2024 | ISSUE 8

THE ONSIDE

ONCI's Credit Intelligence Magazine for Commercial Banking Leaders

NOTES FROM THE SECOND LINE OF DEFENSE

Advancing the frontiers of climate risk management

Meet Eric Wischman, M&T Bank's Climate Risk Officer

SEC

SEC climate disclosure rules finalized – what does it mean for your bank?

ON CLIMATE

The climate journey – from ideation to innovation

OAKNORTH BANK
Pioneering Climate Risk Management

Winner of the 2024 Celent Model Risk Manager Award for Emerging Risks

ON Climate by ONci has given OakNorth Bank the ability to assess climate transition risk on its loan book, allowing its climate and credit risk teams to:

- Calculate financed emissions across the commercial loan book without collecting emissions data
- Mitigate regulatory risk by identifying climate risk in loan books early, allowing the creation of effective climate transition risk strategies
- Incorporate climate risk measurement into regular loan book management and underwriting processes.

Read more about the award-winning partnership

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INSIDE THE ONSIDE

RISHI KHOSLA

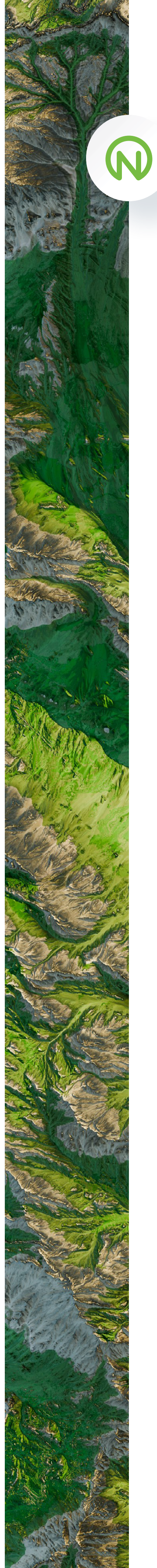
IN 2023, THE U.S. EXPERIENCED 28 EXTREME weather and climate disasters costing at least $1B – the highest number on record – and a significant jump on the 18 that occurred in 2022. The total cost of these 28 events was almost $93B – an extraordinary sum which puts into sharp focus, the huge investment needed to effectively manage and mitigate the risks of climate change.

At OakNorth, we're keenly aware of this and the existential threat it poses to countless commercial banking customers, which is why, at least twice a year, we convene dozens of leading, innovative commercial banks via our Climate Consortium, to share learnings, ideas, and best practices. In March, we held two such meetings – one for the largest U.S. banks, and one for community banks – to discuss the impact of the Securities and Exchange Commission's recent adoption of rules to enhance and standardize climate-related disclosures.

As Eric Wischman, M&T's Climate Risk Officer and the focus of this issue's cover feature, aptly puts it, the objective of such discussions is to make progress in the right places. He and his team at M&T, which is an ON Climate customer and a member of the ON Climate Consortium, aren't trying to prove or disprove what people feel about climate change, but simply want to help the bank make informed, data-driven decisions that lead to successful outcomes for them and their customers. A worthy objective that is setting a leading example for the industry.

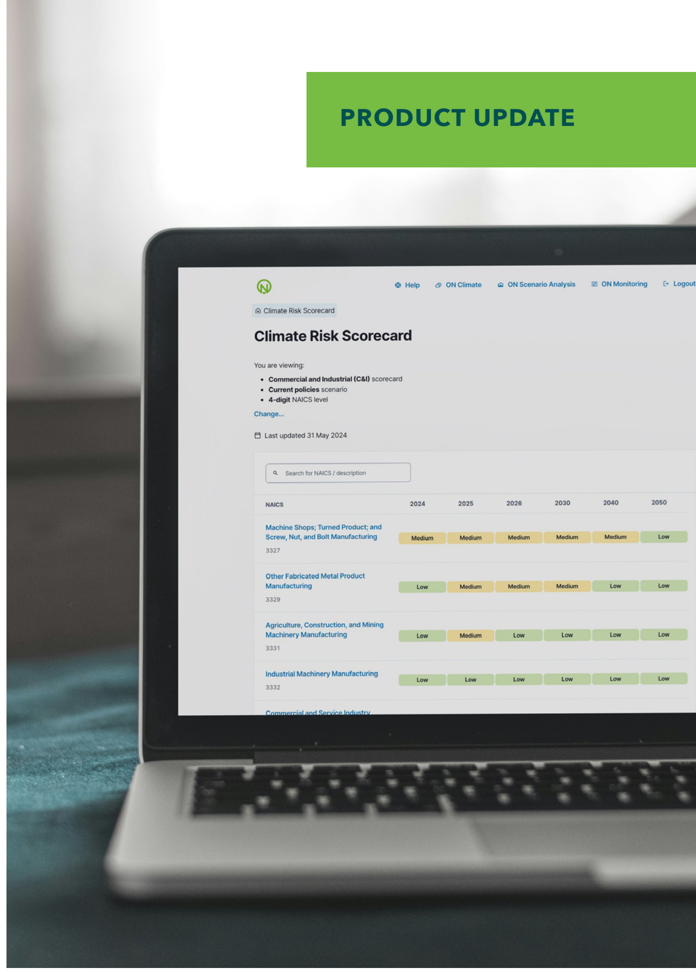
We are proud to be supporting M&T and other leading financial institutions such as PNC and Fifth Third on their climate journeys, and will continue to work with them and others to turn this challenge into a significant opportunity.

