Climate Scenario Analysis for Resilient Strategy

Jacob Park

Director, Sustainable Futures Lab

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The Business of a Better World

TCFD & Climate Scenario Analysis

TCFD | TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

TCFD Technical Supplement: The Use of Scenario Analysis in Disclosure of Climate-related Risks and Opportunities (June 2017)

"For many organizations, the most significant effects of climate change are likely to emerge over the medium to longer term, but their precise timing and magnitude are uncertain. This uncertainty presents challenges for individual organizations in understanding the potential effects of climate change on their businesses, strategies, and financial performance. To appropriately incorporate the potential effects of climate change into their planning processes, organizations need to consider how climate-related risks and opportunities may evolve and their potential business implications under different conditions. [...]

Given the importance of forward-looking assessments of climate-related risk, the Task Force believes that scenario analysis is an important and useful tool for an organization to use, both for understanding strategic implications of climate-related risks and opportunities and for informing stakeholders about how the organization is positioning itself in light of these risks and opportunities. It also can provide useful forward-looking information to investors, lenders, and insurance underwriters."

Why Scenario Analysis?

THE WALL STREET JOURNAL.

Predictions have a dire track record, and have been sadly predictable themselves. Treasury yields have been forecast to rise every year for the past decade [...] yet they have gone down more often than not. Even when they went up, the moves were only once anywhere near what was predicted, back in 2009

The same goes for stock prices. Only rarely is the average S&P 500 forecast of strategists anywhere near the actual result.

The Wall St Journal (March 2018)

Models Often Not Fit for Purpose

External

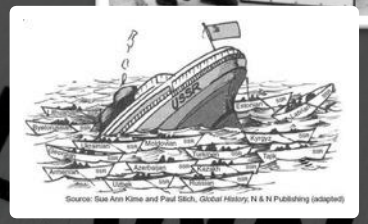
- **The global operating environment** for business is changing in ways that are volatile, uncertain, complex, and ambiguous (VUCA).
- Nonlinear changes are difficult to quantify or model
- Climate change is a “threat multiplier”

Internal

- Our brains evolved with cognitive biases that make it **difficult for us to think realistically about uncertain futures.**
- We rely too much on extrapolation and status quo thinking.
- We frequently respond to uncertainty with denial (oversimplification or false confidence) or paralysis (planning for everything or wait and see).

Scenario a well-known tool to improve strategic thinking in uncertain times

Developed at RAND corporation in 1940s and 1950s to enable **US military to "think the unthinkable"**



Migrated to business world via Royal Dutch Shell, which used scenario planning to **anticipate oil shocks** of 1970s and **collapse of the Soviet Union**

Based on the development and exploration of future scenarios: a set of rich narrative depictions of different plausible futures for the operating context of the business.

Climate Scenario Analysis

BSR Recommendations

Use Scenario Analysis to Improve Strategic Resilience

Scenarios should challenge assumptions

- Climate scenario analysis should be used to grapple with the uncertainty of climate impacts, challenge a company's own potential blind spots about the future, and modify business strategies to make them more robust and resilient.

Demonstrate to investors you are proactive

"The ultimate objective in disclosing the use of scenarios is to build investor confidence that a company is meaningfully engaged on the topic of climate change, that it is looking at a broad range of outcomes and is responsive and proactive, rather than defensive and reactive."

