



**MONETARY AND
CAPITAL MARKETS**

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

FEBRUARY 15, 2022

Fabio M Natalucci

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

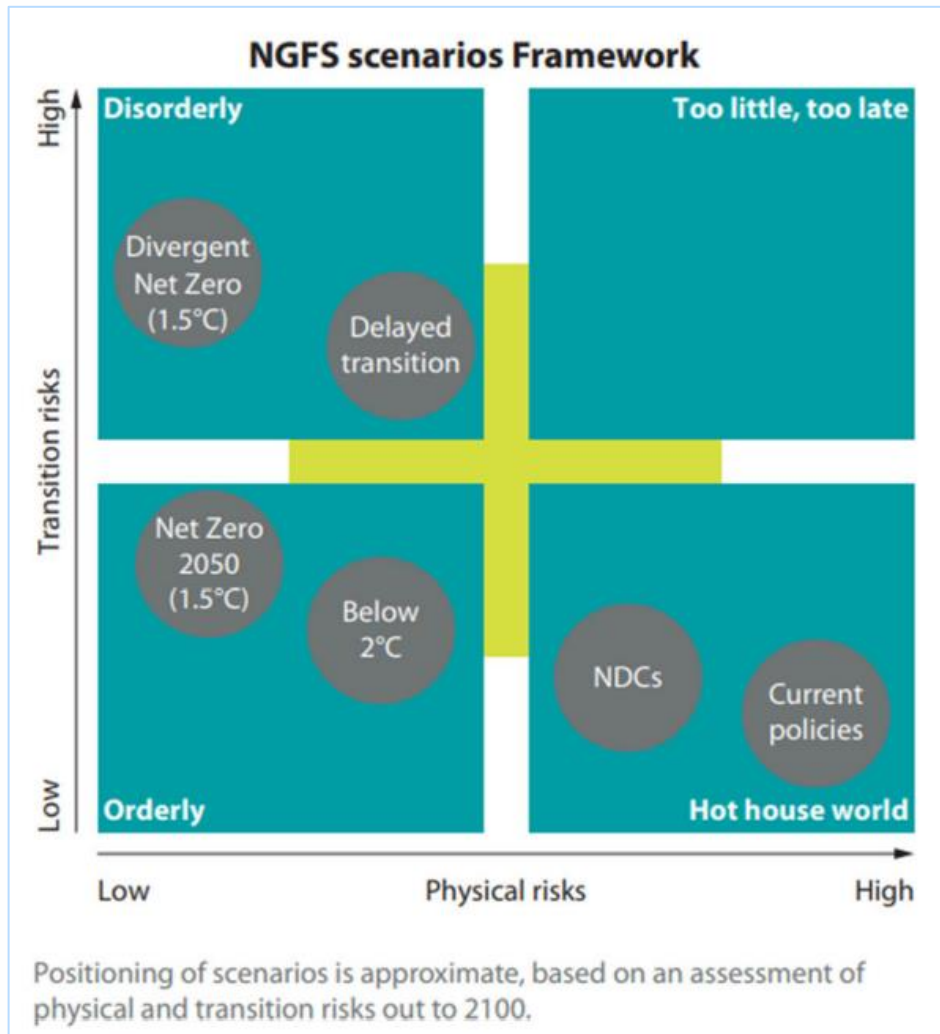
Building upon NGFS work on scenarios

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**

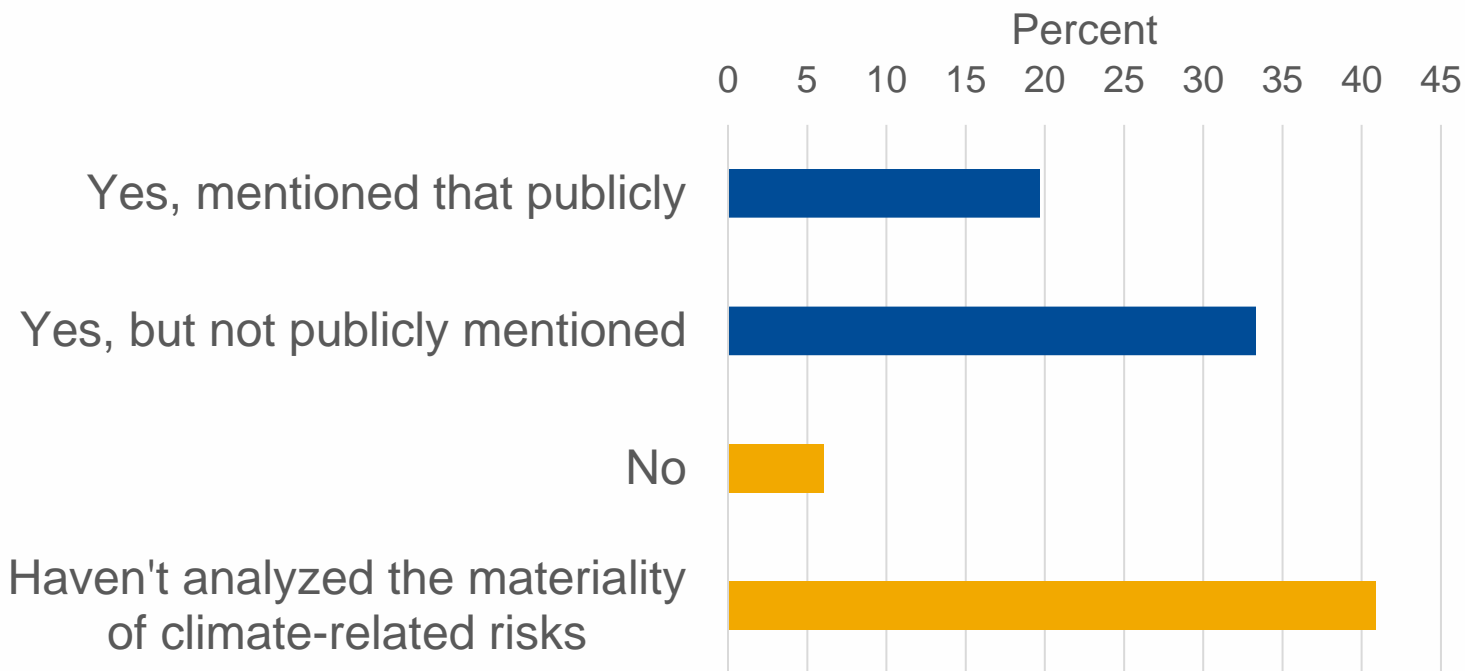
