UKSIF
UK Sustainable Investment and Finance Association

Large investors back Bank of England climate change warning

- Carbon intensive investments putting global economy at risk
- Climate change could reduce UK insurance sector’s appetite to provide cover for specific sets of activities, assets or customers
- Low carbon investment needed for global stability

London, 30 September 2015 – Institutional investors, fund managers and other finance experts welcome Mark Carney’s speech yesterday stressing the risk to global stability posed by climate change.

Key risks to the finance and insurance sectors Carney identified are:

- **Physical risks from climate change** - '*there are some estimates that currently modelled losses could be undervalued by as much as 50% if recent weather trends were to prove representative of the new normal. In addition, climate change could prompt increased morbidity and mortality from disease or pandemics. Such developments have the potential to shift the balance between premiums and claims significantly, and render currently lucrative business non-viable. Absent actions to mitigate climate change, policyholders will also feel the impact as pricing adjusts and cover is withdrawn.*'
- **Claims on third-party liability insurance** – *in classes like public liability, directors’ and officers’ and professional indemnity - could be brought if those who have suffered losses show that insured parties have failed to mitigate risks to the climate; failed to account for the damage they cause to the environment; or failed to comply with regulations.*
- **Stranded Assets / transition risks:** *If that estimate* [IPCC’s estimate of a carbon budget amounting to between 1/5th and 1/3rd world’s proven reserves of oil, gas and coal] *is even approximately correct it would render the vast majority of reserves “stranded” – oil, gas and coal that will be literally unburnable without expensive carbon capture technology, which itself alters fossil fuel economics. The exposure of UK investors, including insurance companies, to these shifts is potentially huge.*

James Bevan, Chief Investment Officer at CCLA said:

"The Bank of England’s public statement that climate risk is a material financial risk speaks to the challenge of so-called stranded assets, and makes planning for declining carbon intensity an absolutely mainstream investment requirement. CCLA agrees that the best immediate means of illuminating the risk are through relevant disclosure that supports informed decision taking. As investors we recognise that the investment risks associated with companies with high carbon intensity are now significant, and CCLA will now work to build coalitions of investors driving change though engagement and co-filing such as with ‘Aiming for A’."

Peter Michaelis, Head of Equities, Alliance Trust said:

“This is a welcome reminder of how dependent economic success is on our natural environment. As Mark Carney said the window of opportunity to manage climate change risk is shrinking and we need to be investing now in the companies leading the transition to a lower carbon economy. He states: 'The more we invest with foresight; the less we will regret in hindsight' this is at the heart of sustainable investing strategies.”

Stephanie Pfeifer, CEO of the Institutional Investors Group on Climate Change (IIGCC) said:

"Mark Carney spoke under the Lutine Bell, the way Lloyds has signalled great events that will affect the market. He chose his setting perfectly. We welcome his focus on more consistent and reliable carbon disclosure that will allow investors to make a more informed assessment of the climate risks in their portfolios".

Simon Howard, UKSIF Chief Executive, said:

"UKSIF welcomes the Governor's speech. He raises issues which the UK sustainable finance sector has been working on for years. We are delighted climate risk is now being taken seriously at the highest levels.

UKSIF, its members and sister organisations are already engaging with the UK Government on issues such as emissions reporting and the funding of renewable energy. We urge the Government to respond positively to the Governor's call for action at the G20 and at COP 21. We know the UK financial sector is open to funding the transition to a low carbon economy and we know that the UK has the necessary skills to create the financial tools to do it. But this cannot happen quickly enough without action being taken by many global authorities. The UK Government has the chance to show leadership here by endorsing Mr Carney's call for companies to disclose more and by giving guidance on possible carbon price paths.

That leadership will help protect UK savings and it will support the UK as a global leader in finance as we embark on the urgently needed move to a more sustainable economy."

-ENDS-

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Interviews with those quoted above are available on request.

Quotes from Carbon Tracker, CCLA, and IIGCC have been previously circulated today.

About UKSIF:

UKSIF is the membership network for sustainable and responsible financial services in the UK. We promote and support responsible investment and other forms of finance that advance sustainable economic development, enhance quality of life and safeguard the environment. We also seek to ensure that individual and institutional investors can reflect their values in their investments.

