SPECTRUM
Asset Management

ESG: Insurance Environmental Risks and Opportunities

August 29, 2022

It has been a comparatively quiet Atlantic wind season thus far. However, this does not make a trend given the significant effect of extreme weather in recent years. Re/insurers face environmental risks and opportunities as well as the challenges of Environmental, Social and Governance (ESG) and energy transition policies.

In 2021, a French regulator-led climate stress test concluded that vulnerabilities associated with physical risks could result in a multiple of current insurance claims by 2050. The strategic response by re/insurers to rising losses has varied. For example, Bermuda based Axis Capital is exiting its once prominent property-catastrophe reinsurance business. Other specialists have also scaled back to lessen associated earnings volatility, while several larger and more diversified global re/insurers have been growing their catastrophe books to take advantage of higher pricing among dislocations. Many re/insurers have also pared specific exposures such as those in California, due to regulatory challenges, and to the prominent Florida homeowners insurance market given factors such as rampant claims fraud and heightened litigation. Such issues coupled with climate trends, coastal population growth and overall inflation are key contributors to rising losses. Nevertheless, re/insurers have an opportunity to mitigate growing societal vulnerabilities by reducing protection gaps.

Insurers also continue to address the energy transition. Several insurers in Europe, representing >11% of world premium volume, have joined the Net-Zero Insurance Alliance, committing to net-zero greenhouse gas (GHG) emissions in their underwriting portfolios by 2050. Many have also made similar pledges on their investment portfolios, which is important as insurers control $trillions in assets. Such commitments can help to lessen their own exposure to assets at a greater risk of becoming stranded, while also potentially raising the cost of capital for high GHG emitting entities. This could help to encourage a safe and reliable energy transition, while potentially curtailing the effects of climate change over the longer-term.

However, industry leaders have also voiced concerns regarding ESG commitments. Regulators have been developing new disclosure requirements which impose punitive actions on violators and the US Securities and Exchange Commission (SEC) has investigated certain “ESG” labeled funds. For insurers, heightened scrutiny could subject corporate policyholders to increased litigation risk and, *e.g.,* lead to new directors & officers insurance liability claims. Also, specifically for insurers making net-zero underwriting and investing pledges, Chubb’s CEO Evan Greenberg has opined that the data available today is insufficient to properly assess in detail the GHG footprints of customer/portfolio holdings. This could subject insurers to liability/regulatory risks. Mr. Greenberg noted that his firm will reduce exposure to select high CO2 emitting industries such as coal, but he also emphasized the need to promote a safe and reliable energy transition to support Chubb’s customers in the oil and gas industry.

We view Chubb’s balanced commentary as pragmatic, particularly considering that global food and energy challenges are heightened by the conflict in Ukraine. More broadly, the insurance industry continues to play an important role in providing solutions for other evolving ESG issues, for example, cybersecurity and the savings needs of aging societies. **We are encouraged by the insurance industry’s commitment to help meet these sustainability challenges.**

Chad Stogel, Vice President
Joseph Urciuoli, Head of Research

Spectrum Asset Management, Inc. is a leading manager of institutional and retail preferred securities portfolios. A member of the Principal Financial Group® since 2001, Spectrum manages portfolios for an international universe of corporate, insurance and endowment clients; mutual funds distributed by Principal Funds Distributor, Inc.; and preferred securities separately managed account solutions distributed by Principal Global Investors, Inc.

A member of the Principal Financial Group®