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MICROINSURANCE

DEMAND AND MARKET PROSPECTS

INDONESIA





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and Development



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ABBREVIATIONS

ACA	Asuransi Central Asia
ADB	Asian Development Bank
AIG	American International Group (U.S.)
ASEAN	Association of Southeast Asian Nations
Askrindo	Pt. Asuransi Kredit Indonesia
BCA	Bank Central Asia
BKD	Village Credit Agencies
BKKBN	National Family Welfare Programme
BPD	Regional Development Banks
BPL	Below poverty line
BPR	Bank Perkreditan Rakyat (People's Credit Banks)
BRI	Bank Rakyat Indonesia
CARD	Center for Agricultural and Rural Development
CCA	Canadian Cooperative Association
CEO	Chief Executive Officer
CMSA	Capital Markets Supervisory Agency
DBO	Dana Bantuan Operasional (a type of education grant)
DEPSOS	Department of Social Affair of the Republic of Indonesia (the Indonesian Ministry of Social Welfare)
DFID	Department for International Development (U.K.)
DG	Director General
DGFI	Director General of Financial Institutions
EPF	Employer Pension Funds
FIPF	Financial Institution Pension Funds
GDP	Gross domestic product
GTZ	German Technical Assistance (Deutsche Gesellschaft für Technische Zusammenarbeit GmbH (Germany)
IDR	Indonesian rupiah (currency)
ILO	International Labour Organization
JPS	Social safety net
KARK	Konsortium Asuransi Resiko Khusus (special risk insurance consortium)
KfW	German Development Bank
KUB	Business grants for social groups
LDKP	Microfinance providers regulated at the subnational level and delegated supervision
LPD	Lembaga Perkreditan Desa (locally registered village banks)
MBA	Mutual Benefit Association
MFI	Microfinance institution
MFP	Microfinance provider
MLT	Ministry of Labour and Transmigration
MoA	Ministry of Agriculture
MoF	Ministry of Finance
NGO	Non-governmental organization
OPK	A rice subsidy programme
PDLPD	Provincial level training centres

PDM-DKE	A community empowerment programme
PKSPU	An employment creation programme of the Government
PLPBK	District-level training centres
PMKS	Social assistants for habitation and economic activities
PMT-AS	Health and nutrition programme of the Government
PNM	An Indonesian development bank
PNS	A social security programme for civil servants
POLRI	A social security programme for members of the Indonesia National Police
PPP	Public private partnership
PPU	Perum Pengembangan Usana
ProFI	GTZ-supported project Promotion of Small Financial Institutions
ROSCA	Rotating savings and credit association
Sipadat	Simpanan Upacara Adat
SME	Small and medium (sized) enterprises
SSN	Social safety net
SWIP	Social Welfare Insurance Programme
TIDRAK	Tabungan Investasi Desa Adat Kedonganan
TNI	A social security programme for members of the Indonesia National Army
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
UPPKS	Income-generating activity for prosperous families
USAID	United States Agency for International Development
WHO	World Health Organization

Non-English Words and Phrases

Arisan	Informal joint financial pool
Gotong royong	Mutual support groups
Hak Pakai	Right of usage
Haram	Not in keeping with Islamic law
Ijon	Advance sale of crops to raise money quickly
Jamsostek	PT Jamsostek is a state-owned insurance company providing services to formal-sector workers
Ketua	*Arisan* leader
Modoroba	Profit sharing
Puskesmas	Primary health centre
Tidak Mampu	Letter of acknowledgement of poverty
Wakala	Fee
Yayasan	Foundation

INTRODUCING MICROINSURANCE

A public private partnership using a market-based mechanism to reduce poverty

What happens when a poor family's breadwinner dies, when a child in a disadvantaged household is hospitalized, or the home of a vulnerable family is destroyed by fire or natural disaster? Every serious illness, every accident and every natural disaster threatens the very existence of poor people and usually leads to deeper poverty. That's where "microinsurance" comes in.

Microinsurance is specifically designed for the protection of low-income people, with affordable insurance products to help them cope with and recover from common risks. It is a market-based mechanism that promises to support sustainable livelihoods by empowering people to adapt and withstand stress. Two-thirds of human beings suffering in the most extreme poverty are women. Often living within $1 per day, they are the most vulnerable.

But will microinsurance actually help those living in poverty by contributing to sustainable livelihoods? We believe it can, and we decided to test the hypothesis in the real world. UNDP approached Allianz AG about working together on a market potential study to analyze the demand, acceptability and affordability of microinsurance products. They immediately saw the value of working in this under-explored area. This public private partnership acquired greater strength when GTZ, with considerable experience in the area of social protection and microinsurance, joined the alliance. The partners agreed to analyze demand for microinsurance products in India, Indonesia and Lao People's Democratic Republic (PDR) and jointly selected a team of consultants to prepare country studies.

The studies clearly indicate that access to microinsurance by the poor and disadvantaged population can contribute significantly to the achievement of the Millennium Development Goals, particularly the goals of eradicating extreme poverty and hunger (MDG 1), promoting gender equality and empowering women (MDG 3) and developing a global partnership for development (MDG 8).

Three country studies

The country studies examine and appraise the most urgent social security risks and needs of poor population groups. They highlight the following aspects of microinsurance supply and demand:

- Existing activities to meet the needs for social safety net mechanisms, including informal strategies;
- The role of government policies;
- Capacity development requirements at various levels;
- The need for advocacy and education to help poor populations as well as potential providers to understand the role of microinsurance;
- The need for ongoing efforts to analyze potential customer profiles, reflect on their ability to pay, and suggest possible products to suit the target groups;
- Possibilities for countries to learn from each other's experiences.

In **India**, the study finds that this country currently has the most dynamic microinsurance sector in the world. Liberalization of the economy and the insurance sector has created new opportunities for insurance to reach the vast majority of the poor, including those working in

the informal sector. Even so, market penetration is largely driven by supply, not demand. Microinsurance in India has valuable lessons for rest of the world, particularly in the regulation of the industry. Certain aspects, such as the quota system need further and closer analysis. The quota system, for example, may be viewed in terms of its costs and benefits: is it an onerous obligation for insurers that creates a barrier to innovation and demand-based products? Or, is it an avenue that may lead to the creation of a microinsurance market that meets the needs of the poor and disadvantaged?

In **Indonesia**, demand is strong for insurance to cover the risks that people are least prepared for and have insufficient means to manage. Such risks include serious illness, poor harvest, death in the family and social obligations. Education of children is a priority, and the potential microinsurance policy holders would like to ensure that an unforeseen shock or stress does not deprive their children. The number of insurers in Indonesia is significant, yet few have explored the low-income market. Consequently there is a critical need for capacity development, primarily in the areas of agent training and market education. This could expand opportunities and lead to market-based tools to assist the poor in securing their lives.

In **Lao PDR**, the country study finds that the social security system is nascent (and practically absent for the informal economy) and microfinance institutions are conspicuously inadequate. The analysis confirms a commitment by the Government in several relevant areas: support for reforms, support for pensions and a social security fund for public employees, support for compulsory social protection for the private sector, and support for a community-based health scheme for people working in the informal sector. The study concludes that the potential for commercial microinsurance is in the future at least a few years away. Meanwhile, for microinsurance to become viable, the Government will need to strengthen the financial infrastructure, develop capacity for potential insurance providers and build knowledge of microinsurance mechanism and products among potential policy holders.

Microinsurance is a low-price, high-volume business and its success and market sustainability is dependent on keeping the transaction costs down. Hardly any satisfactory state-run programme of insurance benefits is now available for poor population groups, people working in the informal sector and other disadvantaged individuals—and private-sector programmes are even rarer. A number of constraints make microinsurance look unattractive, including a lack of political will, scarcity of public funds and absence of a viable business model. The costs of marketing and processing appear to be too high and, in view of the extremely low purchasing power of the consumer base, it cannot be easily apportioned to the target group. Such constraints make microinsurance unattractive at the cursory level. Market analysis suggests that progress can be made particularly when public and private sector work together in generating demand-based and innovative products.

Future steps

Where do we go from here? Building on the recommendations of the studies, pilot activities in India and in Indonesia are being implemented by Allianz AG supported by GTZ on behalf of the German Federal Ministry for Economic Cooperation and Development (BMZ). While it would be critical to address the need to build capacity in nongovernmental organizations (NGOs), trade unions and microfinance institutions, the outcome of pilot activities will point to specific issues to be addressed. Local structures of civil society can help their members gain access to microinsurance and reduce the transaction costs of processing. Market education and skills training are needed on at least two fronts: improving the efficiency of partner-agent distribution methods, and sensitizing potential intermediaries and customers. A

clear strategy for communicating with potential customers that conveys information and knowledge of the products is essential to success. It will also be important to work with governments to strengthen institutions and create an enabling environment. Such an environment is enhanced by transparent and participative consultation process. It ensures that the delivery process for microinsurance services is efficient with minimal transaction costs. It is in these areas that UNDP and GTZ will bring their experience and expertise to bear in making the microinsurance pilots successful.

We anticipate that access to insurance by poor people and entrepreneurs in the informal sector will attract private sector investments, assist in the development of the domestic private sector and lead to the alleviation of poverty. Increasingly, a social protection mechanism such as microinsurance appears to be a prerequisite in national poverty reduction strategies. Despite obvious need, however, it has not been possible for national governments to meet this obligation due to budgetary constraints. A possible solution would be to leverage government strategies with market-based social protection systems. The strategy would benefit significantly from south-south learning and sharing of knowledge, policies and practices.

The provision of microinsurance products and services is an obvious candidate for public private partnerships, as demonstrated in our three country studies. We are hopeful that with the interest shown by visionary private sector partners like Allianz AG it will be possible for forward-thinking bilateral donors such as the German Federal Ministry for Economic Cooperation and Development (BMZ) and GTZ and multilateral organizations such as UNDP with its broad reach and anti-poverty mission to catalyze access to microinsurance by the poor and disadvantaged.

We look forward to hearing from you about the market analysis presented in our three country studies. Indeed, your comments, feedback and ideas for innovative partnerships will be a welcome contribution to the global effort to achieve the Millennium Development Goals.



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EXECUTIVE SUMMARY

Indonesia is a country of 238 million people, one of the largest populations in the world, with the largest population of Muslims. It is a country with vast opportunities and huge numbers of people working in self-employed activities, often low-income. As in many other countries, the self-employed and others who make up the low-income population benefit when they have access to financial services. Typically, these services are savings and credit that they can access through numerous channels. But they find that credit and savings are not enough to support a family during a financial crisis. Commonly, crises such as the death of a breadwinner or the hospitalization of a family member will not only move families to a lower economic level, but also leave them without the tools to recover from poverty.

It is in this context that Allianz AG, GTZ and UNDP selected a team to visit Indonesia to identify the potential for microinsurance.

The purpose of the research was to estimate the demand for microinsurance in Indonesia, as well as its potential supply in terms of risk takers (e.g., regulated insurers and government) and various delivery channels. The information gained should lead to an understanding of the options available for undertaking pilot initiatives. In the long term, the research and implementation of the findings should support the development of sustainable livelihoods by making microinsurance available to the poor and the disadvantaged people as well as workers in the informal sector. It should also lead to exploration of the use of microinsurance as a safety net mechanism to reduce the economic vulnerability of low-income populations.

The team spent nearly two weeks each in five areas of the country, studying demand through focus group discussions and interviews with key stakeholders. Supply and potential were assessed through discussions with insurers, donors, relevant government officials and others. Most of the research was based in Jakarta, but members of the team also visited Tangerang, Yogyakarta, Bali and Aceh.

Demand was strong among potential microinsurance policyholders in several areas of Indonesia. Focus group participants were asked to identify their risks and how they manage them. They identified the following as the **top five risks**: (1) serious illness, (2) education of children, (3) poor harvest, (4) death of relative and (5) social obligations. These risks correlated with the risks that people are least prepared for and have insufficient means to manage. This information enabled the team to identify any gaps that would lead to opportunities for potential products.

With 173 insurers in Indonesia, it was surprising that so few had seen the opportunities in the low-income market. Indeed, these insurers have hardly moved into this market at all. In 2003, the insurance density was $15 per capita, and the insurance penetration was a mere 1.49 percent of gross domestic product (GDP). The Asia averages are $180 and 7.5 percent, respectively. In Indonesia, there is much room for expansion.

It was estimated that there should be an effective market of at least 12 million active policyholders plus their families in ten years. The growth is likely to be relatively slow at the start, increasing rapidly as insurers push out to new markets and develop more and better products. At the same time, market education and the demonstration effect will enhance the

demand. To assess demand for microinsurance, the team applied various methods and consulted several knowledgeable experts

As a start, an insurer would be well-advised to offer two products, both related to life insurance: a life policy and an education endowment policy. The life policy focuses not so much on the funeral, though there is a benefit for the funeral and memorial service, but instead focuses on what happens to the family after a breadwinner is gone. This product provides specialized benefits for two years after the death of a policyholder. The education endowment policy can accommodate the major educational expenses along the way based on a savings plan. This is combined with a life insurance policy so that if the policyholder dies, the rest of the agreed payments will be made. These products represent a good start. As they become stable in terms of systems, procedures and demand, it is fully expected that more advanced products would become ready to test and roll out.

Financing for health care is also in high demand, especially for hospitalization and long-term care, which can have such a detrimental impact on households. The potential for such cover is currently unclear due to the social health insurance component of the Government's relatively new social security legislation.

Potential partners in the effort to provide microinsurance might include:

- People's Credit Banks (BPRs), which have a broad network already focused on the low-income market;
- Commercial banks such as Bank Niaga and Bank Permata that offer access to the low-income market, as well as potentially efficient mechanisms for collecting premiums;
- Microfinance providers (MFPs) such as Diman and Ganesha with clients that are already used to financial products and have a wide rural network;
- Locally registered village banks (LDPs) in Bali that represent an efficient channel to low-income people that could also be used to sell and service life policies;
- Mercy Corps in Aceh, one of the few organizations in that area able to do substantial and effective microfinance work;
- BKKBN (National Family Welfare Programme), which supports thousands of women's self-help and income-generating groups (UPPKS);
- Perbarindo, a training and advocacy organization (not for product distribution).

Capacity development is necessary, primarily in the areas of agent training and market education, for any effort to succeed. Assistance with information systems is also required in Indonesia. Such systems will create limited links between insurers and intermediaries (where possible), and provide on-site technical assistance to address many of the smaller yet important issues that will help microinsurance expand more rapidly and with fewer problems.

Access to microinsurance products including life and education endowment policies, and addressing the constraints noted in this paper, should have a powerful impact by providing tools to help low-income people secure their lives.

CHAPTER I. BACKGROUND

Indonesia is a populous country with a large proportion of low-income people. Significant and varied strategies are required to help them acquire tools that they can use to improve their livelihoods, and then stabilize their household economic status. Numerous microfinance (credit and savings) providers (formal and informal) offer their products throughout the country. As in many other countries, however, formal tools to manage household and business risks are often limited or neglected.

Allianz AG, GTZ and UNDP formed a partnership to study the potential for microinsurance in Indonesia—recognizing a number of likely limitations to risk management. The results of the study should help these institutions and others to understand better the microinsurance landscape in this country, and to identify specific interventions that might improve the provision of microinsurance in terms of quality and quantity. It is hoped that the study would provide an evidence-based theory of change.

It is expected that the results of the research will, in the long term, help in the development of sustainable livelihoods through access to microinsurance by workers in the informal sector. In addition, this should lead to the exploration of the use of microinsurance as a safety net mechanism to reduce the vulnerability of low-income and disadvantaged populations in Indonesia.

The research was intended to estimate the **demand** for microinsurance in Indonesia, as well as the potential **supply** of microinsurance in terms of risk takers (regulated insurers, government, and others) and various delivery channels. This information should lead to an understanding of the options available for undertaking pilot initiatives. Substantial qualitative research was conducted among the members of several organizations in several locations around Indonesia. The supply-side research was conducted through the extensive use of interviews with key persons. Among them, the team met with major informants of government, civil society and the private sector. (For more information on the demand research methodology and the organizations through which clients were identified, please see appendices 1, 2 and 3. See appendix 5 for this study's Terms of Reference and appendix 4 for a list of people met.)

1.1 Macroeconomic snapshot of Indonesia

Indonesia is the fifth largest country in the world by population, yet the 150th in terms of GDP per capita, and it ranks 112th in the human development index. It is a country with much potential for development. Key indicators are shown in table 1.

Table 1. Key Indicators: Indonesia

Category	Value
GDP ($ billions)	632 (*World Development Report*, 2004)
Population (millions)	238.5 (July 2004 est.) (U.S. Central Intelligence Agency)
Population density per km^2	117 (2002) (*World Development Report*, 2004)

Category	Value
Percentage urban population	40.9% (2000 estimate)[1]
GDP/capita ($)	$810, from 2003 (*Asian Development Outlook*, 2005).
GDP growth rate	5.1%, a 2004 estimate (*Asian Development Outlook*, 2005)
Inflation	6.2%, a 2004 estimate (*Asian Development Outlook*, 2005)
Exchange rate (current, IDR per $1)[2]	9,320[3]
PPP GDP per capita ($ billions)	$2,990 (2002) (*World Development Report*, 2004)
Infant mortality (per 1,000 live births)	Total: 36.82 deaths/1,000 live births Female: 31.29 deaths/1,000 live births (2004 est.) Male: 42.09 deaths/1,000 live births (U.S. Central Intelligence Agency)
Under-five mortality (per 1,000)	87/95 (males/females, 2002, *World Health Report*, 2003)
Maternal mortality (per 100,000 live births)	380, a 2001 estimate (United Nations Development Programme, *Human Development Report*, 2003)
Access to safe water (% of population)	78%, a 2000 estimate (United Nations Development Programme, *Human Development Report*, 2004). Note: this figure refers also to improved water sources that may not be safe.
Health expenditure as % of GDP (public/private/total)	0.6%/1.8%/2.4% (2001, from *World Health Report*, 2003)
Health expenditure per capita ($)	$84 a 2000 estimate (United Nations Development Programme, *Human Development Report*, 2004)
Doctors per 100,000 people	16 (1990–2002 estimate, United Nations Development Programme, *Human Development Report*, 2003)
Hospital beds per 1,000 people	0.06 (2001, lowest rate among ASEAN members[4])
Literacy rate	88.5%, a 2003 estimate (U.S. Central Intelligence Agency)

1.2 Basic structure of the Indonesian insurance industry

Insurance penetration and density suggest a large and underdeveloped market in Indonesia. The insurance industry has remained rather stagnant in terms of the numbers of institutions over the five years from 1999 through 2003. The one exception is regarding brokers, where there is often volatility. A breakdown of organizations within this industry is provided in tables 2 and 3.

Table 2. Growth of Insurance Industry by Classification

Insurers and reinsurers	1999	2000	2001	2002	2003
Registered insurers	178	178	175	173	173
Life insurers	62	62	61	60	60
General insurers	107	107	104	104	104
Professional reinsurers	4	4	4	4	4
Social insurers and Jamsostek[5]	2	2	2	2	2
Civil servant and armed forces insurers	3	3	3	3	3

[1] See http://w3.whosea.org/health situt 98-00/c2a.htm (06.05.05).
[2] This exchange rate is used in all calculations of current figures. Currency conversions are rounded and thus approximate.
[3] See http://www.oanda.com/convert/classic (06.05.05).
[4] See http://www.indonext.com/report/report548.html (06.05.05).
[5] PT Jamsostek is a state-owned insurance company providing services to formal-sector workers.

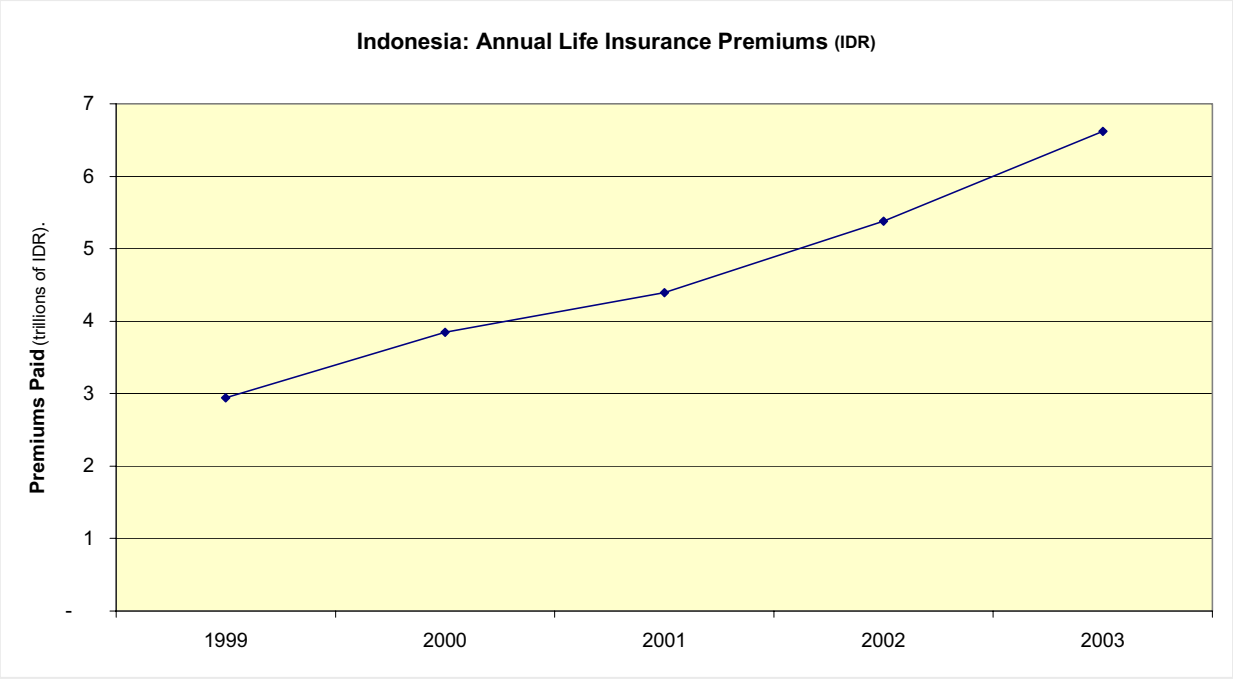
Table 3. Growth of Insurance Support Services

Insurance support providers	1999	2000	2001	2002	2003
Insurance and reinsurance brokers	83	78	91	118	141
Loss adjusters	23	23	23	25	25
Actuarial consultants	18	18	18	19	20

(Source: Indonesian Insurance in 2003. Insurance Council of Indonesia)

Although the number of institutions has remained relatively stagnant, there has been significant growth in terms of premiums received. This is important because it reflects a greater efficiency in the industry that should yield reduced premiums over time. An efficient insurance industry is important for the success of microinsurance. The growth of life premiums from 1999 through 2003 is shown in figure 1.

Figure 1. Indonesia Annual Life Insurance Premiums



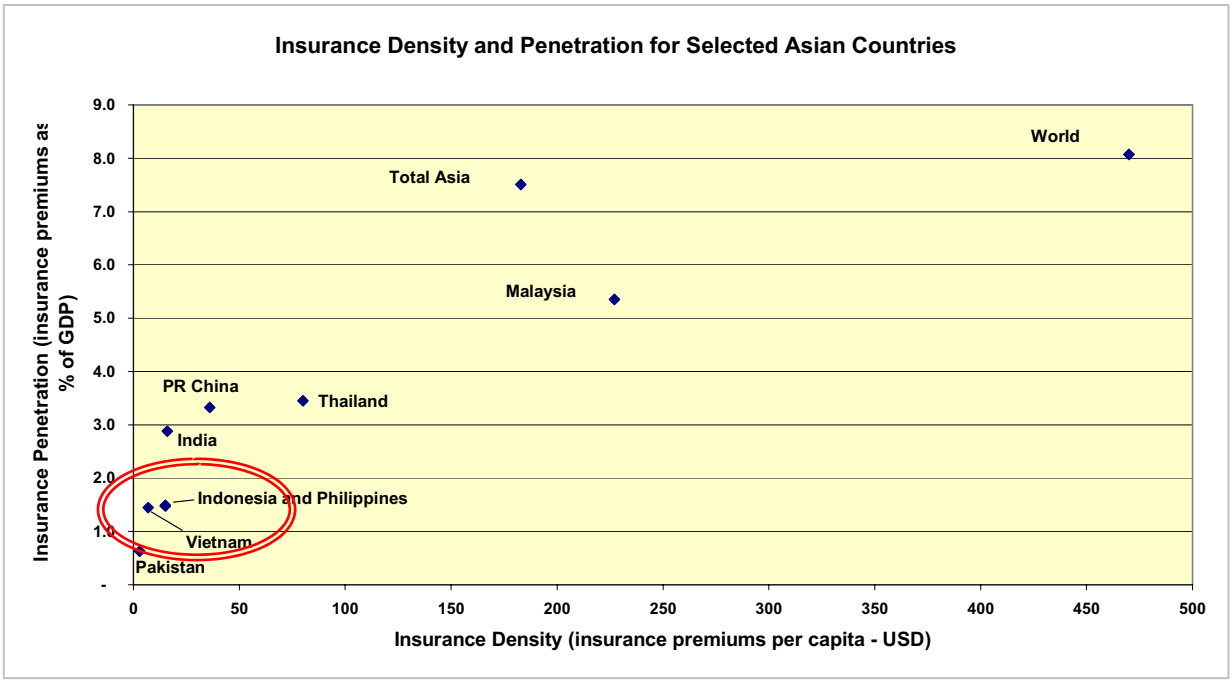
(Data source: Indonesian Insurance in 2003. Insurance Council of Indonesia)

Insurance density is a measure of the annual value of insurance premiums per capita. This is an important measure of insurance activity because it limits the distortion that population might cause in comparing insurance premium activity. In Indonesia, the insurance density for 2003 was $15 for total insurance premiums, of which $7 was for life products and $8 for general insurance products. These values are very low compared to the world average of $470, $267 and $203, respectively. However, the insurance density in Indonesia is similar to that in India and the Philippines. Some neighbouring countries do significantly better, such as Malaysia and Thailand with total densities of $227 and $80, respectively.

Insurance penetration (insurance premiums as a percentage of GDP) is also a good indicator of the strength of an insurance market. In the case of Indonesia, insurance penetration is a mere 1.49 percent of GDP. This is a level similar to that in the Philippines and Viet Nam, but this ratio is far lower than in Malaysia or Thailand, with 5.35 percent and 3.45 percent, respectively.

Figure 2, below, plots insurance density and penetration for several Asian countries as well as the Asian and world averages. With Indonesia grouped with the Philippines and Viet Nam in the very low range of these ratios, it is clear that there is significant potential for growth in the Indonesian insurance market. The already low level of insurance penetration fell even lower in 2003, dropping from 1.87 percent to 1.64 percent, although this was primarily the result of a 30 percent increase in GDP. Premiums increased by 29 percent from IDR30.18 trillion ($3.238 billion) in 2002 to IDR34.14 trillion ($3.663 billion) in 2003.

Figure 2. Insurance Density and Penetration for Selected Asian Countries 2003



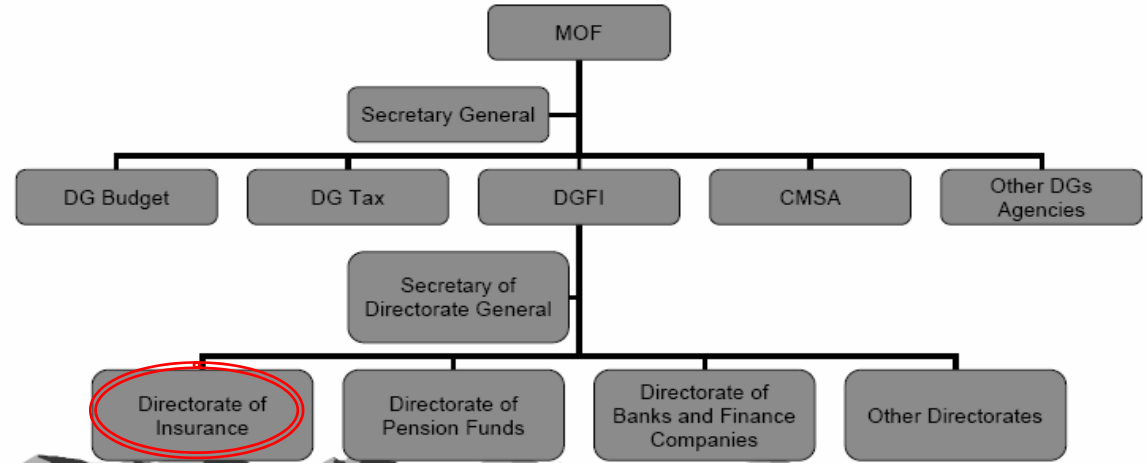
(Data source: Swiss Re: Sigma 3/2004)

These low values for insurance penetration and density reflect a significantly under-developed insurance market with huge potential for growth.

