Low Rate of Penetration for Life Insurance: A Comparison of East African Countries

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Abstract

As per Ethiopian demography the ratio of dependent population on earning age population is not much different i.e. 41.5 percent people are in 0-14 age category and in the 15-64 age category, there are 55.2 percent people. Certainly the life of this 55.2 percent people is very important for the rest of Ethiopian population and to avoid any uncertainty these working age people must be insured. When we see life insurance sector's contribution to GDP(penetration rate) its only 0.41 percent, this becomes more disturbing when we see that only 0.1 percent population have access to insurance services (life and general both).

Many writings on development studies suggest about the importance of savings and its role in countries growth and development. There are sundry of ways in which saving can be invested, insurance is one of them. By purchasing a life insurance product, the person can save a part of his income and earn interest by foregoing present consumption and at the same time can insure his future. Insurance is the most effective risk mitigation mechanism to remit the vulnerability of the people from the impacts of disease, disability, untimely death and natural catastrophes, in a developing country like Ethiopia the need for such a safety net is much greater particularly at the low income levels where vulnerability to risk is much greater and social security programs are not effective.

This study intends to discuss causes for inhibition of life insurance penetration rate, we would also compare life insurance sector's growth of Ethiopia with other East African nations.

This paper is arranged in the following fashion, the first section deals with the background and introduction of the study. Section two will illustrate review of literature and section three will enumerate major findings. Fourth section will discuss conclusion and policy suggestions.

KeyWords: *Gross savings, Life insurance, Penetration rate, Per capita income*

I. INTRODUCTION

A report by KPMG, Africa limited, 2014 says that the world's insurance industry is dominated by wealthiest countries, in particular G7countries have their dominance in this sector. Emerging economies have recently gained attention as they are showing increase in penetration rate. Therefore it comes with no surprise that African insurance market is still underdeveloped except few countries like South Africa. Despite of that there is a surprising thing in African insurance sector and that is penetration rate for life insurance is very low here whereas it is contrary in case of other world. Since many of world's most poor countries belong to African continent, people here cannot afford insurance premiums other than this there are some more reasons reported by the report for the performance of insurance sector in Africa for instance People do not have trust in financial service providers. Given the low per capita income one may imagine how challenging the business environments are, there is not enough incentive for multinational companies to enter African markets and develop the sector. There is also a lack of reliable information making it very difficult to assess peoples credit worthiness. Legal and judicial systems are poor. There is a lack of human capital and expertise. Shallow financial markets make it difficult to raise enough money to capitalize insurance / re insurance companies. And communities often make use of informal forms of insurance rather than using the service of formal insurance.

Ethiopian insurance sector has a long history however history of this sector can be traced formally from 1905. Insurance industry is growing with a satisfactory rate except the life insurance segment as the penetration rate for this segment is 0.3 percent which is much below the average of African continent which is deplorable. Although in Ethiopia there were and still are there traditional institutions of society welfare known as "IDIR" and "EKUB". These traditional forms have some similarity with the modern age insurance services. To understand in case of "EDIR" people from an association where by each members contribute affixed sum, normally to a common fund from which predetermined compensation are paid to members up on occurrence of unforeseen event such as death of family members or relatives. The compensation are meant to cover expenses that a member would incur as the result of the incidents. The EDIR also owns physical assets like tents, household goods like plates, cups, chairs, and other were used during the periods of mourning. The other type of traditional saving is "EKUB" where member contribute affixed sum of money weekly, or monthly to a pool of fund and lots are cost where up on the winners receive the money so collided and used for another member at a premium, if something happens to a member, who had already taken the money, that would not enable him to continue contributing to the fund, his guarantor will have to be held responsible or liable.

From 1975-1994 was the period of state monopoly for Ethiopian insurance sector. The state owned Ethiopian Insurance Corporation (Henceforth, EIC.) which was established in 1975 after the then operating thirteen private companies were nationalized by proclamation no. 26/1975 was operating in the market. National bank of Ethiopia by the virtue of proclamation no 86/1994 (currently revised) is authorized to license and supervise insurance business. The insurance proclamation no. 86/1994 was a landmark in the history of Ethiopian insurance industry. Since then fifteen private insurance companies have been established. It is interesting and surprising to note that until 1994 EIC was enjoying 100 percent market share but due to the entry of new private players its market share is reduced to approximately 50 percent unlike India where Life Insurance Corporation which is a state monopoly up to 1999-2000 was enjoying complete control on the market share but the new players entered and expended the market and therefore market share of Life Insurance Corporation was not much affected. It is a indication that the private firms did not put much effort to create its own market but they shared the existing market with already existing company EIC. In other words these firms are supposed to involve in awareness campaign and also for all companies it is highly desired that they should innovate and design life insurance products best suited to the need of low and middle income Ethiopians.

