Division 41
Financial Systems Development

Microinsurance Sector Study

Sri Lanka

Deutsche Gesellschaft für
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LKR 115 = EUR 1
LKR 97 = USD 1

1. Background, objectives and limitations of the study

1.1 Background

Donor agency interest in microfinance as a method for combating poverty has grown greatly since Consultative Group to Assist the Poorest (CGAP) was founded in 1995. By providing credit for increasing income earning opportunities, and providing savings to build up resources that can be called upon in emergencies, microfinance institutions have played an important role in reducing poor households' vulnerability to misfortunes. Losses though can go well beyond what loans and savings are able to deal with, and even insurance solutions for the poor - microinsurance - are needed. Within CGAP, a working group on microinsurance was established in early 2002. German Technical Cooperation (GTZ) is an active participant in the working group[1] and one of three national development agencies that are funding a 2-year project on Good and Bad Practices in Microinsurance, 2003-4.[2] Apart from, but complementary to the aforementioned Project, GTZ has commissioned this Sector Study on Microinsurance in Sri Lanka in order to obtain information about the environment for microinsurance, the existing supply and demand, as well as the role of donor assistance in this field.

1.2 Objectives

The goals of this sector study are to:

- Analyse the status quo for low income people in the insurance sector, and to give an inventory of all relevant bodies including government, private insurance companies, NGOs, and MFIs
- Present the activities of donors in the insurance sector
- Identify entry points for German Development Cooperation

1.3 Limitations

The Methodology section of the Terms of Reference called for an empirical survey to be done in order to get a better understanding of the demand side for microinsurance. While certainly desirable, the consultants quickly realized that a well considered, representative, and carefully carried out survey would require considerably more time and resources than were available on this mission. We also quickly understood from the review of documents and early meetings that we could obtain a reasonably good understanding of the demand situation from secondary sources. If necessary, a comprehensive demand study can be carried out later.

1 and heading the sub-group on the regulation of microinsurance

2 The project is being administered by International Labour Organisation's (ILO) Social Finance Unit.

2. Sri Lanka

The island country of Sri Lanka, then known as Ceylon, gained independence from British rule in early 1948. Located just south of India, the country has a tropical climate and occupies an area of 66,000 square kilometres. Though still classified as a “developing country”, Sri Lanka’s 19 million inhabitants have achieved a high literacy rate (92%) and educational level, good longevity (73 years on average), and a low rate of population growth (1.5%). Although health expenditures are relatively low (only EUR 26 per person annually, or 3.5% of Gross Domestic Product (GDP), health indicators are the best in South Asia and quite good in an international perspective.

74% of the population are Singhalese, 18% are Tamil and 7% are Moors and Malays. Major religions are Buddhism 69%, Hinduism 15%, and Islam and Christianity each 7%. Languages are Singhala, Tamil and English. The latter is spoken widely throughout Sri Lanka, at least by someone in every area except in remote villages.

The single most important constraint to economic growth in recent years was the armed conflict from 1983 until early 2002; the cessation of active hostilities has led to rapid improvements. Per capita income in 2002 was LKR 83,382 (now equal to EUR 725/USD 963). Real GDP is currently (2nd quarter 2003) growing at 5.5% (2.6% a year earlier); inflation is at 4.3% (11.7% a year earlier); the weighted prime interest rate is 8.87 % (12.66% a year earlier); and unemployment stands at 8.7% (unchanged). Tourist arrivals have increased dramatically (by 24% during the first 10 months of 2003 compared with a year earlier). Exports are led by textiles (51% by value); tea (14%); other agricultural produce (6%); machinery, mechanical and electrical equipment (6%); rubber products (4%); and diamonds and jewellery (4%). Services accounts for 54% of GDP, industry for 27% and agriculture for 19%. The most significant growth in the recent past has been in telecommunications, banking and insurance. Net inflow of foreign private remittances by 1.2 million Sri Lankans residing abroad amounts currently to 7% of GDP, and is important in balancing the net trade and payments deficits.

Government poverty reduction strategies have long been an important element in the economy. In more recent years, deregulation and privatization have played important roles in government policy. Small and Medium Enterprises (SMEs) have a vital role in the economy.

3. Microfinance

3.1 The Microfinance sector in Sri Lanka

The formal[3] microfinance sector in Sri Lanka comprises commercial banks (mainly People's Bank, and Hatton National Bank), the National Savings Bank, Regional Development Banks and SANASA Development Bank, which together have almost 900 branches. The semi-formal[4] MFIs are the over 300 Cooperative Rural Banks (CRBs) with 1,196 outlets; approximately 8,500 thrift and credit cooperative societies (TCCS, or Sanasa); 970 Samurdhi Banking Societies; approximately 200 local or international NGO-MFIs; numerous government rural credit programmes; pawnshops; and over 4,000 post-offices that collect savings. Informal, or non-institutional service suppliers are also numerous. Some of the most important ones include: savings associations, rotating savings and credit associations, funeral or death-benefit societies, traders, moneylenders, input suppliers, friends and relatives.

The microfinance sector in Sri Lanka suffers from major weaknesses and is subject to a number of serious threats. However, there is also no doubt about its strength and great potential. On one hand, it is highly fragmented, with a great diversity of institutions and programmes. Government involvement and subsidies are still common, and politization adds to these problems. The sector in general suffers from weak governance, poor repayment rates, high transaction costs, recurring losses and significant deficiencies in regulation and supervision. Commercial banks have made some efforts to serve the poorer population; however, one suspects that these efforts are merely to boost their image. In addition, it is questionable whether the (state-owned) People's Bank, which has been a valuable service provider in the rural areas, will be able to continue its work. Privatisation could bring about a change of policy towards the poor.

On the other hand, amongst the large number of Microfinance Institutions (MFIs), some promising institutions exist. A few non-governmental organisations (NGOs) are on the edge of becoming operationally self-sufficient and are beginning to seek commercial refinancing. Institutions like the thrift and credit cooperatives (organized in Sanasa), or the Cooperative Rural Banks have been reaching out to many poor and rural-based families. Some of them have the potential to become leading agencies in the cooperative movement.

