ClimateWise Principles

The Fourth Independent Review 2011

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ClimateWise
REDUCING THE RISK FOR TOMORROW

Authored by
pwc

An initiative facilitated by
UNIVERSITY OF CAMBRIDGE
PROGRAMME FOR
SUSTAINABILITY LEADERSHIP

CLARENCE HOUSE

I am under no illusion as to how challenging the events of the last year have been for the global insurance industry. Economic turmoil has stifled investment returns and there has been a seemingly endless onslaught of both manmade and natural catastrophes, from the Gulf of Mexico oil spill to the earthquakes in Chile, New Zealand and Japan. I know that the operational challenges these events have posed are immense. That is why I am so encouraged that ClimateWise members around the world continue to show foresight and determination in challenging themselves to deal with the biggest risk multiplier of all, climate change. Not only are we already feeling its impacts, but we know that we must act today if we are to affect its trajectory in any meaningful way.

What has particularly struck me about these tragedies, though, is not the immediate damage people and businesses have suffered, heart-breaking though that has been. Rather, these events have demonstrated how dependent we are on a healthy, thriving natural environment that can both supply us with vital resources and absorb the impact of the worst extremes. To see the point one only has to think of the lasting devastation suffered by coastal fishing communities when ecosystems are destroyed by oil spills or the plight of inland communities suddenly inundated by tsunamis that would once have been absorbed by mangroves or coral reefs. But, of course, we continue systematically to undervalue Nature's services and to erode natural capital, thus creating a world that is both more risky and far less resilient. Creating a permanent, sustainable natural environment – in harmony with a durable, lasting built environment – is our only choice if we are to avoid seriously short-changing our grandchildren.

The scale of these issues can be utterly overwhelming, so when I met chief executives of ClimateWise member companies earlier this year, I was reassured to learn that they have begun to act on exactly this issue – researching, promoting and even investing in ecosystems like wetlands and forests as key measures to improve the resilience of vulnerable communities against natural catastrophes. I was also fascinated to hear that ClimateWise members are now thinking about how they can encourage their more carbon intensive corporate clients to develop much more sustainable business practices, in recognition of the huge global risks to which they are otherwise contributing.

But what heartened me the most was when I heard that ClimateWise is acting as a "lightning rod" for industry leaders, helping them keep the challenge of unsustainable climate risk on the Board's priority list, supporting collaborative learning where deeper understanding of solutions is needed and galvanizing their collective influence over decision-makers. The world needs much more of this action because all the signs are that there is simply no time to waste – despite what the sceptics may currently be saying.

Charles

Chairman's Foreword

For the past 300 years, insurance markets have helped people chart a more resilient course through a world so often defined by extremes; without the financial safety net of insurance, individuals, businesses, and even governments, would not have been able to bear the risks inherent in the trade and development that has shaped humanity's progress. Yet if the past 40 years that I have spent in the insurance industry have shown me anything, it is that the world is becoming a more extreme place, with climate change up there as the number one risk.

Our frankly cautious response to climate change to date is totally disproportionate to the scale of the threats we face. A 5°C rise in global average temperatures is perfectly plausible over the next century if our emissions escalate on current projections. The planet hasn't been that warm for 30 million years. For me, this puts into context the vulnerability of all of the complex systems we have come to rely on – financial hubs in coastal cities, global agricultural belts, international supply chains – in a timeframe that is but a snapshot in comparison.

So what does this mean for the insurance industry itself, an industry that historically has been so proactive in encouraging society to keep risks manageable, whether it be installing sprinklers in buildings to reduce fire risk or introducing seat belts to lessen the impact of road accidents? This is a question that I prioritised when I was Chief Executive of Swiss Re from 2003 to 2005 and I know that a number of colleagues in the industry have given it similar attention.

Insurers everywhere should be using our industry's core expertise to better understand and communicate the risks climate change poses to our economic and social systems and to forge and promote solutions to bring those risks down to an acceptable level. This independent review demonstrates that insurers across the world are indeed actively playing this role in a variety of ways.

But in my experience, the everyday operational challenges the industry faces mean that it will always be difficult for Boards to give this long-term, creeping threat the scale of response it requires today without new ways of thinking and additional support. That is why I am so excited to have been appointed as the Chairman of ClimateWise. Under Andrew Torrance's guidance ClimateWise has in a few short years expanded its membership beyond its UK base and advanced its aspiration to become a leadership group for collaborative learning and action on climate change within the insurance sector. Our aim now is to build on that progress.

