured's death, either to the deceased's estate or to a designated beneficiary; or in the case of an endowment policy, to the policyholder at a specified date.
Policy	The legal document issued by the company to the policyholder that outlines the conditions and terms of the insurance; also called the policy contract or the contract.
Policyholder	A person or entity that pays a premium to an insurance company in exchange for the coverage provided by the insurance policy.
Premium	The sum paid by a policyholder to keep an insurance policy in force.
Risk	The chance of a loss.
Risk Managing Financial Services	Besides insurance, emergency loans and accessible savings accounts can help low-income persons to manage their risks.
Term Insurance	Provides basic insurance protection for a fixed period of time (the term). Credit life insurance, where the balance of the insured's loan is paid off in the event of their death is an example of a term insurance.
Verification	The process by which claims are determined as being valid, i.e., for life insurance requiring a death certificate and/or attending the funeral of the deceased. Verification needs to balance two objectives: a) to provide proof that the insured event occurred from two independent parties, b) without causing undue hardship for beneficiaries. Also known as claims validation, claims underwriting or adjusting.

INTRODUCTION[3]

Microinsurance is an emerging financial service. It fills an important gap for consumers by providing them with a risk management tool that, when properly designed and delivered, can reduce the vulnerability of low-income households. Microinsurance is not merely downsized versions of existing insurance products, however. It is a subset of insurance that provides the poor with financial protection against certain risks in a way that reflects the cash constraints and coverage requirements of the low-income market. Because microinsurance is highly technical, a careful assessment of market demand prior to its design and delivery is essential.

This report presents the results of a microinsurance demand study undertaken by Microfinance Opportunities of Washington, D.C. (www.microfinanceopportunities.org), on behalf of the Pakistan Microfinance Network (PMN) of Islamabad (www.pmn.org.pk), in November 2005. This demand study is one element of a larger microinsurance product development process that PMN is undertaking. The full process consists of several sequential steps:

1) Microinsurance course – to raise awareness of the issues surrounding microinsurance products. This was conducted by the Microinsurance Centre in November 2004.
2) The demand study – the subject of this report, undertaken by Microfinance Opportunities in October/November 2005.
3) A supply-side study to assess existing and planned microinsurance products – to (1) refine what should be offered, (2) identify potential insurers and other partners that MFIs could work with, and (3) uncover information about the processes, marketing and efficiencies of various options.
4) Insurer partner selection
5) Design of product prototype(s) based on the demand and supply studies
6) A short, quantitative study to determine the demand for the product prototypes
7) Preparation and then implementation of the proposed product – includes training, systems preparation, and documentation of procedures.
8) Pilot test review and evaluation
9) Product rollout

PMN is interested in promoting microinsurance products among its member organizations. It commissioned this study to obtain market research that its members could use to design and deliver microinsurance products for low-income microentrepreneurs throughout Pakistan. Using a set of practical tools, the study obtained information about key financially-stressful events and risks, and the respective coping mechanisms used by microfinance clients in Pakistan. It evaluated the effectiveness of available coping mechanisms and examined the range of formal and informal insurance options available to the poor. Based on this information, it then formulated and tested several microinsurance product concepts as part of PMN's comprehensive microinsurance product development. In the end, although the research focused initially on the demand for microinsurance, the data revealed a *demand for risk-managing financial services* defined more generally. Thus, this report recommends other risk-managing products such as savings and emergency loans where appropriate.

This report is organized as follows. First, we present a brief overview of the methodology used to carry out the research. Then, we review the main findings regarding the risks and economic stressors that microfinance clients face. A discussion of respondents' principal risk-management strategies and their effectiveness for coping with economic shocks follows. We then present product

[3] The authors gratefully acknowledge the contributions of: Monique Cohen, who reviewed and edited this report; Rebecca May, who assisted with the report preparation; and Pamela Young, who proof-read the final report.

concepts that the research team developed and tested with a small sample of clients. We close with a summary of the report and recommendations for PMN. The recommendations emphasize the need for: client financial education; a better working relationship with the insurers; and a systematic product development process for microinsurance.

The authors wish to express their gratitude to Ms. Mehr Shah of the Pakistan Microfinance Network for her unwavering support, as well as to the team of local consultants (Mrs. Ayesha A. Hussain, Ms. Sadaf Zulfikar, Mr. Mohammad Asad Khan, and Mr. Shafique Ahmed Khan) for their dedicated efforts in conducting the field research.

RESEARCH OBJECTIVES AND METHODOLOGY

RESEARCH OBJECTIVES

The study sought to learn about the risks that microfinance clients in Pakistan face, and the risk-management techniques that they use to mitigate those risks, in order to advise the Pakistan Microfinance Network on potential microinsurance products for its member organizations. To this end, the study defined the following key questions:

- What are the most frequent and financially stressful situations faced by poor microfinance clients? What types of financial stress are associated with these events?
- What coping mechanisms do microfinance clients currently use and how effective are they?
- What are the formal and informal insurance mechanisms currently used by the poor?
- How satisfied are microfinance clients with the existing microinsurance products?
- What opportunities are there for microinsurance products to fill the gaps in microfinance clients' risk management strategies?
- What are the next steps for PMN to take to develop microinsurance products?

The responses to the above key questions informed the formulation and testing of several microinsurance product concepts. They will serve as a basis for further microinsurance product development efforts at PMN and within its network.

RESEARCH METHODOLOGY

The objectives of the study determined the choice of methodology – a qualitative, exploratory approach that aimed at obtaining a deep insight into the research areas outlined above. The study collected primary information through a series of focus group discussions using participatory rapid appraisal tools and a number of in-depth interviews using the AIMS loan-and-savings-use tool, adapted to generate information on the demand for microinsurance products.

The sample group consisted of clients from the two largest microfinance organizations in Pakistan – the National Rural Support Program (NRSP), based in Islamabad, and Kashf, based in Lahore. Both organizations offer services to the poor population, but their respective clienteles are different. For one thing, NRSP operates in rural and peri-urban areas in the Islamabad area; Kashf concentrates in the poor, urban neighborhoods of Lahore. Also, NRSP offers their services to both female and male clients, while Kashf serves exclusively poor women. More detailed information about NRSP and Kashf – including client statistics, product description, and operational results – is presented in Attachment 1 the National Rural Support Program and Attachment 2 Kashf Foundation.

Composition of focus groups was predominantly single-gender - exclusively female in Lahore, and separate female and male groups in Islamabad. In a few cases, the groups were mixed-gender. Having men and women together did not have any adverse effects in terms of the quality of information obtained or the equal participation of clients. All participants had been clients of either of the two organizations for at least several months to several years. Based on the levels of monthly household income, which ranged from Rs. 6,000 to Rs. 20,000 (US$100 to US$300), participants were moderately to very poor. Many lived on a dollar or less per day per household member, given the typical family size of four to eight members. About a quarter of female participants generated income through activities like animal husbandry and milk production (in rural areas) or dressmaking (in urban areas).[4] Male participants participated in micro-businesses such as trade, agriculture, and services (e.g. driving rickshaws and taxis), or earned wages as masons, tailors, or daily workers.

Attachment 3 – Field Work Schedule presents the actual schedule of field research and the specific tools used. A total of 44 focus group discussions and 15 in-depth interviews were conducted, with a total of over 350 participants.

