



**CLOSING THE CLIMATE
RISK PROTECTION GAP:
Lessons Learned from
the Caribbean Region**



CLOSING THE PROTECTION GAP

The G7 Climate Risk Insurance Initiative and the InsuResilience Global Partnership aim to have 500 million poor and vulnerable people in developing countries benefiting from direct or indirect insurance by 2025¹. Parametric microinsurance products are critical to closing the protection gap among the most vulnerable. Yet these products are quite new, and there are still many lessons to be learned in how to effectively reach the poor and vulnerable.

DISTILLING LESSONS LEARNED²

The Climate Risk Adaptation and Insurance in the Caribbean (CRAIC) project has been promoting micro- and meso-level insurance for climate risk in the Caribbean since 2011. Given that CRAIC was one of the first programmes of its kind in the region, it was designed as a learning project, allowing the project consortium to capture lessons learned during implementation and update interventions accordingly. The lessons learned through CRAIC are applicable to other small island and coastal states. Munich Climate Insurance Initiative (MCII)³ is publishing these lessons learned to encourage a culture of knowledge sharing on climate and disaster risk insurance topics.

CLIMATE RISK ADAPTATION AND INSURANCE IN THE CARIBBEAN PROJECT

The CRAIC project was conceptualized to address climate change, adaptation, and vulnerability by promoting parametric insurance at the individual level as a risk management instrument in the Caribbean. In order to reach this population, CRAIC developed a microinsurance product called the Livelihood Protection Policy (LPP). The CRAIC project is being implemented by MCII together with its partners, CCRIF SPC (formerly the Caribbean Catastrophe Risk Insurance Facility), ILO's Impact Insurance Facility, DHI, and Munich Re. It is intended to complement other similar instruments at the sovereign level, particularly the services and products provided to 19 Caribbean governments by CCRIF SPC.

¹ <https://www.insurresilience.org/bmz-idf-and-undp-scale-up-efforts-to-strengthen-climate-resilience-as-part-of-the-insurresilience-vision-2025/>

² A full-length lessons learned document will be published in April 2020.

³ MCII was initiated as a charitable organization in April 2005 in response to the realization that insurance solutions can play a role in adaptation to climate change. This initiative is hosted at the United Nations University's Institute for Environment and Human Security. MCII's purpose is to promote public-private protection and insurance solutions for people affected by extreme weather, allowing the public and private sectors to enhance countries' resilience and close the protection gap of vulnerable groups.

LESSON 1

Expectation Setting

While governments, who are CCRIF SPC's main clients, are very familiar with parametric insurance as a tool for disaster risk financing and include it as a part of their fiscal policy framework, the average citizen is not very aware of the parametric insurance that is offered by CRAIC. It is therefore important to engage in consumer education and on the benefits of climate risk insurance in the face of a changing climate. This could contribute to a greater demand for the product.

EDUCATION:
a vital component
of the insurance roll
out process

Parametric insurance can be difficult to understand for first time clients because the payout is determined by an estimation based on the severity of a natural hazard event and not by the actual amount of damage incurred to an asset owned by the policy holder. Also, insurers and project implementers must ensure that potential buyers of parametric insurance products understand that these policies are not designed to cover all of their losses, but rather to provide them with quick liquidity after their policy has been triggered by an extreme weather event.

BASIS RISK:
awareness raising
among policyholders

Basis risk is an inherent aspect of parametric policies. Yet differences between payouts and experienced losses can lead to mistrust in the validity of the models and quality of the products. Implementers must clearly articulate to potential buyers how different perils are measured and how basis risk may affect them. Insurers can minimize the impact of basis risk by augmenting policies with ground-truthing mechanisms and secondary triggers, and by continually improving the models.

PARAMETRIC MODELS:
data collection
for improved model
performance

The validation of parametric models is usually performed using historical records. These data are often scattered across sources of varying quality and accuracy, and oftentimes time series data may be difficult to assess. To improve the accuracy of the models, governments should systematically collect damage records, and insurers should regularly incorporate new and improved (e.g., higher resolution) data into models and product updates. Hazard models also need to take into account the future predicted trends of these losses in light of climate change.

**DISASTER RISK
MANAGEMENT:**
insurance
complements
disaster risk
reduction measures

Practitioners should work with policyholders to build awareness on how parametric insurance should be used alongside other measures to minimize their exposure to natural hazards. When giving trainings on insurance, implementers must also educate participants on its role within a comprehensive disaster risk management strategy.

LESSON 2

Product Design

CRAIC designed the LPP to cover extreme rainfall and winds, with standardized payouts. The project made the product available to anyone in the country who was likely to be affected by these extreme weather events, which led to many valuable lessons on product design.

SEGMENTED APPROACH: product variety for increased viability

Parametric microinsurance needs to be correctly priced and meet the needs of the client if it is to be commercially viable. Certain prices may make the product unaffordable for the poor and vulnerable.

Differentiated products allow individuals to buy the product that most meets their needs. Multi-peril insurance can be especially useful for lower income groups. Products can also be differentiated by hazard, price, trigger levels, payout amounts, and bundled products. Similarly, the needs of men and women may be different, and implementers should consider the gendered aspects and impacts of insurance during product design.

Government-sponsored or subsidized policies for specific target groups that are low-income, highly exposed, or vulnerable to extreme weather events, or those who work in critical sectors, could be beneficial. Governments could do this by paying for part of the insurance premium, eliminating taxes on insurance, or leveraging existing cooperative groups to distribute group policies.

