PKF O'CONNOR DAVIES
ACCOUNTANTS AND ADVISORS

The Impact of Climate Risk Management on Quantitative Easing and Beyond

By Emily M. Berger, CFA, Director of Investment Risk Advisory and Director, Sustainability, Financial Services

Climate risk is the latest existential threat in the portfolio of 2021 worries. While most Americans have endured a brutally hot, humid and inclement summer, it can be hard to see the connection between climate risk and the economy beyond higher prices for commodities, including fruits and vegetables, and related supply chain issues.

However, as the Federal Reserve contemplates the timeline for the quantitative easing of mortgage-backed securities (MBS) and commercial mortgage-backed securities (CMBS) purchases, climate risk is a key consideration in prepayment model methodology which must be integrated beyond the myriad of idiosyncratic factors such as ability and willingness to pay mortgage interest and principal, location, the projected path of interest rates, inflation pressures, among others. Gone are the days when the projected path of interest rates, real estate type and location analysis, and market factors are sufficient pricing model inputs.

Institutional investor, asset manager, private credit fund, and hedge fund purchases of residential and commercial MBS have the advantage of providing a floor to valuations and critical support in a highly uncertain time. Another support is provided by the initiative to build up the lending books of regional and community banks across the country. This diversified lending approach provides a variety of sources of capital which enhances the probability of a soft landing that is not government dependent. The Paycheck Protection Plan (PPP) program introduced many borrowers to the advantages of developing a bank relationship with a local lender that understands their particular needs. Borrowers received a PPP loan that was forgiven by the Small Business Association provided the borrower followed the program guidelines, a very unique program that provided critical financial support to small businesses during an especially challenging pandemic period. This process disaggregated the reliance on universal banks and matched borrowers and lenders in a curated way.

While it is still early days for banks to fully integrate climate risk into their credit underwriting process, planning for idiosyncratic risk is part of the analysis. The Task Force on Climate-Related Financial Disclosures was convened to formalize an approach of determining the important factors related to climate risk, beyond the consideration of business continuity risks.

The recent global urgency on the topic of climate risk and decarbonization was further magnified last week by the newly published report from the United Nations Intergovernmental Panel on Climate Change.

Public companies and their investors should note that the trajectory in improved transparency from utilities and power providers and clarified measurement standards will help to provide more consistency to the exercise of distilling the impact that new climate change legislation and guidelines have from a risk and investment perspective.

Contact Us

For practical advice on integrating the factors relevant to consistent carbon measurement into your investment and corporate decision-making, please contact any of the following:

Marc L. Rinaldi, CPA
Partner-in-Charge
Financial Services
mrinaldi@pkfod.com | 646.449.6309

Emily M. Berger, CFA
Director of Investment Risk Advisory and Director, Sustainability
Financial Services
eberger@pkfod.com | 646.699.2914

Eric P. Gelb, CPA
Senior Managing Director, Business Development
Financial Services
egelb@pkfod.com | 914.341.7049

www.pkfod.com

About PKF O'Connor Davies

PKF O'Connor Davies, LLP is a full-service certified public accounting and advisory firm with a long history of serving clients both domestically and internationally. With roots tracing to 1891, twelve offices in New York, New Jersey, Connecticut, Maryland and Rhode Island, and more than 1,000 professionals, the Firm provides a complete range of accounting, auditing, tax and management advisory services. PKF O'Connor Davies is ranked 29th on *Accounting Today*'s 2019 "Top 100 Firms" list and is recognized as one of the "Top 10 Fastest-Growing Firms." PKF O'Connor Davies is also recognized as a "Leader in Audit and Accounting" and is ranked among the "Top Firms in the Mid-Atlantic," by *Accounting Today*. In 2020, PKF O'Connor Davies was named one of the 50 best accounting employers to work for in North America, by *Vault*.

PKF O'Connor Davies is the lead North American representative in PKF International, a global network of legally independent accounting and advisory firms located in over 400 locations, in 150 countries around the world.

Our Firm provides the information in this e-newsletter for general guidance only, and it does not constitute the provision of legal advice, tax advice, accounting services, or professional consulting of any kind.