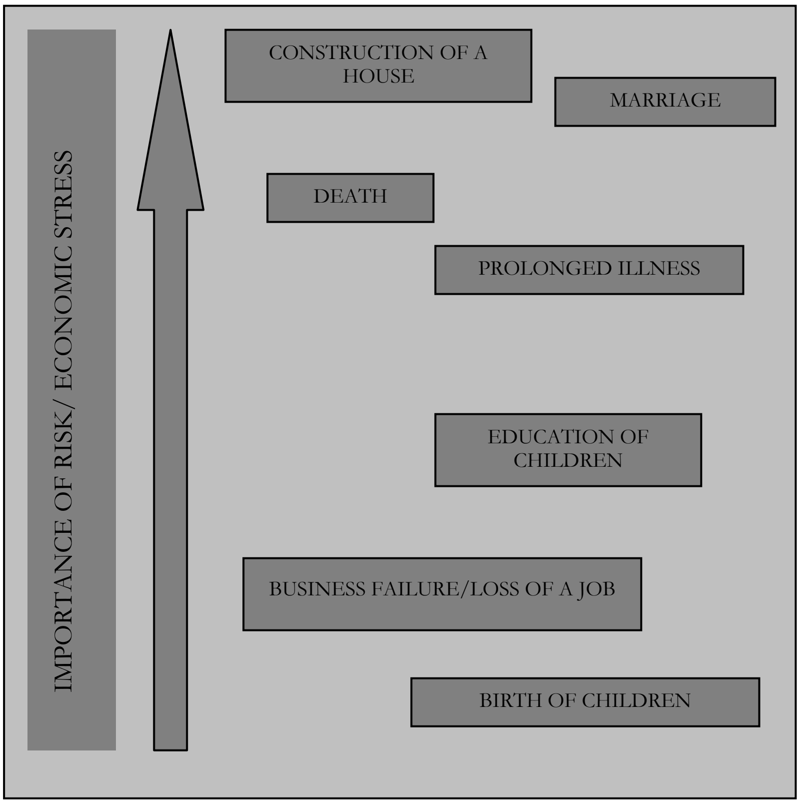
[4] The remainder of the female clients did not report any regular independent business activities.

Low-income families strive to maintain the fragile balance between limited income and on-going financial needs. Given the precariousness of their financial situation, events that require additional expenses can deal a heavy blow to the poor. To better understand their financial implications on low-income households, this study began with a look at these stress-producing events, which can be categorized as either risks or economic stressors. Risks are unpredictable events that result in an economic loss. Economic stressors are predictable events – usually associated with milestones in one's life, like marriage – that put pressure on cash flow when expenditures exceed income. This study included both types of events, thereby allowing for a more comprehensive understanding of the dynamics of household economics, the coping options available to the poor, and the motivations for the choices of risk-managing strategies.

Coping mechanisms fall into two categories. The first consists of strategies that people do ahead of time in order to reduce their vulnerability to shocks and economic stress, such as risk avoidance, risk reduction and efforts to protect against risk. The second consists of loss management strategies that take place after a shock has occurred. The research examined both types of mechanisms and their effectiveness.

Attachment 4 presents a table that summarizes risks, key economic stressors, and coping mechanisms. A comparative ranking of risks and economic stressors by the degree of financial pressure that each exerts on households is presented in Box 1.

BOX 1. IMPORTANCE OF RISKS/ECONOMIC STRESSORS



RISKS

According to respondents, the risks that place the greatest amount of economic pressure on households are:

- Death of a family member
- Prolonged illness
- Business loss or failure

DEATH OF A FAMILY MEMBER

Respondents viewed death in the family as the most stressful risk. In addition to the emotional stress of losing a loved one, the bereaved family is expected to cover all funeral expenses and prepare a sumptuous reception for the mourners. In many locations, the mourning period can last up to 40 days after the actual death bringing the total cost of the funeral and related expenses to anywhere from Rs. 8,000 to Rs. 25,000 (US$133 to US$416).

Precautionary coping strategies are not common in these cases. Some respondents said they had not saved for this event, but a few were able to take advantage of life insurance policies. Other strategies included:

- The use of savings – particularly in the case of an expected death, the family will save by limiting household expenditures and taking on additional work.

- Informal borrowing – predominantly from friends, since borrowing from relatives for a funeral is not considered socially acceptable.

- Insurance – a limited number of clients have access to either MFI-provided insurance or formal insurance.

- Sale of assets (e.g. jewelry or electronics) in situations of extreme hardship – this happens rarely.

During general discussions of risks and economic stressors, respondents did not differentiate between natural and accidental death, but they did distinguish between the death of a relative and that of a household's breadwinner. The latter is clearly more devastating financially, as they described it as an "economic crisis" or "disaster." Respondents provided more details regarding its long-term financial impact on households during discussions of insurance products (see section Significant Gaps and Possible Solutions).

As an unpredictable risk, the economic hardships caused by a death in the family could be alleviated through the introduction of a life/accident insurance product or funeral insurance.

PROLONGED ILLNESS

All participants perceived health issues as a major risk, although they distinguished minor health problems, which they considered easier to deal with, from major illnesses that often require hospitalization and make tremendous claims on household finances. Chronic diseases like hepatitis, diabetes, tuberculosis, and chronic kidney problems – all of which are very prevalent in Pakistan – can place a significant financial burden on many households. Accidents, usually traffic- or workplace-related, can be equally onerous.

Health services are usually available locally, even in rural areas, although the quality of these services is very low because many of the village "doctors" do not have specialized education and are not regulated by the government. For serious problems, people prefer to go to the nearest city, where they can choose between private health service providers, which are expensive, and government hospitals, which are cheaper but offer inferior quality services.

Costs of health services range from Rs. 30-50 (US$0.50-0.83), for a visit to a local village doctor plus some simple medications, to Rs. 100-500 (US$1.67-8.33) for a visit to a private doctor in the city. In cases that require hospitalization, respondents said they use government hospitals that do not charge for the bed. Nevertheless, many end up paying Rs.1,500 to Rs. 3,000 (US$25 to US$50) per day for hospitalizations due to medicine and other expenses like transportation. What's more, families are often expected to host and entertain remote family members who come to visit the sick person, which can add substantially to the already-heavy financial burden.

> *"I spend a lot of extra money on medical expenses. They are even higher than school fees and transportation costs for my children. I have to pay a school fee of Rs 200 per month, whereas one day's worth of medical checkups and transportation requires an amount of more than Rs 200!"*
>
> *Woman client*

Most respondents said they do not use precautionary strategies for dealing with health-related expenses, at least in comparison to other risks and economic stressors. They do save in anticipation of maternity expenses (see Birth of Children), which suggests that people save for predictable events only. Low-income clients may also have too many other pressing needs that they cannot save for health-related expenses, preferring instead to "pay as you go" when health emergencies strike. Respondents described a wide range of coping mechanisms, most of which are loss-managing strategies:

- Home savings – Almost every family has at least Rs. 500 (US$8.33) at home for emergencies in a "mattress account."
- Loans from friends and family – These are widely used and commonly available. Respondents said it is easy to borrow Rs. 1,000-3,000 (US$17-50) to pay for treatment. These loans are interest-free and have no set terms for repayment.
- Additional work to earn more income
- Decrease in household consumption
- Major help from extended family – In several cases, rich relatives will cover the cost of treatment without the expectation of having to be repaid.
- Loans from MFIs – This is a diversion from the stated use of productive loans.
- Liquidation of assets – predominantly jewelry and livestock; land plots in extreme cases
- Borrowing from moneylenders – accessible to the urban population
- Postponement or early termination of treatment, or no treatment at all

Respondents said that, in most cases, they are able to deal with minor health issues. Problems involving chronic illness or requiring hospitalization, however, can debilitate a poor family. Quality savings services could help to minimize such a risk. Another possible solution is specialized health insurance, which appears in sections Coping Mechanisms: Features, Accessibility and Effectiveness and Significant Gaps and Possible Solutions

BUSINESS FAILURE/LOSS OF A JOB

Risks associated with a loss of a job or business failure are generally tied to the general economic situation in the country, and microfinance services are of limited help. The nature of the risk associated with losing business assets due to unexpected breakdowns, theft, or natural disasters is different, however, and could be insurable.

Clients mentioned that the loss of equipment, goods, or premises can cost from Rs. 50,000 to Rs. 300,000 (US$833 - US$5,000) in lost assets, which include goods like livestock, a stream of income, and – in some cases – the entire business itself. At the household level, the loss results in lower consumption and difficulty in repaying loans. At the enterprise level, the entrepreneur may go out of business, although respondents reported that a complete loss of business assets is much less likely to occur compared to other economic stressors or risks.

The precautionary coping mechanisms for dealing with a loss of business assets are:

- Use of home savings
- Use of *committee* savings
- Informal insurance – a group of shopkeepers pay in small amounts monthly and use the money in case of an emergency
- Investment in household assets

After the fact, clients rely on other strategies to recover from the loss:

- Moneylenders – available to the urban population
- Borrowing from friends and family or from an MFI
- Reducing household consumption

An effective response to this type of risk could be a conventional asset insurance product. However, since the respondents perceived these risks as lower priority, such products could be looked into and developed at a later stage.

