Takeholders are increasingly press- 
suring institutional investors to 
divest from companies — particu- 
larly in the fossil fuel, private prison 
and tobacco industries — due to 
predicted long-term impacts of en- 
vironmental, social and governance 
issues.

For most companies in these and 
other industries, investor sources tell 
Agenda that they still think engage- 
ment is more effective in terms of 
agreeing companies address their con- 
cerns. But for those companies that 
may not survive the next 10 years, 
some sources say divestment is the 
only option.

For boards, the climate crisis and 
increasing focus by investors on 
ESG issues not only brings pressure 
to disclose or engage, but threats to 
divest that could ultimately result in 
changes to the composition of their 
investor base.

“We are looking very closely at 
how boards of directors are tackling 
this real challenge and we are ex- 
pecting them to exercise oversight 
of climate risk,” said Liz Gordon, 
executive director of corporate 
governance at the New York State 
Common Retirement Fund. “I want to see [boards] giving it some 
real thought and developing their own strategies that work to make 
money for them and us over the 
long haul.”

NYSCRF, under the direction of 
New York State Comptroller Thom- 
as DiNapoli, restricted investments 
in five coal producers earlier this 
year. In total, the pension has di- 
vested from 22 companies in 2020 
and 2021. It initially sent letters to 
27 coal companies to let them know 
about risk assessments the fund had 
completed, asking the companies to 
respond and provide more information. 
Ultimately, the fund found that 22 
of the 27 companies “didn’t have a 
path forward given their current lev- 
els of capital expenditures and their 
current disclosures didn’t meet a, 
frankly, low bar,” said Gordon.

The fund continues to stay in 
touch with these companies to see 
if there is a change in approach, and 
the companies could become available for investment again if they 
took steps to address risks, Gordon 
said.

NYSCRF is not alone. According 
to a July survey by Investopedia 
and Treehugger, 29% of more than 
700 investors who include ESG cri- 
tera in their decision-making said 
they’ve divested or sold shares for 
ESG reasons. Many other pension 
funds, endowments and other inves- 
tors are considering divestment cam- 
paigns after coming under pressure 
from their own stakeholders. For 
example, Baltimore, Maryland, this 
month directed its pension funds to 
divest from fossil fuels. The city joins 
BlackRock, BNP Paribas, Harvard 
University, the MacArthur Founda-
tion and New York in pulling money 
out of coal and fossil fuel producers 
as the climate crisis becomes more 
urgent.

Similarly, the Maine state legisla-
ture passed a statute in June requir- 
ing the $17 billion Maine Public 
Employees Retirement System to 
divest $1.3 billion from fossil fuels 
within five years and the state trea-
sury to do the same with other state 
funds.

“What we are doing now is study-
ing how to implement the statute 
consistent with our fiduciary duty,” 
said Michael Colleran, COO and 
general counsel at MainePERS. “We 
are examining our current fossil fuel 
exposure in our portfolio and look- 
ing to see what alternatives there are available with comparable risk-
return profiles and costs.”

He continued: “Fossil fuels have, 
over time, become a smaller part of 
our portfolio and in all likelihood 
will continue to do so as people 
move away from fossil fuel and to- 
wars renewable energy.”

At the California State Teachers’ 
Retirement System, divest- 
ment is reserved for “the most ex-
treme cases,” when the fund objects to the core business of the company, the company declines to change or adapt and the money-making situation for the fund is “unsustainable,” according to Chris Ailman, chief investment officer at Calstrs. This includes the coal industry and the firearm industry, he said.

“This is when the risk is too great and will overcome the return opportunity,” Ailman said. The firm has made six divestments, four of which “lost us a lot of money,” Ailman said. The most expensive divestment was tobacco, he added.

The private prison industry is also under pressure. Calstrs divested from CoreCivic and the GEO Group in 2018, and pension funds in New York and Rhode Island pledged to divest as well.

But the fossil fuel industry may be generating the most divestment campaigns these days. Investors pulled an estimated $14 trillion out of fossil fuel companies as of last year.

“There are major pension funds committed to divest, cities that have divested those [fossil fuel] assets, philanthropies, universities — it has spread all over the world,” said Ellen Dorsey, executive director of the Wallace Global Fund and president of the DivestInvest global network, which encourages divestment from fossil fuels. “This is coming after a decade of activism. You are seeing the elite institutions within their sectors now committing. This is going to go fast into the mainstream — the floodgates are open.”

Meanwhile, NYSCRF is currently evaluating 42 publicly traded shale oil and gas companies that derive more than 10% of revenue from crude oil and gas production from shale, including Marathon Oil Corp., ConocoPhillips and Hess Corp.

“Divestment is a last resort — only to use when we see a risk can’t be addressed through engagement,” Gordon said. “It’s a very high bar. We also take the process around it very seriously. We develop policies to articulate why a particular risk rises to that level where we would even consider divestment.”

New York City’s portfolios experienced no negative financial impacts from divesting fossil fuels, according to research that BlackRock conducted for the Teachers’ Retirement System of the City of New York. In future divestment considerations, the fund should keep in mind that “the fossil-fuel-linked securities of each divestment option have underperformed the broader investment market over the last five years,” the report said. As a result, two of New York City’s pension funds voted to divest an estimated $4 billion from fossil fuel securities.

BlackRock itself announced last year that it would remove any companies that generate “more than 25% of their revenues from thermal coal production” from their active portfolios, impacting roughly 0.007% of its total holdings.

Indeed, Dorsey said portfolios that divest from fossil fuels tend to outperform those that do not. For example, at Wallace, which divested from fossil fuels in 2014, the firm is “crushing all of our benchmarks.” Indeed, the fossil-free funds project from As You Sow reports that both State Street Global Advisors’ and Parnassus Investments’ fossil-free indexes have posted higher annualized returns than BlackRock’s core S&P 500 ETF on a three-year and five-year basis as of Aug. 31.

Still, even as some pensions, endowments and others divest from certain industries, others are still buying up those shares. For example, the Financial Times recently reported that hedge funds are buying shares in oil and gas companies other investors divested and posting large gains in doing so.

Engagement

Investors say they generally prefer engagement to divestment. For the NYSCRF, it has “long been committed to engagements. We want our companies to succeed,” Gordon said. “We want to be invested in them for the long haul, which requires a frank discussion about the risks we perceive and how to address those risks.”

This active engagement includes direct meetings with company management and board members, letterwriting campaigns and filing shareholder resolutions, Gordon said.
Similarly, at Calstrs, Ailman said that when dealing with an issue that an industry or company faces that presents an outsize risk, the first thing the firm does is engage, including traveling to the company to meet with management and have a dialogue.

The pension wrote last year that divesting from fossil fuels “fails to address the myriad issues that contribute to climate change.”

“While the major oils are seen as the evil empire, they may be the groups that have the solutions,” Ailman said. “We are a friend, not a foe.” But directors can’t have their heads in the sand when it comes to innovation and adapting to change, he continued. Otherwise, the company will be “like a BlackBerry or Kodak” that won’t withstand the test of time and will lose investors in the process.

But to Dorsey, the divestment activist, engagement in some industries just hasn’t worked. She said investors have engaged companies in the fossil fuels sector “for decades, and it has failed. They haven’t moved the needle at all and are moving against science. The time for engagement is absolutely over.”