

# Risk & Resilience

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November 2021

## Spotlight on environmental risk



beazley

# Introduction

At a time when the COVID-19 pandemic still has the world in its grip and the COP26 summit has delivered both more un-nerving insight into the horrors of climate change and kicked off new ESG reporting requirements, why do businesses say risks in the environmental category are bottom of their list of concerns?

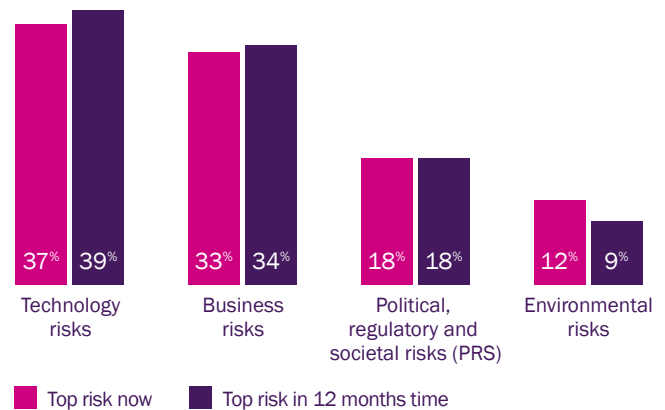
## Environmental risks rank bottom

Only 12% of business leaders in the UK and US rank environmental risks their most pressing concern in 2021. That proportion falls to 9% in 2022.

The latest report in our Risk & Resilience series explores the difference in perception and resilience amongst business leaders to environmental risks including pandemic, climate change, environmental damage, food security and energy transition.

This risk grouping represents the most rapidly evolving category of risk and attitudes to these potential perils are changing at a similar pace. We were surprised that business leaders ranked environmental risks very low in their list of risk concerns when we undertook this research earlier this year, even predicting that their concern would diminish further over the next twelve months. However, C-suite sentiment is likely to have shifted markedly since our field research was conducted as a result of a combination of factors: rising natural catastrophe severity and frequency, supply chain and energy price inflation, continued high COVID-19 infection rates and heightened regulation and litigation.

## Which category of risk is most important to your business today and in 12 months' time?<sup>1</sup>



<sup>1</sup> Percentage of companies in the US and UK ranking environmental risks as their top risk category.



## Key takeaways

- Even with COVID-19 and climate change dominating the news, executives appear to think of this category of global systemic risks as an externality, something that does not impact their bottom line.
- Businesses are focused on near term environmental risks in particular, compliance with regulation and meeting stakeholders' ESG expectations.
- There is potential for a significant disconnect between stakeholder expectations and corporate risk management priorities.
- Companies that are slow to align their operational practices and are not alert to the new regulatory landscape will face new interconnected legal, reputational and regulatory risks.
- Although energy transition risk is a key feature of debate at a global level, it is currently a business blind spot failing to register on boardroom agendas of many of the firms we surveyed.
- Given the pace and scale of environmental change and the measures announced at COP26, it is our hope that environmental risks will become more significant on corporate agendas over the coming year.

## Next steps

COP26 set some very clear priorities for governments, businesses and individuals including encouraging commitments to reduce methane emissions, prevent deforestation and protect biodiversity.

Mark Carney's coalition, Gfanz, announced that it could provide up to US\$130 trillion of capital to help the transition to net zero, while UK Chancellor Rishi Sunak announced firms will have to publish net zero roadmaps by 2023, making the UK, its public companies and financial institutions part of the world's "first-ever net zero aligned global financial centre".

It was also announced that a new board – the International Sustainability Standards Board (ISSB) – will be set up to develop a single global set of sustainability disclosure requirements to try to tackle greenwashing by companies.<sup>2</sup>

The insurance industry can play a key role in helping deliver those priorities – by supporting the transition to a greener future through its underwriting and investment policies.

We believe that firms that heed ESG principles are likely to be better risks over the long term. ESG considerations will become an increasingly significant underwriting factor in the coming years, and we are keen to build relationships with, and support clients that demonstrate strong ESG credentials at this stage.

We recognise that as an industry, we have not seized opportunities as soon as we should have. We cannot accelerate further now without leaving our comfort zone. This will require greater investment in and sharing of data and as we learn more about how ESG principles can reduce risk, we will build the lessons into our underwriting, claims and investment process to deliver innovative insurance solutions that provide additional cover to clients that perform highly against established ESG metrics.

We hope to see tangible benefits in managing **environmental risks** over the next two years and this research indicates where some of the priorities might lie.

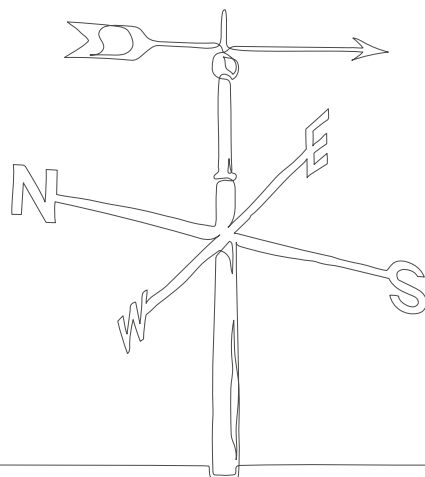
To find out more about this report please get in touch with me.



**Chris Illman**  
Head of Responsible Business  
[chris@beazley.com](mailto:chris@beazley.com)

<sup>2</sup> New body to oversee global sustainability disclosure standards | Financial Times (ft.com)

# Contents



# Ostrich or elephant – why do environmental risks lack urgency?

Despite executives ranking environmental risks as the least important category, behind technology, business and PRS (political, regulatory and societal) risks, businesses are neither head in the sand nor ignoring the elephant in the room with respect to this area of risk. ESG is rapidly moving up the board agenda.

Unsurprisingly, pandemic is rated as the top environmental risk by 35% of respondents, ahead of climate change (25%) and environmental damage (21%). In contrast, food insecurity (10%) and energy transition (8%) risks were ranked much lower.

A closer look at our research findings suggests businesses' concern is displaced into something more immediate. Regulation and legislation – including that relating to environmental risks – are cited by 36% of respondents as the top risk within the PRS (political regulatory and societal) risk grouping. With a raft of regulations coming down the track, executives will be thinking about compliance, the processes they need to put in place to ensure adequate reporting, and the reputational impact of failing to do so.

## Aligning social and corporate goals

Quarterly reporting and shareholder demands require companies to focus on the here and now - on issues directly impacting performance. While companies are not bearing the brunt of the environmental cost of their operations – for example removing plastic pollution from oceans and beaches – there is limited impact on their bottom line. At the moment, environmental risk is more a public or social issue than a concern for private enterprise; the corporate and social agendas are not in sync.

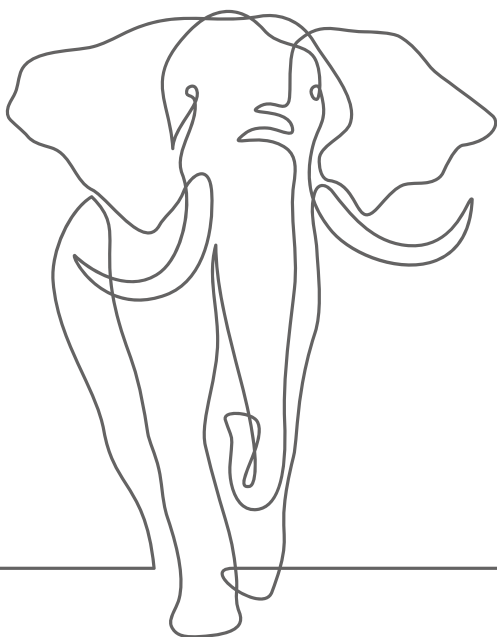
If we are to achieve the transition to a net zero economy in a way that minimises the negative impact on infrastructure, livelihoods and entire economies, however, we will need a unified approach aligning corporate and social agendas.



