OECD Conference on Financial Management of Large-Scale Catastrophes

World Bank Group

Hyderabad, India

Developing Catastrophe Insurance Programs in Developing Countries: Key Challenges and Opportunities

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February 26 -27, 2007

Agenda

① Catastrophe insurance programs in developing countries

② A case study of the Caribbean Catastrophe Insurance Facility

③ Applicability of the CCIF experience to other countries.

④ Key policy issues and recommendations

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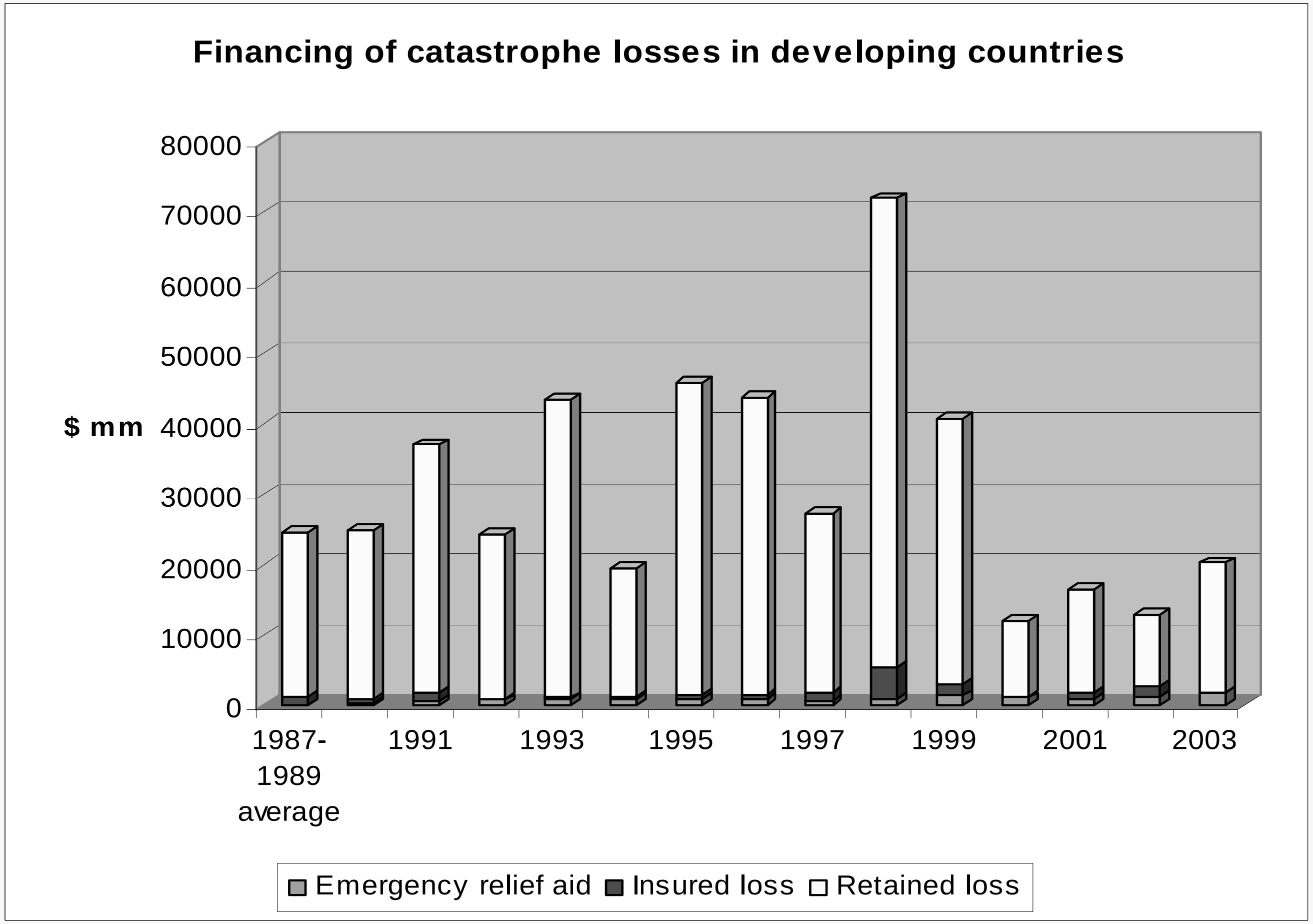
Major sources of disaster finance



Sources: OECD, Munich Re

- Loss retention was on average $31 bn per year

- Loss retention has been highly variable – 50% coefficient of variation

•On average, 92,6% of economic loss was retained by developing countries.