We hope you enjoy this latest issue of the ONside.



INTRODUCING THE CLIMATE RISK SCORECARD

Get a clear view of transition risk across your commercial loan book



Features

- **Tailored C&I scorecards** Available at both NAICS 4-digit and 6-digit detail
- **CRE risk evaluation** Specific for seven property types across every US state
- **Climate forecasts** Annual climate risk projections up to 2050 for each industry and property type
- **Understanding transition drivers** Gain insight into the factors driving your risk scores
- **Regular updates** Our scorecards are updated quarterly to keep you informed

Comprehensive coverage

Analyze climate risks for...

— Commercial & Industrial (C&I) portfolio across all industries with material emissions, at both 4-digit and 6-digit NAICS levels

— Commercial Real Estate (CRE) portfolio for seven property types across all 50 U.S. states

Actionable insights

— Evaluate the drivers that underpin each industry's transition risk score

— Benchmark existing internal climate risk assessments

— Identify which industries and property types to focus on, using climate scenarios including those required by the Fed's Climate Scenario Analysis (CSA)

Enhanced decision-making

— Prioritize the industries, geographical regions, and property types requiring deeper analysis based on climate transition risk levels

— Integrate climate risk within credit risk management and across business lines by leveraging an easy-to-use climate risk scorecard

Why choose our Scorecard?

Proven Expertise

Advanced Technology

Seamless Integration

Proven Track Record

Cost-Effective

Regulatory Alignment

Learn more about the latest ON Climate enhancement

NOTES FROM THE SECOND LINE OF DEFENSE

Advancing the frontiers of climate risk management

M&T BANK WAS FOUNDED IN BUFFALO, NEW YORK IN 1856 AS THE "Manufacturers and Traders Trust Company". Since then, it has grown to one of the 20 largest banks in the country with over $200B in assets. Yet despite being almost 170 years old, the bank has demonstrated a clear appetite to invest and innovate when it comes to new challenges.

We were delighted to get some time to sit down with M&T's Climate Risk Officer, Eric Wischman, to learn more about his role and how he's helping lead the bank's climate risk efforts. In this wide-ranging interview, we discuss how to build climate confident teams, the unique skillsets needed to build a strong climate risk team, and what commercial banking leaders starting out on this journey at their institutions should be considering.

Q: Eric, many thanks for finding some time to sit with us. To kick us off, please can you describe your role as Climate Risk Officer at M&T?

A: My role is focused on ensuring M&T integrates climate risk into all the elements of its risk infrastructure. This includes: credit risk, operational risk, liquidity, market, interest rate, reputational, and strategic risk. My goal is to ensure the bank is doing this in a prudent and reasonable way in the spirit of maintaining its safety and soundness, as well as the broader financial system in which it operates.

My primary objective is to make progress in the right places. I don't try to prove or disprove how others feel about climate change, the intent of our activities is to ensure the bank continues to make informed, data-driven decisions that lead to successful outcomes in the year ahead.

We've gone through a robust risk identification process within M&T, looking at both physical and transition risks, assessing where we think our resources need to be applied, and what risks we feel are most pressing in the near and long term. This helps drive prioritization of activities across different areas of the bank, and ensures we have a clear picture of the type of data and analysis we need to help solve different challenges.

Q: As you note, climate risk touches so many different areas of risk, so where exactly does your role sit within the bank and how do you interact with its different departments?

