Munich Re Needs to Take Bold Action on Climate Change and Coal

Briefing Paper by the Unfriend Coal coalition and Urgewald
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Introduction

Along with Swiss Re, Munich Re is the world's largest reinsurance company, and thus one of the ultimate managers of risk in our society. Munich Re has warned about the risks of climate change for more than 40 years. Yet when it comes to mitigating climate change the company has so far only taken modest steps.

Most importantly Munich Re continues to be highly involved in financing and underwriting coal and other fossil fuel projects. The company has not excluded insuring new coal power plants, and according to new data commissioned for this briefing paper, holds assets in electric utilities which are currently planning new coal power plants to the tune of 13,100 megawatts.

Scientists have concluded that no more coal plants can be built and existing plants need to be retired early for the goals of the Paris Agreement to be achievable in a cost-effective way.[1] Like all enterprises insurers have a moral obligation to align their business with the goals of the Paris Agreement.

The insurance industry also has a self-interest in avoiding runaway climate chaos. "Left unchecked", the British insurer Aviva spells out this threat most bluntly, climate change will "render significant portions of the economy uninsurable, shrinking our addressable market."[2]

This briefing paper summarizes the financial risks arising from climate change for insurance companies, analyzes Munich Re's continued involvement in the coal sector as an investor and underwriter, summarizes the initial steps Munich Re has taken to reduce its involvement, and compares the company's position on coal with market leaders. It concludes with a set of recommendations to the Munich Re management.

Financial risks from insuring fossil fuels

While the economic costs of natural disasters have seen a steadily increasing trend over the past three decades, the first half of 2017 was marked by rather low costs from natural disaster. Such disasters caused

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[1] See Climate Analytics, Implications of the Power Sector for Coal Use in the Power Sector, November 2016, p. 12

[2] Aviva's strategic response to climate change, July 2015, p. 14

global economic losses of $53 billion in the first half of 2017 – less than half the 10-year average of $122 billion for the semester. Of these losses, $22 billion were insured, compared with a 10-year average of $34 billion.[3]

At least as far as natural disasters are concerned, and ignoring the Grenfell Tower disaster, the first half of 2017 may look quite positive for Munich Re. Yet **over the medium and long term, investments in and insurance services for fossil fuels carry significant financial risks for Munich Re and other insurers**.

First, the transition to a low-carbon economy reduces the value of coal, oil and gas companies. **Investments which insurance companies hold in such companies can quickly turn into stranded assets.** Lloyd's of London warns that climate change, and society's response to it, "could potentially strand entire regions and global industries within a short timeframe, leading to direct and indirect impacts on investment strategies and liabilities".[4]

Secondly, the Bank of England's Prudential Regulation Authority warns that **liability claims against companies causing climate change may pose the greatest threats to insurance companies**. "Historical events have shown that over time liability claims can be more disruptive to the insurance industry than losses caused by individual extreme weather events, especially when new sources of claims emerge", the Authority stated in 2015.[5] By this time, it noted, liability claims against asbestos companies in the U.S. had caused estimated losses of $85 billion to insurance companies.

Several cases against fossil fuel companies claiming damages from climate change are currently pending in U.S. courts and in other countries. Three coastal Californian counties and cities for example recently brought cases against 37 fossil fuel companies, including coal companies such as Peabody Energy, Arch Coal and Rio Tinto. **Once such lawsuits become successful, the insurance companies which have covered the liability risks of fossil fuel companies may well end up holding the bag.**[6]

Overview: Munich Re and climate change

Munich Re has for a long time played a leading role in identifying climate risks. The company established a Geo Risks Research department in 1974, and early on warned about the risks of climate change to society and the insurance sector. "For the first time in the history of our planet", Munich Re concluded in 1990, "mankind is about to change the climate significantly and possibly irreversibly, without having any idea of the consequences that will have."[7]

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[3] See The Actuary Magazine, July 21, 2017, and Insurance Journal, July 20, 2017. It should be noted that economic losses are biased towards losses in developed countries, and don't necessarily reflect the human suffering caused by natural disasters.
[4] Lloyd's, Stranded Assets: the transition to a low carbon economy, Overview for the insurance industry, February 2017, p. 4
[5] Prudential Regulation Authority, The impact of climate change on the UK insurance sector, September 2015, pp. 7f.
[6] In 2009, Swiss Re expressed the expectation that "climate change-related liability will develop more quickly than asbestos-related claims and (…) climate change-related litigation could become a significant issue". See Swiss Re, The globalisation of collective redress: consequences for the insurance industry, 2009, p. 3.
[7] Much Re, Windstorm, quoted in Jeremy Leggett, Climate Change and the Insurance Industry, Greenpeace, May 24, 1993.

