THE NAIROBI DECLARATION ON SUSTAINABLE INSURANCE

Webinar 2: Dependencies and impacts for insurers' clients

December 2024

Kipkorir Koskei

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THE NAIROBI DECLARATION ON SUSTAINABLE INSURANCE

Meet your trainer: Kipkorir Koskei

Kipkorir Koskei

- He is the Director of Policy and Strategic Partnerships at the Insurance Development Forum (IDF).
- Kip has over a decade of experience in international banking, as well as delivering global insurance and risk financing initiatives.
- His career includes managing multi-million-dollar infrastructure projects in East Africa and structuring disaster risk strategies across the continent. He holds an LLM from University College London.

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Course agenda

- **Day 1** • Webinar 1: Sustainability Risk Concepts.
- **Day 2** • Webinar 2: Dependencies and Impacts for insurers' clients.
- **Day 3** • Webinar 3: Climate-related Risks and Opportunities for Insurers and the Just Transition.
- **Day 4** • Webinar 4: Sustainable Underwriting.
- **Day 5** • Webinar 5: Sustainable Investments.
- **Day 6** • Webinar 6: Sustainable Finance Reporting and Disclosures.

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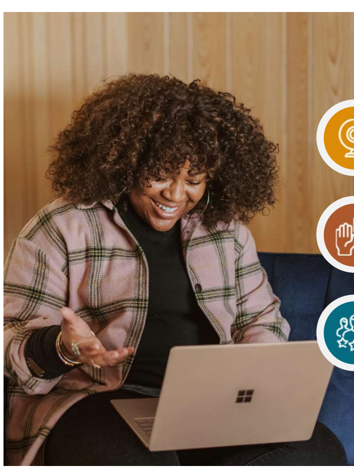
Housekeeping



- Keep your webcam turned on, it helps everybody to feel engaged!
- Ask questions by raising hand
- You are the local experts, so provide insight where possible!

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Skills you will learn

This webinar will help you to:

- evaluate ESG risks, define strategic ambitions and identify and bridge gaps;
- explore the concept of double materiality for the insurance sector;
- understand dependencies and impacts for insurers' clients;
- integrate ESG into existing client risk framework;
- define risk appetite;
- engage clients on risk mitigation.

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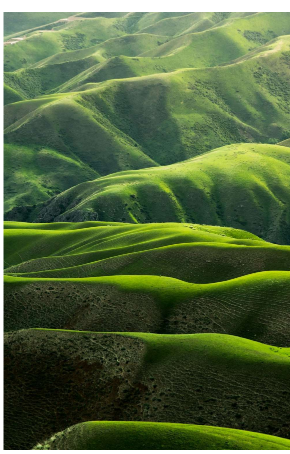
Agenda



1. **Recap Webinar 1: Develop ESG Approach**
2. **Integrate ESG into existing client risk framework**
3. **Define risk appetite**
4. **Engage clients on risk mitigation**
5. **Wrap up and Q&A**

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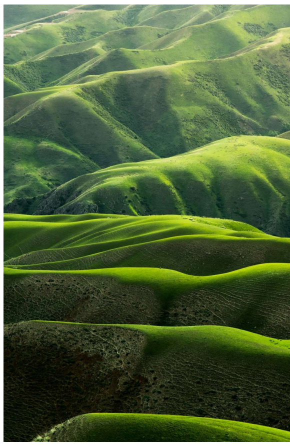

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Implementing the FSD ESG Roadmap

1 Develop ESG approach	• Evaluate ESG risks. • Determine ambition level. • Identify gaps.
2 Define client/portfolio risk framework and appetite	• **Integrate ESG into existing client risk framework** • **Define risk appetite.** • **Engage clients on Risk Mitigation**
3 Assess and escalate climate risk	• Assess Physical Risks • Identify Transition Risks • Comply with Climate-related Regulation
4 Integrate ESG into core operations - Underwriting	• Underwriting Practices. • Product development and claim management. • Client engagement.
5 Integrate ESG into core operations - Investment	• Investment practices. • Sustainable product development. • Client engagement
6 Governance framework, monitoring and reporting	• Develop governance structure. • Set KPIs. • Establish reporting mechanisms

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Step 1: Develop ESG approach

1 Develop ESG approach

- Evaluate ESG risks:
  - Establish processes to conduct a materiality assessment of ESG risks at a firm level, considering geographic exposure, business line, coverage type, economic sector, applicable regulation and client characteristics.
- Determine ambition level:
  - Define where you want to be in relation to science-based targets, industry best practices and peers.
- Identify gaps:
  - Understand your current status in the ESG journey and pinpoint gaps relative to your ambitions.

