

# INDEX-BASED WEATHER INSURANCE

## A CASE FOR MALAWI

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### PRESENTATION OVERVIEW

- ◉ Why weather index insurance.
- ◉ Objective of the insurance.
- ◉ Effects of the 2004/5 drought and the Malawian background.
- ◉ Stakeholders to the project
- ◉ Project workflows
- ◉ Portfolio Results
- ◉ Pre-requisites for program expansion.
- ◉ Major challenges encountered.
- ◉ The success of Harry Kafakaluanda
- ◉ Necessary investments

## OVERVIEW CONTINUED

- ◉ Challenges from insurers perspective
- ◉ How government can expand outreach
- ◉ conclusion

## KEY STAKEHOLDERS

- ◉ Farmers/farmer groups.
- ◉ Banks, micro finance institutions.
- ◉ Government - meteorological office.
- ◉ Insurance companies (Association).
- ◉ Reinsurance companies.

## WHY WEATHER INSURANCE?

- ◉ Smallholder farmers need input financing every year.
- ◉ Have little or no savings to buy high yielding seeds and other chemicals.
- ◉ Need to borrow from banks and other financial institutions.
- ◉ Have no collateral.
- ◉ High risks from weather and high loan default rates deter financing institutions

## THE OBJECTIVES OF WEATHER INSURANCE

- ◉ Give farmers access to finance to buy high yielding hybrid seeds and chemicals.
- ◉ In times of drought, all or part of loan paid off by insurance, allowing farmers to get fresh financing the following season.
- ◉ Protect lenders' capital.
- ◉ Provides income for the Insurance industry.
- ◉ Other stakeholders - extension services and high quality seed will improve long term production and revenues.

## EFFECTS OF 2004/5 DROUGHT IN MALAWI AND BACKGROUND

- ⦿ Recovery rates for lenders in the range 50-70%.
- ⦿ One big bank lost \$110,000 to smallholders farmers in one area.
- ⦿ That bank has stopped lending to those farmers -about 1000 households affected.
- ⦿ 2 microfinance institutions stopped lending to agriculture .
- ⦿ THIS IS BAD NEWS BECAUSE :
  - ⦿ 85% of Malawi is Rural based.
  - ⦿ 36% of GDP comes from Agric
  - ⦿ 87% of total employment is in Agric.
  - ⦿ 64% of Rural income is from Agric.
  - ⦿ 90% of country forex comes from Agric.
- ⦿ Weather insurance concept then introduced by World Bank in 2005.
- ⦿ World Bank had pilot tested the concept in India in 2003.

## PORTFOLIO RESULTS

	2005/6	2006/7	2007/8	2008/9	2009/10
Insured Crops	Groundnuts	Groundnuts and maize	Tobacco	Tobacco	Tobacco
Number of Stations	4	5	2	3	2
Number of insured farmers	892	1716	605	2606	706
USD Sum Insured	\$40,000	\$110,000	\$308,000	\$2,543,345	\$712,521
Premium Rates	5-7%	5-14% (Maize high)	5%	5%	5%
HIGHEST LOSS RATIO SO FAR IS 14% BUT IF THERE IS A CATASTROPHE IT WILL JUMP UP.					

## Prerequisites for program expansion

- Weather infrastructure (only 16 weather stations are automated in Malawi)
  - High station density will increase outreach and also reduce basis risk.
- Marketing organizations with sufficient outreach
  - Started with NASFAM and now working with Tobacco companies.
  - Other bigger organizations willing to participate in expansion project.
- A local insurance company and distributor champion willing to sell policies and intermediate the risk
  - Nine insurance companies grouped together to underwrite risk.
  - For pilot, NO regulatory approval was necessary BUT now regulator to know of every new product.
  - For expansion program will work with Government and World Bank to develop enabling regulatory framework.

## Major Challenge for Malawi

- Unwillingness to buy by farmers
  - Stand alone product - no takers.
  - Product has to be linked to other financial services such as loans.
- Affordability
  - **Financiers and farmers not willing to pay more than 5% premium.**
- Weather infrastructure not available in key farming areas.
  - **This has led to very slow growth in portfolio.**
  - **World Bank working with Malawi Met to install stations in these key areas.**
- Marketing channels.
  - Groundnuts market prone to side-selling.
  - Tobacco chain well established.
  - Tobacco prices have an effect on renewal rate.
  - Potential outreach can be high if proper marketing plan is developed.
- Contract design work and capacity building - Need for locals to be trained.

# THE SUCCESS STORY OF HARRY KAFALUANDA

Harry Kafakaluanda's Old House



## Harry Kafakaluanda's New House



## Harry Kafakaluanda's Words

**“The benefits for me are a better living standard, better food, I have been able to build a better house, and I have bought an ox cart from last year’s earnings. This would not have been possible before”**

## NECESSARY INVESTMENTS

- ◉ Building of local capacity to design contracts in local institutions
- ◉ More automated weather stations in key agriculture areas
- ◉ Training of bank staff, loan officers and extension officers to act as communication channels for insurers
- ◉ Encouragement of more reinsurers to enter the market leading to low premium rates
- ◉ Development of more marketing channels

## CHALLENGES FROM INSURERS PERSPECTIVE

- ◉ Product is new and more complex relative to traditional products
- ◉ Lack of skills in designing products
- ◉ Limited reinsurers leading to lack of competition
- ◉ Premium rates are higher than traditional products hence marketing the products not easy



## HOW GOVT. CAN EXPAND OUTREACH

- ◉ Speed up the upgrade and installation of automated weather stations
- ◉ Ensure proper maintenance of the existing and future weather stations
- ◉ Reduce or remove VAT on premiums as this is targeted at lower income farmers

## CONCLUSION

- Weather Index is not the panacea , it has to be combined with other risk mitigation strategies such as good extension services and good produce markets.
- There are few institutions actively involved in the designing , pricing and marketing of weather index insurance and COMESA should assist member countries in developing this skill so that more people can benefit.
- The impact of this product can be very high, but more work is needed by all key stakeholders to make it work.

- THANK YOU !
- ZIKOMO KWAMBIRI!
- ASANTE SANA!
- WEBALE NYO!
- NATOTELA SANA!