



GOVERNMENT ASSETS: RISKS AND OPPORTUNITIES IN A CHANGING CLIMATE POLICY LANDSCAPE

What impact can climate policies have on government-owned assets, budgets and financial stability?

Approximately 70 per cent of fossil fuel resources worldwide are owned or controlled by governments, and decisions made today regarding long-lived strategic public infrastructure assets – often in the energy or transport sectors – will influence economic growth models for decades.

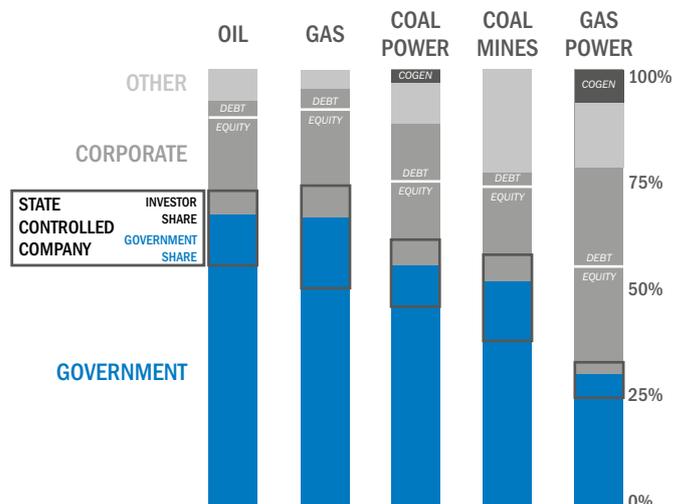
The European Bank for Reconstruction and Development (EBRD) has developed a study that analyses how climate change policies can affect the national accounts of governments and especially the impact they have on the value of energy and infrastructure assets and the cash-flows linked to them.

The workshop “Government assets: risks and opportunities in a changing climate policy landscape” aims to encourage governments to act strategically by making climate change considerations an integral part of their budgets and fiscal policies. It does this by providing a methodology to assess the influence of climate-related policies on national budgets as well as some key principles to improve the resilience of national budgets to changes triggered by those policies.

- ▶ **Prudent budget management** is a priority for all governments, but it has become a particular focus in the wake of the financial crisis.
- ▶ While a debate on the need to assess the potential effect of climate change policies on carbon-related assets made significant progress in the case of private-sector exposure, this has been less of a priority for governments.

- ▶ However, as much as **two-thirds of fossil-fuel reserves and related assets are owned by governments**, particularly in the oil and gas production sectors. A significant portion of energy-related infrastructure resides in the hands of national, local or regional authorities, with wide variations among the different regions of the world. This implies that a significant part of the adjustment in the value of assets – caused directly or indirectly by carbon taxes and prices – will be borne by governments and their taxpayers.

How fossil fuel production is divided between government and investors



Source: Climate Policy Initiative, 2014: “Moving to a Low-Carbon Economy: the Impact of Policy Pathways on Fossil Fuel Asset Values”.

- ▶ **The impact of climate change policies on national budgets may be positive or negative**, depending on a number of factors such as the economic structure of the country, the ownership arrangements for key assets, including private sector participation, risk sharing arrangements in contracts, pricing of CO₂ emissions, the role of subsidies and the pricing policies for infrastructure. It is important that as governments adopt climate change policies they are aware of such differences.
- ▶ **The effects will depend on the market in which affected assets and services compete.** The more global the market that a product or service competes in, the greater the importance of global policies.
- ▶ **For infrastructure** and other public goods which effectively do not have a market price and are local by nature (and state-owned), the **impact** on budgets **will mainly depend on the pricing policy** adopted – full cost recovery price or not of the services provided, for example road tolls – rather than on their intrinsic value.
- ▶ **The structure of contracts for private sector participation in natural resources and infrastructure assets is the key** to understanding the global exposure of governments to climate change policies, particularly in resource-rich countries. Contracts that guarantee fixed or semi-fixed revenue to private investors, as is customary in many instances, give governments a larger share of potential gains from higher use of the infrastructure/price increases of the resource, but this comes at a cost in terms of risk and budgetary exposure. Therefore the choice of contractual arrangements will need to be carefully assessed; generally options where risk is shared between the private and public sectors will be more resilient to climate change policy changes.
- ▶ **The design of climate change policies matters.** Emissions reductions can be achieved by imposing a carbon tax and reducing fossil fuel subsidies, or by introducing feed-in tariffs to renewables and other low-carbon subsidies. Both approaches would eventually lead to a reduction in the value of certain key government-owned assets, but may bring other significant co-benefits, like increased revenue in the case of carbon taxes which can be used to decrease other taxes.

Main natural resources and infrastructure asset classes likely to be affected by climate change policies

Natural resources	Infrastructure
<ul style="list-style-type: none"> • Coal and metal mining • Oil exploration and production • Gas exploration and production • Agriculture and forestry 	<ul style="list-style-type: none"> • Power generation • Electricity transmission • Gas pipelines • Transport (including roads, rail, aviation, ports) • Water and sanitation • Industrial manufacturing (including cement and steel/iron)

Steps to assess the direct impact of climate change policies on national budgets¹



STEP 1
Identify sensitive assets and cash flows; establish a base case



STEP 3
Estimate changes in future revenues and costs and asset value due to climate-related policies



STEP 2
Develop alternative scenarios for climate policy and sensitivities



STEP 4
Assess the impact in terms of changes in economic value between consumers, investors and government

¹ Prepared by the Climate Policy Initiative for the EBRD. The full report will be available at ebrd.com in January 2016. The preparation of the methodology has been supported by the EBRD Shareholder Special Fund (SSF). Printing has been funded through the Clean Technology Fund (CTF).