- ↳ Physical risk increasingly material
- ↳ Transition risk starting to be assessed
- ↳ Using a climate risk assessment matrix for countries under surveillance
- ↳ Key challenges

- **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



- 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

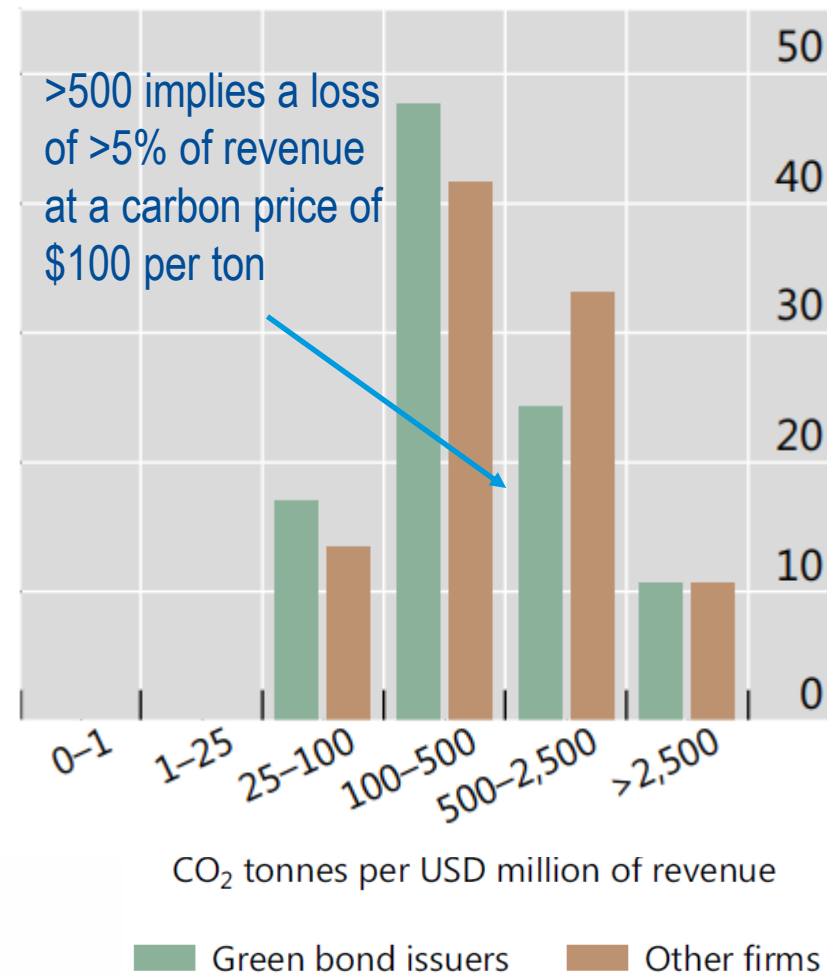
Raising awareness among firms : Transition risks are key

