

INVESTIGATING THE FINANCIAL LIVES OF THE POOR



FOCUS NOTE: Financial Decisions and Funeral Costs¹

By Daryl Collins

Key Findings:

- * Funeral insurance is consistently part of nearly every household portfolio in the Financial Diaries sample.
- * Most respondents have joined a burial society or purchased a funeral plan within the last decade.
- * At face value, when compared to formal funeral plans, burial societies are as good or better value for money (in terms of highest cover per rand contributed).
- * However, this ignores the fact that many burial societies experience cash flow problems, risking insolvency.
- * Moreover, an analysis of household funeral insurance portfolios suggests that it is possible for formal insurers to offer a good value product that would compete effectively with burial societies and be welcomed by consumers.

The Financial Diaries is a year-long survey of financial management in low income households in three areas of South Africa: Langa, Western Cape (urban), Diepsloot, Gauteng (peri-urban) and Lugangeni, Eastern Cape (rural). In a former *Focus Note*², we used the Financial Dairies data to show that funerals dominate the financial lives of the poor. In this Focus Note, we aim to examine the financial decisions related to funeral cover to assess the value that is added by various forms of funeral insurance. Rather than looking at each funeral plan on the market, the Financial Diaries data allow us to look at funeral cover within the context of how *actual* households are using them, relative to their income and other circumstances.

Though households may manage their overall financial lives quite differently, nearly all the

Financial Diaries households have one financial instrument in common: funeral insurance. This funeral insurance can take on several possible forms:

1. Formal funeral plans, with a company like Avbob, Old Mutual or Standard Bank;
2. Burial societies, administered informally through a group; or
3. Funeral parlour insurance plans.

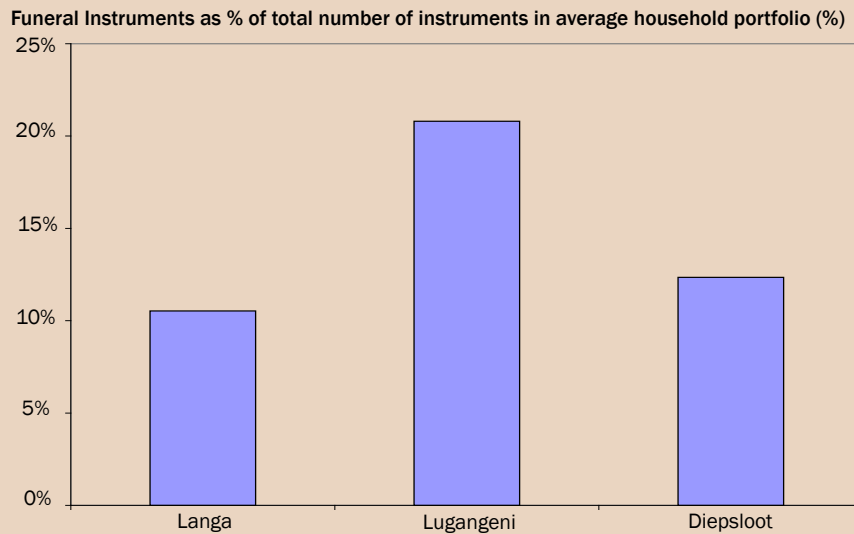
We found that households tend to hold more than one form of funeral insurance. Out of an overall portfolio of 8 to 12 financial instruments, households have at least one informal funeral instrument (a burial society) and one formal funeral instrument (a company or funeral parlour plan). Funeral instruments make up at least 10% of a household portfolio.

¹ Many thanks to Andrew Cartwright of Old Mutual for his helpful comments on an earlier draft.

² See "Funerals and Finance - Events in the lives of Financial Diaries respondents" on www.financialdiaries.com.

