



PROJECT INFORMATION DOCUMENT (PID)

APPRAISAL STAGE

Report No.: AB1447

Project Name	Mongolia: Index-Based Livestock Insurance Project
Region	EAST ASIA AND PACIFIC
Sector	General agriculture, fishing and forestry sector (50%); Non-compulsory pensions, insurance and contractual savings (50%)
Project ID	P088816
Borrower(s)	Government of Mongolia
Implementing Agency	Ministry of Finance
Environment Category	<input type="checkbox"/> A <input type="checkbox"/> B <input checked="" type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined)
Date PID Prepared	March 10, 2005
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1. Country and Sector Background

The agricultural sector plays a central role in the Mongolian economy, contributing around one third of national GDP. The agricultural sector is dominated by livestock husbandry, which has an 87% share of agricultural GDP and supports at least half the population. Livestock provides rural households with an important source of income, jobs and food security, and a means for investing and storing their wealth. The importance of livestock to the livelihoods of poor rural households has increased in recent years with the shift from collectivized farming to family-based herding during the 1990s: the number of herding households doubled between 1990 and 1997.

However, the country is prone to extreme climatic events that can cause high rates of livestock mortality, jeopardizing rural livelihoods. In particular, the frequent droughts and severe winters/springs (known as *dzuds*) can devastate herd numbers. For example, during the period between 1999 and 2002, one third of the national herd was lost in successive *dzuds*. At that time, many households lost all their livestock and their primary source of income, and the impact was felt throughout the economy, with GDP growth significantly pegged back.

The Government of Mongolia has prioritized the development of the livestock sector and, with support from donors, is introducing a program of sectoral reform. This includes greater flexibility in pasture land tenure and increased investment in rural infrastructure and services. A major thrust of government and donor intervention is to respond to the risks inherent in livestock husbandry by supporting improved pastoral risk management (PRM), and this approach is a key element of the PRSP.



Improved pastoral risk management, coupled with existing government activities to mitigate the impact of *dzuds*, for example through the distribution of hay and fodder reserves, can be effective to lower livestock mortality in less extreme *dzud* events. However, such measures are ineffective against more severe weather events, and cannot prevent high levels of mortality. In such instances, herders have to rely upon traditional informal coping mechanisms and *ad hoc* and unpredictable support from Government and international agencies. For affected areas, after immediate relief, the main longer term support has been through restocking programs. Evaluation has shown that these programs can be expensive, poorly targeted and relatively inefficient. Furthermore, restocking can be counterproductive, as it provides little incentives for herders to improve their herd and pasture management to lower mortality. This conclusion is generally accepted by Government, international agencies and herders who have participated in restocking programs.

Livestock Insurance

Insurance is a logical complement to on-going pastoral risk management activities, as it has the potential to protect herders against unavoidable livestock loss, and replaces the need for Government re-stocking programs. Although insurance is recognized as a key element of risk mitigation, the conventional approach to livestock insurance (based on individual losses) has been found to be ineffective in Mongolian conditions. Individual livestock insurance is unpopular with both insurance companies and livestock owners. It suffers from moral hazard and the consequent difficulties and high costs of verifying individual losses. Government provided insurance has been considered, however, the scale of the disasters during 1999 to 2002 made it clear that the resources of Government alone cannot provide full catastrophe insurance and that market-based alternatives need to be considered, which would share risks between herders, the insurance industry, and government. Involving the insurance industry, operating on a commercial basis, has the potential to improve the financial sustainability of livestock insurance and contributes to strengthening the rural finance sector, which is a key element in Government strategy for rural economic diversification.

Insurance Sector

The domestic insurance market is immature and undercapitalized. It was opened to competition in the early 1990s, and the two state-owned insurance companies, Mongol Daatgal and Tushig were privatized in 2003. As of December 2004, 24 insurance companies were licensed and offered non-life insurance only (personal accident, property and liability). The domestic insurance market is highly concentrated with the largest company, Mongol Daatgal, having a market share of 74 percent, and the two next largest companies having a combined share of approximately 8 percent.

