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Welcome Speech: Jack Ehnes, Chief Executive Officer, CalSTRS, USA

On behalf of the California State Teachers' Retirement System I am happy to welcome you to San Francisco.

I did want to first mention Anne Stausboll of CalPERS who I have worked closely with these past seven years. CalSTRS and CalPERS not only share common board members but we also share common strategies in many areas. Having a colleague that genuinely believes in collaboration has been a source of strength for all of us. She will be greatly missed from her leadership role.

We are honored to host this conference and I trust you have been finding the discussions lively and topics timely. This year's theme, Promoting Long-term Thinking and Behavior for Sustainable Capital Markets, perfectly sets the tone for not just this conference, but for the investment world we live in today. Given last Friday's voted on Brexit, the need for stable long-term perspectives on the markets couldn't be greater.

It's appropriate in so many ways that this conference is being held in San Francisco, which is the center of technological innovation and a driving force in growth and productivity around the world. If we may be allowed a moment of parochial pride, just a few weeks ago, it was estimated that if California were an independent nation, it would be the 6th largest economy in the world, surpassing France. As international leaders in fields as diverse as technology, entertainment, agriculture and manufacturing, so California's leadership must also extend as global investors dedicated to the retirement security of millions of California's educators and public employees. We can no longer limit our concerns regarding a company's health to simple questions of profitability and growth. We now understand that companies must tackle complex issues such as climate change. A company that not only addresses risks, but also embraces opportunities, has significant advantages over other companies which believe these issues can be overlooked.

As we saw with the historic signing of the Paris Agreement, times truly are changing. Cities, regions, businesses, investors, civil society groups, and trade unions recognize the wide range of actions that will be undertaken to reach a safe and stable climate in which temperature rise is limited to less than two degrees Celsius.

California is also home to the Sustainability Accounting Standards Board chaired by Michael Bloomberg. With its completion this year of detailing industry specific standards conforming to a materiality standard, we now have, for the first time standards across 79 industries that can be used by investors for determining macro trends, company benchmarking, portfolio allocation and security valuation. Already we see interesting patterns from the standards with 93% of the U.S. equity market impacted by climate risk, 80% of the market by product alignment and safety and 75% of the market impacted by resource scarcity. In light of this, we are now in a time with unprecedented opportunity for institutional investors worldwide to both invest in clean technology and insist via our corporate governance activities that companies address ESG issues.

As we address the stewardship of this great state of California; a place that the world looks to for great ideas, but also faces great challenges. In particular, how do we use our resources to create a sustainable future? How we respond to real threats to air and water quality as well as our transportation infrastructure are the heart of creating and



sustaining the California dream. It's a dream which, without great care, is in great danger. Hard to miss the impact of this when you learn that California had 6,337 fires last year burning over 300,000 acres. This week the Lake Isabella fire has burned over 30,000 acres, 200 structures and lost two lives.

For decades, California has experienced water supply conflicts between the north and south regions. Just 40 miles from here you will find the California Delta, a body of 1100 square miles and composed of 700 miles of waterways. This river delta provides water to 23 million Californians (out of 38 million) and is the lifeblood for our agricultural industry. Years of drought here have created enormous strain on this water supply and the state is currently debating the development of two gigantic underground tunnels 150 feet below ground, 40 feet in diameter and 30 miles long that would more efficiently transport water between regions. There are many arguments for and against the tunnels and it is expected this will be resolved one way or another in the coming year.

Finally, in a state of this size and traffic congestion, transportation is front and center. California has begun the construction of long distance high speed rail. With expected speeds of 220 mph the goal is to provide a trip of 2 hours and 40 minutes from LA to San Francisco. The first leg being constructed is San Jose to the Central Valley by 2025.

Turning to CalSTRS. CalSTRS was established a little more than a century ago. It was begun in 1913 as the pension plan administrator for California's public school educators. For 103 years, CalSTRS has been recognizing the importance of, advocating for, and engaging in, best-practice governance and long-term sustainability. We recognize, and studies have proven, that effective corporate governance of the companies we invest in directly impacts our portfolio performance. This finding should not be a surprise: well-governed companies with proven, accountable management practices are more likely to allocate capital both efficiently and productively.

