

Next in insurance

ESG: A growing sense of urgency



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At its core, insurance is about mutualizing and managing risks, principles that are inextricably linked to environmental, social and governance (ESG) criteria. Carriers have long viewed a robust governance structure and understanding of the impact of extreme weather events on balance sheets as protective of company value.

What's different now?

For starters, employees, business partners, agents and end customers — not just regulators, standards-setters and investors — are vocally expressing concern about ESG-related issues. While these stakeholders' perspectives and areas of influence vary, they share one thing in common: increasing expectations.

80%

of global investors say how a company manages ESG risks is an important factor in investment decision-making.



75%

of global investors say companies should address ESG issues, even if doing so reduces short-term profitability.



76%

of consumers say they will discontinue their relationship with companies that treat the environment, employees, or community in which they operate poorly.



36%

of global insurers told us customers are their top priority when they are defining their ESG strategy, followed by regulators (26%) and shareholders (16%).



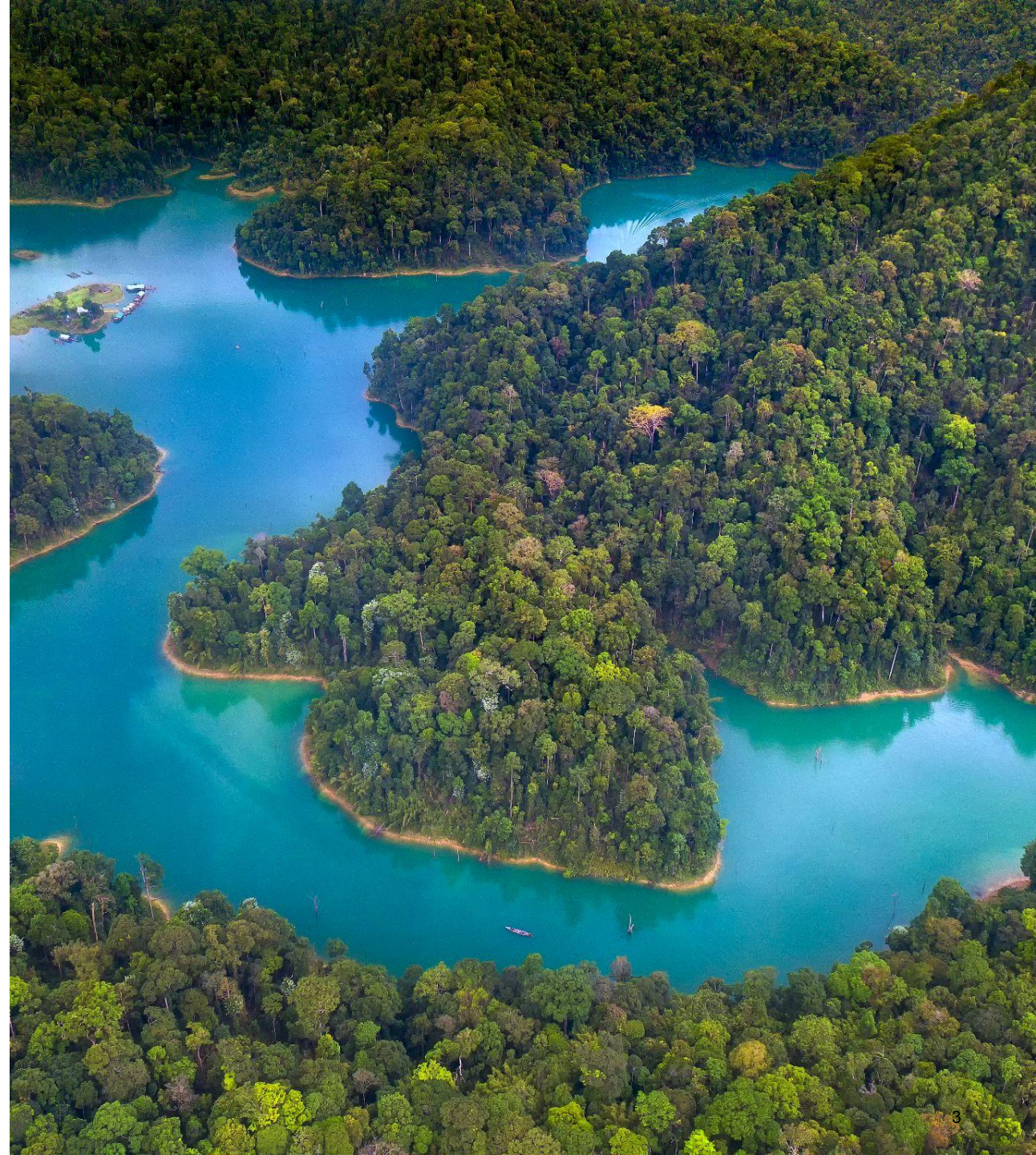
Moreover, recent regulatory developments are forcing insurers to meet expectations with actions, especially on climate concerns. The US Securities and Exchange Commission (SEC) released its [climate disclosure requirements](#) proposal in March. The proposal is the SEC's response to growing investor demands to understand what companies are doing to manage increasing climate change risks and the transition to a low carbon economy. Although insurers are awaiting more specific guidance from the SEC on some proposal topics, they're facing a move from existing voluntary disclosures of climate-related risks to mandatory requirements that potentially carry increased legal liability.



