

Why climate investing goes beyond vertical funds

Last year, investors poured \$10B into European startups working to tackle the climate crisis. As interest in these investments has grown, many new investors have created dedicated climate ‘vertical’ funds.

These vertical funds are often dedicated solely to climate-oriented investments. And yes we need more of them!

But is this the best way – or only – way VCs can invest in startups tackling climate change? Restricting climate investments to a single vertical can result in an investment philosophy that’s very much “all or nothing”, and geared solely towards startups that are only focused on the climate in a much narrower sense. This risks leaving vast innovation gaps in the market and reduces VCs’ capacity to incorporate environmentally friendly investments in all their other verticals. In the end, we need to transform all sectors to achieve a zero carbon economy.

Teams should be looking to discover companies that provide innovations that can be integrated into

existing industries and that help them to help to reduce emissions.

This requires specialist sector knowledge beyond an overarching interest in climate. For example, there is a lot of climate-positive innovation in finding ways to improve efficiency and reduce waste or energy consumption. You wouldn't necessarily think that a packaging startup is a climate startup, but if it can reduce the quantity of materials required or change the type of material used, then its positive climate impact can be considerably big.

A VC's climate-friendly investments should not be limited to explicitly climate change technologies like carbon capture, but should also include any companies that can have a robust and tangible positive effect on the climate and emissions in general. In the end, we need both!

Keep climate investing broad

A vertical team in a VC can fall into the trap of becoming isolated, leaving them underexposed to some of the less obvious knock-on effects in specific industries. As with any specialty, it is a constant challenge to ensure that interdisciplinary innovations don't fall through the cracks for not perfectly fitting with any single team. With climate tech, it should be all interdisciplinary.

This is why teams should instead focus on treating climate as a "horizontal" – a commitment and collaboration across sector-specialist teams to find ways to improve climate outcomes in their sectors. The value of this approach is that it encourages investment teams to leverage their sector and vertical expertise: whether it's deeptech teams investing in technologies and architectures that help improve the power consumption of computing and storage, or industrial teams investing in superior materials and processes to cut waste in the construction sector.

The horizontal approach allows teams to use their sector knowledge to identify and invest in the technologies and business models they know will succeed in the market and make the most difference on the ground.

Climate accountability

Along with a horizontal approach to investing, VCs should also make sure they have rigorous climate accountability standards when it comes to prospective

portfolio companies. Tackling the climate must be a *cross-industry* effort, and have a unique opportunity to embed climate accountability into the core of all new portfolio companies, whether through environmental policy standards or dedicated climate reporting.

While many established companies are now ‘tagging on’ climate policies, VCs have the power to propel companies that are climate-conscious at their core. The same is true of VCs themselves. Rather than ‘tagging on’ a climate team, climate accountability should be applied across the board. When VCs account for climate investment as a horizontal commitment, everyone should aspire to treat emissions reduction as an intrinsic target for all prospective portfolio companies.

The climate should constitute one of the most important umbrella factors, encompassing all vertical interests.

If the climate is seen as a horizontal issue, VCs can not only push for better accountability in their existing investments, it also avoids the ‘all or nothing’ approach discussed earlier.

The process for building this horizontal structure begins with educating partners across all vertical teams so that everyone is a climate specialist. Once environmental policy education and climate consciousness are “horizontal” principles across all teams, accountability will follow in the investments, and the team will make cleaner investments across all its specialties. As well as improving existing investments and portfolio companies, this holistic education will also enable VCs to ensure that crucial interdisciplinary innovation isn’t being missed.

Andreas Schwarzenbrunner is partner at *Speedinvest*.