SUSTAINABILITY AND CLIMATE CHANGE: MAIN POSITIONS OF THE AAE

RMC Webinar

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Observation of Current Situation

- The AAE is deeply concerned about the effects of the climate crisis imposing unprecedented risks
- The currently ongoing climate change is caused by human greenhouse gas emissions
- In the year 2020, global warming has reached 1.2 degrees since the pre-industrial era
- Warming beyond 1.5 degrees will increase physical consequences significantly, at approx. 2 degrees irreversible tipping points in the climate system will be reached
- Consequently, almost all countries committed in the Paris agreement 2015 to the 1.5 degree warming target.

Main Action Points for European Actuaries

We must assure that the pensions and insurance industry maintain their function by answering the three following questions:

1. How can we effectively **manage the risks posed to insurance and pension systems** from the short and long-term policy effects?
   – **social and financial sustainability**
2. How can insurance and pensions **contribute to the transition through investments and transition project insurance** as well as **payout on climate related physical risks** which are insurable?
   – **climate sustainability**
3. For climate risk borne by society which are not currently insurable, or may become non-insurable under current market conditions, how do public policies work with the insurance and pension industries to **assure society is covered** in these areas? – **climate protection gap**

1. Social and Financial Sustainability (1)

With respect to climate change we still underline the basic principle "**same risk - same capital**":

- If so-called 'green supporting' or 'brown penalising' factors are introduced in Solvency II capital requirements, they should be **science-based** and reflect the **quality of investments and the inherent risks**
- If such factors are also introduced on the underwriting side, similar **risk-based requirements** apply
- We acknowledge that the integration of emerging risks cannot rely solely on historical statistics but needs to **factor in forward-looking considerations**

1. Social and Financial Sustainability (2)

- We support the proposed initiatives that contribute to an appropriate **integration of climate risk in Solvency II** (e.g. climate scenarios in the ORSA and regular review of the standard formula w.r.t. Nat Cat scenarios)
- The role of L&H insurance and pension **ensuring financial security** in old age and to **protect against the loss of the ability to work** or to **finance medical treatments and care** should be furthered
- For savings products we support a transparent classification of savings, pensions, and investment products by **ESG criteria** and a clear and informative **sales process**

2. Climate Sustainability (1)

As long-term investors, pensions and insurance **play a relevant role in financing** the climate change transition

- Note that due to long-term investment strategies **investments cannot be restructured immediately**
- **Green supporting or brown penalising factors might not have the full effect, as risk capital often plays a secondary role in investment decisions**
- **Delayed transitioning of asset portfolios** may suffer from insufficiently deep markets at the time the transition occurs and **some assets may become stranded assets**
- We encourage pensions and insurance to **anticipate those asset transition risks**

2. Climate Sustainability (2)

As long-term investors, pensions and insurance **play a relevant role in financing** the climate change transition

- We support the **facilitation of investments in structured green bonds** on debts or loans for transition projects
- Governments and Central Banks should take their part in **providing guarantees** on such bonds where needed and **clearly structured credit risk levels** of tranches
- We support the development and the use of a **science-based taxonomy** such as the one initiated by the EU Commission, as well as the establishment of **Green Bond standards**

2. Climate Sustainability (3)

Non-life insurance can play a major role during the transition in **protecting companies against physical losses** and **providing supporting services**.

- We believe that **underwriting approaches** that **include ESG criteria** in the assessment of risk exposures are important for developing sustainable solutions that price climate change risks appropriately
- Companies should use such approaches to judge and implement effectively their **risk appetite** when pricing or agreeing to insure such risks, as well as the economic capital they need to face these risks

3. Climate Protection Gap

With **limited capacities and increasing physical risks** due to the climate change, insurers adopting well-informed underwriting processes may need to **decline some coverages**.

- **Protection gaps** are areas in which societal risks are not covered by the insurance industry,
  - either because of **lack of penetration**,
  - or because the **risks are uninsurable in profit-oriented markets**.
- The latter can only be covered by **public policy encouragement**
- We support the **early identification** of protection gaps and the **development of shared resilience solutions** between the insurance industry and public protection facilities

Conclusions

Climate change is not just a European issue. Solving the climate crisis will need **action not only from European actuaries or European insurance and pensions undertakings**. We also need a global view.

- Ideally, there should be **no worldwide inconsistencies** or local European regulatory loopholes that can be exploited
- We as the AAE stand ready to support development of comprehensive, proper carbon and pollution **accounting and valuation approaches** to make any such loopholes more transparent

Any questions or comments?