UKSIF was created in 1991 and has around 240 members and affiliates include institutional and retail fund managers, pension funds, banks, research providers, financial advisers, consultants and NGOs. For more information about UKSIF, please visit www.uksif.org.

Background Briefing

What did Mark Carney Say?

Mark Carney's speech on 29th September backed action on climate change from the finance and regulatory community including:

- Better disclosure of information: '*following our discussions at the FSB last week, we are considering recommending to the G20 summit that more be done to develop consistent, comparable, reliable and clear disclosure around the carbon intensity of different assets.*'
- A voluntary Climate Disclosure Task Force, *to design and deliver a voluntary standard for disclosure by those companies that produce or emit carbon* based on the Enhanced Disclosure Task Force.

- Climate change stress testing '*to act as a time machine shining light on risks that may lurk in years to come'*

What have others said about climate risk in the finance sector?

Mercer in June 2015 published 'Investing in a Time of Climate Change report, which unreservedly concludes that climate-related risk factors should be standard considerations for investors because climate change "will inevitably have an impact on investment returns". Mercer states, depending on the climate scenario which plays out, the average annual returns from the coal sub-sector could fall by anywhere between 18% and 74% over the next 35 years, with the effects being more pronounced over the next decade (eroding between 26% and 138% of average annual returns).

The Economist Intelligence Unit in July 2015, in "The Cost of Inaction: Measuring Value at Risk from Climate Change" report commissioned by Aviva, reported that the expected losses to the global stock of manageable assets, in discounted present value terms, are valued at US$4.2 trillion - roughly on par with the total value of the world's listed oil and gas companies. Despite this, carbon is still largely an un-priced externality in the vast majority of investment portfolios.

HSBC in March 2015 published a research note 'Stranded Assets: what next'? identifying stranding through policy, price, and innovation risk. HSBC Group CEO Stuart Gulliver made speech on 25 Sept 2015 stating that: "Increasing the visibility of climate risk would reduce the incentive to maintain a heavy carbon footprint in an investment portfolio, and at the same time incentivise companies and financial institutions to measure and reduce their own carbon footprint."

What are investors doing on climate change?

On carbon footprinting the Montreal Carbon Pledge has 92 signatories now including most recently HSBC, with Assets under Management participating totalling nearly $6 trillion - indicating investors are increasingly interested in carbon risk.

The Asset Owner Disclosure Project is an independent not-for-profit global organisation whose objective is to protect retirement savings and other long term investments from the risks posed by climate change by improving disclosure and industry best practice. Their annual Climate 500 Index ranks asset owners.

Investors are logging many other actions here (non-exhaustive): http://investorsonclimatechange.org/

What could the legal risk in finance sector be from climate change?

The Law Commission Kay Review into fiduciary duties of investment intermediaries found that pension trustees and their asset managers are required to assess and manage financial factors that are relevant to their investment duty of balancing returns against risk. This statement of law in turn derives from a number of legal sources, including the Occupational Pension Schemes (Investment) Regulations 2005 and the common law. If pension fund trustees ignore the financial risks associated with climate change some argue they may be placing members' savings in jeopardy and failing to conduct themselves in a way that balances long-term returns against risk. This could contrary to the law but has not yet been tested.

ClientEarth, through its Climate and Pensions Legal Initiative (CPLI), is investigating what pension funds are doing to manage climate risks that might affect the value of pension pots, and assessing whether they are meeting their legal duties. They are considering bringing legal challenges against those funds not doing enough to fulfil their legal obligations.

What brought about this report?

The Bank of England were first asked in a letter in 2012 by a group of investors, UKSIF, NGOs, and academics to consider systemic climate risks saying: *"we urge [the FPC] to investigate how the UK's exposure to high carbon investments might pose a systemic risk to our financial system and what the options might be for managing this potential threat to our economic security* "

The Parliament's Environmental Audit Committee subsequently called for the Bank to consider the topic, followed by Defra (Department for Environment, Food and rural affairs) formal request in 2013.

In 2013 a project team was established to compile the Climate Change Adaptation Report and lead on the exploration of climate risks in the financial system. This team is supported by an internal working group comprising senior staff within the PRA and is part of the PRA's Insurance Directorate.

The report will be delivered to Defra, for publication thereafter. This report, alongside the others resulting from the second round of Adaptation Reporting, will inform the next UK Climate Change Risk Assessment, to be laid before Parliament in 2017.