

# Illustrative Exercise: Climate Stress Testing of Energy Company

## To do's of illustrative exercise:

1. Read the motivations for conducting a climate stress test of a firm.
2. Read the valuation model of the energy company.
3. Conduct a climate stress test of an energy company.
4. Answer the questions below based on your findings of the stress test.
5. List your findings, with the following structure:
  - a. Show and critically discuss findings on the core questions.
  - b. Show critically discuss findings on the transition & technology scenario questions.
  - c. Discuss validity and ways to improve your energy company stress test.

## Questions of illustrative exercise:

### Core questions:

1. What is the value of the firm with its current business model under the transition and technology risks imposed in the scenario?
2. How might the firm adapt its strategy to maximize value under the given scenario?

*Answer questions 1 and 2 separately for the hot-house scenario, the orderly transition scenario and the disorderly transition scenario. Take the default settings for the technology scenario as given. Conduct the stress test on the type of brown energy company you have been assigned. Select the green energy of your choice and stick to it for the remainder of the questions.*

### Question on transition scenario:

3. How does the timing of the energy company's transition towards a green business model depend on its expectations of the policies to tackle climate change (i.e. the future carbon tax)?

*Answer question 3 by explaining how the timing of the energy company's transition towards a green business model depends on the policy scenario (i.e. hot-house world, orderly transition, disorderly transition). Take the default settings for the technology scenario as given.*

### Question on technology scenario:

4. How might the timing of the energy company's transition towards a green business model depend on its anticipation of the future cost of new investments in green energy?

*Answer question 4 by changing the technology scenario.*

## Questions on how the climate stress test of the energy company can be improved:

5. How could the valuation model of the firm be made more realistic?
6. How could the strategic adaptation of the energy company in light of the climate policies and technological advances be made more realistic?
7. Are all the relevant costs and opportunities arising from the transition of the firm to a low-carbon and low-climate risk model taken into account?
8. How could the climate policy and technology scenarios be further improved and calibrated? For instance, how can an energy company active in one or multiple jurisdictions select the policy scenarios that are most relevant for them?