## Changing environment, changing perceptions

Recent events, including rising natural catastrophe frequency and severity, chaotic supply chains, soaring energy prices, the reality exposed by the Intergovernmental Panel on Climate Change's (IPCC) update on the physical science of climate change, and COP26 will have shifted people's perceptions, opinions and behaviour since our survey was conducted earlier in 2021. When we update the findings in 2022, we expect environmental risk may have risen up the list of c-suite priorities.

It's important to remember, however, that whilst ESG dominates the headlines we need to prioritise the positive tools and technologies that will allow change to happen. If we focus only on compliance requirements or doomsday scenarios, we risk turning off a large part of the global audience that needs to be engaged.



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As part of the wider ESG landscape, there is no question that environmental issues are moving up the agenda. The UK expects larger companies to publish net zero roadmaps and the IFRS has announced it will be introducing global sustainability disclosure standards via the creation of a new Board (the ISSB) and new global standards on climate-related and general sustainability disclosure requirements.



**Chris Illman**  
Head of Responsible Business

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ESG comes up on every call we do. As part of the environmental piece, we ask about carbon use and emissions along with overall ESG goals, policies and procedures. While critical for being a good corporate citizen, these factors could also have a financial impact on the business. Ten years ago there was more of a focus on large industrial clients, on their environmental policies and pollution control procedures, but now the importance of environmental protection is front of mind for most companies.



**Jeffrey Carney**  
Executive Risk Underwriter

# How to strike the right balance between compliance and progress?

Regulatory change is coming thick and fast and impacts businesses in every sector of the global economy.

## Regulatory changes are gathering pace

Companies are currently staring down the barrel of new environmental reporting legislation.

The recommendations of the Taskforce for Climate Related Financial Disclosure (TCFD) will inform two new prototype global standards: one on climate-related disclosures and the other on general sustainability disclosure requirements – both of which will be overseen by a new regulatory body – the ISSB (International Sustainability Standards Board).

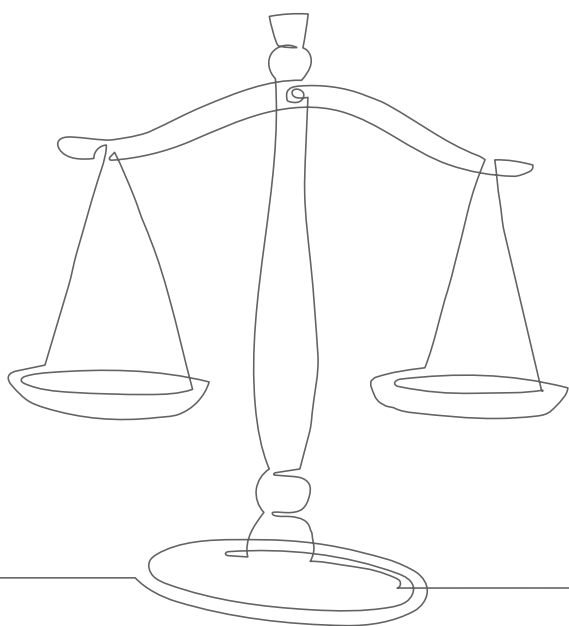
These and the new UK requirement for large companies to publish net zero transition plans by 2023 and the European Parliament Directive on Corporate Due Diligence and Corporate Accountability represent a substantial increase in expectations and in corporate environmental responsibility.

This plethora of regulation is contributing to a complex landscape which will require a high level of corporate focus to ensure compliance and manage reputation risk.

## Legal threats are mounting

While expectations to deliver growth and investment returns remain undiminished, businesses are also operating in a world where stakeholders expect better in terms of environmental risk management. Activist shareholders and pressure groups around the world are demanding that boards behave differently.

- As of May 2021 there were 1,841 climate litigation cases ongoing or concluded around the world.<sup>3</sup> This includes a Dutch court ordering an oil major to cut its CO2 emissions by 45% compared to 2019 levels.<sup>4</sup>
- In September 2021, climate groups Greenpeace and DUH warned a number of car manufacturers and an oil and gas company that they would take similar action to that brought against an oil major.<sup>5</sup>
- This year saw a case brought against a French supermarket by indigenous peoples from the Brazilian and Colombian Amazon and NGOs from France, and the US warning of environmental supply chain violations and threats to biodiversity triggering further climate change impacts.<sup>6</sup>
- At the beginning of September 2021, two French NGOs – Notre Affaire à Tous and POLLINIS – commenced the first ever legal action against a state for its failure to protect biodiversity. The case against the French government was brought during the World Conservation Congress in Marseille which called for governments to protect at least 30% of the planet by 2030.<sup>7</sup>



<sup>3</sup> Global-trends-in-climate-change-litigation\_2021-snapshot.pdf (lse.ac.uk)

<sup>4</sup> Court orders Royal Dutch Shell to cut carbon emissions by 45% by 2030 | Royal Dutch Shell | The Guardian

<sup>5</sup> Climate NGOs in Germany threaten legal action against VW, Daimler, BMW | The Independent

<sup>6</sup> Indigenous Amazonians sue retailer Casino over rainforest destruction | Reuters

<sup>7</sup> A new type of litigation risk?, Zaneta Sedilekova (clydeco.com)

There is a paradox here: while litigation is driving a heightened focus on environmental risk, it could be diverting companies away from a more fundamental consideration of the risks themselves, particularly among businesses looking to defend the status quo, perhaps by utilising the provisions of the Energy Charter Treaty (ECT) which provides a mechanism for companies to sue governments for compensation for lost profits due to policy changes.<sup>8</sup>

Those companies that get the balance wrong risk being tied up in lengthy legal cases and subject to substantial fines. Others may see legal pressure as a stimulus for meaningful change in how they operate.



In the US there have been attempts at climate litigation – municipalities filing suits against major oil companies for example on the premise that their product has caused emissions that have contributed to climate change which in turn has caused property damage due to flooding and weather related catastrophes. We are still in the early stages of this type of litigation and its potential impact could have far reaching impacts for many lines of insurance as well as companies' reputations.



**David Schechter**  
Environmental Claims Manager

## ESG concerns dominate

The rising pressure on companies to provide guidance about their environmental, social and governance (ESG) credentials is both an opportunity and a risk.

On the one hand it clarifies what is expected of companies. On the other it poses risks that businesses, in their haste to comply with new regulations, exaggerate their green credentials or release inaccurate, misleading or misstated information, which could in turn result in shareholder or derivative suits. Activists and regulators alike are intensifying scrutiny on how companies disclose exposure to climate change. Introducing new regulations makes it clear what companies are expected to do, but difficulties arise when you get a spiral of public opinion and pressure driving ever more regulation. This can lead to issues in terms of reporting and misrepresentation, and the potential for litigation.

Companies need to ask themselves searching questions about how their business is dealing with environmental concerns. The insurance industry also needs to ask questions about how companies are monitoring and managing risk in these areas and this should certainly be part of every D&O renewal meeting discussion.



Already there have been claims where a business has suggested that a product or production process is greener than it really is. That generates a reputational issue which impacts share price. That in turn creates the opportunity for a class action. The trend is gathering – the more public opinion pushes for greener, more environmentally friendly products; the more companies want to be seen to be ESG friendly – and the more likely they are to over-estimate their capabilities.



**Catherine McCabe**  
Focus Group Leader,  
International Management Liability,

<sup>8</sup> Secretive court system poses threat to Paris climate deal, says whistleblower | Energy | The Guardian



# Have businesses got their priorities wrong?

Pandemic risk was clearly the top concern at the time our research was conducted, but it was surprising that climate change and its consequences – energy transition risk and food insecurity – were ranked so low compared to others.

The UK in particular experienced well publicised difficulties in regard to energy transition and food insecurity in the autumn of 2021, suggesting the low resilience score awarded by UK leaders to these risks (only 32% felt very prepared to anticipate and respond) was well founded.

