THE BIGGEST ESG OPPORTUNITIES FOR THE GLOBAL INSURANCE INDUSTRY

PART 2 OF A TWO-PART SHEFFIELD HAWORTH SPECIAL REPORT ON ESG

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INTRODUCTION

ESG (Environment, Social and Governance) is one of the biggest priorities in the corporate world today. Certainly, as a talent and recruitment consultancy, Sheffield Haworth has seen a huge increase in ESG-related roles – and the demand for talent with ESG experience or qualifications.

ESG is so all-encompassing as a term that we could almost see it as unhelpful – especially when it comes to defining job roles and the corresponding skills required for them. After all, is a Head of ESG primarily responsible for increasing diversity and inclusion in the workforce? Or do they oversee reporting on the environmental impact of the supply chain? Or are they driving through a series of processes that will make their organisation a net zero carbon dioxide emitter by 2030?

We interviewed five ESG specialists from across the insurance market to get a deeper understanding of the ESG trends and opportunities and what this might mean for the future of the ESG talent market in insurance.

What are the biggest ESG challenges facing the insurance industry?

ESG is so all-encompassing that businesses can have a hard time defining precisely what it is and how to apply it in their operations. Many organisations use ESG as shorthand for environmental issues, for example. They either ignore the social and governance aspects or else they separate them out. It's becoming fairly common today to see companies advertising roles for Head of ESG and Heads of Diversity and Inclusion. Yet diversity and inclusion also fall under the "s" part of ESG.

When even defining ESG is a challenge – much less what it means in the context of a specific business – it's no wonder that confusion persists. Even for those companies pursuing an ESG agenda, the broad scope of the term can lead to problems.

"When I walk into a board room, they tend to want to talk about environmental, then social. When I ask them, 'What about governance?', they will tend to say they're complying with the law but they're not really thinking beyond that," says James Alexander, Environmental Practice Leader at Lockton Companies LLP.

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"There are so many ESG issues that it is essential we remain strategic and focused. The true test of authenticity on ESG is holding our nerve from a business perspective, because we can't do everything," says Michelle Leavesley, Founder of Organisational Risk & Resilience at M&G plc.

"Whilst there may be stakeholder pressure on a range of issues such as animal rights, human rights, financial equality and climate, there are just so many issues that we risk overpromising and underdelivering, or worse, mis-representing ourselves on ESG, leading to reputational issues such as greenwashing," she adds. "So the question for us as an industry is how we prioritise, resource effectively, and have meaningful outcomes."

Keith Davies is the Chief Risk & Compliance Officer at Federated Hermes. He agrees with Michelle's point, adding: "You can't be all things to all people, so therefore it has to be top down. You have to focus on what you genuinely think your purpose as an organisation is and what you stand for. You've got to define that first and then get people to authentically deliver that."

Put another way, companies are under pressure to look at a plethora of environmental and social issues. Yet to have a genuine ESG impact, they need to focus. And that focus should come from a genuine, well-defined purpose, without which their efforts are likely to come across as empty-virtue signalling.

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Julian Richardson is the CEO of Parhelion Underwriting, a well established provider of carbon market insurance solutions which creates innovative insurance products that support investment into sustainable investment opportunities. He founded his company out of a deep desire to use insurance to help mitigate the impact of climate change.

"I spent a lot of time on the broking and then the underwriting side of the oil and gas business," Julian explains. "I became good at insurance, but once you've insured a major national oil company five times, do you want to do it for a sixth time? I wanted to take what I knew and apply it to something that mattered. I have a terrible habit of not accepting the way the world is and trying to make it a better place."

For Julian, a lack of genuine commitment amongst large insurance firms to tackling climate change is one reason why the industry is likely to be slow to make the most of the potential opportunities. He points to a global broking company's recent winning of the contract to place insurance for an East African crude oil pipeline. Once complete, the pipeline is projected to emit 33 million tons of carbon each year, while also displacing towns and villages across the region.

"The International Energy Agency has said that we shouldn't have any new oil projects if we want to meet the two degree target of the Paris Agreement," Julian says. "Brokers seeking to claim ESG credentials should be taking this into consideration."

