

Climate Risks and Financial Systems in LAC

Maria Netto
Giovanni Frisari



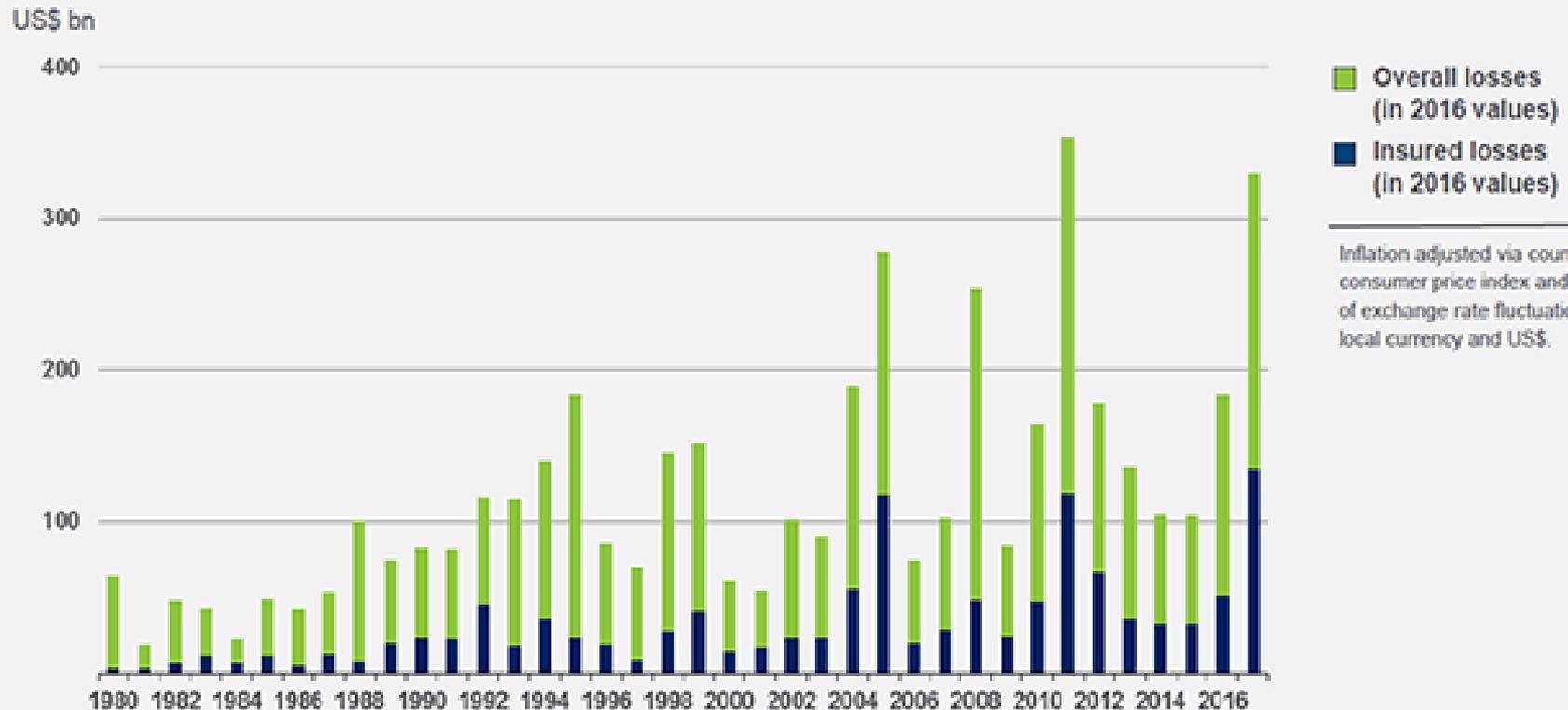


1

Climate Risks and Financial Systems



Natural Disasters and Economic Loss



Cost Of Climate-Related Disasters Soars 150%

Total economic cost of global climate-related disasters over 20-year periods



Climate Change Threatens Financial Resilience

“The combination of the weight of scientific evidence and the dynamics of the financial system suggest that, in the fullness of time, climate change will threaten financial resilience and longer-term prosperity”

U.K. central bank's Governor Mark Carney

- ✓ by causing banks and insurers direct losses from extreme weather
- ✓ by creating future liabilities for financial firms and their clients from those seeking compensation for climate-related losses and
- ✓ by the unexpected costs of shifting toward a low-carbon economy

