BUSINESS ENVIRONMENT COUNCIL
商界環保協會

Climate Readiness of the Insurance Sector in Hong Kong

SECTOR BRIEFING

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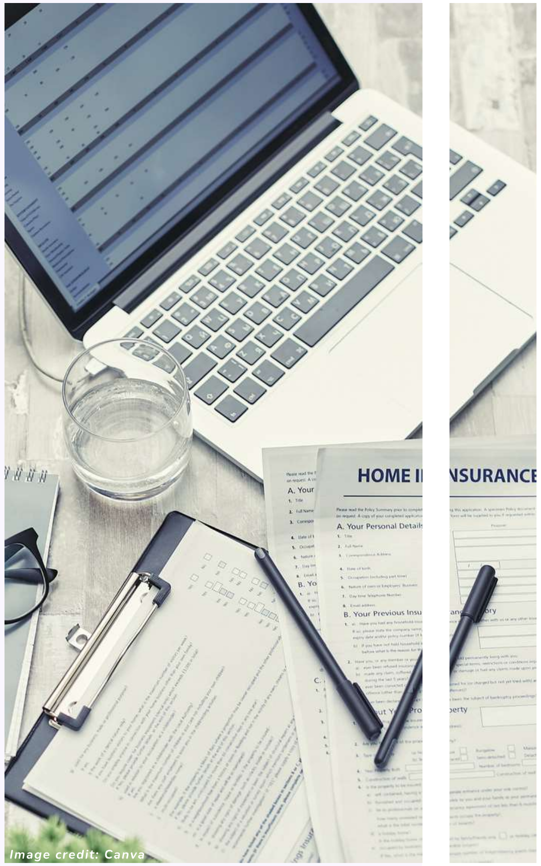

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1. Background

Business Environment Council (BEC) is supported by NWS Holdings Limited in conducting a study over the group's climate readiness for four selected sectors, namely construction, insurance, logistics, and facilities management.

The objective of this study is to comprehensively assess the level of understanding among businesses regarding the concept of net-zero. It aims to gain insights into how businesses are actively striving towards achieving net-zero goals and to understand the good practices followed by various sectors and industries in this regard. Additionally, the study aims to recognise the awareness among businesses about the global trend towards net-zero and to identify the priorities and measures that can assist them in achieving net-zero targets. By examining these points, the study seeks to provide a comprehensive understanding of the current state of businesses' efforts towards net-zero and offer valuable recommendations for achieving a sustainable and environmentally friendly future.

A comprehensive approach was adopted for this study, combining desktop research, stakeholder engagement, and expert input. It involved conducting focus group discussions with sector experts to gain an understanding of the challenges they face within their sector and gain insights into their progress towards climate transition. The focus group discussed the insurance sector's engagement with climate change, including awareness of global net-zero emissions trends and recognition of concepts like "climate transition" and "net-zero." The challenges faced by industry stakeholders in embarking on the path of climate transition were identified, along with potential incentives to drive actions. Participants also discussed policies, support, and incentives that could accelerate the sector's transition, including those implemented by the government or upstream organisations. Upon focus group discussion, an online survey was distributed to stakeholders to gather their input. This multi-faceted approach ensures a holistic understanding of the sector's climate transition progress and captures diverse perspectives from key stakeholders.

This Sector Briefing summarises the performance and challenges of the insurance sector in relation to its climate readiness, drawing on insights obtained from stakeholder engagement. It offers valuable recommendations that can support the sector in its efforts towards a sustainable and environmentally friendly future. By assessing the sector's current state, challenges and providing actionable insights, this briefing aims to contribute to the insurance industry's transition to a low-carbon economy.

2. Global Lens

Image credit: Canva

The insurance industry, as a key player in the global economy, is facing increasing challenges and responsibilities in the face of climate change. With extreme weather events becoming more frequent and severe, insurers must adapt their strategies to address the risks and opportunities associated with climate action and transition. This overview explores how the insurance sector is embracing climate change mitigation and adaptation, adapting its practices, and supporting the global transition to a sustainable future.

The insurance industry has long been aware of and involved in managing physical risks associated with the environment. When it comes to assessing and quantifying physical risks, the insurance industry has a long history of protecting its clients from extreme weather events and natural disasters. It is undoubtedly true that the industry is highly skilled in calculating premiums based on how severe weather will impact their clients, as insurers possess tremendous experience in conducting relevant analysis and research.

The increasing frequency and severity of hurricanes, floods, wildfires, and other disasters have placed significant financial strain on insurers, leading to a heightened awareness of the climate crisis. According to the Swiss Re Institute (2020), global insured losses from natural catastrophes amounted to HKD 592.8 billion (USD 76 billion), a 40% increase from 2019. Research also indicates a long-term upward trend in insured losses due to climate-related risks.

