OECD HIGH-LEVEL ROUNDTABLE ON FINANCIAL PROTECTION GAPS FOR DISASTER RISKS

Summary

On 8 December 2022, the OECD's Insurance and Private Pensions Committee (IPPC) organised a high-level roundtable that gathered stakeholders from international organisations, national governments and the insurance sector[1] in order to **share experience and identify solutions to address the financial protection gaps** that weaken the social, economic and financial resilience of societies and impede sustainable development.

Participants emphasised that financial protection gaps exist for many types of risks, including natural hazards (including climate-related hazards), health, cyber, pandemics and pensions. The scale of these gaps differ within and across countries and for the different types of risks. For example, it was noted that more than 90% of losses from natural hazards are uninsured in developing countries, relative to approximately 60% in developed countries.

> *V20 research shows that 98% of the nearly 1.5 bn people in V20 countries do not have financial protection* - The Honourable Ken Ofori-Atta, Minister of Finance, Republic of Ghana and Chair, Vulnerable Twenty (V20) Group of Ministers of Finance

> *There are widening challenges of insurability around climate change in some areas of developed countries* - Robert Muir-Wood, Chief Research Officer, RMS and Chair, OECD High-Level Advisory Board on the financial management of catastrophic risks

There are different approaches to defining and measuring financial protection gaps which makes it challenging to assess progress. Several participants suggested the need to develop a common understanding of "protection gaps."

Environmental, economic and social trends such as **climate change, digitalisation, ageing populations, urbanisation and globalisation are impacting the magnitude of losses** and could lead to larger financial protection gaps in the future - although some of these trends, such as technology and innovation, could also support the availability of financial protection and enhance resilience. The current economic environment, particularly the increase in inflation, could also exacerbate protection gaps if the level of coverage acquired does not keep pace with increases in rebuilding costs. The particular challenges related to climate change were emphasised given the potential for a significant increase in the frequency and intensity of climate-related extreme events.

> *We simply cannot have hard-earned development gains eroded away in one night of unprecedented rain or due to an unexpected illness* - Michel Liès, Chair, Insurance Development Forum Steering Committee and Chair, Zurich Insurance Group

[1] The Insurance Development Forum, the International Association of Insurance Supervisors, and the World Bank supported the organisation of the High-Level Roundtable.

Gaps in insurance coverage can force households and businesses to rely on savings, debt and financial assistance to recover from the impacts of catastrophic events and potentially undermine their resilience to future shocks. Vulnerable countries and communities have the least ability to finance or absorb losses.

Closing financial protection gaps for disasters

The insurance sector plays a key role in promoting financial protection against disasters by **offering tailored solutions and capacity** to assume some of the risks that would otherwise be borne by households, businesses and governments. However, it was noted by many that the take up of insurance is hampered by a number of demand and supply factors, including limited risk awareness, behavioural biases and affordability and income constraints as well as insurance sector distribution and capacity constraints and insurability challenges driven mainly by increasing losses (underscored by current reinsurance market capacity constraints). The insurance sector needs to continue to develop **simple, innovative, impactful and inclusive insurance products** that meet the needs of different segments of society, including low-income households and those with low levels of financial literacy. The **application of new technologies** can support product innovation and distribution and achieve cost-efficiencies that can improve affordability.

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> *The insurance sector has expertise in climate risk modelling, in finding capital solutions to fund losses and in setting up national programmes which must be put at the service of the collectivity -* Antoine Gosset-Grainville, Chair, AXA

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> *The supervisory role in policyholder protection is not just about those already within the tent but also involves being concerned about the households and companies that are without financial protection -* Jonathan Dixon, Secretary General, International Association of Insurance Supervisors (IAIS)

A number of participants highlighted the insurance sector’s role in supporting societal **risk management** by providing **analytics and expertise** on risk, risk reduction measures and adaptation to climate change. The insurance sector should continue to **address data and information gaps** and make risk information available to other stakeholders, including by providing **access to the risk analytics tools and modelling** necessary to support **risk-informed decision-making** and the development of **government financial strategies** for managing disaster risks.

Participants suggested that **insurance regulators and supervisors are increasingly recognising that they have an important role to play in supporting the availability** of affordable insurance coverage for catastrophe risks and **encouraging take-up** of coverage. Many insurance supervisors address financial protection gaps to support financial stability and policyholder protection objectives and ensure fair, safe and stable insurance markets.

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> *It’s healthy for regulators to determine whether there are regulatory barriers that are keeping people from being able to have access to affordable coverage* - Dean Cameron, Director, Idaho Department of Insurance and President, National Association of Insurance Commissioners

Insurance regulators and supervisors can help provide **an enabling environment that supports innovation while ensuring that any corresponding risks are well managed and mitigated,** including for consumers.

