5 Climate Risk Questions every Built Environment Investor should be asking

Richard Betts[i] | RZB Advisory

Alexandra Faciu[ii] | Alexandra Capital

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Introduction

Climate risk is increasingly becoming a key consideration as to how built environment assets are valued, financed and managed. What used to be often treated as a technical or sustainability-led issue is now increasingly viewed as a financial and strategic business concern. For example, according to the latest World Economic Forum Global Risks Report (2026), the top 3 risks to the global economy over the next 10 years are considered to be climate- and nature-related physical risks[1].

For investors in real estate and infrastructure, this shift in perceived importance of climate risk has important ramifications. Built environment assets are long-lived, location-specific and capital-intensive - making them inherently exposed to both physical climate impacts and the transition to a lower-carbon economy.

At the same time, regulatory and market expectations are evolving. ESG-related standards such as the **EU's CSRD/ESRS**, **IFRS S1/S2** and national versions including in Canada (**CSDS 1/ CSDS 2**) and recently in the UK (**UK SRS 1/SRS 2**) are reinforcing the link between sustainability-related risks and enterprise value. In addition, key stakeholders such as investors, lenders and insurers are placing greater emphasis on how climate risks are identified, assessed and managed.

A key question, then, is no longer whether climate risk is relevant, but how effectively it is being integrated into investment and asset-level decision-making.

Based on our work with organisations across sectors and regions, we highlight five key questions that built environment investors should be asking.

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1. How is climate risk affecting asset valuation and investment decisions?

Climate risk is increasingly influencing how assets are valued and how investment decisions are made. Physical risks such as flooding, heat stress and extreme weather events can affect asset performance and longevity. Transition risks - including regulatory

[1] World Economic Forum (WEF), 'The Global Risks Report 2026': (https://reports.weforum.org/docs/WEF_Global_Risks_Report_2026.pdf)

change, carbon pricing and shifting market expectations - can alter future cash flows and demand profiles.

However, while many organisations now undertake climate risk assessments and scenario analysis, insights generated through modelling are not always fully embedded into valuation assumptions, investment appraisals or portfolio strategy.

New standards such as IFRS S2 are reinforcing the expectation that climate-related risks are considered in terms of their financial materiality and impact on enterprise value. Recent years have also seen a rapid increase in methodologies and tools that can be leveraged to understand climate risk. For built environment investors, this means systematically incorporating climate considerations into core investment processes.

Climate considerations are increasingly shaping valuation practice across Canada and the United States as well, but the market's ability to quantify these effects remains inconsistent. Over the past two decades, sustainability has shifted from a niche concern to a mainstream expectation, driven by institutional investors and evolving corporate priorities. Yet valuation practice has not kept pace. Many appraisals still overlook the financial implications of decarbonisation, leaving climate-related factors largely absent from formal valuation outputs. Limited transactional evidence remains a major barrier, as reduced deal volume and traditional value drivers make it difficult to isolate sustainability's impact.

Where data is available, clear patterns are emerging. Buildings with strong sustainability performance often achieve higher rents, lower operating costs and faster lease-up, suggesting lower long-term risk as decarbonisation requirements tighten. Assets with credible transition plans may also face reduced future capital needs. Still, the evidence base remains thin, and consistent valuation adjustments have yet to materialize across the market.

2. To what extent do we understand physical risk across our asset portfolio?

Understanding physical climate risk is a complex and evolving challenge. While data and modelling capabilities have advanced significantly, there are still limitations in terms of resolution, consistency and forward-looking reliability.

Many organisations now have access to climate risk data, but the extent to which it is being used effectively varies considerably. There is often a tendency to treat physical risk as a one-off assessment rather than an ongoing input into asset management and portfolio strategy.

In addition, physical risk needs to be understood not only at the portfolio level but also at an asset level - taking into account location-specific factors, asset design, resilience measures and operational dependencies.

Importantly, physical risk is dynamic and may accelerate non-linearly over time. An additional, often underexplored, complication is that many climate risks are interconnected. Consequently, understanding physical risk requires a forward-looking perspective that considers how risks may evolve under different climate scenarios and affect long-term asset performance and value.

According to a recent presentation by REALPAC[2] at an event organised by Affine Climate Solutions in April, climate-related risks appear in Canadian real estate valuations only in limited and uneven ways. Appraisers reliably incorporate major HVAC retrofits and electrification projects because these fit within familiar capital-expenditure models. Beyond that, climate considerations show up mainly in narrative sections of appraisal reports, and even then without consistency or a standardized approach. The core valuation mechanics - discount rates, cap rates, rent growth, and vacancy assumptions - remain untouched by climate risk, despite its growing financial impact.

