2022 Insurance Development Event

Current macro and global challenges

The Insurance Institute of Guernsey
Chartered Insurance Institute

Sustainability Version 2.0.2.2

‘Climate risk, pandemia, and war have finally morphed into good (sic) old-fashioned supply and demand shocks, inflation and, most likely, recession.’

Dr Andy Sloan

Netherite & Grunweldt Advisory
CLIMATE CAPITAL & RISK

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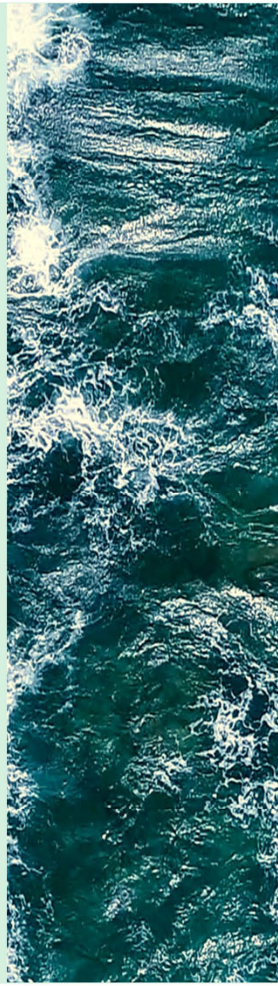

First some introductions…

Dr Andy Sloan

MD, Netherite & Grunweldt Advisory

Founder, International Sustainability Institute, Channel Islands

Non-executive Director

Past roles
IPCC AR6 Expert Reviewer
Established Guernsey Green Finance
Deputy CEO, Guernsey Finance
Director Financial Stability & International Policy Advisor, GFSC
States Economist, Fiscal and Economic Policy Advisor

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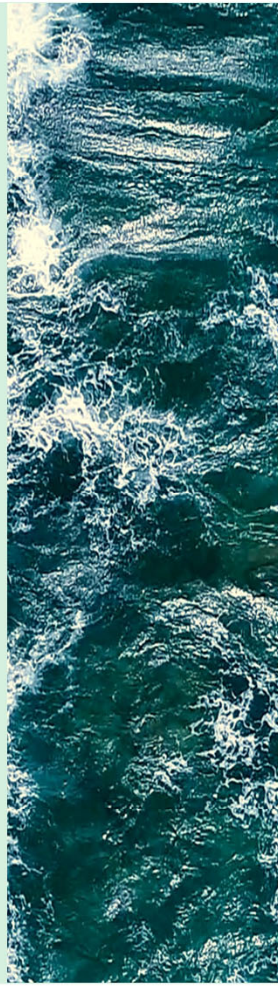

Agenda

The International Security implications of the war in Ukraine — Not good

The resultant direct impact on energy and food commodity prices — Not good

The impact of these commodity price increases on inflation, cost of living globally and a global supply chain that is still recovering from the Covid-19 pandemic — Not good

The impact of the war in Ukraine on European/UK/Guernsey energy supply – and how does this change priorities in terms of action on climate change — Not good

Any current developments/ trends in climate risk and the economy — I'm sure there are some

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Agenda

The International Security implications of the war in Ukraine — Permanent

The resultant direct impact on energy and food commodity prices — Transitory

The impact of these commodity price increases on inflation, cost of living globally and a global supply chain that is still recovering from the Covid-19 pandemic — Transitory

The impact of the war in Ukraine on European/UK/Guernsey energy supply – and how does this change priorities in terms of action on climate change — Transitory

Any current developments/ trends in climate risk and the economy — Permanent

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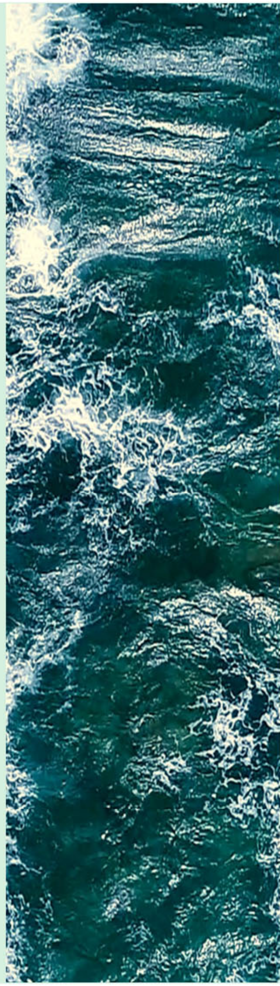

Global Imbalances and ‘Sloan’s Law’

Monetary

Fiscal

Debt

Trade

“Things can remain in an unsustainable position for a very, very long time.”

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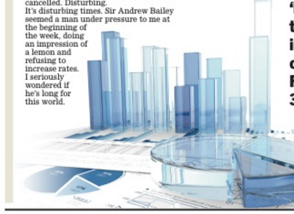
'All progress depends on the unreasonable man'

Andy Sloan offers his thoughts on Kwasi Kwarteng's mini-budget

UK chancellor Kwasi Kwarteng. (31314024)

KAMIKWASI? I don't think so. At the Credit Suisse golf dinner on Saturday night I got asked what I thought about Kwasi Kwarteng's fiscal measures last Friday.



'Flabby, consensual policy thinking is pretty de rigueur in 2022. Someone has to challenge the consensus. Remember the names of the 364 economists that wrote to The Times to condemn Margaret Thatcher's economic policies in 1981? No? I didn't think so'

Never mind Kwasinomics – we're all socialists now

Guernsey's spending growth is out of control – and it's making us poorer and less internationally competitive, argues **Andy Sloan**

ORDINARILY, this column appears on the last Thursday of the month.

'Balancing the books long term is going to need several coordinated moves ... cutting spending must be part of the mix'

And the booby prize goes to...