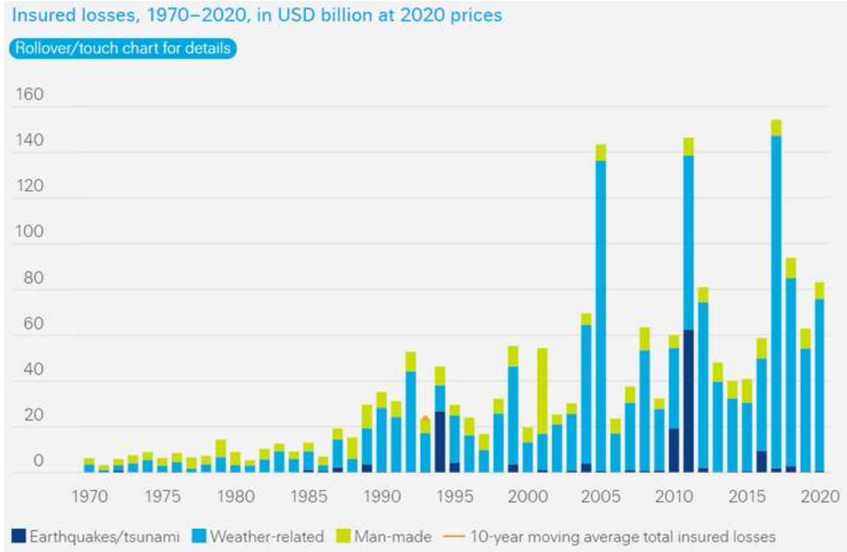

Image credit: Swiss Re Institute

Recognising the heightened climate-related risks and the potential for increased losses, the insurance industry is taking substantial steps to promote sustainable practices and invest in environmentally responsible initiatives. Climate opportunities also serve as important incentives for the industry to assume a leadership role in climate action. The industry sees the chance to be at the forefront of addressing climate change as desirable because it enables them to incorporate climate risk into premium calculations, incentivise claim mitigation, and access recovery funds in the aftermath of natural disasters (Collier et al., 2021). This directly translates into higher profits. Researchers have noted the trend of climate change being "objectified" and "commodified," as insurers and reinsurers view climate change as a potential source of profitability (Lehtonen, 2016).

With the two aforementioned reasons in mind, the insurance industry has indeed gained significant momentum in contributing to climate mitigation and adaptation. Several prominent trends have emerged as examples of the industry's climate actions:

1) Climate Risk Assessment and Mitigation

Insurers are now incorporating climate risk assessments into their underwriting processes. Advanced modelling techniques and data analysis enable them to better assess the potential impacts of climate-related risks on their portfolios. By understanding the vulnerability of various regions and industries, insurers can adjust premiums and coverage terms accordingly, encouraging climate-conscious behaviours and incentivising risk reduction.

2) Green Insurance Products

Insurers are developing innovative insurance products that focus on sustainability and climate resilience, such as the Climate Transition Risk Management solutions for identifying and managing the climate-related risks, ESG investing-focused whole life protection plans and ESG-focused savings plans. These products may include coverage for green buildings, and energy-efficient technologies. By providing specialised coverage for climate-friendly initiatives, insurers support the transition to a low-carbon economy.

3) Divestment from Fossil Fuels

A crucial aspect of climate action in the insurance sector is the shift away from investments in fossil fuels. This shift is driven by the recognition of the significant role that fossil fuels play in contributing to greenhouse gas emissions and climate change. Insurance companies are increasingly acknowledging the risks associated with investing in fossil fuel industries, including the potential for stranded assets and the financial implications of climate-related events. Many insurers are divesting from coal, oil, and gas companies, redirecting their capital towards sustainable industries and green projects. This divestment movement not only aligns the industry's investments with climate goals but also exerts financial pressure on carbon-intensive industries to transition to cleaner alternatives.

4) Climate Resilience Initiatives

Insurance companies are also actively involved in climate resilience initiatives, aiming to strengthen communities and infrastructure against climate-related impacts. They support projects such as coastal protection measures, flood defences, and reforestation efforts, which enhance resilience to extreme weather events and mitigate future losses.

5) Sustainable Governance and Reporting

In addition to their operational efforts, insurers are increasingly incorporating sustainability into their corporate governance structures. Many companies are appointing Chief Sustainability Officers or similar roles to oversee climate-related strategies and ensure they are integrated into their business operations. Moreover, transparent sustainability reporting has become standard practice, allowing stakeholders to assess insurers' progress toward their climate-related goals.

3. Hong Kong's Climate Readiness in the Insurance Sector

In the face of ever-increasing global climate challenges, Hong Kong, as a bustling metropolis perched on the cusp of environmental change, is particularly vulnerable to extreme weather events, rising sea levels, and other climate-related risks. This vulnerability has become a pressing concern for the insurance sector.

With each passing year, the frequency and intensity of natural disasters have intensified, underscoring the critical need for the insurance industry to strengthen its defences against the uncertainties that lie ahead. The industry is significantly impacted by climate change, as the heightened physical and transitional risks it poses require a reassessment of how these risks should be incorporated into the current equation. Additionally, insurers must consider adopting a new pricing and premium model to effectively address these challenges.

3.1 Current State of the Insurance Sector

Data about the industry have shown that the premium earnings of the industry for property damage have increased by around 30% from 2019 to 2021. Within the same period, the net claims incurred for property damages have increased from 1,966.1 million HKD in 2019 to 2,617.7 million HKD in 2021, a 33% jump (Insurance Authority, 2021). While it is not clear what the causes of the rises are, it will not be surprising if those damages partly arise from the increased natural events induced by climate change.

Financial institutions' experience with climate risk measurement

Image credit: HKIMR staff compilation based on the Climate Risk Measurement Survey

Despite the recent shifts in insurance claiming and earning patterns, many insurers have started early to incorporate climate change considerations into their business models and prepare for changes in the insurance landscape. A Climate Risk Measurement Survey commissioned by Hong Kong Institute for Monetary and Financial Research has shown that more than half of insurers (57%) of insurance practitioners started measuring climate risk 2 years ago or earlier, compared to only 20% of banks and asset managers (Hong Kong Institute for Monetary and Financial Research, 2022). As mentioned above, insurers are no strangers to physical environmental risks; the industry already possesses extensive knowledge of translating physical and other risks into premiums, and the industry is able to develop relevant risk assessment and pricing models that also take climate issues into account based on prior experience. With such flexibility, relative to other financial service providers, insurers are in a better position of embracing the changing climate and adapting to a highly dynamic environment.

services, driving the adoption of more sophisticated climate change discussions in the industry. Insurers are recognising the need to integrate Environmental, Social, and Governance (ESG) criteria into their investment strategies. This involves considering factors such as carbon emissions, resource usage, and social responsibility when making investment decisions.

