



The Micro-insurance (or Popular Insurance*) and Brazil

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Summary

The micro-insurance is the tool of micro-finances developed to alleviate poor families and low-income people from specific perils. Basically, it involves all principles that an insurance in general should have, but with products, coverages, premiums and services designed with those people in mind. It can be seen as a way to extend social protection for destitute people or as a new market segment for insurance companies. In the first part of this article, we delineate the micro-insurance main characteristics, its place in the micro-finances, and its distribution models. In its second part, we describe the potential market in Brazil, the existent regulation and the micro-insurance products already commercialized. Finally, in the third and last part, we indicate some obstacles that a commercial micro-insurance probably will face and the reinsurance role in this context.

Key Words

Insurance; low-income people; micro-insurance; micro-finances; popular insurance; mutuals.

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* We will avoid using the expression "popular insurance" throughout this work; we merely use it here because it is the most used expression in the media. According to IAIS (2007, p. 10), "*In Brazil the term 'popular insurance' is used standing for small-scale mass products. However, popular is not the same as micro-insurance since micro-insurance targets low-income households whereas popular insurance is for all kind of customers and just means insurance of small amounts*".

Sinopsis

El microseguro (o seguro popular*) y Brasil

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Resumen

El microseguro es la herramienta de microfinanzas desarrollada para aliviar familias pobres y personas de bajos ingresos de peligros específicos. Básicamente, ello involucra todos los principios que un seguro en general debería tener, pero con productos, coberturas, primas y servicios diseñados, teniendo en cuenta dichas personas en mente. Puede ser visto como una forma de extender protección social para personas carentes, o como un nuevo segmento de mercado para las aseguradoras. En la primera parte de este artículo, delineamos las características principales del microseguro, su lugar en las microfinanzas, y sus modelos de distribución. En su segunda parte, abordamos el mercado potencial en Brasil, la reglamentación existente y los productos de microseguro ya comercializados. Por fin, en la tercera y última parte, apuntamos algunos de los obstáculos que un microseguro comercial probablemente enfrentará, y el papel del reaseguro en ese contexto.

Palabras-Clave

Seguro; personas de bajos ingresos; microseguro; microfinanzas; seguro popular; mutuas.

Sumario

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* Evitaremos utilizar la expresión “seguro popular” en el restante de este trabajo; meramente la empleamos aquí por ser la expresión más usada en los medios. Conforme IAIS (2007, p. 10), “*In Brazil the term ‘popular insurance’ is used standing for small-scale mass products. However, popular is not the same as micro-insurance since micro-insurance targets low-income households whereas popular insurance is for all kind of customers and just means insurance of small amounts*”.

1. Introduction

Every society has risks that should be avoided, and low-income layers always are vulnerable to them. In reality, people who live in low-income communities, either urban or rural, are surrounded by dangers with high impacts to the comfort of their familiar units.

The dangers may hold individual and specific risks, such as illness, fatal accidents, disabilities, loss of properties due theft or fire, and unemployment, as well as risks that affect many people, such as drought, flood, house collapse, recession. Low-income people are more exposed to such risks than the rest of the population and most of the time they cannot deal very well with crisis.

Poverty and vulnerability reinforce one another forming an ever-growing downward spiral. Not only the exposure to risks results in substantial financial losses, but also vulnerable families suffer the continue uncertainty about when and how loss may occur. Due to this perpetual concern, poor people are less likely to take advantage of income generation opportunities, which may reduce poverty (CHURCHILL 2006, p. 12). Obviously, these people do not simply and purely undermine the dangers that surround them; the majority tries to manage the risks and deal with their consequences. Saving money, working extra time in other activities and asking for loans from friends or relatives constitute some of the several strategies used to avoid financial loss. However, such informal protection methods do not resist against unforeseen serial cases. Before they are able to rise again from an adverse situation, a new unforeseen event may happen with more power throwing them back to stage one again. Micro-insurance¹ exists exactly to avoid this kind of situation.

2. Micro-insurance: definitions

There are some definitions about micro-insurance, but the one that became a pattern was created by CGAP (Consultative Group to Assist the Poorest) Working Group on Micro-insurance², reproduced below:

Micro-insurance is the protection for the low-income population against specific dangers in exchange for regular payments of proportional premiums to the probability and costs of the involved risks³. (CHURCHILL, 2006, p. 12)

¹ Micro-insurance is a subject that became in fashion in Brazil in 2007: in May, the World Bank sponsored the "Regional Workshop about access of the low-income population to insurance", and, in September, during the 4th Conseguro (Insurance Seminar), it was brought to attention, through a specific lecture given by the President of Fenaprevi (Federation of Private Pension Fund Carriers). Besides that, the Superintendent of SUSEP (Insurance National Agency) and the Minister of Planning mentioned it during the event.

² "Compelled by the potential of microfinance to reduce poverty on a sustainable basis, nine leading donors and practitioners formed CGAP in 1995 to develop and share best practices, set standards, and develop technical tools and models. Over time, CGAP has become a recognized resource for the industry, providing services and information to a wide array of actors engaged in building, financial systems included. Its mandate was renewed in 1998 and in 2003 for a second and third phase (CGAP II and III). Its membership has grown to 32 agencies, including bi- and multilateral development agencies, private foundations, and international financial institutions" (CGAP, 2007, p. 2).

³ In the original: "Micro-insurance is the protection of low-income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of the risk involved". Our translation.

The main micro-insurance features are the following: (i) low-income population as target; (ii) protection offer for specific risks (determined risks in the coverage condition of the insurance policy); (iii) the service rendered in return to such protection, i.e., the payment of certain amount of money – the premium –, that should remain proportional in relation to the probability of the risk occurrence, plus costs. We have in this definition the insurance distinctive marks – coverage for determined risks through payment of proportional premium to the probability of the loss – added to the idea of hippo-sufficiency, low-income people in the case of the insurance policyholders through the micro-insurance protection. The next definition, extracted from documents produced by OIT, specifies what type of perils are objects of such protection:

Micro-insurance is the offer for insurance product that is designed for low-income people related to cost, stipulations and coverage. It aims at the vulnerability reduction of this market, protecting the domestic budget against great economic shocks, such as a death in the family or a long-term illness⁴ (ILO, 2003, p. 4).

Here we can already realize that micro-insurance does not have as objective only the protection of the hippo-insufficient people, but it is also designed having in mind such people, i.e., who they are, the environment that surrounds them, their needs and their possibilities. Although other types of insurance can reach low-income people, it is not good enough that it is within grasp to be called micro-insurance. In order to be considered micro-insurance, it is necessary that the product is developed for people ignored by the traditional insurance market, i.e., people who do not have access to insurance, merely because there are no products that protect them against perils related to the reality in which they live, or within their possibilities (CHURCHILL, 2006, p. 13)⁵. We have here the reason for such people to need protection: they are vulnerable to financial shocks that affect the family unity budget. Below, another micro-insurance definition that makes it clearer in which context this term is normally used:

Micro-insurance is not confined to any specific product or product line, or any specific supplier. Although its target is to offer coverage to low-income families, it is also important to clarify that the term micro-insurance (...) refers to a service for a specific income segment in the emergent markets, where the insurance market is not well developed⁶ (IAIS, 2007, p. 5).

