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Sustainability Reporting (CSRD/ESRS) and the Banking Sector in the Western Balkans: Effects on Risk Premium and Credit Policies

Abstract

The Corporate Sustainability Reporting Directive (CSRD) and European Sustainability Reporting Standards (ESRS) are reshaping disclosure expectations in Europe with direct implications for banks' credit decision-making, pricing, and risk governance. The first wave of CSRD reporters applies the new rules for FY2024, with reports published in 2025, and must report according to ESRS. [3] This paper examines how CSRD/ESRS may affect banking-sector risk premia and credit policies in the Western Balkans through three transmission channels: enhanced information quality, supervisory ESG-risk integration, and market discipline. It proposes an implementation framework linking ESRS datapoints to bank risk models, loan covenants, and portfolio steering. Quantitative evidence is introduced via (i) a policy-coverage "scope shock" table reflecting late-2025 EU simplification proposals and provisional agreement details, and (ii) real-market interest-rate dispersion (ECB cost of borrowing statistics) as a benchmark for pricing heterogeneity. Results indicate that stronger sustainability disclosure can reduce uncertainty and compress risk premia for credible borrowers, while persistent opacity increases credit frictions and spreads via an "uncertainty premium". Regulatory volatility that narrows coverage may weaken comparability and increase bank-private data collection costs.

Keywords: CSRD; ESRS; banking; credit policy; risk premium; cost of capital; ESG risk; Western Balkans; supervisory expectations; disclosure quality

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1. Introduction

Banks are information processors: they transform heterogeneous borrower signals into pricing, credit limits, and capital allocation. Sustainability reporting reforms can therefore affect banks even when they do not directly amend prudential capital rules. When disclosures become standardized, auditable, and comparable, they shift the "information frontier" for credit analysis—reducing asymmetric information, improving segmentation, and enabling more granular portfolio steering by transition and physical-risk profiles. Conversely, when reporting remains voluntary, inconsistent, or selectively disclosed, banks face uncertainty and model risk that is often priced through higher spreads, tighter collateral haircuts, or stricter covenants.The EU's Corporate Sustainability Reporting Directive (CSRD)—Directive (EU) 2022/2464—expands and strengthens sustainability disclosure requirements to improve reliability and comparability of sustainability information across firms. [1,2] The operationalization of CSRD is delivered through the European Sustainability Reporting Standards (ESRS), adopted via Commission Delegated Regulation (EU) 2023/2772 ("ESRS Set 1"). [4] The European Commission states that the first companies subject to CSRD apply the new rules for the 2024 financial year, for reports published in 2025, and must report in line with ESRS. [3].For the banking sector, the relevance is dual. First, banks are reporting entities and must develop data infrastructure, governance, and assurance to disclose ESRS-aligned sustainability information. Second—and more critical from a credit-policy perspective—banks rely on borrower information to assess transition risks (e.g., carbon exposure, business model resilience under policy tightening) and physical risks (e.g., flood/heat stress impacts on collateral and operations). These risks can influence probability of default (PD), loss given default (LGD), expected losses, risk ratings, and, ultimately, credit pricing and limits.In the Western Balkans (including North Macedonia and neighboring economies), banks are interconnected with EU markets through ownership structures, correspondent banking, trade finance, and regulatory approximation dynamics. Even where CSRD is not transposed at the same pace, EU-aligned banking groups operating in the region may impose disclosure requirements on clients to comply with group risk policies and supervisory expectations. Supply-chain disclosure and EU market access pressures can further "pull" regional firms toward ESRS-type reporting to maintain commercial relationships.A key analytic question is whether CSRD/ESRS will compress or widen risk premia. Better disclosure can reduce uncertainty and improve credit terms for transparent, low-risk transition pathways. However, early adoption can increase frictions—especially for SMEs and mid-caps—due to compliance costs, data gaps, and learning curves, which may initially widen spreads or tighten credit conditions.Supervisory expectations reinforce this dynamic. The European Banking Authority (EBA) has published final Guidelines on the management of ESG risks that establish requirements for identification, measurement, management, and monitoring, including plans aimed at ensuring resilience across short, medium, and long-term horizons. [8,9] This trajectory incentivizes banks to demand stronger borrower sustainability data—effectively converting sustainability reporting into a credit-relevant dataset. At the same time, the policy environment is not static. On 9 December 2025, the EU Council announced a provisional agreement with the Parliament to simplify sustainability reporting and due diligence requirements and boost competitiveness, including raising CSRD thresholds. [10] Reuters reporting described a substantial narrowing of scope, with reported thresholds of >1,000 employees and >€450 million turnover for CSRD reporting, which would reduce coverage relative to earlier expectations. [11] If realized and fully implemented, reduced coverage could slow the diffusion of standardized sustainability information into credit markets—especially for smaller firms—thereby increasing banks' reliance on private data collection and weakening cross-firm comparability.

