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“Climate Risk Disclosure and Information Asymmetry – Do Physical Risks Matter?”

Abstract

Investors show increasing concern about the negative financial implications of the impacts of climate change on business activities. In this regard, we examine the association between information asymmetry and the voluntary disclosure of companies’ exposure to physical risks arising from climate change. On the theoretical basis of information economics, we investigate whether reporting about physical risks is associated with information asymmetry and whether this association is different between companies operating in high and low carbon emission industries. Our analysis is based on a sample of 717 European companies over three years (2011–13) and their information, if any, provided about physical risks in their responses to the questionnaires of the Carbon Disclosure Project (CDP). We find information asymmetry to be significantly lower for firms reporting on physical risks. Moreover, our results indicate a moderating effect of high vs. low emission industry. In high emission industries higher levels of physical risk exposure are related to lower information asymmetry, while the opposite holds for low emitting industries. Our results show the relation between disclosure and information asymmetry is dependent on contextual factors. Moreover we show that a more in-depth view of carbon-related disclosures is warranted, and the effect of climate change on companies is, indeed, of interest to (potential) investors.