Will Big Pension Climate Moves Be a 'Watershed' Moment?

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Public pensions both large and small made some major commitments to decarbonizing their portfolios last year, from shareholder engagement to divestment.

Pension trustees, who are bound to a fiduciary duty to ensure retirees get their benefits, have been slower to embrace green investing compared to endowments and foundations. But, in 2021, a number of major pensions opted to act after concluding that climate change poses a major investment risk.

The nation's three largest pension funds shared in one of the biggest climate wins of the year, after they threw their weight behind activist hedge fund Engine No.1's successful campaign to shake up Exxon's board.

The $312.2 billion California State Teachers' Retirement System was the first institutional investor to back the push, followed by the $254.8 billion New York State Common Retirement Fund and the $495.6 billion California Public Employees' Retirement System.

The campaign was "one of the most important events of 2021 with respect to asset owner pressure in the U.S.," said Jackie Cook, director of sustainability stewardship research for Morningstar. "The success of that campaign depended to a large extent on the support of those large pensions."

The divestment movement also picked up steam last year.

In January, three New York City pensions committed to ditching roughly $4 billion in fossil fuel securities, a move touted as one of the largest fossil fuel divestments in the world.

The $87.3 billion New York City Employees' Retirement System, known as Nycers, and the $8.9 billion New York City Board of Education Retirement System, or BERS, have completed their divestments of approximately $1.8 billion and $100 million in securities respectively, former New York City Comptroller Scott M. Stringer and trustees said in late December. The $102.5 billion New York City Teachers' Retirement System, known as TRS, has dropped over $1 billion in securities to date and will divest from roughly $1 billion more by the first quarter of 2022.

Nycers and TRS further cemented their climate credentials in October by committing to achieve net-zero greenhouse gas emissions in their investment portfolios by 2040.

New York City's divestment was described as a "watershed moment" by Eric Becker, a partner and portfolio manager at Clean Yield, when interviewed by FundFire in June.

“It will be much easier for smaller pension funds to follow suit, as fiduciaries can point to New York’s action as well as the accumulating research showing that it is consistent with fiduciary duty to do so. I expect that the momentum for pension fund divestment will accelerate in the coming years,” he said.

In June, legislators in Maine became the first U.S. lawmakers to require a state pension to divest from fossil fuels. The $18.1 billion Maine Public Employees Retirement System has until Jan. 1, 2026, to drop its fossil fuel holdings.

Baltimore’s three pensions have a five-year deadline, starting in January, to divest from fossil fuels under legislation signed in October, as reported.

Lawmakers in other cities and states are also encouraging their pensions to divest. Three Democratic legislators in Oregon, for example, are urging the state treasurer to strip nearly $2 billion in fossil fuel holdings from the state’s pension fund portfolio, as reported.

But some policymakers are steering their pensions in the other direction.

Texas has moved to direct all state investment funds, including the $196.7 billion Teacher Retirement System of Texas and the $41.7 billion Texas Permanent School Fund, to divest from companies that shun fossil fuel investments.

A new law, which went into effect Sept. 1, prohibits state governmental entities from directly or indirectly holding the securities of a publicly-traded financial services, banking or investment company that “boycotts” energy companies.

In the final week of last year, the $148.1 billion New York State Teachers’ Retirement System announced its plans to divest from $66.3 million of thermal coal stocks and freeze future investments in its top twenty oil, gas and coal company holdings, worth roughly $1 billion, as reported.

The pension will prioritize engaging with these top-20 companies on their climate transition plans and revise its stock proxy voting policies to “more clearly articulate the System’s use of proxy voting to affect climate-friendly change among its portfolio holdings,” according to a release.

Looking to 2022, “engagement and active ownership are very powerful investment strategies, perhaps this is where the largest investors are going to be putting a lot of their emphasis,” said Cook. “But engagement and active ownership for a smaller pension could be engaging with an asset manager, rather than continuing to be invested in fossil fuels.”

“The commitment is to show that you're having a real-world impact,” she said.

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