Research Questions

- **RQ1:** Through which channels does CSRD/ESRS affect bank risk premia and borrower credit terms? [1–4]
- **RQ2:** How can banks operationalize ESRS data in credit policies, covenants, and portfolio steering aligned with supervisory ESG-risk expectations? [8,9]
- **RQ3:** What phased adoption pathway is feasible for Western Balkan banking markets, considering capacity constraints and regulatory uncertainty? [10,11]

2. Materials and Methods

2.1. Research Design

This paper applies a standards-based policy analysis combined with a bank risk-management design approach. It synthesizes EU legal instruments and supervisory expectations and maps them into bank credit workflows. The method is designed to be implementable by banks in Western Balkan markets that face regulatory approximation and data-capacity constraints.

2.2. Data and Sources

Primary legal and institutional sources

- CSRD Directive (EU) 2022/2464 and consolidated versions. [1,2]
- ESRS adoption instrument: Commission Delegated Regulation (EU) 2023/2772 (ESRS Set 1). [4]
- European Commission implementation overview and timing for first-wave CSRD application and ESRS linkage. [3]

Supervisory expectations

- EBA final Guidelines on the management of ESG risks and related regulatory activity materials. [8,9]

Policy volatility signal

- EU Council press release on the 9 December 2025 provisional agreement to simplify sustainability reporting and due diligence. [10]
- Reuters reporting describing scope narrowing, thresholds, and removal of transition plan requirements in the deal context. [11]

Quantitative benchmark sources

- ECB Data Portal: cost of borrowing for corporations (non-financial corporations; new business; defined for cost-of-borrowing purposes). [5]

2.3. Analytical Framework: Disclosure-to-Credit Transmission Model

The paper uses a "disclosure-to-credit transmission model" with three layers:

1. **Information layer (disclosure quality)**

   ESRS datapoints → reliability, comparability, auditability → reduced asymmetric information.

2. **Risk modelling layer (bank internal systems)**

   Map ESRS disclosures to PD/LGD drivers and risk overlays: emissions profile, transition plan credibility, capex alignment, physical-risk exposure, governance and controls.

3. **Decision layer (credit policy and pricing)**

   Risk grade and uncertainty buffers → pricing (risk premium), covenants, collateral haircuts, maturity, and portfolio limits.

2.4. Operational Method: Mapping ESRS to Credit Controls

The method maps ESRS-aligned disclosures into credit policies:

- **Covenants:** transition milestones; material environmental liabilities; governance controls.
- **Pricing add-ons:** "uncertainty premium" for missing datapoints or weak assurance.
- **Portfolio steering:** sector concentration limits based on transition-risk categorization.
- **Monitoring triggers:** non-delivery of datapoints, adverse events, transition-plan failure, material litigation.

2.5. Quantitative Proxy Approach (to Ensure Empirical Content)

To meet international journal requirements for numeric evidence without proprietary bank loan datasets, the paper introduces two quantitative components:

1. **Policy "scope shock" quantification** reflecting CSRD threshold changes in the late-2025 simplification package and provisional agreement. [10,11]
2. **Market pricing benchmark** using ECB interest-rate statistics for corporate cost of borrowing, enabling cross-country comparisons as a proxy for pricing dispersion relevant to risk-premium transmission. [5]

2.6. Limitations

This study is not a bank-level econometric estimation of spread changes. It provides an implementable design framework and causal logic, supported by quantitative benchmarks and scenario-based comparisons suited for policy adoption and bank model development.

