

Powered by Marsh FINPRO

Episode 6

Enhancing capital access to low-carbon initiatives and hedging against extreme weather risks through insurance

Welcome to the *Powered by Marsh FINPRO* podcast. Through a series of interviews with experts from across the energy and power industry, host Grace Brighter will examine key challenges and opportunities brought by the energy transition, and how to approach and manage the evolving management liability risks this transformation brings.

Sarah Baldys:

Welcome to the Marsh *Powered by FINPRO* podcast. Through a series of interviews with experts from across the energy and power industry, this podcast will examine key challenges and opportunities brought by the energy transition, and how to approach and manage the evolving management liability risks this transformation brings.

I am Sarah Baldys, US power and renewables leader at Marsh's financial and professional liability practice, and I am pleased to introduce the host of the *Powered by Marsh FINPRO* podcast, Grace Brighter.

Grace Brighter:

Hello and welcome to *Powered by Marsh FINPRO*. I am your host, Grace Brighter.

This episode we are very happy to have Amy Barnes, Head of Sustainability and Climate Change Strategy at Marsh McLennan.

Amy is responsible for leading Marsh's global strategy on the development of climate and sustainability related initiatives for clients, particularly in relation to the impact of a changing physical risk landscape, improving access to capital for green initiatives, and a more thorough understanding of climate related project risks.

She also participates in Marsh McLennan's Sustainability and Climate Change Program, which focuses on developing sustainability and climate change services. With over 20 years of experience, she has a deep understanding of clients, risk management approaches and offers valuable insights in insurance and risk management decisions.

We are very lucky to have her here with us today.

Hi, Amy. Thanks for being here today.

Amy Barnes:

Thank you very much. I'm delighted to be here.

Grace Brighter:

Great. So to start, Amy, would you mind really explaining your role for those listening? Could you kind of share what a day looks like for you? And I think it would be great if you can touch on some of the key priorities as head of sustainability and climate change strategy.

Amy Barnes:

So that's quite a big question. So, so primarily my role is to support our clients navigating climate and sustainability issues. So I'm not focused on internally how Marsh decarbonizes its business, thinks about sustainability - they're critically important and important for our credibility, but that's not my area of responsibility.

I'm thinking about two main things when I think about my priorities.

One of my priorities is "How do I embed climate and sustainability thinking in the work that everybody does

everywhere" and you guys in DNO find in the film pro-business, do this all the time? You're always thinking about how new sustainability reporting criteria are going to affect the way underwriters look at risk, but likewise we need to be thinking about improved. How does insurance renewal specialty meetings need to evolve to contemplate climate and sustainability issues?

And then there's also the issue of what do we need to innovate, what new products and services do we need to innovate to help our clients as they decarbonize or as they navigate more extreme weather? Unfortunately, or actually probably from my perspective, fortunately, there is no standard day, so I do a lot of public speaking, which I really enjoy and the reason I enjoy that is because it forces you to crisp up your message and make sure you're absolutely clear on your priorities and the message you're trying to get across. But equally, I love working with the team and I love geeking out on the complex challenges of innovating new and solutions.

Sarah Baldys:

So Amy, thinking about climate risk, you know, climate risk seems really complex and sort of a bunch of interrelated risks altogether. I know you spend a lot of time thinking about and working on climate risk, maybe just to start off for the listeners, what does climate risk mean?

Amy Barnes:

So I'm actually going to make it really simple because I think that's one of the things that the climate community has done a really good job of is communicating the complexity and that just makes it harder to navigate.

So it's really simple, it's just two things. We need to reduce the amount of fossilized carbon that we're releasing into the atmosphere and so we need new ways of working that are lower carbon. Even if we were to stop burning fossilized carbon tomorrow, we still have going to have more extreme weather than we're currently seeing. That is baked into our future, so we need to figure out how to adapt to more extreme weather. So they're the only two things. Businesses need to think about how do we act and operate in a lower carbon way? And how do we cope with the extreme weather that's coming at us...and extreme weather we haven't really contemplated before. And then there are layers and layers of complexity sitting behind that as you mentioned.

Grace Brighter:

So thank you, Amy. That was a really great overview of what climate risk is kind of taking things a step further in your current role. We know you speak very often with business and government leaders around the world on climate risk. So could you just share if there's some key trends being?

