

Episode 0 - MI

Climate Risk Is the Most Underpriced Variable in Real Estate

Signal 3 -Capital Allocation & Investor Flows, Signal 1-Insurance Repricing & Availability, Signal 8 - Disclosure, Taxonomy & Regulatory Regimes

Welcome to the first-ever short brief of *Climate-Ready Real Estate Investing*. Each week, in addition to guest expert interviews, our audience receives three short briefs focused on market intelligence - like this one, strategy and underwriting, as well as narratives of current events with future implications. The theme underlying *Climate-Ready Real Estate Investing* is a deep concern for the well-being and viability of our planet, today and tomorrow, and a desire to explore how best to support this USD \$393 trillion industry in making both profitable and forward-thinking, big-picture decisions, borrowing from the Hippocratic Oath to 'first do no harm.'

To kick us off this month, we are reframing climate change as a matter of market structure rather than ideology. To set the stage, the very first thing we will examine is why climate risk is the most underpriced variable in real estate. It's a mistake to think climate risk is just an environmental issue. In real estate, it is a pricing error.

Now let's dive into the first episode.

Market Signal

Climate risk is not yet fully priced into real estate investing. Markets are still valuing assets based on historical comps, recent rent growth, and interest rates — while the climate-driven forces already shifting future outcomes — insurance, operating costs, migration, and regulation — remain largely absent from the analysis. Real estate markets price well what has already happened. They struggle to price what is changing slowly but inevitably.

That gap has a name: mispricing. Buyers are paying today's prices for yesterday's assumptions, and future costs and constraints are not yet fully reflected in valuations. The result is a gap that runs in both directions — mispriced risk on one side, mispriced opportunity on the other.

Deal Breakdown

Let's look at a real-world example.

Two properties can have the same price, the same rent, and the same comps today, yet produce very different outcomes for investors once climate risk starts moving through insurance, operating costs, and buyer demand.

Consider a straightforward scenario. Two identical new-build properties are purchased today at the same price. Property A sits in the Colorado Springs metro, closer to the Front Range foothills. Property B sits in the University District of Greeley in Northern Colorado. On paper, they look nearly interchangeable. Same purchase price. Same short-term rents. Same near-term comps.

But that is exactly where many investors stop their analysis too early.

Because over the next five to ten years, these are not the same asset.

Property A carries a higher acute wildfire risk. That foothills location sits in documented wildland-urban interface territory — the Colorado Springs area has over 51,000 homes in wildfire risk zones, and the Front Range foothills are explicitly identified as high-risk wildland-urban interface (WUI) areas by the Colorado State Forest Service.

Property B, in Greeley's University District, carries a lower acute wildfire risk relative to that of the foothills location. That difference matters for insurance access and premium stability. That said, Greeley carries its own climate exposure profile — notably high heat and drought risk, with a projected 142% increase in days over 94°F over the next 30 years. The point is not that Greeley is risk-free. The point is that the specific risks are different, and those risks are priced differently in insurance and lending markets.

That difference matters because climate risk does not stay neatly inside an ESG (environmental, social, and governance) conversation. It shows up in the cost stack. It shows up in insurability. And eventually, it shows up in liquidity.

Colorado is a strong example. A 2023 study commissioned by Colorado's Division of Insurance (DORA) found that average homeowner premiums in the state rose by 51.7% between January 2019 and October 2022, with the rate of increase accelerating and inflection points coinciding with major wildfires. The same study found that, by 2022, 76% of carrier groups were shrinking their exposures in Colorado.

More recently, Colorado data shows home insurance premiums rose 58% from 2018 to 2023, according to Colorado State University's Regional Economic Development Institute and the Rocky Mountain Insurance Association. That is not a slow drift — that is a fundamental repricing of risk in a market that many investors still assume is stable.

That is the first insight: climate risk gets priced first through insurance friction, not necessarily through headline property values.

So in the short term, Property A and Property B may both rent for the same number. They may both appraise similarly. They may both attract similar buyers. But over time, Property A is more likely to face rising wildfire-related premiums, tighter underwriting, higher reserve needs, and more volatile ownership costs in the foothills insurance market. Property B's insurance exposure looks different — driven more by heat and weather events than by acute wildfire risk — but its near-term insurability in the standard market is more stable.

And markets tend to reward predictability.

The second insight is that repricing often happens suddenly rather than gradually. Investors like to imagine a slow, orderly adjustment. But real estate markets rarely work that way when a key dependency breaks. The break can come when a carrier exits a zone, when premiums double at renewal, when a buyer cannot secure acceptable coverage, or when a lender starts asking tougher questions about hazard exposure and replacement assumptions.

Colorado now has a FAIR Plan — a last-resort insurance option for properties that cannot secure standard-market coverage — and it began accepting residential applications in April 2025. The FAIR Plan itself is explicit: it is a last resort, more expensive than standard coverage, and offers actual cash value rather than replacement cost. That is not a sign of normal market health. That is a pressure-release valve for a stressed insurance market.

So return to the two properties.