⁴ In the original: “Micro-insurance is the provision of insurance products that are designed for low-income persons in relation to cost, terms and coverage. It is intended to reduce the vulnerability of this market to major household economic shocks, such as a death in the family or a long-term illness”. Our translation.

⁵ In the original: “How poor people have to be for their insurance protection be considered micro? The answer varies by country, but generally micro-insurance is for people ignored by mainstream commercial and social insurance schemes, people who do not have access to appropriate products”. Our translation.

⁶ In the original: “Micro-insurance is not confined to any specific product or product line or a specific provider type. Although it is aimed at providing coverage to low-income households, it is also important to clarify that the term micro-insurance (...) refers to servicing a specific income segment in the emerging market jurisdictions where the insurance markets are not well developed”. Our translation.

By this definition, we observe that the general idea of the term micro-insurance is for insurance products, aiming at the low-income population in underdeveloped countries, and where the insurance market itself is still incipient, perhaps due to the absence of legal regulations or the lack of other local conditions to allow its development. Although these micro-insurance general notions are present, its existence is possible in developed countries to assist their destitute people. A good example of that is the industrial insurance, a product sold at the United State's factory gates in the beginning of the 20th century, by the Metropolitan Life Insurance Company, a kind of forebear of the actual micro-insurance products. (MCCORD; ROTH, 2006, p. 1).

Another idea that remains very clear is that there are not exclusive products or coverages of micro-insurance and others of traditional insurance, or that micro-insurance must be commercialized through a specific way to be kept characterized. It is not enough for the insurance to be within low-income people's grasp and to meet one specific need of theirs for it to be characterized as micro-insurance: it must be designed for such people. This broad idea is present in the last definition that we will comment:

Micro-insurance is the insurance which is accessed by low-income people, offered in several types of different entities, but it is managed according to the practices generally accepted in insurance (they must include the Insurance Basic Principles). More important still, this means that the insured risk under a micro-insurance policy is managed according to insurance principles and funded by premiums. The micro-insurance activity itself, therefore, should be within the competence of an insurance domestic regulator/supervisor entity or any other appropriate agency within the national laws of any jurisdiction⁷ (IAIS, 2007, p. 10).

With this definition, we have registered an interesting fact, represented by the micro-insurance commercialization, which is performed by many types of entities, each one with different structures and organizations. We will see basic outlines of these entities when we approach the micro-insurance distribution models.

In the description, the detail that calls our attention is the expression "Insurance Basic Principles", which reminds us that, even having so many peculiarities, the micro-insurance still fits into the classical definition of insurance⁸ (being, therefore, a modality of it). This means, for instance, that in the micro-insurance, the Law of Great Numbers⁹ is also used.

⁷ In the original: "Micro-insurance is insurance that is accessed by low-income population, provided by a variety of different entities, but run in accordance with generally accepted insurance practices (which should include the Insurance Core Principles). Importantly this means that the risk insured under a micro-insurance policy is managed based on insurance principles and funded by premiums. The micro-insurance activity itself should therefore fall within the purview of the relevant domestic insurance regulator/ supervisor or any other competent body under the national laws of any jurisdiction". Our translation.

⁸ An example is the definition of insurance that we find in Rubin (2000, p. 244): "*Insurance – mechanism for contractually shifting burdens on a number of pure risks by pooling them*".

⁹ The Law of Great Numbers, general principle of the observation science, commends that the frequency of certain events, observed in a great number of similar cases, tends to become fixed more and more, as the number of the observed cases increases, becoming closed to the foreseen values by the theory of probabilities.

Due to its several peculiar characteristics, the micro-insurance does need specific treatment, despite having so many things in common with the insurance in general. However, this definition points out that this specific treatment does not necessarily imply an informality of the segment when it states that such institutions should be submitted to a regulatory agency in the country where it operates.

3. Characteristics of micro-insurance

From this four analyzed definitions, we can specify some characteristics inherent to micro-insurance:

- a) oriented to low-income people, since they are the ones whose vulnerability is intended to be removed;
- b) relevant to the insured's reality, since the coverages should be related to the real risks that make part of the lives of these people, otherwise the insurance might fail;
- c) widely inclusive, with few exclusions, since the coverages insure limited risks, with small sums and aiming at protection of hipposufficient people, so that the exclusions will only guarantee the operability of the insurance;
- d) documentation easily accessible to notify a claim, considering the difficulty that these people have to take leave from their jobs, or to pay taxes, whether official or not;
- e) Policies with straightforward conditions and easy to understand, so that the micro-insurance policyholders, who in general are people with little formal education, can understand the product that they bought;
- f) Premiums with low price (rates based on mutualism), since it is also necessary to offer the insured a suitable amount to have the insurance protection, and consequently, billing a premium relatively low in order to guarantee the success of the product;
- g) Low maximum insured amount, since the insured amount shall necessarily correspond to the paid premium, and the latter needs to be low to reach the low-income population;
- h) Mass consumption products, so that it is possible to compensate low premiums with large volume of policyholders with similar perils;
- i) Flexibility of the premium payment, since the domestic budget of the micro-insurance target-public sometimes is inconstant, especially if we consider those people who work within the informal economy or support themselves through casual earnings;
- j) Some effort to create an insurance culture with the client, so as to educate him about the importance to maintain insurance policies in order to avoid shocks caused by unforeseen events and make them loyal; and
- k) Alternative channels of selling, in order to guarantee that the micro-insurance products effectively reach the low-income people to whom they are designed, achieving the risks distribution.

4. Micro-finance and micro-insurance

Micro-insurance is only one of the tools within a wider context called micro-finance. "A micro-finance system can provide the citizens with many financial services, among them loans, savings and insurances" (CALDAS, 2003, p. 3). Below, we present a micro-finance concept, and the distinction between micro credits, since it is not rare to confound both terms:

(...) The concept of micro-finance will be used as a suitable and sustainable financial service rendered for low-income population traditionally excluded from the traditional financial system, utilizing differentiated products, processes and managements.

Within the micro-finance context, the micro-insurance activity is defined as one dedicated to render its services exclusively to small businesses and companies, distinguishing itself from other types of micro-finance activities, essentially by the used methodology, very different from that adopted for traditional credit operations. It is commonly understood as the micro-finance main activity for its importance for public policies in overcoming poverty, through employment and income generation. (SOARES, 2007, p. 52)

Thus, we can punctuate that the expression “micro-finance” means the furnishing of loans, savings and other specialized finance services for people belonging to poor communities¹⁰, or for micro-entrepreneurs.