International context

- **FSB:** NetTask Force on Climate-related Financial Disclosures (TCFD)
- **G20:** work of Central Banks and Supervisors for Greening the Financial System (NGFS)
- **IFC:** Sustainable Banking Network (SBN)
- **UN:** UNEP FI, Sustainable Stock Exchanges Initiative, Sustainable Insurance Forum, Inquiry Initiative, Principles for Responsible Banking
- **IOSCO:** Task Force on Sustainable Finance
- **Investors standards** and principles for ESG, Equator Principles, PRI, etc.
- Many **national governments** developing regulatory frameworks: European Union, UK, China, among others

LAC regional context

- **Green Banking Protocols** and Round Tables: Brazil, Colombia, Mexico, Paraguay.
- **Sustainable Stock Exchange Initiatives:** sustainable indices, exchanges initiatives: Brazil, Chile, Mexico.
- **Public Private Dialogues:** Brazilian and Mexican Financial Innovations Labs
- **Central Banks and Financial Market Supervisors** regulations and pledges: Argentina, Brazil, Colombia, Peru.
 - ➔ Emerging role of regulators
 - ➔ High impact in FIs behaviour
 - ➔ NDBs involvement still picking
 - ➔ Mostly focus on ESG practices

Climate risks and financial systems - Regulatory and Supervisory practices in LAC

- Still an incipient topic!
- High differentiation in awareness and preparation of supervisors and regulators
- Combination of Public and Private Sector led initiatives!

Regulation / Supervisory Measures



Powered by Bing
© GeoNames, HERE, MSFT

Private Sector Initiatives



Regulatory and Voluntary Practices in LAC – TCFD Benchmark Analysis

Issue areas		TCFD	Brazil	Colombia	Mexico	Peru	
		Climate Risk Standards	Res. 4327 Res. 4557	Protocolo Verde	Stock Market Circular	SBS 1928-2015	SMV 033-2015-01
Scope	Climate change mentioned	✓	✗	✓	✓	✗	✗
	Address Financial Industries	✓	✓	✓	✓	✓	✓
	Address Non-Financial Groups	✓	✗	✗	✓	✓	✓
Risk Approach	Identifying risk	✓	✓	✓	✓	✓	✓
	Quantifying risk	✓	✓	✓	✗	✓	✗
	Modeling risk (eg. Stress testing)	✓	✗	✗	✗	✗	✗
	Risk Strategy (including env. risk)	✓	✓	✓	✗	✓	✗
	Governance (considering env. risk)	✓	✓	✓	✗	✓	✗
	Forward-looking Perspective (eg. Scenario Analysis)	✓	✗	✗	✗	✗	✗
Process	Review and categorization of projects	✓	✓	✓	✗	✓	✗
	Compliance with applicable environmental standards	✓	✓	✓	✗	✓	✗
	Risk management system and action plan	✓	✓	✓	✗	✓	✗
Disclosure	Recognition of climate risk as financial risk	✓	✓	✓	✗	✓	✗
	Requirement on disclosure of climate risk	✓	✗	✗	✓	✗	✗
	Report of GHG Emissions (voluntary)	✓	✗	✓	✗	✗	✓

1 – Driver often is not climate risk

2 – Modelling and scenario analysis not yet considered

3 – Disclosure is not typical



Monetary and regulatory instruments: LAC and international practices to support financial system resilience to climate risks

- *Aim:* Identify regulatory and supervision practices under piloting and assess replicability in LAC
- Practices under study:
 - ✓ Assessment of climate risk exposure of the financial sector
 - ✓ Encouraging environmental risk analysis by financial institutions
 - ✓ Creating a green credit market
- Contrasting case-studies with LAC experience:
 - ✓ De Nederlandsche Bank (DNB)
 - ✓ Bank of England (BoE)

Assessment of climate risk exposure of the financial sector

NGFS: “The first step to achieve successful integration of climate and environment-related risks into supervision is to assess possible impacts on financial institutions from both physical and transition effects of climate change.”