Burial Societies and Funeral Plans: A commonality of nearly every household

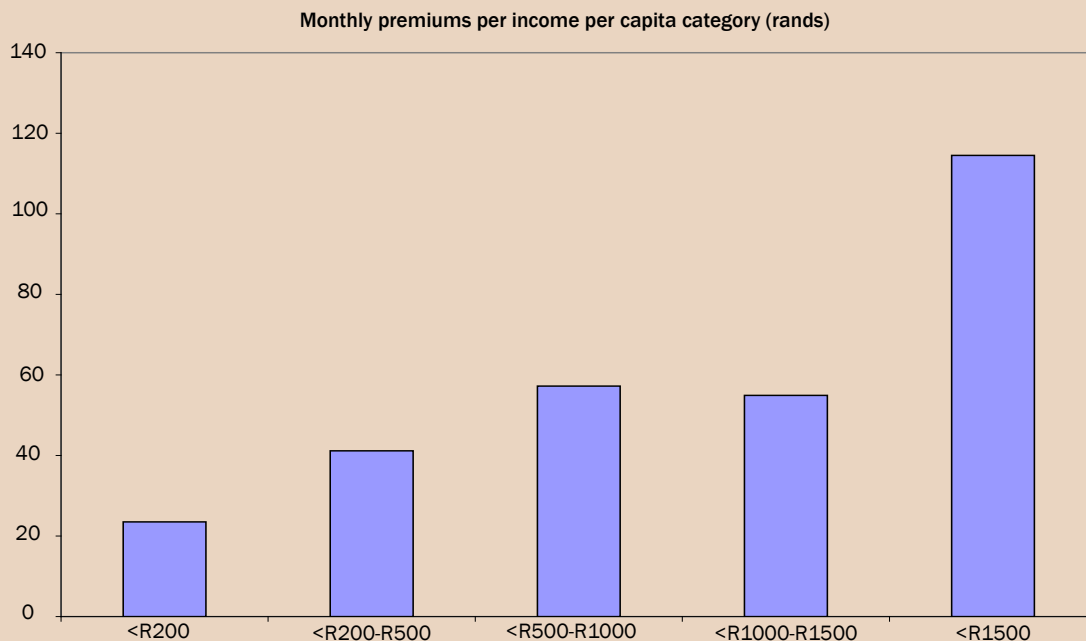
Chart 1: Funeral cover as a percentage of total number of instruments in household portfolio



We found that households spend, on average, 3% of gross monthly income in total on *all* of their funeral cover instruments. Chart 2 below shows the amount spent, over all funeral cover instruments held in the household, on premiums each month in each income *per capita* bracket. While the much better off households (those with income *per capita* of R1500 and above) spent much more on

funeral cover, the other income levels are not too different, especially when considered in terms of proportion of monthly income. The poorest spend an average of R24 on funeral cover per month (4% of monthly income), while households in slightly higher income brackets spend an average of R55 in on funeral instruments (2% of monthly income).

Chart 2: Average spending on both informal and formal funeral instruments

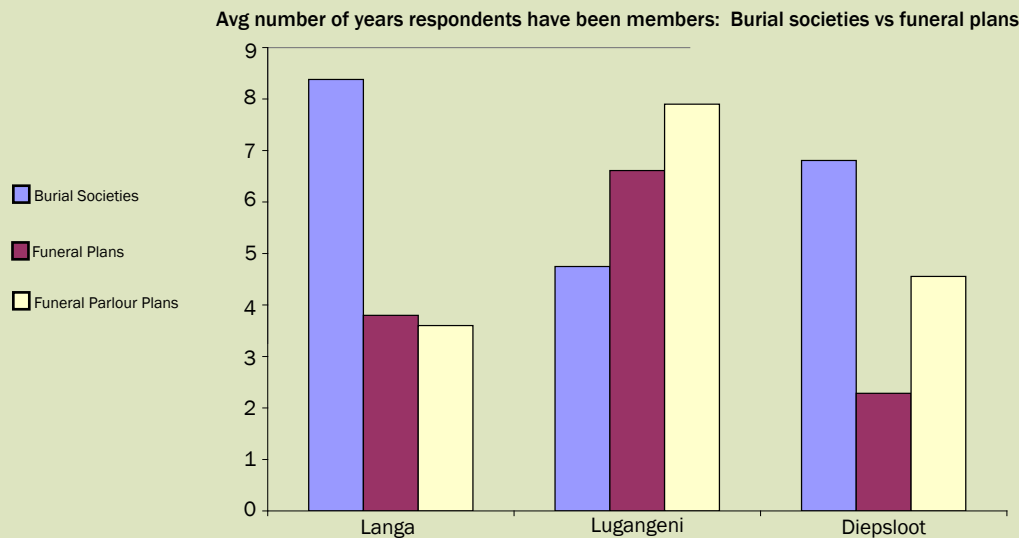


Most memberships are less than a decade old

Although some forms of funeral instruments, particularly burial societies, have been around for a very long time, we found that, on average, funeral instrument memberships are less than a decade old. Chart 3 shows that in the urban areas of Langa and Diepsloot, household have had a much longer history of belonging to burial societies and have had formal funeral insurance for

only three or four years. In Lugangeni, however, there is a longer history of using formal funeral cover, either plans through a formal insurer or through funeral parlours. It may be, however, that households have lapsed and rejoined burial societies in the past, making their current memberships look like a new trend when it might not be.