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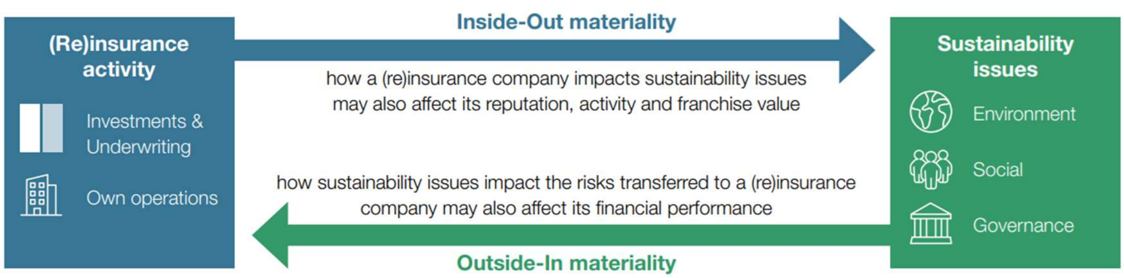
Exploring (double) materiality in the insurance sector



Source: CroForum

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Assessing ESG risks in life insurance

- Mortality: insured dying prematurely
- Longevity: insured living longer than expected and running out of money before dying
- Morbidity: insured developing a condition or contracting a disease
- Hospitalisation: insured requiring private medical treatment

Risk criteria	Mortality	Longevity	Morbidity	Hospitalisation
Air pollution	L+	L-	H+	H+
Regular health checks (e.g. blood pressure, cholesterol)	H-	L+	H-	L-

High positive "H+"	**Increases** the underwriting risk to a **high extent**
Low positive "L+"	**Increases** the underwriting risk to a **low extent**
High negative "H-"	**Decreases** the underwriting risk to a **high extent**
Low negative "L-"	**Decreases** the underwriting risk to a **low extent**
Neutral "N"	**Neither increase nor decrease** the underwriting risk
Not applicable "N/A"	The ESG risk is **not applicable** in life & health underwriting

Source: UNEP FI

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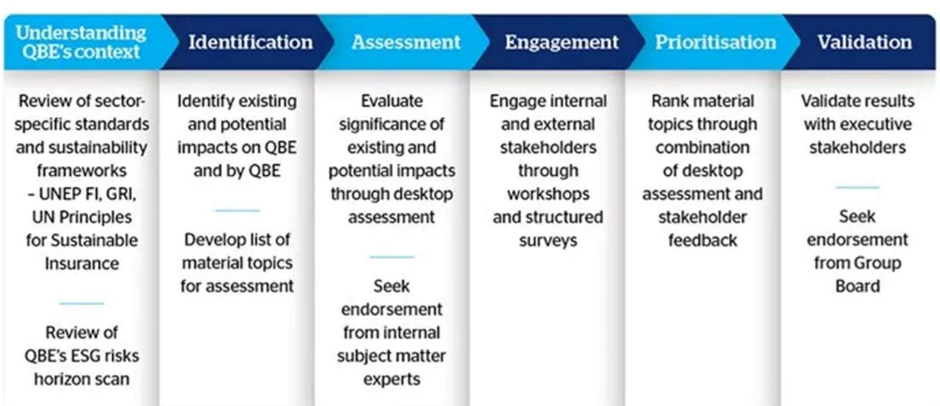
Case study: QBE materiality assessment

