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“Carbon Disclosure, Emission Levels, and the Cost of Debt”

Abstract

In this paper, we investigate the effect of voluntary carbon emissions disclosure on the cost of debt of publicly listed firms. Using a unique and comprehensive database on carbon emissions from CDP (formerly ‘The Carbon Disclosure Project’), we study whether firms which choose to voluntarily disclose their carbon emissions enjoy more favorable lending conditions – in the form of lower spreads on their bank loans – than their non-disclosing counterparts. Our empirical results reveal a significant and negative relation between voluntarily disclosing carbon emission levels and the cost of bank loans for informationally opaque borrowers. Furthermore, we find that higher industry- and firm-size-adjusted carbon emissions have a positive and significant effect on loan spreads. This effect is stronger for borrowers which have only weak control over their emissions. Furthermore, this effect exists for loans arranged by norms-constrained as well as –unconstrained lenders suggesting that spread premia are driven by environmental risks rather than investor preferences.