



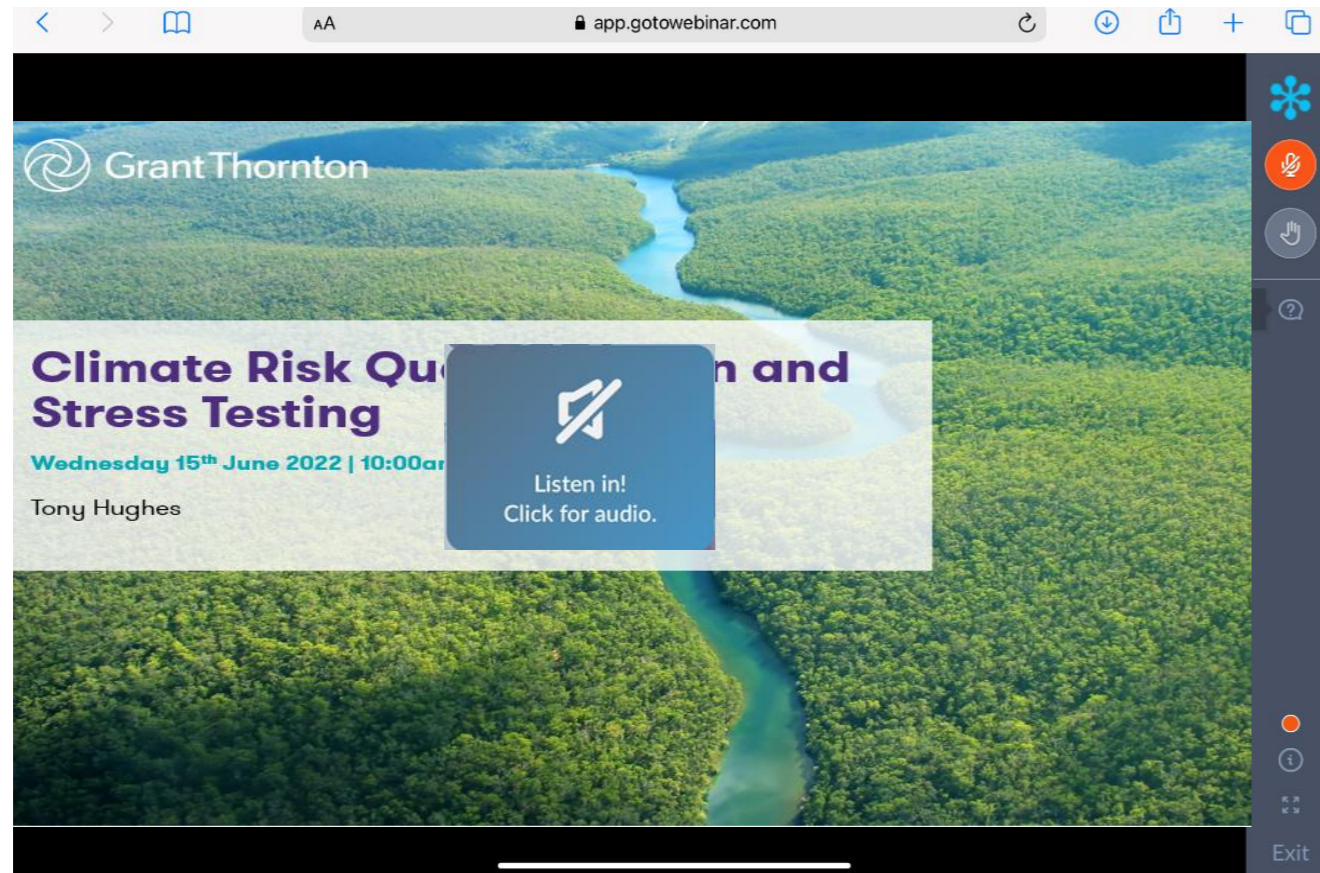
Climate Risk Quantification and Stress Testing

Wednesday 15th June 2022 | 10:00am–11:00am BST

Tony Hughes

Welcome and webinar housekeeping

GoToWebinar Housekeeping: Attendee Participation



Your Participation

Join audio:

