



Climate & Carbon Investment



Today the earth is as warm, if not warmer, than at any time during the last 600 years. The scientific link between global warming and industrial emissions of the six 'greenhouse gases' (carbon dioxide and methane are the main contributors) is beyond dispute, with major short-term implications for forestry and other crops.

The immediate impact of global warming will include increases in the incidence of heavy rainstorms, severe droughts and severe water management problems. Species extinction will occur at more than fifty times the natural rate, tens of millions of people will be displaced, and the consequent limited resources may result in conflicts. The effects of accumulated past emissions will persist for centuries and create negative feedback loops of cause and effect. Climate patterns will become more complicated, and therefore deeply unpredictable.

The 1997 Kyoto Protocol

The Protocol represents a significant step by the international community to address the problems caused by global climate change. Industrialized countries have agreed in principle to binding limits of total greenhouse gas emissions. Although the ratification of the Kyoto Protocol remains in doubt, many governments and corporations worldwide recognize the need to modify emissions to at least Kyoto targets, for strategic and competitive advantage.

The Protocol provides for:

- A first accounting and compliance period for emission reductions between 2008 and 2012
- Minimum reduction targets set at 5% below 1990 emission levels (for many countries this means a 25% or greater reduction on 2008 emissions)
- A system for trading the assigned amount units of emissions, emission reduction units and certified emission reductions as a means of achieving the emission reduction commitments.

The Corporate Response and Carbon Investments

The global energy corporations are already taking positive action to reduce their greenhouse gas emissions by investing in cleaner technology, more energy-efficient design and alternative fuel types. These initiatives require significant investment and long-term strategic planning. In the short-term, prior to 2012, companies are



hedging their risk of non-compliance by trading carbon. The trading unit is one tonne of carbon dioxide equivalent. Current technological solutions to cleaner industrial emissions are expensive, with typical costs of several hundred dollars per tonne of reduced carbon emissions.

Carbon is already a traded commodity, and will soon be traded on major exchanges including those in Australia, the U.K. and the U.S. Trading of carbon credits is a new sector of financial risk and reward which requires security of supply, and precise quality control.

Eligible forestry projects may generate tradable carbon credits for a few dollars per tonne. Climatic change (carbon) projects are investments made solely for the purpose of reducing greenhouse gas emissions or atmospheric concentrations. Forestry may for the first time have an opportunity to be a natural partner for all sectors of industry that wish to hedge their risk of non-compliance. Power companies, motor manufacturers, oil companies, and other energy-intensive corporations are considering investing, directly or via carbon funds, in eligible forestry activities.

We expect considerable more investment into forestry which will lead to a increased demand of conventional forestry coverage against fire and windstorm in the agriculture reinsurance market.

With regulations getting tighter emission compliance will increasingly expose managers of sensitive industries and hence create demand for additional D&O coverage for the respective reinsurance classes.