Although there are historical situations that can fit into micro-finance, its modern phase began only in the seventies, with actions by specialized Non-Governmental Organizations (NGOs) and some banks. Such initiatives were based on small loans without guarantees, average interest rates, very short-term businesses, and participation of credit agents in order to reach clients (SOARES, 2007, p. 14).

The main products of micro-finance are: micro-credit (based on flexible loans), micro-savings (short, medium and long term), micro-insurances (particularly life and health), besides others, like value transfers, real-state finances, and financial investments.

Within the micro-finance framework, the main agents are known as Micro-finance Institutions (MFIs). The MFIs are organizations which offer financial services for low-income people (LEDGERWOOD, 1999, p. 1). Companies that perform credit operations for micro-entrepreneurs¹¹ also fit into the MFIs concept.

Several types of organizations fit into this definition, varying in their legal structure, mission, methodology and sustainability, but all of them have as common point the financial service for a customer portfolio that simply is not offered by traditional banks¹².

¹⁰ “The issue about the access of low-income populations to finance services has been an important subject within the academic environment and in the debates about public policies over the last few years. The evidence of that is the constitution of the 2005 Micro-Credit International Year, by UN (United Nations), and the election of Mr. *Muhammad Yunus*, *Grameen Bank founder, of Bangladesh, Nobel Peace Prize*” (SOARES, 2007, p. 4).

¹¹ Regulated in Brazil by Law 10.194, February 14th, 2001.

¹² Nichter (2002, p. 22-25) identified four MFIs basic types, amongst those which operate in Brazil: a) institutions associated to international networks (such as Women Bank or Accion); b) civil society organizations (such as Non-Governmental Organizations – NGOs – and civil society organizations of public interest (OSCIPs); c) governmental initiatives (examples are the Popular Banks of several States); d) regulated financial institutions which decided to work into this niche (major example is the Nordeste Bank, through its program “Crediamigo” (“Friendlycredit”). It also identifies the credit cooperatives, although it does not consider them into its work scope due to its closed nature, reason that, it alleges, they are not considered in studies published by the World Bank (NICTER, 2002, p. 19).

The main reason for a country to adopt a micro-finance policy is to promote the inclusion of low-income segments of the population, providing them with some protection.

Likewise, the micro-insurance can be understood as a “social inclusion insurance”, since a) it is a tool to reduce the poverty effects whereas it avoids economic shocks that could affect the humblest home budgets; b) it reaches those people undermined by the traditional insurance market, since it aims, as consumer, at the segment of the population that is out of the traditional financial system; c) it is a way to manage risks, to avoid shocks in the budget and to mitigate the impact of certain events, offering an additional tool for these families to allow them to rise after an impact in their domestic economy; and d) it works as a security net for micro-entrepreneurs and low-income families, within the micro-finance context, since it impedes the fall from the level they were raised to, for instance, through micro-credit, and consequently prevents them from returning to poverty.

The following characteristics are present in the micro-finance target public (and, therefore, in the micro-insurance one as well): a) low formal education resulted from an early ingress into the labor market, often pressed by family conditions or by the lack of opportunity to continue the studies – which means low-skilled jobs due to bad qualifications; b) low incomes (per family and per capita), in such a way that they are outside the traditional financial systems for not fulfilling, for instance, the minimum requirements to open a bank account; d) often, they work in the informal economy, since a great part of them work in an independent basis or survives doing extra-jobs, temporary labor, or is sub-employed in many different activities; e) they live in destitute communities or in slums, where there are more people in the same situation, sharing the difficulties; f) precarious to almost-reasonable life conditions, reflecting their financial conditions and housing.

5. Distribution of micro-insurance

The classic micro-finance distribution patterns are naturally applied to micro-insurance, since it is built into them. There are several ways to deliver micro-finance products to their consumers, all of them derived from the four distribution models, which became know as the typical ones: the community-based model, the provider model, the complete service model, and the partnership model.

5.1. The community-based model

It is performed by associations under mutual companies' structure (companies which belong to their clients). After the deductions for the creation/maintenance of the reserves, the profits are distributed to proprietary-clients (CHURCHILL, 2006, p. 341). The mutual associations can be divided in mutual insurance companies (for instance, insurance cooperatives), financial cooperative networks (for example, credit and savings cooperatives), which provide insurance as an aggregate service and mutual insurance association networks, developed with the only purpose of providing insurances to their members.

Mutual insurance companies can be classified in three types. The first one does not require premiums payment, nor a tax on the insurance policies. Also called post-paid, in this organizational type the amount of the damage claimed is charged from the members after the loss

occurrence. Nowadays, this type is in process of extinction. The second type has premiums payment and tax on the insurance policies, whereas the third group has premiums payment, but does not have tax on the insurance policy.

The difference between the second and the third type is that the companies, in this latter group, are often organized to make the insurance policyholders receive dividend bonuses, but losses do not impose additional obligations (hence, they share profits, but not losses), whereas those from the second type are often organized to give the insurance policyholders the possibility to share the profits (by the cooperative perception of the earned premium) and losses in equal terms (CHURCHILL, 2006, p. 341).

There are some people who distinguish the corporative network model from the community-based model. The first being practiced mainly between insurance corporative companies and financial corporative networks, and the latter usually by mutual insurance association networks (CHURCHILL, 2006, p. 337,341). But both work processes are very alike, reason why we chose to analyze them together.

In this distribution model, the client of the micro-insurance product is not only a simple insured, because he also has participation in the MFI, according to mutualism and cooperative principles. In this way, every insured is also co-proprietary of the micro-insurance provider.

Here, the micro-insurance business is managed by the insured-owners themselves. The situation that normally occurs is to have an administration group (generally voluntaries) that takes the most important issues to be voted during the general assembly. Since this distribution model is managed by its own insureds, it has the advantage of reducing moral risk, because they are the ones who most benefit from the positive business outcome. It also brings a comprehensive knowledge about the clients making it easy to adapt the micro-insurance coverage to the insureds needs. However, for the very reason that it is managed by voluntaries, this model brings as main weakness the amateurism of its administration – at least in the beginning. Therefore, a long period of time is needed for training and capacitating programs, as well as hiring specialized technical assistance. And, since there is no people specialized in this type of business, there is also a limited capability to perform coverage and premium adjustments, due to the lack of actuarial and insurance knowledge.

5.2. The provider model

It is used mainly for health micro-insurances and personal accidents. In this model, the service provider (particularly health services, such as clinics and hospitals) enters the insurance arena to produce great volume of business in a given location. Also, it makes possible for different segments of the population to acquire health plans (CHURCHILL, 2006, p. 410). With this distribution model, generally the clients are restricted to its network of professionals and facilities or to professionals authorized by the providers, outside the network the benefits are limited. The great advantage of this distribution model is to tailor the benefits package in accordance with the available services. Normally, customers' service is fast, and so is the insurance claims procedure, as well as the rendering of services, since all micro-insurance inherent activities are gathered in just one carrier. This is a reasonable model very commonly used in markets with little regulation.

