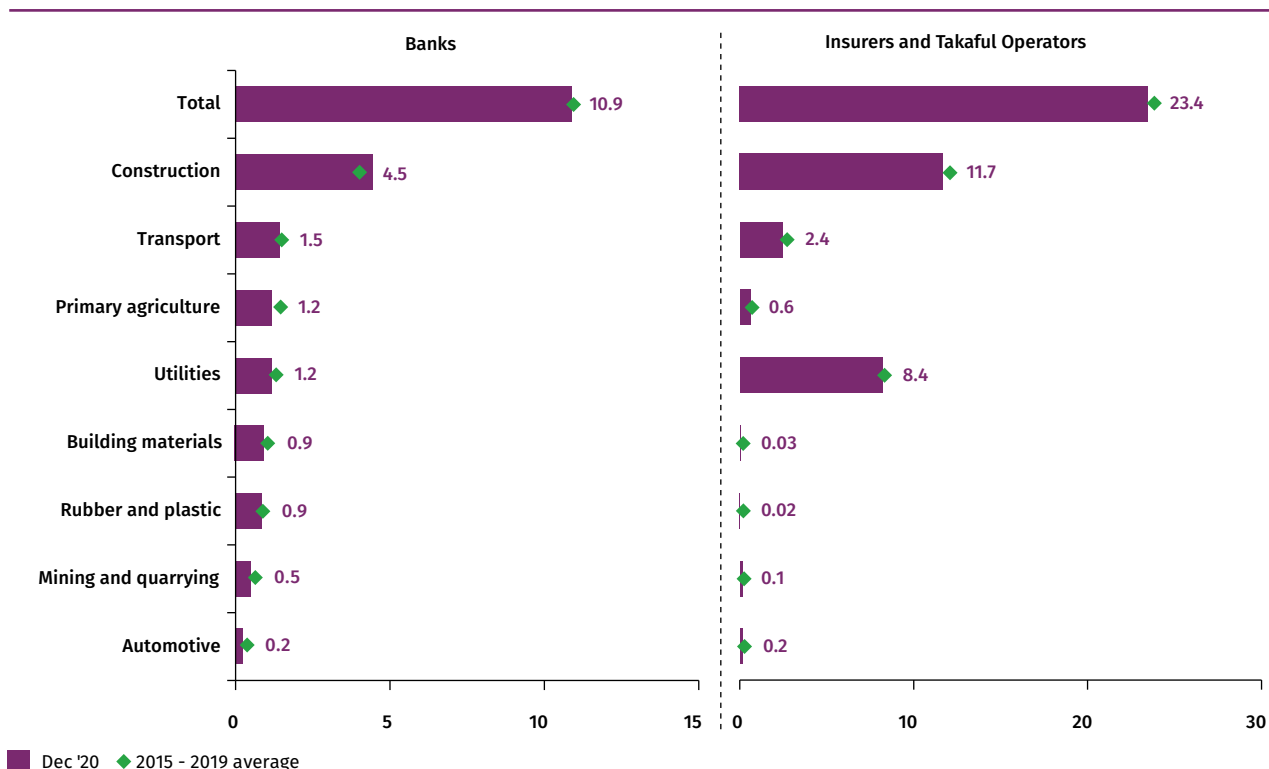


Climate Risk Management by Financial Institutions

Financial institutions have made progress in responding to climate-related risks. More financial institutions have begun to formulate their long-term strategies towards sustainability. These include rebalancing their portfolios, given the implications of potential climate risk exposures on their core lending, insurance businesses, deposit taking, and derivatives as well as investment activities (Chart 2.17). Increasingly, financial institutions are also promoting and helping their customers to adopt sustainable practices through their lending, advisory and/or investment activities.

Chart 2.17: Exposures of Malaysian Financial Institutions in Sectors Potentially Exposed to Climate Change (as % of Total Assets)



Note: 1. Construction includes civil engineering works and construction of residential and non-residential properties; utilities includes power and water; transport includes land, water and air transport; primary agriculture includes mainly palm oil
 2. Figures refer to exposures as at end-December 2020. Exposures are based on existing reporting requirements and will be refined upon full implementation of the Climate Change and Principle-based Taxonomy






Source: Bank Negara Malaysia estimates

Following increased supervisory engagements with financial institutions since early 2020, positive developments have been observed in efforts by financial institutions to incorporate climate risk considerations in their strategies and operations. This included aligning governance arrangements, customer onboarding practices, disclosures and product solutioning (Diagram 2.3).

