



EUROPEAN CENTRAL BANK

EUROSYSTEM

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Members of the European Parliament

European Parliament

60, rue Wiertz

B-1047 Brussels

Frankfurt am Main, 17 December 2021

L/CL/21/258

Re: Your letter (QZ-047)

Honourable Members of the European Parliament,

Thank you for your letter, which was passed on to me by Ms Irene Tinagli, Chair of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 10 November 2021.

The European Central Bank (ECB) acknowledges that the scale and irreversibility of the consequences of climate change call for immediate action from all stakeholders. Elected governments bear primary responsibility to address this issue and have more powerful tools to combat climate change than central banks, but all policymakers need to contribute within their own mandate and areas of competence. This is why climate change reflections were prominent in our recent monetary policy strategy review.

The action plan we announced in July this year presents a comprehensive roadmap for stepping up our involvement in matters relating to climate change.¹ It is a firm commitment by the ECB's Governing Council to consider climate change more systematically in its monetary policy framework. The ECB recently released an

¹ See the press release entitled "ECB presents action plan to include climate change considerations in its monetary policy strategy", available at: https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210708_1~f104919225.en.html.

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occasional paper on climate change and monetary policy in the euro area, which offers detailed insights into its analysis of the implications of climate change for the conduct of monetary policy in the euro area².

Let me mention some of the action points from the roadmap that directly relate to the aspects of monetary policy implementation raised in your letter.

As part of our action plan, in 2022 we will announce details of how we will introduce disclosure requirements for private sector assets as an additional eligibility criterion or as a basis for a differentiated treatment for collateral and asset purchases, taking into account EU policies and initiatives. The aim of the new requirements is to promote more consistent disclosure practices in the market, while maintaining proportionality through adjustments for small and medium-sized enterprises. We will also assess how to further adjust the framework guiding our corporate bond purchases in order to incorporate climate change criteria in line with our mandate. These criteria will include the alignment of issuers with, as a minimum, EU legislation implementing the Paris agreement, measured using climate change-related metrics or against issuers' commitments to such goals. In addition, by the first quarter of 2023 we will start disclosing climate-related information for our corporate sector purchase programme. Eurosystem committees are working exhaustively to develop the adjusted framework needed to support the next steps.

I would also like to point out that the ECB already includes climate change considerations in many aspects related to its market operations. The ECB regularly purchases green bonds under its asset purchase programmes, thereby supporting the efforts of firms and public entities to adopt more energy-efficient technologies and reduce their carbon footprint. We also monitor structural market developments related to sustainability products with the aim of supporting innovation within our mandate. For example, since the beginning of 2021 we have accepted certain sustainability-linked bonds as collateral for our monetary policy credit operations and for asset purchases.

Furthermore, we are already incorporating sustainability-related aspects into our non-monetary policy portfolios. For the ECB staff pension fund, we have replaced the benchmarks for equity funds with their low-carbon equivalents, which significantly reduces their carbon footprint. We have delegated proxy voting for equity investments to investment managers who have signed up to the United Nations Principles for Responsible Investment, requiring them to incorporate environmental, social and corporate governance standards into their voting policies. We also continue to explore further options to address climate change considerations within the pension funds. Moreover, for the ECB's own funds portfolio, we have steadily increased the share of green bonds, partly through investments in the euro-denominated green bond investment fund for central banks introduced by the Bank for International Settlements. In February 2021 the Eurosystem agreed on a common stance for climate change-related sustainable and responsible investment

² See "Climate change and monetary policy in the euro area", *Occasional Paper Series*, No 271, ECB, Frankfurt am Main, September 2021, available at: <https://www.ecb.europa.eu/pub/pdf/scpops/ecb.op271~36775d43c8.en.pdf?f26c937c8b72f2d321adc33893e17197>.

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principles for euro-denominated non-monetary policy portfolios³. This common stance will help all Eurosystem members to contribute to the transition to a low-carbon economy and to EU climate goals. It will increase the awareness and understanding of climate risks while promoting climate-related disclosures.

In the area of financial stability and banking supervision, the ECB regularly monitors and assesses climate-related risks for financial institutions and firms in its Financial Stability Review and in ECB/European Systemic Risk Board reports. In September 2021 the ECB published the results of its economy-wide climate stress test, which show the clear benefits to both banks and companies of acting early and ensuring an orderly transition to a green economy⁴. The results of the exercise will also be used to inform the 2022 supervisory climate stress test, which will be conducted by ECB Banking Supervision to test banks' preparedness to assess climate risks. Moreover, the ECB published its "Guide on climate-related and environmental risks" in November 2020 and, in 2021, asked banks to conduct self-assessments on the basis of the guide and to draw up action plans. The results, published on 22 November 2021, show that, while almost all banks have developed plans to improve their practices, the quality of these plans varies considerably and progress is still too slow⁵. In 2022 ECB Banking Supervision will conduct a full supervisory review of banks' risk management and disclosure practices. The results of this supervisory exercise, as well as the results of the supervisory stress test, will also be used to inform next year's Supervisory Review and Evaluation Process (SREP). Any impact on Pillar 2 requirements will be indirect and via the SREP scores.

Although we have been working to increase banks' risk management capabilities to deal with climate risks, we also believe that banks should incorporate structural changes in the economy to align to the Paris targets in their toolbox, to steer their business towards a smooth transition to carbon neutrality. For this reason, we are very pleased to see that the European Commission has proposed a legally binding requirement for banks to develop and disclose their own transition plans, with the ECB collaborating with other EU agencies in monitoring progress for an orderly transition. These transition plans are crucial, as they will highlight – at any point in time until 2050 – a bank's alignment and potential divergences with the relevant policy objectives through which the EU implements the Paris Agreement. Finally, the ECB is actively contributing to EU and international discussions on the possible revision of the prudential framework to address climate risks, particularly through the Task Force on Climate-related Financial Risks of the Basel Committee on Banking Supervision and the European Banking Authority's (EBA) Sustainable Finance Network.

³ See the press release entitled "Eurosystem agrees on common stance for climate change-related sustainable investments in non-monetary policy portfolios", available at:

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

⁴ See the press release entitled "Firms and banks to benefit from early adoption of green policies, ECB's economy-wide climate stress test shows", available at:

<https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210922~59ade4710b.en.html>.

⁵ See the press release entitled "Banks must accelerate efforts to tackle climate risks, ECB supervisory assessment shows", available at: <https://www.bankingsupervision.europa.eu/press/pr/date/2021/html/ssm.pr211122~6984de0ae5.en.html>.

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The ECB is of the view that further analysis is needed as a matter of priority, notably in the context of the EBA's mandate to report on whether and how regulatory capital requirements should reflect sustainability considerations.

Yours sincerely,

[signed]

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