The size of the insurance sector is far smaller than for other comparable economies and thus there is a real growth potential in the sector. Over the period 2000-2003, the annual gross premium volume increased by 22 percent in 2001, 19 percent in 2002 and 2.8 percent in 2003. However, the 2003 annual gross premium volume was only US\$5.3 million. This gross premium volume represents only



0.44 percent of Mongolian GDP and US\$2.3 per capita. The new Insurance Law, passed in 2004, is an important step to strengthen the insurance industry through improved regulation.

Index based Insurance

The proposed insurance approach to be piloted under this project is highly innovative. It combines self-insurance, market-based insurance and social insurance. Herders retain small losses that do not affect the viability of their business, while larger losses are transferred to the private insurance industry and only the final layer of catastrophic losses is borne by the government. The index-based insurance is not linked to the *dzud* event itself, but to the outcome that is of most concern – large numbers of livestock mortality. The insurance would pay out to individual herders whenever the mortality rate in the local region (*sum*) exceeds a specific threshold. Key to the approach is the availability of good quality livestock mortality data, and through the National Statistics Office, Mongolia has a 33-year time series on adult animal mortality is available for all *sums* and for the four major species of animals (cattle and yak, horse, sheep, goat) which provides the basis for developing actuarial information.

Importantly, the index based approach provides strong incentives to individual herders to continue to manage their herds so as to minimize the impacts of major livestock mortality events (as individual herders receive an insurance pay-out based on regional mortality, irrespective of their individual losses). Thus this form of insurance should have little or no direct effect on herder behavior, except perhaps to reduce the incentive to continually expand herd size as a means of reducing catastrophic losses.

2. Objectives

The development objective of the proposed project would be *to ascertain the viability of index-based livestock insurance in Mongolia to reduce the impact of livestock mortality for herders*. This would be achieved through the piloting of index based livestock insurance in three provinces of Mongolia – Bayankhongor, Uvs and Khenti. Two products would be introduced in the pilot provinces: the Base Insurance Product; and the Disaster Response Product. The viability of both products would be tested during the project.

a) Base Insurance Product (BIP) is a commercial risk product, sold and serviced by insurance companies. Herders will pay a fully loaded premium rate for this product. This product would pay out when the *sum* mortality rates exceed specified “trigger” percentages, (in the range of 7% to 10%, depending on species and location). Based on historical analysis of 33 year time series of livestock mortality data, the maximum payment for the BIP would be when mortality rates reach a specified “exhaustion point” of 30% for Bayankhongor and Uvs and 25% for Khenti (these rates will be subject to review annually, if necessary). The trigger and exhaustion point percentages have been derived from the analysis of historical livestock mortality data. They have been set to balance the



level of coverage and affordability by herders, and will be reviewed throughout the pilot implementation. These numbers will be subject to annual review and change, if necessary.

b) Disaster Response Product (DRP) is a social safety net product financed and provided by Government, which would begin payments at mortality rates exceeding the BIP exhaustion point. Herders who purchase the BIP will be automatically registered for the DRP on the same species at no additional cost. Without the purchase of at least the minimum value of BIP, herders must pay a contribution to the administrative cost of the DRP. The payout structure for DRP will be the same as the BIP.

A successful demonstration of viability during this pilot phase would provide a basis for future expansion and therefore a key outcome of the project would include essential preparatory elements, such as the formulation of an appropriate regulatory framework, a strengthened livestock statistical system, and support to insurance companies to develop linkages with international reinsurance markets.

Key indicators

The key indicator for both the BIP and the DRP would be the intention to continue to provide the products after the lifetime of the project.

For the BIP offered by insurance companies, the key factors that are expected to influence their decision to continue/expand the BIP, would include:

- the willingness of sufficient numbers of herders to purchase insurance (at commercial rates) during the pilot
- the potential profitability of the activity (compared with other lines of business), given the logistical challenges and expenses of working in remote herding communities;
- the identification and negotiation of mechanisms for transferring risk out of the country through international reinsurance markets; and
- the confidence of insurance companies in the regulatory environment and integrity of the public statistical system that underpins the insurance.

For the DRP, offered through the Government, the assessment of the viability of the approach would be informed by impact assessments, financed under the project and conducted after DRP payments are triggered, demonstrate that this approach is effective at providing targeted support to herders, commensurate with herders post-*dzud* recovery needs. For Government to continue to provide the DRP would require financing, possibly from bi-lateral and other agencies that have traditionally provided post-disaster relief in Mongolia. One major uncertainty is whether a catastrophe will trigger DRP indemnity payments during the pilot project period.



The proposed project is consistent with the recently approved Country Assistance Strategy (CAS) objective of reducing rural vulnerabilities. The development of new and strengthened systems of risk management is required to create a lower risk environment for sustained rural economic growth. The CAS states that the Bank will continue to pursue innovative approaches to reduce rural vulnerability, and clearly the proposed project is a key Bank-supported activity to fulfill this goal.

The effects of *dzud* and consequent high levels of livestock mortality have had a major impact on rural poverty. The latest survey, published in 2004, has shown that in the last few years the percentage of rural poverty has increased, to 43.2%, and now exceeds the 31.2% urban poverty. This is a reversal of the situation before the recent *dzuds* when urban poverty was most severe. It is clear, therefore, that strengthened measures are required to mitigate the socio-economic impact of livestock losses due to *dzud* in order to achieve Government policy objectives related to poverty reduction, which is a central component for the Bank CAS.

The expectation is that insurance indemnity payments would be used for productive activities including the replacement of livestock, purchases of goods and services to support risk preparedness and/or enhance livestock productivity and to allow policyholders to engage in alternative or supplementary livelihood strategies. The latter will also be stimulated by an improvement in financial services in the rural areas in which the strengthening of insurance company rural operations, through IBLI, will play a role.

3. Rationale for Bank Involvement

The commercial insurance sector in Mongolia is at an early stage of development and does not have the technical resources to develop an innovative product. The introduction of an entirely new product, such as is proposed, involves significant uncertainties and risks and would not be undertaken without external support.

The Bank has global experience of innovative approaches to insurance for catastrophic events and therefore is well positioned to support this project. Examples with relevant elements include crop insurance in India and Mexico. Another example is the earthquake insurance pool (TCIP) in Turkey, which operates as a catastrophe risk transfer and risk financing mechanism that limits the government's financial exposure to future natural disasters.

The project is also complementary to the on-going IDA-funded Sustainable Livelihoods Project (SLP), currently operating in eight *aimags*, which encompasses a package of initiatives including participatory grazing and pasture management, support to herder self-help groups and support to the hay and fodder enterprise development. The proposed project would have strong linkages to the SLP and would fill an important gap in the PRM activities, supporting herding households and the development of the livestock sector. Other donors, such as IFAD, UNDP and USAID with its Gobi Initiative, are supporting projects with similar objectives to SLP in other *aimags*. A successful pilot of



index-based livestock insurance with the possibility of subsequent extension to a national basis would, therefore, support other donor initiatives for the development of the extensive livestock sector.

4. Description

The central activity of the project would be the piloting index-based livestock insurance (IBLI) in the three *aimags* of Bayankhongor, Uvs and Khenti for three consecutive seasons (2006/7, 2007/8 and 2008/9). These three *aimags* were selected due to their geographical spread, and the relatively low historical correlation of livestock mortality. Offering the insurance over three seasons and over these three *aimags* provides a strong chance that the BIP would be triggered (in some locations) and a reasonable chance that the DRP would also be triggered.

