STRIVE

The Fiduciary Focus

Investment News From a Pro-Shareholder Perspective

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This Week: What Claudine Gay's resignation means for DEI in corporate America; "transition financing" makes a buzzy debut at COP28; An Eye on Energy goes nuclear.

What Claudine Gay's Resignation Means For DEI In Corporate America

Last week's resignation of Harvard President Claudine Gay sent shock waves across America as commentators sought to make sense of her downfall. Accusations of antisemitism and plagiarism were surely at the fore, but some commentators have stepped back to see the resignation as part of the broader, growing movement that is questioning diversity, equity, and inclusion efforts and rejecting the controversial narrative at its core.

Billionaire hedge fund manager and Harvard alum Bill Ackman is among them. Last week, he published a 4,000 word exposition explaining why he believed DEI initiatives allowed antisemitism to take root on Harvard's campus. In his view, DEI programs are "not about diversity in its purest form"—which he describes as diversity of viewpoints, politics, experience, background, and upbringing—but are a "political advocacy movement on behalf of certain groups that are deemed oppressed under DEI's own methodology." Accordingly, "a meritocracy is an anathema to the DEI movement" that is nearly always "illegal . . . in its implementation even if it purports to work on behalf of the so-called oppressed."

Corporate America is taking note. But the proposed cure may be worse than the disease. It's true that many companies are beginning to see the writing on the wall when it comes to their quota systems and DEI programs, particularly after the Supreme Court's affirmative action decision in *Harvard v. Students for Fair Admissions* in June. But rather than set race aside and focus on merit-based policies, many companies are deciding to simply hide their race-conscious policies a little better, judging by a Fortune report last week. DEI websites will become internal memos, memos will become phone calls, once-public DEI job postings will become secretive hires via recruiting agencies and outside consultants. But nothing, substantively, will change.

"It's a way to do the work a little bit more under the radar," one DEI strategist explained. Such a strategy should be deeply concerning to shareholders, not only because it reflects a continued commitment to discrimination, but because it's a tacit acknowledgment that companies know what they are doing is wrong.

DEI strategists may think they're being clever, but you don't need a Harvard degree to see what's really going on.

Climate Activists Shift To "Transition Financing" Strategy To Shut Down Fossil Fuel Companies From Within

"Rizz" may have been the Oxford Dictionary's word of the year for 2023, but "transition financing" will be the hot new phrase for 2024—at least if the ecoactivists that attended last month's UN Climate Change Conference (COP28) have anything to say about it.

The term refers to a strategy where environmentally-conscious investors invest not only in green companies—solar, wind, renewables, etc.—but in traditional fossil fuel companies as well. These investors then use their insider position as shareholders to slowly put the companies out of the fossil fuel business. Notably, the strategy took center stage at this year's conference, even making its way into the final agreement 200 nations signed committing to move away from fossil fuels, Bloomberg reported last week.

The move marks a strategic shift by climate activists to meet net zero by 2050 ambitions. To date, climate activists have chiefly focused on "green financing," which puts capital into sustainable activities such as solar farms and electric vehicles. Transition financing effectively does the opposite. Instead of moving capital away from fossil fuels and into renewables, transition financing intentionally moves capital *into* fossil fuel companies, with the goal of convincing them to cease their core operations.

The dangers are apparent. For environmentally-focused investors, greenwashing risks loom large, as funds slapped with a "sustainability" sticker are now free to invest in green companies, decidedly non-green companies, and everything in between—with little to no oversight or accountability.

For financially-minded investors, the risks are even more dire. Convincing companies to conduct an orderly wind down of operations is the type of financially-catastrophic bad news typically delivered by a bankruptcy judge, not by shareholders.