Catastrophe insurance penetration in developing countries (% dwellings covered)

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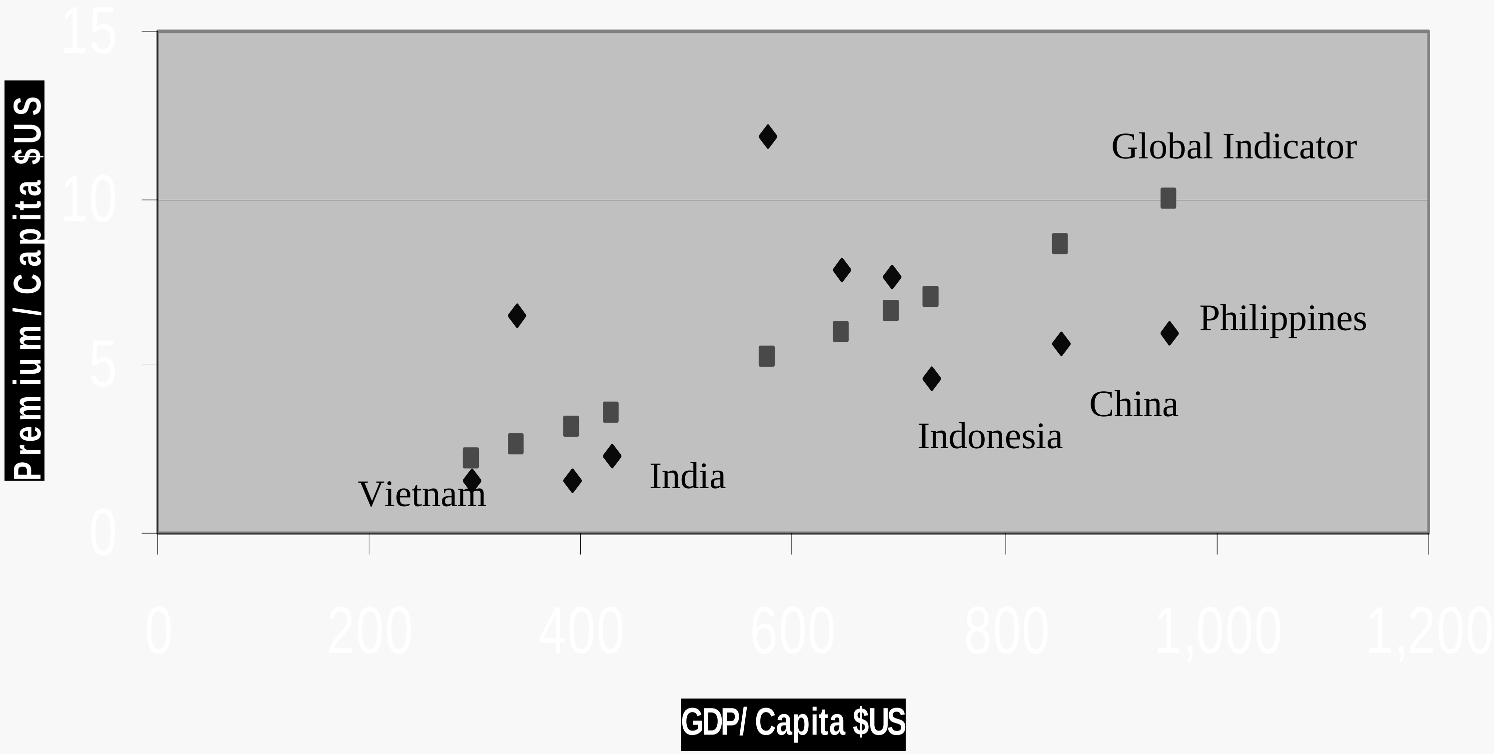

PERSONAL INSURANCE PREMIUM = 1.3*(GDP/1000)^2
PERSONAL CAT INSURANCE PREMIUM = 0.1*PERSONAL INSURANCE PREMIUM

% homes covered

- India – under 0.3%
- Philippines – 0.3%
- Iran – under 0.05%
- Romania – under 4%
- Bulgaria – under 3%
- China – under 0.5%
- Turkey – 18%