Chart 3: Membership length of time



Comparing costs of funeral cover

Comparing the monthly costs of different forms of funeral instruments requires some simplifying assumptions. Usually, costs for funeral instruments are paid every month, but in some of the more informal burial societies, payment might be every time that someone in the group dies. Based on the Financial Diaries payment data over the study year, we estimate payments into these types of burial societies to occur about 5 times per year. These assumptions help us estimate a monthly cost for these types of burial societies and compare the monthly cost for all three forms of funeral instruments in all three areas (Chart 4 on the next page). Formal funeral cover through a company is mostly

held by relatively better off respondents who have formal jobs. These plans cost the Financial Dairies households more on a monthly basis than either burial societies or funeral parlour plans. This makes sense because as an insurer, these companies need to meet rigorous solvency requirements, so the risk to their operations is much lower than either burial societies or funeral parlour plans. But do formal company plans offer better value than burial societies or funeral parlour plans? At first glance, it certainly seems that formal funeral plans are better value, simply because they pay out more at the time of the funeral. Chart 5 shows the median payout for the various types of funeral cover.

This is one of the many funeral parlours in Mount Frere, the closest large town to Lugangeni. Many of the Financial Diaries households in Lugangeni have a funeral parlour plan with a local funeral parlour like this one.



Chart 4: Premium costs per month of different types of plans

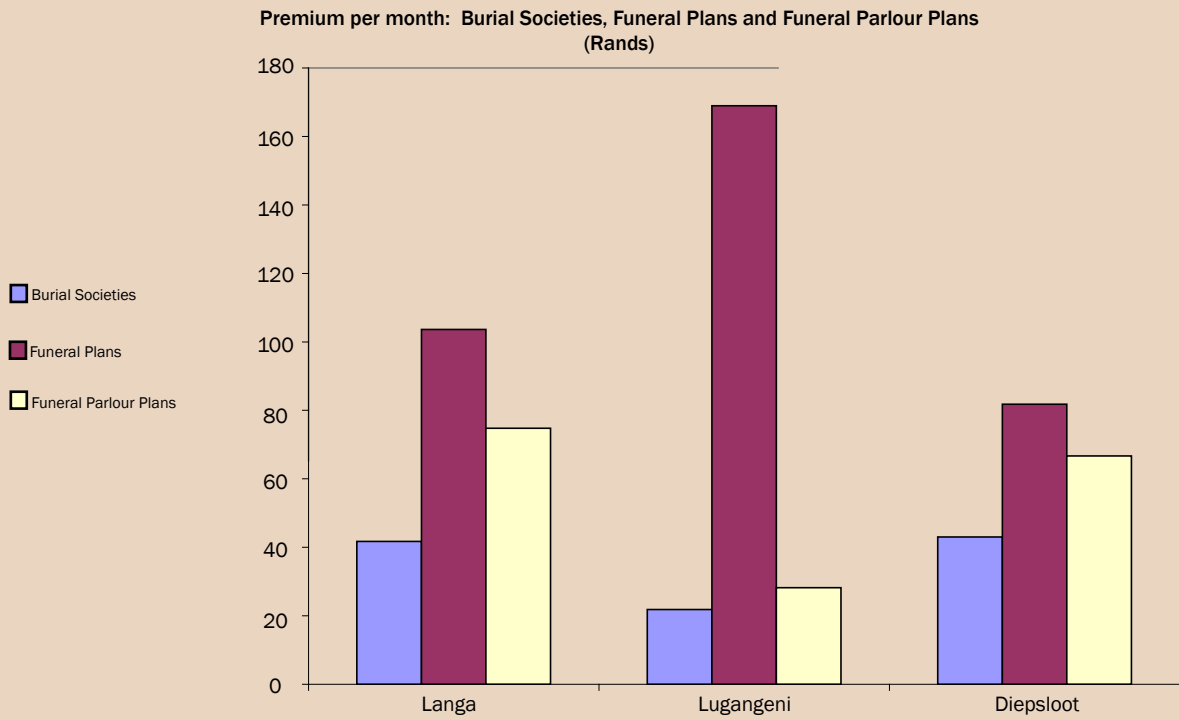
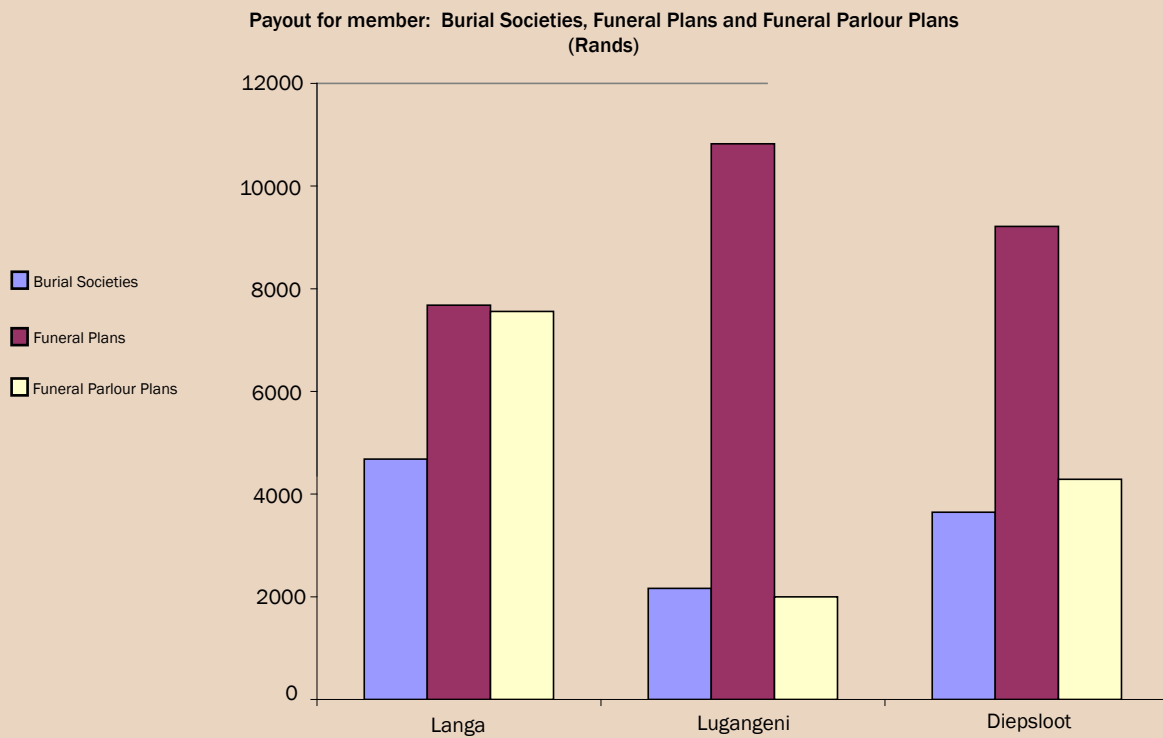