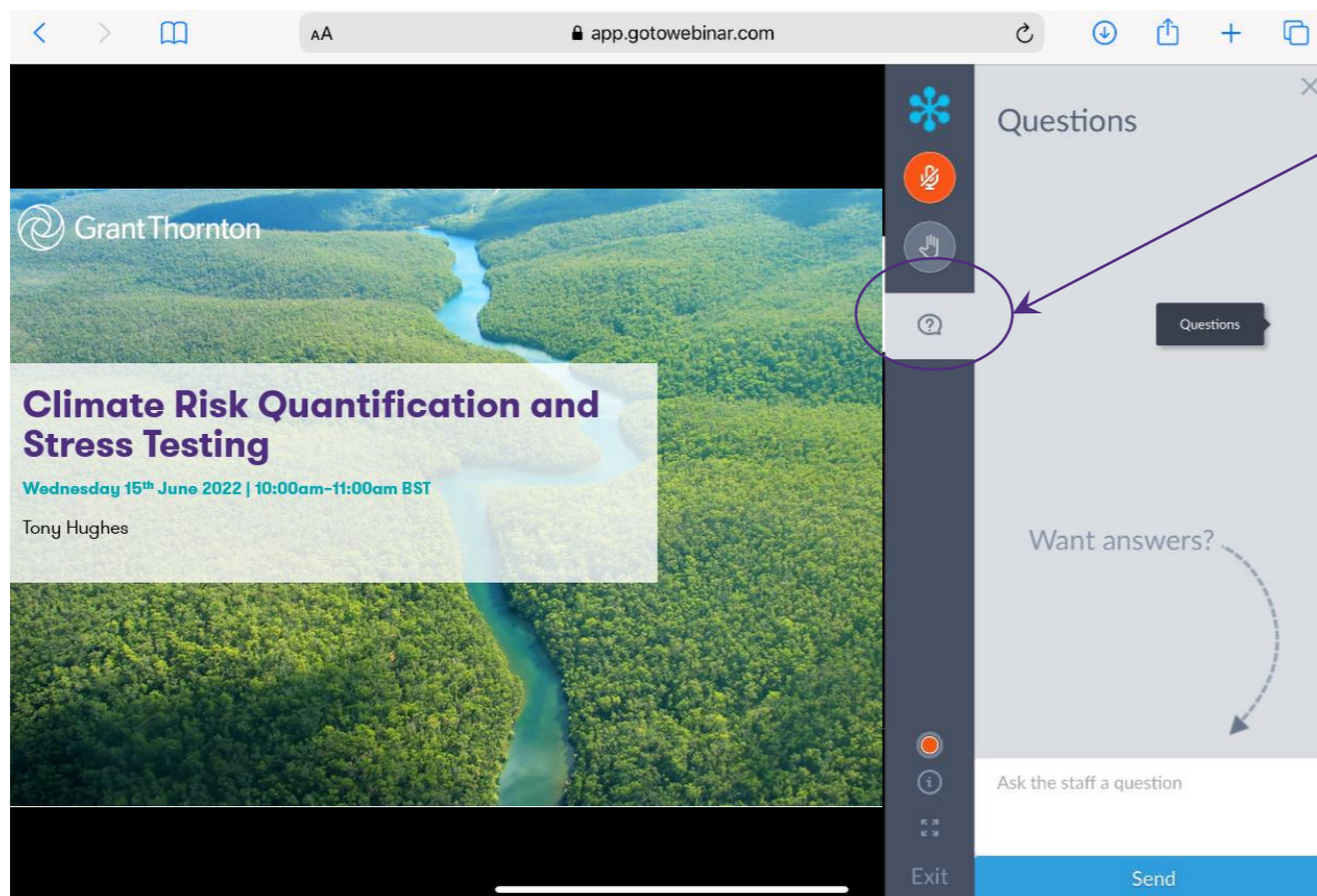
- Click on 'Listen in! Click for audio' in order to join the call.

Submit questions and comments via the controls panel.

Note:

Today's presentation is being recorded and will be provided to all those registered for the event.

