International Labour Office

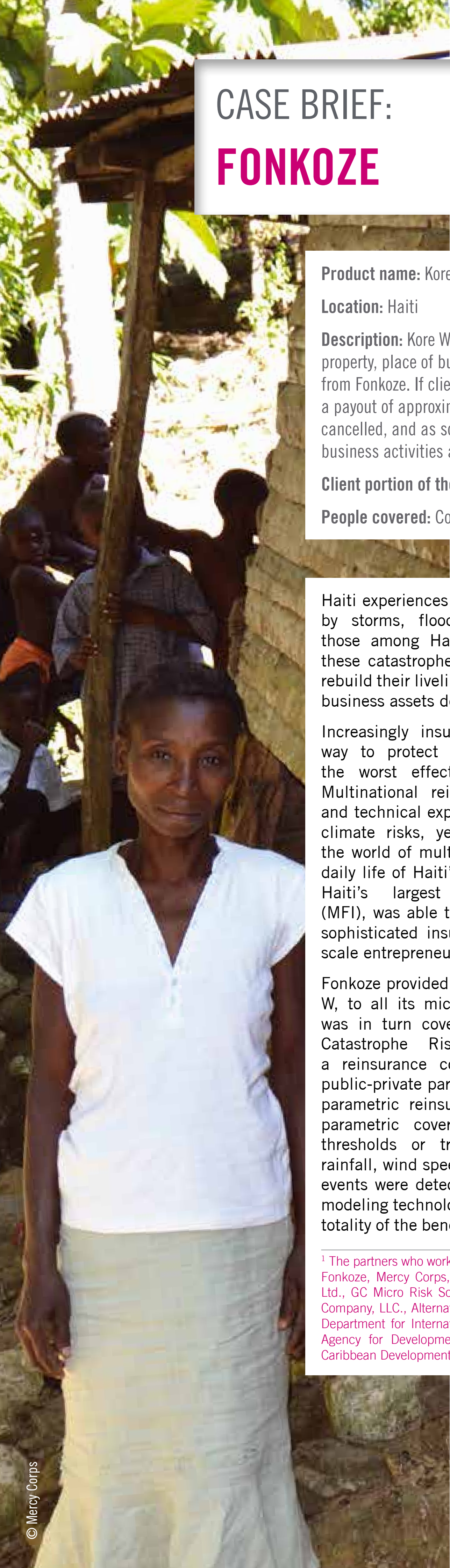
CASE BRIEF:

FONKOZE

Miguel Solana and Alice Merry

micro Insurance Innovation facility

PROTECTING THE WORKING POOR



CASE BRIEF:

FONKOZE

Product name: Kore W

Location: Haiti

Description: Kore W protected small entrepreneurs in cases where a natural disaster destroyed their property, place of business or business inventory. The product was compulsory when clients took out a loan from Fonkoze. If clients suffered damage as a result of a natural disaster, they were entitled to receive a payout of approximately US$ 125 to help them to deal with the loss. Their loan with Fonkoze was also cancelled, and as soon as they were ready, they were able to take out a new loan to help them begin their business activities again.

Client portion of the premium: 3 per cent of the loan amount

People covered: Compulsory for all of Fonkoze's microcredit clients (60,000 by end of 2012)

Haiti experiences regular catastrophes caused by storms, floods and earthquakes. Even those among Haiti's poor who live through these catastrophes face severe difficulties to rebuild their livelihoods with their property and business assets destroyed.

Increasingly insurance is being seen as a way to protect low-income people against the worst effects of such climate risks. Multinational reinsurers have the capacity and technical expertise to take on these large climate risks, yet a chasm exists between the world of multinational reinsurers and the daily life of Haiti's most vulnerable. Fonkoze, Haiti's largest microfinance institution (MFI), was able to serve as a bridge between sophisticated insurance solutions and small-scale entrepreneurs.

Fonkoze provided the insurance product, Kore W, to all its microcredit borrowers. Fonkoze was in turn covered by the Microinsurance Catastrophe Risk Organisation (MiCRO), a reinsurance company set up through a public-private partnership.[1] MiCRO purchased parametric reinsurance from Swiss Re. The parametric cover paid out when specific thresholds or triggers were exceeded for rainfall, wind speed, or seismic activity. These events were detected through satellite and/or modeling technology. MiCRO paid Fonkoze the totality of the benefits from the parametric and basis risk covers, minus a deductible for the basis risk cover of 15%.

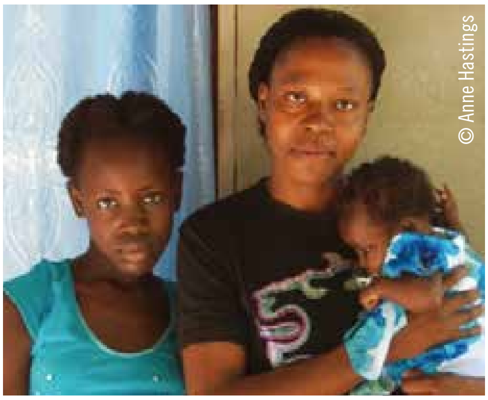
THE ROLE OF THE MFI

It is very common for insurers to sell microinsurance through MFIs. Yet Fonkoze's role was much broader than usual. The insurance product was integrated into the credit product through an automatic premium of 3 per cent of the loan value. However, the insurance product also made use of the MFI's infrastructure at every level, including distribution, educating clients and assessing, servicing, and paying claims.

