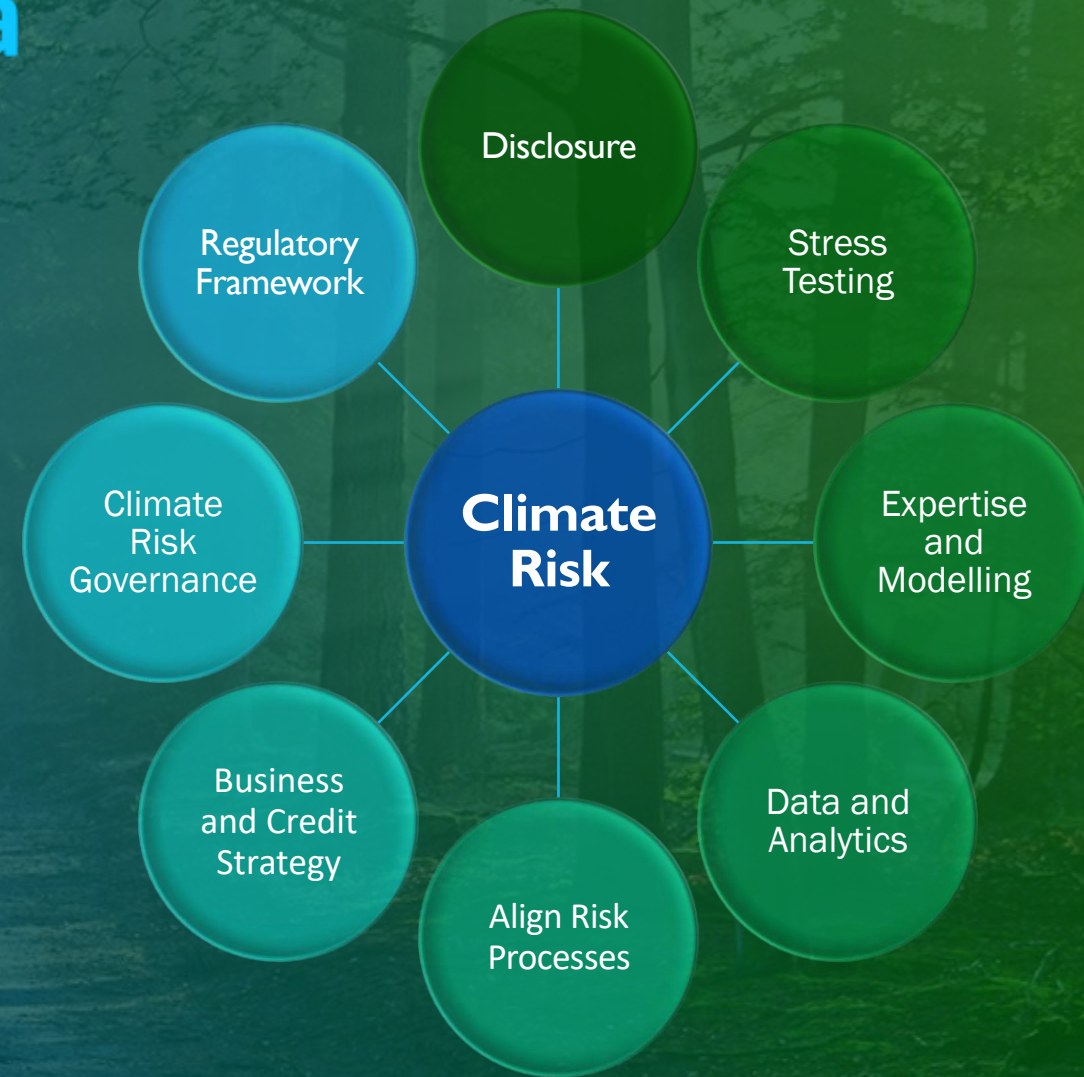


Global Credit Data

by banks for banks

Climate and Credit Risk Measurement Come together!

Join the
Focus
Group





In the next hour:

- AFME - Climate Risk Stress Testing
- Q & A
- Introduction: GCD Climate Risk Focus Group
- Closing Remarks



Constance Usherwood
Managing Director
Prudential policy
AFME



presentation on Climate Risk Stress Testing

...The way forward

Industry Collaboration on Credit & Climate

Data quality
and standards

Limited data
for certain
regions and
sectors

Need for
Data Collaboration
&
Benchmarking

What are my peers doing?

Why GCD?

DATA SHARING

With your
direct peers

SECURITY

ISO 9001
ISO 27001

BEST
PRACTICE
Credit Modelling

COMPLIANCE

With regulatory
requirements
(BCBS239)

49

MEMBER
BANKS

20+

YEARS OF
HISTORY

4

DATA
PLATFORMS

Why GCD?

Surveys &
Analytics

Granular

Low
Default
Portfolios

Industry Standard
data template

LGD/EAD

Secure &
Anonymized

PD

4

Asset Classes –
Corporates, Real Estate,
Banks & Fis, Aircraft,
Shipping, Sovereigns, PB,
etc

DATA
PLATFORMS

Benchmarking

Collateral

Obligor
Name, LEI

Sector (NACE,
GIC, NAICS...)

Location

Why GCD?