A: My role sits within the risk division, the second line of defense within the enterprise risk function of the bank. It's so interdisciplinary and it's helpful to have a person in that role who has a good understanding of all the different risk pillars in the bank, how they work, how they interact, and the logical places to start with integrating climate risk. We established a climate risk working group made up of interdisciplinary individuals from across the organization. This ensures everyone is receiving and hearing the same message, understands the priorities, and are allocating resources based on where prioritization is needed.

Q: What are the biggest challenges in your role?

A: Getting access to the right data and intelligence is a significant challenge – the methodologies that are needed to sufficiently identify, measure, and monitor climate risk are continuing to evolve. We understand this is a difficult problem to solve, but climate is a potential material emerging risk which is why it's so critical the industry works together to figure it out.

Q: This isn't a role you see in many institutions which demonstrates M&T's leadership in this area. How did you come into this role and what about your career path prior to this helped set you up for success in it?

A: I received an environmental science degree from college, so I was convinced I was going to be outdoors and performing field work. Things didn't really turn out that way, so I immediately obtained an MBA after graduating hoping that I'd work in an environmental remediation company – if not in the field, then perhaps on more of the business side. I interviewed and successfully landed my first job at M&T Bank. That was 23 years ago, and I've been here ever since, working across a range of roles in risk management. I spent about a decade in Bank Secrecy Act / Anti Money Laundering (BSA/AML), including two years as M&T's BSA/AML Officer. I then moved into a role where I was responsible for helping the bank build its first risk appetite statement, enterprise risk framework. This involved working closely with the Risk Committee of the Board and Executive Management, ensuring they received appropriate risk reporting from an enterprise-wide perspective. So, when the bank said it wanted to create a climate risk role, I became the natural choice because of my enterprise risk experience, deep risk management experience, and my academics.

When I started my career in banking over two decades ago, I honestly never thought I'd get the opportunity to work in anything related to the environmental sciences, so it feels in some ways like I've come full circle.

Q: What skill sets are needed to build a strong climate risk team?

A: The team needs to have individuals who understand the subject matter and science around climate, as well banking. They also need to be able to get organizational buy-in on a topic and make progress when there's many competing priorities and other challenges. This is why strong communication skills, good stakeholder management, institutional knowledge, and the ability to get comfortable outside the confines of a business-as-usual environment, are critical.

We've chosen to develop and nurture talent internally as there aren't many people in the industry yet who are subject matter experts on this. What we've found to be more important is finding people who really understand the bank and have the willingness and appetite to learn about climate risk.

Q: In 2023, there were 28 extreme weather events in the US where the damage caused exceeded $1B. This was up from 18 in 2022. How useful is historical data such as this in assessing future risk?

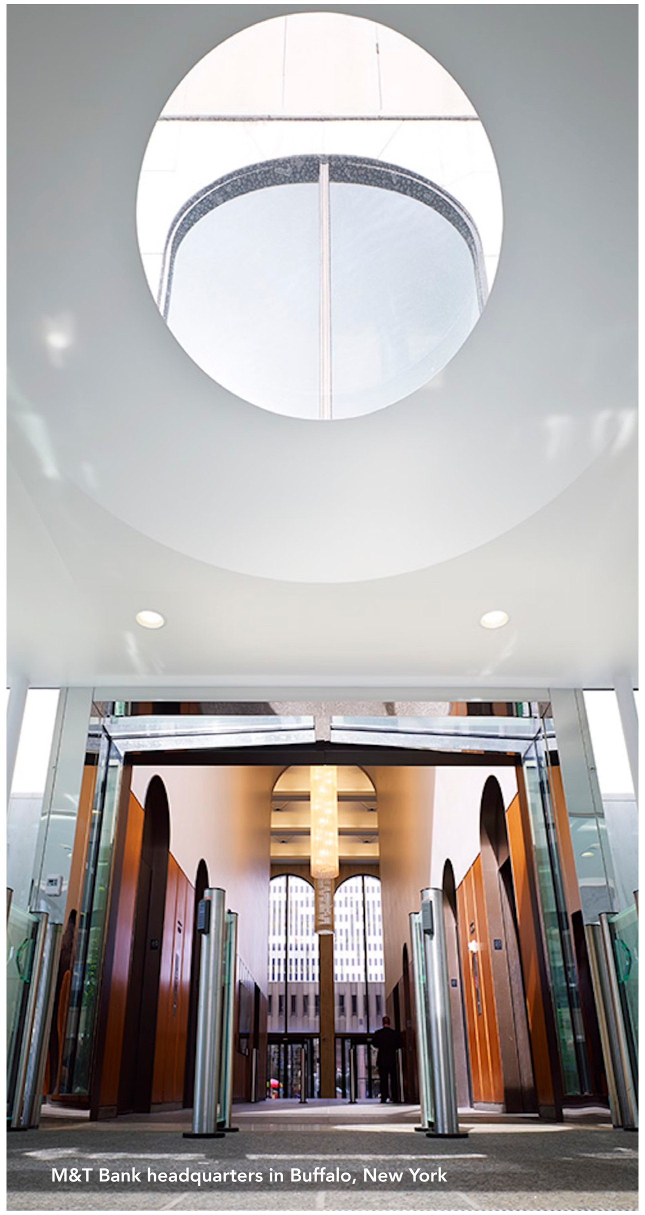
A: As with all risk management, historical reference points can be helpful, but it's also important to take a forward-looking view. Climate risk takes this to an extreme, which the financial services industry is not familiar with executing. From a capital planning perspective, financial institutions are required to use nine quarter forward looking models. From a climate standpoint, we're at times looking at decades. So, building preparedness though leveraging multiple different scenarios to measure transition risk over time is important.