US respondents are generally more confident than their UK counterparts on their resilience to these risks, by around 10 percentage points on average, reflecting a broader pattern of greater conservatism in the UK compared to the US across our research.

## All sectors' attitude to environmental risks

All respondents



UK respondents



US respondents



■ Climate change
 ■ Environmental damage
 ■ Pandemic
 ■ Food insecurity
 ■ Energy transition risk

Percentage of US and UK executives ranking this their top risk rounded to the nearest whole number.

## All sectors' attitude to environmental resilience

All respondents



UK respondents

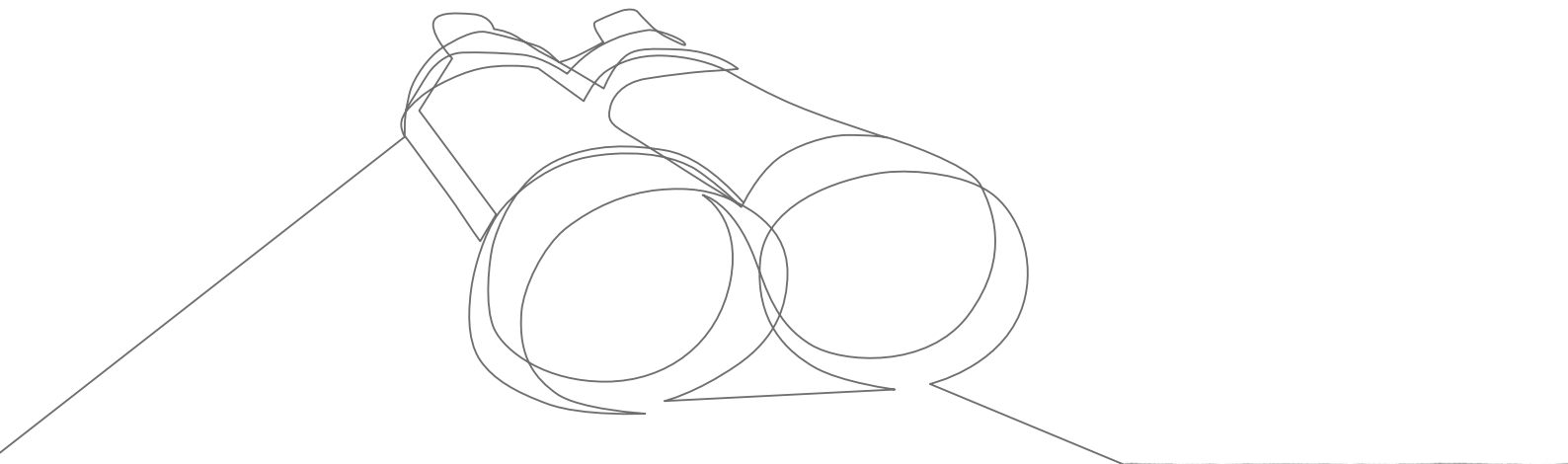


US respondents



■ Climate change
 ■ Environmental damage
 ■ Pandemic
 ■ Food insecurity
 ■ Energy transition risk

Percentage of US and UK executives feeling very prepared to anticipate and respond to environmental risks rounded to the nearest whole number.



# Pandemic risk is a concern but resilience is strong

Energy, financial services and manufacturing business report the highest levels of concern regarding pandemic risk.

Unsurprisingly, pandemic was the clear leader in terms of the environmental risk when our research was conducted in the teeth of global lockdowns, with a median of 35% of businesses ranking it their top risk.

But the sense of resilience to the pandemic was surprisingly strong. At 44%, the median level of resilience to pandemic risk was the strongest of all risks in the environmental category, reflecting the fact that the firms we surveyed were relieved to have survived the first year of lockdown.

Lockdowns may have been unpopular – but they bought time for vaccine development and as a result, confidence levels rebounded.

Energy & utilities feel greatest risk, but reveal highest resilience scores

As the pandemic took hold, energy and utility businesses were in the vanguard of sectors most significantly affected by its impact on society with 41% of executives ranking this their top risk. As populations stayed home, the collapse in demand for fuel at one point saw the price of oil plummet to minus \$37/barrel. Confidence was strong that economies would recover, particularly in the UK where the government was very much on the front foot with economic support programmes.



Sentiment varies by sector and risk. Food and beverage companies are worried about food insecurity risk, energy and utilities feel confident that they are resilient to climate change and heavy industry that they can handle the threat of environmental damage. But environmental risks can't be approached in silos. They are becoming increasingly interconnected and unpredictable – companies in every industry need to take a holistic approach to understanding, managing and mitigating against them.



**Chris Illman**  
Head of Responsible Business



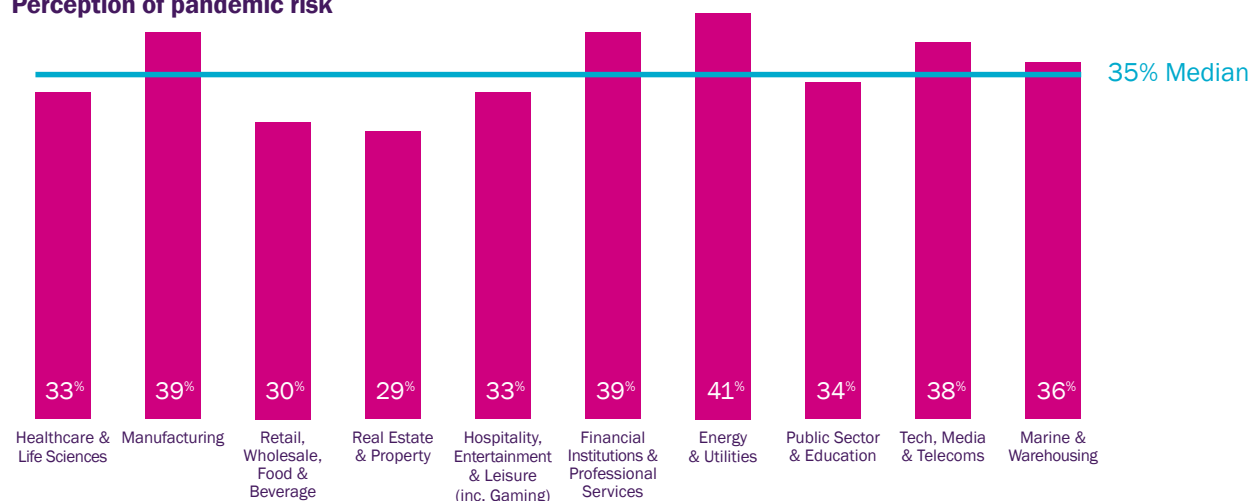
## Government action bolsters financial services' confidence

As inventory swelled, oil traders grew increasingly concerned not just over pricing, but over the world's capacity to store crude oil. Banks and pension funds were acutely worried by similarly fundamental risks – the very real prospect of a global recession and a collapse in the value of assets. The sector was the second most concerned by pandemic risk, rated top by 39% of executives. Government interventions to support the economy provided confidence however that the impact of the pandemic would be well managed, particularly in the US.