Key Challenges: Design Stage

- **Lack of insurance culture and risk awareness.**
- **Low income of population.**
- **An (almost) non-existent function of formal integrated catastrophe risk management inclusive of risk reduction and risk financing.**
- **Lack of risk management culture and insurance expertise in relevant government institutions.**
- **Political resistance to switch from discretional government post-disaster assistance to contractual (insurance).**
- **Lack of confidence on the part of the insurance sector and civil society in government's ability to create a financially efficient and transparent insurance program.**
- **Entrenched or often diverging economic interests**
- **Disincentives to insure provided by unconditional post-disaster donor aid.**

Key Challenges: Implementation Stage (based on experience of TCIP, RCIP, CCIF, GCRF)

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Country level:

- **Passing relevant insurance legislation.**
- **Raising insurance and risk awareness of population.**
- **Ensuring the support and participation of insurance/reinsurance industry in the operation of a scheme.**
- **Maintaining adequate government commitment to the program.**

Program-level

- **Safeguarding the surplus accumulated in the pool from “political hijacking” and ensuring it is well managed.**
- **Putting in place and implementing an adequate risk management framework for the program (including access to reinsurance).**
- **Ensuring adequate pricing of risk coverage.**

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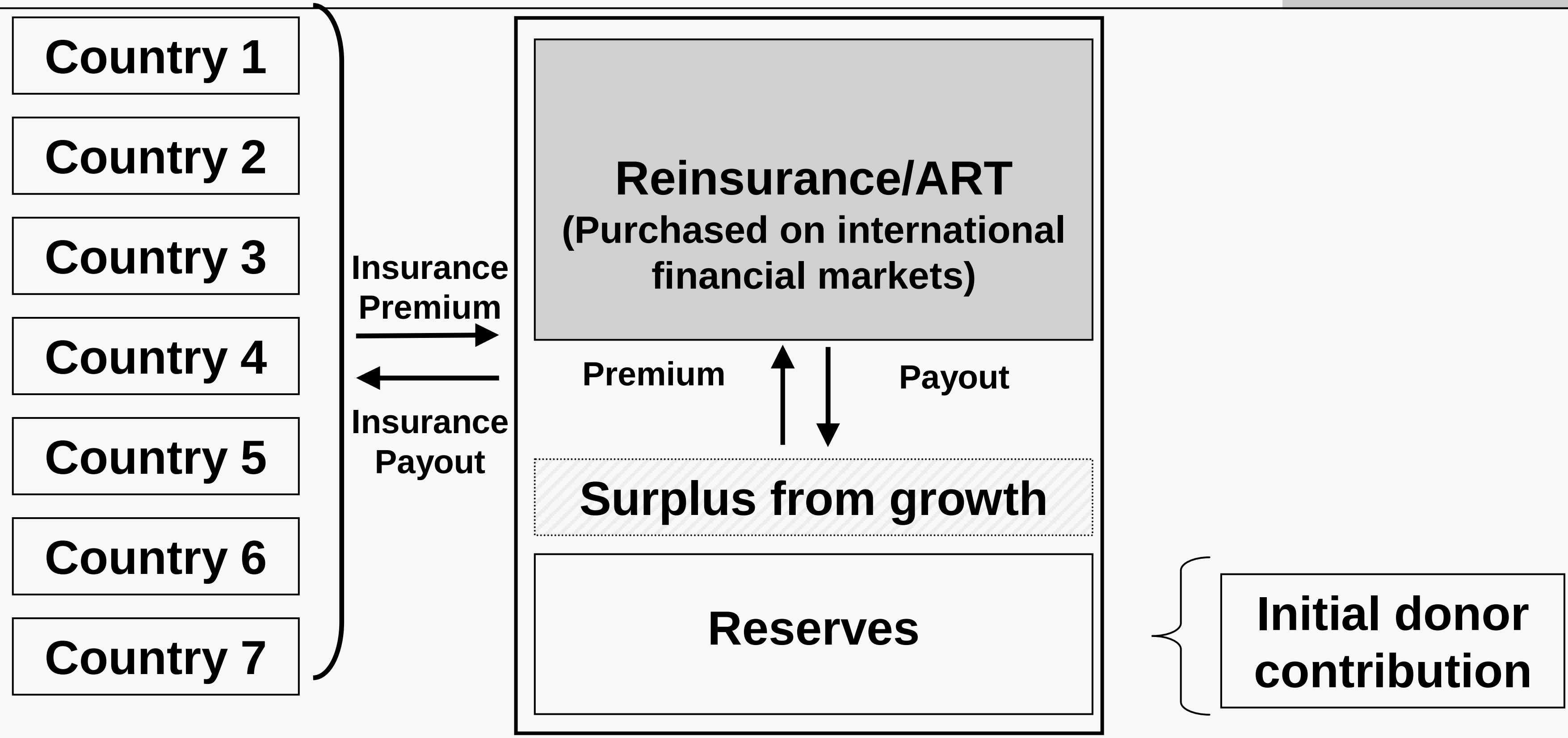
CCRIF: An Insurance Vehicle



Source: Francis Ghesquire, World Bank, 2006

CCRIF will provide the Caribbean governments with parametric catastrophe insurance coverage, thus enabling them to overcome a typical liquidity crunch in the aftermath of a disaster.