KEY ECONOMIC STRESSORS

Respondent cited the following as the top economic stressors, in terms of the amount of economic stress that each puts on a family:

- Construction of a house
- Marriage of a son/daughter
- Education of a child
- Birth of a child

CONSTRUCTION OF A HOUSE

Construction of a house was the most frequently cited source of financial pressure for a household, with costs ranging from Rs. 60,000 to Rs. 300,000 (US$1,000 to US$5,000). Even in multi-generational homes, an addition to a house – which the marriage of a son usually requires – can cost about Rs. 50,000 (US$833). Despite the high cost of construction, many respondents said it was their dream to build their own home, so much so that they are willing to forego other needs – including health-related expenses – in order to achieve it.

> *"I live with my relatives in this village. They are very kind to give me a place to live, but I have to construct my own house one day. I can only think of it and not able to make it happen. The inflation rate is very high and everything else is so expensive. My household expenses alone exceed my income. I borrow loans and try to participate in committees but they are not enough. Construction of my own house is a dream for me!"*
>
> *Woman client*

A few respondents viewed investment in housing as a source of additional income through renting the unit. A typical room brings in between Rs. 1,000 and Rs. 2,000 (US$17 and $US33) per month, with rents increasing due to an influx of post-earthquake population.

Respondents said that they typically use savings and loans from friends and family to construct a house. Savings take two forms: cash (in home and in "*committee*"[5]) and construction materials. Because savings and informal borrowing are rarely adequate to cover the cost, respondents said they will try to obtain "productive" or "microenterprise" loans, without ever reporting the actual use of the loan to the MFI. Clients also reported working overtime, receiving salary advances, and reducing household consumption as means of coping with this expense. In addition, they mentioned that borrowing heavily from family and friends can cause mental anxiety and increase social pressure.

Since housing construction is not an unpredictable risk, microinsurance is not a suitable solution, but a long-term or contract savings product, as well as a specialized housing loan, could be helpful.

MARRIAGE OF A SON/DAUGHTER

Marriages within the family pose a significant financial stress on households, second only to construction of a house. Traditionally, parents are responsible for covering the costs of their children's weddings, which include the reception, dowry for the daughter, and expensive presents for the bride's family from the groom's family. These traditions differ slightly depending on the community and/or ethnicity of the family, but total wedding costs generally fall within the range of Rs. 80,000 (US$1,333) to several hundred thousand.

> *It is difficult for us to marry our daughters. Dowry has always been an issue for us. We have to give our daughters furniture, jewels, clothes, utensils, and gifts to the groom's family. Although we started collecting items for our daughters when they were born, there are many other expenses at the time of a wedding. Providing the guests with meals can cost Rs 30,000-Rs 40,000. We manage by asking our relatives for loans and in-kind gifts. The amount in committees is not sufficient to cover the costs of a wedding, so we pool together two or three small committees."*
>
> *Woman client*

Because weddings are anticipated events, they allow for the use of a mix of precautionary and loss management strategies. Typical coping mechanisms before the event include:

- Starting in-kind savings soon after a child's birth – They include jewelry and expensive household items like furniture, refrigerators, and bedding.

[5] *Committees* are informal community savings groups similar to ROSCAs in other parts of the world. In Pakistan, they typically consist of a dozen to several dozen participants who will contribute on a monthly basis. Monthly contributions vary from Rs.20 to Rs. 3,000 (US$0.33 to US$50) for a period of one to several years. Members usually draw numbers for their turn to get the lump sum.

- Saving cash closer to the time of the event through *committees*
- Borrowing from friends and family
- Borrowing from MFIs – by diverting "productive" loans
- Borrowing from Village Organizations
- Borrowing in-kind from shopkeepers – for example, food or jewelry
- Borrowing from money lenders – accessible to the urban population
- Selling household assets – including land

The social pressure to marry off children – especially daughters – can be great, and respondents said they use all available options in order to live up to their obligations. Coping mechanisms range from relatively low-stress strategies (e.g. long-term savings, *committee* savings, and savings in-kind) to rather high-stress strategies (e.g. sale of assets) that can affect the long-term productive capacity of the household. Some of the traditionally common coping mechanisms, such as in-kind savings, have become less popular as social pressures dictate that gifts purchased for the newly-weds be up-to-date with current styles and fashions, thereby increasing the popularity of cash savings and borrowing. Price inflation and the consequent increase in the cost of goods and services add to the financial pressure on families.

> *"We have to spend a lot on our son's wedding because the girl's family is demanding expensive gold ornaments and items, and we have to provide them. We are seeking loans from shops and relatives for this purpose, our committee is helping us to get through this event, and our family is bringing gifts that we can use. We will have to pay back our relatives in the same way, so we are keeping a record of who has given what. A son's wedding costs about Rs 300,000- Rs 400,000."*
>
> *Woman client*

After the marriage, households must figure out ways of dealing with their debts. Some respondents said that they reduced their consumption and other household expenditures in order to repay these debts. Others reported being in continuous debt as a result of a marriage. Given that most families have several children, the long-term burden of recurring wedding costs is significant.

Respondents viewed the marriage of a son or daughter as one of the most challenging economic stresses. As opposed to the one-time construction of a house, weddings are especially burdensome because large families must pay for the marriages of several children. Access to specialized savings or loan products could provide some relief, although many low-income people have difficulty saving. In these cases, a specific endowment accident and/or life insurance could be more appropriate since these products would force the client to save on a schedule (see page 18 for details).

EDUCATION OF CHILDREN

In general, clients perceived education as an extremely important prerequisite to a better life for their children, and many attached the highest priority to educational expenses. Even those from very poor families said they will set aside money for education. So important is education that a large number of respondents decided to send their children to private schools – even though private schools are more expensive than government schools – because they provide a better education (monthly tuition at government schools is roughly Rs. 20 to Rs. 35 or US$0.33 to US$0.58; private schools charge Rs. 100 to Rs.400 or US$1.67-6.67). The additional cost of materials, books, uniforms, and transportation (predominantly for daughters) can total Rs. 500 to Rs. 600 (US$8.33 to

US$10.00) per month. Families generally prefer to send their sons to schools, especially for further education.

Households pay for on-going educational expenses through current income sources, savings and loans. Seldom is this enough, however, and many children cannot pursue further education as this requires higher expenditure, in terms of both tuition and related expenses. The enrollment fee for college may not be high, but because colleges are usually located in cities, many families cannot afford the higher level of expenditures from supporting a child to live in a distant city.

> *"I used to work in a village-based organization, but I had to leave the job. When I was working, it was easy for me to pay for my children's education, but now I find it very difficult to cover the cost of the educational expense. I prefer to pay for my children's education to everything else, and so I cut on my other household expenses to make sure that I meet every cost of education."*
>
> *Women client*

In order to pay for education, respondents named the following strategies:

- Additional work – increasing regular income
- Cutting down on other household expenses – even food consumption
- Negotiating postponement of school fee payment
- Informal borrowing – from friends and relatives
- Not sending daughters to school
- Pulling children out of school – in cases of extreme hardship

Most families are able to send their children to primary and high schools, although many go into debt in order to meet these recurrent expenses. Savings products could be an appropriate financial solution, but a specialized insurance product – e.g. a life/accident endowment insurance – may be necessary to meet the financial needs of those who pursue higher education beyond secondary school. This option is discussed in section Significant Gaps and Possible Solutions.

BIRTH OF A CHILD

Female respondents differentiated risks associated with childbirth from general health-related risks. They mentioned that families have to come up with additional funds to pay for medical checkups and delivery assistance. These medical services are provided locally, mostly by midwives (expectant mothers seek assistance from hospitals only when there are complications). Because local midwives are generally of very low quality, they often diagnose complications too late, resulting in high mortality rates among mothers and newborns.

> *"It's very difficult to manage our maternal health while living in the village. The doctor is not trained and cannot provide us with the right medications. We have to visit clinics and hospitals in Rawalpindi, which are very expensive - delivery costs about Rs 2000 to Rs.3000 – and also quite far from our village. The local van charges high rates to reach them and – in a few cases – the woman and the newborn died before reaching the clinic in time."*
>
> *Woman client*

Precautionary measures for dealing with pregnancies include:

- Use of home savings or "mattress" accounts
- Once pregnant, specific savings for childbirth – including cash, food, and clothing.

