UNDP Insurance and Risk Finance Facility - Fragile States' Resilience Offer

Introduction and Background

In the current context of rising vulnerability and the compounding impacts of multiple shocks, fragile states emerge as the world's most susceptible countries to risk, hazard and shock.

Characterized by high levels of institutional and social fragility, weak governance structures and lack of resources, or affected by violent conflict, these countries path to sustainable development are paved with many challenges. Recent impacts of the pandemic, multiple wars across the world, the debt crisis, the pandemic and climate change are undermining livelihoods, development and growth at an unprecedented scale in fragile states – for example, the recovery of per capita incomes to 2019 levels is projected to occur only after 2024, indicating a reversal of years of development efforts.

At the same time, insurance and risk finance in emerging markets remains stubbornly underdeveloped and limited, especially in fragile states, with over 95% of risk exposures remaining uninsured, an insurance penetration rate of less than 1% in almost all fragile countries. It is starkly evident that developing countries are particularly vulnerable and ill-equipped to manage and mitigate potential risks effectively, leaving them with little financial resilience. It cannot be surprising the that the United Nations humanitarian appeal for 2023 reached a record US$51.5 billion, which if financed from development assistance, would mean a third of all aid going to keeping people alive, and not to long-term development. This is deeply relevant to fragile states because the bulk of all humanitarian financing is spent in fragile states, and this is the bulk of the financing they receive from aid in general.

From an aid perspective, fragile states receive increasing volumes of aid that is largely only going towards protection and emergency assistance – long-term development aid, and especially aid focused on long-term financial resilience, is largely absent from these countries.

And yet, insurance is an absolute critical tool for the fast-pace of risk and hazard that fragile states experience. Beyond delivering financial protection for families, businesses, countries and the agriculture and public assets on which they depend, insurance and risk finance solutions support fragile countries to better manage shocks and crises in an increasingly risky world.

Scaling up insurance coverage can help catalyze the delivery of the Sustainable Development Goals (SDGs), create a virtuous cycle of economic benefits, unlock adaptation financing and investments, lower the debt burden of countries and individuals in the event of disaster and deliver greater socio-economic livelihoods for vulnerable communities. And insurance and risk financing tools and solutions offer a substantial flexible set of options; they can work with or without governments; finance both crisis more predictably and long-term reconstruction without dependence on the public purse; and deliver both a standard set of solutions (such as parametric insurance for agriculture or public assets) as well as highly specialized financial tools for derisking and financial protection.

In the hopes of preventing humanitarian crises, fostering sustainable development and achieving financial resilience, a global collaborative effort, leveraging both the public and private sector, must be undertaken to ensure long term resilience against risks in these countries, which are home to nearly a billion people.

Yet, for many fragile states, insurance solutions remain out of reach. Mechanisms to mobilize finance rapidly and efficiently for disaster response are often not integrated into budget processes and development frameworks, insurance companies are deterred by restrictive legislation, demand for insurance is also low due to a lack of awareness and/or trust in the insurance sector, and there are also issues related to affordability of premiums. Together, these challenges result in a large protection gap, leaving vulnerable communities exposed to disaster risks and their lives and livelihoods unprotected.

Furthermore, complexity and high levels of risk in fragile states inhibit development. Insurance can be an enabler of complicated operations, required for the advancement of development in a context of a weak sovereign or extreme war risks which deter actors from engagement. UNDP has pioneered approaches which utilize insurance solutions to enable some of the most complex development initiatives (see work in Yemen below). It should also be noted that fragility and conflict does not stop at borders, addressing human mobility sits as a solid pillar of development work within fragility, further exacerbating conflict, development challenges and complexity of interventions to address them.

About UNDP's IRFF

The Insurance and Risk Finance Facility (IRFF) is a flagship initiative housed within UNDP's Sustainable Finance Hub (SFH) and is the first dedicated corporate vehicle for the delivery of insurance and risk finance solutions through UNDP's 140 country offices. The IRFF works in 34 countries across 7 main programmes, with the largest being the Tripartite Agreement between UNDP, the German Government, and the Insurance Development Forum (IDF), representing 20 of the world's largest insurance companies, active in more than 22 countries and financially protecting 64 million beneficiaries. A key element of this agreement is the development of sovereign risk financing and inclusive insurance solutions for climate risks to enhance the financial resilience of vulnerable communities. The IRFF's work covers a range of critical areas where risk transfer and collaboration with the industry can add significantly to delivering on the Sustainable Development Goals (SDGs), and it does so through providing both standard and complex risk transfer and insurance solutions.

