
Consultation Response – Joint ESAs Guidelines on ESG Stress Testing

19 September 2025

Introduction and General Comments:

The Association for Financial Markets in Europe (AFME) welcomes this opportunity to comment on the Joint ESAs Guidelines on ESG Stress Testing. In this respect it would be useful to confirm the timescale for implementing the guidelines for banks and for this to be made public. We understand the first application of these guidelines will be integrated into the EBA and ECB stress test in 2027. If this is the case, we recommend that the ESG stress test is done as a component with no capital adequacy implications.

Question 1 - Please add here any comments on "Title I - Subject matter, scope and definitions"

Question 2 - Do you agree with the list of objectives? Do you have any additional suggestions (addition, removal, precision, etc.)?

Regarding the testing of the resilience of financial entities' strategies and business models against a range of ESG-related scenarios over a medium to long-term horizon (for example, 5 to 10 years or more) (**paragraph 15**) – this should only concern the parts of the portfolio that are most sensitive to ESG factors, and not the entire portfolio. The proportionality principle should be applicable to limit the scope of the analysis if necessary. Further, while we recognise testing of financial entities' strategy and business model resilience may be a helpful exercise for banks to gain insights into potential areas of vulnerability and financial risk transmission channels, it is not an indicator of the likelihood that these specific events will occur or that the resulting impacts will mirror the dynamics of the variables analysed in the scenario analysis. As such, there is a high level of uncertainty around the underlying scenarios, and their likelihood and caution should be exercised in drawing strong conclusions in banks' long-term strategies and capital adequacy. Finally, with respect to section 3.1 the ESAs should confirm there is no intention for the 'S' and 'G' factors to be incorporated into the first materiality assessment exercise given the underdeveloped nature of these aspects.

Question 3 - Do you have any comment or suggestion on paragraphs 16-18 on "Materiality assessment"?

In reference to **paragraphs 7 and 16** on enhancing the focus on the Climate & Environmental components of ESG risk, with particular emphasis on material risk factors from the perspective of financial risk materiality: as outlined in the Guidelines on management of ESG risks published by the EBA – and applicable from 11 January 2026 – with regard to social and governance risks, where quantitative information is initially lacking, institutions' internal procedures should adopt methods that begin by qualitatively assessing the potential impacts of these risks on the institution's

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operations and financial risk profile. These methods should then progressively evolve to incorporate more advanced qualitative and quantitative measures. Institutions are expected to gradually strengthen their approaches in line with developments in regulation, scientific knowledge, data availability, and methodological advancements. With respect to the development of methodologies for the materiality assessment it should be clarified that where required of institutions, they should be able to leverage their own processes for this in line with the ESG risk management guidelines, focusing only on most material portfolios/asset classes, significantly impacted by environmental risks identified by banks. Where Competent Authorities are required to determine the relevant materiality factors for their region, this should consequently only scope in institutions for which such material factors are relevant.

Furthermore, the materiality assessment perimeter should consider the availability of data for the portfolios/counterparties being analyzed, as the size of the counterparty and its disclosure obligations could significantly impact the availability of data and the possibility of conducting stress analyses.

Question 4 - Please add here any additional comments on "Title II - Requirements regarding consistency, long-term considerations and common standards for assessment methodologies in stress testing of ESG risks - 4.1 Objectives".

It is important to have a gradual approach to integrating ESG factors into stress testing frameworks and allow time for firms to develop these capabilities. With reference to **paragraph 21** (Competent authorities should aim to fully integrate ESG factors into overall stress testing framework), we think incorporating the C&E risks into the existing short-to-medium term supervisory stress testing framework as a stand-alone component in the initial stress-testing exercises will avoid the creation of an additional, complementary layer that could result in double-counting through capital add-ons. Industry is strongly concerned that full integration into stress testing would risk double counting given there are elements of climate risk embedded in the macro-scenarios, and further that this would also have capital implications given it feeds through into the P2R which is only intended to cover risks emerging over the following 12 months (whereas we consider ESG risks generally emerge over a longer timeframe). Given this, the competent authority could incorporate ESG into the next Stress Test as an "Annex Document" alongside their main templates to complete for capital assessment. Doing so would be a first step towards integration while ensuring no capital implications for banks and equally eliminating the risk of double count in the macro scenarios, which banks are yet to receive regulatory guidance on.