## Manufacturer sentiment reveals cross-Atlantic split

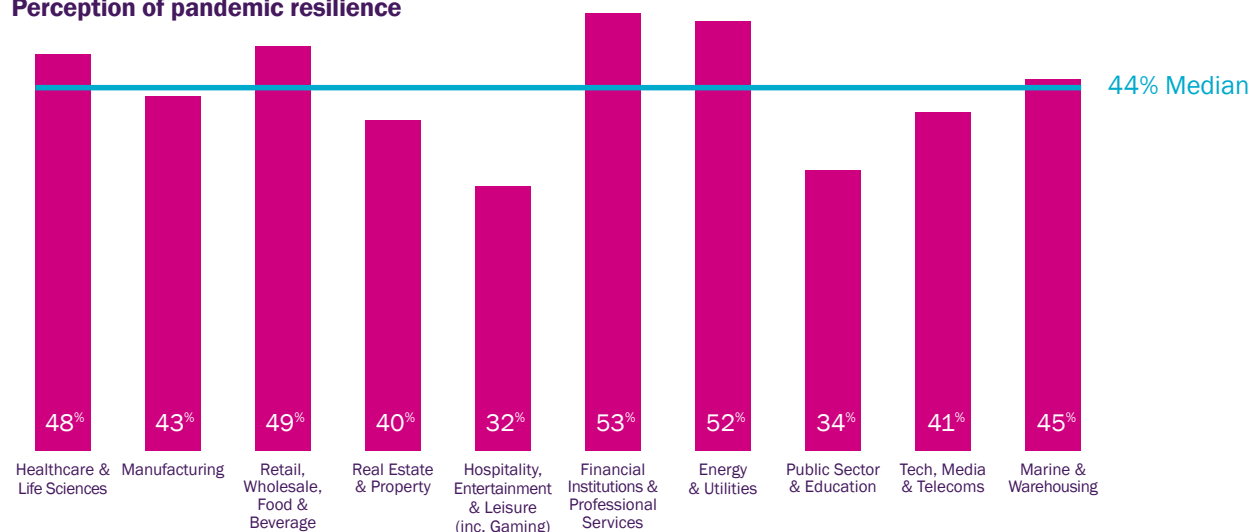
Manufacturers of every kind were buffeted by fast-changing demand dynamics, workplace restrictions and of course supply chain issues during the high points of the pandemic. As we move out of the crisis phase of the pandemic – not all manufacturers have experienced a resurgence in demand. However, US manufacturers are notably more bullish with 59% of executives feeling very prepared to anticipate and respond to this risk, compared to 34% in the UK.

### Perception of pandemic risk



Percentage of UK and US companies ranking the selected environmental risk top, 2021. Median line indicates the mid-point of the data set across all industries surveyed.

### Perception of pandemic resilience



Percentage of UK and US companies ranking the selected environmental risk top, 2021. Median line indicates the mid-point of the data set across all industries surveyed.

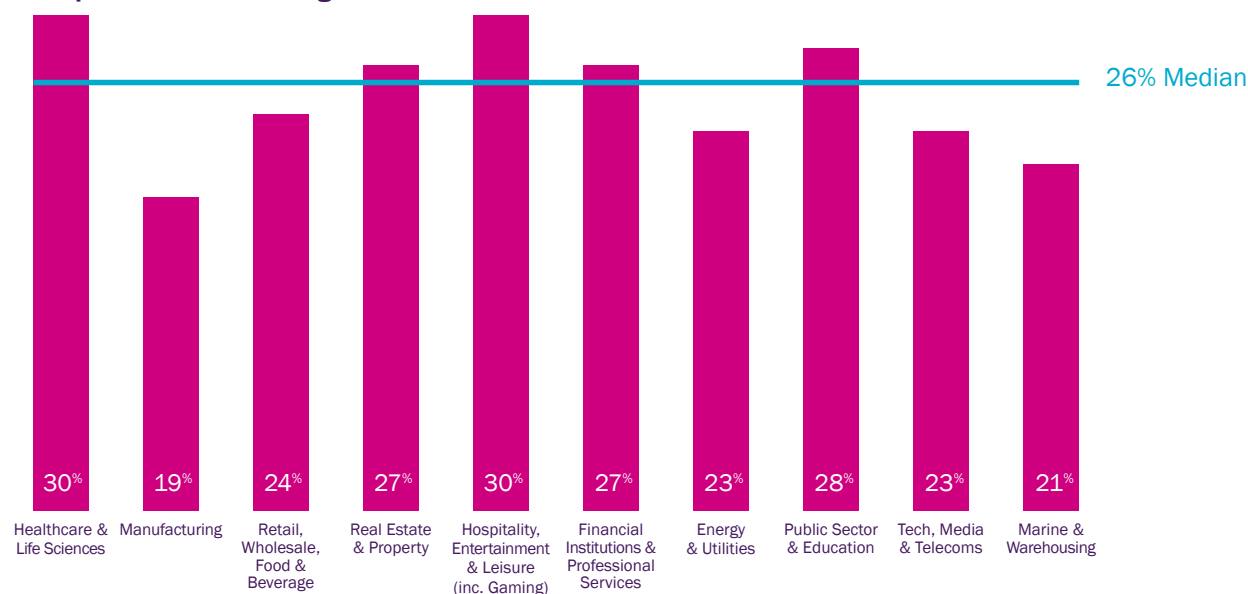
# Resilience to climate risk is weak

Climate risk is perceived to be far less acute than pandemic risk by businesses on both sides of the Atlantic with only 26% of businesses ranking it their top risk.

With a median of just 38% of businesses overall feeling 'very prepared' to combat climate risk, our research reveals it is one of the risks to which businesses feel most vulnerable.

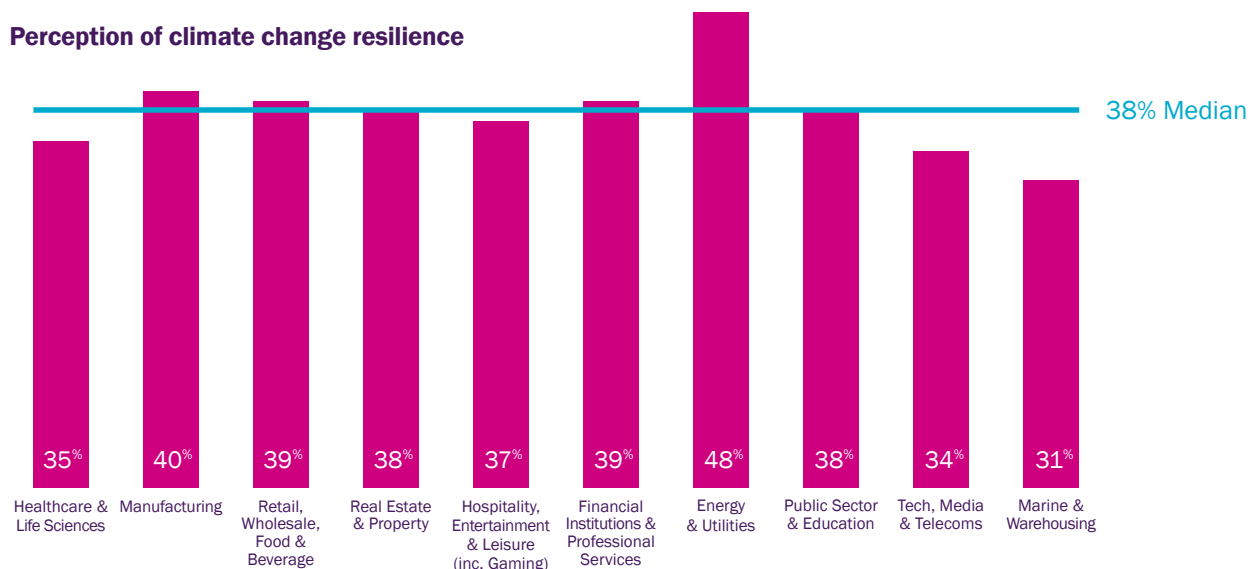
UK businesses in particular are lacking in confidence – a median of just under one third (32%) feel 'very prepared' – maybe because broadly speaking they are subject to less frequent and severe catastrophic climate impacts than their US counterparts. Only in recent years has Europe seen an increase in extreme climate related catastrophes, with stark examples including the recent floods impacting Germany, Belgium and the Netherlands and the wildfires in Greece. Given the spate of such events since this research was undertaken, attitudes will have changed with perception of climate change as a risk likely to have risen with resilience to it moving in the other direction.

## Perception of climate change risk



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
Median line indicates the mid-point of the data set across all industries surveyed.

## Perception of climate change resilience



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
Median line indicates the mid-point of the data set across all industries surveyed.