In addition, the National Association of Insurance Commissioners (NAIC) released an updated climate risk disclosure survey in April. Survey questions align almost entirely with the Task Force on Climate-Related Financial Disclosures (TCFD) framework. This will result in a significant shift towards TCFD-aligned disclosures for US insurers, forcing carriers to think about climate change in multiple facets of their business and confront how they address it.

As a result, a formal and clearly defined ESG strategy is no longer optional. Not only do key stakeholders want explanations of how insurers are addressing the issue, they're also formally mandating them.

- 25% of global insurers told us that “understanding ESG-related regulations and guidelines” is the main challenge in pushing forward their ESG agenda, followed by “understanding how best to take action on ESG” (17%) and “matching ESG initiatives with customer needs” (15%).
- 49% of insurance CEOs say their company does not have the ability to measure their greenhouse gas (GHG) emissions today, despite the SEC’s proposal for new climate disclosure requirements.



Simplifying ESG: What you should focus on now

Gain clarity

Insurers have high ESG ambitions and serious responsibilities but also pronounced capabilities gaps:

- 56% of insurers have future ambitions to develop mature or leading environment-related capabilities but only 24% say they have mature or leading capabilities today.
- 57% of insurers have future ambitions to develop mature or leading social capabilities but only 32% say they have mature or leading capabilities today.
- 80% of insurers have future ambitions to develop mature or leading social capabilities, while 68% say they have mature or leading capabilities today.

Your ambitions and subsequent actions will determine if your corporate strategy fully incorporates ESG considerations or places them to the side. An unfocused strategy or one that isn't anchored in a practical course of action will fail to move your organization forward and hurt your credibility and reputation.

Identifying the factors that align to your ambitions and purpose is a critical step that carriers often overlook. To start, you should evaluate the ESG actions you've already taken. During this initial research phase, you're likely to discover several genuine accomplishments. But you'll need to articulate them in the context of the latest ESG reporting frameworks and regulations.

You then should consider your overall and specific ESG ambitions. Think carefully because the stakeholders who matter most to the long-term viability of your business will measure your ambitions and actions against their own expectations. You should ask yourself: What is basic necessity (e.g., diversity, equity and inclusion commitments) and what could be a real differentiator (e.g., supporting the move to less carbon intensive projects)? You'll also need to decide if keeping pace with evolving regulations will be enough or if you'll want to anticipate or even try to help shape external oversight.

Utilize a pillar by pillar approach

Because ESG has multiple components and stakeholders, it can seem overwhelming as a concept. Disaggregating it greatly facilitates a thoughtful and effective response. In that spirit, the following pages describe a pillar-by-pillar approach to issues currently dominating our discussions with insurers that you can use to inform your activities.

- Only 35% of global insurers tell us their organization's strategy is "significantly focused" on all three pillars of ESG.
- 85% of global insurers believe ESG will impact all functions of their business. They identified investments as the single largest area of impact (91% of respondents), followed by risk and internal audit (90%) and underwriting (88%).
- Global insurers tell us that the main driver of their ESG pursuit is "to minimize the impact from climate change" (26%), "to gain a better reputation as a firm" (11%) and "to minimize risk" (11%).

Environment pillar: Climate

At the 2017 United Nations Environment Program (UNEP) One Planet Summit, AXA's CEO Thomas Buberl said, "A +4°C world is not insurable. Unsustainable business will become uninvestable and uninsurable." As we've seen with the increasing frequency and severity of natural catastrophes, as well as worsening climate-related stresses on every continent, Buberl's words ring even truer today than they did five years ago.