A number of participants suggested that **building societal resilience needs to be a higher priority for governments** as increasing exposure and vulnerability to risk is a critical driver of financial protection gaps. Governments at all levels need to recognise that **investment in risk reduction and adaptation** (as well as climate mitigation) can be both more **cost-effective** than spending for recovery and reconstruction and is **essential for maintaining insurability** in the context of increasing damages and losses. he decisions that governments make now in terms of building codes or land-use planning will have a significant impact on future exposure and the ability of the insurance sector to provide significant coverage. It was noted that insurance companies can also support this effort by **encouraging policyholder risk reduction actions and resilient reinstatement.**

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> *We should be as focused on resilience as we are on inflation – we are now in a race to achieve price stability – we should be in race to propagate resilience* - Jerome Jean Haegeli, Group Chief Economist, Swiss Re

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> *It is not only insurance that will solve protection gaps. To address the causes of protection gaps....we should also be open to other routes that involve the private and public sector* - Petra Hielkema, Chair, European Insurance and Occupational Pensions Authority (EIOPA)

Some participants noted that governments also need to recognise that **insurance might not be the only solution** for addressing financial protection gaps. In some cases, insurance sector exclusions of certain risks are a reflection that risk levels are too high and need to be reduced through **increased investment in risk reduction measures** or addressed through other means such as credit facilities. For some segments of society, income levels may be too low to support the purchase of insurance, highlighting the need to **establish social protection mechanisms.**

Cooperation between the insurance sector and the public sector is critical. This cooperation should aim to **share data and expertise** on risk and risk reduction and **build risk awareness and financial literacy** among households and businesses. It could also entail the establishment of **catastrophe risk insurance programmes** to respond to **capacity constraints or affordability concerns,** particularly if other types of interventions to maintain access to affordable insurance are unsuccessful. Some participants suggested that these types of programmes should be carefully designed to ensure that the **right incentives are in place to avoid adverse selection and moral hazard,** maintain appropriate price signals and support **broad take-up** – although it was also noted that programmes could be designed to support solidarity and mutualisation of risk and may need to include measures to ensure affordability. An ill-designed programme could conflict with other policy objectives if it **leads to reduced incentives to invest in risk reduction, adapt or relocate.** It was noted that the involvement and **support of the insurance sector** as well as consumers is critical for the establishment of a successful approach. Insurance regulators and supervisors could play an important role as a **bridge between the insurance industry and policymakers,** for instance, by supporting the design of policy interventions, as well as **acting as a bridge to consumers**, by supporting financial literacy and awareness efforts.

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> *As a result of the cyclone pool [in Australia], insurance companies intend to remove underwriting restrictions to begin writing additional coverage in medium and high risk areas because they will be able to transfer 100% of the cyclone risk to the pool* - Christopher Wallace, CEO, Australia Reinsurance Pool Corporation

Next steps

Addressing financial protection gaps is an area of increasing focus for international cooperation. A number of participants argued that pre-arranged financing, including public sector funding delivered using an insurance framework, can support governments that are unable to readily access capital markets to respond to disasters. The G7, under Germany's Presidency in 2022 and in partnership with the Vulnerable Twenty Group (V20) of Finance Ministers, **established a Global Shield against Climate Risks** to provide and facilitate more and better pre-arranged protection against climate and disaster related risks and help **close the protection gap for poor and vulnerable people against climate-related losses and damages,** including through the use of premium subsidies and blended finance. **Japan has identified financial protection gaps as a priority for its G7 presidency in 2023.**

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Japan has been advocating in international settings the importance of disaster risk financing - Hideaki Imamura, Deputy Vice Minister of Finance for International Affairs, Ministry of Finance (Japan)

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With the benefit of your experience and expertise, we believe that this guidance will become even more critical as the financial management of disaster risks becomes an increasing priority in international discussions in the G7, G20 and APEC, amongst other forums - Carmine Di Noia, Director, Directorate for Financial and Enterprise Affairs, OECD

The International Association of Insurance Supervisors (IAIS) is developing a framework **for supervisors to address natural catastrophe protection gaps** that is also expected to inform the work under Japan's G7 Presidency.

Building financial resilience has been a priority for the OECD Insurance and Private Pensions Committee (IPPC) and a core part of its work programme for many years, centred on the guidance included in the **OECD Recommendation on Disaster Risk Financing Strategies.** The Committee has recently reviewed implementation of the Recommendation and **will update it in 2023 to ensure that it remains a key international standard** to support government efforts to build financial resilience and address financial protection gaps. The IPPC will continue to consider ways to support international efforts to close financial protection gaps, leveraging its unique ability to bring together policymakers, insurance supervisors and the insurance sector, as well as other stakeholders.

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We need an international body or platform to bring together relevant parties to discuss financial protection gap issues and assess progress on a regular basis – I think the OECD can play an important role here – Yoshihiro Kawai, Chair of the Insurance and Private Pensions Committee

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