



African *Risk Capacity*

Sovereign Disaster Risk Solutions
A Specialized Agency of the African Union



“ Pan-African solidarity in approaching climate risk makes financial sense.”

The African Risk Capacity (ARC) is a ground breaking extreme weather insurance mechanism designed to help African Union Member States resist and recover from the ravages of drought. As currently structured, the international system for responding to natural disasters is not as timely or equitable as it could be. Funding is secured on a largely ad-hoc basis after disaster strikes, only then can relief be mobilized toward the people who need it most. In the meantime, lives are lost, assets are depleted, and development gains suffer major setbacks – forcing more people into chronic destitution and food insecurity in the world’s least developed countries.

ARC is an African solution to one of the continent’s most pressing

4.4 times the benefit

One dollar spent on early intervention through ARC saves nearly four and a half dollars spent after a crisis is allowed to evolve.

challenges, transferring the burden of climate risk away from governments – and the farmers and pastoralists whom they protect – to the ARC that can handle that risk much better. This African-owned, AU-led financial entity uses *Africa RiskView*, an advanced satellite weather surveillance software – developed by the UN World Food Programme (WFP) – to estimate and trigger readily available funds to African countries hit by severe drought. Because such droughts do not happen in the same year in all parts of the continent, pan-African solidarity in the creation of a disaster risk pool like ARC is financially effective. Pooling risk across the continent more than halves the fund requirements to countries of emergency contingency funds, while decreasing reliance on external aid.

How ARC Works

ARC’s objective is to capitalize on the natural diversification of weather risk across Africa, allowing countries to manage their risk as a group in a financially effi-

cient manner in order to respond to probable but uncertain risks. ARC utilizes modern financial mechanisms like risk pooling and risk transfer to establish the contingency financing facility. These techniques, are applied by African countries in innovative ways to lower the cost of the response to disasters, before they become a humanitarian crises, and provide better services to those affected. How it works:

- The initial capital comes from participating countries’ premiums as well as one-time partner contributions.
- ARC works with countries to calculate country premiums and allocate payouts to member countries based on predetermined and transparent rules for payment.
- Countries select the level at which they wish to participate by selecting the amount of risk they wish to retain, and financing they would want from ARC for droughts of varying severity. (ARC will provide coverage for other hazards, including floods, at a later date.)

“ ARC is an African solution to one of the continent’s most pressing challenges”

- Operations plans, which are meant to optimize ARC disbursements, are a prerequisite for participation and take into account existing mechanisms, priorities and needs of each participating government. These plans are evaluated by the ARC Board's Peer Review Mechanism according to standards set by the Conference of the Parties.
- The pool reinsures itself as well as benefits from investment income. This builds and protects the capital available for coverage to member governments.

Early Intervention

ARC payouts arrive in the national treasury within 2-4 weeks of harvest so that the first assistance

120_{days}

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reaches needy households within 120 days – the time period as-set depletion at the household level begins. Experts from Oxford University and International Food Policy Research Institute (IFPRI) conducted a cost-benefit analysis (CBA) to examine the economic advantages and disadvantages of establishing a risk pooling facility as an early response mechanism to severe drought in sub-Saharan Africa.

A further analysis by the Boston Consulting Group, shows the potential benefit of ARC outweighs the estimated cost of running ARC by 4.4 times compared to traditional emergency appeals for assistance, as a result of reduced response times and risk pooling. This means one dollar spent on early intervention through ARC saves four and a half dollars spent after a crisis is allowed to evolve.

Payouts from ARC

Rules for payout from ARC are identified up front, accurately reflect losses faced by member countries, allow payouts to occur

promptly as soon as it is clear the rains have failed, and are based on objective and transparent criteria. To establish these rules, WFP developed a software application, *Africa RiskView (ARV)*, which translates satellite-based rainfall information into near real-time response cost estimates and provides early warning information. ARV serves as the technical engine for ARC, providing guidance to governments on risk transfer level options, risks assessments to facilitate contingency planning and identifying, based on objective criteria and once ARC risk transfer parameters are set, when payouts are due to a country.

Institutional Structure

In July 2012, AU Heads of State put forth a decision to establish ARC as a Specialized Agency of the African Union. 18 Member States initially signed the ARC Establishment Agreement and six additional countries have since signed the treaty. The first Conference of the Parties was

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held in Dakar, Senegal in February 2013, during which the parties elected a governing board and selected Bermuda as an interim jurisdiction for the financial subsidiary until such time that an equally favourable legal and regulatory regime exists in an AU Member State.

Together with the mutual sovereign insurance company, ARC Ltd, the Agency has become one of the most innovative international organizations with the potential to scale to a multi-billion-dollar African natural disaster risk portfolio in the years ahead.

Summary

By merging the traditional approaches of disaster relief and quantification with the concepts of risk pooling and risk transfer, ARC has created a pan-African drought response system that meets needs of those affected in a timelier and more efficient way. ARC provides an important step forward in creating a sustainable African-led strategy for managing extreme climate risks.

ARC Agency Governing Board

Hon. Dr. Ngozi Okonjo-Iweala (Nigeria),
Coordinating Minister for the Economy
and Minister of Finance for Nigeria

Tosi Mpanu-Mpanu (Democratic Republic of Congo),
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Group of Negotiators and Alternate
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Former Minister of Agriculture and
Food Security

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Managing Director of the “Banque
Internationale pour l’Afrique BIA-Niger”
and former Minister of Finance

Diombar Thiam (Mauritania),
Minister of Finance

Dr. Agnes Kalibata (Rwanda),
Interim President of AGRA and Former
Minister of Agriculture and Animal
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* Members of the ARC Agency Governing Board serve in their individual capacities. Titles are listed for identification purposes only.

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