CalSTRS has a long track record of promoting corporate governance policies in the public pension community, with a detailed written policy which dates back to 1978. Our 'Investment Policy for Mitigating Environmental, Social and Governance Risks' and '21 Risk Factors', approved in 2008, clearly drive the direction of our investment strategies. Included in the 21 Risk factors are parameters specific to critical environmental issues such as air quality, water quality, climate change, and land protection. This is in addition to a formal policy on divestment, which was adopted by our Board in 2009.

Corporate engagement and market-wide initiatives are powerful tools that investors wield and encompass proxy voting on a variety of issues. Among these are executive compensation, board diversity, and sustainability and risk management. Changing dynamics within the corporate governance landscape have shifted in favour of institutional investors whose concerns offer long-term horizons. More and more institutional investors are using their influence to bring about positive change related to ESG issues.

Today's modern business operations demand that we confront pressure points in order to maintain a degree of success. This offers us an ideal opportunity to model how we address stakeholder concerns and incorporate them into our strategic planning processes. Increasing interest in environmental and social issues from our stakeholders has taken a more active and publicly voiced perspective in the past several years. Every CalSTRS board meeting in Sacramento is frequented by members of the public and



sometimes protestors urging the fund to take stronger positions on fossil fuel divestment. Many of these concerned individuals are school teachers who do not want their pension funds invested in fossil fuels.

Being global investors comes with great responsibilities. We firmly believe that engagement is the first call of action, and results show that it is the most effective form of communicating concerns with the companies we own. In addition, with the rising dangers of climate change on the forefront of global discussions, CalSTRS has an imperative to address the diversity of risks which are presented. In many ways, CalSTRS has taken an active role in this effort. We provide capital for sustainable development to make a measurable difference in reducing the footprint of greenhouse gas emissions and communicate this regularly. We recognize climate change as a material risk to society, the economy, and the impacts on our investment decisions. We have been at the forefront of tackling climate change issues through policy advocacy, engagement with portfolio companies and investing in climate change solutions.

At CalSTRS, we created an internal 'Green Team,' made up of representatives across all investment groups and asset classes, to further identify ways to avoid or mitigate risks to the investment portfolio posed by environmental, social and governance factors. Last year our environmental sustainability engagements included more than 35 U.S.-based companies on the issues of carbon risk exposure, energy efficiency, hydraulic fracturing risk, methane emissions management, and water risk management. Various shareholder proposals were submitted concerning methane emissions management, with all but two being withdrawn after successful negotiations between staff and the companies.

We also recognize that not all ESG challenges can be addressed by engagement. CalSTRS took the difficult step of divesting from companies selling guns (automatic weapons) that are illegal for sale in California but available for purchase elsewhere in the United States. We also took the step last week of joining scores of institutional investors, including many in this room, of filing suit in Germany against Volkswagen due to the blatant disregard for environmental regulations. Looking forward, CalSTRS will continue to focus its energies in environmental sustainability on Carbon Risk Exposure, Energy Efficiency, Hydraulic Fracturing Risk, Methane Emissions Management, and Water Risk Management.

Board diversity is another area in which we are focusing our energies as an investor. CalSTRS membership of close to 900,000 educators throughout the state is 72 percent female, so supporting the development and advancement of women in leadership positions is directly aligned with the composition of the majority of our membership. We've seen impressive scholarship in this area as well, like that of McKinsey & Company. Their research shows that companies which commit to diverse leadership in management-level positions are more likely to have financial returns as much as 35 percent above their national industry median. So while quotas do not appear as a realistic fix for the diversity gaps in American corporate boardroom, there is a growing acceptance that diversity is a good business practice and adds to shareholder value over the long term.

Our most recent diversity engagements include half dozen successful proposals, with most being withdrawn after successful negotiations with the company. We also continued a previous year's engagement of 130 companies held in the CalSTRS



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portfolio that were listed in the UC Davis study California Women Business Leaders, which identified California public companies that have no women on their boards. CalSTRS takes pride in being a long-term, patient investor and shareholder, which is evidenced through our engagement efforts with hundreds of companies over this past year and as we continue to move forward. Engagement is more critical than ever, especially with the ever-changing universe of issues facing us and our expanding responsibility as fiduciaries to secure the retirement future for California's public educators.

During this conference you will hear from global thought leaders and gain access to an indispensable forum for discussing emerging governance issues, learning best practices from and exchanging topical ideas with peers. We hope you all enjoy conference, the outstanding line up of speakers, and beautiful San Francisco.