

ACTION FOR SUSTAINABILITY

The Banco de Portugal's
approach to ESG
sustainability 2022-25



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Executive summary

Topics such as environmental sustainability, social inclusion and fairness, transparency and good governance practices are unavoidable nowadays.

Over the past 15 years, the acronym ESG (Environmental, Social and Governance), which captures organisations' environmental, social and governance dimensions, has become established as a benchmark in the setting of public policies and sustainability strategies of firms and financial institutions.

It is acknowledged that, without ESG sustainability, the core of central banks and financial supervisors' missions – macroeconomic and financial stability – will always be at risk.

The environmental pillar has been playing a more prominent role because environmental risks, mainly linked to climate change, are an important source of balance sheet risk for financial institutions – thus directly affecting the mission of supervisors – and have broader macroeconomic implications that are potentially relevant to the conduct of monetary policy.

Over the past three years, the Banco de Portugal has been working more intensely in the areas of environmental sustainability and sustainable finance. It joined the Network for Greening the Financial System (NGFS), developed a strategy and work plan, produced studies and analyses, adopted supervisory measures, purchased green bonds, expanded its participation and intervention in national and international structures, reduced its ecological footprint, and developed communication initiatives on these topics.

Despite the increased focus on the environmental component, the social and governance pillars are also materially relevant to central banks, both by virtue of their mission and from a perspective of leading by example.

In the area of social responsibility, the Banco de Portugal has continued to support socially responsible causes and projects in partnership with the community, to promote economic and financial literacy and to encourage the qualification of its employees.

The Bank has also improved its governance model, organisation and processes to meet the demands arising from new tasks assigned to it and from digital transformation, and has embarked on modern, diverse, comprehensive and multi-stakeholder communication.

With this document, *Action for Sustainability*, the Banco de Portugal follows up on its *Commitment to Sustainability and Sustainable Finance*, in force in 2020-21. The document integrates the ESG sustainability-related initiatives of the Strategic Plan for 2021-25. The aim is to convey an integrated view of the Banco de Portugal's position on a topic that has a cross-cutting impact on its activity and to consolidate the guidelines which will steer its action over the next four-year period.

In its Strategic Plan for 2021-25, and within the scope of the five strategic guidelines (SGs) set out therein, the Banco de Portugal identified seven priority initiatives (PIs), which are relevant to ESG sustainability and have guided the preparation of this document:

SG 1 | Financial system robustness

PI 4 – To monitor the implications of climate change and energy transition for monetary policy and financial stability.

SG 2 | Protection of the banking market

PI 3 – To monitor developments and the sustainability of institutions' business models, focusing on digital transformation, operational resilience and environmental risk management.

SG 3 | Recovery and resilience of the economy

PI 1 – To help increase knowledge of public policy issues by means of a more systematic approach, encouraging further debate and analysis and an evaluation culture.

PI 2 – To invest in data compilation and production to support the analyses and studies required for advising on economic agents' behaviour.

SG 4 | Confidence and influence on society

PI 3 – To enhance social responsibility and sustainability in terms of environmental, social and corporate governance parameters.

SG 5 | Governance and internal management

PI 6 – To advance the project to concentrate the Bank's services dispersed across Lisbon in a new building.

PI 9 – To diversify assets under management, taking into account profitability and risk vectors.

In view of these guidelines and priorities, the Banco de Portugal will pursue three focus areas to enhance ESG sustainability within its mandate:

- Area 1 – Integrating climate risks into the missions of the Banco de Portugal;
- Area 2 – Reinforcing ESG sustainability in internal management;
- Area 3 – Promoting ESG awareness among employees and external stakeholders.

To materialise this ambition, the Bank will adopt the motto **"Action for Sustainability"**, with which it intends to reflect the spirit that encourages the daily action of employees across all areas of activity of the Banco de Portugal.

The focus areas for ESG sustainability will be detailed in the annual activity plans and the ensuing initiatives monitored by the Sub-Committee for Sustainability and Sustainable Finance, i.e. the structure coordinating ESG sustainability-related work at the Banco de Portugal.

1 Overview

As an institution whose main missions are to maintain price stability and safeguard the stability of the financial system, the Banco de Portugal is committed to the sustainability of the country's economic and social development process.

In the *Our Common Future* report, published in 1987 by the Brundtland Commission, 'sustainable development' is defined as "development that meets the needs of the present without compromising the ability of future generations to meet their own needs". This definition implies principles of inter-generational equity and conservation of the environment and natural resources, but it is too broad to be operational.

