

## Q4 2023 Pillar 3 ESG reporting

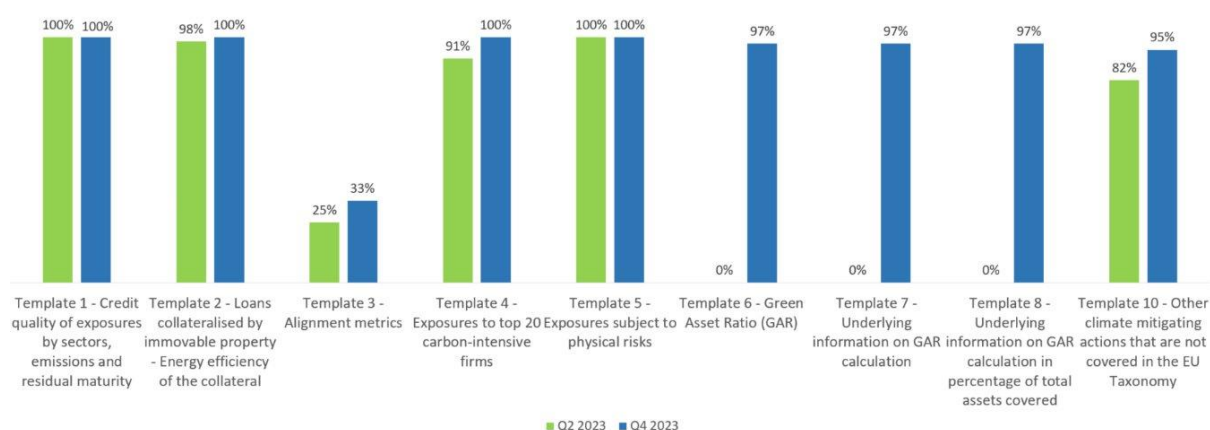
### Pillar 3 disclosures on ESG risks

#### Introduction

This report presents an analysis of the Q4 2023 Pillar 3 reporting on ESG risks for 39 European banks, including 6 Dutch banks. The 39 banks analysed in this benchmark have been selected based on their size and geographic location across Europe. This selection ensures a well-distributed representation among various countries, allowing for an effective comparison with the Dutch market. All banks in scope are considered large institutions which have issued securities that are admitted to trading on a regulated market of any Member State and are under European Central Bank (ECB) supervision. The Pillar 3 benchmark performed on Q2 2023 disclosures covered a scope of 57 banks in total. Unless indicated otherwise, the reported figures of the 39 banks are benchmarked against each other and evaluated for trends and movements between the reporting periods. Additionally, this Q4 2023 analysis includes an assessment of the qualitative ESG disclosures of a selection of banks.

Figure 1 illustrates the frequency of the disclosure of each ESG template and compares Q2 2023 to Q4 2023. It is evident that banks are increasingly disclosing the required templates. It should be noted that for Template 3, disclosure will only become mandatory per Q2 2024.

Figure 1: Pillar 3 disclosures on ESG risks as per Q4 2023 (39 banks in scope) and Q2 2023 (57 banks in scope)



#### Qualitative disclosures

Qualitative ESG disclosures are aimed at increasing transparency regarding the bank's risk management practices and the qualitative context of the quantitative disclosures. They are reported in table 1 (Environment), 2 (Social), and 3 (Governance).

For this report the qualitative ESG disclosures of 4 Dutch banks were analysed. A deep-dive was carried out to see how, and what these banks report, and how the methods of reporting compare to one another.

First, it became clear that all banks report in different ways. One bank used a mapping method by using the tables with references per element to where in their other reports (i.e. annual report, climate change report, human rights report) the information could be found. Another bank used a more descriptive method by elaborating extensively on how their business is organised and discussed elements that are not specifically mentioned in the required Pillar 3 ESG tables, before reporting on the requirements that are explicitly mentioned in these tables. A third bank used a more straight forward method by reporting according to the order of the tables. This diversity in reporting methods and formats can be explained by the non-rule-based character of the requirements set out by the ECB.<sup>1</sup>

<sup>1</sup> See also [https://www.bankingsupervision.europa.eu/press/publications/newsletter/2024/html/ssm.nl240221\\_1.en.html](https://www.bankingsupervision.europa.eu/press/publications/newsletter/2024/html/ssm.nl240221_1.en.html)

