

## DISASTER RISK FINANCING TOOLS AND APPROACHES

- 1. ADB engagement.** ADB attaches significant importance to disaster risk management (DRM) in the Pacific, and has provided considerable loans, grants, and technical assistance (TA) for disaster response, early recovery, and reconstruction. This support has progressively broadened from post-disaster assistance to proactive disaster risk reduction (DRR) through a range of financing mechanisms. ADB provides dedicated funding to its concessional assistance-only countries through the Asian Development Fund (ADF) 12 DRR financing mechanism to spur investment in DRR. ADB often plays a key role in post-disaster needs assessments. For the post-disaster humanitarian response phase, ADB's Asia Pacific Disaster Response Fund, a dedicated quick-disbursing instrument, can provide grants up to \$3.0 million per event within a week of a disaster.<sup>1</sup> Additional concessional funds can be accessed through the ADF Disaster Response Facility for the early recovery and reconstruction phase, although processing associated projects takes time.
- 2.** Since 1987, ADB has offered an emergency assistance loan instrument with extended grace and repayment periods, increased retroactive financing, lower interest rates, and abbreviated processing requirements, facilitating the approval of fast-tracked assistance for early recovery purposes. However, emergency assistance loans can still take 3 months or more to process, and reconstruction loans processed under normal lending modalities can take significantly longer.
- 3. Contingent financing.** ADB piloted contingent financing in the Cook Islands in 2016 as a mechanism to provide more timely disaster-response support, financed through a stand-alone single-tranche policy-based loan from regular ordinary capital resources. To access the contingent financing, the Government of the Cook Islands undertook prior actions to strengthen policy and institutional arrangements for DRM, and the disbursement will be triggered when a state of disaster is declared.<sup>2</sup> This approach is also reflected in the 2017 regional program for Samoa, Tonga, and Tuvalu, from ADB's concessional resources.<sup>3</sup> Both programs include provisions for TA to further DRM reforms, under a program monitoring framework that will support progress toward achieving the governments' long-term DRM goals. The proposed program for Palau reflects the unique features of this support.
- 4. Layered approach to disaster risk financing.** The most cost-effective way of financing disaster response is through a range of tools in a common framework to address different layers of risk, as no single instrument is optimal for responding to all disaster events, which range from frequent small-scale events to rare catastrophic events. The figure shows the range of potential financing tools, and the availability of these tools in Palau—from budget reallocations that address low-impact high-frequency events (such as stormwater overflow), to global bonds that address rare yet highly damaging events (such as high-magnitude earthquakes). As in most Pacific countries, there is a gap for medium-layer risks.

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<sup>1</sup> Between the establishment of the Asia Pacific Disaster Response Fund (APDRF) in 2009 and June 2018, the Pacific has received 13 APDRF grants totaling \$9.4 million.

