Circe Invest's Fiona Frick: How climate risk is moving further into capital markets

As insurers retreat, investors step in

Fiona Frick

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Image: Fiona Frick (pictured) is founding partner at Circe Invest

As wildfires burn forests, floods destroy homes and storms hit infrastructure, the financial impact continues long after the skies clear.

For investors, the deeper shift runs through the insurance system into lending and valuations. When insurers raise premiums or withdraw from high-risk zones, assets become harder to insure, finance and value.

This repricing of climate risk is reshaping portfolios, tightening credit and changing opportunities across global capital markets.

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According to Allianz's Risk Barometer 2025, natural catastrophes are now among the top three global business risks. For five years in a row, insured catastrophe losses have exceeded $100bn dollars.

Insurers once acted as society's shock absorbers, allowing households, companies and lenders to keep credit flowing. But as climate-related disasters multiply, that protection is thinning. Some regions are becoming difficult or uneconomic to insure.

As Allianz board member Günther Thallinger said at the World Economic Forum, "The maths breaks down. Premiums required exceed what people or companies can pay".

In the US, homeowners' insurance premiums rose by 10.4% in 2024 after a 12.7% jump in 2023, according to S&P Global Market Intelligence from January 2025. Behind those numbers are higher reinsurance costs and large carriers leaving wildfire and storm-exposed states.

Early warning system

Insurance has become the market's early warning system for physical climate risk. When coverage becomes expensive or unavailable, it signals that collateral values and credit quality are weakening.

The first ripple appears in property markets. In the UK, about six million people live in flood-risk areas and the Bank of England estimates homes in the highest-risk zones could lose up to 20% of their value in a severe climate scenario.

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The same mechanism affects credit markets. Companies with uninsured or under-insured assets face weaker balance sheets and tighter refinancing conditions as lenders price in higher risk.

Equity markets are reacting, too. An MSCI study from September 2025 found companies exposed to hurricanes and other extreme events underperformed peers, with losses linked to location, sector and adaptation capacity.

Climate exposure is now treated much like leverage or liquidity risk. REITs with coastal or wildfire-prone assets have trailed as insurance costs rise and margins tighten.

Heavy industry companies face similar pressure. Power networks and manufacturers are diverting capital to protect assets from storms, floods and heat, reducing free cash flow and dividend capacity.

Markets have begun to reflect these costs. Bloomberg data shows high-risk companies saw their average cost of capital rise by 22 basis points for every ten-point increase in physical-risk score, with the steepest effects in materials and utilities.

As insurers retreat, investors step in

As traditional insurers retreat, part of the risk is migrating directly to investors.

Aon reports catastrophe-bond issuance of $21.7bn dollars in the 12 months to June 2025, up 19% year on year, lifting total outstanding volume to $54bn. These bonds spread risk and add liquidity but also import "disaster beta" into multi-asset portfolios. Severe events can now move not only insurers' shares but also capital markets.

BoE defends work on climate risk despite allegations of neglect

Regulators are increasingly recognising that climate-related losses can threaten financial stability.

The Bank for International Settlements has warned climate shocks can spread quickly from falling asset values to credit defaults and market volatility, amplifying systemic risk.

The European Banking Authority's Guidelines on ESG Risk Management will require banks in 2026 to integrate climate and environmental risks into their capital planning.

What investors should watch

Investors need to understand how physical climate risks translate into financial exposure across portfolios.

Portfolios concentrated in real estate, infrastructure, equity or credit linked to high-risk regions may face sudden cost shocks when disasters strike or as insurance repricing hits balance sheets.

Watching insurance market signals such as premium inflation, coverage limits or non-renewals can reveal early signs of stress. Investors should also ask if asset managers they work with are integrating physical-risk data into their valuation models.

Conversely, exposure to resilient infrastructure, adaptation technologies and insurance-friendly assets may benefit from the capital rotation already underway. LSEG climate data shows 34% of companies in the FTSE All-World index now report adaptation measures to reduce physical climate risks

In a world where weather moves markets, understanding how climate risk flows through insurance, financing and valuation channels is key to protecting portfolios and capturing opportunities in the new geography of climate-priced capital.

Fiona Frick is founding partner at Circe Invest

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