The microfinance sector has received significant government and foreign support in the form of financial and technical assistance. However, best practices are only recently finding their way into microfinance in Sri Lanka. Amongst these, the most important one is the plan to transform MFIs into regulated intermediaries. There are high expectations that

[3] Those institutions supervised by the Central Bank of Sri Lanka (CBSL).

[4] Those established under secondary rules of various legislation but not supervised by the CBSL.

the new regulatory framework[5] will help to overcome the structural deficiencies of the sector in the years to come.

It is expected that the larger MFIs that are oriented towards financial self-sufficiency will come under the law. This should do away with the un-sound practise of savings mobilization by non-regulated MFIs, contribute to a streamlining of institutions and practices, and thereby, ensure the sustainability of the institutions. This will lead to a better provision of customer services.

The manifold efforts to strengthen micro and rural finance in Sri Lanka are not currently satisfying the huge demand for such services. When it comes to credit, a significant percentage of funds are untapped due to narrow disbursement conditions, such as limitations on regions and/or target-groups and the demand for guarantees, which are often impossible for the borrowing institution to provide. Savings services are widely offered, but often only as compulsory savings; or by unsupervised institutions, a serious threat to customers' funds. As international remittances comprise a significant share of GDP, MFIs also have a market here, but there is little experience. The range of insurance products offered by MFIs is very limited, generally not adequate for the needs of lower-income households and often on a limited project basis (e.g. a NGO receives donor funds for a women's health project).

3.2 Microfinance and its link to Microinsurance

From a conceptual point of view, microfinance institutions can provide a valuable link to the provision of microinsurance. MFIs have important strengths: they have an established institutional framework, are close to the target group and have gained peoples' trust. They have experience in social mobilisation and group methodologies, which can reduce the transaction costs of the insurance provision. They have a vested interest in delivering microinsurance due to cross-selling considerations (i.e. to improve efficiency and tap new sources of income), and because insurance reduces the financial risk for the borrower and the lender. In addition, MFIs can be used for the implementation of demand studies and awareness creation campaigns. Finally, some microinsurance products have a strong savings character (e.g. individual life-insurance, education insurance, other endowments, etc).

In Sri Lanka, the above-described conceptual "strengths" of MFIs as insurance providers can be observed as in many other countries. However, in practical terms, MFIs still have a long way to go in order to become sustainable financial institutions with significant outreach. Major weaknesses of MFIs, if we consider them in the possible role of insurance providers, are their lack of actuarial and other insurance know-how, the need for a considerable capital base for insurance, and the risk of venturing into a new and complex field of financial service provision before they are soundly established. The danger of

[5] Rural Finance Sector Development Act (RFSDA) currently being discussed amongst the stakeholders.

intermingling service lines is a serious threat. Also, channelling donor money for an insurance programme - which is the case with some NGOs - diverts the MFIs from their original role (savings and credit), especially their orientation towards sustainability. It is therefore important to stress that MFIs should only become involved in microinsurance as agents, and not as insurance providers[6].

It is interesting to note that the draft of the Rural Finance Sector Development Act [Part I, (10)] includes “insurance” in the definition of Rural Finance. It is however unclear to what extent insurance will actually be regulated under this Act (regulating MFIs), or under the Insurance Act.

In fact, today, many MFIs in Sri Lanka are involved in microinsurance in one way or the other. At present, the combination of the two service lines, microfinance and microinsurance, is widespread among many MFIs, be it at the government, private or cooperatively organised side. The combination refers either to providing insurance as a service line (mostly health and life insurance); or, to ensuring the credit portfolio against borrower deaths by charging a monthly premium on the sum of outstanding loan balances, or by charging a one-time fee on each loan. The latter method - building-up a loan risk fund - was established by SEEDS[7] (one of the largest and best-performing MFI-NGOs, with 500,000 clients), which has accumulated over USD 800,000 in the past few years, (see chapter 5.2).

It is noteworthy however, that four types of financial services providers, the TCCS, the Rural Cooperative Banks, an Islamic Financial Institution and a group of NGOs, have already introduced a clear distinction between microfinance and microinsurance operations. They have either set up a licensed insurance company (ALMAO, CICL, TAKAFUL), or an informal mutual insurance company in the case of the NGOs (see chapter 5).

3.3 Assessment

Even though the MFIs in Sri Lanka still suffer from important structural weaknesses, their strengths outweigh these weaknesses due to their great closeness to people and interest in serving them, as well as their openness for innovations, also with regard to microinsurance.

An important feature of Sri Lanka is that many poor people are used to financial services due to the many savings and loans schemes and widespread financial institutions. Even though many of these schemes and institutions are heavily criticized, e.g. for their lack of sustainability, they have contributed much to create awareness and some basic financial experience among the poor.

6 For further information, see the Preliminary Donor Guidelines on Microinsurance, adopted by CGAP in October 2003.

7 Established by the Sarvodya movement (see chapter 5); 2.5 % of the loan amount is charged to every loan disbursed.

Some MFIs have taken initiatives in microinsurance, though mostly without donor support. This is an important feature in a country heavily dependent on donors, or government programmes.

The major peoples' movements, cooperatives, NGOs and village-based institutions are working on microinsurance. However, the big commercial players in microfinance might not be serious service providers for microinsurance; as their interest in this segment may only be for publicity reasons, or due to government pressure.

A crucial issue and great opportunity for improving microfinance in terms of both quality and quantity is definitely the upcoming regulation and supervision. It is expected to benefit microinsurance in two ways. The regulatory framework will hopefully not allow for the two business lines to be combined in one institution. In addition, the experiences from the introduction of regulation for microfinance can facilitate regulatory improvements for microinsurance.

To conclude, there is no doubt that microfinance institutions in Sri Lanka have a role to play in delivering insurance services to their customers, primarily as a channelling agent.

4. Insurance

4.1 Regulation

The insurance industry is regulated and supervised by the Insurance Board of Sri Lanka (IBSL) under the Insurance Act No. 43 of 2000. IBSL is housed in the Securities and Exchange Commission (SEC) and has no staff of its own;[8] only two full-time consultants seconded by the Ministry of Finance. Lack of adequate resources limit insurance supervision.

