Social Protection Project Briefs




Developing the Microinsurance Sector in Sri Lanka

Social protection in Sri Lanka is covered by the formal system of social security and social security services provided to informal sectors by institutions such as nongovernment organizations (NGOs) and/or community-based organizations. While most people in Sri Lanka have basic security in food, health, and housing, ensuring income security during old age remains a major challenge. Only about 36% of the working population is covered in one or more formal schemes.[1]

Microinsurance Sector in Sri Lanka

The insurance industry is regulated and supervised by the Insurance Board of Sri Lanka under the Regulation of Insurance Industry Act No. 43 of 2000 (RII Act). The Agriculture and Agrarian Insurance Board created under the Agriculture and Agrarian Act provides microinsurance services to small-scale paddy cultivators and livestock farmers. On the other hand, the Social Security Board of Sri Lanka established under the Social Security Act provides pension and social security benefits to its members. While several insurers registered under the RII Act are offering microinsurance products, these products do not include any survival benefits to policyholders. A few NGOs provide microinsurance services to poor households at affordable prices but operate outside the law of insurance.[2]

Microinsurance in Sri Lanka started as a service to support the microfinance sector initially focusing on providing loan protection insurance and life savings. Eventually, this developed and provided wider range of insurance services extending to welfare and health products. Recently, commercial insurance companies started to operate microinsurance businesses.[3]

Challenges for the Microinsurance Sector

As in the case of other countries, there are no special regulatory provisions for microinsurance in Sri Lanka. The RII Act does not include any provision on the regulation and supervision of mutual insurance companies.[4] There is therefore insufficient focus in institutions and regulations on the promotion of microinsurance. Furthermore, due to high administrative costs, registered insurers are unwilling to market affordable microinsurance products to the low-income sector. This has partly contributed to a concentration of the insurance market in the upper- and middle-income groups and the scarcity of services to the lower-income segment of the population.

The perceived low capacity of poor households to pay premiums also discourages insurance companies. As a result, a vicious cycle has been created—the poor and low-income households know little about insurance services and thus have limited demand for those services, consequently contributing to the lack of interest among insurance companies. However, cost-effective means of delivering affordable insurance services can be developed by linking insurance services to microfinance operations.[5] Microfinance institutions (MFIs) can serve as a valuable and effective link to providing microinsurance because

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they have an established institutional framework, are close to the target group, and have gained people's trust. Many MFIs in Sri Lanka are already involved in microinsurance in one way or the other.

Effective microinsurance services complemented with other financial services like credit or savings are considered to offer more concrete protection compared to other social protection mechanisms such as the government's income supplementation scheme or community-based mutual associations.

Without insurance, the poor may be inclined to engage in activities and invest in asset portfolios with low risk but low returns, which may affect their long-term income and their ability to rise out of poverty. Furthermore, household shocks such as illness or death of a family member may have long-lasting effects: productive assets may be destroyed or sold for survival, health may be undermined, or children may have to leave school. As such, reduced risks through effective insurance services may not only induce investment in economic activities but also reduce the welfare costs to society.

Correspondingly, there is a need to review and amend the policy to focus on promoting microinsurance based on successful international experiences,[6] so that MFI-NGOs can actively participate in life savings, and other forms of insurance without compromising the stability of the sector.

Technical Assistance for Microinsurance Sector Development[7]

The Asian Development Bank (ADB) provided technical assistance (TA) to the Government of Sri Lanka primarily to formulate an integrated framework for the development of the microinsurance sector through favorable policies and sector-wide institutional capacity building. The TA is expected to improve risk mitigation and reduce the vulnerability of the poor and low-income households in Sri Lanka by facilitating access to affordable life and general insurance products. It is primarily focused on conflict- and tsunami-affected areas to support the reconstruction of affected people.

The TA involves two phases: phase 1—a policy and legal review, and phase 2—an awareness campaign and pilot microinsurance scheme. The results of the policy review and market assessment will be widely disseminated through in-country workshops with government agencies, insurance companies and brokers, microfinance institutions, MFI-NGOs, and donors, and published through print and online media.

An important outcome of the TA would be an improved understanding of microinsurance as an effective means of poverty reduction by the government, insurance industry, MFI-NGOs, and grassroots organizations. With better knowledge of the needs of poor and low-income people and the demand for risk mitigation, microinsurance service providers as well as other potential service providers can have a better knowledge of the needs and demand for risk mitigation of the poor and low-income people, and effectively provide services in response to those needs. The awareness campaign to be organized in pilot areas will also help those in poor and low-income households understand and appreciate the benefits of insurance systems.

The TA consultant's second interim report[8] includes a review and analysis of insurance laws and regulations in Sri Lanka to determine their adequacy for the development of the microinsurance sector. Based on the review, certain legal amendments to existing insurance laws and regulations were recommended to promote microinsurance in Sri Lanka.

According to the report, while insurance laws in Sri Lanka require all microinsurance providers to operate under the supervision of a regulatory authority, stringent conditions imposed by the regulatory authority on the insurers may hinder rather than promote the growth of insurance services. Hence, the regulatory framework should also consider the characteristics of different microinsurance providers, the environment under which they operate, and the target population to whom microinsurance products are offered.

It was also suggested that a means to promote microinsurance services is to make it obligatory for registered insurers to market affordable microinsurance products to low-income households through a provision under the RII Act or any of the two delegated instruments, such as "Rules" as prescribed by the government or "Determinants" as formulated by the Board. Another recommendation is to direct insurers to sell a percentage of their insurance policies to low-income households as determined by the Board.

The implementation of the ADB Microinsurance Sector Development Project facilitated a change in the attitude of insurers' regulators, MFIs, and other community-based organizations toward microinsurance. There has been a realization that the vision of microinsurance extends beyond simply providing loan protection cover to the holistic achievement of mitigating risks for the poor and reducing their vulnerability toward risks of life. Furthermore, conducting the extensive microinsurance awareness campaign has also helped convince the poor that microinsurance is an acceptable, affordable, and useful technique for mitigating risks.[9]

Endnotes

[1] Wiedmaier-Pfister, M. and E. Wohiner. 2004. *Microinsurance Sector Study in Sri Lanka.*

[2] ADB. 2006. *Technical Assistance Consultant's Report-Second Interim Report on Sri Lanka: Microinsurance Sector Development.* Manila.

[3] Abeysinghe, L.B. 2007. Strategies to Extend Commercial Insurance to the Poor—Country Experience. Presentation on ADB Seminar on Microinsurance Sector Development Project in Sri Lanka. Colombo.

[4] Footnote 2.

[5] SANASA ALMAO Insurance Company Co., which serves poor and low-income households, offers life insurance products to members of the SANASA credit cooperative. Most of its clients are low-income households with an average monthly income of up to SLRs7,000. Their insurance benefits depend on the premium that they are willing to pay.

[6] The Philippines, for example, has lowered the capital requirements for mutual aid schemes, while Jordan has relaxed the licensing conditions for insurance agents and nongovernment organizations.

[7] ADB. 2006. *Technical Assistance to Sri Lanka for Microinsurance Sector Development* (TA 4761-SRI). Manila.

[8] Footnote 2.

[9] Footnote 3.

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