Recognizing the pressing need to address the unique vulnerabilities and circumstances of fragile and conflict-affected states and building on groundbreaking initiatives that bring insurance solutions to development challenges of Fragile states, the UNDP's Insurance and Risk Finance Facility (IRFF) has developed this offer. It outlines how UNDP delivers bespoke support programmes that leverage the insurance industry's expertise, UNDP country presence and IRFF's ongoing programmatic work and partnerships ecosystem to enhance the financial resilience of vulnerable communities in fragile and conflict-affected states through the implementation of bespoke and innovative insurance and risk finance solutions.

The Approach

The IRFF approach is to use insurance and risk transfer as tools to enable development in fragile and conflict-affected states through three inter-connected areas of work:

1. **Crisis risk assessment and understanding**
2. **Strengthening the foundation of financial risk management**
3. **Insurance and risk finance product development**

The facility will develop and implement this work through a set of interlocking areas of support to countries risk transfer needs:

Crisis Risk Assessment and Understanding

By working with UNDP country offices, academic partners and key government institutions, the IRFF builds evidence, analysis and advocacy on the key risks and current state of inclusive insurance and risk finance in targeted fragile states to build recommendations on potential solutions that could be developed with industry and frameworks that could be enhanced. The following are the key activities:

- Undertake a diagnostic to assess key disaster risks and vulnerabilities in the country, assess the existing ecosystem for disaster risk financing and insurance and the areas of greatest needs
- Map out the government and non-government stakeholders with capacities on the ground with potential to facilitate the implementation of risk finance and insurance solutions to reach vulnerable communities
- Research and development to provide thought-leadership on insurance and risk financing in fragile and conflict states

- Engage the insurance sector to construct and implement an appropriate insurance and risk finance solution for implementation in select countries

UNDP's IRFF Work on War Risk – Ukraine

In light of the ongoing invasion by Russia, Ukraine's resilient recovery process will require substantial investment in economic modernization and to rebuild of critical infrastructure. According to the World Bank's needs assessment published in February 2023, the country has suffered physical damage of US$ 135 billion after one year, and would require up to US$ 411 billion to rebuild over a 10-year period. The estimated costs of reconstruction have reached staggering heights, potentially surpassing the $1 trillion mark.

In the absence of an intervention, the availability of war and political risk insurance will continue to be limited, fostering a cycle of economic decline. To offer war and political risk insurance in Ukraine, a holistic strategy encompassing diverse stakeholders is essential, with the establishment and operationalization of a public-private risk pool emerging as a pivotal solution. The core objective of the risk pool would be to ensure the accessibility of political and war risk insurance at affordable rates over the long term.

UNDP will be working with key institutions and ministries to secure broader development objectives such as attracting the necessary inward investment to support the resilient rebuild and sustainable recovery, de-risking and enabling the growth and development of the domestic MSMEs, reducing the risk of economic backsliding from war-related events and supporting the development of the Ukrainian insurance market.

Strengthening the Foundations of Financial Risk Management

The fragile states offer provides essential insurance and risk finance solutions through the implementation of a foundational programme to strengthen financial risk management led by the IRFF. This programme is tailored to the specific and unique context of Individual fragile states countries, influenced by factors such as the level of risk, socioeconomic conditions, governmental needs, level of conflict and the desired level of technical assistance required to attain both financial resilience and livelihood development.

To this end, the IRFF has a dedicated programme, the Engagement Initiative, through which It works with LDCs, many of which are also fragile states. Separate to this, the IRFF also provides bespoke solutions to targeted countries, based on demand.

The Engagement Initiative: Long-Term Financial Stability and Resilience

UNDP's Insurance and Risk Finance Facility (IRFF) has identified the weakness of sustainable financial risk management within LDCs, as a critical area to be addressed to help LDCs progress and tackle their climate and development challenges. The IRFF has designed a specific programme, the Engagement Initiative, to work with LDCs to tackle the underlying challenges noted above, by building their capacity to adopt insurance and risk financing solutions, integrating risk transfer into government decision-making, including public financial management, enhancing the regulatory and legislative environment for all aspects of financial risk management, integrating risk transfer into key country frameworks such as countries commitments to the Paris Agreement (the Nationally Determined Contributions) and National Adaptation Plans, and driving long-term engagement between government and the insurance industry.

As a direct response to the Doha Programme of Action and the increasing pressure LDCs are facing, the Engagement Initiative will include four in-country components as well a fifth one aiming at enhancing regional and global lessons learnt and advocacy:

1. **Fostering Demand for Insurance and Risk Financing**
2. **Creating Capacity and Understanding for Insurance and risk finance**
3. **Financial Resilience and Fiscal Stability**
4. **Foundational Development for Insurance and Risk Finance**
5. **South-South Learning, Advocacy and Evidence**

Grounding Crisis Financing in Long-Term Governance and Resilience

Crisis financing enables humanitarian actors to undertake anticipatory and relief actions in the immediate aftermath of a disaster. Organizations such as the World Food Programme (WFP), the START Network and the Red Cross have obtained parametric insurance coverage to ensure predictable financing can be channeled toward anticipatory and relief actions in a timely manner. This is only possible if the right policy and programming structures are in place ahead of time which enable crisis financing to be converted to rapid action.