The insurance act is considered to be modern, though only partially implemented. A deficiency in the Act itself is the lack of provisions concerning corporate governance. Some key provisions of the Act are:

- minimum capital of LKR 25 million (EUR 217,000/USD 258,000) is required in order to conduct long term (life) insurance business, and LKR 50 million (EUR 435,000/USD 515,000) in order to conduct general insurance business;[9]
- only limited (share) companies are allowed;
- composite companies (i.e., doing both general and life business) are permitted;
- a qualified actuary must annually evaluate the funds;
- minimum solvency margin in long term business of 5% of the actuarial value of liabilities (minimum solvency provisions for general insurance business are under discussion but not yet agreed);
- insurance companies (once only) and brokers (annually) must be registered;
- insurance companies may do only insurance business;
- insurance agents are appointed by insurance companies or brokers and must be physical persons;
- 30% of the long-term fund of life insurance business, and 20% of the technical reserves of general insurance, must be invested in Government securities and the balance in other investments as determined by the IBSL;
- fire and workmen's compensation insurance are still subject to tariffs, but the motor insurance tariff was deregulated from 1st January 2002;

8 Besides meeting Mr. Kanapadhipillai, one of the full-time consultants, we had the good fortune of meeting Dr Knut Hohlfeld, regulatory expert and consultant for the International Monetary Fund (IMF), who was on a two-week mission to the IBSL.

9 Fire, marine, motor and miscellaneous.

- the Agriculture and Agrarian Insurance Board, the Export Credit Insurance Corporation and the Social Security Board are all exempted, and instead subject to special Acts in each respective area.

The Insurance Act is expected to be revised in 2004, with the most significant change being the increase in minimum capital requirements to LKR 100 million (EUR 870,000/USD 1,031,000) each in order to do life and/or general business.

4.2 Government insurance schemes

Social protection in Sri Lanka refers to the formal system of social security; and as well to social security services for uncovered and poorer sectors being provided by families, through interventions of provider institutions such as NGOs/Community based organizations (CBOs), and by informal group initiatives. Some of the private schemes can well be regarded as microinsurance and are described more fully in another part of this report. Even some government schemes for low-income sectors are forms of microinsurance, but are described in this part of the report.

Most Sri Lankans have basic security in the areas of food, health and housing. The major challenge that remains to be covered is ensuring income security during old age. Only about 36% of the working-age population is covered in one or more formal schemes; the schemes that do exist are inadequate and have major deficiencies; and the population is rapidly ageing. The present and future challenges of old-age social security coverage in Sri Lanka are thoroughly dealt with in a number of studies carried out by the ILO Office, Colombo, during 2003. A main objective is to extend old-age security to “excluded persons”[10] and a National Plan of Action was to be agreed on before year-end 2003.

Samurdhi is a government agency, under its own Ministry of Samurdhi, which is involved in microinsurance. “Samurdhi” means “prosperity” and the Samurdhi Act of 1995 has poverty elimination as its objective. About 2 million families in Sri Lanka (48% of all families) with monthly incomes under 1,500 rupees are eligible for Samurdhi income supplements. Monthly income supplements paid by Samurdhi are 1,000; 700; 500; 350; or 250 rupees per month, depending on the size and income situation of each family. Very few receive the maximum amount of 1,000 rupees per month. Most families receive either 700 or 500 rupees monthly, while smaller, 1-2 person, families receive either 350 or 250 rupees. Income supplements are removed first when families exceed the “empowerment” income level of 5,000 rupees per month.

Families receiving the higher three levels of monthly income supplements (1,000; 700; or 500 rupees) have compulsory deductions made for savings (100 rupees), for insurance (30 rupees) and for a housing lottery (10 rupees). Persons older than 65 years cannot enter the insurance scheme. The death benefit is 5,000 rupees and is paid within 24 hours after death by one of the 24,000 Samurdhi Development Officers. Other benefits are

[10] Self-employed, household workers, migrant workers and unemployed persons.

2,000 rupees on the birth of a first child (1,000 for subsequent births), 3,000 rupees on marriage, and hospitalization benefits of 50 rupees per day for at most 30 days. The Samurdhi insurance scheme is not fully financed by the 30 rupee payments, but no figures were made available to us as to its performance or to how much it is subsidized. As with the family income supplements, it is primarily political considerations that determine the parameters of the program.

The 24,000 Samurdhi District Officers (DO) earn about 6,000 rupees per month and are offered a voluntary insurance plan costing 50 rupees per month. 19,000 DOs have joined. Major benefits are:

- death of a member	25,000 rupees
- death of a parent	15,000
- death of a spouse or child	5,000
- accidental death or total & permanent disability	100,000
- hospitalization (maximum of 30 days	200 per day
- operation	10,000
- school start of a child	500

The government is in the process of reviewing the Samurdhi program with a view to focusing it more - with improved benefits - on the most impoverished 24% of the population. It was said that Samurdhi and SANASA are considering joint ventures in insurance, especially for the better-off poor (the higher 24% of the 48% in Sri Lanka who are poor). A joint venture could involve creating a new insurance company or using ALMAO.

The ***Agriculture and Agrarian Insurance Board*** is a government agency under the Ministry of Agriculture and Livestock, whose purpose is to offer low-income farmers (1) pension, death and disability insurance, and (2) crop and livestock insurance. The Board has 350 employees and 150 field staff. All of the insurance schemes are considerably subsidized but no quantative data was available. No actuaries are involved and the basis for the coverage amounts and premium rates charged seem to be based primarily on political considerations.

Enrolments in the schemes are done individually, the administration and cost levels are very high, and the participation rates are low; in crop insurance, for example, less than 5% of acreage has any coverage. The program as a whole gave an impression of being antiquated and ineffective.

4.3 Private insurance

There are now 13 fully fledged (licensed) insurance companies in Sri Lanka, all privately owned. All but two are composite companies, i.e., doing both life and general business in the same company. ALMAO and Life Insurance Corporation (Sri Lanka) do life business only. The two formerly government-owned companies[11] have now been fully privatized. 4 of the 13 companies are listed on the stock exchange.

Total insurance premiums in year 2002 were LKR 20,281 million (EUR 176 million/USD 209 million), or 1.23% of GDP. 43% of premiums are in life business and 57% in general business. Insurance penetration (i.e., the proportion of the population having some private insurance) is only about 6% in life insurance and 8% in general insurance. Sri Lanka does not have any reinsurance companies.