Indeed, Hong Kong insurers are increasingly incorporating ESG principles into their investment policies as a means to manage climate-related risks and align their investments with sustainable development goals. This trend signals a growing awareness of the long-term implications of climate change on investment portfolios and demonstrates the industry's commitment to sustainable finance.

The Hong Kong insurance industry is grappling with several other climate-related trends that are affecting the game rules as well. In addition to the sophistication of climate change discussions in investment practices, 2 other trends were identified, including the relatively low popularity of ESG insurance products (such as climate risk insurance, sustainable investment-linked insurance products, etc.), and the lack of awareness among frontline workers, including insurance brokers and agents that reflect the missing growth in climate change awareness and sustainability in the local context regarding sustainability issues.

3.2 Policy Measures and Regulations

In recent years, the government has been spearheading policy support to enhance the development of green finance in Hong Kong, of which insurance is undoubtedly an integral part. The government aims to catalyse the decarbonisation of Hong Kong's financial market, including the insurance industry, by establishing a wide range of policy directions, instruments and financial supports.

Decarbonisation Strategies - Hong Kong's Climate Action Plan 2050

In 2021, to address the tremendous challenge posed by climate change, the Hong Kong SAR Government announced its high-level policy directive, "Hong Kong's Climate Action Plan 2050", which sets medium- and long-term climate goals: to reduce carbon emissions by 50% below 2005 level on or before 2035, and to achieve carbon neutrality by 2050 (Hong Kong Environmental Bureau, 2021). As one of China's cities, Hong Kong is also determined to actively contribute to Mainland China's climate goal, which is to achieve the peak of carbon emissions before 2030 and carbon neutrality by 2060. Hong Kong is facing more severe tropical cyclone threats caused by extreme weather. The Government attaches great importance to the capability of Government's infrastructure in combating climate change and extreme weather and formulated measures and implementation plans to enhance their resilience of government critical infrastructure with reference to the recommendations of the resilience study.

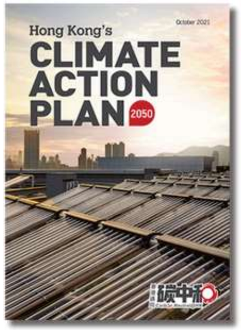

Image credit: Environment and Ecology Bureau

Policy Direction - Policy Address 2022

The Policy Address 2022 reaffirmed the importance of green and sustainable finance as a strategic decarbonisation measure, stating that we will promote the development of Hong Kong as a premier financing platform for governments and green enterprises in Mainland China and around the world (Hong Kong Special Administrative Region Government, 2022). The Hong Kong SAR Government will also develop Hong Kong into an international carbon market by expanding the issuance of the government green bonds with an increase in the total issuance amount by more than five times within the five years from 2021-22 as compared with the pre-2021-22 situation. This strategic direction aligns with the global push for decarbonisation and the transition to a low-carbon economy. Green finance is seen as an essential tool to achieve carbon neutrality by the Hong Kong SAR government. Moreover, we will implement a risk-based capital regime for the insurance industry in 2024 to align with international standards.

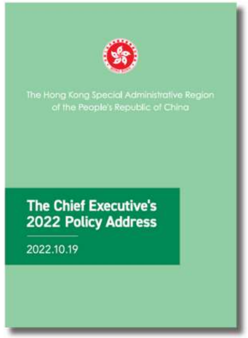

Image credit: Chief Executive's Office

Government's Visions and Missions - Development Roadmap for the Insurance Sector in Hong Kong

Image credit: Financial Services and the Treasury Bureau

In December 2022, the Hong Kong SAR Government released the Development Roadmap for the Insurance Sector in Hong Kong, which outlines a set of visions and missions that attach great importance to strengthening Hong Kong's position as a global risk management centre and insurance hub. Of particular focus is the government's commitment to fostering the growth of a green insurance industry. Recognising the significant impact of climate change and the associated risks it poses to humanity, the Roadmap emphasises the role of the insurance sector in managing and mitigating these risks while also capitalising on emerging opportunities. To achieve this, the government has devised strategies to encourage the industry to expand its market reach, address climate change issues and seize climate-related opportunities (Financial Services and the Treasury Bureau, 2022).

Regional Collaboration - Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area

The opportunities associated with and the development goal for green finance are presented and envisioned in regional and national directives as well. In addition to the local government's support, Hong Kong is embracing the opportunities of integrating into the Greater Bay Area and becoming a regional centre for green finance, as provided in the Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area. The Central Government of China has stated its support for Hong Kong to develop into an international green finance hub and strengthen its green finance leadership role in the 14th Five-Year Plan (Outline of the 14th Five-Year Plan for National Economic and Social Development of the People's Republic of China and the Long-Range Objectives Through the Year 2035) (State Council of the People's Republic of China, 2019).

Image credit: Constitutional and Mainland Affairs Bureau

Alliance of Financial Regulators - Green and Sustainable Finance Cross-Agency Steering Group (CASG)

Under the high-level policy directions for the development of green finance, the Green and Sustainable Finance Cross-Agency Steering Group (CASG) was established in 2022 by the Hong Kong SAR Government to guide and steer the green finance and insurance transition in Hong Kong. CASG comprises multiple financial regulators, including the Insurance Authority, and it was tasked to:

Image credit: Securities and Futures Commission

1. strengthening climate-related financial risk management;
2. promoting the flow of climate-related information at all levels to facilitate risk management, capital allocation and investor protection;
3. enhancing capacity building for the financial services industry and raising public awareness;
4. encouraging innovation and exploring initiatives to facilitate capital flows towards green and sustainable causes;
5. capitalising on Mainland opportunities to develop Hong Kong into a green finance centre in the Guangdong-Hong Kong-Macao Greater Bay Area; and
6. strengthening regional and international collaboration.