The emphasis throughout the project will be on learning, through close monitoring of the pilots. As appropriate, the design and implementation system of the project will be tailored during the pilots, based on extensive feedback from stakeholders, to maximize the acceptability and impact.

The three annual seasons of the pilot would entail three overlapping insurance cycles each lasting 18 months. The main activities and schedule for these cycles is summarized in figure 1. In addition, the project would include initial capacity building to develop the institutional competence to implement the pilots, close monitoring of the progress of the pilots (and where necessary refinement of the insurance products), and preparations for the scaling up of the insurance after the piloting is completed.

Figure 1: Summary of main activities in livestock insurance cycle

<u>Month</u>	<u>Activity</u>
March	① Participating insurance firms in BIP sign contract with Govt; LIIP opened.
April	② April-May: selling season for insurance (by insurance firms). At same time, project finances public awareness campaign for herders and other stakeholders.
May	
June	
July	③ end-May – cut off point for insurance sales.
August	
September	
October	④ Follow up monitoring to determine insurance company and herder perceptions and learn why herders did / did not purchase.
November	
December	
January	⑤ NSO conducts annual livestock census
February	
March	
April	
May	
June	
July	⑥ January – June. dzud mortality (if any) occurs
August	
	⑦ NSO conducts livestock mortality census / survey in project <i>aimags</i>
	⑧ Any due indemnities paid, and LIIP closed
	⑨ Follow-up monitoring



The proposed project would include the following five directly linked components: i) Pilot Index-based Livestock Insurance Programs; ii) Promotion and Public Awareness; iii) Institutional Capacity Building; iv) Monitoring and Evaluation; and v) Project Management.

Component 1: Pilot index-based livestock insurance programs (USD 6.13 million)

The core component of the proposed project would be the piloting of the two index-based livestock insurance (IBLI) products. Under this component the project will support:

- *Livestock Data Collection*: undertaking semi-annual censuses that will serve as the basis for calculation of all settlements to herders and/or insurance companies;
- *IBLI Software Development*: enhancement of the existing educational software, the initial design of three operational software packages for operating the pilots, and the necessary testing, technical support and modification during the pilot period;
- *Training on Pilot Implementation*: the provision of technical support for the training of PIU and insurance company staff, together with the provision of essential materials;
- *Contingent Debt Facility*: approximately USD 5 million would be used to fund any indemnity payments under the DRP and to meet any cumulative shortfall in the Government's stop-loss provision for the BIP; and,
- *Pilot Performance, Review & Refinement*: during the pilots, close monitoring of the performance and stakeholder perceptions of the insurance products would identify design issues that may require refinement of the products. The project will provide technical assistance to initially finalize the legal and institutional arrangements for pilot implementation, and subsequently to refine the technical design and legal arrangements for implementation, as required and appropriate.

Component 2: Promotion/Public Awareness Component (USD 0.86 million)

Under the proposed project, a range of promotion and public awareness (PPA) activities would be conducted to educate key stakeholders on the details of the insurance product and the IBLI pilot. These activities will target herders and herder groups, livestock services providers (e.g. veterinarians), parliamentarians, government officials, insurance companies, commercial banks and other micro-finance institutions, NGOs and donor organizations. Under this component, key activities will be:

- *Identification of stakeholder public awareness needs and concerns*. This needs identification in the first year will inform the content and design of PPA materials, in addition to the selection of appropriate media and dissemination channels;
- *Preparation and circulation of promotional materials*. This will include easily understandable, pre-tested print-based materials;



- *Face to face education of key local stakeholders and clients/beneficiaries.* In an annual campaign in the 3 pilot *aimags*, promotion teams will be trained in product details and sales procedures, including mechanisms to reduce fraud and promote accountability, before going out to the *sums*. They will attempt to achieve the maximum possible direct contact with herders, by individual visits, bag meetings etc and will work closely with local officials and service providers;
- *Radio and TV programs.* These will utilize appropriate channels and airtimes, in order to reach targeted groups;
- *National and provincial workshops.* These will be a fora for learning, consultation, dissemination and review; and
- *Inter-sum and aimag exchange visits.* Such visits will facilitate the sharing of experiences and information between local participants in order to foster the replication of best practice.

