

Scaling up insurance as a disaster resilience strategy for smallholder farmers in Latin America

11th Consultative Forum on microinsurance regulation for insurance supervisory authorities, insurance practitioners and policymakers

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The objective of the 11th Consultative Forum was to foster sound policymaking for the development and scaling up of agricultural insurance across the region. The Forum was the last of a three-event series organised in 2017 on the topic of agricultural insurance as a tool for disaster resilience in the three developing regions of Asia, Africa and Latin America. The first event of the series, which took place in Singapore, in March, covered indemnity and index-based agricultural insurance. The second one took place in Uganda, in May, and focused on index-based insurance as an innovative tool fostering affordability for smallholder farmers.

In Latin America, 20% of the population lives in rural areas and the agriculture sector represents 5.3% of the Gross Domestic Product (GDP). Agricultural insurance, mostly offered as indemnity-based insurance in Latin America, has a penetration rate of only 0.03% of the GDP across the entire region compared to over 0.06% for North America. According to the International Fund for Agricultural Development (IFAD), there are approximately 15 million family farms in Latin America, controlling about 400 million hectares of which 10 million farms are subsistence farms and the rest are intermediate and large groups with different degrees of integration within the markets. Agricultural producers in Latin America are particularly vulnerable to natural catastrophes, which vary widely in type, frequency and severity across the region and even within countries. Drought, frost and floods, on which abnormally warm (El Niño) and abnormally cool (La Niña) sea surface temperatures have a large impact, cause devastating agricultural losses.

Agricultural insurance is key to sustainability and food supply. Agricultural development plays a vital role in poverty reduction and economic growth, particularly in developing countries. It contributes to the nutrition and food security of the population while generating employment and income for all those directly and indirectly involved in the chain of production and distribution of agricultural products. It also contributes to the countries' GDP, and global supply of food and other consumer goods. In developing countries where insurance penetration rates are still very low, scaled agricultural insurance contributes to the faster recovery of economies when a catastrophic event takes place. All considered, scaled agricultural insurance is a key tool in the promotion of agricultural and rural development, contributing to broader development goals and a disaster resilience strategy.

A holistic approach is essential for achieving scale. All stakeholders, including the government, must participate in the scaling of agricultural insurance. In particular, governments' role needs to extend beyond mere payment of premium subsidies. The roles of the different actors involved in the provision of agricultural insurance need to be well defined and understood by all. Coordination among stakeholders is essential for addressing the challenges of the industry (mainly operational related to design and delivery) and the supervisors (regulatory challenges). It is important to note, however, that the value chain in agricultural insurance goes beyond governments, supervisors/regulators and industry to include donors and investors, technical

"To achieve scale, agricultural insurance needs to be part of a holistic approach for agricultural development with basic services in place such as access to inputs, access to data and access to delivery channels in addition to a strong collaboration between insurers, farmers and governments."

Francesco Rispoli,
IFAD, Italy

"Political commitment is needed from the Government to adopt national policies that incorporate risk transfer systems and public-private partnerships, in order to encourage a greater insurance supply."

Carla Chiappe,
Superintendencia de Banca, Seguros y AFP (SBS), Peru

assistance and data providers, beneficiaries, aggregators and transactional platforms, reinsurers and others which can still be identified.

Technology, financial literacy and training need to be factored in for overcoming challenges. In trying to meet the promises of agricultural insurance, considering the stakeholders' objectives and challenges, the following stand out: i) the use of technology - including the use of satellites and scientific agencies, both for product development and for the agility of claims payments; ii) the role of supervisors, industry and aggregators in the development of awareness, education and customers' understanding of agricultural insurance; and iii) the need for training of those involved in the processes, including the sales force.

