



REINSURANCE ARRANGEMENTS FOR THE BOTTOM OF THE PYRAMID PRODUCTS

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Introduction

- Definition of Bottom of the Pyramid
 - Largest but poorest social economic group
 - Found in Urban and Rural areas
 - Generally refers to people who live on less than \$2.5 per day. (Kshs200 to Kshs250)
 - Mainly engaged in farming and in the informal sector
 - 75% of working Kenyans make their living from farming (2006 statistics by Swedish Cooperative Society)



Introduction – contd.

- Activities of the informal sector include:
 - Selling fruits and vegetables
 - Food operation, sale and processing,
 - Selling clothes and shoes (both second-hand and new)
 - Kiosk selling various items
 - Water kiosks
 - Small retailers or hawkers who sell cereals, home suppliers, fuels and other goods.
 - Small manufacturing, production, construction and repair of goods.

(World Bank, 2006, p.32-33)



Introduction – Contd.

- The BoP are exposed to day to day living risks which affects their survival
- The people in this category have no Insurance protection
- Hence, there is a need to focus on this group for mutual benefit



Covers Provided in BoP Products

- Credit Life
- Funeral / Last Expense
- Term Life
- Personal Accident
- Savings Life
- Hospitalization
- Property Insurance
- Agriculture



Features of BoP Insurance Products

- Simple Products
- Easy to understand and administer
- Large number of insured members that cut across different geographical location and occupation
- Cover is sometimes extended to family members
- Small Sum Assureds
- Small Premiums
- Bouquet of benefits
- Generous underwriting requirements for insured member
- Group Underwriting (Location, Occupation, Lifestyle)



Risk Exposures of Insurers

- Individual Risks
 - Lifestyle risk
- Accumulation Risks from one event
 - Location risks
 - Occupation Risks
 - Concentration Risks
- Accumulation of Losses in any one year
 - Total portfolio risk
 - Profitability risk



Reinsurance

- Transfer of liability from the primary insurer to another insurer basically for financial stability.
- Financial instability of BoP schemes has been linked to various factors.
 - Poor program design
 - Weak implementation and management
 - Catastrophes
 - Limited Capacity – Individual skill and organization



Reinsurance Options for BoP Schemes

- Quota Share
- Stop Loss
- Catastrophe Excess of Loss
- Reinsurance Pool



Quota Share

- This is an arrangement where Reinsured and Reinsurer share each and every risk in a pre-determined proportion.

- Features

- Simple to administer in terms of Premium and claims
- Performance experience is the same for Reinsured and Reinsurer
- Higher Commission to offset part of procurement cost
- Reinsurance is on the basis of original terms



Advantage of Quota Share

- A substantial part of the Reinsured cost is recovered through high Reinsurance Commission
- The Reinsurers contribute its proportion towards each and every claim
- Joint approach to handle challenges since Reinsured and Reinsurer have the same experience and proportionate stake.
- Ideal for new business area where there is little or no experience



Stop Loss

- This is an arrangement that protects the Reinsured against an aggregate amount of claims over a period (usually one year), in excess of a specified percentage of the earned premium income, subject to an upper limit.
- E.g. 50% of EGNPI excess of 110% of EGNP
- If EGNPI is Kshs100 million, the cover would be Kshs50 million Xs of Kshs110 million



Features of Stop Loss

- Protects the portfolio, Product or class of business against further loss beyond a certain limit.
- It does not cover individual claims
- The cover is for a period of one year
- Rate is based on rate on line (Premium/Limit) or Pay back or amortization period
- No Reinsurance Commission
- The Reinsured pays all the claims within the year up to the attachment point (i.e. 110%)



Features of Stop Loss – Contd.

- The Reinsurer pays the excess above the attachment point
- The liability of the Reinsurer within the year is limited to a stated maximum amount
- There could be co-reinsurance where the Reinsurer pays less than 100% of the loss above the attachment point. (usually 90%)
- It does not guarantee underwriting profit. The Reinsured would have made losses before the Reinsurer steps in



Merits of Stop Loss

- It protects the Reinsured against fluctuating loss experience from year to year.
- Ideal for products that have good performance record
- Cost of reinsurance is lower
- It can enhance rapid build-up of reserve for the product if the experience is good



Catastrophe Excess of Loss

- This arrangement protects the net account of the Reinsured against risk of accumulation arising out of one event.
- There could be reinsurance protection for the individual losses, but the severity of loss on the retained portion of the individual losses, due to accumulation, may be very high.



Features of CAT XL

- There is an attachment point related to the number of individual claims that must arise out of one event
- The Reinsurer pays the excess above the attachment point up to an agreed maximum
- Premium rate is based on the Reinsured's Net retained sum at risk
- There is premium adjustment at the end of the year based on actual net retained sum at risk



Merits of CAT XL

- It protects the Reinsured from the effect of claim accumulation from one event
- It stabilizes the operating results for both losses and cost of the Reinsured
- It helps in the distribution of the Reinsured's risks



Reinsurance Pools

- Insurers and Reinsurers create a common fund for Micro-insurance Products
- Members subscribe to shares in the pool
- Members cede and receive business from the pool
- Members share aggregate claim according to proportions of their liability.
- Profits, losses, and expenses are shared in the same way.
- A Manager is appointed for the pool
- The pool may be further protected by a reinsurance treaty



Advantage of Reinsurance Pools

- It creates capacity to handle risks of a catastrophic nature like Micro-insurance
- It is ideal where gaps exist in technical skills and knowledge
- It helps to build up data on the risk from a wider perspective



Challenges of Reinsurance Pools

- Management issues
- Members may not show commitment to the pool
- There may be no confidence in the security offered by the pool



Suggested Mix

- Quota Share
- Catastrophe Excess of Loss

- Combining the good features of these two will provide adequate protection for the Reinsured.



Information Required for Reinsurance

- Location of insured members
- Occupational groupings of the class
- Number of members covered according to location and occupation
- Benefits offered by the BoP Product
- Range of sum assured for each benefit
- Premium rate and basis of ratings based on the benefits provided



Information Required – Contd.

- Any past experience – Premium and Claims
- Structure or model of the BoP product
 - Associations
 - MFI's (Micro-finance Institutions)
 - Banks
 - Suppliers
 - Direct Agents



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