The second observation was that banks are most mature in reporting on qualitative Environmental risks in Pillar ESG table 1. All banks were able to report on almost all the Environmental elements of this table. The level of detail was also much higher than that of table 2 (Social) and 3 (Governance). Most banks were unable to report on the qualitative Social disclosures of table 2 in a detailed way, and sometimes even referred to the elements of table 1 (Environmental). All banks were most limited in reporting Governance risks as included in table 3 and often failed to describe how these risks potentially impact their business. Furthermore, the banks hardly described any future targets. These findings align with those of the ECB, who describes that banks “often failed to offer detailed qualitative information and did not clearly differentiate the integration of environmental, social, and governance risks into their governance and risk management frameworks”.<sup>1</sup>

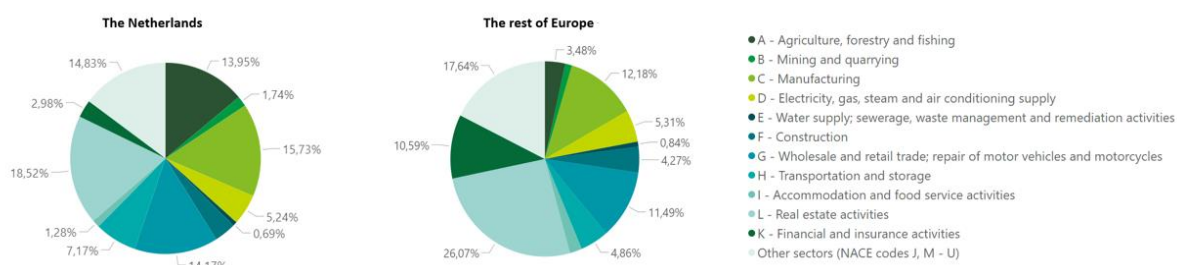
## Template 1

*Template 1 requires banks to disclose their exposure to sectors that highly contribute to climate change*

Figure 2 highlights that banks in the Netherlands and the rest of Europe have the highest exposure to real estate activities (18.52% in NL; 26.07% in the EU). In the Netherlands, 4 out of 6 Dutch banks have an exposure to the real estate sector, whereas for one bank this even amounts to 80.28% of its banking book. In Q2 2023, Dutch banks also reported relatively high exposures to the agriculture, forestry and fishing sector (13.77% NL; EU 3.48%). In Q4 2023, Dutch banks continued to report similar exposure to the agriculture, forestry and fishing sector as in previous quarters, with the figure slightly increasing to 13.95%. Conversely, the banks in the rest of Europe reported a slight decrease in their exposure to this sector, now at 3.48%.

Notably, in our previous report, the ‘K – Financial and Insurance activities’ sector was grouped under ‘Other sectors (NACE codes J, K, M-U)’. In Q4 2023, this sector is presented separately. For Dutch banks, the relative exposure to the ‘K – Financial and Insurance activities’ sector is 2.98%, while for the rest of the European banks, it is notably higher at 10.59%. Besides this reclassification, there is no significant change in the relative exposure to “Other sectors (NACE codes J, M-U)” between Q2 and Q4.

*Figure 2: Share of Gross Carrying Amount (GCA) by sector (%) Q4 2023 – The Netherlands and the Rest of Europe<sup>2</sup>*



### *Exposure towards companies excluded from Paris-Aligned Benchmarks*

In addition to disclosing their exposure to sectors contributing to climate change, banks are required to reveal whether these exposures are excluded from Paris-Aligned Benchmarks (PAB). Figure 3 includes only five Dutch banks, whereas one Dutch bank has no exposure to companies excluded from Paris benchmarks.

The total exposure towards companies excluded from Paris-Aligned Benchmarks of the banks in scope has increased in absolute value with EUR 42 million compared to Q2 2023, but the percentual value relative to total GCA has decreased (Q4 2023: 3.42% and Q2 2023: 3.61%). This decrease of exposure excluded from the Paris-Aligned Benchmarks, relative to total GCA, is observed both for the Dutch banks (Q4 2023: 4.48% and Q2 2023: 4.77%) and the other European banks in scope (Q4 2023: 3.28% and Q2 2023: 3.35%).