In 2021, the Bank will continue to work with the industry to further support strengthened climate risk management and disclosure practices. A key priority will be the implementation of the Climate Change and Principle-based Taxonomy (CCPT), and ongoing development of sectoral guides for the manufacturing, oil and gas, infrastructure and construction sectors. Work will also continue on producing additional practical resources to help financial institutions better evaluate and manage climate-related risks (Diagram 2.4). With finalisation of the taxonomy, financial institutions will begin capturing exposures based on the CCPT for internal risk management and supervisory purposes. This will help support risk management, scenario analysis, stress testing and disclosures. Initiatives to encourage greater adoption of climate-related disclosure by financial

Diagram 2.3: Key Developments Observed in Financial Institutions

Climate-related risk management is gaining traction but at an uneven pace across the industry

	Key observations	Leading initiatives
 <p>Governance & strategy</p>	<ul style="list-style-type: none"> Stronger leadership by Board and senior management on the need to integrate climate-related considerations in business strategies and decisions, and risk management practices 	<ul style="list-style-type: none"> Established dedicated teams and senior management sponsors for climate-related initiatives Specific focus on climate risks as permanent agenda in Board and management committee meetings
 <p>Policy & framework</p>	<ul style="list-style-type: none"> Increasing integration of climate-related considerations into risk management framework and practices 	<ul style="list-style-type: none"> Established group climate risk framework and policies, and risk appetite Subjecting segments of customers to climate risk assessments including in underwriting practices Climate risks embedded in enterprise wide risk management. Developed transition risk management framework for effective monitoring and management of credit risk
 <p>Capacity building</p>	<ul style="list-style-type: none"> Greater focus on enhancing staff awareness and technical capabilities 	<ul style="list-style-type: none"> Established structured training roadmap for staff Hired subject matter experts to provide technical support and expedite knowledge development
 <p>Product development & solutions</p>	<ul style="list-style-type: none"> Introduction of new products such as sustainability-linked loans, insurance/takaful cover for weather and climate risks, and preferential rates for purchase of green products and solutions 	<ul style="list-style-type: none"> Preferential rates for renewable energy technology Invested in alternative technologies and relevant infrastructure projects to support climate risk mitigation and adaptation
 <p>Reporting & disclosure</p>	<ul style="list-style-type: none"> More financial institutions committing and taking active steps to adopt the TCFD recommendations and better quality disclosures 	<ul style="list-style-type: none"> Embarked on data collection initiative Developed Malaysia Flood Catastrophe Modeling to enhance risk monitoring and reporting

More financial institutions have become signatories to the United Nations Environment Programme Finance Initiative Principles for Responsible Banking as well as Principles for Sustainable Insurance

Source: Bank Negara Malaysia

institutions in line with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations, as well as to expand the range of financial products, solutions and activities that support sustainable activities, will be pursued as part of the work of the Joint Committee on Climate Change (JC3). The JC3 will also establish a dedicated workstream to identify and bridge gaps in climate- and environmental-related data required by financial institutions to support risk assessments. In addition, efforts to scale up capacity building programmes for industry players to accelerate their knowledge and skill sets in climate risk management will continue (refer to the BNM Annual Report 2020 for further information on the role and initiatives of the Bank in addressing climate-related financial risks).

Diagram 2.4: Key Achievements in 2020 and Priorities in 2021

Supported by collaboration with industry and partners through the Joint Committee on Climate Change and Value-Based Intermediation Community of Practitioners to promote an orderly transition

**2020
Key Achievements**



Pilot implementation of Climate Change and Principle-based Taxonomy



Conducted assessment on disclosure practices of financial institutions and gaps against the TCFD recommendations



Increased awareness on climate risk-related areas among the public and industry through awareness and education programmes



Consultation on Value-Based Intermediation Financing and Investment Impact Assessment Framework (VBIAF) sectoral guides on renewable energy, energy efficiency and palm oil

**2021
Key Priorities**



Finalisation and implementation of Climate Change and Principle-based Taxonomy



Issuance of industry consultative paper on Guides for Climate Risk Management and Scenario Analysis, and TCFD Application Guide



Finalisation of VBIAF sectoral guides on renewable energy, energy efficiency and palm oil



Issuance of VBIAF sectoral guides consultative documents on manufacturing, oil & gas and construction & infrastructure



Scale-up capacity building programmes

Source: Bank Negara Malaysia