

How Insurtech Can Close the Protection Gap in Emerging Markets

By Susan Holliday

Insurance technology, better known as Insurtech, is a rapidly growing industry that is beginning to disrupt traditional insurance provision in advanced and emerging economies alike, and is creating opportunities and challenges for incumbents, start-ups, and investors. The opportunity offered by insurtech is particularly significant in emerging markets, where a large “protection gap” exists due to low insurance penetration. This has major development implications due to the fact that economic growth and insurance penetration are closely intertwined. Technology and new business models are necessary to close the protection gap in these markets, and companies will need to be able to innovate—either internally, by partnerships, or by investing—to seize the opportunity.

The level of global interest and investment in insurance technologies, or insurtech, continues to grow. While some of the valuations and the proliferation of conferences on the topic suggest an element of hype, the real increase in targeted investments and the number of ideas moving from pilot to implementation are concrete evidence of the impact of insurtech on the insurance industry.

Total investments in insurtech were \$4.4 billion in 2018, according to FT Partners, an investment banking firm focused on the fintech sector.¹ That’s up from \$3.2 billion the previous year, and over 200 transactions were made in 2018. While the level of investment in insurtech reached record highs, there were slightly fewer transactions last year, which likely reflects the fact that the market is maturing in developed countries. Although North America remains the largest area for investment, there have been increases in investments both from and into Asia.

FT Partners also reports \$8.3 billion in mergers and acquisitions, although some of that activity is only loosely connected to insurtech.² Investment is coming from a mixture of accelerator or incubator structures (for early stage investments), venture capital and private equity firms, corporates, and some asset managers and hedge funds. Corporate involvement overall continues to increase, although this offers both opportunities and challenges to insurtech start-ups.

Corporates are business minded and know the pain points in the industry, but they can be slow to make decisions and may have strategic priorities that differ from both the start-up and the other investors, such as wanting exclusive arrangements. In addition, there are many companies that are embracing aspects of insurtech without investing, either by partnering with established tech companies or start-ups, or by building in-house capabilities. In many cases, insurers are doing all of the above.

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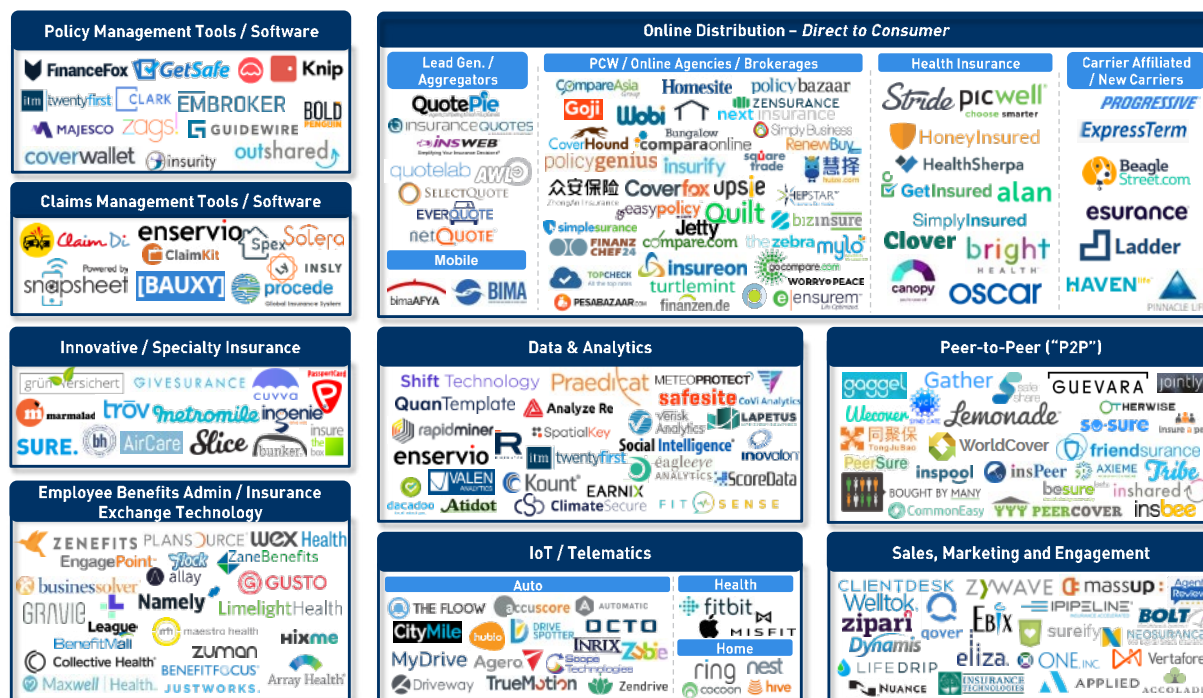


