

CLIMATE CHANGE INSURANCE NEEDS



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The role of insurers in tackling climate change: challenges and opportunities

Climate change is a global challenge posing material risks to society and the economy. Its consequences are becoming more and more apparent particularly on physical risk exposures, for instance in terms of increasing frequency and severity of natural disasters, such as floods, droughts or wildfires. Regarding Europe, EIOPA's dashboard on the insurance protection gap for natural catastrophes shows that currently only around a quarter of the total economic losses caused by extreme weather and climate-related events are insured, leading to a substantial insurance protection gap. The insurability and pricing of climate-related risks become increasingly critical concerns for

insurers and policymakers, and if no countermeasures are taken, the protection gap is expected to widen.

The expected growth in physical risk exposures and insurance claims due to climate change will increase risk-based premium levels over time, potentially impairing the mid- to long-term affordability and availability of insurance products with coverage against climate-related hazards. Moreover, the increased frequency and severity of natural disasters associated with climate change can make it more difficult for insurers to predict the likelihood of future losses accurately and to price insurance products appropriately. In this context, EIOPA will regularly re-assess the appropriateness of the requirements of the standard formula regarding natural catastrophe risk, and if necessary, provide suggestions for potential changes in Solvency II.

The insurance industry has a unique role to play in addressing climate change by making society and the economy more climate resilient. Insurers can develop innovative insurance products that incentivize climate-related risk prevention, for instance through offering lower premiums to policyholders implementing climate-related adaptation measures. Such measures, like anti-flood doors or early warning systems, can reduce the policyholder's physical risk exposures and insured losses. Adaptation measures can therefore be a key tool to maintain the future supply of insurance products with coverage against climate-related hazards and help reduce the climate-related insurance protection gap in Europe.

Insurers play a critical role through innovative products incentivising climate risk prevention.

With its concept of impact underwriting, EIOPA aims to foster the development and discussion about insurance products implementing climate-related adaptation measures in Europe. To better understand the industry's current underwriting practices regarding climate change

adaptation, EIOPA conducted a pilot exercise with volunteering insurance undertakings in 2022. EIOPA found that progress is being made to increase policyholder resilience against climate change by implementing dedicated adaptation measures in insurance products and offering premium-related incentives, but the overall EU insurance market still appears to be at a relatively early stage.

EIOPA sees further room for improvement especially regarding standardising the implementation of climate-related adaptation measures in insurance contracts, for instance through dedicated risk-based certificates and programs. In its discussion paper on the prudential treatment of sustainability risks, EIOPA outlines regarding underwriting activities the framework to analyse the potential for a dedicated prudential treatment of climate-related adaptation measures in the solvency capital requirements for non-life underwriting risk.

While climate change is a growing risk for the insurance industry, it also creates opportunities. By taking a proactive approach to risk management, insurers can not only protect policyholders from losses but also ensure the long-term availability of insurance products and reduce the overall cost of insurance. It is however important to highlight that reaching the objective of adapting the society and economy appropriately to climate change requires further accompanying actions beyond the scope of the insurance industry, for instance in terms of developing and enforcing public building codes reflecting the dynamics of climate change appropriately. Besides considering Public-Private-Partnerships, public actors can also engage in improving the collection and sharing of climate-related loss data and raising awareness about climate change, thereby encouraging insurers and policyholders to adapt to climate change.

By working together, public and private actors can improve the overall understanding of climate-related risks and promote a more sustainable and resilient future. To foster climate change adaptation in the EU, EIOPA will continue its work on impact underwriting, including to raise the public awareness about climate risks and related prevention measures as well as promoting the use of open-source modelling and data.