GoToWebinar Housekeeping: Time for Questions



Your Participation

- Please continue to submit your text questions and comments using the controls panel.

For more information, please contact FSGEvents@uk.gt.com.

Introduction



Tony Hughes

Associate Director

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I've been a risk modeller and macroeconomist for the past 20 years. I currently work for Grant Thornton in London, engaged in consulting on modelling issues, corporate credit risk and ESG. Much of my career was spent in the U.S., though I am a native Aussie.

My primary speciality is credit risk – both wholesale and retail – but my career has been quite eclectic, covering a broad range of risk topics.

Over the past few years I have increasingly moved into ESG. I was invited to contribute the chapter on climate stress testing for an upcoming RiskBooks publication and I have been invited to present at conferences for both industry and academic audiences.

Prior to my work in industry I was an academic in Australia. I earned my Ph.D. in econometrics from Monash University in Melbourne.

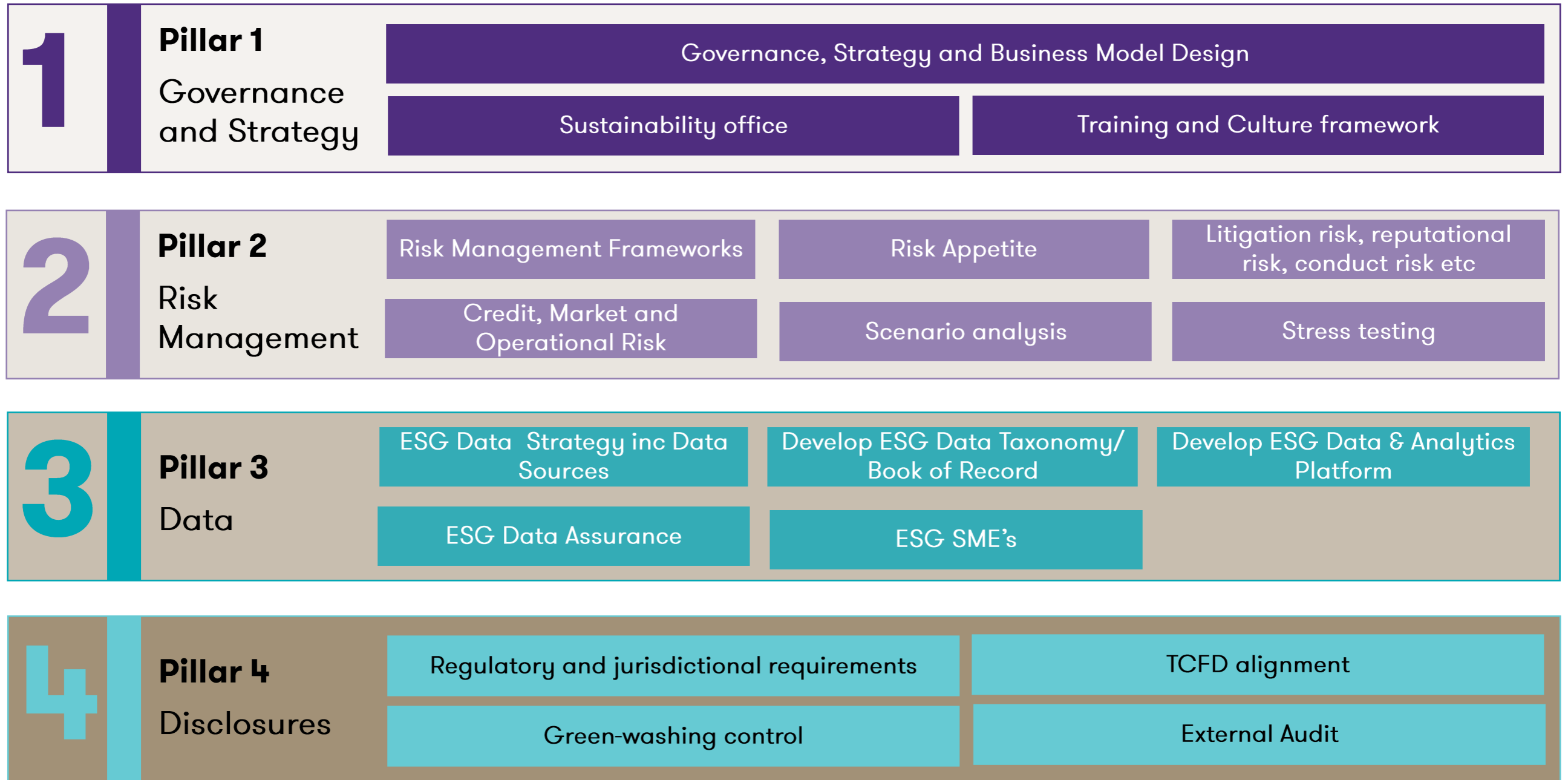
I have been a columnist for the Global Association of Risk Professionals (GARP) since 2018. Past articles are available here:

