

**BlackRock vs Norway Fund
at Shareholder Meetings:
Institutional Investors' Votes
on Corporate Externalities**

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Research Project

- Why do institutional investors engage companies on global externalities such as climate change?
- Two (non-exclusive) explanations
 - Universal ownership (Monks and Minow, 1995)
 - Delegated philanthropy (Benabou and Tirole, 2010)

In a perfect world

- Shareholders are unanimous in requiring executives to maximise the financial value of the firm
- Purely financial objective...
- ... and everything is for the best!
- No need for engagement
- See e.g. Fisher theorem



In reality

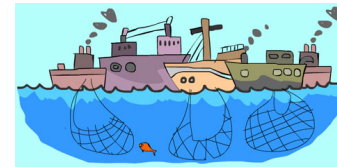
“The modern corporation is an economic institution in which there is always a potential political (i.e. voting) aspect.”

S. J. Grossman and J. E. Stiglitz, On value maximization and alternative objectives of the firm, *The Journal of Finance*, MAY 1977

- See e.g. the empirical analyses of Cunat et al., 2012 and Flammer, 2015



Externalities



- One important reason why shareholders disagree regarding corporate policies might be related to externalities
- Externalities refer to firms' impact on society that are not priced efficiently (CO2 emissions, nuclear energy, excessive use of common resources, Employee training, employee welfare...)
- Investors who value externalities may disagree on the level of externalities the firm should generate

Universal ownership

- Large institutional investors own a significant share in virtually all listed companies and have a long horizon
- They would like firms to take into account negative externalities to avoid deteriorating the **overall financial value** of their portfolios
 - Monks and Minow, 1995, Hawley and Williams, 2000, Mattison, Trevitt and Van Ast, 2011, Dimson, Kreutzer, Lake, Sjo, and Starks, 2013, and Azar, 2017

Universal ownership

- For example, universal owners may want to take into account the negative economic impact that the GHG emissions of a firm on other companies' businesses through water, food, health or migration issues
- Universal owners can also improve the level of coordination among firms' policies towards governance or competition policy
 - Benabou and Tirole, 2016 and Azar, Schmaltz, and Tecu, 2017

Universal ownership

- Impediments to universal ownership influencing engagement
 - Measuring the materiality of externalities?
 - Evaluating consequences on a given firm?

Delegated philanthropy

- Institutional investors such as pension funds, mutual funds and sovereign funds invest on behalf of clients or citizens who may have **preferences regarding externalities** that differ from the ones of companies' managers
- They might want to **promote** these clients' and citizens' values and preferences and induce management to choose the appropriate course of action
 - Heinkel, Kraus and Zechner, 2001, Benabou and Tirole, 2010, Gollier and Pouget, 2016

Delegated philanthropy

- For example, investors may want to communicate their preferred level of precaution regarding climate change to management
- This can only be achieved via engagement
- One important reason why institutional investors may endorse the delegated philanthropy logic is that they care about their **reputation** among clients or citizens

Delegated philanthropy

- Morgan and Tumlinson (2012) offer two reasons why engagement by institutional investors on externality issues is legitimate
 - Companies' actions are less subject to the free-rider problem than individual shareholders
 - Companies' production decisions are more efficient from a social point of view and increases the welfare of shareholders and citizens who care about externalities

Delegated philanthropy

- Impediments to delegated philanthropy affecting engagement:
 - Measuring/aggregating clients or citizens' preferences?
 - Preferences for non-responsible behavior?

Methodology

- Focus on two **archetypical** investors:
 - **BlackRock**: private company listed on NYSE, fiduciary duty to shareholders (PNC Bank, Norges Bank IM, Vanguard, Wellington, BlackRock...) – Equity portfolio around \$2.6 trillion – 3,648 holdings above 3% around the world
 - **Norway Fund**: sovereign wealth fund monitored by the Norwegian Ministry of Finance, fiduciary duty to the representatives of the Norwegian people – Equity portfolio around \$500 billion – Average equity share around 1% around the world

Methodology

- Both funds are **universal owners**
- Both funds have centralized corporate governance teams (31 persons at BR and around 12 at NF)
- Differences between funds:
 - **BlackRock as a standard investor** – Only the universal investor logic may apply
 - **Norway Fund as a responsible investor** – The delegated philanthropy may also apply