5.3. The complete service model

It is very similar to the previous model, but here, the service provider (especially health services) does not work within the insurance business. It is responsible for all aspects of the products development, sales, services and claims, whereas the insurance company is responsible for costs and losses related to insurance, retaining the profits. This model lies between the provider model and the partnership model, generally as a derivation and development of the provider model. It is interesting because this model presents professionalization of the insurance relations, since the services provider acts simply as an agent. Having as a safety net the support of an insurance company, this model has accessibility to its technology and experience. In this case, a diversification of products generally takes place – contributing towards risk reduction. Since it is a legal constituted insurance company, it must attend the requirements of the law about the reserves and technical provisions. Therefore, this model gives the possibility to buy reinsurance. However, prevision is necessary within the legislation, to keep this model working properly. In this model, the services provider concentrates the interface with the client, whereas the insurance company manages the technical area, and that is why the administrative and transaction costs are higher. It is possible for some problems to arise related to the product profile according to clients' expectations, and also problems derived from the information given to the services provider.

5.4. The partnership model

It is the one in which the insurance companies work with distributor agents. In this model, the insurance companies usually are associated to agents with a large client database – generally well established MFIs, although other partners' presence is possible like large retail store networks (regional or national ones), etc. – normally through a single group insurance policy. In the case of a partnership with MFIs, this latter has the benefits of the expansion of its product line (since it starts to offer micro-insurance products) and extra protection for itself and its customers (since it avoids the contamination of the group in case of personal crisis), besides being an extra income source (the commission from the insurance commercialization). In this model, the ideal is that the agents, being MFIs, are able to gather information about their clients to facilitate the conception of suitable products to meet their real needs. Besides, these MFIs would work as intermediaries between the insured and the insurance company, collecting the premiums, transmitting the claims and dealing with the commercial area. The insurance company absorbs the risk of the product and takes care of the entire technical part, including the agents training, the rates calculation, and the product design (according to the information received by the agent), adjusting the business model to the insurance legislation and regulation. Since the insurance company is legally constituted, if needed, it has access to reinsurance. Thus, in this model, the insurance company contributes with its insurance knowledge and the agent with clients and customer service. Since each one is responsible for a particular area, the operation as a whole tends to be more effective. There is also a limited risk to the agent, since the risk and the expertise transmission are with the insurance company. Since the agent works among the insureds (within the same environment), the adverse selection is reduced and, consequently, the transaction costs as well. Obviously, being an insurance company legally constituted, it has access to reinsurance. On the other hand, the difficulty faced in this distribution model

is to find an insurance company interested in participating in this system (we ought to remember that the micro-insurance is a more expensive insurance, especially because it involves the management of a great number of insureds through small individual premiums) and the balanced terms negotiation for all involved (MCCORD; ROTH, 2007, p. 3).

5.5. Why does the partnership model is the best one for the MFIs?¹³

Micro-insurance is a business that requires specific management competence of credit and savings – not exactly the same as the traditional insurances. With the partner-based model, the MFIs do not need to invest their resources to enable and develop an operational structure – saving financial and human resources. Besides, in this model, the MFIs can learn the business without taking on the risk of developing a new activity on their own since they lack the necessary experience. After all, here, the insurance company contributes with its expertise and transmits it to its agents enabling them to do their part (CELARIÉ, 2005, p. 12). In addition, it is possible that the legislation impedes an MFI to participate in the insurance business due to technical, operational and accounting requirements. In Brazil, for instance, in order to constitute an insurance company it is necessary that it has a minimum capital¹⁴, which is very high for most MFIs. On the other hand, only insurance companies, duly registered, can obtain commercial reinsurance. While the MFI is not regularized at the competent agency (in the micro-insurance case, at the SUSEP), it remains outside the conventional market. Finally, through the partnership between insurance companies and MFIs, these latter entities can offer their clients new products, which lower their vulnerability. This way, the possibility of no-payment is reduced, since the micro-insurance keeps at bay a good part of the financial impacts of the insured risks.

5.6. Intermediaries in the micro-insurance distribution

Having presented the four basic distribution models of micro-insurance around the world, one question remains: What is the role of the broker in this market? If the micro-insurance works with reduced premiums, disputing a space in its potential clients' budget, which has to accommodate food and clothes, is there any space left for commissions and administrative expenses? Due to this doubt, a polemic debate has recently emerged within the Brazilian market about the role of the micro-insurance broker¹⁵, apparently resolved with an explanation note, from which an extract is reproduced, as follows:

The relevant issue presented (...) was the need to develop the role of the Insurance Microbroker, or Microagent, or Microproducer, of unionized character, reinforcing even more

¹³ In this part, we developed concepts removed from Celarié (2005).

¹⁴ Until 2007, the minimum capital amount to allow an insurance company to operate within the country was R\$ 7,200,000.00 (CNSP Resolution 73, from May 13th, 2002). From January 1st, 2008 onwards, the rules from the CNSP Resolution 155, from November 21st, 2006, will apply. They state the requirement of a minimum capital compound by a standardized part (according to the region where the insurance company will operate – the amount for the entire national territory will be R\$ 15,000,000.00) and a variable part, according to the paid premium by region, the occurred claims, the adjusted equity and the insurance company's solvency margin.

¹⁵ In reality, this is a note addressed to the public by the SINCOR-RS' President, Mr. Celso Vicente Marini, concerning the subject, which was commented during the lecture made in the 4th Conseguro by the president of Fenaprevi, Mr. Antonio Cássio dos Santos. See Segs.com.br (2007) for more details.

the category. Without this opportunity, the insurance could be distributed only to the most popular classes by brokers as a natural person or a company (including the international, captive, specialized or dedicated to this business segment) duly legalized and unionized, using the space that could totally, or in part, be occupied by the so-called "microbrokers", producing benefits for all involved. The assumption that micro-insurance has low amount premiums must be noted since, for it to be economically justified, it demands a broad and mass commercialization with the lowest costs possible, making feasible the protection of these specific populations, resident and domiciled, mostly in distant places, and many times, with difficult access in such way that the microbroker, as a person from the same community, can play an important role placing and disseminating these insurances, based on the same example of the microcredit-agent found throughout the world. Thus, the objective of the micro-insurance is to offer an opportunity to those potential clients excluded from the market and, normally out of the insurance brokers' traditional spectrum, to acquire insurances not meaning, in any way, that they should stay out of the distribution process. The intention is therefore, and solely, to call attention to the fact that it is necessary to stimulate the existence of microbrokers interested in participating in the business, creating a great opportunity for the country (SEGS.COM.BR, 2007).

