Disaster Risk Finance Learning Series

Supporting Pacific Island Countries towards strengthened financial protection against disasters.

Virtual Learning Episode 4: Risk Transfer: shifting responsibility of risk

Date: 24 October 2022

Summary

Speakers:

- **John Plevin,** Senior Financial Sector Specialist, World Bank.
- **Mr Karlos Lee Moresi**, Programme Adviser – Resilient Development Finance, Pacific Islands Forum Secretariat.
- **Aholotu Palu,** Chief Executive Officer, Pacific Catastrophe Risk Insurance Company (PCRIC).
- **Alexandra Galperin**: Senior Disaster Risk Management Specialist, Asian Development Bank (ADB).
- **Akata Taito:** Inclusive Insurance Solutions Hub Coordinator, Pacific Insurance and Climate Adaptation Programme, United Nations Capital Development Fund (UNCDF).

Moderator

- **Gabrielle Emery,** Head of the Pacific Sub-regional Office, United Nations Office for Disaster Risk Reduction (UNDRR)

Background

PICs and territories are significantly vulnerable to the adverse impacts of climate change-related and geological hazards. In the recent months, the Pacific region has been affected by tropical cyclones, flooding, volcanic eruption, tsunami. Additionally, COVID-19 has significantly rolled back development gains of PICs and has further increased the existing finance gap that PICs need to build a resilient development pathway.

Through the assistance of institutions, such as the World Bank, ADB, PCRIC and more recently UNCDF, risk transfer mechanisms for Pacific Island Countries have become more prominent in the last decade in the Pacific and especially in recent disastrous events such as the volcano eruption in Tonga and the COVID-19 pandemic. These Risk Transfer tools and products are market-based financial arrangements designed to share or transfer risk burdens to a wider pool of stakeholders or investors. These products are intended to provide additional financial liquidity in the event of a disaster. The most common examples of risk transfer are indemnity-based insurance policies, parametric insurance products, and catastrophe bonds. These types of risk transfer instruments reduce the financial burden shouldered by policyholders or bond issuers by helping to ensure that, should a pre-agreed event or set of circumstances occur, a certain proportion of economic losses are transferred to external financial institutions and investors.

Summary of Discussions and Interventions from Panelists

The episode started with a short recap of the key messages from previous Virtual Learning Episodes by Mr Karlos Lee Moresi. In his presentation he highlighted that the Learning Series supports the need to further demystify disaster risk financing (DRF) and identify the appropriate DRF instruments for Pacific Island Countries (PICs). There is a renewed effort at the regional level to support PICs in strengthening financial protection against disaster events. These efforts are coordinated by the Disaster Risk Financing Technical Working Group under the Pacific Resilience Partnership. He also touched upon the Core Principles of DRF, which include: timeliness of funding;

PACIFIC RESILIENCE PARTNERSHIP
STRONGER TOGETHER

different instruments needed to address the different risk layers; the need to tailor access to the right data to inform design and development of different products. He concluded that the current Virtual Learning Episode (VLE) focused on Risk Transfer. Previous VLEs focused on the overall DRF landscape in the Pacific, instruments for preparedness - such as Anticipatory Action or Forecast based Financing and Risk Retention through instruments such as National Contingency Funds and Budgetary measures. Mr Moresi stated that all DRF Instruments have their appropriate situational application and need to be aligned with the national financial capacities and resilience planning.

KEY MESSAGES

The recap was followed by panelists from ADB, World Bank, PICRIP and UNCDF answering some key questions around Disaster Risk Financing and particularly related to Risk Transfer.

1. The first question was addressed to **Akata Taito UNCDF-PICAP** focusing on micro and meso level risk transfer products and to explain what opportunities there are particularly for covering the needs of rural and remote island communities.

Ms. Taito elaborated on the importance of strategic partnership and collaboration with different stakeholders in development of micro and meso level parametric insurance. She stressed the fact that there is limited to no baseline when it comes to climate and disaster risk insurance at a micro and meso level in Fiji and across the Pacific. Further there is a marked absence of insurance regulations. One of the most important elements in developing such a product would be to understand the local context. It was clear that there was a need to develop best practices and guidelines for insurance regulators and practitioners in this space. One component in the development of the product was also to raise further awareness around financial literacy. The design of the climate and disaster risk parametric insurance is based on demand studies. Ms. Taito shared how UNCDF team members visited communities across Fiji to better understand the key climate and disaster risks that vulnerable groups in communities are facing. At the same time identifying how much individuals and farmers could afford and pay for an insurance product.

