9 Steps to Revitalize America's Manufacturing Communities

Action 8: Invest Responsibly

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Rationale

Many cities and states are tapping a growing source of capital right in their backyards: workers' capital, which represents an enormous share of economic and capital market wealth. In 2017, global pension assets in major markets rose to over $41 trillion, according to Willis Towers Watson.[1] U.S. defined pension funds alone stand at over $10 trillion, and worker trustees can be represented on public and multi-employer pension boards with assets of around $4 trillion. That's a lot of capital.

The pension funds of hard-working Americans across the country—such as public employees, teachers, construction workers, and steelworkers—are collectively bargained, deferred wages that are owed to them. They were won only after decades of fighting to ensure retirement security once their working lives had ended. These social gains were a result of the movement of labor and social reformers who sought to balance the power of the "marketplace" with the American dream, paving the way for a prosperous and stable middle class, decent working conditions, and environmentally clean and safe communities. This capital, part of a larger pool of institutional investments owned by working people (and including mutual funds and 401(k)s, insurance funds, endowments, and bank deposits), has been instrumental in the development of the U.S. economy and its capital markets, and those of our global neighbors, fueling growth and prosperity.

While pension funds must provide a good rate of return, these trusts have long-term horizons and growing financial incentives, fiduciary duties, and legal directives to invest responsibly. The 2015 U.S. Department of Labor pension guidance on legality of economically targeted investments (ETIs) recommitted to investments that produce "collateral benefits," targeting investments in business, affordable housing, sustainable energy, and similar concerns that yield good jobs and benefit residents.[2] ETIs are investments that provide risk-adjusted market rates of return, while providing additional benefits to a targeted geographic target area.

Joining many other countries, the United States also encouraged investors to consider environmental, social,

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and governance (ESG) matters in their investments. In the United States and globally, state and national pension funds, banks, and corporations have signed on to the United Nations Principles of Responsible Investment (PRI), which now has around 2,000 signatories representing about $80 trillion in assets.

Key Actions

While states should explore a variety of capital strategies, their most powerful option is to establish a responsible pension investment policy with an economically targeted, in-state component. A responsible investment policy can be applied to other state assets, such as the treasury, and to other sources of the people's money.

- State and city pension funds, and other institutions, should adopt the United Nations PRI, or similar ethical and sustainable investment policies. With this policy enacted, pension managers can apply ESG criteria across all asset classes. For corporate equities investments, that means that the funds can monitor firms on their workforce relations and environmental practices. In fixed income investments, managers can invest in affordable housing and "green bonds."

- State and city pension funds should enact alternative and fixed income investment policy measures to comply with the DOL 2015-1 guidance on economically targeted investments. These investments can include direct, indirect, and pooled investment for advanced manufacturing, efficient transportation, affordable housing, commercial and green construction, infrastructure, and renewable energy.

- Historically, critics have done their best to downplay responsible investments by falsely alleging that they yield concessionary returns. Evidence does not bear this conclusion out: a battery of responsible investment performance meta-studies by institutions like the University of Oxford, Harvard Business School, and Mercer Consulting demonstrate that investors who pay attention to ESG and good corporate governance produce comparable returns and sometimes financial outperformance.

Issues to Remember

- Public and multi-employer pension funds are generally required to include employee/labor representatives on their boards of trustees. In addition to ensuring that pensions are well funded and deliver a solid return, union trustees should use their power to ensure pensions are investing in the interests of beneficiaries and the well-being of the communities where they live. They should champion a long-term, responsible, and activist approach to the management of workers' assets.

- Pension fund fiduciaries can consider ESG factors in their investment decisions. The DOL 2015-1 guidance allows pension funds to take ESG benefits into account as "tiebreakers" when investments are otherwise equal. These criteria can include good human capital and fair labor practices, diversity in corporate boardrooms, and good community neighbor and sustainable environmental practices. Many of these practices—and the avoidance of ESG risk—lead to better long-term productivity.

- ETI and ESG criteria can include job quality and community development. Social criteria in ETI and ESG can include economic development of depressed areas and delivery of high quality jobs. State pension funds should beef up social criteria alongside the implementation of more well-known environmental and corporate governance rules.

Recent Progress

- CalPERS, the California Public Employees Retirement System, has been a leader in responsible and economically targeted investments.[3] In 2001, following extensive due diligence and board approval, CalPERS established the California Initiative, a $1 billion ETI. The California Initiative has invested in hundreds of firms across a variety of sectors, including the industrial, energy, and information technology sectors. More recent investments have focused on infrastructure.

- Since the 1960s, the State of Wisconsin Investment Board has operated the Wisconsin Private Debt Program, which offers senior and subordinated debt financing to companies with operations in the state.[4] In an effort to avoid competing with banks, the program focuses on longer-term, fixed-rate loans to smaller-sized businesses. The board also offers a private equity program focused on Wisconsin-based businesses.

- The New York City Employees' Retirement System (NYCRS) allocates 2 percent of pension assets towards ETIs.[5] The ETI program is designed to address market inefficiencies by providing capital or liquidity to underserved communities and populations citywide. The ETI program's investments have historically been targeted towards affordable or workforce housing for low-, moderate-, and middle-income neighborhoods and populations in the five boroughs, and has invested over $2 billion in neighborhoods since the 1980s.[6]

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Notes

1 "Global pension assets study 2018," Thinking Ahead Institute, Willis Towers Watson, February, 2018, avalable at https://www.willistowerswatson.com/-/media/WTW/Images/Press/2018/01/Global-Pension-Asset-Study-2018-Japan.pdf.
2 "Interpretive Bulletin Relating to the Fiduciary Standard under ERISA in Considering Economically Targeted Investments," U.S. Department of Labor, Federal Register, volume 80, number 206, October 26, 2015, 65,135.
3 "California Investments," California Public Employees Retirement System, updated January 3, 2018, https://www.calpers.ca.gov/page/investments/investment-manager-engagement-programs/california-investments.
4 "Wisconsin Private Debt," State of Wisconsin Investment Board, November 3, 2015, https://www.swib.state.wi.us/single-post/2015/11/03/WISCONSIN-PRIVATE-DEBT.
5 "Economically Targeted Investments," New York City Employees' Retirement System, Office of the New York City Comptroller, accessed April 1, 2019, https://comptroller.nyc.gov/services/financial-matters/pension/initiatives/economically-

targeted-investments/.

6 For more, See John Griffith, Tom Woelfel and Keith Fairey, “Unleashing the Power of Pensions: Expanding Economically Targeted Investments,” Enterprise Community Partners and InSight at Pacific Community Ventures, December, 2015, https://www.pacificcommunityventures.org/2015/12/11/ai3-brief-unleashing-power-pensions/.