Our climate mission is clear

As visibility into the future is restored following the pandemic, the climate crisis comes sharply into view. But organisations need a guide to help them through the green transition their stakeholders, regulators and society at large are insisting on.

There has never been a greater impetus for action on climate change. Corporate risk managers have an essential role in identifying the key risks and opportunities that face businesses, as they design and set out on transition journeys. As they look beyond the immediate and near-term challenges of the pandemic and economic slowdown, not much future gazing should be required to spot the next grey rhino in the room.

George Nassaouati, head of Natural Resources Asia at Willis Towers Watson, was a regular visitor to the region's major cities before COVID hit and remembers the thick smog in some cities such as Bangkok, Beijing, Delhi and Jakarta where visibility was low at times. There has been a realisation that the situation

is no longer viable. "We're seeing a lot of green activities in China now, especially by our energy and power team over there, where they are not only engaging with clients, but also with government agencies as part of China's green energy initiative," he observes.

The past 18 months has given many organisations direct experience of dealing with a major global shock. Depending on the sector, firms have responded to the pandemic in numerous ways – implementing business continuity and crisis management plans, shifting to a remote working model and adapting business models in order to survive the economic impact.

The most successful have been nimble. Firms that have proved most resilient through the crisis have demonstrated an ability to repurpose and a culture that supports risk-based decisions. However, beyond COVID-19, what's next? The deadly virus has not run its course – far from it, in fact – but we already know what the next big challenge is: climate change.

Looking ahead, the climate change challenge looms large. Unlike COVID-19, it is not a shock that companies can claim they were unprepared for, and failure to prepare will not be tolerated by the next generation of regulators, shareholders and wider society.

GOOD METRICS ARE HARD TO FIND

As regulatory frameworks around climate-related risk and opportunity are introduced, one challenge to overcome relates to the data. The inherent complexity of climate change – where even the climate scientists do not always agree on how a warming climate will influence weather patterns and natural perils – makes it very difficult to arrive at meaningful metrics. Due to its expertise in catastrophic risk, the insurance industry is well-positioned to work with insureds to pursue climate-related financial impact data that can inform action.

A message that sits behind the principles of environmental, social and corporate governance is that climate preparedness and transitioning is not just about the individual journey, but wider collaborations between business and society, public and private sector, countries and regions, insurers and insureds.

"Given that many regions in Asia are prone to nat cat events, large corporates generally have a good awareness of physical risk," says James Wong, director of Strategic Risk Consulting, Risk & Analytics in Asia at Willis Towers Watson. "Furthermore, organisations have progressed considerably over the last few years in recognising the potential changes in acute and chronic physical risks over a longer time horizon."

"Not many companies have fully grasped the concept of transition risks and their implications," he continues. "Some have found the broadness and futuristic aspects of this topic quite daunting. In this respect, we find that the Task Force on Climate-related Financial Disclosures [TCFD] is quite useful as it provides a comprehensive framework to help companies identify and assess the climate-related transition risks arising from policies, market, legal and technology changes."

Willis Towers Watson has launched a global modelling tool that uses data and analytics to demonstrate changes in acute hazards, such as extreme wind and flood, as well as chronic stress factors, such as sea level rise and heat stress. The tool considers numerous scenarios based upon a combination of climate scenarios and time horizons.

TCFD: A NEW REPORTING BENCHMARK

The Task Force on Climate-related Financial Disclosures was launched in 2015 to offer a reporting framework for climate-related disclosures.

The aim was to create the data foundations to support better informed investment, credit and insurance underwriting decisions, and to expose climate-related risks to the global financial and investment system.

Recommended disclosures as set out by TCFD are based around four pillars: Governance, Strategy, Risk Management and Metrics & Targets.

The recommendations will likely form the basis of future climate-related regulations around the world, with G7 finance ministers announcing in June their intention to mandate climate reporting in the near future. "Investors need high-quality, comparable and reliable information on climate risks," they stated. "We therefore agree on the need for a baseline global reporting standard for sustainability, which jurisdictions can further supplement."

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James Wong

"In our advisory role, we have supported our clients to enhance their understanding of both physical and transition risks," says Wong. "On assessing transition risks, we work closely with our clients' risk management and sustainable teams to understand where they are at and what they aim to achieve in the next 12 to 18 months."