DATA SHARING

With your
direct peers

SECURITY

ISO 9001
ISO 27001

BEST PRACTICE

Credit Modelling

COMPLIANCE

With regulatory
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(BCBS239)

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MEMBER
BANKS
Global Credit Data
by banks for banks

20+

YEARS OF
HISTORY

4

DATA
PLATFORMS

- Established collector of hard-to-get credit risk experience directly from banks' books
- **Banks** are in the driver seat
- Strong record of data standards and methodology best practice
- Facilitate knowledge exchange
- The platform for credit risk measurement and management



GCD's objective

to contribute to a better understanding of credit risk, to promote **quality, standardization** and **transparency** of data and measurement to improve the ability of the Members to actively **manage** the **credit risk** of their portfolios





Credit & Climate → GCD Climate Focus Group

Key Value

Address **climate** related **credit** risks faced by banks.

Key Focus Areas

Collaborative
credit - climate
community

Climate stress
testing best
practices

ESG/Climate
scoring standards

Environmental
credit risk
modeling

Banks' climate data
benchmarking

Climate credit
reporting
practices

Climate drivers
benchmarking for
credit

Member Regional Focus

US

Canada

Europe

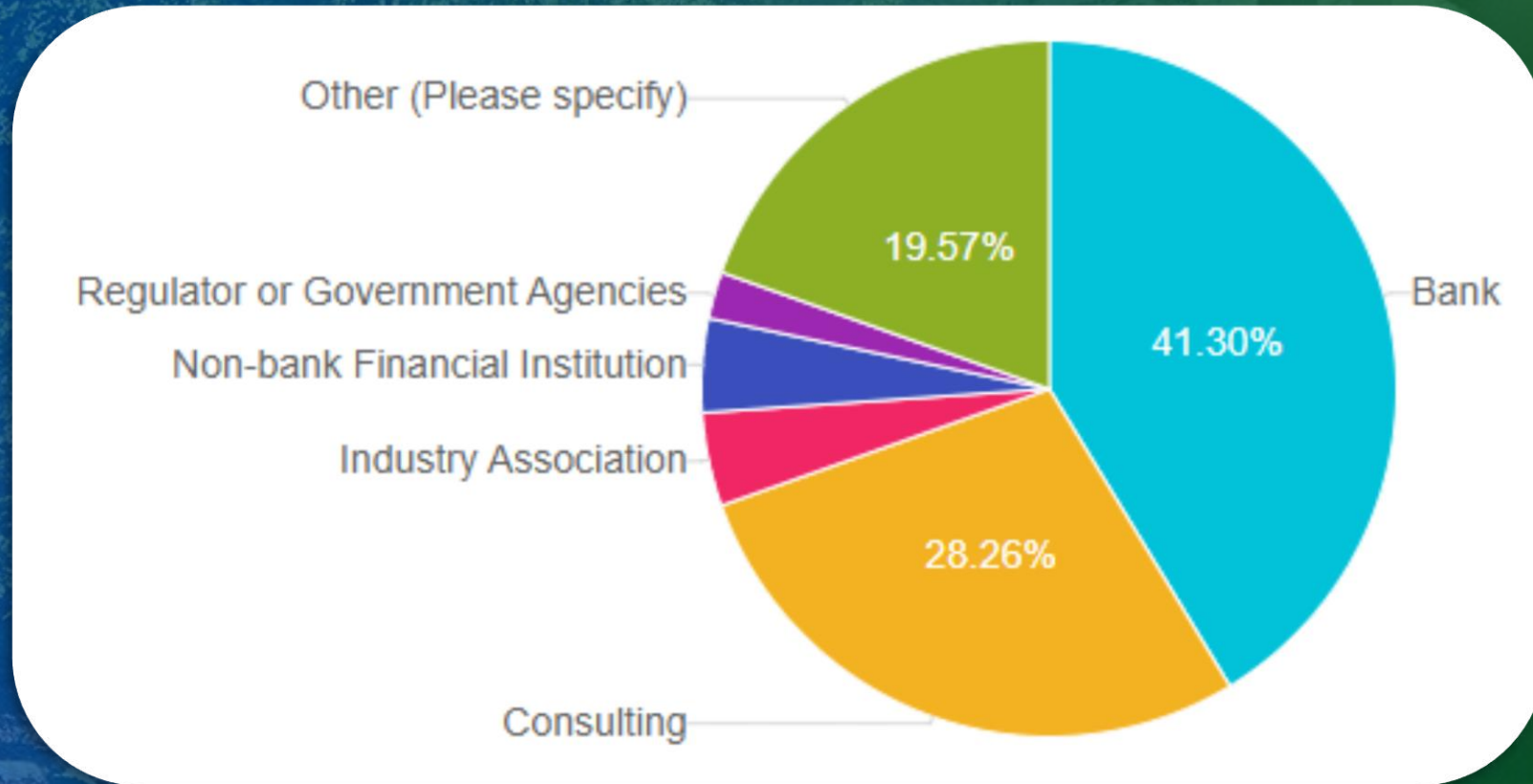
South Africa

Australia and
New Zealand

..and more

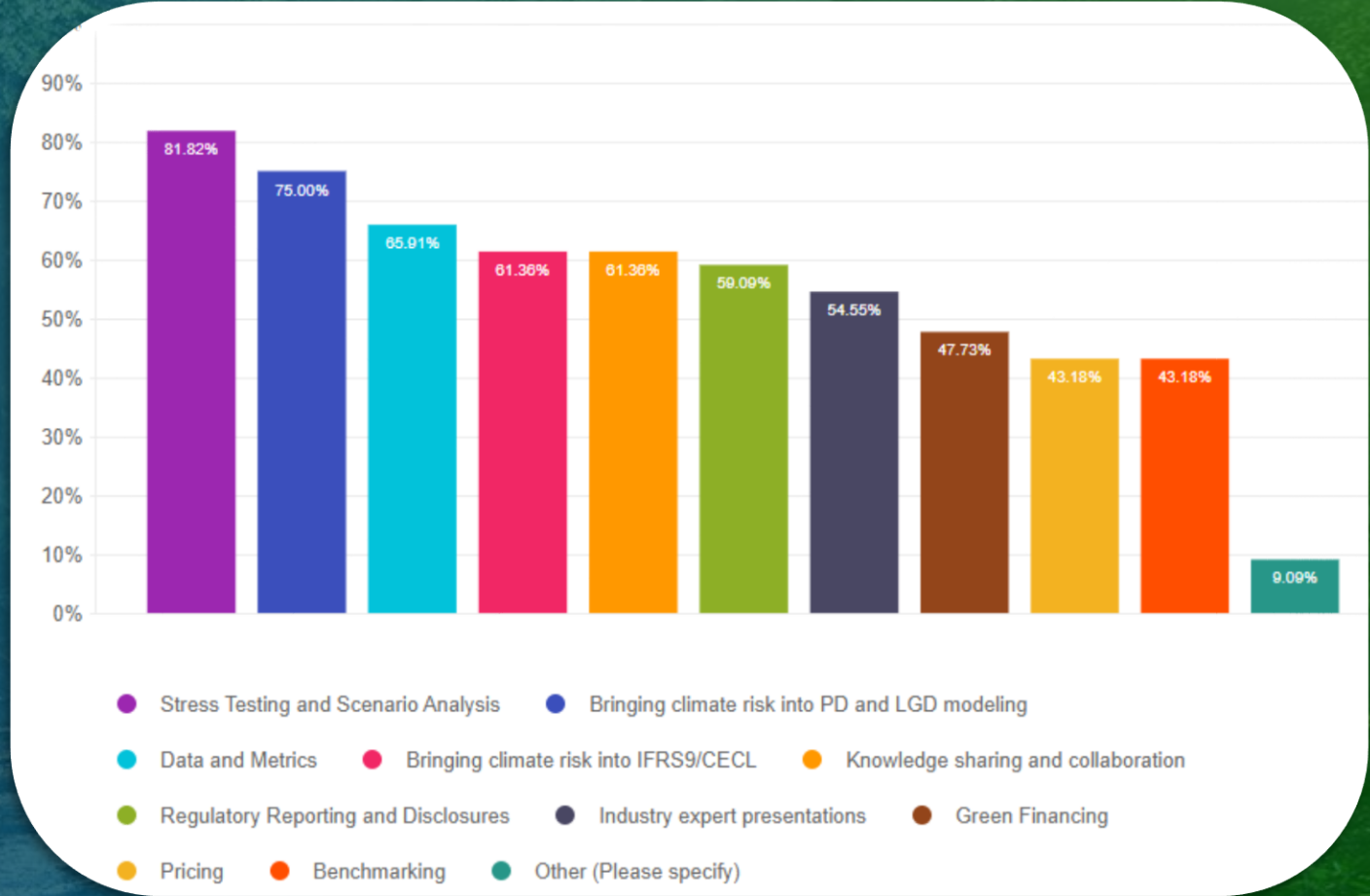
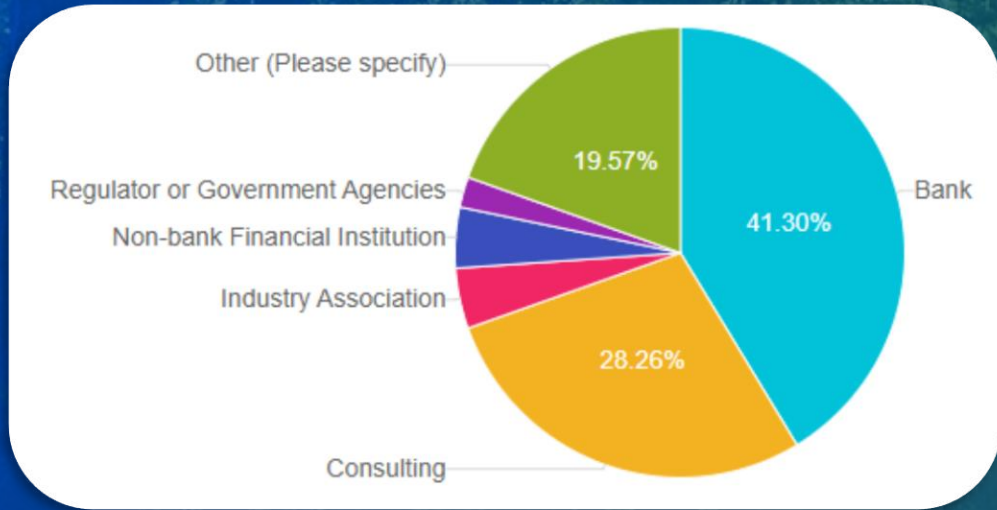


Industry Collaboration!





So many hot topics!



