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MultiCat Program

GFDRR

DISASTER RISK FINANCING & INSURANCE PRODUCT NOTE

The MultiCat Program is a catastrophe bond issuance platform that allows governments to use a standard framework to buy catastrophe coverage on affordable terms through the capital markets. It is part of a broad spectrum of disaster risk financing instruments offered by the World Bank to assist member countries in planning efficient responses to catastrophic events.

Definition of Cat Bond

The catastrophe bond, or cat bond, is a fixed income security that pays periodic coupons to the investor during the life of the bond and insures the sponsor of the bond against a predefined set of natural disasters such as earthquakes or hurricanes. If a covered event occurs during the bond's life, the sponsoring country retains the bond principal to fund emergency relief and reconstruction work. These bonds pay investors higher interest rates/coupons than basic bonds to compensate for the risk of the issuer not having to repay the principal in the event of a major catastrophe. Thus, cat bonds are an efficient tool for countries to transfer some of their natural disaster risk to the capital markets at attractive prices and are a viable alternative to standard insurance coverage for less frequent but more catastrophic disasters. Cat bonds provide countries with multi-year coverage and replace the year-to-year volatility of annual insurance premiums with a fixed cost over the life of the bond.

As an asset class, cat bonds are attractive to investors because their yields are uncorrelated with financial markets. While this portends well for the development of the global cat bond market, many disaster prone developing countries are unable to access them due to the instrument's technical complexity and the expenses involved.

The MultiCat Program gives these governments access to international capital markets to insure themselves against the risk of natural disasters.

Key Features

The program supports a wide variety of structures, including the pooling of multiple risks (earthquakes, floods, hurricanes and other wind storms) in multiple regions. Each bond issued under the platform carries the MultiCat brand name and uses a common documentation and legal and operational framework.

Highlights

- The MultiCat Program helps member countries issue catastrophe bonds to insure themselves against the risk of natural disasters.
- Supports wide variety of structures, including the pooling of multiple risks in multiple regions.
- World Bank acts as arranger: Assists in formulating disaster risk management policy; offers shelf documentation; supports preparation of legal and operational framework; selects service providers.

The World Bank helps customize the bond transaction and acts as arranger, which significantly increases investor comfort. As arranger, it assists the country on its overall natural disaster risk management policy and any technical aspects related specifically to the transaction and works together with other parties involved in the deal (underwriters, legal counsel, modeling agencies, and other service providers) to ensure a smooth and efficient execution process.

Application Process

There is no formal application process. The country signs a service agreement with the World Bank, which details the characteristics of the proposed transaction and the steps to be followed in order to comply with the country's internal regulations. The work to prepare and execute the transaction begins immediately after.

Structure

A special purpose vehicle (SPV) sponsored by the government or government-owned entity issues the cat bond. The bond is placed with institutional investors through investment banks. The SPV invests the proceeds in AAA-rated assets, and pays coupons to the investors from the returns on the investment and the premium paid by the country. If no event occurs during the life of the bond, the SPV returns the entire principal to the investor at maturity. If the trigger condition is met, i.e., a covered event occurs, the SPV liquidates the assets it holds and pays the sponsor all or part of the proceeds, in accordance with the terms of the bond.

Catastrophe Bond under MultiCat Program: Standard Structure

Figure 1 The SPV receives bond principal from investors and invests the proceeds in AAA-rated assets. If no event occurs, investors receive return on AAA-rated assets plus the premium. At maturity, the SPV returns the entire principal to the investor.