Level 1 - PROCESS



Source: QBE

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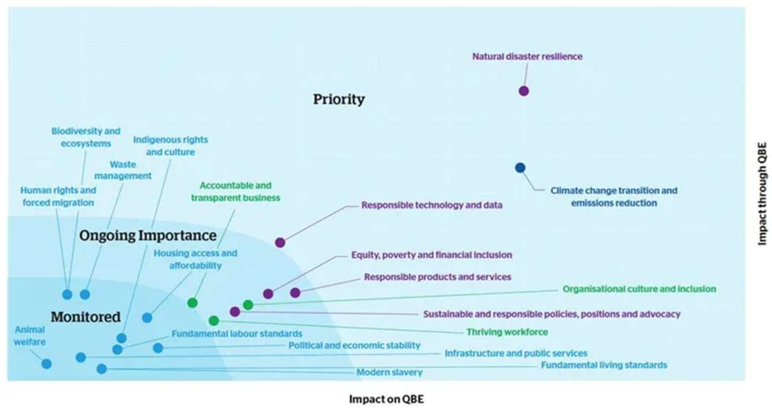
Case study: QBE matrix heat map

LEVEL 2 - QBE materiality matrix

Key:
- Focus Area 1 - Foster an orderly and inclusive transition to a net-zero economy
- Focus Area 2 - Enable a sustainable and resilient workforce
- Focus Area 3 - Partner for growth through innovative, sustainable and impactful solutions
- Monitored



Priority: high importance to stakeholders, with significant impact on the environment, economy and society. Require significant management and strategic focus
Ongoing importance: strategic significance; well-established management processes. Stakeholder interest may vary.
Monitored: relevance to stakeholders, not primary priorities. Several will benefit from activities related to Priority and Ongoing Importance topics.

Source: QBE

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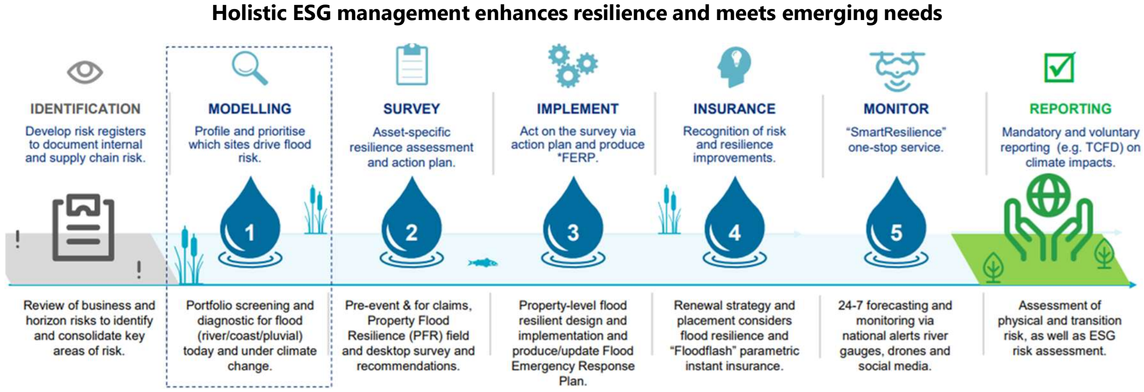
Case study: flood resilience via ESG management

LEVEL 3 – SPECIFIC ISSUE: FLOODING

Holistic ESG management enhances resilience and meets emerging needs



Source: Rob Bailey/Marsh

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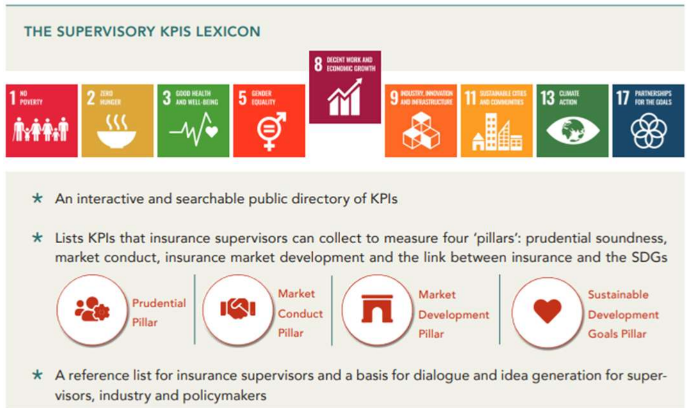
SDGs can be used for target setting

Why insurance matters to the SDGs?