 Climate Stress Testing

 Integration climate risk into LGD and PD models

..and so much more

Global Credit Data

by banks for banks

Get Involved!

Join the
Focus
Group



A Common Path to Improve European Climate Risk Stress Testing and Scenarios Analysis

June 2023



Association for Financial Markets in Europe
www.afme.eu



Contents

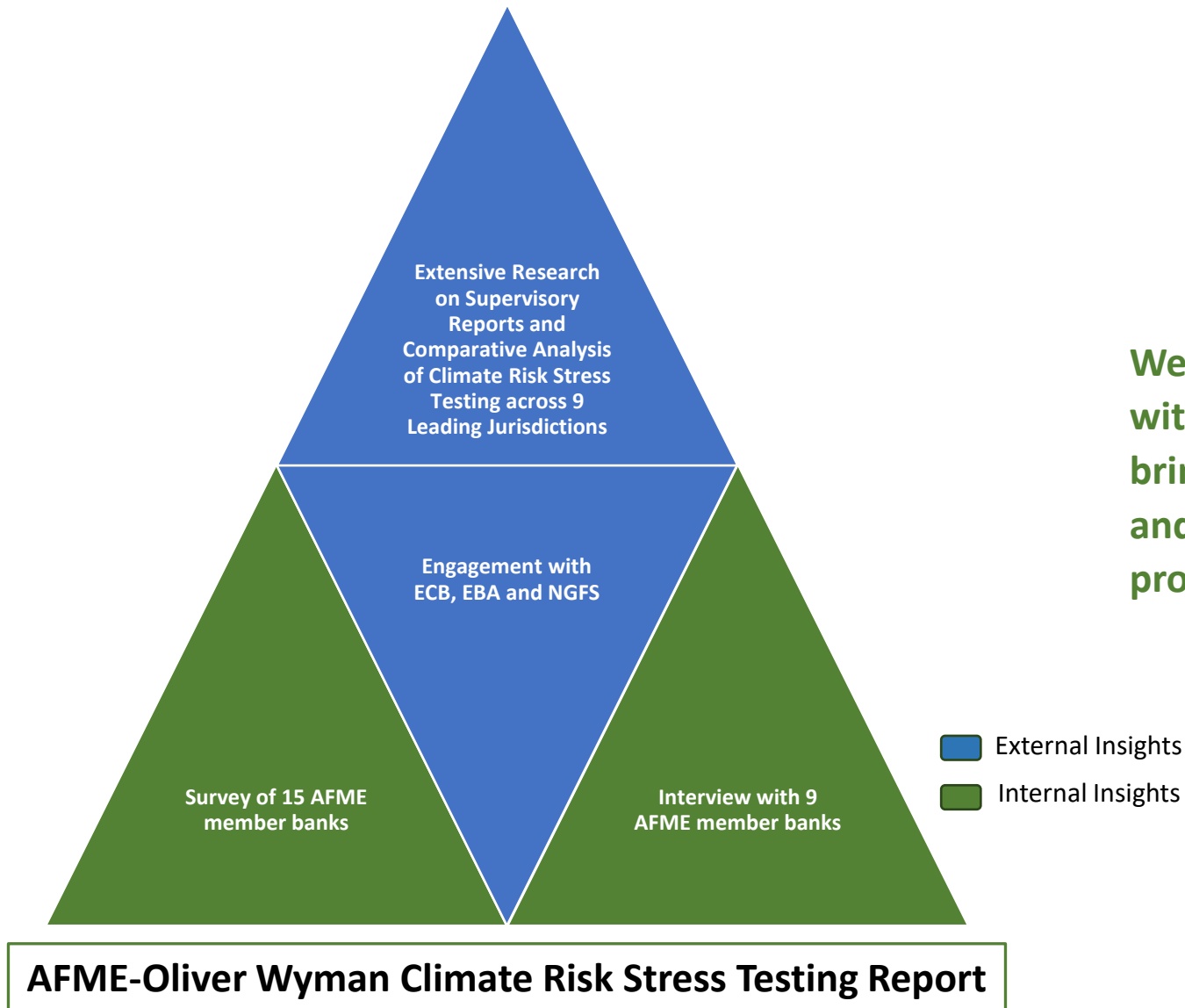
- 1 Purpose of the Report
- 2 Approach to the Design of the Report
- 3 Key Findings – General Overview & Credit Risk
- 4 Next Steps: Considerations in Supervisory Development
- 5 Annex: Recommendations – Credit Risk

Purpose of the Report (1/2)

- ❖ **We aim to take stock of the work banks have already undertaken to drive best practice and bridge efforts of banks and policymakers to improve climate risk stress testing methodology and data.**
- ❖ **[Our report](#) highlights the industry's commitment to work together to build on the ECB effort and drive EU and international initiatives underway.**

Approach to the Design of the Report

Our report builds upon industry learnings from the 2022 ECB climate stress test.



We have collaborated with *Oliver Wyman* to bring additional resource and insight to this project.

Key Findings - Overview



Scope:

87% of banks believe that it is relevant to define materiality thresholds based on exposure and climate “riskiness” to understand the most impacted portfolios in future exercises.



Scenarios:

Most respondents (**67%**) see the lack of short-term scenarios as the biggest challenge and **53%** of banks intend to integrate nature and related risks into scenarios in the next two years.