To achieve its goals mentioned above, one of CASG's main targets is to improve the transparency and communications of the insurance industry and its climate-related disclosure. CASG is also working towards the promotion of data and innovation in the insurance industry to aid the industry's climate transition.

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3.2.1 Climate-related Disclosure

Currently, climate-related disclosure requirements are not applicable to the entire insurance industry; only listed companies are required to report on their climate-related performance. Hong Kong Stock Exchange's (HKEX) Environmental, Social and Governance Reporting Guide (Appendix 27) dictates the major discourse requirements, including what and how companies will disclose, on a comply-or-explain basis (Hong Kong Exchanges and Clearing Limited, 2021). For listed insurance companies, the most relevant required disclosure items include the amount of Scopes 1 and 2 emissions, environmental impacts of their business activities, and community investments.

However, as mentioned above, facilitating the flow of climate-related information is one of the goals of green finance development in Hong Kong, and the disclosure requirements are expected to change abruptly in the next few years, as HKEX is exploring the adoption of the new International Sustainability Standards Board (ISSB)'s IFRS S2 Climate-related Disclosures as the next-generation ESG reporting requirement. The recent HKEX's consultation paper on altering the Appendix 27 rules has shown that a large portion of the IFRS S2 will be implemented in the near future (the year of 2025 according to the consultation paper). This indicates more demanding and challenging disclosure items, such as Scope 3 emissions, insurance-associated emissions, the impact of climate change on insurers' business models, adaptation and mitigation efforts of the insurers and insurers' plans to transition into a climate-friendly future.

In addition, in order to encourage non-listed insurance companies to assume more climate disclosure responsibilities, the Insurance Authority and CASG have collaborated with the Climate Disclosure Project (CDP) on developing Climate and Environmental Risk Questionnaire for Non-listed companies/small and medium-sized enterprises (SMEs) (Hong Kong Monetary Authority, 2023). Those questionnaires are designed for guiding smaller and non-listed insurers to understand the climate-related reporting procedures and processes and possibly attracting more SMEs and non-listed companies to conduct voluntary reporting. This document would be able to not only prompt SMEs to prepare for the proliferation of climate-related reporting activity and enhance their reporting ability but also enable the possible expansion of Hong Kong's climate transition as SMEs are now also invited to participate in the disclosure landscape.

4. Challenges

The insurance industry is greatly threatened by the emergence and deterioration of climate change. The insurance industry is extremely sensitive to risks, due to the nature of the insurance business, and the physical risks associated with climate change, as well as its unpredictability, will force the industry to transform how risks are traditionally assessed and translated into premiums that will reflect future risks.

Many of the climate-related physical risks will impact the insurers. As global temperatures rise and extreme weather events become more frequent and severe, insurers are grappling with a surge in claims related to natural disasters such as hurricanes, floods, wildfires, and droughts. The escalating frequency of these events has strained the industry's capacity to adequately cover losses and would lead to soaring payouts. Additionally, rising sea levels and coastal erosion have increased the vulnerability of properties located in high-risk areas, creating an elevated exposure for insurers. More heat-related diseases, such as heat strokes, and contagious diseases would also arise from a warming climate, and result in more health-related claims. For example, much scientific evidence has pinpointed the fact that vector-borne illnesses such as dengue fevers are very likely to become more common as a warmer climate enables insects to spread globally. There is evidence that shows a linkage between climate change and recent massive infection events such as the COVID-19 pandemic (Rodó et al., 2021).

4.1 Low Awareness and Limited Understanding of Climate Transition

Hong Kong's insurance industry faces a significant challenge with frontline workers, including insurance brokers and agents, being less aware of climate change issues. As crucial points of contact between insurers and clients, these frontline workers play a pivotal role in promoting sustainable and climate-resilient insurance solutions. However, their lack of awareness of climate change and its potential impacts on the industry may hinder their ability to effectively advise customers on relevant policies and risk management strategies, and this issue will then potentially affect the marketability of ESG-aligned products, for instance ESG funds, sustainability-linked loans, ESG insurance products, etc.

- **The ESG or climate concepts are not yet popularised**

The insurance sector in Hong Kong faces challenges in climate readiness due to low awareness regarding Environmental, Social, and Governance (ESG) concepts and climate risks. Despite the significant threats posed by climate change on the built environment and people, these concepts have yet to be widely popularised in many insurance products. This lack of awareness hinders the adoption of ESG and climate-aligned insurance products among the general public.

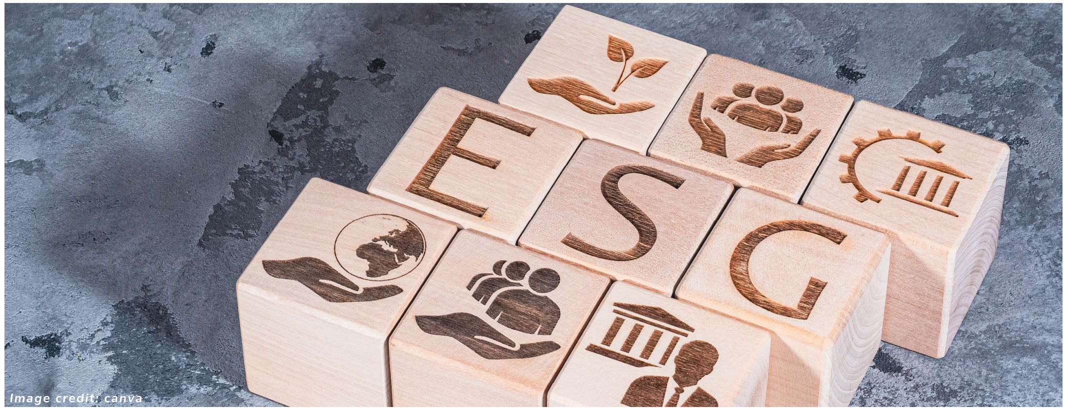
- **Difficult to account or quantity climate risks into life insurance products in the underwriting process**

One specific challenge lies in the difficulty of incorporating and quantifying climate risks in life insurance products during the underwriting process. Life insurance involves assessing long-term risks and projecting future scenarios. Climate risks, which encompass a range of complex and interconnected factors, can be challenging to account for and quantify accurately. This poses a challenge for insurers in effectively integrating climate risks into their underwriting processes for life insurance products.

