ENVIRONMENTAL AND CLIMATE-RELATED RISK INTERNAL SELF-ASSESSMENT

A scorecard approach for a proper integration into Enterprise Risk Management
AGENDA

1. Objectives
2. Process overview
3. Self – assessment
4. Our service offer
ENVIRONMENTAL AND CLIMATE-RELATED RISKS
SELF-ASSESSMENT TOOL

Leveraging on ECB Guide on climate-related and environmental risks and emerging market practices, Avantage Reply has developed a self-assessment tool for financial institutions.

The key objective is to help financial institutions while engaging bilateral discussions with ECB early 2021 and evaluating internal capabilities in terms of Environment and Climate-related risk management framework.

Interactive and practical, the self-assessment tool covers the key building blocks of ERM function and assesses an institution’s readiness and preparedness in identifying, measuring and managing climate-related risks.

Integration of climate dimensions at the highest level of the organization is key due to the transversal impact of climate risk over credit, market, liquidity, operational and other transversal risks.

| Framework assessment in line with ECB expectations and ERM key building blocks allowing institutions to design transversal plan actions to be initiated internally | Combined quantitative and qualitative self rating at a granular and aggregated level (ERM building blocks and ECB expectations) | Collection of qualitative statements for each question | Visualization / Graphical presentation of the results |
The purpose of this **scoring tool** is to provide financial institutions **self-assessment capabilities** to identify **key gaps to the 13 high-level expectations** set out in the **ECB Guide** and regarding ERM key building blocks.

It aims to highlight **institutions readiness and preparedness** in identifying, measuring, managing and monitoring climate (both physical and transition) and environment-related risks. Concretely, it aims to:

- Ensure that institutions have **started thinking about how to integrate** climate and environmental dimensions into their strategic planning and decision-making and risk processes;
- Perform a **gap analysis**, identifying current practices and processes to be amended;
- **Define a detailed action plan**, highlighting interdependencies between actions to create a roadmap given each institution’s business model and areas of improvement;
- Allow the institutions to gather the **knowledge on climate topics**, involving step by step key stakeholders (3 lines of defense, direction and operational);
- **Ease bilateral discussions with ECB** early 2021.
2. PROCESS OVERVIEW

- The exercise is articulated in **four consecutive phases**.
- **The process is iterative** and allows an assessment at a **specific level** as well as **at a broader level** composed of homogeneous duties of a Risk department.
- **Adjusted results, heatmaps and action plan** are communicated through the end of the process depending on institution business model size and complexity.
3.1 SELF-ASSESSMENT

**Contact**

- Informal iterations with the client to have an overview of the ambitions and vision of the institution.
- Estimated workload and number of workshops required. Identification of key stakeholders among all risk departments (ERM, CREDIT, MARKET, LIQUIDITY, OPERATIONAL).
- Workshops wave (tool implementation). Collection of existing documentation.
3.2 SELF-ASSESSMENT

**Questionnaire**

- The questionnaire is composed roughly of **about 50 questions** which gather informations **surrounding 10 macro areas**.
- By conducting the assessment, the institution should be able to **frame and implement an environmental and climate-related risk management framework**.
- In addition, each question is mapped to ECB expectations so that institution’s distance to the expectation can be evaluated and ease discussion with the regulator.

### Key macro areas

<table>
<thead>
<tr>
<th>Rating</th>
<th>Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>No - Not started</td>
</tr>
<tr>
<td>2</td>
<td>No - But action plan defined and stakeholders identified</td>
</tr>
<tr>
<td>3</td>
<td>Not yet - But work in progress (encountering difficulties)</td>
</tr>
<tr>
<td>4</td>
<td>Not yet - But work in progress as planned</td>
</tr>
<tr>
<td>5</td>
<td>Yes – Completed</td>
</tr>
</tbody>
</table>

- To properly reflect the level of maturity of the institution, a **rating of 1 to 5 is assigned**.
- The general meaning of each rating is as follows.
# 3.2 SELF-ASSESSMENT

**Questionnaire**

## Extract

<table>
<thead>
<tr>
<th>#</th>
<th>Modules</th>
<th>#</th>
<th>Questions</th>
<th>Answers</th>
<th>Score by Question</th>
<th>Score by Module</th>
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</thead>
<tbody>
<tr>
<td>30</td>
<td>Risk Monitoring</td>
<td></td>
<td>Has the institution started to conduct a proper climate-related and environmental due diligence, both at the inception of a client relationship and on an ongoing basis ?</td>
<td>Yes - Completed</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>31</td>
<td>Risk Monitoring</td>
<td></td>
<td>Does the institution include in credit-granting process an assessment of how climate-related and environmental risks affect the borrower’s default risk ?</td>
<td>Not yet - But work in progress (encountering difficulties)</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>32</td>
<td>Risk Monitoring</td>
<td></td>
<td>Is the institution able to identify borrowers that may be exposed, directly or indirectly, to increased climate-related and environmental risks ?</td>
<td>No - Not started</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>33</td>
<td>Risk Monitoring</td>
<td></td>
<td>Does the institutions consider climate-related and environmental risks in collateral valuations ?</td>
<td>No - Not started</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>34</td>
<td>Risk Monitoring</td>
<td></td>
<td>Is the institution able to monitor how geographic and sectoral concentration is prone to climate-related and environmental risks ?</td>
<td>Not yet - But work in progress as planned</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>35</td>
<td>Risk Monitoring</td>
<td></td>
<td>Has the institution a pricing framework to support the chosen risk perspective and strategy (limiting exposures to sectors harmful for the environment or the climate) ?</td>
<td>No - But action plan defined and stakeholders identified</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>36</td>
<td>Risk Monitoring</td>
<td></td>
<td>Does the institution keep an eye on rules and standards on sustainability changes (compliance risk) ?</td>
<td>Yes - Completed</td>
<td>5</td>
<td></td>
</tr>
</tbody>
</table>