- **Shields against financial shocks.**
- **Builds resilience**
- **Supports inclusive development**



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Net Zero Asset Owner Aliance support decarbonization target

Engagement targets

Set at least one KPI in two of the following types of engagement:

- Corporate-Engage 20 companies with highest owned emissions or those responsible for combined 65% owned emissions in portfolio (either directly or via membership/asset manager/service provider)
- Asset Manager-Participate in engagements led by the Alliance, or their own internal systematic approach
- Published Positions-Participate in Alliance position paper creation or write their own
- Sector/Value Chain: Participate in Alliance sector work or external sector engagement activities

Sector targets

- Intensity-based/absolute-reductions on all material sectors.
- Scope 3 to be included wherever possible.
- Sector specific intensity KPIs recommended.
- Sectoral Decarbonization Pathways used to set targets.

Intermediate targets for 1.5°C aligned, net-zero world by 2050 with real-world impacts

Sub-portfolio (later portfolio) emission targets

- 22% to 32% CO_2e reduction by 2025 (per IPCC 1.5°C SR scenarios) on equity and debt to listed corporates, infrastructure, and with the same reduction or CRREM national pathways for real estate.
- 50% (40% to 60%) CO_2e reduction by 2030 (per
- IPCC 1.5°C SR scenarios).
- Covers portfolio emissions Scope 1 & 2, tracking of Scope 3.
- Absolute or intensity-based reduction KPIs.

Financing transition targets

- Reporting climate solution investments to the Alliance and ideally showing a positive trend in climate solution investments over time (individual public quantitative progress target is optional)
- Active contributions to Alliance's Financing Transition working or consultation groups

Source: UNEP FI

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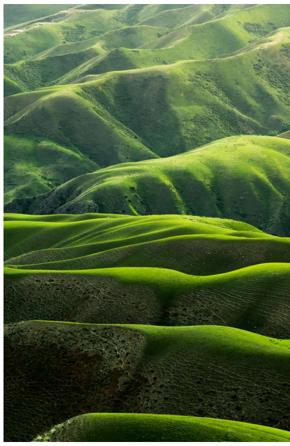

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Step 2: Define client/portfolio risk framework and appetite

2 **Define client/portfolio risk framework and appetite**

- Integrate ESG into existing client risk framework:
  - Embed ESG factors into the client risk assessment by elevating their impact on risk profiles and incorporating relevant metrics into due diligence and monitoring
- Define risk appetite:
  - Establish processes to continuously identify, assess, and prioritize material ESG risks at a counterparty and portfolio level.
- Engage clients on risk mitigation:
  - Work with clients to tailor strategies for mitigating identified ESG risks, provide guidance on best practices and resources to manage residual risks effectively.

Integrate ESG into existing client risk framework

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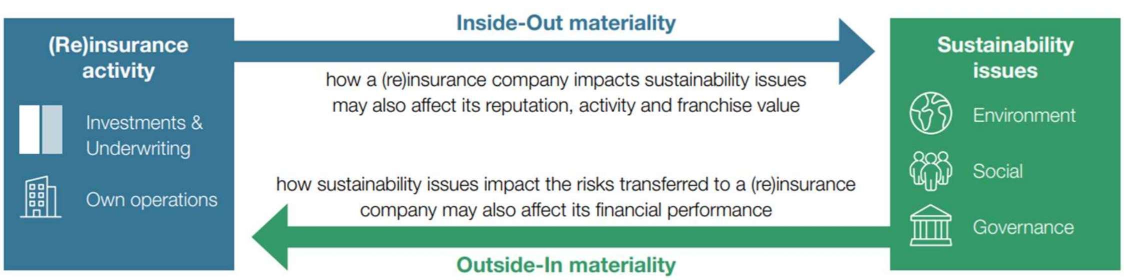
Recap: double materiality in the insurance sector



