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Investing with climate change in mind

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As a member of the three Vermont retirement system boards representing some $2.4 billion in pension funds, I am deeply committed to encouraging the companies we invest in to tackle the issue of climate change and to reduce the impact of such change on their bottom lines. Climate change threatens both the financial returns of these companies and the performance of the Vermont and U.S. economies as a whole. Disclosing those financial risks today is a key aspect of good corporate governance, as it allows investors and owners to understand the risks, and holds management accountable for minimizing their impact.

A lack of disclosure and action by companies today will only increase the costs to address the issue down the line. That is why the Investor Network on Climate Risk (INCR), a group of major U.S. pension and investment funds with over $2.7 trillion in assets and of which I am a founding member, has filed shareholder resolutions this year with dozens of the nation's largest U.S. companies asking them to assess the impact of climate change and new and proposed greenhouse gas regulations on their financial performance.

To boost Wall Street's focus on this issue, the Investor Network on Climate Risk, in partnership with the United Nations, is hosting a second Institutional Investor Summit on Climate Risk at the United Nations in New York this week. This summit provides a high-level forum for leading institutional investors to discuss risks and opportunities and to develop necessary responses. Participation by over a dozen state treasurers and comptrollers, including me, illustrates the broad concern among investors about the financial impacts of climate change.

When the Kyoto Protocol took effect in mid-February 2005, dozens of industrialized countries around the world took a historic first step to tackle global climate change. The European Union introduced quotas and trading on greenhouse gas emissions in January, and other countries that ratified the protocol, including Canada, Japan and Russia, are now following that lead.

While the United States government declined to ratify Kyoto, global companies based in the United States have no choice but to join the carbon-reducing movement. Whether it's GM cars in Canada or Alcoa aluminum in Europe, the carbon footprint from making and using their products is becoming an increasingly important factor for U.S. businesses competing overseas. Companies that fail to manage this carbon exposure in the coming years face enormous financial risks.

However, the new restraints also open up opportunities for developing and utilizing new clean energy technologies — markets that companies like General Electric are already seizing on for new revenues. GE is establishing itself as a world leader in wind-generated electricity — a market the company expects will triple in size worldwide over the next three years and which will generate about $2 billion in revenues for GE this year alone. GE is also investing aggressively in higher efficiency/lower emission technologies that can be incorporated in locomotives, aircraft engines, gas turbines, and other product lines.

Last year, shareholder resolutions resulted in dramatic progress. American Electric Power and Cinergy, two of the nation's largest carbon emitters, both assessed and disclosed aspects of their financial risks and exposure related to climate change and regulatory uncertainty. Also in response to shareholders, ChevronTexaco agreed to disclose its entire greenhouse gas footprint, while Valero Energy, one of the nation's biggest oil refiners, agreed to reduce its greenhouse emissions by 5 percent by 2008.

This year, investors are turning their attention to firms that have been slower to respond — ExxonMobil, Dominion Resources, and General Motors, to name a few. These companies need to tell investors, and their current shareholders in particular, just what climate change and carbon controls will mean to their bottom lines and explain what they are doing to mitigate potential costs and losses.

Understanding the risks is important, but so is action to reduce one's contribution to climate change. That is why I support efforts by a number of companies such as Staples, Consolidated Edison, General Electric, J.P. Morgan Chase & Co., and other proactive companies that are taking clear steps to reduce their energy usage and their emissions of greenhouse gases.

It is also why the trustees of the Vermont State Employees' Retirement System and Vermont State Teachers' Retirement System have agreed to consider a small investment allocation to a money manager investing in companies employing sound environmental strategies. The objective would be to reduce risk to the state's portfolios and to capture market opportunities. Any manager selected will be expected to meet the same standards and performance benchmarks as all other managers in the same asset class.

If we fail to seize this moment, the economic consequences could be severe. U.S. companies will become less competitive and lose market share; foreign competitors will seize control of fast-growing markets for solar, hybrids, and other clean energy technologies; and U.S. employment and growth will both suffer. As a result, investors will bear the burden just as they did a few years ago when corporate negligence and board inaction led to the Enron-era accounting debacles that cost American shareholders billions of dollars.

The message is clear. In the absence of leadership at the national level, it falls to state leaders, business leaders, and financial fiduciaries to push for change and accountability. Action on climate risk is needed today if financial and environmental consequences are to be avoided tomorrow.

Jeb Spaulding is the Vermont state treasurer. INCR is coordinated by Ceres, a national investor coalition based in Boston.