- 51% of global insurance CEOs tell us they have either made a net-zero commitment (22%) or are working toward making one (29%).²
- Among the global insurance CEOs whose companies have made a net-zero commitment, the decision was extremely or very influenced by the need to:
 - Mitigate climate change risks (62%).
 - Meet customer expectations (61%).
 - Drive product/service innovation (54%).
 - Satisfy investor demands (51%).

The viability of initiatives that have pronounced climate impacts typically depend on insurers' investment and underwriting decisions. These decision criteria have started to change and carriers are now making their underwriting exclusions and divestment policies more nuanced and integrating them into decarbonization strategies. Critically, this is taking place in concert with other investor (e.g. Climate Action 100+) and insurer (e.g. Net-Zero Insurance Alliance) coalitions.

To determine how you'll act on climate concerns, you'll need to:

- Understand climate change risks to your underwriting and investment portfolios.
- Determine your financed emissions (investment portfolio allocated emissions) and soon your insured emissions.

You'll also need to:

- Establish decarbonization goals for your investment and underwriting portfolios and define specific pathways and action plans for them. This can be challenging because what may benefit one may not benefit the other.
- Identify and assess product/service opportunities (e.g., energy efficiency insurance, carbon emissions assessment).

Moreover, in the wake of the SEC and NAIC climate announcements we mention above, senior management and the board need to develop an overarching strategy on climate disclosures and risk management. This involves:

- Setting clear disclosure objectives
- Defining key metrics
- Identifying underlying data sources
- Embedding climate-related information into data governance models and management processes



Social pillar: Building trust

ESG is prompting companies to publicly address social issues, providing the industry a unique opportunity to rethink its product portfolio and create innovative coverages that address emerging risks and underserved populations.

- 69% of global insurance CEOs tell us they are extremely or very concerned with the impact of social inequality on their ability to attract and retain key skills.
- 49% of global insurance CEOs tell us they are extremely or very concerned with the impact of social inequality on their ability to sell products and services.
- Increasing shareholder value is among the top priorities in all regions, while creating a fairer society is a primary driver exclusively in Europe.

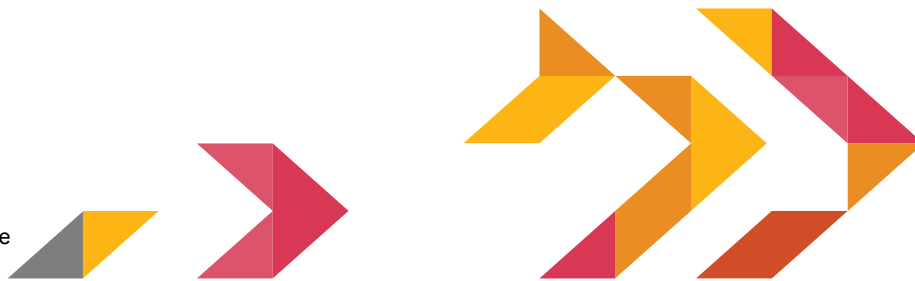
As we note in our recent "[insurance reimagined](#)" report, trust — what the social pillar ultimately promotes — underpins insurance. However, consumers trust financial services companies, including insurers, considerably less than those in other industries. Moreover, the pandemic has accelerated wealth disparities and the erosion of the middle class, contributing to even greater social distrust.

Combined with lack of access and poor financial education, this decline in trust has made customers less likely to buy insurance and led to significant protection gaps and higher economic losses. So far this century, the global protection gap has drastically widened across all sectors, reaching US \$1.4 trillion in 2020. Our analysis estimates it could reach US \$1.86 trillion by 2025.

Against this backdrop, rising stakeholder activism and demands for greater accountability and transparency are influencing insurers' strategic agendas. To strengthen trust, some carriers are focusing on alleviating social injustice by creating a more inclusive social and business environment. They're attempting to bridge access and coverage gaps by educating customers, creating affordable products (e.g., microinsurance) and more effectively distributing them to reach more customers. As we describe in more detail below, some also are forming public-private partnerships with local governments, regulators and policymakers to address financial asymmetries, build solutions for future climate or pandemic-related risks and improve access to affordable healthcare.