CCRIF: Organizational Structure

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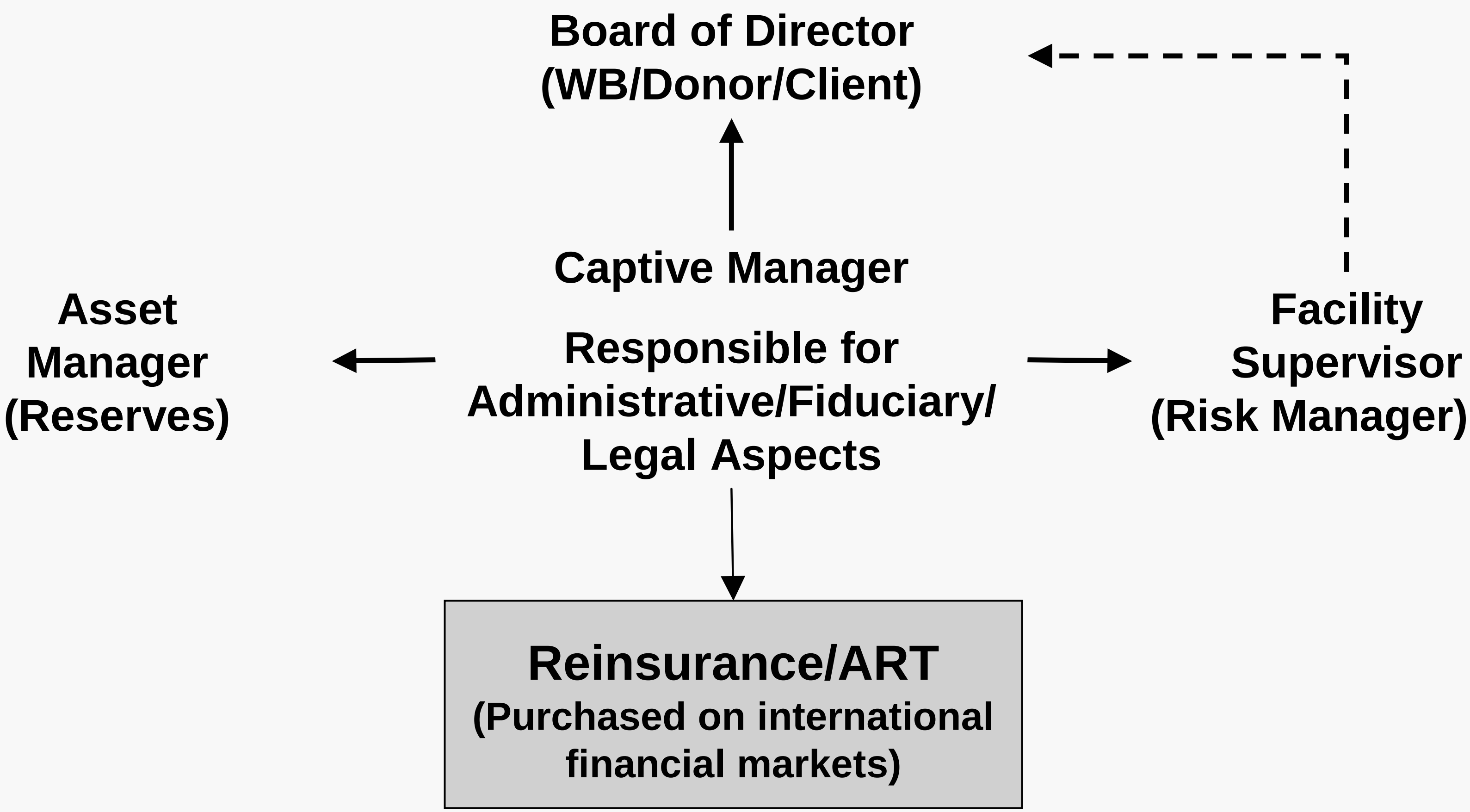

