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LONG VIEW: Victor Makras said San Francisco trustees are going to study the issue, and no fast decision is expected.

Investing

Investors' paths diverge on fossil fuels

Public funds choose engagement, while some endowments divest

By **RANDY DIAMOND**

Public pension funds are lagging behind endowments and foundations in divesting investments in fossil-fuel companies, choosing instead to engage energy companies through discussions and shareholder resolutions.

Stanford University, other smaller college endowments and a coalition of foundations have all taken divestment actions in recent months — with promises of more to come. But the only public pension fund to take up the issue publicly, the $19 billion City & County of San Francisco Employees' Retirement System, is moving slowly.

In what is believed to be a first for a public pension fund, board members of the San Francisco fund held a public hearing last month on divesting from fossil-fuel stocks.

No vote was taken. Afterward, Victor Makras,

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board president, said in an interview that board members "want to study the issue carefully," and that a decision could be at least several years away.

The hearing followed an April vote by the City & County of San Francisco Board of Supervisors calling for the pension fund to divest its holdings in the 200 largest companies that own the vast majority of the world's coal, oil and gas reserves.

Approved a policy

Mr. Makras said the pension board in February approved a policy to consider climate change in its proxy votes at fossil fuel companies. He said the board is considering expanding efforts to engage companies directly.

If board members determine those efforts have failed, only then would they consider divestment, Mr. Makras said.

Equity investments in oil, gas and coal companies made up 5.8% of the pension fund's $10.3 billion equity portfolio as of Dec. 31, pension fund data show.

If the San Francisco retirement system were to decide to divest, it would be the first public pension fund to do so, said Jay Huish, executive director.

The two largest public pension funds in the U.S. — the $300.4 billion California Public Employees' Retirement System, Sacramento, and $184.8 billion California State Teachers' Retirement System, West Sacramento — are known as leaders in socially responsible investing. Both have taken an engagement approach with fossil-fuel companies, rather than divesting.

"Washing your hands of the problem is not going to force fossil-fuel companies to make the necessary changes," said Anne Simpson, senior portfolio manager and director of global governance at CalPERS.

Ms. Simpson said that CalPERS selling its shares could cause negative performance implications for the pension fund. She also said fund executives look at the issue through an economic lens. For example, requiring companies to stress-test assumptions about financial risks posed by stranded energy reserves would help mitigate the retirement system's investment risk over the long term.

"For a fund our size, responsible ownership is the preferred strategy," Ms. Simpson said.

Ms. Simpson said CalPERS engages companies directly and through a network, the Investor Network on Climate Change, organized by CERES, an investor advocacy group addressing climate and other sustainability issues.

Some endowments and foundations have taken more decisive action, although the number that actually has divested is still relatively small.

Stanford University in May became the largest institutional investor to approve a divestment policy. The university, responding to pressure from student and environmental activists, announced its $18.7 billion endowment would sell its stock in coal-mining companies. But university officials rejected demands that it expand the divestment beyond coal to the 200 largest publicly traded fossil-fuel companies.

In June, the University of Dayton, Ohio, board of trustees approved a new divestment policy for the university's $670 million endowment. Divestment of fossil-fuel companies in its domestic equity portfolios will occur first, followed by international equities and, eventually, restrictions on holdings in new private equity and hedge fund investments.

