

A sustainable and profitable future - Can boards of directors meet all expectations?

Zurich, December 8, 2021 - The results of the 9th SWIPRA Corporate Governance Survey confirm the central role of corporate governance in meaningfully integrating sustainability into corporate strategy. The survey shows that Swiss boards of directors are overall well positioned: Institutional shareholders place a high and even increased level of trust in Swiss boards. However, from the shareholders' point of view, boards still take insufficient responsibility for social ("S") and environmental ("E") topics. In their view, it often remains unclear to what extent E&S considerations are incorporated into strategic decisions – from the business model, to compensation, to leadership and the associated board composition or to capital allocation, for example investments in new technologies. A majority of companies is in the process of comprehensively assessing and, if needed, adjusting existing business models, internal structures and responsibilities, as well as comprehensively revising ESG-disclosure. In Switzerland, starting 2024, this sustainability-reporting will become subject to a shareholder vote at the annual general meeting (AGM), and an overwhelming majority of survey participants prefer a consultative say-on-sustainability vote. Therefore, it is important to understand, internally as well as externally, what opportunities and threats arise from E&S factors and which strategic adjustments, if any, should be made. This is necessary to ensure that not only trust in governance remains high in the future, but also that the understanding of the E&S integration in business models is better understood. The survey further provides insights on topics such as ESG reporting standards, the content of non-financial reporting (NFR), E&S in compensation plans, shareholder dialogue and the future format of AGMs.

Next Events

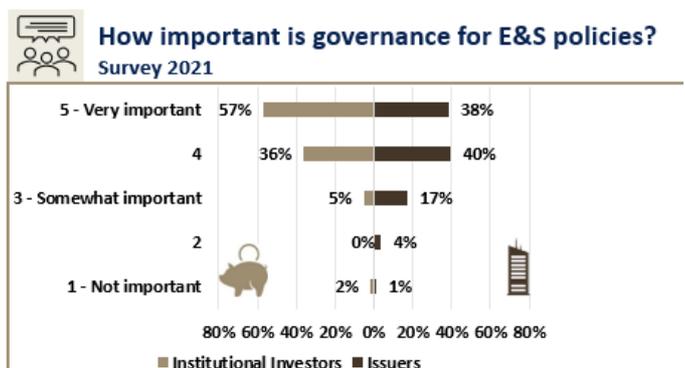
SWIPRA Corporate Governance Survey
Presentation of key findings
8 December 2021

Board Leadership Circle
Event with KPMG (by personal invitation only)
19 January 2022

High confidence in boards, but...

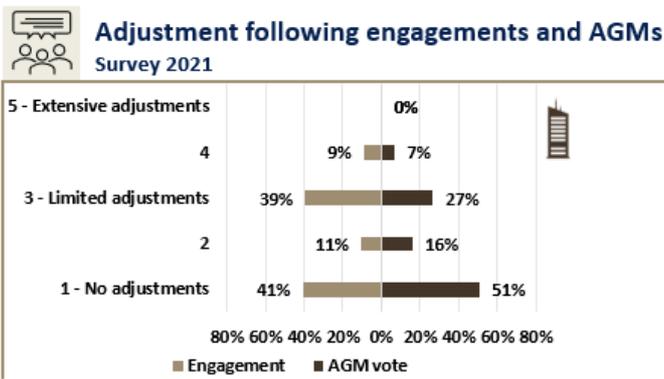
- 69% of Swiss and 63% Non-Swiss institutional shareholders have a high or rather high confidence in Swiss boards (up from 55% and 53%, respectively, in 2018)
- 93% of shareholders and 78% of companies consider a solid governance framework as an important or very important factor for a successful sustainability strategy
- Yet only 31% of institutional shareholders believe that boards assume sufficient responsibility in the area of E&S.

The SWIPRA Survey shows: The overall level of shareholder confidence in Swiss boards is high, but to many market participants it remains unclear to what extent the board is involved and assumes leadership in E&S topics. To some extent, this may be a consequence of the silo approach to E, S and G often observed in recent years. This hardly allowed for a strategically integrated view. It is now up to the companies, especially their boards, to build and explain the structures for this integration within the organization.