Feedback from the monitoring and management information systems will also be used as a basis for tailoring promotion activities in subsequent years of the project.

Component 3: Institutional Capacity Building Component (USD 0.68 million)

This component would provide support to establish the institutional framework and capacity necessary for the potential expansion of the insurance product following demonstration of the viability of the concept. Under this component, the proposed project would support:

- *Strengthening livestock data systems.* The project would support the identification and testing of alternative data collection systems, based on sample surveys, with the objectives of helping NSO to reduce costs and improve accuracy of mortality data;
- *Developing legal and regulatory framework:* Activities under this sub-component would include support for developing the necessary legislation and regulation for IBLI. This would be done in close collaboration with the Financial Regulatory Committee (to be established) and/or the Insurance Supervisory Agency;
- *Examining options for nationwide expansion of IBLI:* Activities would include the preparation of a road map for livestock insurance and an assessment of the fiscal and economic implications of a national program. A country risk financing strategy would be devised to give the Government and the domestic insurance industry the time to become self-supporting by building adequate reserves across time and/or seeking international reinsurance. In addition, support would be provided for linkages with rural micro-finance activities and ongoing pastoral risk management initiatives.



Component 4: Monitoring and Evaluation Component (USD 0.27 million)

This component will be targeted at following and involving a range of stakeholders during the pilot program to track access by different social groups, monitor responses to the new products and to determine if and how herders modify behavior. Findings will be shared with related project stakeholders (i.e. government, donors, etc) to promote learning and project improvement. The M&E component will complement the technical and output-oriented MIS system, and support the PPA component, by focusing on target group perceptions, behaviors and the process and impact of insurance delivery. Key elements will include:

- A *baseline survey* undertaken early in project implementation in order to assess and document the socio-economic and pastoral risk management landscape in the pilot project areas, in addition to herder awareness and experience of insurance;
- *Annual field-based monitoring*, which will involve a purposive sample of herders/clients/agents, looking at who is accessing/buying insurance and reasons why/why not; responses to PPA activities; influence on herder risk management behaviors, etc. Interviews will also include local authorities, finance institutions, livestock services providers, local NGO representatives and rural development project staff;
- *Impact assessments*. In order to examine the social and economic consequences of the pilots, investigate the efficacy of PPA activities and feed into discussions on the future viability of IBLI, impact assessment surveys will be carried out at both the project midpoint and endpoint; and
- *Post-event monitoring framework*. In the event of a significant event and subsequent indemnity pay-out, a monitoring framework plan will be initiated to track the payout process and responses amongst beneficiaries, non-beneficiaries and service deliverers. If such a pay-out occurs during PY3, this framework will be supplemental to and coordinated with the planned impact assessment.

Component 5: Project Management Component (USD 1.23 million)

The final component would provide support to the PIU to enable the unit to function effectively and provide adequate management for the implementation of the proposed project. Support would include operational costs for the PIU, international and Mongolian technical assistance, training for project staff, communications and auditing, excluding salaries.

In addition to the central office, there will be a PIU representative in each of the three pilot *aimags*, responsible for project field activities at that level, including liaison with local government and local staff of rural development projects.



5. Lessons learned and reflected in the project design

Limited investments were made in the livestock sector during the 1990s for developing alternative strategies for mitigating the risks associated with livestock mortality. Towards the end of the 1990s, restocking projects were the main approach to economic regeneration in areas badly affected by *dzud* and to improving the livelihoods of poorer herders. While many agreed that these restocking efforts provided an important short-term safety net, the evaluations of such programs concluded that the approach was generally neither cost-effective nor sustainable in the long run.