The issue in question is not the intermediation of the micro-insurance sales itself (and the insurances as a whole), but how to make its presence more effective among the humblest segments of the population. In each model referred previously (except the community-based model), the MFI has direct contact with the potential insured. Therefore, in relation to the insurance activity, the MFI functions as a microbroker company, and its agents, work as microagents (duly trained to sell micro-insurances). Obviously, in Brazil, specific regulations are necessary to make viable the existence of such professionals, and avoid the risk of them not being recognized by the SINCORs as legal brokers exercising the activity.

Internationally, microbrokers exist in two formats. The first one and more obvious is the *micro-insurance agents linked to an insurance company*. Under this format, the MFI indicates people to the insurance company, who belong to a target-community, to be trained to work as microbrokers. These microbrokers would be responsible not only for the sales, but also for the premium received from the insureds, acting in a similar way to direct marketing¹⁶ (CHURCHILL, 2006, p. 434-435).

The second format is the *independent intermediaries of micro-insurance*. Under this format, essentially, the micro-insurance mimics the traditional insurance marketing, since the independent intermediary might be an

¹⁶ Sales and distribution models used by cosmetic and domestic convenience companies, such as Natura, Avon and Tupperware, in which the agents sell products in their spare time to their relatives, friends, and neighbors.

individual or a corporate structure, collaborating with one or several insurance companies. The difference between the traditional brokerage and the microbrokerage, here, is found in the reduction of the transaction costs and minimum commission margins, compensated by the permanent search of large client groups through alliances with MFIs, rural banks, unions, cooperatives, and even religious organizations (CHURCHILL, 2006, p. 436-437).

6. An Overview of Brazil¹⁷

If we consider the population, the geographical size and the economic figures alone, Brazil has an expressive potential market for micro-finance. Brazil has the fifth largest territory in the world, with 8,514,876.59 square kilometers. It has the fifth largest population, with more than 184 millions of inhabitants, and a GDP equivalent to R\$ 2.322 trillions (US\$ 1,366 trillion, approximately) in 2006. It is the biggest economy in Latin America and the tenth in the world scale, according to the International Monetary Fund's statistics for 2006 (IMF, 2007).

The social-economic characteristics of Brazil also suggest a promising environment for the micro-finance activities. Although Brazil is the eighth biggest economy in the world, and its income exceeds the majority of the Latin American countries, the unequal national income distribution is placed among the most prominent ones in the world – the 10% from the richest population of the country profit 48.9% of the total income. This sloping in the income distribution means, despite its wealth, that Brazil is the country in Latin America that holds the largest number of poor people. Around 34% of the Brazilians live below the poverty line, a percentage similar to countries as Botsuana, Dominican Republic and Panama (NICTER, 2002, p. 9).

Curiously, this high poverty incidence does not necessarily mean that Brazil has today a great offer of micro-finance products. The micro-finance in Brazil has experienced a slow pace of growth, with low penetration rates (only 2% from 8.2 millions of eligible microentrepreneurs). The majority of micro-finance institutions have been keeping the operation in small scale.

Traditionally, some factors have been cited as an explanation for the relative low development of the micro-finance industry in Brazil, including: the macroeconomic instability prior to the hyperinflation control in 1994; the traditional strong credit lines, by the Government's subventions; the still incipient regulatory scenario in spite of the recent advances; a credit market for highly sophisticated consumers and the lack of a clear "demonstration effect" in micro-finance (NICTER, 2002, p. 9).

¹⁷ The statistics data of this section was extracted from the documents freely available at IBGE's website – Instituto Brasileiro de Geografia e Estatística – Brazilian Institute of Geography and Statistics (www.ibge.gov.br), and at ABEP's website – Associação Brasileira de Empresas de Pesquisa – Brazilian Association of Research Companies (www.abep.org). See bibliographical reference for the documents.

Conger (2001) points out what is called “enigma of the big countries”, a phenomenon that, back then, was repeated in countries as diverse as Brazil, Argentina, China, India, Mexico and Nigeria, all emergent countries with big economies and immense financial potential, but with Lilliputian development in micro-finance. Besides the factors indicated in Nichter (2002, p. 9), which were reproduced above, other aspects are also indicated by the cited authors as a cause for this phenomenon: lack of support from microcredit promoter entities (which prefer to invest in poorer countries), the similarity between their micro-finance fomentation policies (they simply ignore the fact that the majority of their economically active population is poor, focusing in small niches), and the general idea that the Government is responsible for taking care of the problems (there is the hope for assistencialism, instead of search for opportunities). This understanding is shared by Soares (2007, p. 24). Christen (2001, p. 3) also points out the absence of MFIs with great credibility in these countries, as well as the issue about opportunity cost.

The Brazilian picture is indeed very intriguing, especially taking into account that the financial market holds a fast growing industry of credit to consumers¹⁸, having focused even more on the low-income clients. The credit companies as well as the retail stores, when expanding their client's database, have made their requirements more flexible to fit into these clients' reality. However, this change of focus is a very recent tendency which emerged due to the success of some retail networks, and besides the need to be consolidated within the market, they have not been disseminated across the other segments of the economy.

Today, the situation in the country still fits perfectly into the Brusky and Fortuna's description (2002, p. 50-53): inappropriate micro-finance products in relation to the clients' needs and inaccessible MFIs for low-income populations (either due to the excess of requirements or to the ignorance of its existence), as well as the obstacles due to these people's cultural perception over credit¹⁹. It is, therefore, an awkward scenario for micro-finance.

6.1. Statistics

In order to better understand the Brazilian picture, we present here some statistic charts, which will allow a good visualization of the current scenario.

The chart ²⁰ shows the Brazilian overall population, divided into age groups. In this chart, from an estimated total of 184.326.387 inhabitants, the three older age groups represent non-regular intervals, whereas the five younger age groups show regular intervals of 5 (five) years each. Therefore, we have here a distortion with the older age groups. It is also interesting to observe that the five youngest age groups keep certain uniformity that indicates a low and standardized infantile mortality during the 25 years prior to the research in use. According to the chart, we can

¹⁸ Nichter (2002, p. 12) points out a fast growth of the credit to consumers in comparison to the working capital, just considering the period between 1999 and 2002.

¹⁹ That is, the popular understanding that the credit is an agreement between the seller and the buyer to divide the property acquisition payment (with no relation to financial operation), and loans seen as a way to finance through money transfer from the loaner to the taker (BRUSKY; FORTUNA, 2002, p. 52).

²⁰ Data extracted from the National Research by Domicile Samples (IBGE).

observe in 2005 that 45.52% of the Brazilian population was born in 1981 or after this year, which characterizes Brazil still as a country of young people. On the other hand, about 9.87% of the population was 60 years old or more, whereas 17.17% was 9 years old or less, which shows that, even with the aging population noticeable in the last few years, there is a larger market for products and services oriented towards children than towards elders.

