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Why better sustainability disclosures matter for the covered bond industry

ECBC Plenary meeting - Helsinki

19 April 2023

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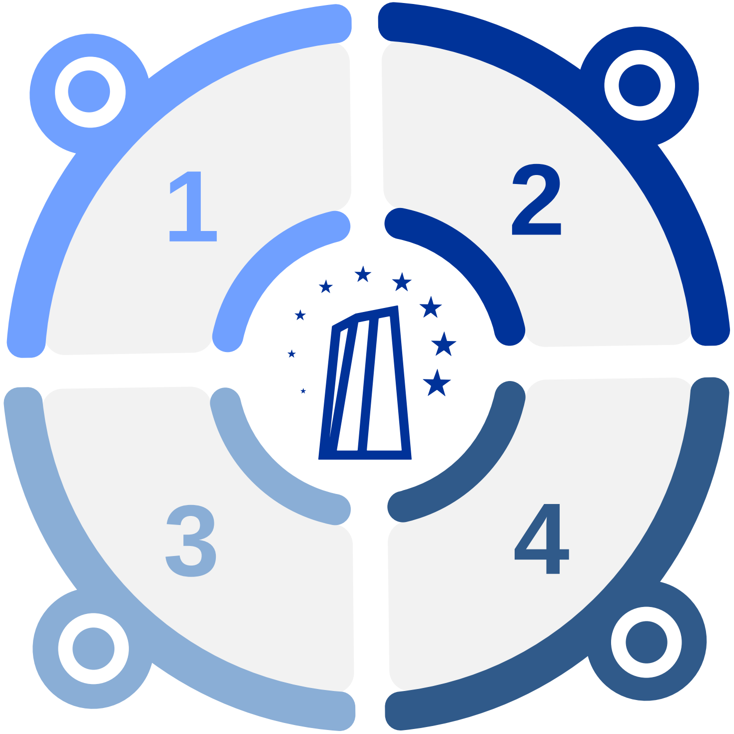
The views expressed are my own and do not necessarily coincide with those of the European Central Bank

Climate action in ECB monetary policy implementation



Corporate bond purchases

Adjustment of market capitalisation benchmark to account for climate change factors

Disclosure requirements

CSRD-based disclosure requirements for issuers

Promote harmonized climate disclosures for structured finance (not in scope of CSRD)*

Collateral framework

Collateral pool composition limits

Integrate climate change risks in haircut reviews

Risk management

Engage for more transparency in credit ratings

Common standards for Eurosystem in-house credit assessment systems

*CSRD – the EU Corporate Sustainability Reporting Directive

Joint work for better disclosures

- On 13 March, ECB and the ESAs* published a joint statement on **climate change disclosures for structured finance products**
  - Need to **enhance climate-data availability** amid investor demand for more transparency
  - Call on originators/issuers to **collect climate-data at loan origination** and fill existing templates voluntarily
  - Call for consistent and **harmonised requirements for similar instruments** (e.g. securitisations vs covered bonds)
- **Work is ongoing for securitisation**, with ESMA leading the **revision of the loan-level templates**, with the potential to include relevant metrics on climate-related risks
- **What about covered bonds?**

* **ESAs** = The European Banking Authority (EBA), the European Securities and Markets (ESMA) and the European Authority Insurance and Occupational Pensions Authority (EIOPA)

Covered bonds could be a trailblazer instrument

- Covered bonds could be a **pioneer in financing the green transition** and **boosting transparency on climate-related risks**
  - Provide funding for green transition where it matters; real estate
  - Manage risks via mortgages on higher energy efficient properties
  - Become a trailblazer in enhancing climate-related transparency

Some key questions:

1. What type of climate/energy-related information is most relevant?
2. Are there trade-offs between green use-of-proceeds vs the climate-related risks of the underlying cover pools or loan vs pool-level reporting requirements?
3. How to close data gaps e.g. for new and existing real estate backed mortgages?

What data are needed to assess climate-related risks in real estate assets?

- Relevant metrics on climate-related **transition** and **physical** risks are tied to the type of assets in cover pools: mostly residential real estate assets
- Requirements underpinning most regulations (EU taxonomy, Pillar 3 disclosures, SFDR…) boil down to a limited number of **basic metrics:**
  - **Energy Performance Certificate (EPC) label**
  - **Energy efficiency** (kWh/m2/y)
  - **GHG emissions**
  - **Location** (physical risks)
- **Such data is still scarcely collected, non-harmonised and access may differ across countries** (e.g. due to data protection legislation)

- Revised **EU Directive on the energy performance of buildings (EPBD) will facilitate access** to data on energy performance and harmonise EPC ratings to some extent…**but more could be done.**

Data details and trade-offs?

- **Use-of-proceeds vs information on cover pool?**
  - **Complementary concepts** that are both relevant
  - Use of Proceeds ➔ measuring climate impact especially for green covered bonds / in line with the approach taken under the EU Green Bond Standard
  - Cover pool info ➔ assessing climate risk of all cover pools for risk management purposes

- **Loan-level vs pool-level information?**
  - Reporting is more challenging for covered bonds than for ABS due to revolving cover pools causing higher operational complexity.
  - Loan-level info is anyways necessary for proper pool-level disclosures
  - Main focus should be on getting actual data

How to close the data gap for real estate backed mortgages?

- The lack of actual data on energy efficiency of buildings and physical climate risks constitutes the main obstacle for properly assessing climate-related risks
- **Getting actual data has first priority** – and banks/issuers play a crucial role:

Stock of existing loans	Flow of new loans
• Relevant for a long time due to slow churn • Strategy needed to **collect real data** • Where real data is not available: accurate and transparent **proxy models**	• Incorporate climate-data collection in **loan origination process** • Allow for **data to be updated** during mortgage lifetime

➢ Filling ECBC's HTT/HDT templates on a voluntary basis (also based one data collected for pillar 3 disclosures) already improves transparency for investors

Concluding remarks

- **Climate Change** does not recognise national or regional borders but is a global challenge – we have to and we can tackle it jointly
- We all have a role within our mandates and **covered bonds could be a pioneering asset class in financing the green transition and boosting transparency on climate-related risks where it matters**; in real estate
- **Covered bond issuers, investors and supervisors would all win from greater transparency via more harmonised metrics and reporting templates,** which help to pave the way towards a more sustainable future