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Climate Change
Risk Overview

Climate change and climate-related risks are a significant challenge faced by financial institutions.

Credit unions should not only consider how climate change impacts their business but must also take into account how business practices and actions may contribute to climate change.

Climate Change

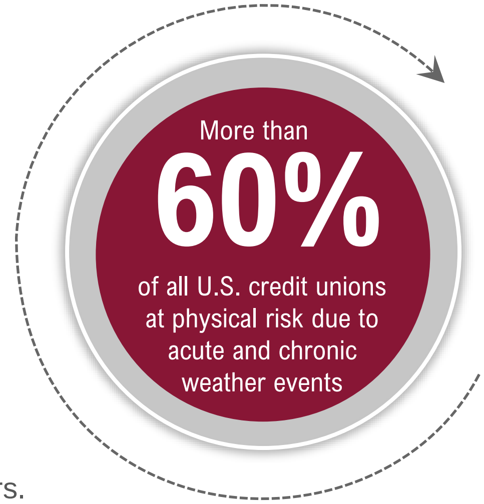
As organizations with a mission and purpose to drive community impact, credit unions can have a significant part to play to ensure that we remain resilient against climate challenges as an industry and as key community leaders and players.

The time to acknowledge the effects of climate change on credit unions is a reality not to be dealt with tomorrow, but an existential challenge to be addressed today.

Climate change poses a great level of risk for credit unions, primarily in the physical and transaction sense. In fact, "**more than 60% of all U.S. credit unions and at least $1.2 trillion in credit union assets** are at physical risk due to acute and chronic climate weather events and hazards," according to a 2022 report (The Changing Climate for Credit Unions) by the Filene Research Institute produced in collaboration with CERES.

While climate change poses great risks to credit union balance sheets, it also offers great opportunities for credit unions to differentiate, grow and meet emerging consumer demands. The report offers seven (7) steps to help credit unions address climate risk:

1. Publicly acknowledge that climate change poses a risk to their balance sheet and to their members.
2. Conduct research and educate themselves, their members, and other stakeholders about climate related risks and opportunities facing their organizations.
3. Begin collecting climate-relevant data for their organization.
4. Adopt the recommendations of the Financial Stability Board's Task Force on Climate-Related Disclosures (TCFD).
5. Conduct climate scenario analysis of their loan portfolios.
6. Invest in their organizations while leveraging partnerships and building system-wide resources.
7. Foster proactive communication among credit unions, national trade associations, state leagues, policymakers, and state and federal regulators.



Extreme Weather Events

Weather events have been growing in intensity in recent decades. An excess of 40 percent of residents in the U.S. reside in counties hit by extreme weather disasters in 2021, while more than 80 percent endured a withering heat wave.

According to the National Oceanic and Atmospheric Administration's (NOAA) National Center for Environmental Information (NCEI), the year 2020 was the most expensive year yet for weather- and climate-related disasters and there were another 20 separate billion-dollar disasters in 2021. This trend is expected to continue as weather and climate-related events increase in occurrence and intensity.

The influence of extreme weather-related events including wildfires, hurricanes, floods and other alarming storms has spread significantly. As the recurrence and severity of these extreme weather and climate events have intensified, so has the cost.

These disasters have an outsized effect on your credit union locations and the health, well-being, economic security and the mobility of vulnerable populations, including low- and moderate-income communities, racial minorities, indigenous populations and children.

Awareness of climate change is very important to mitigate damages and losses before events occur.

Impact on Physical Location of Members & Loan Property

Field of membership may be in geographical areas at high or significant risk of damage or destruction from climate change.

For example, rising sea levels impacting coastal and seaside real estate properties, both commercial and residential, are a continued and growing risk of the climate change impact. These properties are typically valued higher and with insurance companies reevaluating costs and climate change risk; it can impact the affordability and availability of insurance.

As communities, members, industries, and assets are affected, credit unions must consider ways to remain resilient, such as adjusting fields of membership or altering lending portfolios.

Making the lending portfolio sustainable requires diligence. Credit unions that do not make efforts to reduce their exposure through the underwriting of their portfolio will be particularly vulnerable to potential government legislation impacting fossil fuel supply and demand.

As credit unions continue to serve and represent a largely diverse cross-section of the country's population, it is also important to note that many of these communities are underserved and at more risk – including aging members – that could be severely impacted by climate-related events.

Key Questions to Consider

Credit unions need to be aware of these opportunities to address climate risk and incorporate them into their business and financial decision-making.