We note that banks have made considerable efforts in the past three years to implement the ECB C&E expectations. Banks are now preparing for the introduction of ESG risk management guidelines from 2026 which will be implemented incrementally and there are several pillars to complete such as each bank's definition of ESG risk, data sourcing and maintenance, materiality assessments and then scenario creation that assess each bank's vulnerabilities. Only once these are complete can banks start considering stress tests. We also note that SSM banks have been required to establish processes

and manage risks unique to themselves which has resulted in varying methodologies, processes, assumptions and modelling techniques. It is important that competent authorities reduce the discrepancies between assumptions and processes, mainly resulting from the availability of data and information about mitigating levers e.g. for insurance on bank loan collateral. For instance, this could be achieved by leveraging a gross impact approach and ensuring a common and generalized use of insurance by geography to mitigate that gross impacts in a homogeneous way among banks with exposures in those geographies. Consequently, whilst banks acknowledge the intention of EU supervisors to incorporate ESG into the 2027 stress testing exercise, the current planned guidelines do not go into sufficient detail to help banks unify their approaches and therefore any such results from climate or ESG in an EBA exercise could be divergent to banks' internal exercises used for ICAAP.

Longer term, as competent authorities develop their approach to ESG stress testing, scenarios combining both climate and beyond climatic components should be considered by competent authorities.

Regarding **paragraph 22** and the availability of data, we note one challenge is the disconnect between the one-year lag for emissions data and banks' balance sheet data, which the ESAs should take account of. In addition, not all data is disclosed externally – for instance Scope 3 emissions are internally calculated. Guidance should be provided for this.

With reference to **paragraphs 23-24**, we believe it is essential that regulators (at bank, insurance firm and securities level) coordinate their ESG stress tests, sharing scenarios, macro assumptions, and data where possible. This would avoid regulatory gaps between sectors and would ensure a consistent approach across the financial sector. For example, information exchange and alignment of assumed shocks can improve the consistency of the overall exercise. Given the difficulty in modelling interconnections and spillover effects between financial sectors in the context of ESG stress tests, we believe supervisory authorities should directly embed these factors into the ESG scenarios assumptions.

More generally clear guidance on the financial drivers (KPIs) to be used in assessing the resilience of business models would be helpful. A shared set of KPIs would promote homogeneity of assessments across institutions and the effectiveness of prudential monitoring. Specifically, we would also welcome clarification on whether the KPIs used to assess the resilience of the business model would be aggregated - as per traditional exercises - through the capital ratio, or whether instead there would be an assessment of the impact on each of the risks affecting the business model separately.

Question 5 - Do you have any comment or suggestion on paragraphs 27-28 on "scope" and paragraph 29 on "time horizon"?

In **paragraph 27** regarding scope, it is important to highlight that, for cross-border financial groups, competent authorities should ensure that all relevant entities are included in the assessment. Furthermore, once it is ensured that the main entities and geographies are incorporated into the

exercise, making sure that those where ESG risks are most material are duly considered, the inclusion of a residual “Other” category to complete the total balance - as per traditional exercises - should be avoided, given the very high cost in terms of the effort–benefit ratio.

As regards **paragraph 28**, with reference to the “short-to-medium term” label, the guidance should assure that supervisors maintain the current general formulation, i.e., up to 5 years, and do not define a precise time horizon, thus leaving the possibility for banks to define the time horizons for banks’ analyses and label them short or medium within this range. This allows for consistency with other internal requirements or regulatory requirements (e.g., the CSRD, which defines medium-term as 3 years).

