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JOSHUA HUMPHREYS

## The Fiduciary Duty of Fossil-Fuel Divestment

Testimony before the Board of Aldermen  
City of Somerville, Massachusetts  
March 13, 2014

Joshua Humphreys, Ph.D.  
President and Senior Fellow  
Croatan Institute

Mr. President, Honorable Members of the Board of Aldermen,

Thank you for the opportunity to share my views on the resolution before you this evening requesting that the City of Somerville Retirement Board divest from the securities of fossil-fuel companies.

My name is Dr. Joshua Humphreys, president and senior fellow at Croatan Institute, an independent, nonprofit institute for advanced research on sustainability and finance. I am also a fellow at Tellus Institute, the sustainability think tank in Boston. I have become an established authority on trends in sustainable finance, endowment management, and institutional investment.

My research and opinion in these areas have been widely published and regularly cited in both the general and more specialized financial press, including in *Barron's*, *Bloomberg*, *BusinessWeek*, the *Boston Globe*, the *Financial Times*, *Institutional Investor Magazine*, the *Journal of Investing*, *Pensions and Investments*, the *Los Angeles Times*, the *Washington Post*, and on National Public Radio. I have taught at Harvard, Princeton, and New York Universities. I have spoken to audiences and investors across the country on these issues. And I have advised a wide variety of financial institutions and investors on social and environmental risk assessment, evaluation, and management, ranging from the Multilateral Investment Guarantee Agency of the World Bank Group to foundation endowment managers and asset management firms.

Last year, I published a paper called "Institutional Pathways to Fossil-Free Investing," which makes a clear, empirical case for divesting from fossil-fuel securities in prudent ways that meet the fiduciary expectations of long-term

institutional investors.<sup>1</sup> I would be glad to make the study available to members of the Board if it would be helpful for your deliberations.

While many people this evening will undoubtedly make a strong and compelling moral case for divesting from fossil-fuel companies, I would like instead to argue that the even stronger imperative for divestment is rooted in prudent risk management and fiduciary responsibility.

According to research and analysis conducted by an increasingly wide range of financial analysts, from researchers at the London School of Economics to Deutsche Bank and Standard and Poor's, fossil-fuel companies face unprecedented risks associated with the so-called "carbon bubble." In effect, the valuation of fossil-fuel securities, including stocks and bonds and derivatives of them, are inflated because far too many investors assume that the proved carbon reserves of oil, gas and coal on the balance sheets of those companies will be fully exploited. Increasingly, however, regulations of greenhouse gas emissions and other climate-related policies – to say nothing, of the scientific realities of global warming – are making it increasingly unlikely that fossil-fuel companies will be able to extract the full amount of carbon reserves they have discovered. In essence, these companies face substantial regulatory, political and social risk in addition to the risks associated with climate change.

Because of these developments, analysts at Standard and Poor's have already flagged long-dated bonds of small and mid-sized fossil-fuel companies for potential credit downgrades within three to five years. John Fullerton of the Capital Institute has estimated the value of this carbon bubble at more than 20 trillion dollars, roughly an order of magnitude greater than the mortgage meltdown we experienced during the financial crisis. In this sense, divestment from fossil-fuel companies facing such substantial mispricing and stranded-asset risk meets basic tests of fiduciary prudence.

At the same time, alternative fossil-free investing opportunities increasingly abound, with long-term track records of competitive performance that meet or exceed their conventional benchmarks. In my paper, I provide numerous examples of asset managers' actively and successfully managing portfolios without exposure to fossil-fuel securities at various intervals extending from one, three, five, and even ten years. Additionally, a recent analysis conducted by AWJ Capital Partners, a fund of hedge fund manager, documented that more than four dozen funds focused on investing in companies delivering "solutions" to the climate crisis and other resource challenges that we currently face in energy, water, and food supply have

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<sup>1</sup> Joshua Humphreys, "Institutional Pathways to Fossil-free Investing," Tellus Institute, May 2013, available at <http://www.tellus.org/publications/files/fossilfree.pdf>.

overwhelmingly outperformed both their broad conventional benchmarks and the 200 largest fossil fuel companies over the past one, three, five and seven years.