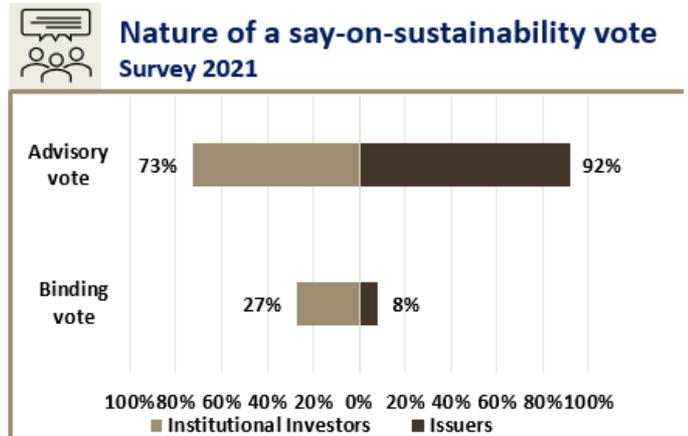
An important tool for explaining the board’s leadership role is the direct exchange between boards and stakeholders (engagements). Besides allowing for an efficient exchange of information, these engagements also have a real impact: 59% of the companies stated that they had made adjustments to their structures in the wake of such engagements. This is a highly relevant finding for the current discussion on levers and impact of “sustainable investing”.



Movement in disclosure, non-binding vote on NFR

- Only 16% of institutional asset managers (IAMs) and 11% of pension funds (PFs) feel that current sustainability reports are sufficiently informative.
- 90% of IAMs miss information on the strategic relevance of sustainability topics and 61% of PFs would like more detailed information on environmental topics.
- The AGM votes on the NFR, expected to become legally required by 2024 in Switzerland, are useful for 81% of shareholders and 58% of companies.
- A clear majority of market participants, 73% of shareholders and 92% of companies, prefer a consultative, non-binding vote on the NFR.

Shareholders' perception of the boards’ insufficient sustainability orientation is related to the quality of disclosure. Current NFR is considered meaningful by only a minority of shareholders; in particular, the strategic relevance of E&S factors is not understood well enough. This is also recognized by the companies. 52% stated that they will comprehensively adjust their NFR until the mandatory AGM vote in 2024. It is essential



that the role and involvement of the board in E&S issues becomes better explained, since this is increasingly important in the shareholders’ assessment of corporate governance.

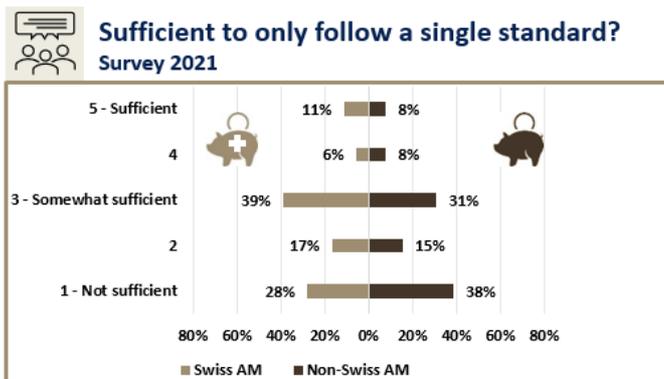
A disclosure standard does not yet make an NFR

- 53% of Swiss and 31% of non-Swiss shareholders prefer the GRI standard to base their NFR on.
- 85% of non-Swiss and 47% of Swiss shareholders have a preference for the SASB standard (the survey allowed multiple choices).
- Only 12% of shareholders feel that the implementation of only one ESG-standard is sufficient to understand the strategically relevant factors of a company.
- 68% of companies intend to publish company-specific information beyond any ESG standard.
- 71% of shareholders and 53% of companies would welcome a minimum legally required ESG reporting standard.

While ESG reporting standards are currently undergoing consolidation, shareholders' preferences of standards differ widely. It can be observed that SMI® companies often comply with several sustainability standards in parallel. For smaller companies, this seems hardly feasible. Further, the survey shows, that the NFR should not only comply with an ESG reporting standard, but be complemented by company-specific, strategic considerations. Given the diverse preferences in the market, it is not surprising that a majority of market



participants would like to see a regulatory requirement of at least one common ESG standard to be applied in order to clarify the current situation. However, the objective of such a mandated standard (focus on E, S, G or everything?) as well as the required effort and resources by companies, in light of company size and business model, would have to be taken into account. Clearly, TCFD reporting (climate-related reporting) that is currently proposed as a mandatory standard by the Swiss Federal Council for all listed companies does not fulfill the aspiration towards a comprehensive consideration and disclosure of the various characteristics of sustainability.