1.3 Status of insurance and/or microinsurance legislation

The insurance industry is governed from within the Office of the Directorate General of Financial Institutions in the Ministry of Finance. Figure 3 shows its organizational structure.

Figure 3. Organizational Structure of the Ministry of Finance
(Source: Isa Rachmatarwata Directorate of Pension Funds "Supervisory Structure of Pension Funds in Indonesia" Ministry of Finance of Indonesia. May 2003.)



No relevant microinsurance law is on the books in Indonesia, and laws commonly seen in other countries that might facilitate microinsurance are absent, such as a Mutual Benefit Associations Law. The one major insurer that is member-owned, Bumiputera, is governed under the traditional insurance law. There is discussion of revising current insurance law, but interviewees noted that microinsurance is not a part of those discussions. This is primarily because microinsurance has been treated under the current insurance statutes, and is not seen as significantly different from traditional insurance.

CHAPTER II. SUPPLY SIDE: TRENDS AND SCOPE IN MICROINSURANCE 'INDUSTRY'

2.1 Overview of the insurance industry

Microinsurance is a recognized concept in Indonesia. Several organizations offer microinsurance products, although the majority of these only 'offer' (more often require) credit life insurance to protect the portfolios of microfinance providers. Several large institutions are actively pursuing microinsurance products. An array of products are offered by member-owned insurers such as Bumiputera, the internationally-regulated insurance company American International Group (AIG) and the company created by the state-owned Bank Rakyat Indonesia, BRIngin Life. Additionally, microinsurance is often seen in informal risk-pooling mechanisms such as the *Arisans*. Although consolidated numbers of microinsurance policyholders over the years are not available, and indeed not maintained, it is clear that microinsurance is growing both in terms of number of covered lives and the array of products offered.

2.2.1 Insurance providers

The insurance sector is responding to new opportunities for economic growth and social protection policy stimulated by the Government. The insurance sector formulated a draft document 'Savings Mobilization toward National Prosperity' that recommends the design and availability of a broader range of long-term products. The life insurance business community recommends increasing savings mobilization through the insurance industry, particularly through pension funds and other long-term savings instruments, as one of the pillars of the economy. In this respect, they recommend that the Government facilitate all economic sectors to play their appropriate roles and create a suitable environment through taxation policy, economic policy, public communication and leadership. The insurers would like the Government to encourage diversification to protect individual savings from the fortunes of different sectors. This initiative as outlined in the draft document demonstrates how the insurance sectors, through insurance products and pensions, can build on the objective to fulfil long-term financial protection for society.

The following are three examples of products being proposed by the insurance sector:

- In the case of the death of the policyholder the survivors receive funds needed for mortgage liquidation and living expenses;
- Long-term savings for life insurance policy or annuity at the time of retirement;
- Long-term savings for educational purposes of a child in the event of premature death of the breadwinner.

Some in the insurance sector indicated an openness to designing microinsurance products for low-income groups (e.g., AIG and Allianz AG). The products would include cover against sickness and other health emergencies in addition to the number of credit life products already offered to small and medium-size enterprise (SME) clients. Moreover, the insurance industry notes that there must be a commitment to assist the Government in expanding policies to improve and increase the insurance density in Indonesia. In this context, they are willing to support education and awareness-building, training workshops, customer mediation and capacity building for the non-banking financial sector.

2.1.2 Insurance, banks and SMEs

When small and medium-size enterprises require loans, banks often ask for collateral to secure the credit. To protect themselves from client default due to death, and the need to collect the collateral of the deceased, a number of banks have set up their own insurance companies offering credit insurance (life and property). Usually the premium is included in the interest for the loan. Private insurers are offering credit life products, and some specialized 'credit guarantee' insurers exist to cover repayment loss by any default. Prominent examples of insurance companies linked to banks are mentioned below:[6]

- **Bank Rakyat Indonesia (BRI)**: BRI is a government commercial bank that began as an agricultural development bank. To increase client reach and profits, microfinance products and services were introduced to low income clients in 1984. At present, services are offered in Indonesia through an independent microfinance unit to both rural and urban clients. In 2001, Bank Rakyat Indonesia (BRI) had 2,790,192 microloan clients, of which 7% are women. Of the 27,045,184 clients that receive microsavings services, over 25% are women.

  SMEs provide 85 percent of the business of the 300 branches and 4,000 units. BRI established BRIngin Life and BRIngin General to provide property and life insurance as collaterals. BRIngin General does not provide the products to SMEs itself but uses the BRI in connection with securing their credits. As individual products are too costly for BRIngin Life, they intend to expand to cooperatives, using them as insurance pools that could then be reinsured by BRIngin.

- **Asuransi Central Asia (ACA)**: This domestic private company takes the lead in SME business. Their objective is to sell insurance to SME owners and provide education in risk management. ACA can build on the dense network of Bank Central Asia (BCA). It is not mandatory to buy credit life insurance when applying for a loan, and ACA has business not related to credit. Although ACA recently moved their insurance offices out of the bank branches, these branches are still their most important channels for selling insurance. ACA attempts to increase the current rate of 10 percent of the non-life portfolio with SMEs through education and training in order to enable them to manage their risks properly. Underwriting seems to be strict and through physical assessment of the risks (mainly owners of shops and small warehouses).

- **Askrindo**: This government-owned company supplements credit provided by banks with credit guarantees to the banks. Because their product covers 70 percent of default losses of banks that they insure, more banks may become interested in lending in the SME market. However, with an unsustainable loss ratio (as noted by management) this is a non-viable product without the intervention of government subsidies.

- **Jiwasraya**: This government-owned life insurer cooperates with the government-owned business development provider Perum Pengembangan Usaha (PPU). Whereas PPU provides a guarantee to the bank, Jiwasraya complements this guarantee with credit life insurance.

[6] Juerg Spiller, Opportunities to Promote Insurance Services for Small Enterprises in Indonesia–Assessment of Situation and Recommendations, Swisscontact Project, Jakarta 2004.

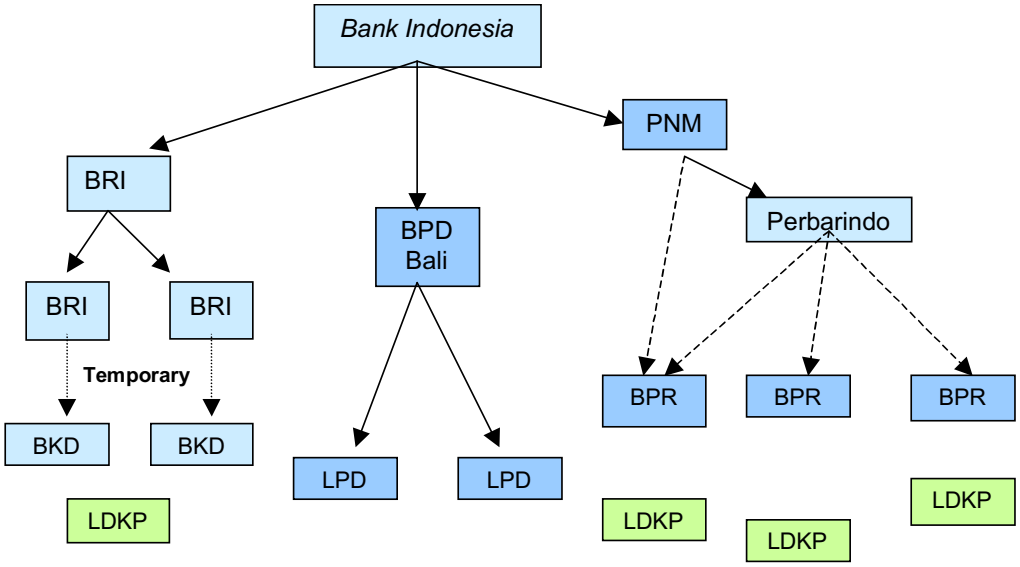
- **AIG/Lippo:** This company is a joint venture between American International Group, Inc. (AIG) and PT Asuransi Lippo Life Tbk. (Lippo Life). It notes in its mission statement that it will work with the low-income masses in Indonesia. Towards this end, they have developed a wide array of delivery channels and speciality products focused on this market.

In life and health insurance, foreign joint ventures are the preferred suppliers of products to SME such as Allianz AG, Prudential, Manulife, AIG, Credit Suisse Life and Pension (Health), and others. For smaller companies, in particular in the informal economy, domestic insurance providers are still the main actor in this market and offer the advantage of a dense network of agents and standardized, simple products.

2.1.3 Microfinance providers

Indonesia has a well-developed banking and MFP system reaching out to villages. In many areas, community members own locally registered village banks, knowns as Lembaga Perkreditan Desa (LPDs). In Bali, LPDs are registered under the Governor of Bali; the possibility of registering other types of microfinance providers regulated at the subnational level (LDKPs) is being discussed. So far, only a few microfinance providers are offering microinsurance, including the LPD Desa Adat Kedonganan in Bali (a product description is provided below). Figure 4 depicts a general overview of the Indonesian banking sector focusing on the potential implementation structure.[7] The chart flows from the country's central bank, Bank Indonesia, which is an independent state institution. It does not indicate the regulatory and supervisory relations between the institutions connected with that bank.

Figure 4. Rural Banking Structure



[7] During interviews with various stakeholders in Indonesia, it was mentioned that Bank Rakyat Indonesia (BRI) is currently supervising the BKDs on behalf of Bank Indonesia. However, supervision can still be improved and needs further support. PNM is not an apex-body for the whole BPR 'industry', although it has ties to quite a number of the BPRs. Perbarindo is a nationwide advocacy organization with regional chapters and training and consulting centres of the BPR industry. Perbarindo has training centres in most provinces. Neither PNM nor Perbarindo hold any operational power over the BPRs, however, and thus, in theory, each BPR would need to be approached individually. PNM and Perbarindo will be crucial, however, in getting buy-in from the BPR industry.

LPD Desa Adat Kedonganan is a registered village bank that provides several microinsurance products. Although 92 percent of all Balinese villages are covered by LPDs, only one, TIDAK (Tabungan Investasi Desa Adat Kedonganan), has developed a savings-cum-insurance package consisting of three products (Saving Investment Customary Village Kedonganan). These products are related to life insurance, school fees and the financial risks incumbent in traditional ceremonies:

- Tabeplus (Tabungan Bea Siswa Plus): This microinsurance product is a combined saving for scholarship fees "plus". In the event of the death/disability of the policyholder, it enables the child to continue his or her education and avoid dropping out of school.
- Sipadat (Simpanan Upacara Adat): This savings fund was designed for the purpose of covering high spending during traditional and ritual ceremonies, especially Panca Yadnya (Five Sacrifices) for the members of Kedonganan Traditional Village.
- Tabungan Sukarela: This product is a voluntary savings scheme.

Table 4. Premiums and Benefits of Tabeplus

Premium / deposit	Benefits	Special benefits
Different types: IDR2,000 per day IDR4,000 per day IDR6,000 per day IDR8,000 per day	LPD profit-sharing from managing Tabeplus at the end of year 12 In the event of death or permanent handicap, the deposit payment will be borne by LPD if the policyholder is not more than 55 years old	Annual savings lottery Savings available as collateral

Box 1. Bank Niaga: A Network Opportunity

Bank Niaga is a commercial bank that works with the low-income market. It offers SME credit products through intermediaries such as big companies reaching out to farmers, as in the case of loans for cattle sold. These loans are provided through companies that sell food and medicine to farmers. For farmers, these companies are focal points for essential transactions, which enhances the efficiency of all types of transactions.

Bank Niaga links with local financial institutions known as People's Credit Banks (BPRs) in several ways. In one example,funds are transferred from Bank Niaga to BPRs for on-lending, with all risk assumed by the BPRs. Another linkage is through joint financing with joint risks, with risks shared, for example, 90 percent by Bank Niaga and 10 percent by BPRs. A third approach is a lending agreement with BPRs that reduces their function as a service agent for Bank Niaga, which assumes all risks.

In addition, in cooperation with CIGNA insurance, Bank Niaga offers credit life insurance for consumer and SME credit. In the event of the death of the policyholder, the outstanding loan balance will be repaid to Bank Niaga. Depending on the amount paid to the bank the remaining amount will be passed to the nominee.

Bank Niaga offers credit insurance against loan defaults. In addition, it could be efficient to sell microinsurance productsl in particular endowment funds and life policies for educational purposes. This is an area where an outside group could have an impact. Management noted that they could imagine sharing responsibility: Bank Niaga would manage long-term savings with another institution designing the product and taking over the risk.

2.2 Overview of existing microinsurance provision

At least two major microinsurance networks are active in Indonesia in addition to BRI: Arisans and Pasar Konsortium. Both are discussed in detail below.

2.2.1 Arisans

Arisans are community-based informal financial groups with no formal governmental registration. They are organized throughout the country in all sorts of combinations such as professional and informal workers, urban and rural, men and women, wealthy and poor. Each *Arisan* group sets its own priorities. While some groups focus on savings, others work to raise business capital quickly and/or offer microinsurance. No credit can be granted to any member. Details of three *Arisans* visited are included in appendix 3.

Members generally conform to the group composition: e.g., family groups, local groups, groups of displaced people from the same area, business groups and many others. Membership is based on criteria such as "Good reputation and character", and begins upon payment of initial premium. Members do not sign contracts.

There are two *Arisan* **goals**. The first goal is to provide coverage for medical expenses, festivity expenses, educational expenses and business set-up costs, as well as death benefits, especially for the less fortunate members of the same family. The more fortunate ones, those with steady jobs, generally already have employee benefits and Jamsostek coverage and will thus use the Arisan as their insurance of last resort. This group accounts for 70 percent of members. The second goal is to create jobs through investment of premiums into small business enterprises.

Premiums range between IDR10,000 and IDR20,000 per month. The *Arisan* leader (Ketua) decides on the premium amount according to the financial capability of members (wealthier members may even voluntarily contribute up to IDR150,000/$16.09). Benefits, however, are equal for all members, regardless of the premium payments. Aspects of premiums also include the following:

- Start-up capital of IDR1 million donated by the Ketua;
- The property certificate of the account holder's house serves as security against account abuse;
- The grace period for lapsed premium is three months;
- No actuarial pricing is carried out;
- Reinsurance is provided by a wealthy clan member (non-member of Arisan) who makes coverage available if the total premiums collected are not sufficient to cover losses;
- The Ketua receives no financial remuneration for administrative tasks;
- Upon reaching a limit of available premium funds of IDR10 million, premium collection will be suspended and funds invested into a start-up business (e.g., a garage). The profits of the business will henceforth cover premiums.

Each **benefit** payment is decided by the *Ketua* of a member's *Arisan* subgroup (in difficult cases, in consultation with two other *Ketua*). Health benefits are not indemnity based, and thus are paid regardless of the actual costs incurred. There are no benefits for outpatient hospital stays, physician visits, maternity or chronic illnesses. For inpatient hospital stays, a minimum stay of three days is required and verified in person by the *Ketua*, who visits the

patient in the hospital. If two members have the same parent, death benefits are only paid once, to the most senior member, upon the parent's death. Coordination of benefits among the various *Arisans* is lacking, so members can claim benefits from all *Arisans* at the same time, since they are members in various *Arisans*.

Table 5. Benefits since November 2004
(Previously, benefits had been limited to death and celebrations. Written benefit tables and premium payment schedules exist.)

Covered item	Benefit (IDR)	Benefit ($)
Elementary school tuition fee	250,000	26.82
Driver's licence course (class A):	250,000	26.82
Inpatient hospital stay	500,000	53.65
Benefit for member's death	750,000	80.47
Benefit for a member's parent's death	500,000	53.65
Start-up capital for a member's new business	1,000,000	107.30
First communion (Catholic) or confirmation	50,000	5.36
Marriage (for example, a dowry in Sumatra)	100,000	10.73

A number of **other issues** affect Arisans. *Arisan* sustainability depends on the fact that a majority of their members are wealthy enough not to make use of their right to submit claims, yet continue to make excess premium payments. Clearly, a social motivation and welfare approach is dominant among group members. It is a common feature to avoid submitting claims. Another issue is that church-linked *Arisans* will seek out voluntary contributions during Mass at church or at group meetings. If the amount collected (premiums) is not sufficient to settle pending claims, they will ask for further donations, Regarding educational benefits, most *Arisans* use very 'flexible' criteria, which are determined by three *Ketua*:

- 'Poor' is not precisely defined (but generally means people without formal work); 'rich(er)' (means members with property/house);
- Children from poor families can receive educational benefits (for elementary school); criteria for receiving educational benefits for high school depend on the cleverness of the child, and this is determined by the *Ketua*;
- Community members can enrol in the educational scheme for the specific purpose of receiving educational benefits. Adverse selection is not considered.

2.2.2 Pasar Konsortium

In 1979, a fire destroyed the Tanah Abang traditional market in Jakarta and caused the Indonesian Ministry of Finance to ask local insurers to provide appropriate fire coverage for traditional markets (vast building complexes owned by local government. with 5–20 m² stalls or slots rented out to shopkeepers). A consortium of insurers came together to share the risk of such catastrophes. This consortium became the Pasar Konsortium,[8] and the concept has spread to the extent that the Pasar Konsortium is active all over Indonesia, in urban as well as rural areas. Most of the policyholders are shopkeepers and are reasonably wealthy.

Table 6. Pasar Konsortium Organizational Structure

Type	Description
Management:	▪ Operational management led by TuguRe ▪ Board of Management consists of members of all Konsortium partners
Members	56 local insurers of which 52 are insurance companies, and 4 are reinsurance companies (TuguRe, IndoRe, NasionalRe, MaReIn)

[8] The official name is KARK (Konsortium Asuransi Resiko Khusus) or the special risk insurance consortium.

Cooperation is based on the principle of **co-insurance**. Some insurers act as policy issuers and risk takers, others solely as risk takers (including all reinsurance companies). The policy-issuing company receives 15 percent commission, and 85 percent of the premium is given to Pasar Konsortium as follows: 5 percent of 85 percent goes to operational management (TuguRe), and 5 percent of 85 percent goes to the Board of Management for administrative expenses.

Products and benefits of the Pasar Konsortium include fire insurance for building and construction, which is usually purchased by the owner of a traditional market (government/local administration). There is also insurance for *Hak Pakai* (right of usage) against fire, which is purchased by shopkeepers to insure the reestablishment of their businesses in case of fire. *Hak Pakai* can be used as collateral to obtain loans. Shopkeepers (including small shopkeepers and traders) also purchase stock insurance. No personal accident insurance, life or health cover is available.

Premiums paid by shopkeepers are about IDR1 million per month and are based on the risk rates below.

Pasar Konsortium risk rates:

- 24/1000 for base risk (constructions in good condition and with appropriate fire protection);
- 36/1000 for group I rated risk (mediocre condition);
- 48/1000 for group II rated risk (bad condition).

Pasar Konsortium profitability:

- Loss ratio over 100 percent;
- Large traditional markets in big cities are responsible for high loss ratio;
- Claims experience in rural areas is much more favourable;
- Retention limit for the Konsortium is only IDR2 billion;
- Excess of loss is covered by foreign reinsurance company;
- Because of the low retention limit, the Pasar Konsortium is working profitably.

Among **other issues** of the Pasar Konsortium, claimants are generally required to provide complete records of all transactions to receive full insurance benefits. Exemptions from this rule are common, however, especially when big fires destroy the records of many shopkeepers. The sum insured for a whole building (paid by government as owners) in bigger cities often amounts to IDR50 billion–IDR100 billion. Regarding fraud, insurance fraud is not perceived as occurring with small shopkeepers and traders. Fraud does occur among local administration/government but is extremely hard to prove (e.g., when a market is to be demolished to make way for a shopping mall and/or when major renovations are due).

2.2.3 Legislative frameworks and industry initiatives

The Directorate of Insurance supports insurers moving downmarket. Their efforts are without a specific strategy, but they report that they tell the pension funds and others that there is business in the low-end market. Thus far, microinsurance initiatives have either been conducted under the framework of the existing law (AIG/Lippo, Bumiputera), or without legislation, yet with the full knowledge and often the participation of local governments (*Arisans*).

There have been several interventions by the insurance industry to provide microinsurance in Indonesia. The simplest approach has been by insurance companies that are linked with or owned by banks. The banks may require that all borrowers purchase their credit life insurance, and they also may sell additional risk management products. Their focus, however, is only on their own client market. BRI is an example of such an institution.

AIG/Lippo has taken a more innovative approach. These organizations have their own insurance agents but they have also been working with other organizations as agents to sell their array of microinsurance products designed especially for this market. This strategy has taken insurance products to places where they are rarely seen.

Bumiputera is a member-owned insurer. In other countries, these have been very successful when they reach large scale. However, Bumiputera has experienced significant financial difficulties over the years. Possibly a different mutual benefit association might be structured in a manner that could be successful. Ownership is attractive to members, as long as they are not left with onerous work to do in support of the institution. This can occur when there is a substantial membership, and a professional insurance management team.

2.3 Sharia insurance products: future potential for microinsurance

The emergence of insurance that complies with the principles and laws of Sharia will have a major impact on the potential for microinsurance. Sharia is the legal framework within which the public aspects and some private aspects of life are ruled for those living within the state and who belongs to the Islamic community. Indonesia is the most populous Muslim country in the world, and insurance companies are now recognizing the importance of responding specifically to their needs and requirements.

Most Sharia-compliant insurance currently focuses on the upper-middle and high-income markets. It is people in the low-income market, however, who are most likely to be reluctant to purchase products that do not comply. When low-income people have a choice between Sharia and non-Sharia-compliant products, the Sharia products may have an advantage. Therefore, it is possible that having Sharia-compliant products could aid institutions that are trying to reach the low-income market. More research is required to confirm this supposition.

Numerous groups and organizations throughout Indonesia have potential demand within their ranks for Sharia-complaint products but insurers have not yet approached them. These could yield a major source of microinsurance policyholders for the insurer who is innovative and willing to take a chance.

2.3.1 Takaful insurance

Takaful in Arabic means “joint guarantee”. It is an insurance system that complies with Sharia. Most of the insurance companies in Indonesia are either developing or have developed Takaful insurance products, and even Takaful divisions, to respond to and develop the growing demand from the Islamic community.

Takaful insurance is governed by the Ministry of Finance and its Insurance Directorate, but licensing and continued operation as a Takaful insurer or Takaful division is dependent on the continuing approval of the National Board of the Sharia Council. The 18 members of the National Sharia Board must approve requests for new Takaful products before the

Insurance Directorate will begin their approval process. This process involves a review of several aspects of the product in order to confirm conformity with Sharia law. This includes: how transactions are managed, how investments are made, into which investments Sharia premiums will be placed, and how earnings will be distributed.

In order to ensure continued compliance, the Board requires a three-member Sharia committee to be housed within the insurance company to review regular transactions and policies, and to guide management in their product and process decision-making regarding Sharia aspects of operations.

Table 7. Takaful and Commercial Insurance

Takaful insurance	Commercial insurance
Policyholders share in operating and investment results	Policyholders pay premiums which become the property of the insurance company
Operating surpluses are held in reserve to offset future losses but remain the property of the policyholders	All risk and all operating results (regardless of profits or losses) are borne by the insurance company
Distribution of earnings is defined in the policyholder agreement	

Figure 5 illustrates the differences between Takaful insurance and commercial insurance. Specifically, it shows how a premium payment is applied .

2.3.2 Other aspects of Sharia compliance

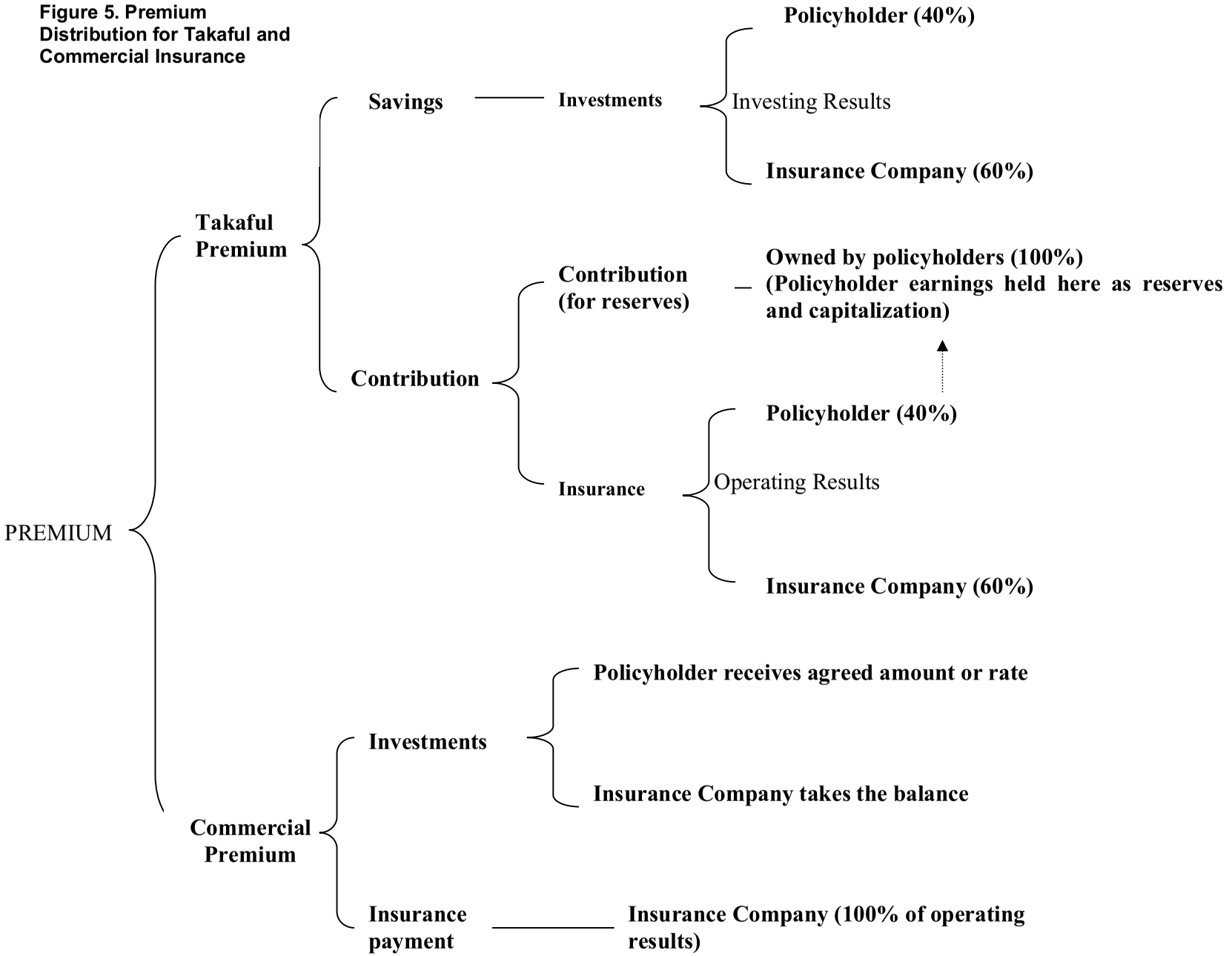
Another factor that must comply with Sharia law is the investment of insurance contributions and savings. In the past, this has been a limiting factor. As of June 2005, however, there were 16 *modoroba* bonds, and the Government was in the process of developing its own. Typically, there are restrictions on investments by the central banks requiring a certain mix of investments. It will be necessary for these requirements to be carefully reviewed, to ensure that the required investments comply with Sharia, while the portfolio is maintained with policyholder security as a primary objective.

How insurance is sold is also a factor in developing a Sharia-compliant product. Takaful insurance can be sold by an intermediary as long as three criteria are met:

- The intermediary must charge a **fee**, not a commission;
- Buyers must understand that the intermediary is only a pass-through to move their premiums to the Sharia insurer more efficiently;
- Any proceeds (premiums) must be held in a separate account and not commingled with other intermediary funds.

At this point, no Islamic scholars are saying that microinsurance is *haram* (religiously wrong), but for Sharia microinsurance to be effective the local religious leaders must give their approval. One way to assist in the promotion of microinsurance could be to have the Sharia insurance council members make public statements to educate the population. It is clear that in some way religious leaders will need to be involved in order to promote microinsurance.