Data:

Most respondents rely on external data providers for climate (**100%**) and physical risk data (**87%**).



Risk Types:

While most respondents support improving the approaches to credit (**100%**) and market risk (**67%**), there is a growing appetite among banks surveyed (**up to 20%**) to explore the impact of climate risks on other financial risk types such as reputational and funding risks

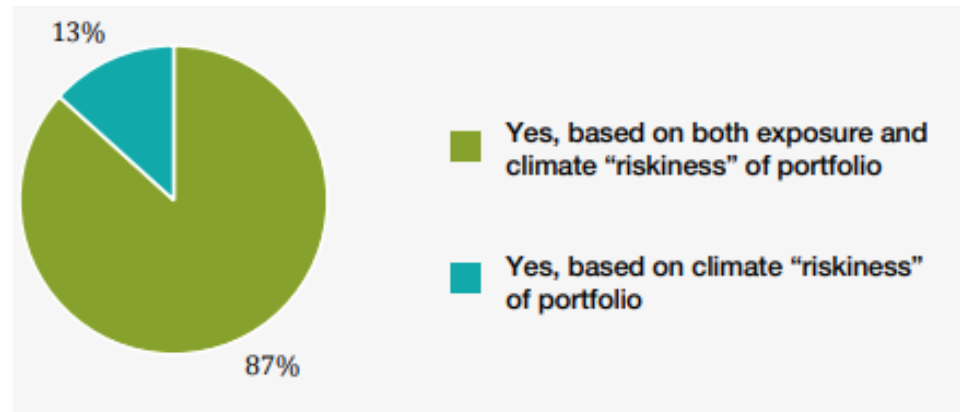


Time Horizons:

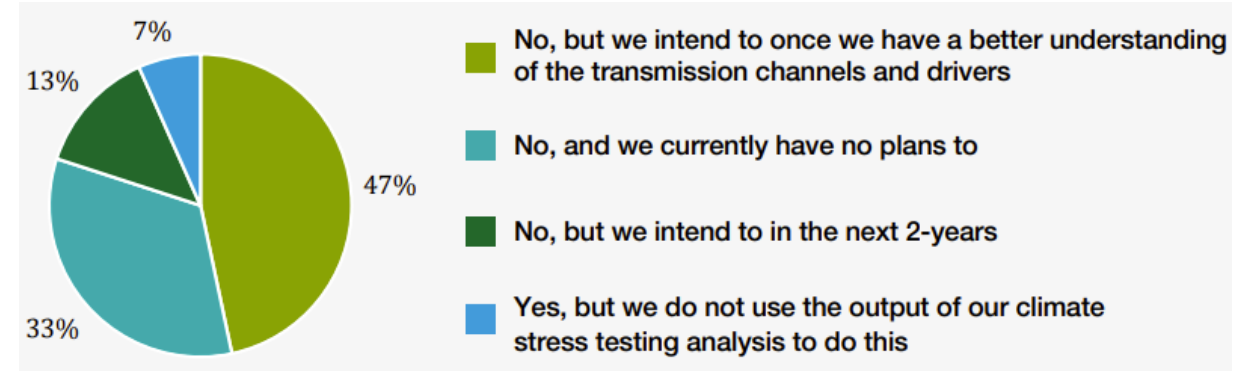
67% of banks would welcome more focus on shorter time horizons (i.e. 3-5 years) in future stress tests.

Key Findings (Credit Risk) – Data Visualisation (1/3)

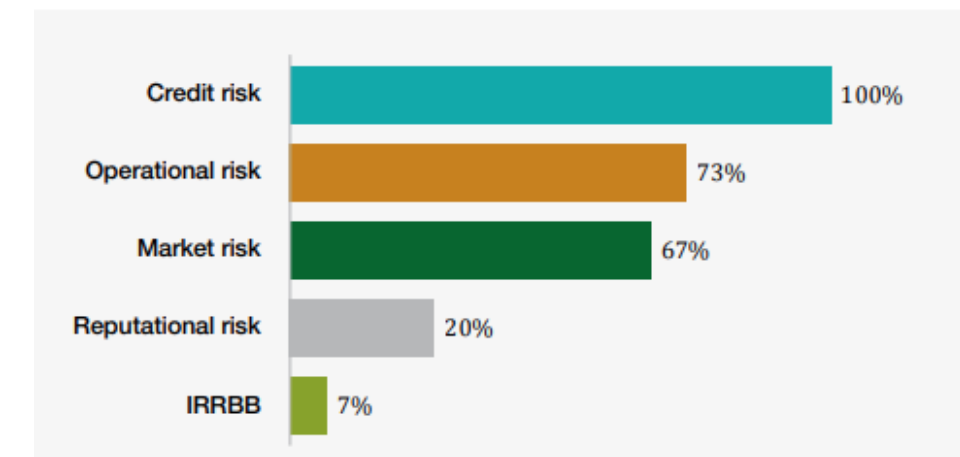
i Would it be helpful to introduce materiality thresholds to focus on relevant portfolios for credit risk?