The main classes of ***general insurance*** in 2002 were:

- fire	21.4% of premiums
- marine	8.1%
- motor	38.8%
- misc	31.7%

The largest ***general insurers*** in 2002 were:

- Sri Lanka Insurance Corporation Ltd	42.4% of premiums
- Ceylinco Insurance Company Ltd	22.5%
- Union Assurance Ltd	10.5%
- Janashakthi Insurance Company Ltd	8.2%
- Eagle Insurance Company Ltd	7.8%
Total	**91.4%**

The largest ***life insurers*** in 2002 were:

- Sri Lanka Insurance Corporation Ltd	32.1% of premiums
- Ceylinco Insurance Company Ltd	27.2%
- Eagle Insurance Company Ltd	21.1%
- Union Assurance Ltd	10.8%
Total	**91.2%**

As seen, 5 companies dominate with 91.4% of the general insurance market, while 4 companies have 91.2% of the life insurance market. The 3 companies found on both lists - SLIC, Ceylinco and Eagle - together have a market share of 72.7% in general insurance and 80.4% in life insurance.

Access to reinsurance for Sri Lankan insurance companies has been a growing problem after the attack on the World Trade Center in New York in September 2001.

Visits were made to the Insurance Board of Sri Lanka (IBSL) and the following six insurance companies: Sri Lanka Insurance Corporation, ALMAO, Eagle, Co-operative Insurance Company, Life Insurance Corporation (Lanka), CEYLINCO and Amana Takaful.

[11] Sri Lanka Life Insurance Corporation and National Insurance Corporation.

Sri Lanka Insurance Corporation (SLIC) was, after nationalization in 1961, for a long time the state-owned monopoly insurer. It was recently privatized and sold to a wealthy individual. It is still a force to be reckoned with (see tables above), as it has the largest market shares in both general and life insurance. However, it once had 100% and its position has continually been eroded. Our visit to a lower level manager in the midst of a large department gave a distinct, but admittedly superficial, impression of an old-fashioned and bureaucratic operation. There is no special emphasis on poor people or the low-income segment.

All Lanka Mutual Insurance Organization (ALMAO)*,* a microinsurer, does life business only and has a capital of LKR 28 million. Representatives of 7 funeral aid societies inaugurated ALMAO with 182 members in 1991. Encouraged by the SANASA movement, the number of participating societies grew within 10 years to 1,233 covering over 37,000 members. Since merging in 1996 with the insurance section of the SANASA Federation of Thrift and Credit Societies, ALMAO also offers loan protection and life savings insurance to the member societies, and offers property insurance thru Sri Lanka Insurance Corporation. ALMAO was formally registered as an insurance company in July 2003. ALMAO Broker Company, a subsidiary, offers insurance products of all other insurance companies to individuals and firms outside of the SANASA movement.

At the end of 2002, ALMAO had 47,000 life insurance policyholders, 773 societies with loan protection coverage and 161 societies with life savings coverage. Its potential market comprises some 8,000 SANASA societies with 850,000 members.

Eagle is a composite insurer focusing on the high-income market. It was recently sold by the Zurich Group to the Bank of Ceylon (Sri Lanka's largest commercial bank) and the privately owned National Development Bank. The new owners were motivated by the expected synergy effects of bank assurance (marketing of banking and insurance products to the same clientele).

Top management's view is that people commonly expect "welfare" either from the state or from the extended family. Savings is not a habit in a formalized way, which is why Eagle's top management believes that only enforced savings will work. It is critical to the success of microfinance/microinsurance solutions that savings/premiums be automatically deducted at source. The fact that there is no unique social security number system in Sri Lanka is a problem; combined with the low awareness of insurance, it means that many benefits, even from the state Provident Fund, are never collected.

Co-operative Insurance Company Ltd ("Samagi") started operations in March 1999[12]. It is a composite company with paid-up capital of LKR 84.3 million; 99.6% owned

[12] Ellis Wohlner made consultancy missions to Sri Lanka in November 1996 and May 1997 on behalf of Swedish Co-operative Centre (SCC), a Swedish NGO; first to ascertain if it was feasible for the Sri Lankan co-operative movement to convert its principal insurance agency into a full-fledged insurance company, and second to conduct a co-operative insurance seminar for co-operative leaders in order to agree on the necessary steps for implementing the creation of a co-operative insurance company. Because certain key recommendations were ignored, SCC abandoned its intentions of providing technical assistance to the new company.

institutionally - mainly by the rural co-operative banking sections[13] of multipurpose co-operative societies - and 0.4% by individuals. There is no restriction on the sale of shares to interests outside the co-operative movement.

The company's primary mission is insuring co-operative societies for general insurances like fire, motor, cash-in-transit, etc, and for loan protection insurance on the loans issued by rural co-op banking sections. It also markets insurance coverages to individuals, primarily the members of co-operatives. The potential market comprises over 10,000 co-operative societies and their over 5 million members.

Samagi has expanded rapidly in terms of staffing and offices, already having 18 branch offices and 128 employees. Expenses are extremely high; at 81% of net earned premiums in general insurance for year 2002, and at 73% of net premiums in long-term (life) insurance. General insurance claims incurred were at 57% of net earned premium - a reasonable level if expenses had been contained. Accumulated losses thru year 2002 stood at LKR 26.5 million, meaning that remaining capital was only LKR 57.8 million, or more than 17 million below the minimum capital requirement of 75 million for doing both general and life business. Management's perhaps overly optimistic forecasts for year 2003 call for a doubling of gross premium volume (to at least 200 million) and the production of a small operating profit.

The most urgent needs of Samagi are to strengthen its capital position; control its expenses; obtain adequate reinsurance; computerize its operations.

Life Insurance Corporation (Lanka) is a wholly owned subsidiary of the state-owned Life Insurance Corporation (India) and was established in March 2003, using funds remaining blocked in Sri Lanka when insurance was nationalized in 1961. Although doing only life business, it has LKR 100 million of paid-up capital and plans to raise it before long to 500 million.

Life Insurance Corporation (Lanka)'s mission statement is to become the largest provider of life insurance in Sri Lanka, for all demographic groups. In India, insurance regulations require that life companies have at least 25% of their lives insured from rural areas (villages with populations under 1,000). LIC (Lanka)'s parent in India has a year-old specially designed policy for reaching the poor.[14]

Ceylinco Insurance Company is part of the *Ceylinco Group*, a major player in financial services and one of the three largest commercial/industrial groups in Sri Lanka with some

[13] Also known as "cooperative rural banks".