Figure 5. Premium Distribution for Takaful and Commercial Insurance



2.4 The Government and social protection

The Government of Indonesia and local government authorities have not yet seen microinsurance as a priority area. Several steps have been taken by the Indonesian Government to better regulate MFPs but it is a process that will take some time. Indeed, microinsurance is not specifically regulated anywhere except in India. For microinsurance to work, it is important that MFPs should have the freedom to act as agents. It should, however, be clear that MFPs should never take insurance risk. Recent issues pertaining to microinsurance include the following:

- The Ministry of Finance is discussing the option of linking BPRs (People's Credit Banks) to unregulated MFPs (LDKPs), rural community funds, and credit institutions. In addition, the Ministry also may require the registration of these unregulated groups;
- The regulator has eased the conditions for obtaining a license for agents, which both agents and brokers need in order to sell insurance;
- MFPs (LPDs) have been regulated in Bali under the Governor of Bali since September 2002;
- Leasing under Sharia does not require an official licence.

2.4.1 Current situation of safety net mechanisms / social security systems

Social security is under revision due to the new social security reform Act No. 40/2004 (signed October 2004). The law provides benefits for health care, work accident benefit, old age and pensions, and death. The implementation of this Act will have significant implications on those risks for workers in the formal economy and the beneficiaries of social assistance, including the poor and economically disadvantaged in the informal economy. The poor and disadvantaged, however, will be enrolled in stages as government takes over the contributions for these groups.

The process of formulating the specific rules, regulations and procedures has been initiated. During the five-year transition period mentioned in the Act, the existing social security executive bodies[9] will continue to exist, giving the same benefit to its segment as provisioned in the existing Acts.[10]

Under the Indonesian Constitution (article 28, clause H 3), all people shall have the right to social security. In article 34 (2), the State assumes the responsibility for developing a "social security system for the whole people and empower those who are disadvantaged and vulnerable in accordance with the human worthiness."

Responding to this responsibility, the Government has formulated programmes for civil servants (PNS), the Indonesia National Army (TNI), the Indonesian National Police (POLRI), and for those who are working in the formal sector (>10 employees). State-owned social insurance companies have been appointed to conduct the programmes. These companies are PT

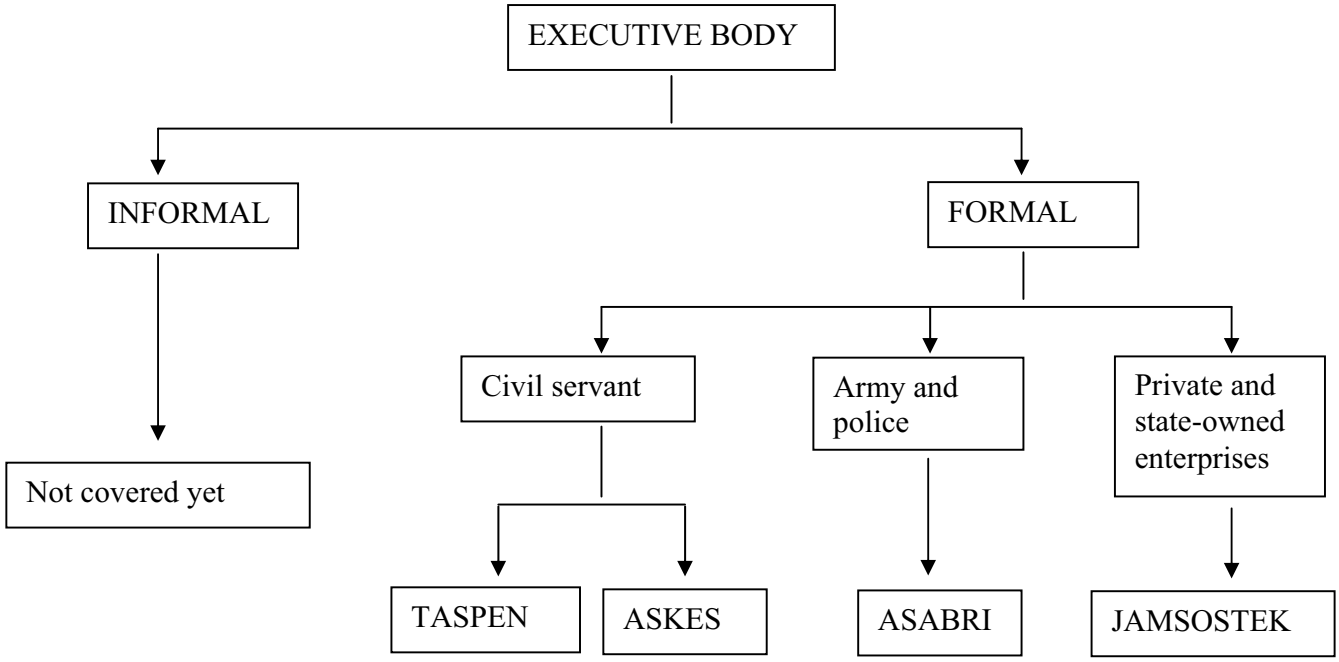
[9] PT Jamsostek, PT Askes, PT Taspen, and PT Asabri.

[10] For Perusahaan Perseroan (Persero) Jamsostek: Government Regulation no. 36/1995, for Dana Tabungan dan Asuransi Pegawai Negeri (Taspen): Government Regulation no. 26/1981, for Asuransi Sosial Angkatan Bersenjata Republik Indonesia (Asabri): Government Regulation no. 68/1991, for Asuransi Kesehatan Indonesia (Askes): Government Regulation no. 6/1992

Asabri, PT Askes, PT Jamsostek and PT Taspen. PT Jamsostek provides services to formal-sector workers as a part of the Government's Social Welfare Insurance Programme (SWIP).

Several social security and social assistance programmes for the informal economy, self-employed, marginal groups and the poor are implemented by the Ministry of Labour and other ministries. In this context, the Ministry of Labour, Department of Social Affairs developed a Social Welfare Insurance Programme (SWIP) targeted to those who are "classified as marginal groups and … considered to have potential social problems."[11] The Government applies a quota due to budget constraints and covers approximately 60 percent of the poor (providing approximately <IDR100,000 per month per person).

Figure 6. Existing Social Security Executive Structure
(Source: Jamsostek: The Resume of Act no.40 year 2004, National Social Security System in Indonesia, Jakarta 2005)



In addition to providing social insurance to the formal economy, PT Jamsostek has introduced some schemes for the informal markets. According to the new Social Security Act, the company is supposed to expand selected benefits to informal economy workers.

2.4.2 Current benefits

The Government's SWIP benefits include: death benefit of IDR200,000 to IDR600,000; accident and sickness benefit at least for 30 days as inpatient, or for treatment in hospital for at least 5 days up to IDR100,000 per year; and savings benefits are available at the end of the insurance period. The premium is IDR5,000 per month. The age range is 21 to 59 years old. Workers or self-employed with minimum income of IDR200,000 per month.

[11] Directorate of Social Assistance, Directorate General of Social Relief and Assistance, Department of Social Affairs of the Republic of Indonesia: SWIP – Social Welfare Insurance Programme, Jakarta

The benefits of PT Jamsostek's 2004 employees' social security scheme (which is a pilot project for self-employed workers) offers benefits according to government Regulation No. 14 (1993), specifically an employment accident benefit, death benefit of IDR5 million, and funeral expenses of IDR1 million. PT Jamsostek offers soft loans to microenterprises and casual wage earners in construction and cigarette factories.

Other programmes such as health and cash benefits for old age are operated through the Department of Social Affairs (DEPSOS). The Municipality of Jakarta offers back-to-school programmes and educational assistance. KUB provides business grants for social groups. PMKS offers social assistance for habitation and economic activities. Kredit Usaha Tani/KUT gives loans to small-holding farmers and rural entrepreneurs. The Ministry of Agriculture's Directorate of Social Relief and Assistance offers in-kind and cash assistance for victims of natural disasters.

After the financial crisis of 1997/98, which caused severe problems for many people, the Government introduced social assistance measures in several areas:

- Food security, through Social Safety Net (SSN/JPS), with rice subsidy programme OPK;
- Education, with scholarships and Dana Bantuan Operasional, DBO grants:
- Health and nutrition programmes providing free health care for poor people, higher quality food for babies and mothers, PMT-AS;
- Employment creation programmes for the poor and unemployed (PKSPU);
- Community empowerment through the creation of business opportunities and local socio-economic infrastructure, PDM-DKE;
- Fuel tax compensation through a system that provides financial support to alleviate health costs for poor households.[12]

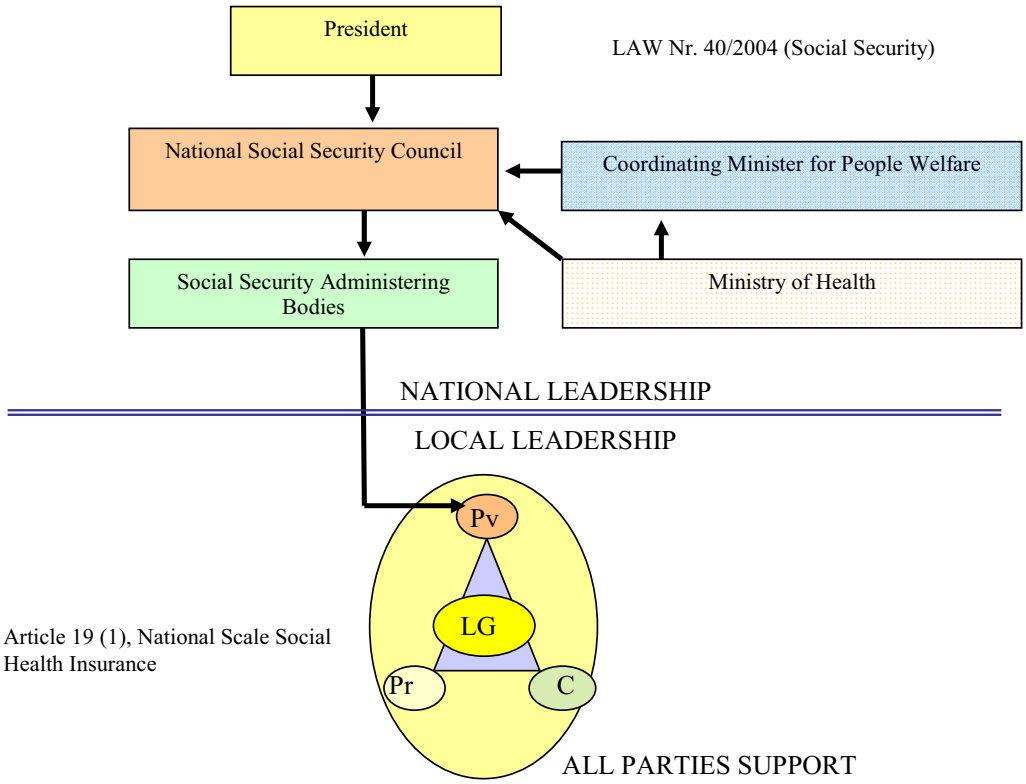
2.4.3 Future situation under the new Social Security Act 40/2004

With the social security system under revision at this time, much remains to be defined and tested, including the specific rules and regulations as well as the implementing structure. One of the most important advantages under the new social security law is the lean management structure, contrary to the current fragmented responsibilities between various ministries.

At the national level, a National Social Security Council will be established consisting of 15 members. Government, employers, employees and experts will all be represented. An administrative body will be responsible for the implementation. The Ministry for People Welfare will act as the coordinating ministry, and other ministries such as the Ministry of Health will become members of the National Social Security Council. At the local level, steering committees consisting of all stakeholders (local government, provider, payer, communities) will be set up. This participatory process is in accordance with the Decentralization Act (No. 32/2004, article 22) providing a stronger role for the provincial government and communities, including the development of effective social security systems. Figure 7 illustrates how Social Health Insurance will be implemented and managed.

[12] The fuel tax compensation system is currently piloted in 13 districts and municipalities. The system's targeting approach is similar to SSN. About 20 percent of compensation funds amounting to IDR4.43 trillion in 2003 are used to cover prepayments of health costs for the poor.

Figure 7. Structure of Social Security Law & Implementation of Social Health Insurance



Py = payers; Pr = providers; C= community, LG= local government

(Source: Amended from GTZ Social Health Insurance project, Kick-off Workshop March 2004)

2.4.4 Broadly defined future benefits

In the future, benefits will cover health insurance, work accidents, old age and pensions, as well as a death benefit. This benefits package is only broadly defined at this time, and needs to be further specified. It includes the following features:[13]

- **Health benefits:** individual health services, which will include health promotion, preventative and curative treatment, and rehabilitation (including medicines and medical supplies used as necessary). An employee who has more than five family members and who wishes to include other family members is required to pay an additional contribution.

- **Work accident benefits:** health services appropriate to her or his medical needs and cash compensation in the event of an employee being involved in a work accident, suffering work-related illness or permanent total disability or death.

[13] Law of the Republic of Indonesia, Number 40 of 2004, The National Social Security System

- **Old-age pension:** received from the age of retirement up until the time of death. Cash benefits are paid at once to participants when they reach the age of retirement or suffer permanent total disability. In the event of the death of a participant, his or her legal heirs are entitled to receive old-age pension benefits. The amount is determined based on the total accumulated contributions made plus a return on their investments. Partial payment of old-age pension benefit may be made up to a certain limit after participation of a minimum of 10 years. The public pension scheme should ensure an adequate standard of living in the event that a participant suffers a loss or reduction in his or her income because he or she is of retirement age or has suffered permanent total disability.[14] Regular monthly payments from the age of retirement up until the time of death after making contributions for a minimum of 15 years (for further details see art. 41 of the Law).

- **Life insurance:** will provide compensation to a participant's heir in the event of his or her death. The amount of life insurance benefits shall be determined based on a nominal value.

2.4.5 Specific regulations in the future benefits package

In general, workers who pay contributions are covered, and their premiums shall be determined as a percentage of wages to be shared by employers (joint responsibility). The amount of health insurance, work accident insurance, old-age pension and life insurance contributions for participants who do not receive a wage and those receiving social assistance is to be determined based on a nominal amount (based on minimum wages) that will be reviewed periodically providing reduced benefits. In particular, the following specific regulations will be applied:

- Life insurance contributions for participants who receive a wage will be borne entirely by the employer. The amount of life insurance contributions for participants who do not receive a wage will be determined based on a nominal amount, to be paid by the participant;
- Work accident insurance contributions for participants who receive a wage will be determined as a percentage of wages or income and borne in full by the employer;
- In the event of a participant experiencing permanent total disability and unable to pay contributions, his or her contributions shall be paid by the Government;
- Public pension is not provided for non-wage earners.

2.4.6 Current situation: Effectiveness and gaps of social protection

The social security system in Indonesia is primarily focused on workers in the formal economy, including the civil service. According to the appraisal report on social health insurance in Southeast and East Asia, 100 percent of civil servants, greater than 10 percent of formal-economy workers, and less than 5 percent of informal-economy workers are covered by social security systems.[15] Even within the formal sector, considerable disparities exist between public

[14] Disability pension, received by participants who are disabled as the result of an accident or as the result of illness, up until the time of death; widow/er pension, received the pension until the time of death or remarriage; child pension, received by the child heirs of a participant, up until the age of 23 years, or until he or she starts work, or marries; parent pension, received by the parent heirs of an unmarried participant, up until a certain time limit established by statute.

[15] A. Alkatiri, J. Hohmann, C. Lankers, H. Thabrani: Development of a Social Health Insurance for Indonesia, Jakarta, Nov 2000

sector workers and the few private sector workers who are covered by occupational benefits, a slightly larger group covered by Jamsostek,[16] and the majority who are dependent on the basic provisions of the labour law (e.g., 6 percent of the labour force can expect pension or retirement benefits).[17]

More than 90 percent of the population is excluded from formal health insurance schemes, as estimated in an International Labour Organization (ILO) study in 2004.[18] This is due primarily to the "opt-out" clause for self-insured persons and those purchasing more generous health packages than those provided by Jamsostek. Given the limitation of benefits regarding hospital stays and specific treatment, and the restricted choice of providers, many employers believe that it is not worthwhile to join the scheme, and thus opt out.

Shortcomings

The current social protection programme has a number of shortcomings, as described in a study on social protection programmes carried out by the United States Agency for International Development (USAID)[19] and also in a 2002 ILO report.[20] In general, many of the potential beneficiaries were not aware of the programmes. In the case of the JPS Social Safety Net Programme, the constraints seem to be related more to implementation and control mechanisms than to the basic concept:

- Programmes were underbudgeted and as a result provide inadequate benefits;
- Community grants or loans were faulted, the objectives were not well understood, and hence activities were not properly targeted to benefit the poor;
- The Government lacked an adequate administrative network, especially for implementing the JPS. As a consequence, many target groups did not receive the benefits of the social assistance programme. Instead, 'leakages' to higher-income groups were noted.[21]

Closer attention to targeting, administrative control and good governance (including better coordination between ministries) could improve delivery and enable better access to benefits and services.[22]

The ILO report on the Extension of Social Security specified an increase in private expenditures in total health care spending over the last several years from 54 percent in 1995 to

[16] Only 5 percent of the employers are members of Jamsostek. Subsequently, in 2000 about 17 million employees of about 35.8 million wage-earning and salaried workers were enrolled in Jamsostek. As employers can opt out from the health insurance only 2.9 million workers (including their families) were enrolled in Jamsostek health insurance, less than 5 percent of eligible people.

[17] E. Adam, M. von Hauff, M. John: Social protection in Southeast and East Asia, Friedrich Ebert Stiftung, Singapore 2002

[18] Xenia Scheil-Adlung, ESS Paper no. 19, Sharpening the Focus on the Poor: Policy Options for Advancing Social Health Protection in Indonesia, ILO, Geneva 2004

[19] C. Stuart Callison, Social Protection Programs: Components, Priorities, Strategic Choices and Alternatives for Indonesia, USAID, Jakarta October 2002

[20] ILO Report, Restructuring of the Social Security System in Indonesia, Jakarta 2002

[21] According to the USAID study and the ILO report, the scholarship programme reached 96–99 percent. But the percentages of poor households were only 6 percent in primary schools, 12 percent in lower secondary and 5 percent in upper secondary schools. The health programme covered 98 percent. Again, the fraction of the poor was very small. The nutrition programme reached 15.9 percent of all pregnant women and children under three–79 percent were from non-poor families.

[22] The poor are entitled to free treatment in public hospitals. However, they have to receive a document certifying their poor status and the referral by the *puskemas* (local primary health centre). Several respondents experienced a substantial delay in receiving documents. In the event of severe illness, patients could not wait and checked into the hospital at their own expense.

76.3 percent in 2000 (Ministry of Health, Indonesia, 2003). This increase is funded mostly from out-of-pocket spending, prepaid plans, and risk-pooling plans. In 2000, about 50 percent of public health expenditure was allocated to pharmacies, drugs and medical equipment; 39 percent to hospitals; and 11 percent to health centres and sub-centres.

Lack of access to health services is mainly caused by high out-of-pocket payments, inequities in budget allocation, and significant underfunding, despite the relatively large number of local primary health centres, called *puskesmas*. These provide basic health services at low cost, but the quality of services differs widely (Bali is a positive example of effective services). The poor can apply for a letter for discount at *puskesmas* and government hospitals, but access is limited by a nationwide quota system set up by the Government and proof of meeting the criteria of being "poor enough." Apparently, in some regions, timeliness of receiving the letter is not a problem, whereas in others, the poor did not receive the document in time and were forced to utilize health services at their own expense. According to interviews taken in the context of the current study, the different respondents who were able to obtain the letter reported coverage as either 50 percent or 100 percent of total costs.

Figure 8. Population Coverage by Social Health Protection Scheme



Source: ILO 2002

The recently signed social security law can be considered to be one step towards broader coverage. Of the five sub-components of the law, the Government is focusing first on implementation of the National Health Insurance. This component aims at universal health coverage including informal-sector workers, although this is a long-term goal. In the meantime, voluntary coverage will be possible for those who are not covered. Given experience in the Philippines and other countries, however, it is unlikely that many of the self-employed will voluntarily pay the Government their social security dues.

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The draft legislation aims at addressing the main concerns in existing schemes. It intends to improve equity through extending risk pooling, subsidizing the poor, and lowering cost sharing. Government subsidies deriving from central and local governments are expected to cover premiums of some 40 million people considered as poor.[23] Thereby, the high out-of-pocket rate should decrease, and an integrated scheme also might lead to improved governance and administration. The Decentralization Policy (Law 32/2004, art. 22) provides for extended autonomy and participation of local authorities and communities.

Local health councils or committees could advocate for increased health funding. They could work towards a participatory approach consisting of a broad "coalition of all stakeholders in health care" from various levels including social partners, local authorities and representatives of

[23] *The Jakarta Post*, 2004

the poor. These councils might also provide feedback to central and local governments, e.g., on quality monitoring, planning and health-care needs, and thereby support the setting of priorities and adjustments in budget allocation.

2.5 The informal sector: opportunities for distribution

The informal sector in Indonesia is vibrant in many areas. It was especially vibrant in some of the areas visited on this mission: Bali, Jakarta and Yogyakarta. Some level of microinsurance is already being developed and operated by churches and women's groups and small informal groups. Among the most sophisticated are the *Arisans*, discussed above. It is important to recognize that *Arisans* and likely many of the other informal groups are reliant on financial inputs from non-members. Such inputs would come from church contributions and general collections, and members who have no intention of claiming against the pool. In many ways, this system may be a way for people to avoid losing face when in need, and is certainly preferable (usually for both parties) to having to ask individuals for assistance.

The informal sector offers an important opportunity for distribution of microinsurance products. Many small informal organizations are already trying to provide cover for their members, although this is often insufficient to cover the costs. Others are reliant on donations. The linking of some of the more developed informal-sector groups like the *Arisans* could provide improved coverage and an efficient means for an insurer to collect premiums. *Arisans* should be a primary target for distributing microinsurance.

2.6 Banks and others: widespread providers

Several banks have been discussed above that create their own insurance units to facilitate the offering of microinsurance products to their members. Bank assurance with the credit life and disability products is reasonably common, and microfinance providers are widespread across the country, both urban and rural. Some are providing basic insurance, although those offering credit are more focused on portfolio protection and the basic products that offer such protection.

Because of the very large Indonesian population, it can be relatively easy to grow any programme very quickly. Any microinsurance programme should be prepared for rapid growth. An example is BRIngin Life that provides mandatory credit life and other voluntary products to BRI clients. BRIngin Life manages all the individual transactions on paper in the field and then inputs the transactions in the head office. BRIngin's client base is nearly 10 million.

Microinsurance success is predicated on efficiencies. When looking for a bank or other institution to partner with in the delivery of microinsurance products, it is critical for both parties to conduct a due diligence exercise to ensure that it is the right partner organization. Manual recording is very inefficient. Among the concerns are the reputation of a given company and the transparency of its activities.

Corruption is a reality, and the Office of the State Minister for State Enterprise has recently quantified the allegedly most corrupt state enterprises. In its list (see figure 9) several institutions

discussed in this paper appear prominently as among the most corrupt: BRI, Bank Mandiri and Asuransi Jiwasraya. Insurance is a business of trust. The low-income population especially is sceptical about non-tangible products. It will be important to select partners carefully.

Figure 9. Alleged Corrupt State-owned Enterprises



Alleged corrupt SOEs

Companies	Business	Companies	Business
1. Bank Rakyat Indonesia	Banking	9. Pupuk Kalimantan Timur	Fertilizer
2. Bank Mandiri	Banking	10. Angkasa Pura I	Airport operator
3. Bank Negara Indonesia	Banking	11. Pelabuhan Indonesia II	Seaport operator
4. Perusahaan Listrik Negara	Power	12. Pelabuhan Indonesia III	Seaport operator
5. Asuransi Jiwasraya	Insurance	13. ASDP	Transportation
6. Perusahaan Gas Negara	Energy	14. Djakarta Lloyd	Shipping
7. Indofarma	Pharmaceutical	15. Televisi Republik Indonesia	Television station
8. Rajawali Nusantara Indonesia	Trading	16. Radio Republik Indonesia	Radio station

Source: Office of the State Minister of State Enterprises

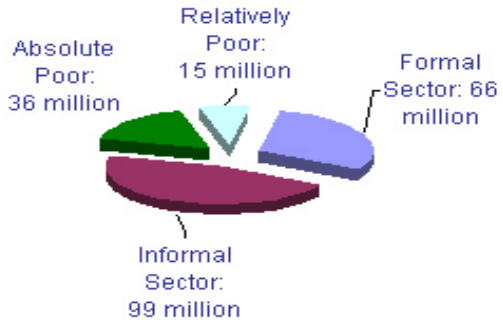
CHAPTER III. THE DEMAND SIDE: CUSTOMERS AND MAJOR RISKS

3.1 Characteristics of likely microinsurance customers

The potential market for microinsurance in Indonesia is immense. With a population of 238 million, 53 percent of the people live on $2 per day or less. Researchers estimate that two fifths of the population near the poverty line are highly vulnerable to even modest shocks to the economy.[24] Large numbers of people live in high-risk environments, the majority in rural areas.

Figure 10 illustrates the sectors into which Indonesia's diverse population falls: formal sector, informal sector, relatively poor, and absolute poor. These sectors are relevant to the characteristics of likely microinsurance customers.

Figure 10. Indonesia Population Distribution



The first microinsurance customers are most likely to come from among the base of current microfinance and SME borrowers. It is estimated that about 10 million micro-enterprises have access to formal financial institutions. It is believed, however, that 43 million people depend on micro and small businesses to make their living.[25] Thus, the market for microinsurance provided through these intermediaries could easily be substantial. These Indonesian micro-entrepreneurs are engaged in activities such as farming, shopkeeping, food processing, trading and small-scale manufacturing. The majority of respondents who participated in our research were employed in these activities. The respondents also engaged in the production of handicrafts and raising livestock.

[24] Jansen, Stefan, Michael Hamp and Alfred Hannig. "Microfinance in the Rural Financial System and the Development of the Local Economy"

[25] 'Indonesia Country Profile', Asia Resource Centre for Microfinance, Banking with the Poor web site (last update 22 March 2005).

3.2 Major risks and risk-management strategies of low-income groups

Risks are varied and widespread. Over the years, people and communities have developed a wide range of coping mechanisms to deal with uncertainties, mitigate risks and manage after suffering a loss. These strategies are typically not tailored for a particular risk, but are applied as needed. The most important risks for low-income groups in Indonesia can be categorized as life cycle, business, environmental and social risks:

- **Life cycle risks** are events that happen in the course of most lifetimes and require large sums of money, such as weddings, funerals or births;
- **Business risks** are related to business activities;
- **Environmental risks** are related to the physical environment and climate, such as flooding and tidal waves;
- **Social and cultural risks** include social obligations, including the demands to provide support or reciprocal gifts to family, neighbours and community members.

Risks can also be categorized as co-variant and idiosyncratic. Idiosyncratic risks affect only one individual or family at a time; examples include an accident or serious illness. Co-variant risks affect a large number of people at the same time; for instance floods, earthquakes, and avian flu. Generally speaking, environmental and social risks are co-variant, while business and life cycle risks are idiosyncratic.

Table 8. All Risks Identified by Focus Group Participants

	Identified risk	Number of Mentions	Number of Times Ranked in Top 4
1	Serious illness	14	12
2	Education of children	12	12
3	Poor harvest	5	5
4	Death of a relative	8	4
5	Social obligations	6	3
6	Marriage of children	4	3
7	Business loss	7	2
8	Accident	6	2
9	Lack of business capital	5	2
10	Inflation	5	2
11	Birth of child	4	2
12	Loan payment to MFP	3	2
13	Building/renovating a House	2	1
14	Floods/rain	2	1
15	Non-payment of credit	3	0
16	Theft	1	0
17	Drought	1	0
18	Death of animals	1	0
19	Job for child	1	0

	Identified risk	Number of Mentions	Number of Times Ranked in Top 4
20	Unemployment of youth	1	0
21	Competition	1	0
22	Old age/retirement	1	0

The top ten risks identified in the research in Indonesia are: serious illness (requiring hospitalization), education of children, poor harvest, death of a relative, social obligations, marriage of children, business loss, accident, lack of business capital, and inflation. Of these, **insurable** risks include: (1) serious illness, (2) education of children (through a life policy), (3) poor harvest, (4) death of a relative and (5) accident. Each of the five insurable risks will be examined in the following sections.

Significant but **non-insurable** risks include social obligations, business loss, marriage of children and inflation. Respondents identified social obligations as a burden, but they are also an advantage. Social norms require that neighbours and community members pitch in with gifts and donations in times of death and marriage. While reciprocal obligations may be a burden one day, they may be a benefit the next.

Business losses are related to other risks, including the non-payment of credit extended to purchasers, inflation (in which input prices go up but the entrepreneur is not able to pass on the higher cost to the final consumer), and loan repayment. Business losses were perceived as particularly burdensome because the research subjects were all microfinance clients. These clients rely on their business income for the money to repay the microfinance loan; therefore, business losses threaten their ability to repay their loans. Lateness in loan repayment is not only personally embarrassing because they are part of a group, but it can reduce access to credit in the future. Thus, the stress resulting from business losses goes beyond the actual loss of income.