Five to ten years out, Property A may still be standing, occupied, and technically rentable. But it may also carry meaningfully higher costs and appeal to a narrower buyer pool. Property B may not immediately produce higher rent. Still, it may hold a stronger position on the insurance-access dimension — where investors increasingly pay for cost stability, ease of financing, and insurability.

That is the strategic takeaway: climate exposure is no longer just a physical-risk question. It is a valuation and exit-liquidity question.

The market signal to watch is not only where fires, heat, hail, or other weather events occur. It is where insurance remains available on reasonable terms, where ownership costs stay manageable, and where future buyers can still close without friction. Because in the next phase of this market, the better asset may not be the one with the highest theoretical upside. It may be the one that remains easy to insure, finance, and sell.

Where does that leave us in our investment decision-making process? I'll answer a question with a question...

Strategic Implications

What if the market is still pricing real estate as if climate risk were a future concern, while insurance, operating costs, and capital markets are already treating it as a present one?

That gap is where the investment story is changing.

Climate risk is often discussed as a physical, environmental, or policy issue. In real estate, it is something more immediate and more consequential: a financial transmission mechanism. It does not move through the market as a single isolated variable. It moves through multiple channels at once — insurance, operating costs, financing, migration, and regulation — and each channel can alter asset performance before traditional valuation metrics fully catch up.

Start with insurance.

Insurance is often the first market to register stress because it has no choice. Carriers and reinsurers must translate exposure into price, terms, deductibles, exclusions, and capacity

decisions in real time. Property markets, by contrast, can remain anchored to recent sales, legacy assumptions, or investor optimism for much longer. That is why insurance often functions as the first-mover signal. When premiums rise sharply, when deductibles widen, when coverage becomes thinner, or when carriers pull back altogether, that is not just an operating expense story. It is an early sign that risk is being repriced somewhere in the system before property values have fully adjusted.

And once insurance weakens, liquidity can follow. Because when coverage becomes uncertain, lending becomes more complicated. Buyers become more selective. Transaction friction rises. Assets that looked straightforward to finance begin to require more scrutiny, more reserves, or more conservative assumptions. In other words, when insurance breaks, market function often begins to break before appraised value does.

The second channel is operating cost pressure. Climate exposure does not hit the income statement evenly. Heat drives higher cooling loads. Storm activity accelerates wear on roofs, drainage systems, paving, and building envelopes. Over time, what seemed like a normal asset can start demanding abnormal maintenance. Then come the capital decisions: backup power, insulation upgrades, drainage improvements, defensible space, fire hardening, water management, resilience retrofits. These are not always dramatic one-time shocks. More often, they show up as a steady upward drift in expense intensity.

That is what makes them dangerous from an underwriting standpoint.

They compress NOI gradually, which means they can be missed at acquisition and felt later in operations. And because they do not arrive evenly across markets, two properties with similar purchase prices today can produce very different economics over time. The issue is not simply that costs are rising. It is that they are rising unevenly, and the dispersion matters.

Then comes financing and exit risk. Lenders do not need to make a dramatic public statement for climate risk to change credit conditions. They can express that concern quietly by using lower leverage, higher reserves, tighter debt-service coverage requirements, stricter insurance conditions, or more conservative assumptions about future performance. For borrowers, that becomes particularly important at refinance. If expenses have risen faster than expected and NOI has weakened, the same asset may not refinance on the terms originally underwritten.

And that pressure does not stop there.

Exit buyers will be looking at the same climate exposure, the same insurance market, and the same operating trends — often through a more cautious lens than the original buyer. That can reduce bid depth, increase cap-rate sensitivity, and widen the gap between what sellers think an asset is worth and what buyers are willing to pay. Climate risk, then, is not just about current cash flow. It is about the future availability, price, and confidence of capital.

The fourth channel is migration. Climate risk is also a demand story. Households and businesses increasingly consider livability, utility reliability, water access, recovery capacity, and insurance affordability when choosing where to live and invest. Over time, that can push demand toward

regions perceived as more stable, more reliable, and easier to insure. In those places, rent growth, occupancy, and investor confidence can strengthen. In more exposed markets, demand may not disappear, but it can become less durable, less predictable, and more expensive to serve.

That matters because demand shifts eventually become value shifts. They may begin quietly, with slower absorption here or stronger rent growth there. But over a full cycle, migration can reshape local pricing power. Climate risk is not only a downside variable. It is also a capital-allocation variable, because capital tends to follow the markets where demand proves more resilient.

The fifth channel is regulation. Regulation often arrives after insurance repricing or operating stress, but it can still have major economic consequences. Once losses rise and political pressure builds, building codes tighten, disclosure requirements expand, efficiency standards increase, and resilience measures that once felt optional begin to look mandatory. Elevation requirements, fire-hardening standards, stormwater upgrades, energy retrofits — all of these can become future costs embedded in today's purchase.

That is why regulation is best understood not as a separate issue, but as delayed cost recognition. The market may ignore it early. But when compliance eventually arrives, the owner pays for the lag.