The commercial viability of the conventional livestock insurance programs offered were also highly questionable given the inherent challenges associated with coverage for losses of individual herder households (i.e. data quality, moral hazard, adverse selection, underwriting costs, loss adjustment costs). Conventional insurance further reduced the incentive for individual herders to invest in pastoral risk management so as to reduce livestock mortality. Despite these challenges, conventional livestock insurance was often a condition of participation in “restocking” programs during the 1990s. Nonetheless, over time the experience of conventional livestock insurance associated with restocking proved unsatisfactory both for herders and insurance companies.

The IBLI has been designed to directly address some of the fundamental flaws of the previous product and with several key criteria in mind: 1) the insurance would not reward poor livestock management; 2) the insurance must be affordable by a large number of herders; 3) the insurance must be financially sustainable and profitable for private insurance companies; 4) the first products should focus on the most significant covariant risk; 5) a proper role for government should be carefully identified; and 6) the insurance should work in harmony with other initiatives, including pastoral risk management activities and post-disaster assistance.

There is no direct precedent for the proposed IBLI but the use of area-based index insurance for crop yields addresses a number of similar problems to those of Mongolian herders in that many farmers can have a crop failure from the same event at the same time (e.g., drought). Individual insurance of crop yields would also involve high monitoring costs and the risk of reducing incentives for farmers to adopt drought mitigation farming practices. Several of the key guiding principles and experiences of index-based crop insurance in countries including India, Mexico and the United States have been used to inform the design of the IBLI. For example, the Government of India has recently decided to reform the current scheme and to place it on an actuarial footing. Starting in 2006, premiums will be charged on a commercial basis and the Government's support would provide up front premium subsidies. Such a sound financial and actuarial approach aims to introduce more discipline in the program and to transfer catastrophic losses to the international reinsurance market. The IBLI scheme also uses an actuarial approach, with a clearly defined Government role and the potential for international reinsurance.



The stakeholder consultations undertaken during project preparation have shown that there is considerable interest in the IBLI, nonetheless, extensive promotion will be required to overcome negative perceptions of traditional insurance.

6. Financing

Source:	(\$m.)
BORROWER/RECIPIENT	.3
INTERNATIONAL DEVELOPMENT ASSOCIATION	7.5
JAPANESE PHRD CO-FINANCING GRANT	1.3
FIRST INITIATIVE (UK)	0.6
Total	9.7

7. Implementation

Given the limited financial capacity of the insurance industry in Mongolia, it may be unable to absorb the potential major losses under the IBLIP. It is therefore proposed to establish a Livestock Insurance Indemnity Pool (LIIP), managed by the PIU under the project, and to operate each insurance cycle as a joint venture between insurance companies and Government. The LIIP has features of both a reserve fund and risk pooling for the insurance companies. Each participating insurance company would deposit a guaranteed indemnity contribution (stop-loss exposure plus estimated reinsurance premiums) into the LIIP through an account held at a commercial bank before the insurance sales season. In addition, they would deposit the full premiums collected from the herders minus their administrative costs. The Government would offer reinsurance at an actuarially fair price on the exposure beyond a stop loss for the LIIP of 105 percent of herder premium deposited (the premiums for this reinsurance would be deposited in the BIP Reserve). At the end of the each insurance cycle, payments to the herders would be made first from the LIIP, then from the BIP Reserve and finally from the contingent debt facility (assuming exhaustion of resources at each level). Any surplus left in the LIIP after settlement with the herders, will be distributed among the participating insurers. Given that monies would be transferred from various accounts, if needed, it was agreed that a payment account would be setup to collect all these transfers and make final payments.

The IBLIP will be managed by a Project Implementation Unit (PIU) located within the Ministry of Finance. The PIU will be responsible for the overall implementation and management of the IBLIP and will report to a steering committee, chaired by either the Minister of Finance, or their designate. The committee will be made of members of the Government, private sector, and possibly academia.