### Link with Expectation

<table>
<thead>
<tr>
<th>#</th>
<th>Modules</th>
<th>#</th>
<th>Questions</th>
<th>Link with Expectation</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>30</td>
<td>Risk Monitoring</td>
<td></td>
<td>Has the institution started to conduct a proper climate-related and environmental due diligence, both at the inception of a client relationship and on an ongoing basis ?</td>
<td>7,5</td>
<td>5</td>
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<tr>
<td>31</td>
<td>Risk Monitoring</td>
<td></td>
<td>Does the institution include in credit-granting process an assessment of how climate-related and environmental risks affect the borrower’s default risk ?</td>
<td>8,1</td>
<td>3</td>
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<tr>
<td>32</td>
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<td>Is the institution able to identify borrowers that may be exposed, directly or indirectly, to increased climate-related and environmental risks ?</td>
<td>8,2</td>
<td>1</td>
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<tr>
<td>33</td>
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<td>8,3</td>
<td>1</td>
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<tr>
<td>34</td>
<td>Risk Monitoring</td>
<td></td>
<td>Is the institution able to monitor how geographic and sectoral concentration is prone to climate-related and environmental risks ?</td>
<td>8,4</td>
<td>4</td>
</tr>
<tr>
<td>35</td>
<td>Risk Monitoring</td>
<td></td>
<td>Has the institution a pricing framework to support the chosen risk perspective and strategy (limiting exposures to sectors harmful for the environment or the climate) ?</td>
<td>8,5</td>
<td>2</td>
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<tr>
<td>36</td>
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<td></td>
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<td>5</td>
</tr>
</tbody>
</table>
Help institution have a brief overview on the maturity of current processes
Highlight areas of weaknesses
This heatmap should ease the institution while discussing with JST teams. Read with the heatmap below, it could help the institution to prioritize the actions to be initiated/continued.

- Practical and visual tool that should help the institution to frame a project and initiate necessary actions to implement an environmental and climate-related risks management framework.
- It can also be used to monitor project progress, by updating questions’ answer once tasks have been performed and documented.
Expert and methodological support in ALM, Finance and Risk around strategic risk management and management processes, governance of Finance and Risk functions, risk modeling and scarce resources (capital, liquidity) and stress tests.

- Our teams support CROs and CFOs from the design of target systems to operational implementation at Group or entity level.
- Our missions last from 1 month to 1 year. On average, they last 6 months.

4.1 AVANTAGE REPLY FRANCE

Service offer

- Strategic diagnosis, gap analysis and benchmarking
- Definition and design of steering processes and dashboard
- Organizational and governance redesign
- Deployment and operational implementation
- Modeling and Quantitative studies
- Subject matter expert support
4.2 AVANTAGE REPLY FRANCE
Environmental and Climate risk management service offer

Business and risk alignment
- Advice and challenge on integrating environmental and climate-related issues into business planning and risk management including risk appetite, corporate planning, product development, business model changes.
- Advice and challenge on embedding climate risk management into strategic processes.

Governance
- Gap analysis and options to implement a RACI approach for environmental and climate-related risks.
- Design and implementation of a dedicated environmental and climate-related risks risk management function.

Data quality and analytics
- Advice, analysis and challenge on data sourcing, quality and processing, and reconciliation relevant to the quantitative analysis for climate risk.
- Frameworks and tools for reviewing and challenging data outputs for climate risk quantification.

BMA and Risk Id
- Business model and risk driver analysis (mapping of activities, products, ...)
- Environmental and climate risk identification and definition (transition risk, physical risk, reputation risk...)
- Portfolio analysis and sensitivity to transition and physical risk (incl. sector/geographic exposures).

Risk measurement & management
- Design and implementation of “Climate quality index” to incorporate climate risk costs to credit risk models.
- Design and implementation of green/brown scorecard approach / green weighting factor (bonus/malus for RWA).

Stress testing / scenario analysis
- Advice and challenge on the end to end climate risk stress testing /scenario analysis including:
  - Interpreting and applying prescribed methodology.
  - Scenario generation linked to risks and business drivers.
  - Models and other approaches to projections.
Contacts

Nathanael Sebbag
Associate Partner

Reply France
3 Rue du Faubourg Saint-Honoré
75008 Paris - France
tel +33 (0) 1 70 23 08 74
mob +33 (0) 6 29 47 16 10
www.reply.com
n.sebbag@reply.com