

Press release

Paris, 6 July 2023

The ACPR launched its second climate stress test covering the insurance sector today

The Autorité de contrôle prudentiel et de résolution (ACPR) publishes the assumptions and expectations of its new climate stress test exercise, exclusively dedicated to insurers. The ACPR expects major market mobilization for this stress test, which remains voluntary. It follows a pilot exercise conducted in 2020 in which 15 insurance groups participated, representing approximately 75% of insurers' total balance sheet.

"Stress tests have become essential tools for financial institutions to measure the impacts of climate change on their business model, their capacity to absorb shocks and thus refine their climate risk management strategy, particularly in view of the development of their transition plans. We are following a supportive approach, as this exercise will have no impact on the capital requirements of participating undertakings," said Nathalie Aufauvre, Secretary General of the ACPR.

This second exercise in the climate stress test proposes methodological changes resulting from discussions with insurers in 2022. A short-term horizon (2027) is added to the **long-term horizon (2050) to explore scenarios that combine physical and transition risks in a consistent manner. The impact of these risks is measured on the assets, liabilities, balance sheet balance and, for the short-term scenario, solvency.**

The results **will be the subject of a public report published in 2024 presenting the market-wide impacts** of the scenarios, and will continue to foster exchanges with undertakings thereafter.

"The methodological changes are designed to strengthen the strategic, methodological and prudential dimensions of the previous exercise in order to adapt it to increasingly difficult climate conditions, recent methodological developments and the specific challenges faced by insurance institutions, especially relating to their strategic planning," explains Laurent Clerc, director of research and risk analysis at the ACPR.

- From a strategic point of view, the exercise aims to strengthen insurance institutions' ability to anticipate the consequences of climate change and the ecological transition for their business, in both the short-medium and long term, and to adapt their strategies accordingly.
- From a methodological point of view, the exercise should improve the analytical tools available to insurance companies and the supervisor. The assumptions provided are based on more granular data, allowing for a better sectoral and geographical differentiation of risks. The scope of the risks considered is also broader (e.g.: consideration of the macroeconomic and financial consequences of chronic physical risk). This work is being done in collaboration with insurance institutions, the Caisse Centrale de Réassurance (CCR) and AON for the modeling of the physical risks on the liabilities side, as well as with expert economists of the Banque de France for the modeling of transition and physical risks on the assets side.

- Finally, the exercise aims to explore new dimensions of risk assessment: thus, the short-term scenario will make it possible to analyze the impact of extreme but plausible hypotheses - which may be in the blind spot of risk analysis - on the loss ratio, earnings and solvency of undertakings. The long-term scenario will include a quantitative and qualitative analysis of uninsurability risk and the prevention of the consequences of climate change.

The climate change and climate loss ratio scenarios take into account the most recent projections by the IPCC and the NGFS, the network of supervisors and central banks for the greening of the financial system.

The **short-term scenario** is one of the innovations of this exercise. It theorizes that exceptional climate loss ratio will result (a combination of droughts identical to those observed in France in 2022, followed by floods leading to dam bursts, such as the events observed in Germany in 2021, or to landslides, such as those observed in Italy in May 2023), which will cause financial markets to adjust abruptly, owing to the anticipation of transition policies that are now considered inevitable.

Two long-term scenarios, based on NGFS research, describe the economic and financial impacts of transition trajectories, one orderly and the other delayed, aimed at reducing the temperature to below 2°C by 2050. The economic impacts affect insurers' balance sheets and are combined with an increase in physical risk, which materializes through natural disaster events (droughts, floods, marine submergence and cyclone), health risks, and macroeconomic and sectoral impacts. **The ACPR preferred scenarios that were comparable in terms of their point of arrival at the target temperature and hence their physical risk level, but that differed in terms of the timing of the transition, making it possible to measure the cost of inaction.**

This exercise will be followed by a new European climate exercise, with the European Commission mandated by the three European supervisory agencies to conduct a stress test in 2024 assessing the medium-term resilience of the financial sector linked to the transition risk implied by the fit-for-55 package.

Provisional timetable:



About the ACPR

The Autorité de contrôle prudentiel et de résolution (ACPR) is the administrative authority operationally attached to the Banque de France that supervises the banking and insurance sectors and ensures financial stability. The ACPR is also responsible for protecting the customers of the supervised institutions and ensuring the fight against money laundering and the financing of terrorism. It also has resolution powers. The ACPR's operational departments come under its General Secretariat.

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