This gap is increasingly difficult to justify. Catastrophic insured losses have risen dramatically, from an annual average of less than $1 billion per year between 2001 and 2010 to $8.5 billion in 2024[3], signalling escalating physical risk. Yet only a small share of the market has access to reliable, decision-grade ESG data that could inform valuation inputs. Compounding the issue, Canada's appraisal standard, CUSPAP[4], contains no explicit sustainability requirements, even as the updated International Valuation Standards (IVS) that came into effect in 2025 mandate the identification and analysis of material ESG factors.

3. What does the transition to a low-carbon economy mean for asset performance?

In addition to physical risks, built environment assets are increasingly exposed to transition risks associated with the shift to a low-carbon economy. These include regulatory developments, such as energy performance standards and disclosure requirements, as well as changes in tenant expectations, technology and market dynamics.

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[2] Real Property Association of Canada is the national association representing Canadian commercial real estate

[3] IBC (Insurance Bureau of Canada): https://ibc.ca/ns/resources/media-centre/media-releases/2025/2024-shatters-record-for-costliest-year-for-severe-weather-related-losses-in-canadian-history-at-8-5-billion.

[4] Canadian Uniform Standards of Professional Appraisal Practice (CUSPAP) is a set of professional standards established by the Appraisal Institute of Canada (AIC).

For many assets, particularly older buildings, this raises questions around retrofit requirements, capital expenditure and long-term viability. Assets that are not aligned with emerging standards may face increased costs, reduced demand or, in some cases, the risk of becoming stranded.

Transition planning is therefore becoming an important component of investment and asset management strategies. This involves not only setting targets, but also understanding the practical steps required to achieve them and the associated financial implications.

For investors, the key issue is how transition considerations are integrated into investment decisions, asset management plans and capital allocation processes.

For valuations specifically, the central challenge is how these transition dynamics translate into the financial assumptions that underpin asset value. Buildings that fail to decarbonise face growing obsolescence risk as tenant expectations evolve, lending criteria tighten, and regulatory requirements become more demanding. Yet, as the same REALPAC presentation notes, two structural barriers keep these realities from being reflected in appraisal models. Appraisers are reluctant to adjust core inputs without clear transactional evidence, but such evidence cannot emerge until valuations begin differentiating between climate-aligned and climate-exposed assets. At the same time, appraisal practice is anchored in historical comparables, while transition risk is fundamentally forward-looking. The result is a persistent disconnect: climate impacts are widely acknowledged, but they remain largely absent from the quantitative assumptions that determine value.

4. How will climate risk impact financing, insurance and investor expectations?

Climate risk is increasingly influencing the broader financial ecosystem surrounding built environment assets. Lenders, insurers and investors are all incorporating climate considerations into their decision-making processes.

From a financing perspective, there is growing evidence that climate risk is being reflected in lending terms, due diligence processes and access to capital. Similarly, the insurance market is already responding to physical climate risks, with implications for both the availability and cost of coverage in certain locations or for certain asset types.

Investor expectations are also evolving. There is increasing scrutiny of how organisations are identifying, managing and disclosing climate risks, particularly in the context of emerging reporting frameworks and standards. There is increasing scrutiny from auditors, investors and other stakeholders regarding how organisations identify, manage

and disclose climate risks, including the linkage between climate-related disclosures and financial statements.

For built environment investors, this means that climate risk is not only an internal issue, but one that affects relationships with external stakeholders and access to capital.

Across North America, climate considerations are also increasingly shaping the financial landscape surrounding real estate. One of the most significant developments is the rise of green financing mechanisms that directly support decarbonisation and deep retrofit activity. These solutions are beginning to influence how capital is deployed, how projects are structured, and ultimately how investors assess long-term asset performance.

In the United States, the market has evolved a wide array of financing tools—more than fifteen distinct mechanisms - that lower the cost of capital for energy-efficiency and low-carbon upgrades. Among the most prominent is C-PACE, which enables owners to fund efficiency improvements, renewable energy systems, and other eligible measures through an additional property-tax assessment. This structure provides long-term, low-friction repayment and can significantly improve project economics. Other U.S. green financing programs offer tighter spreads, higher loan-to-value ratios, or blended incentives that make deep retrofits more financially viable. Collectively, these tools are accelerating decarbonisation by reducing upfront barriers and aligning financing structures with long-term sustainability goals.