[14] The scheme is partly subsidized and designed to provide life insurance protection to the rural and urban poor. Eligible persons are those who are: between 18 and 59 years old; below or marginally above the poverty line; and a member of an approved vocation/occupation group. Minimum membership size for the group is 25. Premiums are INR 200 per annum (the Indian rupee is worth slightly more than twice the Sri Lankan rupee); are collected thru a "nodal agency" (NGO or similar); paid for half by the Social Security Fund and half by the member and/or nodal agency and/or State Government; and provide the following coverage: natural death - 20,000 rupees; accidental death or total and permanent disability - 50,000 rupees; permanent partial disability due to an accident - 25,000 rupees.

115 companies and 25,000 employees. Ceylon Insurance Company was registered in 1939, the country's first insurance company, and nationalized in 1961. It obtained a license in 1988 to again do insurance business, now as Ceylinco Insurance Company. The company has a broad range of life and general insurance products and a branch office network of 77 branches for life and 62 branches for general. The company gives an impression of being modern, efficient and innovative, and focused on middle and higher income segments of the population. Its representative's assertion that the company wants/tries to reach out to the poor was not corroborated by either the company's annual report or by outside observers.

Amana Takaful began operations in 1999, restricted only to Muslims. Since 2000, it sells to anyone. The word "takaful" itself is a generic term implying that the company complies with Muslim Sharia law. According to the company representatives, about half of the Muslims in Sri Lanka want Sharia-compliant products. Ownership of Amana Takaful is 80% by the Amana Group (banking, insurance, asset management) of Sri Lanka and 20% by Takaful Malaysia, which also provides actuarial and other technical support, as well as reinsurance.

Amana Takaful is still quite small, with about 400 corporate and 5,000 individual clients. It professes to want to reach the poor and is currently especially targeting the low-income self-employed.

After the mission, a copy of Takaful's Annual Report for the financial year ending 31st March 2003 was received. It shows operating losses of 13.4 and 13.6 million rupees respectively, for the last two financial years, on revenues, respectively, of 19.0 and 5.4 million rupees. As in the case of Samagi above, the losses are basically due to extremely high expense levels. Insurance claims have been quite modest. Accumulated losses since Takaful's start amount to 44.9 million, leaving a capital balance of only 30.1 million at 31st March 2003. This is far below the minimum of 75 million necessary for doing both life and general business.

4.4 Assessment

Insurance in Sri Lanka was nationalized in 1961. Until 1979, when a second state-owned company was established, there was only one state-owned insurance company doing insurance business in the country. Liberalization, begun in the late 1980's, has led to the gradual establishment of private companies. This development has gained momentum and accelerated in recent years. Privatization of the two state-owned insurers has also contributed to sharper competition. Foreign investors are entering the insurance market. While the insurance industry is still quite small - with a total market penetration of probably less than 10%[15] - it is certainly growing more rapidly than the economy as a whole. An

[15] The Annual Report of the Insurance Board of Sri Lanka mistakenly adds the population penetration figures for life insurance and for general insurance, and arrives at a certainly too high figure for total penetration. Best estimates for 2003 are that the population penetration of life insurance is 6% and for general insurance 8%. Motor third party liability insurance is compulsory and it is among car owners - a definitely wealthier segment of the population - that one will also find most life insurance policyholders.

enormous potential remains to be exploited. The establishment of additional companies and the overall growth of the business have implied a stiff competition for the limited supply of qualified insurance professionals.

Insurance regulation and supervision needs to be further developed. It is, for example, unfortunate that the Insurance Act does not allow for mutual or co-operative insurers; nor does it spell out any rules concerning corporate governance. Minimum capital requirements are being set at higher and higher levels, and without consideration of product mix, risk profiles and insurance amounts; levels that can make it increasingly difficult to meet the needs of the poorest segments of society.

Government insurance programs have seemingly grown up “ad hoc”, based on political considerations. Actuarial evaluations of the programs have not been performed either before establishment or during ongoing operations. Present reform plans do not envisage making the programs self-sustainable; rather, they will continue as highly subsidized insurance options for the poor.

Private insurance is generally “sold”, not “bought”. That is to say, that except for an obligatory coverage like motor third party liability insurance, individuals respond more to selling efforts than actively seeking insurance. This is confirmed by the fact that a majority of individual life insurance policies automatically terminate within a year or two due to non-payment of premiums. Individual insurances are very expensive due to the high costs of marketing, sales, commissions, underwriting and individual administration. For low-income segments, with low coverage amounts and relatively low premium-paying capacity, these expenses can easily exceed the amount paid out in claims. The only really cost-efficient way to cover significant numbers of people is through group insurance schemes. Such schemes are not only cost-efficient; they also permit the inclusion of many less attractive risks that would otherwise be excluded in the underwriting process.

It is apparent that, with few exceptions, the private sector insurers will continue to focus on the still largely unexploited market of high and middle-income households.

5. Microinsurance

5.1 Regulation

Consistent with the worldwide situation in general, there are no special regulatory provisions in Sri Lanka for microinsurance. As will be seen below, there are today informal microinsurance schemes operating outside of the law. Increasingly tough requirements coupled to more regulatory and supervisory enforcement will ultimately close the door for these schemes.

5.2 Existing schemes

There are currently a number of informal microinsurance schemes in operation in Sri Lanka (in addition to the formally licensed insurance company ALMAO, reported on in the Insurance section of this report).

SEEDS (Sarvodaya Economic Development Services Ltd), founded in 1988, is the economic arm of the Sarvodaya movement, which began in 1985. Sarvodaya is a movement for empowering the rural poor through savings and credit, social and cultural activities, nurseries, libraries, etc; the total development of the community. There are currently 3,100 village societies with 300,000 savers and 150,000 borrowers. SEEDS, has a staff of 670, including 70 persons at the head office and provides services on a fee basis for capacity building. It has a banking division, an enterprise development division and a training division.