Just as the evidence mounts within climate science that greenhouse gas emissions have fueled unprecedented levels of global temperature rises during the industrial era so too do the data increasingly demonstrate that divestment from fossil fuels need not lead inevitably to under performance. To the contrary, it appears to be a prudent approach to investment as well as the right thing to do. I encourage you to pass the resolution with all deliberate haste.

Thank you for the opportunity to present my views on this extremely pressing issue.

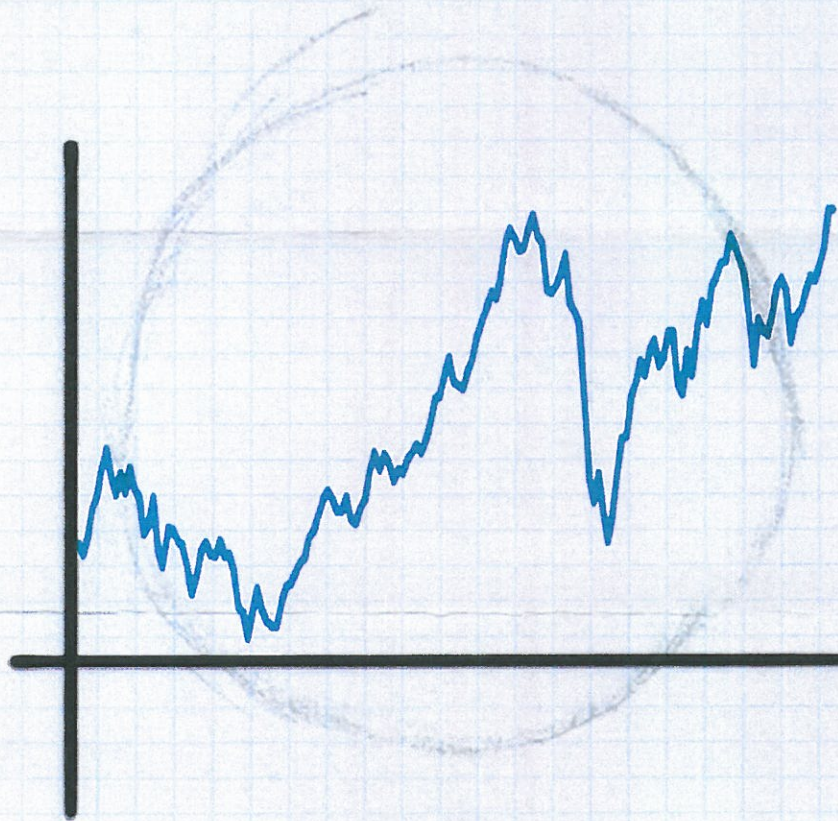
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# INSTITUTIONAL PATHWAYS TO FOSSIL-FREE INVESTING

Endowment Management in a Warming World

Joshua Humphreys



May 2013

**John Long**

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**From:** Joshua Humphreys [josh@croataninstitute.org]  
**Sent:** Thursday, March 13, 2014 11:38 PM  
**To:** John Long  
**Subject:** Written statement for testimony before tonight's public hearing, with supplemental paper  
**Attachments:** Humphreys Testimony Somerville Board of Aldermen 20140313.docx

Dear Mr. Long:

President White asked me to forward you the paper to which I referred earlier tonight during my testimony before the Board of Alderman so that the board members could review it.

I therefore attach herewith a written copy of my statement for the record, with the full citation to the paper to which I referred, "Institutional Pathways to Fossil-free Investing" (2013). It can be found online here: <http://www.tellus.org/publications/files/fossilfree.pdf>

Sincerely,

Dr.  
Josh  
ua Humphreys

Joshua Humphreys  
President  
Croatan Institute