<https://www.garp.org/risk-intelligence/columns/risk-weighted>

I also blog extensively on LinkedIn. Recently the topic I have primarily addressed is ESG and climate stress testing. You're invited to check out my work:

<https://www.linkedin.com/in/hughesaw/>

Our approach to ESG - the 4 pillar structure



The Precautionary Principle & Bank Safety



The consequences of climate change are so devastating, we can't wait for the models to be perfect before acting...

But does the precautionary principle apply to questions of financial safety and soundness?

“Don’t you get it?” Two Key Questions at the Heart of Financial Climate Risk

Are banks at risk due to physical/transition risk?

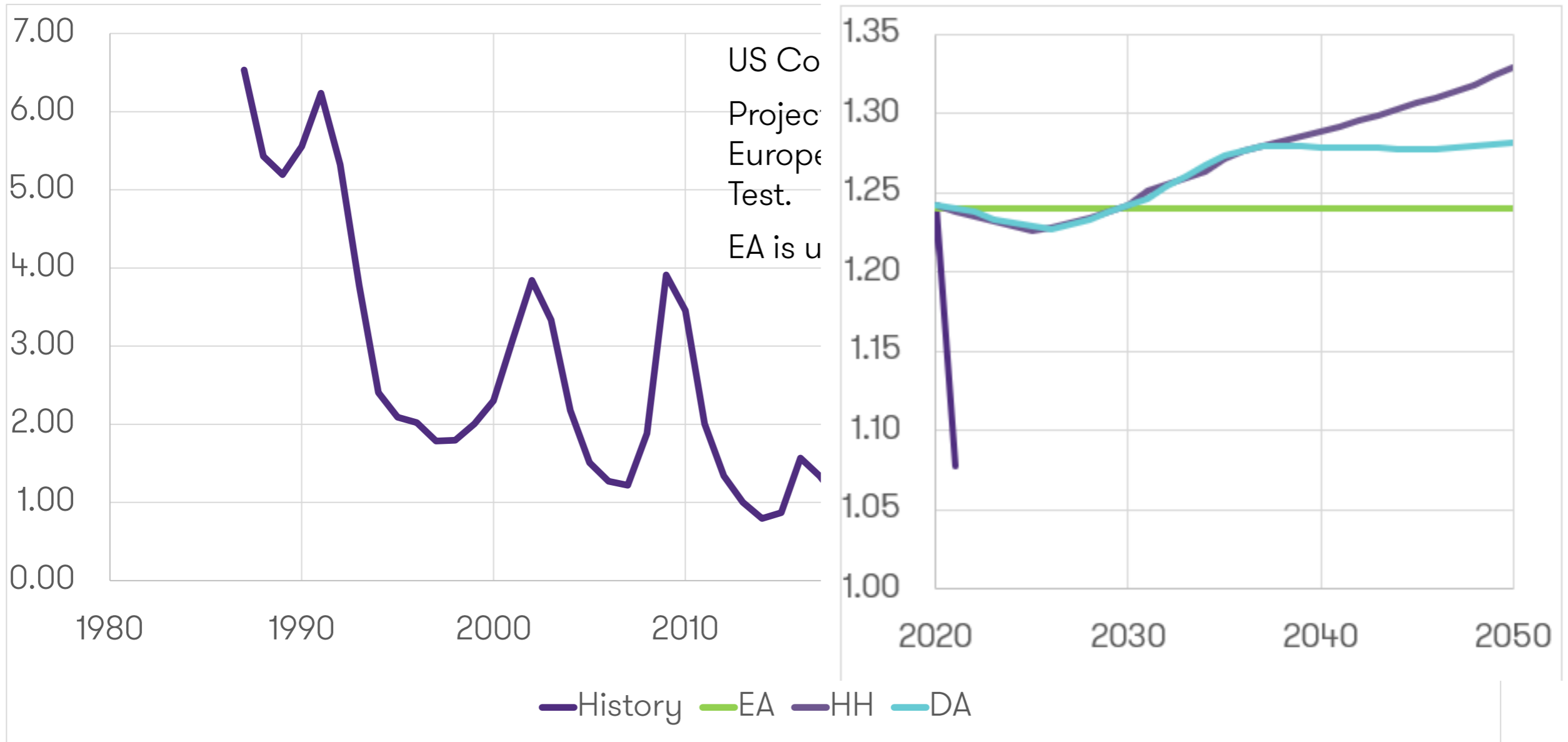
- This question concerns the **survival of banks**, not of people.
- The issues raised are **important** but not **existential**.
- Avoiding bank crises, regardless of the cause, will help us in the climate fight.
- Climate is not the most proximate threat for banks.