So what is the core insight? Climate risk is not a single underwriting adjustment. It is a multi-channel financial force. It moves through insurance. It moves through operating costs. It moves through financing conditions, migration patterns, and regulation. Each channel matters on its own, but the real investment impact comes from the way they interact. Higher insurance can weaken lending. Rising operating costs can pressure refinancability. Demand shifts can alter growth expectations. Regulation can force capex into already-compressed assets.

That is why this matters now.

The market does not always reprice these channels all at once. For long stretches, they can remain partially disconnected. Insurance may be signaling one thing while transaction values still imply another. Operating stress may be building even as lenders have only just started to respond. Demand may already be shifting while valuation models remain backward-looking.

And that disconnect is where opportunity — and risk — live.

Because the investors who win in the next cycle are unlikely to be the ones who treat climate as a headline. They will be the ones who understand it as a system of financial transmission channels, and who underwrite those linkages before the broader market fully prices them.

The real question is no longer whether climate risk matters. The real question is which markets are still pretending it does not.

Future Signal

The next market transition is not broader recognition of climate risk, but explicit financial pricing of that risk within underwriting and valuation frameworks. As markets convert physical exposure into credit terms, operating assumptions, and asset pricing, climate shifts from a qualitative

concern to a measurable pricing factor. That transition is significant because explicit pricing tends to quickly compress ambiguity. Once climate risk becomes an underwriting input, it stops being a narrative and starts being a valuation driver.

Appraisal frameworks are likely to evolve toward greater recognition of resilience, insurability, and recovery capacity as differentiating asset characteristics. Assets with similar location, rent, and physical specifications may no longer justify similar values if their long-term operating durability differs materially. This would formalize resilience as a component of value rather than a peripheral consideration. When resilience enters appraisal logic, value dispersion becomes easier to justify and harder to ignore.

Lenders can incorporate climate exposure through leverage, reserves, insurance requirements, and forward operating assumptions without making climate the overt centerpiece of credit policy. As a result, repricing may emerge first through financing conditions rather than through headline valuation cuts. This channel matters because debt markets often impose discipline faster than transaction markets do. Credit tightening is often the mechanism by which climate exposure first reaches asset prices.

Institutional capital is increasingly oriented toward durability, liquidity, and operating resilience over long hold periods. As those preferences intensify, capital is likely to cluster more heavily in markets perceived as more stable and more financeable. That concentration can widen valuation premiums in favored regions while weakening bid depth in exposed markets. Capital does not reward resilience evenly, but over time, it tends to reward it decisively.

High-risk markets may not experience smooth long-term markdowns; they may instead reprice through step-change events tied to losses, insurance disruption, financing resets, or regulatory shifts. This pattern is important because it creates the appearance of stability between shocks while preserving the potential for abrupt valuation adjustment. Investors who assume a gradual decline may understate the risk of discontinuity. In exposed markets, repricing risk is often less about slope than about the timing of sudden adjustments.

A more relevant forward metric is climate-adjusted NOI: income after incorporating realistic insurance escalation, climate-linked operating expense pressure, resilience capex, and financing friction. Traditional NOI can overstate economic durability when those channels are excluded or understated. Climate-adjusted NOI provides a more disciplined view of sustainable earnings power and should become increasingly important in asset selection and valuation. The assets that appear to yield well today may not be the assets that sustain yield once climate-adjusted NOI becomes the standard lens.

We started this brief by stating that climate risk is the most underpriced variable in real estate, and we went on to make that case. So how do you best act on that premise?

Stakeholder Takeaway

For investors:

If climate risk is not in your underwriting, your assumptions are incomplete.

These are the actions you should take immediately:

- Identify exposure (heat, water, insurance, regulation)
- Translate that exposure into costs and risk
- Adjust pricing accordingly

The opportunity is not just avoiding risk — it is identifying where resilience is still undervalued.

I ask the same question at the end of every show, because if you could enjoy 20/20 hindsight before you learn the hard way, your clients would truly adore you. If you could see years into the future and use that understanding today to make differently-informed decisions now, what would your portfolio look like today?

That wraps it up for today. The next brief is titled "*Why Climate Risk Is an Underwriting Variable, Not a Moral Debate*." Be sure to subscribe to *Climate-Ready Real Estate Investing* to receive free downloads for our Market Intelligence and Strategy & Underwriting briefs. Listen to the [podcast](#) and find us on [LinkedIn](#). If you'd like to be a guest on the show, you can register at www.climatereadyre.com, the place where resilient returns and resilient communities meet. Until next time, I'm your host, Jamie Wolf — be good and do better for today, tomorrow, for you, and for all. KNOW YOUR SIGNALS AND BE CLIMATE-READY!

OUTRO – CTA

This has been the intelligence briefing on *Climate-Ready Real Estate Investing*, where we explore climate through a financial lens to achieve resilient returns and resilient communities. Find us on LinkedIn and Twitter. To get the Climate-Ready Deal Framework™ to help you re-evaluate your deals, go to www.climatereadyre.com, enter your email address, then check your inbox. See you next time!

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