Source: CroForum

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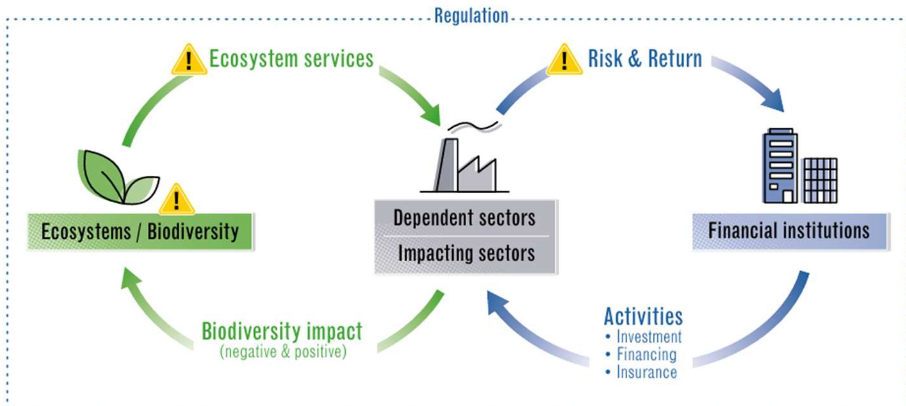
Double materiality at the counterparty level



Source: Finance for Biodiversity

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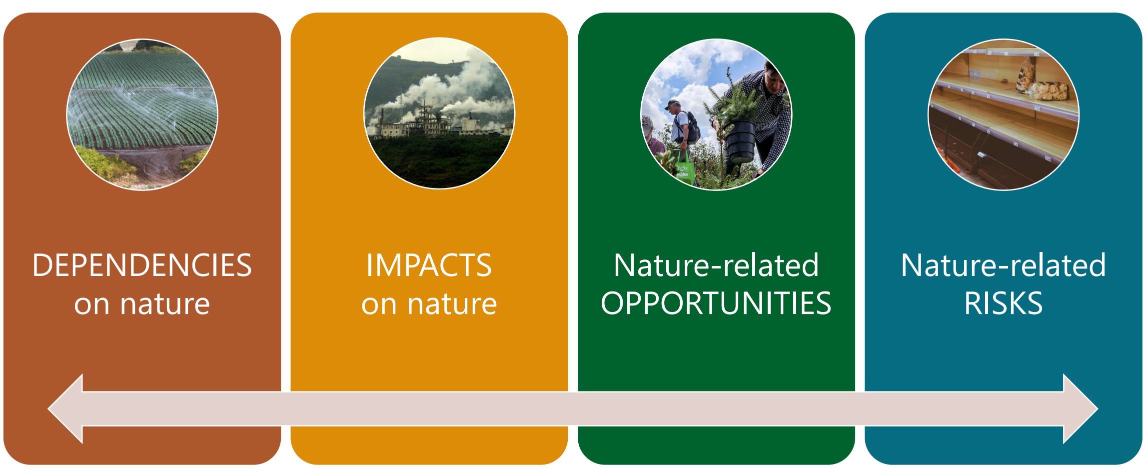
Four key sources of double materiality



Source: TNFD

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ESG risks that increase payouts for life insurers in Africa

1 **Economic inequalities & poverty, including water & sanitation issues**	• Increase mortality rates and health-related claims and premiums for life insurers among lower-income groups.
2 **Public health crisis**	• High prevalence of HIV/AIDS in some African countries has historically increased life insurance claims and affected the overall mortality experience of insured populations
3 **Pollution**	• Air pollution can lead to respiratory diseases, cancer, and chronic conditions, increasing health-related claims for life insurers, especially those with health riders or critical illness benefits. • For example, urban air pollution raises respiratory disease incidences, driving higher claim payouts..