To take the next step, you'll need to:

- Understand current performance on the social dimension (e.g. workforce diversity and inclusion metrics).
- Articulate ambitions for social sub-dimensions (e.g. customer privacy, distribution, price discrimination, coverage redlining).
- Identify and assess product/service opportunities (e.g., property coverage for social enterprises).
- Prioritize social opportunities and define an implementation roadmap.

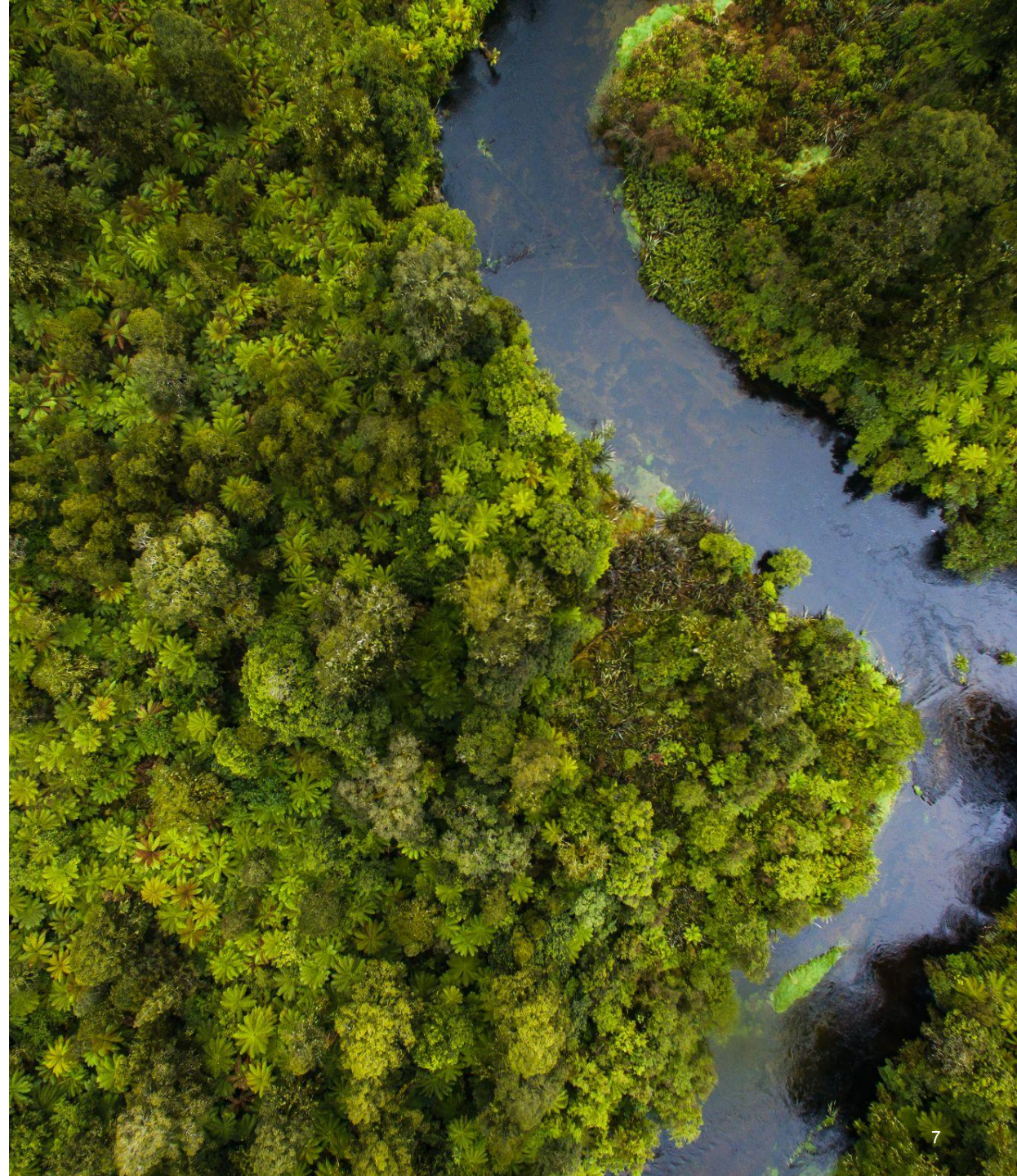


Governance pillar: Incentives

ESG calls for responsible organizational actions and behaviors, including transparency, and well-understood and clearly-communicated business ethics, as well as the recognition that diverse viewpoints lead to more informed decisions. Thanks in part to the heavily regulated nature of the industry, insurers rate themselves highly in the governance dimension. In the global ESG insurance survey we cite elsewhere in this report, insurers consider their governance ambition to be the most advanced, with four-fifths of respondents indicating mature or leading status.