Over the past 15 years, the acronym ESG has become a key benchmark in the definition of public policies and the strategies of firms and financial institutions, linking the environmental, social and governance dimensions of organisations to the concept of sustainability.

Without environmental, social and governance sustainability, macroeconomic and financial stability will always be at risk.

The environmental component has become more prominent, as environmental risks, mainly related to climate change but also to other phenomena such as biodiversity loss, are an important source of risk for the balance sheet of financial institutions – thus directly affecting the mission of supervisors – and have broader macroeconomic implications that are potentially relevant to the conduct of monetary policy.

However, the growing importance of the environmental component in central banks' sustainability concerns does not cancel out the social and governance pillars, which remain materially relevant and subject to central bank attention and action, by virtue of their mission and also from a perspective of leading by example.

A survey of the Banco de Portugal's main stakeholders in 2020 as part of the preparation of the *Sustainability Report* showed that the topics identified as relevant to the Bank are still very much linked to the governance and social pillars. Within the governance pillar, respondents highlighted issues such as transparency, ethics, independence and risk management and, within the social pillar, the Bank's role as a promoter of economic and financial literacy and responsible employer.

ESG sustainability has a cross-cutting impact on the Banco de Portugal's entire activity, both in terms of its statutory missions and tasks and in the corporate sphere. The purpose of this document, which incorporates the Strategic Plan 2021-25 initiatives related to environmental, social and governance sustainability, is twofold:

- To convey an integrated view of the Bank's position and guide its action in the field of ESG sustainability over the next four years;
- To follow up on and deepen the *Commitment to Sustainability and Sustainable Finance* (hereinafter 'Commitment'), published in March 2020.

Chapter 2 recalls the path already taken by the Banco de Portugal to integrate ESG sustainability into its actions and describes the environmental sustainability strategies of a diverse set of central banks, thus providing a basis for comparison with what the Banco de Portugal has done for this ESG sustainability pillar.

Chapter 3 describes the vision and focus areas that will guide the Bank on ESG sustainability over the next four years, taking into account the guidelines and priorities set out by the Board of Directors for the 2021-25 period, and following up on the 'Commitment'. The initiatives will be implemented in the annual activity plans and monitored by the Sub-Committee for Sustainability

and Sustainable Finance, the in-house structure set up in June 2020 to coordinate ESG sustainability-related work at the Banco de Portugal.

2 ESG Sustainability: where do we stand?

2.1 The path already taken by the Banco de Portugal

Social and environmental responsibility is one of the Banco de Portugal's values, embodied in its successive strategic plans and reflected in its action as a central bank and financial supervisor, as well as in its internal management. The quality of the governance model has also been the subject of attention by the Bank, which has introduced several innovations and improvements in recent years, as reported in the Board of Directors' annual reports.

In early 2020 the Bank published the *Commitment to Sustainability and Sustainable Finance*, a document guiding its position and intervention in the field of ESG sustainability. The main focus was on the environmental pillar and therein, on the climate change dimension, the most relevant to the mission of safeguarding the stability of the financial system and that whose effects are most felt. The 'Commitment' established four focus areas: (i) risk identification and assessment; (ii) internal sustainability practices; (iii) national and international intervention; (iv) communication and cooperation. Box 1 describes the main initiatives undertaken in the implementation of the 'Commitment', taking these four focus areas as reference.

In July 2021 the Banco de Portugal published its first *Sustainability Report* relating to the period from 1 January 2019 to 31 December 2020. The report describes the Bank's performance in promoting sustainable development, based on the material topics identified by its stakeholders. The report was prepared in accordance with the Global Reporting Initiative standards for sustainability reporting.

The following paragraphs briefly describe the main milestones of the Bank's path towards incorporating each of the ESG sustainability pillars into its activity.

Environmental pillar

The Banco de Portugal has been working more intensely on issues related to environmental sustainability and sustainable finance, especially in the last three years. Joining the NGFS (Network for Greening the Financial System) in December 2018 was an important milestone, as it gave visibility to the Banco de Portugal's commitment to contribute, within its mandate, to the global effort to promote environmental goals, and particularly to combat climate change.

Since then, the Bank has drawn up a strategy and work plan, produced studies and analyses, adopted supervisory measures, purchased green bonds, substantially expanded its participation and intervention in national and international structures, reduced its ecological footprint and developed climate change-related communication initiatives.