ESG risks that increase payouts for non-life insurers in Africa

4 **Motor**	• Climate-related extreme weather events: More frequent and severe storms, floods, and heatwaves can lead to increased vehicle damage claims and higher payouts. • Shift towards sustainable vehicles: The transition to electric and low-emission vehicles may affect repair costs and payouts due to specialized parts and technicians.
5 **Property**	• Natural disasters: Climate change-induced events such as hurricanes, wildfires, and floods can result in more frequent and costly property damage claims. • Risk Mitigation Measures: Installing flood barriers, fire-resistant materials, or other protective measures can reduce the risk of damage from extreme weather events
6 **Commercial**	• Supply chain disruptions: Climate-related events can cause business interruptions, leading to increased payouts for business continuity insurance. • Regulatory changes: New ESG-related regulations may require businesses to adapt their operations, potentially leading to new types of claims and payouts in liability insurance.

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Case study: Chaucer's balanced scorecard

- Identify risk criteria across ESG pillars
- Define data points for measurement.
- Prioritize and weight criteria/data points.
- Partner for data and platform integration.
- Integrate scorecard into decision-making across all functions of the company.
- Measure and assess progress.
- Build a roadmap for data quality.
- Set future targets and metrics

Source: UNEP FI

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EXERCISE 1

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Assessing risks and impacts your client is facing

1. Go into breakout rooms, select one person to be the notetaker and use the Excel spreadsheet that was provided
2. For each sector, capture two social risks and two environmental risks you think an individual company or client may face (5 mins)
3. As a group, Discuss how these risks could impact an insurance company offering insurance to that client. (5 mins)
4. The notetaker will briefly share findings with the plenary.

AGRICULTURE

MINING

ENERGY

INDIVIDUALS (i.e. LIFE)

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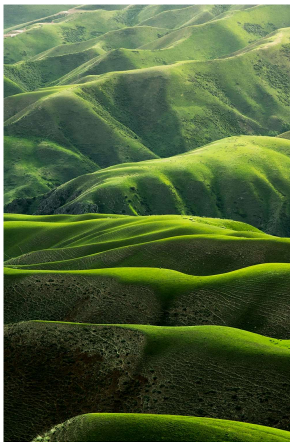

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Define risk appetite

2 **Define client/portfolio risk framework and appetite**

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- Engage clients on risk mitigation:
  - Work with clients to tailor strategies for mitigating identified ESG risks, provide guidance on best practices and resources to manage residual risks effectively.

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Two key types of ESG risk appetites

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Financial ESG risks

Focus on how ESG issues can impact insurance claims:

1. Claims frequency and severity
2. Underwriting profitability
3. Reserve adequacy
4. Reinsurance costs

Ethical ESG risks

- Focused on the broader impact of a company's activities on society and the environment.
- Objective is to evaluate the sustainability and ethical implications of a company's operations, regardless of their financial impact.

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Effects of financial and ethical risks for insurers

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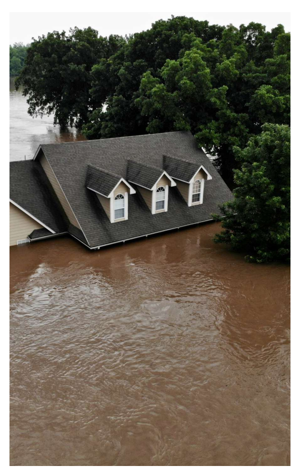
	Financial Risk	Ethical Risk
ESG risk appetite defines acceptable risk levels	Increases probability of payout	Ethical decision to avoid business
Crucial for sustainable underwriting	Impacts amount of potential claims	Based on sector's societal/environmental impact
Guides decision-making process	Quantifiable through risk models	Aligns with company values and reputation
Supports long-term business resilience	Influences pricing and coverage terms	May require predefined sector exclusions



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Impact of financial risks at a client level

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Claims frequency and severity

ESG exposure at a client level can lead to more frequent or costly claims. For example, climate change (an environmental factor) may increase the frequency and intensity of natural disasters, resulting in higher property damage claims.

Reserve adequacy

Emerging ESG risks for clients may require insurers to reassess and potentially increase their loss reserves, impacting their financial stability.

Underwriting profitability

ESG risks at a client level can erode the profitability of certain insurance lines. Social factors like changing work patterns or governance issues such as cybersecurity vulnerabilities can lead to unexpected increases in liability claims.

