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LIVES



# Climate Risk Financing

## Anticipatory and Early Actions for Climate Hazards

Climate change is not a threat in the distant future, but a present-day emergency that is already threatening lives, livelihoods and economies. The global climate crisis is driving more frequent and intense floods, heatwaves, droughts, and storms. The number of these extreme weather events has quintupled in the last fifty years, with projections that climate-related disasters could reach up to 560 each year (or 1.5 per day) by 2030. These climate shocks affect food-insecure people disproportionately, destroying crops, livestock and vital infrastructure.

Each year, the humanitarian sector and governments spend billions to prepare for, respond to, and help people recover from increasingly destructive climate-related disasters. Humanitarian responses are typically mobilized only after an extreme weather event has resulted in catastrophic loss and damage for the most vulnerable and food-insecure people. For slow-onset events, such as droughts, assistance reaches people often

months after crops have failed and livestock are lost, and when many households have already resorted to negative coping strategies. Efforts to provide more timely assistance to vulnerable populations, as well as better informed and forward-looking approaches to crisis management are urgently required.

Investments in disaster risk reduction activities at the community level, anticipatory action before a forecasted extreme weather event or its immediate impacts materialize and early action immediately after a hazard hits can reduce humanitarian response needs and costs, mitigates impacts on lives and livelihoods and provides a more dignified approach to humanitarian assistance. Particularly in the case of drought, the cost of mobilizing a humanitarian response can be greatly reduced when anticipatory action and early action systems are in place prior to a failed harvest. Through deploying climate risk financing mechanisms that allow for predictable anticipatory action and early



action, WFP can significantly reduce the human suffering and capital losses from weather and climate-related extreme events.

## MOVING FROM CRISIS RESPONSE TO CLIMATE RISK MANAGEMENT

WFP is collaborating with a range of public and private sector partners to develop climate risk finance programmes that help governments and vulnerable households to anticipate, absorb and rapidly recover from climate shocks. Many of these programmes rely on parametric triggers that are based on independent, verifiable and frequently reported data points. These triggers enable an early release of flexible funding for predefined action plans that get executed either before or immediately after a shock occurs.

The key benefit of climate risk financing programmes is that they enable predictable management of risks through targeted preventive action at the moment when it is most needed. This reduces reliance on ad-hoc resource mobilization following a climate shock, which is the prevailing paradigm in many humanitarian programmes. Climate risk financing programmes provide donors with an opportunity to invest in approaches that transform the current humanitarian model, from a repetitive and reactive humanitarian response, towards a forward-looking and proactive risk management model.

## OVERVIEW OF WFP-SUPPORTED CLIMATE RISK FINANCING INSTRUMENTS

The different climate risk financing programmes currently employed by WFP have different comparative advantages. Each programme demonstrates efficiencies in addressing a range of climate shocks, depending on their frequency, severity and geographical impact.

1. **Anticipatory Actions (AA)** is defined as acting ahead of predicted hazards to prevent or reduce acute humanitarian impacts before they fully unfold. This requires pre-agreed plans that identify partners and activities, reliable early warning information, and pre-

agreed financing, released predictably and rapidly when an agreed trigger-point is reached. This approach is changing the way the humanitarian system responds to extreme-weather events by creating a proactive and 'anticipatory' system – filling the gap between long-term disaster risk reduction interventions and post-disaster humanitarian relief efforts. In 2022, WFP is developing AA mechanisms alongside governments and other key humanitarian partners in 21 countries in Asia, Africa and Latin America and the Caribbean. In 2021, WFP distributed US\$8,6 million to support anticipatory action programmes, helping vulnerable people to prevent the effects of extreme weather on their food security and nutrition in six country activations.

2. **Micro or Inclusive Insurance** is a means to protect low-income people, usually excluded from traditional financial services, against specific perils in exchange for regular premiums payments that are calculated based on the likelihood and cost of the covered risk. When applied to rural and agricultural areas, these policies protect households from the risk of drought or floods. Micro-insurance is considered an effective tool for food-insecure smallholder farmers to better manage climate-related risks, overcome vulnerability and achieve resilient livelihoods, while also enabling risk-informed investments and growth in the agricultural sector. In 2021, through the R4 Rural Resilience Initiative, WFP promoted access to a variety of micro-insurance products for 380,000 farmers and pastoralists in fifteen countries, as one component of an integrated climate risk management approach.
3. **Macro & Meso Insurance** refers to insurance coverage at a national (macro) or institutional (meso) level to protect vulnerable communities or an entire population. One example is the sovereign insurance product offered by African Risk Capacity Ltd (ARC) to vulnerable African countries prone to extreme drought risks. ARC allows countries to manage climate risk as a group, in a financially efficient manner, by

pooling together many country level policies covering diverse climate risks across the continent. Under a WFP and Start Network initiative, humanitarian organizations can complement the insurance coverage of ARC Member States by purchasing an additional 'Replica Policy', which could double the number of beneficiaries receiving assistance when an extreme drought event occurs. When a payout is triggered, pre-defined operational plans identify how resources and assistance will be coordinated and delivered by the respective government and by WFP. This means that all decision-making is done before a disaster strikes, and that WFP's actions complement those of national emergency response agencies. Three ARC Replica policies triggered payouts totaling US\$9.45 million in West Africa during the 2021/22 season, with the payout in Mali of US\$7.1 million being the largest WFP has received to date. In 2022, WFP's ARC Replica policies continue to provide drought protection for vulnerable communities, with Mali, Burkina Faso and The Gambia confirmed to receive payouts that guarantee US\$10.7 million for assistance, which could reach as high as US\$15 million.

