CREDIT SPECIAL

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European Banks:
EBA publishes pilot exercise on climate risk

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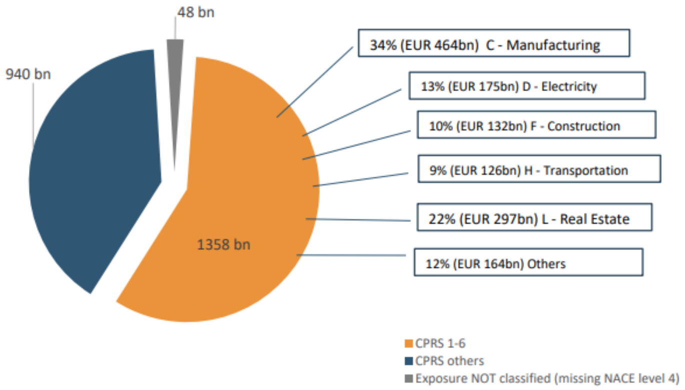
The European Banking Authority (EBA) has published the findings of a pilot exercise into the scale of the risks associated with climate change for banks. According to the exercise, almost 60 % of the exposures analysed were in sectors that may be sensitive to transition risk. The regulator emphasised the need to fill gaps in data so as to ensure a smooth transition towards low-carbon activities. Furthermore, the authority pointed to large differences between institutions on the implementation of the EU taxonomy classification. In our view, these findings support our assessment that sustainability has long since become a key factor for competitiveness and that collecting and evaluating data, in particular, pose enormous challenges.

On 21 May 2021, the European Banking Authority (EBA) published the results of its pilot exercise on the scope of climate-related risks for European banks. The exercise involved 29 major banks from 10 countries, which together represent around 50 % of the European banking sector's total assets. The study examined their exposure to large corporates domiciled in the EU, while loans to SMEs were excluded. The classification of assets according to climate-related risks was based on different methods, including the relatively new EU taxonomy (for more information see Credit Special "European bank bonds: Supervision wearing green-tinted spectacles" of 8 December 2020).

According to EBA's exercise, 58 % of the banks' exposures analysed were allocated to sectors that might be sensitive to transition risk (CPRS - Climate Relevant Policy Sectors). EBA also reiterated the importance of more wide-ranging disclosures on institutions' transition strategies to enable supervisors to adequately assess the associated risks. In addition, it stated that a crucial factor was the continued expansion of banks' data infrastructure.

High transition risks

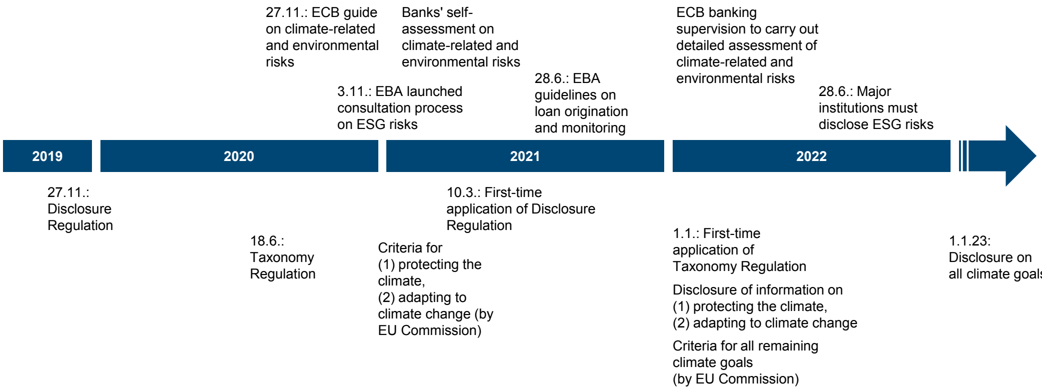
Exposures analysed by transition risk



Sources: EBA, Helaba Research

The findings also showed big differences between banks on their progress in implementing the EU taxonomy, with the most recent aggregated proportion of green activities - the green asset ratio (GAR) - amounting to 7.9 %. However, since some sectors are relatively strongly affected by climate-related risks, the study indicated that the level of transition risk varied accordingly between institutions. It went on to say that, overall, collecting and evaluating climate-related data is still in its infancy and that considerable effort on the part of banks is needed to improve tools for assessing transition risks.

In our view, the findings of this exercise support our assessment that, in particular, collecting and processing extremely large volumes of data in connection with managing and disclosing climate-related risks and activities pose challenges for the banking sector and entail enormous amounts of time and resources (see Credit Special “Nachhaltigkeit rückt in den Fokus” of 4 July 2019). Regulators and supervisors across the world are vocal in highlighting the financial risks associated with transitioning banks' activities towards net-zero carbon business models. EBA's remit is to integrate sustainability criteria into the banking supervision process, having drawn up an action plan as early as December 2019. At the same time, we believe that the transition towards a net-zero carbon economy offers significant earnings potential for banks. Consequently, the issue of sustainability has long since become a key element of banks' strategic focus.



Sources: ECB, EBA, Sustainable Finance Disclosure Regulation, Taxonomy Regulation, Helaba Research

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