NEW YORK STATE OF OPPORTUNITY. Department of Financial Services

2 Investing Initiative

An Analysis of New York Domestic Insurers' Exposure to Transition Risks and Opportunities from Climate Change

June 21, 2021

Content

- Introduction
- Introduction to 2DII
- PACTA Methodology
- Results
- Strategies for Mitigating Transition Risks
- Next Steps

Introduction

- DFS's proposed Guidance for New York Domestic Insurers on Managing the Financial Risks from Climate Change
  - Comment period ends on June 23, 2021.

- Purpose of this report – support New York insurers to understand their transition risks on their investments

Climate Risks are Accelerating

- Worsening physical risks
- Worsening transition risks
  - Policy and regulation changes
  - Low-carbon technology advancement
  - Changing public sentiment and demands
- Companies, asset owners, and asset managers make net zero carbon emission pledges.

Financial Markets and Regulators' Attention on Climate Risks

- Stranded assets
- Rating agencies' actions
- Federal Reserves Board's climate committees
- International regulators' climate stress tests

Questions Answered in the Study

- What holdings are most exposed to transition risks and their sizes?
- How does my investee companies' transition plans impact my risks?
- Which climate scenario is my portfolio aligned with?
- How does my portfolio compare to the market benchmarks and peers re: transition risk?
- How can I mitigate the transition risks?

Introduction to 2-Degrees Investing Initiative

2 Investing Initiative

Introduction to 2-Degrees Investing Initiative

Founded in 2012

Working globally, with offices in Paris, New York, Berlin, Brussels, and London

Collaborate with financial institutions, nonprofits, universities, policymakers, and supervisors

Non-profit, non-commercial

Aligning financial markets & regulations with climate goals

2-Degrees Investing Initiative Research Themes

PACTA

Climate scenario analysis

Retail investing

Supporting consumers' sustainability goals

Risk management

Supporting long-term risk supervision

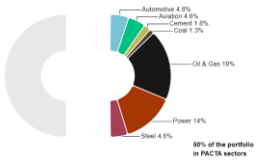
Impact

Studying financial institutions' impact in the real economy

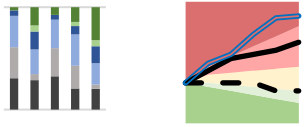
Paris Agreement Capital Transition Assessment (PACTA) Methodology

PACTA Methodology

1) Exposure to High carbon sectors



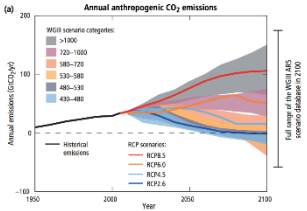
2) Alignment of a portfolio is benchmarked against **climate change scenarios** and the **market**



Insurance Company

Physical Assets in the Real Economy

Climate Change Scenarios



NEW YORK STATE OF OPPORTUNITY. Department of Financial Services

2° Investing Initiative

Data Input

- Equity and corporate bond portfolios of 250 New York domestic insurers' ("insurers") 2019 Schedule D data.
- Investee companies' physical asset-level data and production plans
- Climate scenario data

*Provided by Asset Resolution

Climate Scenarios Considered

- Fossil Fuel Production and Power Generation
  - Current Policy Scenario (CPS)
  - Stated Policy Scenario (STEPS)
  - Sustainable Development Scenario (SDS) – Paris Agreement-Aligned

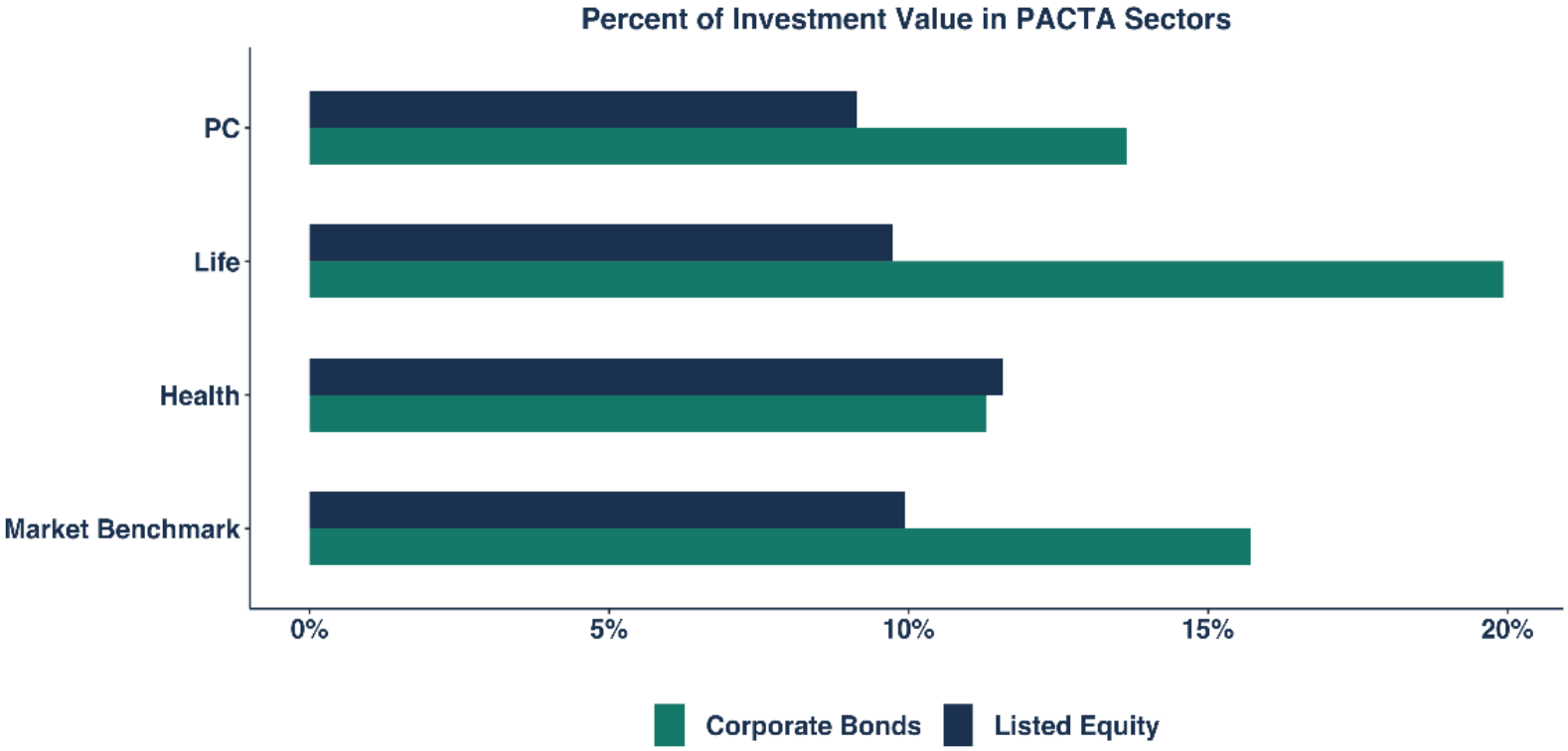
- Automotive
  - Reference Technology Scenario (RTS)
  - 2 Degrees Scenario (2DS)
  - Beyond 2 Degrees Scenario (B2DS) – Paris Agreement-Aligned