In the right circumstances, integrating climate risk financing mechanisms, such as micro & macro insurance and anticipatory action, with social protection can be a cost-effective and low-regrets strategy for assisting vulnerable people before and during crises. Linking social protection systems with early warning and pre-arranged financing can ensure the sustainability and scalability of these approaches, allows for better targeting of beneficiaries, improves aid coordination and enables rapid delivery of assistance to populations most vulnerable to climate risks.

## HOW WFP IS INTEGRATING CLIMATE RISK FINANCING TOOLS

As vulnerable communities are exposed to a wide range of climate-related risks, a comprehensive climate risk financing strategy should combine approaches to anticipate, prepare for and absorb impacts occurring at

different risk levels and timeframes. Layering these different approaches can ensure that all segments of a population are protected from a wide range of climate-related risks.

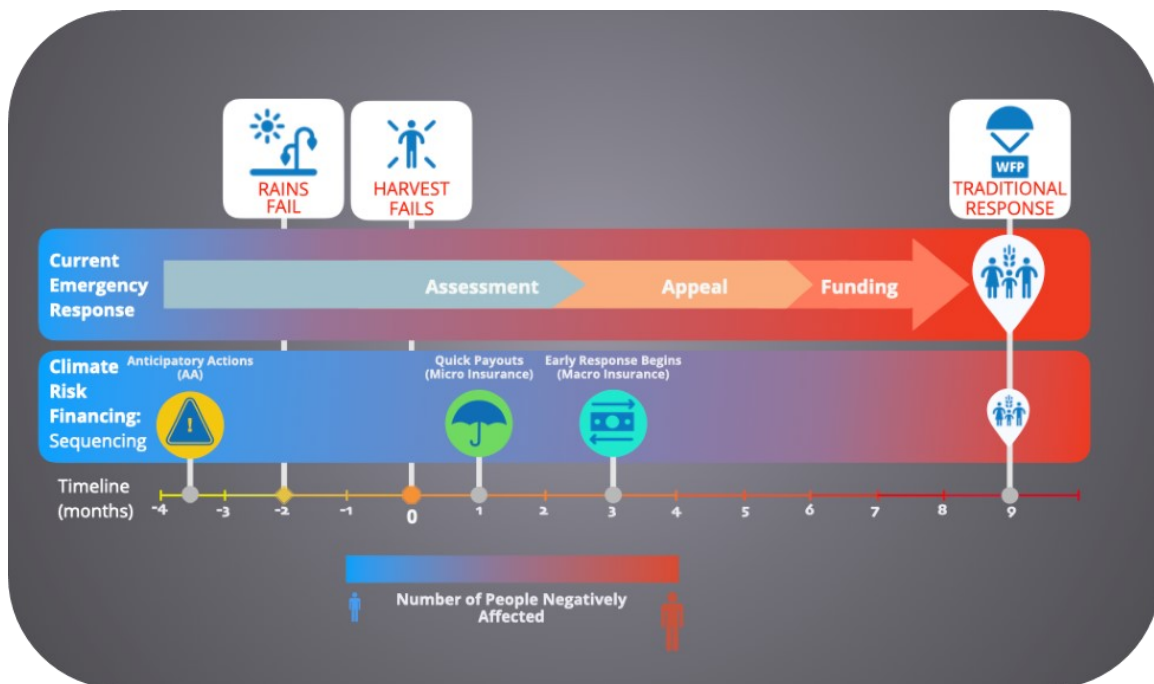
WFP's climate risk financing programmes have distinct advantages in different contexts in terms of timing, administrative requirements, transfer sizes, geographical reach, vulnerability levels and potential for implementation at scale. These tools can complement each other effectively through:

- **Data sharing:** When implemented jointly, these mechanisms can utilize multiple and complementary data sets that will improve the efficiency of the parametric indices and provide additional sources of information for monitoring, with the potential to reduce gaps in assistance and protection.
- **Sequencing:** Anticipatory actions are triggered before a shock occurs in order to reduce and prevent, to the extent possible, the impact of the forecasted hazard. Micro-insurance provides assistance soon after a covered risk materializes with payouts typically transferred directly to an individual policyholder. Insurance payouts complement the anticipatory actions to enable a faster recovery and increases communities' ability to withstand future shocks. Assistance received by households through macro insurance is distributed through both humanitarian and government agencies, which may be mobilized after AA and micro-insurance, although still much earlier than a conventional humanitarian response (See Figure 1).
- **Targeting:** All climate risk finance instruments aim to protect resource-poor population groups that are vulnerable to climate shocks and food insecurity. However, by providing a protective layer for income generating activities, such as smallholder farming, micro-insurance may be



more appropriate for households that have productive resources (land, labour or capital) as it influences investment behaviour and access to financial services even if a shock does not occur. When AA and insurance are implemented simultaneously, insurance payouts can support faster recovery if a catastrophic shock exceeds the mitigation potential of anticipatory actions. Similarly, after an extreme weather event, macro insurance payouts can provide timely assistance and safety nets to the most vulnerable members of the population.

Climate risk finance tools can be more effective when implemented as part of an integrated risk management strategy that promotes investments in reducing disaster risk, with the most appropriate combination of tools for the risk profile of the country. As part of an effort to strengthen this integrated programming approach, WFP is currently assessing the feasibility and potential costs and benefits of integrated climate risk financing in Burkina Faso and Zimbabwe, where WFP currently implements anticipatory action, microinsurance and ARC Replica. Throughout implementation, WFP will ensure that effective monitoring and evaluation mechanisms are in place to measure the impact and analyse how these programmes improve the resilience and food security of WFP beneficiaries.



**Figure 1.** An example timeline of when a rainfall shortage results in a food crisis and when the various climate risk financing programmes provide assistance to affected populations compared to a traditional humanitarian response. This illustrates WFP’s specific programmes and when these approaches are triggered (AA, R4 and ARC Replica).

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