

# Randal K Quarles: Disclosures and data - building strong foundations for addressing climate-related financial risks

Speech by Mr Randal K Quarles, Vice Chairman for Supervision of the Board of Governors of the Federal Reserve System, at the Venice International Conference on Climate Change, Venice, Italy, 11 June 2021.

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## Introduction

Thank you for inviting me today. It is an honor to be here and, after more than a year of remote conversations, it is truly wonderful to see so many people in person.

As Chair of the Financial Stability Board (FSB), I have the privilege of collaborating with the Italian G20 Presidency, the G20 Finance Ministers and Central Bank Governors, and with the FSB membership on the most pressing issues affecting financial stability.<sup>1</sup> Among those issues, one of increasing focus is understanding and monitoring climate-related financial risks. Given the global nature of climate change, this demands a coordinated international effort.

The FSB published last Wednesday a Climate Roadmap that presents a comprehensive and coordinated plan to address climate-related financial risks. The FSB's roadmap dovetails with the ongoing work of the G20 Sustainable Finance Working Group (SFWG) to develop a broader sustainable finance roadmap.

Today, in my role as Chair of the FSB, I would like to focus on the two foundational components of the FSB roadmap: disclosures and data. Globally consistent, comparable, and reliable disclosures, as well as a broader set of high-quality, relevant data, together, can provide the basis to assess climate-related financial risks and the impact on financial stability.

## Disclosure

The FSB was an early leader in bringing attention to the importance of reliable, entity-level disclosures to assess and manage climate-related financial risks and opportunities. In 2015, the FSB submitted a proposal to the G20 to create an industry-led disclosure task force on climate-related risks.<sup>2</sup> The work of this FSB-sponsored Task Force on Climate-related Financial Disclosures, or TCFD, has led to greater recognition of the importance of climate-related financial risk and of comparable and reliable disclosure. The early development of industry-led recommendations and a usable framework by users and producers of this information was critical. The four core elements of the TCFD recommendations have provided a widely accepted framework for disclosures—covering governance, strategy, risk management, and metrics and targets. The task force has continued to provide significant support to those seeking to disclose and has encouraged steadily increasing uptake. These initial steps greatly helped to define appropriate parameters, drive towards consistency, and give the public sector a running start in developing their own approaches.

Now it is time to build on that work. It will be useful to establish a globally consistent baseline standard for climate-related disclosures. Globally consistent and comparable entity-level disclosures by non-financial companies, banks, insurers, and asset managers are increasingly important to market participants and financial authorities as a means of providing information needed to assess and manage risks.

The G20 Presidency, in developing its 2021 work program, asked the FSB to encourage more consistency in disclosure practices. As a start, the FSB surveyed what financial authorities across our membership were doing to promote disclosures. Almost all our members have

already set requirements, guidance, or expectations or plan to do so. We found some heterogeneity in the approaches they were taking. Some members prefer mandated disclosure while others would make it voluntary. There is also variation in the desired scope of disclosures. However, there is a trend towards an important baseline that focuses on one-way materiality—or the financial risk that climate change could have on a particular entity—based on the TCFD recommendations. The majority of our membership are already using the TCFD recommendations as a baseline for their own requirements or guidance.

The International Financial Reporting Standards Foundation (IFRS), in consultation with other international organizations, will develop a set of standards, starting initially with climate and building upon these TCFD recommendations. As reflected in our December 2020 statement, the FSB supports IFRS's advancement of an International Sustainability Standards Board to take this work quickly forward.<sup>3</sup> This work holds the promise of providing baseline standards that could inform or be built upon by national authorities as they develop their approaches to climate-related financial disclosure or broader sustainability disclosure.

The initial focus of the IFRS will be on climate standards, while allowing for interoperability with individual jurisdictions' frameworks, that may go beyond climate-related impacts. Consistency in one-way disclosures would provide a needed avenue for accurate and appropriate risk assessment and comparability to assess investment decisions. Simultaneously, the IFRS standards are intended to provide flexibility for national authorities to build on the baseline. The "interoperability" feature will allow jurisdictions to address broader or jurisdiction-specific concerns in a manner consistent with their legal and regulatory frameworks, and indeed to go further in scope or faster if they wish. Given the importance of this work, we encourage the IFRS to press forward as quickly as possible. In the interim, the FSB continues to encourage jurisdictions that are implementing frameworks to base them on the TCFD recommendations to avoid unnecessary fragmentation.