Bundling insurance with non-insurance products, such as credit, may increase client value. Such products can protect financial institutions from extreme weather events while also increasing access to credit.



SOCIAL PROTECTION:
aligning microinsurance schemes with social protection strategies

Market-based approaches struggle to reach the poor. Social protection systems should recognize natural hazard and climate change risks and address these as part of a holistic effort to reduce vulnerability. Linking climate risk insurance with social protection provides an opportunity for governments to reduce the financial burden of disaster response while facilitating access to products that help the poor and vulnerable to cope with climate and natural hazard impacts.

DISTRIBUTION CHANNELS:
identifying the value proposition for the distribution channels

Microinsurance often targets people located in remote areas who may not have access to insurance offices. People will rarely travel long distances to purchase insurance. Insurers thus leverage commonly-accessed distribution channels that reach the target population. By using banks as distribution channels, financial inclusion may increase access to insurance along with other services. However, the product must be designed to also add value for the seller.

VULNERABLE INDIVIDUALS:
using customer-centric design to meet needs

Insurers should consider how potential policy holders will purchase and pay for the product and build this into the product design. Aligning premium payment dates with the policyholders' income streams is one way to improve affordability. Allowing premiums to be paid on a monthly or even weekly basis rather than requiring an annual lump sum also makes the product more accessible.

GROUP POLICIES:
applying discounts to incentivize group sales

If group and individual sales are to be offered in tandem, there should be a discount applied to the group premium. Otherwise there is no incentive for group leaders to consider purchasing a group policy on behalf of their members. Individual sales may not be viable for all insurers, so covering multiple individuals through a single group insurance contract may be a key to success.

LESSON 3

Market Development

In addition to the actual design of a product, CRAIC needed to develop the market for these types of insurance solutions. Market development is a critical component of closing the protection gap.

PARTNERSHIPS: scaling up through collaboration with local NGOs and governments

At the policy level, ministerial champions and regulators are instrumental for a new insurance product. Scaling may also require the support of the government, which often possesses practical networks to reach target groups. Likewise, working with local NGOs can be instrumental in scaling, as they often have strong community ties, understand the local scenarios, and can provide a platform for educating clients about the product. Local NGOs and governments also often have the trust of the local population.

CREATING COMPETITION: success without picking winners

Introducing competition in the market among insurers and distribution channels can provide the impetus for insurance companies to advertise, educate and sensitize at a greater scale to increase their market share and motivate innovations in product offerings and outreach techniques. By creating specialized products, insurers can differentiate themselves from competitors and target particular market sectors they see as more aligned to their overall business strategy.

DIGITAL SOLUTIONS: facilitating sales and distribution of products

Digital technologies can play a role in customer acquisition. Insurers should investigate how sales agents could better use digital solutions when making their first sales. Renewals and keeping in touch with the customers through demand-oriented service messages could also be done digitally. Regulators play a key role in creating an enabling environment.

PARTNER BUY-IN: the business case for parametric microinsurance

Microinsurance should not be seen by local insurers, reinsurers and distribution partners as part of their corporate social responsibility strategy. Rather, partners should invest their resources into product development and roll out, increasing their dedication to the success of the product. Implementers should communicate expected associated staff, marketing, and sales costs clearly to partners. Expectations must be realistic, however, noting that this market segment is nascent and will take a few years to mature.

LESSON 4

Engagement for Sustainability

The CRAIC project brought together partners from the private sector, public sector, and academia to implement its project activities. Creating strong partnerships is key to a successful project.

INTEGRATION OF INSURANCE: **building general understanding**

Implementers should seek to strengthen general insurance awareness and capacity through training and technical assistance. In some cases, it may be possible to integrate educational material on parametric insurance into the governments' pre-existing training materials on disaster risk management and resilience building.

SUSTAINABILITY: **integrating microinsurance into country and regional institutions**

Implementers seeking to create sustainable parametric microinsurance products should consider how they can be integrated into country and regional institutions. Implementers may want to reach out to regional risk pools to see how microinsurance can be integrated into their offering to governments and work towards closing the climate risk protection gap⁴.

ENGAGEMENT WITH GOVERNMENTS: **embedding insurance into adaptation plans**

Climate risk insurance should be embedded into countries' climate change adaptation strategies and disaster risk management plans. In addition, the development of holistic disaster finance strategies, including climate risk insurance, can help ensure that disaster response dollars are efficiently spent and address the needs of the most vulnerable.

⁴ <https://www.insuresilience.org/wp-content/uploads/2019/09/The-Future-of-Disaster-Risk-Pooling-for-Developing-Countries.pdf>

About MCII

The Munich Climate Insurance Initiative was initiated as a charitable organisation by representatives of insurers, research institutes and NGOs in April 2005 in response to the growing realization that insurance solutions can play a role in adaptation to climate change, as suggested in the UN Framework Convention on Climate Change and the Kyoto Protocol. This initiative is hosted at the United Nations University Institute for Environment and Human Security (UNU-EHS). As a leading think tank on climate change and insurance, MCII is focused on developing solutions for the risks posed by climate change for the poorest and most vulnerable people in developing countries.

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<http://www.climate-insurance.org/projects/climate-risk-adaptation-and-insurance-in-the-caribbean/>

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Federal Ministry for the
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