Q: What advice and learnings can you share with other commercial banking leaders that are just starting out on this journey in their institutions?

A: Explore measurement tools and look at scenario analysis from both the short and long term, as it can help assess where the potential issues are or could be in the commercial loan book. Specific to transition risk, start speaking with relationship teams as they're going to be the ones on the front line who understand customers best and will support customers in their transitions in the future.

Q: What role do partnerships with companies such as OakNorth play in your climate risk strategy?

A: OakNorth has been an important partner for us, as it's providing a product that would be difficult for us to build internally from a time and resource perspective. The information provided by ON Climate is useful in helping us determine how to think about transition risk. The team has also been responsive and receptive to feedback we have about how the product can be improved, which is great as it means we can work collaboratively to improve outcomes for our institution and our customers.


M&T Bank headquarters in Buffalo, New York

FEDERAL RESERVE CLIMATE SCENARIO ANALYSIS RESULTS

Unpacking Banks' Preparedness in Managing Climate Risk

THE FEDERAL RESERVE CONDUCTED a pilot climate scenario analysis (CSA) exercise in 2023, asking six of the top US banks (Bank of America Corporation; Citigroup Inc; The Goldman Sachs Group, Inc.; JPMorgan Chase & Co.; Morgan Stanley; and Wells Fargo & Company) to participate. The aim was to understand the participants' climate risk-management practices and challenges and to enhance their ability to identify, estimate, monitor, and manage climate-related financial risks.

The Fed CSA pilot involved both a transition and a physical risk module. Banks estimated the climate impacts on corporate, commercial real estate, and residential loans. The exercise shed light on banks' governance, climate data challenges, existing framework limitations, and risk exposure estimations. Areas of focus included: analyses across various time horizons, chronic risks, indirect impacts, insurance dynamics, scenario design, and risk management capabilities.

KEY TAKEAWAYS

TRANSITION RISK MODULE

- Participants used a combination of macroeconomic variables from the NGFS scenarios, baseline emissions data, and their own internal assumptions as a part of their credit risk modeling
- Participants faced significant challenges in modeling the macroeconomic and sectoral implications of different transition pathways, relying on third-party vendors' climate frameworks, databases, and proxies to complete analyses
- Translating climate impact into climate-adjusted credit risk parameters (e.g. PD/LGD) required a scenario analysis framework that extended d own to the obligor-level in order to forecast climate-adjusted financials

PHYSICAL RISK MODULE

- Participants assessed the risk of direct and indirect impacts from multiple physical perils across various regions using hazard estimates ranging from property to zip code-level
- A range of internal and external data gaps were highlighted, requiring data from third-party vendors to estimate building characteristics, repair costs, and insurance premiums
- Participants leveraged existing credit risk models to determine how physical shocks could affect credit risk parameters for individual loans

OUR APPROACH TO MEASURING CLIMATE RISK

It's clear that climate scenario analysis is fundamental to translating transition and physical climate-related risks into financial impact at the portfolio and obligor level. Designing and building a climate scenario analysis framework requires robust data sets (internal and external), modeling capabilities, and subject matter expertise.

ON Climate enables banks to quantify climate impact through automated climate scenario analysis, leveraging banks' internal data sets, NGFS assumptions, and our ONCI climate database to overcome data challenges and existing framework limitations. Our solutions range from a climate risk scorecard to analyze risk concentrations to forecasted climate-adjusted financials at the obligor/property level to drive climate-adjusted credit risk parameters.

