

Environmental and Climate Risks in Financial Analysis

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Abstract

The assessment and consideration of risks in the analysis of companies and projects play an important role in investment decisions. In the context of climate change new significant types of risk arise. It can be shown that climate risks are additive, increasing the whole risk exposure significantly. Relevant studies have shown that depending on the sector climate risks will affect the value of assets (value at risk) up to double-digit percentage. Applying common methods and procedures these risks are generally determined and measured insufficiently. Thus, the provision for environmental and climate risks in granting of credits, sell-side / buy-side research or due diligences is not adequately, although existing approaches would generally allow a valuation of these risks.

The first target of this paper is firstly to analyse the problem of the ‘debasement’ of historical data especially in the light of climate change. Furthermore, relevant approaches for the process of financial analysis will be outlined in order to implement environmental and climate risks by means of adjusted risk premiums. In this context these approaches represent practical potentialities for the implementation of risk premiums as well as fundamental factors that have an impact on the investment decision. Here an important connection between risk measure, economic reference parameter and valuation method is developed.

Keywords: climate change, risk assessment, valuation, risk management, risk measure, financial analysis, environmental risk

JEL-classification: G20, Q51, Q56