With inflation rampant **Andy Sloan** rates past performance of central bankers

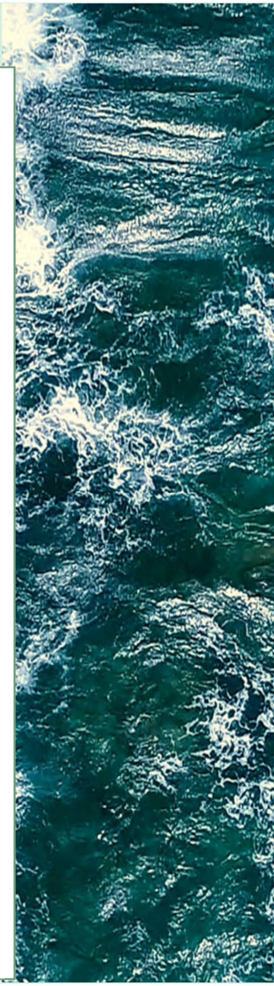
Former Governor of the Bank of England Mark Carney, whose tenure began in July 2013 and ended in March 2020, oversaw a decade of free money creating a range of new structural imbalances. All unsustainable, says Dr Sloan. (31182079)

SPOILER alert. Mark Carney.

Christine Lagarde has served as President of the European Central Bank since November 2019. (31182092)

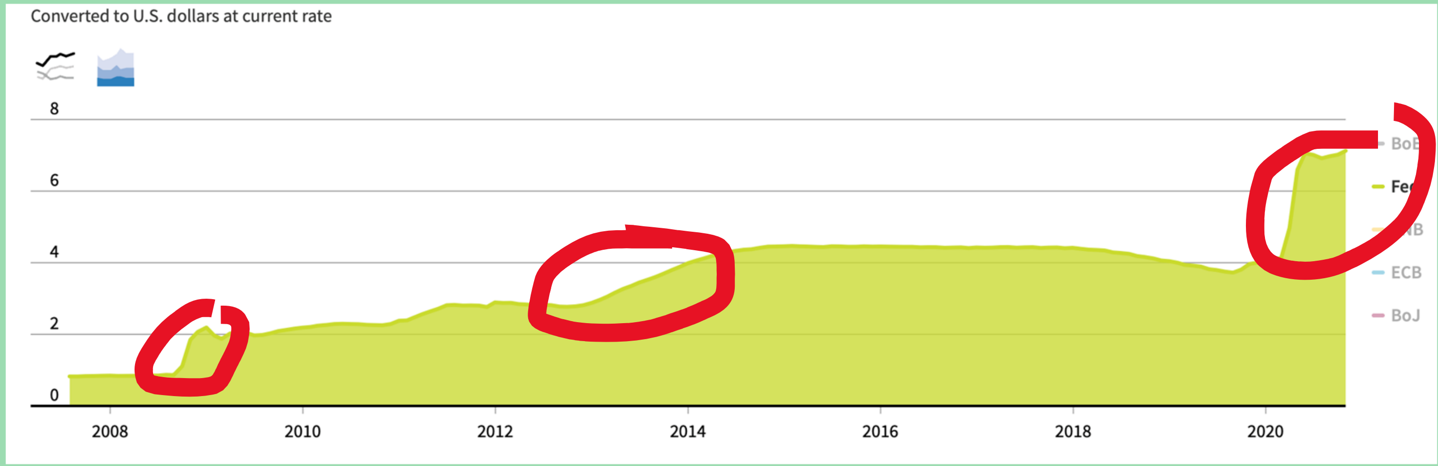
'Economic policy debate was absent throughout this wasted decade. Group think prevailed. Policy makers and technocrats instead busied themselves with consensus moves without critique. No thought to real world consequences or costs'

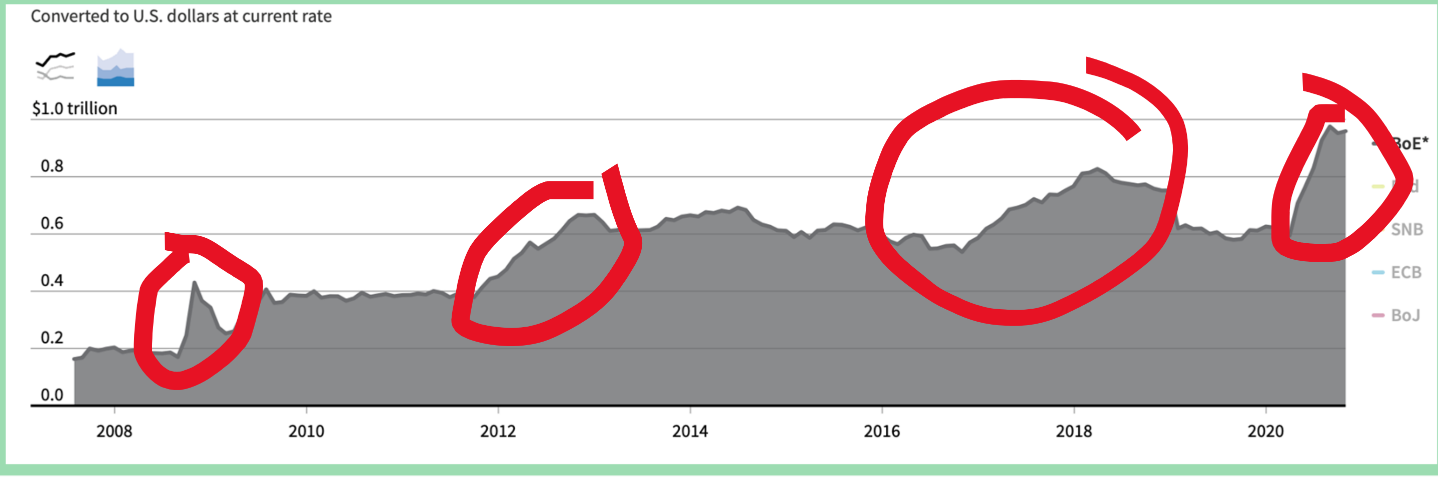
Andrew Bailey has been Governor of the Bank of England since 16 March 2020. (31182101)



