

Central Asia Regional Economic Cooperation Program Disaster Risk Engagement Meeting

Session 3: Roadmap for a CAREC Disaster Risk Transfer Facility

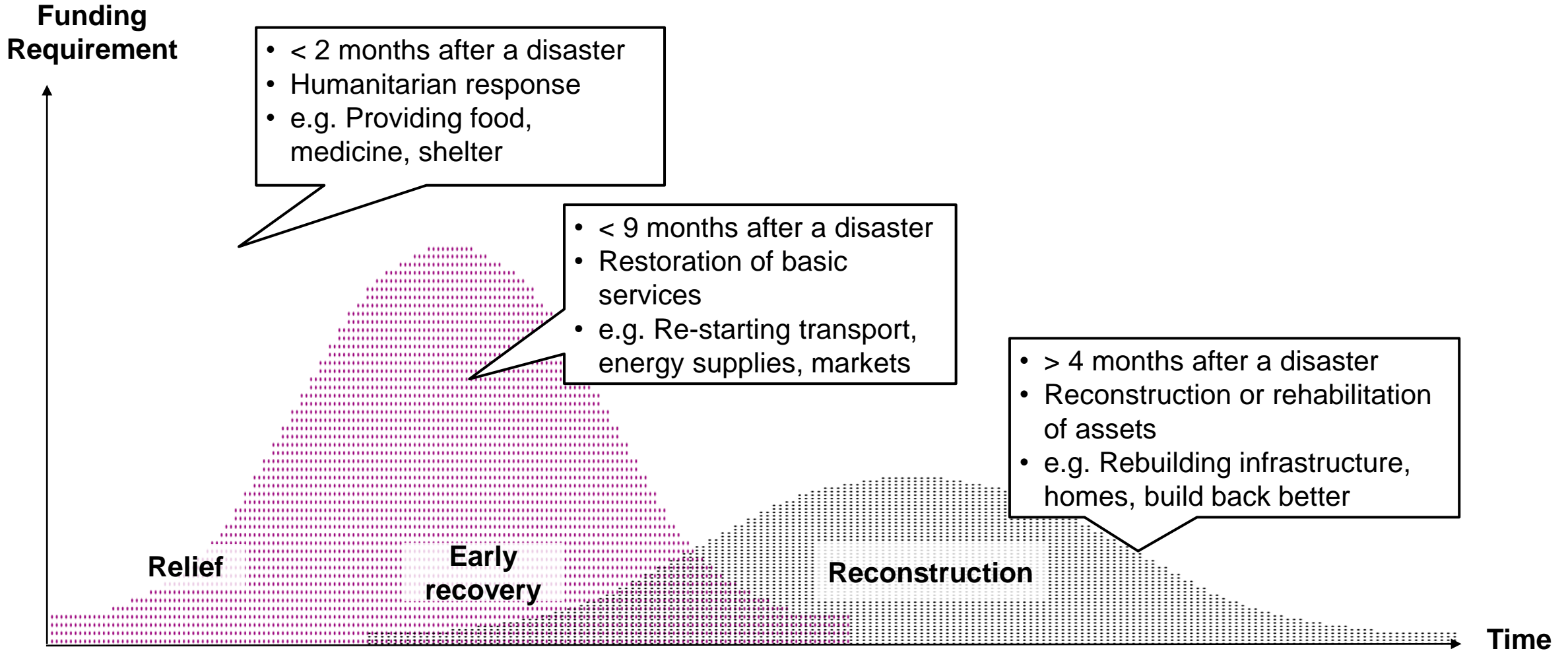
Islamabad, Pakistan
July 2023



Introduction: Recap of the Fundamentals

Requirement for Immediate Post Disaster Liquidity

Immediate Funding is Key



Source: Vivid Economics

Parametric Insurance

Fast Payment After an Event

A different type of insurance

- Parametric policies respond to an event, not a proven loss like traditional indemnity insurance
- This means that loss payments can be made virtually immediately after the event
- No time and cost of post disaster loss adjustment
- Countries can buy insurance against windstorm, earthquake and excess rain
- Countries know the expected pay-out within 3 day (allowing them to plan/spend) and will have recovered the money within 14 days

