

# South East Europe and Caucasus Catastrophe Reinsurance Facility



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## Background information

- The World Bank – UNISDR South Eastern Europe Disaster Risk Mitigation and Adaptation Programme (SEEDRMAP) and Central Asia and Caucasus Disaster Risk Mitigation and Adaptation Initiative (CAC DRMI) assessed the need of financial tools for promoting disaster risk transfer options in SEE and CAC countries.
- The reviews highlighted that the access to insurance for homeowners and Small Medium Enterprises (SMEs) in SEE and Caucasus is key to reduce the fiscal impact of disasters on countries' fiscal positions.
- Promotion of insurance and reinsurance products in SEE was included in the the European Commission regional programs and received financial support from the World Bank and the Swiss Government.

## Sources of Funding

- The World Bank (US\$35 million)
- The Swiss Government (US\$4.5 million)
- The European Commission (??)
- Global Environmental Facility – US\$8.5 million (under submission)
- UNISDR – through technical cooperation



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## Advantage for Regional Approach

- Diversification of Risks
- Reduction in Premium Costs
- Sharing experience among the various countries
- Support from International organizations and secure a larger amount of funds from Trust Funds





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## What is the current state of catastrophe insurance market in SEEC countries?



- Catastrophe insurance in SEEC countries is nascent – around 0.5-3 % of houses, SMEs and farmers are covered against geo-hazards and weather related perils.
- The existing insurance coverage often lacks the sufficient claims paying capacity to ensure payment of claims in case of a major catastrophic event.
- Companies have little incentive to develop this line of business due to severe underpricing of risk, the lack of risk management tools (accumulation control systems, risk models, etc.) and qualified staff.
- Reinsurance is difficult to obtain for small portfolios of risk with little premium.



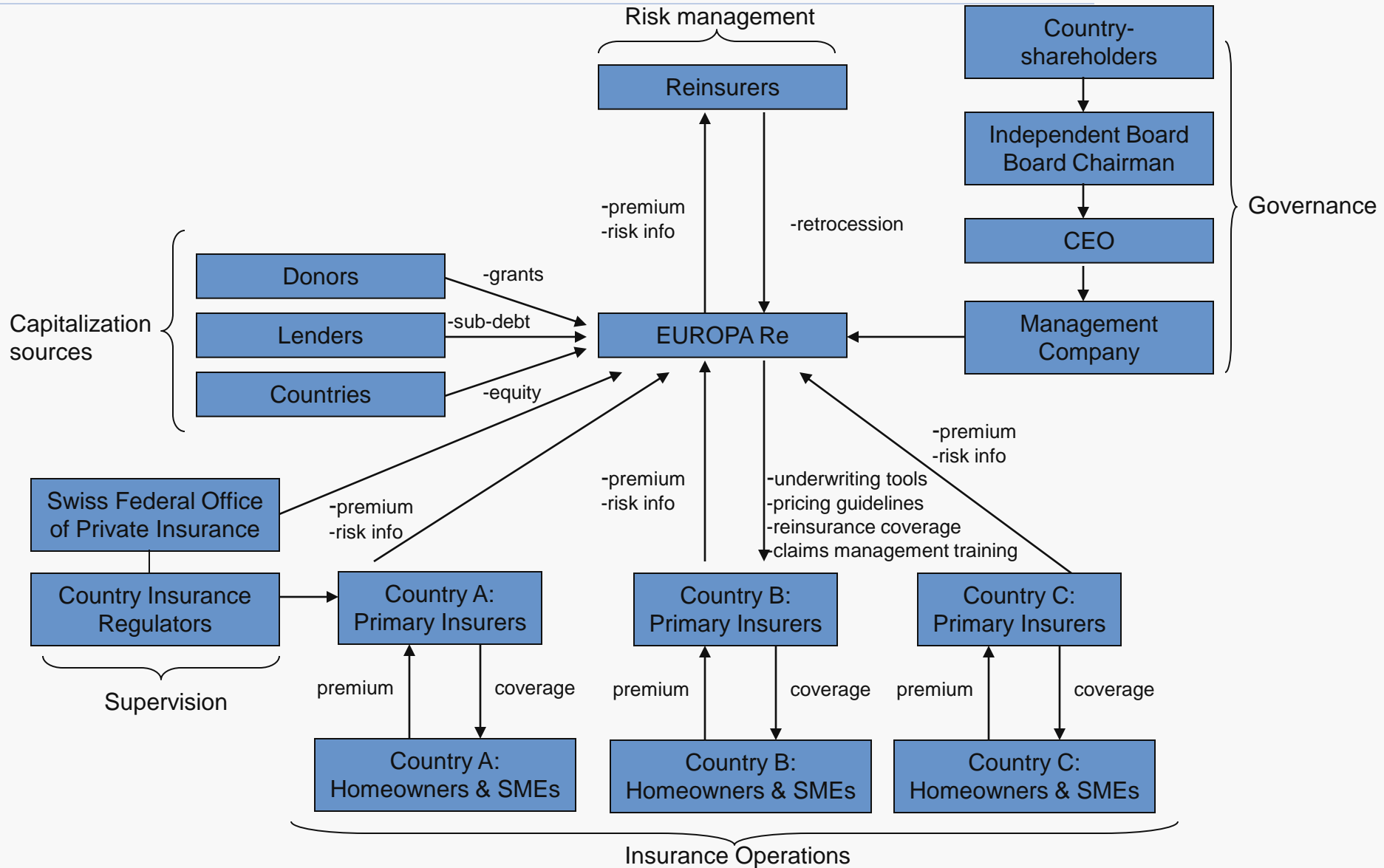
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## Main features of Europa Re

