Fossil Fuels Divestment

Dear Friends,

Over the past year, many colleges and universities have investigated divestment of endowment from firms that have investments in fossil fuels as a way of applying financial leverage against the use of carbon-based energy while promoting alternative sources.

Here at Haverford, the dialogue was initiated in the summer of 2012 by a number of thoughtful students who, consistent with a national campaign, specifically asked the College to freeze all endowment investments in 200 companies identified as having the greatest proven reserves of coal, oil, and natural gas and to unwind all existing investments in these companies over a five-year period. The matter was referred to our Board's Committee on Investments and Social Responsibility (CISR), which includes Investment Committee representation, in order to explore what such a move could mean for Haverford.

The students who initiated this conversation expressed profound concern about the effects of climate change arising from the burning of fossil fuels, and they have challenged the College to engage thoughtfully on how we as an institution and as a community can act within our sphere to mitigate this global threat. As an institution committed to values of ethical concern and social responsibility, the College commends these students for initiating this important conversation. The dialogue has been serious, positive, and informed by the understanding that we must balance needs with ambitions.

The CISR's deliberations on this matter included meetings with the concerned students as well as an open forum with the broader College community, and were supported by research conducted by the College's investment office. Based on the CISR's recommendation, and for the reasons discussed below, the College's governing Board of Managers has by consensus decided not to pursue divestment; however, the College will continue to engage with seriousness the larger question of how we as an institution and as a community can become more environmentally sustainable, and how we can contribute to a reduction or mitigation of human-induced climate change.

Background. As an institution of higher learning and a "perpetual institution," we seek to educate the world's best students not just for today or for the foreseeable future, but forever. The strength of the College's endowment is critical to this vision. Unlike the typical "savings account," which functions as a reserve for some future need, the endowment is expected both to grow and fund current operations. In our case, the College relies on endowment to cover approximately 27% of the annual budget. If endowment growth does not keep pace with the expense of running a world-class educational institution, the difference must be offset by expense reduction and/or revenue from other sources (e.g. tuition increases).

Decisions involving endowment management can have repercussions for decades, with consequences magnified by the effect of compounding. That's why changes of the magnitude contemplated by fossil fuel divestment – which involve not just a specific instrument or even asset class, but are defined by business activity – must not be taken lightly.

Investigation. Haverford's current practice is not to invest endowment assets in the stocks of individual companies, so the College currently has no direct investments in any of the 200 companies that are the subject of the divestment request. (The only exception is a small portfolio managed by the CISR specifically to permit the College to engage in shareholder activism with respect to selected companies.) The College does, however, invest a substantial portion of the endowment in co-mingled mutual funds managed by third-party investment managers. These co-mingled funds may include investments in fossil fuel companies. The terms of these investments with third-party managers do not allow the college to screen for individual stocks. The key objectives of this strategy are to minimize the costs of managing the endowment, while allowing the College to gain diversified exposure to key economic sectors. We believe that this strategy works well for the College.

In this context, the request to divest from fossil fuel companies can be seen as comprising two requests: first, a request to substantially alter the investment philosophy and structure of the endowment portfolio to enable the College to screen for individual companies; and second, a request to apply a screen to eliminate investments in any of the 200 named fossil fuel companies.

The College's investment office performed an analysis to estimate the costs associated with divestment, and concluded that the costs would be significant. First, replacing the college's co-mingled fund investments with investments that allow for the selection and screening of individual stocks would result in a significant increase in the annual cost of managing the endowment. Second, the College believes that a portfolio that excludes a major asset class will under-perform a more fully diversified portfolio, and in some scenarios, this under-performance could be very significant, with implications for the College's operations and its ability to carry out its educational mission.

Because our research indicates that divestment should be regarded as a cost (rather than a revenue-enhancing change), it should be weighed relative to the value of myriad other expenses such as financial aid, need-blind admission, preservation of campus assets, faculty and staff compensation, academic resources – indeed, any of the (nearly) countless other expenses the College incurs each year.

Such expenses are managed via our budgeting process, which involves more than the mathematical balancing of line items on a spreadsheet. Rather, decisions about expense allocation derive from mission. And when viewed in such a light, relative to other costs, we don't believe that divestment will enhance our educational mission or provide the means of support for other expenses that, in our view, *do* support that mission. In fact, because it would likely depress endowment value going forward, divestment is not merely of a lower priority; it would undermine our ability to achieve our core goal of educating the world's best students so that they may lead lives of purpose in whatever communities they serve. In our view, then, the cost of divestment would be better put toward enhancing our students' ability to engage with the underlying issues that have given rise to a desire for divestment in the first place.