Chart 1 – Brazil – Resident Population 2005

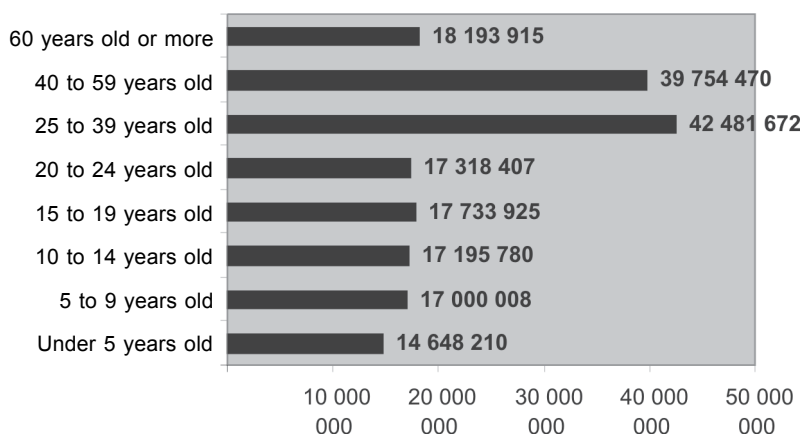


Chart 2²¹ considers people at the age of 10 years old or more, according to the monthly income classes (figures from 2005²²). This chart includes incomes of any nature, including employment, allowances, pensions, and any other social benefits. For that reason, this chart is not suitable as a way to measure the economically active population²³.

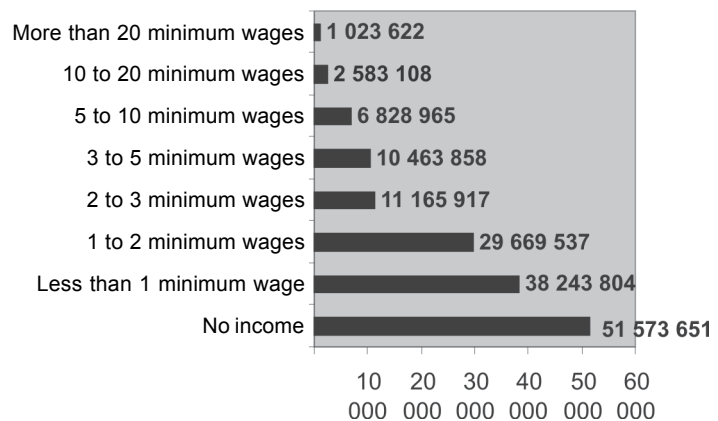
Here, from an estimated total of 151,552,462 people, 34.03% are within the group so-called as “no-income”. The large income concentration becomes evident through this chart, since only 0.68% has an income above 20 minimum salaries. On the other hand, the first three salary layers added together (ignoring the “no-income” group), and comparing the number of people within these layers as a total of the Brazilian population, we have 42.9% of the Brazilian citizens receiving up to 3 (three) minimum salaries.

²¹ See note 22.

²² The minimum salary for 2005 was R\$ 300.00 – USD128.17, exchange rate USD1.00 = BRL2.3407 on 12/30/2005. For 2007, the minimum salary was R\$ 380.00 – USD206.42, exchange rate USD1.00 = BRL1.8409 on 09/27/2007.

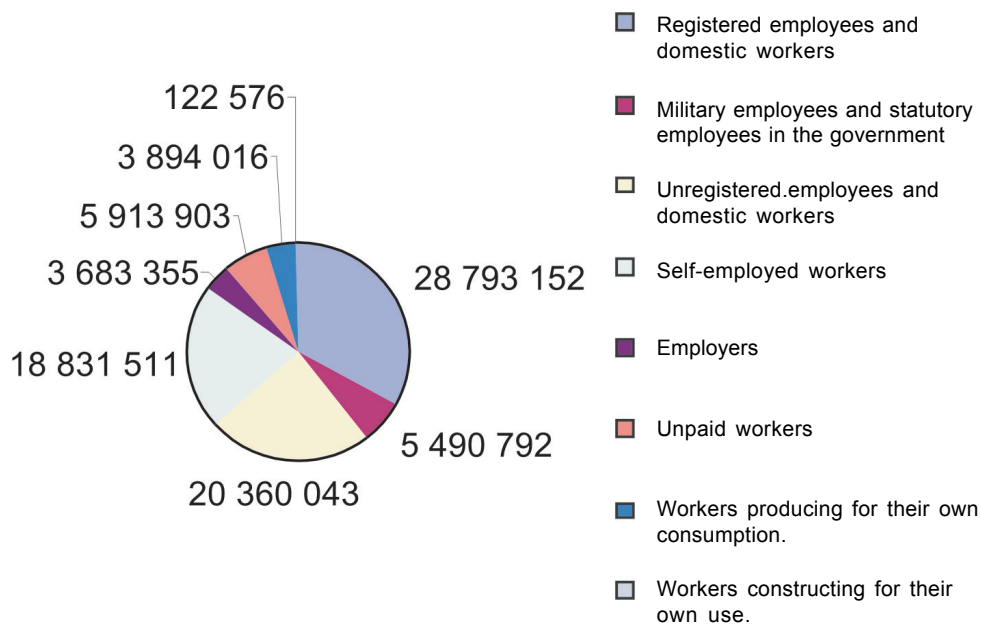
²³ According to IBGE, the economically active population detains the potential of labor which the productive sector can count on, i.e., the occupied population (those people that, in a given referential period, worked or had a job but did not work. For instance, people on vacation), plus the unemployed population (those people that did not have a job, in a given referential period, but were willing to work, and, took the initiative of, for instance, consulting other people, newspapers, etc.).

Chart 2 – Brazil – income of people older than 10 years old



Probably in Brazil, micro-insurance products would have as a target public, people with monthly income of up to 3 minimum salaries according to the World Bank representative (UOL, 2007). This income layer is equivalent to a universe of more than 79 million potential clients of a micro-insurance product, and about 80% of all Brazilians with some income source.

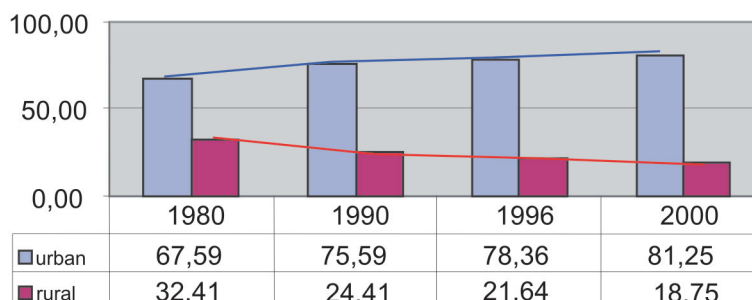
Chart 3 – Brazil – people by occupation



On Chart 3²⁴, we have the occupied population (from an estimated total of 87,089,348 people for 2005), classified by practiced occupation. The fact that the occupied population responds for only 47.25% of the Brazilian total population for the same period deserves attention.