However, insurers have considerable room for improvement. For example, at the corporate level, transitioning to a low-carbon economy includes tax incentives to encourage complementary investments and behaviors. These incentives have become available in a time of extensive scrutiny of corporate tax remittances. Publicly explaining your tax strategy and tax principles is a proactive governance move that can show how you're striking the balance between organizational benefit and the greater good. It also can position your company as a force for positive change and a dynamic player in a more socially conscious environment.

Carriers also have far to go in how they reward executives and lower level employees. Less than half of FTSE 100 companies have tied [executive pay](#) to ESG measures and progress has been even slower further down the chain of command. This represents a prime opportunity for carriers to embed ESG objectives into the entire organization and increase employee commitment to the issue. To accomplish this and determine how your incentives align with ESG in other areas, assess:





- Current alignment of pay to ESG outcomes and also determine if you have gender or other pay gaps
- Controls (including for third-parties) over activities that go against effective governance and could incentivize bad behavior (e.g., deceptive business practices, bribery and money laundering)

While there are many direct benefits of taking steps like these, there also are indirect benefits, including the reinforcement of brand value for current and future employees. As we note in our recent report on [talent acquisition and retention](#) in the insurance industry, meaningfully acting on well-articulated ESG initiatives can be a strong lure for prospective and existing employees. And, in fact, 84% of insurance CEOs say their internal stakeholders are significantly concerned about climate change.

Don't go it alone: the importance of partnerships and collaboration

ESG presents challenges that can be difficult for an organization to solve entirely on its own. Although you have to address some things by yourself, fully tackling all three pillars will require collaborating with your peers in and outside the industry and joining forces with investors and other stakeholders. Fortunately, insurers largely recognize this and are acting accordingly.

93% of global insurers tell us their organization is very likely or likely to consider working with industry groups in their ESG pursuits, followed by 70% in the case of partnerships with other companies. Additionally, 60% are very likely or likely to consider working with academic groups.

Furthermore, carriers are actively involved in global ESG initiatives:

- 80% of global insurers tell us they've taken action or are planning to take action in the next 12 months in order to align with the UN Principles for Responsible Investment.
- 72% of global insurers tell us they've taken action or are planning to take action in the next 12 months in order to align with sustainable development goals.
- 70% of global insurers tell us they've taken action or are planning to take action in the next 12 months in order to align with the Task Force on Climate-Related Financial Disclosures.
- 68% of global insurers tell us they've taken action or are planning to take action in the next 12 months in order to align with the UN Principles for Sustainable Insurance





Insurance as ESG leader

The insurance industry's core strength is assessing and determining how to manage life, health, property and liability risks. ESG risks are no different. In certain areas, notably climate, the insurance industry can play a leading role helping other industries understand and act on ESG pillars. After all, which industry knows more about and can better explain climate risk than insurance? Moreover, because of their vital economic role as underwriters and investors, insurers have the ability to significantly influence climate impacting businesses and development initiatives. Many carriers are already taking related action, assessing and changing their underwriting and investment standards according to ESG principles.

That said, ESG is a major challenge for insurers. Not only are they figuring out how to help others manage related risks, they're also trying to determine the many ways ESG affects them. And in certain areas — notably the social pillar — they have as much if not more to learn and act on as companies in other industries.

Fortunately, many insurers aren't sitting on the sidelines. They're actively participating in global ESG initiatives and publicly touting their importance. They're regularly engaging with a variety of interested and affected parties to determine the best ways to meet ESG requirements and understand their implications. As we note elsewhere in this "Next in" series, the next step is for carriers to more consistently show what they're doing and how their actions benefit current and prospective stakeholders. If they can, they'll be genuine leaders, not just one group of participants among many.

Note: All survey data cited in this report is from the [PwC 2022 Global CEO Survey](#) and the as of yet unpublished PwC 2022 Global ESG Insurance Survey.

Contact us



Jeannette Mitchell
Insurance Trust Leader
PwC US
jeannette.mitchell@pwc.com



Xavier Crepon
Global Insurance ESG Leader
PwC US
xavier.r.crepon@pwc.com



Marie Carr
Principal, Consulting Services
PwC US
marie.carr@pwc.com

www.pwc.com



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