The ClimateWise Collaborations developed by members to help them tackle issues beyond the influence sphere of any one organisation are a valuable tool already at our disposal. It is a natural fit for our industry to be contributing to efforts to adapt society to the inevitable change locked into the system. Nevertheless, we must not overlook the fact that unless we control the limits of that change – through the necessary processes of increasing energy efficiency, decarbonising energy generation and promoting the earth's natural carbon sinks – we will soon find we cannot adapt our way out of everything.

Realising this vision requires strong partnerships with key industry players and policy-makers alike and I look forward to ClimateWise playing its part in driving this change.

John Coomber
Chairman, Climatewise
Member of the Board, Swiss Re

Introduction

The insurance sector faced considerable challenges during the Fourth ClimateWise reporting period (June 2010 to June 2011). External pressure from regulatory change, natural catastrophes, continued economic difficulties and sovereign debt crises have affected all aspects of activity, from underwriting, through claims, asset management and investment performance to operations, finance and compliance functions.

The Centre for the Study of Financial Innovation (CSFI) published its 2011 Insurance Banana Skins Report(1) during the period. This report surveys 'a global sample of nearly 500 practitioners and close observers' of the sector. It identified that the most pressing challenge the sector faces is the burden of regulation. However, among the challenges identified, natural catastrophes featured as the fifth most urgent (up from 22nd place in 2009), a reaction to the earthquakes in New Zealand and Japan. Climate Change was ranked down at the 20th most pressing issue, up from 28th in 2009, but still a long way off the priority list and a far cry from the 4th place in the 2007 survey.

Also during the reporting period, Munich Re's Topics Geo 2010(2) analysis identified that of the 950 natural catastrophes recorded in 2010, 90% were weather-related. This made 2010 the year with the second highest number of loss-related natural catastrophes since 1980 (2007 being the highest) and exceeds the annual average for the past 10 years (785 events per year). Overall losses amounted to $130bn, of which about $37bn was insured. According to Munich Re, this puts 2010 among the six most loss-intensive years for insurers since 1980.

Therefore, while weather related losses continue to impact claims, climate risk as an issue is still not seen as pressing as the more immediate regulatory pressures and economic conditions. That is not to say the sector is taking no action. This year's ClimateWise members continue to demonstrate recognition of the important role insurers and the insurance sector has in developing and encouraging the transition to a climate resilient and adequately adapted lower carbon global society.

The ClimateWise Managing Committee appointed PwC as the independent reviewer for this fourth review. The ClimateWise Principles are designed to enable members to work individually and collectively to reduce the economy's and society's long-term risk from climate change, within the confines of a competitive market. The six principles cover all aspects of the diverse insurance sector's response to climate risk and require the members to:

1. Lead in risk analysis
2. Inform public policy-making
3. Support climate awareness amongst customers
4. Incorporate climate change into investment strategies
5. Reduce the environmental impact of their own business
6. Report and be accountable.

ClimateWise members have committed to publish a statement as part of annual reporting, detailing the actions they have taken to comply with the ClimateWise Principles. This annual statement is central to the continuing credibility of the ClimateWise initiative. It serves to hold ClimateWise members to account as well as acting as a show-case for its members to demonstrate their own progress and provide leadership for the wider insurance industry. These reports form the first stage in the analysis of compliance against the principles. A second stage of analysis takes place in the form of a telephone interview. This interview is designed to more fully understand the level of compliance against the Principles and sub-principles and gain further evidence of progress if required.

This year, the review considers the submissions from 26 members, the submission from the Lloyds Market being consolidated into one report for Lloyd's of London. It also incorporates first time submissions from two new members; Willis and If P&C.

Executive Summary

Despite the considerable challenges that ClimateWise members have faced, from a variety of external economic, regulatory and natural catastrophe pressures, members continue to demonstrate their commitment to the ClimateWise initiative, as evidenced by the reporting of activity across the principles in 2011.

Overall, ClimateWise members have maintained the high levels of compliance seen in the 2010 Independent Review, with average compliance across all the principles standing at 88% (2010: 88%). This performance builds on the previous three years of continued growth in compliance, from 65% in 2008. Posting further growth in compliance in this reporting period was always going to be difficult against the backdrop of the external market challenges. Therefore maintaining compliance at just under 90% can be seen as something of a strong performance.