Upon the death of a member of a Sarvodaya society, the now 6-year old microinsurance scheme pays off the outstanding debt of a borrower to the society and also refunds the already paid-off part of the loan to the family of the deceased. The scheme is financed by a one-time, up-front charge of 2.5% on the face amount of a loan, which is then placed in a special fund at SEEDS. Loans are generally of relatively short duration; most being for 1-2 years. The fund has continually grown and stands today at LKR 86 million. No actuarial evaluation has ever been made of the fund adequacy. SEEDS regards SANASA and Samurdhi as its main competitors.

SEEDS is planning to have a feasibility study done for its insurance fund and of demand for microinsurance, possible linkages and partnerships, etc. The study[16] might be partially financed by NOVIB (the Dutch Oxfam). While insisting on maintaining its own independent program, SEEDS already has some contact with Yasiru and the prospect of possibly receiving technical assistance from RaboBank and Interpolis of Holland.

[16] The study is intended to be done in 2004 and is expected to be done by an international consultant with experience in the design of microinsurance schemes in Asia.

Yasiru Mutual Provident Society is the microinsurance wing of the All Ceylon Community Development Council[17]. The ACCDC is an NGO registered in 1993 that is working with social mobilization and organization of the poor in 10 districts of Sri Lanka. At the end of year 2002, it comprised 17,000 households with 36,000 members. One of the 17 major activity areas is "risk management by the poor (microinsurance)". Yasiru evolved from the concept of the funeral society, reflecting the need for a more comprehensive coverage. It was legally established under the Societies Act in December 2000.

The word "provident" is used instead of "insurance" in order to avoid coming under the Insurance Act, but the legality of doing so is very questionable. Yasiru's plan has been in operation for 3 years and has 6,500 insured. The RaboBank Foundation in Holland and its affiliated Interpolis Reinsurance Company have given very comprehensive financial, technical and reinsurance support, and will likely continue to do so for another 2-3 years.[18]

Yasiru operates in four districts[19] and lacks actuarially calculated premiums. Premiums are said to be too high, but this information could not be verified. A comprehensive social mobilization programme prepares potential members and officers for Yasiru services.

The Yasiru plan is sold and serviced (premium collection) by 200 village "animators". The coverage may be subscribed to by members less than 65 years of age and may be taken for one, two, three, five or ten units. The monthly premium for one unit is 10 rupees and the benefits are:

- accidental death of a member	6,000 rupees
- accidental permanent disability of a member	12,000
- natural death of a member before 65 years	3,000
- death of a member's dependent[20]	3,000
- member/dependent's hospitalization, max 30 days	30/day
- children's benefits under a separate agreement	

Yasiru reports a claims rate of only15-17 % (in 3 years, 350 cases), but this, if correct, may well be due at least in part to unawareness of the coverage. Two-thirds of the members are women. During its three years of operation, Yasiru has learned some valuable lessons; e.g. regarding the policy towards dependents (was too openly defined) and the need for waiting periods for health coverage (it is hard to check the health of new entrants to the scheme). Therefore, terms and conditions have been continually adapted.

Six other NGOs have joined ACCDC in the microinsurance scheme and there are hopes of involving up to 60 others who together have 200,000 members

[17] The Sinhalese name is: Samastha Lanka Praja Sangwardhana Mandlaya (SLPSM).

[18] Gerard Pierik is a recently retired executive of Interpolis Re and happened to be on one of his biannual consultancy visits at this time.

[19] Hambantota, Moneragala, Kalutara, Gampaha.

[20] "Dependents" are defined as children from 1 to 18 years, spouses, parents, siblings, cousins, nieces, nephews, aunts and uncles.

5.3 Assessment

The considerable demand for microinsurance is confirmed by the number of schemes that have begun and the numbers of people and organizations that have been involved. Generally, the schemes are quite young and still experimental. It is still too early to assess their sustainability. The increasingly onerous requirements for minimum capital for doing insurance business may be a serious impediment to the future development of microinsurance in Sri Lanka.

No comprehensive financial data was readily obtainable on any of the microinsurance schemes looked at; ALMAO, SEEDS or Yasiru. Neither was there time available to do field visits and obtain a sense of how these schemes function on the local level. These and other aspects - including the regulatory and supervisory matters - will need to be studied in depth if GTZ decides to go further in this area.

6. Donors in Microinsurance

6.1 Support activities

Donor support for microinsurance is still very limited. Besides the combined programmes, there is only one scheme that receives significant technical support from a donor agency. Yasiru, a mutual microinsurance institution, receives significant technical assistance from the Netherland's RaboBank Foundation[21] via the RaboBank Group's reinsurance company, Interpolis Re.[22] They have supported Yasiru since 1997, long before its formal inception in December 2000. So far, RaboBank Foundation has provided them with technical support in the form of an international insurance expert who makes regular visits. Financial support for operations (salaries) and investments (computers, software) amounts so far to approximately EUR 200,000. Total support for the planned project period of 5 years is expected to amount to EUR 300,000. Interpolis's support is limited to Yasiru, but aims at including as many other NGOs as possible. Its focus is on technical assistance to the institution and its products, with the aim of widening Yasiru's coverage to the whole island. The expansion strategy is at its initial stage, and could not be assessed in detail.

These so-called combined programmes are understood as NGO, or government implemented programmes (e.g. Samurdhi) consisting of a broad range of activities: a savings and credit component, income-generating activities, water supply, childcare, and a wide range of social security programmes (similar to microinsurance) for example for health, nutrition, the elderly, emergencies within the family or death. Some of these schemes are described in recent mapping exercises[23]; however, a complete picture of their objectives and activities is not available. These schemes do social work on behalf of a donor agency, or for a donor but through the government, and are social insurance schemes in a wider sense.

The International Labour Organisation (ILO) is implementing a project called "Extending the coverage of social security[24] to the excluded and the poor". The first phase of the project is almost finished. Small case studies of Yasiru and ALMAO were conducted and a mapping of microfinance and microinsurance providers was published. Besides these studies, ILO's focus at present is not on the private microinsurance providers, but on social security (e.g. pension schemes for household and migrant workers; establishment of a National Action Plan with the stakeholders). This ILO programme is financed by the Netherlands. ILO is not otherwise involved in microinsurance.

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21 Rabobank and Interpolis Re also support microinsurance schemes in India and the Philippines.

22 Interpolis Re is thinking about starting a reinsurance company for microinsurers world-wide.

23 E.g. from ILO/IPID (2003), and GTZ (2003).

24 "Social security", as used here, is restricted to old-age security schemes.

