RESILIENCE

Integrating Risks into the Financial System:

The 1-in-100 Initiative

Action Statement

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CLIMATE SUMMIT 2014

UN HEADQUARTERS · NEW YORK
23 SEPTEMBER · #CLIMATE2014

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Integrating Risks into the Financial System: The 1-in-100 Initiative

Industrial and economic development is coming under increasing strain due to climate change and its consequent risks and impacts. Yet the reflection of disaster risk in the regulation of capital and procedures of accounting have yet to mature.

According to the OECD, in 2012, institutional investors held over $83 trillion in assets. This includes pension funds, endowments, foundations, investment funds – and insurers. In fact insurers account for almost $25 trillion in assets. Of this, only a very limited part – less than 1 percent – is invested in climate resilient infrastructure. At the same time, it is estimated that 60% of the area expected to be urban by 2030 has yet to be built. Actors from the financial sector, including banks, insurers and other institutional investors, play an important role in building resilience through integrating risk management into business practices and financial decision making.

Public, private and mutual sector insurers have a particular knowledge of, and responsibility for climate risks and the opportunities manage risk. They are acutely aware of the current scale and nature of these risks and the reality of what lie ahead. Following major losses in the early 1990s, the insurance industry, which embraces public, private and mutual sectors, underwent a fundamental transformation to manage its climate and catastrophic risk. Through a 'smart' underwriting of capital and reforms of regulation that set forth stringent requirements on the financial strength of insurers to meet their obligations in the most extreme circumstances, the resilience of the insurance sector has been transformed. This was essentially the result of a series of interlinked regulatory metrics, financial regulation and reporting, credit ratings, accounting standards and investor analysis and accountability.

This demanded much better understanding of climate risk and triggered a rapid evolution of scientific and analytical tools to inform management and operations. Over the last two decades, the insurance sector and its regulators have been supported by members of the global science and engineering community and the capabilities of specialist modelling organizations that have provided rigorous frameworks of hazard, exposure and vulnerability.

While there is still much to learn, the insurance industry is now far more resilient and able to meet its commitments with much greater certainty - even in years of unprecedented losses. These insights must be shared and applied across the financial sector and wider economy.

The insurance industry will save millions of lives and livelihoods and billions of dollars in the decades ahead by integrating climate and disaster risk into the very heart of economic and financial decision making. It will stimulate and reward the creation of resilient cities, prompt new metrics for asset value and vulnerability and recognize sound business.

The key metric to mainstream climate and natural disaster risk is the “1-in-100 year stress test”. It evaluates the maximum probable annual financial loss that a company, a city, a region, or even an individual farm or property, could expect once in a hundred years: one long life time. In other words, it indicates that there is a 1 percent chance of the identified disaster occurring within the next 12 months.

As part of the '*Integrating Risks into the Financial System'* initiative under the Resilience, Adaptation and DRR Action Area, the Climate Change Support Team, Executive Office of the Secretary-General, UNISDR and the World Economic Forum have convened a unique coalition of accounting organizations, asset managers, central banks, credit ratings agencies, risk modelers, financial regulators and science leaders to confirm these principles and support the goals of securing commitments to accelerated and ambitious action in Climate Summit 2014.

The Climate Summit 2014 provides the opportunity for clear, sustained commitment to support the implementation of the Hyogo Framework for Action on Disaster Risk Reduction, the achievement of the Sustainable Development Goals and the climate change convention – to make 2015 a turning point.

Overarching Objectives and Deliverables:

This initiative seeks to stimulate and reward climate resilient investments and recognize the sound business models, strategies and plans that generate societal and commercial co-benefits. It will develop, test and apply incentives in the financial system. It also seeks to strengthen the support to the science and data required for analyses of risk that underpins these changes to the financial system.

Specifically, a consortium of partners (from finance, science and public sector) commits to:

- Invest a year in preparation and pilot application of 1-in-100 year climate risk metrics across banking and securities regulation; incorporate them within public and private accounting standards; require reporting of these metrics on an annual basis based on the tools and experience of the insurance industry.

- Liaise further with the relevant regulatory authorities and stakeholders through to the end of 2015 to determine how this approach can be applied and implemented within processes and protocols with an aspiration for climate and disaster risk and resilience to be incorporated within the financial system by 2020.

- Establish a Resilience Modelling & Mapping Forum that will bring together leaders from the science, capital and policy domains to coordinate research programmes and data collection; create and maintain common standards; and provide shared, open, modelling and mapping platforms to enable urgently needed interoperability and services

- Coordinate at least $100 million annual investment into public science research by the global insurance industry from 2016 onwards and that this can support aligned funding and shared programs and facilities with public agencies.

Working with UN partner agencies, working groups and member governments, provide guidance on the appropriate language and elements that can be consistently incorporated into the 2015 processes including the post-2015 framework for disaster risk reduction, the SDGs and COP21 in Paris to provide the optimal linkage between these instruments and the global financial system.

Base-line, targets and impacts:

Currently, only the insurance industry routinely tests its investments against annual losses associated. By 2015 it will develop and initiate adoption of standards for risk evaluation that subjects portfolios and assets to a 1-in-100 year stress test and integrate these standards into financial instruments. It will initiate implementation of guidelines and standards for financial system and products by 2020.

Alliance structure and mechanisms for monitoring and reporting:

Partners convene within the framework of the 1-in-100 Initiative with support from the UN Office for Disaster Risk Reduction (UNISDR) and the World Economic Forum. The 1-in-100 Initiative will report back with a statement of progress and recommendations with respect to contributions to the UNFCCC outcomes. As part of the initiative, sustained reporting mechanisms associated with appropriate international bodies, frameworks and accounting/ratings services will be established.

The initiative remains open to all interested governments and businesses and welcomes suggestions, and ideas.

Committed partners

1. Carbon Disclosure Project (CDP)
2. Future Earth - International Council for Science
3. International Cooperative & Mutual Insurance Federation (ICMIF)
4. International Insurance Society (IIS)
5. PricewaterhouseCoopers (PwC)
6. Prince's Accounting for Sustainability Project (A4S)
7. Standard & Poor’s Ratings Services
8. United Nations Office for Disaster Risk Reduction (UNISDR)
9. Willis Group

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