A. *Objectives of the study*

In this study we are looking for reasons for such a low rate of penetration despite the fact that in recent years Ethiopian economy is growing with a pace why insurance sector particularly life insurance is not picking up fast. Specific objectives of this study are as follows:

i) To discuss causes for low penetration rate.

ii) To compare life insurance sector penetration rate with other economic indicators such as GDP and per capita, in case of Ethiopia, Kenya and Tanzania.

iii) To suggest efforts to be made for mobilization of small savings and even for mobilization of saving through innovative products.

II. REVIEW OF LITERATURE

Ethiopian Financial Sector is about banking and insurance services. Both the sectors performance was considered to be stable from last five to ten years. In 2012/13 there was 19 commercial banks and 15 insurance companies from 17 and 14 respectively in 2011/12 and the no. is growing every year. A list of all insurance companies in both life and non life sector is given below:

List of Life Insurance Providers in Ethiopia

S. No.	***Name of the company***	***Year of Establishment***
1.	Ethiopian Insurance Corporation	1975
2.	National Insurance Company of Ethiopia	23-09-1994
3.	Awash Insurance Company S.C.	01-10-1994
4.	Africa Insurance Company S. C.	01-12-1994
5.	Nyala Insurance Company S. C.	06-01-1995
6.	Nile Insurance Company S. C.	11-04-1995
7.	Global Insurance Company S. C.	11-01-1997
8.	The United Insurance S. C.	01-04-1997
9.	NIB Insurance Company	01-05-2002
10.	Lion Insurance Company S. C.	01-07-2007
11.	Ethio-Life and General Insurance S. C.	23-10-2008
12.	Oromia Insurance Company S. C.	26-01-2009
13.	Abay Insurance Company	26-07-2010
14.	Berhan Insurance S. C.	24-05-2011
15.	Tsehay Insurance S. C.	28-03-2012

Source: National Bank of Ethiopia – Insurers

Among the fifteen players EIC is the biggest player however life insurance segment definitely need attention. A study conducted by Daniel and Tilahun in 2013 on "Specific factors that determine insurance companies performance in Ethiopia" provides the exposition about relationship between return on total asset (ROA, as a dependent variable) and age of company, size of the company, growth in writing premiums, liquidity, leverage and loss ratio are taken as independent variables. Study reveals that company size, tangibility and leverage are positively related with return on total asset, whereas loss ratio is negatively related with ROA. Therefore as per this study company size, loss ratio, tangibility and leverage are important determinants of performance of insurance companies.

Sadhak 2006 (cited by mamtasingh, 2011) has observed that there is a very significant relationship between the demand for life insurance and various macroeconomic variables. High growth of GDP induces an economic effect through higher per capita and disposable income and savings, which in turn create a favorable market demand for life insurance also provides support to the capital market and savings data pertaining to Indian life insurance and macroeconomic variables broadly indicate a close relationship and interdependence between macroeconomic variables and life insurance demand.

Various similar studies have been conducted all across the world on buyers behavior towards life insurance product and they support the finding of Sadhak 2006. For example a study by Mark. J. Browne (1993) concluded that demand for life insurance is positively correlated with income. ZakariasMekonnen (2010) also certifies factors such as age of the buyer, monthly income, and number of dependents in family does have a positive and significant influence on purchage decision. Other than these Mekonnen provide an exposition on how religion influences purchase decision for life insurance product. Some researchers have shown how educational status of the buyer has significant influence on their attitude towards life insurance.
Therefore to understand the life insurance sector and its performance we will compare macroeconomic variable such as GDP growth rate, Per capita and savings of Ethiopia with comparatively better performers in terms of penetration rate i.e. Kenya and Tanzania.

III. METHODOLOGY

This study is of descriptive nature. We have looked at the trend of savings and GDP growth rate for last nine years i.e. from 2005 to 2013 and also we have seen the trend of per capita income growth rate for last nine years as to compare and understand what is pulling the penetration rate of life insurance back in case of Ethiopia.

To compare East African countries we have basically taken three countries, Ethiopia, Keyna and Tanzania as these countries are growing with a sustainable rate of growth since last ten years.
Data utilized in this study is secondary, which is collected from World Bank, National Bank of Ethiopia and company websites in case of branch availability in Ethiopia.

