

# Prospects for sustainable disaster insurance provision in Africa through the African Risk Capacity

Findings from the ARC evaluation

## Introduction

### Context

The response to natural disasters in Africa has traditionally been largely reactive and has relied on international emergency appeals to secure funding after a disaster has occurred, which is often slow and insufficient. This problem becomes particularly acute in the case of drought, where appeals for international aid are not made when the rains fail, but months later when there is a severe humanitarian situation: where people are suffering from food insecurity, where malnutrition rates are rising sharply, and where people are using negative coping mechanisms, such as selling assets, getting into debt, or taking children out of school.

### ARC

ARC was established by the Africa Union in 2012 as **an African-owned, index-based weather risk insurance pool and early response mechanism** that combines early warning, disaster risk management, and risk finance (see: African Risk Capacity Group). ARC support includes the configuration of weather risk models, pooled risk insurance, and a programme that aims to build capacity on disaster risk and its management. The expectation is that this will provide better early warning information and will allow African governments to better plan for, prepare for, and respond to weather risk emergencies, enabling a swifter response to drought and other emergencies, and ultimately protecting vulnerable households through the rapid provision of support to disaster-affected people.

**ARC comprises two entities:** **ARC Agency** builds capacity in member countries to plan for and respond to climate disasters and raises awareness of ARC; it is funded by donor grants. The **ARC Insurance Company Limited** (ARC Ltd) provides risk transfer services –

particularly insurance – and operates on a commercial basis. To date, ARC's main focus has been on drought risk insurance.

Since its founding in 2012, ARC has broadened its offer to include rangeland drought and tropical cyclone insurance products, and is currently developing insurance products for outbreaks and epidemics, and for floods. ARC has also introduced **innovative approaches to supporting premium cost-sharing** for countries where these costs are prohibitive:

- ARC has introduced **premium subsidies** to support the growth of the risk pool in the short to medium term, and to increase coverage by providing additional premium financing for countries.
- **ARC Replica** is a parallel scheme for humanitarian organisations which helps increase coverage and brings governments and humanitarian partners together to strengthen coordination, preparedness, and response. Premiums are fully paid by donors.

To be eligible to take out an insurance contract with ARC Ltd member states must sign a memorandum of understanding with ARC Agency and complete an extensive preparatory and capacity building process, at the end of which they are awarded a certificate of good standing. As part of this process, a national technical working group is set up, which brings together professionals from various government agencies to undertake capacity building on risk modelling, contingency planning, and risk transfer parameters. The risk modelling component includes customisation of Africa RiskView (ARV), ARC's proprietary software application, which is used for predicting the early onset of drought.

A core objective of ARC is to **ensure that assistance is received by vulnerable households earlier than is the case with typical humanitarian aid**. From the receipt of the payout, the target is for assistance to reach the first beneficiary in 120 days and the intervention to be completed within the next 180 days. Assistance is typically provided to households as cash, food, livestock food subsidies, or nutritional support.

### ARC evaluation

Oxford Policy Management is undertaking a 10-year independent evaluation of ARC, financed by the UK’s Foreign, Commonwealth and Development Office. This note reflects selected findings from the second formative evaluation of ARC, conducted in 2021–22. The full evaluation report (Oxford Policy Management, 2022), and other summary briefs and reports from previous phases of the evaluation, can be found here.

This briefing note summarises the evaluation’s findings on ARC’s work to create demand for its products, and on its long-term sustainability. Two other briefing notes will summarise findings on ARC’s capacity development and its value for money.

## Findings

### Increasing demand

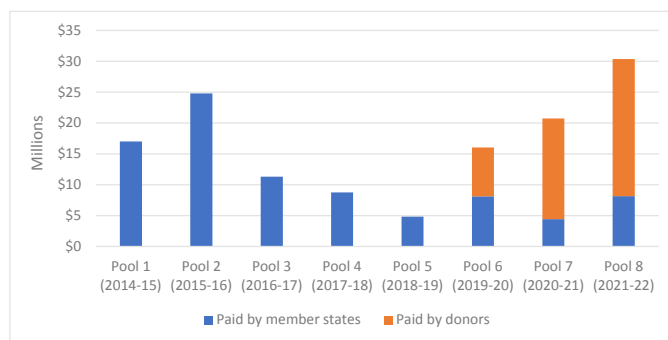
#### Summary findings

ARC’s approach to generating demand focuses primarily on expanding its product offering and addressing constraints to risk pool accession. However, the pace of developing and releasing new products has been slower than expected. Despite efforts to update it, concerns about ARC’s drought risk model persist and may undermine demand. The risk pool has grown considerably in recent years. This appears to be due in large part to the introduction of premium subsidies, and due to Replica, while the number of new countries joining the pool remains below target. Member states value the drought insurance and Agency’s engagement, yet caveat this with concerns about receipt of payouts, and note challenges with customising the risk model.