Source: Francis Ghesquire, World Bank, 2006

A case study of the Caribbean Insurance Facility

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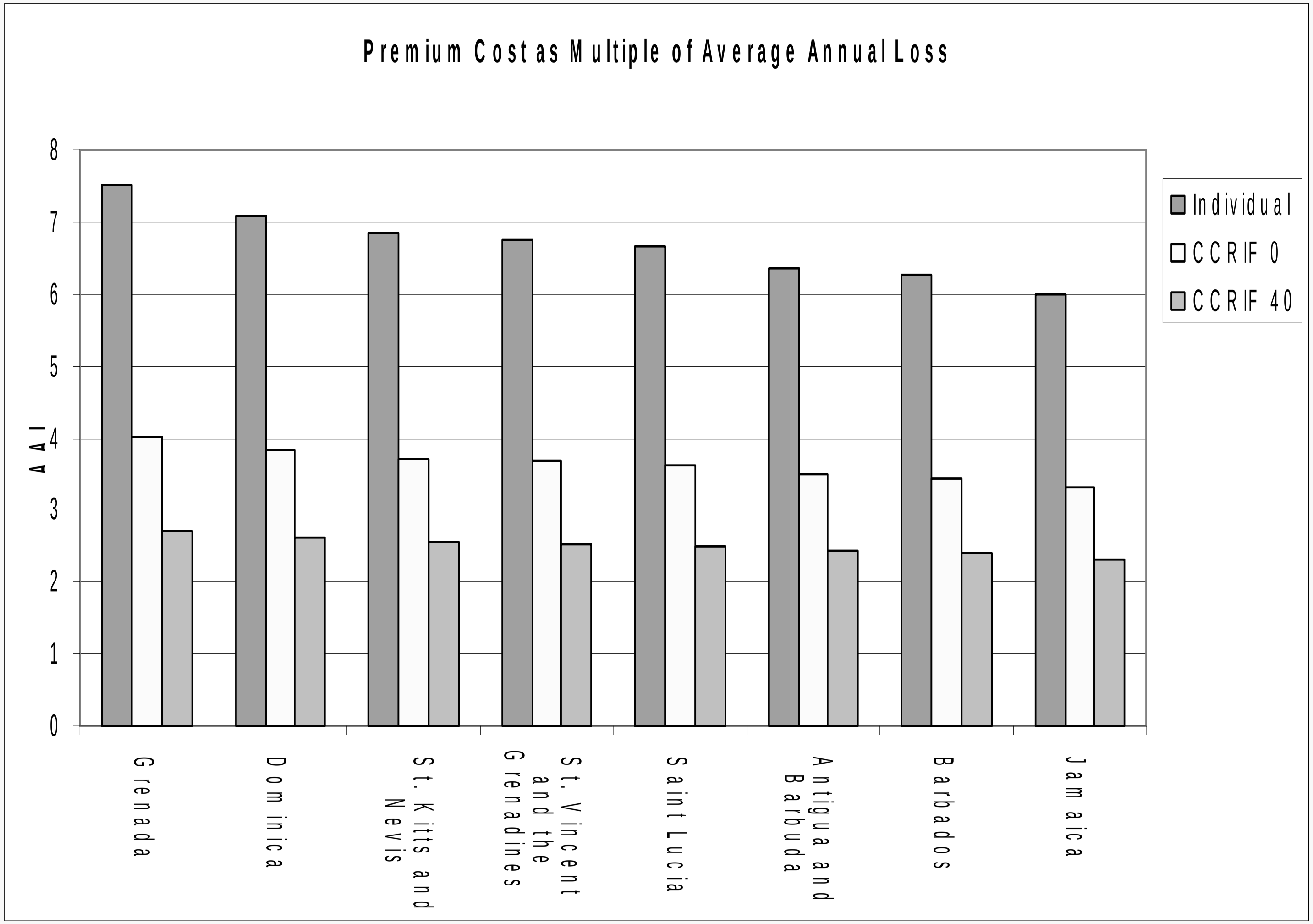
Diversification benefits from regional risk pooling



Source: Francis Ghesquire, World Bank, 2006

Key challenges faced by the CCIF: Design stage

- Mastering support for the project within World Bank
  - Internal reviews, management support, lending in support of premium.
- Ensuring countries' commitment and participation in the program
  - premium payment, terms of coverage, ownership of surplus, and termination fees.
- Ensuring donor support to the program
  - feasibility studies, program capitalization and working capital
- Securing support of the global reinsurers
  - Program management, risk transfer

Key challenges faced by the CCIF: Implementation stage

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- Maintaining countries’ interest and participation in the program.
  - Finding the right balance between providing affordable coverage and ensuring financial sustanability of the program.
- Implementing adequate risk management.
  - Risk retention, risk transfer, survival probability.
- Ensuring continuous support of reinsurers.
- Achieving a sound financial and operational management of the facility.

