Application of Climate-Related Risk Scenarios to Asset Portfolios

SUSTAINABLE INSURANCE FORUM (SIF) AND INTERNATIONAL ACTUARIAL ASSOCIATION (IAA)

William Harding

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The global leadership group of insurance supervisors and regulators working together to strengthen understanding and responses to sustainability issues.
SIF OVERVIEW

- Launched in December 2016.
- UN convened - SIF Secretariat hosted by the UNDP FSH.
- Core partner: global standard setting body – International Association of Insurance Supervisors (IAIS).
- Observer of the Network for Greening the Financial System (NGFS).
- Dynamic platform for insurance supervisors.
SIF PARTNERS

- Access to Insurance Initiative (AII)
- Financial Centre for Sustainability (FC4S)
- Financial Stability Institute (BIS)
- International Association of Insurance Supervisors (IAIS)
- International Monetary Fund (IMF)
- NGFS (Network for Governmental Financial Stability)
- UN Environment Programme (UNEP)
- UN Environment Finance Initiative (UNEP Finance Initiative)
SIF KEY ACHIEVEMENTS
SIF 2021 HIGHLIGHTS

Capacity Building Programme

CLIMATE TRAINING ALLIANCE

SUPPORTED BY: BIS IAIS

NGFS

FSI and A2ii online training modules

Partnership with the IAIS

- Climate Risk Steering Group (CRSG)
  - SIF Secretariat and key members represented on all three CRSG Workstreams: (i) scenario analysis, (ii) data, and (iii) gap analysis. SIF leading work on scenario analysis.

- SIF/IAIS Application Paper on the Supervision of Climate-related Risks in the Insurance Sector
  - SIF/IAIS launch event
  - SIF/IAIS/PSI industry webinars
  - A2ii/IAIS Dialogue series
SIF Scoping Study: Nature-related Risks in the Global Insurance Sector

- Launched during COP26 - input to TNFD.
- Press release + report viewed more than 1000+ times.
- Presented at:
  - UN PSI’s Nature-Positive Insurance Series;
  - SIF COP26 Event (900 attendees across day);
  - Banco de Mexico and Center for Latin American Monetary Studies (CEMLA) conference ‘Biodiversity and Environmental Challenges for the Financial System’.
Outlines supervisory and regulatory practices in implementing the TCFD recommendations.

Builds upon the SIF’s recognition of the TCFD recommendations as the preeminent disclosure framework for climate-related risks.

Launched during COP26.

Press release + report viewed nearly 400 times.

Part of TCFD Knowledge Hub.
Partnership with the International Actuarial Association

- Supporting the development of IAA’s series of papers and webinars covering topics from actuarial modelling to product management to the application of climate scenario analysis.

- The SIF will provide a regulators’ perspective to the development of IAA papers, and conduct webinars to discuss and promote this work.

  - SIF/IAA/Society of Actuaries in Ireland Webinar on Climate-Related Scenarios Applied to Insurers and Other Financial Institutions - held on 14th October 2021 during Climate Finance Week Ireland (400 attendees across the day)
Biodiversity and nature risks – training module

Supporting climate risk considerations within actuarial process (IAA partnership)

Capacity development CTA
Webinars: nature risk, net zero, scenario analysis, disclosure

Climate risk within regulatory capital regimes
Scenario analysis

SIF-IAIS Scenario Analysis workstream: Project plan overview

Sources of Knowledge
- Survey stocktake
- Publicly available material
- Knowledge in jurisdictions
- Knowledge in specialists (e.g., NGFS)
- TCDC

Knowledge in exercises (delivered in different means)
- Own research
- Virtual workshops

Material for each scoping item
1) Scenario Analysis Framework for supervisory authorities
2) Setting objectives and SA scope
3) Understanding Scenario Analysis Phases and setting Realistic Timelines
4) Aligning Scenario to policy and firm work
5) Scenario Design
6) Build capacity & capability where to look for help
7) Communicating results
8) Challenges in SA
9) Resources

Synthesis of material for knowledge out sessions
- Slide decks, spreadsheets, and report summaries

Knowledge out sessions
- Virtual workshops
- Hybrid workshops
- Drop-in sessions
- Feedback from sessions will inform next steps
- Material for dissemination
ICP 15 and ICP 16 include Standards for supervisors to require insurers to:

- Construct their investment portfolio so that it is adequately diversified and allows for the payments to policyholders and creditors as they are due
- Invest in a manner that is appropriate to the nature and duration of its liabilities
- Invest in assess where it can properly assess and manage the risks
- Include in their ERM framework an explicit investment policy
- Include an ALM policy in their ERM framework

Both transition and physical risk have the potential to affect investments:

- credit/counterparty default risk (eg an increase in the probability of default or loss given default)
- market risk (eg a change in the value, trend, or volatility of an asset or derivative, in particular equity, property or spread risk)
- liquidity risk (eg as a result of a sudden cash outflows as a result of a natural hazard)

Insurers may also influence the strategy and business of the firms in which they are investing, to reduce the impacts of climate change
# Regulatory scenario analysis

## Overview of published exercises

<table>
<thead>
<tr>
<th>Participation</th>
<th>BoE</th>
<th>ACPR/BdF</th>
<th>ECB</th>
<th>DNB</th>
<th>BoC</th>
<th>APRA</th>
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<td>Time horizon</td>
<td>30 years, physical risks 60 years</td>
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<td>30 years</td>
<td>5 years</td>
<td>30 years</td>
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<td>Balance sheet</td>
<td>Static, dynamic element in questionnaire</td>
<td>Static to 2025, dynamic to 2050</td>
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<td>Static</td>
<td>Static</td>
<td>Static, Proportional (dynamic) element</td>
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<td>Scenarios</td>
<td>3 NGFS scenarios</td>
<td>3 NGFS scenarios + 1 other</td>
<td>3 NGFS scenarios</td>
<td>3 shocks</td>
<td>3 NGFS scenarios + 1 other</td>
<td>2 NGFS scenarios</td>
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<tr>
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<td>Transition, physical + litigation</td>
<td>Transition, physical insurers only</td>
<td>Transition and physical</td>
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<td>Transition and physical</td>
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<td>Bottom-up</td>
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<td>Counterparty</td>
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<td>Credit</td>
<td>Credit + qual other risks</td>
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Source: Bank of England Centre for Central Banking Studies, Climate scenario analysis and stress testing webinar, 9–10 September 2021
CONTACTS

STEPHEN NOLAN
Head of Secretariat, UNDP-convened Sustainable Insurance Forum (SIF)
stephen.nolan@undp.org

WILLIAM HARDING
Head of Implementation, UNDP-convened Sustainable Insurance Forum (SIF)
william.harding@undp.org

sustainableinsuranceforum.org