Methodology

- Study how the two investors vote shareholder resolutions on Environmental (E) and Social (S) issues - e.g., GHG emissions, nuclear safety, GMOs, human rights, diversity - **proxy for externality issues**
- Compare votes on shareholder resolutions on E and S issues to
 - Shareholder resolutions on Governance issues
 - Management resolutions on G and Financial issues
- Focus on investors' **opposition to management**
 - Management opposes all resolutions on E and S issues
 - Identical to studying support of investors for E and S negative externality mitigation policies

Methodology

- Test what factors are driving corporate engagement of institutional investors on externality issues
- Two logics might explain such engagement:
 - Universal ownership
 - Delegated philanthropy
- If BlackRock engages companies on externality issues, the universal ownership logic is at work
- If the Norway Fund engages more, the delegated philanthropy logic is at work

General assembly meetings

- General meetings (GM) provide shareholders with a corporate governance mechanism
 - Exercise their voting rights, meet the management and challenge certain strategic decisions
- Resolutions submitted at GM may be sponsored by the management or by shareholders
 - cover financial, environmental, social, governance issues
 - In the US, proposals are submitted under the SEC 14a8 rule, by shareholder holding at least \$2,000 or 1% of the company's securities
 - Rules vary in Europe: min 5% in the UK or France, 1% in Austria, 1% in the Netherlands, one single share in Germany or Nordic countries

Our empirical study

- Focus on 35,382 resolutions at 2,796 corporations across the world for the year 2014
- Resolutions at which **both** BlackRock (BR) and Norway Fund (NF) **voted**
- Data:
 - Votes from SEC filings for BlackRock and from the web for Norway Fund
 - Firm characteristics from Factset (market cap, ROA...)
 - Financial data from Bloomberg
 - Extra-financial ratings from MSCI ESG STATS
 - Analysts' forecasts from I/B/E/S

Data on environmental issues

	Number of voted resolutions	Rate of opposition to the management by sponsor of the resolution			
		BlackRock		Norway Fund	
		<i>Management</i>	<i>Shareholder</i>	<i>Management</i>	<i>Shareholder</i>
Environmental issues	69	-	4%	-	49%
Animal welfare	2	-	0%	-	50%
Animal testing	1	-	0%	-	0%
Animal welfare policies	1	-	0%	-	100%
Climate	24	-	4%	-	83%
Climate change and GHG emissions	24	-	4%	-	83%
Environment and sustainability	34	-	0%	-	23%
Hydraulic fracturing	3	-	0%	-	67%
Nuclear safety	15	-	0%	-	0%
Sustainability reporting	16	-	0%	-	50%
Others	9	-	22%	-	33%

Data on social issues

	Number of voted resolutions	Rate of opposition to the management by sponsor of the resolution			
		BlackRock		Norway Fund	
		<i>Management</i>	<i>Shareholder</i>	<i>Management</i>	<i>Shareholder</i>
Social issues	257	6%	9%	7%	49%
Consumer issues	10	-	10%	-	10%
Genetically modified ingredients	8	-	13%	-	13%
Other consumer responsibility	2	-	0%	-	0%
Diversity	11	-	9%	-	73%
Board diversity	4	-	25%	-	75%
Discrimination	1	-	0%	-	0%
Sexual orientation	6	-	0%	-	83%
General corporate issues	40	23%	0%	23%	0%
Charitable contributions	40	23%	0%	23%	0%
Human rights	20	-	10%	-	35%
Human rights proposals	20	-	10%	-	35%
Political activities	176	0%	9%	1%	55%
Lobbying	29	-	10%	-	38%
Political contributions	147	0%	9%	1%	65%

Data on governance issues

	Number of voted resolutions	Rate of opposition to the management by sponsor of the resolution			
		BlackRock		Norway Fund	
		<i>Management</i>	<i>Shareholder</i>	<i>Management</i>	<i>Shareholder</i>
Governance issues	28 396	3%	12%	8%	36%
Audit practices and risk management	3 113	2%	0%	7%	8%
Audit practices	3 111	2%	0%	7%	9%
Risk management	2	-	0%	-	0%
Board accountability and responsiveness	18	0%	0%	0%	20%
Ability to remove directors	13	0%	0%	0%	0%
Tax transparency	5	0%	0%	0%	100%
Board independence	51	100%	16%	100%	88%
Competitive activities of directors	1	100%	-	100%	-
Independent chairman and directors	50	-	16%	-	88%
Board structure	20 557	2%	5%	7%	7%
Appointment	20 143	2%	0%	7%	1%
Board composition	167	1%	0%	1%	38%
Others board related proposals	86	1%	47%	3%	47%
Related-party transaction	161	1%	-	6%	-
Compensation/Remuneration	4 462	5%	2%	11%	47%
Employee compensation	1 606	6%	0%	11%	15%
Executive compensation	2 856	4%	3%	10%	53%
Shareholder rights	195	21%	35%	20%	49%
Call special meeting	20	0%	33%	0%	67%
Proxy access right	22	0%	47%	0%	53%
Takeover defenses	87	29%	53%	26%	20%
Voting formalities	66	8%	24%	12%	54%