When there are very few resources available, an expectant mother may take more drastic measures, like:

- Not seeking needed medical assistance

While there is a need for a comprehensive health insurance that covers childbirth, such a policy could prove difficult to provide from the supply side because adequate premiums are likely to be prohibitively expensive for most clients (for more information, see section Significant Gaps and Possible Solutions).[6]

COPING MECHANISMS: FEATURES, ACCESSIBILITY AND EFFECTIVENESS

LOW-STRESS COPING STRATEGIES

Borrowing from family members and friends. Local cultural traditions condition the specific features of coping mechanisms available to the low-income population in Pakistan. Very strong community, family, and ethnic (*baradri* system) ties make borrowing from family members and friends a widely used and easily accessible method of managing a crisis. In most communities, individuals can access an instant loan of up to Rs. 3,000 (US$50) in case of need. The lender will not ask for interest and, in most cases, will not fix a repayment date, expecting to be repaid whenever the borrower is able. Respondents said they used such loans for almost all household purposes, including health problems, accidents, and businesses.

Savings. While there are special occasions for which people will save (notably, marriages), all respondents (apart from the poorest) reported keeping a relatively small amount of money at home in a "mattress account" for emergencies. These amounts ranged from Rs. 200-300 (US$3.33-5.00) to Rs. 2,000-3,000 (US$33-50) and are "safety cushions" to be used in times of need.

"*Committee*" savings. Similar to ROSCAs in other countries, *committees* form a traditional system of informal, community-based savings circles. They are particularly popular among women, who use them to save with a special purpose in mind.[7] Respondents reported participating in more than one *committee* depending on their needs. Though common, *committees* have limited use in crisis management, since only a few *committees* will allow a member to jump the line and access cash immediately in an emergency.

Loans from MFIs. Access to microfinance services remains limited for the low-income population in Pakistan[8], but wherever they are available, MFI loans are widely used for managing emergencies. A few MFIs – including Kashf – have begun offering a wider range of loan products, including a loan designed specifically for use in an emergency. Yet the study discovered that

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[6] Research in Nepal found that women did not want health insurance for maternity because it was the family's responsibility to pay for maternity expenses. The women did not want it to become solely their responsibility. (Simkhada et. al., 2000.)

[7] Members will pay in an agreed upon monthly installment and receive a lump sum when their turn comes (decided by drawing lots). Respondents participated in committees with monthly payments ranging from as low as Rs. 20 (US$0.33) up to several thousand rupees yielding lump sums from less than Rs. 1,000 (US$33) up to Rs. 300,000 (about $5,000).

[8] Data for 2004 show just over 300,000 borrowers and over 1 million savers nationally while the outreach target is 6 million. (Performance Indicators Report 2004, www.pmn.org.pk.) The population of Pakistan was estimated to be 162.4 million as of July 2005. (CIA, World Factbook, www.cia.gov.)

borrowers do not always use loans for the originally stated purpose. In group discussions, respondents reported intermittent use of general (or "productive") loans for emergencies, and that of emergency loans for business investments. The finding is not surprising, as other studies have also highlighted the fungibility of microfinance loans.

HIGH-STRESS COPING STRATEGIES

The four coping mechanisms described above are low-stress, easily accessible and widely used. They are effective in mild to medium crises. In cases of major emergencies requiring larger amounts of money, however, these strategies are usually supplemented by other, higher-stress solutions (see Attachment 5 Montgomery's Classification of Coping Strategies by Their Level of Stress). All high-stress responses result in the loss of productive capacity and lower future living standards for the household.

Liquidation of assets. The selling of valuable household items like refrigerators, TV sets, jewelry, and business assets (in rural areas, these include livestock and land) can provide quick cash.

Borrowing from moneylenders. Moneylenders operate predominantly in urban areas. They generally charge a very high price for the loan (10% interest per month) and allow for no partial payments. As a result, the amount paid on interest can be several times the principal amount.

Ignoring the situation. In cases of extreme poverty, families will ignore health problems or stop spending on children's education.

High-stress responses can provide temporary relief, but it could also ruin a family's economic situation in the long run because of the following reasons:

- A lower income level – after selling off business or productive assets
- A debt trap – as a result of borrowing and taking on too much debt
- Lowering of living standards – after selling off household items

Ignoring health problems is particularly dangerous, since it could lead to a total loss of income due to the inability to work. In more extreme cases that – unfortunately – are not uncommon, it could even lead to death.

Despite the availability of several different kinds of coping mechanisms, respondents often reported that they could not cover either the economic losses that they had incurred or the large expenditures that exceeded their normal, day-to-day household expenses.

Participants of the study were not typical of the poor in Pakistan in that – unlike the majority of the low-income population – they have access to microinsurance services through Kashf and NRSP. Yet they did not emphasize microinsurance during the discussions. While the NRSP product is probably too new to have any impacts, the same does not hold for the Kashf product – an observation that raises the question of the contribution that Kashf microinsurance is making to the risk-managing strategies of their clients.

FORMAL INSURANCE PRODUCTS

The availability of microinsurance is growing in Pakistan. Formal insurers are reaching down-market to the lower-income population and expanding geographically through the use of insurance agents. Both Kashf and NRSP offer microinsurance products to their members, with Kashf offering a compulsory life/accident insurance tied to a loan, for the duration of the loan and NRSP offering a voluntary health insurance introduced in October 2005. The study used focus group discussions to explore client satisfaction with both products. Details are discussed below.

KASHF LIFE/ACCIDENT INSURANCE

Kashf offers life/accident insurance in cooperation with a national insurer, New Jubilee Insurance Company. Kashf acts as the agent and the purchase of insurance is compulsory for all borrowers. The current microinsurance product has the following characteristics:

FIGURE 1: KASHF'S LIFE/ACCIDENT INSURANCE PRODUCT

ACCESS	**COMPULSORY**
Coverage	Accidental or natural death of the borrower
Benefits	Rs. 7,500 (US$125) to cover funeral expenses, plus the outstanding loan amount is written off
Premium	1.5% of loan amount
Method Of Premium Collection	Payable at the branch at the time of loan disbursement or to the team leader of the loan group
Claims Process	Documents to be presented to the branch proving the client's death (death certificate or cemetery slip). Benefits paid same day or the day after a client's death
Documentation	Records of the premium payment are entered into the borrower's book and acknowledged by the client through a thumbprint

The insurance product serves a dual purpose: on the one hand, it drastically reduces Kashf's credit risks related to the client's death because it pays off the balance of the loan outstanding; on the other hand, it provides specific but limited protection to clients. The clients mentioned that the funeral benefit of Rs. 7,500 (US$125) is helpful for covering immediate expenses, but it is insufficient to meet the overall cost of a funeral, which is usually around Rs. 20,000 to Rs.25,000 (US$333 to US$417)). Since the insurance benefit covers only 30 to 35% of total costs, other means are required to cope with a funeral. For example, a family may have to use its savings, borrow from friends and family, or borrow from moneylenders. In general, clients did not highlight the fact that the remainder of the loan is written off.

The respondents valued the simplicity and convenience of the claims process and benefit payment. The fact that the money is available to the family of the deceased the day the death occurs was very important to them. They liked being able to keep all records of the insurance-related transactions in one book, just as they do for loan and savings.

> *"My daughter had a loan of Rs. 10,000 from Kashf and she died of hepatitis. The Kashf people visited me to pay their condolences. They gave me Rs. 7000 and waived the remaining loan installments. With the Rs. 7000, I managed guests and certain other expenses. For the rest I had to borrow from neighbors."*
>
> *Woman client*

The majority of the participants in the insurance program have a good understanding of the product offered. Some participants expressed confusion about whether the policy also covers other family members, suggesting the need for better client education on this product. Most clients felt that the premium amount – set at 1.5% of the loan amount – was affordable.

In one of the four groups, respondents said that they would not have paid for the insurance had it not been obligatory. Even though they knew of cases in which insurance was paid, they did not want it, possibly because of its affordability or the general (negative) perception of insurance. The demand for microinsurance among microfinance clients is thus far from certain. To understand more fully the demand for microinsurance, segmenting the client market and assessing demand more carefully is crucial. The data, while not definitive, indicate that poorer clients are less inclined to purchase insurance if it is voluntary.