In 2021 UNCDF launched the first parametric insurance covering cyclonic events to 1,388 households and a coverage of FJD1000 and FJD2000. During the pilot phase consultations with end users resulted in the further enhancement of the product to include rainfall. The team approached the Department of Social Welfare to also add a climate and disaster risk insurance to Social Protection. The was the first time in the world an insurance product linked climate and disaster risk and social protection. Within the next 3 years the Government of Fiji is looking at increasing the number of social welfare recipients in this system. The insurance product provides vulnerable farmers and individuals to quick access to cash and therefore enhancing their resilience and accelerating their recovery.

2. The 2nd intervention was made by **John Plevin, World Bank** describing what Risk Transfer is and future directions on such instruments.

Mr. Plevin explained how all costs of a severe disaster come in a very short timeframe. In order to solve this, we can transfer risk or share the risks. Insurance is applying the same principle to a larger group of people. Meaning, we share the risk but also the associated costs to run the scheme. At a sovereign/ government level it protects national budgets and reduces the volatility of the same. The World Bank is looking at how sovereign insurance and risk pools are placed alongside other investments and financial instruments, which can pay for more frequent losses, linking it to micro and meso insurance and to invest more into physical resilience.

3. The PCRIC has historically been involved in supporting the region's sovereign risk insurance pool. Mr **Aholotu Palu**, shared some of the lessons being derived through this experience and what opportunities are developed in the risk transfer space.

PCRIC was established 2016 as a captive insurance company in the Cook Islands and has been the only provider of sovereign insurance in the Pacific. The insurance product is designed to provide Government's with access to cash following a cyclone or earthquake focusing on supporting immediate relief needs. Mr Palu emphasised the importance of understanding the correlation between economic development of PICs and disasters. The 2020 consultations with 10 PICs conducted by PCRIC confirmed that there is still demand for financial protection amongst PICs. He further encouraged PICS to have a clear strategy in place that identifies DRF instruments based on their risk profile, as insurance is only one instrument and cannot cover all costs related to disasters. Another point he raised is, that PICs must be able to afford the premiums that come with these instruments and where necessary to support with additional resources. Risk transfer instruments also need to be contextualized. In early 2023 PCRIC is looking at 2 new products covering excess rainfall and droughts. Consultations with PICS on these products are already underway.

4. The ADB features prominently in risk transfer through the Disaster Resilience Program. Mrs **Alexandra Galperin**, talked about some of the opportunities ADB is looking at to help countries strengthen financial protection to disasters and what do countries need to do to be able to better engage with donors like ADB?

Mrs Galperin shared that there are a range of DRF instruments available to address post disaster needs and also assist in emergencies through loans and grants. These instruments however could take up to 2 months to be set up. Through the ADB Contingency Fund, ADB has the ability to provide assistance immediately, in form of general budget support and complement other assistance and financing instruments. For any country to be eligible for the assistance, countries need to complete a set of legal, institutional or policy reforms in the area of DRM. Since 2020, 10 PICs have signed up to the program which now also includes Health emergencies. Assistance is provided when a Declaration of Emergency is issued by the affected government. ADB is entering the 4th phase of the Pacific Resilience Program and will continue to provide technical assistance to PICs in risk assessment capacity development. In order that PICS can also better understand the physical burden of climate and weather events in the next 10-20 years, Mrs Galperin said that financial resilience also depends on quick allocation of disbursement, emergency procurement, emergency planning etc. The program will aim to strengthen the capacities in this field.

Concluding Remarks of Panellists

Aholotu Palu, PCRIC: More effort needs to be made for PICs to understand better that insurances are not a cost but an investment. Strengthening of capacities around DRF in PICs is still a high priority. Collectively we need to be more proactive in achieving this.

Alexandra Galperin, ADB: DRF really needs to take a collaborative approach in order to improve existing products. The necessary risk data needs to be improved.

John Plevin, World Bank: We need to continue to build the momentum on DRF in the Pacific and at the same time ensure the quality of instruments is appropriate. We need to make it right from the start.

Akata Taito, UNCDF: More awareness around insurance products is needed for individuals to understand the benefits of different products. So that households and individuals see insurances as investment and no longer as an additional cost.

To learn more, you can access the recorded Session on VLE 4 here.