These quarterly reports highlight recent developments and achievements related to Maryland's pension system.

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MANAGING CLIMATE RISK

BACKGROUND

In a 2020 report, the Federal Reserve Board of Governors identified climate change as a critical emerging risk to the stability of the U.S. financial system. Both the energy transition and physical impacts wrought by the changing climate present risks and opportunities for the Maryland State Retirement and Pension System's investment program. Extreme weather events, wildfires, and rising sea levels threaten physical infrastructure, agriculture, coastal real estate, and the companies insuring them, while the shift from fossil fuels to renewable energy reshapes the profitability profile for energy-related businesses.

Just as investors assess cybersecurity risks posed by new technologies, or liquidity risks associated with various investment strategies, it is essential to evaluate the multifaceted impacts of climate change, which influence global financial markets through physical disruptions, regulatory changes, and evolving energy demands. For pension funds like Maryland's, these changes represent risks with potentially profound financial implications that could affect the ability to achieve the long-term returns necessary to secure retiree benefits.

MARYLAND'S APPROACH TO MANAGING CLIMATE RISK

The Maryland State Retirement and Pension System (SRPS) is proactively incorporating climate considerations into its $70 billion portfolio by:

- **Conducting an annual risk assessment report,** which includes an evaluation of the portfolio's exposure to climate-related risks and transition-readiness.
- **Integrating climate factors into the asset allocation process**, and associated portfolio modeling and scenario analysis, to ensure alignment with long-term investment objectives.
- **Considering climate risk when selecting and monitoring investment managers –** through due diligence and oversight – to ensure they are factoring climate risks into the investment decision-making process.

To further demonstrate its commitment to address climate change risk, last quarter the SRPS Board of Trustees approved a charter for a **new Climate Advisory Panel**. This charter outlines member qualifications, responsibilities, meeting protocols, and fiduciary requirements. The establishment of the Panel follows legislation adopted in 2022 that requires SRPS to include climate change as an investment risk factor and authorizes the Board of Trustees to assemble a Panel of experts to support this initiative. The Panel will include at least three external experts in the analysis of climate change risk. Together, **this Panel will help the SRPS develop objectives, strategies and policies for establishing a path to a long-term sustainable portfolio** consistent with fiduciary duties and the goals and objectives of the System's investment program.

KEY RESPONSIBILITIES OF THE CLIMATE ADVISORY PANEL

- **Risk Mitigation:** Recommend how to best measure and track the risks associated with climate change on the System's assets, and the impact that the System's portfolio may have on climate change; and assist in the development of Maryland's annual climate risk report.
- **Opportunity Identification:** Advise on opportunities for investment in technologies and industries aligned with the global energy transition.
- **Policy Development:** Offer recommendations to incorporate climate risk factors into investment processes, objectives, and policies – such as due diligence and proxy voting – based on best practices and current science related to climate change risk.
- **Strategic Planning:** Establish a strategic plan to achieve a long-term sustainable portfolio, and track and report on climate-related investment initiatives.

NEXT STEPS

Investment staff will support the Panel in executing its mandate, ensuring that climate-focused initiatives are implemented effectively. The Panel will be assembled and begin its work this year with an evaluation of the 2025 climate risk report.

The SRPS is inviting qualified candidates with expertise in climate risk analysis, sustainable investment strategies, or climate policy to express interest in serving on the Panel. Submissions can be sent to cdavis@sra.state.md.us.

HOW OTHER STATE PLANS ARE TACKLING CLIMATE RISK

More state pension funds are addressing climate change challenges by taking proactive steps to integrate climate considerations into their investment processes. For example:

- **California:** The California Public Employees' Retirement System (CalPERS) and California State Teachers' Retirement System (CalSTRS) have both implemented comprehensive climate action plans, focusing on reducing exposure to high-carbon assets and investing in low-carbon technologies.
- **New York:** The New York State Common Retirement Fund has committed to achieving net-zero greenhouse gas emissions across its investment portfolio by 2040. It actively engages with portfolio companies on sustainability issues and has allocated billions to climate solution investments, such as renewable energy and energy efficiency projects.

By learning from other states and leveraging expert insights, Maryland's pension fund can better protect its assets while promoting a sustainable future for retirees and the community.

The Maryland State Retirement and Pension System (SRPS) provides retirement, death, and disability benefits for over 420,000 members, including state employees, teachers, police, and judges. A 15-person Board of Trustees, led by the Treasurer and Comptroller, oversees the system. The Board and several committees meet regularly to set policies that guide investment strategy, and to review operations and performance. State Retirement Agency (SRA) staff execute the work to ensure timely benefits distribution and investment of plan assets for a fully funded retirement system.

02/10/25