In November 2021, on the occasion of 'Finance Day' at the United Nations Climate Change Conference (COP 26), the "*Banco de Portugal's Pledge on Climate Action*" was released, in which the Banco de Portugal set out the commitments and intended actions to reach the climate targets agreed upon by the European Union and the Portuguese government. It also took stock of the sustainability-oriented initiatives carried out until that moment.

Social pillar

Social responsibility is one of the Banco de Portugal's values and reflects its commitment to actively contribute to a fairer and more inclusive society. The Bank's action within this pillar has resulted in outreach activities and initiatives in partnership with the community in support of socially responsible causes and projects. The Bank has also sought to strengthen its position as an organisation that generates jobs and wealth.

In the last decade, the Banco de Portugal has worked with the community through social responsibility and volunteering initiatives and currently has a permanent network of 140 volunteers.

In 2019 it set out a financial and social support policy. This policy establishes areas of intervention and criteria for awarding support. Initiatives are ranked according to their contribution to improving the economic and financial literacy of the Portuguese people and to enhance knowledge in economics and finance. Awarding sponsorship follows principles of transparency and equal opportunities for entities requesting support from the Bank, of commitment to the supported entities and of regular assessment of existing partnerships and funded projects.

In the field of economic and financial literacy, the Banco de Portugal, jointly with the other financial supervisors, has been responsible for the implementation of the National Plan for Financial Education since 2011. It has also developed initiatives to help citizens better understand the economy and central bank functions. Among these are Room 8 and the Financial Education Centre of the Money Museum, as well as the series of decoders and podcasts released on the Bank's website and social media.

As a responsible employer, the Banco de Portugal has focused on training its employees, providing them with financial support for attending higher education courses and specialised courses. In 2016 such investment was reinforced with the creation of a corporate academy. A Management and Leadership School and a Data Science School were set up within the academy in 2016 and 2020 respectively. As regards diversity and inclusion, a 2020 study on the gender pay gap confirmed gender balance in terms of the functions performed, except for top management, and overall balance in the annual merit-based promotion process.

Governance pillar

In the Strategic Plan 2017-20, the Banco de Portugal set as a guideline the alignment of its organisational and governance model with best practices within the Eurosystem central banks.

Over the past four years, the Bank has improved its governance model, organisation and processes to meet the demands arising from new tasks assigned to it and from digital transformation. It developed a risk management and control model characterised by independence and segregation of functions, incentives to expertise and integrated risk management with the Bank's strategic planning. The regulatory framework governing ethics and business conduct was strengthened, through more systematic procedures to prevent conflicts of interest and control limits to private financial transactions. The Banco de Portugal's Data Protection Officer was also appointed and a data protection office was established.

The Banco de Portugal enjoys independent status, which is essential for the pursuit of its mission. As a counterpart to that independence, and as a public service institution, it is responsible for observing high standards of transparency and being accountable for its activities, the resources used and the results achieved. Over the last four years, the Bank has therefore focused on developing modern, diverse and comprehensive communication that is tailored to its various stakeholders.

Box 1 • “Commitment to sustainability and sustainable finance” – Where we stand

The *Banco de Portugal's Commitment to Sustainability and Sustainable Finance* published in March 2020 defined four focus areas in the field of ESG sustainability for the 2020-21 horizon: risk identification and assessment; internal sustainability practices; national and international intervention; communication and cooperation.

Area 1 – Risk identification and assessment

The first area concerns building the capacity to identify, assess and mitigate the financial risks associated with the impact of climate change, assess the macroeconomic impacts of climate change and overcome data gaps.

In the field of financial stability, the Bank has sought to measure Portuguese banks' exposure to corporations in sectors most sensitive to climate transition risks. In June 2021 it published a [study](#) showing that over 60% of exposures are in climate-policy-relevant sectors.

The Banco de Portugal was also involved in the preparation of the ECB's *Guide on climate-related and environmental risks* released at the end of 2020. This Guide is addressed to significant institutions within the Single Supervisory Mechanism and sets out supervisory expectations in four domains: internal governance, risk management, scenario analysis and the disclosure of meaningful information. In April 2021 the Banco de Portugal extended application of the Guide to less significant institutions subject to its direct supervision by means of Circular Letter No CC/2021/00000010. Supervisory dialogue will integrate climate risks as of the second quarter of 2022 and in the meantime a self-assessment exercise on current practices and future action plans has been launched with institutions.

