Subsidies for Agricultural Insurance

Governments pay over $20 billion per year
Is this a good way to spend public money?

- We don’t really know one way or the other. We know some of the benefits and costs, but no comprehensive economic (C/B) analyses since the 1980s of the producer and consumer gains from subsidized versus unsubsidized insurance.

- However, there are lessons about how to design insurance subsidies to increase the likelihood that they will achieve their purposes and be more worthwhile.

- Paper examines three types of agriculturally related insurance.
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<tr>
<th>Type Insurance</th>
<th>Main features</th>
<th>Reason for subsidy</th>
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<tbody>
<tr>
<td>Agricultural insurance</td>
<td>Insure production risks in commercial farming</td>
<td>Market failures and externalities that limit development of insurance markets. No reason for a sustained subsidy</td>
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<tr>
<td>Insurance for disaster relief</td>
<td>Compensate farmers when insured disasters occur to protect livelihoods and assets</td>
<td>Saves on disaster relief programs and speeds up payments. Can be used to encourage <em>ex ante</em> risk reduction</td>
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<td>Insurance for other policy purposes</td>
<td>Assist target groups of poor farmers</td>
<td>Makes insurance accessible and affordable</td>
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<td>Income support</td>
<td>Premium subsidy is an income transfer</td>
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<td>Protect financial lending institutions</td>
<td>Reduces risk exposure to encourage greater lending</td>
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Common problems with subsidies

- Premium subsidy exceeds the actuarially fair cost of the insurance leading to excessive risk taking
- Poorly targeted or insurance not linked to access to credit, technology and other farm inputs
- Inelastic demand for insurance leads to high subsidy costs if want widespread participation
- Worsens inequality - large farms gain the most
- Politically hard to contain or remove a subsidy
Some best practice guidelines

- Establish that the insurance is the best intervention
- Develop a clear policy statement and financing plan
- Select capable implementing agencies and insurance programs
- Cap payments
- Keep premium subsidy below actuarially fair cost of insurance. If must go over then adopt corrective measures
- Use subsidy to promote competition between private insurers
- When targeting poor farmers, partner with credible institutions that can reach the right farmers and ensure the insurance is linked to credit, etc.
- Manage intersections when programs overlap
Complications: Overlapping insurance

- Agricultural insurance
- Insurance for disaster relief
- Insurance for other purposes (poor farmers)