“Climate change is changing our world for ever”, Munich Re’s current vision on climate change states. “Only if we manage to anticipate these changes appropriately, and align our business model correctly to the changing world around us, will we be able to deal effectively with the risks from climate change, while also profiting in the long term from the areas of emphasis in our business management.”[8]

Munich Re’s climate activities focus on risk assessment, risk management solutions, and asset management:

- As part of its risk assessment, the company has set up a specialized research and development department to analyze the impacts of climate change on its business model.
- The company views climate change as a business opportunity, and has created new services to insure the risks of renewable energy projects or the climate risks facing agriculture. It also develops and tests new ways to manage climate risks via insurance through its Munich Climate Insurance Initiative.
- Finally Munich Re has committed to integrating climate risks in its asset management, e.g. by growing its investments in the renewable energy sector. In 2006, the insurer was the first German company to sign the new Principles for Responsible Investment.

Munich Re as a fossil fuel investor

After pension funds, insurance companies are the second biggest group of institutional investors. As asset managers they have a significant influence on the direction of the global economy.

The research firm Profundo investigated the fossil fuel investments of 15 leading European insurance companies in a report published in May 2017.[9] At this time, **Profundo identified at least $2,168 million of Munich Re assets invested in fossil fuel companies. This amounted to 8% of all investments found.** Fossil fuel shares made up $393 million and bonds, some $1,774 million of Munich Re’s investments.

In recent years approximately 750 institutional investors representing more than $5 trillion in assets have decided to divest their assets from fossil fuels in one way or the other.[10] This group includes at least nine insurance companies, including leading insurers such as Allianz, Aviva, AXA and Swiss Re.

In early 2016, Munich Re joined this group, putting into effect a policy not to hold “any equities of companies which generate more than 50% of its revenues with coal production or power generation with coal."[11] Munich Re disclosed this policy in response to a survey by the California Insurance Commissioner but did not otherwise publicize it. The company explained to the authors of this briefing that “as a matter of principle we do not publish our internal investment guidelines”.

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[8] Quoted from https://www.munichre.com/en/group/focus/climate-change/mission-and-vision/vision/index.html, accessed on July 25, 2017.

[9] Profundo, The involvement of European insurance groups in the fossil fuel sector, May 2017

[10] See https://gofossilfree.org/commitments/, accessed on July 25, 2017

[11] See California Department of Insurance, https://interactive.web.insurance.ca.gov/apex/f?p=201:3:0:::3:P3_NAIC_YEAR:2015%20%2010227&cs=31EF06815A8965928A1959AAEE1A8D3FE, accessed on July 25, 2017

Munich Re's divestment decision is a positive start, but its threshold of 50% coal revenues or power generation is unreasonably high and the inclusion of equities but not of bonds is not consistent.[12] In comparison, peer companies such as Allianz and Swiss Re include both bonds and equities in their policies and are use a divestment threshold of 30%. The policy bars Munich Re from investing in the equities (but not in bonds) of coal giants such as Indian's NTPC (coal share of 94%), China's Shenhua (90%) or Huaneng (71%).[13] As the examples below demonstrate, it still allows the insurer to hold assets in major coal developers around the world.

Munich Re as a fossil fuel underwriter

For better and for worse, insurance companies play an essential role in underwriting the development of industrial society. No highrise could be built, no factory operated without insurance. The same is true for climate-destroying coal mines, pipelines and thermal power plants.