The workers in the informal economy (i.e., workers and employees who work with no formal register or are self-employed) totalize more than 40 million people. If we exclude workers with no salary, workers who produce for their own consumption, and workers in the construction for their own use (approximately 9 million people), then, we can see that the informal economy responds for more than half of the workers with some occupation.

Chart 4 – Brazil – Urban Concentration 1980 - 2000



On Chart 4, we see an increasing urbanization of the Brazilian population in the last 20 years, during the 20th Century. This tendency, verified in Brazil throughout that century, became even more pronounced due to the accelerated industrialization of the big centers. Furthermore, this is a typical trait in Latin America, i.e., the urbanization degree of the society, or more specifically, the substantial urban nature of poverty (DERCON, 2004, p. 6). It does not mean that there are no destitute people in the rural zones; Chart 4 simply reflects the urban concentration that occurred throughout this last century, as well as the income concentration and the social misbalance of this area.

Table 1 – Brazil – Familiar average income by class²⁵

CCEB Class 2008	Familiar average income
Class A1	R\$ 9.733,47
Class A2	R\$ 6.563,73
Class B1	R\$ 3.479,36
Class B2	R\$ 2.012,67
Class C1	R\$ 1.194,53
Class C2	R\$ 726,26
Class D	R\$ 484,97
Class E	R\$ 276,70
Total Average Income	R\$ 1.432,84

²⁴ See note 22.

²⁵ Brazil 2008 Economic Classification Criteria (BECC), using figures of 2005. The BECC measures the consumption capacity of the researched people (2007).

On Table 1, we observe the distribution of the average income according to the 2008 Brazilian Economic Classification Criteria, BECC, to be used by the research institutes from 1st January 2008 onwards (ABEP, 2007). We emphasize (using a shadow format) the classes of interest for micro-insurance. This Table indicates that the familiar average income of Class C1 is within the 4 (four) minimum salaries limit – above the current 3 (three) minimum salaries²⁶, and a little below 4 (four) minimum salaries of 2005²⁷. Thus, the micro-insurance target should consider those people who belong to classes C, D and E.

6.2. Regulation about popular insurances²⁸ in Brazil

According to the information disclosed by SUSEP in May 2007, the only products that have specific regulation are the “popular collective life insurance”²⁹ and the “popular car insurance”³⁰ (SIMÕES, 2007, p.14).

According to Simões (2007, p. 14), the popular collective life insurance would have as a target the bank account holders with income inferior to R\$ 1,000.00, or around 3 minimum salaries. This insurance would cover natural and accidental death, plus additional coverages, such as funeral expenses, pharmacy and “basic basket” (a staple monthly food supply). This modality would have a minimum premium of R\$ 6.00, and a minimum insured capital of around R\$ 3,000.00.

The popular car insurance aims at covering 10 to 20 year old cars. This insurance is characterized by the coverage acquisition of a given capital (payment of the fixed amount in national currency stipulated by the parties at the moment of the insurance purchase). However, the underwriting criteria for the popular car insurance would be more severe than that of the traditional product (it would include mandatory inspection and would have a lower acceptance rate). On the other hand, in order to make the premiums viable, with lower costs in relation to the traditional insurance, the services have to be reduced too. The deductible should be higher with fewer options, giving preference to a network of accredited garages for car repair.

In the rural area, the Ministry of Agrarian Development developed in 2004, together with the Bank of Brazil (Banco do Brasil), the Familiar Agriculture Moneylender Insurance. It is exclusively for credit takers through PRONAF – Programa Nacional de Fortalecimento a Agricultura Familiar (National Program to Strengthen Familiar Agriculture), for rural credit operations (mandatory) covering Death and Extra Indemnity.

In relation to other insurance sectors, for instance fire and other coverages (Comprehensive), there are no specific norms for micro-insurance, nor segregation of statistic data sent to SUSEP. The products are the traditional ones when commercialized, only using alternative commercialization channels and limited to lower capitals (SIMÕES, 2007, p.18).

²⁶ That is, R\$ 1.140,00. See note 25.

²⁷ That is, R\$ 1.200,00. See note 25.

²⁸ See note 3. The information in this section is based on SIMÕES (2007).

²⁹ SUSEP Circular 267/2004.

³⁰ SUSEP Circular 306/2005.

6.3. Micro-insurance products in Brazil³¹

Among the products that we could consider as micro-insurance that are commercialized in Brazil³², we point out the Funeral Expenses Aid, Life and Personal Accident, Credit, Home (fire, lightning and explosions), Familiar Agriculture Moneylender, and Popular Car Insurance (both mentioned previously). This relation is merely exemplificative³³. However, according to the SUSEP's information, the most popular insurance in Brazil has been Funeral Expenses Aid (SEGUROS.COM.BR, 2007). Even if Credit insurances, especially moneylender products, have increased expressively in 2007 (BRITO, 2007).

The currently used distribution channels include retail store chains (either national or regional), banks, ATM machines, public convenience rendering service companies (for instance, telephone operators, water providers, etc.), unions and social and professional associations, as well as churches and neighbor associations (especially Life products).

The great majority of the distribution channels presented here follows the same partnership model. The distributions have had great success through retail store chains (especially for credit products), banks and ATM machines³⁴.

7. Commercial micro-insurance challenges

The following difficulties have to be faced when a micro-insurance line is implemented:

- a) *High operational costs*: In the micro-insurance, the individual premiums are necessarily small. These small premiums are compensated by the increase of the clients' portfolio. However, the operational cost becomes higher, since there is the need to manage contracts with a large number of insureds.
- b) *Challenges for the insurance business in general*. In any insurance line, there is the possibility of moral hazard (insured property carelessness), adverse selection (bad risks, with random possibility above the average range), fraud (bad-faith act aiming at deluding others), and abuse (improper insurance use). Micro-insurance is not an exception.
- c) *Lack of institutional and regulatory patterns*. Since in Brazil the micro-insurance does not have specific regulation (except car and Life in Group, for now), a certain degree of legal uncertainty may arise in relation to its possibilities, as well as some political arbitrariness over its fiscalization and lack of official certification.

³¹ The information about micro-insurance mentioned in this section was collected from news in newspapers during the first semester of 2007.

³² We could have included in this relation the Extended Warranty Insurance (which fits in with the popular insurance notion since it reaches the population of Classes C, D and E; however, according to OIT, it would not fit within the micro-insurance market – See note 3).

³³ We identified some insurance companies and broker companies, which work with mass products for Classes C, D and E. They are: Aon Affinity Latin America, Marsh & McLennan Companies, Porto Seguro, Chubb do Brasil, Luizaseg (Cardif and Magazines Luiza) and American Life.