It is also key to point out that members of ClimateWise, in signing up to the principles and reporting against them, are indicative of a section of the industry that is more advanced in addressing climate risk. In September 2011, Ceres released a report entitled 'Climate Risk Disclosure: Evaluating Insurer Responses to the NAIC Climate Disclosure Survey'(3). While clearly focussed on the North American market, the report concluded "while the NAIC survey revealed a broad consensus among insurers that climate change will have an effect on extreme weather events, only 11 of the 88 companies reported having formal climate risk management policies in place, and more than 60 percent of the respondents reported having no dedicated management approach for assessing climate risk". In contrast, the level of compliance across the ClimateWise Principles demonstrates that, for most members, activities supporting management and assessment of climate risk are well established.

At the individual member level, the compliance ranking table (Appendix C in the full Review report) shows there have been a number of key movements in the year. We have seen both considerable advances and falls in the ranking among the membership. The quality of reporting and activity for four members has seen their ranking advance by over 8 places in the table. However, those that fell back struggled to show year-on-year progression or were overtaken as others improved.

For the first time this year we have included an 'Integration Analysis' as a measure of how well members are linking climate change and corporate strategy. A summary of the methodology is on page 31. The analysis concluded that a little over three quarters of members score either gold or silver (having achieved a total score of 80% or above). Only two members scored below 50% demonstrating that the majority of members are making progress in linking climate risk to strategic statements and providing evidence of activity in key functions of the organisation. However, only 27% of members were able to demonstrate a fully integrated approach to climate risk. These members were awarded gold status in the integration analysis.

This year has seen a change to the scoring methodology which now sees an overall compliance score awarded which also includes an element for disclosure. This change is designed to simplify the scoring and reporting process. Further details of these changes are included in Appendix A in the full Review report.

A summary and detailed review of compliance and reporting against the ClimateWise Principles are contained the full Review report along with case studies identified in the course of the analysis and recommendations and conclusions from the independent reviewer.

The Independent Reviewer's Main Conclusions

It is encouraging to see ClimateWise members maintain the high levels of compliance with the principles in the face of unprecedented economic and operational turmoil in the sector. However, as observed last year, we continue to see a wide spectrum in both the approach to reporting against the principles and in the depth and quality of activity to achieve compliance. In this period in particular, we have observed that a large proportion of members have struggled to demonstrate year on year progress. This is most relevant in relation to Principles 2 – 'Inform public policy-making' and 5 – 'Reduce the environmental impact of their own business'. The former is a reflection of the fallout from a disappointing outcome at the Conference of the Parties (COP) 15 in Copenhagen and the difficulty in engaging leadership in the business regarding COP 16 in Cancun. As a result, a significant number of responses to this principle were identical to those received for the Third Review period.

One area of the principles which has seen the highest increase in compliance is sub-principle 4.3 – 'Encourage improvements in the energy-efficiency and climate resilience of our investment property portfolio' which has seen an 18% rise. This increase appears to have been driven through better reporting and disclosure of efforts in this area, aligned with a couple of leading practice examples which are highlighted in the report. Previous reviews have highlighted the relative low performance of this sub-principle.

In relation to principle 5, compliance dipped from record levels in last year's review again as a result of a lack of year on year progress in employee engagement activity, evidenced by identical responses in a significant number of member reports. The driver for this is not clear; it may be that budgetary constraints have prevented new activity, or that members are struggling for new approaches to engaging employees on the issues. Either way, we see this as a key issue to be addressed and one in which ClimateWise may be able to support through its collaborative group activity.

Our new integration analysis has highlighted that seven members, a little over a quarter (27%) of the membership, can clearly demonstrate a fully integrated approach to climate risk across core business operations. These 'gold' ranked members consistently provided a strong external strategic statement relating to climate change, articulated how the issues affect core functions and how the organisation is addressing the issues in those functions. Those that achieved the gold ranking also supported the strategic commitments with full or near full compliance across all the relevant sub-principles, thus evidencing that the member's strategic statement was supported by action in the core functions.

However, we continue to see a lack of explicit evidence or specific reporting that strategic linkages are being made across the principles among the majority of the membership. As suggested in the last review, those that are able to demonstrate that activity in one principle is informing and supporting activity in another are able to articulate strong evidence that climate risk is an integrated, embedded part of core activity. This is particularly true for research informing product development and/or investing activity. Similarly, we see a good level of disclosure relating to governance structures and high level board responsibility for managing climate risk. However, what we see much less of is evidence that the executive oversight is leading directly to climate risk being incorporated into core business strategy and planning. We therefore feel there is more that members could do in their ClimateWise reporting to be more explicit about the cross-principle linkages the business is making and the direct impact climate risk and opportunity is having on core functions.