Monetary policy

Monetary policy





Global debt issuance: non financials

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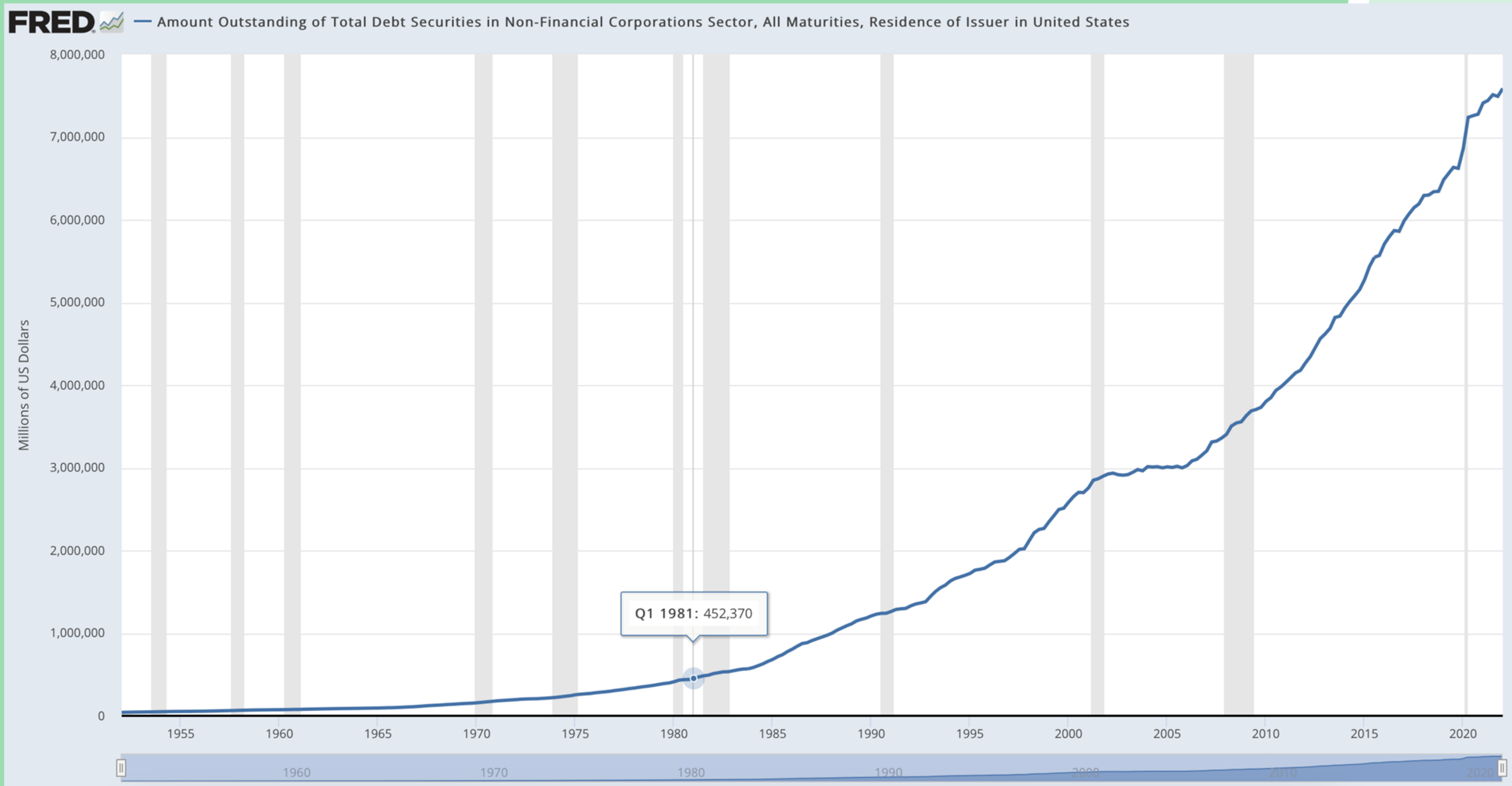
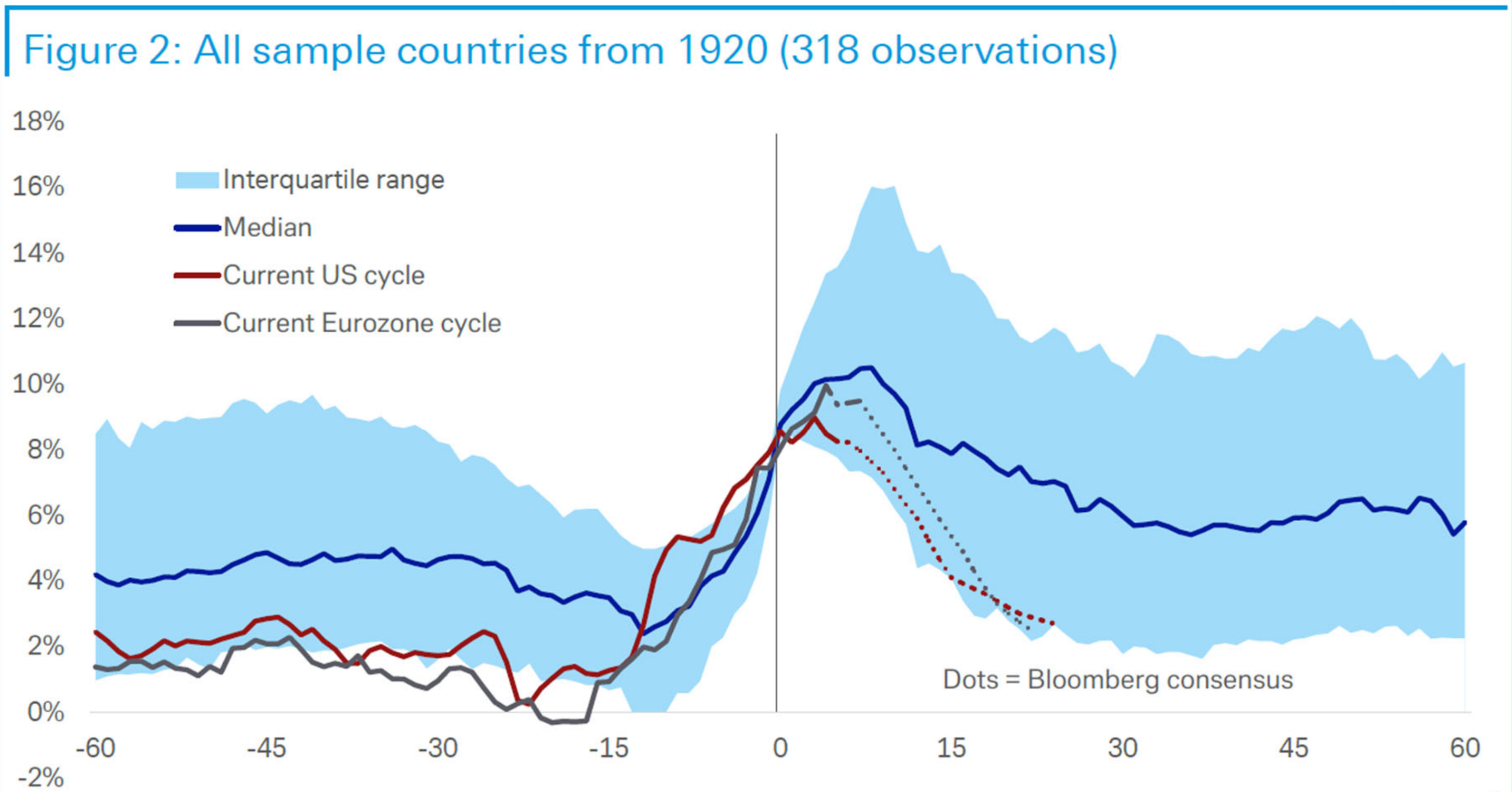


