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The Fiduciary Focus

Investment News From a Pro-Shareholder Perspective

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This Week: Tennessee sues BlackRock over ESG investing; CCP crackdown erases billions from Chinese gaming companies; an Eye on Energy analyzes new EU methane emissions restrictions.

Tennessee Sues BlackRock Over ESG Investing

Tennessee has sued BlackRock for allegedly misleading investors over its ESG investment strategies, the Financial Times reported late last month.

The 73-page complaint alleges that BlackRock violated Tennessee's consumer protection laws by repeatedly promising investors that it was investing their money to maximize financial value alone, while BlackRock was in fact using those investments to push companies to adopt environmental and climate goals instead.

The complaint details BlackRock's involvement in groups like Climate Action 100+ and Net Zero Asset Managers, through which BlackRock has committed to using all of its assets under management—not just those in its ESG funds—to push climate goals. The suit claims that BlackRock has fulfilled these commitments by pushing U.S. energy companies like Exxon and Chevron to cut emissions and pressuring other companies from Walmart to Berkshire Hathaway to United Airlines to pursue net zero goals. And critically, BlackRock engaged in this activism despite promising investors in its standard, non-ESG funds that BlackRock "does not seek to follow a sustainable, impact, or ESG investment strategy."

But financially-focused investors were not the only ones who may have been misled. The complaint also alleges that BlackRock deceived investors in its ESG funds by claiming that ESG investing maximizes long-term financial returns, which Plaintiff alleges BlackRock knew was not true. The complaint cites admissions from BlackRock personnel as well as academic studies on how ESG investing underperforms. One cited study, for example, concluded that companies with the highest sustainability scores tended to underperform those with the lowest scores by 2.16% to 5.76% annually.

The first-of-its-kind suit is the latest in Tennessee's efforts to protect its citizens from conflicted, ESG-aligned financial services providers. In September, Tennessee Attorney General Jonathan Skrmetti launched an inquiry into the Big Four accounting firms over their ESG-related conflicts of interest and potential antitrust violations. He also signed onto a letter last Spring to 53 asset managers, warning them that pursuing ESG goals with client money likely breaches their fiduciary duties.

The complaint doesn't put a number on the damages the State seeks, but it could be huge: Tennessee asks the court to force BlackRock to return all of the "ill-gotten gains" it has earned through its deception, including all profits and provide compensation to Tennessee consumers. The suit also asks the court to force BlackRock to rectify its practices moving forward. BlackRock, of course, has denied the claims.

Tencent And NetEase Shares Plummet Following CCP Video Game Crackdown

Chinese gaming companies Tencent and NetEase saw shares plummet upon the CCP's announcement of new rules imposing strict limits on how much consumers are allowed to spend on gaming apps, Fortune reports.

The announcement stunned investors, who felt the video game industry was in the clear after Chinese regulators had backed off the industry in 2022 and most of 2023, following a wave of similarly hard-hitting screen time restrictions in 2021. At the time, state-owned media criticized smartphone gaming as "opium for the mind." The new rules will not only limit the amount players can spend in game, but will also prevent games from rewarding players for logging in each day or live streaming.

Following the announcement, shares in the NASDAQ-listed companies dropped dramatically. Shares in Tencent—China's largest publicly traded company—fell %12, wiping out over $40 billion in value. NetEase shares dropped 25%.

The announcement should serve as an important reminder not only to investors, but to U.S. companies that do business there: The CCP wields total control over the private sector, rendering any investments in the region subject to its whims.

Even More Companies Tie Executive Pay To ESG Goals, New Report Shows

A new report by the Conference Board finds that more companies are tying executive compensation to meeting climate and diversity goals than ever before, Fortune reports.

A full 54% of S&P 500 companies now tie their executives' pay to reaching climate goals, up from just 25% in 2021. The use of diversity metrics has now jumped to 75% of pay plans, up from 52% in 2021, even in the wake of the Supreme Court's *Students for Fair Admissions v. Harvard* decision and subsequent wave of discrimination suits filed against corporate America.

The continued use of ESG metrics in executive compensation plans should come as no surprise, as the practice has been pushed on companies by large asset managers including BlackRock and State Street. Both managers routinely vote in favor of ESG-aligned executive compensation policies across corporate America. And they lead by example. BlackRock holds back 25% of its executives' incentive awards if they do not meet certain "ESG and organizational achievements." State Street likewise touts that it "holds leadership accountable via pay decisions for our Diversity Goals," including doubling the percentage of Black and Hispanic individuals in leadership positions by 2024, and "leverag[ing] [State Street's] stewardship efforts" to "combat[] racism."

The Conference Board report concludes: "ESG backlash, which has been mounting since early 2022, has not dissuaded companies from continuing to integrate ESG-related performance metrics into the incentive plans for their CEOs and senior executives."

Straight From Strive

BlackRock Tries To Rewrite History

Oh BlackRock.

As the self-proclaimed king of stakeholder capitalism and the ESG movement has faced increasing criticism, an interesting dynamic has emerged, explains Strive CEO Matt Cole in his latest piece for Townhall.