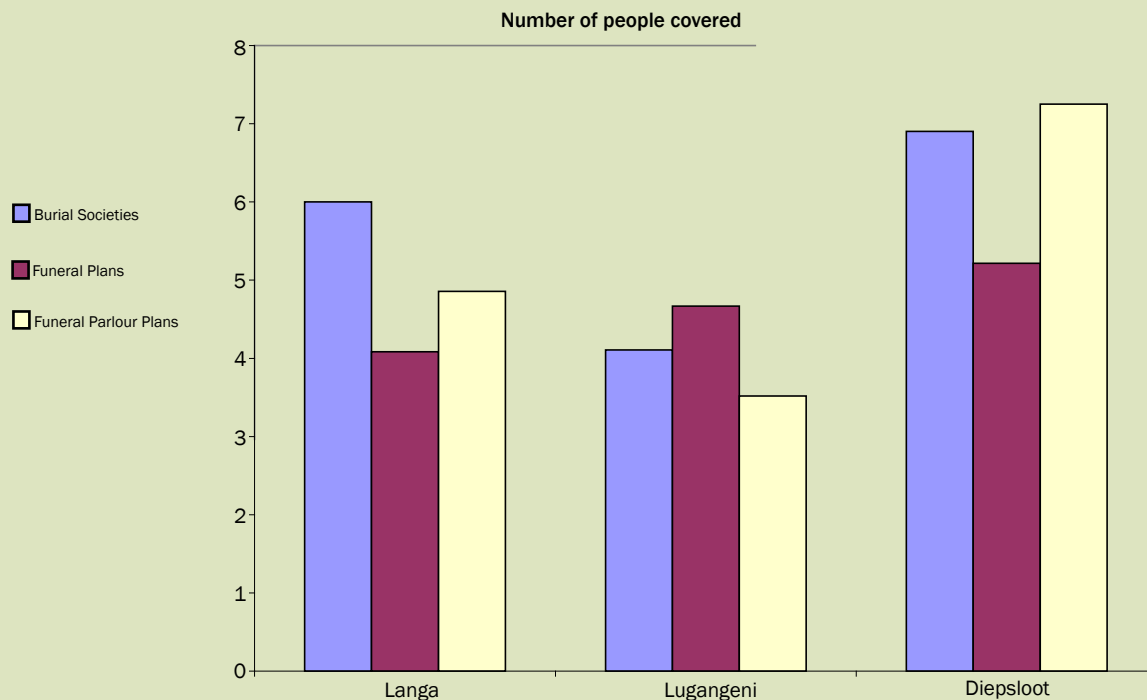
Chart 5: Payout for member for different types of funeral cover



Putting together a cost benefit analysis

A more accurate way of comparing premiums and cover is to assess the “cover per rand contributed.” This is simply the cover that the insured would receive for each member covered over the monthly premium paid. We compiled data for the 123 Financial Diaries households that had any type of formal funeral plan, burial society and/or funeral parlour plan and did a rudimentary cost benefit analysis. This analysis takes into account differences in the number of people covered under each plan. On average, the number of people covered tends to range from about four to six, and the different number of people covered by the types of plans is fairly small.

Chart 6: Number of people covered in different types of plans



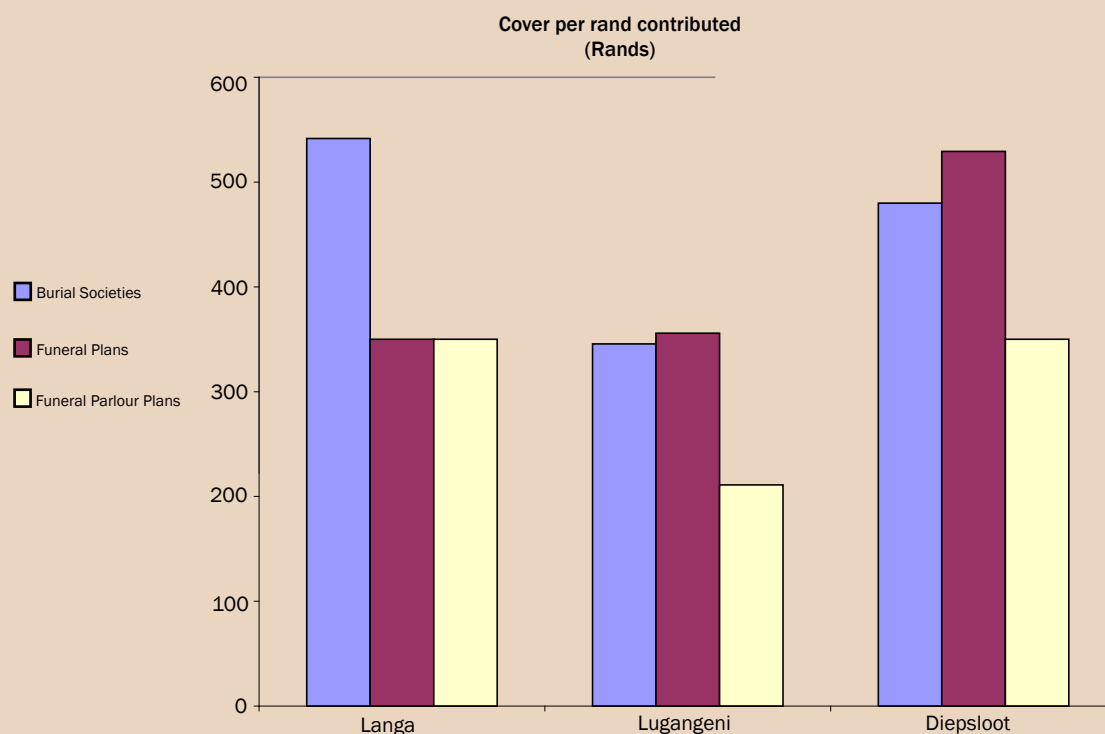
“Cover per rand contributed” measures the total benefit that would be received by the member (assuming everyone covered by the plan died) divided by the monthly premium paid for the policy. However, not all funeral insurance pays out in cash, some pay in-kind, particularly funeral parlours plans. So we needed to make a few assumptions to estimate the total benefit of the plans. Our interviews with one of our respondents, an undertaker, helped us to estimate the value of an in-kind benefit to be R5 000. In a similar way, some burial societies also pay out in-kind rather than cash (by donating vegetables or other food to the feast, for example). In these cases, we estimated the value of this payout to be R2 000. The total sum of benefits for all members covered was the value of the benefit of the plan.