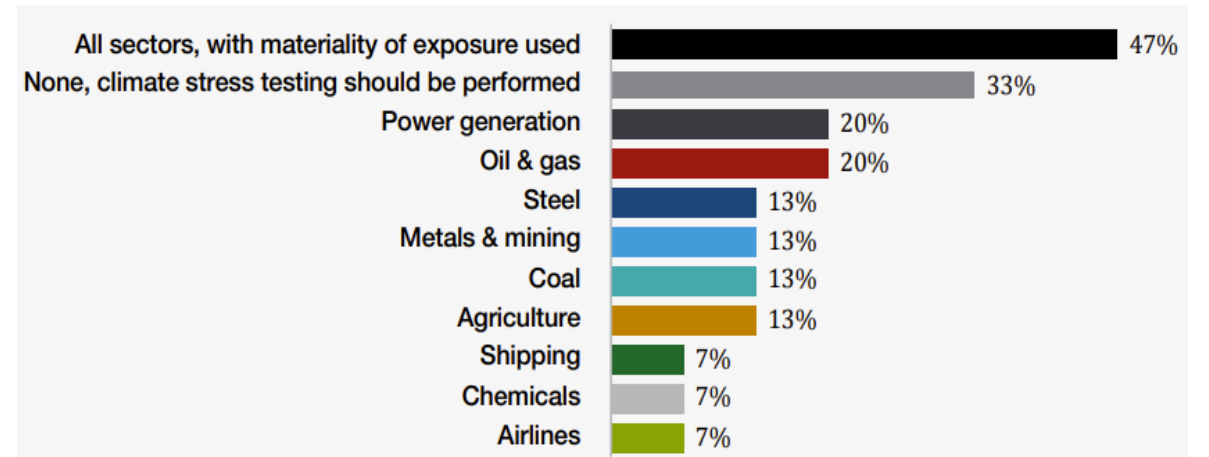
i Do you consider climate risk with your IFRS9 expected loss modelling?



i Which risk types do you believe should be included in the next EU supervisory stress test?

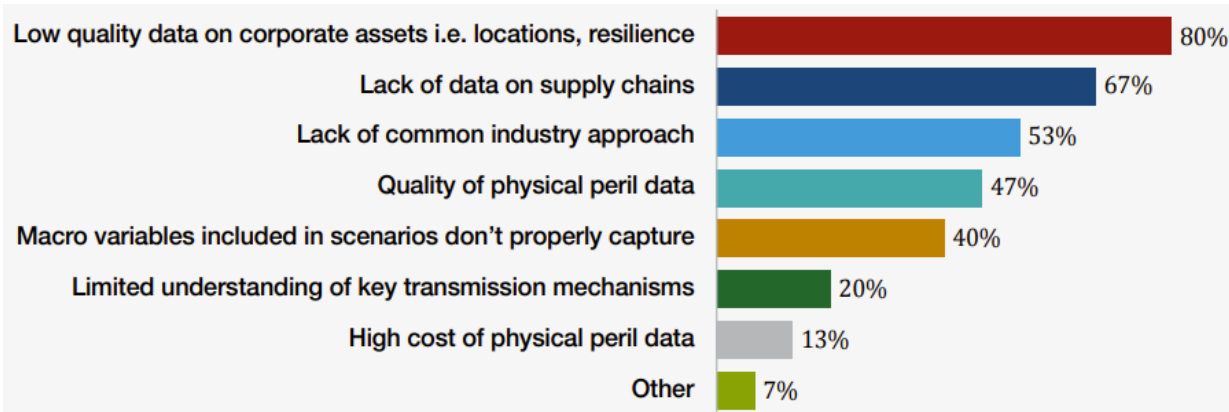


i Which sectors do you believe that counterparty-level analysis is useful?

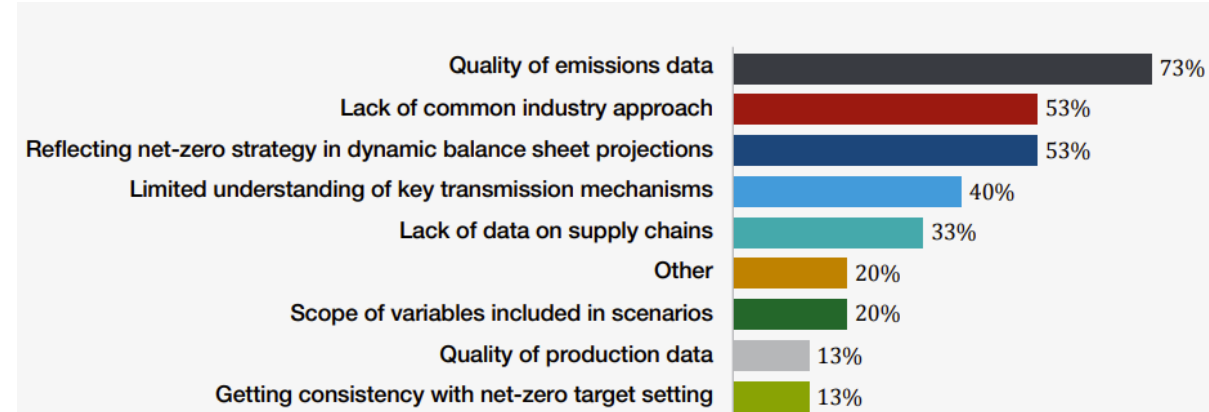


Key Findings (Credit Risk) – Data Visualisation (2/3)