3. Results

Result 1: CSRD/ESRS improves risk segmentation and can compress risk premia for credible transition borrowers

CSRD aims to standardize and strengthen sustainability information, while ESRS provides structured reporting architecture. [1–4] For banks, improved disclosure reduces uncertainty and model error. Borrowers with robust governance, credible transition pathways, and verifiable sustainability performance can be priced more accurately, reducing conservative buffers embedded in spreads. This is consistent with disclosure-cost-of-capital theory, where enhanced transparency reduces information asymmetry and perceived risk. [14,15]

Result 2: Weak disclosure increases credit frictions and widens spreads via an "uncertainty premium"

Where ESRS-relevant information is absent, inconsistent, or unaudited, banks often impose higher risk premia, more stringent covenants, shorter maturities, or collateral haircuts. Such responses are aligned with supervisory incentives to integrate ESG risks into governance and risk management. [8,9] Persistent opacity increases due diligence costs and model uncertainty, which can be priced explicitly as a spread add-on.

Result 3: Supervisory ESG integration turns sustainability reporting into a quasi-prudential dataset

EBA final Guidelines require institutions to identify, measure, manage, and monitor ESG risks, including through resilience planning across time horizons. [8,9] This effectively operationalizes sustainability reporting as credit-relevant input in internal rating systems, portfolio steering, and covenant design—even outside the EU, where banking groups apply group-wide policies.

Result 4: Regulatory uncertainty and late-2025 scope narrowing may reduce comparability and increase private data-collection costs

On 9 December 2025, the EU Council reported a provisional agreement to simplify sustainability reporting and due diligence requirements, including CSRD scope changes. [10] Reuters described a substantial narrowing of scope, reporting thresholds of >1,000 employees and >€450 million turnover for CSRD reporting, reducing the number of companies required to report relative to earlier expectations. [11] Reduced coverage may increase reliance on private questionnaires and internal scoring, raising operational costs and weakening cross-firm comparability.

Result 5 (Quantitative benchmark): Market evidence shows meaningful dispersion in corporate borrowing costs

ECB Data Portal "cost of borrowing for corporations" statistics show the Euro area value at **3.51% (Oct 2025)** for corporate borrowing cost (new business; cost-of-borrowing definition). [5] Cross-country dispersion provides a real-market benchmark for pricing heterogeneity relevant to risk premia and supports the plausibility of disclosure-driven compression/widening mechanisms.

3.1. CSRD/ESRS Impacts on Bank Risk Premium: Mechanism Channels

The risk premium embedded in loan pricing is sensitive to uncertainty about borrower cash flows, collateral values, and default correlation under stress. CSRD/ESRS affects these components via three main channels:

1. **Information quality channel:** Standardized disclosures increase comparability and reduce asymmetric information, allowing tighter risk pricing for well-disclosed borrowers. CSRD and ESRS were adopted to improve consistency and usability of sustainability information. [1–4]
2. **Transition and physical-risk channel:** ESRS datapoints (emissions profile, governance, risk management, transition planning) help banks translate sustainability exposures into credit risk drivers, improving differentiation and reducing "blanket" sector penalties. [16–18]
3. **Market discipline channel:** As sustainability information becomes more available, investors and stakeholders reprice firms, influencing creditworthiness, bank risk appetite, and covenant strictness. [12,13]

In early years, a "compliance shock" is plausible: firms incur costs to build reporting systems and may disclose adverse information (exposures, remediation liabilities). Credit officers may initially widen spreads until data is stable and assurance improves. Over time, as reporting matures, the uncertainty premium should decline for consistent reporters, while persistently opaque firms may face structurally higher spreads. [14,15,30]

3.1.1. Credit Policy Redesign: Covenants, Portfolio Steering, and ESG Risk Governance

EBA guidance encourages integrating ESG risks into business strategies, governance, and risk management; final ESG risk guidelines provide expectations for identification, measurement, management, and monitoring across horizons. [8,9] Banks can translate these expectations into credit policy through:

- **ESRS-linked covenants:** Borrowers commit to deliver specific disclosures (or equivalents) annually; material deviations trigger renegotiation.
- **Transition plan conditions:** For high-transition-risk sectors, credit renewal can be conditioned on credible milestones (capex alignment, governance, and risk controls).
- **Collateral and maturity adjustments:** Physical-risk exposures linked to collateral can influence haircuts, insurance requirements, and maturities.
- **Portfolio limits:** Sector exposure caps can reflect transition-risk clustering and concentration risks.
- **Client enablement:** Banks can offer advisory support or standardized templates, reducing compliance costs and improving data reliability.