- What is Europa Re?
  - Non-profit catastrophe reinsurance company owned by SEEC countries whose sole objective is to increase the level of catastrophe insurance coverage among government agencies, homeowners, farmers, SMEs and any businesses exposed to weather risk and geo-hazards in member states.
- What perils will it cover?
  - Weather related perils (Flood, Drought, Freeze, and Hail) and Geo-hazards (Earthquake and fire following)
- Why would governments invest in a reinsurance company?
  - To facilitate demand for private catastrophe insurance through proactive demand-boosting policies and reducing their own fiscal risk exposures to disaster risk.

# Europa RE at glance:





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## Professional operational management

- Europa RE will be managed by an independent insurance services company (Management Company) with dedicated full time and highly experienced technical staff.
- Management company will be selected through a global tender on the basis of:
  - technical qualifications of proposed management team;
  - IT capabilities
  - cost
- To ensure the quality of Europa Re operations, compensation of Management Company will be linked to the operational performance of the company.
- The company will adopt the state of the art risk management systems.





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## Good governance



- Good governance is crucial to the success of EUROPA RE.
- The company will have a clear separation of business operations from the government ownership of the facility.
- EUROPA Re will have an independent professional Board of Directors consisting of reputable insurance/reinsurance professionals with well established track record in the industry.
- Overall strategic oversight and policy decisions will remain with country shareholders which will be developed and exercised through Annual Meetings of Shareholders and Advisory Policy Board.



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## Sound regulatory framework



- EUROPA RE will be domiciled in Switzerland – the country with one of the most advanced and sound regulatory regimes in the world.
- Besides minimum capital requirements required under Solvency I, as of 2011 the company will have to comply with risk-based solvency requirements prescribed by Swiss Solvency Test – which results in an almost 10 fold increase in the amount of solvency capital required for a catastrophe reinsurer compared to Solvency I.



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## What countries are expected to join Europa Re?

- So far the following IDA, IDA/IBRD blend countries are expected to become (or already became) shareholders in Europa RE:
  - Albania
  - Bosnia and Herzegovina
  - Georgia
  - Macedonia
  - Serbia



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## What are the benefits for Europa Re country shareholders?

- Membership in Europa Re will reduce the country's own fiscal risk exposure to natural disasters through:
  - Expanded private insurance coverage of homeowners, SMEs and farmers
  - Coverage of government own assets
  - Potential insurance coverage of government own social obligations to socially vulnerable segments of population exposed to natural disasters
- Participation in the program will jump-start the development of local catastrophe and weather risk insurance market through the creation of country specific risk models, regulations, pricing and actuarial guidelines, and new products – all to be funded by international donors.
- The program will result in reducing systemic risk for the financial sector, particularly in EQ prone countries, as banks' collateral and solvency of insurance companies will be protected.



