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**Research Report**

## Pro-poor climate risk insurance: the role of community-based organisations (CBOs)

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## Pro-Poor Climate Risk Insurance – The Role of Community-Based Organisations (CBOs)

### Summary

In the face of increasingly frequent extreme weather events, the need to manage climate risk becomes more urgent, especially for the most vulnerable countries and communities. With the aim of reducing vulnerability, climate risk transfer in the form of climate risk insurance (CRI) has been gaining attention in climate policy discussions. When properly designed, CRI acts as a safety net against climate change impacts by providing financial support after an extreme weather event. Two main types of insurance enable payouts: indemnity (traditional) insurance or predefined parameters (index-based) insurance. Individuals, groups, or even governments may take out policies with either type of insurance and receive payouts directly (insurer to beneficiary payout) or indirectly (insurer to aggregator to beneficiary payout). Direct insurance is usually implemented at the micro-level with individual policyholders. Indirect insurance is usually implemented through group contracts at the meso-level through risk aggregators and at the macro-level through the state.

While promising, risk transfer in the form of CRI also has its share of challenges. Within the United Nations Framework Convention on Climate Change, the lack of accessibility and affordability of CRI for poor and vulnerable groups have been identified as barriers to uptake. In light of climate justice, asking the poor and climate-vulnerable groups - most of whom do not contribute substantially to anthropogenic climate change - to solely carry the financial burden of risk transfer is anything but just. Employing a human rights-based approach to CRI may ensure that the resilience

of poor and climate-vulnerable groups is enhanced in a climate-just manner.

Indigenous peoples are some of the poorest and most climate vulnerable groups. Often marginalised, they rarely have access to social protection. The strong communal relationship of indigenous peoples facilitates their participation in community-based organisations (CBOs). CBOs are a suitable vehicle for meso-insurance, in which risk is aggregated and an insurance policy belongs to a group. In this way, CBOs can facilitate service provision that would otherwise be beyond the reach of individuals.

Conclusions of this briefing paper draw on a conceptual analysis of meso-insurance and the results of field research conducted in March 2018 with indigenous Palaw'ans in the Philippines. We find that CRI needs to be attuned to the differential vulnerabilities and capacities of its beneficiaries. This is particularly true for poor and vulnerable people, for whom issues of accessibility and affordability need to be managed, and human rights and pro-poor approaches need to be ensured. In this context, meso-insurance is a promising approach when it provides accessibility and affordability and promotes a pro-poor and human rights-based approach of risk transfer by:

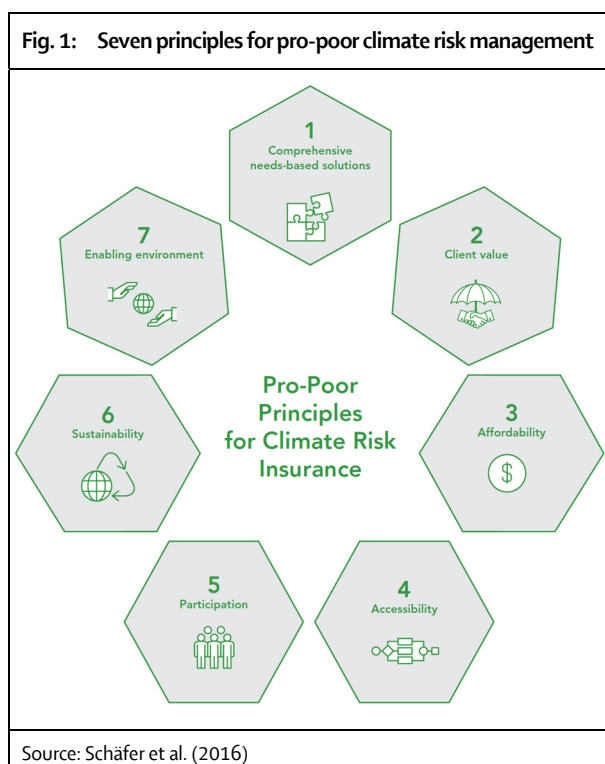
- Properly identifying and involving target beneficiaries and duty-bearers by employing pro-poor and human rights principles.
- Employing measures to improve the financial literacy of target beneficiaries.
- Designing insurance models from the bottom up.

### The need for a pro-poor climate risk transfer and the role of a human rights-based approach

Climate change exacerbates poverty. The poor, who are currently categorised by the World Bank as those living on less than USD 1.90 per day, are usually more vulnerable to climate-induced extreme weather events. The poor are hit harder by the impacts of climate change due to their lower adaptive capacity given their lack of access to formal social protection and schemes that aim to reduce poverty and vulnerability to social risks. The impacts of extreme weather events and their increased frequency and severity due to climate change pose a threat to basic human rights, including the right to life, water, food, shelter, health, subsistence and social protection. These rights can be impaired either directly, for example, through physical damage, or indirectly via forced displacement. Disasters usually aggravate pre-existing vulnerabilities and patterns of discrimination (Waters, 2018). In order to be mindful of the poorest and most vulnerable populations, the call has been made for a pro-poor and human rights-based approach to climate risk insurance (CRI) (see Schäfer et al., 2016).