Can banks help us to combat global warming?

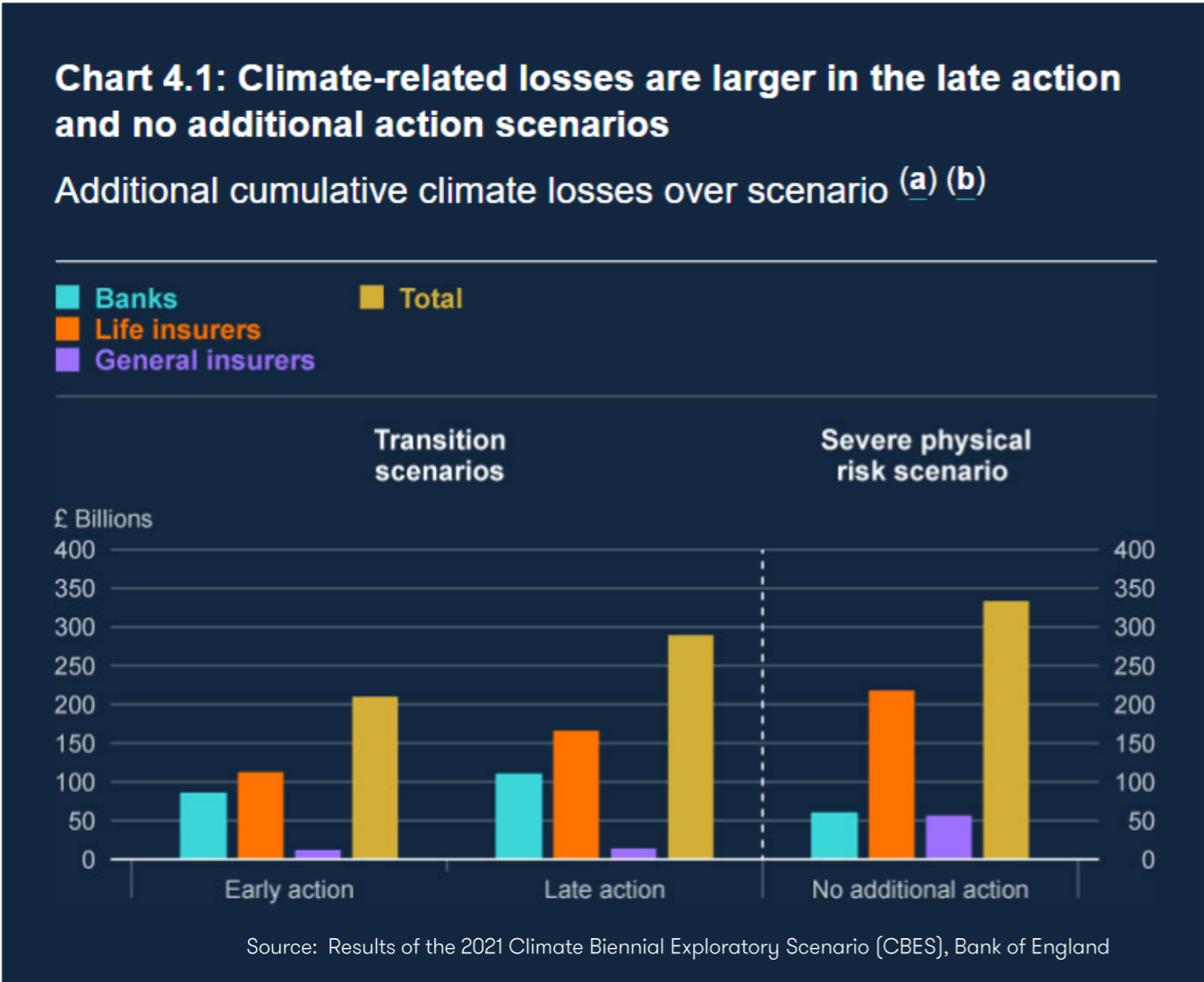
- Eg, Can disclosures help reduce global temperatures?
- I don’t know. Let’s do it!