Amy Barnes:

So for the first 10-15 years of climate sort of having more space in in corporate discourse, the conversation has really been on decarbonization. And there's been a sense that if we start talk about adapting to climate change that we've given up on decarbonization, and that's now changed. You can tell from my accent that I'm from the UK, and that's where I'm talking to you from right now, but I still I used to live in the US and I still watch the US weather. And the weather extremes that you guys are experiencing are being noticed by executives. And so businesses are now saying yes, we need to decarbonize, but the conversation has shifted really noticeably, probably in the past two years, to far more focus on adaptation. And so I know we're mainly talking to people about D&O, financial risks on this on, on this in this conversation, but when we think about climate risk, we think about more than just the potential they have to damage property.

It isn't just that we may have devastating wildfires, or we may have floods, or we may have hailstones that damage our solar panels, we also need to think about things, and execs are really worried about, a thing called ecosystem services. Now that's a fancy way of saying the things that we rely on nature for, and so it's easy to think about the almond farmers in California who need pollinators to pollinate their trees, but a lot of people aren't thinking about how much we use water in manufacturing, and so a data point that I find fascinating is in Taiwan.

For the past three years, they've [Taiwan] been paying farmers not to plant rice so they've got enough water to make semiconductors, and increasingly the trend that we're seeing around business and public sector is thinking about these impacts of climate change and how are our systems going to cope with more extreme weather, whether that's more water, less water, too much heat, not enough heat. So that that's a that's a really growing thing.

Sarah Baldys:

It's really interesting to think about too, because it's this is an issue that just effects all industries. You know it's agnostic to any type of business, and so when we're thinking about advising executives or, you know, on corporate strategy? How should executives and boards be considering climate risk, you know, in their strategic planning and risk analysis?

Amy Barnes:

So I love your question because it's about strategic planning and risk analysis, but probably I think where I'll start with is reporting because reporting is where a lot of the risk that you worry about Sarah comes from and we know that there's always more D&O risk when there are more reporting standards.

So the US is a really complex environment because although we may not have federal regulations, there are regulations in different states that require different amount of reporting. And then for your multinational clients that have operations in Europe, any of those have sizeable operations in Europe will also be impacted by the reporting requirements either in the UK or in Europe. So I think that's the first area of make of risk manager of making sure that the reporting is clear, concise and complies with the law because all the regulations I should say to make sure that you're managing that part of the risk.

But then when it comes to strategy and how a board may be found, or a leadership may be found to culpable of not managing the strategy, that's really complex because you could be criticized if you don't move fast enough and there will be a group of stakeholders who will criticize organizations for not decarbonizing fast enough, and there are another group of stakeholders that could well level criticize criticism for decarbonizing too fast and getting that balance right, I'm afraid, there is no silver bullet for, but being really clear on the rationale behind the decision making and how you're deploying your capital expenditure to support the path that you're taking.

So that strategic risk is very complex to navigate.

It's simpler in places like Europe, where the legislation is clearer. The legislation forces people to act in some way, but absent that, that regulatory incentive, even if you can see the direction of travel and even if you know you need to invest over 20 to 30 year time horizon

when regulation is going to change over that, it makes it sort of extremely difficult to land there.

And then, when Grace and I were talking just now, I was talking about the emerging theme or the accelerating theme of climate adaptation. And I think recognizing that extreme weather is happening more often and in places we wouldn't expect it... So in last April, catastrophic floods in Dubai, not an area that you associate with flooding, necessarily. And so it's also unexpected weather, not just extreme weather, and so how do you protect your assets from that to make sure that not just damage to asset, but make sure your operations can continue? But also, how do you protect your people?

And actually, with our sister business, Mercer, in the next few weeks, we're going to be publishing a report that shows the number of people in the US, number of colleagues in the US that have been impacted by climate events, and I can't quite remember the number, but it's over 70% of employee survey and it's thousands of employees have been surveyed have said they have been affected by extreme weather in the past 18 months. And so you've got your assets to think about your operations and your people critically, so those people how are your people affected in the event of emergency, but also how are you planning for changes to the way your workforce has to work?

So, really interesting piece of work done by one of the construction companies in the US looking at extreme heat and they found that when they had their operative turning up to work, many of them were turning up to work already dehydrated. If you're dehydrated, your coordination's compromised, your decision making's compromised, you're more at risk. Really low-cost intervention of giving people a nudge to get hydrated, making sure there are hydration stations as soon as people get to work, so really anticipating some of those really low cost activities and I realize I'm going long on this answer because there are so many things to do and it's such an important area, that some of the things are easy and low cost, but some of them you need to start planning now because if it's a large CapEx, when do you fit that into your planning to make sure it's one affordable? And as you buy or develop new projects, how are you contemplating, how are you modelling future climate risk to make sure you're building something that will be fit for the extreme weather we're experiencing in 20 or 30 years' time?