UNDP is a key development partner to governments, working to strengthen all the above structures which enable humanitarian actors, to work closely with governments and through government systems to enable rapid anticipatory action and emergency relief.

Bespoke Solutions

The IRFF meets countries where they are and works with them to provide solutions to their individual challenges. This work entails the development of foundational elements to support the strengthening of risk finance and insurance.

The IRFF works to foster understanding and demand for the use of insurance and risk finance in development. It can also entail working to strengthen national strategic frameworks that govern risk management, and it can also work to strengthen social protection programmes, ensuring that they are shock-responsive and able to channel financing in the event of a disaster.

For example, the IRFF developed a policy brief to support the integration of insurance within UNDP led cash-for work programmes, with the Country Office in Syria showing great interest in exploring the link between insurance and post-crisis recovery work schemes, since most of the beneficiaries employed under this programme do not have any insurance towards the risk they face. To address this, the IRFF will leverage its ecosystem of private sector insurance partners to design tailored and innovative insurance mechanisms that can be implemented within these programmes and work with governments to implement such schemes into sovereign protection nets to cover these workers/beneficiaries against relevant types of risks, whether health related or climatic.

Insurance and
Risk Finance
Facility

Insurance and Risk Finance Product Development

In order to deliver financial resilience and pursue sustainable development, the IRFF Is working with industry partners and governments to develop innovative and bespoke solutions to fragile states countries. This work is diverse and cuts across a broad spectrum of themes and delivers different products including:

Products

Sovereign Risk Finance

UNDP works with industry and government develop and implement risk financing solutions that in almost any context. Within UNDP's current portfolio this work includes several large agricultural initiatives in Ethiopia, public asset insurance for flooding in Nigeria, and is developing similar schemes in Mozambique. Core to this work is close cooperation between both industry and government and the building of government capacity to financially manage risk alongside the development of actual risk financing solutions. UNDP is also working with industry to develop risk financing and insurance solutions where there may be a challenge to work with national or sub-national authorities.

Insurance

While risk financing solutions are critical to financially protecting large collections of public and private assets, lives and livelihoods, the development of national insurance markets, national industry and insurance products is critical to long-term financial risk management. Insurance markets in fragile and conflict-affected states is often very weak, a reflection of the conflict or institutional/social fragility, and yet these markets are precisely what needs to be developed over time to ensure national capacity to manage risk. UNDP there works with national insurers to build their capacity to develop and distribute insurance products, even in fragile states, and in 2024 will launch a Challenge Fund to directly build new insurance products across more than 20 countries.

Specialized Financial Vehicles

While insurance and risk financing are the two most typical aspects of financial risk layering in countries, risk transfer itself is highly flexible, and can be utilized even in the complex situations such as fragile states. UNDP works with industry and others to develop and implement tailored specialized financial vehicles and solutions which can operate outside of the normal parameters.

Risk Financing in Yemen

The two examples below from Yemen provide a snapshot of the innovative application of insurance solutions for some of the greatest development challenges and the transformative impact of insurance in complex contexts.

Averting an Ecological Disaster

Constructed in 1976 and converted a decade later into a floating storage and offloading facility (FSO) for oil, the FSO Safer was carrying 1.14 million barrels of light crude oil. However, maintenance of the FSO Safer was suspended in 2015 upon the outbreak of the conflict in Yemen. As a result, the structural integrity of the 47-year-old vessel has significantly deteriorated, and was at high-risk of breaking apart.

The UNDP-led operation, which involved the transfer of the oil to a replacement vessel and the scrapping of FSO Safer at a green salvage yard, was highly complex and involved a range of environmental, geopolitical, financial and humanitarian risks experts. However, without insurers offering their balance sheets to underwrite the residual financial risk, the mission could not go forward.

UNDP, through the support and services of the Insurance and Risk Finance Facility, was able to bind coverage thanks to its deep, long-term collaboration with the insurance industry. More than 100 individual underwriters have been involved in the issuance of an exceptionally specialised set of policies covering FSO Safer, the STS operation and the replacement vessel. While the FSO Safer project is a very important, urgent and high-profile example, embedding insurance-thinking into development cannot be limited to individual interventions.

The IRFF, together with UNDP Country Offices, will continue to provide tailor-made solutions for FSCs and crowd in insurance and risk finance for sustainable development.