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The ClimateWise Principles

Principle 1: Lead in risk analysis

1.1 Support and undertake research on climate change to inform our business strategies and help to protect our customers' and other stakeholders' interests.
1.2 Support more accurate national and regional forecasting of future weather and catastrophe patterns affected by changes in the earth's climate.
1.3 Use research and improve data quality to inform levels of pricing, capital and reserves to match changing risks.
1.4 Evaluate the risks associated with new technologies for tackling climate change so that new insurance products can be considered in parallel with technological developments.
1.5 Share our research with scientists, society, business, governments and NGOs through an appropriate forum.

Principle 2: Inform Public Policy Making

2.1 Work with policy makers nationally and internationally to help them develop and maintain an economy that is resilient to climate risk.
2.2 Promote and actively engage in public debate on climate change and the need for action.
2.3 Support work to set and achieve national and global emissions reduction targets.
2.4 Support Government action, including regulation, that will enhance the resilience and reduce the environmental impact of infrastructure and communities.
2.5 Work effectively with emergency services and others in the event of a major climate-related disaster.

Principle 3: Support climate awareness amongst customers

3.1 Inform our customers of climate risk and provide support and tools so that they can assess their own levels of risk.
3.2 Encourage our customers to adapt to climate change and reduce their greenhouse gas emissions through insurance products and services.
3.3 Increase the proportion of repairs that are carried out in a sustainable way through dialogue with suppliers and developers and manage waste material appropriately.
3.4 Consider how we can use our expertise to assist the developing world to understand and respond to climate change.

Principle 4: Incorporate climate change into our investment decisions

4.1 Consider the implications of climate change for company performance and shareholder value, and incorporate the information into our investment decision making.
4.2 Encourage appropriate disclosure on climate change from the companies in which we invest.
4.3 Encourage improvements in the energy-efficiency and climate resilience of our investment property portfolio.
4.4 Communicate our investment beliefs and strategy on climate change to our customers and shareholders.
4.5 Share our assessment of the impacts of climate change with our pension fund trustees.

Principle 5: Reduce the environmental impact of our business

5.1 Encourage our suppliers to improve the sustainability of their products and services.
5.2 Measure and seek to reduce the environmental impact of the internal operations and physical assets under our control.
5.3 Disclose our direct emissions of greenhouse gases using a globally recognised standard.
5.4 Engage our employees on our commitment to address climate change, helping them to play their role in meeting this commitment in the workplace and encouraging them to make climate-informed choices outside work.

Principle 6: Report and be accountable

6.1 Recognise at company board level that climate risk has significant social and economic impacts and incorporate it into our business strategy and planning.
6.2 Publish a statement as part of our annual reporting detailing the actions that have been taken on these principles.