In **paragraph 29** it would be helpful to have a greater level of detail regarding the construction and internal consistency of the scenarios, particularly with regards to the underlying macroeconomic assumptions and the incorporation of compound risks or amplified effects from initial ESG shocks. In this regard, we would like to have more clarity on how the authorities intend to ensure consistency across scenario variables and whether a specific methodology is planned to capture indirect and secondary impacts (paragraph 30), in line with what is also recommended by sources such as NGFS or ECB. More precise guidance on this would enhance the reliability of the exercises and comparability across entities.

Question 6 - Do you have any comment or suggestion on paragraphs 30-33 on scenario design and application?

Generally, supervisors should strive not to create overly complicated stress tests, the results of which may be too difficult to interpret. They should instead consolidate the foundations and technical assumptions of their climate-economic scenarios. In cases where supervisors provide the scenarios, we suggest the following:

- Institutions would appreciate it if the scenarios were to be provided in advance given the novelty of this exercise (there have also been instances of errors when scenarios have been sent during previous stress tests, which could be mitigated).
- Clarify what is meant by considering ‘different narratives’. Supervisors should always provide scenarios with their projections. In case institutions receive only a narrative, it would make it a more complex exercise for institutions.
- In addition, we also consider the coverage of variables provided should be very broad, otherwise institutions would be forced to expand the scenarios including many assumptions.
- The above should also apply for alternative scenarios.

Confirmation that scenarios only cover climate scenarios at this stage (i.e. not ‘s’ and ‘g’). While we understand the need for several scenarios, this will nonetheless be burdensome for firms and should also be viewed in light of broader stress testing requirements. . For instance, regarding **paragraph**

32, we suggest the number of scenarios are limited (2-3 maximum) so that both the stress test analysis of the broader stress testing framework (capital/liquidity and strategy/business resilience) remains manageable and effective.

Question 7 - Do you have any comment or suggestion on paragraphs 33-35 on "top-down vs. bottom-up approaches"?

Where a bottom-up approach is followed, authorities should assess whether smaller firms which may not have the capacity to undertake this type of exercise should be excluded from the scope.

It is essential to balance resource-intensive testing with tailored assessments to ensure acceptance of the framework.

Furthermore, we support the view that hybrid approaches that integrate both top-down and bottom-up calculations should be allowed/considered. Less advanced banks could default to top-down calculations, while more sophisticated banks would have the option to perform bottom-up calculations using their own models in accordance with relevant climate scenarios. This approach would facilitate a gradual transition as expertise in ESG matters improves.

Question 8 - Do you have any comment or suggestion on paragraphs 37-40 on "level of granularity"?

The level of requirement for the input granularity level of the stress test must take into account the usability of the output granularity level of the stress test and the aggregation of stress test results from banks participating in the exercise. There is no value in having overly granular data as input to the stress test if this level of granularity is not usable/exploited in the output of the model.

We note it is not always possible to obtain the location of portfolio exposures. Therefore, the principle of proportionality should apply in respect of the requirement for geographic granularity at the NUTS level 3.

As regards the level of data granularity described in **paragraph 37**, we would also like to point out the practical challenges in achieving granularity beyond the industry level (e.g. at the level of specific technologies such as "breakthrough technologies"). Such granularity may not be currently feasible due to data limitations and classification ambiguities.

Additionally, we would like to highlight that breaking down physical and transition risks by risk category could also be difficult to operationalize. For instance, in the case of transition risk, it may not always be feasible to clearly distinguish between impacts driven by policy changes, technological shifts, or market dynamics, especially when such drivers interact or overlap.

We would therefore suggest that the guidelines adopt a more pragmatic approach, acknowledging that, for most authorities and institutions, sectoral-level granularity — both for exposures and risk drivers — remains the most realistic and actionable target in the near to medium term.

Question 9 - Do you have any comment or suggestion on paragraphs 41-44 on "balance sheet assumptions"?