Market Benchmarks

- For corporate bonds – Bloomberg Barclays Global Aggregate Corporate Bond Index

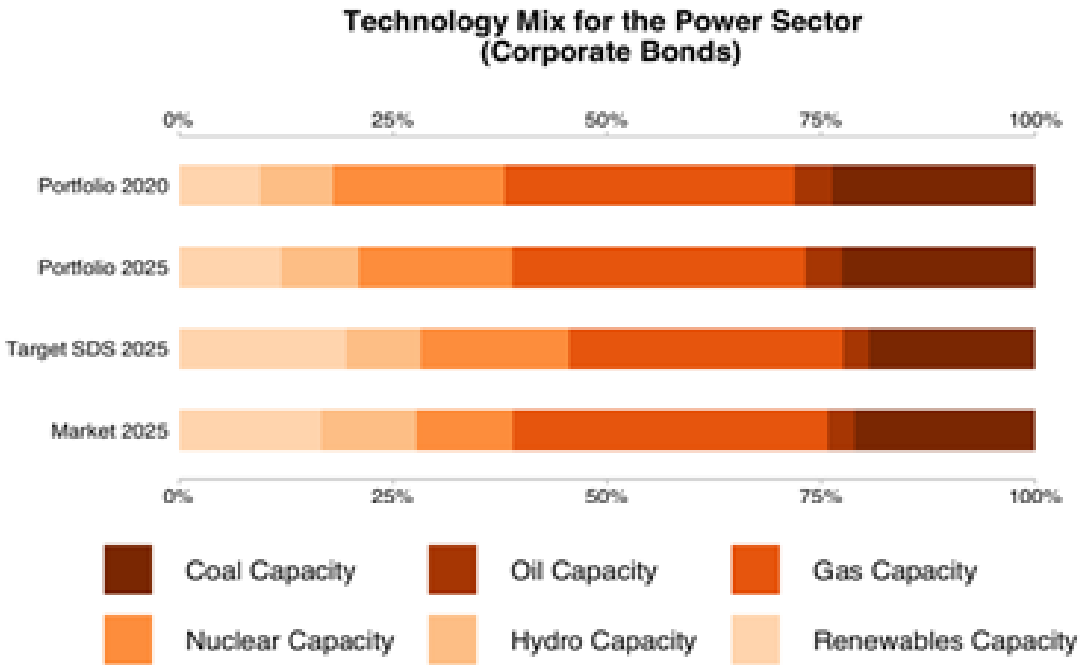
- For equities – MSCI All Country World Index

Outputs – 1) Exposure to High Carbon Sectors



2) Scenario Alignment – Technology Mix

- Portfolio's exposure to technology mix (%)

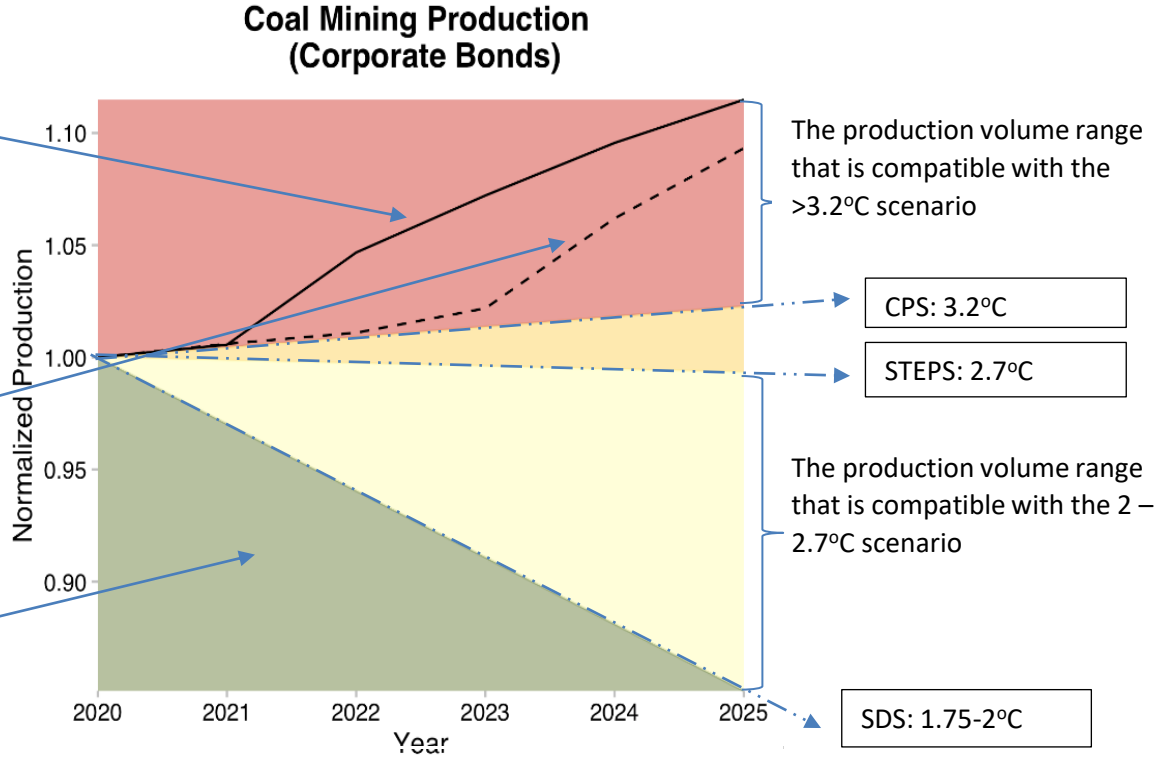


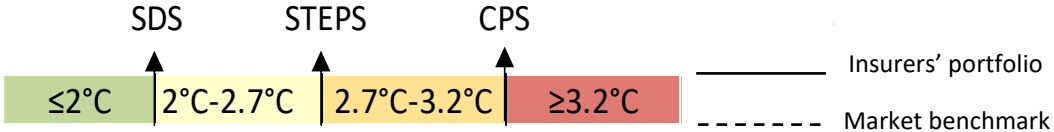
2) Scenario Alignment – Production Volume Trajectory

The amount of coal production allocated to the insurers' corporate bond portfolios based on their holdings, based on the five-year capital plan of the investee companies.

The amount of coal production of the market benchmark.

Colored areas denote the production volume ranges that are compatible with different climate scenarios.