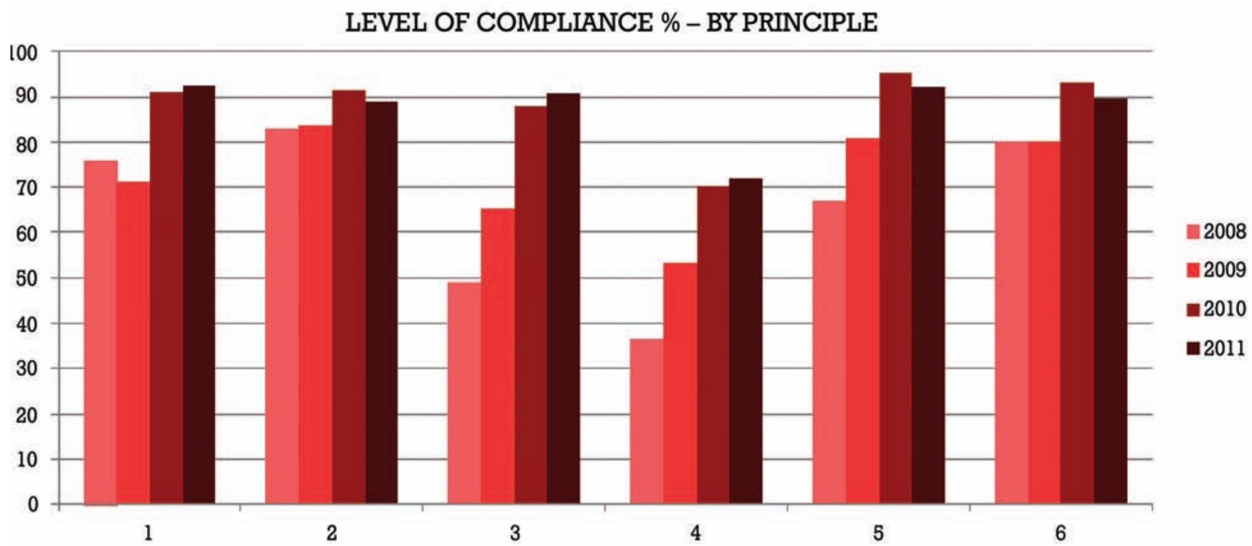
Summary of Findings

This independent review is focused on determining the level of compliance against the six ClimateWise Principles. The overall finding of the analysis of the 26 member reports shows that the level of compliance has remained at the high level achieved last year and stands at 88% across the principles. Four of the principles now have a compliance score of 90% or more.

The findings highlight that over 70% of all member responses to sub-principles achieve full compliance and disclosure, whereas fewer than 5% achieve a zero score. Both of these trends show an improvement over the previous year and although overall compliance has marginally reduced in three principles (2, 5 and 6), members continue to demonstrate a strong commitment to reducing climate risk, through climate change adaptation as well contributing to risk mitigation through their work reducing carbon emissions.

The scoring has changed this year in order to simplify the way in which disclosure and compliance are measured. This has resulted in slightly lower scores overall for previous years due to the fact that disclosure now forms part of the compliance score. Crucially this has not altered the overall movement of progression against the principles that the membership has shown year on year.

Figure 1: Principle by principle comparison at group level (2008-2011), % Level of compliance.



Activities to comply with **Principle 1 – 'Lead in risk analysis'** should play to the core strength of insurers. It is critical to the development of a climate resilient and adequately adapted lower carbon economy that the insurance sector is able to accurately assess and price the risks associated with climate change, incorporate this insight into other core activities (such as asset management) and share the research with others. It is therefore encouraging that ClimateWise members' overall compliance across principle 1 has now reached 93%. This is a slight increase on the previous years' already high level (91%). Compliance with sub-principle 1.3 'Use research and improve data quality to inform levels of pricing, capital and reserves to match changing risks', identified last year as critical to the integration of climate risk into core processes, was an area that saw continued increase in compliance. At 96% compliance it is at its highest level ever, building on progress made since the 2009 review.

For the fourth year running principle 1.4 'Evaluate the risks associated with new technologies for tackling climate change so that new insurance products can be considered in parallel with technological developments' proved to be the area which members continue to find challenging. However, this does not mean there have been no developments; in fact some members are actively targeting this area and have developed new products and services as low carbon technology and understanding of the associated risks matures. This is in addition to some of the more established policies for household cover for wind turbines and solar panels.

Principle 2 – 'Inform public policy making' again proves to be an area where members perform well with a compliance score of 89%. Although the overall score is slightly lower than the previous year it is not due to any particular factor; seven members improved their score and seven members saw their score decrease. Members continue to highlight a number of public policy interventions across the sector and provide examples of engagement with government agencies, civil society and international bodies to help inform and shape public policy. A number of members reported their support to the discussions around the future of the ABI's Statement of Principles for the provision of flood insurance, a key area for the insurance industry in the UK. Sub-principle 2.5 ('Work effectively with emergency services and others in the event of a major climate-related disaster') saw a significant rise in the level of compliance as members advance their reporting of activity in preparation and planning procedures for climate-related disaster events.

The improvement in compliance has again been maintained in **Principle 3 – 'Support climate awareness amongst our customers'**. The level of compliance has now reached 91% up from 88% last year. This is the strongest uplift across all the principles this year, as it was in 2010 and a clear area of focus. Members demonstrate a commitment to supporting awareness among customers by informing them of climate risks and providing support and tools so that they can assess their own level of risk. A variety of methods are being used to communicate with customers, with the use of online social media identified as an effective tool. In relation to sub-principle 3.3 ('Increase the proportion of repairs that are carried out in a sustainable way through dialogue with suppliers and developers and manage waste material appropriately') the majority of members made reference to their involvement in the ClimateWise Collaboration on Built Environment looking at how insurers reduce the environmental impact of the claims process so as to contribute cost-effectively to mitigating risk.