Inflation



Source : GFD, Bloomberg Finance LP, Deutsche Bank

UK and Italy

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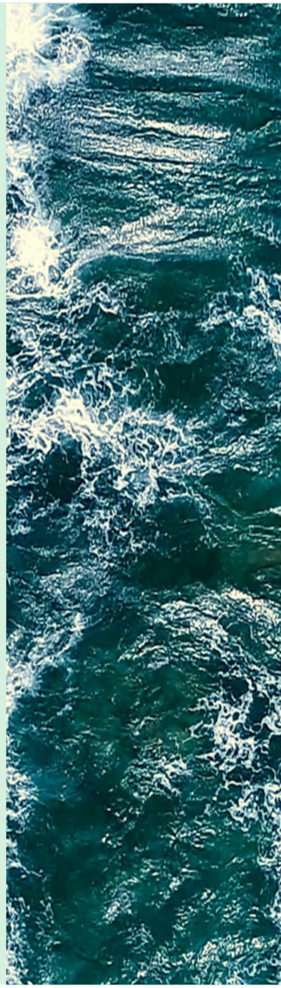
'We're off to Italy for a spot of political stability.'



UK and Italy

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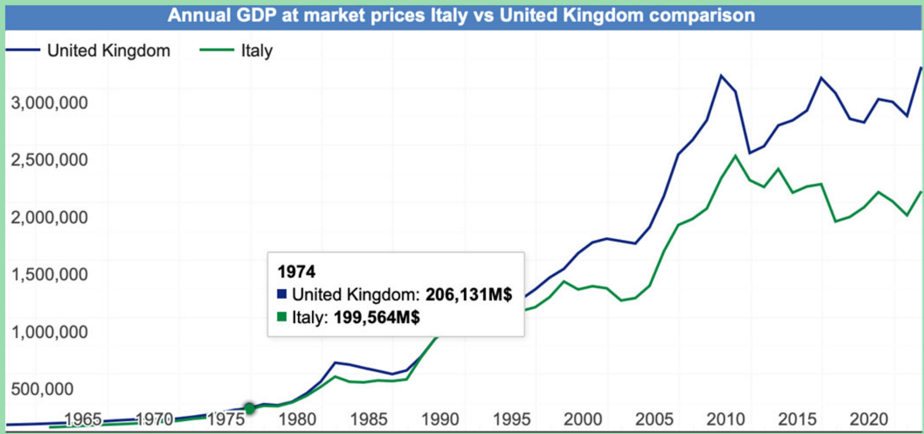

