

Towards macroprudential frameworks for managing climate risks

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What do we know about climate risks and financial stability

- Climate risks are potential systemic risks
- Climate systemic risks are likely to be underestimated
- Unfolding path of climate risks is key for the level of financial (in)stability
- An orderly transition starting now is the scenario that minimizes risks for financial stability
- An orderly transition starting now comes with frontloaded transition risks

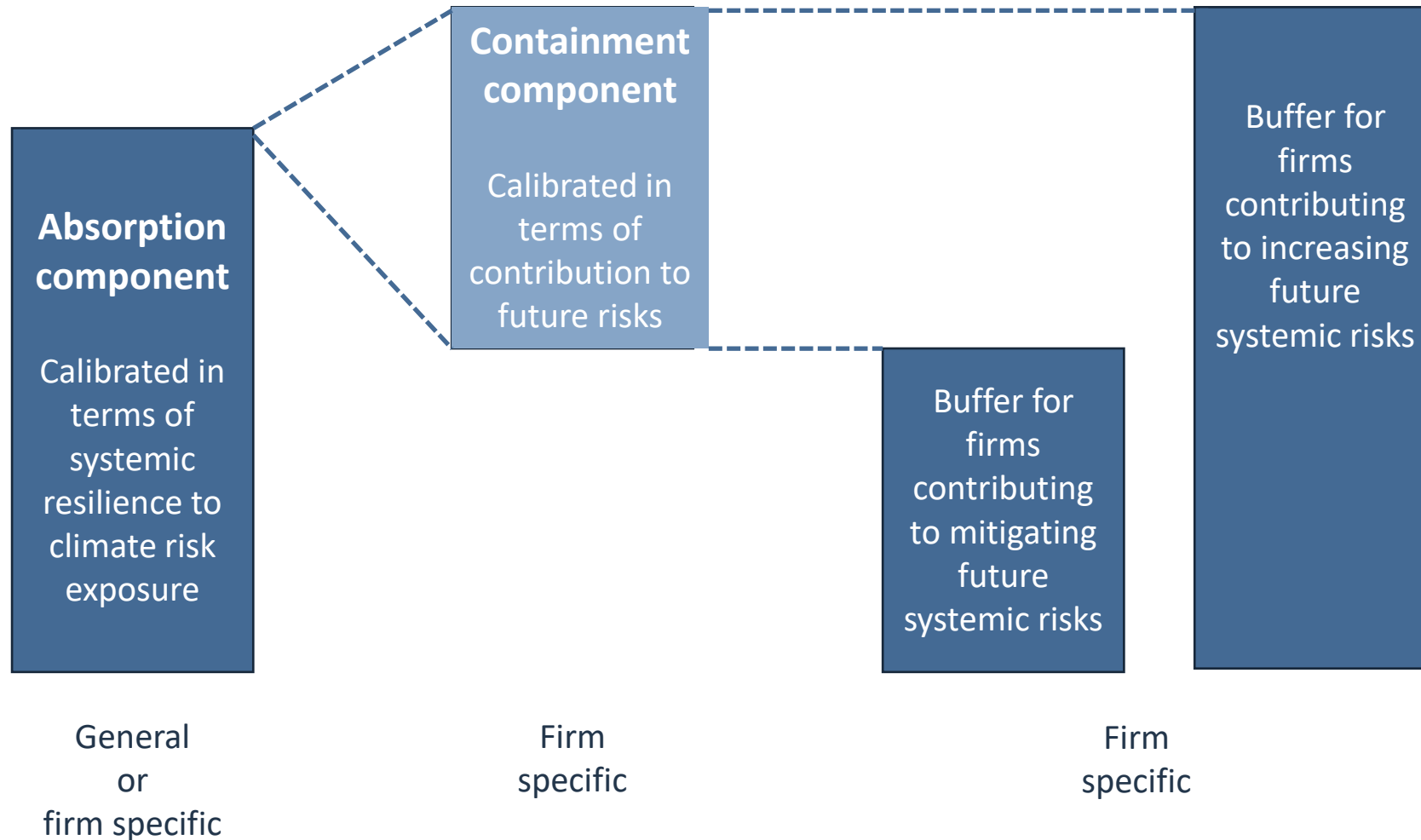
Addressing climate risks with macroprudential policy

- Potential systemic risk requires adequate macroprudential policy response
- Holistic response, starting with sound micro prudential policy, is necessary
- Existing macroprudential policy toolkits can be deployed now to address climate systemic risks, although with possible adaptations to reflect their unique features
- Good macroprudential policy aims at
 1. Increasing resilience of financial system (absorption component)
 2. Mitigating the build up of systemic risk (containment component)

Systemic Risk Buffers– a tool available to European authorities

- SyRBs are a capital-based tool that has been used by national European authorities to address systemic risks with features like climate risks
- Principles of SyRBs for climate risks
 1. A component to absorb physical and transition risks – Function of individual and systemic exposure
 2. A component to mitigate the build-up of climate risk – Function of individual contribution to future systemic risk (i.e. contribution to the transition)
 3. A dynamic adjustment to the evolution of transition path

Blueprint for climate SyRB – Absorption and mitigation components



Blueprint for climate SyRB – Dynamic adaptation to transition path



**Absorption
component**

2025
Starting point



**Absorption
component**

2028
Orderly
transition
scenario



**Absorption
component**

2028
Late and
disorderly
transition
scenario

Implementation

- Link with concentration risk
- Margin of conservatism principle
- Progressive deployment as data and experience develop
- “Try-evaluate-adjust” approach with some tolerance for potential errors
- International coordination warranted but not necessary