Challenges:

- ✓ Historical data a poor indication of future risks
- ✓ Finding the right level of granularity
- ✓ Translating physical and economic models into useful financial risk measures

LAC Regulators and Supervisors: First Reaction

CHALLENGES	OPPORTUNITIES
High Institutional segmentation among supervisory and regulatory systems	Institutional Coordination is key, mandates are typically shared across different entities
High heterogeneity in level of capabilities and preparation in the region	Cross-country Knowledge exchanges as a driver for action
Data availability, format and consistency is low in most countries	Combine qualitative and quantitative approaches to suit different contexts
Lack of consensus on definition,	Need of a common taxonomy and guidelines
Low Awareness of materiality and relevance of climate related financial risks	Physical risks perceived generally as more relevant but exposure to transition might be underestimated

2

Implications for NDBs



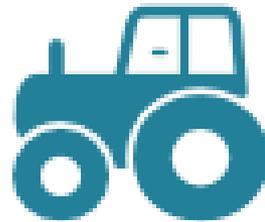
From ESGs to an integral approach

- Risks of negative environmental impacts **of** investments made – **ESG** policies
- Risks associated to potential negative impacts of climate change or change in environment **in** investments made - **stress testing and resilience**
- Risks associated to **delays and uncertainties of policies** and measures governments develop to comply with environmental national goals – **financial planning and design.**
- Opportunities relating to **efficiency gains** (natural resources savings, reduction of costs) OR **explicit pricing** provided to environmental assets (ex. carbon price) – **portfolio classification, financial planning and design.**

LAC NDBs



90% SME financing



85% Agriculture



75% Infrastructure



65% Housing/
construction

Take Aways

- Need to “tropicalize” methodologies and cover important sectors such as agriculture
- Balance between “self / market regulation” versus “standardization” and “regulation”.
- Importance to engage, develop incentives and educate NDBs, Fis, investors and market players up front.
- Key role of enabling environment – transparent regulation is the most important signal to markets.
- Bottom up approaches and ownership from players is key
- Exchange of experiences and role of international initiatives play an important role: PRI, CBI, Sustainable Stock Exchanges, IOSCO, FSB, Global Compact, UNEP FI
- Digital economy and “Fintechs” allow for new ways to assess, tag and promote investments in sustainability.

Supporting our partners



Financial Innovation Labs: Public Private Dialogues



LAB

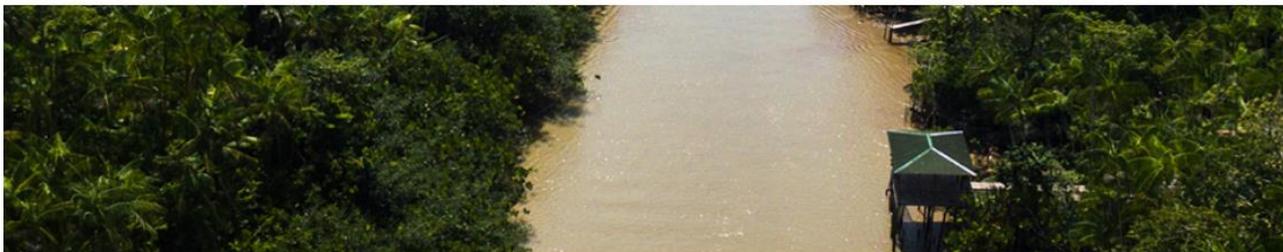
Grupos de Trabalho

Agenda

Imprensa

Contato

Acesso Aos Membros



Sobre o LAB

O Laboratório de Inovação Financeira (LAB) é um projeto conjunto da Associação Brasileira de Desenvolvimento (ABDE), do Banco Interamericano de Desenvolvimento (BID) e da Comissão de Valores Mobiliários (CVM), que reúne diferentes setores (financeiro, consumidor, provedor, regulatório) para um fórum de discussão intersetorial. O intuito é fomentar a criação de instrumentos de investimento e de estruturas financeiras, que maximizem a alavancagem do setor privado e que otimizem o uso de fundos de doadores. Dentre os principais desafios estão: identificar gargalos ao investimento privado em soluções sustentáveis em setores como energia, transporte, agricultura e água; desenhar instrumentos financeiros para alavancar investimentos, como linhas de financiamento e mecanismos de gestão de risco; e analisar instrumentos inovadores e boas práticas que possam ser replicadas por instituições financeiras de desenvolvimento. O LAB é um espaço para debater experiências internacionais e construir um diálogo intersetorial organizados em grupos de trabalho (GT) sobre quatro temas: Finanças Verdes, Fintech, Instrumentos Financeiros e Investimentos de Impacto e Títulos Verdes.



Supporting National Assessments of Climate Risk and Financial Systems

- Impact of Climate Related Risks on Brazilian Banking Sector (focus on physical risks)
- TCFD- Gap Analysis for Mexican banks (focus on Governance and Processes)
- Impact of Climate Related Risks on Colombian Financial Sector (focus on transition risks)

Thanks!

<https://www.greenfinancelac.org/>