The staff of the PIU will include a director, component and *aimag* coordinators, and staff with responsibilities for finance, administration, procurement, and general administration. In addition to these fulltime PIU staff, staff members from the Ministry of Food and Agriculture (MoFA), the Ministry of Justice, and the National Statistics Office (NSO) may be seconded to work with the PIU on a part time basis in order to facilitate close collaboration with their respective ministries.

As stated previously, the Government stop loss provision governed under the LIIP will limit the risks for the participating insurance companies. As a condition of participation, companies will have to make advance payments for reinsurance, thereby avoiding reserves and solvency issues, which might jeopardize any indemnity payments and/or their other lines of business. Since any major livestock disaster within the pilot could have significant fiscal implications, the positioning of the project within the Ministry of Finance, with representation from other concerned ministries and stakeholder groups, was deemed to be the best option.

As the risk assessment capabilities of Mongolian insurance companies is limited, particularly for an innovative product such as IBLI, the project will invest in the development of user friendly software and appropriate training for insurance companies and PIU staff. It is envisaged that the software will assist in ensuring that the calculations are transparent and feasible for as many potential participants as possible. Software will also be made available to the insurance sales agents in the *aimags*.

Template insurance contracts will be prepared by the project for both the BIP and DRP. The project will also arrange for the printing and distribution of individually numbered multi-part forms for use by the insurance agents. There will be four copies to each contract: a copy for the herder, one for the insurance companies and two copies for the PIU for the reconciliation and management of the LIIP and BIP reserve accounts and to maintain a comprehensive MIS project data base. Transmission of one of the PIU copies will be by the insurance companies while the second will be from insured herders, via the *aimag* PIU offices. By comparing the two copies, the possibilities of data entry errors or fraud will be reduced. There will be another set of contracts that will establish the agreements between the Government, PIU and the insurance companies. The insurance companies will be required to meet minimum eligibility criteria to participate in the IBLIP. In addition, they will need to prepare a business plans detailing their plans for implementation and management of the IBLI.

As a statutory function, NSO will continue to be responsible for the livestock censuses. The project will provide additional resources to meet the additional costs of the June livestock census, to improve access for the livestock count and to strengthen monitoring of the counting activities.

8. Sustainability

Several factors are important for the sustainability of the project, particularly in view of its untested nature. Government ownership during project preparation and commitment to implementation are critical. The project enjoys strong support as demonstrated during the Mongolia CG meetings of



November 2003, when the index-based livestock insurance scheme was endorsed as a key priority. It is an element of overall pastoral risk management as outlined in the GoM's Sustainable Livelihoods Program. Through a comprehensive consultation process, discussions have also been held with parliament and the Chairs of the Standing Committees on Rural Development and Social Policy have advanced their support for the pilot. Mechanisms for government's continued engagement include the proposed Steering Committee and the location of the PIU within the Ministry of Finance.

This pilot has been designed to test the feasibility of two insurance products, with the intention, if successful, of expansion of the BIP on a commercial, national basis, beyond the life of the project. Insurance companies will make individual decisions, based on their experiences during the pilot and taking into account the relative profitability and future administrative costs of IBLI. Through the institutional capacity building component, the project aims to utilize and strengthen government and national institutions, such as the NSO, commercial insurance providers and the overall regulatory framework for insurance.

The DRP is a social rather than commercial product which, in the event of a major disaster, may expose Government to a significant fiscal risk. Unless there is a catastrophic event early in the IBLIP, there may be insufficient data on the medium term economic and social impact of any indemnity payments to permit Government to make an informed decision on the continuance of the DRP. Other critical sustainability factors thus include the design of M&E arrangements that will allow any implementation difficulties to be addressed early in the life of the pilot, thereby enhancing the overall quality of project design. Coordination with other risk management initiatives – both governmental and NGO – will be managed by the PIU and supported by the M&E dissemination and learning workshops.