³⁴ We would like to point out that such distribution channels are reached by partnerships among broker companies and retail stores or banks.

- d) *Natural catastrophes exposure.* There is always the possibility of catastrophes, but every insurance company tries to avoid damaging events of high frequency. This concern also has to be present when we deal with micro-insurance, although in Brazil we do not have to worry about this matter.
- e) *Conflict of Interests between partners.* In the micro-insurance, there is always the possibility of a conflict of interests between partners who are interested in the humanitarian aspect (especially MFIs) and partners interested in the commercial aspect.
- f) *Risk analysis and calculation.* For the segments whose needs are met by the micro-insurance, there is generally a lack of data to allow a detailed analysis of the involved risks, which makes the conception work and the product design much harder.
- g) *Balance between needs and possibilities.* When a micro-insurance product is conceived, some situations are envisioned where the insured needs an insurance, but the coverage of which is not viable. Balance is necessary between them.
- h) *Sustainable agreements between the insurance industry and the Government.* Since the micro-insurance answers, primordially, the demands of humanitarian proposals it is interesting that the insurance industry should obtain subvention from the Government for such products, without interference or omission from either party.
- i) *Language used in the insurance policy.* Micro-insurance has to be accessible for its clients, particularly in relation to the way the clauses are written as far as coverage is concerned. A comprehensive study in Brazil is necessary in order to elaborate specific clauses and conditions to answer the requirements of the Código de Defesa do Consumidor (Consumers' Defense Code), and to adapt the technical terms to a simpler writing. This is one of the greatest challenges for the business.
- j) *Administration and control.* One of the biggest challenges of the micro-insurance is to manage and control the insured, since the business is only viable if that happens. It is necessary to have in mind that it is not possible to merely apply the traditional insurance business model. It is essential that adaptations are made to cater for the differentials of the insureds.
- k) *Lack of prevention culture and risk mitigation.* Low-income people are exposed to many risks and although they try to administrate it, the risk is often ignored until it is too late. Thus, one of the functions of the micro-insurance is to discipline these people about how to prevent against risks or, at least, to diminish their impact.
- l) *Premium collecting model.* This is perhaps the most delicate matter of all that was mentioned here, since we refer to people with low salaries who are often late with the payment of some bills. For the micro-insurance to be viable it is necessary, on the one hand, an efficient premium collecting to avoid non-payments, and on the other hand, flexibility for the payment to be made respecting the insured's possibilities.

8. The reinsurance role for micro-insurance

The value of the reinsurance is in increasing the insurance company's capacity to conduct its businesses while reducing the long term underwritten risk costs (CHURCHILL, 2005, p. 525). And this is valid for insurance companies that operate in traditional patterns as well as for

other insurance business models. Thus, reinsurance is able to offer several benefits for insurance companies willing to operate with micro-insurance. Both insurance and reinsurance companies have a fundamental role to play if micro-insurance projects are to succeed. They can concretely contribute, for example, by implementing business processes that may, over a period of time, reduce the costs related to the underwriting procedures for low-income people, since the micro-insurance companies could expand the financial capacity of their businesses and underwrite more and bigger risks. The successful partnerships would bring more businesses for both parties. However, reinsurance is only one, among many, of the current alternatives to increase the micro-insurance underwriting capacity, available only for insurance companies legally established.

The reinsurance is able to provide for the micro-insurance companies the following particularities:

- a) Underwriting experience, especially for insurance companies derived from MFIs;
- b) Access to world resources and experiences, including products development, distribution channels and premium collecting mechanisms;
- c) Access to world resources and experiences from its own corporate group, as well as from international partners;
- d) Higher financing capacity, since it allows the insurance company to transfer part of its risk to the reinsurer;
- e) Catastrophe protection, limiting its effects and protecting the insurance companies from big transitory fluctuations of the financial results;
- f) Long-term stability, since it balances out the insurance companies' accounts taking responsibility over part of its flotation risks in the loss ratio, its portfolio changes and its underwriting errors; and
- g) Insolvency protection, generating a stronger financial basis for the insurance company, since it increases its liquidity.

9. Conclusion

From this brief study, we verified that micro-insurance is still an area not much explored (not only in Brazil), even if it accommodates a high number of potential insureds. We also concluded that micro-insurance is projected for underdeveloped and developing countries where the social disproportion is high. However, many initiatives that can be considered prior to micro-insurance occurred in developed countries – and we actually make reference to initiatives in the beginning of the 20th Century. This change of focus is interesting, having its origin in the modern notion of micro-finance which appeared during the seventies (SOARES, 2007, p. 14). Today, it is impossible to dissociate micro-insurance from micro-finance.

Curiously, there are two ways to see micro-insurance: one, as a way to soften the social disproportion so that the society becomes more egalitarian; the other, as a new threshold of the insurance businesses, only waiting to be crossed.

Taking into account all that was presented and commented so far, we do know that the key-principles for the micro-insurance success are massification, alternative channels for sales and premium low prices. Without these three principles, there is no way micro-insurance can succeed. But, at least in Brazil, there are still some difficulties to overcome:

the most severe ones are the lack of specific regulation for micro-insurance operations in general, the fiscal burden (which can be too heavy to yield profit in the micro-insurance operations), and the sustainability of the operations itself. It is also necessary to overcome obstacles such as the limited distribution channels, the adherent supervision, the requirements (which have to be simplified), the explicit need of solvency mechanisms and a closer approach to the consumers' language.

Once such obstacles are surpassed, and considering the recent goodwill demonstration from the Government related to this matter³⁵ not forgetting the interest showed by the insurance market, we do not see how micro-insurance would not succeed in Brazil. In spite of attracting attention lately, Brazil included, most of the material about the subject comes from lectures, with the rare exception of Craig Churchill's work, cited by us several times.

Through this short study presented here which, far from exhausting the subject, serves as a simple introduction for the many aspects of the micro-insurance business, we hope to stimulate other authors to study in depth this new insurance field.

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³⁵ “The Federal Government intends to support the Micro-insurance development in Brazil. That is what the Planning, Budget and Management Minister, Paulo Bernardo, who was the opening lecturer of the 4th Conseguro – Conferência Brasileira de Seguros, Resseguros, Previdência Privada e Capitalização (Brazilian Conference of Insurance, Reinsurance, Private Pension and Annuities), informed [promoted by the Federação das Empresas de Seguros e de Capitalização (Brazilian Federation of Insurance and Annuity companies), held in Rio de Janeiro, from 12th to 14th September of 2007].

The Minister said that the Government wishes to act as a partner and to regulate the Micro-insurance, and that 'he will bring numbers which interest the entire population'. 'We want to help the development of this insurance market that, surely, is one additional element to push the sustainable growth of the country' (FENASEG, 2007). Brackets ours.

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