

Climate-related scenario analysis

What is scenario analysis?

Climate-related scenario analysis provides a structured way for management to consider how climate-related risks and opportunities could impact their business model and strategy. It can help management to understand the potential implications for business and financial performance over time and identify strategies to be resilient in these different futures and to take advantage of opportunities presented.

Scenarios typically take uncertainty of the future as a given in reviewing risks and opportunities. Scenario analysis is not a form of sensitivity analysis and does not rely on probability.

Scenario analyses are characterised by answering ‘what-if’ questions and therefore do not aim to forecast or predict (by assessing likelihood). To answer the what-if questions, scenario analyses provide results based on a number of assumptions of a plausible future following a certain pathway.

Typically, the outcome of climate-related scenario analysis will depend to a large extent on regulatory, societal and supplier responses – e.g. assumptions over who bears the cost in a particular scenario. So, scenario analysis would need to consider both the transition and physical impacts but also how different parties respond to those impacts.

Scenario analysis can be qualitative, quantitative or some combination of both. Qualitative scenario analysis explores relationships and trends for which little or no numerical data is available. Quantitative scenario analysis can be used to assess measurable trends and relationships.

Presenting scenario analyses in an annual report

If management is using scenario analysis, it may be useful to present this in its annual report. When presenting scenario analyses, management will need to carefully describe the assumptions and method of preparation so that users are not confused by the scenarios presented. For example, if management is assuming that a majority of the costs of a climate-related measure are borne by consumers, then this would need to be explained.

Scenario analysis can help investors assess the possible exposures on a business in a range of hypothetical circumstances, but will not generally be designed to reflect management’s views of the most likely scenarios and hence by their nature may be different from the assumptions underlying the financial statements as required by the applicable accounting framework. Nevertheless, management need to consider if the assumptions underlying the financial statements are in sync as appropriate with the company’s strategy and the climate-related matters discussed elsewhere in the annual report.

Example

An energy producer might consider several transition risk scenarios that might reflect a combination of:

- climate-related government actions (e.g. carbon tax);
- economic changes (e.g. the price of electricity generation decreases substantially due to the high level of renewable generation); and
- social changes (e.g. consumers select renewable energy when possible, even if prices are slightly higher).



home.kpmg/ifrs

© 2021 KPMG IFRG Limited, a UK company, limited by guarantee. All rights reserved.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.

KPMG International Standards Group is part of KPMG IFRG Limited.

KPMG refers to the global organization or to one or more of the member firms of KPMG International Limited ("KPMG International"), each of which is a separate legal entity. KPMG International Limited is a private English company limited by guarantee and does not provide services to clients. For more detail about our structure please visit <https://home.kpmg/xx/en/home/misc/governance.html>

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

This publication contains copyright © material of the IFRS® Foundation. All rights reserved. Reproduced by KPMG IFRG Limited with the permission of the IFRS Foundation. Reproduction and use rights are strictly limited. For more information about the IFRS Foundation and rights to use its material please visit www.ifrs.org.

Disclaimer: To the extent permitted by applicable law the Board and the IFRS Foundation expressly disclaims all liability howsoever arising from this publication or any translation thereof whether in contract, tort or otherwise (including, but not limited to, liability for any negligent act or omission) to any person in respect of any claims or losses of any nature including direct, indirect, incidental or consequential loss, punitive damages, penalties or costs.

Information contained in this publication does not constitute advice and should not be substituted for the services of an appropriately qualified professional.

'IFRS®', 'IASB®', 'IFRIC®', 'IFRS for SMEs®', 'IAS®' and 'SIC®' are registered Trade Marks of the IFRS Foundation and are used by KPMG IFRG Limited under licence subject to the terms and conditions contained therein. Please contact the IFRS Foundation for details of countries where its Trade Marks are in use and/or have been registered.