FIGURE 1 Insurance Technology—Industry Landscape and Selected Category Descriptions

Source: FT Partners. “Prepare for the InsurTech Wave—Overview of Key Insurance Technology Trends,” Dec 2016.

Types of Insurtech

While there are many and varied technologies that can be applied to the insurance industry, here we focus on a few buckets that are close to the core business and are expected to continue to have a significant impact on the industry. These initiatives tend to focus on certain pain points either for the insurance buyer or for the insurance company.

For example, a price comparison site or online broker may make it easier for a customer to find and buy insurance at a

fair price. However, there are many different types of business models within these categories. In this respect, buyers, partners, and investors need to beware. Some companies offer a true choice of products, with an element of education or advice and a fast and seamless buying experience. At the other end of the spectrum are those companies that appear to offer price comparisons but in actuality are merely devices to generate leads and collect phone numbers, which can lead to nuisance calling or mis-selling.

Fully digital insurance company	Online brokers/advisers	Aggregators and platforms	Process improvers	Data and analytics	Other
<ul style="list-style-type: none"> Regulated risk carriers Full end-to-end digital insurer Provide cheaper prices 	<ul style="list-style-type: none"> Likely to be regulated Convenient for customers Provide some form of advice and education as well as price 	<ul style="list-style-type: none"> Provide price comparison, lower prices, and convenience for consumers Successful in UK Usually need to be able to integrate their technology with companies 	<ul style="list-style-type: none"> Use technology to improve parts of the insurance value chain (e.g. claims) Lead to lower costs and better customer service 	<ul style="list-style-type: none"> Includes telematics for driving, wearables, and interactive mobile health Work with insurers to obtain and analyze data, leading to (potentially) better pricing and a more useful, interactive customer experience, and behavior 	<ul style="list-style-type: none"> Includes technology important to insurers (e.g. satellites, drones, agri- and weather-tech) Can make insurance more affordable in remote areas

FIGURE 2 Areas of Insurtech Innovations

Source: Author

By increasing efficiencies in the insurance industry, technology is bringing benefits to both insurance companies and their customers. An example is the sale of “bite sized” insurance or “insurance on demand.” By using digital interaction, artificial intelligence (AI), and in some cases a wider range of data sources, companies have been able to offer insurance for shorter periods, such as a month rather than six months or a year. This has helped make insurance more affordable, especially in markets where it is difficult or impossible to set up periodic payments.

Another aspect of this is insurance that can effectively be switched on and off, for example insuring a bicycle when the owner lends it to a friend, or a laptop when the owner is traveling with it. Short-term policies have always existed for policies such as travel insurance, but the use of digital technologies has made this application more practical and cheaper to administer.

A related development—one often associated with the Internet of Things (IoT)—is the evolution of usage-based insurance. The best-known example of this is in the auto insurance industry, with per-mile policies and dynamic pricing based on driving behavior. Usage-based insurance allows insurance to be much more granular and personalized. While usage-based insurance can incentivize better driving behavior and cut costs for some drivers, it doesn’t always work perfectly, as there may be safe drivers

who need to drive a lot or drive in certain areas, activities that may cause them to pay more for insurance. Discovery, an insurance provider in South Africa, has built on its well-known model in the health and wellness space to offer a rewards system based on loyalty and driver performance.

Telematics, or long distance transmission of computerized data, has other uses outside of pricing motor insurance, including encouraging safe driving, monitoring commercial vehicles and their cargo, and logistics and supply chain management, to name just a few.