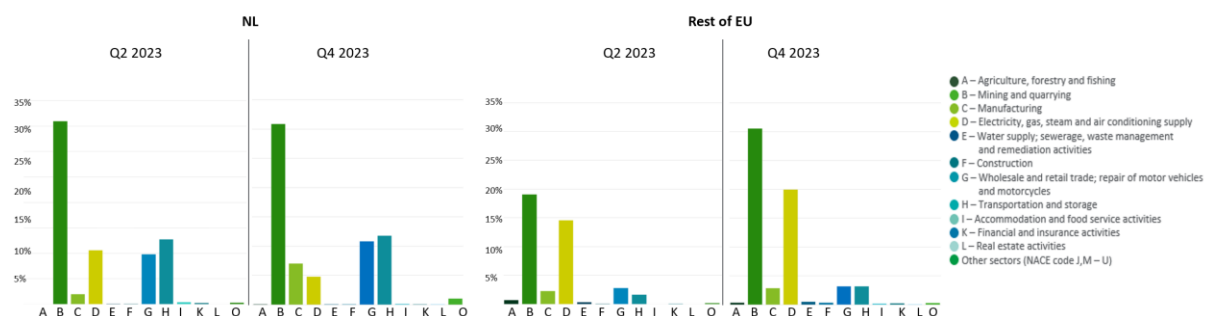
Compared to Q2 2023, Dutch banks have experienced an increase in their relative exposure to the companies in the manufacturing sector (Sector C) and wholesale and retail trade (Sector G) that are excluded from the Paris-

<sup>2</sup> The rest of Europe does not include the Netherlands

aligned benchmarks. However, the relative exposure towards companies in the electricity, gas, steam, and air conditioning supply sector (Sector D) that are excluded from the Paris-aligned benchmarks has decreased.

In contrast, the rest of Europe has experienced different trends during the same period. Notably, the mining and quarrying sector (Sector B) and the electricity, gas, steam, and air conditioning supply sector (Sector D) have both experienced increases in exposure excluded from Paris-Aligned Benchmarks, in comparison to total GCA towards these sectors.

Figure 3: Exposure of Dutch banks and banks in the Rest of Europe towards companies excluded from Paris Benchmark as percentage of GCA



## Template 2

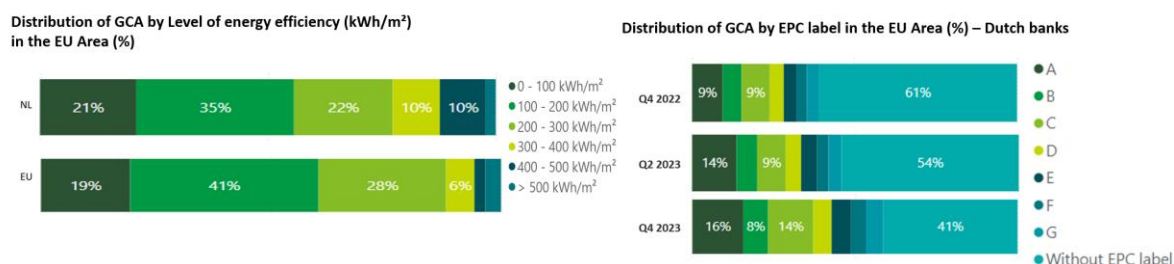
Template 2 discloses information on the loans collateralised with real estate, based on the energy efficiency of the collateral

Dutch banks still have room for improvement in terms of disclosing energy efficiency and EPC labels. Figure 4 shows that, on average, Dutch banks report lower energy efficiencies in their portfolios compared to the rest of Europe (56% report an energy efficiency of  $\leq 200$  kWh/m<sup>2</sup> for NL; 60% for the EU). Compared to Q2 2023, both the Dutch and European banks disclose a lower relative amount of collateralised loans with an energy efficiency  $< 200$  kWh/m<sup>2</sup> (Q2 2023: 58% for NL; 70% for the EU). It is observed that some banks are still in the process of improving their methodologies for estimating energy efficiency scores, which could explain the lower energy efficiencies disclosed compared to Q2 2023. The percentage of energy proficiencies that are estimated, compared to total reported gross carrying amount, remains constant between Q2 2023 and Q4 2023 for both the Dutch and other European banks.

It is interesting to see how banks are applying different methods to estimate the energy efficiency scores, whereas for example banks map energy efficiency scores by utilizing data from energy distribution system operators or estimate it using average Scope 1 and 2 emission factors per NACE sector from Partnership for Carbon Accounting Financials (PCAF).

Dutch banks have continually reduced the relative amount of GCA without EPC labels since Q4 2022. Figure 4 suggests that Dutch banks are improving the process of determining EPC labels. Also, Dutch banks provide several reasons for the improvement of EPC labels, whereas for example the rise in A labels is attributed to new inflows and the migration from lower energy labels to label A. New inflows typically have a new energy label, as it is currently mandatory in the Netherlands at the time of sale or purchase transactions. For the other European banks, a slight increase has been observed in the relative amount of GCA without EPC labels between Q4 2022 and Q2 2023, followed-up by a decrease in Q4 2023.

Figure 4: Distribution of GCA by level of energy efficiency (kWh/m<sup>2</sup>) and EPC label in the EU-Area as disclosed by Dutch banks



### Template 3

Template 3 discloses the distance to the IEA Net Zero Emissions by 2050 Scenario (NZE) regarding GCA by sector. Disclosure of this template is mandatory as of 30 June 2024, but banks that are already estimating their Paris Agreement alignment must disclose the information required by the EBA.

In Q4 2023, of the 39 banks in scope, only 13 disclosed Template 3. These banks report a reference year between 2020 and 2023 for the alignment metrics. Remarkably, four banks within the scope of the benchmark, including one Dutch bank, report a negative distance value to NZE for specific sectors, such as the power and automotive sectors, indicating to be below the intensity ratio for 2030 by IEA's decarbonisation path.

Interestingly, while some banks disclose their alignment metrics and distance to NZE, only three banks indicate their targets for three years after the reference year. For the banks in scope that do disclose their targets, they most often do so for the power sector. Also, it is worth mentioning that two of the banks in scope set a target through an absolute financed emissions metric, for respectively the power and oil & gas sectors, while all other banks only set relative targets.

### Template 4

Template 4 shows the exposures in the banking book to the top 20 carbon-intensive companies in the world.

Dutch banks are exposed to some of the most carbon-intensive companies in the world. Among the 39 banks in scope, a Dutch bank reports the highest exposure to the top 20 carbon-intensive companies relative to total GCA in both Q4 2023 and Q2 2023 (1.04% and 1.4%, respectively). Additionally, compared to the rest of Europe, Dutch banks on average report a higher relative exposure to the top 20 carbon-intensive counterparties (Q4 2023: 0.39% Q2 2023: 0.26%), while for the other European banks the average values remain the same in both periods (0.10%). This suggests that banks across Europe, including Dutch banks, have not yet shown a reduction in their exposure to the top 20 carbon-intensive companies. It is also observed that some banks have a higher relative exposure to these top 20 companies compared to prior reporting periods. Three out of six Dutch banks have top 20 carbon-intensive counterparties in their portfolio in Q4 2023, which is the same as in Q2 2023. However, if the Dutch bank with the highest exposure to the top 20 carbon-intensive companies is excluded, the average relative exposure of Dutch banks would decrease to 0.07%, which is below the 0.10% European average.

The general approach to defining the largest carbon-intensive company relies on the Climate Accountability Institute's Carbon Majors Data Set, Moody's database combined Scope 1 and 2 emissions values, or the CDP's full GHG Emissions Dataset. All six Dutch banks used the same benchmark in Q4 2023 as in their previous disclosures.

Figure 5: Top ten European banks, with the highest disclosed relative exposure towards the top 20 most carbon-intensive companies compared to total gross carrying amount



## Template 5

Template 5 discloses acute and chronic climate change physical risk exposure of banks. Banks currently use different methodologies to estimate sensitivity to this risk.

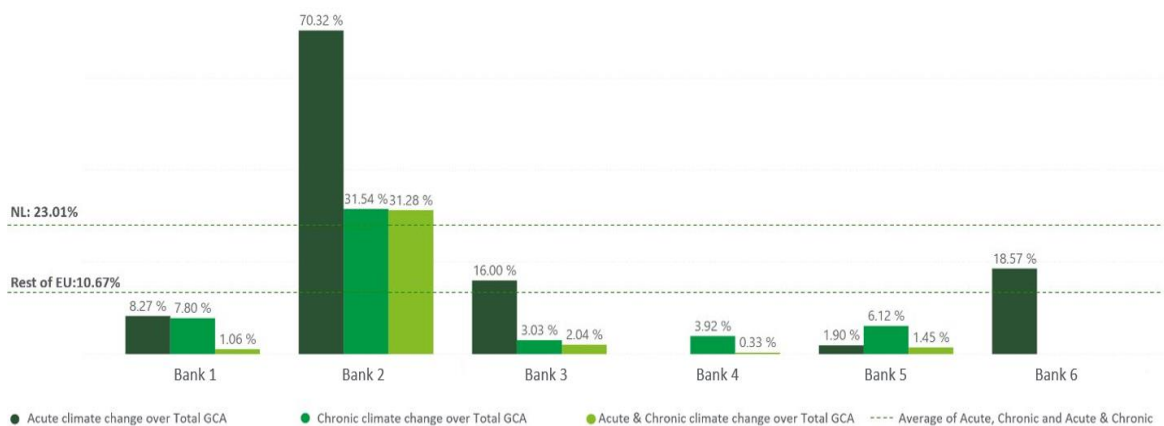
In Q4 2023, all 39 banks disclosed information on Template 5 (see Figure 1). Figure 6 illustrates the relative exposure to physical risks of six Dutch banks from their loans granted to sectors that significantly contribute to climate change risk. Notably, the highest relative exposure to acute climate risk compared to total GCA was reported by a Dutch bank at 70.32% (Q2 2023: 88.74%). The data reveals that all Dutch banks are sensitive to impact from climate risks, both acute and chronic. Dutch banks encounter acute climate risks more frequently than chronic climate risks. Additionally, the average exposure to acute, chronic and combined climate risks is 23.01% (Q2 2023: 11.77%) for Dutch banks, compared to 10.67% (Q2 2023: 7.48%) for the rest of the EU.

A key difference between Q2 2023 and Q4 2023 is that two Dutch banks disclosed a lower relative sensitivity to physical climate change, while one bank indicates an increasing rate of both chronic and acute & chronic climate risks.

### Methods used to determine acute, chronic and acute & chronic climate change risks

Banks' methods for analysing physical risks appear ambiguously defined in the Implementing Technical Standards (ITS). Consequently, banks have developed their own approaches to estimate these risks, employing varying criteria and interpretations. This lack of standardized methods complicates accurate risk assessment and comparison across banks. Differences in interpreting total sensitivity to acute and chronic climate change further complicate meaningful comparisons, potentially reflecting varying prudential risk management practices rather than actual risk levels.

Figure 6: Share of GCA(%) sensitive to impact from climate change physical events - Exposure towards sectors that highly contribute to climate change risk of Dutch banks



## Template 6

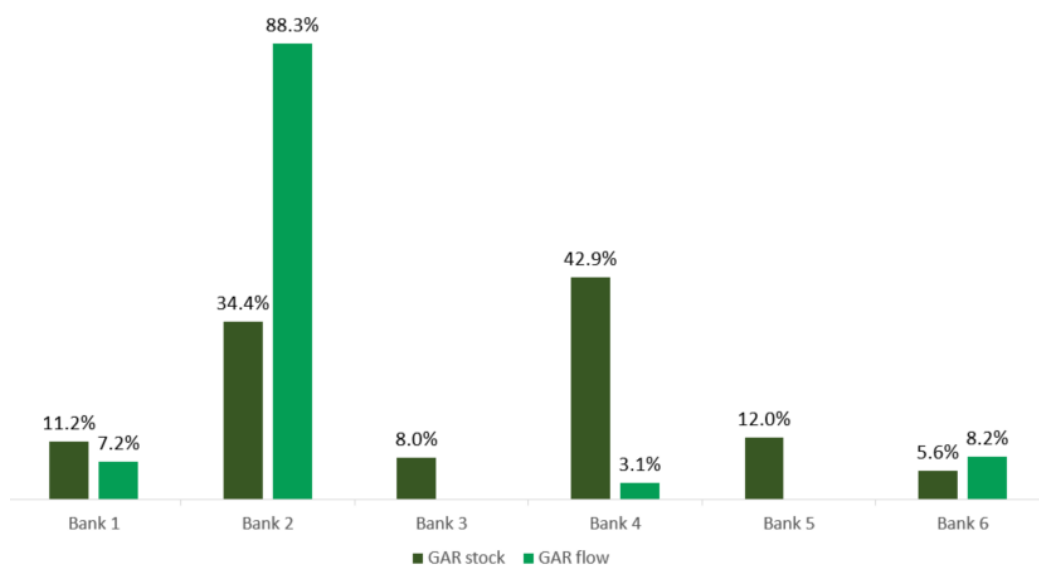
Template 6 discloses the overview of the KPIs as calculated based on Templates 7 and 8, including the green asset ratio (GAR).

The primary purpose of Template 6 is to summarize the GAR ratio in terms of climate change mitigation (CCM), climate change adaptation (CCA), and the coverage ratio, which is the KPI for covered assets over the banks' total assets. In addition, GAR stock refers to the assets on the bank's balance sheet at a particular point in time, and the GAR flow refers to the proportion of a bank's new financing (i.e. during the year prior to the disclosure reference date) that is aligned with the EU Taxonomy.

A high coverage ratio indicates that a significant portion of the bank's assets can be considered 'sustainable' and aligned with the EU Taxonomy. All Dutch banks disclose the GAR stock in relation to their total assets, but it is observed that two Dutch banks do not disclose the GAR flow at all. Although not elaborated upon in their disclosures, potential explanations for not disclosing a value for the GAR flow could be the lack of new financing of green assets, potentially due to limited opportunities for green investments, or could also be related to challenges in measuring or reporting green assets correctly.

It is interesting to mention that one Dutch bank reports an extremely high coverage GAR flow of 88.3%, this suggests that it is making efforts to ensure its newly originated loans are relatively more "green". Another Dutch bank has completely opposite KPIs. From the Dutch banks in scope, it has the highest GAR stock ratio (42.9%) but the lowest GAR flow ratio (3.1%), suggesting that this bank has limited new financing in sustainable activities or EU taxonomy-aligned activities.

Figure 7: Percentage of KPIs for covered assets over the banks' total asset (Coverage ratio) - Dutch Banks



## Template 7 & Template 8

Template 7 discloses the details of the GAR. The template differentiates between counterparty types and product types, allocating the exposure to the different taxonomy categories for each of the climate goals. Template 8 discloses the percentage value compared to GCA as disclosed in Template 7.

The purpose of Template 7 is to detail how banks calculate the GAR ratio and provides more information on asset allocation. Template 8 displays the extent to which credit institutions' activities qualify as environmentally sustainable, allowing stakeholders to understand the actions instituted to mitigate climate change transition and physical risks.

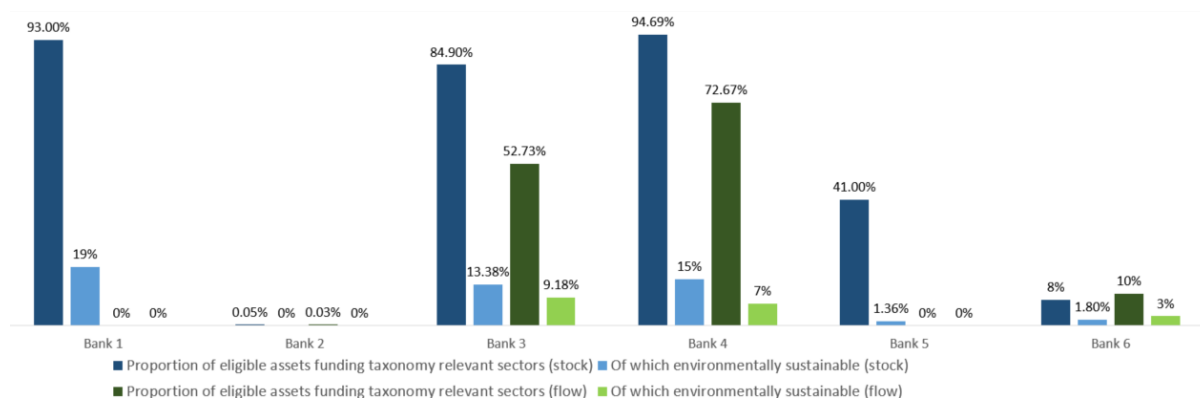
Template 8 distinguishes between assets that contribute to climate change mitigation and those that contribute to climate change adaptation. It is observed that only one bank discloses assets that are identified as contributing to climate change adaptation (stock: 0.09%; flow: 0.2%). Hence, this report mostly continues to focus on climate change mitigation.

All six Dutch banks disclosed the assets eligible for GAR calculation, and the proportion that is eligible for funding taxonomy relevant sectors. It is interesting to see that three Dutch banks reported that over 80% of their total stock of covered assets<sup>3</sup> is considered eligible for GAR calculation and eligible for funding taxonomy relevant sectors (i.e., sectors defined as environmentally sustainable according to the EU Taxonomy).

However, when assessing which part of these assets is also considered environmentally sustainable (i.e. assets contributing to one of the six environmental objectives<sup>4</sup> as outlined in the EU Taxonomy), it is noted that this proportion is significantly lower.

Furthermore, one Dutch bank reported an extremely low proportion of eligible assets funding taxonomy relevant sectors. Although this could be an indication of the bank having mostly non-Taxonomy-aligned exposures, it is also observed that institutions mention to face significant limitations to align certain portfolios towards the EU Taxonomy standards, which may be due to challenges in data quality or data availability which still requires improvements for future reporting cycles.

Figure 8: Proportion of assets eligible for GAR calculation that is considered eligible funding for taxonomy-relevant sectors significantly and of which is considered environmentally sustainable - Dutch Banks



## Template 10

Template 10 discloses climate change mitigation actions which are not covered in the EU Taxonomy, however, these products are still considered to support climate change objectives.

In Template 10 banks disclose quantitative and qualitative information on their climate change mitigation actions that are not covered in the EU Taxonomy. The number of banks in scope that report Template 10 significantly increased from 82% in Q2 2023 to 95% in Q4 2023. From the 39 banks in scope, it is observed that approximately 80% of the actions disclosed in Template 10 are focused on the mitigation of climate change transition risks, while 20% is focused on the mitigation of climate change physical risk.

Five Dutch banks have submitted Template 10. The types of products included in this template by Dutch banks are, amongst others, green bonds, specifically contributing to mitigating climate change transition risks and project finance related to renewable energy production, storage and transmission and Real-estate loans with a definitive energy label of A or above. Interestingly, while banks were finalizing their EU Taxonomy-related assessments, it is noticed that banks mentioned that some products no longer considered as not covered in the EU Taxonomy and hence from this disclosure period onwards disclosed on Template 7 instead of Template 10.

<sup>3</sup> Assets aligned with any of the six environmental objectives of the EU Taxonomy

<sup>4</sup> The six environmental objectives are: 1. Climate change mitigation, 2. Climate change adaptation, 3. The sustainable use and protection of water and marine resources, 4. The transition to a circular economy, 5. Pollution prevention and control, 6. The protection and restoration of biodiversity and ecosystems.

## Final thoughts

The Pillar 3 reports provide reasonable insights into the banks' ESG risks for regulators, investors and other stakeholders. We will continue to update our benchmarking analysis twice a year to incorporate new data and trends as reporting practices mature. We will also perform specific peer group analyses to offer clients across Europe tailored insights and advice, helping with all aspects ranging from data collection to solution implementation.

While institutions have disclosed several of the Pillar 3 templates various times – except for Template 6, 7, and 8 which were disclosed for the first time per Q4 of 2023 – there are indications that disclosure process is not yet fully mature. Variations in reporting methodologies across different disclosure periods not only complicate comparisons over time but also suggest that banks are still refining their reporting and control mechanisms. Potential challenges remain in areas such as regulatory interpretation, data availability and quality, the expertise required to implement all relevant reporting and disclosure criteria, and the capacity to align with other reporting standards (e.g., CSRD, EU Taxonomy, ECB Guide, and other upcoming requirements) and setting up a control framework. In the next disclosure period of Q2 2024, banks will also need to disclose their portfolio alignment metrics to the IEA Net Zero Emissions by 2050 Scenario and GHG scope 3 emissions, which will provide valuable new insights for the benchmark.

We encourage all organizations to take active measures to prepare for consistent and transparent ESG-related reporting. To discuss any of the themes mentioned in this article, or for help with your own Pillar 3 ESG reporting, please contact Anne-Claire van den Wall Bake-Dijkstra, Eric de Weerd, Shirley van Dorst or your usual Deloitte contact.