How Some Long-Term Investors are Fighting for Sustainability

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Last week, Ceres and its Investor Network on Climate Risk released an illuminating analysis of how some major companies are responding to shareholder engagement on environmental, social and governance (ESG) issues.

The report, which covers the 2014 and 2015 proxy seasons, makes clear that long-term investors are putting increasing pressure on public companies to undertake ESG initiatives. Moreover, while most company responses are incremental and tailored to placate pesky activist shareholders — and others fall short entirely — these investors have won some significant sustainability victories.

About Ceres and its approach

Ceres, which created the Global Reporting Initiative (now the leading sustainability reporting standard) in 1997, is a veteran of the sustainability space, and its Investor Network on Climate Risk consists of over 115 institutional investors with collective assets of more than $13 trillion.

Last week's report examines the efforts and outcomes of many of these long-term investors (mostly socially conscious funds like Domini, Walden and Arjuna Capital, but also major pension funds like the New York State Common Retirement Fund and the California State Teachers Retirement System) to impact companies' ESG behavior.

Ceres works with these investors to engage corporate management and boards through targeted shareholder resolutions, many of which are withdrawn before a vote because the company agrees to address the issue(s) raised in the resolution.

As Ceres points out, use of this tactic to advance a sustainability agenda has increased dramatically in the last decade-and-a-half. To illustrate, Ceres tracked fewer than 10 shareholder resolutions related to climate change in 2001; by 2015, Ceres counted 167 such resolutions. That period also saw the rise of impact investing and the launch of the divestment movement, as investors continue to devise creative ways to leverage the power of the dollar for good.

Overall results

In order to track the effectiveness of shareholder engagement, Ceres asked investors who had submitted ESG-related shareholder resolutions or engaged in dialogues with corporate leadership, to provide an assessment of the "completeness" with which companies had fulfilled their commitments.

Investors were asked to rank responses on a scale ranging from 1 through 5, with 1 being, "The company met its stated commitment and took further action," and 5 being, "The company did not meet its stated commitment." In some cases, the deadlines for action have not yet arrived, so a response could not be measured.

In total, the report covers 91 total company commitments relating to sustainability reporting, greenhouse gas (GHG) emission reductions, sustainable agriculture/deforestation, fossil fuel risks and on other topics, including lobbying. Of these 91 responses, nearly three-quarters (73 percent) fully met their stated commitments (a 2 on the scale), and a total of 86 percent at least "mostly" met their commitments (a 3 on the scale).

Positive impacts in agriculture

Given that most companies met their commitments to investors, how significant were the actions that shareholder resolutions generated?

Based on the data compiled by Ceres, company commitments related to sustainable agriculture and deforestation seem to have the highest potential for environmental and social impact. This is particularly true regarding company commitments to responsibly source palm oil, a number of which were extracted as a direct result of shareholder pressure.

Take the case of Archer Daniels Midland (ADM). Based in Chicago, ADM's more than 33,000 employees operate on six continents and in more than 140 countries. In 2014, ADM's net sales amounted to $81.2 billion. It ranks 34th on the Fortune 500 list. What ADM does or does not do, in other words, can make a real difference to the environment and the communities in which it and its suppliers operate.

When companies clear forests and peatlands in order to harvest palm oil and other food commodities, startling amounts of GHGs are emitted. In fact, according to the EPA, corporate changes to land for food production purposes account for approximately 17 percent of annual global GHG emissions, or what the entire transportation sector emits each year. Deforestation also leads to a slew of other environmental and social problems, including erosion, biodiversity loss and conflicts over land rights.

In light of this potential damage and ADM's position as a primary soy and palm oil purchaser, in 2015, Green Century Capital Management and the New York State Common Retirement Fund introduced a resolution asking ADM to implement a policy requiring that all soy and palm oil sourced by ADM come from areas not associated with "clearing of high conservation value (HCV), high carbon stock (HCS), or peatland areas, or exploitation of workers and local communities."

Following the introduction of that resolution, ADM worked with investors to develop a No-Deforestation Policy. ADM instructed its suppliers to cease engaging in deforestation and peatland clearance, while it partnered with The Forest Trust to map its supply chains and develop action plans. In furtherance of its policy, ADM is working with the government of Brazil and hundreds of small farmers to develop a sustainable palm venture in Parà, Brazil. When its No-Deforestation Policy was unveiled, ADM became the first major supplier of agricultural commodities to implement a no-deforestation policy for both soy and palm oil production.

To be sure, ADM was not the first major player to commit to ending palm oil production-related deforestation. In the second half of 2014, Cargill, Kellogg, Unilever, Nestle, General Mills, Danone and other major food suppliers committed to satisfying the United Nations' New York Declaration on Forests pledge to "cut natural forest loss in half by 2020, and strive to end it by 2030."

With ADM, investors built on this momentum and secured the most significant no-deforestation pledge from a major food company to-date. In total, investor pressure has persuaded "top palm oil suppliers representing approximately 96 percent of globally-traded palm oil" to adopt no-deforestation policies for the palm oil they trade.

Disappointments

Not all investor efforts were as successful and, unsurprisingly, fossil fuel companies appeared the most intransigent. Of the 15 investor proposals included in the Ceres report, only six fossil fuel companies fully met their commitments and two "only partially" complied.

The most disappointing actor profiled here was ExxonMobil (Exxon). Investors have been urging extractive companies like Exxon to move away from further investments in carbon-heavy reserves because, apart from the climate impacts of these activities, the reserves may end up abandoned if demand for fossil fuels continues to ebb. Exxon does not agree.

In 2014, Arjuna Capital and As You Sow introduced a resolution calling for Exxon to, among other things, explain "how it stress-tests capital investment opportunities and risk in a scenario where global temperature rise is limited to 2 degrees Celsius." The investors withdrew that resolution when Exxon agreed to publish a report on the issue.

In the report, however, Exxon asserted that there was "limited basis for concern" of such a scenario ever arising, because "any future capping of carbon-based fuels to the levels of a 'low carbon scenario' is highly unlikely due to pressing social needs for energy." As Arjuna and As You Sow explain, the 2-degree scenario means that "some fossil fuel companies will not be able to sell some or all of their reserves, thereby stranding those assets and causing the value of the company to decline." Yet, Exxon ignored the question entirely, suggesting that one of the largest global oil companies does not take seriously the prospect of a future with significantly lower fossil fuel usage.

The Ceres report features other shortfalls, of course, but it mostly suggests a promising future in shareholder activism to advance sustainability goals. The potential is there for influential investors to continue to hold corporate feet to the fire on these issues; it will be interesting to see what happens next.

http://www.triplepundit.com/2015/10/long-term-investors-fighting-sustainability/