

Climate Change Conference 2007

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Introduction

The 2007 Insurance Times Climate Change Conference took place in London on the 12th and 13th March 2007. The conference was attended by approximately 100 delegates including Re-insurers, Underwriters, Catastrophe Managers, Risk Mangers, Journalists and Fund Managers.

This report will provide an overview of the conference and will go on to summarise the messages delivered by the key speakers.

Overview of the conference

The Conference took place at a highly timely moment; it followed the Channel 4 programme, “*The Great Global Warming Swindle*” and took place on the day when the Chancellor of the Exchequer and leader of Her Majesty’s Opposition both made key speeches on Global Warming.

It is fair to say that the vast majority of course delegates were present because they believe that human actions are contributing to Climate Change and that the results of Climate Change were likely to be so severe that substantial investment in changing human behaviour was worthwhile. However there was a dissenting, outspoken delegate who, throughout the conference, suggested that Climate Change was not the result of human actions but a natural phenomenon.

The conference considered various issues relating to Climate Change and these, in particular related to:

- The effects on the world and insurance if Climate Change is not acted upon
- Impact on business and investors
- United Nations Environment Programme
- Incorporating Climate Change into Underwriting
- The Scientists’ view of Climate Change
- Cutting Emissions, Carbon Markets

Each of these will be considered, within this report, in turn.

Opening Address (Stephen Byers MP)

The Opening Address was presented by Stephen Byers MP who declared that in his view the “debate is over” essentially the evidence and scientific community opinion is now overwhelming, Climate Change is happening and it is as a result of human activities. Stephen Byers referred to the evidence and recommendations in the Stern Report. In addition he referred to the level of interest from the United Nations, the World Bank and the G8 (the next meeting of which will include the World’s five greatest polluters).

Sir Nicholas Stern (Head of the Government Economic Service and Adviser to the Government on the economics of climate change has recently issued a report (The Stern Report). This report had identified that the cost of Climate Change to the World

would represent a cost of 5% of World Gross Domestic Product (GDP). The effects of Climate Change would affect the poorest and most vulnerable populations of the World. The cost of preventing Climate Change amounted to only a small proportion of the World's GDP.

Stephen Byers argued that the 1% GDP cost was well worth paying, even if one did not wholly accept that human actions were causing Climate Change the gamble of not taking the action was not worth taking. The risks associated with Climate Change were just too great to be ignored. Insurers should take note that it is calculated that a 5% increase in wind speeds would equate to a doubling of the cost of storm damage repairs.

The UK could take the stance that it is responsible for only 1% of the World's carbon emissions, anything done in the UK could be considered insignificant. Deforestation for instance contributes 18% of carbon emissions. However, the UK could and should take a lead in this matter.

The effects on the World and insurance if Climate Change is not acted upon

The effects on the World, should Climate Change not be addressed, were considered in this session. From Insurers perspective the greatest issue to be considered is the potential for a 400% rise in weather related events. In the UK alone two million properties are at risk of flooding despite the fact that the UK is one of only three economies investing in flood protection.

It is estimated that the Flood risk is being subsidised by around £1 Billion and this is not equitable. There needs to be a balance between flood protection schemes and subsidising the Flood cover premium. There is a strong argument that Insurers should play a role with scientists and the City investors in tackling Climate Change.

A change in the pattern of tropical cyclones in the Atlantic Basin has been identified; this has resulted in a continuous growth in damage and costs having to be met by Insurers. Climate Change has been identified as the cause of the change in the pattern and as a result there has been a change in the hazard, the risk and loss distribution. Vulnerability to Insurers will increase should Climate Change not be arrested.

From the Lloyds perspective, Lloyds are of the view that larger catastrophic events could be anticipated with the result that more capacity to deal with claims and more capital will be required to meet claims. The likelihood, severity, frequency and locations of losses from weather related incidents are all set to increase. When things go wrong it is human nature to look for someone to blame and the possibility of class actions against emitters of pollution and building designers could not be ruled out.

Impact on business and investors

Alan Brown Head of Investment at Schrodgers started this session with a review of how investors may respond to Climate Change. He described four possible reactions by investors as follows:

- Ethical Approach – In his view such an approach was unlikely.

- Activist – This would be the approach of retail investors, this would be decisions by buyers to buy “green products”.
- Fiduciary – This would be where there would be penalties for non Climate friendly investments and where non-green investments would be marked down.
- Amoral – This approach is where investors recognise that others will take a moral stance, even if the investor does not see the moral argument investments will be made taking into account the possible actions of others.

Alan Brown took the view that investors will invest where they can earn the highest possible return, he pointed out that the World Bank have not taken an Activist stance but more of a Fiduciary approach.

United Nations Environment Programme

The UN are taking a proactive approach via their United Nations Environment Programme Finance Initiative which involves a Public-Private Partnership to which there are 160 signatories of very large worldwide financial institutions. The mission is to “identify, promote and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations”.

The United Nations are seeking to raise awareness on current and emerging sustainability issues and trends and seek to support the initiatives of the Insurance industry to encourage a sustainable future.

The UN highlight the fact that that one billion people in the World live on less than a \$1 a day. The UN recognise that the World’s poorest will be the most severely affected by climate change. The UN see helping the poor out of the poverty trap as a fundamental role, Insurance is a vital tool for sustainable development.