3.3 Risk ranked #1: Serious illness

Illness, particularly serious illness, was most often cited as the top risk. Illness can take many forms. It can be chronic, such as diabetes. It can be rare but major, such as appendicitis or stroke. It can be small and frequent, such as the flu or childhood diseases. The financial impact of illness also varies. Generally, illnesses that require hospitalization have the largest impact on a household's budget. Small illnesses can have a major impact on a family if they happen often enough or affect several people in the household at once. The harshest impact on a family comes from a long-term illness that requires multiple hospitalizations. People use their savings to cope with the cost of hospitalization. Although savings are easily accessible, they are usually inadequate to cover the entire expense. *Arisans* are invaluable as sources of lump sums of cash. although sometimes inadequate. Family and friends can provide loans quickly but they are often small and for limited durations. Formal insurance usually provides less than full coverage and is not timely, and low-income people have very limited access to it. Borrowing from banks can be a timely and effective strategy for those who have the collateral to access sufficiently large loans.

The text below will address four topics:

- Impact of serious illness

- Informal coping strategies for serious illness
- Formal insurance mechanisms for coping with serious illness
- Loss management strategies for serious illness

3.3.1 Impact of serious illness

Illness is a stressful event for families because they know that they must take care of it immediately or it will worsen. It is an expense that cannot be postponed. Small and frequent illnesses include flu, stomach problems and fever. People will try to work through these ailments, or they may stay at home and rest until they are better. If they need treatment, they can go to a community clinic, where a visit to the doctor and some medication can cost about IDR60,000 to cure this type of illness.

As people age, they become ill more often and suffer small, frequent illnesses that can take a toll on a household's finances. One woman reported that as her parents grow older, the cost of medical care is increasing, since they need treatment more often for a variety of conditions such as high blood pressure and asthma.

Serious illness is not very frequent but when it strikes, it often requires hospital care. For example, one woman's child had appendicitis and spent a month in the hospital. The cost was IDR18 million. Another woman's son was in the hospital for one week at a cost of IDR1 million. In another village, four people out of 565 were currently in the hospital. The villagers reported that the average cost of hospitalization was IDR15 million to IDR20 million.

Childbirth can also represent a significant medical expense. Delivery by a midwife at home can cost more than IDR1 million. A normal delivery by a doctor with a two-day hospital stay reportedly costs IDR1.5 million, while a delivery requiring a Caesarean section and a more extended hospital stay costs about IDR5 million.

Chronic illnesses can eat away at a household's financial well-being. One woman, a diabetic, needs to have check-ups three times a month, each at a cost of IDR150,000.

The highest risk is that stemming from a serious long-term illness requiring multiple hospitalizations. The story of Mrs. A. in box 2 illustrates the impact.

Box 2. The Impact of Longterm Illness: The Story of Mrs. A.

Mrs. A. is 48 years old and her husband is 59. They have raised five children during their marriage and now have six grandchildren. Four of their children are married, and one son remains at home. Mrs. A.'s husband supported his family by working for a housing construction company as an assistant draftsman. The construction business was not always a reliable source of income due to the inconsistency of projects, but his salary was sufficient to provide a livelihood for his family, although not enough to save for the future.

When Mrs. A.'s husband turned 47, he was forced into retirement due to illness. At the time, he received a one-time payment of IDR1.5 million and three months' salary worth IDR240,000 as compensation. Today, 12 years later, he continues to suffer from heart problems, diabetes and high blood pressure. Mrs. A. has been the sole breadwinner for her family ever since he retired. Most recently, she supports her husband and their youngest son. She has a small shop where she sells items such as rice, cooking oil, soap and toothpaste.

About a year and a half ago, Mrs. A.'s husband fell ill and was admitted to the hospital for six days, which cost IDR3 million. Because the family did not have any savings, she was forced to sell her husband's motorcycle for IDR4.5 million. One month later, her husband fell ill again and had to return to the hospital, this time for eight days. The hospital bill totalled IDR4 million, money that she did not have. Mrs. A. was forced to sell her big portable radio for IDR450,000 and seek assistance from her married children and other relatives.

As a result of the difficulties in paying for these two hospital stays, Mrs. A. did not take him to the hospital the next time he was ill. But her husband usually visits the doctor regularly every 20 days and takes alternative medicines. Her total costs for this medical care are IDR100,000every 20 days. To save money, sometimes Mrs. A.'s husband forgoes the visit to the doctor, and she uses a photocopy of an old prescription to get new medicine for him.

Her husband's medical costs have been a drain on the household budget. In order to meet these expenses, Mrs. A. reduced the capital in her business, and she has had to ask her children and relatives for financial assistance. She gets occasional support from her mosque as her husband and son work for it from time to time.

Nevertheless, Mrs. A.'s shop became smaller. After her husband's second trip to the hospital, Mrs. A. took out a microfinance loan from Diman. She invested most of this IDR500,000 loan in her shop. The balance she used to participate in an *Arisan*. Currently, she participates in four different *Arisans* contributing a total of IDR65,000 per month. This participation gives Mrs. A. access to lump sums of cash in case of an emergency. Mrs. A. has received a total of three microfinance loans. For the most part, she has used the money to invest in her shop and diversify her goods for sale. She has also stopped taking capital out of her business to avoid it becoming even smaller.

Despite the assistance of the microfinance loans, about one year ago, Mrs. A. started to borrow from a moneylender. She borrowed IDR100,000 for 30 days at 20 percent interest. However, once she finished paying the loan back, she immediately took another one of the same amount. She has been doing this for the past 12 months.

Her husband has demanded that she stop borrowing from the moneylender because it is expensive. Their son has recently become engaged. This engagement has already cost her IDR950,000 that she paid for partly from her microfinance loan of IDR200,000 and partly by gifts from her other children. Now the family has to pay for the upcoming wedding. The responsibility for this expense will also fall on Mrs. A., since her engaged son does not have a steady job. She is hoping that her other children and relatives will help her out.

Mrs. A.'s story demonstrates the corrosive impact of long-term illness on a family. As a result of the illness, the family's income was reduced. As medical expenses mounted, the few valuable assets that they owned were sold. Mrs. A. started to de-capitalize her shop but wisely decided to stop that. She was fortunate in that she had access to microfinance loans to help her expand her shop again. Her shop provides a small but consistent income that allows the family to meet their most basic day-to-day needs. When extra expenses come along, however, Mrs. A. is forced to look for assistance from relatives or even to resort to loans from moneylenders.

3.3.2 Informal coping strategies for serious illness

People mitigate the risk of illness in several ways. Only a minority of households have access to formal, employer-provided insurance for health-related costs. Most rely on informal strategies. Households save money as much as they can. Families that can afford to will save in banks, while others save with informal savings collectors or with their prayer groups. Some households in more rural areas reported purchasing livestock that can be used as savings, and many women purchase gold jewellery to keep as savings. Most households that we interviewed participate in at

least one *Arisan*, and many participate in multiple *Arisans.* Below is a closer look at some of these informal strategies for coping with serious illness:

- **Prevention of illness**: Two groups mentioned that they try to keep their houses clean and keep mosquitoes out in order to prevent the spread of dengue fever.

- **Self-insurance and savings**: Some respondents have the ability to save in formal banks, such as BRI and Bank Mandiri. BRI requires a minimum deposit of IDR100,000 to open an account and a balance of IDR50,000 to maintain the account. Some interviewees reported that they could save IDR100,000 per month, some IDR100,000–IDR200,000. Only one woman reported being able to save IDR200,000–IDR300,000. Most women who had bank accounts had their own accounts separate from their husbands'**.** Only a few women reported sharing bank accounts with their spouses.

  Most respondents did not have a bank savings account; some clearly could not afford such an account. Respondents gave many reasons for not saving at a bank, including bank branches being too far away with prohibitive transportation costs and the fact that they would be embarrassed to deposit the small amounts that they have in the bank. They also find the necessary paperwork and the banking hours inconvenient.

  In poorer villages, savings collectors will hold savings for people for a small fee. For example, one woman in the Tangerang area deposits money with a savings collector, who comes and collects IDR2,000 from her every day. The collector then deposits the money in BRI. The saver does not earn interest on her savings, but she has a booklet showing how much she has deposited, and there is no fee for this service. The depositor can access her savings for Eid Al Fitr (Festival of Breaking the Fast) and emergencies only. For convenience, she can withdraw the money by going to the savings collector's house that is near by, at any time. She has IDR148,000 on deposit. This service combines features of mandatory savings with a high level of convenience for the saver. Although the saver earns no interest, she saves money by not having to pay for transportation to the bank or incur the transaction costs of waiting in line. Several other respondents reported participating in other informal savings programmes such as saving with their prayer teacher.

  Some respondents used savings that they had put aside for their children's school fees to meet medical expenses. This is a stressful strategy for these families, as school fees are the second-highest ranked risk for poor families in Indonesia. Such a strategy only postpones the problem.

- **Arisans**: As described earlier, *Arisans* are informal financial systems used by people from virtually all levels of the economy in order to convert small sums of money into large useful sums, or into household goods. Most *Arisans* are cash-based and non-specific. There are a surprisingly large and varied number of *Arisans* in existence in the locations researched. A few *Arisans* are tailored to meet specific financial or household needs. Respondents join these *Arisans* in order to achieve goals, such as purchasing a motorcycle, paying school fees or preparing for religious festivals.

Table 9. Types of Arisan

Type	Description
Cash-based, lottery system	Most cash *Arisans* are arranged on a lottery basis, whereby participants' names are selected randomly to determine who will have their turn to take the payout. Several of these also allow for an auctioning of turns. This means that someone who is not selected, but wants to take a turn now, can offer to take a discount on the amount in the pot, in effect paying a fee for the privilege of taking the turn early. In one group, the price of taking a turn early is IDR20,000. The typical cash *Arisan* requires contributions of IDR10,000 to IDR30,000 every week or every month. Membership varies but an unusually large group would be in the range of 60 to 70 members. Membership is normally around 30 to 40 people.
By Group: Example: Prayer groups	Women reported participating in *Arisans* with their prayer groups. Contributions ranged from IDR5,000 to IDR20,000 per week.
Example: Neighbourhood	All families residing in a particular neighbourhood or RT participate.
By Location: Example: Market- based	Individuals who work in marketplaces participate in *Arisans* organized in the market. These groups tend to be large, 100 members, and contributions are made daily. One group collects IDR1,000 per person per day.
By Purpose: Example: School fees	One respondent reported participating in an *Arisan* for school fees. She contributes IDR2,000 ($0.21) per week and uses the payout for tuition and examination fees.
Commodity-based	Many respondents reported belonging to commodity *Arisans*, where they are able to save up for what would otherwise be large and expensive purchases. The most commonly reported commodity *Arisan* is for food requirements during the Eid Al Fitr festival. The second most common form of commodity Arisan is the one for everyday household items, such as sheets and plates.
For religious holiday: Example: Eid Al Fitr	Participants deposit IDR1,000 per day for one year, and just before Eid Al Fitr, they receive rice, oil, and other food commodities that they need for this religious festival.
Example: Eid Al Aduha	13 participants contribute IDR5,000 per month. They use a lottery system to determine whose turn it will be. There is a drawing two times per year, the winner acquiring a sheep (value about IDR500,000). Under this system, it can take about 6 years to get a sheep, which is then used for the celebration of the Eid Al Aduha (Festival of the Sacrifice).
For household purposes Example: Household goods	Weekly or monthly contributions. Participants receive household goods such as sheets, furniture, dinner plates, or floor mats when it is their turn. For example, one such group has 40 members who contribute IDR1,000 per month.
Example: Motorcycle	There are 30 participants who contribute IDR100,000 per month. When it is someone's turn, they receive a motorcycle.

An interesting feature of *Arisan* participation in Indonesia is that individuals participate in several *Arisans* at one time. Most people that we interviewed participate in at least one *Arisan*, but some individuals participate in as many as seven. On average, people who participate belong to two. Participation in more than one *Arisan* diversifies an individual's financial management strategies. It is important to note that *Arisan* participation also has a significant social aspect to it, which suggests that another reason for participation in more than one *Arisan* is for the purpose of maintaining social ties as much as for the financial benefits. This, in turn, suggests that belonging to a group provides benefits in terms of reciprocal ties. The contributions to *Arisans* can be made

daily, weekly, every two weeks, or monthly, with monthly being the most common frequency cited. The amount of the contribution varies by group. Respondents reported contributing as little as IDR1,000per day up to IDR150,000 per month.

Box 3. The Mosque Social Fund: Variation on an Arisan

In one hamlet, respondents reported that their mosque organized a variation on an Arisan. Members of the group deposit IDR10,000 per month. Of this, IDR4,000 is put into the Arisan pot and the payout is awarded to one person on a lottery basis, as in a normal Arisan. The other IDR6,000 is deposited in a social fund, which is used to allot loans to members of the group at 3 percent interest per month.

While *Arisans* are not designed or tailored to meet specific risks, the importance of participation in an *Arisan* is that it represents a source of emergency lending in times of need. If participants have not yet taken their turn in a cash *Arisan*, they can request to take their turn early in return for paying a small fee or taking a discount on the amount in the pot. This strategy is particularly useful for households coping with serious illness.

- **Saving with assets**: Several respondents reported selling assets to cover large medical expenses. People prepare for emergencies, such as illness, by purchasing assets when they have excess cash. The most popular savings vehicles are gold jewellery and livestock. Gold jewellery is a popular form of savings because it retains its value and can be sold quickly in case of emergency. For that reason, some women reported buying five to ten grams of gold jewellery at a time. For some respondents in rural areas, cows were an even better form of savings because of their versatility; they can give birth to calves, the manure can be used on the fields, and the cows will eat the stubble in the fields after harvest. The use of livestock for savings, in contrast to using gold, depends on the availability of land.

- **Gifts from relatives and children**: Some respondents reported getting help from relatives and children in cases where they do not have enough money to meet medical expenses. For example, one woman's son paid her entire medical bill of IDR20 million from his own business. However, only a few respondents discussed support from children as an intentional self-insurance mechanism. Relatively poorer villagers in the Yogyakarta region reported investing in their children's education and career development, with the expectation that their children will look after them in their old age and when they are ill. This particular group of villagers is engaged in traditional handicrafts with the skills handed down from one generation to the next. The strategy of self-insurance has worked for these people for a very long time, but it is risky now as it depends on the children following tradition and taking on responsibility for the parents. It is not clear that the younger generation will be both willing and able to do this.

- **Bina Swadaya Social Fund**:[26] Respondents who are members of a particular Bina Swadaya microfinance group have a social fund. This group has 60 members, including every family in the village, each member contributing IDR500 per month. The social fund has a balance of IDR400,000. If a family that belongs to the group has a need, the fund will contribute IDR20,000, and members will also make a private contribution. This

[26] Details for Bina Swadaya are provided in appendix 2.

strategy, while well intentioned, will not provide much assistance in helping with the magnitude of medical costs.

3.3.3 Formal insurance mechanims for coping with serious illness

Some respondents were fortunate enough to have access to formal insurance mechanisms through employment or other means. These formal options include the following:

- **Health insurance through a formal-sector job**: Families with a husband or wife working in the formal sector often have access to some type of formal health insurance. There appears to be no standard in terms of the level of coverage provided, however. One respondent reported that her husband's job covered 70 percent of the cost of hospitalization for her family members, while another reported that her husband's job reimbursed 50 percent of the costs of treatment in a private hospital. Others reported that some jobs provided health coverage for the worker only and not the family.

  While health insurance can protect a family from financial ruin in case of a long hospitalization, in the short run, families may be forced to borrow money from wherever they can in order to pay for medical treatment in advance, and then wait for the reimbursement from the insurer later. Access to health insurance through employment is easier for people who live in areas with factory jobs, such as the Tangerang region. Access to factory employment, however, is difficult. Respondents reported that it is difficult to get hired if one is older than 25, and that factories do not want workers over 30 years of age. This suggests that older people, who generally have more health problems, are the least likely to be employed in jobs that would provide health insurance. Rural residents have less access to this kind of work.

- **Letter for discount at puskesmas and government hospitals**: Poorer families can obtain assistance with health care costs from the Government if they meet the criteria of being sufficiently poor. This requires that they apply to the local authorities for a letter.[27] The letter will allow them to get free or discounted medical care at *puskesmas* (local primary health centres) and at government hospitals.

- **Individual health insurance**: Very few respondents reported accessing health insurance at their own expense. One woman reported that she purchased health insurance from AIG/Lippo for herself and her husband, who own and run a repair shop for moulding equipment. Because she is concerned about the possibility of her husband being injured by machinery, she pays IDR350,000 every three months for insurance that covers hospitalization, but not outpatient care, such as visits to the doctor. She also has accident and life insurance for her husband. This woman and her husband employ four workers, for whom they do not have insurance; nevertheless, it is generally the employer's responsibility to take care of workers injured on the job.

[27] The letter is called *Surat Keterangan Tidak Mampu* or "Letter of Acknowledgement of Poverty".

3.3.4 Loss management strategies for serious illness

Most of the respondents find that their risk reduction strategies, whether formal or informal, are insufficient to handle large and sudden expenses for medical care. As a result, when respondents experienced serious illness in their immediate family, they have resorted to loss management strategies. They resort to these strategies after exhausting all of their available risk reduction coping mechanisms.

- **Use of business profits**: The first place that respondents will look for funds to cover medical costs is their current income. If current income is insufficient, microentrepreneurs may start to use the capital in their business, which is a highly stressful strategy, as it reduces the amount of income that they can earn in the future.

- **Borrowing**: When savings are insufficient, poor people will borrow from whatever sources are available. All the microentrepreneurs that we spoke to had access to loans from microfinance institutions. But these institutions typically will not permit loans for the purposes of covering medical expenses. Microfinance loans are restricted for use as working capital for the enterprise, and as a result, microentrepreneurs need to tap into other sources for loans. Although microentrepreneurs may not be able to apply to an MFP for a loan to cover the costs of illness, they may divert some portion of the loan intended for their business to pay their medical expenses.

- **Banks**: Some respondents reported borrowing from banks, such as BRI, Bank of Central Asia or Bank Mandiri. Banks require collateral such as title to a house or to land, or a steady job or certificate of ownership of a motorcycle. Thus, these loans are only available to households with a family member who owns some property or has a formal-sector job. We found that respondents in the rural areas around Yogyakarta were more likely to own land than those in the Tangerang region. The amounts that were available from banks depended on the value of the collateral. Bank loans can be timely in that respondents reported that they could get a loan from BRI in two to three days.

- **Friends and family**: Respondents also reported borrowing from friends and family. Loans from family and friends are typically interest free, but the amounts available are usually limited and also have a short duration. As focus group participants pointed out, the neighbours have their problems, too.

- **Workplace**: Families with one person in a formal-sector job often have access to interest-free loans through the workplace. Many women who have husbands employed in factories report that, in the case of medical expenses, they can borrow from the cooperative at their husband's job. Loan repayments are deducted from the worker's wages. The amounts that can be borrowed depend on the company and/or on the repayment capacity of the family. One woman reported that her family could borrow up to IDR1 million. Another said that she could borrow about IDR1 million but when asked about IDR2 million, she replied that the repayments would be IDR100,000per week, which was too much. In one case, we learned that loan payments are due weekly, although the worker is paid twice a month. This arrangement will cause the family some

hardship as the loan repayments are not coordinated with salary payments. This strategy is only accessible to permanent employees of factories and large companies.

- **Moneylenders**: As a last resort, respondents note that people will borrow from moneylenders. We only encountered one person who privately admitted to us that they borrowed from a moneylender. In general, people report that they are afraid of moneylenders and avoid going to them because they are so expensive. The rates charged by these informal lenders range from 15 to 20 percent per month. Some moneylenders require collateral, others do not. It can depend on the relationship between the client and the lender. Some note that amounts less than IDR2 million can be borrowed without collateral but larger amounts require some kind of guarantee. The advantage of going to a moneylender is that loans are accessible immediately.

- **Pawning assets**: Similar to borrowing from neighbours, some respondents report that people will sell household assets, such as television sets, to their neighbours to raise needed funds. This type of exchange allows for an opportunity for the household to buy back the TV when they have money in the future. Other people pawn household items at government-owned pawnshops, which offer good rates. (Private pawnshops are more like moneylenders. They charge high interest rates.) Pawning is a particularly popular strategy during Ramadan. This is a relatively low-stress strategy.

  But pawning can be a high-stress strategy when individuals resort to pawning farmland, such as paddy fields. Pawning 1,000 square meters of land can raise IDR5 million. In such cases, the family that has pawned their field will end up working as casual labourers for other families, or they will become pedicab (bicycle rickshaw) drivers and, as a result, the family's income will decrease. A variation of pawning fields is called *ijon*, which is the advance sale of crops for a cheap price. In this case, the harvest all belongs to the moneylender, so if the harvest is good, the moneylender reaps all the benefits, but if the harvest is bad the farmer has to reimburse the moneylender in cash. This is a very high-risk strategy, as the family will not only lose their harvest or livelihood, they also may need to find cash at harvest time.

- **Friends and family**: Respondents also reported borrowing from friends and family. Loans from family and friends are typically interest free, but the amounts available are usually limited and also have a short duration. As focus group participants pointed out, the neighbours have their problems, too. Selling assets: Respondents who are unable to borrow or pawn items will start to sell their assets. The first kinds of assets to be sold are those that have been purchased for precautionary reasons, such as livestock, gold jewellery and household electronics. For example, one woman had to pay an IDR1 million hospital bill when her son was sick. First, she sold her TV, then her goats and last of all, she sold 10 grams of gold jewellery. She told us she has nothing left now. Next, people will sell items such as motorcycles, which can be considered productive assets. Lastly, people will sell their land. Respondents in rural areas, particularly in the Yogyakarta region, reported that they could sell land quickly, often to their neighbours, and raise large sums of money, more than if they had pawned the land. This strategy was

reported more often in the Yogyakarta area while use of the Ijon strategy was reported only in the Tangerang area.

3.4 Risk ranked #2: School expenses / education of children

School fees are not ordinarily associated with risk. A risk is defined here as an unexpected, unpredictable event causing a financial loss. School fees are predictable and expected. However, focus group participants insisted on including these costs as a risk. Ordinarily, school fees are not expected to be an insurable event; yet in Indonesia many people purchase endowment insurance to help pay for school costs. Endowment insurance works like a forced investment programme. Payments are made on a regular basis and then payouts are received at a certain point or points, in time. (See below for more details.)

Respondents perceived school fees to be the second most financially burdensome event in their lives. There is insurance for this on the commercial market in Indonesia. For these reasons, school expenses are included as a risk in this analysis. The following section will address key aspects of this risk:

- Impact of school expenses
- Informal coping strategies for school expenses
- Formal insurance mechanisms for coping with school expenses
- Loss management strategies for school expenses

3.4.1 Impact of school expenses

The education of their children was the number one priority of the people interviewed for this research. School expenses were ranked second highest of all the risks facing these low-income families. The pressure to find money to pay school fees affects younger families with children in pre-school up through high school. While a university education is also expensive, we encountered only a few families that are trying to send their children to university. The pressure that families feel is immense. As one respondent put it: In contrast to illness, education "is more expensive and you cannot avoid it. In the case of illness, you can recover. You can't recover from school fees." The impact of school fees also affects the students: "When parents cannot afford school, children cannot concentrate on their studies."

The costs of going to school include registration fees (once a year), tuition (twice a year), examination fees (twice a year), uniforms, and supplies. Parents are also trying to send their children to extra classes for computer or English-language skills, which must be paid for separately. Education is costly whether it is at a government school or a private school. In some locations, respondents reported that private schools are better and that parents who can afford to do so send their children to private school. In other areas, people stated that the government schools are better and more expensive than the private schools. Some families send their children to religious schools. The impact of school costs is most severe in June, due to end-of-year examinations, and in July, due to the costs of registration and tuition for the New Year. In December, school costs are also high due to the start of the second semester.

One woman reported that it costs her IDR1 million a year to send three children to private school. Two are in elementary school, and one is in junior high school. Fees for a different

private school were IDR700,000 for one-time registration, IDR60,000 for uniforms, and IDR20,000 per month for a child in elementary school.

In the Yogyakarta area, it is reported that monthly school fees are:

Primary School	IDR5,000
Junior High School	IDR15,000–IDR25,000
High School	IDR50,000
Extra Classes	IDR5,000–IDR7,500

In addition to monthly fees, there are annual registration fees of IDR60,000 final examination fees of IDR600,000 for senior high school students, examination fees for lower grades (twice a year) of IDR100,000 and book costs of IDR100,000 per year.

3.4.2 Informal coping strategies for school expenses

Focus group participants reported that people would get the money from wherever they could to pay school fees. Several groups voted this risk the most financially burdensome of all the risks facing their household.

- **Self-insurance and savings**: Parents try to save in order to have the funds for school fees. Parents who have difficulty saving will pay tuition in advance, by paying in instalments to the teacher.

- **Arisans**: If possible, respondents will use their turn in the *Arisan* to pay school fees.

- **Saving with assets**: People save for educational expenses by buying cows.

3.4.3 Formal insurance mechanisms for coping with school expenses

- **Education endowment insurance**: Several women had insurance to assist them in paying school fees. In this way, consistent premium payments yield benefits at all major educational milestones, and will cover the full benefit upon the death of the policyholder. Three examples of how these work are included in table 10. Each of the policies pays pre-determined benefits at the end of a covered student's completion of each level: kindergarten, elementary school, junior high school, and high school.

Table 10. Examples of Education Insurance

	Policy Value (IDR)	Term	Premium Amount per month (IDR)	Payout Schedule: When	Amount (IDR)
1	10,000,000	15 years	129,000	After kindergarten After elementary school After junior high school After high school	500,000 1,000,000 1,500,000 5,000,000 plus all premiums paid.

	Policy Value (IDR)	Term	Premium Amount per month (IDR)	Payout Schedule: When	Amount (IDR)
2	20,000,000	Unknown	100,000 per child (for 2 children)	After kindergarten After elementary school After junior high school After high school	2,000,000 Unknown Unknown Unknown
3	2,000,000	12 years	21,000	After kindergarten After elementary school After junior high school After high school	200,000 (10%) 400,000 (20%) 600,000 (30%) Unknown

These education endowment insurance policies were purchased from Bumiputera. In addition to providing payouts to families at milestones in a child's educational career, these insurance policies cover the child in case of accident (reimbursing 50 percent of hospitalization) and cover the breadwinner in the family in case of death. If the breadwinner dies, the family no longer has to pay the premiums of the education policy, and the family will still receive the scheduled payouts.

Affordability of the premiums is an issue for some women. One woman reported having dropped out of an education insurance policy because she could no longer afford the premiums. In one case, the insurance salesman provided a woman policyholder with a piggy bank. Only the salesman has the key for the bank. The woman deposits IDR1,500 every day. In this way, the premiums, which are collected once every three months, are not a burden for her. The coverage of educational insurance is not complete. Another woman reported that her son needed IDR1,000,000 to start high school. The payout from her insurance policy was only IDR600,000. She had to use IDR400,000 from her savings to cover the rest.

3.4.4 Loss management strategies for school expenses

- **Enterprise proceeds**: Parents use the income from their businesses as the first source of funds for school fees.

- **Borrowing**: Respondents noted that microfinance loans are for working capital purposes. Also, some reported that they could borrow from the Bina Swadaya programme to have enough money to send their children to school. Usually Bina Swadaya loans are to be used for productive purposes, such as investment in a business activity.

- **Friends and family**: Respondents would borrow from family and friends if necessary.

- **Workplace**: Women respondents noted that they could borrow from their husband's workplace to pay for school fees. One example given was that of a loan from a husband's office co-op. The loan was for IDR1.5 million, which was repaid over 15 months. The payments were deducted from his salary. This example is ill suited to paying school fees as school runs on a 12-month cycle and the loan lasted for 15 months.

- **Selling assets**: If families have insufficient cash or savings on hand to pay school fees, they will sell their livestock and household assets such as TV sets and jewellery.

3.5 Risk ranked #3: Loss of harvest or poor harvest

Agricultural activities can be risky, with few coping mechanisms to mitigate the risk. Farm households, however, diversify their income by growing different crops, by investing in livestock and by pursuing off-farm enterprises.

3.5.1 Impact of poor harvest

Poor harvest was identified as a risk in both the Tangerang and Yogyakarta regions. Pests, such as insects and mice, can lead to harvest losses, while drought can reduce crop yields. The impact falls hardest on households that rely on the harvest for both their income and food. For these families, the majority of their income is earned in two or at most three months of the year, corresponding with the harvests. If the harvest is not good, they will earn little or nothing. Farmers can show a loss if the costs incurred for inputs such as fertilizer and pesticides are more than the income they make from the harvest. These households will have to cope on little money until the next harvest.