Grace Brighter:

Thank you, Amy. That was that was great and very insightful.

You know, you mentioned some of the impacts of climate change and some of the considerations that should be made from a board-level perspective and I think you started to get a little bit into this next question, but, are you able to really help us understand how a company can assess their own climate risks? So in other words, how do you really quantify the potential financial costs of damage to infrastructure?

Amy Barnes:

Okay, so we're gonna. So, so the way you frame that question, we're just gonna focus on climate adaptation and not the cost of transitioning to low carbon.

I think that's a great question and I'm in danger of geeking out, and so just feel free to like, press the buzzer if I'm going too deep at any moment but...

We've been modelling CAT risk for decades now, and when we think about CAT risk, we tend to think about acute risk, so we think about the wind and the floods that can come, but some of the climate change risks are chronic risks such as heat and water scarcity and some of those other risks, so there are some new perils that we're not quite as good CAT modelling, but if I park those sort of modelling uncertainties and just assume that we've got good models for all the perils, there's a lot of work that's been done to then to adjust those for climate change, to anticipate what those models will look like in in you hear people talking about warming in 1 1/2° and two degrees in three degrees warming environment, we can then look at the likelihood of those weather events.

That isn't far enough, though. We can't just go from how likely is it that the hazard happens. We need to turn that into what's my financial exposure to that? And so then we need to think about what's the building's vulnerability, I already said I used to live in the US and I lived in Houston, and the apartment block I lived on, I can't remember the bottom six floors of the apartment block were all carpark, so actually very little economic damage in the event of a flood, and so as you can. But whereas if I'd lived in a if I'd lived in a sort of a single family dwelling, my flood risk would have been very much higher, so you can see that the impact of the hazard isn't the same for every asset type.

So the initial scanning that companies need to do is to understand what hazards could be affecting their sites, and then you need to understand what's my vulnerability to that hazard? And then the work that we do is helping people to say, OK, how do I make an intervention? What action can I take to reduce my vulnerability to that hazard? And then importantly, because we're really good at pricing risk, we can then give people a return on investment of those interventions and when on a timeline, they may be needed because climate change is a process, and so we may well say that like by 2035, you really do need to have flood defenses, but you don't need to fund those in 2025...I'm getting my years...by 2035, you may need to invest in flood advances, but you don't need to flood the fund that in 2026, this is the time window in which you should be doing.

So we can kind of revise on what action should be taken, what the return on investment of those are and when in the next three, 5, or 10 years, you should be prioritizing those investments.

Sarah Baldys:

So this makes me think about sort of the energy transition overall because it is on this sort of arc of transition. And so thinking about all of that and the integrated nature of all of those components of this, how do you evaluate sort of the potential effects of, you know, emerging or changing policies and regulations? Changes to the supply chain, changes to customer demands? You know, so much change, and that's why we call it a transition, but in all of this, you know, I just wonder how you're thinking about that.

Amy Barnes:

I think it's a very complex world to navigate because there are so many uncertainties. And as we've seen before, these CAPEX projects or investments over 20-30, fifty years and if you think, I mean...Sarah, you cover all of the energy and power business, so nuclear, even longer investment time horizons, and so how do you make decisions when there is so much regulatory volatility, we've got cost volatility - be that tariffs or just or just general cost inflation that we've seen. We've seen geopolitical instability, and then also within the supply chain that climate risk I mentioned Taiwan earlier in our conversation about lack of water or or the fact that we have a water dependency for semiconductors.

What we've seen in 2024, we saw a number of European automotive manufacturers having to make financial statements because they've been impacted by floods in Switzerland that had affected the aluminum industry and floods in Slovakia that had affected their supply chains. So there are these many fold risks that people need to navigate and how do you make decisions to invest with that much uncertainty?

There's a really nice expression that one of my colleagues has been using that I'm going to shamelessly steal, which is know more, do more. And I think having visibility of those risks allows you to make decisions because you can see how much volatility and how much uncertainty is, you can figure out what's within your tolerance, and so knowing that you have vulnerabilities within your supply chain and Sarah, I think you know the work that we've been doing building the centrist capability, so we can help people have visibility, their supply chain and see where the vulnerabilities are, from concentrations of bottlenecks or geopolitical or credit risk or all of those risks that are bundled up. The more you know, the more you can do, because you can decide on the return on investment of resilience.

So some of the clients that we've worked with - I'm going to go back to the automotive industry - have decided that the way they're going to manage their risk is increase their working capital in certain parts of their stock. It may be that they diversify their supply chain to make sure that they've got alternative actors. And so I would say that it's really complex, but I think that the best, your best chance of success is to know more so you can do more and so uncover all of these risks.