An integrated approach is essential when preparing and evaluating proposals for agricultural insurance products. There are essential technical issues that must be well understood by the insurer for the success of an agricultural insurance product, such as, understanding the needs of the insured, knowing the data and testing the product and verifying its viability. Nevertheless, some aspects require involvement of other stakeholders in the process of development and design. Depending on the focus and complexity of the agricultural insurance product, these aspects could include: i) selection of adequate and existing distribution channels; ii) attention to the costs of implementation; iii) care with reputational risk; iv) reinsurers' participation in all stages of the process; and v) the involvement of supervisors who understand the products so that they can protect consumers. In this context, the need for clarity and transparency among all partners is crucial to the success of the product.

Agricultural insurance development requires partnership as it is a much more complex product than those of other branches and insurers do not have the necessary expertise to develop it through their own means. In the case of Latin America, reaching the appropriate scale for the provision of agricultural insurance is still more challenging when compared to other regions, as there are fewer farmers than in Asia, for example. To achieve intended results, insurers need to establish partnerships on many levels. These include collaborating with data providers to obtain information about the severity levels of climate-related events across the country. In the case of an index-based agricultural insurance product, support from different entities, such as the supervisor, is essential to ensure that the product is acceptable and understandable. Still, cooperation between partners should go beyond launching a product and should extend to identifying the social impact of marketing to consumers. The importance of involving all stakeholders is necessary from the beginning, to build trust based on ongoing dialogue and commitment.

Lack or inaccurate data creates insecurity. Quality, availability and accessibility of data is a significant challenge for index-based agriculture insurance, since its absence or inaccuracy creates uncertainty for stakeholders, especially for insurance supervisors and reinsurers. Given their complexity, index-based agriculture insurance products are generally not well accepted by supervisors/regulators, on the one hand because they have no experience with them, on the other because of their concern for consumer protection. Similarly, though in principle, reinsurers want to be involved in this market, they are often not comfortable with the risks, and this affects prices.

“How can different stakeholders with their specific objectives and mandates, come together to provide a sustainable value proposition to farmers?”

Pranav Prashad,
*ILO's Impact
Insurance Facility,
Switzerland*

“Many small farmers do not see climate risk as their main risk. Often they prefer climate risk to be integrated into a more comprehensive product covering several risks.”

Erik Geurts,
BlueOrchard, Peru

Examples of practical implementation in the region in Peru and Guatemala

Catastrophic and commercial insurance products for agriculture are developing and growing in Peru, where the essential factors of success include a strong commitment by the State, public-private cooperation, stakeholders' knowledge of the sector, promotion of accessible insurance products and constant monitoring. Catastrophic agricultural insurance is a 100% subsidised insurance coverage, aimed at subsistence farmers, launched by the Ministry of Agriculture who, through a bidding process, determines which crops are to be covered and the corresponding rates. The role of the insurance supervisors within this process is limited to product approval, ensuring that products are in line with the conditions set up by the Ministry, including the determination of loss and the adjuster determining whether the yield has gone down to the trigger levels. The process for approval of commercial agricultural insurance products is similar, but dependent on private initiatives and aimed at clients of financial institutions. Conditions have to be clearly stated in the policy so that customers are able to understand the product.

In Guatemala, from the supervisory perspective, the registration of index-based products is part of the national strategy for financial inclusion. The primary focus of this strategy is quality and well-being of the clients and integration with other financial services. As a result of this comprehensive policy, an index-based catastrophe insurance product was launched. This product is linked to a financial institution and covers micro-loans against catastrophic events, such as earthquakes, drought and rainfall, when client activities are interrupted. A collaborative relationship with the regulator resulted in full support in obtaining product design approval for which the premiums were calculated as a fixed percentage of the loan amount, including taxes and specifying thresholds for each event. The Guatemalan example includes a number of other success factors, such as, the training of sales force, the training of business agents for follow-up, the possession of adequate training and follow-up materials, and ensuring that clients understand the products. The partnership with the financial institution ensured clients' loyalty in the payment of premiums and support in the quick settlement of claims payments.

