Your Investments Actually Can Reduce or Increase Climate Change

Do the investments you make actually impact the climate or affect carbon emissions? It turns out that they do. Here's why your investments matter and what you can do to align your investing with your climate values.

Investments Impact Climate

The investing choices you make can indeed affect climate change and lead to increases or decreases in carbon emissions, directly or indirectly.

If you invest in stocks or bonds of a company with high greenhouse gas (GHG) emissions such as oil & gas or manufacturing companies, for example, you're showing the stock market and financiers – and your friends, if you talk about your investments - that these types of companies are attractive. The effect is similar with companies that are less obvious, such as firms that provide fast fashion, meat, air travel and more. Your investment can also make it easier for those companies to get loans or other funding, since they can show they have support from more investors. When you and others invest, bankers and investment managers can be more likely to support these companies' activities.

On the other hand, choosing to invest in GHG emitters also usually means not choosing to invest in eco-friendly firms such as solar power or electrical vehicle companies. Having fewer investors shows less support for them can make financing harder and signal to other investors that they're less attractive.

Direct investments in property, cryptocurrency, timber or other sectors can also make a difference. If you invest without looking at their environmental impacts, you may be even more actively supporting buildings, crypto-mining, deforestation or other activities that create carbon emissions.

These impacts and others exemplify how your choice of investments, or even not choosing, has an impact on climate.

Climate Change Affects Investment Returns

While your investments affect climate change, climate change can also have a huge impact on the returns on your investments. Two risks are especially prominent.

One is physical risks, whereby climate change effects on weather, water availability, sea level, heat or other factors affect the company in which you invested. For example, returns could be lower if canal levels in Europe are too low for companies to ship their goods, the temperature is too hot for farmers to grow crops or factory employees to work, beverage or fashion companies lack water to produce products, or hurricanes and typhoons shut down businesses.

Another is transition risk. A company may have lower sales, for example, if regulators restrict exports to Europe because carbon emissions in production are too high, place penalties on fossil fuel companies due to their products or restrict agricultural companies from expanding based on their land use practices. During the transition to new regulatory regimes, companies may have lower revenue. Companies may also face lower revenues if they have to spend to transition to renewable energy, reduce emissions from smokestacks or take other actions to reduce their impact.

Reputational and technology risks can also affect companies. An increasing number of corporations and consumers prefer to buy from firms with more sustainable practices, for instance, so a company with a reputation for higher emissions or poor environmental controls could face lower sales. When new climate-friendly technology such as solar and wind power or more sustainable steel and concrete production make current technologies more expensive or inefficient, traditional companies may sell fewer products or services.

The lower revenues from these and other climate-related changes can reduce the value of your investments.

Investing with Your Climate Values and Goals

If you want to align your investments with your climate-related values and goals, it's important to start by figuring out what your beliefs actually are.

Your values are what you believe in and the principles that guide you. Researcher Brene Brown suggests identifying your top two values, and she has created a helpful list to choose from. If your values include environment and nature, for instance, you'll probably want to look for investments that prioritise them. If you care most about wealth without caring about environment, you may do something different.

It is also helpful to look at your investing goals. You may want short-term rather than long-term returns, for example, or you may want to invest in any company regardless of their climate impact rather than selecting firms with strong sustainability practices and lower climate risk.

Once you identify your values and goals, it can be helpful to create a personal investment policy statement. The statement, which reflects your values and goals, can help remind you of your guidelines for investing. You can also create ethical guidelines to align investments with your values. Values and goals such as these can help guide your selection of investments, and you can also use them if you talk with a financial advisor.

Using a Climate Lens to Select Investments

How you select investments that align with your climate values depends on how you invest.

If you invest in mutual funds, unit trusts, exchange traded funds (ETFs) or index funds, you can select ones that invest according to environmental or climate principles. Read information about the fund and select it carefully, though, since the names of some funds may not match what they do or what you expect. And since ESG is far broader than climate, choosing an ESG fund may not deliver what you want. Organisations such as Morningstar and Yahoo Finance have insights about funds' climate practices. By choosing funds that align with your values, you can make sure you invest the way you want.

If you rely on a financial advisor to manage your investments or provide advice, you can use your investment policy statement to explain the investments you want to make. Explaining the impacts of climate change and the types of companies you prefer is essential. The advisor can provide written confirmation. You should also monitor their selections, especially in the early stages after you explain your focus, to make sure they align with your climate values.

If you invest in stocks or bonds directly, a simple framework is to use positive screens or negative screens. Positive screens mean you look specifically for companies with a positive environmental impact, such as renewable energy companies. Negative screens exclude companies in sectors such as fossil fuels or mining that have a negative climate impact.

You can also examine companies individually by analysing at their sustainability reports and annual reports, or you can leverage tools or advisory firms such as Yahoo Finance and Morningstar to gather more information.

Monitoring the Results

When you select investments, whether through a fund or with an advisor or on your own, you can evaluate them to make sure they align with your climate values. That initial analysis, though, doesn't mean the investment will continue to perform as you want.

A mutual fund or index fund may shift the stocks and bonds it invests in over time, for example, or an investment advisor may select investments that don't match your preferences. And a company you selected for stock or bond purchases may change direction over time.

It’s important, then to monitor investments regularly. With a fund or an investment advisor’s selections, you can check the individual companies in the portfolio. You can also read a fund’s or a manager’s portfolio analysis or sustainability report. You can also read the sustainability report and the annual report for companies you or they select. Yet another method is to use analysis by Morningstar, Yahoo Finance or other sources to check on the firms.

Does Your Investment Make a Difference?

It can be easy to think that your individual investment is so small compared to the millions or billions invested by fund managers that it doesn’t matter. Actually, the impact is large. Our investment decisions express our concerns about climate change. Combined with others, your impact is larger than a single investment. And talking about our actions with others creates a ripple effect that can lead others to follow a similar path. Your investments do make a difference.