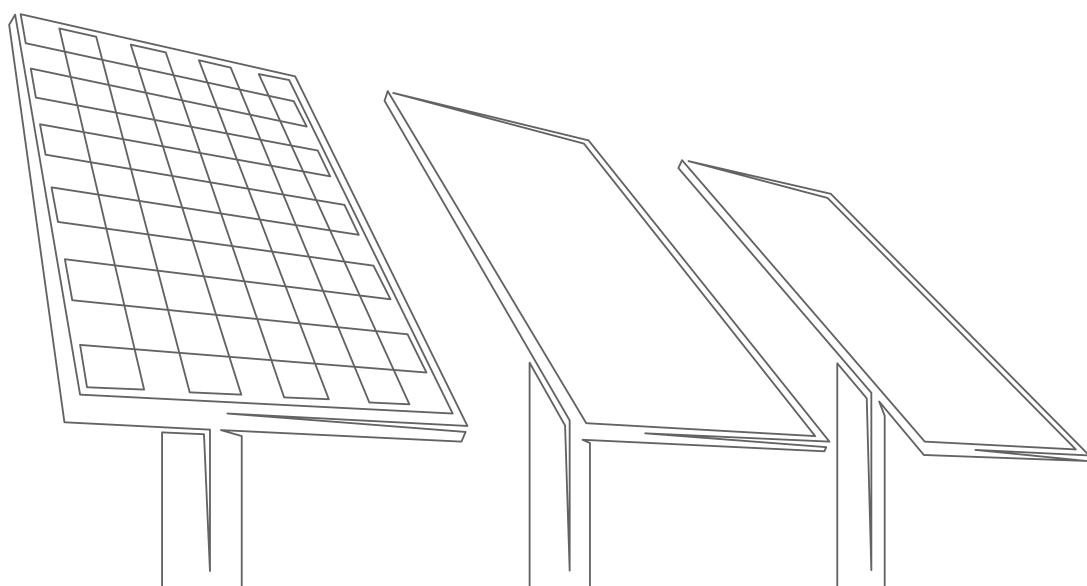
## Energy firms ahead of the curve on climate change

Energy and utility businesses show interesting responses on climate change. They are both notably less concerned than other sectors – with only 23% overall ranking this their top risk. However almost half (48%) are resilient – or very prepared to anticipate and respond. Climate is an existential risk for every business, but energy and utility companies have had some of the most forceful legal and regulatory interventions. This, combined with their position at the forefront of the energy transition has put them ahead of the curve in terms of their strategic response.

## Marine and warehousing least prepared

The sector least prepared to manage climate risk is marine and warehousing. Supply chain risk was a growing concern for businesses everywhere even prior to the impact of pandemic lockdowns, as climate change places stress on infrastructure that was never designed to deal with the extreme high temperatures, flooding, ice and wind damage that are now becoming routine.

The predictability of these events is less certain, but they will in all likelihood become more frequent: perhaps moving a ‘1 in 100’ event to more like an annual occurrence, by the end of this century.<sup>9</sup>



<sup>9</sup> IPCC report points to more intense hurricanes in future: KCC ([insuranceinsider.com](https://www.insuranceinsider.com))

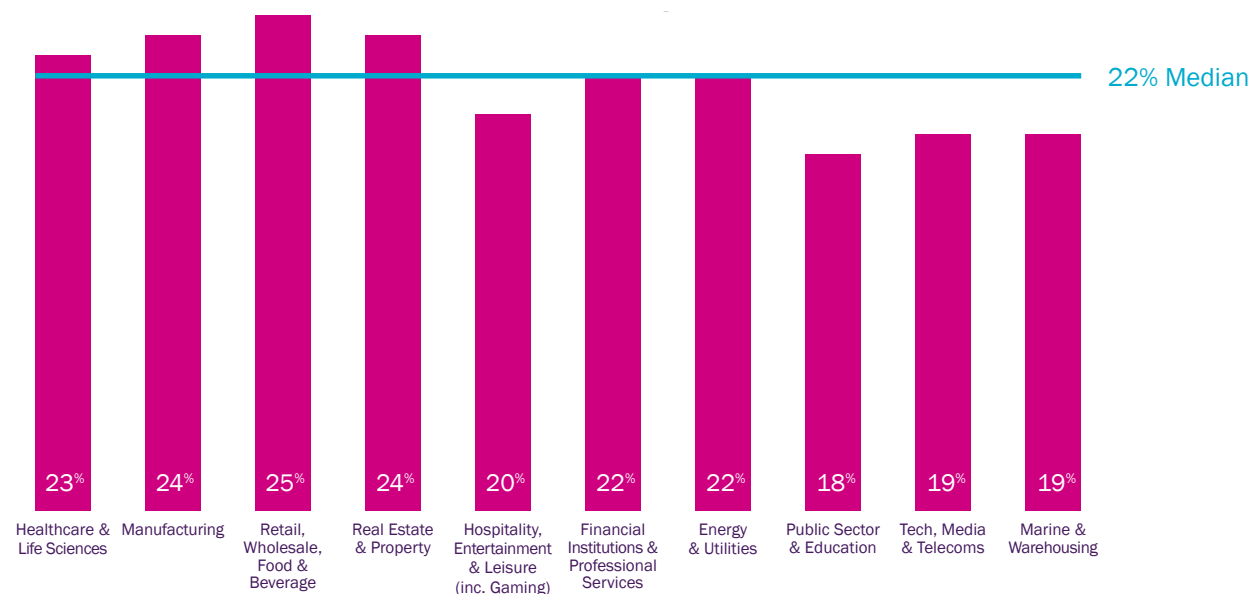
# Environmental damage stats speak to insurance success

In insurance terms, environmental damage is perhaps the most traditional and best understood of the risks in this category.

Environmental damage is ranked the leading risk by just over one fifth (22%) of businesses, but a median of 41% report they feel resilient and very prepared to manage a risk for which insurance mitigation has long been available.

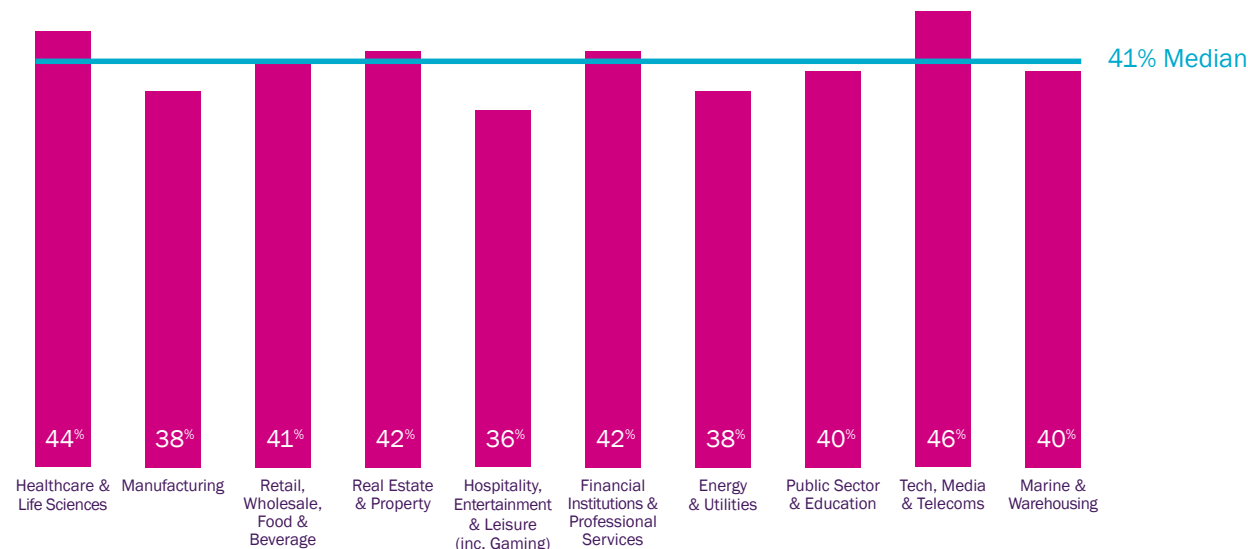
The risks of environmental liabilities occurring are increasing in the face of natural catastrophe events, as seen post Hurricane Ida, when a petrochemical refinery began polluting excessively. Maintaining that resilience might need ongoing risk engineering and management plus regular policy wording reviews to ensure the same comprehensive insurance products remain available.

