



Can financial markets be tapped to help poor people cope with weather risks? /

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Monografía

Poor households in rural areas are particularly vulnerable to risks that reduce incomes and increase expenditures. Most past research has focused on risk-coping strategies for the rural poor, specifically on micro-level and household actions. These are risks that can be shared within a community or extended family. These strategies are effective for independent risks, but ineffective for covariate or systemic risks. Skees, Varangis, Larson, and Siegel focus on private and public mechanisms for managing covariate risk for natural disasters. When many households within the same community face risks that create losses for all, traditional coping mechanisms are likely to fail. Such covariate risks are not uncommon in many developing countries, especially where farming remains a major source of income. The authors focus on risks related to weather events (such as excess rain, droughts, freezes, and high winds) that have a severe impact on rural incomes. Weather insurance could cover the covariate risk for a community of poor households through formal and informal risk-sharing arrangements among households that are purchasing these weather contracts. Given recent Mexican innovations targeted at helping the poor cope with catastrophic weather events, the authors use Mexico as a case study. In Mexico, poor households are exposed to systemic risks, such as droughts and floods, that affect the economic livelihood of their region. Catastrophic insurance is useful for small farmers, although commercially oriented small farmers may wish to obtain coverage for less catastrophic events. Weather insurance could meet this need. It pays out according to the frequency and intensity of specific weather events. Because weather insurance depends on the occurrence and objective measure of intensity of a specific event, it does not require individual farm inspection that can be very costly for small farms. The authors argue that a key issue of delivering insurance to small farmers is the existence of producer organizations. In Mexico, the farmer mutual insurance funds provide a good example. These funds provide insurance to their members by pulling together resources to pay for future indemnities and reinsures itself from major systemic risks that could hurt simultaneously all their members. This paper--a product of Rural Development, Development Research Group--is part of a larger effort in the group to find new approaches to help rural households cope with risks. The authors may be contacted at jskees@pop.uky.edu, pvarangis@worldbank.org, dlarson@worldbank.org, or psiegel@worldbank.org

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