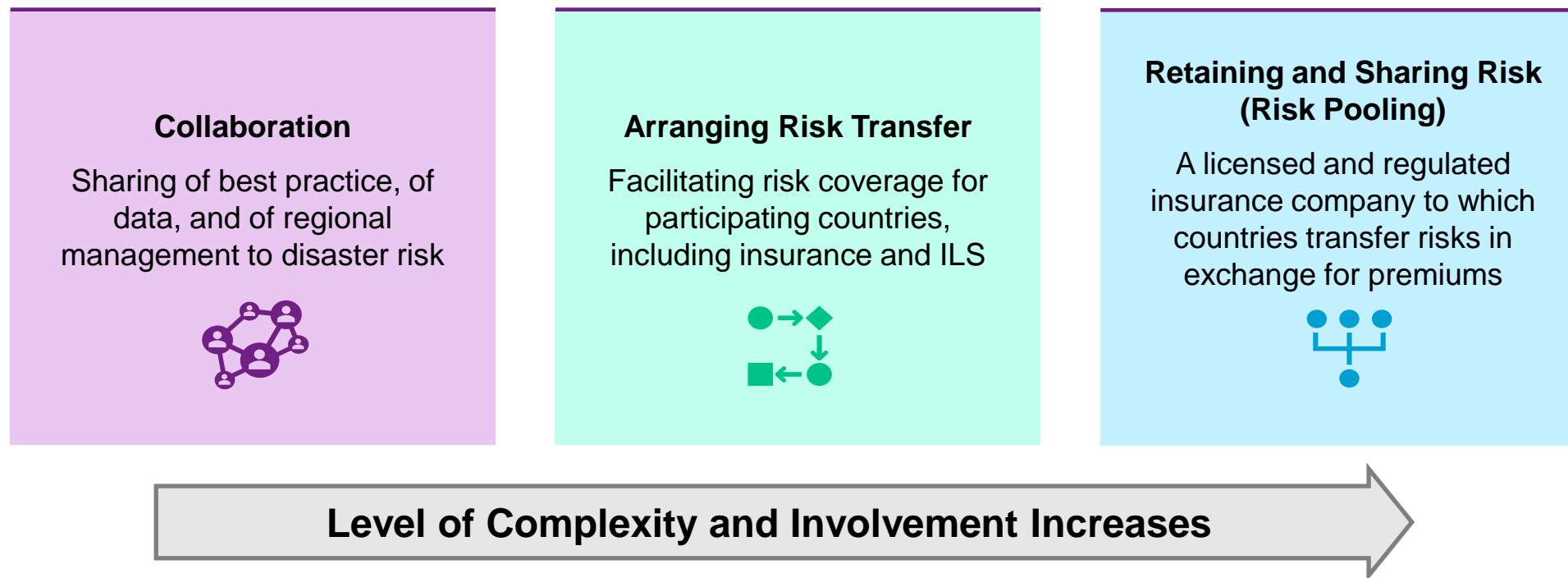
TRIGGER	INDEMNITY	PARAMETRIC INDEX
Speed of pay-out	Red	Green
Transparency	Yellow	Green
Cost effectiveness	Yellow	Green
Basis risk	Green	Yellow

- FAST ✓
- OBJECTIVE ✓
- COST-EFFECTIVE ✓

Existing Regional Risk Facilities and Lessons for CAREC

Functions of a Regional Risk Facility

Countries around the world have collaborated on regional risk financing, including in the Caribbean and Central America, in South America, in Africa, in the Pacific, and in Southeast Asia. A regional facility can serve one or several functions:



Determining its function and form would be informed by factors including countries' needs in DRF, international cooperation and public and foreign relations policy goals of the countries and funding partners, and countries' levels of commitment to participate in a regional facility.

Existing Regional Risk Facilities



CCRIF SPC
The Caribbean Catastrophe Risk Insurance Facility



SEADRIF
SOUTHEAST ASIA
DISASTER RISK INSURANCE FACILITY



Alianza del Pacífico¹



African Risk Capacity



PACIFIC CATASTROPHE RISK INSURANCE COMPANY

¹Refers to the 2018 the Pacific Alliance catastrophe bond placement, which was a joint issuance to four sovereign entities, rather than a regional risk facility.

CCRIF SPC (formerly the Caribbean Catastrophe Risk Insurance Facility)

The First Regional Emergency Response Scheme



Background

- In 2004 Hurricane Ivan wreaked havoc in the Caribbean. It caused damage of nearly \$4 billion (at current values), with severe loss and damage in Grenada, Jamaica and Cayman Islands; but social impact was much higher
- Aid was promised, and whilst some of it arrived it was too little and, crucially, too late. A reliable source of immediate post disaster funds that can reduce reliance on unreliable overseas largesse was needed.

