The Emerging Markets Investors Alliance recently hosted a panel examining the economic implications of climate change and how investors should assess climate shocks. Moderated by Fergus McCormick, Senior Advisor at EMIA, the discussion featured Stéphane Hallegatte, Chief Climate Economist at the World Bank; Sean Kidney, CEO and co-founder of the Climate Bonds Initiative; and Gernot Wagner, climate economist and senior lecturer at Columbia Business School.

The discussion commenced with the common understanding that climate change is not an isolated environmental issue but a sovereign development and economic issue as well. Hallegatte then distinguished between two climate change phenomena: sudden climate shocks, such as a hurricane or wildfire, and the "slow burn" of long-term environmental degradation. Because slow-burn climate impacts lack the visibility of sudden shocks, they attract less attention and are given less consideration by policymakers, investors, and the public. Wagner noted that a single day above 90°F can reduce annual payrolls by 0.04 percent. Here, Hallegatte noted that these two climate scenarios feed into each other. For example, gradual sea-level rise damages economies by making coastal flooding more prevalent and severe. This is where, as the panelists pointed out, current modeling falls short because it is difficult to capture the nonlinear and volatile effects of slow-burn climate impacts.

Financial markets are adjusting to climate shocks as an economic issue, mainly through credit ratings and bond spreads. Spreads serve as a way to price physical risk. But they also expose sovereigns to lower ratings, as sovereigns become more susceptible to climate shocks. On this note, the panelists encouraged bondholders and rating agencies to reward good governance and the ways in which a country invests in climate-shock safety systems. Kidney highlighted Jamaica, which received a credit rating upgrade, partly because its catastrophe bond and disaster preparedness demonstrated resilience following a major hurricane. Still, the real danger is the secondary impact of the initial shock.

Kidney noted that the 2010 Russian heatwave quadrupled global wheat prices, and caused social unrest in countries unequipped for that price change.

The panelists also highlighted new financial tools that are becoming more popular. They pointed to resilience bonds, which conveniently slot into green bond portfolios, meaning they are easy to buy and sell while offering low borrowing costs for governments. Tokyo floated a resilience bond, and it was met with overwhelming demand. It was seven times oversubscribed, which showed a strong appetite for investing in efforts to address future risk. Alongside resilience bonds are taxonomies, which Kidney described as a “shopping list for the future” that establishes criteria for infrastructure investments, ensuring governments consider climate risks and avoid unnecessary exposure. Hallegatte explained that borrowing for climate adaptation can improve long-term debt sustainability by protecting future GDP, even if it raises debt in the short term.

The webinar concluded with the panelists offering three pillars of advice: they encouraged adopting a value mindset, using simple stress tests, and prioritizing transparency and governance. Investors should look decades ahead and avoid reacting to short-term market fluctuations. They should avoid using overcomplicated models that create a false sense of precision, and instead rely on historical events and questions such as, “Can this economy survive if the frequency of major hurricanes doubles?” Finally, we should reward countries that are transparent about their climate shock risks and risk-mitigation strategies. Climate preparedness is not only about geography; governance is more important.

The Emerging Markets Investors Alliance advances informed dialogue on economic and investment challenges across emerging markets. This project explores how climate risks can be measured and incorporated into assessments of sovereign resilience, creditworthiness, and long-term investment value.