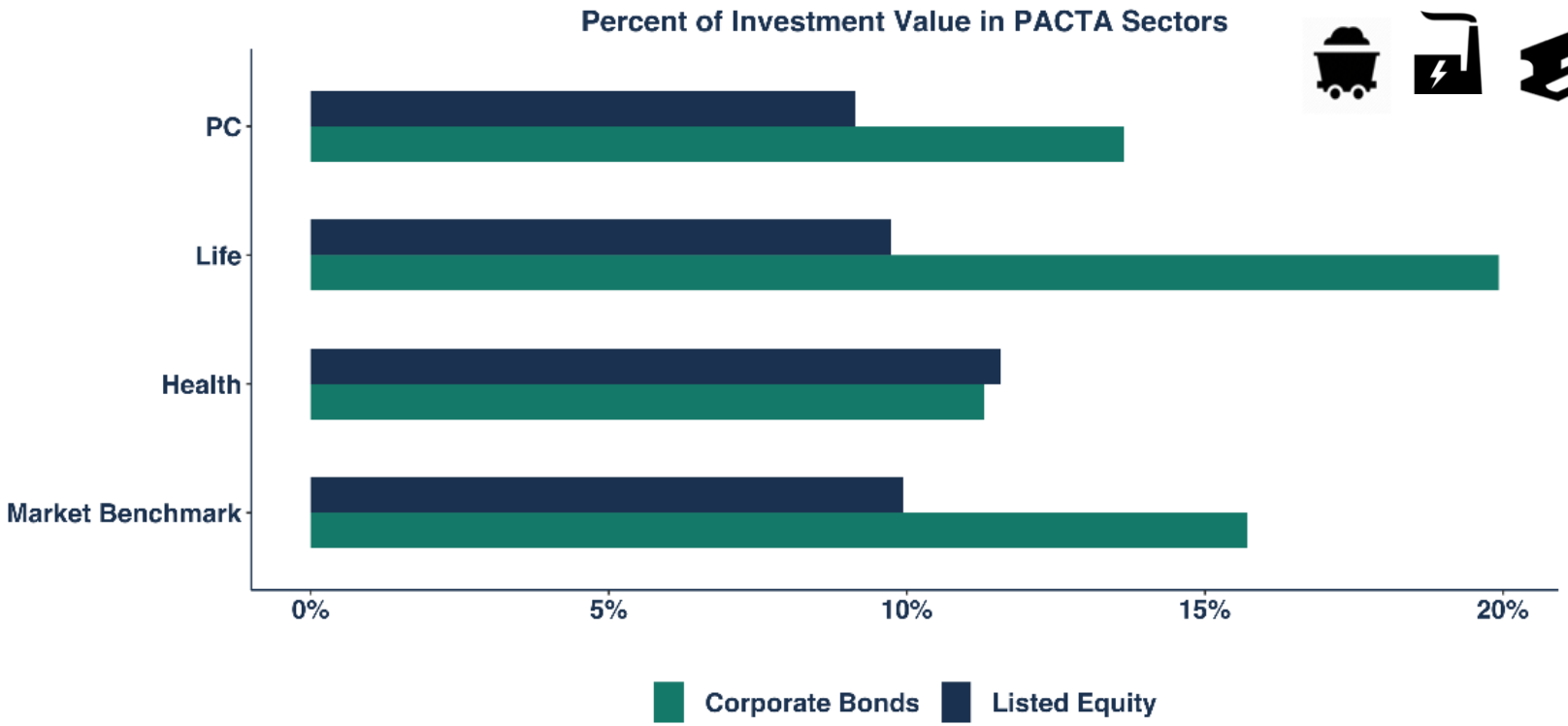
Analysis Results

- Exposure
- Peer comparison
- Alignment
  - Fossil Fuels
  - Power
  - Automotive

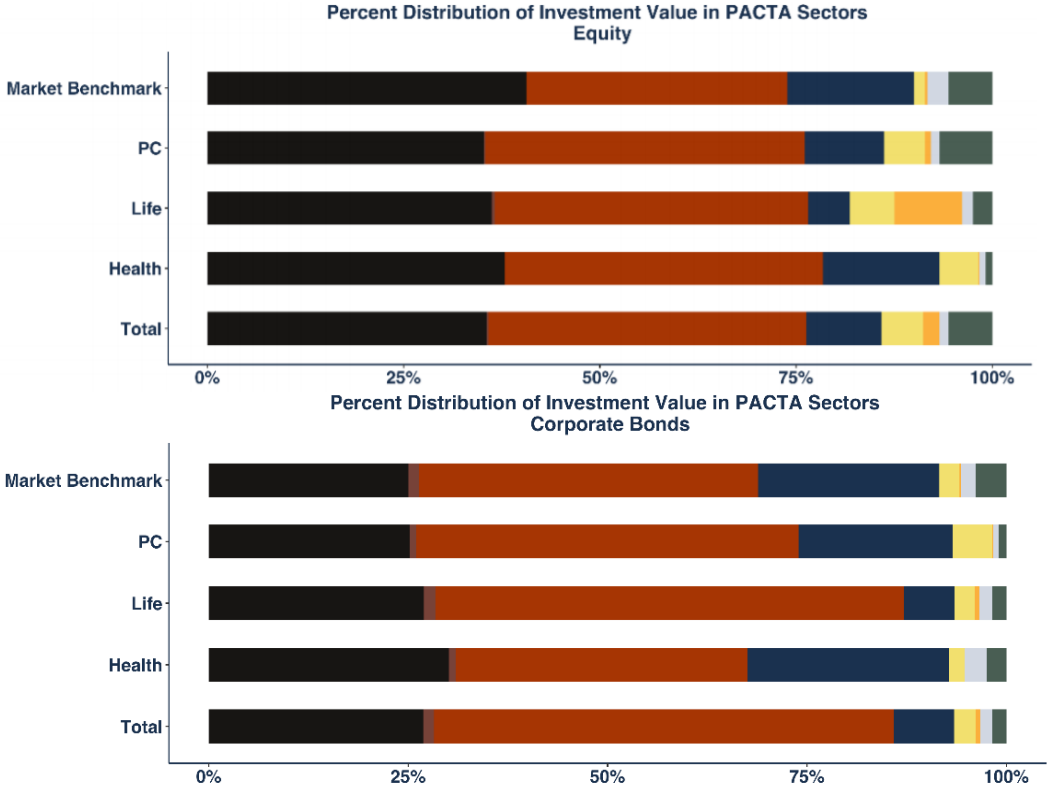
Summary

- Insurers' investments in 2019 had meaningful exposure to carbon intensive sectors.
- The five-year forward-looking capital plans of most insurers' investee companies in these sectors were not Paris-aligned,
  - except for natural gas production, natural gas-fired power generation, and electric vehicle production.
- Insurers' portfolios often less Paris-aligned than market benchmarks