The Munich Climate Insurance Initiative (MCII) has formulated seven pro-poor principles for CRI. These guiding principles, shown in Figure 1, aim to ensure that insurance schemes are designed and implemented in a manner that “does no harm” and “leaves no one behind”. However, the exact embodiment of a human rights-based approach to CRI remains vague.

Firstly, fostering human rights should be an *end goal* of CRI. Secondly, it should be guaranteed that the *process* of setting-up a CRI scheme respect and foster human rights.



The process itself should be in line with human rights standards, meaning that the most vulnerable need to be identified, involved through active participation, and given access to complaint mechanisms. CRI schemes can contribute to both dimensions, that is, the end goal and the process. They are intended to enhance the sustainable resilience of those facing climate-related risks. Improving resilience through premium outlay (e.g., financial or agricultural, like seed provision) can help those affected by disasters to refrain from other “coping strategies that would further endanger their rights, [for example,] consumption smoothing” (Schäfer et al., 2016). By holding an insurance policy, dependence on charity would be replaced with an enforceable claim, which could contribute to the empowerment of marginalised groups and the fulfilment of human rights.

A first step to any human rights-based approach is the identification of rights holders and their corresponding entitlements, as well as duty bearers and their corresponding obligations. Rights holders, in this case, are those affected by the impacts of extreme weather events. Duty bearers are first and foremost national states that are required to protect their citizens. However, if national states are incapable, responsibility should - in line with the “common but differentiated responsibilities and respective capabilities” (CBDR) principle and the “polluter pays principle” - shift to those who contributed to the anthropogenic climate change. This means that big emitters, like companies or states, should bear the costs. In the case of CRI this could mean providing premiums as well as financial and technical support to set up schemes.

However, positive outcomes will only be achieved if the process itself respects basic human rights principles. Any scheme should be designed to strengthen the capacities of rights holders. Hence, the participation and ownership of insurance beneficiaries must be guaranteed from the very beginning, rather than simply including them in the implementation process. Crucial are also empowerment measures, such as capacitating financial literacy and ensuring equal decision-making. Furthermore, the process should be transparent and non-discriminatory; it should incorporate a complaint mechanism, compliance mechanisms and procedures, and transparent financial structures to thwart corruption.

Lastly, it is important to respect endemic socioeconomic structures and resilience strategies. In the absence of insurance, farmers traditionally have developed several community-based coping mechanisms to deal with weather-related risks, such as risk sharing arrangements (Fuchs & Wolff, 2011). Rather than weakening traditional climate risk management approaches, insurance solutions should be carefully integrated into them. If not designed and implemented carefully, CRI may cause more harm than good. For instance, if the poorest and most vulnerable people do not have access to insurance due to high premium costs, existing social inequalities will be exacerbated (e.g., impacts on gender).

### The advantages of meso-insurance in promoting pro-poor risk transfer

Despite having gained much attention in recent years, CRI uptake in the developing world is still low. However, meso-insurance looks promising for increasing CRI uptake. Typically seen as group contracts, meso-insurance makes use of risk aggregation. Its policyholders are intermediaries, such as community-based organisations (CBOs); value chain actors, such as agribusiness companies; or monetary financial institutions (MFIs). Payouts are made to these risk aggregators, which then distribute the benefits to individuals.

Meso-insurance schemes are well-suited to address climate risk among vulnerable groups that have strong communal relationships. CBOs are member-based and have the ultimate objective of empowering individual members and improving their livelihoods through collective action (i.e., production, saving, credit and marketing). If properly used, CBOs are an ideal vehicle with which to articulate the pro-poor principles mentioned above and increase the value of insurance by building up resilience. This can be attained by:

1. Reducing transaction costs and facilitating distribution (corresponds with Principles 3, 4 and 5):
  - Target group: Insurers can tailor their products and messages to the needs of specific groups offering a critical mass for outreach.
  - Social capital: CBO leaders can codify messages in ways that are more effective for disseminating insurance knowledge.
  - Ease on payment of premiums: CBOs can facilitate the adjustment of premium payments to the timing of members' cash flows.
2. Embedding insurance provision into the catalogue of services offered by CBOs (corresponds with Principles 1, 2, 4 and 6):
  - Complement to other risk management strategies: CBOs are usually used to pool individual risks, such as funeral costs. In many instances agricultural extension is delivered through CBOs. Insurance can effectively complement these forms of risk pooling and risk preparedness by mitigating residual risks and transferring these to capital markets.
  - Linkages to other markets: Insurance can act as a catalyst to deepen the relationship of CBOs and input dealers or middlemen. Similarly, MFIs prefer to engage with CBOs and may consider insurance as a form of collateral that improves credit access.
  - Financial literacy: The use of financial instruments at the CBO level can foster the development of financial skills for group members, if scheme partners and group leaders craft protocols that ensure the transparency of processes.