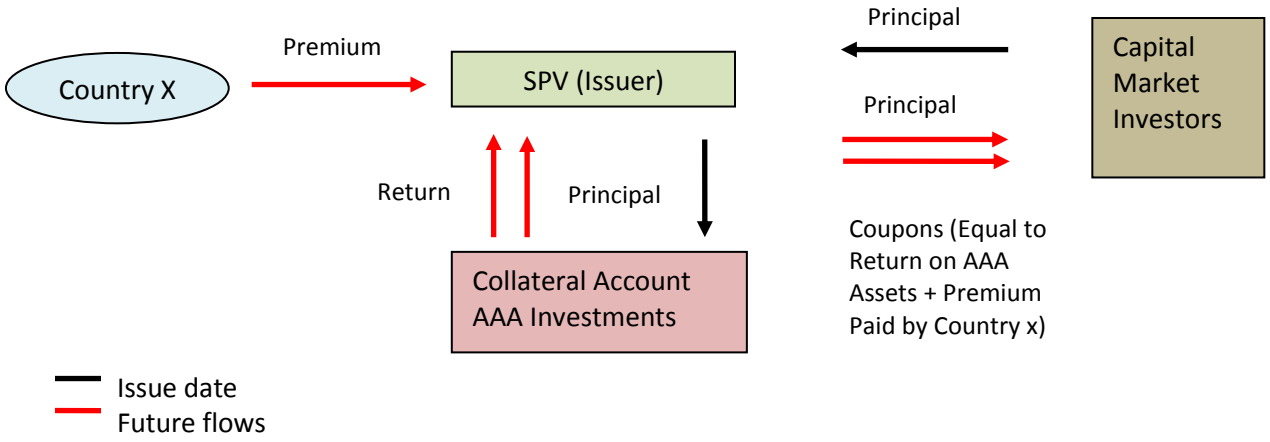
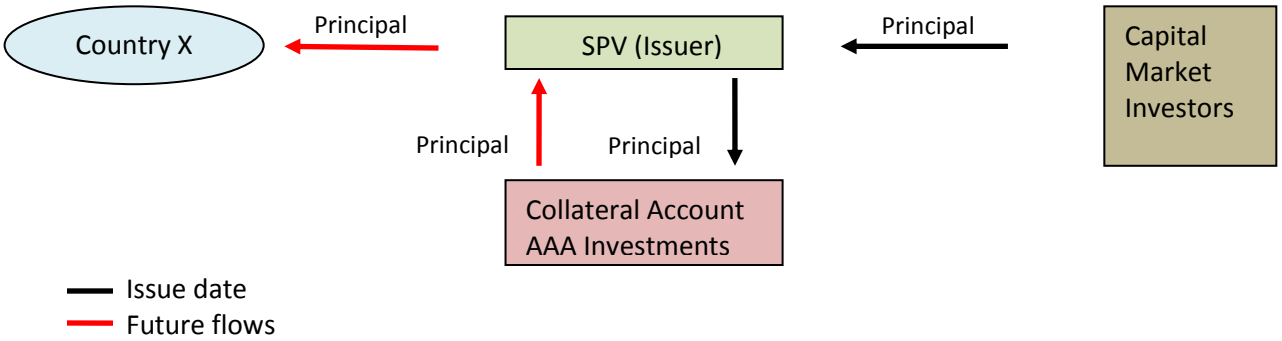


Figure 2 The SPV receives bond principal from investors and invests the proceeds in AAA-rated assets. If covered event occurs, then the SPV liquidates the assets of the collateral account and gives all or part of the principal to the country (based on the terms of the bond).



Summary Term Sheet of Cat Bond under MultiCat platform

Insured entity	Government or government-owned entity
Covered perils	Any peril that can be modeled
Trigger	Parametric, indemnity, modeled loss
Covered amount	Depending on market appetite
Term	Normally 3-5 years, but can be up to 10 years

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GFDRR is able to help developing countries reduce their vulnerability to natural disasters and adapt to climate change, thanks to the continued support of its partners: ACP Secretariat, Australia, Bangladesh, Belgium, Brazil, Canada, Colombia, China, Denmark, Egypt, European Union, Finland, France, Germany, Haiti, India, Ireland, Italy, Japan, Luxembourg, Malawi, Mexico, The Netherlands, New Zealand, Norway, Portugal, Saudi Arabia, Senegal, Spain, South Africa, South Korea, Sweden, Switzerland, Turkey, United Kingdom, United States, Vietnam, Yemen, IFRC, UNDP, UN/International Strategy for Disaster Reduction, and The World Bank.