- How is climate change being treated as an environmental issue and a strategic consideration?
- Has the credit union addressed climate change in polices and business practices?
- What is the credit union's approach to address climate change or corporate commitments to climate change reduction practices?
- Does climate change impact or potentially impact the continuity of business operation?
- How does climate change impact business within your membership communities? Is your credit union able to withstand significant changes?
- Does climate change lead to modifications to property, equipment, branch office locations, and other credit union planning?
- What impact, if any, does climate change have on talent retention and/or recruitment?

Transition risks…

Transition risk stems from the economy seeming to make a move, or transition, towards a lower or net-zero carbon economy, through the reduction of dependence on fossil fuels. Transition risks are policy and legal; technology; market; and reputational.

This in turn represents a shift in the economy and market forces, which can introduce additional costs and perhaps make investments less valuable. Assets that have a high carbon footprint or that are linked to carbon-heavy industries could also be "stranded" meaning the value of some assets used to secure loans could decline in value rather than appreciating.

Physical risks…

- Acute
  event-driven including increased severity of extreme weather events (e.g., hurricanes, floods, etc.)
- Chronic
  longer-term shift in climate patterns (e.g., sustained higher temperatures, rise of sea levels, chronic heat waves, etc.)

Many experts believe climate-related change is moving faster than many financial services leaders realize.

Awareness of climate risk has grown substantially in recent years. Regulators, policymakers, employees, and civil society asking organizations – including financial institutions - to disclose their risk management capabilities and, if needed, take steps to improve them.

The industry outlook:

- Regulators are pushing climate change to the foreground for financial services organizations.
- Rules put in place for organizations may, in time, trickle down to credit unions.
- To remain compliant with evolving rules, credit unions will need to be prepared to adapt.

Critically, credit unions must identify and assess the climate-related risks and opportunities they are exposed to. This goes for business operations, as well as your financial activities.

Organizations should identify and assess exposure to climate risk and develop a planned response. Developing a strategy for navigating climate risks and opportunities requires looking at 'What If' scenarios that show how climate issues might impact credit unions' strategic and financial planning.

Credit unions must identify how they'll transition to a low-carbon and the changing climate. One strategy is to invest in green industries and provide financing to companies focused on climate change, thereby reducing climate risk in their lending portfolios.

Climate Change Risk Overview

Considerations in four core areas of operations

Governance

Disclose the organizations governance around climate-related risks and opportunities

- What is the Board's oversight of climate-related risks and opportunities?
- What is management's role in assessing and managing climate-related risks and opportunities?

Strategy

Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's business strategy and financial planning. Consider…

- Which climate-related risks and opportunities can be identified over short, medium, and long term?
- What is the impact of climate-related risks and opportunities on the organization's business, strategy, and financial planning?
- Does the organization have a business resiliency strategy that considers climate-related scenarios?

Risk Management

Disclose how the organization identifies, assesses, and manages climate-related risks

- What is the process for identifying and assessing climate-related risks?
- What is the process for managing climate-related risks?
- Are the processes for identify and managing climate-related risk integrated into the overall risk management of the organization?

Metrics & Targets

Disclose the metrics & targets used to assess and manage relevant climate-related risks / opportunities

- Are the metrics used to assess risks and opportunities in line with the organization's strategy and risk management process?
- What targets will be used to manage climate-related risks and opportunities and performance against targets?

What else should be considered?

- Hybrid or remote work models; public transportations and other carpool commuter options and incentives
- Physical structure adoption of green building benefits
- Environmental impact program to encourage suitability and action commitments by employees, membership, and Field of Membership communities
- Adoption and active commitment to corporate policies and governance to reduce carbon footprint and further mitigation strategies within the organization and surrounding communities through investments and business strategies
- Develop and implement climate risk governance from Board, management, staff, and members
- Tailor business, loan, and credit strategies
- Align climate risk exposures with risk processes, risk appetite, and business strategy

Climate change does not stand alone; it stands within other risks and exacerbates them. Physical risks brought on by climate change can present a microscale of physical damages but can also create macro-changes on the economic side.

As a primary example, the agriculture industry may suffer due to changing weather patterns and issues with crops. Additionally, housing prices may fall due to constant flooding in new areas etc. These are all prominent issues that could become harsh realities.

Transformational change is necessary to confront and adapt to the increasingly severe impacts of climate change. Credit unions are in unique position to aid in this transformation.

Why It Matters…

Climate changes affects all of us. As climate-related events accelerate, credit unions can expect significant impact on our most vulnerable people and communities, those that often lack the finances and supporting infrastructure to withstand and recover from these disasters.

Experience shows that credit unions who are most responsive to member needs during or immediately after climate crises are rewarded with member growth, visibility, and loyalty – which can also lead to long-term sustainability of the credit union and community.

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