On the macroeconomic side, the Bank has published [research papers](#) and the [systematisation](#) of knowledge about climate change and economic policies intended to mitigate its effects. Efforts have also been made to set up a repository of climate data and exposure of enterprises to climate risks. In September 2020 the Bank signed a partnership with APA, the Portuguese Environment Agency, to participate in a three-year project aimed at assessing the Portuguese territory's vulnerability to climate change. The project also involves the Directorate-General for Territory, IPMA (the Portuguese Institute for Sea and Atmosphere) and the Faculty of Sciences of the University of Lisbon. The Bank leads the analysis of the macroeconomic impacts of climate change and energy transition.

The Bank also participated in discussions on the implications of climate change for the conduct of monetary policy, in the context of the review of the Eurosystem's monetary policy strategy.

Area 2 – Internal sustainability practices

The second area of the 'Commitment' refers to internal sustainability practices, in two dimensions: the management of the Banco Portugal's asset portfolio and the reduction of its ecological footprint as an organisation.

Over the past two years, the Bank has incorporated ESG principles into the guidelines for the management of its own investment asset portfolio. In 2020 it invested in the German Treasury's inaugural issuance of green bonds and in 2021 it purchased bonds from the euro-denominated BIS green bond fund (it had already invested in the US dollar-denominated BIS green bond fund in 2019). Internal work for the strategic review of the management of own investment financial assets was finalised, covering, inter alia, the incorporation of ESG principles. As part of the agreement released by the Eurosystem in February 2021, the Banco de Portugal committed to measuring and disclosing the carbon footprint of its own investment financial assets.

In January 2020 the Bank joined the Lisbon Green Capital 2020 commitment, undertaking to implement ten initiatives in the fields of energy, water, circular economy and citizenship by 2030. In 2020 the Bank implemented part of these measures, along with others not included in this commitment. In particular, in the area of energy, the Banco de Portugal: signed a new contract for the supply of electricity (which ensures that, excluding the regional offices of the Azores and Madeira, the energy in all of the Bank's buildings comes entirely from renewable sources); conducted a feasibility study for a photovoltaic power plant in the Carregado Complex; and used LED lighting to reduce energy consumption.

In 2020 the [General Framework of Principles for Contractors of the Banco de Portugal](#) was also approved, whereby entities with which the Bank signs contracts for the provision of goods or services are required to observe the Bank's ethical standards and commitment to economic, social and environmental sustainability.

Three relevant initiatives are currently under way: a mobility study aimed at informing the future sustainable mobility policy; the update of the calculation of the Bank's ecological footprint by calculating greenhouse gas (GHG) emissions, covering its 19 buildings; and participation in an ECB-led project to assess the environmental impact of the issuance of euro banknotes and coins (€ Product Environmental Footprint Project).

In July 2021 the Banco de Portugal published its first [Sustainability Report](#) relating to the period from 1 January 2019 to 31 December 2020. The report describes the Bank's performance in promoting sustainable development, based on the material topics identified by its stakeholders. The report was prepared in accordance with the Global Reporting Initiative standards for sustainability reporting.

Area 3 – National and international intervention

The third focus area set out in the 'Commitment' concerns the Banco de Portugal's intervention in national and international fora where measures with a potential impact on the financial system are discussed.

At international level, the Banco de Portugal participates in around 20 structures specifically devoted to environmental sustainability, within the scope of the European Central Bank, the Single Supervisory Mechanism, the European Systemic Risk Board, the European Banking Authority, the Bank for International Settlements and the NGFS.

At national level it is part of a group on sustainable finance (*Grupo de Reflexão para o Financiamento Sustentável*), chaired by the Ministry of Environment and Climate Action, and in July 2019 it signed the *Carta de Compromisso para o Financiamento Sustentável em Portugal* (a letter of commitment to sustainable finance in Portugal). It is also part of the National Council of Financial Supervisors' contact group for sustainability and sustainable finance, which aims to strengthen cooperation among national authorities and structure communication on this topic.

The Banco de Portugal contributes to the ongoing discussions across all these structures and seeks to encourage reflection on aspects that are relevant to the Portuguese economy and financial system.

As of the end of 2020 the Bank has also developed an integrated exercise to identify, analyse and attempt to mitigate issues raised in external representation structures that may be of concern to the Portuguese economy, the Portuguese financial system or the Bank itself. In 2020 and 2021 these structures produced and published several reports, with input from the Bank and covering areas such as: climate scenarios, definition of supervisory expectations, risk assessment and management, monetary policy, asset management, market analysis, research priorities and prudential regulation (within Pillars 2 and 3).