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## What is the exit strategy for government shareholders?

- Government shareholders will be able to sell up to 30% of their shares in 3 years from the commencement of Europa Re operations and up to 100% within 5 years to Europa Re or private investors.
- Upon exit government shareholders will receive at least the full amount of their principal equity contribution plus accrued interest (equivalent to a yield on a 5-year Treasury bond plus IBRD spread).





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## Regulatory and policy actions expected from member states

- The success of Europa Re will depend on countries' success to:
  - create the enabling regulatory and legal framework for the operations of the program;
  - carry out extensive public information and awareness campaigns about the availability and benefits of catastrophe insurance products;
  - Insure at least a part of government assets exposed to disaster risk – government buildings, life-line facilities (schools and hospitals)
  - Carry out policies that will encourage sound disaster risk management practices by homeowners and companies, e.g.:
    - linking mortgages in disaster prone areas to catastrophe insurance
    - limiting post-disaster aid to a defined amount or a fraction of insured limit
  - actively participate in program's governance through shareholders meetings and participation on policy advisory board.



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## How can the countries finance their equity contributions to Europa Re?



- A country's contribution to the facility is set at a flat rate of \$5 mm.
- IDA eligible countries can borrow from the WB regional IDA facility on IDA terms to finance their equity contributions.
- The regional IDA contributions will match the countries' own IDA allocations at a 2:1 ratio – i.e., if a country puts in \$1.66 of its own IDA contribution the World Bank regional facility will match it with \$3.33 mm of regional IDA.
- The availability of regional IDA expires in the summer of 2011.
- Countries not eligible for IDA can borrow on IBRD terms.



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## Traditional catastrophe insurance products to be supported by Europa Re



- Traditional catastrophe insurance products will be supported through the development of risk models and pricing and underwriting guidelines, as well as regulatory reform.
- Hail insurance – coverage against damage to crops in case of hail.
- Earthquake insurance – coverage against damage to property and contents in case of an earthquake.
- All insurance products will be sold through local insurers, which will also settle claims.





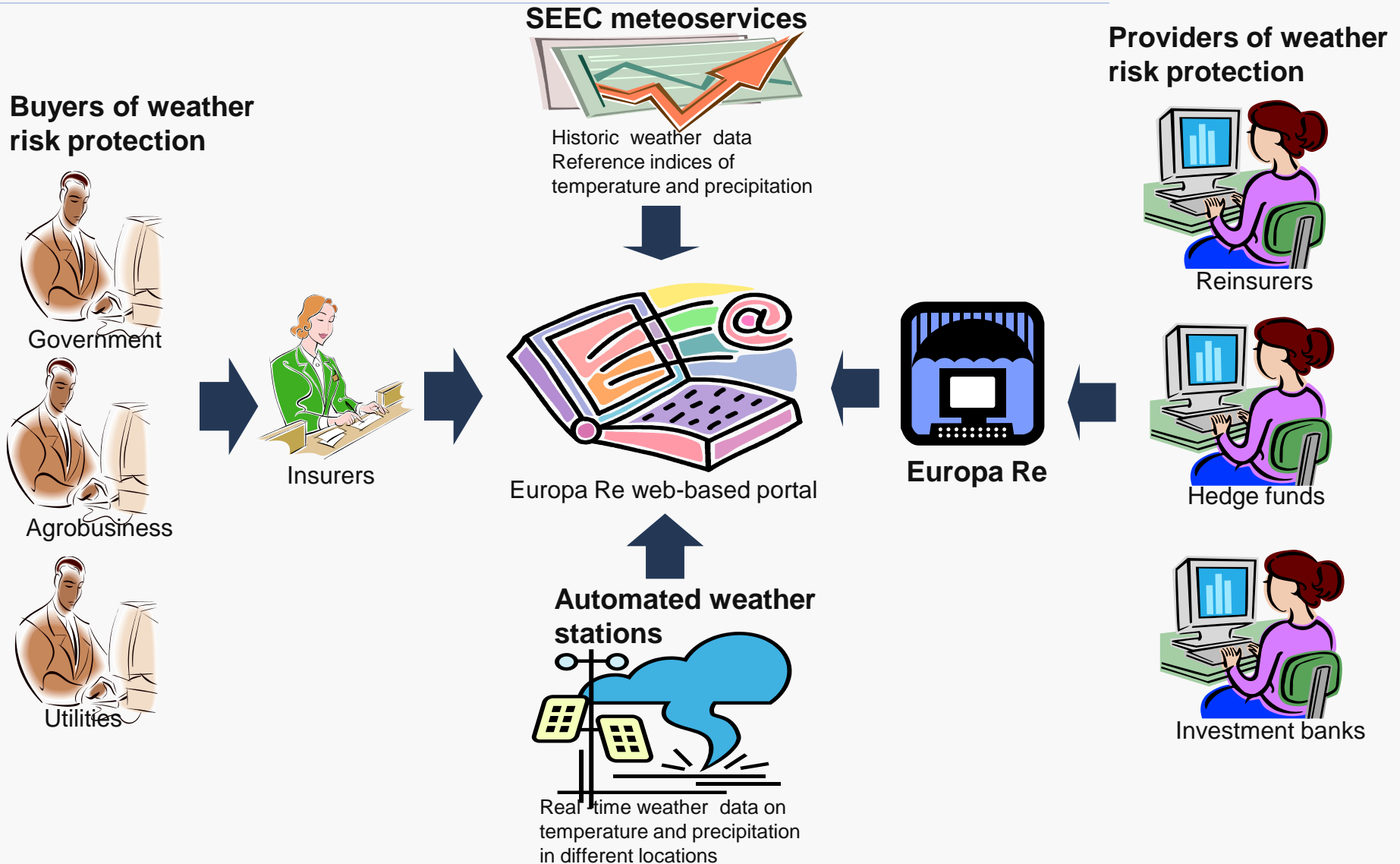
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## Key features of weather insurance products by Europa Re