Understand climate risk in your portfolio today, by leveraging our climate risk scorecard.

SEC CLIMATE DISCLOSURE RULES FINALIZED

What you need to know

The SEC voted on Wednesday March 7th to adopt final rules requiring disclosure of certain climate-related risks and emissions. There's a lot of detail to unpack - some of the key components that will be relevant for commercial banks to follow.

WHAT IS REQUIRED UNDER THE RULES?

The final rules will require disclosure of:

- Climate-related risks that have a material impact on business strategy, results of operations, or financial condition;
- Where activities to mitigate or adapt to a material climate-related risk have been taken, description of expenditures incurred and the resulting impact on financial estimate/assumptions;
- The use, if any, of transition plans, scenario analysis, or internal carbon prices;
- Oversight by the board of climate-related risks, and role of management in assessing and managing these risks;
- Processes for identifying, assessing and managing material climate-related risks, and whether and how this is integrated into overall risk management system/processes;
- Information about climate-related targets or goals, impacts on financial estimates and assumptions as a result of such target/goal, and action to make progress towards meeting such target/goal;
- For large accelerated filers (LAFs) and accelerated filers (AFs), information about material Scope 1 and Scope 2 emissions; an assurance to report thereon;
- The capitalized costs, expenses, and losses incurred as a result of severe weather events and other natural conditions (e.g. hurricanes, tornadoes, flooding, drought, wildfire, extreme temperatures and sea level rise).

WHAT HAS CHANGED?

Compared to the draft rule released in 2022:

- Only LAFs and AFs need to disclose Scope 1 & Scope 2 emissions – no requirement for others
- No requirement to disclose Scope 3 emissions (including financed emissions)
- "Material" as qualifier throughout – including for Scope 1 & 2 emissions

SEC

WHO DOES THIS COVER & WHEN DOES IT COME INTO PLACE?

All SEC-registered firms are covered - with compliance date depending on the status of the filer as LAF, AF, non-accelerated filer (NAF), smaller reporting company (SRC), or emerging growth company (EGC). See following table for details:

COMPLIANCE DATES UNDER THE FINAL RULES[1]

Registrant type	Disclosure & Financial Statement Effects Audit		GHG Emissions/Assurance			Electronic Tagging
	All reg. S-K & S-X disclosures, other than as noted in this table	Item 1502(d) (2), Item 1502(e)(2), & Item 1504(c)(2)	Material Scope 1 & 2 GHG emissions	Limited assurance	Reasonable assurance	Inline XBRL tagging
LAFs	FYB 2025	FYB 2026	FYB 2026	FYB 2029	FYB 2033	FYB 2026
AFs (other than SRCs & EGCs)	FYB 2026	FYB 2027	FYB 2028	FYB 2031	N/A	FYB 2026
SRCs, EGCs, & NAFs	FYB 2027	FYB 2028	N/A	N/A	N/A	FYB 2027

[1] As used in this chart "FYB" refers to any fiscal year beginning in the calendar year listed.
[2] Financial statement disclosures under Article 14 will be required to be tagged in accordance with existing rules pertaining to the tagging of financial statements. See Rule 405(b)(1)(i) of Regulation S-T.

Item 1502(d)(2) will require a registrant to describe quantitatively and qualitatively the material expenditures incurred and material impacts on financial estimates and assumptions that, in management's assessment, directly result from activities to mitigate or adapt to climate-related risks disclosed pursuant to Item 1502(b)(4).

Item 1502(e)(2) will require a registrant to describe a transition plan if it has adopted the plan to manage a material transition risk.

Item 1504(c)(2) will require a registrant to disclose any progress toward meeting a disclosed target or goal (under 1504(a)) and how such progress has been achieved.

THE TIME TO PREPARE IS NOW

Given the final rules differ in many aspects to the SEC's initial proposal, we would recommend reading the SEC's useful four-page factsheet, if you're not inclined to read the full 885-page document. With regard to timings, the reporting deadline for FY 2025 is the March 1st, 2026, and given the large amount of information that will be required, banks need to start preparing for climate-related disclosures right away.