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Mainstreaming CCRIF

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- The concept of regional risk pooling can be applied to other parts of the world – the Pacific Islands, for instance;
- Individual country risk assessments should be carried out first.
- Can CCRIF be extended to cover other larger developing countries?
  - Governance issues.
  - Capitalization/size of risks covered.
  - Use of public subsidies.

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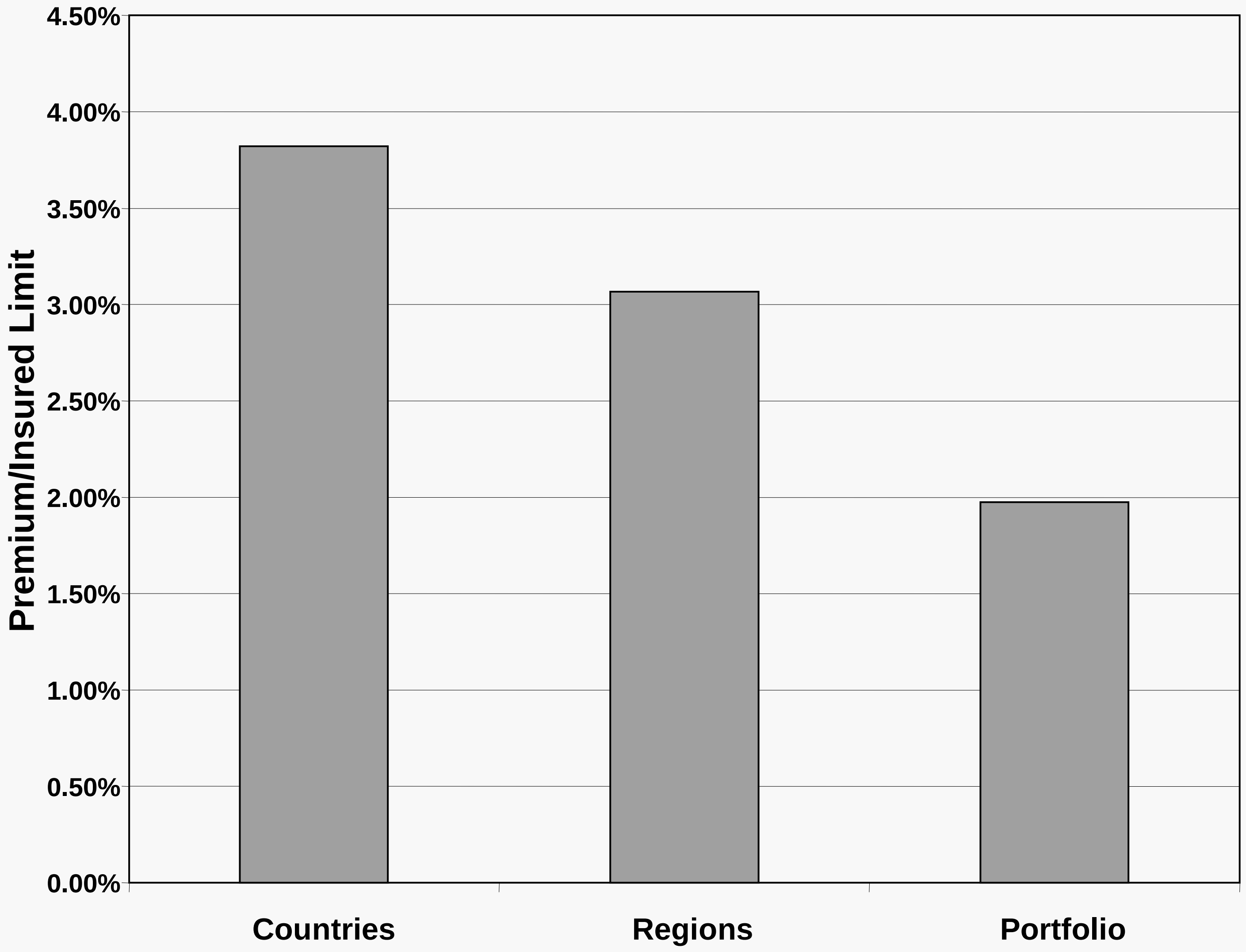
Benefits of global risk pooling: Global Catastrophe Insurance Facility