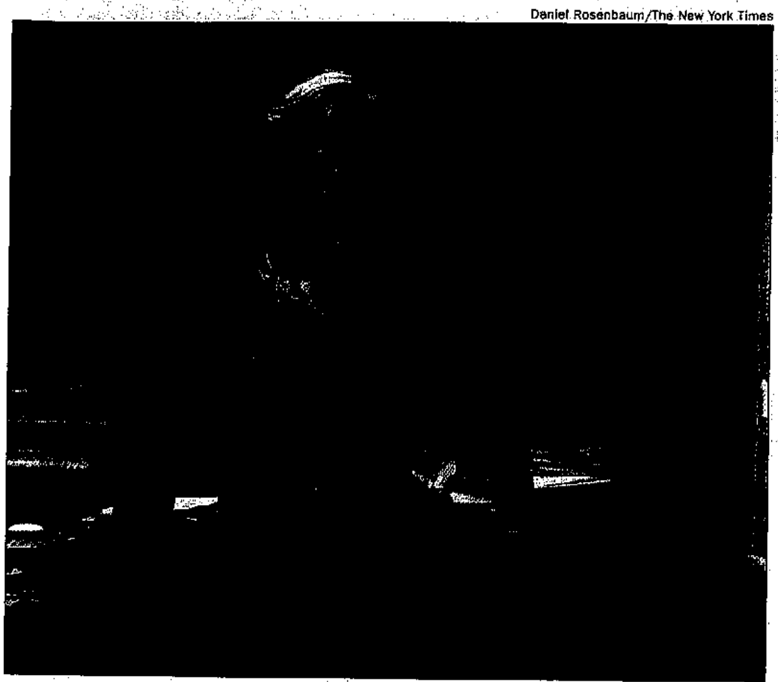
And in April, Pitzer College, Claremont, Calif., announced plans to divest its $125 million endowment of fossil-fuel stocks.

But others, like the $32.7 billion Harvard University endowment and the $2.9 billion Brown University endowment, have rejected calls for divestment.

Announcement coming

More institutional investors will announce at a United Nations climate summit in September that they will be divesting fossil-fuel company investments, said Ellen Dorsey, executive director of the Wallace Global Fund, Washington. The $125 million foundation was one of 17 foundations, with assets totaling $1.76 billion, to announce joint divestment efforts in January. Ms. Dorsey would not identify the other investors who will be announced in September, but said

Daniel Rosenbaum/The New York Times



IN QUESTION: Ellen Dorsey doesn't think engagement will be effective.

their combined assets will be significantly more than the first wave.

She said the approach by pension funds to engage fossil-fuel companies won't work, noting major companies are intent on burning their reserves and continue to maintain government regulation limiting carbon emissions won't occur.

"Prudent investors are listening to the warnings that fossil-fuel stocks are overvalued, as we cannot possibly burn the reserves coal, oil and gas companies currently hold without cooking the planet," Ms. Dorsey said.

But the effect of a fossil-fuel-free portfolio on investment returns is also the subject of debate.

At the June 18 San Francisco public hearing, Thomas Kuh, the Boston-based executive director of MSCI Inc., said the firm's analysis showed a fossil-fuel-free index had underperformed the MSCI World index and the MSCI USA index for the 10-year period ended May 31, but outperformed for the one-, three- and five-year periods as of the same date.

One major university that in the next few months could make a divestment decision regarding its $7.8 billion endowment is the University of California system, Oakland.

Board of Regents Chairman Bruce Varner in May announced a task force would be formed to study the issue. Mr. Varner said task force members would meet with the university's new chief investment officer, Jagdeep Singh Bachher, and the university's investment committee.

"We'll have some definitive recommendations or comebacks for our meeting in September," Mr. Varner said in an audio tape of the meeting on the university website.

There is a reason endowments and foundations have been the first movers on fossil-fuel divestment, said Roger Urwin, global head of investment content at Towers Watson & Co. in London.

"They invest more with a mission purpose," Mr. Urwin said. "They find it easier to invest in a way that is aligned with their stakeholders."

Public pension funds, on the other hand, are more cautious, Mr. Urwin said.

"They will usually say, finance first, anything that reduces my opportunity isn't good for diversification," he said.

Mr. Urwin said, however, the issue of ending investments in fossil-fuel companies won't be going away anytime soon and what happens in Paris in late 2015 at a U.N. climate conference could have global implications for fossil-fuel divesture.

The organizing committee for the conference has said it wants to obtain what has been elusive so far: a worldwide agreement on limiting greenhouse gas emissions. ■