Recommended next steps commercial lenders of all sizes should look to implement:

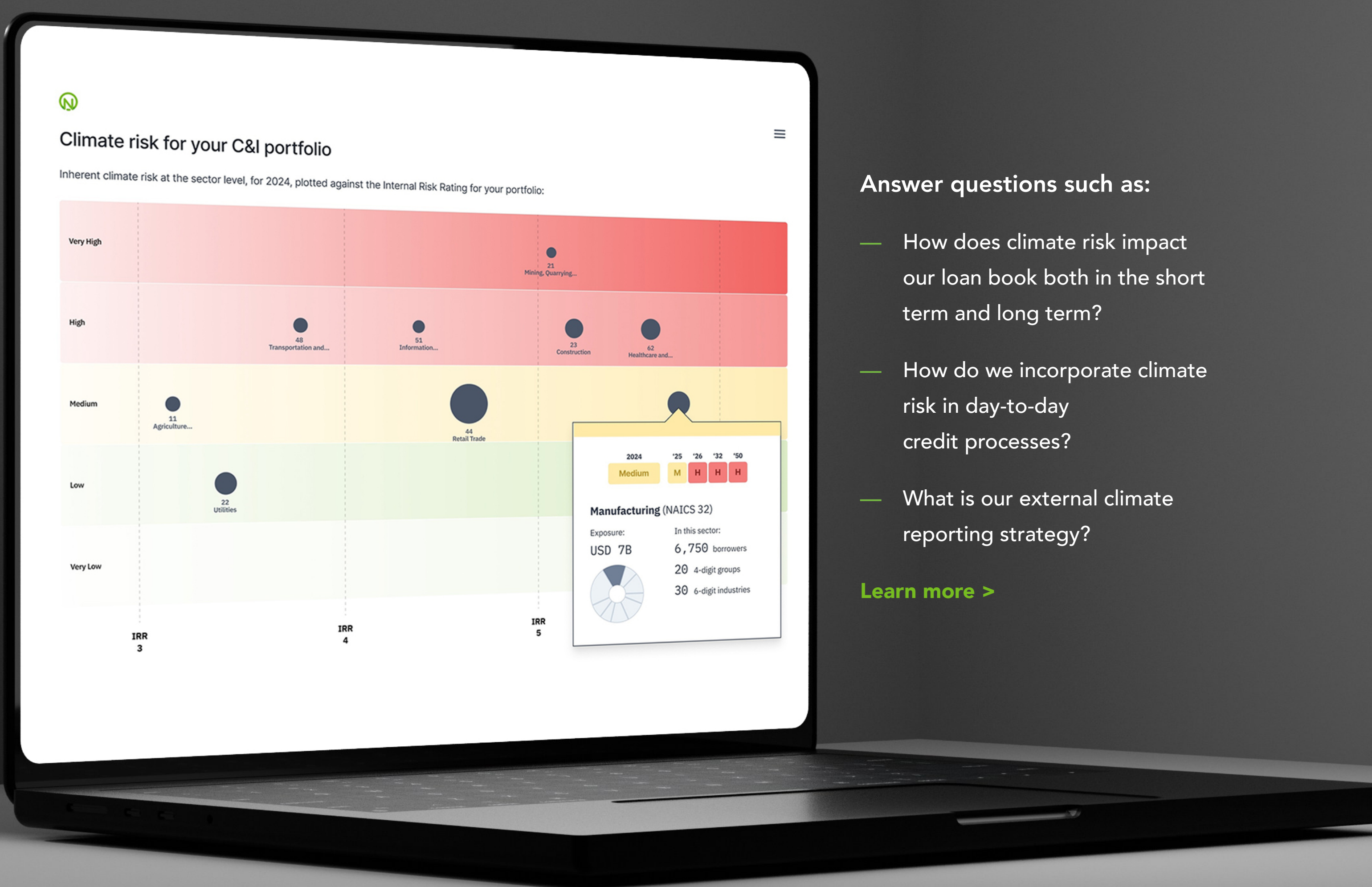
- Run climate scenario analysis models across entire loan books, including in both the short and long term;
- Partner with colleagues across different functions, such as finance, sustainability / corporate responsibility, who will be responsible for preparing climate disclosures;
- Benchmark, continue discussions with peers, and liaise with industry bodies to help inform standards for material climate risk disclosures.

ONCI

Now available in ON Climate

How can your bank incorporate climate risk into its day-to-day credit processes?

Aligned with the latest guidelines from the US Federal Reserve, banks can now assess climate risk impact (financed emissions and transition risk) on their loan book annually, from 2023 to 2050, at a borrower, industry, sector, and loan book level.



Answer questions such as:

- How does climate risk impact our loan book both in the short term and long term?
- How do we incorporate climate risk in day-to-day credit processes?
- What is our external climate reporting strategy?

Learn more >

Lend smarter. Lend faster. Lend more.