Another IoT-related trend is insurers partnering with fitness apps and wellness platforms. This can encourage healthy and risk-reducing behavior and also gather data. And it can drive customer engagement, as consumers tend to interact with an app or the platform more frequently than they would with the insurance company itself. Examples of this include Discovery in South Africa and Goqii in India, which has partnered with Max BUPA and also with Axis Bank. These are examples of companies adding services and rewards for customers to promote a healthier lifestyle, but also to increase the number and quality of interactions with the financial services provider.

Clearly, insurtech is impacting the entire insurance value chain, from product development all the way to policy claims and management (Figure 3).

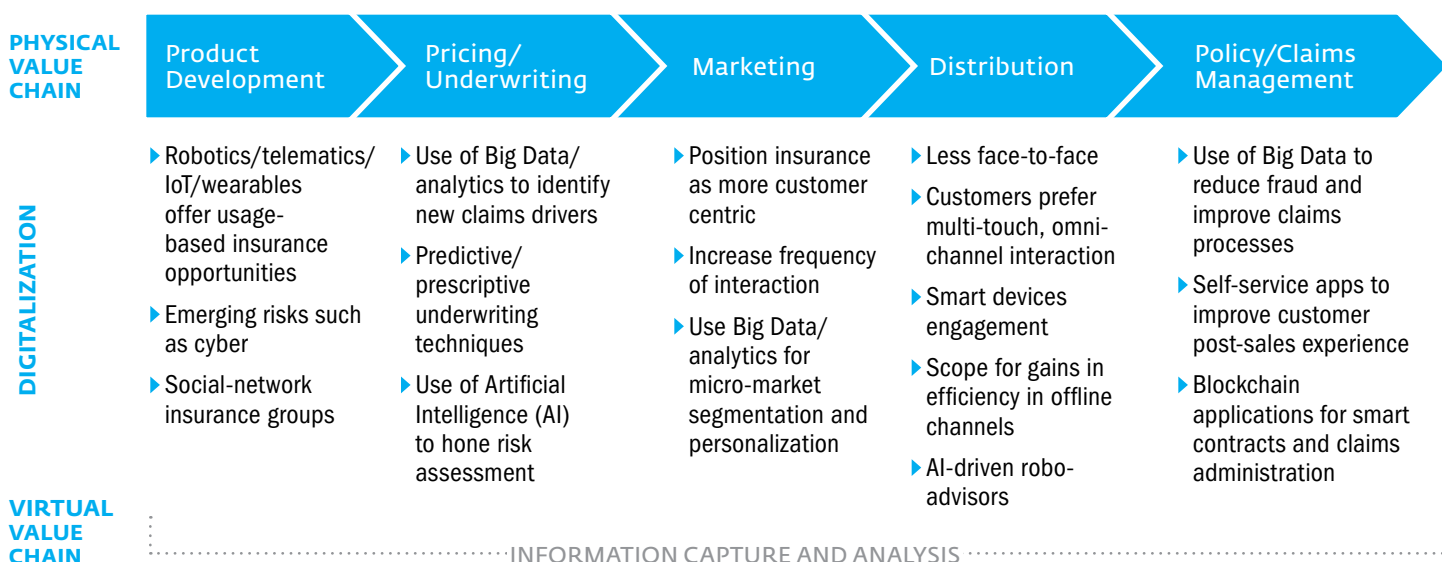


FIGURE 3 How Technology is Affecting the Insurance Value Chain

Source: Swiss Re Institute, 2017. “Introduction and Focus”, p. 13.

How Insurtech is Impacting the Industry

When fintech first emerged, the primary focus was on payments and lending, and later on digital banking. Many early fintech companies attempted to compete directly with incumbents by using technology to disrupt the business model and, in many cases, take advantage of loopholes or gray areas to remain outside of the regulatory environment. This is analogous to Uber challenging traditional taxi cabs or limousine booking services. As time went on, it became more difficult to avoid regulation, so many start-ups decided to become regulated entities.

Banks and payment companies started cooperating with start-ups and even buying them, as well as developing their own digital services in order to remain competitive. In due course, earlier and larger disruptive start-ups began making acquisitions of their own. PayPal buying Venmo is an example of this.