Principle 4 – 'Incorporate climate change into our investment decisions' remains the area of relative underperformance for the membership but overall compliance across the sub-principles this year has risen to 72% from 70% last year. This headline figure hides a number of swings in performance across the sub-principles, namely 4.1 and 4.3. Firstly, sub-principle 4.1 ('Consider the implications of climate change for company performance and shareholder value, and incorporate the information into our investment decision making') has seen a reduction in compliance of approximately 14%. There are differing approaches among the membership, with a large number of members committing to considering environmental, social and governance (ESG) factors alongside mainstream company analysis and using analysis to inform investment portfolio construction and investee company engagement. On the other hand there are members with investment strategies that do not include climate risk considerations as they are not deemed to be a significant driver of financial value. The second area to show significant movement was sub-principle 4.3 'Encourage improvements in the energy-efficiency and climate resilience of our investment property portfolio' which has seen compliance increase by 18%. The main driver was evidence of greater efforts to understand and act upon the energy efficiency of property portfolios; this is positive progress and to be expected as energy reduction relates directly to cost and value.

Compliance with **Principle 5 – 'Reduce the environmental impact of our business'** continued to be very strong, at over 92%. However, compliance levels are slightly down on the previous year (95%) as members have struggled to demonstrate year-on-year progression, particularly in relation to sub-principles 5.1 (engaging with suppliers) and 5.4 (engaging with employees). For many members policies and procedures to reduce the direct environmental impacts of their businesses are well established as part of their sustainability strategies. Understanding the environmental impact of the whole value-chain is particularly pertinent for general insurers as they seek to understand and reduce the environmental impact of the claims process. Last year we saw one member working to understand the carbon footprint of their entire supply chain (both direct and indirect). In the current year we have seen further progress in the calculation of the carbon footprint for the complete value-chain of a product. This has resulted in a product specific carbon reduction target.

Compliance across **Principle 6 – 'Report and be accountable'** remains high, at 90%. Members take reporting and accountability seriously which is highlighted by the number of members who reported that responsibility for managing climate risk and sustainability strategies has reached the highest levels of their organisation. In relation to reporting progress a small proportion of members produce a well structured, separate report specifically outlining efforts to address the ClimateWise Principles and publish this document on public websites. Others refer to ClimateWise membership within Corporate Responsibility (CR) reports and on CR websites and also guide the reviewer to these reports to demonstrate compliance with sub-principle 6.2 ('Publish a statement as part of our annual reporting detailing the actions that have been taken on these principles').

Summary of Recommendations

Principle 1 ('Lead in risk analysis') achieved the highest level of compliance across the ClimateWise Principles and improved slightly on the previous year. While activity to support the accurate pricing of risk is critical and must continue, we have seen a small number of members report research activities outside of underwriting. For example, research programmes to understanding consumer attitudes and needs relating to climate risk and adaptation have been cited this year. It is recommended that this type of wider market research and analysis must continue if the sectors' response is to be effective. We would also continue to encourage members to better demonstrate how their research is informing wider business strategies and explicitly articulate how their research is being integrated across all Principles.

Compliance across **Principle 2 ('Inform public policy making')** remains high as members continue to engage in debate with policy makers. Members have increased dialogue on the issue of adaptation to climate risk, reporting their involvement in a number of different studies. Although it is recognised that many of these studies are longer term in nature, it remains important for members to cite the relevant adaptation activities they have been involved with during the reporting period. It is challenging to assess compliance for members who continue to use examples from prior years where no new activities have been undertaken.

Members who continued to have difficulties providing relevant examples in relation to sub-principle 2.5 ('Work effectively with emergency services and others in the event of a major climate-related disaster') should also be looking to take actions in relation to planning for climate-related disasters. There is evidence of leading practice in planning for such events among the members but it is not universal and more work can be done in this area.

With reference to **Principle 3 ('Support climate awareness amongst our customers')**, there continues to be some significant barriers preventing the attractiveness and uptake of lower carbon solutions and resilient repairs by consumers. These barriers could be addressed by members looking at the lifecycle rather than upfront cost and providing innovative financing options that recognise initial higher capital costs are often offset with much reduced operating expenses. More importantly this highlights the real need for members to seek further insight from their research activities to help identify the barriers and address these with the development of products and services relating to reducing their environmental impact. There is an onus on the sector to lead the consumer on this journey, through education and communication. Members need to develop solutions that effectively communicate climate-related risks and reward mitigation and adaptation. These need to be made accessible and acceptable for the mainstream consumer.