## **Data**

The need for high quality, reliable data doesn't stop at firms' disclosures, however. International initiatives are needed to improve data quality and address data gaps, and ultimately to establish a basis of comprehensive, consistent, and comparable data for global monitoring and assessing climate-related financial risks. We published a separate report on this topic last week.

Our data needs include data on the underlying drivers of physical and transition risk and financial institutions' exposures. The challenges here are considerable. To understand the financial risks, better information is needed on the underlying physical risks, including the sorts of extreme weather events that pose greatest risks to the balance sheets of households, firms, and financial institutions. Comparable data is also needed on the nature of jurisdictions' climate-change targets and progress in meeting them. All this information needs to be related to financial risks—including financial institutions' exposures to non-financial counterparties.

This is not an easy task. The current lack of usable data is a reflection of difficulties in transforming existing information on the drivers of climate risk into reliable metrics that quantify financial risks. The key here is to find metrics that are forward-looking, recognizing that the nature and magnitude of future climate-related risks may differ from those in the past.

Improved financial risk data can also help achieve the financial stability mandates of financial authorities. For example, the FSB is exploring how to assess the degree to which climate-related risks might be transferred or amplified by different financial sectors, including the interdependence of banks and insurance firms. Climate-related risks vary across jurisdictions, and we need to look at how risks might be amplified by feedback loops with the real economy. Such analysis will contribute to a more comprehensive and global understanding of how to assess climate change and potential effects on the financial system, but those efforts are

hampered by a variety of data limitations.

The FSB is working with international bodies, such as the International Monetary Fund, and other international groupings, such as the Network for Greening the Financial System (NGFS), to assess climate data gaps and to identify steps to address them, with a special emphasis on ensuring cross-sectoral and international consistency. For example, the FSB plans to coordinate work with the NGFS on the issues surrounding scenario analyses, which some jurisdictions are using or contemplating, and the financial metrics that would be useful for such an analysis, both at the level of the firm and the overall system. Examining scenario analysis presents many challenges: A very long time horizon—which requires dynamic balance-sheet analysis—and the need to capture the interplay between the macro-economy and drivers of climate-related risks are two such challenges that would need to be overcome.

## Conclusion

Today, the FSB is well-positioned to lead in the next phases of the work required to assess and address climate-related financial risk. The FSB's mandate, its diverse membership, and its connection to the G20 make it the ideal forum to forge a consensus on the appropriate path forward. The FSB, as laid out in its roadmap, has taken on a critical role in coordinating and carrying forward work that will make the global financial system more resilient to the threats posed by climate change. The roadmap establishes a strategic vision for addressing climate-related financial risks, which sets out how we will coordinate with other standard-setting bodies and international organizations in order to progress towards our goal. Our Climate Roadmap leverages the FSB's strength as a coordinating body, provides some structure to the vast amount of work on climate-related financial risks currently going on internationally, and clarifies interdependencies between workstreams and between issues.

The Climate Roadmap sets the course and promotes consistency through, among other things, building consensus around common principles, best practices, and cross-jurisdictional alignment. These include the two broad objectives that I have focused on today—establishing consistent, comparable, and reliable information through a global baseline standard for disclosures and through improving the availability and quality of data. The roadmap also includes work on analytical tools and policy approaches developed for identifying and managing climate-related financial risks. We have a long road ahead of us, but every journey begins with the first steps. The FSB will continue to leverage its strengths to coordinate and contribute to understanding and addressing the challenges to the financial system that arise from these risks.

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<sup>1</sup> The views expressed in these remarks are those of the speaker in his role as FSB Chair and do not necessarily reflect those of the FSB or its members.

<sup>2</sup> See [www.fsb.org/2015/11/disclosure-task-force-on-climate-related-risks-2/](http://www.fsb.org/2015/11/disclosure-task-force-on-climate-related-risks-2/).

<sup>3</sup> See [www.fsb.org/2020/12/the-implications-of-climate-change-for-financial-stability-2/](http://www.fsb.org/2020/12/the-implications-of-climate-change-for-financial-stability-2/).