9. Lessons Learned from Past Operations in the Country/Sector

Limited investments were made in the livestock sector during the 1990s for developing alternative strategies for mitigating the risks associated with livestock mortality. Towards the end of the 1990s, restocking projects were the main approach to economic regeneration in areas badly affected by *dzud* and to improving the livelihoods of poorer herders. While many agreed that these restocking efforts provided an important short-term safety net, the evaluations of such programs concluded that the approach was generally neither cost-effective nor sustainable in the long run.

The commercial viability of the conventional livestock insurance programs offered were also highly questionable given the inherent challenges associated with coverage for losses of individual herder households (i.e. data quality, moral hazard, adverse selection, underwriting costs, loss adjustment costs). Conventional insurance further reduced the incentive for individual herders to invest in pastoral risk management so as to reduce livestock mortality. Despite these challenges, conventional livestock insurance was often a condition of participation in "restocking" programs during the 1990s.



Nonetheless, over time the experience of conventional livestock insurance associated with restocking proved unsatisfactory both for herders and insurance companies.

The IBLI has been designed to directly address some of the fundamental flaws of the previous product and with several key criteria in mind: 1) the insurance would not reward poor livestock management; 2) the insurance must be affordable by a large number of herders; 3) the insurance must be financially sustainable and profitable for private insurance companies; 4) the first products should focus on the most significant covariant risk; 5) a proper role for government should be carefully identified; and 6) the insurance should work in harmony with other initiatives, including pastoral risk management activities and post-disaster assistance.

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The stakeholder consultations undertaken during project preparation have shown that there is considerable interest in the IBLI, nonetheless, extensive promotion will be required to overcome negative perceptions of traditional insurance.



10. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment (OP/BP/GP 4.01)	[]	[X]
Natural Habitats (OP/BP 4.04)	[]	[X]
Pest Management (OP 4.09)	[]	[X]
Cultural Property (OPN 11.03 , being revised as OP 4.11)	[]	[X]
Involuntary Resettlement (OP/BP 4.12)	[]	[X]
Indigenous Peoples (OD 4.20 , being revised as OP 4.10)	[]	[X]
Forests (OP/BP 4.36)	[]	[X]
Safety of Dams (OP/BP 4.37)	[]	[X]
Projects in Disputed Areas (OP/BP/GP 7.60)*	[]	[X]
Projects on International Waterways (OP/BP/GP 7.50)	[]	[X]

There are over 30 different ethnic groups in Mongolia, of which the Khalkh are the majority (80%). Of the selected pilot *aimags*, Uvs in the far west has an ethnically diverse population, including Dorvod (40% of the population) and Bayad minority groups (35%), as identified in the social assessment carried out for the Sustainable Livelihoods Project. Khenti has a small minority Buriad population. These groups are, however, not distinguished from the majority Khalkh by language, religion or herding/livelihood practices. OP 4.20 has therefore not been triggered and a separate Indigenous Peoples Development Plan is not deemed necessary.

As the IBLI products will be available to *all* herders, regardless of ethnicity, the potential benefits of the project may be accessed regardless of ethnic identity and, given its nature, the project is not expected to have any specific effects on the minority populations. However, through the M&E component, diversity issues will be systematically monitored to track whether access for all is enabled.

No other safeguard policies related to the environment or social issues are triggered.

* By supporting the proposed project, the Bank does not intend to prejudice the final determination of the parties' claims on the disputed areas



11. List of Factual Technical Documents

Background documents:

- i) Examining the Feasibility of Livestock Insurance in Mongolia
- ii) Economic analysis of historical livestock mortality in Mongolia

Preparation documents:

- iii) Design of Index Based Livestock Insurance Program
- iv) Stakeholder Consultation and Promotion
- v) Risk Assessment
- vi) Research on Legal Framework
- vii) Ratemaking Procedure

Implementation document:

- i) Project Implementation Manual

12. Contact point

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