NRSP HEALTH INSURANCE

NRSP offers a **combination of health, accidental death, and disability insurance** to their clients in cooperation with Adamjee Insurance Company. The National Rural Support Network, the umbrella organization for a dozen local rural support organizations – the largest of which is NRSP, negotiated the service, involving a one-time purchase of 150,000 policies at a cost of Rs. 31,200,000 (US$520,000), which the MFIs would resell to final users. NRSP's partners are not obliged to provide insurance for their clients, although most choose to do so. The program started in late October 2005. By the end of November, about 70,000 of policies had been sold through local community organizations.

FIGURE 2: NRSP'S HEALTH INSURANCE PRODUCT

Access	Voluntary, offered to rural members of community organizations
Coverage	Health and accident – hospitalization over 24 hours, accidental death and disability
Benefits	Up to Rs. 25,000 (US$417); disability pro-rated depending on severity
Premium	Rs. 208 (US$3.47) per annum, plus Rs. 42 (US$0.70) to NRSP for administration (Rs. 250 total (US$4.17))
Method of Premium Collection	Payable at the community organization
Claims Process	Death, disability, or illness need to be documented by a certified doctor. Expenses born by the insured person will be reimbursed
Documentation	Insured persons are issued a written policy

Since the product has been introduced only recently[9], respondents had no experience with the actual use of insurance when the research was carried out. In terms of understanding of the product itself, there were different opinions:

[9] At the time of the study only half a dozen claims were being processed and it is difficult to evaluate the actual time the claim will take to be processed.

- Some considered the insurance to be obligatory for borrowers – raising questions about how it is being sold
- Others believed that the policy also covers family members
- Few mentioned that the policy covers health – most mentioned death and accident only
- None could articulate the process for obtaining a payout in case of illness

The situation could improve once clients start to file claims. For now, they seemed satisfied with the convenience and affordability of the policy, but some thought that the premium should be reimbursed if they do not file a claim. Again, this demonstrates the need for better client education on microsinsurance products. Nonetheless, there was a strong feeling that the scheme is legitimate, in large part because of NRSP's good reputation. In other words, clients are buying the insurance based on their trust in NRSP.

OTHER FORMAL INSURANCE SERVICES

About three-quarters of the respondents were familiar with the insurance services offered by formal insurance companies. Even in rural areas, people knew about insurance because formal insurers are trying to penetrate the market through agents who are often members of local communities. Respondents were most familiar with the following products, both of which are provided by the State Life Insurance Company of Pakistan:

- Endowment life/accident insurance
- Regular life/accident insurance

Most clients said that they see insurance as a preferred way to save, since it has an added bonus of a lump sum payment in case of death or accident. They use insurance to save for special needs, including children's marriage, education, and even paying off larger debts. The fact that they used endowment insurance products as a means to save shows that they were familiar with the product.

Because of the high premiums required by formal insurance policies, which ranged from Rs.1,500 (US$25) to Rs 6,000 (US$100), only upper- and middle-levels of low-income respondents (those with over Rs. 10,000 or US$167 in monthly household income) used insurance. To pay for the premium, these clients saved through *committees*. Insurance policies were drawn for periods from 5 to 20 years, with coverage ranging from Rs. 30,000 to Rs. 150,000 (US$500 to US$2,500).

SIGNIFICANT GAPS AND POSSIBLE SOLUTIONS

The focus group discussions and individual interviews revealed that, in many cases, the coping mechanisms of the microfinance clients are only partially or minimally effective in emergencies or economically stressful situations. As a result, families can lose assets, fall into debt traps, and remain indebted for long periods of time. These gaps suggest opportunities to introduce new risk management instruments to help low-income households reduce their vulnerability and better cope with particularly stressful risks. Microinsurance products that can fill such gaps include endowment insurance for the education and marriage of children, health insurance, and extended life insurance.

The research team designed product concepts based on the information gathered in the study. It then presented these product concepts to microfinance clients in iterative focus group discussions and solicited their reactions. After each discussion, the research team adjusted the product parameters to better meet the needs and expectations of the clients. Because the goal was to get an indication of clients' willingness to pay for the product, its pricing was based on similar products, and not on actual costs. No insurance companies or insurance professionals reviewed the prices.

MARRIAGE AND EDUCATION OF CHILDREN

Respondents said marriage and the education of their children are very important, and both cause significant economic pressure on families. Current coping mechanisms (primarily *committee* savings) are not fully satisfactory because these savings schemes have limited time periods and relatively small lump sums. Also, *committees* are less popular in urban areas where community ties and mutual trust are weaker. An endowment insurance product, which combines features of insurance against loss of life/accident with an attractive savings mechanism, could help to reduce some of the financial pressures resulting from marriage and education expenses. To test this idea, the research team designed prototypes to address the following:

- Provide low-income people with a lump sum adequate to cover or significantly contribute to financial needs associated with children's marriage or education
- Make the product affordable, especially in terms of the size of a single payment (possibility of annual or monthly payments)
- Make the product attractive and competitive by providing accumulated funds that yield annual interest
- Provide a convenient and simple procedure through a trusted local organization with minimal paperwork

To better understand respondent's needs and preferences in this area, researchers presented an education endowment insurance product to clients from NRSP and a life endowment product to clients from Kashf. The product parameters are listed in the table below:

FIGURE 3: LIFE AND EDUCATION ENDOWMENT INSURANCE PRODUCT CONCEPTS

ATTRIBUTE	NRSP: EDUCATION ENDOWMENT	KASHF: LIFE ENDOWMENT
Coverage	Life Children 10 years and up Period of 10 years Coverage between Rs. 10,000 (US$167) and Rs. 25,000 (US$417)	Life Accident related disability Children 5 yrs and up Minimum term: 10 yrs Minimum amount Rs. 24,000 (US$400)
Benefit	Insurance amount in case of death % of total amount in case of disability % accrued (at 5% per year) plus insurance amount	Insurance amount in case of death % of total amount in case of disability % accrued (at 5% per year) plus insurance amount
Claims Process	Death certificate Approved hospital disability certification	Death certificate Approved hospital disability certification
Provider	NRSP in partnership with an insurer	Kashf in partnership with an insurer
Proximity	Payment on maturity, at HQ Purchases at branch	All transactions done at the branch office
Price/ Frequency of Payment	Signed written policy Annual or monthly, depending on period and amount of insurance	Monthly payments Amount depends on insurance amount and period 2 missed payments – insurance cancelled, no interest paid Late payment fee for missed payment – 10% of payment

In presenting the products, the researchers highlighted the savings component of both products. With the education endowment product, they stressed the purpose of the accumulated premium. For the second product, they stressed the general life insurance. The life product concept included fines and a cancellation policy (in case of failure to pay) to obtain an understanding of clients' commitment to the product and, indirectly, their willingness to pay.

When presented with the product concepts, respondents focused on the savings aspect of the product by calculating the accumulated amount for marriage or further education. They were trying to strike a balance between affordability of annual or monthly premium payments and the actual amount that they were supposed to receive on the maturity of the insurance policy. Most reported that they will be able to afford monthly payments of Rs. 200 to Rs. 400 (US$3.33 to US$6.66) and preferred to pay this smaller monthly amount than the more sizeable annual payments. Also, the focus on the savings components overshadowed their coverage in the event of death of the insured person. With the education endowment insurance, for example, the clients were comfortable with the product concept as it had a purpose. Kashf clients were fine with the idea of late payment fines and policy cancellation, as they perceived these measures as helpful in maintaining premium payment discipline.

Although many of the respondents were longtime clients of trusted microfinance institutions whose other services they value highly, some of them felt uneasy with the idea of a long-term commitment to endowment insurance. Some wanted additional government guarantee to the whole process. They were not interested in the insurance partners, which suggests that customers will likely associate microinsurance with the MFI that sells the insurance and not the insurer, where the product originates.

HEALTH INSURANCE.