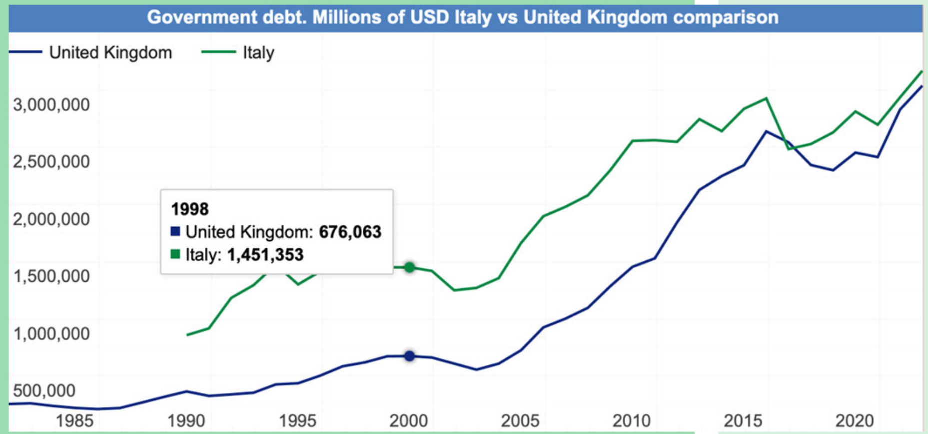

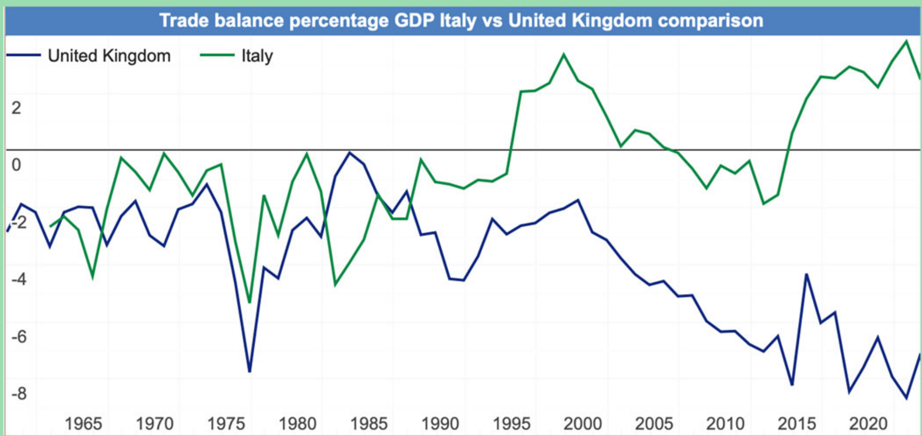

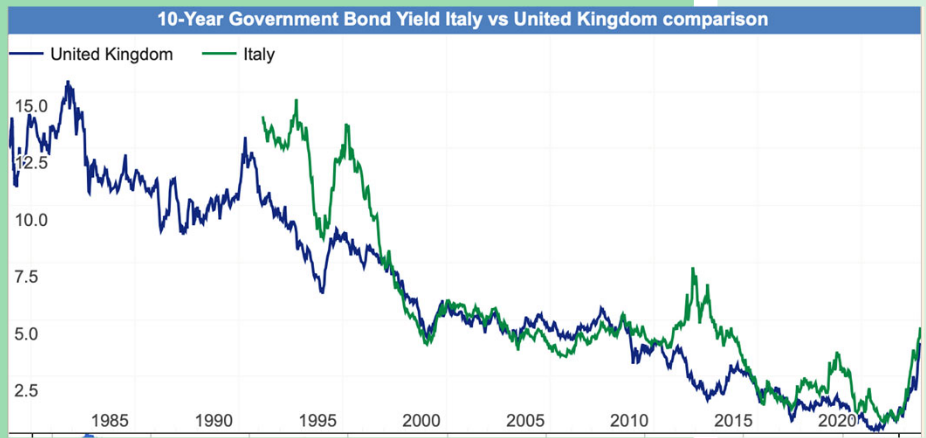

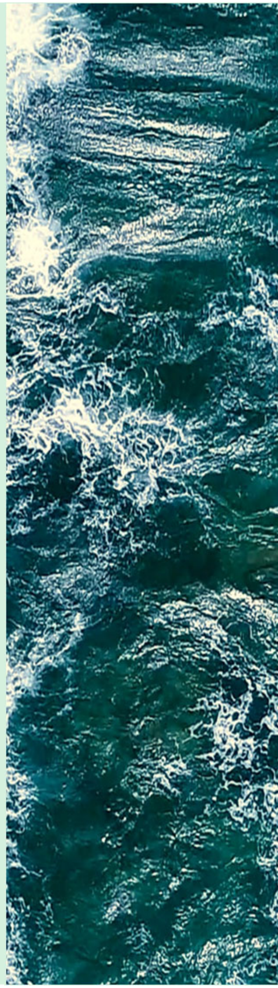

Climate Risk and reporting in the Channel Islands

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Climate risk should not just be a tick-box exercise

Climate change is not going away, despite having been displaced by more populist concerns, says **Andy Sloan**

'ALL firms, following our environmental amendments to the Code of Corporate Governance in 2021, need to consider how to adapt their business models as a matter of urgency as international standards on environmental sustainability are quite likely to be promulgated over the course of 2022.'

The Guernsey Press this week reported this nugget from William Mason's contribution to the GFSC's 2022 Annual Report. The report added that the GFSC had said its intent 'was to encourage firms not so advanced in their sustainability thinking to prepare for a future where green considerations and disclosures are likely to become the norm and part of international standards'.

'What does promulgate mean?' was the immediate response I got when I lifted the same quote last month for a client presentation.

Also this week saw the International Sustainability Institute Channel Islands publish a report on the relevance of these international standards on climate risk disclosures (TCFD for those that like their acronyms) to private wealth and private capital.

The elevator pitch? Climate risk doesn't discriminate between publicly listed and private assets, so go figure. If beneficial owners of private capital have no other information about climate risk, knowledge of the temperature alignment of their assets and portfolios will be vital for prudent stewardship.

It's been an interesting first half of 2022. Climate change, despite the GFSC and my best efforts, has been knocked off its number one spot of issues of populist concern. It's been displaced by more mundane things like war, having enough money to pay the bills, and global famine. Issues that from our fortuitous position atop the global economic pyramid we'd rather complacently assumed had been consigned to history books.

It was therefore almost with ironic timing that climate risk popped up in BWCI's actuarial review of the States pension scheme published the other week.

I'm sure BWCI must have been provided a fuller report than the version published by the States because, other than as an exercise in box ticking, I couldn't understand the rationale of inclusion of climate risk accompanied by such limited discussion.