In carrying out its role as advisor to the Government, the Bank has mainly supported the Ministry of Finance by providing input to the analysis of legislative initiatives and definition of the national negotiating position, including in 2021 under the Portuguese Presidency of the Council of the European Union.

Area 4 – Communication and cooperation

The fourth and final focus area of the Banco de Portugal to address ESG sustainability challenges is communication and cooperation with external entities.

In this context, in 2020 the Bank hosted a [session on sustainability and sustainable finance](#) specifically addressed to the banking system, and participated in public communication and dissemination initiatives. In November 2021 the [Banco de Portugal Pledge on Climate Action](#) was released, setting out the commitments and main initiatives to contribute to the climate goals taken on by the European Union and the Portuguese State. In the same vein, in October 2021 the Banco de Portugal introduced at two of its most important conferences – the *Financial Stability Conference* and the *31st Lisbon Meeting* – sustainability and sustainable finance panels.

As regards internal communication, in 2021 it set up a permanent section devoted to sustainability issues in the Bank's in-house magazine.

2.2 The central banks' approach to environmental sustainability

This section summarises the environmental sustainability strategies of a number of central banks that have stood out for focusing on environmental issues and in particular climate change. Although several of the central banks considered have more comprehensive corporate social responsibility strategies, the environmental dimension is the most prominent from the perspective of a central bank's core business, also having the greatest similarities among the approaches followed.

The summary covers central banks of different sizes, geographies and institutional frameworks and seeks to systematise each of their approaches to environmental sustainability in the fields of governance and accountability and of strategy, medium-term goals and main initiatives.

15 central banks are covered, among which five are outside the European Union: Reserve Bank of Australia, Bank of Canada, Bank Negara Malaysia, Reserve Bank of New Zealand and Bank of England; a non-Eurosystem EU bank: Sveriges Riksbank (Sweden); and nine Eurosystem banks: Banca d'Italia, Banco de Portugal, Banque de France, Banque Nationale de Belgique, Central Bank of Ireland, Deutsche Bundesbank, European Central Bank (ECB), De Nederlandsche Bank and Suomen Pankki.

Governance and accountability

As regards **governance**, there is a wide range of approaches, from more structured top-down models to undefined predominantly bottom-up models. However, there has been a shift towards increasingly structured approaches, reflecting the growing importance and cross-cutting nature of sustainability.

At the Bank of England, the Executive Director responsible for prudential supervision has been appointed sponsor for climate risks and tasked with proposing to the Governor the strategy for addressing these risks and overseeing its implementation. Bank Negara Malaysia has assigned similar responsibilities to its Deputy Governor.

The ECB, the Banque de France and the Central Bank of Ireland have recently set up structural units with dedicated resources (around 10 FTE in the case of the ECB) to coordinate their environmental sustainability-related initiatives. The Bundesbank has established an internal network – Nachhaltigkeit (meaning sustainability) – to support its participation in the NGFS, where it coordinates a workstream devoted to “Scaling up Green Finance”.

The Banco de Portugal follows a mixed and predominantly bottom-up approach. Replacing an informal inter-departmental group established in March 2019, it set up in June 2020 an inter-departmental structure – the Subcommittee for Sustainability and Sustainable Finance – chaired by a member of the Board of Directors and supported by a technical secretariat. This structure has been tasked with monitoring and ensuring consistency in the initiatives carried out in the field of sustainability. Responsibility for individual initiatives and their implementation is predominantly of the Bank's Departments. In the same vein, Suomen Pankki has set up a joint network with the supervisory authority, chaired by the Deputy Governor, with the aim of defining best practices for integrating the various aspects of sustainability into this Bank's activities.

As far as the other central banks analysed are concerned, no information has been found on their websites about the sustainability governance model in force, suggesting that a more informal and bottom-up approach will tend to prevail in these cases.

In the area of **accountability**, most central banks disclose information on their environmental sustainability strategies and initiatives in their annual reports or sustainability reports. In addition, several central banks have publications specifically devoted to environmental topics.

Some central banks, including those of Canada, Malaysia, the United Kingdom, France, the Netherlands and Finland, publish or soon plan to publish reports on the ecological footprint of their business and portfolios of assets under management, which follow at least partially the recommendations of the **Task Force on Climate – related Financial Disclosures** (TCFD). The ECB, the Bundesbank, the Banca d'Italia and the Central Bank of Ireland publish an environmental report annually, setting out the main initiatives undertaken and the results achieved.