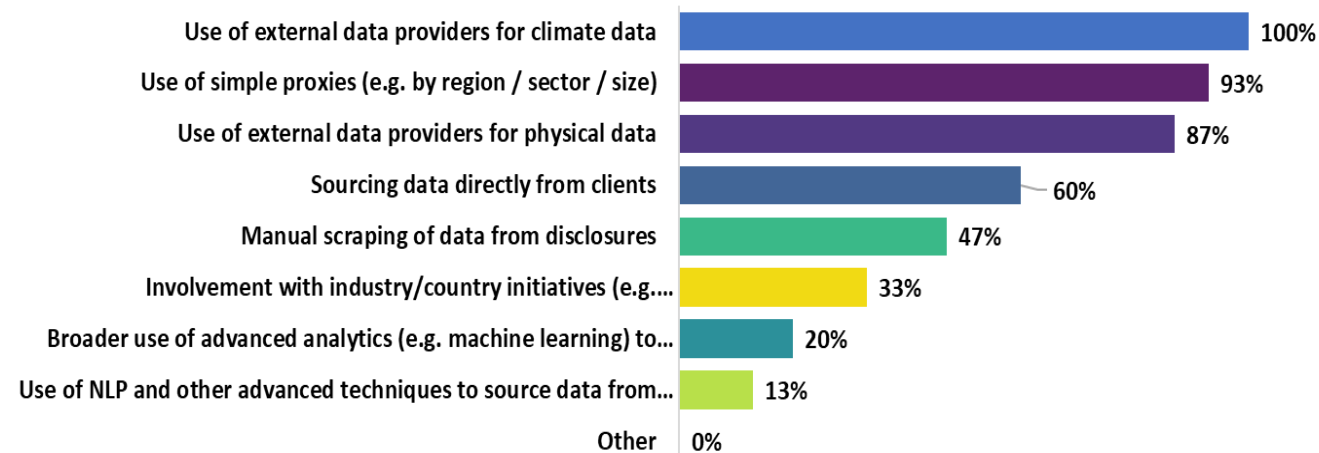
i How What are the biggest challenges to corporate physical risk modelling currently?



i How What are the biggest challenges to corporate transition risk modelling currently?

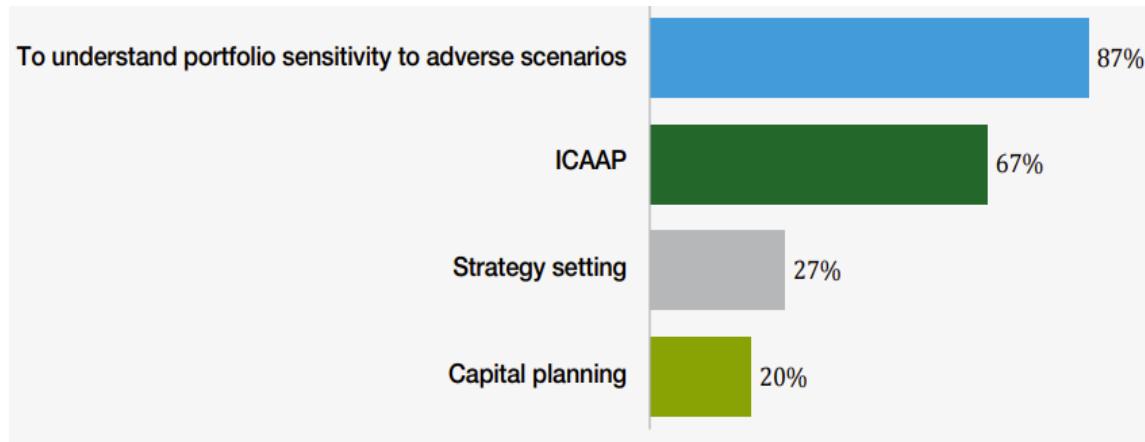


i How are you looking to address gaps in data coverage?

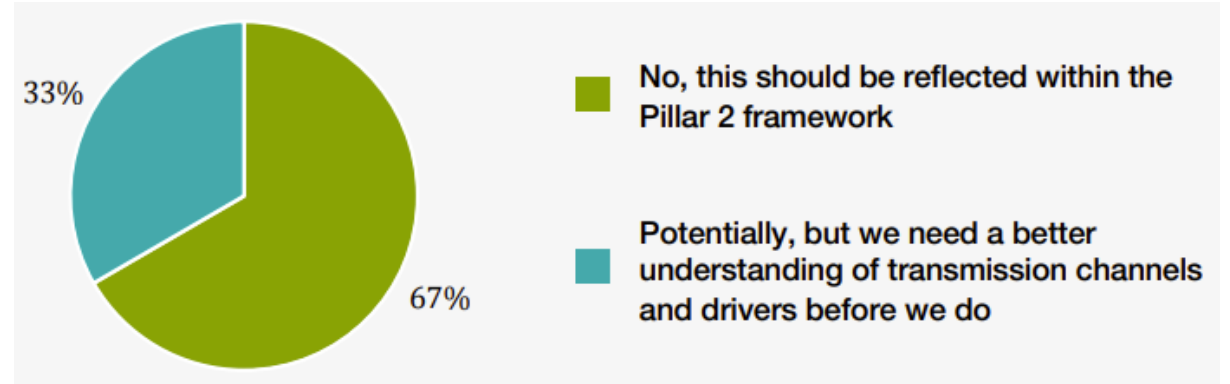


Key Findings (Credit Risk) – Data Visualisation (3/3)