The analysis showed that climate risk was potentially the biggest risk faced by the scheme, other than a potential drop in equity indices of 25%. So why no full discussion?

I'm guessing one could argue the report complied with the letter of the GFSC requirements, if indeed they apply to the scheme – I'm not aware they do, but I would argue without proper discussion not their spirit.

Inclusion would have been more meaningful if there'd been more granularity to the analysis, for instance if it had looked at the differential impact across asset classes and what it might mean for the scheme's investment strategy.

'Climate risk is something that's got to be done meaningfully. If the risk factors are to mean anything, then based on the potential impact of climate risk alone, the States should have pause before reducing their [pension fund] contributions'

The issue is, though, analogous to the global situation – the hot issue with the States pension scheme wasn't the climate risk, it's the proposed cut to the States contributions to the scheme.

By virtue of publication schedules, Richard Digard beat me to commenting on the proposals from P&R to reduce the employer contributions. P&R's premise being that, according to its own rules (not those pesky international ones), for assessing the solvency of the pension scheme, the scheme is now around £100m. in surplus. Against being around £100m. in deficit as it was the previous time it was valued in 2016.

But that's a bit of a liberal interpretation of now. Now actually means back in December 2020 when it was re-valued. Apparently, nothing in the intervening period has happened to question the soundness of basing decisions on information that is 18 months out of date. Double digit inflation, the highest rate in 40 years, seemingly not a good enough reason to pause.

I'm not getting into it today, but it seems to me a perplexing way to 'save' £9m. of annual contributions. The States would save more money just by freezing pay and there'd be less risk to the scheme.

I worry with the implications of the proposals, the triumph of short-term solutions over long-term strategy.

As I've said before, you can do the wrong thing for a long time before it bites you. And appreciating something isn't sustainable can take a long time to realise. Which is, perversely, the rationale underpinning the actions of global financial regulators requiring firms look at and take into account climate risk in their strategic deliberations.

Climate risk is something that's got to be done meaningfully. If the risk factors are to mean anything, then based on the potential impact of climate risk alone, the States should have pause before reducing their contributions.

But the issue seems to have no bearing on the current contribution proposals, which makes me question the value of bothering with the risk analysis in the first place.

I've gone a bit large this time out on talking climate change and climate risk reporting because it's illustrative. The issue hasn't gone away because there's a war on, reporting has been on the cards for the finance sector for the last five years, so whatever else is going on in the investment world, the GFSC reminds us about it. For all the GFSC's faults (there are one or two, apparently) it does set its sights on the long view. It can do so by virtue of its devolved institutional arrangements, an enviable position (and in response to the juveniles (sic) who shout out 'quis custodiet ipsos custodes', the answer there is it's supposed to be P&R).

There's no parallel mechanism or analogous institutional arrangements for oversight of domestic financial affairs. Indeed, we have a peculiar situation whereby P&R gets to pick and choose the manner it reports on the state of play of the pension scheme. Ordinarily I'd expect it to be prescribed by a higher institutional arrangement. In the UK, governance rules would be in place setting such things in stone, guided by statute.

There are few constitutional quality checks and balances on States financial reporting or statements. The Guernsey Economic Policy Group have felt obliged on more than one occasion to publish a strong critique of the accounts.

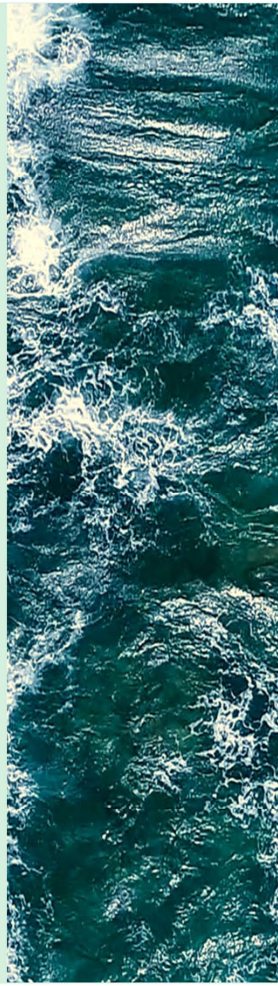
I said a few months back that the quiet culling of the Fiscal Policy Panel last term was a scandal. It was put in place by myself for a good reason – to institutionalise expert scrutiny of the fiscal practice, performance and policy of the States. Sorry, to be 100% accurate and fair to Deputy Trott, the States put it in place as a result of a policy letter presented by Policy Council, signed by the then chief minister, Deputy Trott, following my advice and recommendation.

I recently offered my services, only slightly tongue in cheek, to resurrect these arrangements but I didn't get a call. But I'm serious, putting this type of structure back in place is in my view an important and necessary move for the States. It would improve transparency and decision making. Institutionalising such advice would also help ensure finances are sustainable long term.

It would also ensure that assessment of climate risk doesn't become a tick-box exercise for the States.

"All firms, following our environmental amendments to the Code of Corporate Governance in 2021, need to consider how to adapt their business models as a matter of urgency as international standards on environmental sustainability are quite likely to be promulgated over the course of 2022."