Health issues pose serious risks to households, particularly in cases of prolonged illnesses and health emergencies. While it is difficult to address chronic and long-term illnesses through an appropriate microinsurance product, researchers attempted to develop and test two health insurance product prototypes. These prototypes addressed the following:

- Make the claim process simple and fast
- Make the premium amount affordable and easy to pay
- Limit eligibility to cases that pose maximum stress and are least amenable to abuse, such as hospitalization

Clients from both Kashf and NRSP reviewed the product concepts for health insurance, which were as follows:

FIGURE 4: HEALTH INSURANCE PRODUCT CONCEPTS

ATTRIBUTE	NRSP: HEALTH	KASHF: HEALTH 1
Coverage	Hospitalization minimum 2 days Non-chronic conditions only Up to 55 years of age	Hospitalization requiring surgery Non-chronic conditions only Up to 55 years of age
Benefit	Lump sum Rs. 14,000 (US$233) (calculated cost of 7 days at Rs. 2,000 per day (US$33) Paid after 2 days after hospitalization notification	Rs. 1,000 (US$17) for every day in hospital of insured person Up to 15 days per year i.e., maximum of Rs. 15,000 ($255).
Claims Process	Hospitalization certificate has to be presented Money paid at the hospital or at home Paid 2 days after receipt of notification of hospitalization	Hospitalization certificate has to be presented Money paid within 1 week of presentation of documents
Provider	NRSP in partnership with an insurer	Kashf in partnership with an insurer
Proximity	Documentation produced and signed at the branch Money paid either at the hospital or at home	All transactions done at the branch office
Price/Frequency of Payment	Rs. 1,200 (US$20) once a year or Rs. 100 (US$1.67) per month	Rs. 300 (US$5) once a year payable quarterly – Rs. 75 (US$1.25)

The concepts for Kashf and NRSP differed, particularly in their pricing. Prices in Islamabad, where NRSP is located, tend to be much higher than in Lahore, where Kashf is based. The cost of transportation also differs for the two clienteles. For NRSP clients who live in rural areas, transportation costs can be substantially higher than for Kashf clients. Given these differences, the two product concepts differed in their pricing structure. In the case of hospitalization, the proposed NRSP health product provides a lump-sum amount of Rs. 14,000 (equal to the cost of 7 days in the hospital). To be eligible, a client must have a minimum stay of 2 days in the hospital. In contrast, the proposed Kashf health insurance product would pay Rs. 1000 per day of hospitalization for up to a maximum of 15 days per year or a maximum payment of Rs. 15,000.

Most respondents were positive about the affordability of the suggested products. Many believed that the premium amount would be either reimbursed or accumulated in their accounts should there be no claim in the period. When they realized that this would not be the case, they suggested that at least a portion of the premium should be reimbursed. Another option could be to have discounts on subsequent premium payments. Thus the willingness to pay for this product is not clear.

Respondents also stated that, in case of health emergencies, having insurance will be better than borrowing from family or friends because it would eliminate the stress and embarrassment from having to ask others for money.

EXTENDED LIFE INSURANCE

This product concept primarily addresses the limitations of the current microinsurance product offered by Kashf. While the Kashf life insurance product is helpful in case of a client's death (it writes off the remaining loan and pays a benefit of Rs. 7,500 or US$125), it does not cover the death of the main breadwinner of a family, who typically is not the borrower. In cases where the main breadwinner is the husband or son of the borrower, his death can jeopardize loan repayment as the borrower tries to juggle between competing demands on her relatively smaller income, including funeral expenses, household consumption, and loan repayment. In other cases, the borrower may not have an independent income at all; she may have been providing her loans to the main breadwinner. In either situation, a borrower who loses the main breadwinner of her family will find it extremely difficult to repay her loan.

> *"I think Kashf shall provide insurance for our husbands too. We work by sitting at home and they go out and sell our products door to door. They are more exposed to external risks and anything can happen any time. If some thing happens to them we will lose our incomes too."*
>
> *Woman client*

Kashf initially offered coverage for the husbands of their female clients, but it later limited the service to borrowers only due to the high costs of coverage. The product concept addressed this issue and tested clients' reactions to a more expensive insurance that provides coverage not only for women, but also for their husbands or sons. (For the details of the existing Kashf microinsurance product, see Attachment 2: Kashf Foundation.)

The product concept was as follows:

FIGURE 5: EXTENDED LIFE INSURANCE PRODUCT CONCEPT

ATTRIBUTE	LIFE +
Coverage	Wife and husband (or a son for widows) Life, accident leading to disability
Benefit	Unpaid balance of loan is written off Rs 7,500 (US$125)one time payment in case of death Pro-rated payment in case of disability
Claim Process	Death certificate or cemetery slip Payable next day Accident/death notification within 3 days of the event Disability evaluation and payment within 1 month
Provider	Kashf in partnership with an insurer
Proximity	All transactions done at the branch office
Price/Frequency of Payment	3% of loan at disbursement Option – amount withheld from loan at disbursement Any additional Rs.100 (US$1.67) paid as premium buys Rs.1,000 (US$17) of benefit

The clients responded mostly positively to the pricing of the product, even though it is twice what they are paying now. If such a price could be supported by the supply side, this modified product will drastically expand the relevant risk coverage of female Kashf clients. Additionally, the product will be easy to implement since no changes are required in the delivery process. Clients also expressed interest in accessing a voluntary life/accident insurance that is not bundled with a loan, as the existing insurance coverage is good only so long as they have a loan outstanding.

CONCLUSIONS:
IMPLICATIONS FOR FUTURE DEVELOPMENT OF MICROINSURANCE

The purpose of this study was to identify the most economically stressful risks facing low-income microentrepreneurs in Pakistan, the strategies that they use to deal with these risks, the gaps in these coping mechanisms, and the needs for better risk-managing financial strategies.

The microfinance clients at NRSP and Kashf face many economically stressful and risky events. The life-cycle events that cause the most financial stress include constructing a house and the marriage of children. The most stressful unpredictable risks are death of a family member – especially that of a breadwinner – and prolonged illness.

Clients avail themselves of many different types of coping strategies. They have a habit of saving, but they are often unable to save very much at home, and the amounts that they save at their MFIs are inaccessible in times of crisis. They also participate in informal savings clubs – *committees* – which they use to save usefully large lump sums for specific purposes. These sums are usually available on a schedule but not on short notice. Clients also benefit from strong social networks, including family and friends, that will help them by providing loans when needed. Clients of Kashf have access to emergency loans through their MFI, although the research suggested that they tend to misuse these loans, making them less effective in case of a real emergency.

Despite the range of both formal and informal financial services that is available to low-income clients, they remain vulnerable to economic shocks. Clients have limited means to cope with expenditures larger than the normal day-to-day expenses or with large financial losses, particularly those with lasting consequences. Many clients end up in long-term debt after experiencing an economic shock. In such situations, families experience a decline in their standard of living and fall deeper into poverty.

RISK-MANAGING FINANCIAL SERVICES

The impetus behind the development of microinsurance products is the desire to protect low-income people from economic shocks. Yet there are risk-managing financial services aside from microinsurance that can reduce the vulnerability of low-income people. They include savings and emergency loan products. Each product has a particular role to play.

- Emergency loans are intended to protect people from the need to sell off assets or take on extremely high-priced debt.
- Savings products are for people who have the ability to plan ahead and can afford to put some money aside.
- Insurance is to protect people against insurable risk (or risks that can be observed and are idiosyncratic – i.e. they only affect one person or one family at a time).

It is generally agreed that insurance is not an effective response for situations in which:

- Losses are certain to occur
- Losses are small because the associated administrative and transaction costs would make the product too expensive in relation to the loss.
- The risk is covariant and affects many people in the risk pool at the same time – for example, an earthquake or other natural disaster.

- The insured person has control over the insured risk.[10]

Generally, saving and loans are more appropriate for covering economically stressful life-cycle events, while insurance is best for risks that are unpredictable and result in significant losses.

PRODUCT CONCEPTS

The research with NRSP and Kashf clients suggested that there is demand for the following microinsurance products:

- Endowment insurance for the education and marriage of children
- Health insurance
- Extended life insurance

These products were designed to meet client needs in terms of the coverage, affordability of premiums, ease and frequency of payment, ease and timeliness of claims processing, and payment. Research has shown that low-income people prefer smaller and more frequent premium payments that they can make from home or at meetings with the MFI. They also prefer less paperwork and quick payment in case of a claim[11].

Although savings and loans are appropriate solutions for expensive life-cycle events, the clients had an overwhelming preference for an insurance solution to education and marriage expenses. Savings was their second choice and loans were third,[12] even though savings would be a very suitable product for managing education and wedding expenses. We speculate that insurance is more popular than savings because (1) clients currently do not have access to safe, secure and voluntary savings services and (2) they like the forced savings aspect of endowment insurance.