Reinsurance costs

As ESG risks become more prominent with clients, reinsurance for certain perils may become more expensive or less available, affecting an insurer's risk transfer strategies and overall risk profile.

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Key exclusions: unethical activities and breach of UNGC

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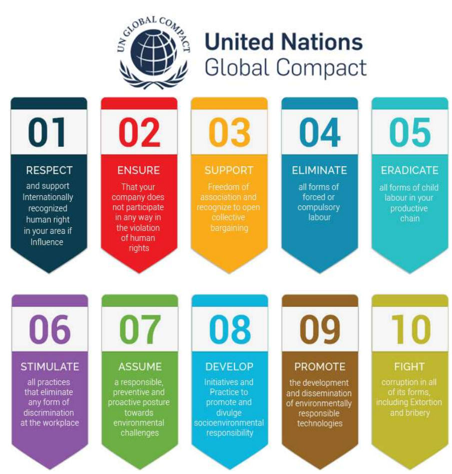

Source: Russell, Morningstar Direct, Deutsche Bank Estimates

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Case study: AXA's exclusion list

Coal, oil and gas

- Annual thermal coal share of revenues ≥15% or annual production ≥20Mt
- Annual thermal coal share of power production ≥15%
- ≥50% of production or revenues from tar oil sands
- Ultra-deepwater oil and gas exploration and development projects

Ecosystem Protection

- Companies involved in deforestation and natural ecosystem conversion
- Unsustainable palm oil production

Controversial Activities

- Controversial weapons manufacturing (e.g., anti-personnel landmines)
- White phosphorus weapons production
- Tobacco manufacturing

Ethical Concerns

- Companies in violation of international norms and standards (e.g., UN Global Compact Principles, ILO Conventions, OECD guidelines)
- Companies involved in severe ESG-related incidents

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Poll

While engaging with a client company in the mining sector, you obtain confirmation that they have been regularly involved in confirmed cases of chemical pollution.

Would you 'exclude' doing business with the company, or would you integrate the risk into the premium?

Write your answer in the chat and why you decided on that answer.

A — **Exclude**

B — **Integrate risk in premium**

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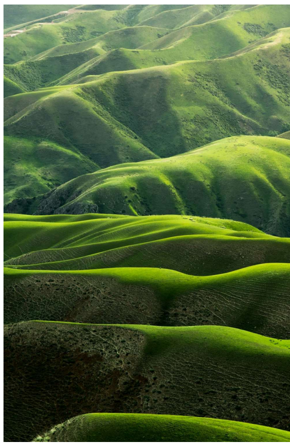

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Engage clients on risk mitigation

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- **Engage clients on risk mitigation:**
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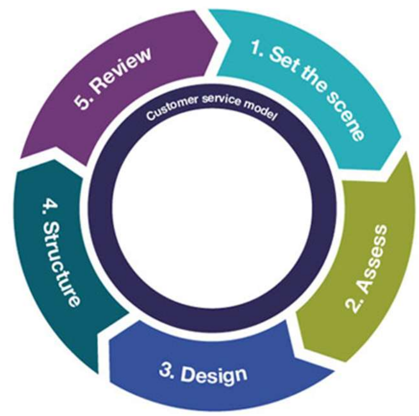
How can insurers and their clients engage on risk mitigation

Corporates need to engage with sustainability, but their level of awareness differs.

Insurers need to have structured conversations with their clients on sustainability and the risk mitigating and risk transfer solutions that support it.

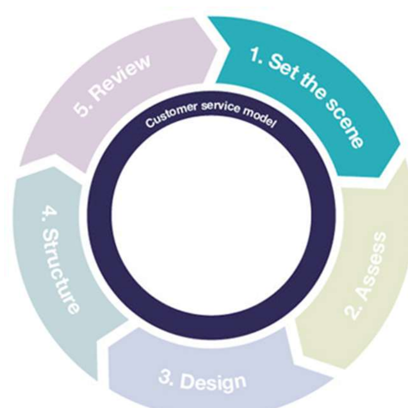


Source: CISL

Set the scene

Target outcomes of this phase

- Deeper understanding of sustainability pathways specific to client's business and sector, and assessment of the client's current position in their ESG journey
- Alignment on the role of risk management and insurance in supporting business resilience while protecting societies and natural environments
- Client openness to exploring how insurance solutions can support their sustainability transition