**Growing the risk pool** is a key element of ARC’s effort to insure 150 million vulnerable African people against disasters, to ensure insurance premiums are affordable, and to establish ARC’s financial viability. Once member

states complete the preparatory process described above they are eligible to join the risk pool, which is done by purchasing an insurance product.

**Table 1**  
Total premiums paid by risk pool and source of finance (all insurance products)



**The size of ARC’s drought risk pool has grown considerably in recent years**, from three member countries in 2018/19, to 13 in 2021/22. The growth in total premiums received has been driven largely by premium subsidies, and by Replica, as well as by the introduction of new insurance products (rangeland drought and tropical cyclone). Despite this growth, the **number of countries with insurance policies has not grown in line with targets** and does not appear to be on track to achieve targets in the short term.

**Table 1:**  
Target and actual number of member states with ARC insurance by year, 2020–24

Peril	Baseline (2019)	2020		2021		2022	2023	2024
		Targets	Actual	Targets	Actual	Targets	Targets	Targets
Drought	11	11	11	17	13	20	22	22
Tropical cyclone	0	2	1	2	1	2	2	3
Flood	0	0	0	0	0	3	3	3
Outbreaks and epidemics	0	0	0	2	0	4	6	8

**Member countries frequently value ARC’s drought insurance highly** but caveat this with concerns about whether they will receive a payout when it is needed, and about the difficulties with customising the drought risk model to their countries’ needs. Factors which drive decisions to purchase drought insurance include the expectation of receiving a payout when one is due, the price of premiums, confidence in the drought model, the relevance of drought to a given country, and the availability of other financial products for middle-income countries. As one country-level respondent noted of ARC’s drought insurance:

**‘In theory, it’s really valuable. If it actually triggered a payout it would be really valuable. ... I would have really liked it to work to be able to show the government that ARC is valuable.’**

Some respondents to the evaluation noted that **the work with ARC adds to a sense of ownership and empowerment as regards governments managing their drought risk themselves**. Among other ARC products and services, ARC’s support to government capacity building is valued positively, as is its technical support for ARV customisation and for the development of drought response plans. **ARC Replica** is valued by ARC respondents for offering an opportunity to increase ARC’s scale and coverage of member states. Country-level respondents value Replica’s increased coverage and additional technical expertise in relation to supporting strategic planning with non-government partners on how to approach relief distribution, including ensuring this is collaborative and more efficient and effective.

ARC is undertaking **activities that aim to increase interest and demand among its member states**, and is developing a portfolio of new products that respond to member country needs. This includes new insurance products that aim to meet country needs, such as flood insurance, meso-level insurance options, and consideration of sub-sovereign products for countries that are less financially constrained. However the pace of development is slow.

## **ARC’s sustainability**

### **Summary findings**

ARC’s longer-term sustainability is uncertain. ARC Ltd’s Inclusive Growth Strategy appears overambitious. In the near term, the Fundraising Strategy identifies a US\$ 68 million funding gap for ARC Agency, which is to be filled through donor support. However, donor support to ARC Agency is fragile. There is, however, an opportunity to rebuild confidence since there is still considerable support for the value of ex-ante insurance products and disaster preparedness capacity building. There are generally positive views regarding the clarity of ARC’s mandate, but there are concerns that ARC lacks a detailed strategy to deliver to this mandate.

In the near term, **ARC’s Fundraising Strategy identifies a US\$ 68 million funding gap for ARC Agency over the next five years**. ARC’s solution for filling this gap

is donor support. However, a number of donors that have supported ARC from its inception no longer provide funding to ARC Agency because they have lost confidence in it due to challenges with the transparency of, and responsiveness from, ARC, prolonged product development timelines, inadequate funding preparation, and ineffectiveness in the division of roles between Agency and Ltd. However, there is an opportunity to rebuild this lost confidence. The same donors still believe in the important role of the ex-ante insurance products that ARC Ltd provides and they have switched their expenditure to premium financing or premium purchases.

