JOHN SCOTT

Head of Sustainability Risk, Zurich Insurance Company Ltd

ESG & Climate-risk: Implications for the financial sector and EU policy

Despite the pandemic crisis, environmental risks dominate the risk landscape according to the WEF Global Risks Report, for which Zurich is a strategic partner, with 4 out of the 5 top risks being environmental.

The most common perception of climate change risks is the 'physical risks' (melting polar ice caps, sea level rise, retreating glaciers and changes in severe weather patterns). Demands for rapid reductions in greenhouse gas emissions aligned with the Paris Agreement are coming from scientists, climate activists, civil society and increasingly the finance sector. This is driving climate related 'transition risks' as the global economy transforms, moving towards a net zero global economy. New low-carbon technologies are changing investor preferences and consumer sentiment. All of which requires new policy frameworks to influence supply and demand of low carbon products / services and successfully deliver the EU Green Deal.

This transformation comes with risks on a shorter time frame than the physical risks of climate change. The economic and societal impact of the "just" transition will be felt sooner than many might expect. The public and private sectors must act now and focus on developing strategies that build resilience and adapt to climate change. Only then will they be able to take steps that drive the low-carbon transition while managing the risks and opportunities that come with it.

Changes in climate risk assessment and disclosure

The Taskforce for Climate related Financial Disclosure (TCFD) framework for climate risk disclosure is now widely accepted and in some jurisdictions is now mandated for financial services companies.

Discussion and consultation are ongoing to better assess and disclose climate risks. Key issues are about the assumptions inherent in long-term scenario-based analyses, or stress tests and the implications for capital and solvency in the short-term. There are also challenges with standardizing forward-looking metrics and the lack of data on which to base quantitative assessments of climate change risks. This requires using different quantitative and qualitative tools, data and metrics to monitor and assess exposure to physical, transition and liability risks.

Lessons learned

The insurance industry has a long history of analyzing natural catastrophe risks and is addressing the complex task of building long-term climate science simulations into these models. Zurich proposes analytical and risk management tools such as climate risk advisory services to clients to better understand the impacts of climate change on their physical assets and supply chains.

EU policy priorities

Policymakers should enact legislation to continue raising awareness around protection, infrastructure, information gaps for citizens and businesses and to build adaptation and resilience through sustainable investments, sound and adequate risk management tools and metrics. Public-private partnerships will be required to accelerate the delivery of critical policies supporting the transition to a net-zero economy.

The EU Green Deal and Climate Adaptation Strategy is an important first step in this, as will be the ongoing EIOPA work on ESG considerations in pricing and underwriting.