Investment Exposure

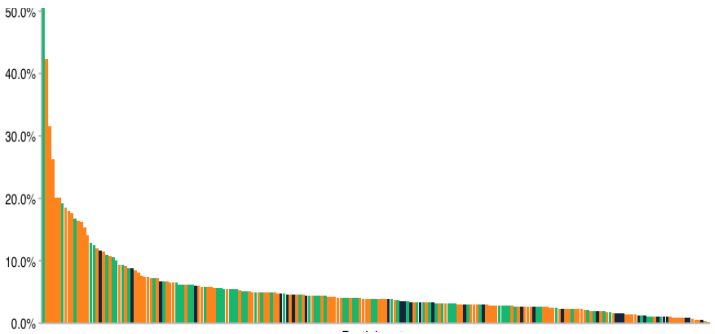


Distribution of Investments in PACTA Sectors

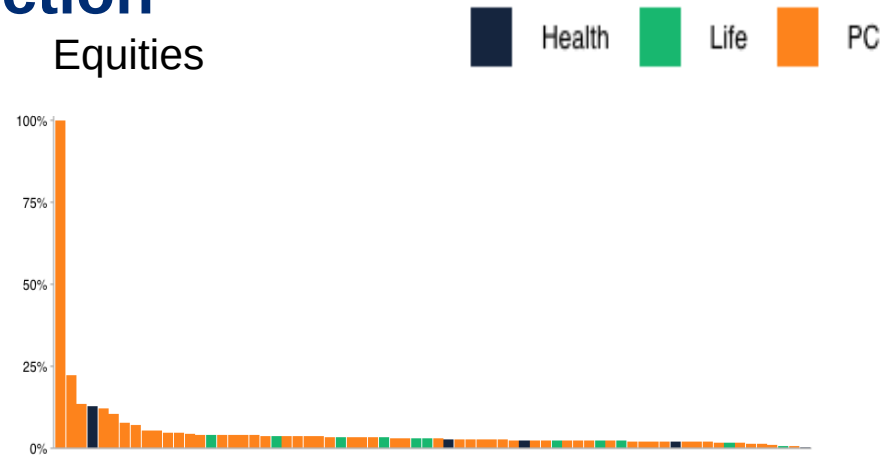


Holdings in Fossil Fuel Production

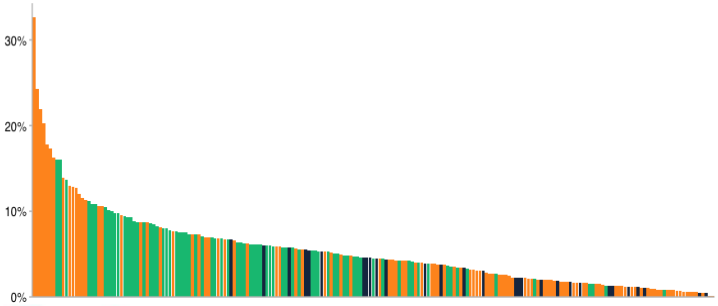
Corporate Bonds

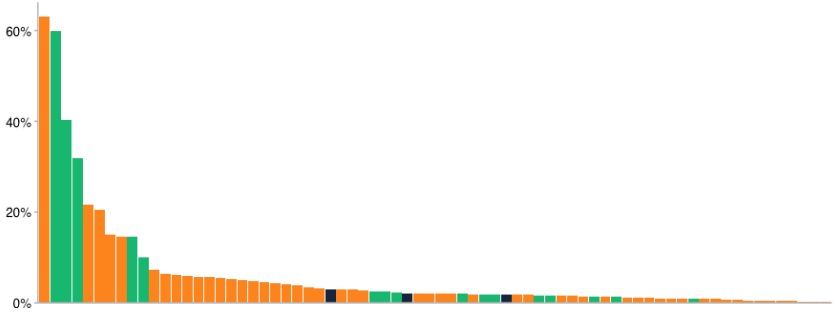


Equities

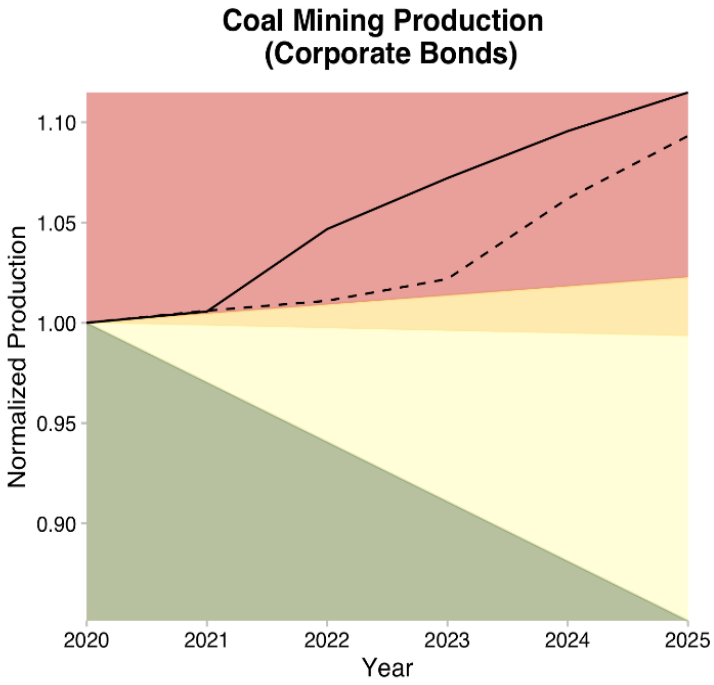


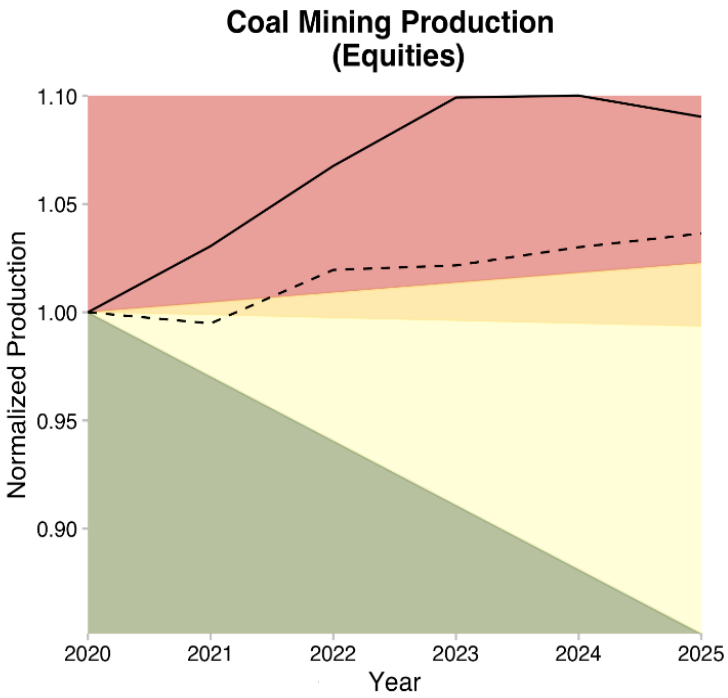
Holdings in Fossil Fuel-Based Power Generation

