Discussion of “Climate-related risks: A financial stability angle for Europe”

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1. Sustainable finance from a risk management perspective

2. Sustainable finance from a reallocation/alignment perspective
1. Sustainable finance from a risk management perspective

- Adapting IMF FSAP analysis to climate-related risks
- Building upon NGFS work on scenarios
- Raising greater awareness among supervisors
- Enhancing data availability on physical and transition risks
- Reinforcing the analysis of transition-related risks, beyond carbon pricing
Reinforcing climate risk analysis methodologies: Working together with NGFS and its members

• Adapting IMF FSAP analysis to climate risks
  ➔ Physical risk increasingly material
  ➔ Transition risk starting to be assessed
  ➔ Using a climate risk assessment matrix for countries under surveillance
  ➔ Key challenges

• Building on the NGFS work on scenarios
  ➔ Potential interactions between physical and transition risks; compounded risks (e.g., Covid)
  ➔ Beyond carbon pricing: other transition risks?
  ➔ Is the orderly scenario baseline always relevant?
  ➔ Adapting key hypothesis: balance sheet hypothesis, tipping points
Raising awareness and supporting supervisors

Climate-related risks as material threat to stability

- Yes, mentioned that publicly
- Yes, but not publicly mentioned
- No
- Haven't analyzed the materiality of climate-related risks

IMF survey among 64 supervisors suggests that more than 40 percent have not analyzed the materiality of climate risks

- NGFS work is crucial
- FSB work on climate vulnerabilities and data
Raising awareness among firms: Transition risks are key

- Aftermath of COP26: updating NDCs and need to close the “climate ambition gap”
- Targeted emission reduction policies are becoming more likely, including carbon pricing applications.
- Yet, with realistic carbon prices, some firms will face challenges – and thereby banks lending to them
- Open question:

  Should supervisors concentrate on a limited number of firms (i.e., the ones with the greatest carbon intensity per $million of revenues) to ease the reporting burden of supervised institutions?

Distribution of carbon emission intensity for >16000 firms globally

Based on Scopes 1–3 emissions

>500 implies a loss of >5% of revenue at a carbon price of $100 per ton

Source: Ehlers, Mojon and Packer (2019)
Enhancing data availability on climate-related risks

- Lack of forward-looking and granular data to assess financial stability risks and differentiate between “green” and “brown” assets
  - Need for reliable and comparable climate-related data (“carbon” data + geographical data on asset locations)
  - Improvements in data accessibility
  - Role of assurance, through verification and audit mechanisms

- A mix of policy interventions: A Climate Finance Architecture
  - IMF Climate Change Indicators Dashboard
  - NGFS forthcoming data repository

- High quality, consistent and comparable climate data
- Use of well-defined and decision-useful metrics, certification labels and methodological standards
- Globally shared principles for classifications
- Adoption of global disclosure standards
2. Sustainable finance from a reallocation/alignment perspective

- Principles for sustainable finance classifications
- Global disclosure standards
- Transition finance is key
- Consistency amongst net-zero methodologies
- EMs play a key role in the process, while facing unique challenges
Sustainable finance classifications, disclosures, and net-zero methodologies

Greater consistency and science-based approaches are urgently needed

IMF working with other IOs and the G20 SFWG

- Operationalization of the G20 principles for sustainable finance classifications
- Convergence towards a global disclosure framework is key: role of the ISSB
- Development and use of decision-useful metrics, certification labels and methodological standards

Source: IMF ESG monitor, 30 November 2021
Financing the transition requires scaling up private finance and new instruments

- Surge in sustainable debt issuance, with green bonds dominating but sustainability-linked debt growing exponentially (+295 percent compared to 2020 levels) – including in EMs

- Preferred instruments vary across EMs, with green bonds remaining the largest segment

- Advantages of sustainability-linked debt (transition for the entire business model, built-in verification mechanisms) but lack of minimum standards in AEs and EMs (disclosures, verification, difficulties of assessing forward-looking metrics…)

Building a science-based transition finance framework is a priority for this year

Source: IMF ESG monitor, 8 February 2022