EBRD and the Global Centre of Excellence on Climate Adaptation

Consider a Broad Range of Climate Risks and Opportunities

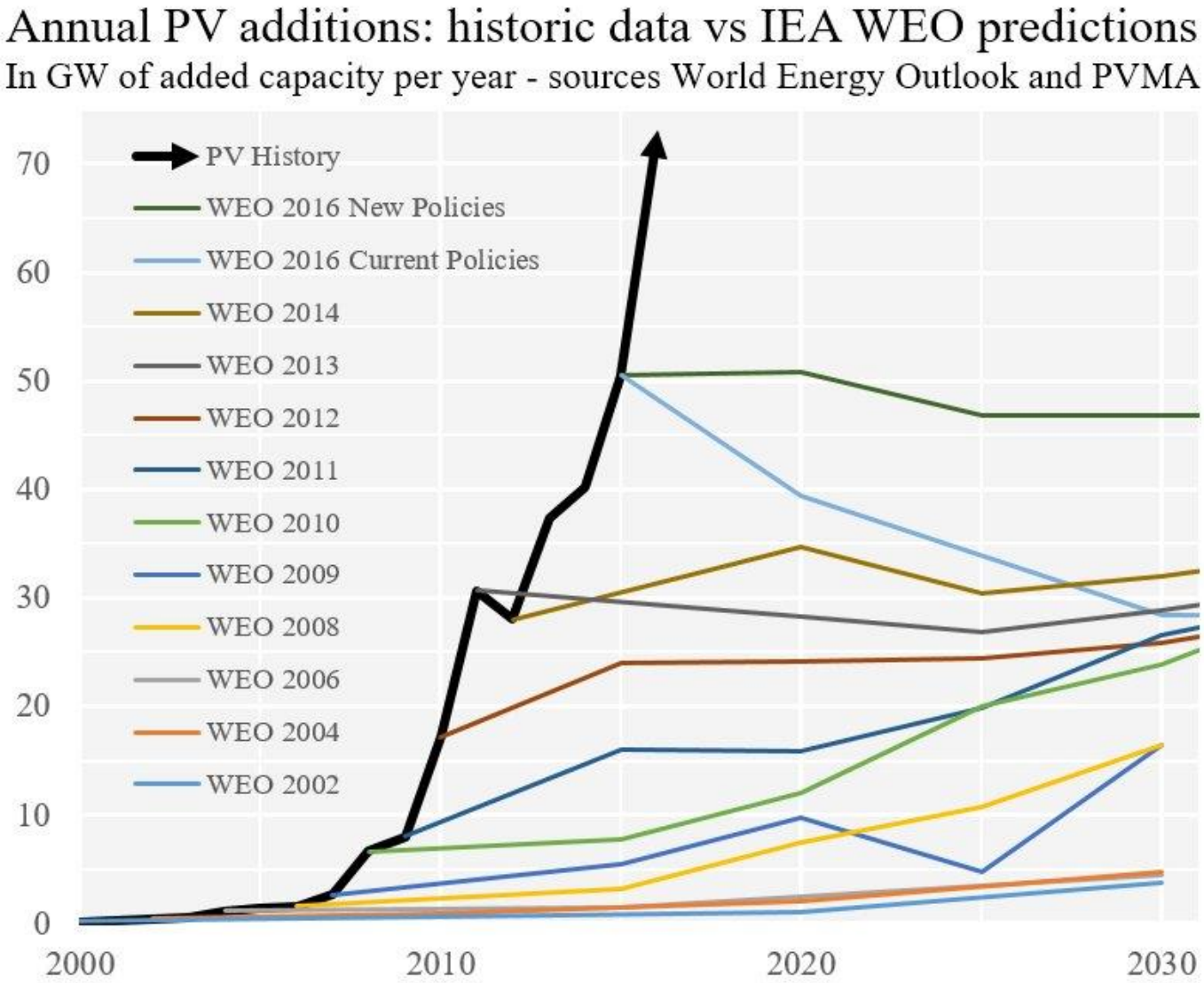
Consider both physical and transition risks

Explore cascading impacts

Use Scenarios Tailored for the Business and Leverage Data from Diverse Sources

Explore critical uncertainties for the business

All Scenarios Have Their Strengths and Limits



Thank you

Jacob Park
Director, Sustainable Futures Lab
jpark@bsr.org

BSR is a global nonprofit organization that works with its network of more than 250 member companies to build a just and sustainable world. From its offices in Asia, Europe, and North America, BSR develops sustainable business strategies and solutions through consulting, research, and cross-sector collaboration.

Jacob Park, Director, Sustainable Futures Lab: jpark@bsr.org
Asako Nagai, Director: anagai.ic@bsr.org

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