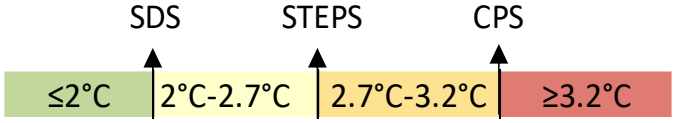




Coal Mining – Production Volume Trajectories



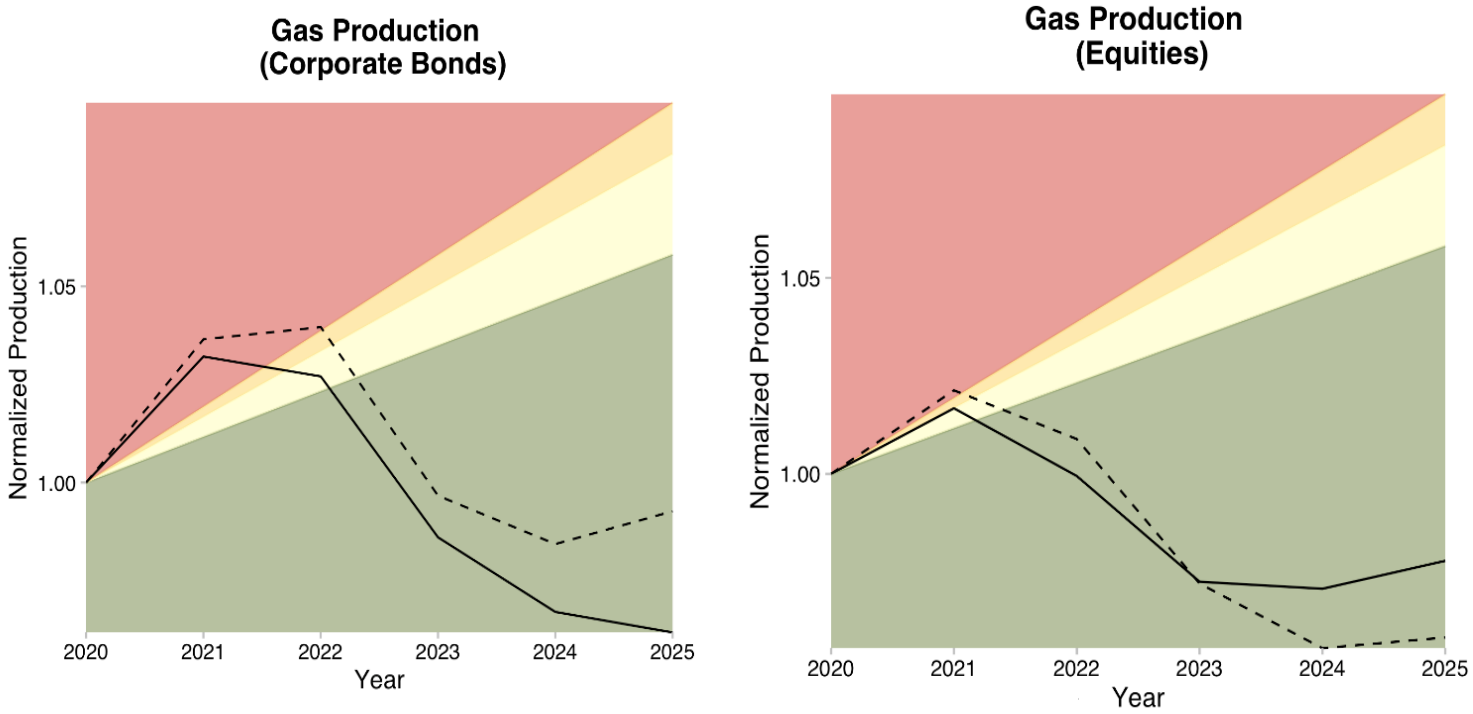


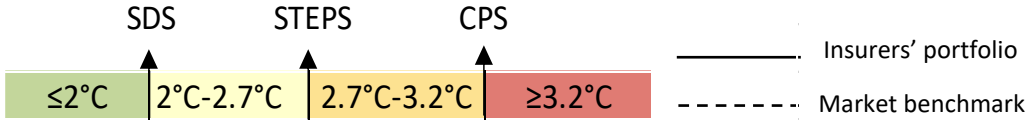


Insurers' portfolio

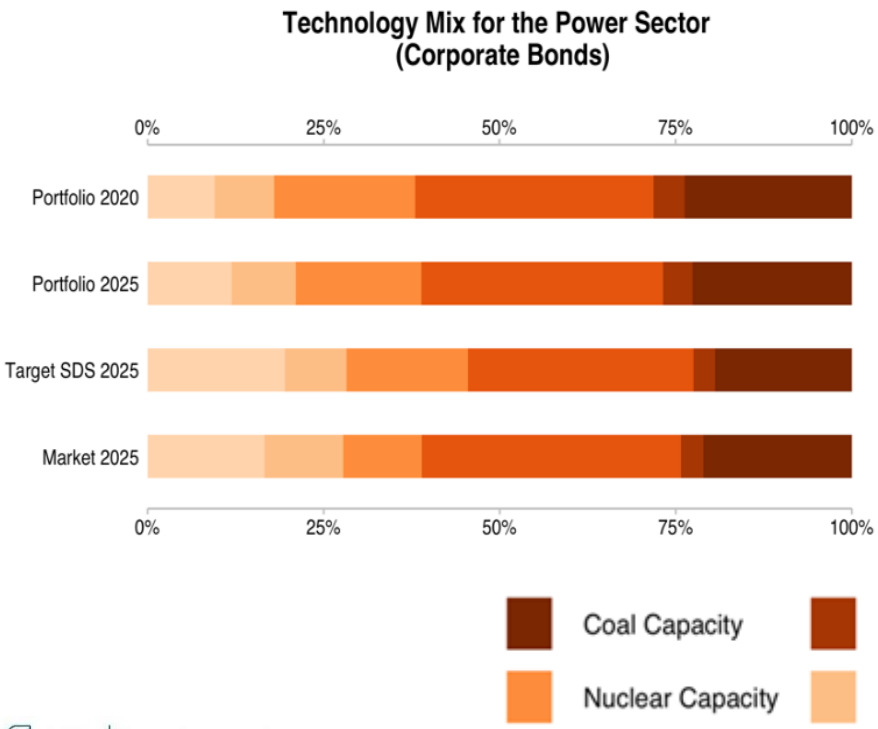
Market benchmark

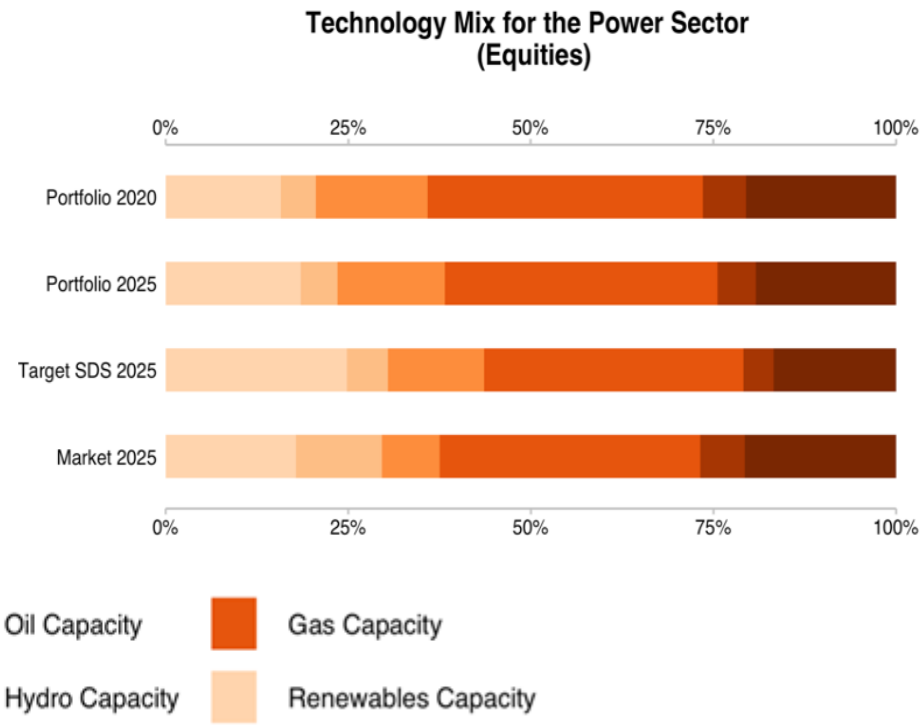
Natural Gas Production – Production Volume Trajectories



