How to make climate adaptation and resilience investable

By Umar Ashfaq / 15 August 2024

Investors have an unavoidable opportunity to help society withstand the impacts of a warming planet

Avoiding the worst impacts of a warming world will demand both a transition from the burning of fossil fuels to renewables and investment in climate adaptation and resilience. To date the overwhelming share of climate finance has focused on decarbonisation, with climate-proofing coming chiefly from governments to harden infrastructure against weather-related ravages.

Demand for solutions that can reduce the risks and impacts of climate change is generating opportunities for private investors. Few companies, however, identify as climate resilience or adaptation companies. This presents an impediment for investors who might otherwise view technologies and solutions designed to protect society from the physical risks of climate change as an investment theme.

One solution for sustainability-minded investors may be to identify firms engaged in the business of climate adaptation and resilience, suggests analysis by the Global Adaptation and Resilience Working Group and the MSCI Sustainability Institute. The analysis used artificial intelligence to identify companies that offer technologies or equipment that can help governments, businesses or households prepare for and adapt to the realities of a changing climate.

We found that products and services from more than 800 publicly listed companies (about 11% of listed companies globally) contribute to climate adaptation and resilience. The analysis harnessed an AI large language model to surface companies whose businesses span activities ranging from water-efficient agriculture and supply chain resilience to weatherisation of power infrastructure and building.

The analysis is one of the first to test the potential of investing in publicly listed equities to further climate resilience and adaptation. It may also be the first use of AI to prototype an investable universe of adaptation and resilience companies from among them.

This comes as people in every country and segment of society are making changes to adapt to a warming world. Extreme heat and natural disasters intensified by climate change increasingly threaten lives and livelihoods. The US alone registered a record number of billion-dollar disasters in 2023, which marked the hottest year globally on record.

Demand for technologies and solutions that help society predict extremes of weather, protect public health, produce food, construct buildings and avoid disruption is likely to grow. The United Nations Intergovernmental Panel on Climate Change has observed that climate-related losses and damages will be increasingly difficult to avoid.

'Climate impacts are now inevitable,' noted Jay Koh, chair of GARI and co-founder and managing director of The Lightsmith Group, a climate-focused private equity firm. 'There's an opportunity to invest in technologies and solutions that help us understand those impacts and help us to manage and even transcend them.'

A growth theme for investors

GARI, with support from the MSCI Sustainability Institute, has developed a model for identifying companies offering products and services that enable climate adaptation and resilience. The framework for Climate Resilience Investments in Solutions Principles provides a comprehensive approach for identifying companies in the business of adaptation and resilience across regions, sectors, growth stages and asset classes.

'Adaptation and resilience, which has been an important theme for policy-makers, public finance and non-governmental organisations, is emerging as a theme for growth-minded investors, who understand the inevitable demand for innovative resilience products and services,' observed Linda-Eling Lee, the MSCI Sustainability Institute's founding director.

Researchers from GARI and the Institute applied the CRISP framework to the world's listed equities. We used an LLM to identify companies that offer products and services that help to prevent, respond or recover from physical risks associated with a changing climate. The researchers later validated the results manually.

The companies identified range from traditional engineering firms to businesses developing new tools for climate risk analysis. Others included manufacturers of industrial products such as steel and cement that emit high levels of emissions but provide critical inputs for infrastructure that resiliency demands.

Roughly one-third of the companies identified are domiciled in emerging markets, highlighting the global opportunity that adaptation and resilience represents. While the analysis focused on listed equities, it can be replicated within the universe of private markets.

We anticipate that the CRISP framework would play a key role in helping investors differentiate companies as they build out their investment theses geared toward adaptation and resilience.

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