Rather than own its pro-ESG stances or claim a change of heart, the nine-trillion-dollar asset manager has chosen a different path: Attempt to rewrite history by claiming it never adopted stakeholder capitalism at all. With, of course, a wink and a nod to its ESG-focused clients who *love* the fact that BlackRock uses all of its clients' investments—red state or blue state, in ESG funds or not—to push their shared social and climate goals.

The duel-position BlackRock is trying to take isn't just baffling, it's simply not true. Cole's new article dismantles BlackRock's arguments piece by piece, exposing how the company and CEO Larry Fink have misled both clients and the investing public.

As we enter 2024 and look forward to the year ahead, here's hoping Mr. Fink's New Year's Resolution was to focus on candor. Otherwise, more lawsuits and defections may be on the horizon.

Read the full article here

An Eye on Energy

European Union to Limit Methane Emissions from Gas Imports

In November, the European Union announced a new law to limit methane emissions associated with oil and natural gas imports. Methane is a major component of natural gas, some of which escapes into the atmosphere during the production process.

The EU has eyed methane reductions, particularly by the fossil fuel industry, as a key way to fight climate change. Methane is much more potent than carbon when it comes to global warming, and up to 24 percent of anthropogenic methane emissions are from oil and gas operations.

The specifics of the new policy are still uncertain. The most demanding part of the new law—the emissions limits—won't go into effect until 2030, and regulators have not yet determined what, exactly, those caps will be. Nor have they announced the penalties for noncompliance. Monitoring, reporting, and verification requirements will be imposed beginning in 2027, but, again, no specific penalties have yet been set.

The new law will likely pose operational and financial challenges for major natural gas exporters to the EU. There are ways to reduce methane emissions—by upgrading equipment, implementing leak detection and repair programs, replacing gas-fired engines with electric ones and purchasing pressurized storage tanks, among other things—but none of them are free. And the associated monitoring, certifying, and verifying isn't free either.

The impact on U.S. producers is particularly difficult to predict. The U.S. has numerous liquefied natural gas (LNG) operators and a diverse supply of gas sources. Some of those sources include associated gas, which is the natural gas produced from oil wells. The methane emissions from these sources are harder to mitigate, given that this source of natural gas requires venting and flaring to produce. U.S. operators must also comply with a matrix of existing U.S.-based state and federal regulations, which will complicate compliance efforts. U.S. producers also sell into many global markets, not just the EU.

That said, the EU is a major destination for U.S. LNG. In October 2023, 67.6 percent of U.S. LNG exports went to Europe, making it one of our most important energy trading partners. And the U.S. is expected to remain the primary replacement for Russian gas into the EU for the foreseeable future.

Accordingly, the EU must be careful that it does not discourage critical suppliers or raise the cost of its gas imports. No one can predict how tight the global gas market will be in 2027. But American LNG has proven its ability to save Europe from an energy crisis, and as more LNG export terminals come online in 2024, America will be well positioned to continue to serve the European market going forward (at least assuming the U.S. refrains from imposing costly regulations of its own). As Europeans continue to battle elevated electricity and gas prices this winter, the climate bureaucrats in Brussels would be wise to consider the real-world economic effects of their proposals as they work to quantify the limits and penalties they intend to impose.

The Best of the Rest

Additional stories about ESG investing, company happenings, and more.

- Sustainability officers across corporate America recite platitudes about fighting climate change after COP28 climate conference.
- DEI rollback hits colleges and universities; could corporate America be next?
- CCP sanctions U.S. data firm in retaliation for U.S. policy that China perceives as a "smear" campaign, including the Uyghur Forced Labor Prevention Act.
- Research on ESG investment preferences wins honorable mention for Moskowitz Prize at Northwestern University; shows investors who (mistakenly) believe ESG funds outperform financially more likely to allocate money to such funds.
- ESG funds face weak demand despite the fact that performance is bolstered by tech sector holdings.
- House expands antitrust probe to ISS and Glass Lewis; new subpoenas seek documents on efforts to push climate change agenda, as well as coordination with BlackRock and others.
- Netflix faces backlash for latest attempt to use children's programming to push controversial social and political messaging.
- Multinational energy company Iberdrola inks new ESG-tied credit line; rates will be adjusted upwards or downwards annually depending on whether the company sufficiently reduces emissions and increases gender diversity.
- Vanguard sued over website terms that silence users; plaintiffs allege terms and conditions prevent users from disparaging Vanguard in violation of California law.

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What Makes Strive Different?

While many asset managers push companies to focus on other stakeholders such as employees, suppliers, the environment and society at large, we live by a strict commitment to shareholder primacy — the belief that **the purpose of a for-profit corporation is to maximize long-run value for investors. Click here** to learn why shareholder primacy is so important.

How Does Strive Maximize Value?

Our corporate governance team engages with the companies in which our clients are invested to advocate for the pursuit of excellence in corporate America. We are aggressively apolitical when it comes to utilizing our corporate governance tools and demand that companies focus exclusively on delivering long-term financial value for investors. The corporate governance team also determines how to cast our shareholder votes at annual meetings and special elections, evaluating each proposal through the lens of maximizing financial return.

Our research team conducts deep analysis of macro economic trends, market developments, and industry- and company-specific metrics to identify potential risks and opportunities for our clients. We then incorporate the results of this research into our engagement and voting strategy, and share it with our clients in the form of white papers and market research reports so they can make the most educated investment decisions possible.

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