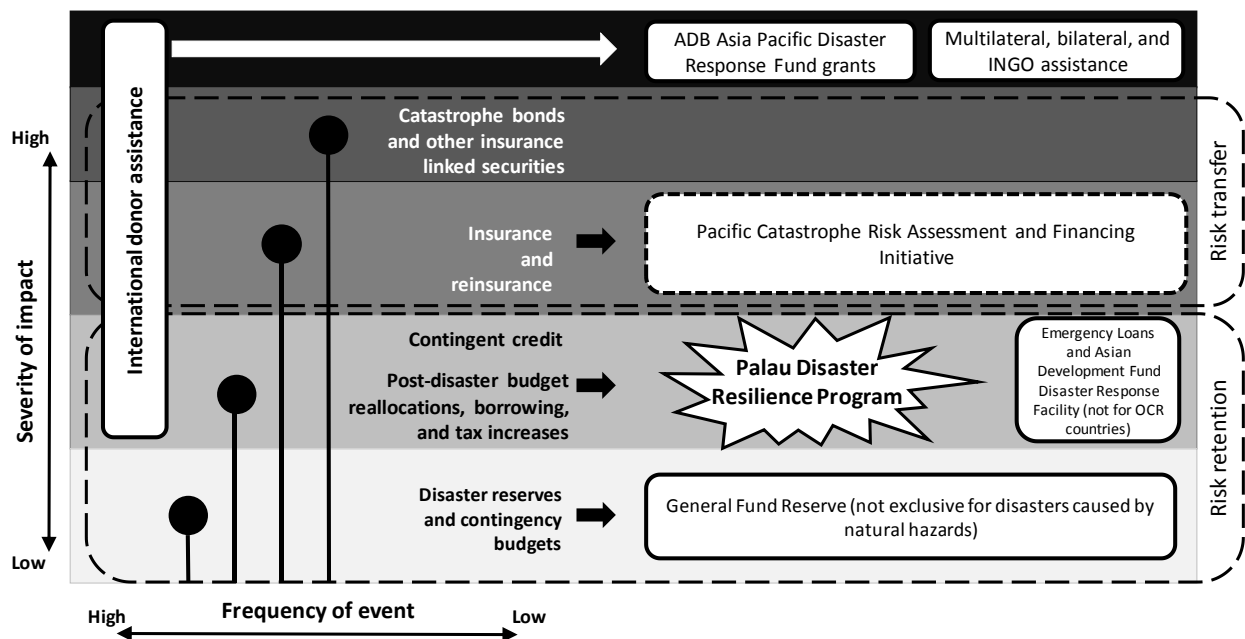
<sup>2</sup> ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Loan to the Cook Islands for the Disaster Resilience Program*. Manila.

<sup>3</sup> ADB. 2017. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Loans, Policy-Based Grants, and Technical Assistance Grant for the Pacific Disaster Resilience Program*. Manila. Under the program, the participating countries—Samoa, Tonga, and Tuvalu—have entered into a memorandum of understanding that will be the basis for collaboration among them in exploring, developing, and establishing the most suitable collaborative regional mechanism for contingent financing. TA support will provide options for a sustainable regional mechanism to channel disaster contingent financing, allowing funds to be replenished, additional countries to join, and other donors to contribute to the contingent funds.

5. There is strong demand from Palau for additional instruments to strengthen financial preparedness for disasters, and a clear need for this, given the rising incidence of disaster events. Ideally, a comprehensive disaster risk financing strategy would combine both ex ante mechanisms (arranged ahead of a disaster occurring, such as disaster reserves, contingency budgets, contingent credit, and insurance) and ex post mechanisms (post-disaster budget reallocations, borrowing, and international assistance). The precise mix would depend on the relative cost-effectiveness of alternative instruments for specific layers of risk in individual country contexts. Contingent financing is particularly cost-effective in addressing risks pertaining to events that would exhaust annual contingency budgets and any national reserves (such as the General Fund Reserve), but are too frequent to be covered cost effectively through insurance.

6. **Proposed program.** The proposed program intends to cover the medium-layer risks gap. It provides Palau with a source of financing for response, early recovery, and reconstruction activities for disaster events caused by all types of natural hazards. It will complement existing disaster risk financing instruments/options available to Palau (figure), including the General Fund Reserve (which is not exclusively for disasters) and parametric disaster insurance (which is still under consideration).<sup>4</sup> Its unique features are as follows: (i) it can make a payment quickly and use the funds flexibly with no additional requirements, beyond national public financial management requirements, to track and report on expenditures; (ii) the amount that can be released is significant in terms of immediate response needs; (iii) the amount is not dependent on any assessment of loss or measure of the intensity of the natural hazard; and (iv) funds are available for disaster events triggered by any type of natural hazard.

**Disaster Risk Financing Layers and Existing Tools in Palau**



ADB = Asian Development Bank, INGO = international nongovernment organization, OCR = ordinary capital resources.  
Source: ADB

<sup>4</sup> The government is considering typhoon insurance cover through the Pacific Catastrophe Risk Insurance Company for low-frequency high-impact events.