L’illusion du répit : Comment les risques climatiques et environnementaux continuent de menacer la stabilité bancaire

The Illusion of Respite: How Climate and Environmental Risks Continue to Threaten Banking Stability

Abstract:

While the ESG regulatory landscape appears to soften—marked by the NZBA dissolution and Omnibus negotiations—the fundamental climate and environmental challenges facing European banks remain unchanged. Four structural pillars persist: the ECB's unwavering supervisory stance, including the introduction of a "climate factor" from 2026; inadequately quantified transition risks threatening both corporate clients and bank profitability; underestimated physical and nature-related risks creating hidden balance sheet vulnerabilities; and substantial growth opportunities in the €2+ trillion annual transition investment market. Banks must strengthen their risk quantification capabilities and seize commercial opportunities to ensure both financial stability and successful client transition financing.

The ESG regulatory landscape for European banks is undergoing a phase of transition and uncertainty. After several years marked by strengthened sustainability requirements, banking institutions face a more complex, even contradictory context, notably affected by upheavals in American policy. The recent dissolution of the Net Zero Banking Alliance (NZBA), following announcements by several banks of their withdrawal from the coalition, illustrates the growing tensions between climate ambition and operational realities.

Meanwhile, negotiations around the Omnibus package, aimed at simplifying and clarifying the regulatory framework, are struggling to reach conclusion, leaving sector players in limbo. In August, the European Banking Authority (EBA) even requested a pause from regulators in the rollout of new Pillar 3 requirements, which mandated banks to publish data concerning the environmental risks they face. These developments reflect divergent expectations from stakeholders—regulators, investors, civil society—making banks' ESG trajectory more difficult to chart.

Yet beyond these turbulences, several pillars remain unchanged and structural:

1. A supervisor maintaining course

The European Central Bank (ECB) maintains a firm stance on integrating climate risks into banking supervision.

ECB President Christine Lagarde reaffirmed this position by emphasizing to the Commission the importance of preserving, in the Omnibus amendments, the "benefits of sustainability reporting for the European economy and financial system." The alignment of climate and environmental risks with supervisory requirements remains one of the priorities outlined by the ECB for the next two years, and a first institution has been sanctioned with a fine for deficiencies in assessing these risks.

A significant recent example of the ECB's climate strategy: the announcement in early summer of the introduction (from mid-2026) of a "climate factor" in its collateral framework. This decision marks a key first step in integrating climate risks into financial risk management. In short, the more carbon-intensive and climate-exposed banks' portfolios are, the more expensive their refinancing will be.

2. Substantial transition risks to financial stability

Transition risks, well identified since the rise of Net Zero strategies, remain insufficiently quantified, even though they represent major financial risks for companies—loss of competitiveness and lower profitability, or even limited financing capacity—and therefore for banks. Indeed, some companies face "investment walls" necessary for their decarbonization and the management of these transition risks. This "wall" grows with short-term inaction and should lead in the medium to long term to investment needs that are too large relative to their debt capacity, and thus to potentially substantial losses of commercial opportunities for banks.

Beyond Net Zero commitments, banks must quantify and integrate these transition risks into their climate strategy from a risk management and financial profitability perspective.

Banks' pricing and credit allocation models must also evolve to integrate these risks from the outset. Otherwise, banks risk accumulating too many highly exposed assets and, conversely, not financing enough projects contributing to the transition.

3. "Hidden" physical and ecosystem risks still largely underestimated

Physical risks encompass the tangible impacts of climate change: acute risks—often called extreme weather events (droughts, cyclones, floods)—and chronic risks such as rising temperatures and changes in precipitation patterns.

They are not new: economic losses linked to extreme weather events cost more than $417 billion in 2024, of which less than 40% involved insured parties (source: Gallagher Re). Despite their increasing frequency and severity and their immediate financial impacts, physical climate risks remain largely underestimated by banks. Some have launched initial initiatives, but the majority of banks are far from having the necessary tools to quantify them or to deploy comprehensive adaptation strategies. They therefore constitute "hidden risks" likely to weigh on their balance sheets in the long term due to not being fully controlled today.

Nature-related risks will also have a major impact on banking portfolios: ecosystem degradation is accelerating due to economic activities, while all sectors depend directly on them. According to an ECB study conducted in 2023, 72% of companies in the eurozone would be critically dependent on at least one ecosystem service provided by nature.

Facing these growing risks, banks must focus on the most crucial issues for their portfolios, select priority themes on which to act, and develop appropriate offerings accordingly (circular economy, water management, pollution control, deforestation).

4. Growth opportunities to seize

Beyond developing management systems for these multiple climate and environmental risks, the transition presents immense commercial opportunities that banks must seize.

While some prevailing narratives suggest that "the transition is slowing down," investments in the energy transition exceeded the $2 trillion mark in 2024 and were up 11% compared to 2023 according to BNEF. The International Energy Agency forecasts these investments will increase to $2.2 trillion by the end of 2025, twice as much as investments in fossil fuels.

Regarding climate change adaptation, financing needs range between €120 billion and €400 billion per year by 2030 depending on sources (UNEP, IPCC, Climate Policy Initiative). A large portion will occur in developed economies and through already mature solutions that will be carried by companies (not exclusively public projects).

Banks must combine risk analysis and commercial opportunities to build a sustainable transition strategy. This relies on a thorough understanding of client challenges and targeted actions, before developing the necessary expertise and financial innovation dynamics.

Thus, despite certain political narratives, climate and environmental issues remain largely unchanged for banks. They must strengthen their tools for quantifying transition and physical risks in order to respond to regulators, contribute to financial stability (their own and that of the system), and finance their clients' transition.

Authors: Inès Galichon, Head of Financial Institutions Development, and Clément Le Guyader, Consulting Manager at Blunomy.