"These include assessing and quantifying the financial impact of the identified risks and opportunities, giving a relative prioritisation of risks, helping to shape effective risk responses to identified transition risks," he continues. "We have worked with numerous real estate groups on this, given that many have had progressive carbon targets and experienced increased demand in green buildings."

In May, Willis Towers Watson launched Climate Transition Pathways (CTP), an accreditation framework to provide insurance companies and financial institutions with a consistent approach to identifying which organisations have robust transition plans aligned to the Paris Agreement. As part of the initiative, organisations meeting CTP principles gain access to the insurance capacity and capital they need to support their transition to sustainability.

Rowan Douglas, head of the Climate and Resilience Hub at Willis Towers Watson, explains: "We are ensuring these organisations are supported through an orderly transition and can continue to access insurance, and benefit from a greater level of certainty around the future availability of risk capacity, helping them deliver a more sustainable future."

BUILDING MOMENTUM

The landscape is already shifting. Firms are under greater pressure from stakeholders, including regulatory supervisors and investors more than ever

AYALA CORPORATION: LEADING BY EXAMPLE

***StrategicRISK* spoke to Victoria Tan, head of group risk management and sustainability at Ayala Corporation, about the reality of leading the charge on sustainability, in a place where climate change already impacts daily life and risks.**

Ayala Corporation has taken a proactive approach to climate risk and sustainability due to the country's significant exposure to natural perils and the range of industry sectors it operates within. As Tan explains, inaction was never an option.

"Just a few hours ago, it rained heavily in this part of the world and the internet was down. At Ayala, we're focused on both physical and transition risk but of course we can relate more on the physical side, because there is the risk of frequent flooding, typhoons and sea level rise."

FEELING PHYSICAL RISKS

"Even before the TCFD framework or discussion on climate change risk became a requirement, we already knew we had to do something about the physical risk. For instance, our Globe Telecoms business was significantly hit by Super Typhoon Haiyan (known locally as Yolanda) in 2013, resulting in more than $10m in insurance claims."

Rapid deployment of engineers to areas hardest hit was held up as an example of the private sector's increasingly important role in relief efforts. And since then, Globe has continued to build a reputation for disaster recovery and building resilience into its infrastructure, including construction of hybrid telecom towers that can withstand wind speeds of up to 250 kph.

"The physical risk part of climate change is something we can easily discuss because it is something we experience almost every day: the severe heat we are experiencing right now and flooding we will see during the rainy season."

The organisation's electronics manufacturing firm IMI, which is located in the typhoon-exposed province of Laguna, takes its duty of care to staff seriously. "They will send employees home in company vehicles or stay in the vicinity if there is a typhoon. They have areas where employees can stay safely if it is too dangerous to return home."

'WE WERE DOING IT ANYWAY'

From a transition risk perspective, she does not anticipate climate-related regulation, such as carbon tax, to come into place soon. However, the company is preparing anyway, in anticipation of COP26 and wider commitments to reduce carbon emissions.

"With Biden as US president, the commitment to the Paris Agreement has been strengthened. Here in the Philippines, the government is building stakeholder engagement. I don't know yet how it will translate into regulatory requirements, but when it happens, it will be quite impactful."

In 2019, the government supervisor announced all publicly listed companies should begin reporting on sustainability risk in their annual reports, with a view to making this mandatory by 2023 on a 'comply or explain' basis.

"Since Ayala Group has been reporting on ESG since 2008, a decade before this requirement, there has been minimal impact upon us because we were doing it anyway. Our investors have been asking us to disclose, but until recently there was very little requirement from the government."

SPEARHEADING RESEARCH

For several years, external risk advisors have supported the organisation at a parent level with its natural catastrophe risk modelling in order to better understand how natural perils could impact the business and its different operating companies.

On climate change, the company has again commissioned external consultants to understand the financial impact of climate change to our industry verticals and to determine the right metrics and targets for GHG reduction.

"The end result of this scenario analysis for Ayala, as a parent company, is to make a decision on capital allocation that will help us mitigate the impact of climate change and that will help invest in adaptive solutions."

"At an operating company level, Globe can't get out of telco because that's their business. So they will have to come up with innovative solutions and consider new business models and their role within the community. They are part of the community so by helping to build a more resilient community, it will benefit everyone."