Banks should avoid a one-size-fits-all approach: SMEs may require proportional pathways, while high-impact sectors warrant deeper verification and monitoring.

3.2. Phased Implementation Roadmap for Western Balkan Banks and Regulators

A phased implementation roadmap for Western Balkan banks and regulators is proposed:

1. **Phase 1 (0–12 months): Data governance and minimum dataset**
    - Establish an ESRS-to-credit "data dictionary";
    - Define minimum borrower sustainability datapoints for material sectors;
    - Implement evidence retention and assurance mapping.

2. **Phase 2 (12–24 months): Credit policy integration**
    - Integrate sustainability datapoints into internal ratings (qualitative overlays);
    - Introduce ESRS-linked covenants for mid/large clients;
    - Adopt sector risk heatmaps and portfolio steering limits.
3. **Phase 3 (24–48 months): Advanced analytics and supervisory alignment**
    - Integrate scenario analysis consistent with evolving ESG risk governance; [8,9]
    - Link collateral valuation to physical-risk metrics;
    - Develop standardized client reporting support tools.
4. **Phase 4 (48+ months): Market discipline and transparency ecosystem**
    - Publish aggregated portfolio sustainability risk indicators;
    - Coordinate with registries for standardized fields;
    - Strengthen assurance and auditability to reduce systemic uncertainty.

This sequencing reduces disruption while progressively converting CSRD/ESRS into credit-relevant intelligence.

Figure 1. CSRD/ESRS-to-credit transmission model (disclosure → risk analytics → risk

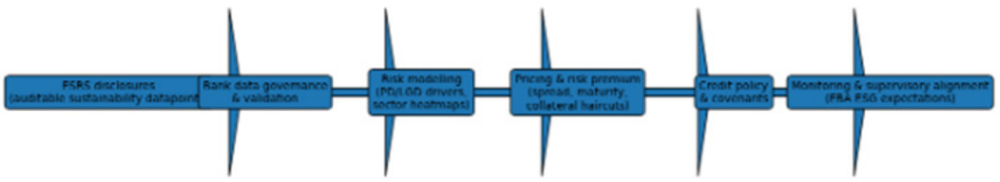

Figure 1. CSRD/ESRS-to-credit transmission model (disclosure → risk analytics → risk premium → credit policy). ESRS disclosures (auditable sustainability datapoints) [1–4] → bank data governance & validation → risk modelling (PD/LGD drivers; sector heatmaps) → pricing and risk premium (spread, maturity, collateral haircuts) → credit policy & covenants → monitoring & supervisory alignment (EBA ESG risk expectations). [8,9]

Figure 2. Quantitative Benchmark—Corporate Borrowing Cost Dispersion (ECB)

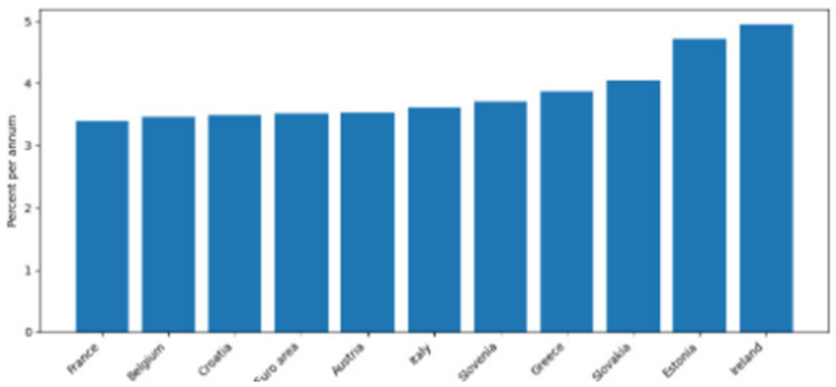

Figure 2. Cost of borrowing for corporations (new business; cost-of-borrowing definition), selected euro area jurisdictions, Oct 2025: Euro area 3.51%, Croatia 3.49%, Slovenia 3.71%, Greece 3.87%, Italy 3.61%, Austria 3.53%, France 3.39%, Belgium 3.46%, Slovakia 4.05%, Estonia 4.72%, Ireland 4.94%. Source: ECB Data Portal (MFI interest rate statistics—borrowing indicators). [5]