Note that this analysis does not attempt to quantify any of the social benefits of burial societies. As a member of a burial society, one usually receives a great deal of physical assistance and moral support around

the time of the funeral. Not only do fellow members provide emotional support during the mourning period, but they also take on a significant role of preparing and serving the feast during the burial, often providing the cookware and eating utensils.

Higher cover per rand contributed means better value. Chart 7 on the next page shows cover per rand contributed across different types of cover and across the three areas. It is noteworthy that there are significant differences across the areas. In Langa, burial societies offer better value than formal funeral plans or funeral parlour plans. In the other two areas, formal funeral plans offer slightly better value than burial societies. Across all areas, however, funeral parlour plans offer less value. Overall, it would appear that burial societies offer as good, if not better, value as formal funeral plans, if one take into account the social benefits noted above.

Chart 7: Cover per rand contributed across different areas and different types of funeral cover



Are households maximising their portfolios?

A phenomenon that we noted earlier in this *Focus Note* is that households usually hold several different forms of funeral cover in their portfolios – they seldom rely on only one plan. One reason for this may be that they know the payout from just one instrument may not cover the whole funeral. In an earlier *Focus Note*, we found that a funeral costs about R10 000³ and as Chart 5 shows, most plans pay out much less than this. We also found that households tended to match the specific need in the funeral to the source of the cash flow. For example, one burial society might pay for the vegetables for the feast, while the undertaker plan pays for the coffin and undertaker fees and yet another burial society will pay for the sheep to slaughter for the feast.

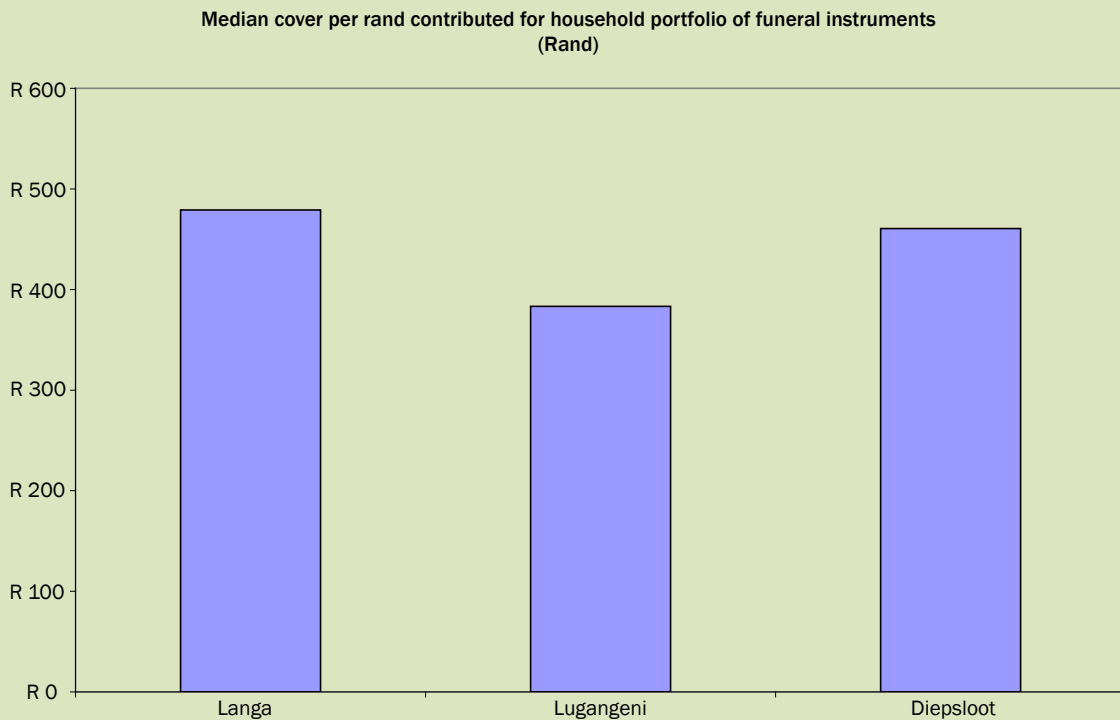
Households may hold a number of funeral cover instruments in their portfolios for different reasons,