Canada is moving in a similar direction, though through a more centralized approach. The Canada Infrastructure Bank's Building Retrofits Initiative[5] mirrors many of the advantages seen in U.S. programs, offering long-amortisation loans, elevated LTVs, and exceptionally low borrowing costs - potentially as low as the 10-year Government of Canada bond rate when certain conditions are met. These terms materially shift the economics of retrofit projects, enabling owners to pursue comprehensive upgrades that might otherwise be financially out of reach. As more organizations tap into this platform, the market is beginning to see how targeted financing can accelerate progress towards net-zero objectives.

5. Is governance keeping pace with climate risk?

As climate risk becomes more financially material, it is increasingly seen as a key governance issue. Many investors and stakeholders increasingly expect boards and executive teams to oversee climate-related risks and opportunities and ensure their integration into strategy, risk management and reporting.

[5] https://cib-bic.ca/en/building-retrofits-initiative/

Standards such as IFRS S1/ S2 reinforce the importance of governance, requiring organisations to disclose how climate-related risks are overseen and managed at the highest levels.

In practice, however, governance structures are still evolving. In many organisations, responsibilities for climate risk remain fragmented across functions, and there may be gaps in terms of accountability, expertise and integration with core decision-making processes.

For built environment investors, strengthening governance is critical to ensuring that climate considerations are embedded consistently across investment, asset management and reporting activities.

Across North America, progress on climate-related governance has been uneven. While many organisations have adopted forward-looking approaches, most initiatives remain voluntary, and the degree of integration varies widely across markets and sectors. The result is a landscape where leading firms demonstrate strong oversight and strategic alignment, while others are still building the structures, expertise and accountability needed to manage climate risk effectively.

In the United States, the policy environment has encouraged a proliferation of sustainability frameworks and market-driven initiatives, but governance expectations are largely shaped by investor pressure rather than regulatory mandate. Many companies have developed sophisticated climate strategies, yet the absence of consistent national requirements means that practices differ significantly across regions and industries. This variability creates challenges for comparability, disclosure quality and the integration of climate considerations into core decision-making.

Canada is moving toward a more coordinated approach. A notable development is the federal government's commitment to mobilising public and private capital in support of the transition to a net-zero economy. Budget 2025 reaffirmed support for the development of made-in-Canada sustainable investment guidelines, a national taxonomy, led by the Canadian Climate Institute in partnership with Business Future Pathways. This initiative brings together major financial institutions and technical experts to ensure the guidelines are science-based, credible and aligned with global best practices. The resulting taxonomy will serve as a voluntary market tool to identify "green" and "transition" investments, offering clarity for investors, lenders and other stakeholders. By establishing a common reference point, it is expected to play a critical role in directing capital toward net-zero aligned activities, particularly in higher-emitting sectors where new technologies and processes can deliver meaningful reductions.

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What this means for built environment investors

Taken together, these questions highlight a broader shift. Climate risk is no longer a peripheral technical consideration - it is becoming central to how built environment assets are assessed, managed and financed. It has become a core business issue.

The key challenge is no longer identifying climate risks, but embedding their management into portfolio- and asset-level decision-making. This requires stronger cross-functional integration, clearer governance and more systematic linkage between climate insights and financial outcomes.

Organisations that are able to do this effectively will be better positioned to manage risk, protect asset value and respond to evolving market and regulatory expectations.

Summary

The themes explored in this paper point to a fundamental shift in how climate risk is understood and managed within the built environment. What was once treated as a peripheral sustainability issue is now a core determinant of asset value, operational resilience and access to capital. Physical and transition risks are reshaping performance expectations, financing conditions and regulatory obligations, while new standards are tightening the link between climate exposure and enterprise value. Yet the market remains in transition. Data gaps, inconsistent valuation practices and evolving governance structures mean that many organisations are still not fully translating climate insights into financial decision-making.

For investors, the imperative is increasingly clear: climate risk needs to be embedded into the assumptions, governance structures and decision-making processes that shape investment and asset management outcomes. Organisations that adapt effectively will be better positioned to protect value, meet evolving stakeholder expectations and navigate the transition to a lower-carbon economy.

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[i] Richard Betts, Founder and Managing Director, RZB Advisory; Technical Expert, SAM Curated (https://rzbadvisory.com)

[ii] Alexandra Faciu, President, Alexandra Capital; Founder and Curator of SAM Curated (https://www.samcurated.com)