Insurance largely skipped this first phase for a number of reasons. First, in some areas such as underwriting it is almost impossible to avoid being a regulated entity. Even where we have seen new insurance companies being set up, they usually rely on support from traditional insurers or reinsurers, particularly in the early years. This may lead to starting as a Managing General Agent (MGA) and becoming a full stack insurer later, as we have seen with Next Insurance in the United States, which focuses on small businesses. The MGA model is likely to prove helpful in emerging markets, with the caveat that in many countries, current legislation doesn't properly cover this business model. Second, many insurtech start-ups are focused on working with the industry to make it more efficient, often by focusing on the claims process, providing telematics solutions, or adding AI and data analytics.

Relationships between insurance providers and insurtech start-ups are developing in a number of different ways, and it is becoming clear that no insurer or broker can afford to ignore insurtech. Consequently, there are several choices about how to engage: partner, invest, buy, or develop in-house proprietary solutions. We are seeing most companies developing both partnerships and in-house solutions, while some have also made investments (usually in addition to partnering) or have acquired start-ups as an alternative to developing solutions in house. In the wider sector, we are seeing various types of players combine forces, and some of these are more likely to be disruptive than others.

Partnerships between insurance companies and insurtech and fintech firms, while not without cultural and

operational challenges, generally improve customer service and make the production process cheaper and more efficient. Increasingly we are seeing new players that at first glance have little or nothing to do with insurance. For example, in Asia, ride sharing company Grab is partnering with Chubb to offer insurance to drivers and customers as part of a strategy to become the go-to app for consumers, while also offering payments, car lending, and other services. Some “new economy” companies may be frustrated with the pace of change in the industry, and so are partnering with new insurtechs. An example is Amazon, which is partnering with and has invested in Acko, a new digital insurance company in India.

It remains to be seen which of these matches will last, which are marriages of convenience, and which will end in divorce. The experience of insurers and banks partnering, an arrangement known as bancassurance, has often resulted in unforeseen problems, including the misalignment of interests.

The Opportunity in Developing Countries

The penetration of insurance (measured by the ratio of premiums to GDP) in developing countries is generally much lower than in advanced economies. Typically, the insurance industry takes off when GDP per capita reaches \$5,000 (Figure 4).

A 1 percentage point increase in insurance penetration is typically correlated with a 2 percentage point increase in GDP.³ Insurance supports economic growth and more prosperous societies have more goods and services to insure.

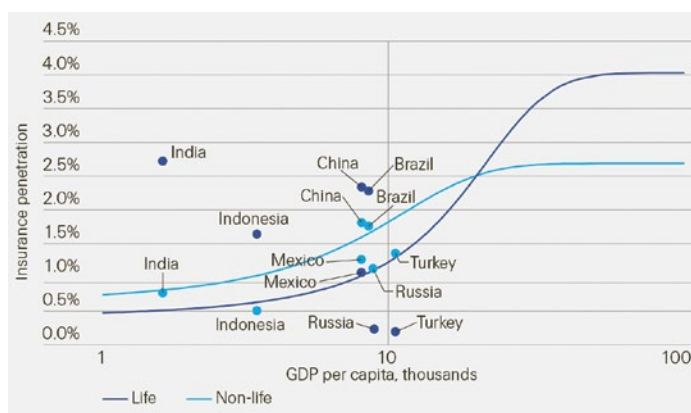


FIGURE 4 S-Curve for 2016, Selected Emerging Markets

Source: Swiss Re Institute. 2019. “Emerging Markets: The Silver Lining Amid a Challenging outlook.” *Sigma* 1/2019, see Figure 14.

There are two other important facets to consider when looking at the role of the insurance industry in emerging economies. These relate to the protection gap for natural disaster risks and healthcare. There is a large protection gap in these areas in many countries of the world, but it is particularly noteworthy that 58 percent of 2018 natural disasters occurred in developing countries but only 26 percent of them were insured (Table 1).

TABLE 1 Natural Catastrophes in 2018: Number of Events Economic and Insured Losses by Region, in billion US\$

	NUMBER OF EVENTS	INSURED LOSS		ECONOMIC LOSS	
		IN BN\$	IN %	IN BN\$	IN %
North America	68	52.9	62.5	80.5	48.8
Asia	104	20.4	24.1	54.7	33.1
Europe	44	7.7	9.1	20.7	12.5
Oceania/Australia	9	1.6	1.9	2.3	1.4
LAC	20	1.3	1.5	4.9	3.0
Seas/Space	6	0.6	0.7	0.7	0.4
Africa	53	0.2	0.2	1.3	0.8
TOTAL	304	84.7	100	165.1	100

Source: Swiss Re Institute.