The research demonstrated that, of all the predictable life-cycle events, house construction caused the most economic stress on families. It also caused emotional stress as it resulted in households having to live with their relatives and/or take on large amounts of debt. MFIs should investigate addressing this need with a long-term loan product such as a mortgage.

A less frequent risk but one that causes microentrepreneurs financial trouble is business losses due to fire, theft or natural disaster. PMN should investigate insurance for business goods and assets, after the other insurance products (mentioned above) have been developed.

Most low-income people cannot afford more than one product. NRSP's product addresses this problem by combining several kinds of coverage in one policy. The effectiveness of these existing microinsurance products in Pakistan is unclear. The testing process of product concepts is limited. The willingness to pay for one microinsurance product does not translate into willingness to pay for many products. The question of which single insurance product would most effectively serve low-income households in Pakistan remains unanswered. We don't know enough yet about the substitution effect of microinsurance. Will microinsurance become a substitute for other financial services? Or will it become an additional product for clients? For low-income households, it seems likely that endowment insurance would become a substitute for savings mechanisms that they are

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10 p. 24-25. Manje, Lemmy and Craig Churchill " The Demand for Risk-Managing Financial Services in Low-Income Communities: Evidence from Zambia" Social Finance Program and InFocus Programme on Boosting Employment through Small Enterprise Development, Working Paper No. 31. (ILO: Geneva, n.d.)

11 Monthly premium payments work best for microentrepreneurs but in rural areas annual or seasonal payments are more convenient due to seasonal variations in cash flow.

12 Only a small sample of clients were asked to rank the strategy for coping with these economic stressors.

now using. But this calls into question whether these households can afford the endowment insurance since it contains the cost of the insurance component as well as the savings component. Clients will make trade-offs.

CLIENT EDUCATION AND MARKETING

The discussions with the clients suggested the need for better client education on insurance and how it works. The desire of clients to receive a refund if they don't incur the condition that the insurance covers shows a lack of understanding of the principles upon which insurance is based, and will be a challenge to the successful implementation of an insurance product. For this reason, endowment products are more popular with clients (in fact, endowment insurance products operate much as a forced savings product). Financial education is key to the long-run success of insurance, as clients will not continue with a product if they are disappointed with the outcome or feel that they have been cheated of their money. Education should cover the nuts and bolts of the insurance product itself (coverage, premium amount, how to pay the premium, how to make a claim, where to make a claim, etc.) as well as the way in which insurance works (i.e., it pools risks by collecting payments from many people in order to make larger payments to individuals who suffer a loss). Financial education efforts will take some time but they are key to ensuring that clients are informed consumers of microinsurance products.

Discussions with the respondents suggest that, in marketing insurance, MFIs could focus on selling 'peace of mind.' Many respondents mentioned mental anxiety or emotional stress when talking about how they coped with large economic risks. Relying on social networks such as *baradri,* though helpful, also causes people stress because they end up worrying about having to ask for help and then having to repay their peers.

Unfortunately, perceptions of insurance among low-income populations are not always positive. The research found several respondents who had had bad experiences with insurance. While their experiences may have been the result of a poor understanding of the insurance policy, respondents also mentioned problems with fraud committed by insurance agents or a lack of good faith on the part of insurance companies. Education and marketing efforts will need to address this poor perception.

MFI-INSURER PARTNERSHIPS

Clients have a high level of trust in their microfinance institution, but they have no interest in the insurance companies that actually offer the microinsurance product. If there are any problems with the insurance product, they will blame the MFI. Conversely, if the insurance product is a huge success, they will praise the MFI. Thus, MFIs must be very careful about which insurance companies they choose for partners. They must work with the insurance companies to get the product right before they roll it out on a large scale. A bad experience with a microinsurance product has the potential to erode clients' confidence and damage the MFI's overall business. On a related note, MFI staff must know the microinsurance product very well and take care to ensure that all MFI products get adequate attention from front-line staff to avoid having one product cannibalize the business of the other.

In both cases examined here, Kashf and NRSP introduced microinsurance due to the initiative of the insurer. MFIs do not have a good feel for the cost structure of the products offered, resulting in a very weak negotiating position. In the future, there needs to be more participation from MFIs in the product development and implementation process.

Pakistan can boast a well-established insurance industry and a number of solid MFIs with considerable outreach to the potential, but – as of yet – untapped, microinsurance market. Hence, PMN could facilitate MFI-insurance company partnerships though educating insurers and demonstrating to them the advantages of innovating and entering this market.

NEXT STEPS FOR PMN

This demand study is one small part of a larger microinsurance product development process underway at PMN. Since some of the Kashf clients reported that they would not have bought the life insurance policy had it not been mandatory, PMN and the MFIs should go slowly in introducing new microinsurance products. The recommended process which was outlined in the introduction is a systematic method for developing viable products. Its remaining elements include:

- A supply-side study to assess existing and planned microinsurance products. This helps to (1) refine what should be offered, (2) identify potential insurers and other partners that MFIs could work with, and (3) uncover information about the processes, marketing, and efficiencies of various options.
- Partner selection
- Design of product prototype(s) based on the demand and supply studies
- Short, quantitative study to determine the demand for the prototype
- Preparation and then implementation of the proposed product, including training, systems preparation, and documentation of procedures.
- Pilot test review and evaluation
- Product rollout

The supply study should allow PMN and the MFIs to obtain a better sense of the available partners and viable products (from the insurers point of view). We recommend that PMN undertake a quantitative demand research, which would involve developing a questionnaire and surveying a significantly large sample of microfinance clients. It could hire a local firm to conduct the survey. The quantitative research would complement the qualitative research by showing the number of people that face specific risks, the costs of those risks, and the frequency with which those risks occur.

Individual MFIs should conduct market segmentation to identify sub-groups within their respective clienteles before they design product prototypes. This research had hoped to uncover differences in demand between urban and rural residents, and between men and women. The research did not find many definitive differences along these dimensions, but it did demonstrate that there are significant differences in the income levels of clients within a single MFI that can result in different types of demand for and use of risk coping mechanisms. The quantitative survey could investigate market segmentation in greater detail.

The market for microinsurance is not limited to microfinance borrowers. The ability to offer microinsurance products presents MFIs with an opportunity to tap into a larger market of low-income people. Therefore, any future research should include an investigation into the potential of this currently unserved market.

Since MFIs provide insurance companies with access to a large, untapped market, they should participate more actively in further studies and the microinsurance product development process, possibly even sharing costs with the insurers. The development of successful microinsurance products will require working closely with the insurance company partners.

ATTACHMENT 1. THE NATIONAL RURAL SUPPORT PROGRAM[13]

Mission

NRSP works to release the potential abilities, skills, and knowledge of rural men and women, to enable them to articulate their aspirations, and to effectively marshal the resources they need to meet their identified needs. The purpose is poverty alleviation - enabling people to break the cycle of poverty, which begins with lack of opportunity, extends to the well-known miseries of economic and nutritional poverty, and leads new generations to endure the same conditions. The process is social mobilization - bringing people together on new terms for a common purpose. The conceptual tools are 'social guidance' (recruiting local men and women who will take on a leadership role), advocacy, capacity building, and awareness raising. The programmatic tools are training, support to institutions, micro-credit, infrastructure development, natural resource management, and 'productive linkages'

Legal status: Company limited by a guarantee.

Founded: 1991.

Governance: Twenty-two-member board of directors, three of whom are Government Ministers. The board develops NRSP strategy; management is accountable to the board.

Organization: NRSP delivers microfinance services through Microfinance Enterprise Development Program (operational in 25 districts) and Urban Poverty Alleviation Program (covering 5 districts) covering most of the country

Client base: 12% urban, 88% rural; about 25% of borrowers - women

Product offering

Loans. Loans are provided both through group guarantee and village banking mechanisms. Initial loan size is up to US$166 with increments (up to 50% of the amount) each cycle. All loans are for productive/business purposes. Loan periods vary from 6 to 18 months.

Savings product is introduced through community organizations. The clients are encouraged to save and each savings group maintains a separate account at a local bank. Savings are used either directly by savers or used for internal lending.

