

# The ECB's climate-related tests push ESG guidelines forward

## Article

**The news:** The European Central Bank's (ECB) first round of climate-related bank stress tests could pave the way for global standardization.

**More on the tests:** The ECB added a climate-risk component to its biennial bank stress testing, conducted during H1 2022. The new climate test was comprised of three [modules](#):

- A questionnaire on banks' capacity to conduct the climate stress tests
- A comparative analysis on the sustainability of the banks' business models and their exposure to companies that produce the most emissions
- A bottom-up stress test

The tests **evaluated** how banks would hold up through various scenarios, such as how a flood would impact mortgage values, or in the most extreme instance, how banks would handle a “hot-house” scenario in which the global temperature increased by three degrees Celsius. Preliminary results showed that even the toughest scenarios left banks' capital reserve well above their requirements.

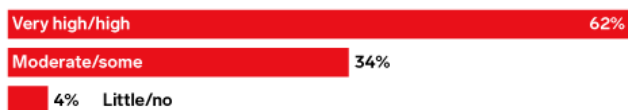
**A preview of results:** This week, the ECB will release the official results, which it said will be aggregated, rather than broken out individually for each bank.

- The banks reported their results differently, resulting in some gaps in the available data. Their full balance sheets were not taken into consideration, so the results don't necessarily provide a full picture of what could happen.
- Some critics have pointed out that the scenarios contained generous assumptions and did not consider the domino effects of certain events or how they might interact. They argued that the test scenarios were too weak.

Due to the inconsistencies, the ECB said the first set of results will not have a direct impact on capital reserve requirements or internal management at the banks. Over time, the ECB expects to converge on a methodology for the stress tests.

**Extent to Which C-Level Executives Worldwide Expect Climate Change to Impact Their Company's Strategy and Operations, Oct 2021**

% of respondents



Note: n=2,083; in the next 3 years  
Source: Deloitte, "2022 CXO Sustainability Report," Jan 18, 2022

272782

eMarketer | InsiderIntelligence.com

**Mixed responses:** Reactions to the tests were mixed.

- Banks at first pushed back on the need to conduct the tests, but after going through the process, some banks said the information gathered will help them refine their climate-related strategy in the future, according to Bloomberg.
- Alternatively, lobbyists are using the results to combat climate-related restrictions and requirements, claiming they are too tight and that banks are in a good position to handle an adverse scenario.

**The big takeaway:** Currently, firms around the world are making climate-related pledges, but there is not much holding them accountable. The ECB’s movement toward standardization could become the first steps toward developing a broader, much-needed globalized set of environmental, social, and governance (ESG) guidelines that is enforceable by regulators. It wouldn’t be surprising to see other countries, like the UK and the US, adopt similar stress tests, which would change the behavior of banks whose capital requirement thresholds were on the line. It may also help advance climate-related agendas in countries like the US, where the subject has faced steep hurdles.