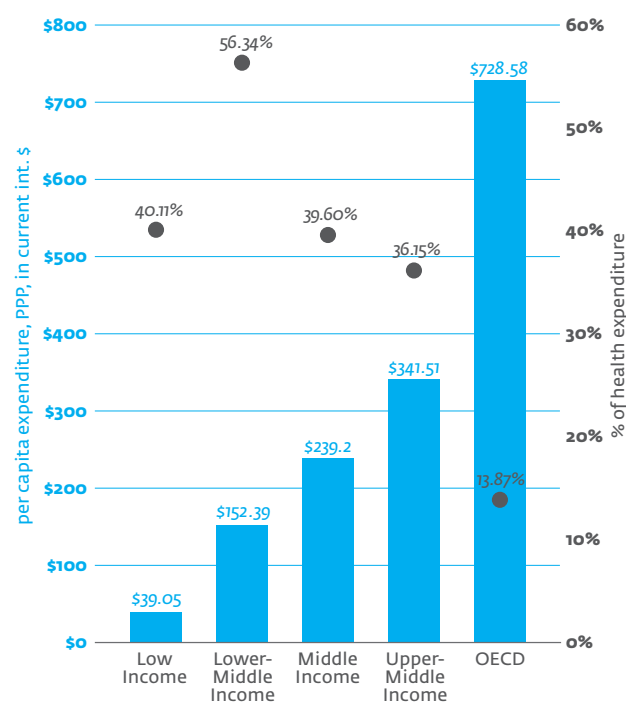
Also, many emerging market countries lack a comprehensive healthcare system and a developed health insurance market, which results in high out-of-pocket spend by those who can least afford it (Figure 5a). Out-of-pocket health expenditure as a percentage of total health spending is particularly high in lower-middle income countries (Figure 5b).

How Insurtech Can Help Close the Protection Gap

Although the majority of insurtechs currently operate in North America, Western Europe, and developed Asia, an increasing number are gaining traction in developing countries. We believe there are some areas where insurtech will be particularly powerful as many emerging markets make the leap to digital.

In countries such as Kenya and China, mobile banking and payments are already advanced and widely adopted. In other countries, digital financial services are only just

a. Out-of-pocket health expenditure by country groups, current international \$, 2016



b. Out-of-pocket health expenditure in selected countries, current international \$, 2016

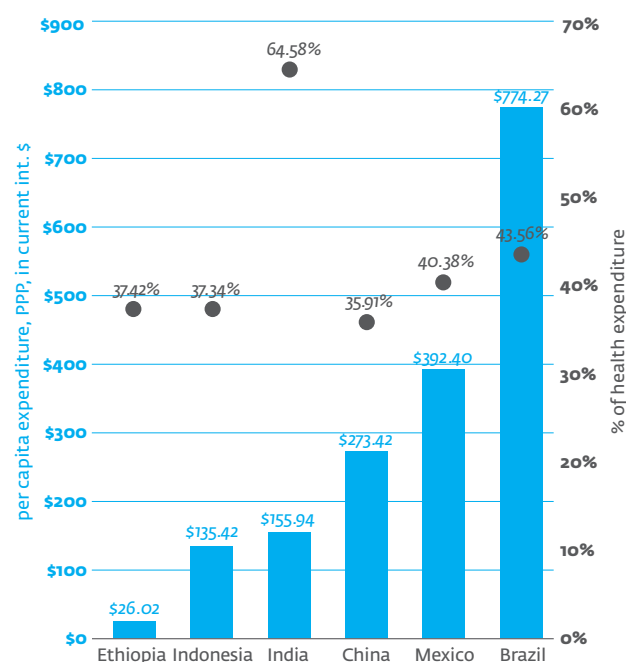


FIGURE 5 Out-of-pocket health expenditures

Source: World Development Indicators (WDI).