Industry research should focus on the 2nd question, not the 1st.

2021 ECB Stress Results Were Not Economically Significant...



CBES: “...Costs of a transition to net zero look absorbable for banks and insurers.”



Report uses 3 scenarios “Early Action” (EA), “Late Action” (LA) and “No Additional Action” (NAA).

The CBES uses a “Counter-factual” (CF) baseline. “No additional headwinds from climate risks”

Cumulative bank credit losses were EA ~ £90b higher; LA ~ £110b higher; NAA ~ £60b.

A 10-15% drag on profits across the system. Insurers bear more of a brunt, so banks are more marginally impacted.

CBES Results Were Sharply Distinct From the ECB's Parallel Findings...

For wholesale loans, the ECB found that physical risks eventually dominate.

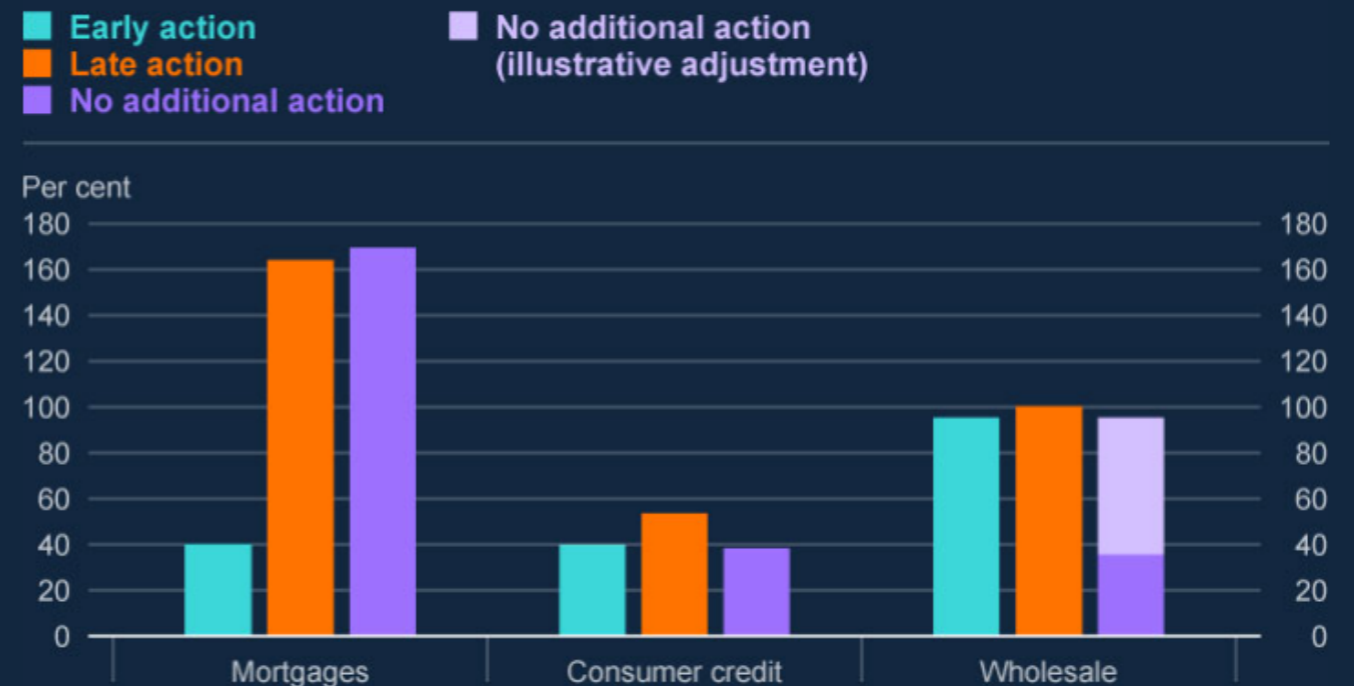
Scenarios use a static balance sheet assumption