Solution

- CCRIF SPC is a special insurance company owned by trust, with that trust representing the interests of Caribbean governments
- It offers parametric insurance policies to Caribbean governments

Successes and Challenges

- **CCRIF SPC insurance products work.** Over 14+ years CCRIF SPC has made 56 payments to 16 member countries totalling US\$245 million. Every single payment has been made within 14 days of the event.
- **The cover is good value.** CCRIF SPC manages premium by use of its pooled capital augmented by reinsurance which can be purchased efficiently due to the diversity of its portfolio
- **CCRIF continues to grow and innovate.** Expanding coverage options, improving policy conditions and innovating to cover new risks.
- **The benefits are more than just insurance.** A catalyst for better risk understanding and post disaster response planning as well as supporting the sharing of ideas, data and best practices.

African Risk Capacity (ARC)

A Program with Capacity Building at its Heart



Background

- Formed in 2014 by the World Food Programme African Risk Capacity (ARC) is an agency of the African Union with an associated mutual insurer.

Solution

- At its core ARC is a parametric drought/crop failure insurance pool, but more important is the work it does to improve risk understanding and emergency response after disasters within member governments
- Before being allowed to buy cover, countries must obtain a Certificate of Good Standing, meeting minimum standards of financial probity.
- They must also commit to engage in risk management processes and ultimately to purchase appropriate insurance cover

Successes and Challenges

- **Speed of payment in key.** ARC provides funds immediately after an event to protect, feed and rehouse those affected in an effort to save lives and reducing damages to livelihood.
- **The programme is cost-effective.** An Oxford University study for African Risk Capacity showed that \$1 received immediately after a drought occurs is worth up to \$5 of aid received later.
- **Basis risk must be balanced against benefit** when considering overall programme value.



Background

- Pacific Island Countries (PICs) are highly exposed to adverse natural hazards, including tropical cyclones, earthquakes, volcanic eruptions, and tsunamis
- PICs suffer an average of more than \$280 million per year in damages from disasters¹. Human and physical environments are also adversely impacted.

Solution

- The Pacific Catastrophe Risk Insurance Company (PCRIC) was established in 2016 to address climate and disaster risks across 14 PICs
- It is a specialised disaster risk insurance provider.
- Current product offerings include parametric insurance policies covering tropical cyclones and earthquakes (including tsunami)

Successes and Challenges

- To date, four pay-outs have been made for an aggregate amount of more than US\$11 million.
 - Two were made under PCRAFI, the other half were made by PCRIC.
- The pay-outs were all received immediately post-disaster(s) and were the first financial injections of emergency funds made into each country.



¹Source: <https://pcric.org/>

Pacific Alliance



Background

- The Pacific Alliance is a regional initiative that promotes the economic integration of Chile, Colombia, Mexico, and Peru

Solution

- Joint issuance and marketing of catastrophe bonds to cover 4 countries
Issued in 2018 and covered US\$1.36 billion earthquake risk for 2-3 years, the largest sovereign risk insurance transaction
- Now exploring a new bond with new hazards, potentially including tropical cyclones, drought, floods and/or cold weather

Successes and Challenges

- By working together, the interest in the deal was very high - the cat bond attracted more than 45 investors globally, ranging from ILS funds to pension funds to reinsurance companies.¹
- Peru received US\$60 million in 2019 when a magnitude 8.0 earthquake triggered its catastrophe bond protection



Pacific Alliance countries. Source: Artemis.bm

¹Source: <https://thedocs.worldbank.org/en/doc/192341554318525877-0340022019/original/casestudyfinancialproductsPacificAlliancefinal4.1.2019.pdf>