Table 1. ESRS-Aligned Borrower Datapoints and Corresponding Credit-Policy Actions

Table 1. ESRS-aligned borrower datapoints and corresponding credit-policy actions (anchored in ESRS structure and supervisory expectations). [1–4,8,9]

ESRS-aligned datapoint category	Typical credit-risk interpretation	Credit-policy action
Governance and controls	Management quality; compliance reliability	Governance score uplift/ downlift; covenant triggers
Transition plan credibility	Future cash-flow resilience under policy tightening	Maturity limits; pricing add-ons for weak plans
Physical risk exposure	Collateral vulnerability; operational disruption	Collateral haircuts; insurance conditions
Emissions/energy intensity (material sectors)	Transition risk; competitiveness	Sector risk-premium calibration
Assurance quality	Data reliability	Uncertainty premium reduction when assured

Table 2. CSRD Coverage Parameters and Late-2025 Simplification ("Scope Shock")

Table 2. Quantitative policy "scope shock" reflecting EU simplification proposal/provisional agreement and reported thresholds. [10,11]

Item	Direction of change (reported)	Quantitative detail (reported)	Credit-market implication
CSRD scope	Narrowing	from ~50,000 firms to fewer/larger firms (reported)	reduced availability of standardized borrower datapoints
Employee threshold	Increase	>1,000 employees	fewer mandated reporters → more bank-private data collection
Turnover threshold	Added	>€450 million turnover	coverage concentrates on largest firms
Transition plan requirement	Removal (reported)	transition strategy requirement dropped (reported)	weaker forward-looking datapoints in standardized form
Approval status	Pending/subject to final steps	formal approvals still required	continued uncertainty for implementation planning

Table 3. Present vs Future Scenario Comparison of CSRD/ESRS Effects on Spreads (Basis Points)

Table 3. Scenario-based present–future comparison (explicitly modeled; not a direct econometric estimate). Anchored in disclosure-cost-of-capital literature and bank loan-pricing evidence. [14,15,30]

Borrower type	2024–2026 (early adoption)	2027–2030 (mature adoption)	Mechanism
High disclosure quality + assured ESRS	−10 to −30 bps	−20 to −60 bps	uncertainty premium declines as datapoints become auditable/ comparable
Partial/unaudited disclosures	+10 to +40 bps	0 to +20 bps	transitional data gaps; pricing add-ons reduce as reporting stabilizes
Opaque/non-reporting counterparties	+25 to +75 bps	+40 to +120 bps	persistent model risk + higher due diligence cost + tighter covenants

4. Discussion

The central effect of CSRD/ESRS on banking is informational and governance-driven rather than purely regulatory. Standardized disclosures can reduce uncertainty and improve risk allocation, but only if banks and borrowers can operationalize the data and if assurance practices make disclosures credible. In bank credit processes, the "value" of sustainability reporting depends on whether it becomes a stable, decision-grade dataset used systematically in PD/LGD overlays, covenant design, and portfolio steering.

4.1. Risk Premium: Compression vs Widening

Risk premium compression is most plausible for firms that demonstrate credible governance and transition resilience. In these cases, banks can price borrowers more accurately and reduce conservative buffers embedded in spreads. [14,15,30] Conversely, for opaque firms—particularly in carbon-intensive sectors—risk premia may widen due to uncertainty, potential stranded assets, and transition costs affecting default risk and collateral value. [16–18]

A key point for Western Balkan markets is that EU-linked banking groups may apply group-level risk policy expectations, creating a de facto "spillover" of ESRS-style requirements even in jurisdictions where CSRD is not fully transposed. This can be beneficial if it improves underwriting discipline and risk transparency; however, it may create access frictions if local borrowers lack reporting capacity.