Even more worrisome is the fact that, particularly after COP28, the groups calling for this change have the financial clout to make it happen. The Glasgow Financial Alliance for Net Zero (GFANZ), for example, praised the strategy, explaining that its members support a "managed phase out" that would send such industries into early retirement. That would be one thing if GFANZ were made up of college protestors and fringe climate zealots. But it's not. GFANZ is made up of 500+ financial institutions, including behemoth asset managers like BlackRock and State Street, who commit to using their collective $57 trillion in assets under management (*i.e.*, client funds) to drive net zero policy. Understood properly, then, "transition financing" isn't just financing the green transition, it may mean transitioning many investors' savings and retirement accounts from the black to the red.

ISS and Glass Lewis Update 2024 Proxy Voting Policies

Proxy advisory firms ISS and Glass Lewis have updated their proxy voting policies for 2024. The changes are minimal and reflect the proxy advisory duopoly's refusal to retreat from its pro-ESG strategies.

ISS, for its part, made almost no changes at all. That's not good news, considering that it supported nearly two-thirds of all ESG shareholder proposals made by the nonprofit As You Sow, covering issues ranging from climate change to diversity to workers' rights.

Glass Lewis made a handful of changes, but most will only up the pressure on companies to adopt Glass Lewis's social policies. The advisor will now seek to oust board members at Russell 1000 companies that do not require board level oversight of environmental and social issues. It will also oust board members if large companies in targeted, high-polluting industries do not adopt TCFD-approved climate goals or if insufficiently diverse companies do not make timebound commitments to meet Glass Lewis's gender and racial quotas.

Both advisors have been targeted by lawmakers for their outsized role in influencing the outcome of corporate elections. But only time will tell whether these efforts yield fruit for corporate boards trying to stay out of the political fray or for the financially-minded investors who are hoping for the same.

U.S. Companies May Be Obscuring China-Reliant Supply Chains, Rather Than De-risking Them

U.S. companies may be obscuring their supply chains, rather than truly lessening their reliance on China, the Wall Street Journal reported Saturday.

As the risks of relying on China have become more apparent, companies from Apple to Mazda have made headlines for moving Chinese factories to neighboring Asian nations or Mexico. But a new report from the Wall Street Journal suggests that these moves may not be truly lessening companies' reliance on China. That's because these manufacturing plants are often assembling components that are still made in the world's largest communist nation, meaning companies are lengthening their supply chains without really changing them.

According to the Journal, these "superficial" rearrangements could make manufacturing more expensive without achieving greater supply chain resiliency. That's certainly true. But it will also make it more difficult for shareholders to assess a company's true exposure to China risk, underscoring the need for full transparency by American companies that do business in the region.

New Research Debunks Influential Article Claiming Sustainability Outperforms

Frequent readers of our newsletter know there have been several recent studies showing that ESG investing does not outperform financially. And that prior studies purporting to link diversity and financial performance have similarly come under scrutiny.

But new research highlighted by the Political Forum Institute last week casts serious doubt on what is perhaps *the* leading study claiming that sustainability and financial performance go hand in hand.

The study under scrutiny is the one led by Harvard professor Robert Eccles, which claimed to find that companies that voluntarily adopted environmental and social goals performed better financially than companies that didn't. The article has been cited thousands of times—more than any other piece from *Management Science* in the past decade—including by the Securities and Exchange Commission to justify favoring ESG-related investment policies.

The author, Professor Andrew King of Boston University's business school, presents his findings as follows:

> Do High Sustainability companies have better financial performance than their Low Sustainability counterparts? An extremely influential publication in Management Science, "The Impact of Corporate Sustainability on Organizational Processes and Performance," claims that they do. It has been cited thousands of times, referenced by Wall Street fund managers, and used in testimony before the U.S. Senate. Yet, after reviewing the report, I conclude that its critical findings are unjustified by its own evidence: its main method appears unworkable, a key finding is miscalculated, important results are uninterpretable, and the sample is biased by survival and selection. After correcting these problems, I replicate the original analysis and conduct additional empirical tests. Despite considering estimates from thousands of models, I find no reliable evidence for the proposed link between sustainability and financial performance.

Well then.