He adds that Uganda sits on the East African Rift Valley. That region has huge potential for geothermal energy resource which can now be de-risked and brought to market via more specialist insurance products.

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"If the insurance industry put a fraction of their capability and resource behind it, they could really make a difference in using insurance to bring geothermal energy to reality rather than just doing the same old thing," he says.

James Alexander points to another challenge that many in the industry may not be thinking about enough. “With TCFD and other kinds of climate and sustainability reporting, companies are now reporting on how much they’re impacting the environment. This goes against the traditional basis of liability insurance, which is to insure against unforeseen events.”

He adds: “With climate reporting, companies are proving their awareness of exactly how much they’ve been polluting or emitting carbon, or whatever it might be. This is likely to change the way climate risks are insured in the future. The industry will work this out eventually but in the meantime we are likely to see some real disruption.”

What are the biggest ESG opportunities facing the insurance industry?

Of course, the ESG challenges facing insurers now are reminiscent of the challenges the industry has faced regarding cyber security risks or renewable energy investments in the recent past – a point made by both Keith Davies and Natalia Dorfman, the CEO and co-founder of carbon market insurance startup Kita. If those markets are any guide to the future, that suggests that what are currently specialist risks will become mainstream and essential items, becoming huge revenue generators for the insurance industry within the next decade.

The carbon removal market alone could be worth around $1 trillion by 2050, thinks Natalia. "The Intergovernmental Panel on Climate Change states we need to remove billions of tons of CO_2 annually for the remainder of the 21st century to enable a liveable and sustainable future for all. This is a scale-up task at unprecedented speed and magnitude, and it represents a huge opportunity for a new insurance market. Likewise, insurance is essential to enable this rate of growth."

Julian, who has been providing carbon market insurance solutions for over 10 years, agrees on the huge potential for the carbon markets to provide lucrative work for insurers – if they can move at the speed needed to make the most of it:

If you’re not net carbon zero in 2050 you won’t exist as regulations and customer and stakeholder preferences evolve. Whilst you should, you don’t have to want to save the planet to become NCZ; you just have to want to save your company.”

“The big opportunity is creating new products and solutions to support the environmental integrity, increase the liquidity and reduce the cost of capital associated with carbon markets. The potential for the carbon offset market to grow to tens of billions of dollars in size in the next few years is very real.”

For Keith, the real opportunity is to use ESG as another way to secure the future viability and profitability of a business at the same time as trying to have a positive impact on the world around you.

“The board of the business is responsible for the long-term success of that business,” Michelle agrees, adding: “ESG is really just another very important lens that needs to be applied to assess the decisions made today and the impact they have on tomorrow.”

“To my mind, ESG is actually all the factors that impact the long-term value of the company,” Keith adds. “If you’re not net carbon zero in 2050 you won’t exist as regulations and customer and stakeholder preferences evolve. Whilst you should, you don’t have to want to save the planet to become NCZ; you just have to want to save your company.”

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What is the mindset shift necessary to make the most of these opportunities?

To become an authentic champion of ESG requires a significant mindset shift, according to all those we interviewed. Significantly, however, as Keith points out, having to deal with a new set of risks is nothing new for the insurance or asset management industries:

"A lot of people seem confused about the best way to respond, and many of them are looking at this as a kind of regulatory obligation or made-up subject. But this was exactly the same when credit risk emerged back in the 90s and it was exactly the same with operational risk in the 2000s – and cyber risks even more recently."

Right now, finding the necessary skills for ESG is a challenge, as is finding enough quality data to work with. Keith continues:

> **Don't admire the problem; just shape the solution."**

"We're focusing on new areas that haven't really been done before. So you're not going to go out there and find ready-made frameworks and ready-made people. Most people are moaning that the data isn't very good. That's true but in five years' time, it will be. So in the meantime, we just have to live with it and work with what we have. Don't admire the problem; just shape the solution."

Another significant mindset shift required is in knowledge – knowledge more broadly across insurance organisations of what ESG is or what it means. As Julian explains: "We, in the industry, definitely need to develop our depth of understanding of what ESG and sustainability mean. If you look at the investor community, they've been using ESG insights to inform investment decisions for years, where insurance is still catching up."