Director General's Statement, GFSC Annual Report, 2022



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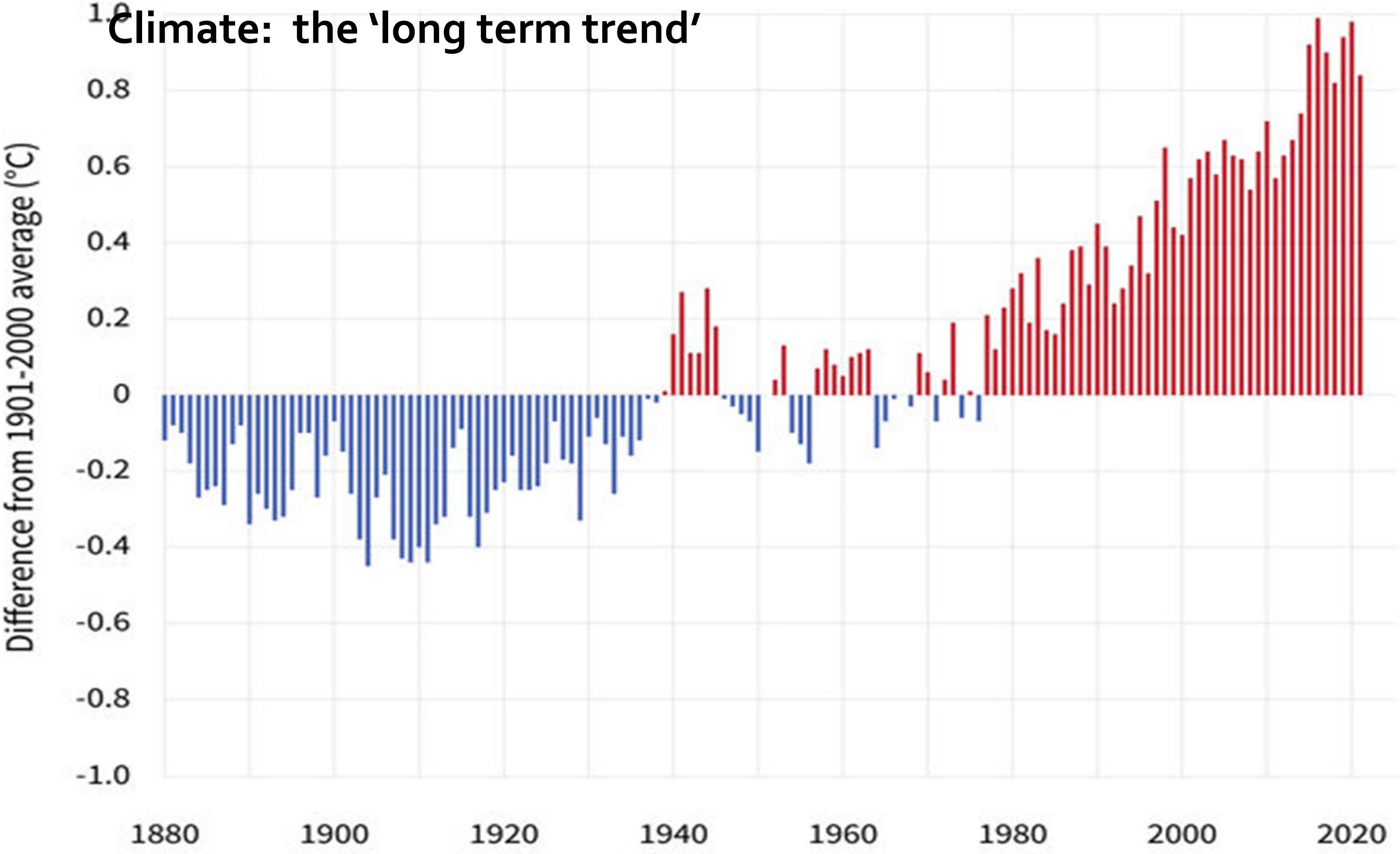
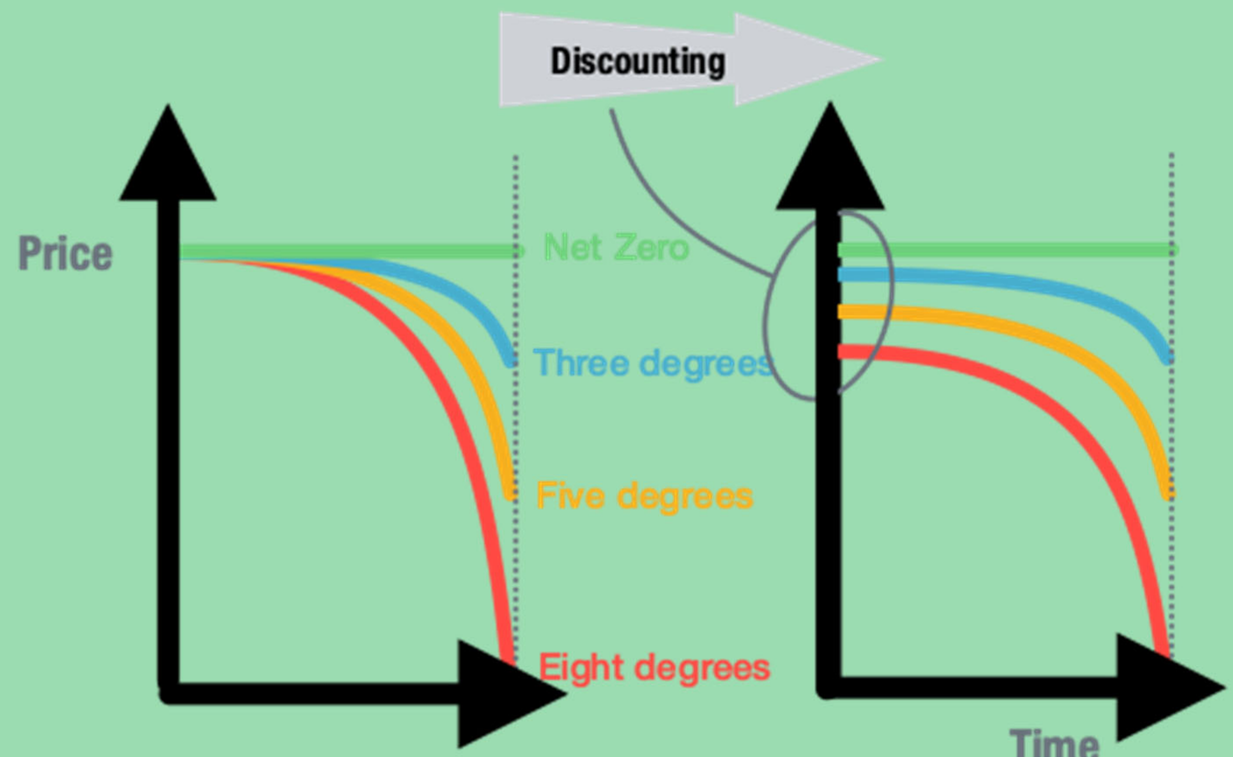
Climate: the ‘long term trend’



How it works, climate risk. A simplified model.