Note: left axis, blue bar, per capita expenditure, PPP, in current international \$; right axis, gray dots, percentage of current health expenditure. Country level data available on WDI.

starting to take off, yet watching YouTube on mobile phones or online shopping is already common. This suggests that the market will not just be digital first but digital only. However, there are some caveats. Insurance is less well known and understood in many emerging markets than it is in Western Europe, North America, and Japan.

In some cases, there are legitimate trust issues associated with insurance. This is because in the past some insurers did not pay legitimate claims and brokers failed to pass on premiums, leaving both the customer and the insurer in the lurch. In this context a level of personal trust is required, and consumers and small business owners may need help before they feel confident enough to buy insurance on their tablet or mobile phone. In this context we see an increasing importance (perhaps surprisingly) of call centers and tech-enabled agents. In these cases, the agent or call center worker can be aided by digital technology and even artificial intelligence to answer questions and help customers buy policies quickly and easily. Historically, insurance purchases often required multiple visits to an office, long turnaround times, reams of paper, and the costs and errors that resulted from these.

Shorter-term and on-demand policies are also likely to offer benefits in emerging economies where there is a lot of informal work and it may be difficult to pay for an annual policy. These types of products may also be more attractive to younger people, informal workers, and gig economy participants.

Fraud has always been an issue in the insurance industry, which relies heavily on trust. Insurtech is delivering clear value here and it will be even greater in emerging markets. This includes using digital technology to settle claims faster, improving customer service, and reducing the risk of extra costs being accumulated. Customers can now take photos or videos on their phones, if necessary in conjunction with a remote loss adjuster, to assess the damage and quickly begin the repair process.

Digitalization also makes it easier for both the insured and the insurer to track the claim, which further boosts customer satisfaction. The claims area is one of the most fruitful for applying AI, and this has already taken off in developed markets. AI can be used to identify potential fraud or cases where something is awry. Insurance companies in the United States and Europe are already seeing major cost savings in this area, which in turn can make these companies more sustainable and keep insurance prices affordable.

Enabling Factors for Insurtech in Emerging Markets

There is clearly great potential for insurance to grow in emerging markets and insurtech and tech-enabled business models will be integral to this growth. However, insurtech is not a silver bullet. Unlike in mature markets where people tend to start with auto, renters, and property insurance, in developing countries the entry point is more likely to be life insurance (often linked to a loan) or health insurance, especially for lower-income individuals.

Some of the important enabling factors for insurtech to make a difference are:

Compulsory Motor Third Party (MTPL) Liability

Insurance. This is important for auto (motor) insurance, and for pedestrians injured in motor accidents. In addition, it begins to build some knowledge of insurance and gives insurance companies a base from which to introduce other products. Ideally the market should not be tariffed so that good driving can be rewarded.

Financial literacy. This is an issue in many countries, not just emerging markets. Many people and small business owners don't understand the risks they face and may end up losing all their savings due to events such as illness or loss of their business to flood or fire. Insurtech can play a role in this, with advice and education on the web, gamification, call centers, and chatbots, etc. But literacy ideally should start in school so that pupils at an early stage understand saving and borrowing and the options that exist to build and protect wealth. Banks and microfinance institutions also have a role to play here.

Biometric ID. This can play a big role in preventing fraud, which otherwise drives up the costs of insurance for honest customers, particularly in health insurance. While not essential, the experience in India and some African countries has indicated this type of identification removes a significant barrier to developing better insurance solutions

Access to mobile networks and WIFI. While some apps can record data and upload it later, access to a strong network or WIFI at some point in the day is critical. For example, ACRE Africa is a parametric program for farmers to allow for replanting when there is no rain for 21 days after planting. It relies on mobile access to activate the program by using the unique code on the packet of seed, and on M-PESA mobile banking to compensate the farmer for replacement seed.

Payment mechanisms. Mobile payment opportunities for both premiums and claims speed up the processes, cut costs, and reduce opportunities for fraud.

Digital signature. This is also not essential, though the requirement for wet signatures slows down the process and introduces frictional costs. As a society becomes more digital and mobile-based, we recommend that regulators accept digital signatures. This can be done by leveraging Know-Your-Customer (KYC) from other sources such as Mobile Telephone Networks (MTN) or banks.