Grace Brighter:

Thank you, Amy. I think pivoting a little bit this is probably a great segue into our next question. What is really the role of insurance in managing climate risk?

Amy Barnes:

Okay, so two big jobs it has to do. So if we go back to transition, the decarbonization of the economy. First and foremost, the reason I think - I don't want to put words in your mouth - the reason I love the industry I work in is because we are the lubricant of the financial services system. Nothing happens without us. Planes don't fly, hospitals don't get built, people generally can't afford to take risk unless we do our jobs well, and so that means for the new low carbon technologies, we

need to make sure that insurance is there to allow those businesses to invest and to allow banks and other people to lend.

And so, insurance...I'm sure everyone on the call knows is traditionally underwritten on the basis of past losses, so how well do we understand the likelihood of loss? And that's really hard when you're talking about a new technology or you're scaling a technology into a scale, it's never been used before or you're using it in a way it hasn't been used before, in conditions it hasn't been used before. How do we help underwriters quantify that risk to make sure those new technologies are insurable?

But there's much more insurance that insurance can do to support the transition than just that operational risk. It's really hard to get funding for a transition project unless you have an offtake now, there, aren't we? The insurance can't underwrite offtake per say, but there are elements that can be insured, such as price volume. If your off take is dependent on the sun shining or the wind blowing, entirely insurable. If you have credit risk in your supply chain or with your contractors, insurance can take some of that off the table. There are elements of strategic and financial risk that insurance can also help with, as well as technology performance and all kinds of other disruptions. Geopolitical risk, FX risk. We don't really provide FX risk, but you may have export controls if you're investing in another country, you may have concerns about export controls and not being able to get hard currency out of the country.

So that's one area where it tends to be, it's conventional insurances that we need to cover for new technology. The other place that insurance really needs to have a greater role is when we think about adaptation.

So with adaptation, more extreme weather events, we often hear insurance being criticized, and especially in the US at the moment, a lot of homeowners are frustrated by the insurance industry, and I can absolutely understand why they have those frustrations. But I think we need to recognize that what insurance does really well is price risk and it's a risk signal and we need to be listening to that risk signal because it will tell us...it gives an, it gives us an indication of what actions we may need to take. And so when it comes to adapting to climate change, the problem isn't insurance, the problem is the underlying risk. So let's use insurance as a pricing signal to help us take the actions we need to take to reduce the risk, so things stay insurable.

I know that sounds a bit circular, but I think it's really important to understand that insurance will not save us from adaptation, it will buy us time. It may be that you need a parametric insurance because at the moment while you reduce your risk, you're still very exposed to extreme weather, but all that's doing is buying you time because when it stops being a risk and it becomes a certainty that every year you will get flooded, that insurance will no longer be available.

Sarah Baldys:

So thinking a little bit more about this. So from the perspective of underwriters, maybe just turning it on its head a little bit...What could they or should they be looking for to sort of gain comfort that a company is managing this risk or has a plan for adaptation that is something that they can feel comfortable ensuring?

Amy Barnes:

And so I think that this this is one of the one of the conflicts - not quite the right word in the insurance industry - is that underwriters tend to think on a 12-month cycles and the issues that we're talking about are multiyear, multi decade issues and so, in reality, an underwriter today isn't too worried about whether you're resilient for 2030 because they can just choose not to write your risk, which is why it's even more important that the corporate's taking a proactive attitude to managing their risk, because there's a very...sorry, insurers absolutely want to write business, I'm not suggesting that they don't, but they do have a walk away if the risk hasn't been managed well.

So I think especially when we're thinking about DNO and financial lines insurance, a lot of the focus is on reporting and are people reporting clearly and concisely? Are they overstating? And you may...I think we're very familiar with the term greenwashing. Overstating environmental claims is a really big concern, but increasingly, people are talking about "greenhushing" because this can be a partisan issue...people wanting to downplay the work that they're doing, in which case that's also could be bad for an underwriter's perspective, because if a company's doing a lot, they could be accused by one party of not taking sufficient action. And so I think underwriters just having a really clear understanding of the company's strategy both around decarbonizing and building the resilience for the future and giving feedback - I'm now asking on behalf of insureds if underwriters can give feedback – about, "Yep, this is fine for this year, but in

future this is the direction we'd expect to see" and not be scared of giving that feedback because I think insureds want to hear that signal of what actions are expected from them in the future.