Data on market shares and specific underwriting contracts in the insurance sector is not available. Yet Munich Re has a specialized energy division, and based on market intelligence reports and the company's marketing, **Profundo considers Munich Re a leading fossil free underwriter with a high involvement in the sector.**[14]

Munich Re claims that it integrates environmental, social and governance (ESG) criteria into the decision-making process for underwriting contracts, e.g. in the risk assessment of major infrastructure projects. Furthermore ERGO, the primary insurance group of Munich Re, does not underwrite any oil drilling operations in the Arctic.

In April 2017, AXA decided to no longer offer insurance services to coal companies in the interest of a consistent climate policy. In contrast, Munich Re (including ERGO) has so far not taken any steps to rule out underwriting new coal projects. The company is, in other words, prepared to insure the coal projects of companies in which it would no longer invest. **Coal insurance is not consistent with Munich Re's role as an investor, and marks blind spot of the insurer's climate policy.**

Company examples

According to new data compiled by the research firm Profundo for this briefing paper, Munich Re still holds a total of $103.6 million in bonds of nine electric utilities in the U.S., Europe and South Africa which in total are operating well over 100,000 megawatts of coal and gas power plants.

Most importantly, **Munich Re continues to hold $21 million in bonds of Eskom, AES Corporation, RWE AG and CEZ AS, four utilities which are currently planning to develop some 13,100 megawatts of new coal power plants in the Czech Republic, Germany, Hungary, India, the Philippines and South Africa**.

South Africa's Eskom derives 91% of its electricity and more than 50% of its revenue from coal. Under its divestment policy could no longer hold equities of the utility and it is inconsistent that the insurer is

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[12] At the Munich Re AGM in April 2016, Chairman Nikolaus von Bomhard claimed that the divestment policy covered both equities and bonds, but the language quoted above and the evidence presented below suggests that this is not the case.

[13] Data from Urgewald's Global Coal Exit List, https://coalexit.org/database, accessed on July 25, 2017

[14] Profundo, The involvement of European insurance groups in the fossil fuel sector, May 2017

investing in Eskom bonds instead. For the other utilities the coal share of the revenues (or where not available, of the power generating capacity) is 34% for AES, 41% for RWE and 47% for CEZ, respectively.[15]

Munich Re also holds $80.7 million in Southern Company and two of its subsidiaries, Alabama Power and Georgia Power. Southern Company, a large U.S. utility, no longer plans new coal power plants but according to a study in 2007, was the biggest greenhouse gas emitter among the country's utilities at the time.[16] The coal share of Southern Company's power generation is currently 31%.

Munich Re defines coal companies as entities which derive more than 50% of their revenues from coal. This definition is less thorough than the one used by its peers. **If Munich Re covered bonds as well as equities in its policy and used the same 30% threshold which Allianz and Swiss Re apply to define coal developers, it could avoid investments in companies which undermine the Paris Agreement such as AES, RWE and CEZ and other large coal utilities such as Southern Company.**

Conclusion and recommendations

As an investor and underwriter of coal companies, Munich Re has taken initial steps but need to do more to match the activities some of its leading peer companies have taken to address their responsibility for averting catastrophic climate change.

In June 2017, Urgewald and 12 other member organizations of the global Unfriend Coal coalition **asked Munich Re to take the following actions on coal and climate change:**

- By October 2017, Munich Re needs to adopt a policy to stop underwriting and divest from coal companies (broadly defined as companies deriving at least 30% of their revenues or electricity generated from coal);
- Beyond October 2017, Munich Re will also need to stop underwriting and divest from other fossil fuel companies;
- As the company withdraws from the coal and fossil fuel sectors, it needs to increase its support for clean energy sources accordingly.

In November 2017, the Unfriend Coal coalition will publish a scoring exercise which will analyze and rank the positions of 25 leading insurance companies, including Munich Re, on coal and climate change. **By following the above recommendations, Munich Re can protect its long-term self-interests and contribute to its ultimate mission in society: to protect its customers from catastrophic risk.**

Contacts:

Regine Richter, Energy expert at Urgewald, +49 170 2930725, regine@urgewald.org

Peter Bosshard, Finance Program Director, The Sunrise Project, peter@sunrisepoject.org.au,
+1 510 213 1431

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[15] Profundo, Munich Re holdings, July 31, 2017

[16] MacDonald, Lawrence, CGD ranks CO2 emissions from power plants worldwide, Center for Global Development, November 14, 2007