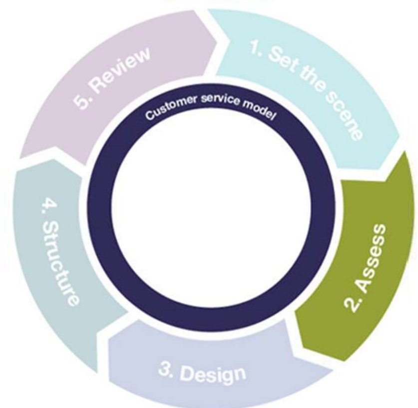


Source: CISL

Assess climate issues – target outcomes

Target outcomes of this phase

- Collection of relevant ESG risk data and current risk management practices
- Shared understanding of the baseline risk position, sustainability goals, and current progress in ESG risk management
- Mapped insurance implications of ESG risks and opportunities, alongside potential risk transfer solutions



Source: CISL

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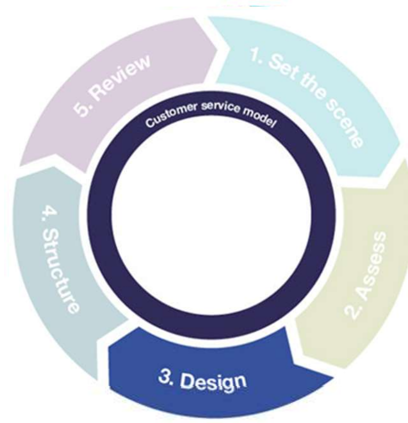
Design client transition plans for climate issues – target outcomes

Target outcomes of this phase

- Client has a comprehensive ESG risk management plan that combines prevention, mitigation, and transfer
- Appropriate sustainability and risk reduction targets established, which can be embedded into insurance structures and products
- Clear understanding of how insurance solutions can support positive environmental and social impact



Source: CISL

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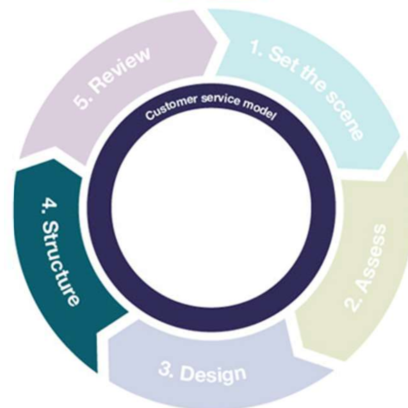
Structure financing solutions for clients' climate transition – target outcomes

Target outcomes of this phase

- Insurance solutions structured to address client's current ESG risk transfer needs while supporting long-term sustainability strategy
- Agreement on coverage terms, conditions, and pricing that reflect ESG performance
- Policy terms finalized and coverage bound with clear ESG-linked features



Source: CISL

Review progress on climate issues – target outcomes

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Target outcomes of this phase

- Insurance coverage effectively supports client's ESG risk management objectives
- Monitoring mechanisms established to track ESG performance and risk reduction
- Identification and resolution of barriers to scaling sustainable insurance solutions and risk management practices

Source: CISL

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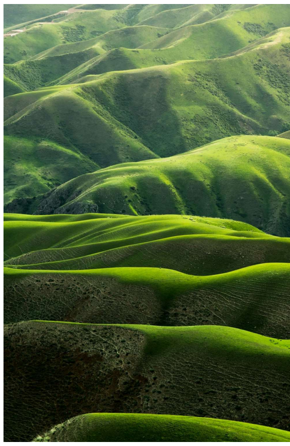

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Wrap up

This webinar has looked at

- how to develop an ESG approach, evaluating ESG risks, determining ambition levels and identifying gaps
- the concept of double materiality and the dependencies and impacts for the insurance sector.
- how to define client/portfolio risk framework and appetite, integrating ESG into existing client risk framework, defining risk appetite and engaging clients on risk mitigation.

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