Sarah Baldys:

Just to follow on to that too, I think in terms of hearing that anything that is informative, you know to our clients and to companies on what their best practices should be or not just should be, but how to prioritize those - and you made that point earlier, Amy, about you know what you might need to do this year versus in 5 or 10 years from now and it's it is such a critical role that insurance can play to help inform that whole ecosystem and how companies can be thinking about this.

Our clients also need to be able to communicate clearly in the renewal process in their submissions and kind of back and forth so.

Amy Barnes:

And we, and we can help them do that. We can absolutely help them do that.

Sarah Baldys:

And then maybe we can talk, you mentioned greenwashing and thinking about ESG and corporate commitments and disclosures and all of that. First of all, that has, as you mentioned, gotten a lot of attention and focus from the D&O underwriting community, for obvious reasons, but I've heard that there's some movement away from ESG as sort of we thought about it for the last few years and kind of moving into some, you know, different ways of conceptualizing the same thing. You know, first of all, is that accurate, and then also what's the impact of that shift?

Amy Barnes:

So, my economics 101 class said that the job of business is to make money now and, in the future, and the investment community some years ago now said we need to see more than just the report and accounts to understand abilities, a company's ability to make money in the future. We think other things are important as well. Are they taking care of the environment? Are they managing their business well? Are they taking care of their people and the communities they operate in, and do they have good governance? Are they well managed? So we want to have more data that supports

our understanding of a company's ability to make money in the future.

So it was always ESG was always a construct of the investor to community trying to get a sense of that. ESG hasn't been a term that's been widely used...ESG then became a term that was more widely used because investors cared about it. So corporates cared about it. But organizations like the United Nations have always been focused on sustainability and they have 17 sustainable development goals that they focus on because they haven't been so worried about aspects like governance, which is an area that the investors are clearly very focused on. So I think what we have seen and partly because it's seen as a partisan issue now which I say I do find a bit surprising because I find that if you take certain elements out, like most businesses want to be good corporate citizens and want to behave well in the communities in which they operate, most companies want to do right by their employees, and then we want their employees to go home safe every and come back in tomorrow, and most companies want to abide by the environmental regulation. And if you don't have good governance, then go home. So. So. But there has been a shift away from it...a shift to really talking about broader sustainability and actually it was governance, the white bedfellow for those other factors anyway. And so I think we are seeing the term ESG used yet less the term sustainability used more, but I think it's all within the spirit of trying to get a sense of abilities, a company's ability to make money now and in the future.

Grace Brighter:

Great. Amy. So to sort of close out the conversation here today, I we think it would be great if you could share your two cents on you know what, what lies ahead with respect to climate risk and if you could kind of share what gives you optimism?

Amy Barnes:

So the reason, so the reason I'm up, I feel optimistic is I've just come back...

Marsh Energy hosts an energy conference every two years, I've just come back from that - 1000 people, more than 700 clients from 56 countries, and the direction of travel is everybody is trying to figure out how do we decarbonize, recognizing we need to make the energy demands of today and that there are areas of energy poverty that we really need to support, have

access to the great outcomes that access to energy to give of better health outcomes, better economic outcomes, better Business outcomes. And so we know that there's work to do to make to improve access to energy.

The Ukraine war has taught us about energy security, but everyone is thinking about at the same time, how do we decarbonize? So that's exciting. The fact that adaptation is now firmly on the agenda and not just the private sector, but businesses are also thinking about "What action do we need to take to make sure that we are resilient to extreme weather?"

I don't want to be overly optimistic there because it's fewer companies than I would like are having that conversation, but most of the large asset management real estate companies that have got large footprints really are taking this very seriously and building it into their strategies. And so there are definitely bright spots out there.

And then we see and we see some cities that are really very far advanced in their thinking about how they support adaptation, so I'm going to tell you an example from the place that I live. I live outside London in the countryside and the authority that I'm in is trying to reduce flooding in the cities, and so we have some land with our house, so they've asked if they can come and build ponds on our land to store water when it rains, it's an initiative called "Slow the Flow." So everyone upstream of the cities, they're saying if all of the land upstream city can just take a bit more water, we will reduce the impacts of floods of of of will reduce the volume of water coming down and hitting the vulnerable houses there.

And it's really exciting seeing some of these initiatives kick off and people like me just being excited at the idea of someone coming and putting a pond on my land.

Grace Brighter:

Great. Well, with that, thank you so much for joining us Amy, you know, this conversation is going to be extremely insightful for Marsh colleagues, our insurance partners, maybe those who are risk managers or those key decision makers at various organizations, so we really appreciate your time today.

Amy Barnes:

I appreciate the opportunity, thank you both so much.

Grace Brighter:

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