These paragraphs should retain a flexible approach towards banks being able to adopt a static or dynamic balance sheet approach, including with regard to medium to long term horizons. In this context, we would expect guidance from the supervisory authorities that ensure methodological consistency with current regulatory stress testing practices already in place, such as ICAAP climate stress tests or Business Environment Scans. Aligning ESG stress testing with these established practices would enhance continuity, operational efficiency, and comparability across institutions.

In respect of developing long term scenarios, we do not think attempting to model the risks in the longer term (5 + years) is a realistic or viable way of producing any certain or reliable results which could inform business decisions at this point in time.

Question 10 - Please add here any additional comments on "Title II - Requirements regarding consistency, long-term considerations and common standards for assessment methodologies in stress testing of ESG risks - 4.2 Principles and methodological considerations" (45-49).

We suggest providing further clarity on the criteria to be applied for the inclusion of foreign subsidiaries' portfolios within the scope of ESG stress testing exercises **in paragraphs 44 and 45** in line with the overarching proportionality principle by targeting specific subsets of entities that are more exposed to ESG Risks. In particular, we would welcome alignment with existing supervisory practices used in current regulatory stress tests, ensuring consistency in the treatment of cross-border entities and avoiding methodological divergences.

Regarding **paragraph 46** on the proportionality principle and the inherent challenges of conducting an assessment for business purposes over such a long-time horizon (>10years), we deem that both qualitative and quantitative approach should be foreseen by the regulator. Qualitative outcomes should be appropriate for longer time frames, where uncertainty increases and data limitations are more pronounced. This mixed approach should ensure that the analysis remains both meaningful and operationally feasible, while still offering insight into the potential strategic implications of different climate paths.

Question 11 - Please add here any comments on "Title II - Requirements regarding consistency, long-term considerations and common standards for assessment methodologies in stress testing of ESG risks - 4.3 Organisational and governance arrangements" (50-63).

To avoid potential misalignment or duplication, it is important that any public disclosure follows the same principles, terminology, and reporting formats already used in current regulation. In this context, we recommend that competent authorities initially favour the publication of aggregated ESG results until methodologies, data quality, and interpretation frameworks reach a sufficient level of maturity. A phased approach would reinforce comparability, limit the risk of unintended market distortions, and promote a clear and harmonised understanding of ESG-related financial risks across institutions. Individual results should not be published.

Furthermore, while we acknowledge the importance of incorporating climate-related risks into the broader supervisory process, we believe that the current level of models' maturity does not yet support the use of quantitative results from climate stress tests to inform capital requirements. The methodologies and models used for climate stress testing are still evolving, and climate-related risk assessments are subject to significant uncertainty, both in terms of scenario design and transmission channels. We would therefore recommend that, at this stage, climate stress test results be used for exploratory and risk identification purposes only, and not to determine capital adequacy or be integrated into the SREP process at this point.

Regarding **paragraph 53**, we note the scarcity of data to be used in the analyses (e.g., GHG emissions, emission reduction targets, type of energy sources used), as well as the different coverage among portfolios/geographies. Furthermore, some providers serve only certain industries/geographies or client types, and different providers often provide different data. In such a fragmented and heterogeneous context, we recommend the data is to be provided by the regulator based on common disclosure frameworks and external resources, limiting as much as possible data collection from Financial Entities to avoid asymmetries and ensure consistency of analysis and judgment.

Regarding **paragraph 54** on the use of proxies for data gaps, proxies must be identified and assessed properly to avoid asymmetries and ensure consistency of analysis and judgment.

Question 12 - Do you have any additional and/or general comments on the Consultation Paper?

We support the application of the guidelines in the first instance as part of the 2027 Stress Test (and not before), this should include C&E risks as a separate component without capital adequacy implications under a separate Annex template. Given ongoing implementation of other ESG regulatory requirements simultaneously, we believe that supervisors need sufficient time to implement these guidelines properly and firms need sufficient clarity on the approach to be taken.

Question 13 - Do you have any comments on the Impact Assessment?

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AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.¹

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