**There is a lack of clarity as to how ARC views its long-term funding solutions**. Apparent inconsistencies between ARC Ltd’s Inclusive Growth Strategy and the Group’s Fundraising Strategy call into question the Group’s approach to establishing income streams apart from donor support. ARC Ltd’s strategy is to diversify into different areas of revenue (reinsurance and retrocession) and new product offerings (micro- and meso-level insurance). This may be sound, but the rate at which ARC Ltd proposes to do this does not appear plausible. The Group Strategy’s emphasis on sovereign governments raises concerns, given the trend of recent risk pools being heavily subsidised. Sovereign insurance sales are also undermined by weakened confidence in the drought risk model.

Some of the noted **constraints to ARC’s longer-term feasibility** relate to the following issues: the ‘volatility’ of the environment in which ARC intends to sell its products (countries not having dependable budgets with which to buy disaster insurance); whether ARC is adequately responding to country needs (product diversification and accurate customisation); limited awareness of disaster risk financing and how insurance can be used to manage disaster risks; and the mistrust that has grown in recent years due to some cases of delays in, or a lack of, expected payouts.

Regarding ARC’s organisational setup, the **new Group Board provides cause for optimism regarding improved governance and accountability** across the ARC Group. However, the **division of labour between ARC Agency and ARC Ltd is a cause for concern**. There is an understanding that ARC’s treaty basis requires a division of the entities, but the current division of roles creates challenges and inefficiencies, including ARC Ltd having little oversight as to how the products it underwrites are developed, improved, marketed, and sold. Among member states, the biggest threat to their buy-in is their weakened confidence in the risk model. Among donors, support for ARC’s premise and objectives remains enthusiastic, but this enthusiastic view is consistently followed up with a disclaimer that ARC’s execution of its objectives and mandate is weak.



## Recommendations

The evaluation makes recommendations for a number of different stakeholders, drawing on findings from each of the evaluation questions. The main recommendations made that are relevant to the demand for ARC's products and its long-term sustainability are as follows:

1. **ARC Group** should **clarify and agree its core 'value proposition'** with its main stakeholder groups, including its Board, donors, and member states. ARC should then focus on delivering to its core value proposition in the immediate future, and should avoid widening its ambitions until this core proposition is being delivered.
2. **ARC Agency** needs to **identify strategies to help recipient governments improve implementation of their drought response** – particularly the timely, sufficient, and well-targeted delivery of support.
3. **ARC must address the immediate funding crisis faced by Agency**, which will impact both Agency and Ltd. This crisis should be addressed through the agreement of a **two-year reform plan**, coupled with an **inclusive strategy development process** that sets out how longer-term challenges will be addressed after the end of the current strategy period in 2024.
4. **ARC** should develop the **ARC Group Strategy for the post-2024 period**. This should provide a clear outline of how it will address both high-level strategic questions as well as other financial, organisational, and operational issues which are not addressed prior to 2024. The process needs to involve a wide group of stakeholders, including the African Union and the development partners who will be asked to finance it.
5. The strategy process must **examine and resolve the more fundamental questions about ARC's structure and mandate**. This should include the fundamental question of ARC's core purpose and value proposition; the question of whether ARC Agency and ARC Ltd should continue to operate under a unified strategy and Board; the treaty basis for ARC; and ARC's relationship with the African Union and with the World Food Programme.
6. **ARC Ltd should also develop a clearer long-term diversification and business plan** and long-term financial strategy, which should include a clear rationale for entry into new market areas, a reduction in the level of reinsurance, and more effective growth in sales through work with ARC Agency.
7. **Donors** should agree on shared objectives for ARC and how to best combine funding in support of ARC in order to **avoid setting up competing priorities for ARC**.

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### References

Oxford Policy Management (2022) 'Independent Evaluation of the African Risk Capacity: Second Formative Evaluation Final Report'

## About Oxford Policy Management

Oxford Policy Management is committed to helping low- and middle-income countries achieve growth and reduce poverty and disadvantage through public policy reform. We seek to bring about lasting positive change using analytical and practical policy expertise. Through our global network of offices, we work in partnership with national decision makers to research, design, implement, and evaluate impactful public policy. We work in all areas of social and economic policy and governance, including health, finance, education, climate change, and public sector management. We draw on our local and international sector experts to provide the very best evidence-based support.

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