Nor do we believe that divestment would produce any benefit to the broader society that is commensurate with its cost to the College. Fundamentally, we are not persuaded that the availability of investment capital from college endowments – let alone Haverford College's endowment – is likely to put any constraint on the ability of the targeted companies and their consumers to exploit their fossil fuel resources. Taken together, the endowments of the nation's colleges and universities represent a small fraction of the capital that is available to fossil fuel companies.

Clearly, then, any impact of a decision to divest would be symbolic in nature. And while recognizing the power of symbolic actions to propel social justice movements, we believe that the symbolic power of the action here in question is undermined by a number of considerations.

- The divestment campaign does not distinguish between the dirtiest coal company and the cleanest natural gas company – it paints all with the same broad brush. Yet, natural gas produces roughly half the carbon dioxide per unit of energy as coal. (It was recently reported that US carbon dioxide emissions have fallen dramatically to levels last seen in 1995, due in large part to the recent shift from coal to natural gas.)
- The divestment campaign focuses exclusively on fossil fuel companies to the exclusion of other carbon-producing activities such as the automobile industry, the airline industry, and farming.

Methane, for example, is a worse greenhouse gas than carbon dioxide, and animal husbandry accounts for a huge amount of the country's methane emissions.

- The campaign focuses on 200 companies identified as having the largest proven reserves of fossil fuel resources, but does not address investments in other companies with marginally smaller fossil fuel reserves, or in companies with closely related activities, such as drilling and exploration services. When the College investigated a claim that a portfolio can be "optimized" to exclude the 200 named companies while closely tracking the performance of a broad index fund, we learned that this was accomplished by replacing the excluded fossil fuel companies with other, smaller fossil fuel companies and associated service companies. We question the symbolic power of a strategy that would merely replace certain fossil fuel companies with other players in the same or related industry.

In sum, we do not believe that the requested divestment action is an appropriate strategy for the College to adopt in addressing the problem of climate change. Fortunately, there is much that we can do, as an institution and as a community, to make a meaningful contribution:

- The endowment has almost 3% of assets specifically invested in alternative and renewable energy investments–a good example of applying financial resources in the service of a worthy principle in which we expect to earn significant investment returns and that also serves our educational mission.
- The College buys 100% of its electricity from renewable sources.
- The campus Committee on Environmental Responsibility is managing our transition to practices leading to carbon neutrality. In addition to sponsoring a 'green purchasing' policy for campus operations, CER has partnered with specific departments in order to promote sustainable practices, ranging from local sourcing in the Dining Center and composting food waste, to energy conservation strategies. You can read its Climate Action Plan on our website; highlights include:
    - Electric sub-metering all major dorms, Dining Center and Magill Library. Submeters assess energy use and performance of individual buildings, creating opportunities for energy and capital expenditure savings while allowing us to better pinpoint problem areas.
    - Building light sensors. The stairwells in the KINSC, for example, are filled with natural light, so lights are not needed during the day. Light sensors shut the lights off when not needed and turn them on when they are; we are installing motion sensors campus-wide.
    - Building automation systems. Automated control scenarios minimize electrical consumption across the campus, enabling the College to earn money by shedding electrical load when the potential curtailment earnings are at their peak.
    - GIAC Retro-commissioning. Over time, green buildings may not work as efficiently as designed. Retro-commissioning involves testing to see if they are functioning properly. Some issues may be as simple as an adjustment, while other issues may be more complicated. The more efficient the building, the less wasted energy – and the more money we save.
- As mentioned, the CISR maintains a small portfolio of stocks selected to enable the community and students to participate in shareholder activism with respect to companies that present particular social and environmental concerns. We believe that with student participation, this strategy could be deployed more effectively to confront companies with the environmental effects of their activities.

Conclusion. The College needs to balance ambitions with resources, in concordance with our mission and long-term goals. Fossil fuel divestment as currently envisioned is not the right step for Haverford at this time. But this does not signal disinterest in environmental considerations; on the contrary, Haverford's role as energy user and steward of environmental resources should remain fundamental to decision-making about virtually all aspects of community life.

For this reason, the Board of Managers has asked for a comprehensive review of strategies and tactics in our quest for sustainability, for presentation at February's meeting of the Board: What steps are we taking? Why? To what effect? What improvements can we make? We look forward to working with students, faculty and staff over the coming months in providing such an assessment.

Ultimately, when it comes to the broad question of Haverford's role in safeguarding our natural resources, community members on both sides of the divestment question likely have far more in common than they have disagreement. We look forward to continued productive partnership in navigating the best path forward for Haverford.

Sincerely,

Daniel Weiss
President
November 5, 2013