- 27 countries
- 2 perils

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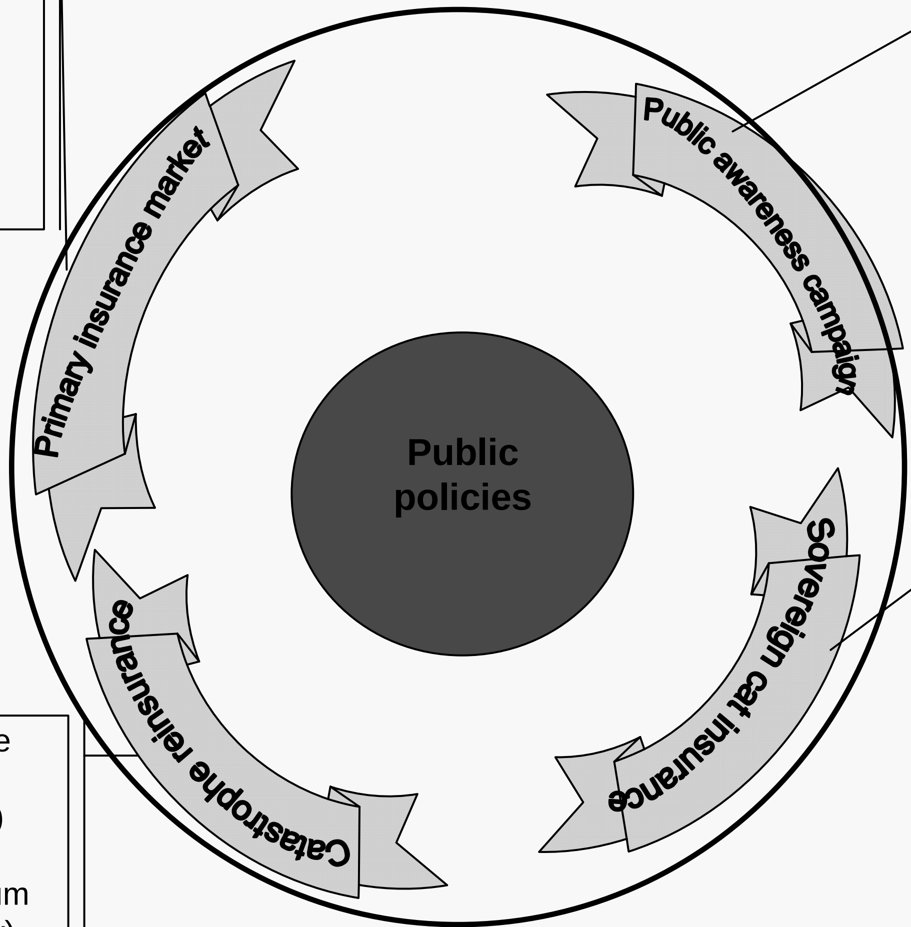
Enabling public policies for catastrophe insurance

Making insurance compulsory or semi-compulsory (Turkey/Romania/Columbia/France);

Creation of national pools;

Drawing a clear line between public and private liabilities (Spain)

