"Practices and Issues on Climate-related Risk Management" (June 2025)

Overview

- ✓ FSA complied the report which illustrates practices and issues of financial institutions in addressing climate-related risks, building on the "Supervisory Guidance on Climate-related Risk Management and Client Engagement"(2022).
- ✓ Based on initiatives in approximately **20** financial institutions ("FIs", including major/regional banks and life/non-life insurance companies)

Key Findings

(details in the next page)

- ✓ FIs have progressed their practices in four areas: Strategy and Governance, Recognition and Assessment, Risk Management, and Client Engagement
- ✓ Yet, they face challenges as well, such as
  - ➢ Quantification of climate-related risks and integration into conventional risk management framework
  - ➢ Tough dilemma: financed emission would temporarily increase when they finance their clients to support their transition to net zero

Next Steps

- ✓ FSA will continue to hold discussions with FIs regarding their climate-related risk management and client engagement.

FSA also considers that specific measures to address climate-related risks would differ depending on the size and characteristics of FIs.

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Strategy and Governance

Practices

- Consider climate-related risks as one of the material risks and formulate strategies to achieve set targets
- Establish sustainability-dedicated committee
- Conduct internal audit on climate-related issues

Issues

- Conversion of long-term climate-related strategies to business plans and day-to-day operations
- Consistency with clients' strategy and with Paris Agreement
- Knowledge gap among staffs

Recognition and Assessment

Practices

- Identify transmission channels of climate change
- Utilize qualitative risk assessments and climate scenario analysis

Issues

- Micro-level, detailed company-by-company analysis
- Utilization of the results of analysis in client engagement and loan/investment decision-making process

Risk Management

Practices

- Integrate climate-related risks into the Risk Appetite Framework (RAF)
- Monitor exposures/emissions
- Reflect clients' initiatives in internal ratings, borrower classifications, and engagement policies

Issues

- Integrate into conventional risk management frameworks such as setting and enforcing hard limits on capital or risk amounts, due to
  - High level of uncertainty
  - Insufficient non-financial data and underdeveloped methods

Client Engagement

Practices

- Not divest immediately but engage with high-emitting clients to reduce climate-related risks/emissions
- Provide various solutions, including finance provision, to clients according to their needs and phases

Issues

- Raise awareness among clients, especially small and medium-sized enterprises
- Temporally increase in FEs due to transition finance
- Ensuring profitability and a balanced risk-return profile