Mortgage losses high due to energy refit. Physical losses mainly in 10% of post codes.

Consumer loans were relatively unaffected.

Chart 4.3: Climate impacts are highest for banks' wholesale and mortgage portfolios

Banks' climate losses as a proportion of counterfactual losses (a)
(b)



Source: Results of the 2021 Climate Biennial Exploratory Scenario (CBES), Bank of England

Do the results simply reflect the macro scenarios? What if banks could respond, dynamic balance sheet?

Some Notes on Sam Woods' CBES Speech

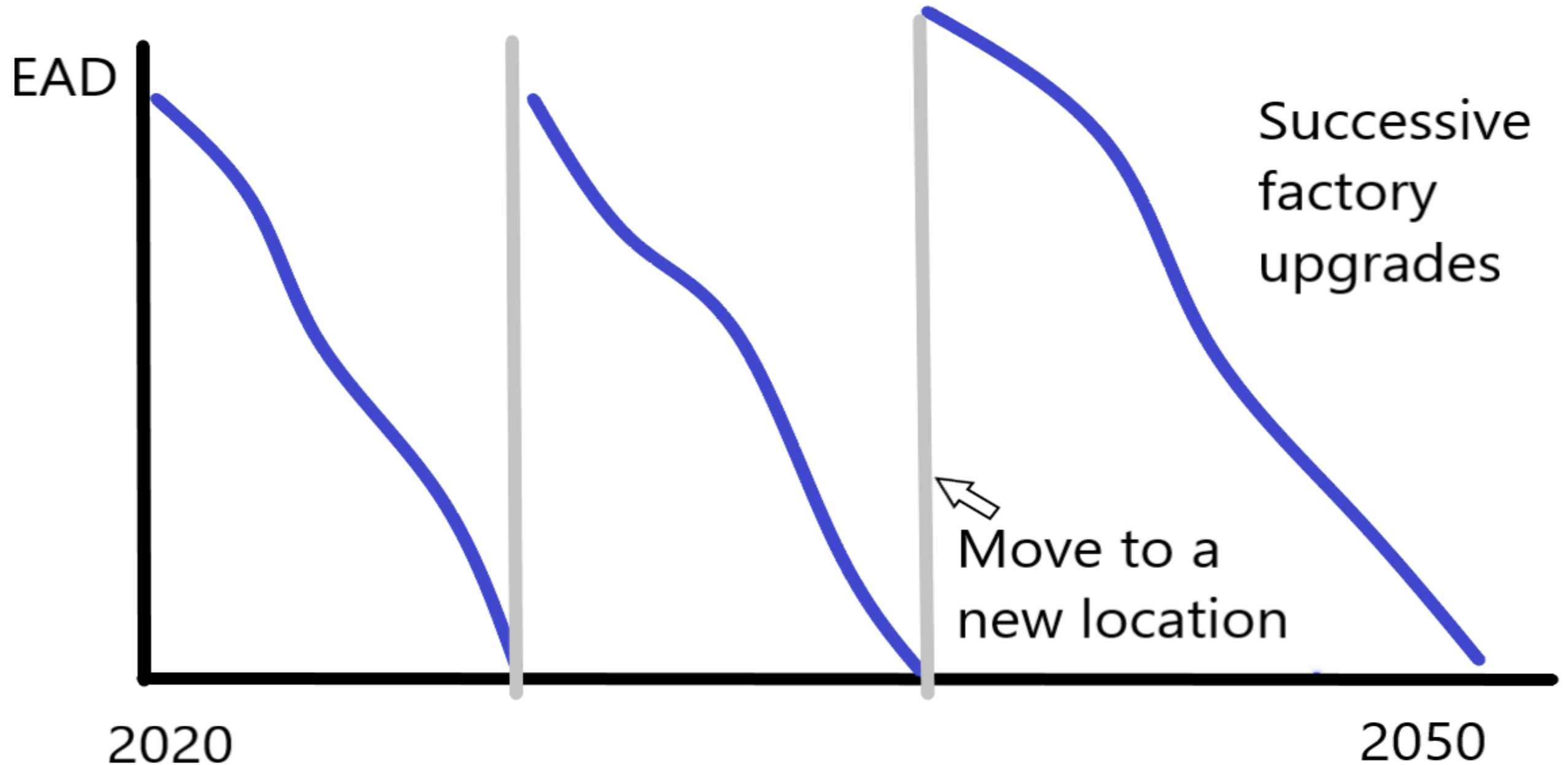
Will there be a climate related capital charge?