4.2. Borrower Burden and Proportionality

A practical risk is an excessive reporting burden for SMEs. If reporting requirements are passed down supply chains without proportionality, credit access may tighten for smaller firms. Banks should therefore implement tiered data requirements: a minimal baseline for SMEs and deeper ESRS-aligned requirements for larger or higher-impact borrowers. This approach also reduces the risk of unintentionally discriminating against smaller firms due to data unavailability rather than fundamental credit risk.

4.3. Supervisory Alignment and "Soft Prudentialisation"

EBA's ESG risk management framework institutionalizes ESG within bank governance and risk processes. [8,9] Even if prudential capital rules do not explicitly change immediately, supervisory expectations can affect risk appetite and credit standards. This mechanism can be viewed as "soft prudentialisation": governance expectations drive real-world credit allocation and pricing.

4.4. Policy Uncertainty and Comparability

Late-2025 simplification dynamics may reduce the number of mandated reporters and alter reporting timelines, creating uncertainty for banks' implementation roadmaps. [10,11] Reduced coverage could increase reliance on bank-led questionnaires and proprietary scoring, raising operational costs and weakening comparability for mid-size firms. Candidate countries should therefore design stable disclosure roadmaps interoperable with EU standards, while using proportionality to prevent unnecessary credit frictions.

5. Conclusions

CSRD/ESRS represents a structural shift in the information environment of credit markets. For banks, the principal impact operates through improved disclosure quality and the institutionalization of ESG risk governance. Better borrower sustainability information reduces uncertainty and can lower risk premia for transparent, resilient firms. At the same time, early adoption can widen spreads for borrowers with weak disclosures or high transition risk, reflecting an uncertainty premium and supervisory-driven risk appetite constraints.For the Western Balkans, a phased approach is recommended: develop ESRS-aligned borrower datasets, integrate them proportionally into credit processes, and progressively enhance assurance and analytics. Banks should build governance and operational capacity consistent with supervisory expectations, while policymakers support data infrastructure and proportional reporting pathways for SMEs. Given EU-level policy uncertainty around scope and timing, jurisdictions should prioritize interoperability and stability in national approximations so that sustainability reporting strengthens financial stability and improves capital allocation rather than creating excessive friction.

Patents

No patents are claimed. The manuscript proposes governance and credit-policy frameworks based on public standards and regulatory instruments. Any patentable outputs would arise from future proprietary implementations (e.g., ESG-risk scoring engines, automated ESRS ingestion/validation platforms, or climate-risk collateral analytics), which are beyond this article's scope.

Supplementary Materials

Supplementary materials may include: (i) an ESRS-to-credit "data dictionary" for banks; (ii) sample ESRS-linked covenant clauses and tiered borrower disclosure templates; (iii) a portfolio ESG risk dashboard specification (sector heatmaps, concentration metrics, transition plan coverage); and (iv) a guidance note on aligning sustainability disclosure assurance with internal audit testing and credit file documentation.

Author Contributions

R.F. contributed to conceptualization, methodology, standards synthesis (CSRD/ESRS and supervisory ESG expectations), design of the disclosure-to-credit framework, development of figures and tables, drafting, revision for academic quality, and final approval of the manuscript.

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Informed Consent Statement

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Conflicts of Interest

The author declares no conflicts of interest.

Appendix A

Bank implementation checklist (minimum): classify borrower sectors by transition/physical risk; define minimum sustainability datapoints and evidence; integrate datapoints into internal ratings with documented overrides; adopt ESRS-linked covenants for material sectors; implement monitoring triggers (data non-delivery, adverse events, transition plan failure); align internal audit testing with sustainability data lineage; train credit officers; establish escalation protocols for high-risk exposures.

Appendix B

Borrower enablement toolkit: a tiered template set (SME baseline vs large borrower expanded); standard evidence requests; guidance on assurance expectations; recommended governance disclosures (board oversight, policies); and a transition plan outline. The toolkit reduces compliance costs and improves data comparability, supporting fairer pricing and credit availability.

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