## Perception of environmental damage risk



Percentage of UK and US companies ranking the selected environmental risk top, 2021. Median line indicates the mid-point of the data set across all industries surveyed.

## Perception of environmental damage resilience



Percentage of UK and US companies ranking the selected environmental risk top, 2021. Median line indicates the mid-point of the data set across all industries surveyed.

## Retailers, food and beverage firms rank environmental damage highest

Retail, wholesale, food and beverage companies rank environmental damage their most pressing concern in this category, with a quarter saying this is their top risk. Any kind of pollution incident, particularly one that affects the soil or ground water is of course going to be particularly detrimental to food and drink producers. UK producers are the most concerned and the least resilient to this risk. US businesses are both less concerned by the risk and 21 percentage points more resilient.

## Heavy industry shows strong resilience

Heavy industry, oil and gas and manufacturing have traditionally been the sectors most associated with environmental risks and all are near the top end of the scale in terms of prioritising these risks with 22% of energy companies ranking this risk top and 24% of manufacturers. Perhaps because of triggering environmental incidents and the associated litigation, neither sector scores very highly on the resilience spectrum compared to other sectors, with 38% feeling 'very prepared' to anticipate and respond to environmental risk.

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As an industry we have understood the threat of environmental liabilities for many decades and have created solutions that aim at delivering positive outcomes for the environment, coupled with protection to enable businesses to operate in an effective but responsible way. The challenge we now face is ensuring we can find a sustainable path that maintains that same high level of protection as climate change increases the occurrence of natural catastrophes and creates events, such as flooding and migration, that lead to new and different exposure patterns.



**Jayne Cunningham**  
Focus Group Leader  
Environmental Liability

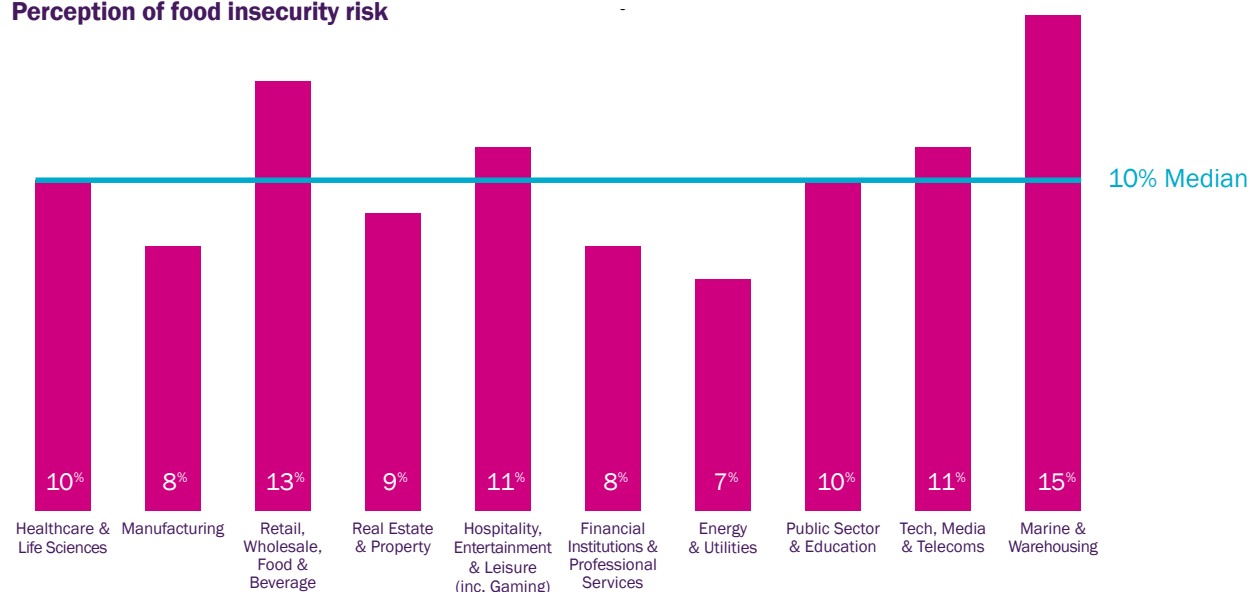


# Food insecurity is crystallising

The combined impact of pandemic and climate change means that food insecurity risk is now becoming a fact of life.

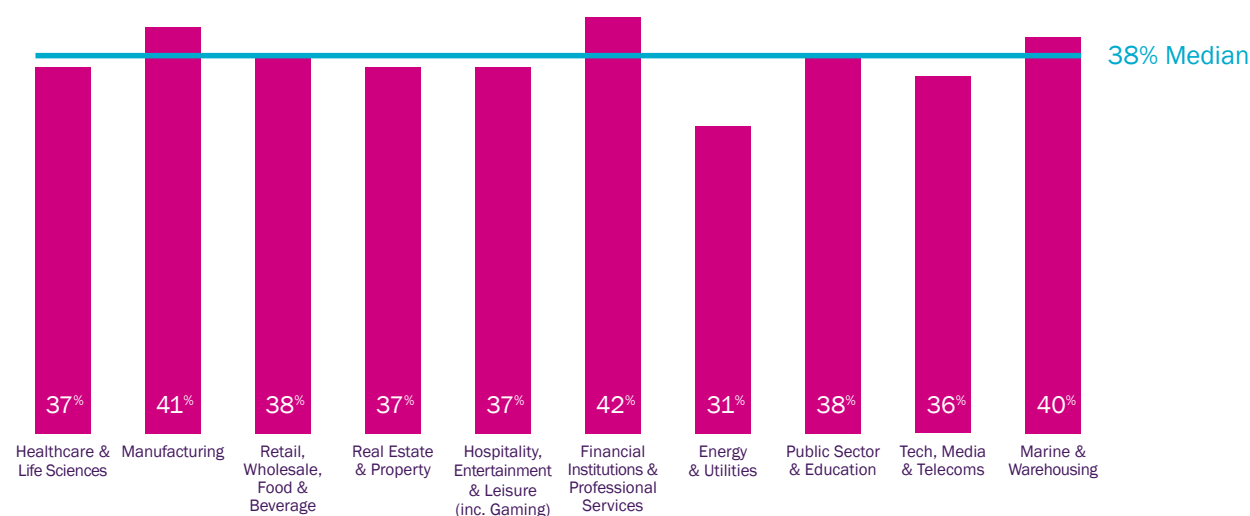
A combination of climate change impacts all round the world in terms of drought, wildfires, storms, flood damage and rising seawater levels are diminishing the stock of land suitable for agriculture. Biodiversity is also in retreat as land is increasingly used in unsustainable ways – for example as part of a monoculture – or inefficiently to grow crops (animal or vegetable) that require high levels of water or other resources that are in short supply.

## Perception of food insecurity risk



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
Median line indicates the mid-point of the data set across all industries surveyed.