An Eye on Energy

The Future of U.S. Nuclear Energy

In the United States, there is increased interest in using nuclear power to reduce the carbon footprint of the electric power industry. Over the last 20 years, the U.S. has conceded its role as a leader in this industry to focus on renewable energy.

Nuclear energy's contribution to electricity generation in the U.S. will decline with aging plants unless it deploys advanced nuclear technologies by 2030. At the moment, there are 93 licensed nuclear power reactors at 54 sites in the U.S., generating 20% of our nation's electricity. Their average age is now 42 years, after 13 nuclear reactors were prematurely closed from 2013 through 2022, with two additional closures expected by 2025.

The most recent units to come online, Georgia's Vogtle Unit 3, in June 2023 and Tennessee Valley Authority's Watts Bar 2 reactor in 2016, were the first reactors to be built in the U.S. for two decades. All U.S. reactors are initially licensed to operate for 40-years, and they may apply for up to two 20-year renewals from the Nuclear Regulatory Commission. Under the current mix of licenses, all of today's reactors will be shut down by 2055.

This represents a major risk because nuclear plants provide an essential baseload power needed to fuel the American economy, unlike intermittent wind or solar power. Whether new reactors will be constructed will depend on their costs. Vogtle's Unit 3 and 4 were expected to cost $14 billion and their total cost is now estimated at over $30 billion.

New technology is nuclear energy's best hope to overcoming regulatory and financial barriers. Small modular reactors (SMRs) offer lower capital requirements, greater scalability, and siting flexibility for locations unable to accommodate traditional large reactors. Nuclear reactors range in capacity from about 300 megawatts—for SMRs—to around 1600 megawatts, with the average reactor around 900. It would take 800 wind turbines—or around 8.5 million solar panels—to equal the energy output of one average nuclear reactor.

Although promising, SMRs are experiencing growing pains: last Friday, leading nuclear energy startup NuScale Power laid off 40% of its employees after recently canceling its first-of-its-kind Idaho plant due to cost overruns caused by inflation and high interest rates.

Ultimately, the U.S. should still emerge as the global leader in SMR technology. Investments into extending the life of existing reactors to their full 80-years and in ensuring that advanced nuclear technologies like SMRs become commercially viable are vital to American energy security.

Join Our Next Webinar!

Join Matt Cole, CEO and CIO at Strive, and Anson Frericks, Senior Advisor and Co-founder of Strive, tomorrow, Wednesday, January 10, 2024 at 2:00 p.m. EST as they discuss what it means to be a mission-driven company and uncover the guiding principles that have shaped Strive's journey.

Click here to register

The Best of the Rest

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

- KFC, McDonald's and Starbucks investing heavily in China; fast food industry continues to be lured by huge Chinese consumer market, despite risks presented by China's economic and political woes and deteriorating U.S.-China relationship.
- Public utilities regulator concerned that pro-ESG asset managers are hurting energy prices and reliability for Americans; seeks public input on potential change to rule that allows the Big Three to invest in public utilities.
- Apple and Disney shareholder will vote on AI proposals at annual meetings following the Securities and Exchange Commission's ruling allow the proposals on the corporate ballot.
- Senator Ted Cruz calls for U.S. semiconductor production boosts to mitigate vulnerability to China.
- France adopts new ESG investment rules requiring certain sustainable funds to drop fossil fuels; may trigger wave of divestment while also increasing the number of labels and causing confusion for investors.
- Warren Buffet: Anti-Stakeholder Capitalist; Buffet expert pushes back on claim that the famed investor supports stakeholder capitalism, telling Forbes "it's mostly distracting noise, and food fights and actually not good for people and the country. Buffet has some very practical observations in order to achieve economic prosperity."
- Former Kentucky Attorney General to lead pro-capitalism group the 1792 Exchange; as attorney general, Mr. Cameron authored the nation's first formal opinion letter explaining that socially and environmentally motivated investing violates fiduciary duties.
- World Economic Forum sets agenda for Davos 2024; "trust" will be a key theme.
- SEC still mulling climate rules; speculation abounds.

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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.