- **Low popularisation of green insurance products among the general public**

Another contributing factor to the low awareness is the limited understanding of climate transition among brokers and agents. Their lack of knowledge and awareness regarding climate-related risks and the importance of ESG considerations can hinder the popularisation of green insurance products. Efforts have been made by both the private and public sectors to address this.

For instance, initiatives like the AXA Academy and the Hong Kong Monetary Authority (HKMA) have taken steps to raise awareness and build capacity in the insurance industry. AXA Climate School offers comprehensive online training for global companies to upskill and engage employees in sustainable transition. On the other hand, HKMA offers free learning resources and paid courses on sustainable development, ESG investment and market trends. It is noted that there is a need to further strengthen capacity building efforts to ensure that brokers and agents are well-equipped to promote and explain the benefits of green insurance products.



4.2 Low Popularity of ESG Insurance Products

- **Challenges of effectively communicating the benefits of ESG insurance products to customers**

The insurance sector in Hong Kong faces significant challenges when it comes to the low popularity of Environmental, Social, and Governance (ESG) insurance products. One of the main obstacles is effectively communicating the benefits of ESG insurance products to customers. There is often a mismatch between how insurance providers perceive the role of ESG in insurance products and how customers understand and prioritise these factors. Insurers recognise the importance of integrating ESG considerations to manage climate risks, but customers may prioritise financial returns and traditional insurance coverage, unaware of the broader societal and environmental implications.

This low awareness creates a disconnect between intensified climate risks and the public's perception of the need for additional insurance coverage. Many individuals fail to connect the dots between the increasing frequency of extreme weather events and the necessity for enhanced protection. The lack of awareness hinders their understanding of the potential risks they face, leading to a reluctance to invest in comprehensive coverage that adequately safeguards against climate-related perils.

The limited public awareness of ESG and climate change poses a significant obstacle for insurers in effectively conveying the urgency of adapting to evolving risks and fostering a culture of preparedness. Without a deep understanding of the relationship between climate change and insurance needs, customers may overlook the value and benefits of ESG insurance products. This, in turn, hinders insurers' ability to promote and popularise these products, which are specifically designed to address climate-related risks and support sustainable practices.

4.3 Risks of Greenwashing

- **Many funds or investment portfolios that claim to be sustainable might actually contain unsustainable assets**

The insurance industry faces a significant challenge related to the risks of greenwashing. Greenwashing refers to the misleading or exaggerated claims made by funds or investment portfolios about their sustainability or ESG credentials. While many funds and investment products claim to be sustainable or environmentally friendly, there is a concern that they may actually contain unsustainable assets or fail to meet the expected ESG standards.

This challenge arises due to the lack of standardised definitions and regulations surrounding sustainable investments. Without clear guidelines and oversight, there is a risk that some investment products may engage in greenwashing practices to attract environmentally conscious investors. This poses a problem for the insurance sector, as insurers may offer investment-linked insurance products that include such funds, inadvertently promoting greenwashing and misleading customers.

The risks of greenwashing extend beyond the reputational damage to both insurers and the investment industry as a whole. It also undermines the effectiveness of sustainable investments in driving positive environmental and social change.

The heightened risk of greenwashing presents substantial challenges for the insurance industry in the Southeast Asian region. This risk is amplified by the region's relatively less stringent sustainable finance regulations and the absence of clear definitions for sustainable assets, in contrast to markets where more mature and developed regulation has been implemented to prevent greenwashing, such as the European Union market. Without robust regulations and precise criteria to distinguish sustainable assets, asset managers and securities issuers have great flexibility in self-determining and proclaiming if their products are sustainable. In some cases, if investors unknowingly invest in funds that contain unsustainable assets, their capital may inadvertently support activities that contribute to environmental degradation or social harm. This misalignment between investors' intentions and the actual impact of their investments can erode trust and confidence in sustainable finance and impede progress towards climate readiness.

Investing in greenwashed products and securities would expose insurers to substantial risks, including impaired long-term investment return and reduction of their ability to create profits and value. This challenge reflects the insufficient collaboration between regulatory bodies, industry stakeholders, and insurers on establishing transparent guidelines and promoting responsible practices in sustainable finance, which is supposed to safeguard both the environment and the development of the insurance sector.

4.4 Difficult in Deducing Scope 3 Emissions

- **Lack of standardised methodologies to compare emissions across companies in the insurance sector and hence lead to inconsistent reporting practices**

The insurance sector in Hong Kong faces challenges in calculating Scope 3 emissions, particularly for investors and companies involved in providing financial services to manage their investment portfolios. Scope 3 encompass indirect greenhouse gas emissions generated by activities outside the direct control of companies. One of the key obstacles is the lack of standardised methodologies to compare emissions across companies within the insurance sector, resulting in inconsistent reporting practices. Without consistent methodologies, it becomes challenging to accurately assess and compare Scope 3 emissions, hindering efforts to measure and manage the sector's environmental impact effectively.

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- **Difficult to determine the boundary setting in Scope 3 calculations as the sector interacts with various stakeholders, including policyholders, reinsurers, and investment partners, also the sector includes a wide range of activities (e.g. underwriting policies or investing in companies)**

Another challenge lies in determining the boundary setting for Scope 3 calculations within the insurance sector. This is because the sector interacts with multiple stakeholders, including policyholders, reinsurers, and investment partners, and engages in a wide range of activities such as underwriting policies and investing in companies. The complexity arises from identifying which activities and stakeholders should be included in the emissions calculations, making it difficult to establish clear boundaries. The interconnected nature of the insurance industry further complicates the process of attributing emissions accurately to specific activities or partners, thereby impeding comprehensive measurement of Scope 3 emissions.


