

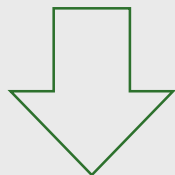
# MSMEs, climate risk & insurance

*Kickoff Workshop Breakout Group*





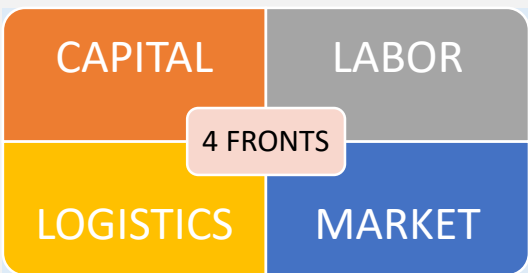
## CLIMATE IMPACTS



## DAMAGES TO

# MSMEs

via



## Coping strategies of MSMEs

Country	Natural hazard	Damages on 4 fronts	Coping strategy	Response barriers
Sri Lanka <sup>35</sup>	Torrential rain/Tropical storm, causing flood and landslides in 2016	<b>Capital:</b> Around 2/3 of MSMEs completely lost/damaged their equipment; Disrupted cash flow, loss income MSME and damage to buildings.  <b>Market:</b> Loss of trading income	Reliance on relief agencies' distribution of capital goods (tools, equipment, machinery)	Lack of (financial) risk management mechanisms, low levels of customer and supply diversification
Philippines <sup>36</sup>	Typhoons Ketsana and Parma, causing flooding in 2009	<b>Capital:</b> Closure of firms and home-based enterprises due to damages to property and equipment; damaged raw material and inventory; Closure of restaurants and guest houses due to property damage; damaged high value crops	Remittances for reconstruction with around 13% of micro-entrepreneurs being able to recover lost incomes; 11% refinancing via loans;	Lack of disaster risk reduction, business risk assessments and business continuity planning; Small workforce, and limited market

## Importance for the economy

- MSMEs account for 99% of all business and over 60% of employment.
- MSMEs contribute 35% of GDP and 25% of the country's total exports revenue.
- It is also estimated that 60% of all exporters in the country belong to the MSME category. MSMEs are able to contribute in exports through subcontracting arrangement with large firms, or as suppliers to exporting companies.

## By sector

- Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles: 461,765 establishments or 46.25% of MSMEs
- Accommodation and Food Service Activities: 144,535 establishments or 14.48% of MSMEs
- There are over 1 million Sari-Sari stores in the Philippines with market value: USD 10 billion = PHP 500 billion. It accounts for roughly 70% of all sales of manufactured goods across the Philippines. 94% of the population shop in these stores per month



## **MULTI-RISK (PROPERTY) INSURANCE:**

Businesses can protect their operations against a variety of risks relevant in the context of climate change, including insurance products against fire and property damage, windstorm and other natural perils and business interruption. Multi-risk property insurance typically covers a range of

## **BUSINESS INTERRUPTION INSURANCE:**

Business interruption insurance safeguards income losses resulting from the disruption of business activities. In this case, the risk protected against is not related to the loss of physical assets but to the potential loss of assets due to business disruption. For example, while properties (fixed asset) are being repaired or inventory is re-stocked (non-fixed asset) and business operations can only be

## **CREDIT-LINKED INSURANCE**

Credit-linked insurance can protect both the lender and the borrower against a risk of default. In this case, the insurance contract could be designed to protect the lender (typically a bank) against climate-related income losses of its client. The policy would be taken out by the financial institution and ideally work to improve the risk-profile of the borrower. Though it is usually the case that credit-linked insurance increases the cost of borrowing, it can allow for credit access for more risky clients.

## **PERSONALIZED INSURANCE FOR MICRO-ENTREPRENEURS**

Bundled personal insurance: Combined with further coverage, e.g. funeral, injury, fire and specific perils, insurance products which cover both, personal as well as asset-related risks might be a means to target especially micro-entrepreneurs.

## MSME Characteristics

- Typically, less organized and less consistent (i.e. no use of standardized procedures, such as accounting, systematic bookkeeping, and production of business plans, detailing operations, products, employees and marketing processes)
- Low awareness of climate-related business risks and entrepreneurial risk management techniques (such as business continuity planning)
- Low levels of financial literacy, potentially substantiating misunderstandings in terms of product coverage and eroding trust in insurance
- Differing economic cycles
- Large share of micro and small businesses are unregistered and/or have a lack of business licenses
- Lack of financial resources and access to finance to invest in productivity and risk reduction measures (to increase their insurability and bring down premium costs), so insurance remains unaffordable
- Willingness and ability to pay for insurance quite low

## Market characteristics

- Archipelago consists of over 7000 islands, making comprehensive product distribution difficult
- Prohibitively high costs for mobile telecommunication (and payment) services

## **Regulation and policy frameworks**

- Limited policy information on index-based/parametric insurance and lack of regulation
- Constraints to affordability due to VAT applied to insurance purchase: General taxation for the non-life insurance sector is among the highest in ASEAN at approximately 26.5%
- Sufficient legislative provisions and policies crafted to support MSME resilience (e.g. NDRRMP, NCCAP, MSMEDP), but gap in execution with view to translation in sub-national action plans
- MSME's are neglected in regulation as it falls between household (consumer protection) and corporations

## **Distinct risk profiles and high transaction costs**

- Specific product requirements: micro-enterprises similar but not congruent with households, SMEs falling in the missing middle - Only few providers offer (micro) insurance products against disasters, even fewer for MSMEs;
- Disaster risk insurance in the Philippines perceived as high-risk product, not only but particularly with view to the agricultural sector (average of 20 typhoons per year); unprofitable
- Insurers' lack of access to data and information on MSMEs as a client base; in addition to having to price potentially unknown climate risks (lack of pricing strategy data)
- Few existing providers with experience in index-based insurance solutions and lack of in-house capacity