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One contributor said that while we've seen a host of people appointed as Head of ESG or Head of Sustainability over the last few years, many of those people lack any deep knowledge or understanding of what ESG is. "Lloyd's has appointed one of their internal PR people as Head of Sustainability. If that doesn't shout greenwash on its way, I don't know what does!" they said.

More ESG education was a key theme for Michelle too. She pointed out that one of the largest investments that she made when embedding ESG into her company's risk frameworks was in education, since everyone on the team was learning about ESG and its associated risks at the same time.

Another thought raised by several interviewees was the need for a more collaborative approach to ESG across the industry. Michelle points out, for example, that following M&G's initial lead the entire financial services industry came together to combat online fraud, resulting in the UK's Online Harm Act.

"I'm proud that we collectively influenced that," Michelle says, "but what else should we be collectively influencing from an insurance perspective?" Her implication is clear: insurers should be collaborating more and sharing information to help solve climate challenges collectively.

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She also believes that the current Better Business Act campaign – which has the support of over 1,000 UK businesses – could help. Its goal is to make company leadership accountable to all stakeholders – customers, locals in the areas where companies do business, even employees – rather than just shareholders, in an attempt to get them to act more responsibly, more holistically, and less for short-term financial gain.

It's a point that resonates with Julian at Parhelion. "The industry's involvement in the East African oil pipeline shows, the industry will keep on doing what it does unless it is pressured to do something else," he says. "And there are a lot of people within our industry that want to be part of the solution, but they either don't quite know how or don't have the corporate support."

One step change in global corporate governance that James at Lockton finds significant is the increasing acceptance of common standards for a company's operations regardless of where in the world they are.

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"Before now, it was common practice for a Western company to run its european operations to higher safety and environmental standards than its operations in, say, Nigeria or India," he says. "Now that's no longer acceptable. It has to be the same everywhere. This will raise governance standards and is good from a stakeholder perspective, though it may be more expensive for the shareholders!"

What kinds of new skills, traits or talent will the industry need to make the most of these opportunities?

Experienced ESG talent is in short supply. However, traditional insurance skills can help to serve an ESG agenda, according to our interviewees..

When it comes to developing specialist insurance products around sustainability, our interviewees identified a need for skilled underwriters, data scientists, and data analysts as well as specialists in new emerging markets. In other words, climate tech startups and boutique insurance firms need a mix of technology and data skills, traditional insurance skills, and specialist market insight.

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For Michelle, people with the ability to be flexible and adaptable offer the most potential for ESG-related roles. As Michelle adds: "You want people who are comfortable not knowing all the answers, because right now we don't have all the answers."

Keith agrees, saying: "There's no set rules or frameworks yet. So those are the sort of people you need – those who can think creatively and live with imprecision." He adds that you also need people who want to continually learn: "You've got to want to learn about it. Climate science is fascinating when you get into it, but if you don't want to get into it – or learn about other new and tangential areas - you probably shouldn't be in an ESG role or leading an ESG initiative."

Where can insurance firms source ESG talent right now? How can they train or develop ESG skillsets within their existing workforce?

The shortage of experienced talent has led many within the industry to prioritise hiring those with ESG qualifications. However, as Michelle says, "“It's interesting to see that emphasis on academic qualifications but in reality, we need people who can create and apply practical approaches for our businesses.

“I have interviewed a significant number of ESG candidates over the past 12 months across a number of business areas and geographical territories. Too often candidates default to text book solutions and are unable to paint a picture of what they would do practically in not just identifying and managing the risk but how they would take people with them on the journey For me, at the moment I'm going to take someone with that practical mindset over academic qualification every time.”

Natalia at Kita thinks that individual mindsets are key – along with traditional insurance skillsets. When it comes to knowing the nuances of the carbon market, this is something that the existing experts at Kita can train new starters in once the company starts to grow. As Natalia says: “I can try and hire an actuary who understands the voluntary carbon market but that is challenging. So you have to hire for flexibility and mindset – something that goes double for us because we're a startup.”

For Julian, a strong proposition is a great tool for attracting talent: “We've been really lucky with the people that we've been able to engage, whether it be at the board level or at the underwriting level or the operational level. People are motivated by our proposition and our vision.”