The impact of poor harvests goes beyond the farm household. With reduced supplies of rice, the price of rice will increase. All other households will have higher daily food expenses. Microentrepreneurs will not only have higher grocery costs but will also have lower income as other households cut back on non-food expenditures to cope with higher rice costs. Additionally, they may not be paid for goods that they already sold on credit, as people have less income.

3.5.2 Coping strategies for poor harvest

While we did not learn of any formal or informal insurance schemes for agricultural activities, there are a few coping strategies for poor harvests:

- **Diversification of income sources**: The household of one sharecropper is obliged to rely only on her husband's income from formal employment when her harvest fails. Under the local share-cropping system, she works someone else's land and in return, she can keep one bag out of every five that she harvests. We did not find any participants whose households were involved solely in agricultural activities. This suggests that income diversification is a widespread risk-reducing strategy.

3.5.3 Loss management strategies

- **Reduced consumption**: Farm households will cut back on their consumption in order to make ends meet. They will reduce the number of meals that they eat from four per day to one or two only.

3.6 Risk ranked #4: Death of a relative

The death of a relative was ranked as a lower risk than serious illness in terms of the financial pressure posed by life cycle events. This is because death in the family occurs less frequently than illness (or school expenditures) and because the costs of illness can be wider ranging and more unpredictable than the costs of a funeral and memorial services.

For Muslim households in Indonesia, funeral expenses may not be met by borrowing with interest. Borrowing from friends, relatives and neighbours can be timely and accessible but it does not cover the full costs of these expenses. Savings are also timely and accessible but often are insufficient on their own to cover the costs of funerals. Families find they must patch together funds from various sources to meet these unexpected expenses.

Research did not come across any examples where the breadwinner of the family had died. However, it is clear that in such cases, the impact of the death lasts much longer than through the 1,000th-day ceremony. In the Tangerang region, respondents noted that if a breadwinner dies, it means the loss of at least IDR200,000 a month in income. In this situation, the children will have to stop going to school as there will not be enough money to pay for the school fees. Thus, the impact will continue into the next generation.

The section below will address four topics:

- Impact of the death of a relative
- Informal coping strategies for death of a relative
- Formal insurance mechanisms for coping with death of a relative
- Loss management strategies for death of a relative

3.6.1 Impact of the death of a relative

The economic impact of a death in the immediate family or household can be significant. In addition to the pain and emotional suffering the family goes through, the costs of the funeral and memorial services are substantial. The traditional funeral ceremonies in Java include the funeral, a 7-day memorial ceremony held at the house, and ceremonies on the 40th day, 100th day, 1 year, and 1,000th day after the death.

The costs involved in the funeral itself include the cost of the coffin, obtaining the death certificate, and purchase of the grave plot. These costs are reported to be in the range of IDR500,000 (not including the grave plot) up to IDR2.5 million. The 7-day ceremony involves entertaining large numbers of people in the family home for 7 nights after the death, having prayers said by the mullah at the house, and having Tahlilan, or night prayers, said. The cost of entertaining and feeding up to 150 people can be IDR300,000 per day. Others report the total cost of the 7-day ceremony to be IDR3.5 million. Tahlilan can cost from IDR10,000 per person per day (about 10 people for 14 days) to IDR4 million–IDR5 million. The 40th-day ceremony costs about IDR1 million, and about 50 people would attend. The 100th-day ceremony is the largest of all the memorials with more guests than the 40th-day event. The cost can range from IDR1 million–IDR2 million depending on the kind of food served. One respondent noted that the death of a parent usually costs between IDR10 million and IDR20 million altogether.

3.6.2 Informal coping strategies for death of relative

As in the case of illness, families frequently turn to family resources in an attempt to "self-insure." Some of these strategies are examined below.

- **Reduced expenditures**: The interviewees noted that people could manage the costs of a funeral in a number of ways. Poorer people will hold the 7-day ceremony but will not have the other memorials. The cost of prayers will be more or less depending on who

does them. One of the interesting points about coping with the costs of a death is that respondents across the board mentioned that it is not possible to borrow at interest to pay for a funeral. This was not true for any other risk event and is only true for Muslim households. The inability to borrow with interest puts extra pressure on a family that does not have sufficient funds to pay for all the funeral costs at once. This is important to note because funeral costs are immediate; they cannot be put off to a later date.

- **Savings**: Respondents said they would use savings if they had them. Some respondents noted that generally savings would not be enough to cover the entire costs of a funeral, while others suggested that most of these costs would be paid for out of savings.

- **Gifts from relatives and neighbours**: In the case of death and a funeral, people will receive gifts from their relatives, friends, and neighbours.

- **Informal insurance mechanisms**: Bereaved families will receive donations from their community.

3.6.3 Formal insurance mechanisms for coping with the death of a relative

- **Life insurance**: Very few respondents had access to formal life insurance. Two respondents noted that their families had purchased life insurance because they were worried about what would happen should the breadwinner have an accident or die. The first couple has insurance through AIG/Lippo, costing IDR150,000 per month, paid monthly. The exact amount of coverage is unknown but it covers accidents as well as death. The second couple has life insurance for the husband through Bumiputera. It is an IDR50 million (policy and costs IDR560,000 every six months or IDR93,333 per month.

3.6.4 Loss management strategies for death of a relative

- **Banks***:* People will not borrow from a bank in order to pay for a funeral as they are prohibited from paying interest on a loan for these expenses.

- **Family and friends**: Loans from family, friends, and neighbours in case of a death will be interest free. In such cases, wealthier neighbours will lend money with flexible terms. If borrowers cannot pay back these loans all at once, they will pay in instalments.

- **Community funds***:* In addition to donations, some village families can borrow from community funds at no interest.

- **Moneylenders**: Respondents will not borrow from moneylenders to pay for funeral expenditures.

- **Pawning assets**: Families will try to sell their assets to friends and neighbours first to raise money for a funeral. Later, they will save in order to buy back their things.

- **Selling assets**: Selling assets is not a timely strategy in times of death. Respondents would have to borrow the needed funds first from family and friends. Then after the funeral and 7-day ceremony are over, they will sell their assets to pay off the loans. Respondents noted that people would sell their livestock, property, or land if necessary.

- **Taking a second job**: Families who have used up their other coping mechanisms and have gone into debt to pay for a funeral will take on other jobs to earn enough income to pay back their creditors. Focus group participants reported that people would drive motor cabs or work as *kuli* (casual) labour to earn this extra income.

3.7 Risk ranked #5: Accidents

The impact of accidents can be substantial, with monetary costs rivalling those of serious illness, because accidents often require hospitalization too. The incidence of accidents is rare. The types of accidents identified by the research include vehicular and industrial accidents. Industrial accidents can include accidents in large, multinational factories and accidents in small home-based industries. Home-based industries are not necessarily small artisanal operations, they also include industrial operations, such as fabrication of mechanical parts, offset printing, etc.; activities that require heavy machinery and chemicals, operations that pose hazards to the workers and the families that have these businesses attached to their houses.

Respondents stated that factory accidents whether in large or small operations are rare, but can be very significant. An example was given of a neighbour who had both hands cut off in a factory and could no longer work. The factory did not pay very much compensation to this person. Another woman who has a home industry said that potential accidents are a source of worry for her because she would be responsible for her workers if they were injured. That said, however, she had not purchased insurance for them.

One focus group participant that we met had hit a bicycle with his truck. The bicycle had three people on it. One was seriously injured and required one month in the hospital to recover. The other two were less seriously injured. The total cost came to IDR8 million, which the man was required to pay very quickly.

3.7.1 Coping strategies for accidents

- **Self-insurance**: In the case of a big vehicular accident such as the truck accident, self-insurance mechanisms are inadequate in terms of the coverage required.

- **Informal insurance**: No informal insurance mechanisms appear to cover accidents.

- **Formal insurance**: All drivers are required to renew their license every year. At that time, they pay a tax and the premium for insurance from Jasa Rahardja, a government-owned insurer.[28] This insurance will provide a maximum of IDR10 million in case of death due to a vehicular accident. The mandatory car insurance paid out IDR2.5 million,

[28] Participants referred to this insurance as Travellers Insurance.

or less than one third of the total costs of the accident, in the truck example above. While the insurance payout helped, the coverage was insufficient to allow the man to avoid more stressful coping strategies.

3.7.2 Loss management strategies for accidents

The truck driver could not negotiate the hospital bill and was required to settle it quickly. As a result, he had to sell his house to raise the remaining IDR5.5 million. He was fortunate in that his brother was willing and able to purchase the house at short notice, which leaves open the option of regaining the house in the future. He was also fortunate in that he owned a second house that he could move into right away.

There are little or no self-insurance strategies that can provide sufficient coverage in the case of a serious accident. Informal insurance is not available. The formal, mandatory government insurance is helpful, but provided less than one-third the necessary coverage in the example cited. In cases of accidents, people are forced to fall back on more stressful loss management strategies, such as selling valuable assets.

3.8 Analysis of risk management strategies

3.8.1 Self-insurance

Savings: Low-income groups in Indonesia have a variety of mechanisms by which they can save cash. Unfortunately, at this time they are not able to save cash with their microfinance institutions because under current regulations these institutions are not allowed to mobilize savings. Saving with MFPs would be safer and more profitable for microfinance clients than some of their other options, such as entrusting their savings with savings collectors. Cash savings as a self-insurance is a timely and accessible strategy. Since low-income groups have difficulty saving, the coverage of household savings is inadequate to cope with most risks.

Arisans: *Arisans* are an effective self-insurance mechanism because they force people to save and they can provide greater coverage in times of need, providing access to large lump sums of cash. Timing can be a problem if the person in need cannot wait their turn to get the cash. *Arisans* appear to be accessible to anyone but membership depends on acceptance by other group members. *Arisans* provide a network of relationships that people can use in case of need.

Saving with assets: Saving with assets such as livestock, jewellery and, in some cases, land, is a very popular self-insurance strategy. The coverage provided by asset-based savings depends on the size of the asset. This strategy is accessible to all households, depending on how much money they are able to save. The disadvantage of assets used as self-insurance is timeliness; the larger the asset, the more difficult it is to sell. Fire sales of assets can lead to a loss of value for the seller. In many cases, people will first borrow to pay for the emergency and then sell their asset, to ensure that they are paid the full value of the asset. Saving with livestock can be risky, as animals can sicken and die. Some focus group participants had been badly impacted by the epidemic of avian flu in recent years.

Gifts from family, friends, and the community: Gifts from family, friends, and the community can be a timely and accessible strategy in the face of an emergency. But generally the coverage from gifts is low.

3.8.2 Informal insurance mechanisms

Assistance from the Pasantren (Muslim Educational Institution): Assistance from the Pasantren depends on the community, and the coverage of assistance from this group is low.

Bina Swadaya Social Fund: There was only one instance in which the social fund was mentioned by a focus group, although this is a regular feature of the Bina Swadaya programme. The coverage of assistance from the social fund is very low and is only accessible to families who participate in the Bina Swadaya programme.

Community funds: Community assistance is forthcoming for particular risks, such as the death of a relative. Coverage is usually low, and accessibility depends on residence within a certain area.

3.8.3 Loss management strategies

Use of business proceeds: The first line of defence in times of financial crisis is current income from a microenterprise or a salary. The accessibility and timeliness of this strategy are excellent, but the coverage is very poor. The costs of the most significant risks far outweigh the monthly or weekly incomes of low-income people.

Borrowing from banks: Bank loans can be an effective strategy for families that are able to access them. Collateral, such as land, house, motorcycle ownership, or proof of a steady job, is necessary to access bank loans. These loans can be timely, and large amounts may be borrowed depending on the collateral. Thus, for the less poor, this is an effective strategy for managing a crisis. Bank loans do come with their own built-in risk. We came across two examples of people who had lost their homes to a bank because they could not repay their loans. The loans were not taken out for emergencies.

Friends and family: Loans from family, friends, and neighbours can be a timely and accessible strategy in the face of an emergency. Generally the coverage of these loans is low, however.

Borrowing from the workplace: Loans from the workplace are another effective strategy. Amounts up to IDR1,000,000 can be easily obtained, and larger amounts are possible. These loans are timely but they are accessible only to permanent employees of the company issuing the loan. In some cases, a co-op organized at the company issues the loans.

Moneylenders: Loans from moneylenders are the last resort for coping with a crisis. These loans are timely and are accessible to anyone willing to pay the high cost. The coverage is also good, with large amounts available if the borrower has collateral.

Pawning of assets: Pawning assets is a variation on the theme of selling assets. This strategy can provide good coverage, in that a large amount of cash can be mobilized, but it is risky if the *ijon* system is used. Farmers can lose their right to the harvest and also still end up owing money to the lender at harvest time, if the harvest is not sufficient. Timeliness can be an issue, and the *ijon* strategy is only accessible to those who own land.

Sale of assets: The coverage provided by sale of an asset depends on the value of the asset. As shown above, in cases of large expenses, people can sell their houses. If this is not possible, they will sell several smaller assets. The timeliness of asset sales is not good. Normally, the larger the asset, the longer it will take to sell, therefore this strategy must often be used in combination with another strategy to overcome the problem of the time factor. Accessibility depends on the household's ability to accumulate valuable assets.

3.9 Formal insurance mechanisms

Formal health insurance through the workplace: Employer-provided health insurance could protect families from the devastating impacts of a serious illness. This insurance is accessible only to people who work in a formal-sector job. The coverage of this kind of insurance varies considerably from employer to employer. Some policies cover entire families, others cover only the employed person. While some policies provide a high level of reimbursement of medical expenses, others provide 50 percent. The timeliness of health insurance can be difficult for poor families because they must pay the full cost of the medical care and then wait to be reimbursed. This leads to the need to combine this strategy with another, such as borrowing.

Individual health insurance: Individual health insurance policies are accessible to those who are able to pay the premiums and who are accepted by the insurance company based on their medical examination. We do not have any information about the timeliness or coverage of this strategy.

Individual education endowment insurance: Endowment insurance for educational expenses is accessible to households that are able to pay the premiums. The timeliness of this policy is good, with funds becoming available in time for the student to begin a new level of schooling. A drawback is that the coverage may not be adequate to cover the total cost of education, and as a result, parents may need to combine this strategy with other forms of self-insurance. (See table 11 below for examples of education policies.)

Individual life/accident insurance: This insurance is accessible to households who can afford the premiums. The timeliness of claims payments is unknown. Based on the example shown in the table below, the coverage is adequate to pay for funeral costs; however, not counting funeral costs, the policy would provide an income equivalent to 16 months of the household's reported income. This might prove inadequate for a young family if the breadwinner died. (See table 11 below for example of life insurance policy.)

Letter for discount at puskesmas and government hospitals: The coverage provided by this letter is limited to government clinics and hospitals. The coverage was variously reported as

50 percent or 100 percent of total costs. Timeliness is not an issue because the insurance works by discounting the price actually charged to the patient. Accessibility is very limited and depends on meeting the criteria of being poor enough.

Car/motorcycle insurance: This insurance is mandatory for all drivers. As shown in the example above, the coverage proved to be inadequate for the truck driver who injured the cyclists. The coverage covers accidents, not theft, and the timeliness of payments is unclear.

Retirement insurance: This insurance is accessible to households that can pay the premium. It generally is a 15-year policy with payout at the end of that time. The amount of the policy in the example below would suggest that the coverage would be inadequate to provide for early retirement.

Table 11. Examples of Insurance Products Purchased by Low-income Families

Insurance Policy	What Is covered	Premiums	Claims Process	Impact
Life Insurance (from Bumiputera)	Death and accident. Policy covers husband only. IDR50 million policy.	IDR560,000 per 6 months. Opened policy in 2002. They will pay premiums for 15 years.	They have not submitted a claim yet.	When their income is low, they have to pay insurance by advance instalments (i.e., monthly payments) in order to meet the quarterly and semi-annual payments. They have never been late with a premium. This is a particular problem for them since they have 5 separate insurance policies.
Satisfaction with Services	Premiums are collected at their home by salesman from Bumiputera. They are satisfied with this arrangement.			
Areas of Dissatisfaction	The wife still is unclear about some of the details of this policy.			
Old-Age Insurance (from Bumiputera)	Retirement. Policy is for IDR35 million. Covers the husband only.	Premiums to be paid for 14 years. IDR300,000 per 3 months. They started this policy 5 years ago.	There has been no payout yet as her husband is not of retirement age.	
Satisfaction with Services	Premiums are collected at their home by salesman from Bumiputera. They are satisfied with this arrangement. They feel that they have a good understanding of this product.			
Areas of Dissatisfaction	Wife reports that when she does not have enough money, she prefers to pay IDR100,000 ($10.73) monthly rather than IDR300,000 every 3 months. She calls Bumiputera, and a salesperson will come and pick up the payment. She also would prefer not to pay all the premiums on all the insurance policies at once.			

Table 11 (continued)

Insurance Policy	What Is covered	Premiums	Claims Process	Impact
Education (1) from Bumiputera This was the first policy that they bought.	Policy covers oldest child. IDR7 million policy. This is an endowment policy.	IDR153,000 per 3 months. They started this policy 5 years ago.	When child graduated from pre-school, they received IDR500,000. That was 2 years ago.	
Satisfaction with Services	Premiums are collected at their home by salesman from Bumiputera. They are satisfied with this product and purchased additional coverage as a result.			
Areas of Dissatisfaction	None			
Education (2) from Bumiputera	Policy covers second child. IDR10 million policy. This is an endowment policy.	IDR450,000 per 3 months. They started this policy 2 years ago.		
Satisfaction with Services	Premiums are collected at their home by salesman from Bumiputera. They are satisfied with this product and purchased additional coverage as a result.			
Areas of Dissatisfaction	None			
Education (3) from Bumiputera	Policy covers oldest child. To cover university expenses. Policy is worth IDR7 million. This is a 7-year endowment policy.	IDR139,000 per 3 months.	The claim will be made when the child is ready for university.	
Satisfaction with Services				
Areas of Dissatisfaction				

CHAPTER IV: DEMAND, CHALLENGES AND OPPORTUNITIES

4.1 Types of products in demand

Education endowment: The overwhelming interest among the focus group participants that we interviewed was for endowment insurance, particularly education insurance, and to a lesser extent old-age insurance. Families with children below 18 years of age would be primarily interested in education insurance for their children. As we mentioned above, the number one priority for families with school-age children was the education of their children. As one group put it, "Health is uncertain and should not be worried about too much but education is mandatory." Respondents holding education policies reported starting them when their children were as young as 2 years old. Typically, these policies would continue until the child left high school. The market for education insurance would include all families with children from newborns up to 18 years old. Roughly speaking, these would be families with parents between 18 years old and 40–45 years old. Research found only one example of an insurance policy to save for the cost of a university and we met only a few parents who were sending their children to a university. This may be a microinsurance market in the future.

Retirement endowment: Some respondents whose children had grown up were already participating in or interested in retirement insurance. This is another form of endowment policy that assists an individual to save for old age. The low-income market is not likely to be able to afford several insurance products at once. Assuming that families place the top priority on the education of their children, the demand for retirement insurance will come from families in which the children are already out of school. In general, the parents or policyholders would be expected to be 40 years old and above. The need for retirement insurance will be strongest among microentrepreneurs working in the informal sector, and more so for households in which neither spouse works in the formal sector. These households have no access either to government social insurance or to company retirement plans.

Health insurance: As already demonstrated, serious illness is by far the most significant risk facing low-income households. Long-term serious illness has the potential to reduce families to absolute poverty by whittling away their assets. The costs of hospitalization are such that no low-income families can cope by using self-insurance alone. Health insurance that covers the cost of hospitalization would help households avoid the necessity to use the most stressful loss management techniques, such as selling assets, like their house or rice fields, or borrowing from moneylenders. The market for health insurance may not be as strong as that for education insurance. Households that have experienced a health crisis understand how expensive and stressful it is. Those who have not experienced this kind of crisis are more concerned about day-to-day financial pressures. Furthermore, they perceive serious health problems to be rare events.

Life and accident insurance: The demand for life insurance is unclear. The cultural perception of life insurance, given local superstitions, is a barrier to acceptance of this product in

low-income communities. While funeral expenses can be high, they can also be managed. Families receive help and assistance from friends, family, and the community. Therefore, we do not see a demand for a microinsurance product that covers funeral expenses alone. The more significant risk for low-income families is the death of a breadwinner. Life microinsurance that provides a benefit for surviving family members, rather than just enough to cover funeral expenses, would be more valuable for households and possibly higher in demand.

It seems that the few people who are purchasing life insurance on an individual basis are better educated than many of their neighbours. The willingness to purchase life insurance seems less a question of affordability for them than a question of attitude. They seem to have a clearer idea of the risks they face in their life and the implications of those risks for their family. For example, Mr. G. said that he has to drive long distances for his business, which causes him to fear the possibility of having an accident and being killed. He worries what will happen to his family. This has led him to purchase a life insurance policy for himself. Mrs. O. and her husband have a home industry with dangerous equipment, and she worries what will happen to her husband if he is injured by the machinery, so she purchased an accident and life insurance policy for him. These stories suggest that marketing campaigns for life microinsurance that focus on the impact of risks on the surviving family members might be successful with this particular market segment.

The market of low-income people who live in rural areas can be divided into those who own land and those who do not. Those with land can use it as collateral for bank loans in times of crisis, opposed to those without land who have to rely on patching together a variety of strategies to obtain sufficient cash to deal with their emergency. Those with land are also better able to keep larger livestock, which serve as a form of savings. Those with little or no land can keep chickens, ducks, and goats, which are less valuable.

4.2 Affordability

The low-income market's willingness to pay can be assessed in two ways. The first is by asking people what they would be willing to pay. In order to do this, one needs to present a product prototype for them to respond to. In the absence of a prototype, one can only ascertain the maximum amount that people would be willing to pay in general. One cannot be certain whether people would be willing to pay that amount for a specific microinsurance product.

The focus group participants stated that they could afford to spend from IDR10,000–50,000 per month. One respondent who is familiar with insurance suggested that his neighbours, who were less well off than he, could afford insurance if they earned IDR20,000–25,000 per day.

Another way to look at the affordability of insurance is to look at the amounts that are currently being invested in *Arisans*. Assuming that people would be willing to shift *Arisan* contributions (which are effectively a form of savings) to insurance premium payments, we can see that low-income groups such as those who participate in microfinance programmes can afford somewhere between IDR20,000 and IDR100,000 per month.

The question of affordability is also a question of billing and payment methods. The practice of existing commercial insurance companies is to collect premium payments from the homes of the customers, every three months. All the current customers that we spoke with expressed satisfaction with the collection of premiums from their home. This reduces the transaction costs for the policyholder. One respondent, who is no longer a policyholder, was not satisfied with at-home collections because she has a stall in the marketplace. The concern that she would miss the salesman and not make her payment was a great source of stress for her and one of her reported reasons for dropping the insurance policy. We believe that she also found the premiums expensive.

Payments every three months are a hardship for some customers. The poor have urgent demands on their cash every day. For most, payment of insurance premiums would be easier if they were broken down into smaller instalments such as monthly payments. One woman, previously mentioned, has managed this problem with the help of her insurance salesman by using a piggy bank into which she deposits a small amount each day (IDR1,500). At the end of three months, she has sufficient savings to pay her premium. For families that depend more on agriculture for their livelihood, payments every four months or even every six months might be more suitable because they have high levels of income two or three times a year corresponding with the harvests.

4.3 Role in reducing vulnerability and supporting entrepreneurs

Microinsurance in terms of reducing vulnerability needs to be looked at on three levels: credit-related, general, and long-term products.

4.3.1 Credit-related products

Credit-related products are those that simply repay an outstanding loan on the death or sometimes the disability of the borrower. These products provide little or no additional benefit to the deceased's family. In some cases, the policy will pay the total borrowed amount of the loan, and the balance of the coverage goes to the family. However, this is not reliable since the benefit is different after each loan payment. Many MFPs and banks require such a policy on borrowing.

'Policyholders' in Indonesia and almost everywhere else that these products are "offered" believe these simply protect the institution, and many see the premiums as a way for the bank or MFP to get more fees from them. Although insurance companies like these policies, this could be done more simply by the lenders increasing their reserves somewhat and setting up a separate "Reserve for possible death or disability," treating this just as they treat the "Reserve for possible loan losses." This product has little impact in reducing vulnerability since usually lenders will not aggressively collect from the remaining family for microfinance-type loans.

4.3.2 General insurance

General insurance can have a major impact on vulnerability, especially regarding health insurance. Health and poverty are integrally linked. If low-income people can obtain health insurance that is a direct pay system from insurer to provider, this can have a major impact on poverty. One paper noted that of the low and middle income people admitted to one hospital in

Indonesia, 25 per cent left in a position where they were now economically under the poverty line. To have health microinsurance would have had a major impact on these people.

Other studies from South Africa and Uganda show clearly that the low-income insured will use health facilities significantly earlier in the disease cycle. This means less time away from work, less expensive care and treatment, and a healthier family overall.

General insurance can also help mitigate the loss of livestock, although this insurance is difficult to manage. Such policies can reduce the impact of major losses from fire, or other disasters. In Banda Aceh, the international insurers paid claims soon after the tsunami, and their policyholders were able to start to rebuild their lives and livelihoods. Policyholders of other insurers, still waiting for claims payments, were still living in refugee camps.

4.3.3 Long-term insurance

Long-term cover allows people to plan better and to smooth their income more evenly. Education life policies where policyholders contribute regularly over time to cover major expenses of education are in great demand in Indonesia. As long as the payments are maintained a life cover will come into effect on the death of the policyholder, covering the continuing, contracted expenses of the child's education. Holders of such policies note that otherwise they would not be able to maintain their child in school.

Long-term insurance linked with savings can also help people manage life cycle events, such a wedding, and old age/retirement. People believe that their children will take care of them in old age, but this is increasingly becoming a fallacy throughout the developing world, and especially in urban areas where life may be most difficult.

Long-term life insurance can also have a major impact on surviving widows if the policy is designed properly. A widow is responsible for the costs of the funeral, which are manageable, but then also cover the costs of the various memorial services. For these she may receive assistance from family and friends. But she also has to continue maintaining the household, which may include several children. What life insurance can do for her is to provide a lump-sum payment at death, and then provide for basic necessities for one to two years afterwards. This not only helps with the immediate needs after death, but also helps the family maintain a reasonable standard of living while things are put in order.

Low-income people can and do significantly benefit from the income-smoothing opportunities that come with microinsurance. These products complete the financial products toolkits that people need. Too many bank and MFP clients improve their lives and then fall back into deep poverty because there was no safety net for them. Providing access to insurance provides that safety net and helps people secure the gains they make with other financial products.

4.4 Problems, obstacles and opportunities

Analysis of the research identifed cultural and social barriers that hinder the widespread adoption and use of microinsurance and risk reduction measures.

4.4.1 Insurance understanding

The knowledge of insurance in the community varies quite widely, but is generally poor. Many people we interviewed had heard of insurance but the majority of them could not explain how it works. A minority of respondents were policyholders who participated in endowment insurance for education or retirement, or who purchased life and/or accident insurance. All respondents who owned motorcycles or cars (again a minority) were covered by mandatory insurance (referred to as "travellers insurance") that is purchased annually when the vehicle registration is renewed. Respondents also had a low level of understanding of Jamsostek, the Government's social insurance programme offered to formal-sector workers, despite the fact that several respondents had immediate family workers who participate in this insurance. This raises the question: How well do formal-sector workers understand the state insurance programme that they are participating in? It also reinforces the belief that too little is being done to educate people about insurance and its benefits.

Discussions with interviewees suggest that there is confusion about the distinction between an insurance policy that pays out based on the occurrence of a specific risky event, such as an accident or death, and an endowment policy that is basically an investment programme. Since endowment insurance for education is very popular and has been marketed in some low-income communities, there is an expectation that all insurance results in a certain and defined payout. This is not necessarily the case for accident or life insurance. This confusion has led to some disappointment for people who purchased insurance with unrealistic expectations of what the return would be.

On a number of occasions, respondents noted that insurance is not available where they live and that insurance companies need to undertake marketing in their village. As one woman said about insurance: "We are still in the dark about it."

