EUROPEAN CENTRAL BANK

EUROSYSTEM

Christine Lagarde
President

Ms Hannah Fischer
and Members of Koala Kollektive
via Email: mail@koalakollektiv.de

Frankfurt am Main, 11 March 2021
CL/21/51

Re: Your letter (ClimateAction_OpenLetter_ECB_KK)

Dear Ms Fischer,
Dear Members of Koala Kollektive,

Thank you for your letter, received on 15 February 2021.

Let me first emphasise, on behalf of all ECB Executive Board members, that we fully recognise the relevance of climate change for our mandate. The scale and irreversibility of the consequences of climate change call for immediate action from all stakeholders, each within their own mandates and areas of competence. Accordingly, the ECB is continuously and progressively stepping up its involvement in climate-change related matters.

We have already taken a number of concrete measures to this end across all areas of ECB competence, and particularly so in the areas of monetary policy, financial stability, and prudential supervision.

Regarding monetary policy, the ECB has been keeping favourable financing conditions in the wake of the pandemic, which create an environment that is generally supportive to investment, including in green and energy-efficient technologies. Moreover, as regards its operations, the ECB regularly purchases green bonds under its asset purchase programmes, thereby supporting the corporate and public sectors' increasing efforts to adopt more energy-efficient technologies and reduce their carbon footprints. By purchasing green bonds under our asset purchase programmes, we actively support the EU's climate goals. The ECB currently holds around a fifth of the outstanding volume of eligible green bonds, and since the start of this year bonds with coupon structures linked to certain sustainability performance targets are now eligible as collateral for our credit operations and for outright purchases

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for monetary policy purposes.[1] In addition, the ECB has already taken steps towards incorporating sustainability considerations in its non-monetary policy portfolio. For example, the ECB has decided to use parts of its own funds portfolio to invest in the euro-denominated green bond investment fund of the Bank for International Settlements and to increase its share of green bonds in this portfolio over the coming years.[2] Furthermore, the ECB and the National Central Banks of the euro area have recently agreed on a common stance for applying climate change-related sustainable investment principles in their euro-denominated non-monetary policy portfolios.[3] Moreover, we are analysing – in the context of the on-going ECB strategy review – potential avenues for further integrating climate change considerations into our monetary policy operational framework.

In relation to your question on supervisory measures and financial stability, I would like to stress that the ECB has identified early on the potential systemic significance of the risks to financial stability stemming from climate change. As shown in a preliminary analysis published in the ECB Financial Stability Review, climate change-related risks have the potential to become systemic for the euro area, in particular since there are indications that markets are not pricing the risks fully[4]. A marked reassessment of climate risk by markets could have substantial effects on the euro area financial system, including banks[5]. That is why the ECB has been taking concrete steps to strengthen the role of climate risk in both financial stability monitoring and banking supervision. Regarding the former, the ECB is integrating climate risks in financial stability monitoring by developing a state-of-the-art monitoring framework – as exemplified in a recent joint report of the Eurosystem and the European Systemic Risk Board (ESRB)[6] – as well as by integrating climate risk in the stress-testing framework. The ECB is currently developing and implementing a top-down climate stress-test to assess the materiality of transition and physical risk on corporates and financial institutions: initial results will be published by mid-2021.

Regarding the supervision of individual banks, ECB Banking Supervision has already taken substantial steps to improve banks' awareness and preparedness to manage climate risks: most notably, it recently published a Guide on climate-related and environmental risks explaining how it expects banks to safely and prudently manage and disclose these types of risks in a transparent manner under the

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1 See https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200922~482e4a5a90.en.html.

2 See https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210125~715adb4e2b.en.html.

3 See https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210204_1~a720bc4f03.en.html.

4 See "Climate change and financial stability", *Financial Stability Review*, ECB, May 2019, available at: https://www.ecb.europa.eu/pub/financial-stability/fsr/special/html/ecb.fsrart201905_1~47cf778cc1.en.html

5 See "Euro area banks' sensitivity to corporate decarbonisation", *Financial Stability Review*, ECB, May 2020 available at: https://www.ecb.europa.eu/pub/financial-stability/fsr/focus/2020/html/ecb.fsrbox202005_03~eaf7ae06be.en.html.

6 See "Positively green: Measuring climate change risks to financial stability", ESRB, June 2020, available at: https://www.esrb.europa.eu/pub/pdf/reports/esrb.report200608_on_Positively_green_-_Measuring_climate_change_risks_to_financial_stability~d903a83690.en.pdf?c5d033aa3c648ca0623f5a2306931e26

current prudential framework[7]. In line with the supervisory expectations outlined in the Guide, institutions are expected to incorporate climate-related risks as drivers of existing risk categories into their risk management framework. Institutions are expected to take a comprehensive, strategic and forward-looking approach to the management and disclosure of climate-related and environmental risks. ECB Banking Supervision has already started supervisory dialogues with institutions on the basis of this Guide. Banks were asked to conduct a self-assessment in line with the supervisory expectations outlined in the guide and to draw up action plans on this basis. The ECB will then benchmark the banks' self-assessments and plans and challenge them in the supervisory dialogue. In 2022, it will conduct (i) a full supervisory review of banks' practices and take concrete follow-up measures where needed and (ii) a supervisory stress test exercise on climate risk to assess the overall climate stress framework of banks.

In line with its activities mentioned above, the ECB takes an active role in the Network for Greening the Financial System (NGFS) and joined the Network's Steering Committee in 2020. It contributes to all five dedicated work streams of the network (microprudential and supervision; macro-financial; scaling up green finance; bridging data gaps; and research). Finally, further underlining our commitment to steadfast progress on addressing the climate challenge within all our areas of competence and promoting a smooth transition towards a low-carbon economy, the recently established ECB-internal climate change centre will further help harness internal expertise and shape the ECB climate agenda.

Yours sincerely,

[7] See "Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure", ECB, November 2020, available at: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf .