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The European Banking Authority

Submitted: EBA Consultation Response Portal

Draft Guidelines on ESG Scenario Analysis

MSCI[1] welcomes the opportunity to comment on the European Banking Authority's (EBA) draft guidelines on ESG Scenario Analysis ("Consultation document"). As a leading provider of climate risk data and analytics to the global investment community, MSCI has collected climate and ESG-related disclosures from thousands of companies globally for over two decades and developed tools to assist investors in their analysis of climate and ESG risks in their portfolios.

MSCI supports the EBA's draft guidelines on ESG scenario analysis and the integration of ESG scenario analysis into business decisions and bank risk frameworks as an essential for financial resilience.

For the purposes of this submission, we comment in more detail in Annex 1 on those matters where we believe MSCI's expertise and experience to be most relevant. We have the following general comments set out for your kind consideration.

1. **Strengthening Climate Stress Testing (CST) and Climate Resilience Analysis (CRA) –** A structured approach that aligns short-term CST with longer-term CRA could help ensure coherence between immediate risk management actions and longer-term strategic planning. More clarity on how insights from CST and CRA can be jointly operationalized would support consistent application across governance and risk functions. This would enable institutions to more effectively bridge financial risk monitoring with forward-looking business model resilience.

2. **Integrating iterative feedback loops –** Incorporating iterative feedback loops within the scenario analysis framework could enhance institutions' ability to adapt over time to new data, insights and evolving climate risks. Positioning iteration as a core element, especially following the impact assessment phase, could enable continuous refinement of assumptions, scenarios, and methodologies. This approach would reflect the dynamic and long-term nature of climate and ESG risks, and thereby help institutions improve scenario quality and resilience planning over time.

3. **Improving practical implementation of ESG scenario analysis –** Providing more detailed guidance on the required level of granularity in the design and execution of ESG scenario analysis could enhance the quality and usability of the outcomes. This could include practical guidance on adapting ESG analysis to different types of assets and portfolios, understanding how ESG risks affect them, and using suitable discounting approaches depending on whether the impacts are short- or long-term. Practical illustrations, particularly on indirect transmission effects or

[1] MSCI ESG Ratings, research and data are produced by MSCI ESG Research LLC, a subsidiary of MSCI Inc.

sector-specific risk mapping, would facilitate more consistent application across institutions and use cases.

4. **Expanding scenario sources for broader ESG coverage –** Broadening the range of recognized scenario sources could help institutions capture the interconnected nature of climate, biodiversity and energy. Incorporating complementary perspectives from global institutions such as the Intergovernmental Panel on Climate Change (IPCC), the International Energy Agency (IEA), and the Worldwide Fund for Nature (WWF) could strengthen the overall depth and comprehensiveness of scenario analysis. Such inclusion would enable a more diverse set of pathways and assumptions, allowing institutions to reflect a wider spectrum of ESG risk drivers in their assessments.

5. **Clarifying alignment with governance and strategy –** More clarity on how scenario analysis outcomes are expected to inform governance structures and strategic planning could enhance practical implementation. This includes outlining the connection to internal control frameworks, senior management engagement, and board-level responsibilities. Promoting cross-functional coordination and the use of consistent assumptions across business units would further support the effective integration of scenario analysis within the institution's broader risk and governance framework.

We appreciate the opportunity to contribute to this Consultation document and remain committed to supporting the EBA's continued efforts to strengthen the ESG risk management practices across the banking sector.

Please do not hesitate to contact us to discuss our submission.

Yours sincerely,

/s
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Question 1 - "Do you have any comments on the interplay between these Guidelines and the Guidelines on the management of ESG risks?"

MSCI: We acknowledge the clear interplay between the Consultation document and the Guidelines on the management of ESG risks[2]. The scenario analysis guidelines effectively complement and operationalize the broader ESG risk management guidelines, particularly regarding the forward-looking dimension of risk-based assessments. Specifically, the draft guidelines on scenario analysis provide essential detail on setting appropriate scenarios, defining transmission channels, and outlining methods for assessing resilience of both financial and business models to ESG factors.

However, to further enhance this interplay, we suggest that the EBA explicitly highlights how institutions should align scenario analysis outcomes with the specific governance and risk management processes detailed in the Guidelines on the management of ESG risks.[3] This could include clearer guidance on integrating scenario analysis results into decision-making frameworks and internal control processes, ensuring a consistent and holistic approach across an institution's governance structures. Additionally, explicitly cross-referencing key sections between both guidelines could reinforce coherence and facilitate more effective implementation by institutions.

Question 2 - "Do you have comments on the proposed definition of scenario analysis and its various uses in the banking sector as presented in Figure 1?"

MSCI: We acknowledge the clear definition and comprehensive overview of scenario analysis and its various uses in the banking sector, as depicted in Figure 1 of the Consultation document. The proposed definition effectively captures the multifaceted nature of scenario analysis as a critical tool for understanding, managing, and communicating ESG-related risks and opportunities.

To further enhance the clarity and practical value of Figure 1 of the Consultation document, we suggest that the EBA explicitly clarifies the interconnections and potential feedback loops among the identified uses. For instance, highlighting how informing strategy and adapting risk management practices can mutually reinforce each other would emphasize the dynamic nature of scenario analysis.[4] Additionally, incorporating illustrative examples of how scenario analysis can support business model adaptation, and the identification of new business opportunities would help institutions better visualize and implement these strategic applications.

Question 3 - "Do you have comments on the proposed distinction made between short-term scenario analysis (CST) and longer-term resilience analysis (CRA) as illustrated in Figure 3?"

[2] Final Guidelines on the management of ESG risks (EBA, January 2025)
[3] Paragraphs 88-92 of the EBA's Final Guidelines on the Management of ESG Risks
[4] NGFS Climate Scenarios for central banks and supervisors - Phase V (NGFS, February 2025)

MSCI: We support the distinction proposed by the EBA between short-term CST and longer-term CRA, as illustrated in Figure 3 of the Consultation document. However, our analysis on annual heat-related scenario-based losses from selected asset level activities presented in our answer to question 12 (please refer to the Figure 3 below in this response document), underscores the importance of considering both shorter- and longer-term time horizons for climate stress testing, as the impacts from extreme weather increase markedly over longer-term time horizons. The use of longer-term time horizons is particularly relevant when addressing potential mismatches between longer-duration liabilities and shorter-duration assets, given the increasing significance of climate and ESG factors over extended periods.

We suggest that the EBA provide additional clarity and practical guidance on how institutions can effectively integrate insights from both CST and CRA into a coherent decision-making framework, ensuring alignment between immediate risk management actions and longer-term strategic planning.

Question 4

"Do you have any comments on the interplay between these Guidelines and the Guidelines on institution's stress testing?"

Answer: Additional clarifications from the EBA on how institutions should manage the inherent uncertainty associated with long-term ESG scenario analysis would be beneficial. Specifically, guidance on best practices for addressing the uncertainty in key assumptions, scenario plausibility, and data availability over extended time horizons would be valuable. Such clarification would strengthen the effectiveness of both short-term and long-term resilience analyses.

As explained in our response to Question 3, there is a clear necessity for institutions to incorporate longer-term financial resilience analysis into their stress-testing frameworks. This is essential to adequately capture and manage evolving physical climate risks and to ensure a comprehensive understanding of vulnerabilities across longer horizons.

Question 5 - "Do you have comments on the Climate Scenario Analysis framework as illustrated in Figure 4?"

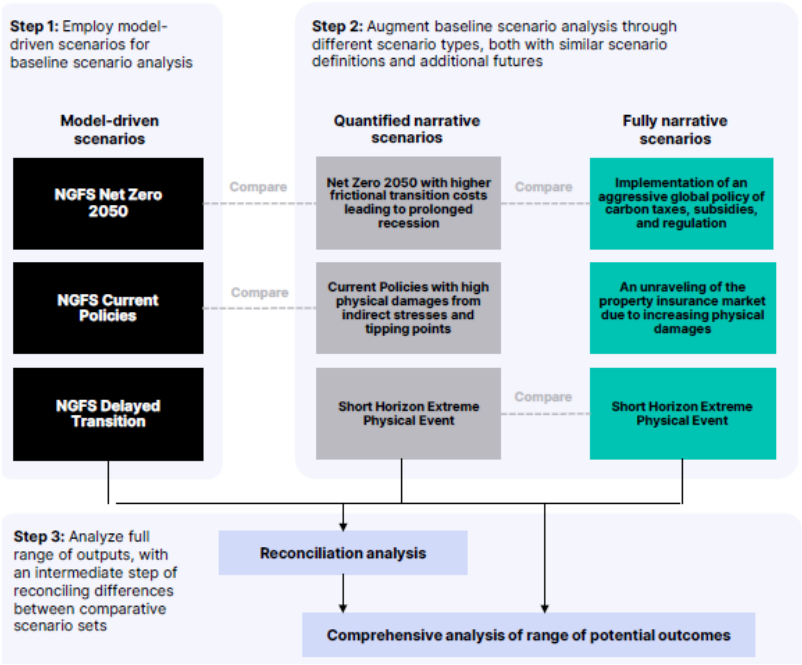
MSCI: Regarding the Climate Scenario Analysis framework outlined in Figure 4 of the Consultation document, we acknowledge its structured and comprehensive nature. The clear step-by-step approach provides helpful guidance for conducting both short-term CST and longer-term CRA.

To further enhance this framework, we suggest that the EBA explicitly encourages institutions to integrate iterative feedback loops between the defined steps, particularly after the impact assessment (Step 6). Given the evolving and complex nature of climate-related risks, such iterative loops would enable continuous

improvement and refinement of scenarios, assumptions, and methodologies based on insights from earlier stages of analysis.

Additionally, we suggest that the EBA provide clear guidance regarding the expected level of granularity in scenario selection and data collection processes, differentiating explicitly between short-term scenario analysis and longer-term resilience assessment. This would help institutions better tailor their analyses and ensure practical and actionable outcomes. For example, in our practical guide on the use of climate scenarios, we classified climate scenarios, examined their strengths and weaknesses, and provided guidance for their application.[5]

Figure 1: Example of complementary scenario framework for climate stress testing and resiliency analysis



Source: MSCI Sustainability Institute, December 2024

Furthermore, providing more guidance on how to differentiate across asset classes, as well as how to apply discounting approaches for both short and long-term scenario projections could help institutions improve their practical implementation.

For physical risks, we suggest emphasizing the value of granular, asset-level assessments and exploring the distribution of outcomes across extreme weather event probabilities (e.g., 100-year versus 200-year events).

Lastly, greater transparency and effectiveness could be achieved by disaggregating scenario assumptions into distinct components, such as:

- Carbon price levels (e.g., testing lower, mid-term, and higher carbon price pathways)
- Rate of warming (e.g., 1.5°C vs. 2°C vs. 3°C)

[5] How can I use climate scenarios? A practical guide (MSCI Sustainability Institute, December 2024)

- Policy timing and implementation (e.g., early vs. delayed policy actions
- Frequency and severity of physical risks (variations in extreme weather events)

Question 6 - "While respecting the definitions provided in other parts of the regulation, is there any concept/s used in these guidelines that it would be useful to include in an annexed glossary?"

MSCI: Regarding the glossary, we suggest the EBA consider including clear definitions of the following terms explicitly used but not fully defined within the draft guidelines:

- Dynamic balance-sheet approach (referenced in Figure 4)
- Transmission channels (referenced in Section 5.2)
- Climate resilience analysis (CRA) (introduced in Sections 4 and 6)
- Climate stress test (CST) (introduced in Sections 4 and 6)
- Central scenario (referenced in Section 5.1)

Including these definitions in an annexed glossary will enhance clarity and support consistent understanding and implementation across institutions.

Question 7 - "Do you have comments on section 4.1 Purpose and governance?"

MSCI: We welcome the EBA's clear articulation of the purpose and governance guidelines for ESG scenario analysis, as outlined in points 11 to 20 of the Consultation document. These guidelines significantly advance institutions' ability to proactively and strategically manage ESG risks. Specifically, we support the emphasis on embedding scenario analysis into broader governance frameworks and strategic processes, thereby integrating ESG considerations firmly into mainstream business-as-usual (BAU) governance practices.

The structured approach recommended by the EBA, highlighting both financial resilience through CST and business model resilience via CRA, provides institutions with a comprehensive toolkit for addressing ESG challenges effectively.

We particularly acknowledge the emphasis placed on senior management's endorsement and active involvement, as stated in points 15 and 20 of the Consultation document. Clear governance structures and board-level oversight are critical to ensuring the effective integration of ESG risks into strategic decision-making process.

Additionally, the emphasis on the cross-functional collaboration in paragraph 18 of the Consultation document is essential. Ensuring consistent assumptions and leveraging diverse expertise within the institution contribute significantly to the comprehensiveness and practicality of scenario analyses. We support the EBA's guidance and anticipate its successful implementation, which will further embed ESG considerations into core governance frameworks and contribute to enhancing strategic resilience over the long-term.

Question 9 - "Do you agree with the proposed references to organizations in paragraph 28? Would you suggest alternative or complementary references?"

MSCI: We agree with the EBA's proposed references to credible scenario sources outlined in paragraph 28 of the Consultation document, namely scenarios developed by internationally recognized institutions such as the Network for Greening the Financial System (NGFS), the Joint Research Centre of the European Commission (EU JRC), and national government bodies. These references represent authoritative and widely accepted sources noted for scientific rigor and relevance.

However, we suggest considering additional complementary sources to enhance scenario comprehensiveness. Specifically, scenarios developed by the Intergovernmental Panel on Climate Change (IPCC)[6] could be included, given their widely recognized global benchmarks in climate science. Moreover, scenarios from specialized climate research organizations such as the International Energy Agency (IEA)[7] could offer valuable insights, particularly with their detailed pathways covering global energy transitions and policy implications under various climate objectives. Additionally, incorporating scenarios from organizations such as the Swiss Re Foundation and WWF[8] could help institutions explore pathways specifically addressing biodiversity, ecosystem services, and nature-based solutions—thus broadening the scope and depth of ESG scenarios.

By integrating these varied sources, institutions can better address the interconnectedness of climate, energy, biodiversity, and societal factors, which is critical for comprehensive ESG scenario analysis.

Question 10 - "Do you have additional comments on section 5.1 Setting climate scenarios?"

MSCI: Regarding section 5.1 on Setting Climate Scenarios in the Consultation document, we suggest that the EBA more explicitly emphasizes the importance of institutions regularly updating and refining their climate scenarios in response to evolving scientific findings, regulatory developments, and technological advancements.

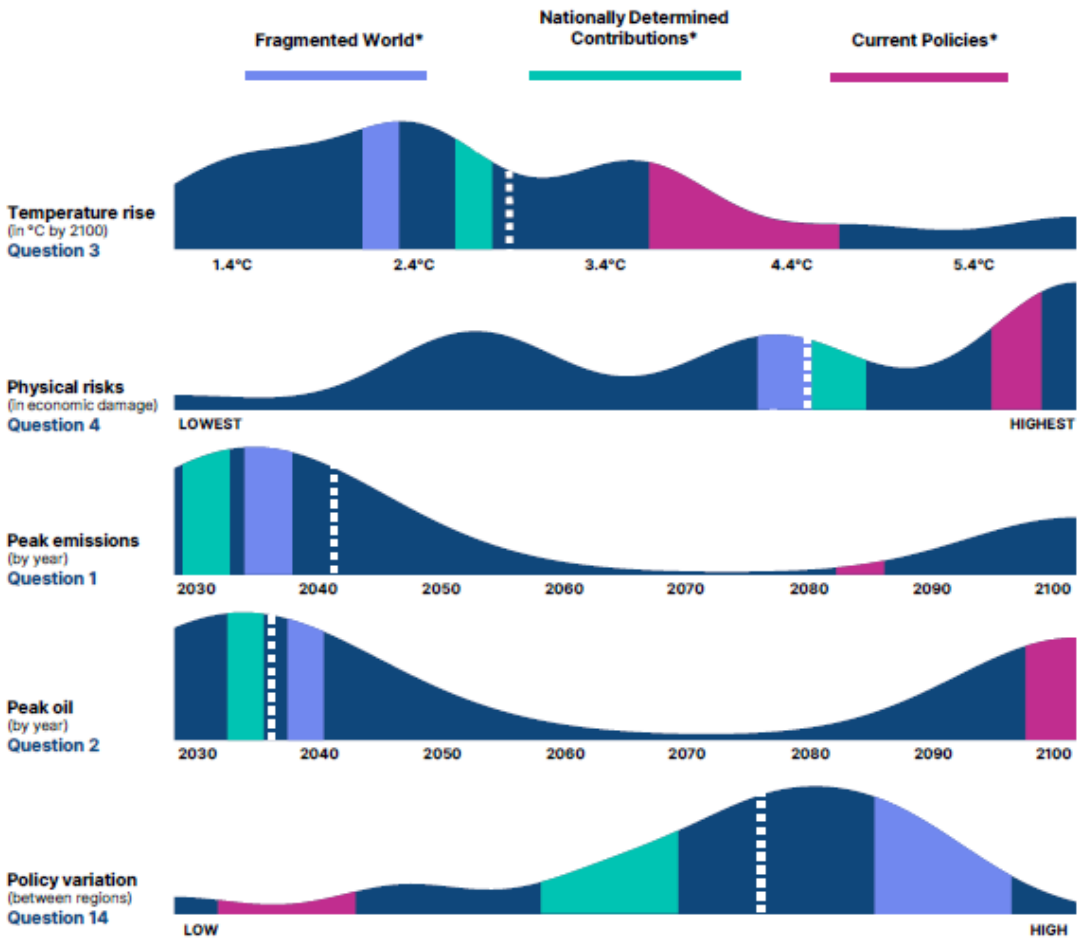
Recent insights from MSCI's climate risk outlook study[9] indicate that a majority of financial sector respondents (57%) already perceive physical climate change as having a significant impact on the global economy, reflecting growing concerns around the potential economic losses from both acute (i.e., hurricanes, wildfires and floods) and chronic extreme weather events (i.e., sea-level rise, prolonged heatwaves). An additional 36% of financial sector respondents expect significant

[6] Chapter 4: Future Global Climate: Scenario-based Projections and Near-term Information (IPCC, August 2021) ; Investors envision a 2.8C future, with greater risk of severe weather (MSCI Institute, October 2024)
[7] World Energy Outlook 2024 – Analysis - IEA (IEA, October 2024)
[8] Biodiversity Challenge About the Programme (Swiss Re Foundation, March 2023)
[9] Investors envision a 2.8C future, with greater risk of severe weather (MSCI Institute, October 2024)

economic impacts in the near future, underscoring market awareness of climate risks coupled with uncertainty about their timing and severity.

Given these findings, institutions would benefit significantly from clear and timely guidance on how to prioritize scenario factors based on their specific business models and regional exposures. Clear criteria or illustrative examples demonstrating the proportional application of scenarios would further support institutions in responding effectively to evolving physical and transition risks.

Figure 2: What the market thinks: Respondents' expectations versus common climate scenarios (n=350)



Source: MSCI Sustainability Institute, "What the Market thinks – A Climate Risk Survey", October 2024, scenarios from the Network for Greening the Financial System (NGFS) for central banks and supervisors.

Question 11 - "Do you have comments on the description of the climate transmission channels?"

MSCI: We find the climate transmission channels outlined in Section 5.2 of the Consultation document to be comprehensive, clearly structured, and aligned with industry best practices. The distinction between microeconomic and macroeconomic channels along with the categorization of risks provides a useful framework for institutions.

However, practical implementation would significantly benefit from more detailed guidance on how institutions could effectively apply these identified transmission channels into their portfolio-specific analyses - for instance, assessing physical risk impacts on real estate lending or transition risk impacts on energy-intensive sectors. Furthermore, clarifying the EBA's expectations on the appropriate granularity when mapping climate transmission channels to specific asset classes or sectors would be particularly helpful. In addition, providing illustrative examples or methodological approaches for capturing indirect or secondary transmission channels, especially those related to value chains, spill-over effects, and local economic impacts, would further enhance usability.

Lastly, although the Paragraph 52 of the Consultation document outlines clearly how transmission channels map to broader risk categories, institutions would benefit from specific illustrative examples demonstrating how climate-driven impacts may materialize across distinct risk types, particularly liquidity and operational risks, which are often less intuitively linked to climate factors.

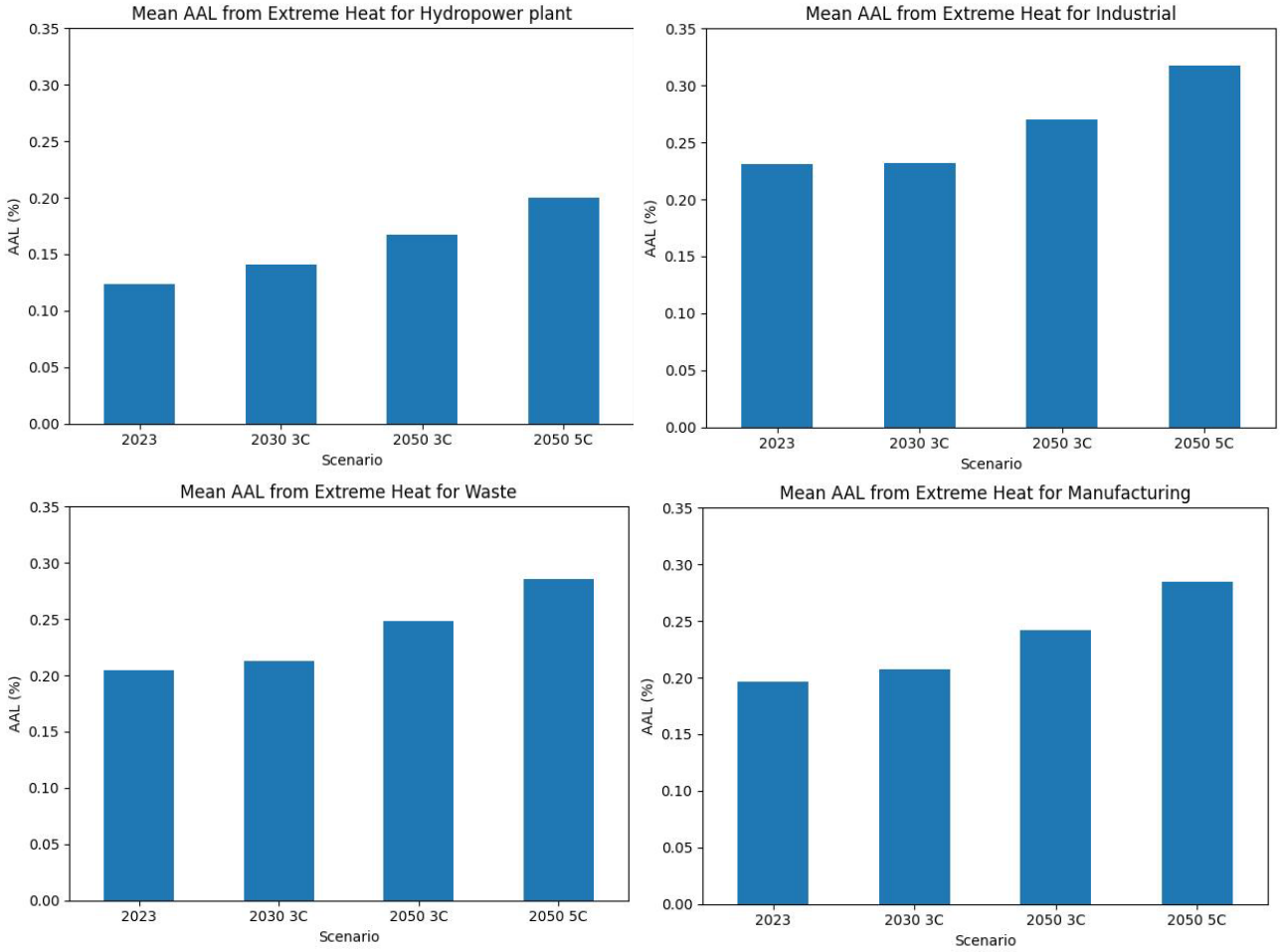
Question 12 - "Do you have comments on climate stress test (CST) tool and its use to test an institution's financial resilience?"

MSCI: Regarding section 6.1 on the CST, we acknowledge its clear integration with existing stress testing frameworks, particularly ICAAP and ILAAP methodologies. To further support institutions, we suggest that the EBA provides more detailed guidance on managing uncertainties related to long-term climate scenarios, particularly regarding the quantification and validation of assumptions. Additionally, providing best-practice examples or case studies on applying climate shocks at the exposure level could significantly enhance institutions' practical understanding and implementation of CST exercises.

More specifically, our sample analysis (please refer to the Figure 3 below in this response document) demonstrates that meaningful risk differentials, as measured by the Average Annual Loss (AAL) due to extreme heat, become significantly more pronounced over longer periods, particularly beyond a ten-year horizon. For instance, the mean AAL is notably higher under scenarios projected for 2050 compared to those for 2030 or the 2023 baseline, with the highest risk exposure identified in the 2050 scenario under a 5°C increase (please refer to the Figure 3 below in this response document).

This evidence highlights the necessity for banks to incorporate longer-term financial resilience analysis into their stress-testing frameworks to adequately capture and manage evolving physical climate risks and ensure a robust understanding of physical risk vulnerabilities.

Figure 3: Average annual heat-related scenario-based losses from selected asset level activities



Source: MSCI ESG Research, data as of April 2025.

Moreover, similar dynamics were observable for climate-related transition risks. Our recent analysis of the impact of scenario-based transition risks on lending practices[10] indicated moderate short-term impacts due to economic inertia. However, beyond a ten-year horizon, we found that climate-adjusted scenario-based probability-of-default metrics increased substantially—by approximately 22-100%—highlighting the importance of incorporating longer-term analyses into stress-testing frameworks to adequately capture evolving transition risk exposures.

[10] How Climate-Transition Risks May Impact Lending Practices (MSCI ESG Research, March 2025)

Figure 4: The impact of climate transition risks on credit defaults over the short and long-term

Source: A. Ludzuweit and G. De Melo Silva, "How Climate-Transition Risks May Impact Lending Practices", MSCI ESG Research, March 2025. The graph represents the percentage difference over baseline risk of the EVIC-Weighted aggregated forward PDs which represents the sum of policy risk, including emissions scopes 1, 2 and 3 at years 5, 10 and 15 of the term structure based on a 2°C NGFS disorderly transition scenario.[11]

Question 13 - "Do you have comments on the Climate Resilience Analysis (CRA) tool and its use to challenge an institution's business model resilience?"

MSCI: With regard to section 6.2 in the Consultation document on CRA, we support the detailed approach outlined by the EBA as an effective method for challenging the resilience of an institution's business model over longer time horizons. We suggest providing further guidance on how institutions can effectively integrate qualitative analyses with quantitative projections within the CRA, including specific examples or illustrative case studies. Additionally, more explicit clarification on the interplay between CRA outcomes and strategic planning decisions would further enhance institutions' ability to operationalize CRA findings effectively.

[11] For further insights, refer to "Introduction to Climate-Adjusted Probabilities of Default", MSCI ESG Research, August 2023, for additional methodological insights. Source: MSCI ESG Research, as of December 2024.