Lessons Learned from Existing Regional Facilities



1 The schemes work

2 Disaster risk modelling is essential for making informed management decisions

3 Basis risk, real and political, needs to be addressed

4 There must be a balance between product affordability and financial sustainability

5 Local/regional stakeholders' interests must be represented

Overall, the Benefits of Regional Risk Facilities Overcome Basis Risk

It's Not All About How Much Is Paid Out



Speed of Payment

The size of claim payment is known within days of event

Payment is received shortly after



Budget Certainty

Less reliance on central government / international generosity

Pooling reduces exposure to re/insurance market price volatility



Risk Awareness

A catalyst to improved risk understanding

Supports risk-informed prioritization of disaster risk reduction actions



Preparedness

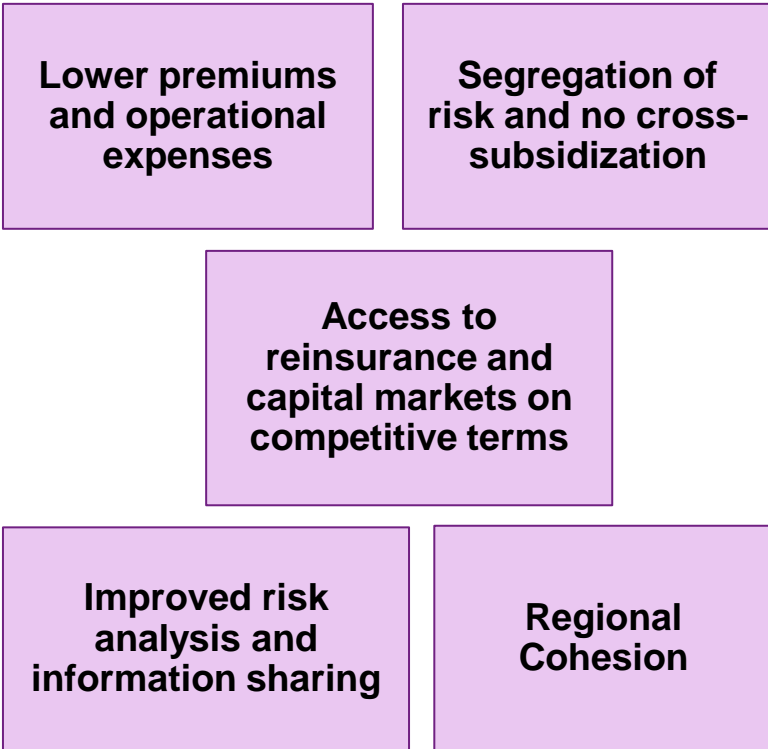
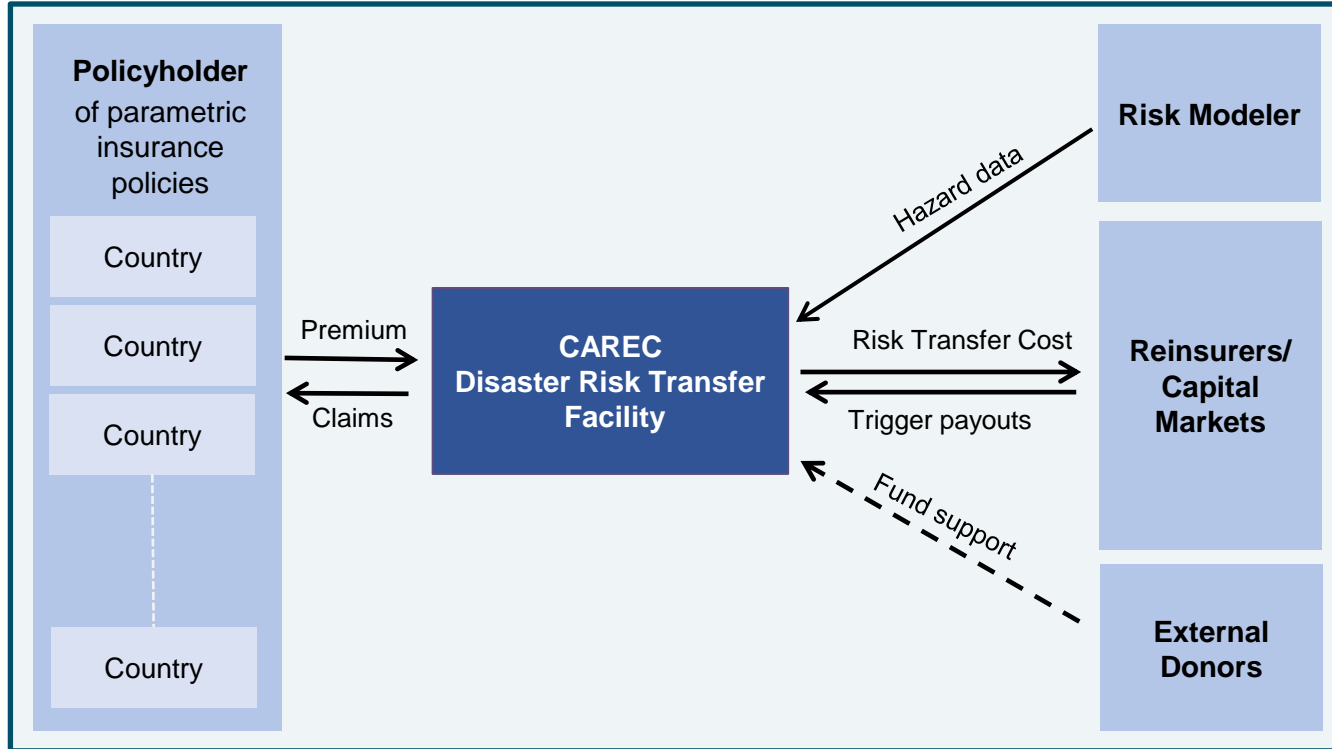
Schemes can encourage development of detailed, audited contingency plans