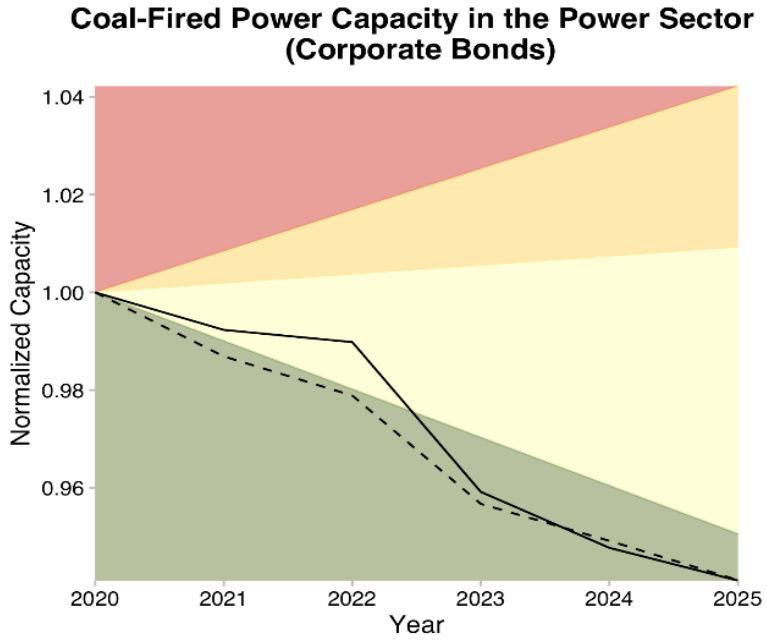


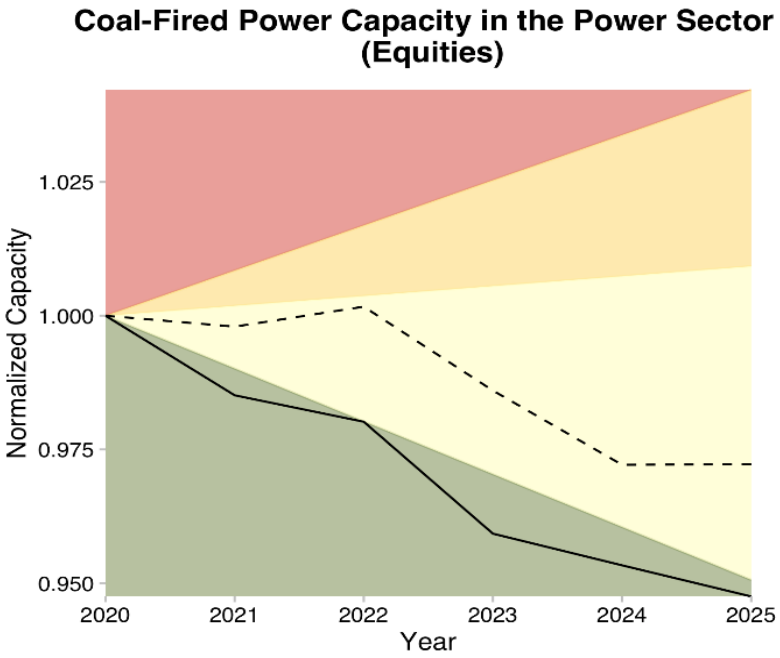
Power Sector – Technology Mix

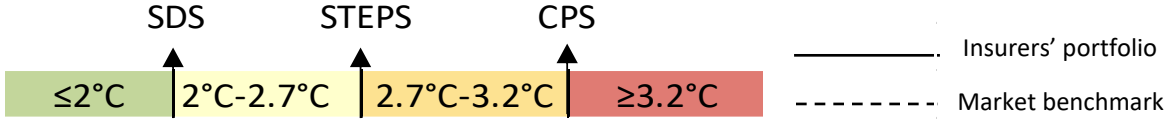




Coal-Fired Power – Production Volume Trajectories