but what is the impact on the value of their overall funeral instrument portfolio?

Chart 8 on the next page shows the median cover per rand contributed for *household* portfolios of funeral cover across the three Financial Diaries areas. The cover per rand contributed for each household was created by taking an average of the cover per rand contributed across all the funeral instruments held by each household in the sample. The median of each of these household portfolios was then taken across each area. The chart shows that households in the two urban areas are enjoying better value than in Lugangeni. To gain a better understanding of how households manage these portfolios, we look at case studies for two households: one in an urban area and one in a rural area.

³ See “Funerals and Finance - Events in the lives of Financial Diaries respondents” on www.financialdiaries.com.

Chart 8: Cover per rand contributed for household funeral insurance portfolios



Case study 1: Burial societies provide more benefits than formal funeral plans

Khaya* is an older man living with his wife and eight children in the hostels of Langa. He receives a disability grant of R740 per month. His wife has several part-time jobs cleaning homes. His daughter is the highest income earner in the household, earning R1 400 per month, a fact he did not know until we asked about her wages!

Khaya has belonged to a burial society for the past 31 years. His wife recently joined another well known burial society and his daughter bought a funeral plan from one of the well-known retail banks. The overall cover per rand contributed on the household portfolio of funeral instruments is R1 131, much better than most households in Langa.

Table 1: Khaya's Funeral Instrument Portfolio

Instrument	Member	Description	Monthly Premium	Expected payout	Cover per rand contributed
Burial society	Khaya	Members come from same place in Eastern Cape	R24	R2 000	R1 667
Burial society	Wife	Large burial society	R81	R10 000	R988
Funeral plan	Daughter	Well known retail bank	R50	R10 000	R740
Overall portfolio					R1 131

*Note: Names of respondents have been changed to protect their identities.

In Khaya's case, burial societies provide good value. Khaya's burial society involves a very small monthly premium and small cash payout but it pays for a lot of things in-kind, including the undertaker's fee, the funeral costs and the transport of the body back to the rural areas. It also covers a large number of people - three adults, including him, plus seven children. His wife's burial plan is more expensive but has a higher payout. It has such a high cover per rand contributed because it covers so many people – nine adults, including her and her husband, plus six children. His daughter's funeral plan costs less than her mother's burial society for the same payout, but only covers four adults, including her, plus four children.

Burial society meetings are usually carefully organized, with committee members checking the payments at monthly meetings.



Case study 2: Formal funeral plans provide better value

Mzwamadoda* is an older man who lives in Lugangeni with his wife, Tembisa, one child and six grandchildren. They manage to get by month-to-month on one old age grant and one disability grant (R740 per month each). Tembisa is a member of three burial societies and the policy holder of three funeral plans. Mzwamadoda is a member of one burial society. They are getting reasonable value from this portfolio - the overall cover per rand contributed is R513 compared to a median cover per rand contributed of R383 in household funeral portfolios in Lugangeni.

All the same, this is a household that has become fairly exuberant about spending on funeral cover, joining five out of the seven plans in the past four years. When we spoke to them, they said they saw other people joining and saw the need to cover funeral costs. They guess that a funeral these days costs about R15 000, but they also point out the prayer services in the days before the funeral are also very expensive.

All of the plans cover Mzwamadoda, Tembisa and their two daughters. A third daughter is covered in all but three of the plans. If Mzwamadoda were to die, a total of R50 100 would be paid out for his funeral from all of the plans. The same amount would be paid out for Tembisa. For his daughters, R33 600 would be paid out. By most standards, this is a hefty sum for a funeral. They are getting good value out of their portfolio, but are they perhaps slightly over-covered?

*Note: Names of respondents have been changed to protect their identities.