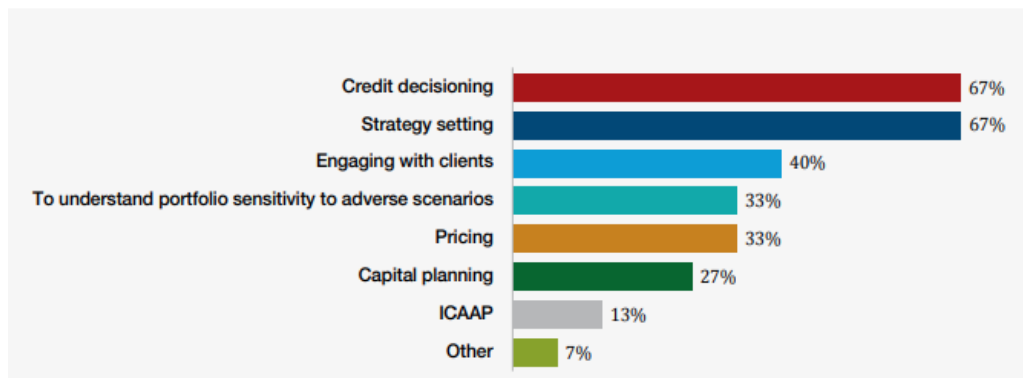
i How do you use results of supervisory climate risk stress tests internally?



i Do you think climate risk should be included within the Pillar I capital framework?



i Are there any use cases which you don't currently use climate risk stress testing output for currently, but intend to within the next two years?



Next Steps: Considerations in Supervisory Development (1/2)

Climate Risk Stress Testing Report Launch:

AFME held a [webinar](#) (Thursday 22 June 2023) to further discuss the state of play of industry climate risk stress testing and common challenges and provide supervisory insights - in particular regarding short term scenarios and Pillar 2 - from the ECB and industry participants among others.

The ECB and NGFS are working to **develop a conceptual framework for nature-related consideration** – the ECB is providing recommendation to the NGFS scenarios workstreams on how to integrate nature related risk into climate risk scenarios.

Next Steps: Considerations in Supervisory Development (2/2)

NGFS Work on Short-Term Scenarios

- ❖ The ECB is supporting the NGFS to provide better scenario narratives and horizons as part of key priorities for the next 2 years. These will cover new short-term scenarios which are grounded in the long-term scenario framework but with a 3-5 year time horizon. This will allow for:
 - A more **dynamic** translation of shocks to near-term impacts
 - Accounting for shocks that have a **short-term impact** but may subside in the long-term, including **cyclical factors, compound shocks** and **feedback loops**
 - Incorporating the role of **expectations and preparedness**
- ❖ Q3/ Q4 2023: The NGFS will publish a conceptual framework reflecting the NGFS workstream members' thinking on short-term scenarios, specifically applications, narratives, shocks and calibration and possible modelling frameworks.
- ❖ This will then guide the modelling team which is chosen (there was a recent tender for applications which has now closed), it will also guide institutions wishing to align with the NGFS in terms of development of short-term scenarios
- ❖ Q4 2024: New NGFS short-term scenarios which have the potential to be used in climate stress tests, monetary policy assessment and economic assessments.
- ❖ ***Fit-For-55 Climate Risk Stress Test Exercise***: The work of the NGFS on short-term scenarios will not be considered in the preparation of the 2024 ESAs exercise. Templates have now been made available for this exercise and are under consultation.
- ❖ ***EBA stress testing mandates in CRR3***: to cover both internal and regulatory exercises, de minimis. Due by entry into force of CRR3 + 12m (i.e. 2025-2026)

Annex: Recommendations - Credit Risk (1/3)



Future regulatory Climate Risk Stress Test exercises should run at a minimum every 2 years and leverage off the experience of the ECB 2022 exercise.



Banks **support the 'Fit for 55' exercise in 2024** but early clarity on the process and data requirements would be welcome.



Future regulatory stress tests should consider interaction with other supervisory initiatives and banks internal obligations.



Future regulatory Climate Risk Stress Test exercises should continue to concentrate around three main risk types – (credit, market, and operational).



While NGFS scenarios provide a good global baseline for banks, there will continue to be a need for banks to integrate their own data and relevant scenarios to support meaningful and quantifiable scenario analysis. Banks are already moving forward on this.

Annex: Recommendations – Credit Risk (2/3)



Future regulatory Climate Risk Stress Test exercises should focus on short-term horizons of 3-5 years. While challenging, almost half of members support also **maintaining a 30-year long-term horizon and introducing medium-term horizon of 10 years.**



A dynamic approach for long-term transition risk is preferable but challenging, on the other hand **a static balance sheet approach is deemed more appropriate for short-term scenarios.**



Sourcing of proxy data is still a major challenge and further regulatory guidance on this would be welcome. Additionally, **CSRD will also help to address data gaps, though banks will still need to rely on external data providers and use their own initiatives to source client-level data.**



Regarding credit risk assessment, future Climate Risk Stress Test exercises should consider a smaller scope of NACE codes, focusing on the most exposed sectors and highest emitters as well as a more granular breakdown.



The **IFRS9 model is relevant and should be maintained** in future regulatory Climate Risk Stress Test exercises.



For now, regulators should only consider climate risks in Pillar II provisions. Most respondents still use supervisory climate risk stress testing results primarily to understand portfolio sensitivity and as part of their ICAAP.

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