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4.5 SME's Passive Role in Decarbonisation

- **Smaller insurers are less active in decarbonisation, compared to larger companies**

In Hong Kong, the insurance sector faces a challenge in achieving decarbonisation due to the passive role of small and medium-sized enterprises (SMEs) within the industry. It has been observed that smaller insurers tend to be less active in decarbonisation efforts when compared to their larger counterparts.

This passive role of SMEs in decarbonisation can be attributed to various factors. Firstly, smaller insurance companies may have limited resources and capacities to invest in sustainable practices and initiatives. Decarbonisation efforts often require significant financial investments, research and development, and infrastructure upgrades, which can be more challenging for SMEs with constrained budgets and limited economies of scale.

Secondly, smaller insurers may lack the necessary expertise and knowledge to navigate the complexities of decarbonisation strategies. Implementing sustainable practices and transitioning to low-carbon operations require specialised skills, technical know-how, and access to relevant networks. SMEs may face challenges in acquiring and retaining talent with expertise in sustainability and climate-related issues, which can hinder their ability to actively engage in decarbonisation efforts.

Moreover, the passive role of SMEs in decarbonisation may also stem from a perception that sustainability initiatives are more relevant to larger companies with greater resources and market influence. SMEs may prioritise immediate operational concerns and cost management, perceiving decarbonisation as a secondary priority. This mindset can lead to a lack of proactive actions and a limited focus on integrating sustainability into business strategies and operations.

5. Recommendations

The unpredictability and climate change have added another layer of uncertainties and difficulties to insurers' long-term profitability and sustainability. As the climate crisis persists, the insurance industry faces the critical task of adapting its risk models, developing new products, and collaborating with governments and policymakers to foster resilience and ensure the continued availability of affordable coverage for communities at risk. Due to our limited understanding of climate change and its long-term consequences on society and the economy, insurance companies, particularly those focused on long-term coverage, will encounter challenges in accurately assessing and evaluating the financial implications of climate change.

Addressing climate transition in Hong Kong requires the collective efforts and involvement of various industry stakeholders. Businesses across sectors, including finance, energy, transportation, and real estate, need to recognise the urgency and importance of climate action. Collaboration among industry players is crucial to share best practices, develop innovative solutions, and drive the adoption of sustainable technologies and practices. Additionally, policymakers and regulators play a vital role in creating an enabling environment through the implementation of supportive policies, frameworks, and incentives to encourage climate-friendly investments and practices.

Engaging consumers and raising awareness about the importance of individual actions in mitigating climate change is also essential. By working together, industry stakeholders can collectively address climate transition, reduce greenhouse gas emissions, and build a sustainable and resilient future for Hong Kong.

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Statutory Body

Image credit: Canva

Industry Practitioners

Image credit: Canva

Joint Effort

5.1 Statutory Body

Enforce Clear Guidelines and Standards

01 Mandate insurers to integrate climate considerations into their business operations

The statutory body plays a vital role in facilitating the climate transition of Hong Kong's insurance industry by providing a conducive regulatory and policy environment. By imposing regulations that encompass climate risk disclosure requirements, the statutory body creates a framework that incentivises insurers to be transparent about their climate-related practices and investments.

Through the mandated integration of climate considerations, insurers are compelled to assess and manage climate risks effectively. This involves incorporating climate risk models and data into their underwriting processes, enabling them to accurately evaluate the potential impact of climate change on insured assets and liabilities. By integrating climate risk analysis, insurers can develop appropriate coverage options and price premiums that reflect the true risk associated with climate-related events. This not only enhances the sector's ability to manage climate risks but also promotes the long-term viability and profitability of insurers in the face of a changing climate.

Moreover, by enforcing climate risk disclosure requirements, the statutory body fosters transparency within the insurance sector. Insurers are encouraged to disclose information about their climate-related practices, strategies, and investments, providing stakeholders with valuable insights into their climate readiness. This transparency enables customers to make informed decisions when selecting insurance products, while investors can assess insurers' alignment with climate goals and their contribution to sustainable development.

Additionally, the integration of climate considerations incentivises insurers to adopt proactive measures to mitigate climate risks. Insurers may develop innovative products that incentivise customers to adopt sustainable practices or provide coverage for green technologies. By aligning their investments with low-carbon and environmentally responsible activities, insurers can contribute to the financing of climate-friendly projects, supporting the transition to a greener economy in Hong Kong.

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5.1 Statutory Body

Extend ESG Disclosure to Non-Listed Companies

01 Boost climate data availability and transparency but enable the public and investors to holistically scrutinise the ESG performance of insurers

As mentioned above, only listed companies are currently required to conduct ESG disclosure and reporting, while non-listed companies are not required. By expanding the scope of ESG disclosure, the availability and transparency of ESG data can be significantly boosted. In order to enhance data availability, the Green and Sustainable Finance Cross-Agency Steering Group (CASG), co-chaired by the Hong Kong Monetary Authority and the Securities and Futures Commission, has recently provided more tools on its official website in February 2024, including the sustainability disclosure e-portal with digitalised CDP questionnaires, GHG emissions calculation tools and estimation tools of the GHG emissions associated with their investments for financial institutions. This enables both the public and investors to holistically scrutinise the ESG performance of insurers and facilitates informed decision-making.

Furthermore, extending ESG disclosure to non-listed companies would promote transparency within the insurance sector. The public and investors would gain access to a wider range of ESG information, allowing for a more holistic assessment of insurers' commitment to sustainability. This transparency would enable stakeholders to make informed decisions and identify insurers that align with their values and climate goals. It would also encourage healthy competition among insurers, driving them to improve their ESG performance and climate resilience.