Data on financial issues and total

	Number of voted resolutions	Rate of opposition to the management by sponsor of the resolution			
		BlackRock		Norway Fund	
		<i>Management</i>	<i>Shareholder</i>	<i>Management</i>	<i>Shareholder</i>
Financial issues	5 716	3%	6%	5%	26%
Others issues	944	4%	1%	6%	7%
Total	35 382	3%	9%	7%	34%

Descriptive statistics

Variable	N	Mean	Std. Dev.	Min	Max
Panel A: Measures of agreement					
oppos_atleystone	35 382	0,09	0,28		
oppos_blackrock	35 382	0,03	0,16		
oppos_norway	35 382	0,08	0,27		
Panel B: Resolution characteristics					
shareholder proposal	35 382	0,02	0,15		
resolution ES	35 382	0,01	0,10		
resolution G	35 382	0,80	0,40		
Panel C: Country and firm ESG ratings					
Country Rating ES	35 382	0,62	0,06	0,36	0,69
Country Rating G	35 382	0,78	0,12	0,14	0,95
Company Rating ES	35 382	4,91	1,49	0,50	9,95
Company Rating G	35 382	6,57	2,68	0,00	10,00
Panel D: Firm characteristics					
mktpcap	35 382	14 923	32 209	48	439 000
roa	35 382	4,57	8,34	-99,50	189,00
pricetobook	35 382	3,84	32,69	0,19	1 540,00
salesgrowth	35 382	0,22	4,70	-1,04	177,00
assetturnover	35 382	0,79	0,70	0,00	9,39
volatility	35 382	38,55	13,02	14,04	202,92
analyst dispersion	35 382	0,13	1,02	-54,22	27,68

Opposition to management

	Probit coefficients		
	(1) BR or NF oppose	(2) BR opposes	(3) NF opposes
Shareholder proposal*resolution ES	1.867***	1.028***	1.818***
Management proposal*resolution ES	0,089	0.435**	0,146
Shareholder proposal*resolution G	1.594***	1.220***	1.507***
Management proposal*resolution G	0.327***	0.238***	0.296***
Country rating ES	-2.768***	-5.334***	-2.195***
Country rating G	1.108***	1.752***	0.900***
Company rating ES	-0,018	-0,026	-0,016
Company rating G	-0.038***	-0.040***	-0.036***
Mktcap	-0.048***	-0.056**	-0.048***
ROA	-0,011	-0.085*	0,009
Pricetobook	0,004	-0,010	0,003
Salesgrowth	0,015	-0,012	0,017
Assetturnover	-0,026	-0,010	-0,028
Volatility	-0.048**	-0.091***	-0.037*
Analyst dispersion	0,001	-0,013	0,003
Industry fixed effect	yes	yes	yes
Country fixed effect	yes	yes	yes
Observations	35 382	35 367	35 382
Pseudo R2	0,062	0,085	0,058

Main results

- **Both investors oppose management more for E&S shareholder resolutions than for management resolutions on financial issues**
- **Only Norway opposes management more for shareholder resolutions on E&S than on governance issues**

Robustness checks

- Identical results when we focus on firms for which we know the **holdings** of the two investors from SEC Filings 13F – 6,037 resolutions voted by both investors in 548 firms
- Identical results when focusing on **climate change** issues – Clearly an externality
- Identical results when focusing on **active equity portfolio** of BlackRock – 8,782 resolutions voted by both investors in 658 firms
- Identical results **with and without country fixed effects**, and with a **bivariate** analysis

Extensions

- Study two other universal owners in 2014:
 - **Vanguard** (\$4.4 trillion of AuM): not more opposition to management on E&S issues than on financial issues
 - **State Street** (\$2.6 trillion of AuM): Same results as BlackRock
- Future work: study more recent time periods and other responsible investors

Conclusion

- Engagement of corporations on externality issues by institutional investors in line with delegated philanthropy, less with universal ownership
- Our study **questions the objective of the firm** and decision-making tools such as NPV used by corporations

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THANKS FOR YOUR ATTENTION!!!

COMMENTS ARE WELCOME