Renewable Power – Production Volume Trajectories

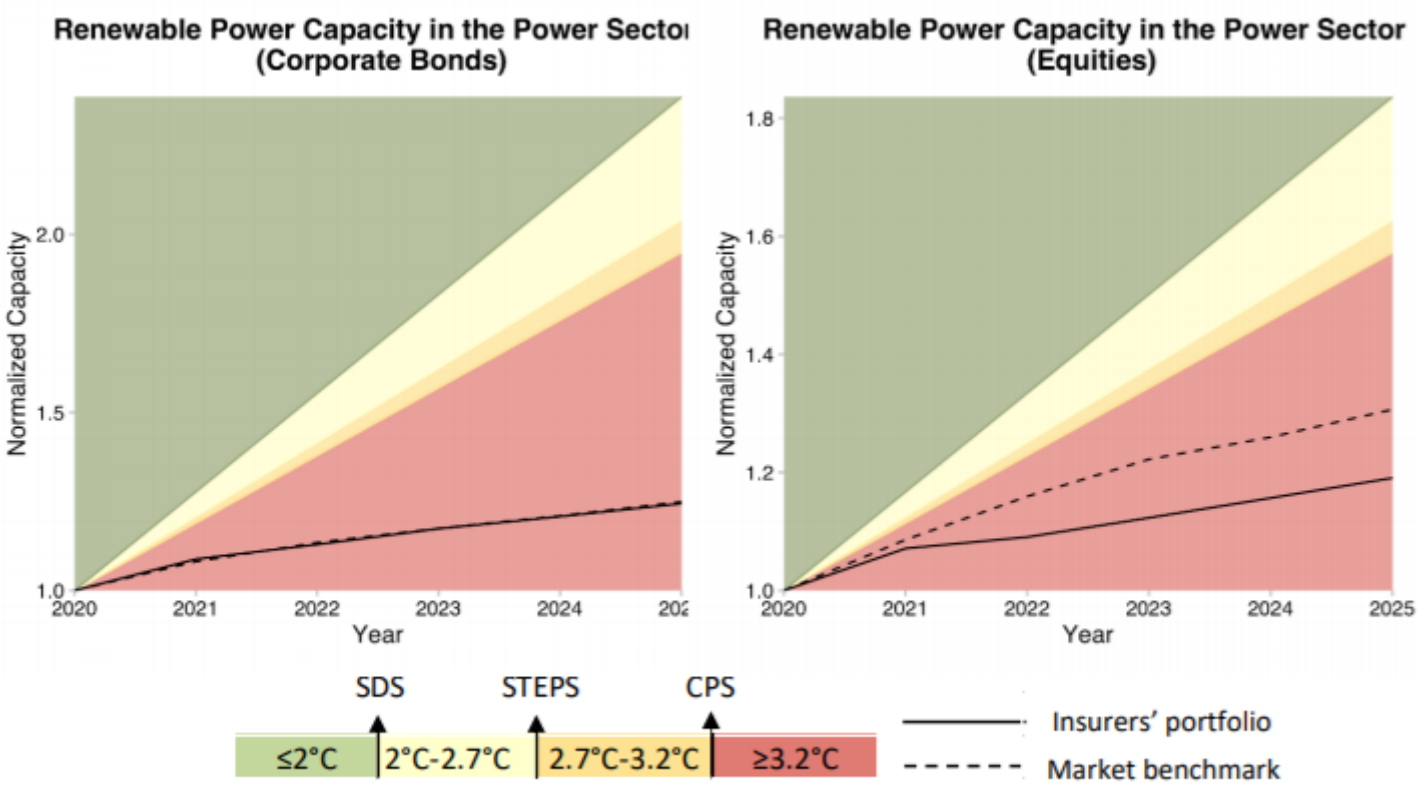
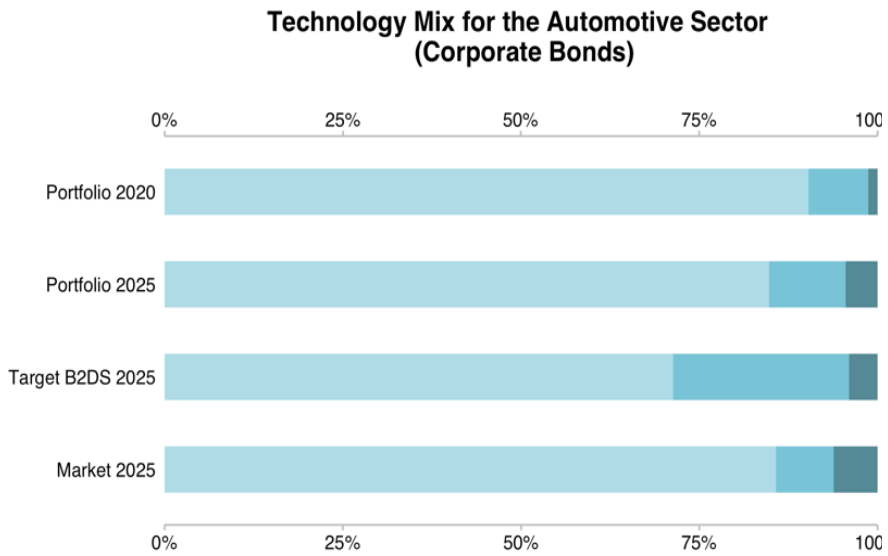
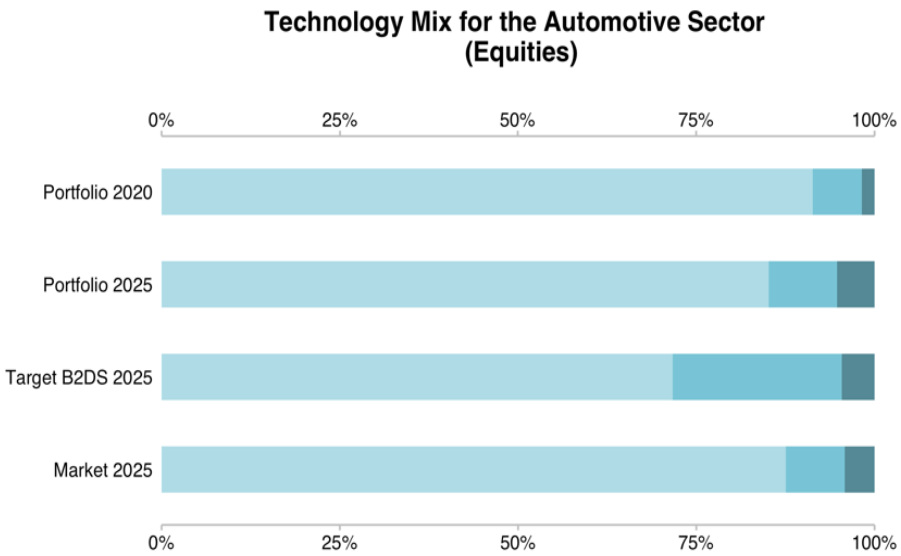