The UN have set up projects for “Principles for Sustainable Insurance, this is a landmark project to develop and implement sustainability guidelines for the global insurance industry. The UN point out that where environmental, social and corporate governance (ESG) issues should be integrated into core practices of Insurers.

The UN have also considered the issue of responsible investment. By adopting ESG issues into investment policies Insurers company value will increase in the long term.

Insurance is the World’s largest industry with approximately \$3.4 trillion in annual premium revenue in addition to \$1 trillion investment income. The core strength of the Insurance industry is its risk management ESG and sustainability is the way forward.

Incorporating Climate Change into Underwriting

There was a consensus that Climate Change is here to stay and that the World is likely to experience more frequent and severe weather related events. Underwriters currently rely on historic data, as the World’s weather is changing future risks will be different. In Europe stronger winds are anticipated and in the UK there will be a much greater risk of flooding.

An interesting fact is that by 2020 about 75% of the World's population will live close to coastal areas. Modelling firms should take account for a potential sea level rise.

More specifically to the UK changing storm patterns are likely to result in hurricanes in the Bristol Channel and of course there is a flood risk to London.

The fact that a 5% increase in wind speed will double the cost of storm reparation costs was reiterated. There is an increasing number of properties being constructed on flood plains without adequate defences. In addition the building of properties affects the flood plains as drainage is altered by the addition of tarmac and concrete.

Further there has been a trend for lower quality housing and the greater addition block policies has obscured the real risk of. The agreement with the Government is that the Government will build flood defences if Insurers cover the risk.

There is a strong argument for Insurers to start sharing best practice and Insurers should note the rising trend of Business Interruption claims, a 60% rise in costs has been identified by AXA in the last four years.

Small to Medium Enterprises (SMEs) account for a large proportion of the UK's GDP. SMEs are severely affected by Climate Change and currently indicate that a 30 to 40 times by 2080. This would mean that flooding would cost the UK economy £42 billion every year at today's prices.

The Scientists' view of Climate Change

The scientists' view of the effects of Climate Change can be expressed as follows:

- 30m annual retreat of coast line in the UK
- 1m rise in sea level is threat to 1 billion people and 1/3 of World's agricultural land
- 60 cm rise would flood 26,000 km² of the US
- 1m rise in sea level would require the Thames Barrier to be Raised up to 30 days a year
- Netherlands, Shanghai, Cairo, Tokyo, New York etc all under threat from flooding

Cutting Emissions, Carbon Markets

The Carbon Markets operate in the same way as any other market. In effect the European Union were able to release Carbon credits into the market place and these credits can be traded. The price has fluctuated considerably. The starting price was €30 but has dropped to €1.50. It is also possible to earn Carbon Credits by green energy production such as Hydro Electric Power. There are risks associated with Carbon Markets as follows:

- | | |
|--------------------------|----------------|
| • Political Regulatory | Not Insurable |
| • Reliability/Confidence | Insurable |
| • Pricing | Part Insurable |

- Sourcing

Not Insurable

The benefits of Insurance are that it creates enhanced access to capital; it increases confidence in delivery, enhances credit value and provides asset protection. Less uncertainty equals less volatility.

Rt Honourable Michael Meacher MP

Right Honourable Michael Meacher MP presented a key note address to the conference. The following is a summary of this address.

Profound changes can be expected in wind, droughts and hundreds of thousands of people could die as a result of Climate Change from flooding and an increase in Malaria, dysentery etc. The World has, at most, ten years to cut pollution emissions and the UN estimates that there will be 50 million environmental refugees in this decade.

There are other matters of concern. Nuclear installations were built on coast lines far from conurbations, these areas are now threatened by rising sea levels. Waste dumps are similarly located.

The Stern report quoted three options:

- Do nothing – Result 8 degree Celsius rise in temperature resulting in billions killed. Only one tenth of the World's population could be supported.
- Stabilise Carbon in the atmosphere at 450 parts per million (Currently 430 with 2.3 part per year annual rise)
- Stabilise at 550 parts per million

Stern recommends Option three but this is still too greater risk to take and Option two should be adopted. The UK must be wholly focused in the effort to reduce Carbon Emissions. The threat faced by the UK is greater than that faced in 1940. The way Britain can tackle this is by:

- Adopting five year targets in reduction of Carbon Emissions
- Extend Carbon Trading to families
- Shift from massive power plants to local power plants
- Reduce Aircraft emissions year on year
- Produce food locally
- New buildings to have optimum insulation
- Gaining moral and political authority to put pressure on USA and, China, India etc.

Other Presentations

In addition to the foregoing the Conference looked at such issues as Physical Risk Management and Data Modelling.

It is of particular interest that the first US Insurer to issue a Policy Statement on Climate Change was AIG in May 2006. There is now much greater pressure on the

US Insurance Companies to take an environmentally friendly approach. The pressure is coming from shareholders and the greater feeling of social responsibility.

In addition, whilst the US Government has not taken lead, individual states, in particular California, are leading the way.

Summary

This report has outlined the content of the Climate Change Conference and looked at the key presentations delivered. The views expressed are those of the presenters. It should be noted that during the conference questions were taken from the floor. The overwhelming view was that the Insurance Industry has an interest in taking a lead role in challenging the behaviours that are attributed to creating Climate Change.

There is considerable work to be done and Insurers are taking steps to adapt. Insurance, as an industry is used to adapting to the challenges of new risks and the Climate Change risk must be similarly faced.