Principle 4 ('Incorporate climate change into our investment decisions') remains a challenging aspect of the ClimateWise Principles and therefore some of the recommendations outlined in previous years remain valid. Although there have been some very good examples of members who are establishing integrated strategies in relation to climate risk and investments, there remains a significant number of members who have not started these conversations. The sector as a whole is not realising the potential it has to influence change. Investment teams need to be more actively engaged in climate risk and understand how this can be linked to the company's overall business strategy. Dialogue between responsible investment teams and core investment teams is happening in some companies but this remains an area for improvement. There is a widening distance between those members who are engaged on this issue and those who are not.

Those members who did not score well in relation to sub-principle 4.2 ('Encourage appropriate disclosure on climate change from the companies in which we invest') should be looking to develop a more proactive approach to encouraging investee companies to adopt better disclosure and reporting practices. Leading practice in this area is being achieved by a select few who are actively engaging and influencing investee companies on a number of levels to ensure they demonstrate transparency and a commitment to behavioural change in the long-term. There is an incentive for investors, the 2011 Carbon Disclosure Project Report(4) concluded; 'Companies in the Carbon Disclosure Leadership Index and Carbon Performance Leadership Index delivered approximately double the total return of the Global 500 companies between January 2005 and May 2011. This suggests a strong correlation* between good climate change disclosure and performance, and higher financial performance.'

(*correlation: statistical correlation, based on daily returns, between 2011 CDLI and the Global 500 is 0.5, and between the 2011 CPLI and Global 500 is 0.6 (from 1 January to 31 May 2011). It is likely that other factors will influence the relationship between financial performance and high carbon disclosure and performance scores. These could include the capability of the management or the company's broader approach to identifying and capitalising on opportunities or managing risks)

Communication of investment strategies to shareholders and customers is an area which could see further improvement. This and the dissemination of climate change knowledge to pension fund trustees rely too much on passive, indirect methods of communication. These are the worst performing sub-principles and members do not appear to be addressing them in a strategic manner. Members have a wealth of knowledge and experience in relation to the impacts of climate change which could provide great benefits to pension fund trustees so that they can consider these issues when making investment decisions.

Members have performed well in **Principle 5 ('Reduce the environmental impact of our business')** and have demonstrated good progress against recommendations made in previous years. In the future, the challenge for members is to maintain momentum and further develop the sophistication of activities in this area, particularly focusing on aligning activities to support core business strategies.

In particular, it is important that members develop a more sophisticated understanding of the indirect impacts of their operations. Understanding the environmental impact of supply chains is a first step in this process and is something that few members are currently doing. Once members have this information it will be possible for them to develop more sophisticated and more targeted reduction plans, for example, by understanding the carbon footprint of specific products and claims value chains. Experience from other sectors would suggest that significant cost savings are achievable through carbon reduction in supply chains. This is another area where the power and scale of the sector is not being brought to bear in a strategic manner.

There is also the opportunity for members to drive innovation through engaging with employees on how climate change presents both risks and opportunities for core business functions. To date employee engagement has mostly been focused on raising awareness of the issue and encouraging employees to reduce their direct impact. There is a risk that saturation point is approaching and employees will become disengaged with the issue. Members can maintain momentum and help drive business performance by helping employees to understand how climate change issues may influence business strategy, and what role they can play in its design and implementation.

Principle 6 ('Report and be accountable') achieved a high level of compliance and members have been able to clearly articulate the type of climate change responsibility assumed at board level and the concrete actions taken over the course of the year. An additional step towards leading practice would be for members to describe the impact these actions are having within the Principles to further demonstrate senior level involvement in strategic decisions.

Members' ClimateWise submissions vary widely in size, format and style and approach to public reporting is also varied. We would encourage the ClimateWise Managing Committee and members to agree a standard format for reporting and encourage greater public disclosure specifically in response to ClimateWise Principles. This would improve comparability and assessment. In addition, members should assess whether examples from prior years are relevant to demonstrating continued progress against the principles and be more transparent in communicating those areas where no activity has been undertaken in the current year.

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