In February 2021 the Eurosystem central banks agreed on a **common stance** for applying sustainable and responsible investment principles in the management of their non-monetary policy portfolios, with a view to a harmonised reporting of the carbon footprint of these portfolios in line with the TCFD recommendations as of 2023 (with reference to 2022).

Strategy, medium-term goals and main initiatives

Most of the central banks analysed publicly assume environmental strategies and goals, in some cases incorporated into broader ESG strategies and goals. The approaches are wide-ranging and cover in almost all cases both the central bank's core business and corporate sphere.

As regards central banks' **missions**, the goal is to integrate climate risks into financial stability, monetary and supervisory policies, and economic research and analysis, as well as to contribute to the global effort of addressing climate change. Some central banks have implemented or announced the intention to carry out climate stress tests on banks and insurers. They have also published climate change-related research work.

Furthermore, fora have been set up with other supervisors and the industry to share information and best practices in the field of climate risk management. Examples are the Joint Committee on Climate Change, which brings together financial supervisors from Malaysia and industry representatives; the Climate Financial Risk Forum, established by the financial conduct authority and

the prudential regulation authority of the United Kingdom; the French Commission Climat et Finance Durable; and the Sustainable Finance Platform, set up by De Nederlandsche Bank. The Banco de Portugal participates in a sustainable finance group (*Grupo de Reflexão para o Financiamento Sustentável*), chaired by the Ministry of Environment and Climate Action, which brings together financial supervisors, associations representing the sector and a number of individual institutions. The Bank is also part of the National Council of Financial Supervisors' contact group for sustainability and sustainable finance.

In the **corporate sphere**, the aim is to reduce the ecological footprint of central banking operations, including in the management of portfolios of own investment assets and pension funds and in banknote production. The ECB has an environmental management policy in place since 2007, with strategic targets and metrics, subject to models and external verification under the Eco-Management and Audit Scheme (EMAS) since 2010. A number of central banks have announced quantitative targets for reducing their ecological footprint:

- Bank of Canada – reducing GHG emissions from facilities by 80% by 2030, with reference to 2018, to reach net-zero emissions by 2050;
- Bank of England – reducing GHG emissions (scopes 1 and 2 and business travel) by 63% by 2030, against a 2015 baseline;
- Banque de France – achieving carbon neutrality in 2030 and reducing GHG emissions by at least 10% by 2024, compared with 2019;
- Banco de Portugal – aligning activities with the 1.5°C increase limit set out in the Paris Agreement and with the climate neutrality goals set by the European Union;
- Central Bank of Ireland – reducing GHG emissions (scopes 1 and 2) by 50% by 2030 and achieving carbon neutrality in 2050;
- De Nederlandsche Bank – aligning its own-investment portfolio with the agreements set out in the Paris Climate Agreement by 2050;
- Deutsche Bundesbank – reducing GHG emissions by 25% by 2025, with reference to 2013-14;
- Suomen Pankki – achieving carbon neutrality of the investment portfolio by 2050.

In order to achieve their environmental targets in the corporate sphere, central banks have implemented initiatives aimed at:

- Auditing energy consumption and waste generation;
- Reducing consumption and increasing energy efficiency;
- Incorporating renewable energy;
- Reducing water consumption;
- Improving waste management;
- Reducing paper and plastic consumption;
- Improving mobility patterns;
- Integrating principles of environmental sustainability into procurement policies;
- Promoting biodiversity;
- Communicating and raising workers' awareness to ESG issues;
- Promoting new working models and workspaces.

Some central banks explicitly mention having incorporated climate risk into their operational risk management policies. The De Nederlandsche Bank has even carried out a stress test on its balance sheet to assess sensitivity to transition risk, following, with a few adjustments, the approach it outlined for the financial system. As part of the review of its monetary policy strategy, the ECB has announced that it will carry out a climate pilot stress test of the Eurosystem balance sheet in 2022.

3 Vision and priorities for ESG sustainability

3.1 Vision

Environmental sustainability, social inclusion and fairness, transparency and governance practices are now key issues, with a visible and material impact on public policies and on the business strategies and models of firms and financial institutions.

As described in the previous section, the Banco de Portugal, like the majority of central banks and financial supervisors, is closely monitoring this reality and has been integrating ESG sustainability concerns – in particular the environmental pillar and, within it, climate change concerns – into its policies and internal management.