ESG incentives – Search for a system and transparency

- 81% of shareholders and 86% of companies support ESG incentives in performance-based compensation
- For 77% of shareholders and 51% of companies, ESG incentives should be reflected in short-term and long-term compensation instruments.
- Only 12% of shareholders are satisfied or very satisfied with the current pay-for-performance transparency in qualitative targets, and 24% are satisfied or very satisfied with the description of qualitative performance targets.

Companies (90%) and shareholders (84%) see ESG factors as relevant to companies’ long-term value generation and support explicit ESG incentives in compensation plans. 27% of shareholders even believe that a portion of the board’s fees should be explicitly linked to sustainability targets.

According to a majority of survey participants, these ESG-incentives should focus management attention and action on specific, for the company strategically relevant ESG issues. The integration of such targets should take place in short- and long-term compensation components. The difficulty lies in finding and setting ESG incentives that not only promote strategic ESG goals and support associated behavior, but also allow a tangible assessment from the outside.

Companies stuck between a rock and a hard place in addressing the “E” and the “S”

- 71% of IAMs see a high or rather high sensitivity of their customers with respect to ESG, compared to only 29% of companies.
- Only 17% of IAMs see no or almost no willingness of their clients to pay for ESG, while companies perceive 36% of their clients to have such a limited willingness to pay for ESG.

The adoption of business models and the stronger focus on strategic ESG goals, especially climate-related targets and CO₂ reductions, respectively, often requires companies to also make substantial investments. These are in particular requested by the financial industry as part of "sustainable investment" strategies, using engagements and AGM votes to insist on these requests at board level. At the same time, however, companies are often confronted with very price-sensitive consumers who show little willingness to pay for sustainability. Consequently, in the short term, companies would have to rely on their customers’ willingness to pay higher prices and/or on the capital market being satisfied with lower returns. Neither is currently the case, on the contrary. More regulation could even lead to a situation where necessary investments for a company’s future business are not made or are delayed due to short-term constraints. Hence, politicians and the public must better understand that necessary business transformations to better incorporate ESG is a very long-term and capital-intensive process that requires substantial capital.



AGM formats, engagements and further insights

- For future AGMs, 70% of shareholders (40% of companies) voiced a preference for a hybrid form, including real-time Q&A (41% of shareholders, 23% of companies) and live e-voting (37% of shareholders, 27% of companies). 48% of companies, but only 16% of shareholders prefer a physical-only AGM.
- According to the survey, engagement access to the board has improved for non-Swiss shareholders, but was less for Swiss shareholders. This may be related to the size of institutional shareholders.
- 27% of companies expect a high or rather high impact on their suppliers in developing countries due to the counter-proposal to the corporate responsibility initiative
- 63% of the companies expect that these suppliers will have to adapt internal processes, 56% that more extensive reporting will have to be prepared.
- 23% of companies reported having a compliance management system (CMS) in place for human rights, 17% for conflict minerals.
- 85% of shareholders and companies see added value in an *internal* audit of the NFR. Though, for only 26% of investors it is clear from companies' disclosure how responsibilities on non-financial issues and processes are reflected and monitored by the "Three Lines" framework.
- Only 21% of shareholders and 12% of companies estimate the benefits of an external audit of the NFR to be higher than its costs. The benefits come, according to 77% of the companies and

shareholders, primarily from a third-party review of ESG data by the external auditor.

About the SWIPRA Survey 2021

In collaboration with a team of researchers from the Institute of Banking and Finance at the University of Zurich, all companies listed on the Swiss Performance Index SPI® as well as institutional shareholders from Switzerland and abroad were invited to participate in the 9th SWIPRA survey on corporate governance in Switzerland. During the survey period (September/ October 2021), 76 Swiss companies listed on the SIX Swiss Exchange, representing about 73% of the market capitalization of the Swiss Performance Index, and 73 institutional asset managers and asset owners from Switzerland and abroad participated. The participating shareholders, around 38% of them based abroad, represent at least 30% of the equity investments managed worldwide (Source: IPE) and hold substantial stakes in Swiss companies.



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SWIPRA Services is working with a high-profile think tank to further develop corporate governance and CSR in Switzerland.

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