4.4.2 The perception of insurance

In a few locations, the perceptions of one insurance company, Jiwasraya, and by association, insurance in general, were bad. Respondents stated that they were distrustful of Jiwasraya because company personnel had committed fraud. Unsuspecting customers had purchased policies and paid premiums to a salesperson. When they had a claim, they contacted the main office and discovered that there was no record of their policy. Additionally, focus group participants claimed that the company did not inform the public very well about the product, i.e., what it was for, what was covered and how much it cost. People who had purchased Jiwasraya products said that the procedures were too complicated, that it was not easy to make a claim and get money back. One woman's father had a policy through this company and the family felt cheated. Some respondents noted that it is easier to save money and then withdraw it when it is needed. The stories about Jiwasraya's fraud have led to a deep distrust of this company and of insurance salespeople in the Yogyakarta region. Efforts to market microinsurance in this area will have to overcome such distrust.

There was a general sense in the focus groups that people prefer to save or invest their money in such a way that they can be certain that they are able to access it later. These groups did not accept the idea of paying into a policy and not necessarily receiving anything in return. This

suggests that endowment insurance will be in greater demand than health, accident, or life insurance.

The perception among the majority of the respondents is that they cannot afford insurance. This, however, was combined with a low level of knowledge about insurance and its costs. Respondents were open to the idea of insurance, however, and said that the insurance companies needed to market in their areas and provide more information about the products.

There is a widespread perception in low-income communities that it is not good to talk about bad things such as death. Ganesha Microfinance had offered a microinsurance product to its clients for a brief time. This product was designed to provide a benefit in case of illness or death. It was discontinued due to regulatory issues. Some Ganesha clients informed us that the product was not popular because people did not understand it. The clients who reported this said that they had understood the product and those who did, liked the product. But the majority of clients thought that by offering such a product, Ganesha was encouraging them to fall ill and die. The perception was that the MFP was wishing them bad luck. Efforts to market life insurance will need to be undertaken sensitively and take into account such superstitions.

Personal service: In Bali, people have come to expect personal service even if that means that an insurer must send an agent on horseback to accommodate them. For microinsurance to be successful, it must be efficient. These different requirements are likely to clash in Bali.

4.4.3 Institutional barriers to the integration of microinsurance and risk management

The insurance regulations require initial capital for life insurers of IDR100 billion and for non-life, IDR200 billion. This is certainly a barrier to new microinsurance companies, although such new institutions are not appropriate at this time in Indonesia.

The law also only allows the State to sell and manage the compulsory Road Traffic Act cover that is essentially third-party motor insurance. The fixed-price premiums are set by Parliament and are paid through vehicle taxes, and the Government holds the risk. This restricts a potentially lucrative business line to the State. Although this does not impact microinsurance directly, if insurers were to take on this business in a profitable manner, the income would go to strengthening the insurer.

There is no agents' association and thus no mechanism for them to be self-policing. This creates problems because agents (80,000 for life and 5,000 for non-life) are the front-line people selling this intangible product to people with limited or no knowledge. This can lead to the high non-renewal rates that we see in other countries with poor microinsurance marketing. This is expensive for insurers and could result in significant increases in premium costs for microinsurance products, especially given a commission system.[29]

It is possible that the Sharia Council could present a barrier given the entry requirements for selling Sharia Insurance–approval by Council, and a three-person Sharia body sitting in the institution. Sharia-based insurance will be important to the significant growth of microinsurance.

[29] Allianz, for example, works through a commission system, with agents receiving 90 percent of the premium in the first year.

The Council acts as the gatekeeper to this market, and such a role often creates inefficiencies and additional costs to entry.

There are public administration issues that complicate efficient operation of insurance as well as microinsurance. For example, one person interviewed questioned how insurers could even confirm the identities of their policyholders, since many people reportedly have two or three identification cards. This makes management very difficult for an industry that needs to manage its risk efficiently.

As in many countries, there is no comprehensive infrastructure by which the self-employed can be accessed easily for insurance transactions – premium payments, service, and claims.

Pension fund regulations will soon be strengthened to require licensing of corporate and individual agents. Although this should promote better knowledge flow to customers, such a requirement will make it more difficult for insurance intermediaries, such as microfinance providers who may help to mitigate the limited infrastructure, to offer such products. There will need to be accommodation for intermediaries selling microinsurance, and these products should be limited and self-underwritten so that the agent is simply selling a clearly defined financial product.

Although Bumiputera is a mutual insurance company, Indonesia has no regulations covering Mutual Benefit Associations (member-owned insurance organizations). Bumiputera is able to comply with the current insurance laws because of its size and stability. But this lack of regulation hinders the potential for other member-based organizations to also offer insurance products to their members. One insurance official noted that there is no interest in government now in addressing the lack of a Mutual Benefit Associations law.

Health insurance is one of the insurance products most in demand. One key component in providing health insurance is the ability to work with providers of reasonable quality services. This imposes a constraint on the growth and expansion of health insurance. In a World Bank study researchers found that of 12 essential drugs identified by the Government, public hospitals had, on average, only 10 percent of these available. Hospitals of high quality and fully stocked medicine cabinets may be difficult to identify.

Taxation policies have a negative affect on selling insurance, especially for the low-income market. As of June 2005, the Government was working on a proposal to levy a 10 percent value added tax on insurance premiums. The World Bank and the Insurers' Association were working to oppose this.

Insurers are currently operating under a '3 T' system whereby policyholders pay tax three ways: on earnings that generate the funds to pay premiums, on the earnings of the fund, and on the receipt of benefits. Additionally, insurance payments for long-term insurance on employees are not deductible from tax calculations for employers. All these issues restrict the growth on long-term savings and insurance. Such products help fuel growth in many developed countries, but only when there are tax incentives.

Among the issues that these tax laws create are that in order to participate in long-term insurance programmes, low-income people would end up becoming registered with the Government and thus susceptible to all the other issues and costs of formal-sector operation. The policies should all be reviewed for possible abolishment if there is an expectation of low-income people participating in formal risk management programmes.

In 1997/1998, there was a 30–40 percent devaluation of the Indonesian rupiah. This led to a sharp rise in inflation and had a negative financial impact on long-term savings and pension accounts.[30] This may result in a lingering negative market perception that might make long-term savings unattractive at this time, especially to the lower-income markets. This will place even more importance on proper market education.

4.4.5 Risk-pooling limitations and opportunities

A significant limitation to microinsurance is the lack of data to use in risk underwriting and premium setting. Although there are 18 actuaries in the country to analyse the data, and indeed by law each insurance company must have a fellow of the Society of Actuaries of Indonesia on its staff, mortality and morbidity data are simply not available for the lower-income markets. Proxies are used, but ultimately, this lack of information leads to the application of loadings to protect the insurer, but increase the premium prices for potential policyholders.

As an example, there are Indonesian-developed mortality tables from 1995 and 1999. In the first table, three companies, of the over 60 life insurance companies, contributed data to compose the tables. In 1999, the data from 16 (of 62) mostly local insurance companies was compiled. This severely limits the usability of the data. Additionally, because the data are drawn from insurance companies, and because there has been effectively no microinsurance, these data would not relate to the low-income microinsurance market.

Allianz AG and others use mortality tables from the United States from 1958 and 1980. Some large organizations like Bumiputera and BRI's BRIngin Life may have enough life years from among their policyholders that they could develop mortality tables that would better help them in setting a risk premium with more limited loadings, and thus a more appropriate premium for the policyholders.

There are limited investment opportunities for Sharia products. In general, however, the volume of Sharia-based services, products, and businesses appears to be growing rapidly and this will likely create additional investment opportunities, though how they will respond to long-term asset/liability management issues is questionable.

Concerning the use of MFPs as intermediaries, there is uncertainty about the future ability of MFPs to offer financial services given the regulations that will become effective in 2007. For example, the Ganesha Foundation, one of the key demand research partners of this study, will not be able to offer financial services once these regulations are implemented. In addition, consideration of the insurance transaction flow will be important in using intermediary MFPs because of tax regulations with which MFPs and most of their clients are not necessarily in compliance. Thus, these issues may limit the potential use of such intermediaries.

[30] Swiss Re Sigma 7/2003.

4.5 Potential partners

4.5.1 List of potential partners

Potential partners who share common vision and the desire to learn and implement the new-product segment of microinsurance would include the following:

Potential partner	Description
BPR	BPRs provide a broad network focused on the low-income market already. This network could fairly easily be used to penetrate the low-income market in a massive way
Commercial banks	Banks such as Bank Niaga and Bank Permata that offer access to the low-income market, as well as potentially efficient mechanisms for collecting premiums. An additional benefit is that these often work through linkages with lower-level financial product providers
MFPs	MFPs such as Diman and Ganesha with clients that are already accustomed to financial products and have a wide rural network
LPDs	LDPs in Bali represent an efficient channel to low-income people in Bali that could also be used to sell and service life policies
Mercy Corps	Mercy Corps in Aceh: one of the few organizations in Aceh that does substantial and effective microfinance work
National Family Welfare Programme (BKKBN	The National Family Welfare Programme (BKKBN), which supports thousands of women's self-help and income-generating groups (UPPKS), is one of the biggest national institutional networks in terms of numbers and outreach even in rural areas, and may be considered as a partner, in particular in the Aceh Province
Arisans:	*Arisans* are not formal entities, and may maintain informal accounts, but they are an endemic presence throughout the country, and typically, these types of organizations have financial needs that go beyond what they are able to offer on their own. This is a good link with microinsurance although the efficiency is limited. They have a long history, however, and have been reasonably successful. A national organization does bind many of them together, and this could help in an efficient intervention
Perbarindo:	Though not a partner for product distribution, Perbarindo is a training and advocacy organization. There is a strong component of training in microinsurance, and as microinsurance grows, it will be increasingly likely that there will be legislative issues to address. Perbarindo is well placed to provide these services
Religious leaders	Religious leaders will be necessary partners (again, not as distribution channels) because they provide significant guidance to their members, and are often the most important opinion leaders, especially in rural areas. Their opinions about insurance are likely to influence a significant portion of the market. They should be educated about microinsurance and kept informed about the benefits that are being provided. Care must be taken, however, to maintain independence of the products from the religion and its leaders. Their general support for microinsurance should be sought

4.5.2 Potential PPP partner organizations in Indonesia

Details on key potential PPP partners that exist in Indonesia include: (1) Microinsurance services delivered through the banking system in collaboration with the GTZ-supported project Promotion of Small Financial Institutions (ProFI); (2) Health microinsurance complementing health-care services in collaboration with the GTZ-supported health project (*Proyek Sistem Kesehatan* or SISKES) and PLAN Indonesia, the Indonesian section of PLAN International, an international development organization with NGO status; and (3) Microinsurance as an instrument of social protection in the context of the new Social Security Reform law (medium term indirectly linked to PPP).

4.5.3 Microinsurance through banks in collaboration with the ProFI project

The GTZ-supported ProFI project offers opportunities to cooperate with the following three organizations for adding microinsurance to their portfolio:

Permodalan Nasional Madani (PNM): PNM is a kind of Indonesian Development Bank receiving funds from the Indonesian Government, the Indonesian Central Bank, the Asian Development Bank (ADB), and its own equity. On the one hand, it transfers funds through Perbarindo, the national apex body of local financial institutions (BPRs). On the other hand, it supports BPRs and large cooperatives directly. BPRs differ in size and number of clients ranging from1,000–10,000 customers. For qualifying BPRs, PNM operates training institutions at the national level as well as five decentralized training centres and 13 branches at the provincial and district level.

Perbarindo: Perbarindo is the national apex body of 2,200 local financial institutions (BPRs). Perbarindo focuses on information dissemination to their member BPRs, lobby work, development of training modules and capacity-building but has no enforcement power on them. On special occasions, they conduct training programmes with PNM.

PDLPD/PLPBK and registered village banks (LPDs): Contrary to all other regions of Indonesia, in Bali the local banks (LPDs) are registered under the Governor of Bali. LPDs are owned by their members and morally supported by the local Desa Adat (the customary villages). They cover 92 percent of the Balinese villages. The LPDs are trained by the provincial-level training centre PDLPD and the PLPBK located in every district.

4.5.4 Project strategy and products

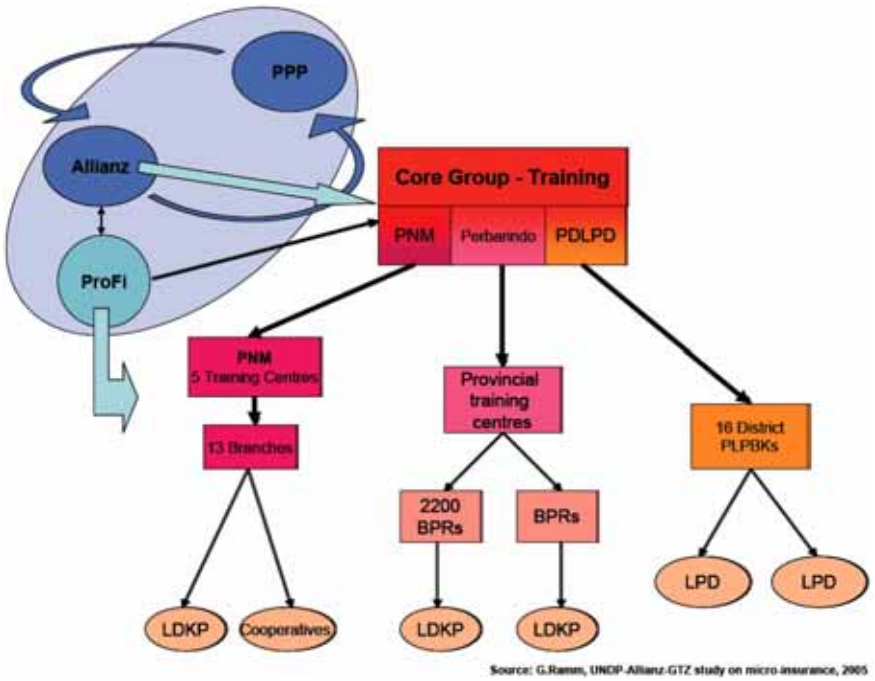
The banking sector in Indonesia offers the advantage of maintaining a well-established training infrastructure at the national level linked through decentralized training institutions at the provincial and the district level. They reach out to the local banks–either LPDs in Bali or BPRs and small financial institutions (LDKPs) in other regions. They consist of group members, thus ensuring the ownership and commitment of implementing microinsurance services.

In order to develop a network of training institutions offering microinsurance capacity-building, a suggestion has been made to set up a core group of trainers to be recruited from the PNM national training institute, Perbarindo (national level) and PDLPD (provincial training institute in Bali). They can subsequently disseminate information and microinsurance advisory

services to their decentralized training centres. Those centres will be in a position to approach the local banks that sell and service the microinsurance products to their clients and/or members.

Figure 11 depicts the potential implementation structure from the national level to the villages. It does not indicate regulatory or supervisory relations between the institutions.

Figure 11. PPP Structure



This strategy would enable the PPP project to utilize the scarce funding in an effective and efficient manner while providing inputs to the national-level organizations, ensuring that the training institutions through their infrastructure reach out to the provinces, districts, and villages. It is suggested that pilot region(s) be identified according to two criteria: a) a large number of strong BPRs and/or LDKPs (maybe cooperatives as well) and b) easy monitoring by ProFI.

In order to ensure quality of training and services, however, collaboration with ProFI should follow these guidelines:

- Assist the training organizations to set up the core group of trainers consisting of the training organizations mentioned above;
- Assist the training institutions to initiate this process at provincial and district branches;
- Follow up the process of curricula and training material development and participate in selected training;
- Monitor training at the decentralized training institutions;
- Assist in demand assessments for product design in selected project regions;
- Assess effectiveness and efficiency of microinsurance services provided to clients.

The demand assessment carried out in the context of the country study by Allianz AG, GTZ and UNDP indicated two products that could be most easily offered:

- A life insurance product that covers ceremonies and the families' transition upon the loss of a breadwinner;
- Long-term endowment for children's education.

The demand study revealed that the education endowment product would best be provided for two income groups: one with smaller contributions for the lower-income groups and one with a higher premium for slightly higher income groups. This product could be possibly administered in collaboration with the banking sector (investment of funds), using an array of delivery channels.

The conditions and the benefit package should be jointly developed with the potential customers. Both products are most suited for local banks and MFPs because there are important financial inputs for premium collection and servicing. Capacity-building will be of utmost importance. Thus, training modules and advisory services could possibly be developed in coordination or information exchange with Bajaj Allianz in India, as part of the South-South exchange of knowledge and technology.

4.5 Health microinsurance collaboration project

Health microinsurance in collaboration with the GTZ-supported health project (SISKES) and PLAN International/Indonesia was also explored.

The demand study revealed the highest demand for health insurance (in particular hospitalization). The success of health microinsurance depends to a large extent, however, on the availability and quality of the health-care facilities and services. Furthermore, preventive care and close contact to primary health-care services usually enhances the health status of members and subsequently contributes to reducing premiums for health microinsurance. Despite the high demand for health coverage, it is suggested that the simpler microinsurance products be developed first, in collaboration with the banking sector. In the meantime, the preparatory work for the more complex health benefit package can be started.

4.5.1 Collaboration with ongoing projects

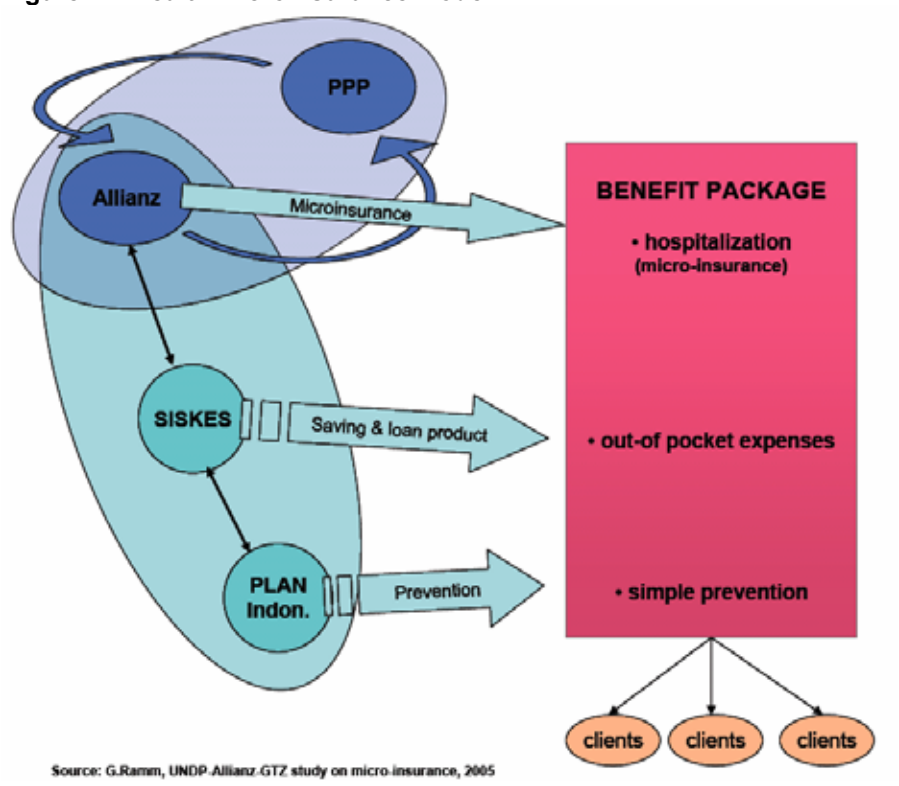
Taking these factors into account, the suggestion is to start health microinsurance in collaboration with ongoing projects, including the GTZ-supported project Improvement of the District Health Services in the NTT (Nusa Tenggara Timur province (SISKES) and PLAN Indonesia, the Indonesian section of PLAN International.

While SISKES aims at improving the range and utilization of health services in hospitals and primary health-care services, PLAN Indonesia contributes to revitalizing basic health services. SISKES (in cooperation with private sector partners and bi- and multilateral donor agencies) improves management and health-care services in collaboration with the Ministry of Health, educational institutions, NGOs, and Joint Health Councils. In collaboration with the Government and UNICEF, PLAN Indonesia has organized strong community groups and health committees.

Furthermore, village health workers, midwives and NGOs/MFPs are trained in (preventive) health care.

Thus, these two projects complement each other and provide the basic requirements for introducing health microinsurance. As both organizations have offices in Kupang, NTT region, it is advisable to use the existing infrastructure to start health microinsurance.

Figure 12. Health Microinsurance Model



4.5.2 Project strategy and products

In order to provide maximum protection at the lowest possible cost a three-tier approach is suggested: protection for hospitalization/coverage of outpatient costs/prevention. The innovative benefit package consists of different instruments of all three components:

- **Protection for hospitalization**: For risks occurring with a low probability at high costs microinsurance is most suitable. The benefit package will be designed based on an assessment in the project region.

- **Coverage of outpatient costs**: Basic treatment is provided at primary health centres (*puskesmas*) at relatively low cost. Depending on the quality of services and the severity of diseases, patients consult private doctors, specialists, and obtain secondary-level treatment, resulting in high costs. For such circumstances a special savings product combined with emergency loans seems to be the most appropriate instrument–although these products may not be in a position to cover all costs.

- **Prevention**: Selected preventive measures for the most common diseases should be introduced to all future clients.[31] In Indonesia, the most appropriate prevention method is yet to be assessed. Ease of implementation must be considered so as to minimize the costs. It is essential that it can be provided to every client. Other, more comprehensive, preventive healthcare measures could be implemented as a supplemental activity, but they should **not** be integrated into the inclusive insurance package.

This complex package requires coordination between all the partner organizations, focusing on the core competency of each organization:

4.5.3 Development of the microinsurance product

This would be done in collaboration with the relevant stakeholders. PLAN Indonesia would be in a position to conduct assessments on the most frequent diseases and the demand for microinsurance. Subsequently, the multipliers of PLAN Indonesia such as village health workers, midwives, and NGOs could carry out awareness- and capacity-building, reaching out to the potential microinsurance clients. Marketing and servicing of the microinsurance product is feasible through PLAN Indonesia's partner structure of NGOs/MFPs and community-based organizations such as mutual support groups (*gotong royong*) or savings and credit groups (e.g. *Arisans*).

Assessment of the most relevant **outpatient** and inpatient coverage may be provided by SISKES considering the experiences of PLAN Indonesia at the microlevel. If feasible, SISKES may be in a position to negotiate better terms and conditions for the outpatient treatment. ProFI could assist in the design of the savings and emergency loan products.

Building upon the trained structure of health workers, NGOs/MFPs, local health committees, and community groups' **prevention** could be supported by PLAN International/Indonesia. They would define the most important preventive measures such as worm infections, malaria, and HIV, and jointly with SISKES define those (simple) measures that can be incorporated into the benefit package.

4.6 Microinsurance and the new social security law

Microinsurance can fill the gap between the demand for risk management instruments and the supply of risk management mechanisms. In this context, appropriate social security schemes play a role (if the provision of risk protection is ensured, low-income groups would not buy microinsurance for these risks).

The new law provides that "Participants in the health insurance scheme are all people who have paid contributions or whose contributions have been paid by the Government."[32] For the poor, the government subsidy will be given in nominal amount. For work accident and old age pensions, a participant is a person who has paid contributions. As quoted from the same law,

[31] One example is Uganda, where two deworming pills were provided annually to members, protecting them from worm-related diseases. The cost of the pills was added to the microinsurance premium.
[32] Source: Law no 40/2004

"For participants who do not receive any wages, the contributions are based on certain nominal amounts that will be determined periodically by the Government." Public pensions and life insurance will not be provided for people who cannot pay contributions.

As these provisions are long-term perspectives yet will not cover all parts of the population, microinsurance could be an appropriate mechanism to complement the benefits mentioned in the law. Through the project Development of a Social Health Insurance System in Indonesia (SHI), it is attempting to incorporate microinsurance as one instrument of other social security systems. If the Indonesian Government would accept this approach, a number of advantages are expected such as:

- Systematic development of microinsurance products through state-owned and private insurance providers;
- Enabling organizations of civil society to assist and/or offer microinsurance services complying with the legal framework and help to ensure the viability of insurers;
- Creating a suitable regulatory environment (e.g., allowing microinsurance activity and protecting consumers from misleading selling practices–this is even more important because the client base is often uneducated and lacks the ability to assess the performance of the insurer);
- Promoting formal-sector insurance institutions to enter the low-income market and adjust their delivery channels according to the requirements of low-income clients.

Since the Social Health Insurance project contributes to defining the rules and regulations as well as the implementation structure of the Social Security Systems law, SHI can lobby for promoting microinsurance. These activities, however, are not part of the current PPP project.

4.7 Competition: Strengths and weaknesses

Strengths and weaknesses of institutions currently offering microinsurance are noted here. The number of institutions offering microinsurance is very limited, except credit life insurance linked to the banking sector. Thus, the assessment covers only a few organizations:

Table 12. Strengths and Weaknesses of Microinsurance Organizations

Organization	Strengths	Weaknesses
Arisans (Catholic network)	Strong solidarity groups Widespread network	Very social welfare minded Not viable/sustainable microinsurance schemes No capacity-building structure Very hierarchical Decision-making dominated by leaders (*Ketua*), maybe even by bishops
Other Arisans	Source of emergency lending	Not suitable to meet specific clients' needs

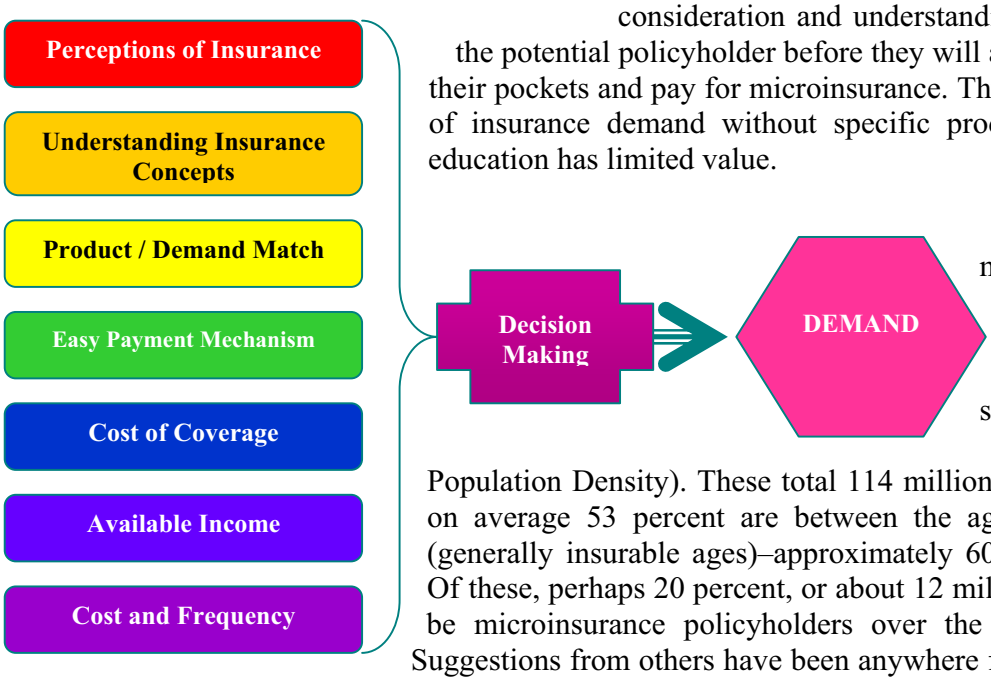
Organization	Strengths	Weaknesses
Pasar Konsortium	Well-developed network Suitable delivery structure as all potential clients are located in one vicinity (marketplace)	Currently not for low-income people (or only for a few) Prone to fraud by the local government Financially strong traders and shopkeepers (including the local administration) may dominate decision-making
Jamsostek	Established network of branches	So far focused on formal workers with little extension to informal economy Complicated procedures Benefit package not suitable to low-income clients Fraud by employers (e.g. underreporting of salaries and false contributions) Non-registration by employers (thus no social security for employees)
LPD	Membership-based Good ownership Professional management Legal entity: official registration Training infrastructure available Geographical cluster, thus easy to train, implement and monitor microinsurance	Lack of knowledge of microinsurance
MFPs and People's Credit Banks	Membership-based Good ownership Broad network of local banks Access to training facilities Relatively quick loan disbursement	Higher loans have to be supported by collateral (e.g., assets, land title)
Cooperatives (e.g. oil producers)	Large membership Geographic centralization	Probable lack of awareness and knowledge of microinsurance Probable limited capacity to operate microinsurance schemes due to lack of experience
Registered banks in cooperation with insurance providers	Well-established infrastructure Access to training facilities Outreach to the poor in cooperation with local banks (e.g. BKDs, LDKPs) Professional staff	Knowledge of insurance business but lacking microinsurance concepts Dependency on local banks for servicing of microinsurance products

CHAPTER V. MARKET STRATEGY

5.1 Estimate of the demand and market potential for microinsurance

An estimate of the total market potential for microinsurance has many facets. Figure 13 outlines many of the components that must fall into place as part of the decision-making process of a potential policyholder. Other microfinance products are simpler in this respect than microinsurance because savings and credit are tangible – you put the money in and you can get the money out, or you get money and repay it. An intangible product requires much more consideration and understanding on the part of the potential policyholder before they will actually reach into their pockets and pay for microinsurance. Thus, any estimation of insurance demand without specific products and market education has limited value.

