Climate Change, SIDS and Insurance

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Issues for further consideration (c)

Is insurance the most suitable mechanism for risk transfer?

What needs to be done first in order for insurance schemes to be successful (e.g. comprehensive risk assessment)?

What is insurance, why do we need it

Insurance is the equitable transfer of the risk of a potential loss, from one entity to another, in exchange for a premium and duty of care

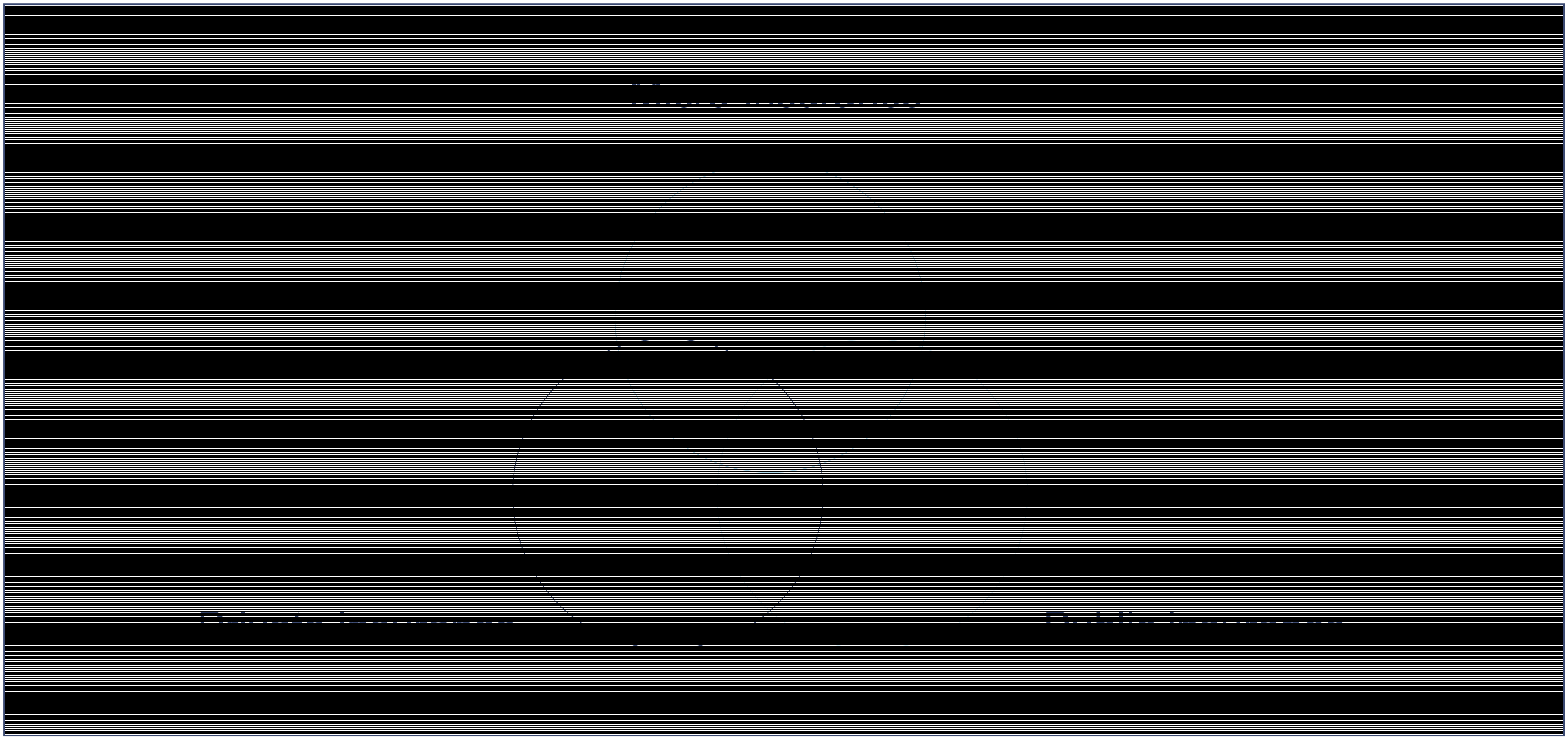
- Developing insurance would be beneficial even without CC
- Mechanism for risk-pooling between parties and over time
- Immediate access to predictable level of funds for disaster relief
- Provides incentives for risk management
- Expertise in disaster mitigation and post disaster recovery
- Providing information through its measurement and pricing of climate risks

Limits of insurance for SIDS

- Expensive: (You have to pay for risk transfer + Volatility loading + Expenses + Profit of insurer)
- Insurers pull-out in bad times
- Unpopular
- Cyclical market leads to volatility
- Lack of economy of scale and concentration of risk
- Moral hazard
- Lack access and coverage (<40% in OECD)

Although there are limitations of insurance, current low penetration means that any expansion will be beneficial

Integrated solution



Risks to SIDS

Acute	**Chronic**
Wind storm	Sea-level rise
Storm surge	Change precipitation
Drought	Temperature rise
Flood	Change in acidity of oceans

Specific insurance needs of SIDS

- Vulnerable individuals: e.g. poor and marginal groups, people living in vulnerable areas
- People and companies
- Governments: post catastrophe
  Infrastructure
  Post disaster liquidity
  Post disaster recovery

Private insurance will reduce post-disaster strain on governments

Micro-insurance

- Normal insurance with multiple policyholders under each policy
- Partnership between NGO and large insurer
- Provides funding for risk mitigation
- Must be combined with education
- Proven existing models (e.g. Basix in India and Hurricane-resistant home improvement program in St Lucia)
- Insurance companies enthusiastic

BUT

- Lack of economies of scale - insurers like potentially large markets
- What happens in catastrophe?

Proposal: Design SIDS micro-insurance model with partner

Developing private market

- Should do anyway and low cost
- Size of market and spread of risk
- Regulation and tax
- Develop domestic market and/or attract foreign capital
- Provide attractive business environment
- Capacity building
- Contributes to economic diversification
- Example of Bermuda

Proposal: Strategy required to develop private insurance markets

Caribbean Catastrophe Risk Insurance Facility (CCRIF)

- Captive fund set up by the World Bank with Caribbean countries
- Provides post-disaster liquidity
- Parametric pay-out occurs if an event exceeds a trigger level
- Limited ambitions – likely to get off ground
- Parametric so immediate pay-out
- Captive so no profit loading, low admin and politically sustainable
- High concentration of risk: limited risk pooling
- Reinsurance and cat bonds expensive due to proximity to Florida
- Integration with local insurers
- Commitment from governments

Proposal: Extend geographically and scope (if successful)

Insurance techniques for policy purposes

- Risk prevention is best form of insurance
- Resource allocation decisions
- Estimate cost, e.g. Hurricane Gilbert 1998 $1-4bn vs Hurricane Ivan 2004 $360m
- Jamaica $100m - $500m per annum from hurricanes
- Maldives: “Cost” of loss of sovereignty: $50bn

Proposal: Simple risk premium calculations required