Provides a forum for shared expertise, potentially for shared resources

Options and Roadmap for a CAREC Risk Facility

Potential Structure for a CAREC Risk Facility

A Longer-Term Goal for Risk Transfer and Regional Cooperation



Key Considerations at Each Stage of Facility Development



Pre-Requisites

- Determine the role of the ADB
- Obtain countries formal request/confirmation to participate in the facility
- Conduct more detained risk modelling in coordination with member countries



Stage 1: Facility Creation

- Country of domicile or recognition
- Operational entity or legal nature, including ownership structure
- Sources of initial capitalization
- Corporate governance structure
- Key advisors
- Initial product offering

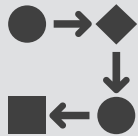


Stage 2: Facility Operation

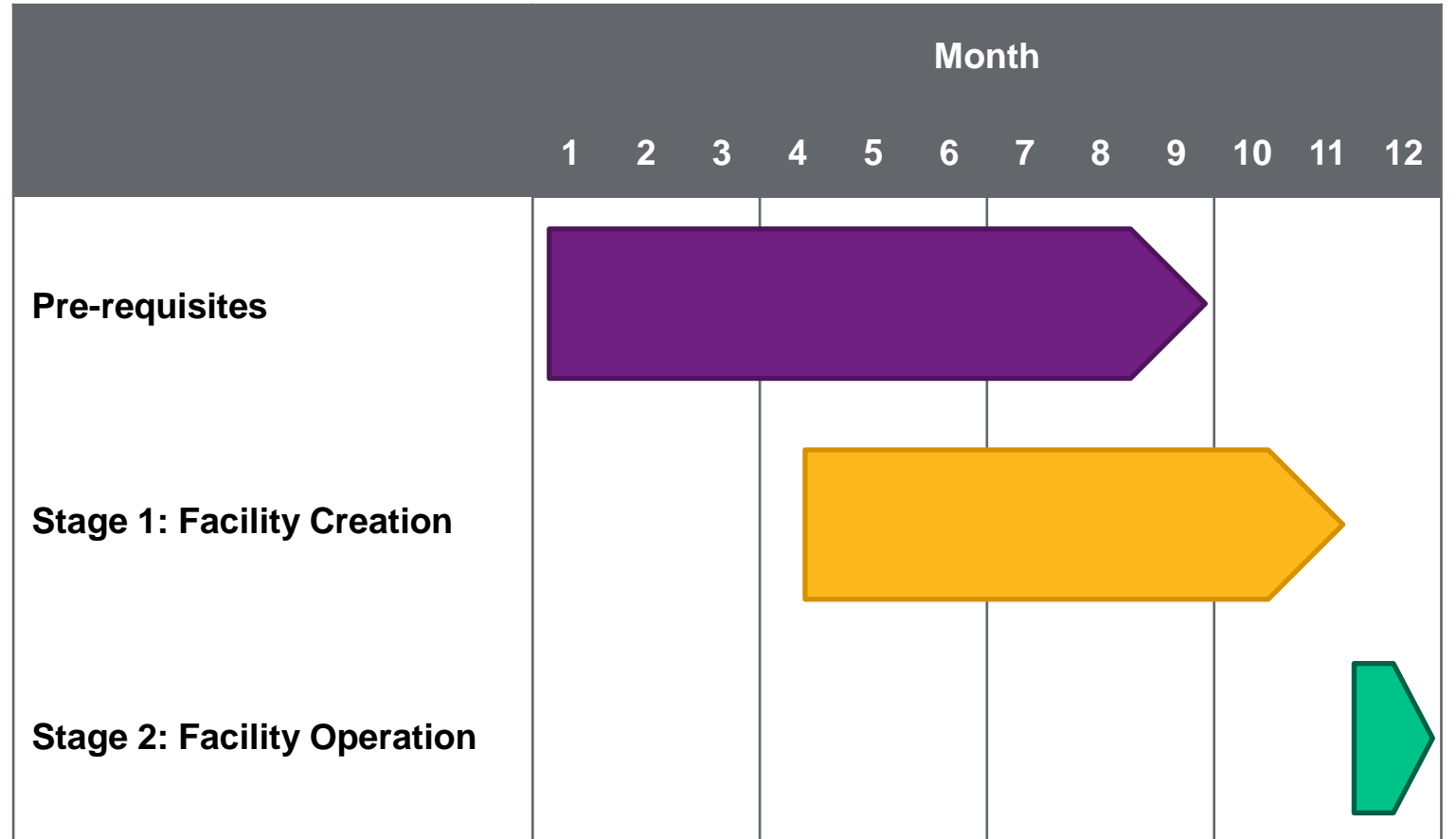
- Operational structure
- Alternative sources of capital required for longer-term financial sustainability
- Evolution of its products
- Country engagement program.