- 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



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

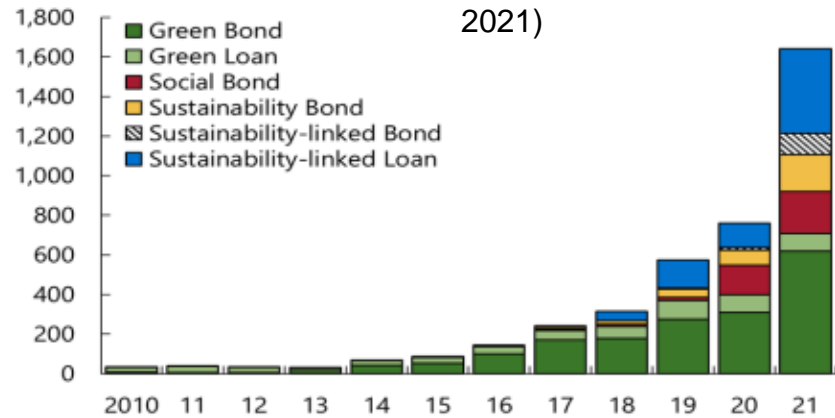
- ↪ Operationalization of the G20 principles for sustainable finance classifications
- ↪ Convergence towards a global disclosure framework is key: role of the ISSB
- ↪ Development and use of decision-useful metrics, certification labels and methodological standards



Source: IMF ESG monitor, 30 November 2021

Financing the transition requires scaling up private finance and new instruments

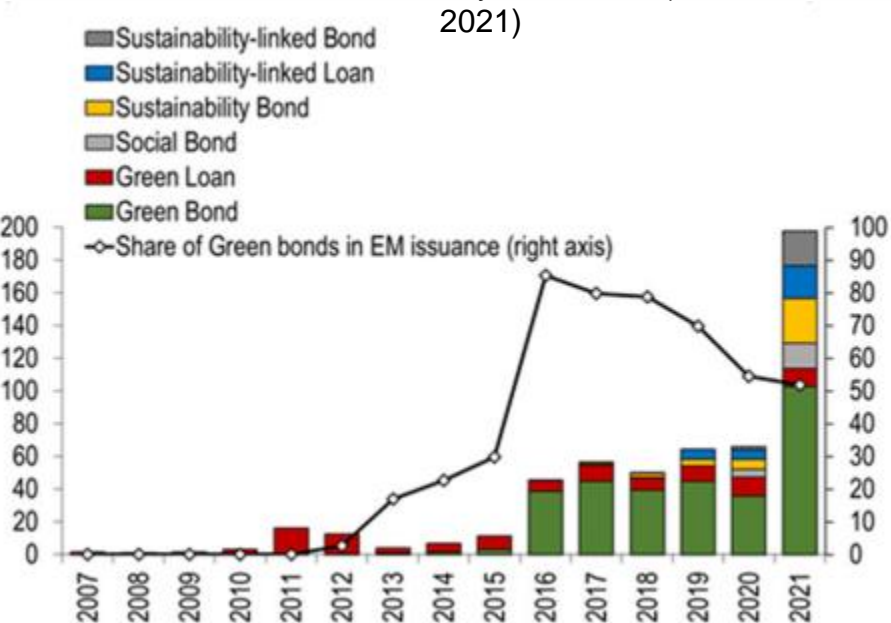
Global Sustainable Debt Issuance by Instrument (USD bn, as of Dec. 2021)



- 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

EM Sustainable Debt Issuance by Instrument (USD bn, as of Dec. 2021)



- 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