3. Reducing basis risk (mismatch between benefits from actual losses and contract-stipulated benefits) by better targeting payouts (corresponds with Principles 2 and 6): CBOs can determine the losses experienced by members with more accuracy, thus enhancing the effectiveness and fairness of payouts.
4. Involving CBOs in disaster risk management (corresponds with Principles 1, 2, 5 and 6): Traditionally CBO members pool their labour to minimise market costs, as well as engage in communal works for risk prevention or post-disaster relief. Payouts can provide timely liquidity in the aftermath of climate shocks in order to facilitate reconstruction works.

To sum up, CBOs possess attributes that facilitate the provision of certain services and enhance market access, which would otherwise be beyond individuals' reach. In this context, climate insurance can potentially generate a double gain. Firstly, by acting as a collateral and improving the delivery of multiple services at the group level, which in turn can enhance the resilience of members. Secondly, by providing a safety net that protects CBOs against climate risks that can easily disrupt their functionality, thus improving the sustainability of these groups.

### Indigenous Palaw'ans after tropical storm Bolaven: Climate frontliners that can benefit from meso-insurance

Indigenous Palaw'ans are an example of a vulnerable group that could benefit from group-based meso-insurance schemes when coping with extreme weather events. This became clear in 2018, when tropical storm Bolaven hit the island of Palawan and destroyed several livelihood sources (e.g., fruit-bearing trees). Business disruption is a consequence of extreme weather events; a meso-insurance scheme may be able to protect the community's livelihood diversification activities. The Palaw'ans have a strong communal relationship and are organised into a CBO called SPABP (*Samahang Palawano ng Amas, Brooke's Point*) that coordinates the community's forestry enterprises, such as resin tapping from almaciga trees (*Agathis philippinensis*). In light of the advantages discussed in the previous section, this CBO could play a key role in setting up an effective meso-insurance scheme.

The field research sought to gauge the Palaw'ans' awareness of insurance and willingness to pay. Since they live in the uplands, where there are no paddy farms (which are often the target of crop insurance), the Palaw'ans were unfamiliar with insurance. When asked whether they would be interested in insurance, the Palaw'an representatives said they were willing to learn more about it. Indigenous peoples living in the highlands have a different risk profile from lowland farmers, who are usually the target of crop insurance schemes. A comprehensive needs-based solution (Principle 1) would accurately assess indigenous needs and climate risks and identify complementary risk management



strategies. The communal nature of the indigenous Palaw'ans has enabled the establishment of their people's organisation, which could increase accessibility (Principle 4). Lastly, bottom-up consultations, such as field visits, would operationalise Principle 5 by increasing the participation of vulnerable groups in the design and implementation of CRI.

### Way forward

Insurance provides a unique opportunity to address climate risks in poor and vulnerable communities. However, for CRI to serve its purpose of protecting the poor and vulnerable from impacts of extreme weather events, its design needs to be attuned to the differential vulnerabilities and capacities of its beneficiaries. Meso-insurance with a strong community focus that follows a pro-poor and human rights-based approach is a promising way to do so. Specifically, we emphasise the following objectives and recommend them as important departure points for insurance design and policy-making:

*Properly identify insurance beneficiaries and duty-bearers:* Climate vulnerable communities with limited financial capabilities should be prioritised by employing the pro-poor

principles. In line with the CBDR and "polluter pays" principles, big emitters should carry the financial and technical burden of CRI if national states are unable to do so.

*Increase financial literacy of target beneficiaries:* Capacitating the financial literacy of target beneficiaries empowers them and leads to increased transparency and vigilance against financial mishandling and corruption. An improved understanding of insurance as risk transfer may increase uptake.

*Ensure bottom-up design of insurance:* Target beneficiaries should be involved from the very beginning of insurance design. This allows the design to be tailored to the needs and capacities of the beneficiaries, increasing the specificity of the insurance product. This also allows beneficiaries to identify a trusted aggregator.

The relative flexibility and broader reach of meso-insurance's group contracts compared with micro-insurance's individual contracts have the potential to tackle the challenge of accessibility and affordability of CRI for poor and vulnerable groups, especially if undertaken using a rights-based approach. As climate change impacts worsen, urgent action is needed, and the resilience of poor and vulnerable groups must be strengthened in a climate-just manner.

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