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5.1 Statutory Body

Financial Subsidies

01 Establish financial subsidies to actively promote and invest in sustainable products for market stabilisation and balance with financial returns

This would be a particularly important consideration for Hong Kong as the city is now developing its ESG regulations and requirements. Considering the substantial uncertainties of climate change, and how it would develop in the future, the insurance sector could bear the tremendous loss if the actual impact and, hence the damages of climate change are more severe than estimated. The government might consider producing financial support for the insurers to enhance their resilience against unexpected losses caused by climate change.

It is also recommended that the government adopt a comprehensive approach in which both positive and negative incentives are provided to accelerate the climate transition of the insurance industry. By providing positive incentives, such as grants, or subsidies, the government can encourage insurers to develop climate-friendly products and services. These rewards can stimulate innovation and attract private sector involvement in sustainable initiatives.

Image credit: Canva

5.2 Industry Practitioners

Integrate Climate Issues into the Industry

Insurers should further the integration of climate issues into the industry 01

Fostering the integration of climate issues into Hong Kong's insurance industry is crucial for its climate transition. To achieve this, the industry should proactively incorporate climate-related risks and opportunities into its business strategies. This includes conducting comprehensive risk assessments and scenario analyses to identify climate-related vulnerabilities in their portfolios and developing innovative insurance products that address emerging climate risks.

The integration of climate issues into the industry involves developing comprehensive frameworks and tools to evaluate these risks. The Hong Kong Monetary Authority's (HKMA) climate stress test, for instance, allows insurers to assess the potential impact of climate-related events on their portfolios and solvency. By subjecting insurers to various climate scenarios, the stress test enhances their understanding of the financial risks associated with climate change and encourages them to strengthen their risk management practices.

Moreover, the efforts of the statutory bodies and regulators are crucial in facilitating the integration of climate issues. They provide guidance, establish standards, and enforce regulations that promote climate readiness within the insurance sector. The HK Insurance Authority's related plan, for example, outlines a roadmap for insurers to integrate climate considerations into their business operations. This plan can include initiatives such as risk assessments, product innovation, and training programs aimed at enhancing insurers' climate resilience and sustainability.

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5.2 Industry Practitioners

Incorporate Climate-related Risks and Opportunities into Business Strategies

Actively conduct comprehensive risk assessments and scenario analyses 01

Within the insurance sector, it involves a complex and evolving nature of climate-related risks. Insurers need to assess potential risks associated with extreme weather events, changing regulatory landscapes, and shifts in consumer behaviour driven by climate concerns.

By actively conducting comprehensive risk assessments, insurers can gain a better understanding of the potential impacts of climate change on their operations, including their underwriting practices, investments, and claims exposure. Scenario analyses play a vital role in assessing climate-related vulnerabilities. Insurers can develop a range of scenarios that consider various climate trajectories and their potential consequences. This allows insurers to stress-test their portfolios against different climate scenarios, evaluating the financial implications and identifying areas of vulnerability. By incorporating climate-related scenarios into their risk assessment processes, insurers can make informed decisions and develop robust strategies that account for climate risks.

Develop Innovative Products

Develop innovative insurance products to address emerging climate risks 01

Unleashing the benefits of innovative practices and products and the strategic usage of data are the main drivers of decarbonisation within the insurance industry in Hong Kong.

Insurers can leverage technology and data analytics to develop innovative products that address climate risks more effectively. Utilising satellite imagery, climate models, and sensor data, insurers can assess risks in real-time and provide proactive risk management solutions. For instance, insurers can offer usage-based insurance products for electric vehicles, where premiums are based on actual driving behaviour and carbon emissions. This encourages sustainable transportation choices and helps reduce greenhouse gas emissions.

Moreover, the government can foster public-private partnerships to support research and development of innovative insurance products tailored to address climate challenges. Collaborative efforts can lead to the creation of more comprehensive and affordable climate-related insurance solutions.

5.3 Joint Effort

Foster Partnership

Collaboration between insurers, statutory bodies, and regulators is vital to overcome the challenges in integrating climate issues into the industry. Regular dialogues and consultations can ensure that the frameworks and guidelines align with the evolving understanding of climate risks. Furthermore, sharing best practices and knowledge exchange among industry stakeholders can foster innovation and accelerate progress in climate readiness. However, it is important to recognise that integrating climate issues into the insurance industry requires a long-term commitment and collaboration.

Aside from partnering with statutory bodies and regulators, partnerships with climate experts, research institutions, and environmental organisations can provide valuable insights and enhance the industry's understanding of climate challenges. By adopting transparent reporting practices on climate-related initiatives and progress, the insurance sector can build trust with stakeholders and attract ESG-conscious investors. Increasing collaboration between the insurance sector and academia can also foster capacity-building as the academia can continue to provide up-to-date climate science and information and thus, allow insurers to be continuously informed.

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5.3 Joint Effort

Capacity Building

01 Equip insurance professionals with skills to address climate concerns and provide clients with climate-resilient solutions

To enhance capacity building within the insurance sector in Hong Kong, it is essential to focus on sustainability education and awareness-building. The government should invest in comprehensive sustainability education programs to empower citizens with knowledge about environmental issues, sustainable finance, and responsible investment strategies. Initiatives like the "Chin Family" platform managed by the Investor and Financial Education Council (IFEC) can be expanded to offer more learning opportunities and promote sustainable insurance products to the general public in a simple and enjoyable way. The Chin Family Financial Literacy Schools Programme, commissioned by the Investor and Financial Education Council, acts as an example in effectively communicating financial topics to students. This program supports schools in implementing a comprehensive approach to financial literacy education and integrating it into their curriculum, along with values education. To further promote sustainable and green finance knowledge, it is important to explore additional collaborations with the Chin Family. This can involve leveraging the Chin Family platform to provide educational resources and tools that specifically focus on sustainable and green finance. By expanding these collaborations, the public can be better educated about the principles and practices of sustainable finance, leading to more informed financial decision-making and a greater emphasis on environmental sustainability.