In the next four years, the Banco de Portugal intends to enhance ESG sustainability by continuing and deepening the path followed in recent years. To materialise this strategic ambition in the field of ESG sustainability, the Bank will adopt the motto:

..... “Action for sustainability”

, which reflects the spirit that should encourage the daily action of the Bank’s employees.

Continuing the trend of the last three years, and given the relevance of environmental risks, the environmental pillar will be dominant and will continue to require more in-depth, cross-cutting attention from the Bank. This will require a considerable effort of national, and above all, international coordination, the Bank being involved in around twenty specific structures.

3.2 Priorities

Within the framework of the strategic guidelines (SGs) for the next four-year period, the Bank has established a number of priority initiatives (PIs) that are relevant to guide its ESG sustainability actions, namely:

SG 1 | Financial system robustness

PI 4 – To monitor the implications of climate change and energy transition for monetary policy and financial stability.

SG 2 | Protection of the banking market

PI 3 – To monitor developments and the sustainability of institutions’ business models, focusing on digital transformation, operational resilience and environmental risk management.

SG 3 | Recovery and resilience of the economy

PI 1 – To help increase knowledge of public policy issues by means of a more systematic approach, encouraging further debate and analysis and an evaluation culture.

PI 2 – To invest in data compilation and production to support the analyses and studies required for advising on economic agents’ behaviour.

SG 4 | Confidence and influence on society

PI 3 – To enhance social responsibility and sustainability in terms of environmental, social and corporate governance parameters.

SG 5 | Governance and internal management

PI 6 – To advance the project to concentrate the Bank's services dispersed across Lisbon in a new building.

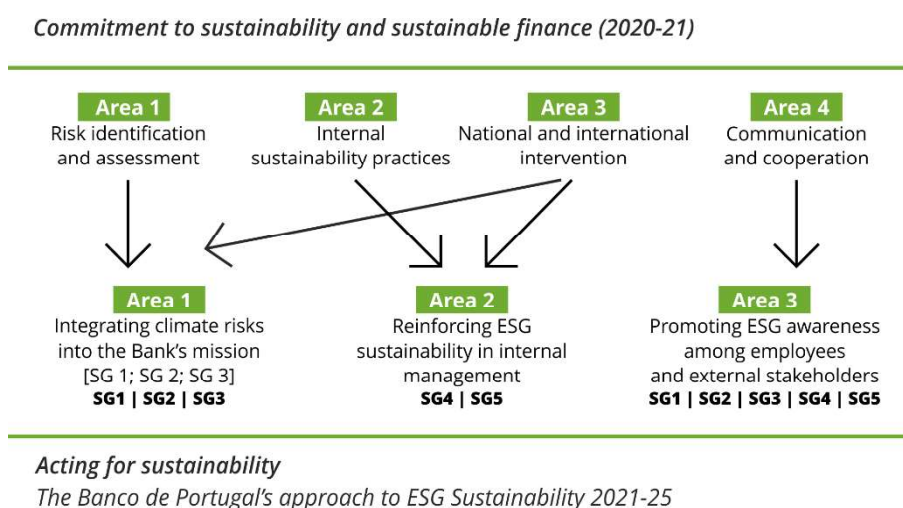
PI 9 – To diversify assets under management, taking into account profitability and risk vectors.

In view of these guidelines and priorities, set out in the Strategic Plan 2021-25, the Bank will adopt three focus areas to enhance ESG sustainability within its mandate:

- Area 1 – Integrating climate risks into the missions of the Banco de Portugal;
- Area 2 – Reinforcing ESG sustainability in internal management;
- Area 3 – Promoting ESG awareness among employees and external stakeholders.

As illustrated in Figure 1, the three areas now outlined for the horizon of the Strategic Plan 2021-25 correspond to areas 1, 2 and 4, as set out in the *Commitment to Sustainability and Sustainable Finance* for the 2020-21 horizon (with Area 3 of the 'Commitment' – National and international intervention – having been integrated into the new areas 1 and 2):

Figure 3.1 • From 'Commitment to Sustainability and Sustainable Finance' to 'Action for Sustainability – the Banco de Portugal's approach to ESG sustainability 2022-25'



Area 1 – Integrating climate risks into the missions of the Banco de Portugal

Interactions between the environment and the financial system and between the environment and monetary policy raise many relevant issues that the Bank must continue exploring, otherwise it will fail to fulfil its mission.

It is important to understand the implications and transmission channels of environmental risks and transition policies to cyclical and structural developments in the economy, to the financial system and the conduct of monetary policy, and to incorporate climate-related factors into economic forecasting and analysis models.