Figure 16. Renewable Power Capacity Trajectories Relative to Climate Scenarios

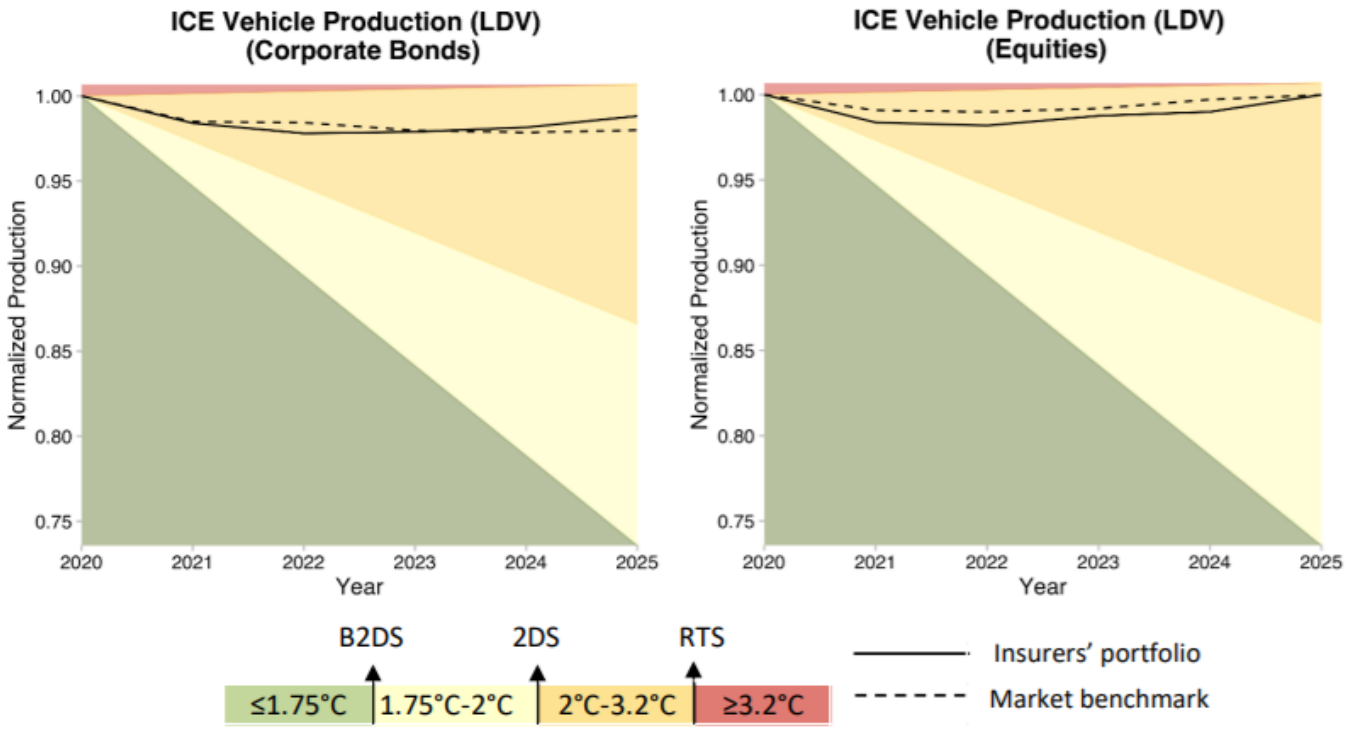
Automotive – Technology Mix





Electric Hybrid ICE

Internal Combustion Engine – Production Volume Trajectories



Electric Vehicle – Production Volume Trajectories

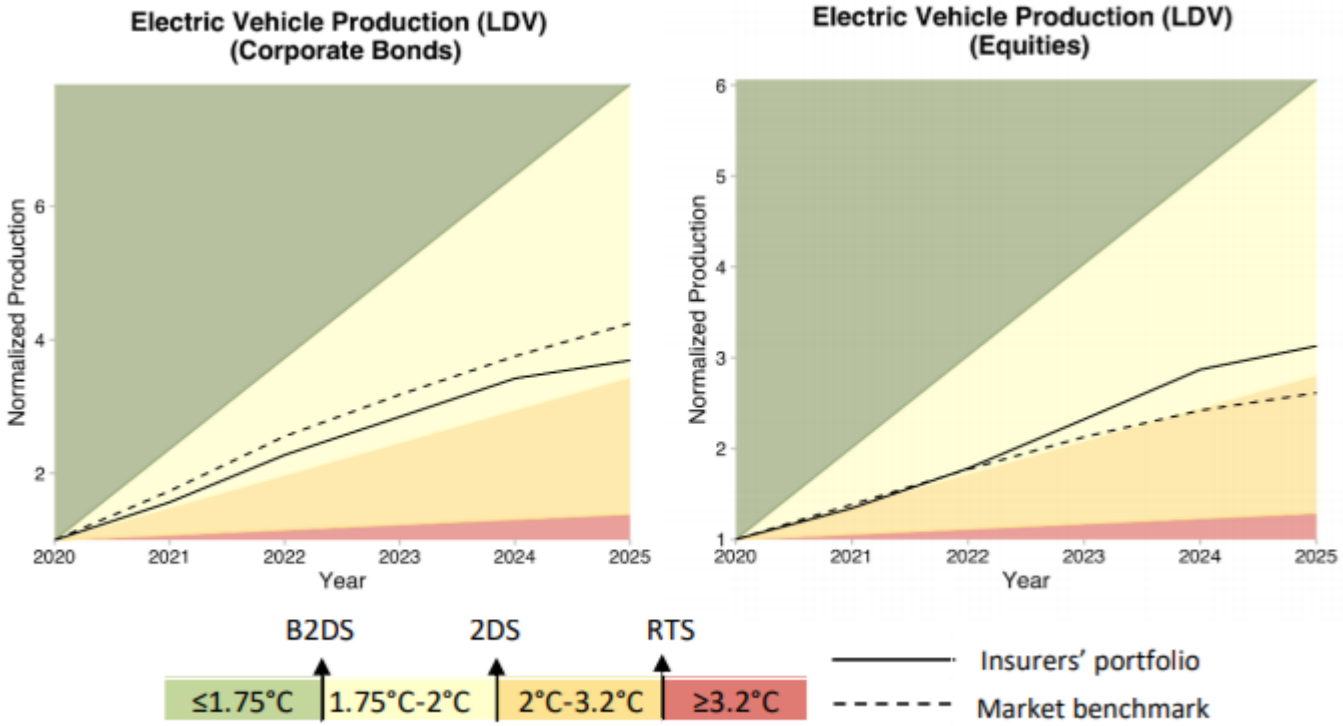


Figure 20. Production Volume Trajectories of Electric Light-Duty Vehicles (LDV) Relative to Climate Scenarios

Strategies for Mitigating Transition Risks

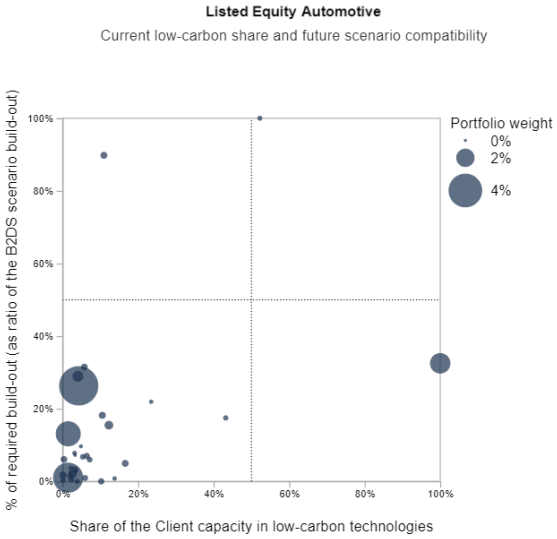
Strategies for Mitigating Transition Risks

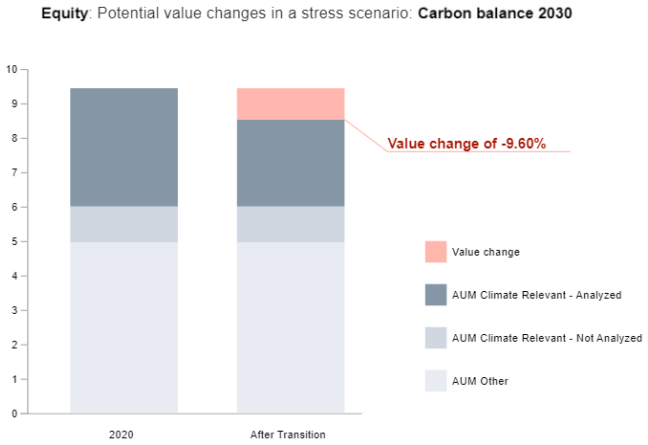
- Divestment
- Investment
- Exclusion
- Engagement
- Setting climate-related investment conditions
- Engage your third-party asset manager(s)
- Explore industry networks on climate risks and opportunities

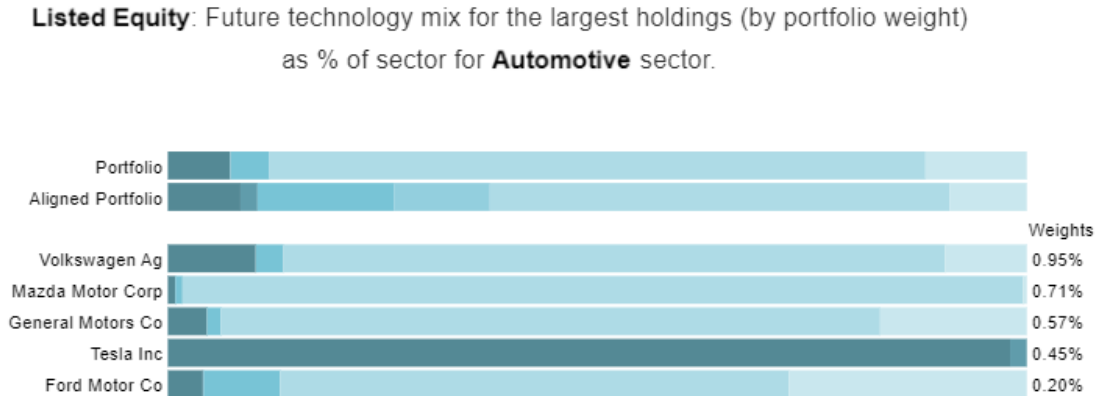
Next Steps

Next Steps

- Individual Reports
- More information and mock reports accessible at [Transition Monitor.com]
- Webinar 2 (12th July)
  - Individual Reports
  - Q&A with 2DII
  - Additional Tools – Climate Action guide and stress test







of
vices

Contact:

Yue (Nina) Chen

climate@dfs.ny.gov