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Financed emissions and a simple metrics set

'Knowledge of the temperature alignment of assets and portfolios will be vital for prudent stewardship.'

International Sustainability Institute Channel Islands

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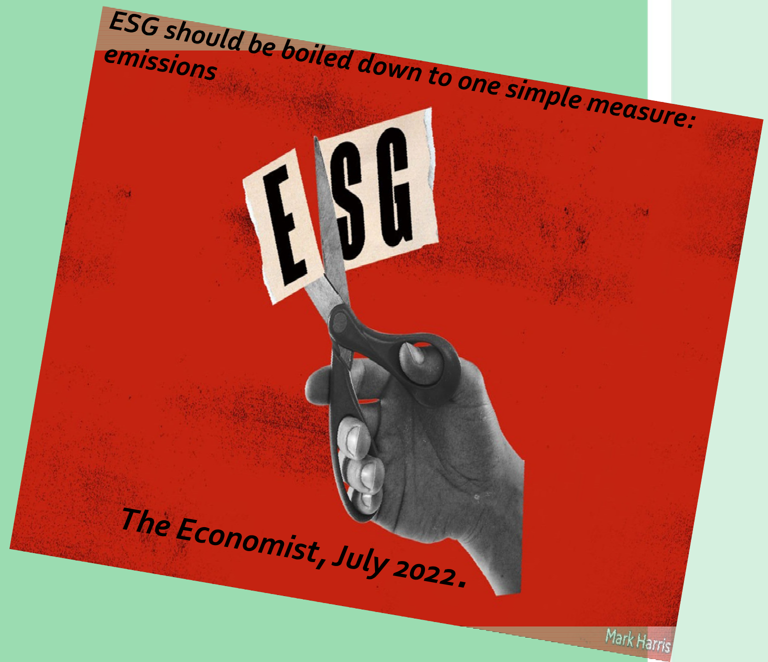

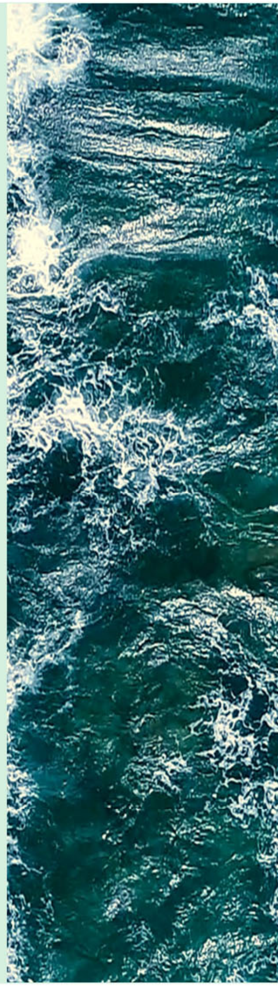

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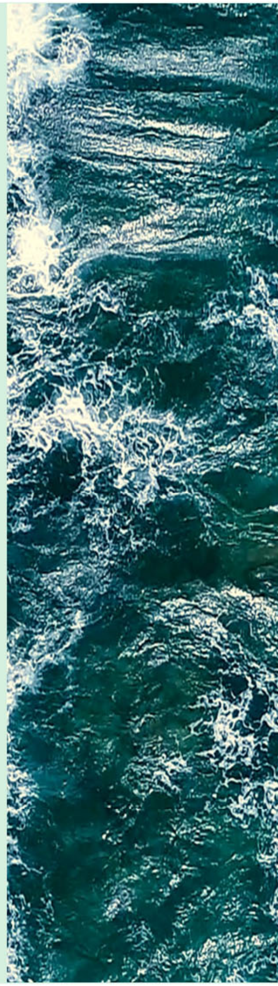
The future is now, climate risk reporting



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Conclusions

So what lessons can be learnt from all that?

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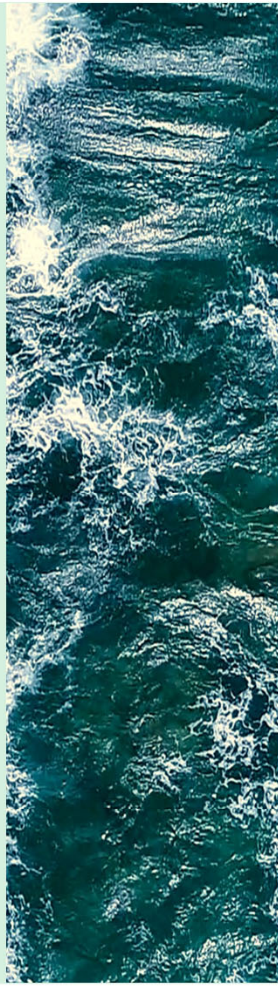

Conclusions

Economically we're going through a pivotal time.

Many of the macroeconomic variables: interest; inflation; etc are undergoing a structural break or change.

The global economy has suffered a series of exogenous shocks, but the many policy errors are endogenous.

Many of these shocks are transitory, as are their impacts, but many economic fundamentals need permanently rebalancing.

Through all this the transition to net zero may take a different path but climate change remains with us.

Firms will still have to adapt and plan accordingly.

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