It would have been impossible for Fonkoze to have sent central staff to assess the damage experienced by each of its clients in remote locations across the country. It therefore made use of Centre Chiefs – borrowers elected by their centre to perform a number of duties on its behalf in that area. For the insurance claims assessment, Centre Chiefs visited each client to record the damage that they had experienced, filled out forms to record the claims, and reported them to the nearest Fonkoze branch.

Initially, specially trained management staff also visited the centres after a disaster to review the reports filed by the Centre Chiefs and help the centre reach a consensus about which claims should be paid. However, the process was too slow, and not suited to deal with many large events in a short time. It took an average of 44 days for Fonkoze to pay claims in 2011. A MILK brief produced by the Microinsurance Center suggested that the delay in paying

[1] The partners who worked together to launch MiCRO included Fonkoze, Mercy Corps, Swiss Re, Caribbean Risk Managers Ltd., GC Micro Risk Solutions® division of Guy Carpenter & Company, LLC., Alternative Insurance Company (AIC), the UK Department for International Development (DFID), the Swiss Agency for Development and Cooperation (SDC), and the Caribbean Development Bank (CDB).



"Kore W is such an important tool. It really is a big deal for us to know that we can stand up quickly after a natural disaster has passed. We can continue to live and hope and feed our kids." - Guerda Pierre, a Fonkoze client and Centre Chief

claims was eroding the value of the product as clients still had to resort to informal financing while they waited to receive payouts.

In its second year of operation frequent and severe disasters strained the claims process. Kore W paid out to almost 28,000 clients as a result of multiple events that struck the country that year. This included tropical storm Isaac (in August 2012) and hurricane Sandy (October 2012). It was difficult to send just 11 specially trained management staff to over 1,100 centers affected by the disasters, and waiting for them to facilitate decisions inevitably delayed claims. As a result, when hurricane Sandy struck, Fonkoze decided to drop the requirement for management staff to carry out facilitation meetings with the centres. By this time Centre Chiefs had become much better at evaluating damages and submitting the claims. As long as they identified fewer than half of the clients as victims, the claims were paid without further investigation. Clients could still call a toll-free line if they were not satisfied with the claims process.

LESSONS FOR THE FUTURE

By 2012, the value of the product for clients was increasingly clear,[2] and many improvements had already been made. Nonetheless, as a result of the severe series of disasters in 2012, the product was stretched to its limits financially. During its first year, the payouts to Fonkoze from the parametric policy matched very closely the amount Fonkoze paid out to its clients for the damage they suffered. However, during 2012 its clients suffered significantly higher losses than were recognized through the parametric policy. Both Swiss Re and MiCRO had established annual overall limits on how much they would pay, but Fonkoze's commitment to its clients was unlimited. Though its losses were ultimately offset by grants, Fonkoze was forced to stop offering Kore W in its existing form for the time being.

Although the product is currently not being distributed in Haiti, MiCRO is preparing to offer a catastrophe microinsurance product in other countries in Central America and the Caribbean. These schemes can learn a great deal from Fonkoze's experiences. Parametric products are new and payouts may not yet accurately reflect the damage experienced. The MFI cannot accept the level of risk that Fonkoze faced. Substantial time and capital is therefore needed to fully test and refine a parametric product, and to ensure all parties are sufficiently protected.

Fonkoze also demonstrated that MFIs can be a powerful channel to provide catastrophic insurance to low-income people. Their close relationship with clients made them well placed not only to enrol clients, but also to assess, service and pay claims, as well as to build trust and understanding among clients.

"I am convinced that low-income people require a number of different tools to manage the risks they face. Insurance is one of the most important. We haven't gotten it right yet, but I am not giving up yet either." – Anne Hastings, Director, Fonkoze Financial Services

[2] Milk Brief #23

INSURANCE MAKES CLIENTS MORE LOYAL TO THE MFI

Mandatory catastrophe microinsurance cover linked to a credit product can improve the performance of an MFI by protecting its portfolio and reducing the client drop-out rate. In the first year that it provided Kore W to its clients, Fonkoze's drop-out rate was the lowest in its history, at 10 per cent compared to previous rates of between 20 and 25 per cent. Furthermore, insurance payouts had a significant effect: in branches where no clients received insurance payouts, the drop-out rate was 14.1 per cent, whereas in branches where a portion of the clients received payouts, the drop-out rate was only 8.7 per cent.

Fonkoze also wanted to know whether claim rejections were alienating clients. It therefore carried out a brief analysis of retention rates among clients who had submitted a claim but were refused. Overall, 84 per cent of these clients took out another loan. Fonkoze's experience therefore suggests that adding mandatory catastrophe cover does not undermine credit activities and can even increase client loyalty.

Housed at the International Labour Organization's Social Finance Programme, the **Microinsurance Innovation Facility** seeks to increase the availability of quality insurance for the developing world's low income families to help them guard against risk and overcome poverty. The Facility was launched in 2008 with generous support from the **Bill & Melinda Gates Foundation** to learn and promote how to extend better insurance to the working poor. Additional funding has gratefully been received from several donors, including the **Z Zurich Foundation** and **AusAID**.

See more at
www.ilo.org/microinsurance