Main Stages of CAREC Risk Facility Development and Roadmap



A Risk Facility Implementation Roadmap will facilitate discussions among the facility's key actors, allowing countries to finalize decisions on important matters and eventually craft plans for execution.



Annex

Main Stages of CAREC Risk Facility Development and Roadmap



Phase and Task		Month											
		1	2	3	4	5	6	7	8	9	10	11	12
Pre-requisites	Determine the role of the ADB and the CAREC Secretariat	█											
	Obtain countries formal request/confirmation to participate in the facility		█										
	Conduct more detained risk modelling in coordination with member countries			█									
Facility Creation	Formal discussion between the ADB, participating countries and technical partners				█								
	Propose composition of the CRF Steering Committee					█							
	Outline the Facility Creation and Facility Operations decision						█						
	Finalize Steering Committee Membership							█					
	Agree dates for Committee's inaugural meeting								█				
	Propose draft agenda for first gathering									█			
	Inaugural Steering Committee meeting										█		
Facility Operation	Agree general timeframes of decision-making on the facility												█
	Agree specific timeframes for each decision point in the Facility Creation and Operations stages												█
	Agree persons accountable and responsible for the due diligence exercises												█
	Agree other next steps identified by the Steering Committee												█

Disclaimer



This analysis has been prepared by Willis Limited for the Asian Development Bank under a Technical Assistance contract.

Willis Limited has relied upon data from public and/or other sources when preparing this analysis. No attempt has been made to verify independently the accuracy of this data. Willis Limited does not represent or otherwise guarantee the accuracy or completeness of such data nor assume responsibility for the result of any error or omission in the data or other materials gathered from any source in the preparation of this analysis.

There are many uncertainties inherent in this analysis including, but not limited to, issues such as limitations in the available data, reliance on client data and outside data sources, the underlying volatility of loss and other random processes, uncertainties that characterize the application of professional judgment in estimates and assumptions, etc. Ultimate losses, liabilities and claims depend upon future contingent events, including but not limited to unanticipated changes in inflation, laws, and regulations. As a result of these uncertainties, the actual outcomes could vary significantly from Willis Limited's estimates in either direction. Willis makes no representation about and does not guarantee the outcome, results, success, or profitability of any insurance or reinsurance program or venture, whether or not the analyses or conclusions contained herein apply to such program or venture.

Willis does not recommend making decisions based solely on the information contained in this analysis. Rather, this analysis should be viewed as a supplement to other information, including specific business practice, claims experience, and financial situation. Independent professional advisors should be consulted with respect to the issues and conclusions presented herein and their possible application. Willis makes no representation or warranty as to the accuracy or completeness of this document and its contents.

Willis does not provide legal, accounting, or tax advice. This analysis does not constitute, is not intended to provide, and should not be construed as such advice. Qualified advisers should be consulted in these areas.

Willis makes no representation, does not guarantee and assumes no liability for the accuracy or completeness of, or any results obtained by application of, this analysis and conclusions provided herein.

Acceptance of this document shall be deemed agreement to the above.