In 2005, NRSP introduced a health/accident ***insurance product*** in cooperation with Adamjee Insurance Company. The product is offered only in rural areas and entails an annual premium of US$4.15. The insurance covers accidents and hospitalization up to the amount of US$417. The claim process is based on reimbursement principle and since no claims have yet been processed, it is difficult to evaluate processing time.

[13] Data obtained from NRSP (interviews with managers), Pakistan Microfinance Network “Performance Indicators Report – 2004” and NRSP official web site

Key Operational Results, 2004

Operational Sustainability	103%*[14]
Financial Sustainability	90%*
PAR, over 30 days	6.1%*
Number of Active Loans	Over 125,000
Average Loan Size	US$155
Urban/Rural Clients	12%/88%
Female Clients	About 25%

[14] Data marked with * refer to 2004

ATTACHMENT 2. KASHF FOUNDATION[15]

Mission

To provide cost-effective and quality microfinance services to poor women, by adding value to women's existing economic opportunities in order to enhance their role in economic and social decision-making. At the same time, Kashf aims to contribute to a sustained improvement in clients' incomes in order to enable them to move beyond the poverty trap.

Legal status: NGO.

Founded: 1996.

Governance: Eight-member board of directors, four of whom are women. Board is comprised of committed and experienced professionals. Board members meet on a regular basis to review policy and to identify future directions for program development. Members are elected every three years.

Organization: Thirty branches.

Client base: 100% women.

Area of operations: Lahore, Pakistan.

Product offering

General loans (about US$140). Provided for a productive purpose, the general loan is a twelve-month loan with twenty-two equal installments, and can be renewed each year with a graduation step of US$18. However, the renewal is contingent on both the center and group's ability to repay all their loans.

Consumption loans (about US$30) for families to meet unplanned expenditures or emergencies. The consumption loan is a six-month loan with twelve equal installments that is tied to the savings of the customer with a ratio of one to three: if a customer saves one dollar she can access three dollars as a loan.

Flexible savings product which provides customers with the opportunity to deposit in multiples of Rs. 10 (US$0.17) and offers open withdrawal facility at the center meeting or, in case of emergencies, at the branch office. Kashf is not promoting the product since it is limited by law to keep savings raised in their current account hence making it financially non-viable.

In 2001, Kashf entered into collaboration with Adamjee Insurance, Pakistan's largest insurance firm. They are now working tiwth the New Jubilee Insurance Company. Every member who obtains a general loan is required to avail of the ***insurance product***. The one time insurance fee is about US$1.60 and covers natural/accidental death. In case of death of the borrower, the outstanding loan is written off and the family receives a on-time payment of Rs. 7,500 (about US$125).

[15] Data obtained from Kashf (interview with Operations Manager and official web site), Pakistan Microfinance Network "Performance Indicators Report – 2004" and Women's World Banking website

Key Operational Results, 2004

Operational Sustainability	187%
Financial Sustainability	155%
PAR, over 30 days	0.7%
Number of Active Loans	87,389
Average Loan Size	$118
Urban/Rural Clients	85%/15%
Female Clients	100%

ATTACHMENT 3. FIELD WORK SCHEDULE

Rural Clients, Islamabad

Date	Meeting 1		Meeting 2	
Thursday, 11/17/2005	1M	1F	1M	1F
Friday, 11/18/2005	2M	2F	3M	4/5 F
Saturday, 11/19/2005	4/5M	9A F	**9A** M	9A F

Urban Clients, Islamabad

Date	Meeting 1		Meeting 2	
Monday, 11/28/2005	1M	1F	1M	1F
Tuesday, 11/29/2005	2M	2F	3M	4/5 F
Wednesday, 11/30/2005	4/5 M	9A F	9A M	9A F
Thursday, 12/1/2005	10/11 RF	10/11 RM	10/11 UF	10/11 UM

Urban Clients, Lahore[16]

Date	Meeting 1		Meeting 2	
Monday, 11/21/2005			1	1
Tuesday, 11/22/2005	2	2	3	4,5
Wednesday, 11/23/2005	9A	9A	9A	9A
Thursday11/24/2005	Concept Development		Concept Development	
Friday, 11/25/2005	10,11	10,11	10,11	10,11
Saturday, 11/26/2005	Analysis, Reporting		Analysis, Reporting	

Legend :

F – Female clients

M –Male clients

1 – Risks and Risk Management Strategies (FGD)

2 – Life Cycle Risks (PRA)

3 – Time Series of Risks (PRA)

4 /5 – Seasonality of Income, Expenditures & Risks(PRA)

9A – Client Satisfaction with MI - Current clients (FGD)

10/11– Microinsurance Product Concept Testing (FGD)

[16] KashfKashf in Lahore has only female clients

ATTACHMENT 4. KEY ECONOMIC STRESSORS/RISKS, COPING MECHANISMS & GAPS

Key Risks	Coping Strategies	Gaps
Accident/Death	Insurance – limited access and use Use up savings Borrow from relatives (baradri) Borrow from money lenders Sell assets Reduced consumption More work	Savings are never adequate for the purpose Relatives frequently do not have enough to lend Savings are usually with a "committee" – not readily accessible Borrowing from money lenders is an enormous stress – interest is 10% per month flat and the loan has to be repaid in a lump sum
Unexpected Serious Illness	Savings Borrow from relatives Borrow from money lenders More work Reduced consumption and household expenses, including school fees Sales of assets	Savings are never adequate for the purpose Relatives frequently do not have enough to lend Savings are usually with a "committee" – not readily accessible Borrowing from money lenders is an enormous stress – interest is 10% per month flat and the loan has to be repaid in a lump sum
Marriage Of Children	Savings – mainly with "committees" and in-kind Relatives bring presents Long-term endowment insurance – only a few people have access to this Borrowing from relatives Borrowing from money lenders Purchases of jewelry and other goods on credit from sellers	Insufficient low stress strategies Often families are left with considerable debt
Education Of Children	Covered from on-going income sources	Covered from on-going sources of income Unless saved through a "committee" no other coping mechanisms to meet the need

	Significant percentage of household expenses If in difficulties, children are pulled out of school If hard to afford – daughters are either not sent to school or pulled out earlier compared to sons In cases of extreme poverty – children do not attend school altogether Financial means necessary for college are saved up through "committees"	
Birth Of A Child	Use of savings Gifts from relatives Borrowing from relatives in case of complications and more medical assistance needed	More stress in cases of complications - frequently lack of financial resources leads to death of mother and/or newborn Traditional midwifery services are available locally (even in smaller villages) – more complicated cases need to be treated at hospitals
Construction Of A House	Help from relatives Savings Sequencing of the project – level of initial completion just adequate to move in – other work is done as money is available or never Staying in an extended family	Social pressure to start a separate household for elder sons as they marry – the youngest stays with the parents

ATTACHMENT 5. MONTGOMERY'S CLASSIFICATION OF COPING STRATEGIES, BY LEVEL OF STRESS

COPING STRATEGY	NOTES
Low-Stress Coping Strategies	
Expenditure saving activities (gathering fuel, fodder, culinary condiments from common lands) Changes in diet (cheaper foods) and reduced consumption (eating less) Periodic migration by one or more household members to look for higher wage income Calling in small informal debts from kin and neighbors	Primarily effective for dealing with minor shortfalls in income; are relatively low value and reversible; insufficient for meeting major crises and contingencies
Medium-Stress Coping Strategies	
Using up cash savings Pledging future labor in return for advanced wages or loans Taking cash or kind loans from kin and neighbors Taking cash or kind loans from moneylenders and shopkeepers	Likely to help counter sudden crises and contingencies, but are less reversible, & reduce future coping capacity. They may therefore act as " ratchets" forcing a household further into poverty (especially if an initial crisis is compounded by subsequent shocks)
High-Stress Coping Strategies	
Mortgaging or pawning assets (utensils, jewelry, land, etc.) Sale of nonproductive assets (initially small ones, such as household utensils; or larger ones such housing materials, tin roofing sheets etc) Sale of working capital at knock-down prices (e.g. stocks of paddy to be husked, petty trading goods to be sold) Sale of productive assets (small animals, livestock, tools, plots of land etc.) Pull children out of school to work Leave a microfinance program	Hard to reverse; indicators of severe distress and increased vulnerability to further stress. May constitute ratchets from which a household may be unable to recover.

Source: Montgomery 1996.