⁴ This is the same household used in Case study 2 in "Stocks and flows: Quantifying the savings power of the poor" on www.financialdiaries.com

Table 1: Mzwamadoda's Funeral Instrument Portfolio

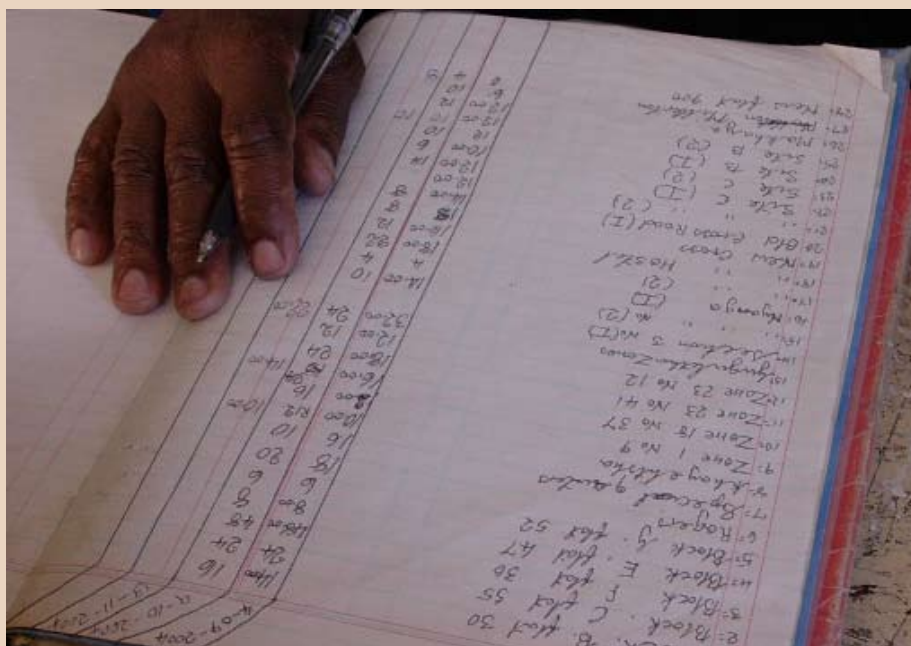
Instrument	Member	Description	Monthly Premium	Expected payout	Cover per rand contributed
Burial society	Tembisa	Pay in cash when someone dies	R60 each time	R2 600	R 520
Burial society	Tembisa	Pay in-kind when someone dies	About R50 each time	R1 500	R288
Burial society	Mzwamadoda	Pay monthly	R100	R10 000	R100
Burial society	Tembisa	Pay monthly	R60	R5 000	R242
Funeral plan	Tembisa	With well known retail bank	R30	R6 000	R800
Funeral plan	Tembisa	With well known retail bank	R38	R15 000	R1 263
Funeral plan	Tembisa	With unknown company	R100	R10 000	R380
Overall portfolio					R513

It is interesting to note which plans seem to be working the best. On a value basis, the formal funeral plans appear to have the most benefit for the lowest cost – not an unusual situation in Lugangeni. It is also interesting that the burial society with the highest payout is not necessarily the best value. This shows that a well-priced funeral cover can offer as much value as a burial society and be a welcome part of a household funeral instrument portfolio.

Sometimes burial society members can pay their monthly fees directly into the burial society bank account and bring the deposit receipt to the meeting.



Record books in this burial society are hand-written and kept up to date with members' payments.



Conclusions

One aspect of funeral cover that this Focus Note has not explored is the risk of the institution offering the cover. Because the Financial Diaries uses data from the household point of view rather than the institutional point of view, we can offer no new insights into the risk of each type of funeral cover. Genesis⁵, however, reports that many funeral parlour plans are illegal and therefore present a very high risk to the consumer. The FinScope⁶ survey shows that close to 10% of burial societies run out

of money. The analysis presented in this Focus Note must be considered within the context of these institutional risk factors.

With that in mind, although burial societies appear to offer comparable value to formal funeral plans, the last case study shows that it is not impossible for a formal bank to offer a good value product that would compete effectively with burial societies and be welcomed by consumers.

⁵ Genesis Analytics. 2005. "A Regulatory Review of Informal and Formal Funeral Insurance Markets in South Africa". www.finmark.org.za

⁶ FinScope 2003. Please see www.finmark.org.za for more details.