- Mr Woods seemed to scotch the idea: “don't think it is the best tool to address directly the causes of climate change.”
- Prefer to keep capital active in the fight to reverse CC.
- “Are current capital levels sufficiently high to guard against unexpected shocks during the transition?”
- Is there evidence that past recessions were worse due to CC?

Development of climate risk frameworks is moving ahead.

- Woods seems happy with the progress made in the industry
- Mooted the idea of using capital as a cudgel to get banks to take the issue seriously.

What's missing? Will Scenario Projections for Losses Become More Extreme in Future?



Questions?



Grant Thornton's upcoming events

Please email FSGEvents@uk.gt.com for more information

Event	Date/Time	Description	Registration link
Virtual Forum: Whistleblowing forum - measuring effectiveness	Tuesday 21 st June 10:00 am – 11:00 am	What does a good whistleblowing framework look like? Join us for insight and guidance on this essential element of risk management. You'll learn how to build a framework that protects people who raise concerns, and fits into your firm.	https://bit.ly/38h604J
Webinar: CPD Accounting Update - Appointed Representative (AR) regime	Wednesday 22 nd June 10:00 am – 11:15 am	How can firms prepare for the FCA's proposed changes to the Appointed Representative regime? Our panel looks at how the changes impact Principals' management and oversight of Appointed Representatives, from initial strategic decision to the termination of arrangement. You'll also find out more about the FCA discussion paper on regulatory hosting.	https://bit.ly/36Lmf9g
Event: The financial services NED network: Leadership	Wednesday 22 nd June 12:00 pm – 14:00 pm	The value of NEDs' leadership and independent insight is rising. Join our financial services NED network forum for an insightful lunch and get guidance on understanding and leveraging your leadership style.	https://bit.ly/3PAyCGY
Webinar: Regulation and risk management: emerging trends	Thursday 23 rd June 10.00 am - 11.00 am	Get insight on some of the challenges and emerging trends in regulation and risk management that we're actively advising banks on, including the impact of financial stress on credit risk models, such as IRB and Impairment calculations (IFRS9).	https://bit.ly/3NDvxE2
Webinar: Machine Learning and its application in Financial Industry	Wednesday 29 th June 10.00 am - 11.00 am	What is machine learning? And what does artificial intelligence mean for work? Join us to understand its benefits and risks, and get insight on how it may evolve, including potential regulation.	https://bit.ly/3NDvxE2