

Micro-Insurance for Natural Disasters Concept, Present and Future Outlook

Haresh C. Shah

Obayashi Professor of Engineering, Emeritus Stanford University

Founder and Senior Advisor, Risk Management Solutions, Inc.

Catastrophe risk transfer through insurance and reinsurance has been widely used in developed parts of the world for the past two decades in an orderly fashion. The scientific and technological basis for the quantification of risk over this time has made the available insurance/reinsurance products quite robust as well as universally adapted. Unfortunately, these products are mainly used in developed parts of the world due to the level of catastrophe risk and the premium structure. Thus, **the modern knowledge of quantification and understanding of catastrophe risk has not been of great benefit to many in developing parts of the world.**

It is well known that after each catastrophic event, it is the poor who are impacted the most. Due to extremely low level of risk (in monetary terms) of these poorer sections of any society, the insurance/reinsurance industry has not paid much attention to helping them. Thus, a typical rural farmer who may lose his “hut” and his means of generating income after a disaster is completely devastated since he and millions like him are not covered by any insurance. In countries like India, there is also a lack of purchasing power for poorer people to insure themselves against healthcare risks. **Micro-insurance as a concept and as a potential product is targeted for such people. It is estimated that almost a billion individuals who are at risk due to natural or man-made catastrophe events do not have any risk transfer mechanism.** Because of the size of these potential aggregate losses from such poorer sections of the society, the governments (of developing countries) do not have the resources to help these people.

Micro-insurance may be the means by which such market can be developed and helped. Even though the individual value at risk from rural areas of Asia is low, the aggregate market is immense. This has been noted by major insurance and reinsurance players around the world. The World Bank, the Asian Development Bank, individual countries, and most insurance/reinsurance companies are very much interested in micro-insurance as a concept. Micro-insurance, which is a subset of micro-finance, has been

concentrated on non-catastrophic areas; hence the need to increase concentration on the catastrophic areas.

Some of the issues facing micro-insurance as a viable product for the poorer sections of our societies (bottom of the economic pyramid) are:

1. There is a general lack of awareness of micro-insurance in the community, which requires strong promotion of the concept.
2. Many corporations are either not convinced of the commercial viability of such kind of initiatives or have yet to figure out how to offer products to the “bottom of the pyramid”.
3. Technology would be essential in lowering transaction costs for such schemes and facilitating new ideas such as remittance financing of micro-insurance.
4. For the micro-insurance scheme to be sustainable, the premium must satisfy the market value of risk while being affordable to the poor. Other issues to be considered included premium payment mode and procedures as well as management of claims.

Moving forward, we need to identify the economic and delivery models for bringing micro-insurance as a product to those who need it the most. This will involve understanding and quantifying risk for this section of the society. Collaboration with “social entrepreneurs” will be essential. Development of this concept for a vast majority of rural and often poor of the developing world in general and Asian context in particular is not an option. It has to be achieved. We have the technologies, financial modeling capabilities and interest of the insurers/reinsurers to make this happen. A synergistic work of engineers, risk analysts, insurance experts, social entrepreneurs, governments and NGOs will be necessary to make this a reality. We also need to select a region for implementing a pilot project either in India or in Philippines so that we understand the challenges of implementing this concept.