To this end, the Bank will:

- Build databases to make it possible to identify and quantify the impacts of climate risks on financial stability;
- Assess the exposure and resilience of the Portuguese banking system to climate-related risks and develop climate stress testing capacities. Work is under way to assess the sensitivity of

banks' exposures to a carbon tax and to model the credit risk of non-financial corporations based on scenarios provided by the NGFS, notably considering the incorporation of sectoral gross value added (GVA) projections and differentiation at firm level according to their emissions;

- Assess the alignment of Portuguese banks' risk management and reporting practices with supervisory expectations and take the necessary actions;
- Adapt the models and methodologies underlying monetary policy analysis and operations, with a view to attaining the primary objective of price stability, while ensuring prudent risk management. The Bank will contribute to the work within the ECB roadmap to include climate change considerations in the monetary policy strategy, released in July 2021. In this context, the Bank will promote the adaptation of the climate stress testing of the Eurosystem balance sheet to its own balance sheet by 2025;
- Invest in data compilation and production to feed climate change-related analyses and studies;
- Incorporate climate change considerations into the research agenda to inform public policies. In this context, the Banco de Portugal participates in a project led by the APA – the Portuguese Environment Agency, the results of which should be released by the end of 2023 (see Box 1). In addition to leading the assessment of the macroeconomic effects of climate change, the Bank will also be involved in assessing socio-economic scenarios, modelling sectoral impacts, identifying adaptation measures, developing adaptation narratives for the various sub-regions and also communicating and managing the project.

Area 2 – Reinforcing ESG sustainability in internal management

In **managing its own investment assets**, the Banco de Portugal will:

- Gradually strengthen the principles of sustainable and responsible investment. The following are expected, within the horizon of the Strategic Plan 2021-25: (i) the transition of part of the existing portfolios to responsible investments; (ii) possibly, at a second stage, the setting-up of portfolios devoted to sustainable investments; and (iii) the reinforcement of exposure to corporate bonds that incorporate ESG sustainability parameters;
- Publish a responsible investment letter during 2022;
- Release, as of the first quarter of 2023, information on environmental metrics for the portfolio of own investment assets, in line with the goals announced by the Eurosystem in February 2021;
- Continue to participate in national and international working groups with the aim of establishing mandatory harmonised reporting templates and requirements for environmental metrics.

In 2023 the Banco de Portugal will also publish a roadmap to **reduce its ecological footprint as an organisation** and align its internal management activities with the limit of increasing the average global temperature by 1.5°C as advocated in the Paris Agreement and with the climate neutrality goals set by the European Union and the Portuguese State. The Bank will promote an integrated environmental sustainability policy in building management, ensuring the reduction of consumption on its premises. The project to concentrate the services dispersed across Lisbon in a single building will be particularly relevant from this viewpoint.

A **social responsibility policy** that promotes citizens' economic and financial literacy, the integration of people with disabilities, diversity and equal opportunities should also be pursued.

At **governance** level, among other initiatives, the Bank will:

- Review accountability on ESG sustainability and include ESG reporting in the annual report of the Board of Directors, to be disclosed in 2022;
- Strengthen transparency through evaluation exercises, including by continuing and deepening the 2021 in-house exercise to assess the Banco de Portugal's position regarding the IMF's

Central Bank Transparency Code in the field of anti-money laundering and countering the financing of terrorism.

The integration of ESG principles into the Banco de Portugal's corporate functions requires, as a **precondition**, robust and up-to-date information to support decision-making, management and accountability. To this end, **databases** will be set up to enable:

- Measuring the carbon footprint of own investment financial assets;
- Measuring the Bank's ecological footprint;
- Meeting ESG reporting needs;
- Monitoring the performance of ESG goals and carrying out cost/benefit analyses.

When developing these databases, the Bank will seek to create synergies, including by exploring opportunities for data sharing or joint procurement within the Eurosystem and by ensuring broad based access to data at the Bank for the various purposes for which they may be needed.

Area 3 — Promoting ESG awareness among employees and external stakeholders

The aim is to showcase the work carried out and the results achieved on ESG sustainability through dissemination initiatives, stakeholder dialogue and training, as part of an ESG communication policy that fosters debate and knowledge dissemination. To this end, the Bank will:

- Launch a section devoted to ESG sustainability on the institutional website in 2022;
- Promote awareness-raising activities addressed to its external stakeholders, with a focus on the banking sector, and its employees;
- Incorporate climate concerns into its economic and financial literacy initiatives.