Regulation for different models. As discussed earlier, many insurtechs start off as managing general agents before they become full stack insurers. In many developing countries the MGA concept is not officially recognized. We believe that acknowledging different business models—including insurance companies, MGAs, brokers, agents, and price comparison sites—and regulating them appropriately is important. Even though the consumer is often not aware of the differences, this is important for adequate protection without stifling innovation. The United Kingdom, with its long history of insurance regulation, provides a good example of a comprehensive approach.

What Obstacles Remain?

Insurance companies in mature and emerging markets need to understand the challenges and opportunities of new technologies. In some countries there are few strong incumbents. There, for the market to develop, either regional or global champions will need to see insurtech as justifying the economics of entering the market, or new companies that employ new business models will need to be supported. There is no one-size-fits-all solution as different markets are at different stages of development. In-house innovations, partnering with insurtechs, and corporate VC-type investments are all valid ways to do this, but execution is critical.

Conclusion

The increase in the availability of data and the opportunity to personalise coverage also have downside risks. Using wider sources of data can help people or companies that lack a traditional credit history, but without some form of social security it is unlikely that the insurance industry can cover the poorest and sickest individuals.

Governments, regulators, institutions like the World Bank, and the private sector need to work together to create a framework where insurtech can be developed to increase resilience and financial inclusion.

Box 1 About IFC and Investing in Insurtech

IFC—a sister organization of the World Bank and member of the World Bank Group—is the largest global development institution focused on the private sector in emerging markets. We work with more than 2,000 businesses worldwide, using our capital, expertise, and influence to create markets and opportunities in the toughest areas of the world. In fiscal year 2018, we delivered more than \$23 billion in long-term financing for developing countries, leveraging the power of the private sector to end extreme poverty and boost shared prosperity. For more information, visit www.ifc.org.

IFC's investments in insurtech include equity participation in Hellas Direct, a technology-driven direct insurer writing motor and property insurance in Greece and Cyprus. The company's innovations include offering short-term policies and 48-hour claims settlements. In 2018, IFC provided a €3.5 million investment in Hellas Direct, part of a \$7 million equity offering by the company to help expand its offerings within the Greek insurance market. The investment will help diversify Greece's financial sector and make car insurance accessible and affordable to more Greeks and improve customer service.

IFC also invested in Indian insurtech start-up Coverfox, an online licensed insurance broker, through its holding company, Glitterbug. Based in Mumbai, Coverfox provides motor, health, life, and investment products, offering policies directly and through its network of technology-enabled point-of-sales people. Its proprietary technology allows users to compare and purchase coverage from leading insurance companies. IFC provided a \$10 million equity investment in a funding round that included corporate venture capital firm Transamerica and other existing investors. IFC's investment will enable Coverfox to build its portfolio, expand geographical coverage, and deliver insurance products to underserved customers, including women, unemployed youth, students, and rural customers.

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Please see the following additional EM Compass Notes about financial services in emerging markets:

Basic Business Models for Banks Providing Digital Financial Services in Africa (Note 68); *The Case for Responsible Investing in Digital Financial Services* (Note 67); *How a Know-Your-Customer Utility Could Increase Access to Financial Services in Emerging Markets* (Note 59); *Modelo Peru: A Mobile Money Platform Offering Interoperability Towards Financial Inclusion* (Note 54); *Blockchain in Financial Services in Emerging Markets—Part II: Selected Regional Developments* (Note 44); *Blockchain in Financial Services in Emerging Markets—Part I: Current Trends* (Note 43); *Digital Financial Services: Challenges and Opportunities for Emerging Market Banks* (Note 42); *Can Blockchain Technology Address De-Risking in Emerging Markets?* (Note 38); *How Fintech is Reaching the Poor in Africa and Asia: A Start-Up Perspective* (Note 34).

¹ FT Partners FinTech Industry Research. “2018 InsurTech Almanac.” FT Partners, January 2019.

² Ibid.

³ Lloyds. 2015. “City Risk Index 2015–2025.” Executive Summary.

Additional Selected EM Compass Notes Previously Published by IFC Thought Leadership

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Note 67: The Case for Responsible Investing in Digital Financial Services

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