Figure 13. Components of Demand



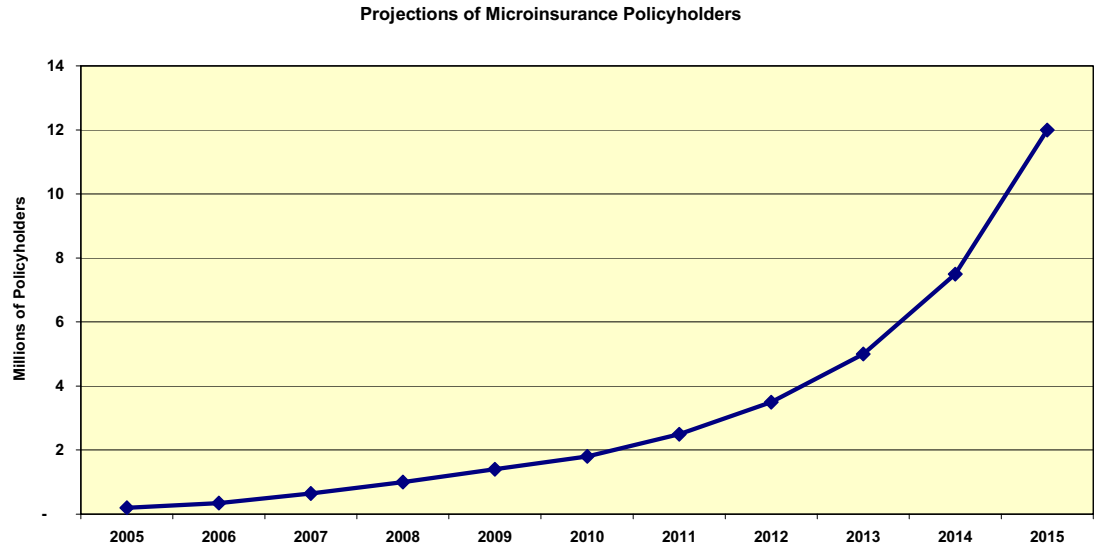
The market for microinsurance is generally the relatively poor and the informal sector (figure 10: Indonesia Population Density). These total 114 million people. Of these, on average 53 percent are between the ages of 20 and 59 (generally insurable ages)–approximately 60 million people[33]. Of these, perhaps 20 percent, or about 12 million people, could be microinsurance policyholders over the next ten years.[34] Suggestions from others have been anywhere from 25 million to 35 million as insurable. Over time, the insurable population will probably increase to numbers in this range as access is broadened. But 12 million active policyholders at the end of 2015 is a reasonable expectation. Any growth assumes mass availability of products, marketing, and market education that respond to the components noted in figure 13.

Growth will come slowly at first as people begin to get used to microinsurance, and will grow faster as more and more people gain trust in the microinsurance providers and their products. A conservative projection over the ten years is likely to look somewhat like the graph in figure 14.

[33] http://www.nationmaster.com/country/id/Age_distribution

[34] Generally based on utilization ratios of voluntary microinsurance products in other countries. This amount increases depending on insuring children, or geriatrics.

Figure 14. Projections of Microinsurance Policyholders



5.2 Distribution systems

Distribution of microinsurance products will take several approaches.

Direct selling by general agents*:* This is unlikely to be very successful because of incentive issues on the side of the agent, and distrust on the side of the clients. In other countries, this approach has had very limited success.

Direct selling by specialized agents*:* AIG in India has developed an interesting and seemingly effective mechanism for distributing their products. They identify a person in a village who will be the agent for their area–somewhat like the old-time 'Avon Lady'. With some training and proper educational and marketing tools, these agents can be especially effective. There is a limitation for these agents in that their market area is rather small but this may be appropriate for their skills. This is a model that should be tried in Indonesia, possibly in Bali where personal service is so important.

Indirect selling by general agents: In this model, insurance company agents work directly with leaders of organizations that have a large outreach into the low-income market. This model has proven very effective in other countries. Although the premium per policyholder is small, using these groups creates enough of a financial incentive for the agents to motivate them to work hard to get these groups. This might work very well with *Arisans.* This model should be tested in Indonesia.

Education and marketing through Islamic organizations: Sharia products will be a necessity to reach the potential market. Islamic organizations and leaders will need to be

addressed in such a way that the market understands the benefits and opportunities under Islam. Potential interventions might include an effort by the Sharia Council, which approves Sharia-compliant products and institutions, to advocate the benefits of insurance. Additionally, efforts should be made to educate local Islamic leaders about insurance and its benefits so that they may speak to their congregations based on knowledge. The Sharia committees within the insurance companies should be able to assist in developing these linkages.

AIG/Lippo offers microinsurance through several innovative delivery mechanisms. These include post offices and department stores. Although these efforts are not yet as successful as hoped, this type of approach might be very successful for this market.

Placing insurance sales locations where low-income people live and work. ICICI Lombard sells life insurance from computer kiosks. Simply having such access could facilitate growth in microinsurance, as long as the controls are good.

Swisscontact has developed a strategy for efficiently expanding the market for microfinance that could easily be adapted for the delivery of microinsurance. Table 13 shows the Swisscontact system for training intermediaries to offer credit. Swisscontact management agrees that this network could be used for microinsurance, as long as the service providers are given products that they can sell.

The intermediaries in the current credit programme with Swisscontact include: Mandiri, Mandiri Sharia, BRI, Niaga, Bukopin, Commonwealth, and Jabar. These organizations might also make good partners for microinsurance since they are already working within the target markets.
.

5.3 Marketing

Generally, acceptance of microinsurance requires educating and marketing to the low-income market. Marketing of the product requires going to the client, as the microfinance programmes do now. It will also require using consistent and trusted agents for marketing, promotion, premium collection, and claims reporting.

5.3.1 Relationship with customer

The relationship between the insurance product representative and the customer is crucial to the customer's level of comfort with the product. This suggests that sales of microinsurance through existing microfinance programmes may be successful if the relationship between the loan officer and the client is already solid. Microfinance clients highly value their MFPs and the services that the MFPs provide. They respect and trust the loan officers from these organizations; therefore the MFP staff would be credible marketers.

Insurance companies such as Bumiputera and Jiwasraya have marketed their products by going door to door in communities. This method appears to have had mixed results due to the hit-or-miss aspect of finding people at home. In some communities, people had heard of insurance and knew of the existence of different products, while in other communities, people reported that no marketing had been done. Furthermore, even in communities where people

reported that insurance companies had been marketing, not all respondents had contact with insurance people, and many respondents reported not understanding insurance. This suggests that door-to-door methods of marketing do not achieve 100 percent coverage. Other methods of marketing microinsurance will be required to reach the target market.

5.3.2 Marketing strategies that might be tested

Marketing microinsurance is mostly a task of market education. This education needs to be carried out in ways that make sense to the potential clients and fit within their busy schedules. Some methods that have proven effective include:

- Posters with mostly illustrations and little text so that people can understand quickly without having to read the poster;
- Brochures or small cards with insurance information are important as they enhance the physical evidence of the product;
- Theatrical performances are effective in conveying the concepts of microinsurance;
- A three-step approach has shown limited success, where an agent speaks to a mass gathering, then comes to the villages represented at the mass gathering and speaks there, and finally, identifies those that are interested and comes back to market by family;
- Marketing through large group organizations has had some success, but requires good training of the front-line staff;
- The best method anywhere is that of the demonstration effect. When people see that insurance actually does pay claims, this dramatically enhances interest;
- Since the message must be consistent, the use of mini-flip charts with the illustrations and text imprinted helps when presenting the product.

Both of the respondents that met during interview who had purchased life insurance on their own had commented on how they were worried about what would happen should the family breadwinner (in both cases the husband) be injured or die. In both cases, it appears that these couples are better educated than their neighbours. Nevertheless, a marketing campaign that focused on selling peace of mind to people who worry about how their family would cope with the loss of the breadwinner might be successful. The focus should be on the welfare and well-being of the surviving family members, rather than on the event itself, such as an accident or death, since people don't like to talk about bad events.

Endowment education insurance would sell itself if the price were right. An example of an endowment education policy is that of Bumiputera, which offers a popular policy. The product has a premium of IDR227,000 every three months. The benefits help cover the costs of entering each new grade grouping. The policy pays on graduation from:

Kindergarten	IDR1 million
Primary school	IDR3 million
Junior High School	IDR5 million
Senior High School	IDR Depends on total savings

Endowment education insurance should probably be marketed towards women as they may have more influence in making decisions regarding the children. Our impression is that married couples tend to make decisions together; therefore, other products can be marketed to both men and women. This product assists policyholders with the lump sum payments that are required at the start of each new school grade grouping, and continues payment after the death of the policyholder.

5.3.3 Marketing considerations

Common mistakes in marketing centre on misunderstandings of the low-income market. Examples might include posters that are filled with complex text, or television advertising when most of the market does not have a television set. It is critical that any marketing efforts be vetted by focus groups of likely policyholders. This will save much money, time, and confusion.

CHAPTER VI. RECOMMENDED MODELS

6.1 Prototype

Product 1: Breadwinner Life Insurance

Premium	Straight insurance product with a 10-year duration at a set premium/contribution
Coverage	Covers spouse (should be mostly husbands) for death
Benefits	• Initial IDR1 million ($107) for funeral expenses and the 7-day remembrance • Cover for two years for the following: • Children's health care • Continuing school fees • Monthly grocery allocation • Monthly utilities if appropriate
Delivery channel	Banks, MFPs, *Arisans*
Marketing	Posters at key locations, announcement at any large functions with many low-income people, possibly radio if there is a station that most people listen to, sponsoring a soap opera on the radio if there is one that is very popular
Target market	Breadwinners of households with children

Product 2: Education Endowment

Premium	Life insurance portion plus a savings component that will pay agreed fees when needed (flexibility is important)
Coverage	Covers death of the policyholder
Benefits	- Pays a benefit at each stage of educational development (primary, secondary, tertiary); - Benefits paid from savings, or from the insurance policy on death
Delivery channel	Schools, banks, MFPs, *Arisans*
Marketing	Posters at key locations at schools, announcement at any large functions with many low-income people, brochures for parents to take home, agent on site during visiting days, hospital nurseries, paediatricians' offices
Target market	Men and women with young children

The most important risk management need identified in the demand research was the need for health-care cover, especially that of hospitalization and long-term treatment. At this point, such products are not being wholeheartedly recommended for several reasons. These include:

The implementation of the social health insurance component of the Government's relatively new social security law is not fully clarified. For an insurer to make the investment needed to develop a profitable health microinsurance product, a long-term vision is necessary. This vision is seriously clouded by the ambiguity of the outcome and implementation effectiveness of the social health insurance programme;

Another effect of the social health insurance programme is that, typically (as in Kenya, the Philippines, and others), when a government announces that it will be providing "free" health care, low-income people are unwilling to participate in a private health insurance programme, seeing it as a waste of their money;

In getting more regulated insurers involved in microinsurance, usually the most successful process is to begin with relatively easier products like credit life, term life, and endowment life products. This helps insurers understand the low-income market better and the processes and controls required for success. After this, health insurance products may be introduced.

6.2 Benefits: Customer needs satisfied

Allianz AG currently has a retention rate of about 60 percent and this is moving upwards. They calculate in budgets that 70 percent will renew, and their goal is for 80 percent renewal.

General aspects of customer retention include: customized products; fast claim management; simple procedures; a good understanding of the product; easy premium payment processes, and matching the product with the real demand of the market.

In Indonesia, it is likely to be increasingly important to offer products that respond to Islamic customs and rules. Some key issues will include:

- Strong cooperative/mutual principle such as sharing of profits or keeping profits in a "mutual" security fund to be used when the number of claims is increasing;
- Using systems other than interest and commissions such as purchasing the insurance form, collecting service fees instead of premium payments.

For endowment policyholders:

- Mechanisms that permit clients to pay premiums in a flexible way (time-wise as well as amount-wise);
- If flexible payment is not possible, suitable means to deal with lapsed payments should be identified in order to avoid the reduction in the benefit amount when the policy matures;
- Inclusion of the provision to borrow funds for emergency purposes.

Others:

- Existence of accessible grievances mechanism and consumer protection;
- Close contact with and trust of agents (hypotheses: the less educated and poorer the clients are the more "hand-holding" is needed on the part of the agent).

The key to customer satisfaction is making sure that they understand what they are buying before they buy it. When people do not understand they will leave as soon as they can, and they will complain about the product.

6.3 Life cycle

These products will start slowly and catch on when people see the results. Because these are both longer-term products, the "demonstration effect" will take longer and slow the pace of growth.

Once these products catch on, people will recognize the benefits of insurance and will want to move to additional products. This has happened in several countries and would be likely also to occur in Indonesia. Though these products are likely to remain staple products for insurers, clients will soon push for health coverage, property insurance, and some level of livestock and crop insurance. This is a common evolution. Starting people with a good solid life product, or in this case two products, is a good way for everyone to understand how to manage this market.

CHAPTER VII. OPERATIONS

Because it is critical to minimize costs to make microinsurance marketable, it is important not to have any separate procedures or staff to manage microinsurance until absolutely necessary. Initially, there should be no operational adjustments except for the requirements of a new product line.

In order to facilitate the transaction of information the insurer will need to have a way to electronically capture the relevant data with the intermediary (if at all possible) and process this without paper. When this is possible, labour is significantly reduced, as are errors.

The internal audit department should include microinsurance intermediaries in their audits to control against potential fraud. Management should also consider using an exception method of tracking clients if they are unable to acquire information electronically. In this case rather than warehousing all the paper records of all the policyholders, they could make the intermediary prove that the deceased was insured. This saves much time and effort.

Insurers will need to be able to track client information where possible for use in understanding the mortality and morbidity rates of their markets. Since this information is not available, collecting it themselves may help to set premiums more in line with real costs.

7.1 Capacity needs

There are four insurance training institutions in Indonesia. Some say, however, that there is no trust in the quality of these institutions. A closer assessment should be made before investing more in their capacity.

In order for microinsurance to be successful there will need to be some training of insurance staff and agents in how microinsurance is different from traditional insurance, and how to approach the low-income market. This could possibly be done through the Institute of Risk Management that is a combination of the Akademi Assuransi Indonesia (AAI) and Lembaga Pendidikan Assuransi (LPAI) and provides insurance training to the industry. Training of trainers' courses should facilitate offering courses on microinsurance from the Institute. Agents will also need training in Sharia-based microinsurance.

Most important is the need for market education. The insurance industry and its associations, as well as the insurance directorate, and religious leaders should be able to provide general education. Additionally, front-line staff expected to sell microinsurance should be trained to provide correct information to their clients. Tools for marketing such as training tools, brochures, and posters designed specifically for this market will be necessary.

More specific market education might be provided through organizations like Bina Swadaya that has three sectors of activity: microfinance, training and education, and a research centre. The

training and education arm might be appropriate for market education. They currently work out of 12 regional offices, with 2,500 groups, representing over 55,000 households.[35]

Traditionally, staff of MFPs that act as intermediaries for microinsurance products have not performed well. It is critical that they be:

- Well trained to understand and appreciate the benefits of insurance;
- Have proper tools to use in presenting microinsurance;
- Be compensated in some way for their sales;.
- Have microinsurance sales included in their official targets.

Some additional capacity development needs include:

- Establishing and implementing customer service standards;
- Carrying out of demand, supply, feasibility, and customer satisfaction studies;
- Information about risk management strategies and the concept of microinsurance;
- Establishment of an appropriate management information system (MIS);
- Data collection, analysis and microinsurance administration;
- Implementation of appropriate microinsurance monitoring (including renewals of contracts);
- Establishment of a microinsurance monitoring system;
- Development of mechanisms to control adverse selection, moral hazard and fraud;
- Development of clear performance expectations and targets;
- Evaluation of staff and establishment of an effective compensations system to promote productivity and staff commitment;
- Development of customer satisfaction tool and application of the same;
- Interpretation of data from MIS and the monitoring system;
- Establishment of effective internal control framework, including segregation of tasks;
- Recruitment, placing, and training of appropriate staff.

7.2 Other resources required

In order to improve the chances of success for the microinsurance initiatives some of the other resources required include:

- Improved training of Insurance Directorate supervisors so that they can understand microinsurance and the risks involved with it, and how that will impact their evaluations;

- It would be helpful to have someone in Indonesia coordinating the microinsurance improvement activities. That person could work with the training institutes, assist with the marketing campaigns, provide assistance to insurers and intermediaries, and provide some legislative lobbying. Two to three years should be sufficient to get things moving, and implemented successfully;

- A specialized microinsurance broker might fulfil the microinsurance advocacy and promotion role. In the traditional sense, insurance brokers represent policyholders by

[35] Mr. Riza Primahendra, Bina Swadaya.

identifying their needs and sourcing insurance to respond to those needs. A microinsurance broker could act in the same way, simply focusing on microinsurance and the currently unserved insurance market. The start up or support of a microinsurance broker would leave a continuing presence;

- A mass education effort to begin getting people to hear about and understand insurance.

7.3 Legal structure

At this point, three things must be addressed. The first is that financial legislation for banks and insurance companies is being reviewed. Both are potentially very important to the expansion of microinsurance, and should they be restricted from the intermediary role that would limit the growth and expansion of microinsurance.

The second is mutual benefit association legislation. It would be helpful to give MBAs the ability to formalize their insurance provision under a structure owned by the policyholders. It is somewhat difficult to make adjustments for MBAs that would not open the door to potentially undesirable companies.

Third is legislation for agents. In order to use intermediaries to market insurance, the front-line staff cannot all be licensed as insurance agents. There should be a legal entity such as an institutional agent where the institution is accredited but not all its field or front office staff.

The legal structure for intermediary MFPs is questionable at this time given impending legislation that will limit or eliminate their ability to manage insurance-related financial transactions.

7.4 Financial activities

7.4.1 Technical assistance and funding activities

To accomplish the activities noted above would require significant donor input, mostly in the form of grants, but also possibly in the form of long-term convertible loans for the microinsurance broker. Some of the activities discussed are consolidated here for ease of understanding. The costs offered here are gross estimates and are intended to include transport and other operational costs.

Table 13. Technical Assistance and Funding Activities

Idea	General description	Estimated cost	Activities covered
Training programmes for insurers and intermediaries	Develop training of trainers' materials and a curriculum and train local insurance trainers.	$100,000	Develop materials, local training in several regional sites, website, and distance learning structure.
Market education	Develop training of trainers' materials and a curriculum. Integrate this into bank, MFP, *Arisan*, and other meetings where low-income people might be. Mass media campaign focused on low-income market. Local theatre productions to show how insurance works and why it is beneficial.	$300,000	Develop and test materials, training in several regional sites, mass media campaign (several languages and media types and outlets), theatre production development, testing and implementation in numerous areas in Indonesia.
Microinsurance broker	Training for existing broker or placement of a specialized microinsurance broker. Operational subsidy to cover the first two years on a diminishing scale to cover for the start-up time for this new business area.	$200,000 for existing broker; $250,000 for new broker	Operational subsidy for years one and two. Office set-up; software and hardware set-up; staff selection and training; branch offices identified and staffed; communications infrastructure; legal requirements.
On-site technical assistance	A microinsurance specialist to be placed in Jakarta for two years to provide technical assistance as noted above.	$250,000	Two years of international consultant; office; staff; travel, and other operating costs.
Processes and formalization	Covers many of the target setting and monitoring points from above. These could be done by the on-site technical assistant at no additional cost, or they could be done by separate consultant visits.	$100,000	A series of consultant visits, developing benchmarks, creating software analysis tools and reporting mechanisms.
MIS technical assistant	Would do the programming to link the insurers and intermediaries for paperless activities. This would be a local person.	$25,000	Several programming linkages developed between regulated insurers and microinsurance intermediaries.

With these activities implemented, it is likely that the growth graph presented in figure 14 may still only reach 12 million, but the slope would be much greater with much less time spent below 2 million.

7.4.2 Identifying the donor community and its interest in microinsurance

Despite the increasing relevance of microinsurance, no donor agencies support these programmes in Indonesia. Many are reluctant to get involved–probably (also) due to lack of knowledge and concepts. The chances of promoting microinsurance may be higher when multi- and bilateral agencies implement already microfinance projects. ILO, the World Health

Organization (WHO) and the European Union are currently involved in social security and may include microinsurance as one instrument of social security for informal-economy workers. Apart from GTZ, the following initiatives are among the most concrete:

- ADB is going to assess the possibility of microinsurance in the context of its Aceh livelihood programme. The decision on microinsurance will be taken based on the results of the study;

- Save the Children is interested in exploring microinsurance in the context of its economic development and microfinance coaching programme in Aceh. If this project could be successfully implemented, expansion to other regions would be considered;

- Swisscontact has conducted a study on the opportunities to promote insurance for SME that could be added to its microfinance training programme. Currently it is felt that there could be a way to link microinsurance to the SME and microfinance programme. This may not happen in the immediate future, however.

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CHAPTER VIII. CONCLUSION

Microinsurance in Indonesia is in a rather nascent stage. although there is activity.. Demand reports show significant demand from the low-income market for insurance products: hospitalization, education endowments, life insurance and property cover. An estimate of the potential for active microinsurance policyholders at the end of 2015 is about 12 million (see figure 14). This is likely to be achieved through slow growth in the first few years leading to very rapid growth later.

In order to achieve this potential, insurance companies must develop products that are specifically focused on the low-income market. They must use market education and promotion techniques that will have an impact in altering current attitudes about microinsurance.

Two products are recommended for pilot testing. The first is a life insurance product that covers some of the costs of the funeral and memorial services, as well as providing certain benefits to the household over a period of two years. The second recommended product is an education endowment product to help people ensure that they have the necessary large sums of money when they need them to keep their children progressing through school.

Health microinsurance is also a critical requirement for this market, but the ambiguities of the social heath insurance component of the Government's current social protection legislation makes this more difficult to develop and implement successfully.

These products, and others that should follow them, as well as the market education that will help develop the demand, should have a powerful impact on the low-income market by providing tools to help people secure their lives.

APPENDICES

Appendix I: Methodology

The research was carried out using qualitative techniques including focus group discussions (FGDs), participatory rapid appraisal techniques (PRAs) that incorporate FGDs, and individual interviews. The types and numbers of tools used are shown in the table below.

Typically, the focus groups had 8 to 11 participants. These participants ranged in age from about 20 to 50, with a small number of older participants. All participants were borrowers in one of three microfinance institutions: Ganesha Microfinance (Yayasan Ganesha Keuangan Mikro); Dian Mandiri Foundation 'Diman' (Yayasan Dian Mandiri); and Bina Swadaya.

Research Tools and Numbers Interviewed

Microfinance Programme	Ganesha	Diman	Bina Swadaya
Research Tool:			
Focus Group Discussion on Risk	2	1	3
PRA on Life Cycle Risks and Coping Mechanisms	1	1	1
PRA on Seasonality of Income and Risks	1	1	2
Individual Interview: Loan and Saving Use Over Time	1	1	
Individual Interview: Client Satisfaction with Formal Insurance Products			1
Number of People Interviewed:			
Number of Women Interviewed	38	22	47
Number of Men Interviewed			15

Locations of research:
The FGDs, PRAs and interviews were conducted in or near the homes of clients of the microfinance institutions. Clients of Ganesha were located in rural parts of northern Tangerang around the town of Talek Naga. Clients of Dian Mandiri Foundation were located in and near the town of Tangerang. Clients of Bina Swadaya were located in Sleman, north-west of Yogyakarta and in the area of Imogiri to the south of Yogyakarta.

Appendix II: Information on Microfinance Institutions

Diman (Dian Mandiri Foundation)
Diman is an affiliate of Opportunity International. Diman has 12 branches located in the Tangerang region of Indonesia, to the west of Jakarta. The community in which we held focus groups contained clients who are indigenous to the area. This is unusual as a high percentage of Diman clients are migrants from other regions of Indonesia. The Diman clients that were interviewed were more urban than clients from other MFPs who participated in the research.

Diman Loan Programme
Diman offers three kinds of loans. Most of the clients interviewed had borrowed trust bank loans; a few had borrowed small group loans. No individual loan borrowers were met.

Trust Bank Loans
Solidarity Group Loans issued to groups of 20 clients each
Small Group Loans
After four cycles, clients can graduate from trust banks to small groups
Solidarity Group Loans issued to groups of three to five people
Individual Loans
Require collateral

Diman – Loan Parameters

	Trust Bank Loans	Small Group Loans	Individual Loans
Amounts: (IDR)	500,000–2,000,000	3,000,000–5,000,000	3,000,000-10,000,000
Interest (per month)	2.5%	2.5%	2.5%
Average Loan Sizes: 1st Cycle 2nd Cycle 3rd Cycle	 618,617 1,063,393 1,711,742		
Loan Term:	20 weeks (5 months)	6 months	
Payment Frequency	Weekly	Weekly	Monthly

Diman Statistics

Outstanding Loans ($)	750,712
Operational Sustainability (%)	73.87
Financial Sustainability (%)	63.10
Arrears >30 days	3.24
Number of Staff	127
% Women Clients	86%

Diman: Client Characteristics

Client Type	Trust Bank Loan	12,817
	Small Group Loan	223
	Individual Loan	27
Location:	Urban	44%
	Semi-urban	38%
	Rural	18%
Gender	Male	16%
	Female	84%
Displaced Migrant		77%
Age (years old)	<21	1%
	21–30	18%
	31–40	47%
	41–50	26%
	>50	6%
Marital Status	Married	92%
Education	None	3%
	Primary School	35%
	Secondary School	28%
	More than Secondary	34%
Average No. of People in Household		4
Type of Business	Manufacturing	6%
	Trade or Retail	50%
	Food Services	26%
	Transport	4%
	Other Services	12%
	Agriculture or Livestock	1%

Ganesha Microfinance Foundation

Ganesha is a minimalist Grameen replication that provides one basic loan over a 50-week period with a flat interest rate of 30 percent per annum (or 2.5 percent per month). Borrowers are organized in groups of three to five women. Four to five of these groups are organized into a centre. All clients are women, as is most of the staff. Ganesha does not require collateral for its loans.

The programme operates in rural areas of Tangerang, to the west of Jakarta. Ganesha has three branches and serves over 4,000 clients. Using targeting techniques such as a housing index, Ganesha makes small loans to some of the poorest women in Indonesia. Many of Ganesha's clients are landless labourers involved in petty trade, preparing and selling food, livestock rearing and vegetable growing. Ganesha plans to move further downmarket and offer loans as small as $20, if possible.

The Ganesha clients were, on average, the poorest that were interviewed in all the focus groups. Ganesha had offered a microinsurance product in the past but had to discontinue it, along with a savings product, due to regulatory issues. As a registered *Yayasan* or foundation, Ganesha is not permitted to mobilize savings.

Ganesha Statistics (as of March 2005)

Total Active Clients	4,523
Loans Outstanding ($)	194,678
Average Loan Outstanding/Client ($)	43
Loans in Arrears (>4 weeks)	0
Operational Self-sufficiency	90%

Bina Swadaya: Yogyakarta Regional Office

Bina Swadaya provides savings and credit services to clients organized into self-help groups. Generally, Bina Swadaya extends loans to a large group such as a village-wide group. That group has a committee that accepts applications from the members and makes decisions about extending loans to individual families. The group is responsible for collecting loan payments and repaying Bina Swadaya. The term of the loan from Bina Swadaya is for one year. Individual loan terms will vary but all loans must be paid back in time to the group in order to repay Bina Swadaya on the due date.

In addition to loans, Bina Swadaya encourages savings, and encourages the groups to set up social funds. The social funds are created from small contributions that vary from IDR100 to IDR500. Members pay these contributions at monthly meetings. If a member of the group becomes ill or dies, a donation can be given to the family from the social fund. If a borrower dies before paying back the loan, the borrower's heirs are responsible for paying it off. Savings vary according to the groups.

Since Bina Swadaya lends to large groups often made up of every family in a village, targeting is carried out by selecting certain geographic areas. Bina Swadaya has selected particular rural areas outside of Yogyakarta in which to provide loans. As a result, there is more socio-economic variation within a single group at Bina Swadaya than at the other MFPs included in this research. This variation was reflected in the focus groups in which it was obvious that some participants were better off than others. Generally, however, most of the focus group participants would be considered poor.

