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Investing in a Changing Climate

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Driven by an abiding interest in the long-term financial stability and growth of the companies in which we invest, Connecticut's $21 billion pension fund has been working collaboratively with industry leaders on issues of corporate governance reform and disclosure. Among them, we are urging a fuller assessment of the financial implications of climate change.

Scientists have come to widespread agreement that climate change will dramatically affect natural resources and lead to extreme weather conditions—both of which have ramifications not only for us as individuals, but for our businesses, our investments, and our economy.

Many nations are acting now to reduce carbon emissions—the root cause of global warming—with new laws that impact how businesses in various industries can operate. While our federal government is not a signatory of the Kyoto Accords, approved by 150 nations, numerous state governments, including my home state of Connecticut, have been less reluctant to advance public policies that have already begun to affect businesses.

On the investment front, the Connecticut Retirement Plans and Trust Funds (CRPTF) and an expanding array of leading institutional investors are seeking corporate assessments and disclosure of the impact of these new and proposed regulations, and a changing business climate, on long-term financial performance.

Our actions are consistent with our fiduciary responsibility to exercise shareholder rights in the best interest of the more than 160,000 beneficiaries whose pension funds are entrusted to our care—individuals who depend on these assets for their future financial security.

Just as we consider traditional risk factors, such as a company's financial performance, earnings, profits, and history of returns, our due diligence also includes consideration of corporate governance practices and business planning to deal with new and advancing risks and business opportunities—to the extent that companies provide investors with that information.

For many of our portfolio companies, the consequences of climate change, if not properly managed, could adversely affect their bottom line and therefore the long-term performance of our investments. For example, companies could face the prospect of losing their competitive edge, incurring litigation costs, making capital investments that lose value due to new government policies, absorbing the impact of new physical risks and higher energy costs, and dealing with additional unforeseen capital expenses.

All of these factors—and others—can erode shareholder value and place today's seemingly solid investment in jeopardy for the hundreds of thousands of Americans who rely on those investments. Additionally, individuals holding a mutual fund or stock in any business that suffers financially as a result of inadequate preparation for the changing regulatory and competitive business realities—let alone the physical impact of a weather-related event—can be hurt.

Therefore, we have posited that companies that do not conduct essential due diligence put us all at risk, not only from the environmental effects of global warming, but from the economic shockwaves as well.

It is therefore imperative for companies to provide shareholders with clear and accurate information about their current and future economic health and well-being, and how they would respond to new government regulations and other factors associated with climate risk. This would permit investors to better understand the risks and hold company managementaccountablefor responding, as well as provide insight into the degree to which management is poised to take advantage of the business opportunities offered by new, so-called “clean technologies.”

The CRPTF was the first public pension fund to file a climate risk resolution at American Electric Power (AEP) in 2001. That effort led to AEP’s first-in-the-industry report to investors on climate risk, a step followed first by others in the industry, and then by leading firms in other key industries. Unquestionably, companies are beginning to recognize that climate change can have far-reaching effects on their business.

Beyond that, my administration helped inauguratethe Investor Network on Climate Risk (INCR) in 2003, bringing together major U.S. pension and investment funds with more than a trillion dollars in assets. That effort has grown significantly, with scores of Wall Street’s leaders and the nation’s top institutional shareholders gathering for the second time in 18 months earlier this year at the United Nations, with an increasing number of participants agreeing to a plan which includes a commitment to invest $1 billion in clean technology.

That commitment underscores a central point in this effort: Where there is risk, there is also opportunity. As investors, we need to take notice of an emerging market sector, such as the development of clean technologies and energy-efficient real estate. More of our businesses should take advantage of opportunities to develop new products, processes and technologies, much as GE has done. This is a growing space on the investment horizon that shows great economic promise.

As a nation, if we fail to seize this moment the economic consequences could be severe. U.S. companies could become less competitive and lose market share; foreign competitors could take control of fast-growing markets for clean energy technologies; and employment and growth could easily suffer.

I prefer to believe that as a nation, we will choose a different path. I remain optimistic that broader business preparation for the economic ramifications of climate change will persist as the common interest of institutional investors and corporate decision-makers continues to gain clarity.

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