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CalPERS getting pushback on ESG efforts

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CalPERS is trying to stick to its ESG plan despite opposing forces.

CalPERS is finding that it's not easy being green, as it battles push back from anti-ESG forces as well as those that want the $492.8 billion pension fund to divest from fossil fuels.

California Public Employees' Retirement System, Sacramento, has had a rough time of it lately. Close to three years after CalPERS scored a big win, leading an investor group that replaced three directors at Exxon Mobil Corp., the oil and gas giant in January dealt CalPERS and other investors a serious blow. It is suing two activist investors over a climate-related disclosure shareholder proposal even though the investors have withdrawn the proposal.

A month later, five companies including J.P. Morgan Asset Management, State Street Global Advisors and PIMCO left Climate Action 100+, the largest investor-led engagement climate change initiative and which CalPERS helped launch.

At the same time, a California bill that would require CalPERS and the $325.9 billion California State Teachers' Retirement System, West Sacramento, to stop investing in fossil fuel companies and to divest from existing fossil fuel investments by July 1, 2031, is back for a second year winding its way through the state legislature. **CalPERS and CalSTRS both oppose the bill**.

And CalPERS board members are voicing increasing concerns with the treatment of workers at private equity-backed companies despite the majority of the board voting on March 18 to **increase the pension fund's allocations** to private equity and private credit.

CalPERS is an active owner and it is part of its fiduciary duty to keep tabs on how companies manage their risks from climate change as well as from treatment of its employees, said Marcie Frost, CalPERS CEO, at the March 20 board meeting.

"As we have seen there are company CEOs who were leaders in ESG who are no longer in these roles," Frost said. "It shows how important it is to stay a collective."

Frost said that she had planned to appear before the state legislature to give CalPERS' side of the story and explain its sustainable investments plan but the hearing was canceled.

"We understand the divestment bill is still active but we want to give a counterpoint," she said. "CalPERS has a much longer time horizon than a particular legislator."

Frost said she planned to tell the legislative committees that CalPERS has already committed $47 billion to climate solutions, largely in public equity and real estate, and has plans to double that amount by 2030.

"This will cut carbon of CalPERS' portfolio by half," Frost said. She added that CalPERS officials believe that it is a highly achievable goal and consistent with their fiduciary duty.

At the same meeting, board Chairwoman Theresa Taylor said that how well CalPERS "manages risk and climate risk is at the heart of providing retirement benefits to our members."

"Lately one risk is misinformation when it comes to the issue of sustainable investments," Taylor said. She noted California's fossil fuel divestment bill and more than a dozen states that are considering or have passed anti-ESG bills.

"As president of the CalPERS board let me be clear, we are fully committed to managing climate risk to preserve long-term value for our members in line with our fiduciary duty," Taylor said. "It is part of our investment analysis, and we will continue to work with likeminded investors to advocate on the importance of sustainable investing."

As for Exxon's lawsuit and the managers that left Climate Action 100+, Taylor said during a proxy voting and corporate governance report at the investment committee meeting that "all of the work that we've done over the past 20 years is being pushed back on."

"I think we need a plan and that plan needs to include whether or not we keep these people in our portfolio," Taylor said.

Taylor was also one of the board members that questioned whether the board should change its asset allocation. Among other reasons, Taylor said, "private equity-owned businesses have a lot of problems," including worker harassment.

After a closed session, Taylor ended up seconding the successful motion that increased private equity by 4 percentage points to 17% and boosted its new private debt allocation 3 percentage points to 8%. It also cut public equities by 5 percentage points to 37% and fixed income by 2 percentage points to 28%. Real assets remains at 15% and leverage stays at 5% of the entire portfolio.

Drew Hambly, CalPERS' global equities investment director, also at the investment committee meeting said that he thinks that more companies will leave Climate Action 100+, mainly U.S. companies and that at that time, five companies had quit. BlackRock Inc. had also transferred its participation in the initiative to BlackRock International. Hambly said that more companies have joined than have left the initiative: 72 members were added in the second half of last year vs. five that left.

Frost added that CalPERS officials have engaged with the exiting companies with whom the pension fund has a relationship.

When it comes to Exxon and other high fossil fuel emitting companies in CalPERS' portfolio, Hambly said the pension fund's strategy of cordial engagement with companies to encourage them to share some data on emissions and plan to reduce emissions has worked. He noted that CalPERS' successful 2021 campaign was three years ago when the price of oil was lower than it is today.

“It’s a more difficult challenge with the price of oil for these companies to completely stop doing that business,” Hambly said.