- Weather risk insurance products supported by Europa Re will enable agro-producers (growers, packers, exporters, etc.) and weather sensitive enterprises (hydropower stations, utilities, airports) to reduce financial losses due to damaging weather conditions.
- Governments will also be able to cover their own social safety net obligations to farmers by obtaining parametric weather insurance contracts from the program.
- Coverage pays out based solely on weather measurements and is not contractually related to insured's losses. However contract customization can ensure a tight correlation between the two.
- No claims process or proof-of-loss is required. Payout is automatic if an adverse weather event specified in the insurance contract takes place.

# Insuring weather risk in SEEC countries





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## Examples of parametric weather risk insurance products offered by Europa Re

- **Drought protection** – provides financial compensation in case the minimum level of rainfall during a certain period does not occur.
- **Freeze Protection** – allows to protect agro-businesses from freeze-related losses. The contract pays out if the temperatures drop below the historic average to such a degree that it causes financial losses to businesses and government.
- **Heat Stress Protection** – protects against surges in temperatures during a growing season compared to a historic average.
- **Storm Flood Protection** - pays out each time rainfall exceeds the chosen threshold over a specific number of days.
- **Snowfall Protection** – pays out in case the level of snow accumulation during the winter is above or below historic average.



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## Potential clients for weather risk insurance products

- **Ministries of Agriculture** – insuring their own social safety net obligations to farmers in cases of extreme weather events.
- **Hydropower stations** – insuring loss of power output (and revenue) in cases of drought (i.e. lower than average precipitation).
- **Power stations** – insuring loss of revenue in cases of warm winters (due to reduced demand for heating) and cold summers (due to reduced demand for cooling).
- **Resorts** – insuring against loss of revenue due to lost days (due to adverse weather conditions) during a tourist season
- **Agro-businesses** – insuring against loss of revenue due to extreme weather events that affect crop yields.



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## Status of Europa Re

- Albania, Serbia and Macedonia already secured funding from the WB loan for their equity contributions.
- Negotiations with Georgia, B&H and Montenegro are expected in the coming two months.
- Countries sign the Shareholders Agreements with Europa Re.
- Countries disburse their equity contributions to Europa Re by early 2011 and receive share certificates.
- Europa Re starts the technical preparatory work in member countries in the late 2010 - early 2011.
- Europa Re launches its operations in the fall of 2011 thus making a range of innovative catastrophe insurance products available in SEEC member countries.



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