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Climate risk is changing where investors put their money – even as NZ relaxes disclosure rules

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Across New Zealand and Australia, the impacts of a warming climate have been slowly changing how investors weigh up risk and returns.

Both countries have been experiencing more extreme events such as floods and bushfires, all while policy shifts and rising carbon prices increase pressure on firms to adapt.

As these risks grow more visible, investors are increasingly interested less in how well a fund has previously performed, and more in how likely it is to hold up in an uncertain future.

In recent years, each country has also introduced regimes mandating large companies and financial institutions to report how climate-related risks – from physical impacts to changing regulations – could affect their business.

These requirements are now being scaled back in New Zealand, with the government removing mandatory reporting obligations for more than half the 164 companies that have been subject to the rules.

By raising the threshold for inclusion in the regime from NZ$60 million to $1 billion in market capitalisation, only the very largest listed companies would still have to report.

Yet a newly released report from Deloitte suggests those underlying pressures justifying climate-risk disclosures have not gone away.

Investors, lenders and other stakeholders still expect clear information on how companies are managing climate risk – regardless of whether reporting is mandatory.

Furthermore, our research suggests these disclosures have been helping drive change that goes well beyond making climate-related financial risks more visible.

How investors are rebalancing risk

In our study, we examined more than 2,700 mutual funds across Australia and New Zealand, representing over US$500 billion in assets.

We found that as climate-related uncertainty increases, investors are paying closer attention to returns delivered by funds with strong "environmental, social and governance" (ESG) ratings.

This suggests these ratings are no longer being treated simply as signals of values or ethics, but as indicators that a fund may be better prepared for a changing economic and regulatory environment.

In fact, our results show the link between past performance and investor inflows is significantly stronger for funds with high ESG ratings.

We observed that a 1% increase in past performance leads to markedly larger inflows (new money from investors) for these funds than for those with weaker sustainability profiles.

Another key finding was that investors respond differently depending on the type of climate-related risks they are considering.

When concerns around climate policy and regulation increase, investors tend to shift towards more sustainable funds, suggesting they see firms adapting early to a lower-emissions economy as better positioned over the long term.

In our data, this type of "transition risk" was actually associated with increased investment flows, reflecting expectations that policy and technological change will favour more sustainable firms.

By contrast, physical risks such as extreme weather events tend to trigger a broader pullback from riskier assets.

These risks were associated with net outflows (more money being taken out than put in), as investors respond to immediate, tangible losses by reducing exposure rather than reallocating within the market.

Even during periods of heightened climate uncertainty, however, funds with stronger ESG profiles continue to attract relatively higher investor confidence.

More broadly, we found that climate uncertainty itself makes investors more reliant on past performance as a signal of managerial skill – especially for funds with strong ESG ratings.

A changing market climate

As with Australia's reporting regime, which came into effect from the start of last year, many of New Zealand's requirements have focused on improving transparency.

Our findings suggest these frameworks may be doing much more than that. They appear to be helping influence how capital is allocated in markets.

It remains to be seen how the government's reforms will affect this dynamic, particularly as many companies and managed investment scheme managers exit the mandatory reporting regime.

However, as Deloitte's report notes, stepping out of the reporting regime does not remove market expectations, because climate risk remains central to how capital is allocated.

For companies and investors alike, the implications of this trend are significant.

While the amended legislation eases specific reporting liabilities for directors to encourage transparency, firms that are better positioned for a low-carbon transition may find it easier – and potentially cheaper – to access capital. Those that lag face growing pressure.

For fund managers, this means ESG should no longer be treated as a peripheral consideration, but as a core part of how risk and performance are managed and communicated.

For investors, it's clear this rating is serving as a useful guide to where to put their money.

What we are observing may be the early stages of a broader shift, where success depends as much on how funds are positioned for the future as on their past performance.

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