



By: *Fiona Watson*

Markets are getting things wrong once again, now in connection with climate change



As business, government, and nonprofit leaders debate the future of climate **action** ahead of the United Nations Climate Change Conference (**COP30**) in Brazil, the global economy remains vulnerable to acute and chronic climate-driven shocks whose impact could be more severe than that of the 2008 global financial crisis.

At a time when many governments and businesses continue to underestimate and underprice physical climate risk, we must remember that neither financial markets nor regulators are always right.

What if their current complacency about climate risks is catastrophically wrong?

The 2008 financial crisis and its aftermath showed how fast our expectations can be shattered.

In the mid-2000s, deregulation and simplification were the norm: balance sheets were run thin, and profits and losses ran high.

Financial engineering boomed as risks were packaged, diluted, and obfuscated, and as credit was given where it hadn't been earned.

In the face of all this, expressions of concern were drowned out by the din of transactions. But the signs were there. The fundamentals were not right.

By late 2008, the global economy was teetering on the brink of collapse. In the space of days, longstanding banking giants were swept away. Only government bailouts prevented the entire financial system from melting down.

Collective humility

The post-crisis banking sector looks very different than the one that preceded it. Owing to tougher rules and tighter oversight, good governance and resilience restored trust in the banking sector.

Long-term investors – pension funds and

insurance companies – patiently endured years of expensive recovery before value was restored and dividends resumed.

The post-crisis era was marked by collective humility and acceptance of systemic risk

If the banks had gone, so, too, would those holdings, and most of today's financial system with them.

The post-crisis era was marked by collective humility and acceptance of systemic risk.

This was reflected in the Financial Stability Board's **recognition** in 2015 of climate change as perhaps the greatest systemic threat of all.

A dangerous lapse

Ten years later, however, our systems and processes remain ill-equipped to measure and manage the systemic risks posed by climate change.

With the focus on climate issues slipping down investors' **agendas**, this is a dangerous lapse.

From broken supply chains and damaged assets to infrastructure shocks, public health crises, and community disruption, many businesses are already feeling the profound impact of climate change.

Nor is the problem confined to headline-grabbing disasters. Subtle, chronic effects are quietly eroding value, often in ways that our systems are ill-equipped to detect or manage. Once again, the fundamentals are not right.

US satellites show that the intensity of extreme weather events is now double the average recorded in the 2003-20 period

Data from NASA underscores this point. US satellites **show** that the intensity of extreme

weather events is now double the average recorded in the 2003-20 period.

This trend has tragic **consequences** for human well-being. In Africa, for example, 23 million people faced acute hunger in 2023, owing to record droughts.

The global economy is also taking a beating. Research by the World Economic Forum finds that weather-related damage to businesses, infrastructure, and other fixed assets may have almost tripled since 2000.

The bill for the last decade **topped** \$2 trillion, with costs in 2022-23 alone reaching \$451 billion.

Markets are getting things very wrong once again

Yet rather than take steps to mitigate these risks, many investors, corporations, and governments continue to incentivize activities that compound them.

Leading companies must battle to convince their boards and investors to buy into forward-looking strategies.

Banks – the traditional stewards of opportunity – are struggling to manage lending risk associated with new and emerging technologies.



Markets are getting things very wrong once again. One exception is the insurance industry. Experts at pricing risk, these firms are learning fast

The business case for pre-emptive resilience and innovation just isn't clear enough to overcome the allure of the status quo. In other words, markets are getting things very wrong once again.

One exception is the insurance industry. Experts at pricing risk, these firms are learning fast.

Between 2023-24, climate-related disasters **forced** insurers to shell out \$143 billion in claims payments.

More and more of them are doing the math and concluding that climate coverage simply doesn't add up. They must either hike premiums to exorbitant levels or exit the disaster-risk market altogether.

The latter scenario is all too likely. Günther Thallinger, a board member at the global insurer Allianz, recently **warned** that: "entire regions are becoming uninsurable" as key asset classes degrade "in real time." If markets haven't realized this, that is because it takes time to work through the system.

The global economy has a massive blind spot

The parallels to past crises are clear. Again, expressions of concern are being drowned out.

This time, though, the stakes are higher, the effects are more widespread, and the consequences will be irreversible.

The global economy has a massive blind spot, and unlike in 2008, there is no one on the winning side of the short bet. We all will lose.

Of course, there is a difference between a systemic blind spot and an ordinary one. We know the spot is there, but our financial system cannot address it until it is translated into monetary terms.

We need to mobilize executive action across the private sector to improve how we measure, manage, and respond to climate risks

For this, we need to mobilize executive action across the private sector to improve how we measure, manage, and respond to climate risks.

Working with capital providers, standard setters, and policymakers, we need to align actionable information with the need to allocate capital toward climate-change mitigation and adaptation.

But having the numbers is not enough. To paraphrase Ernest Hemingway, climate collapse is a process that happens slowly, then all at once.

Businesses and investors must create and maintain the capacity for rapid change within our organizations and across our value chains and spheres of influence. This starts with humility and acceptance of systemic risk.

The 2008 financial crisis shocked the world and demonstrated that nothing can be taken for granted. The stakes now are far higher, and there can be no bailouts. We must pursue pre-emptive action, and we must do it immediately.

Fiona Watson is Vice President of the World Business Council for Sustainable Development.