Image credit: Investor and Financial Education Council

In addition to government efforts, the insurance sector itself needs to undertake initiatives to enhance public awareness and education. This can be achieved through collaborative campaigns with environmental organisations and government agencies to highlight the importance of ESG factors in insurance products and the role of insurers in managing climate risks. Equipping insurance professionals with the necessary skills and knowledge to address climate risks is crucial. Training programs should be developed to enhance their understanding of climate science, risk assessment methodologies, and sustainable insurance solutions. By providing comprehensive education and professional development opportunities, insurance professionals can effectively assess and manage climate-related risks, and offer clients climate-resilient insurance solutions.

Furthermore, insurers can bridge the gap between customer expectations and ESG considerations by developing tailored insurance products that align with customers' financial goals while integrating ESG factors. Clear and transparent communication about product features and benefits is crucial to help customers make informed decisions and appreciate the value of ESG-aligned insurance coverage.

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Collaboration among insurance companies, industry associations, and regulatory bodies is vital to develop comprehensive guidelines and standards for incorporating climate risks in insurance practices.

02 Increase collaboration between the sector and academia

Moreover, academia can play a significant role in conducting research that informs the development of innovative insurance products and risk assessment models. By partnering with academia, insurers can leverage scientific expertise to enhance their understanding of climate-related risks and develop cutting-edge solutions. This collaboration can result in the creation of tailored insurance products that effectively address the unique climate risks faced by individuals, businesses, and communities in Hong Kong.

Through enhanced education, the insurance industry can then cultivate a more environmentally literate customer base, driving demand for green insurance products and encouraging insurers to integrate sustainability considerations into their offerings, thereby contributing significantly to Hong Kong's journey towards a more sustainable future. Frontline workers and customers being more aware of sustainability issues will catalyse the climate transition of the insurance industry, as frontline workers can help promote sustainable products to their clients, and customers are more willing to purchase sustainability-aligned and climate-friendly products.

And again, investing in continuous education and capacity-building programs for insurance professionals will ensure they are equipped to effectively address climate concerns and provide clients with climate-resilient solutions. Through these joint efforts, the insurance industry can play a pivotal role in advancing sustainable development in Hong Kong while contributing to global climate resilience goals.

6. Conclusion

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The challenges faced by the insurance industry in Hong Kong are multifaceted and require comprehensive and collaborative efforts from various stakeholders. The impacts of climate change pose a significant threat to the industry, with rising temperatures and increasing extreme weather events leading to mounting claims and strained capacity.

The lack of awareness among the public about climate risks and the disconnect between these risks and the need for enhanced insurance coverage further exacerbate the situation. Additionally, the unawareness of climate change issues among insurance brokers and agents, coupled with the risk of greenwashing, adds complexity to the industry's transition towards sustainability.

In the face of the challenges encountered by the insurance sector, a concerted effort from all stakeholders is necessary to transform Hong Kong's insurance industry into a resilient and environmentally responsible sector. By fostering awareness, integrating climate considerations, and implementing transparent standards, the industry can contribute to both local sustainability goals and global climate resilience efforts.


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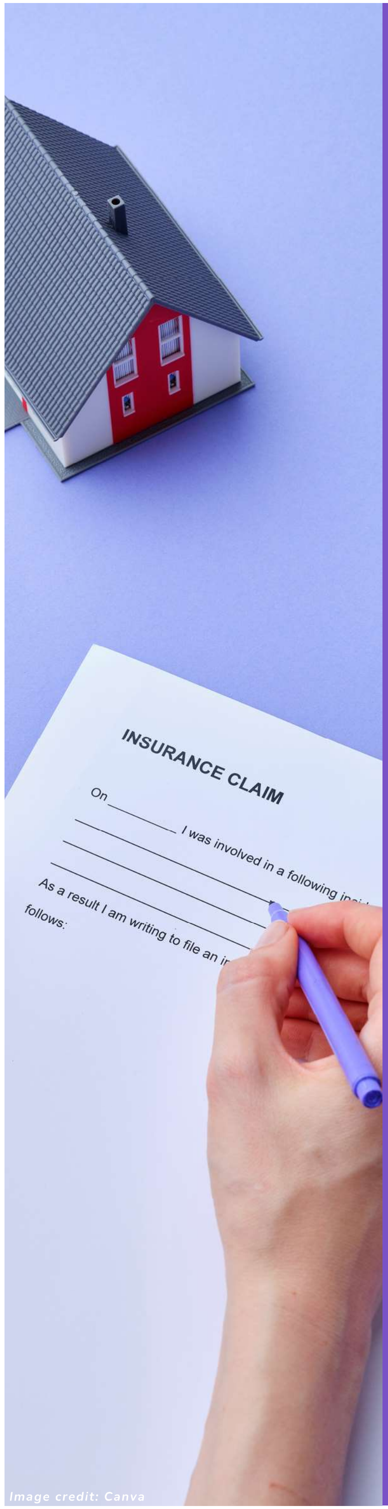

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About BEC

Business Environment Council Limited ("BEC") is an independent, charitable membership organisation, established by the business sector in Hong Kong. Since its establishment in 1992, BEC has been at the forefront of promoting environmental excellence by advocating the uptake of clean technologies and practices which reduce waste, conserve resources, prevent pollution and improve corporate environmental and social responsibility. BEC offers sustainable solutions and professional services covering advisory, research, assessment, training and award programs for government, business and the community, thus enabling environmental protection and contributing to the transition to a low-carbon economy.

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