## Perception of food insecurity resilience



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
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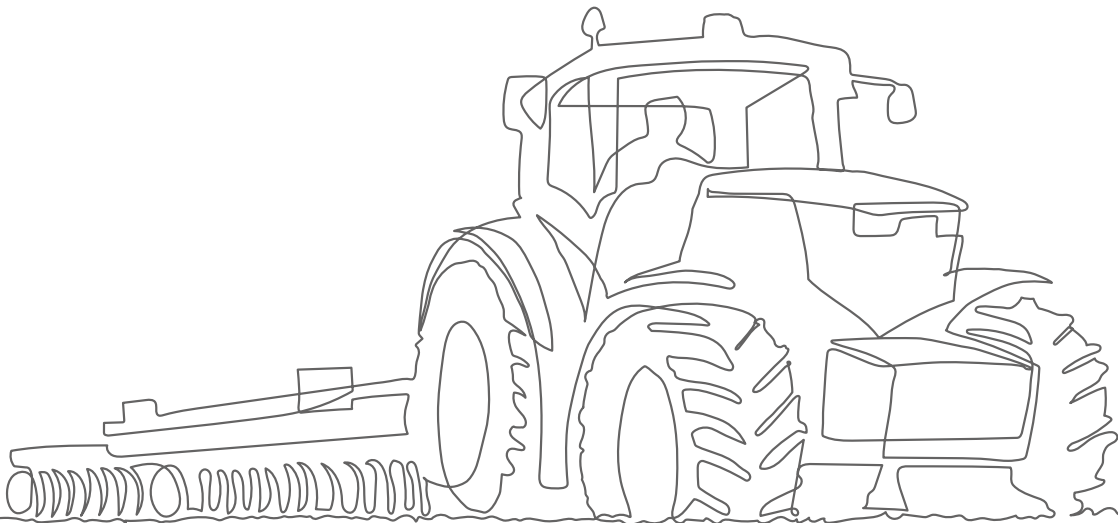
## Uncertainty impacting resilience

The retail, wholesale, food and beverage sector is the most concerned by food insecurity risk and rightly so as it is their core product, with a median of 13% of businesses rating this their leading risk in this category. Given the uncertainty around the extent of the impact of increasing extreme weather on staple crops such as rice and wheat, they should also be concerned about their resilience to this risk. Currently, only 38% of businesses in this sector feel 'very prepared' to manage food insecurity risk.

Meanwhile, a French supermarket is believed to be the first company facing action for sourcing beef in a way that is deemed to be contributing to deforestation, causing a threat to biodiversity and contributing to climate change.<sup>10</sup> We have already seen how a case against one oil major (is encouraging copycat actions – similar developments here will intensify food insecurity risk.

## Food insecurity will rise up the risk agenda

A combination of factors including policy changes and new legal precedents, together with growing awareness of how consumption of products that negatively impact the environment can ultimately lead to food insecurity will lead to the issue rising up the board agenda in the coming months.



<sup>10</sup>Amazonian groups sue French supermarket chain over deforestation - BBC News

# Energy transition risk fails to register

Despite the fact that energy transition risk is a key feature of debate at a political level globally, it fails to make the boardroom agenda in the US or UK.

A median of just 9% of businesses say it is their top risk in this category, falling to just 6% in the US. Nevertheless, a median of 41% feel 'very prepared' to anticipate and manage the risk – with US sectors feeling strikingly more secure.

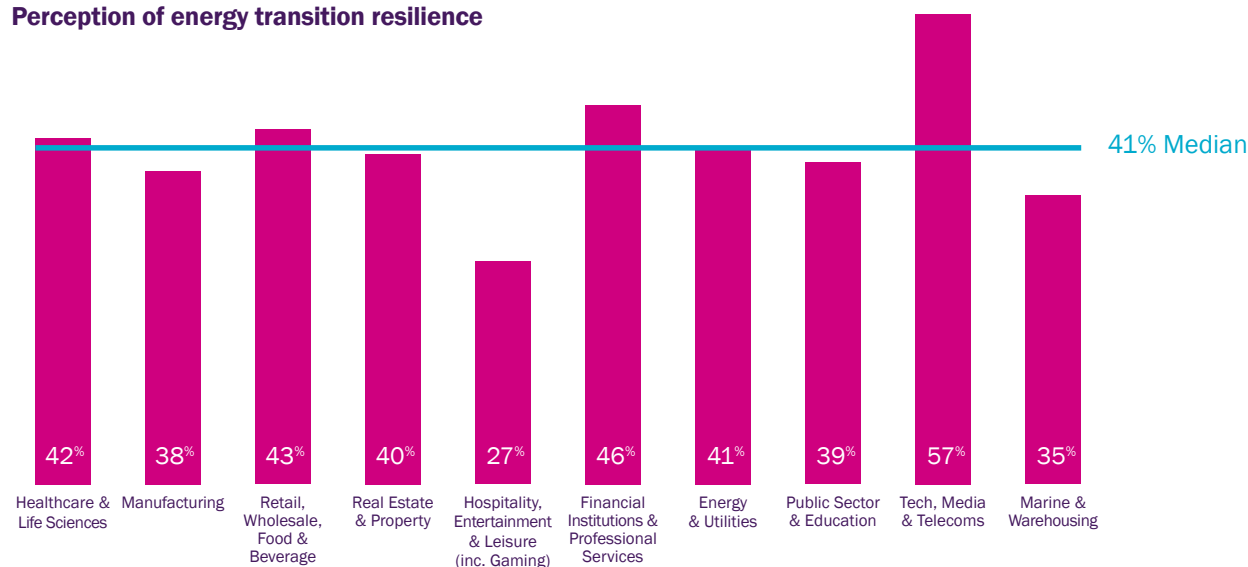
Such high levels of confidence may reflect the fact that energy reform is far less advanced in the US than in the UK, which has already designated emissions zones in cities, named dates for ending petrol and diesel use in cars and begun the phasing out of gas fired boilers in housing construction and renovation. In October, the UK Government announced plans to incentivise people to install low-carbon heating systems as they replace their gas boilers over the coming decade.

## Perception of energy transition risk



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
Median line indicates the mid-point of the data set across all industries surveyed.

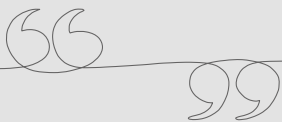
## Perception of energy transition resilience



Percentage of UK and US companies ranking the selected environmental risk top, 2021.  
Median line indicates the mid-point of the data set across all industries surveyed.

## Confronting hidden risks

In part, some of the difficulty in terms of energy transition is gaining oversight of the whole value chain. In a foretaste of things to come, the dramatic hike in the price of natural gas in September 2021 had unexpected knock-on effects on other industries in the UK including food and drink production. It is notable that when asked earlier in 2021, only 9% of respondents in this sector rated energy transition as their top risk, while 43% were confident in their resilience to it. These figures seem likely to be turned around significantly when our research is refreshed next year.



Supply chain networks have typically been designed for efficiency, cost and proximity to markets but not necessarily for transparency or resilience. In this era of increasing interconnected risk, these factors need to be taken seriously so companies can embed sustainability throughout the value chain to reduce waste, increase efficiencies and stay ahead of the competition. Ultimately, transparent and sustainable supply chains not only create positive impacts for organisations' own corporate interests, but also for society and the environment.



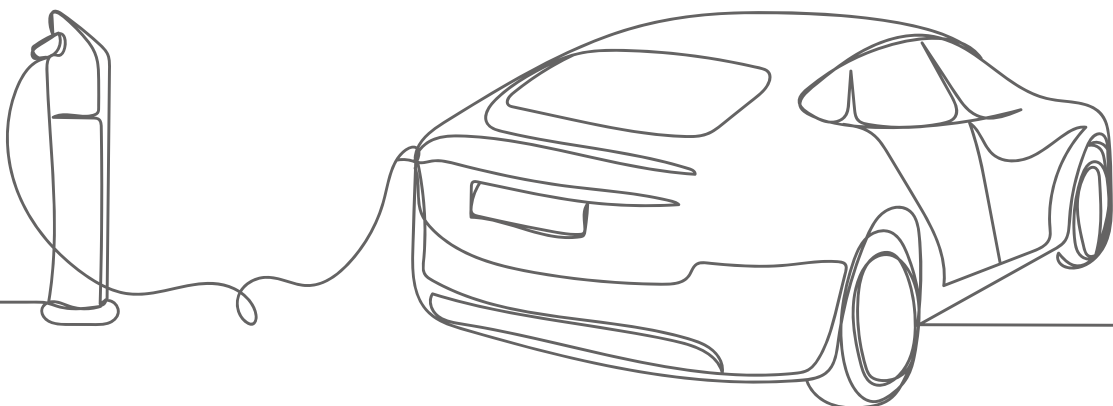
**Chris Illman**  
Head of Responsible Business

## And unexpected consequences

Even when companies embrace energy transition issues with the creation of new products and new payment mechanisms, the environmental and associated reputational issues are not always apparent. This is one area where failure to take appropriate action now may result in elevated product recall or D&O risk down the line.