The Worldbank's support activities have not been analysed since we were informed that they are not involved in the direct promotion of microinsurance. However, they appear to be promoters of various MFIs involved with social security or microinsurance schemes (Kandy Women's Association, Hambantota Women's Association, Sarwordya, Ministry of Social Development, Ministry of Samurdhi). At present, they are focusing on social security, particularly pensions.

USAID supported the Women's Federation of Hambantota until 2000, but with a focus on microfinance. This NGO is said[25] to be among the largest and best-performing MFIs in the country, and to have a microinsurance component. However, we were not able to verify this.[26]

Some others microinsurers received limited assistance: CICL got assistance from Sweden in the planning stages. TAKAFUL gets assistance from its shareholder in Malaysia. Beyond that, there was no evidence of donor, or any other external support in microinsurance.

At present, most bilateral and multilateral donors are in the process of reorienting their strategies and programmes, which also influences microfinance and microinsurance. We had the impression that some donors might be putting microinsurance on their agenda due to the discussions we had with them. This was so in the case of Canadian International Development Agency (CIDA), Swedish International Development Cooperation Agency (Sida), and United States Agency for International Development (USAID), which are currently undertaking reviews of their economic and support strategies for the finance sector.

From some microinsurance providers, we heard that the Japanese Government and NOVIB (Netherland's OXFAM[27]) are considering supporting microinsurance. However, no further information could be obtained.

The outline of the Asian Development Bank's (ADB) Rural Finance Sector Development Programme does not explicitly plan to support microinsurance; "insurance" is only generally mentioned under the assessment of the financial needs of the rural population.

6.2 Assessment

Apart from RaboBank, no other donor agency has gotten, or is explicitly planning to get, involved in microinsurance. The three donors visited (CIDA, Sida, USAID) expressed their interest in microinsurance, even though none of them seemed to have had the issue on their agenda prior to our visit.

[25] Controversial assessments were heard which could not be verified.

[26] Hambantota is located in the south of Sri Lanka.

[27] Oxford Society for Famine Assistance.

Even though we could not visit all donors, we got the impression that private microinsurance is a rather new topic for the donor community. In general, we perceived that donors don’t know very much about the subject.

A prominent Sri Lankan social development expert argues that microinsurance is a donor-driven issue. We were unable to obtain an appointment with him, but raised this point in various discussions with practitioners and other experts. They strongly objected to this assumption because evidence from the field (the demand for such services wherever they are offered) seems to prove the opposite.

7. Key Findings

1) There are clear indications of demand for microinsurance in Sri Lanka. In addition, the framework conditions are favourable for its development. These favourable conditions include a well-educated and literate population, a high level of social organization, and relatively high levels of food and health security. Also, most institutions and customers have experience of insurance services. Therefore, if peace continues to prevail, Sri Lanka would make a good "laboratory" for microinsurance development.

2) Large commercial insurers have, generally, no serious interest in serving low-income segments since the market potential in the higher-income segments is still huge.

3) There are a considerable number of social mobilization programmes - government or NGO/donor - with heavily subsidized insurance components. Their long-term sustainability is questionable.

4) A few smaller private insurers have the interest and potential to cater successfully for the low-income segment.

5) Some microfinance institutions are already playing an important role in the promotion of microinsurance.

6) Donors that promote microfinance are generally interested in microinsurance but have limited know-how. Donor coordination is a priority issue.

7) GTZ has a strong presence in Sri Lanka and is already an important player in rural and financial sector development.

8. Recommendations

As a lead agency in financial sector development in Sri Lanka, GTZ should consider playing a similarly leading role in microinsurance, at least as long as microinsurance is related to financial sector development.

GTZ should consider possible future support to microinsurance during the up-coming programme appraisal mission of January 2004. The main focuses should be on the Sri Lankan government's position regarding private microinsurance, on the linkage of microinsurance and microfinance, and on how microinsurance will be regulated.

If interested in proceeding further, GTZ should analyse potential partners and possible strategies for supporting microinsurance development. Two possible strategies are to follow a systemic approach (framework conditions, institutions, demand side), or an institutional approach (one or various microinsurance providers, sector institutions).

GTZ should in any case during 2004 contribute to the policy dialogue with respect to the regulation of microfinance and microinsurance (e.g. with regard to the new RFSD Act).

GTZ should provide feed-back to government and all other institutions visited during this study and distribute information material (e.g. the CGAP Working Group on Microinsurance's "Preliminary Donor Guidelines on Microinsurance", and information on relevant contacts) in order to clarify the position of GTZ and enrich the discussion on microinsurance.

Appendix 1: Abbreviations used

ADB	Asian Development Bank
ACCDC	All Ceylon Community Development Council
ALMAO	All Lanka Mutual Assurance Organization Ltd
CBO	Community based organization
CICL	Co-operative Insurance Services Ltd (“Samagi”)
CIDA	Canadian International Development Agency
CGAP	Consultative Group to Assist the Poorest
CRB	Cooperative Rural Banks
DO	District Officer
GDP	Gross Domestic Product
GTZ	German Technical Cooperation
IBSL	Insurance Board of Sri Lanka
ILO	International Labour Organization
IMF	International Monetary Fund
IPID	Institute for Participatory Interaction in Development
IPS	Institute for Policy Studies
LKR	Sri Lankan rupee
MFI	Microfinance institution
NGO	Non-governmental organization
NOVIB	Netherlands OXFAM (= Oxford Society for Famine Assistance)
RBIP	Rural Banking Innovations Project
RFSDA	Rural Finance Sector Development Act
SCC	Swedish Cooperative Centre
SEC	Securities and Exchange Commission
SEEDS	Sarvodaya Economic Development Services Ltd
SME	Small and medium enterprises
Sida	Swedish International Development Cooperation Agency
TCCS	Thrift and credit cooperatives
USAID	United States Agency for International Development

Appendix 2: Organizations and People met

1) Institute for Participatory Interaction in Development (IPID)
   Ms. Mallika R. Samaranayake, Chairperson
   Mr. S.W.K.J. Samaranayake, Executive Director

2) International Labour Organozation (ILO), Sri Lanka
   Ms. Claudia Coenjaerts, Director
   Ms. Shafinez Hassendeen, Senior Programme Officer