In an age of greater public awareness and concern, just having a strong and consistent vision around climate change and sustainability will, in itself, act as a strong and attractive proposition. This is because talented individuals increasingly want to work for companies with a strong ESG agenda – even in the Oil and Gas sector, as Julian points out.

Several other interviewees pointed out the same. Younger consumers tend to want greener products and services, while younger employees want to work with firms that share their values – and this increasingly means companies with clear ESG credentials.

Finally, Keith adds that where ESG experience might not exist within insurance, firms may need to go and find it elsewhere. “When I needed someone with experience related to reputation and brand, I went to the Marketing industry,” he explains. “If you want someone with experience around human rights, you can look for people who have worked at government organisations. If you want someone with climate change experience, try scientific institutions. The talent is probably out there if you're creative about where to look.”

Top Takeaways

- Asset managers have been using ESG principles to guide business decisions for years, while insurers are lagging behind.
- Insurance firms need to ensure they have a deep understanding of what ESG is and how it could apply to them.
- The lack of insurance products promoting net zero or other sustainability goals is due to the fact that the market remains small.
- The potential future market for ESG-related insurance products is huge.
- To have a positive ESG impact, companies should focus on their purpose and not allow themselves to get distracted.
- ESG should be driven by genuine commitment, not treated as a regulatory obligation.
- Lack of commitment and lack of focus can be perceived as greenwashing and have a negative impact on brand reputation.
- Traditional underwriting skills can be as important to developing ESG products and services as specialist knowledge or skills.
- A strong and provable commitment to ESG can be a great way to attract top talent.
- If you're looking for senior leaders with ESG experience, look to adjacent industries.
- ·A practical mindset is likely to outweigh academic qualifications when hiring for senior ESG roles.
- The most important traits for ESG roles are: creative thinking, flexibility, adaptability, the ability to get things done and make decisions without having all the data to hand, as well as the capacity and drive to learn more about ESG.

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ABOUT SHEFFIELD HAWORTH

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Our vision is to be the leading global consultancy in people and transformational change. We specialise in executive search and interim placements, leadership advisory, change management, and information and data services. Clients benefit from deep industry insights, our wide-ranging networks and high standards of delivery from our global team. We work with private and public companies across financial services, professional and business services, high-growth technologies, and multinational corporates.

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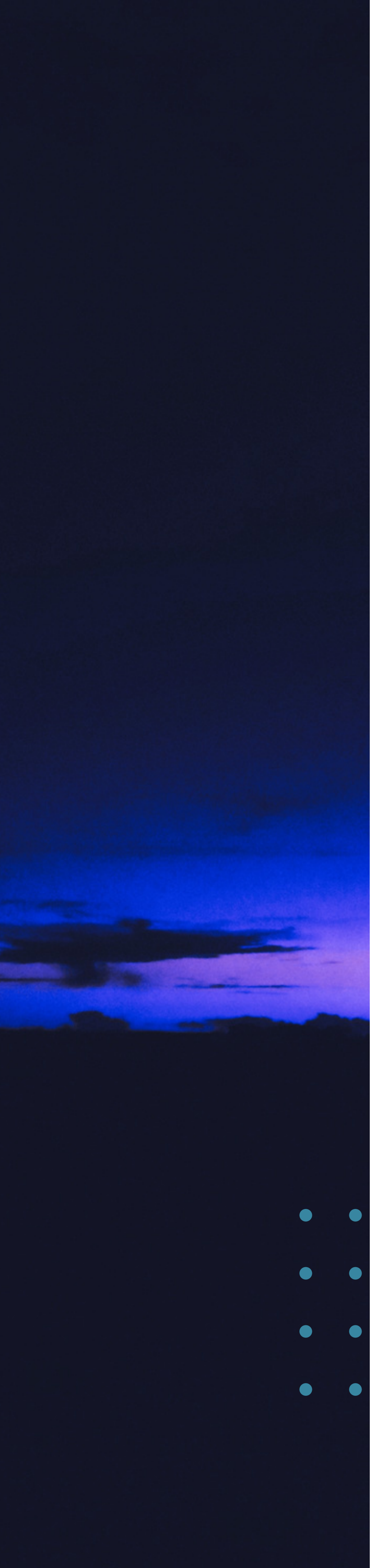

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