A number of key factors of success to scaling up agricultural insurance were identified and emphasised during the Consultative Forum in Peru. On their basis, we draw the following recommendations:

Key takeaways and recommendations for action to the industry:

- Engage early on with governmental entities and the supervisory authorities when developing an agricultural insurance product, understanding the regulatory framework in place;
- Identify risk transfer needs of the target market in order to develop relevant products;
- Get support from reinsurers and good technical assistance providers to design innovative products and foster local capacity building, obtaining an in-depth knowledge of the subject;
- Properly use technology and data, and maintain the data infrastructure systems;

“Agricultural insurance is an effective resource, in order to stabilize the vulnerable classes in light of the nature effects and to counteract poverty.”

Enrique Rafael Lucas Estrada,
Superintendencia de Bancos de Guatemala, Guatemala

“Insurance is only part of the puzzle of disaster risk management. Stakeholders must be open and transparent about the expectations and the possibilities.”

Andrea Camargo,
Microinsurance Catastrophe Risk Organisation (MICRO)

- Ensure proper understanding of the product by the client, aggregator and supervisor such as insurable interest, covered perils and other product specifications;
- Engage in financial literacy programmes for the clients to support customer awareness;
- Maintain continued training of the industry sales force;
- Continuously monitor results while evaluating their impact on the clients and the market.

Key takeaways and recommendations for action to the supervisors:

- Keep an open dialogue and lead the process of cooperation between all stakeholders;
- Understand and raise awareness on the importance of index-based agricultural insurance as a tool to overcome production risks and enhance the livelihoods of smallholder farmers;
- Raise awareness with other governmental entities about the role of index-based agricultural insurance to achieve national public policies;
- Encourage public-private partnerships;
- Build internal expertise on agricultural insurance, to obtain an in-depth knowledge of the subject;
- Enable a regulatory framework that provides a proportionate approach for agricultural insurance and that keeps pace with technological developments;
- Promote financial literacy programmes, creating customer awareness;
- Support the appropriate and efficient use of subsidies;
- Maintain ongoing monitoring of results;
- Engage in constant dialogue with other supervisory authorities from other jurisdictions to learn innovative approaches.

A number of these recommendations have also been stressed at the events in Singapore and Uganda. As a conclusion, below is a list of additional key takeaways from these two forums:

For the industry:

- Establish smart public-private partnerships to deliver simple, accessible and affordable products;
- Keep products as close as possible to experience and farmer needs;
- Invest in obtaining high-quality data for index insurance;
- Leverage a full range of technologies to innovate and improve cost-effectiveness of key processes such as claims verification and pay-out and reduce administrative and transaction costs;
- Work with supervisors and policymakers to clarify to them the technical aspects and support needed for agricultural insurance to work.

“Agricultural insurance has evolved considerably since the 1990s. Many partnerships have evolved in that respect. These bring together the public and the private sector and involve NGOs, farmers’ associations and microfinance institutions, all partnering with private insurers.”

Katharine
Pulvermacher,
*Microinsurance
Network*

“Didactic financial education tools are necessary to overcome challenges with customers and to foster an informed and smart decision-making.”

Jose Guillermo Lopez
Cordon, *Aseguradora
Rural, Guatemala*

For the supervisors:

- Understand and raise awareness on the importance of index-based agricultural insurance as a tool to overcome production risks, especially in extreme weather events, and to enhance the livelihoods of smallholder farmers;
- Stay at the forefront of initiatives to develop agricultural and index insurance;
- Engage in dialogue with policymakers and industry on how insurance should be integrated into broader policy frameworks such as disaster risk management;
- Pursue a formal collaboration with other stakeholders based on clear objectives, strategies and outcomes in key areas such as data sharing;
- Continue building internal technical expertise and understanding of index insurance products;
- Continue pursuing strategies to develop farmers' understanding of insurance.

“We hope that the 11th Consultative Forum can inspire new ideas and that the initiatives, the learning and information obtained can be shared and multiplied to obtain responsible solutions. And that all stakeholders in their respective jurisdictions can work together to make insurance markets more inclusive.”

*Regina Simões,
Access to Insurance
Initiative*