Appendix III: Details of Arisans Visited

Several *Arisan* groups were visited during the course of this study, and descriptions of how *Arisans* are organized are based on these visits. These specific *Arisans* are organized in three ways:

- Family or clan (including family groups with accepted hierarchies based on seniority)
- Ketua RT (principal of one block or neighbourhood)
- The Church

Arisan Type	**Description**
Family *Arisan*	▪ Group of 28 men ('members') of the same family of the 'Sinaga' ethnicity and all people living in their households ('under the same roof'). Total membership is approximately 100 persons. ▪ The group is split into 3 subgroups with 6 members, 10 members, and 12 members, respectively. 3 Ketua of the 3 subgroups form the 'executive committee' of the Arisan. Average monthly premium: IDR20,000. Less wealthy members pay IDR10,000.
Clan *Arisan*	Group of 130 men ('members') and their families of the 'Sinaga' ethnicity living in the locality of Depok, approximately 600 persons. The group is divided into several geographic sector groups. Monthly premium: IDR10,000.
Ketua RT–Batak Kampung *Arisans* (Kampung: city-quarter, block, neighbourhood)	▪ Group of all Batak men and their families living in the same vicinity, regardless of their subgroup memberships. ▪ 3 senior members are *Ketua* of 3 existing subgroups. ▪ 3 *Ketua* form the executive council, which meets once every 3 months. One of the *Ketua* is the legal account holder of the *Arisan*'s bank account. They hold this office for a two-year renewable term.
National-level women's church *Arisans* (approximately 225,000 members) Structure: National association (DPD) 17 provincial offices of DPD: related to almost every Bishop Branches: linked to churches Groups consisting of 25 members	**Products**: Premium IDR1,000/month (if they encounter deficits then collection of additional contributions) Benefits: inpatient health coverage lump sum IDR100,000; education benefits Group activities: group members are involved in many social activities as well as welfare activities such as vocational training/household economics Premiums are distributed as follows: 50% held by the group for benefits, the reserve, 30% 'self' (as savings), 10% for the Bishop, and 10% for national level-association

Appendix IV: Terms of Reference

Microinsurance: Demand and Market Prospects: India, Indonesia, and the Lao People's Democratic Republic

1. Introduction

Allianz[36] has expressed interest in being a partner with UNDP and GTZ in market research to estimate the demand for microinsurance interventions in three major Asian markets (India, Indonesia, and the Lao People's Democratic Republic). This represents a mutually beneficial opportunity for UNDP and Allianz. For UNDP, it would create access to microinsurance to meet the demand, so far unsatisfied, to reduce the vulnerability of over 3 billion people, and it has the potential to assist in achieving the MDGs. For Allianz, it would provide a leadership niche in this growing industry. Microinsurance also constitutes a new market opportunity for Allianz. In partnership with UNDP, Allianz could make an important contribution to the development of the nascent microinsurance markets. A consumer base of practically half of the global population presents a significant market with a lucrative potential for the insurance industry. Given the added threat of human-induced climate change, the insurance industry can proactively assist in reducing the vulnerability of poor people in developing countries to weather-related natural disasters.

The underlying premise of this proposed partnership is that the delivery of microinsurance will benefit poor and low-income groups, establish local entrepreneurs, and strengthen livelihoods. This will be driven by the creation of safety mechanisms for managing risks, and shocks and stresses including natural hazards. The hypothesis is that access to insurance by entrepreneurs in the developing countries will draw private-sector investments and promote national development priorities.

2. Background

Currently over 1 billion people–two thirds of them women–live in extreme poverty on less than $1 a day without access to most of the social services basic to a decent quality of human life. This figure rises to nearly 3 billion, if a standard of $2 is used.[37] The success of the strategy to reduce the proportion of people living in poverty is contingent upon generating income-providing activities, augmenting access to resources necessary for livelihoods, building assets, and assisting the poor and the disadvantaged populations to manage risks.

Vulnerability to risks from stresses and shocks including illnesses, injuries, property loss, and premature death are everyday realities for the poor. Additionally, it is the poor people occupying marginal, dangerous, and less desirable locations to live and eke out livelihoods, who are hardest hit by natural disasters. In 2000, leaders of 189 nations agreed on eight Millennium Development Goals including their commitment to reduce the proportion of people living in abject poverty by 50 percent by 2015. Simultaneously, in the face of economic globalization, it has become necessary to think

[36] Allianz is one of the leading global services providers in insurance, banking and asset management. Allianz is working in more than 70 countries, and it is one of the five leading asset managers in the world. Allianz has demonstrated strong commitment to the broader goals of sustainable development.
[37] OECD. 2001. DAC guidelines on Poverty Reduction. Paris.

innovatively in order to reduce the vulnerability of poor people to shocks and stresses through provision of safety net mechanisms to manage risks.

Micro and small enterprises employ a significant portion of the labour force in developing countries, albeit in 'survivalist' employment and in the informal economy. The informal economy provides employment for the majority of people, particularly women, in the developing world. Besides providing low incomes, the informal economy does not provide any formal means to manage risk.

Many of the micro and small enterprises operate outside the legal system, and this also contributes to their low productivity. These enterprises lack access to financing and long-term capital, which is the basis for providing sustainability to all entrepreneurial activities. Additionally, the institutions that finance such enterprises are themselves prone to the risks of the borrowers, a fact that can constrain their going to scale. For instance, microfinance providers (MFPs) allow low-income entrepreneurs to borrow money and are therefore vulnerable to the same risk as their clients. In the event of a risk event striking borrowers or a family member, their ability to repay the loan is in serious jeopardy. While MFPs use several options[38] to protect themselves from the risk of non-payment, none of them is perfect.

Micro and small enterprises can be engines of growth, if they are developed to generate income and wages for their clients and support their transition out of poverty.[39] In addition, since reducing vulnerability is about risk management, risk management should be an intrinsic component of sustainable livelihoods. Microinsurance[40], though relatively new, provides such an option to the 'working' poor people. Microinsurance aims to provide protection to low-income people against specific risks and hazards in exchange for premium payments proportionate to the likelihood and costs of the risks involved.[41] At the same time, there is a need to explore safety net and insurance mechanisms that would, in particular allow poor people to alleviate the economic impact of natural disasters.

Informal mechanisms such as savings and other traditional risk management structures[42] have proven to be too costly and therefore unsustainable as long-term coping strategies.[43] While the private and formal sectors appear to be the most suitable to provide microinsurance products–as they can design and offer sustainable and long-term risk reduction strategies that are also profitable–this role is yet to be explored comprehensively both as a business model and as an intervention for social protection. It is equally important to understand how microinsurance relates to government policies and the role of the Government and the public sector in terms of creating an enabling environment, laying the foundation for its efficient implementation through developing capacity, strengthening institutions and infrastructure, and disseminating information for the development of microinsurance opportunities as safety net mechanisms.

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[38] Expect the group to repay; Try to claim from the estate; Write off the loan as a bad debt; Self-insure; Partner with an insurance company.

[39] Sievers, Martin and Paul Vandenberg. 2004. Synergies through Linkages: Who Benefits from Linking Finance and Business Development Services? SEED Working Paper No. 64. ILO. Geneva.

[40] Access to insurance reduces the vulnerability of households and increases their ability to take advantage of opportunities. Moreover, by reducing the impact of household losses that could exacerbate their poverty situation, insurance enhances the stability and profitability of households.

[41] Cohen, Monique and Jennefer Sebstad. 2003. Reducing Vulnerability: The Demand for Microinsurance. Microsave-Africa. Nairobi.

[42] Targeted savings and consumption loans including Rotating Savings and Credit Societies and savings clubs can help the poor to cope with day-to-day events, but as risks increase in magnitude and uncertainty, losses increase and simple savings and loan activities are unable to manage those losses. Brown, Warren (2000): Why MFPs are providing insurance to low income people? Dhaka.

[43] Kawas, Celina and Marla Gitterman. 2000. Roundtable on Microinsurance Services in the Informal Economy: The Role of Microfinance Institutions. The Ford Foundation. New York.

Microinsurance to manage risks for population with low incomes and low insured values has limited precedent. Although MFPs have demonstrated interest in participating in the microinsurance industry[44] as in fact many of the existing products have been defined for the clients of an MFP, it is critical that the finances and management of the insurance business are separated from the MFP's savings and credit activities. Part of the reason lies in the fact that the microinsurance product could have high transaction costs and the difficulties in controlling moral hazard and adverse selection. While households understand microfinance very well, their limited understanding of insurance that could lead to a bias against insurers. Microfinance providers may also be challenged by the need to achieve scale, and skills requirements for actuarial analysis, investment opportunities, and regulation.

MFPs have employed different strategies for providing insurance to their clients. For instance, institutions like SEWA or ASA in India,[45] in collaboration with national public insurance companies and private insurance providers such as Bajaj Allianz and GTZ, have provided integrated insurance schemes covering sickness, death, widowhood, maternity, and loss of flood, fire, and riots to its clients. MFPs in Uganda, in partnership with American International Group (AIG) have offered a group personal accident and credit life and disability policy in Uganda since 1997. The premium is bundled with the cost of auxiliary financial services into the MFPs' interest rates, or as a separate fee. Gaining from its experience in Uganda, FINCA International has offered the same AIG product in Malawi, the United Republic of Tanzania, and Zambia. A private insurance company, Delta Life Insurance, provides a combination of life and endowment microinsurance products, called Gono-Grameen Bima. CARD Bank in the Philippines, through its Mutual Benefits Association (MBA) has been offering life insurance policies with long-term savings. Canadian Cooperative Association (CCA) China has recently started a small pilot health programme consisting of an integrated health insurance approach for its clients. The programme is being supported by funds from the Canadian Government as well as client membership fees.

The lessons learned from the limited number of ongoing activities clearly emphasize that microinsurance is a highly technical operation, and that it is vital to better understand the market potential and efficient delivery of microinsurance services. Apparently none of the initial microinsurance ventures were preceded by any form of market potential study that looked at the demand and acceptability of the product, development costs, cost of premiums or their affordability based on a sustainable business model. Furthermore, none of the products launched until now were followed up, or included the education of clients, insurance service providers and other stakeholders, or disseminated relevant information on a broader basis. This is part of the reason why the client turnover rate in some of these initiatives has been large, and many of them have failed to show even a modicum of the potential profits microinsurance is potentially capable of. There is indeed a lot to understand prior to introducing microinsurance as a viable market initiative to help poor people cope with income erosion to reduce their vulnerability while providing a new business opportunity to forward-looking insurance companies.

Microinsurance is a nascent market. If microinsurance can be delivered in a cost-effective manner through MFPs and other civil society organizations, the significant numbers of their clients who are in need of insurance services per se represent a profitable segment for the insurance industry. Previous attempts to launch microinsurance products have quickly revealed some key factors for success in implementation:

- Products should be launched after a careful market study including qualitative consumer surveys;
- Products should be designed in close consultation with the stakeholders;

[44] Response to demand from clients, reducing household risk, protecting the institution, and an additional business opportunity.
[45] India is leading insurance industry expansion into emerging Asian markets. Both India and China are opening their enormous markets to overseas companies, which will create market expansion opportunities for the insurance sector.

- Information and knowledge of the products must be clearly communicated to and shared with the potential customers;
- Claims must be settled as quickly as possible;
- The transaction costs of delivery must be clearly understood, appropriately allocated, and minimized;
- The product provider must have considerable knowledge and experience of the actuarial side of insurance provision;
- Products must be launched sequentially starting with simple products (life/funeral, catastrophe insurance) and then moving into more sophisticated products such as health.

Hence there is a need to initiate market potential studies in a limited number of countries. It is also recommended that the outcome of the studies be implemented through timely, pilot, 'learning by doing', microinsurance initiatives that are based on sound business models and practices premised on well-defined market and comprehensive market analysis. It is hoped that the success of such smaller pilot initiatives would allow microinsurance initiatives to be taken to scale and achieve wider acceptance and validation. The pilot initiatives will also assist in delineating and creating an enabling environment, and putting it in place to ensure that the process is efficient and transparent with minimal transaction costs. In addition, the lessons learned from the pilots will provide a valuable estimate of the extent and nature of capacity development at the human, institutional, and system-wide levels that is required for local governments, civil society, and the private sector to make microinsurance a viable business.

The countries of interest would include India, Indonesia, and the Lao People's Democratic Republic. While India has a large number of existing microinsurance activities, Indonesia has an active microfinance and microenterprise system and intends to expand social security systems to the informal economy. In the Lao People's Democratic Republic, one of the group of the least developed countries, demand is high, and the Government already supports social health insurance. Additionally, in India the government policy directs the insurance industry to spend a certain amount of resources to improve the quality of life for poor people.

3. Objectives of the study

It is in the above context that the UNDP–Allianz–GTZ joint market research and exploration of microinsurance interventions in selected countries is being formulated. The first step is to review the existing experiences through a desk study and then undertake market-based studies in a limited number of countries to acquire a better knowledge and understanding of the potential for microinsurance and efficient delivery of demand-based products. It is hoped that the study would provide an evidence-based theory of change to make microinsurance a sustainable alternative for providing safety net mechanisms for poor and disadvantaged communities.

3.1 Overall long-term objectives

To substantiate linkages between microfinance, development of entrepreneurs and sustainable livelihoods through the availability and access to microinsurance by the workers in the informal sector.

Explore the use of microinsurance as a safety net mechanism to reduce vulnerability of livelihoods of the poor including impacts of climate-induced natural disasters.

Goals of this activity

- To estimate the demand for microinsurance in three countries of Asia.

- To estimate the potential supply of microinsurance in terms of risk takers (regulated insurers, governments, and others) and various delivery channels. This estimation will include a discussion of transaction costs for delivery of microinsurance services.
- To explore the option of undertaking pilot initiatives through the development of a basic process outline inclusive of estimated costs.
- To foster dialogue and cooperation between the insurance industry, governments, and civil society, and enhance North-South and South-South partnerships.

3.2 Benefits of UNDP–Allianz–GTZ collaboration

A joint study on microinsurance will benefit from the unique capabilities of the three partners. By virtue of extensive country offices and projects that work closely with developing countries' governments, the private sector, and civil society, UNDP and GTZ provide an in-depth understanding of national policies, institutions and capacities, an excellent ability to convene diverse stakeholders, and make available experiences from several microinsurance projects. Allianz, as a leader in the insurance market, brings the knowledge of insurance market structures and product design to the partnership.

4. Activities needed to generate outputs

The market study will explore options for engaging the insurance industry in providing microinsurance as a safety net mechanism for the developing countries by assisting in risk management and strengthening the development of local entrepreneurs and other poor and low-income groups within the overall framework of sustainable livelihoods and Millennium Development Goals (MDGs).

A team of three international consultants will complete the activity (one of the consultants heading the team). These consultants, knowledgeable about microfinance and microinsurance initiatives globally, will receive country-specific technical information from national insurance experts. This activity would also include discussions with other microinsurance providers in the country such as ICICI Lombard. These inputs will include desk activities such as briefings on the state of the market in the target country, as well as acquisition and provision of secondary data relating to the insurance industry, including: Insurance laws and regulations; insurance commission annual reports; microinsurance activities; and available studies on the sector especially those that relate to the low-income market. In-country experts will also provide access to any relevant documents and/or studies including those conducted by Allianz in the target countries, as well as assist in obtaining entry for interviews by the consultants as appropriate. The assistance of the insurer in the advisory capacity will be limited, in order to ensure the objectivity of the results and recommendations and broader viability of the market intelligence activities.

Further inputs are expected from UNDP, GTZ, and other organizations, if required. The studies will be conducted in teams of two with additional contribution by the national Allianz insurance experts to prepare a business plan for undertaking potential pilot projects in at least two countries jointly selected by the organizations who will fund the future projects (details are elaborated under para. 5).

In particular, the experts will analyse the lessons learned from prominent past and ongoing microinsurance activities globally, and prepare a comprehensive report for each of the three selected countries covering the issues addressed in the Terms of Reference provided below. The experts will ensure that the paper is cohesive, clear, forward-looking and uses out-of-the-box thinking to identify pathways for the implementation of policy and microinsurance incentives that promote cost-effective adoption of risk management strategies and have practical recommendations that can be implemented at the field level.

The paper will cover the following:

I. Landscape review

The research should glean critical lessons for enabling policy environment, barriers, and incentives for marketing microinsurance as a business product by engaging the insurance industry in partnership with the national governments, and capacity development demand for implementing microinsurance initiatives at the ground level. It should cover:

A. Literature review and analysis.
B. Relevant institutional and legislative frameworks.
- Available knowledge sources and networks including current providers of microinsurance at the ground level as well as the insurance companies that underwrite the microinsurance;
- Assess the most important risks and the vulnerability of poor and low-income groups and analyse the current risk management strategies applied by them.
- Analyse the options of risk management strategies available in the selected countries and identify the gaps of risk management tools (including linkages of microinsurance with national social security programmes).
- Identify successful microinsurance initiatives and evaluate the possibility for, and potential impediments to, their replicability;
- Identify market barriers to the adoption, use and sustainability of cost-effective microinsurance and risk reduction measures;
- Identify cultural and social barriers that hinder the widespread adoption and use of microinsurance and risk reduction measures;
- Identify institutional barriers (regulatory, governmental, development banking, legislative) to the integration of microinsurance and risk management and elaborate on relevant reforms supporting social security in the informal economy, if any;
- Identify demand centres of microinsurance as well as the areas for which microinsurance is most desired.
- Examine the role of microinsurance for reducing the vulnerability of low-income groups and on the development of local entrepreneurs.

II. Role of governmental, civil society, disaster community

Identify and evaluate government policies and strategies in place for providing an enabling environment for microinsurance at the state/community levels, and highlight important lessons; include funding sources, business prospects, etc.;

Identify community initiatives including microfinance-led initiatives to provide microinsurance to local clients. Highlight important lessons; include funding sources.

Define capacity development needs (human, institutional and system-wide) for implementing successful microinsurance initiatives.

III. Insurance/reinsurance industry: Market opportunities

Identify insurance industry market strategies (including products of interest) and ongoing initiatives to provide microinsurance and reducing vulnerability, and increasing physical and economic resilience (risk management, risk pooling, incentives, funds). Note vision, funding sources.

Assess the insurance products in the context of other risk management tools for poor and low-income groups (state-supported programmes and informal systems such as savings and credit products).

Identify partners (in the selected countries) who share a common vision and the desire to learn and implement the new product segment of microinsurance.

Qualitatively estimate potential demand and market potential for microinsurance (in three countries) including clients' comprehension of the concept of insurance, understanding of risks, and willingness and ability to pay according to different social and economic groups.

Provide present viable business propositions and recommendations for design and delivery of microinsurance products; broadly estimate the transaction costs including consideration of the capacities and institutional capabilities of microfinance and local development banks to deliver insurance benefits.

Identify development banking and commercial banking initiatives to provide microfinance and/or safety net mechanisms for the governments or communities to increase physical and economic resilience.

IV. Bilateral, multilateral, and other donor communities

Identify donor communities and their interest in microinsurance;
Identify risk pooling limitations and opportunities.

V. Action plan: Undertaking pilot interventions

Synthesize critical lessons learned from previous initiatives undertaken to determine both the key factors for success, and the barriers, and operational and institutional impediments, to the implementation of microinsurance strategies for risk management, risk transfer and risk reduction.

Identify creative and innovative pathways for advancing the implementation of policy and insurance incentives that promote cost-effective adoption of risk management strategies.

Identify areas in which funding support may be necessary, including linkage of microinsurance with development of local entrepreneurs.

Identify capacity development needs.

Planning meeting

In order to ensure that all parties are clear on the objectives, approach, and expected outputs, it is necessary to have all parties meet to plan this activity. Because of cost constraints, this meeting should take place as a teleconference with parties from Allianz, GTZ, and UNDP, as well as the core consulting team, Michael J. McCord, Monique Cohen, and Gaby Ramm. This meeting should take place before the first field visit.

Output

An output in the general form of a business plan will be provided for each country, following the basic outline below:

Executive summary
Includes a synopsis of the national strategic business plan that summarizes the highlights of the plan.

Vision/mission
Provides a snapshot of the present stage of microinsurance in the country, plus a picture of where the industry is going given Allianz/UNDP/GTZ intervention as suggested in the plan. Included will be summary of the goals, objectives, and requirements on how to get there.

Microinsurance overview
This section provides basic information about microinsurance in the country, including issues of: regulation, competition, social protection programmes, other government, private, civil society, and donor initiatives and plans that make up the structure of microinsurance and insurance in the country. This section will also include a discussion of key international lessons learned.

Demand analysis
In this section we will define the microinsurance market in the country, the general characteristics of the target market, assessment of current risks impacting the market, how the market currently manages these, and where there might be potential demand opportunities in terms of products and services. This section will also include consideration of the benefits of microinsurance over those of currently utilized risk management strategies. Finally, it will include a discussion of market risks to product introduction. Some specific information will include:

Existing risks experienced by low-income populations,
How poor people prioritize risk,
The strategies they use to mitigate risks ahead of time and to cope with shocks after they occur,
Significant differences in coping behaviour by gender.

Annex 1 provides a detailed explanation of the methodology for conducting the demand analysis.

Product/Service strategy
A detailed review of formal- and informal-sector microinsurance initiatives will identify:

- potential partnerships
- products
- interested MFPs, insurers, and others
- delivery channels
- transactional processes between the different organizations (agents and insurers)
- general potential product opportunities with a product development strategy
- additional research required
- potential relationship structure issues between different institutional partners
- capacity development requirements
- output indicators
- risks to the product(s) including governmental, regulatory, legislative, supervisory, environmental, cultural, and others.

Marketing/Market education plan
This section will discuss the marketing requirements of insurers, delivery channels, and the potential market. Some suggested areas of market education would be addressed based on lessons from the demand analysis. Delivery strategies will be addressed.

Financial plan
This section will include:

- a basic draft outline of the costs of testing and implementation.
- a discussion of potential profitability
- an estimate of additional donor/investor inputs required.

Support documents
This section includes a variety of additional documents to substantiate the plan.

6. Duration and costs

Country	Final product due on or before:
India	30 April 2005
Indonesia	31 August 2005
Lao PDR	31 August 2005

7. Qualifications and experience

The candidates should have an advanced degree in a field related to finance, insurance with an emphasis on microinsurance and microfinance and international development, and 10–12 years of professional experience in implementing such initiatives at the field level. Experience in dealing with issues of insurance, safety net mechanisms, or risk management at the level of government, civil society, communities, or the private sector is highly desirable.

S/he should have a good understanding and experience in the area of poverty alleviation, sustainable development, development of entrepreneurs and building partnerships between diverse stakeholders. The consultant should have a good knowledge base of MDGs and be well experienced in the role of insurance in reducing vulnerability and strengthening sustainable livelihoods. Excellent writing skills in English are necessary. The candidate should be able to function effectively in an international, multicultural environment. S/he must be fluent in both spoken and written English. Knowledge of other UN official languages is an asset.

Annex 1: Methodologies to be applied in demand research

Methodology:
Microfinance Opportunities will use the qualitative research methods it has developed and used in other microinsurance market research studies. These include focus group discussions (FGD), participatory rapid appraisals (PRA), and individual in-depth interviews.

1. Focus group discussions and participatory rapid appraisals

A variety of qualitative tools and techniques will be implemented including focus group discussions that address low-income populations' risks and risk management strategies, PRA tools including the life cycle, time series of crisis, seasonality of income, expenditures, savings and credit, and seasonality of risks. These will be used to investigate:

A. Risk and risk management strategies
Range of risks and the effectiveness of the coping strategies (indigenous/informal group insurance mechanisms, formal insurance and other instruments) used to address them.
Ranking of key risk in terms of the financial stress and lump sum cash needs to cope with them.

Changes in risks, their impact, and coping mechanisms over time.

Changes in cash flow, financial needs and prevalence of shocks in the course of the year.

Identification of vulnerability of and coping mechanisms used by different income groups.
Client use of financial services, including credit, savings and insurance to manage risk both before and after the event.

B. Client satisfaction with existing insurance schemes for poor households
FGDs will be held with members, ex-members, and non-members of existing insurance schemes for poor households in order to learn about the level of satisfaction with and understanding of these products.

Individual interviews
In-depth interviews will be held with key informants who are members of indigenous, informal, group-based insurance schemes or who are policyholders with existing insurance schemes. Individual interviews

will also be used to explore the demand side issues related to affordability. This will generate information for the purposes of learning more about:

Indigenous/informal insurance schemes and the importance and use of savings and loans to manage risk
Interviews will be held with key informants to ascertain the use of indigenous insurance schemes and the use of savings and loan products to manage risk.

Information related to the demand for microinsurance products
The AIMS/SEEP loan use tool will be used to investigate the use of savings and loans by microfinance clients to cope with key risks. These interviews will identify clients' pre-existing financial obligations in order to determine their willingness and ability to pay for microinsurance.

Appendix V: List of People Met

People visited in Indonesia:
Jakarta and vicinity

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Ms. Ahmir ud Deen	Managing Director Employee Benefits	Allianz Life Indonesia	amir.ud.deen@allianz.co.id	www.allianz.co.id	T=62-(0)21-5299-8888
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Mrs. Yustiana Mustafa	Consultant	Bumiputera			T= 62 (0)21-4722358

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Banda Aceh

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Appendix VI: Comments on Aceh and Microinsurance

On December 26, 2004, the area of Aceh suffered a terrible tsunami that killed many thousands of people and destroyed large amounts of property. The situation there was dire, and much of the world community stepped up to help. During the work in Indonesia, one team member spent about one full day in Aceh to review the situation and look for options for microinsurance and also for a worthy activity on which to spend $1 million promised by one of the funders of this project.

Aceh was still clearly in a state of clean-up and refugee management, and had not yet turned the corner towards focusing on development. Most of the people there were emergency specialists, and the development specialists had yet to arrive. This was interesting given that the Government had recently asked UNHCR to leave, judging the refugee crisis to be over.

Institutions were starting to be given some direction, since the Government had set up an office and officials to coordinate the Government's objectives. This happened in May, over four months after the crisis. With government representatives present in Aceh, many of the major donors were hoping for more guidance.

And there they were, waiting with sacks of money to help in the rebuilding of Aceh and the other affected areas. Many hundreds of millions of dollars were waiting, poised for final decisions about how the rebuilding would occur.

It was clear that many houses would need to be built or repaired. One thought for microinsurance was to insure the building loans, and to use the donation money to fund inspectors that would ensure that proper building standards were followed to limit the potential for future damage. It was initially seen as necessary that the donation money should in some way support the commercial microinsurance operations. This strategy created benefits on many levels. It was learned, however, that the Government would rebuild and repair the destroyed and damaged homes. As of May 2005, the Government had agreed to pay IDR10 million for basic damage, IDR20 million for a substantially damaged home, and IDR28.8 million for a destroyed home. It was thus expected that there would be no housing loans, and thus it would be very difficult to sell house insurance.

The potential for microinsurance in general in Aceh is somewhat ripe. People have seen disaster and have seen some insurance companies pay claims responsibly, yet have also seen others that still had not settled claims while the claimants are still living in refugee tents. Microfinance will get a large boost from the development activities that will ensue as numerous donors begin to pour their contributions into the area. As microfinance develops, and people begin to return to business development, it is likely that a reasonably strong demand for microinsurance will ensue. A good partner there would be Mercy Corps, which has already been working to get banks to move downmarket. Linkages with other technical assistance programmes may also prove effective. Rather than aggressively pushing microinsurance in the early reconstruction period, it will be important to promote the benefits of insurance throughout the market so that the environment is ready for the products when offered. Thus, linkages with many of the development agencies and projects may help prepare the market. If possible, microinsurance information and general financial education should be provided as part of almost any training programme being offered in and around

Aceh. Although we did not do demand research there, it is expected that the demands will be similar to the results presented above.

Also, the ADB has a major project starting that includes microinsurance. It would be good for insurers to try to connect with that effort.

Donation money is flying into Aceh, and there can be some linkage benefit to microinsurance. Some suggestions:

- Because health insurance is typically constrained by poor-quality health care, an investment in improving the hospitals in that area may prove beneficial;
- Often one of the highest causes of death in microinsurance programmes is road accidents. With reconstruction of roads, there could be an investment in reducing the likelihood of road accidents, such as through signage, speed bumps, and better road design;
- Because there is an expectation of other major earthquakes in the area, an investment could be made in expanding the reach of early warning systems so more people can be prepared in the future;
- There is a significant problem with inflation in the Aceh area especially with regard to building materials given that the demand is, or will be, huge for limited resources. An investment could be made in the construction and start up of brick factories around Aceh to help increase the supply of bricks and thus potentially result in lower prices. This would help everyone.

Aceh has potential as a market for microinsurance, and efforts should be made to direct donor activities to recognizing this so that the new Aceh will have some protection behind it.