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MIT's Environmental, Social, and Governance (ESG) Investment Framework

MIT's endowment is dedicated to the support of MIT. Each year, resources from the endowment are spent to help support financial aid, cancer research, the fight against climate change, and countless other efforts led by MIT faculty and students. Because investment returns accrue to the sole benefit of MIT's mission, we strive to earn high real rates of return over the long-term. A successfully invested endowment allows MIT to have a positive impact on the world.

In our search for high returns, we restrict ourselves to investment choices that comport with MIT's values. In many situations, these ethical considerations depend on specific situational dynamics, making it impossible to construct a simple set of rules to make decisions. As a result, we must respond to individual circumstances based on our knowledge of MIT's values and the guidance we receive from the Institute's leadership and governance. When important and complex social investment issues arise, MIT convenes members of the community to discuss the Institute's position and to make recommendations to the administration and the MIT Executive Committee.

ESG in Practice

Historically, MIT was able to engage in discussions about the social consequences of individual investments. This process was enabled by the fact that we used to hold a relatively small number of securities and we held them directly in MIT's control. In 1970, for example, MIT's endowment held approximately 250 different securities. Four stocks – Eastman Kodak, Ford, GM, and IBM – constituted almost 25% of the portfolio. Today, the picture is very different. Like other large endowments, we now invest primarily through commingled funds controlled by external managers, rather than owning stocks and bonds directly. We have exposure to well over 5,000 different public and private securities globally across hundreds of different funds. As a result, we do not have real-time transparency into portfolio holdings, we do not control which securities are bought and sold, and we have exposure to many individual positions that are de minimis in size.

Not surprisingly, the tools needed for the effective implementation of an ethical investment policy have changed. Because the vast majority of our investment portfolio is invested in commingled funds where we have no ability to set security specific restrictions, divesting from individual securities has become a less effective option. While we can decide not to hold certain securities directly, this action carries less weight as the only investments we currently pursue directly are real estate assets located around campus in Cambridge. We maintain the ability to write in security specific restrictions where we maintain separately managed accounts in MIT's name but these accounts also constitute a relatively small percentage of the portfolio.

Our primary line of defense today is to choose investment managers who apply an ethical lens to their activity. We have turned down numerous managers based on this filter. Some decisions are easy. In recent years, for example, we passed on a manager who was cavalier about the possibility that a portfolio company was using child labor, a manager who had an executive linked to a stock-option backdating scheme, a manager who had purchased a company and tried to avoid paying pension liabilities, and a manager who, according to a reference, sought potentially illegal information about upcoming quarterly earnings from a company director.

Other decisions fall into a grey area. For example, we passed on a patent fund (in which investment managers buy patents and work to realize value from companies whose products use the intellectual property) because we were concerned about how we would distinguish between the activities of a legitimate defender of intellectual property and the activities of a patent troll. We passed on a life settlements fund (where investors buy life insurance policies and get higher returns if people die earlier than expected) because we were worried there might be incentives to convince less-informed people to sell their policies too cheaply. We passed on the opportunity to purchase old-growth timberland despite the blessing of a major conservation organization because we were worried about the environmental impact. In all of these examples, we could see reasonable people making a different decision based on the details of a specific situation and a deep understanding of how a particular manager conducts its activities.

Our second line of defense is engagement. Although we lack direct ownership of securities, we can still lobby companies to change behavior. In 2020, for example, we joined Climate Action 100+, an organization that brings investors together to push for improved corporate disclosures and reduced greenhouse gas emissions. We also can use engagement to influence manager behavior in certain situations. A few years ago, one of our real estate managers was considering the purchase of a warehouse building in California where one of the tenants was a marijuana grower and distributor. Under California law, the property owner would become a party to the cultivation and distribution of a controlled substance. While the manager maintained full contractual discretion to proceed with the purchase, they reached out to investors for advice. Investors, including MIT, questioned the wisdom of becoming a test case of state law versus federal law. While the manager was separately coming to the conclusion to pass on the acquisition, investor arguments helped make a stronger case.

Our final line of defense is manager divestment. Because we do not control investment decision-making, we must ultimately end a relationship with a manager if we do not agree with their behavior. This behavior could range from ill-treatment of employees to bad partnership actions to disregard for environmental regulations to ownership of assets that we believe conflict with MIT values. For example, in recent years, we have ended relationships with a manager that owned a Canadian oil sands investments, a manager who engaged in multiple related party transactions, a manager whose personal behavior displayed lack of judgment, and a manager who decided it was inconvenient to honor our contractual agreement. Sometimes it can take significant time to exit a relationship depending on the nature of our legal contracts and the liquidity of the underlying assets.

Case Study: Climate Change

Our investment stance with regard to climate change has changed dramatically in recent years. Fifteen years ago, we pro-actively sought out fossil fuel investments to add to the portfolio given their ability to hedge against the Institute's energy costs. Once it became clear that fossil fuels were not fit to be the energy source of the future, we removed the special status of these investments and built in three additional hurdles to ownership. First, we incorporated the physical risks of climate change into our thinking. Here, we look to avoid investments that would be damaged by the physical impacts of climate change, such as ownership of real estate in a flood plain. Second, we incorporated the financial risks of climate change into our thinking. Here, we shortened the duration over which we assumed fossil fuel investments would earn returns. Finally, we incorporated regulatory risk into our thinking. Here, we burdened new investments with the potential impact of sensible new potential regulatory actions even if those regulations were not actually in place. These actions led to an exit over the past decade from several oil and gas focused managers and over a 75% decline in our oil and gas exposure.

In addition to incorporating climate risk into our investment decision making, we decided to pursue engagement activity as a means of using voice to push for additional progress. We ask managers to incorporate the risks of climate change into their investment thinking and end relationships where they do not. In 2020, we joined Climate Action 100+ to push for increased corporate disclosures and for transitions to cleaner energy sources.

As a direct investor in Cambridge real estate, MIT has the opportunity to show leadership on climate issues in other ways. In 2017, MIT signed an agreement to purchase the ten acre Volpe site in Cambridge. Working closely with the City of Cambridge and the local community, we created a development plan in which we will develop all-electric residential buildings (eliminating on-site fossil fuels), install a state-of-the-art wastewater recycling system (reducing potable water consumption), and raise the entire site to the projected 2070 100-year flood elevation.

Finally, we have begun analysis to identify ways we could move our investment portfolio to net carbon neutral over time. Our initial steps are directed at gathering the information needed to track the carbon footprint of the portfolio and exploring the practical steps involved in carbon offsets. As a means of ensuring near-term progress, we have committed to offset all carbon emissions from the Volpe real estate project.