Comparison of Various Macroeconomic Factors for East African Countries

Table: GDP growth (annual %) and Gross Savings (% of GDP)

Country name	Ethiopia		Kenya		Tanzania	
GDP growth and Gross Savings	GDP	Savings	GDP	Savings	GDP	Savings
2005	11.8	21	5.9	17	7.4	17
2006	10.8	18	6.3	16	6.7	17
2007	11.5	26	7	17	7.1	23
2008	10.8	25	0.2	14	5.6	22
2009	8.8	22	3.3	15	5.4	18
2010	12.6	28	8.4	13	6.4	19
2011	11.2	33	6.1	11	7.9	19
2012	8.6	31	4.5	11	5.1	17
2013	10.5	-	5.7	-	7.3	17

Source: World Bank: Data/ Table

However among all African nations after South Africa performance of Kenyan life insurance has gained felicitation as it is most innovative country in African continent despite of that even Kenyan life insurance sector is not picking up robustly. A comparative table is given below which gives insight about life insurance penetration rate of three countries and population, National income and per capita in USD.

Table: Country wise penetration rate, Population, GDP and Per capita (2013)

S. No.	Country Name	Life Insurance Penetration Rate	Population in Millions	National Income in Billions (USD)	Per capita, PPP (USD)
1	Ethiopia	0.3	94.1	47.53	1,380
2	Keyna	3.17	44.35	55.24	2,780
3	Tanzania	0.9	49.25	43.65	2, 430

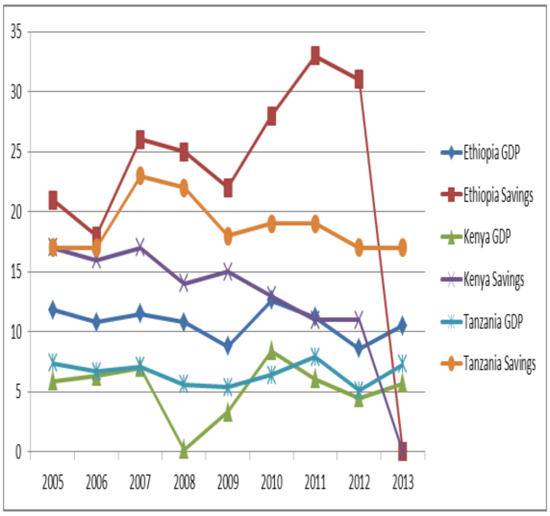
Source: NBE and World Bank/ country profile

However there is a sustainable trend in per capita income (world bank/data/GNI per capita) of an average Ethiopian but as compared to Kenya and Tanzania it is lower. Probably this is one of the reasons for low rate of penetration for life insurance sector in Ethiopia with the background of Mark j. Browne's study which establishes a positive relation between insurance demand and per capita income of the buyer.

Ethiopian economy is growing with a sustainable growth rate of approximately ten percent from a decade. Economic theories suggest that for sustainable future the relation between GDP growth rate and Financial sectors growth should be positive. In other words we may say that savings must grow to support the GDP growth, in particular institutional savings play a vital role in financing investments domestically. If we see last ten years data for GDP growth rate and domestic savings a same direction trend can be found for these variables.

Other than Ethiopia Kenya and Tanzania are also showing positive relation among GDP growth and growth rate of savings in below given table:

Caparison of Annual GDP growth and Gross Savings as % of GDP



Source: Prepared by the author

The graph shows that Ethiopia's economic growth is better than Kenya and Tanzania and therefore we cannot say that low rate of life insurance penetration is a result of poor GDP growth. To see the comparative picture of other macroeconomic variable and its relation to the given low penetration rate we compared savings of these countries with their per capita income.

Table: Gross Savings (% of GDP) and Per capita, PPP(Current international $)

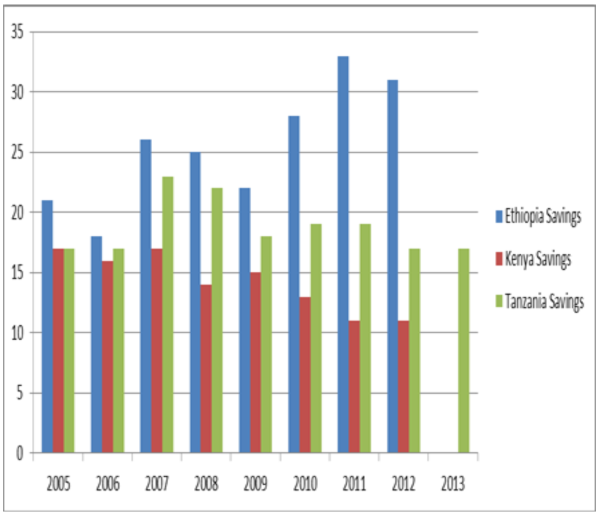
Country name	Ethiopia		Kenya		Tanzania	
Gross savings and Per Capita on PPP	Savings	Per Capita	Savings	Per Capita	Savings	Per Capita
2005	21	650	17	1990	17	1590
2006	18	730	16	2120	17	1710
2007	26	810	17	2270	23	1840
2008	25	890	14	2260	22	1910
2009	22	950	15	2290	18	1980
2010	28	1060	13	2440	19	2060
2011	33	1170	11	2590	19	2210
2012	31	1260	11	2670	17	2270
2013	-	1380	-	2780	17	2430