Addressing Food Insecurity Through Large-Scale Specialised Financing

Over 16 million Yeminis go to bed hungry every night, with at least five million facing food insecurity at critical levels. This is mainly a food affordability, rather than a food availability issue. Given that Yemen is 90% dependent on imports to meet its food requirements, transportation costs make up a significant portion of the price of food.

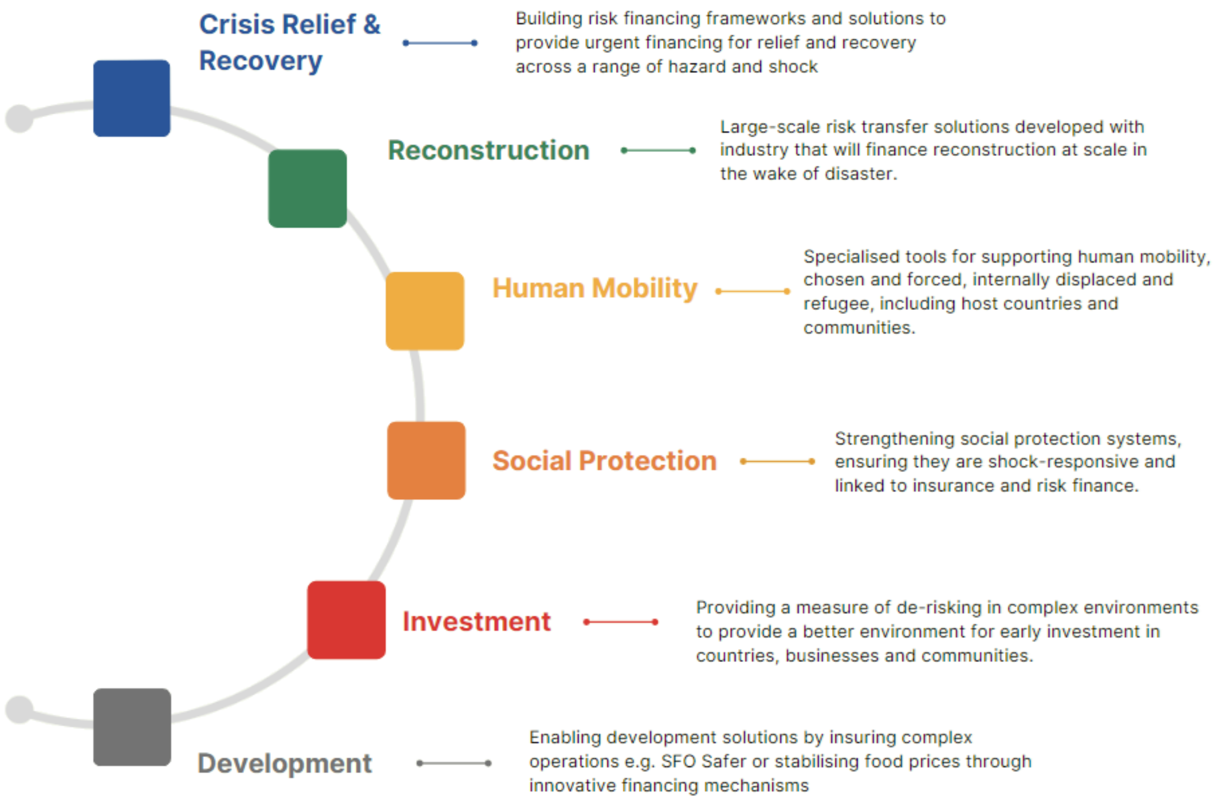
Yemeni waters have historically been classed as 'customary risk', with hull insurance charged at 0.025% of a ship's value. Since the outbreak of the conflict in Yemen, however, the south Red Sea has been designated 'high risk'. As a result, any ship calling at a Yemeni port must purchase additional war risk coverage, increasing the cost of insurance 16-fold to 0.4% of ship value . These additional costs, which are passed onto Yeminis in the form of higher food prices, contribute significantly to the food insecurity present in the country.

As part of a comprehensive response strategy, UNDP, on behalf on the UN in Yemen, has recommended a five-point plan to reduce the cost of food in Yemen. One of those five recommendations focuses on reducing war risk premiums, thereby bringing the cost of insurance back down to 'normal' rates.

With technical leadership from UNDP's IRFF, UNDP's Yemen office has been pursuing the re-establishment of an insurance guarantee fund as a fast and effective way to reduce the cost of food. UNDP has signed a MoU with the Minister of Transport of the Internationally Recognized Government (IRG). This forms the basis of a partnership with the IRG, the Port of Aden and the insurance industry to lowering war risk premiums.

Applying Risk Transfer to the Reality of Fragile and Conflict-Affected States

The solutions outlined in this offer are targeted to help countries and communities manage risk financially in complex contexts. And below you can see some of the reality of fragile contexts where the offer is already being implemented



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