3) Insurance Board of Sri Lanka (IBSL)
   Mr. Kanapadhipillai, Consultant
   Dr. Knut Hohlfeld, Consultant (Germany, on a 2-week mission for IMF)

4) Sri Lanka Insurance Corporation Ltd (SLIC)
   Mr. Pushpa Siriwardena, Asst General Manager (Fire)

5) ALMAO
   Mr. P. A. Kiriwandeniya, Chairman (and Chairman of SANASA Development Bank)
   Mr. Manilal H. Perera, CEO
   Mr. L. B. Abeysinghe, General Manager
   Mr. M. Piyatissa, Senior Manager

6) SEEDS
   Mr. Shakila Wijewardena, Managing Director
   Mr. Emil Anthony, Deputy Managing Director/Director, Banking

7) ILO, Subregional Office for South Asia, New Delhi
   Mr. Johan Woodall, Senior Specialist in Social Security, New Delhi
   Mr. Denis Garand, Consultant (Canada)

8) CIDA, Sri Lanka
   Mr. Joseph Sebhatu, Director, Program Support Unit
   Ms. Arleene Kumeradasa

9) Sida, Sri Lanka
   Ms. Åsa Heijne, First Secretary, Embassy of Sweden

10) Eagle Insurance
    Mr. Chandra Jayaratne, Managing Director
    Mr. Deepal Sooriyaarachchi, Chief Operating Officer
    Mr. Pushpakumar Gunasekera, General Manager/Head Actuarial

11) Agricultural and Agrarian Insurance Board
    Mr. U.R. Chandradasa, Farmers Pension Director
    Mr. R.B. Wijekom, Deputy Director, Actuarial Research & Marketing [crop ins]

12) GTZ, Sri Lanka
    Dr. Roland F. Steurer, Director
    Mr. Armin Hofmann, GTZ Principal Advisor, Rural Banking Innovations Project
    Ms. Anke Wolf, Junior Expert
    Mr. Richard Gant, Microfinance & MSME Consultant

13) CICL ("Samagi")
    Mr. Upali Herath, Managing Director
    Mr. S.A.H. Mohideen, Chief Executive Officer

14) Life Insurance Corporation (Lanka) Ltd
    Mr. R. Gopinath, CEO & Managing Director
    Mr. S.S. Mathiaparan, General Manager

15) YASIRU Mutual Provident Society
    Mr. Sunil Silva, Chairman/Chief Executive
    Mr. Gerard Pierik, Consultant Interpolis (Holland)

16) USAID, Sri Lanka
    Mr. Lionel Jayaratne, Senior Project Management Specialist

17) Samurdhi Authority of Sri Lanka, Ministry of Samurdhi
    Dr. Sunil Jayantha Nawaratne, Director General

18) Ministry of Samurdhi
    Ms. Kumari Nawaratne, Secretary/Commissioner General & Chairperson of Social Security Fund

19) CEYLINCO Insurance Company Ltd (general insurance)
    Mr. Ajith Perera, Senior Assistant General Manager

20) Amana Takaful Ltd
    Mr. Ehsan Saheef, Director - Finance
    Mr. Mubin Sanoon, Senior Executive - Business Development

21) People's Bank
    Mr. W.J. Martin Fernando, Addl. General Manager
    Ms. Sylvia Bitter, CIM Advisor (Human Resource Policy & Manpower Planning)

22) Ceylinco Grameen Credit Co Ltd
    Mr. Susantha Suraweera, Director - Operations

Appendix 3: Studies and Report

N°	Title	Publisher/Author(s)	Place, Date
1	Farmers' and Fishermen's Pension and Social Security Benefit Scheme	IPS V. Eriyagama, R. Rannan-Eliya	Colombo, 27-2-2003
2	Strategies for Improving the Health of the Poor	DFID/IPS Dr. Ravi P. Rannan-Eliya	22-4-2001
3	Assessment of the Employees Provident Fund	ILO/IPS	Sri Lanka, 8-2003
4	Diagnostic Report on Social Security Situation in Sri Lanka	ILO/IPS	August 2003
5	Takaful Annual Report 2002 and information documents	Takaful	
6	Feasibility Study on starting a Cooperative Insurance Organisation Sri Lanka	Ellis Wohlner, SCC	November 1996
7	The ALMAO Insurance Programme	Sabbir Patel	January 2003
8	Regulation of Insurance Industry, Act N° 43 of 2000 (Insurance Law of Sri Lanka)	Insurance Board of Sri Lanka	9th August, 2000
9	Annual Report 2002	Central Bank of Sri Lanka	
10	Extension of Coverage of Social Security to the Excluded and the Poor in Sri Lanka	IlO/IPID	Colombo, January 2003
11	Report on the Rural Finance Sector Development Program	Asian Development Bank	November 2003
12	A Preliminary assessment of Sri Lanka's Health Sector and steps Forward	W. Hsiao, K.T. Li Harvard University, IPS	Cambridge, USA 16-1-2000
13	Draft Rural Finance Sector Development Act	Ministry of Rural Economy	July 2003
14	Reducing Vulnerability: The Demand for Microinsurance	Microsave Africa, Cohen, Sebtad	March 2003
15	Case Study on 'Yasiru' Mutual Provident Programme	ILO/IPID	
16	Yasiru Mutual Provident Program	YASIRU	
17	Company Profile All Lanka Mutual Assurance Organization LtD.	ALMAO	
18	Company Profile Co-operative Insurance Company Ltd	CICL	
19	Micro-insurance in Developing Countries	Interpolis Re G. Pierik, F. Dekkers	April 2003

N°	Title	Publisher/Author(s)	Place, Date
20	Quarterly Economic Review Third Quarter 2003	Economic Intelligence Unit, Ceylon Chamber of Commerce	Sri Lanka III-2003
21	Informal Financing of Small-scale Enterprises in Sri Lanka	GDI Berensmann and others	Bonn, October 2002
22	Microinsurance: The Risks, Perils and Opportunities - a Guide through the Questions to address before Developing a Product	SED Journal Warren Brown	March 2001
23	Making Insurance Work for Microfinance Institutions: A Technical Guide to Developing and Delivering Microinsurance	ILO Craig Churchill, Dominic Liber, Michael J. McCord, James Roth	2003

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