

The Role of Insurance in National Adaptation Plans (NAPs)

Making the Case for Insurance in the Context of NAPs

The Challenge: Moving from Ex-post to Ex-ante Risk Management Using Insurance

- Rising severity and frequency of extreme weather events undermine resilience of poorer countries and their citizens by weakening their capacity to recover and absorb losses.
- Government post-disaster aid programmes or ad-hoc international assistance are not necessarily timely or financially adequate and pose uncertainty to national budgets.
- ➔ Risk sharing and transfer instruments (incl. insurance) can reduce immediate and long-term financial impact of sudden-onset extreme weather events on governments and households.

Risk Layering: Need for an Intelligent Mix of Approaches

- High-frequency/low-severity risks: Prioritise risk prevention and reduction activities.
- Low-frequency/medium-severity risks: Mix of risk prevention & reduction measures + risk transfer (international financial markets)
- Very low-frequency/high-severity risks: Mix of risk prevention measures + risk retention + risk transfer and insurance (regional insurance pools, crop-/ individual asset insurance, etc.)

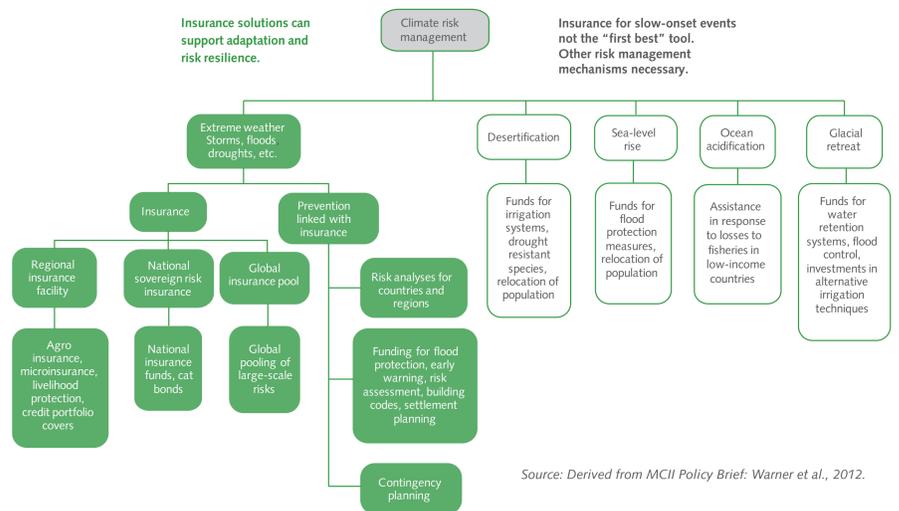
Limits: Insurance in the Context of Slow Onset Risks

- Insurance not appropriate/feasible for slowly developing and foreseeable events or processes that happen with high certainty and are very likely to affect a large area.

Preconditions of insurable risks:

- (1) Unpredictability – losses occur suddenly and cannot be foreseen;
- (2) Ability to spread losses over time and space.

Helping vulnerable people to get more resilient against climate change impacts: How to address major risks

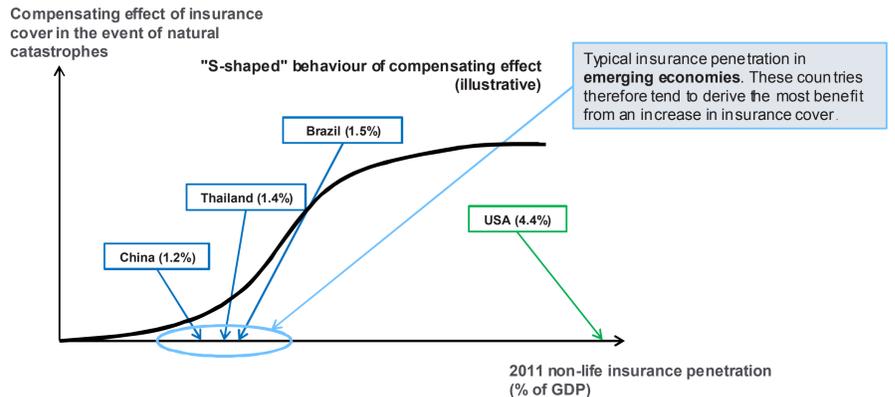


Source: Derived from MCII Policy Brief: Warner et al., 2012.

The Benefits of Insurance for NAPs

- **Creating a Buffer:** provide financial liquidity via fast payouts immediately after a loss, help nations better plan financial needs for adaptation.
- **Providing Space of Certainty:** a safety net for climate-resilient and productive, yet high-risk investments.
- **Risk and Loss Assessment:** identify needs and policy priorities, raise awareness, and expose new risk management options.
- **Incentivizing Risk Reduction:** encourage loss-avoiding measures through contract design (e.g. loss-reduction = reduced premium)
- **Safeguarding Growth:** countries with high insurance penetration show a positive GDP trend and sustainable growth after a catastrophe, whereas countries with low insurance penetration suffer from a negative GDP deviation.

Variations of the compensating effect of insurance cover against natural catastrophies



Source: Munich Re Economic Research based on Engmaier and Stowasser (2013)

Case Studies: Applying Insurance as a Tool to Address Climate Risk

The R4 Rural Resilience Initiative – Reaching vulnerable and poor populations

- Tests a comprehensive climate change adaptation approach in Ethiopia using a set of integrated tools: insurance, credit, savings, and disaster risk reduction;
- Provides insurance in exchange for participation in risk reduction activities;
- Enables participants to establish small-scale savings used to build a 'risk reserve' to buffer against climate shocks and to later progress to cash paying insurance schemes.

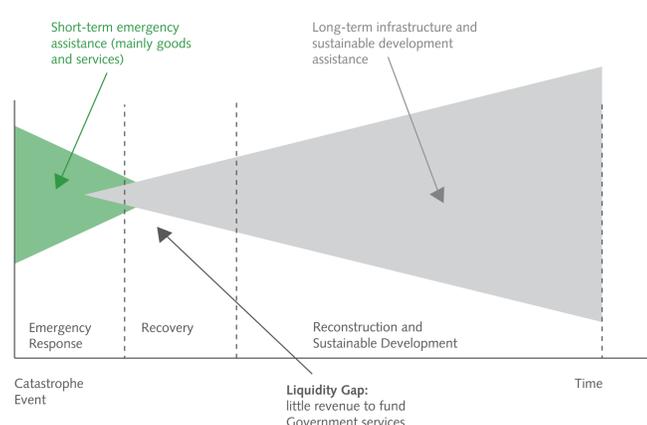
The Africa Risk Capacity (ARC) – Contingency planning and risk transfer

- Uses a continental sovereign risk pool and early response mechanism designed to help African Union Member States respond to extreme weather events;
- Expects national governments to create a contingency plan identifying how ARC funds will be used to ensure livelihood protection;
- Allows governments to make informed decisions on ARC's financial services and enables risk-informed fiscal management of natural disaster risk.

The Caribbean Catastrophe Risk Insurance Facility (CCRIF) – Combining risk transfer with regional risk capacity and forecasting in 16 Caribbean Countries

- Uses a multi-country catastrophe risk pooling facility including parametric insurance;
- Contributes to regional risk management and makes rapid payouts in case of extreme events in order to bridge the post-disaster liquidity gap;
- Can design institutional models to have transparent government structure, allow private sector engagement, and serve as conduits for international adaptation funding.

Sovereign liquidity gap occurring after a disaster: Bridging the gaps through insurance



Source: Ghesquiere and Mahul, 2012.