In one example, an electrical vehicle manufacturer announced that it would accept payment in bitcoin for its electric vehicles, citing its ability to make the company more flexible and maximise returns on its idle cash. However, when the environmental implications of this decision were made plain, the decision was rapidly reversed.

As activist pressure grows and the impact of climate change becomes more obvious regulatory and legislative interventions around energy transition will become an increasing reality.



# How should the insurance industry respond?

## ESG concerns create both challenge and opportunity for the insurance industry.

High profile markets, such as Lloyd's of London, are firmly in the cross hairs of stakeholders and activist environmental groups over their support for carbon intensive sectors and projects, but have declared their support for a clean transition by setting ambitious targets well above those of the UN.

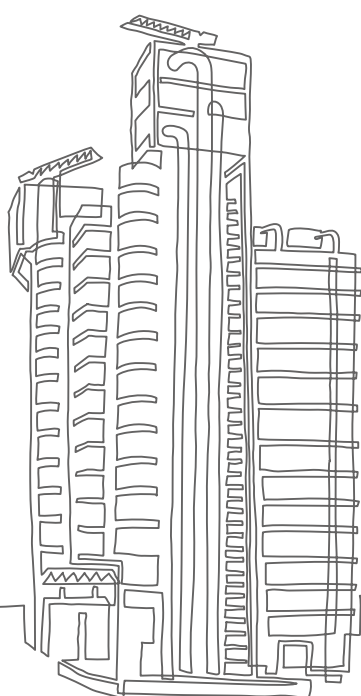
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The insurance industry has a pivotal role to play as an influencer of what happens in client industries. Increasingly, the ability to secure financing to grow a business will depend on the ability to secure insurance to protect it – this in turn makes insurers accountable for investment choices.



**Will Roscoe**  
Head of Alternative Portfolio Underwriting



## Underwriting models are being challenged

New hazards will emerge as the transition to a greener economy takes place, requiring new products and new underwriting solutions. The challenges in shifting to clean fuels, such as hydrogen, are significant. Losses on offshore wind and on large solar plants have been substantial for example – green assets are just as exposed to catastrophe risk as traditional energy assets – possibly even more so.

Traditional modelling particularly around natural catastrophe exposures and, more broadly, past loss experience have not been predictive of the future, and that will need to be corrected. This will require coupling a deep knowledge of the risk landscape with technology advancements to map a better future, something that will require significant investment over time.

Much work still remains to be done to create a common framework for evaluating the strength of businesses' green credentials. However, progress is already under way through moves like the Sustainable Markets Initiative<sup>11</sup> and ClimateWise<sup>12</sup> initiatives to support insurers to make informed decisions as part of the transition to a greener economy. It is also hoped that policies announced at COP26 will have a marked impact, including particularly the creation of the new International Sustainability Standards Board (ISSB) that is introducing new prototype global standards on climate-related disclosures and general sustainability disclosure requirements.

Initiatives like these are sparking a huge amount of collaboration across the industry to create common methodologies and appraisal mechanisms. The issue, as always, however, will be the quality and availability of the data needed to support informed decisions and how the industry implements new approaches in order not to destabilise communities dependent on particular energy sources for employment and power. The sometimes competing demands of the E, S and G agenda mean that for a while, insurers and others will be performing something of a careful balancing act, one that must end in favour of progression over paralysis.

<sup>11</sup> HRH The Prince of Wales launches new partnership with the global insurance industry to drive action to tackle climate change (lloyds.com)

<sup>12</sup> ClimateWise | Cambridge Institute for Sustainability Leadership

## Portfolio management will need to step up

As obligations change, the industry will require new techniques for portfolio management. And there will be many more dependencies to model. The industry will need to determine for example what is the correlation between more frequent floods and the economic activity in a given region, making the work of underwriters even more complex. As underwriting becomes more strategic, and more insurers reconsider their participation in areas including thermal coal, tar sands and Arctic energy exploration, it is hoped that companies with strong ESG credentials are, or will become, better risks. The insurance industry has a role to play here in encouraging a model of financial stewardship that helps countries and businesses transition to new energy models in a way that fairly balances the interests of current and future generations, developed and developing economies.

## Insurance solutions need an overhaul

Environmental risks present a significant threat to the insurance industry. They have the potential to generate complex, integrated claims that straddle traditional areas – from pollution and environmental damage, through to new areas of risk like greenwashing and reputation damage. But they also represent an opportunity to work with clients to go beyond pure risk transfer to improve management and mitigation of risks to minimise the likelihood of a loss event.

Driving better alignment between business and social agendas is a complex challenge that requires long-term solutions and dedication if we are to succeed. A key factor in that success will be working together to forge stronger, deeper relationships and clear prioritisation to invest in a strategic roadmap creating a more sustainable planet for all.

Delivering on these objectives will require more breakthrough innovation in this space, greater collaboration around standard-setting and regulation, and a heightened sense of urgency to deliver real solutions.



The link between ESG credentials and loss ratios is beginning to be established and access to more high quality data is improving. Progressive solutions to problems as complex and wide-ranging as these that speed up the transition will not be developed overnight nor in response to unrealistic demands, but through market alignment, collaboration and further sharing of data.



**Chris Illman**  
Head of Responsible Business



As underwriters, our goal is to be able to pick and reward strong performers and to identify which businesses are on the cusp of better ESG performance and to have open discussions with them. We want to support as many companies as possible to improve ESG performance and in time make a full transition to net zero.



**Will Roscoe**  
Head of Alternative Portfolio Underwriting

## About our Risk & Resilience research

During January and February 2021 we commissioned research company Opinion Matters to survey the opinions of over 1,000 business leaders and insurance buyers of businesses based in the UK and US with international operations. With a minimum of 40 respondents per country per industry sector, respondents represented businesses operating in:

- Healthcare & life sciences
- Manufacturing
- Retail, wholesale, food & beverage
- Real estate and construction
- Hospitality, entertainment & leisure (including gaming)
- Financial institutions & professional services
- Energy and utilities (including mining)
- Public sector & education
- Tech, media & telecoms
- Marine & warehousing.

Survey participants were asked about their views on insurers and insurance, as well as on four categories of risk:

- **Technology** – including the threat of disruption, failure to keep pace with changing technology, cyber risk and intellectual property risk.
- **Business** – including supply chain instability, business interruption, boardroom risk, crime, reputational and employer risk.
- **Political & economic** – including strikes and civil disruption, changes in legislation and regulation (including ESG), economic uncertainty and war & terror.
- **Environmental** – including climate change and associated catastrophic risks, environmental damage, pandemic risk, food insecurity and energy transition risk.

Of the firms surveyed in both the US and the UK there was an equal split of respondents across company sizes of: \$250,000 - \$1 million, \$1,000,001 - \$10 million, \$10,000,001 - \$100million, \$100,000,001 - \$1 billion, more than \$1 billion.

## Our panel of contributors

We would like to thank our panel of insurance and risk management experts whose insight about our quantitative research has informed our findings throughout this report.



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This is the fourth in our series of Risk & Resilience reports, which explore business leaders attitudes to risk and their perceived resilience to these risks both now and in 12 months' time. To view our other Risk & Resilience reports please visit:

[www.beazley.com/risk-resilience](http://www.beazley.com/risk-resilience)

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