Public risk awareness, education campaigns

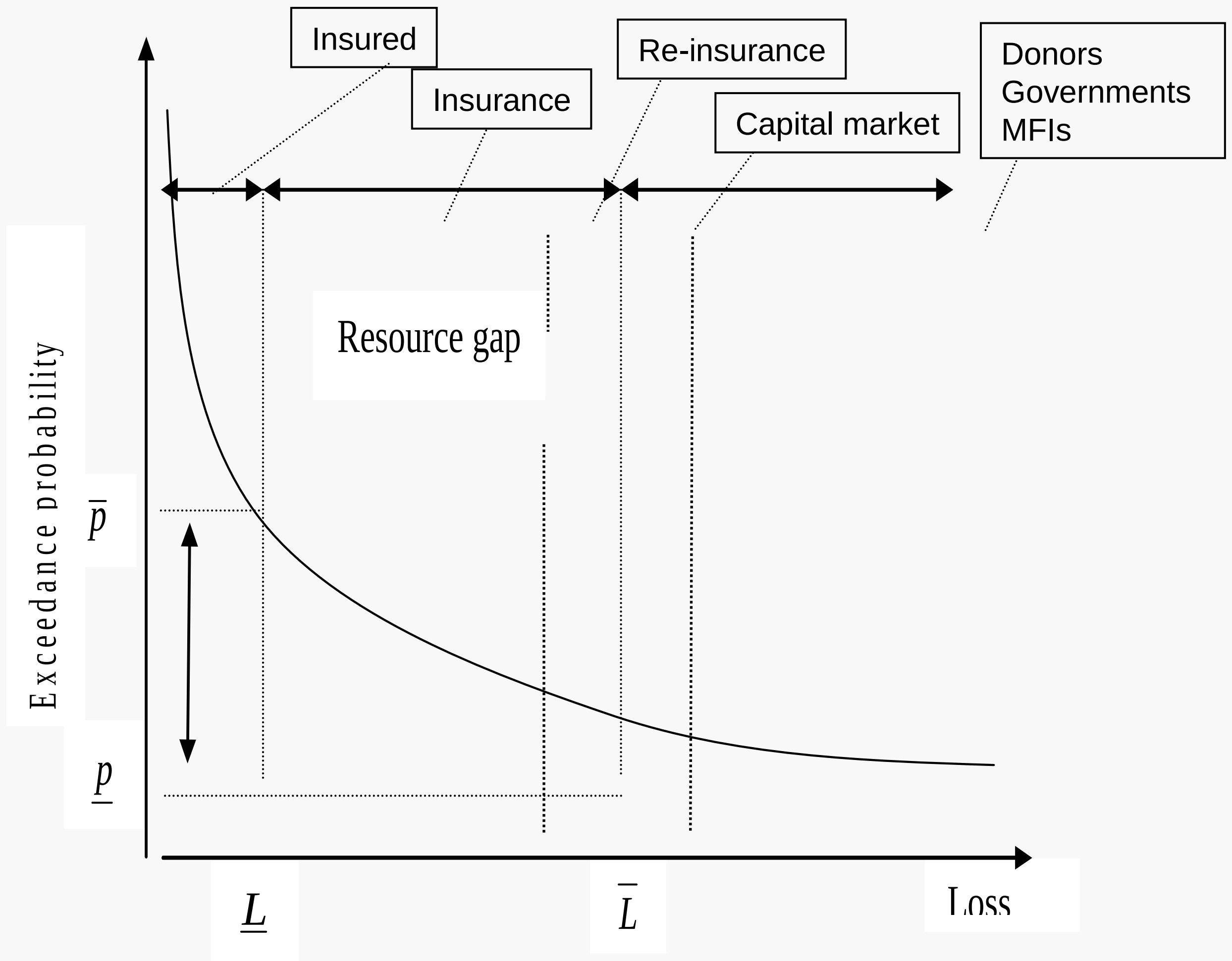


Sovereign catastrophe risk coverage (Mexico bond, Caribbean Cat Facility, GCIF)

Making catastrophe reinsurance capacity more affordable for developing countries through (i) global mutualisation of risk; (ii) partial risk retention; (iii) premium subsidies to poorest nations; (iv) subsidies for market infrastructure and product development

Low cost of IBRD capital

Finding the right fit between public and private risk financing in case of natural disasters



Avoiding the distortion of private risk markets should be the overarching concern of aforementioned public policies

Achieving complimentarity between donor supported programs in catastrophe risk insurance and the market

- Avoid the distortion of risk markets by ensuring that donor supported catastrophe insurance programs:
  - Follow (not lead) global reinsurers on price;
  - Deal with new market segments (governments, or demand from households/SMEs due to government-policy actions; new products – e.g., 3 year contracts).
  - Provide direct premium subsidy (not capital) ONLY to the poorest countries/social strata
  - Limit subsidies to product and market infrastructure development
  - Adhere to competitive bidding on ALL (premium and product development) subsidies provided by donors to market – “NO monopoly licenses!”
  - Seek better country commitment to ex-ante risk financing in providing post-disaster donor aid.

Conclusions

- Catastrophe risk pooling at the national, regional and global level in developing countries results in considerable diversification benefits that can result in improved affordability of insurance coverage.
- Catastrophe risk financing with private sector participation should become an important part of donor disaster-related aid programs.
- Creation of PPPs in risk financing should complement rather than distort private risk markets.
- Development of institutional catastrophe risk management capacity at the country level should include a risk financing function.