Tan continues: "We should also remember what our chairman, Jaime Augusto Zobel de Ayala, shared during the 2017 UN's 10 SDG Pioneers awarding event: 'Businesses cannot thrive in a degraded environment and in a society rife with inequities. Ignoring these issues threatens our ability to create long-term value and jeopardizes the sustainability of the enterprise and the markets.'"

before. While currently voluntary, it is anticipated that climate-related reporting frameworks, such as the TCFD, will soon be mandated. But climate change preparedness is much more than a tick-box, compliance exercise.

As governments go into this year's COP26 meeting in Glasgow, it is an opportunity for the corporate world to prepare its own climate transition pathways. This includes quantifying the likely physical and transition impact of climate change on the business now and into the future and setting out the necessary goals in order to adapt and improve resilience.

"Climate change is now impossible to ignore," says Wong. "Physical climate risks increasingly threaten the bottom line, whilst regulator, investor and consumer pressure, demand greater action to understand, report and manage climate risk exposure."

"At the same time, the economy-wide transition to net zero, new technology and market sentiment will disrupt business models and pose new challenges and

AN ENERGY SECTOR UNDER PRESSURE

Energy firms risk action from climate lawyers, stakeholder pressure and issues securing insurance if they fail to transition away from fossil fuels and towards more sustainable, renewable sources.

The energy sector is on the frontline of the shift to zero-carbon emissions: a transition that will continue to ramp up, with wind and solar capacity set to double over the next five years, according to the International Energy Agency. In total, investment in the renewable energy sector will reach $16 trillion by 2030.

The sector is also highly exposed to the physical risks arising from a more extreme climate, including more severe natural perils and sea level rise. Offshore wind arrays, for instance, must be built to withstand the force of tropical cyclones, which may become more powerful.

Meanwhile, there are legal and reputational risks to consider, particularly for those firms that fail to adapt as quickly as they should. In a landmark ruling against Shell, a Dutch court ruling the energy giant should reduce its greenhouse gas emissions by 45% from 2019 to 2030. Climate lawyers are preparing to take on other energy firms that opponents say are not transitioning quickly enough.

In Asia-Pacific, the signs are encouraging that energy firms are taking their responsibilities seriously. However, it is not a transition that can occur overnight, explains Willis Towers Watson's Nassaouati.

"In certain countries like the Philippines, Indonesia, China and India, there is a heavy reliance on coal. So it's very difficult to transition these countries, but there has definitely been an awakening within the governments of India, China and others, that this needs to change."

This is where the broker comes in. "At the moment, many of our clients have coal assets but have started to transition into other sources of energy. We're happy to partner with these clients and to support them as they move away from coal towards wind or solar."

Meanwhile, pressure is mounting on the insurance industry to step away from insuring thermal coal projects, with Adani's highly controversial Carmichael coal mine in Australia fast becoming the poster child for campaigns such as Unfriend Coal.

From a broker perspective, it is important to emphasise the growing risk financing costs associated with fossil fuel projects and the challenges in securing insurance cover.

"The insurance capacity is reducing for coal projects so the costs will go higher, making a firm's capital expenditure on such projects unviable," says Nassaouati. "It becomes uneconomical. Previously, offshore wind and solar plants were more expensive, but now the renewable energy market is becoming more economical."

"So we've already engaged with a number of clients to ask: 'How are we going to work together to transition out of your coal assets? What are your plans in the next five, ten years to move away from those assets?"

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Head of Natural Resources Asia, Willis Towers Watson
George Nassaouati

opportunities for all companies. Businesses that do not address climate risks are likely to fail, facing increased pressure on profitability, liability risk and potentially restricted access to capital and liquidity."

Physical risks are top of mind for businesses in asset heavy sectors such as real estate and hospitality. Many real estate firms are demonstrating a proactive approach in considering the risks and opportunities relating to climate change. The financial services industry also share these concerns, due to the exposure of the physical assets within banks' investment portfolios.

"In Asia-Pacific, many businesses are still trying to understand the full implications of what climate transition means to them. Many organisations are at an identification stage, while others are somewhat ahead of the curve by going deeper, such as quantifying the financial impact of the risks and opportunities, as well as assessing whether they are investing and acting appropriately to mitigate the downsides or to take advantage of the upsides."

By being ahead of the curve, these organisations will be better positioned to identify opportunities that arise. There is a clear 'business case', according to New Zealand's Sustainable Business Council, as "businesses that integrate sustainability well outperform those that don't". **SR**