Source: World Bank/Data/Table

much below. Probably this is one of the reasons for low rate of penetration for life insurance sector in Ethiopia as indicated in the study by Mark J. Browne that demand for life insurance and income of the buyer are positively related.

Other than low per capita income availability of branch offices and awareness about life insurance product and how it is different than traditional EDIR and EKUB are also important causes for low rate of penetration. In Ethiopia, if we pay attention on branch offices location, out of total branches 50 percent of them are concentrated in Addis Ababa. It translates that major part of Ethiopia does not have access to the branch offices for any insurance product a table given below shows availability of branch offices for all 15 insurance companies.

Comparison of Gross Savings (% of GDP)
Comparison of Per Capita Income at PPP (Current International $)



Source: prepared by the author

Although there is a sustainable trend in per capita income of an average Ethiopian but as compared to Kenya and Tanzania its

Source: Prepared by the author

Table: No. of Branch offices in Addis Ababa and other Regions

S. No.	Company Name	No. of Branches in Addis Ababa	Regional Branches with their Name
1.	Ethiopian Insurance Corporation	6	9
2.	National Insurance Company of Ethiopia	10	12
3.	Awash Insurance Company S. C.	23	12
4.	Africa Insurance Company S.C.	4	8
5.	Nyala Insurance Company S. C.	17	9
6.	Nile Insurance Company S. C.	15	11
7.	Global Insurance Company S.C.	7	6
8.	The United Insurance S. C.	6	10
9.	NIB Insurance Company	1	22 Sales outlets
10.	Lion Insurance Company	7	6
11.	Ethio-Life & General Insurance S.C.	12	1
12.	Oromia Insurance Company S. C.	6	5
13.	Abay Insurance Company	9	7
14.	Berhan Insurance S.C.	7	Information unavailable on Webpage
15.	Tsehay Insurance		Webpage unavailable
Total		**130**	**118**

Source: Company Websites

The above given table gives a clear idea that most of insurance companies have concentrated their business in Addis Ababa as more than 50 percent branches are in Addis Ababa.

IV. CONCLUSION

It should be understood clearly that savings through life insurance guarantee full protection against risk of death of the saver. Also in case of demise, life insurance assesses payment of entire amount assured whereas in other savings scheme only the amount saved (with interest) is payable. This is one thing other difference between life insurance and other mode of saving is that life insurance allows long-term savings since payments can be made effortlessly because of easy installment facility built into the scheme. In case of insurance it is easy to acquire loans on the sole security of any policy that has acquired loan value. Besides, a life insurance policy is also generally accepted as security even for a commercial loan.

Ethiopia is a peaceful country and a growing economy, the fruits of its economic growth must reach to its people. Insurance being a financial service not only mobilize small savings of the household but these tiny savings can be used for nation building and therefore economy as well as its people will be benefited. However it also true that financial market of Ethiopia is not well developed for instance there is no stock market, reinsurance companies are not present therefore it is a challenge in front of Ethiopian insurance companies to expand and at the same time be profitable.

International Experiences suggest that the penetration rate starts growing at a certain level of per capita income, and here Ethiopia will certainly take time to reach, it is needless to say that the economy is moving in right direction. Nonetheless some timely moves may boost the growth of life insurance sector for instance if Ethiopian companies can collaborate with the Kenyan companies to learn their lessons of how to reduce transaction cost, Life insurance density (The ratio of premium per capita) could be improved. According to Business Monitor International (BMI) Kenyan companies have been more innovative than those in other African countries. For instance Kenyans can pay premium via their mobile phones through platform like M-PESA and Airtel money. It is also recognized in New York Times in an article about Kenyan innovation which says “writing tiny policies in only possible rather feasible if the process of signing people up, verifying claims and making payouts is nearly free” and thanks to electronic weather stations and mobile phones it is sufficiently cheap.

Another positive initiative could be taken by FDRE government by introducing tax benefits for life insurance policy holders, it may also boost penetration rate as well as insurance density.

African continent today is considered to be less developed for life insurance segment and Ethiopia is among the poor ones in terms of rate of penetration nevertheless the promising rate of economic growth proposes huge potential for the development of life insurance segment.

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