BBVA comments on BCBS principles for the effective management and supervision of climate-related financial risks

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BBVA welcomes the Basel Committee on Banking Supervision's publication of *principles for the effective management and supervision of climate-related financial risks* and appreciates the opportunity to give its feedback to the related public consultation.

BBVA is a customer-centric global financial services group founded in 1857. The Group has a solid leading position in Spain, is the largest financial institution in Mexico, and has leading franchises in South America. It is also the leading shareholder in Turkey's Garanti BBVA and has an important investment, transactional and capital markets banking business in the U.S. BBVA is committed to sustainable development. Helping our clients transition towards a sustainable future has been defined as one of the strategic priorities of the Group.

Financial Institutions have an important role to play in the achievement of a net zero economy, not only by accompanying our clients in their transition, but also by ensuring the financial resilience to ESG risks through their integration in the banks' risk management. However, climate-related financial risks, which are rightly recognised by the principles as drivers of existing risks, are new and there is a high level of uncertainty around them.

BBVA is therefore pleased to share some general remarks regarding the principles proposed by the Basel Committee:

- Several authorities, such as the ECB, have already issued supervisory expectations for climate-related risk management by banks. In this fast-evolving context and potentially fragmented landscape, the global alignment of prudential and supervisory standards is key. We therefore welcome the development of a common baseline for internationally active banks, which is necessary to ensure a level playing field for market players. We believe supervisors and banks can indeed benefit from the Committee's guidance to foster alignment and a common understanding in terms of supervisory expectations for addressing climate-related risks.

- Regarding scenario analysis, BBVA recognizes the usefulness of such a tool to fulfill climate risk analysis. The design of different climate scenarios makes it possible to disentangle the uncertainty around climate change and its multiple repercussions across the economy and the financial system. The convergence around the NGFS set of scenarios as the reference for the industry is welcome. However, huge challenges remain for a novel process with chief differences with traditional stress tests, with data and modeling capabilities under construction.

Additionally, a staggered approach for climate stress testing exercises, starting with climate risk rather than with a more comprehensive approach on all types of risks derived from climate change, would be welcome.

- The integration of climate-related financial risks in the risk management frameworks is still at an early stage. Banks are still facing challenges linked to integrating climate-related risks into banks' strategies, governance and risk management processes, including the lack of the necessary data, methodologies and information to design such strategies. The integration into the Supervisory Review and Evaluation Process (SREP) of the climate Stress Test exercises and the potential capital impact via Pillar 2 is therefore premature and should be avoided in the short term. Before introducing any effective prudential measure, time and accurate guidance are needed, as well as a solid risk-based empirical analysis. Rushing and pushing in excess can be a source of transition risk for banks. We would therefore recommend a phased approach for the introduction of climate-related risk management expectations.

- A special remark should be devoted to the lack of empirical analysis and guidance on the transmision channel related to operational risk. This drawback has been already recognized by the Task Force on Climate-related financial risks in its different pieces of work[1]. Additionally, another source of concern comes from the consideration of strategic and reputational risk within the operational risk framework.

To conclude, risk understanding and management is key for the development of sustainable finance. Therefore, BBVA welcomes and supports the development by the Basel Committee of a common baseline for the effective management and supervision of climate-related financial risks. Global alignment of prudential frameworks and standards is key. Taking into account that banks are still at an early stage in the process of integrating such risks in their strategies, governance and risk management, we encourage the BCBS to take a phased approach and to take into consideration the developments already achieved in other jurisdictions. The translation of this work in progress into binding requirements could be premature and consideration should be paid to its communication to the market, in order to avoid misunderstandings.

[1] see, for instance, BCBS (2021): Climate-related risk drivers and their transmission channels.