

7. SWIPRA-Survey on Corporate Governance in Switzerland

Corporate Social Responsibility – Lack of mutual understanding, rethinking required

Zurich, November 6, 2019 - Results from the 7th SWIPRA Corporate Governance Survey show that institutional shareholders find it difficult to understand how corporate social responsibility is anchored in corporate strategies. For their part, companies often do not understand how their socially responsible actions influence shareholders' investment and voting decisions at shareholder meetings. Better disclosure and a broadly-based governance dialogue between shareholders and boards of directors will help to close these gaps in mutual understanding. This is important since a large fraction of institutional investors believes that boards of directors are not acting diligently enough in terms of corporate social responsibility. Contrary to previous years, a majority of investors expect to see performance targets related to socially responsible behavior to be included in the compensation framework. Many market participants will have to change their views, as the topic of corporate social responsibility cannot be treated as an abstract, detached issue by itself, but needs to become an integral part of corporate strategy and its implementation.

Corporate Social Responsibility – Mind the gap

Society and shareholders have high and increasing expectations with regard to socially responsible entrepreneurship or Corporate Social Responsibility (CSR). However, there is a lack of mutual understanding as to "how" a business is run and managed: only 17% of institutional investors indicate that they recognize how companies integrate CSR in their corporate strategies. On the other hand, only 41% of companies listed in Switzerland understand how institutional shareholders incorporate CSR information into their investment decisions. And for only 48% of the companies it is clear how information on CSR impacts shareholders' voting behavior at Annual General Meetings (AGM).

These gaps in mutual understanding can be bridged with a change in the way disclosure is done and by intensifying the dialogue between boards of directors and institutional investors ("engagements"). 73% of the shareholders participating in such engagements aim at developing a better understanding of the individual situation of a company. Yet only 45% of Swiss institutional investors engage in such a dialogue, compared to 89% of non-Swiss investors. The latter usually hold relatively large stakes in Swiss companies and predominantly pursue a passive, index-tracking investment approach, tying them to the member stocks of an equity index over the long term. These investors revealed in the survey that they predominantly use engagements to actively influence their investee companies' governance structures. Consequently, changes in corporate governance, in particular related to compensation and corporate social responsibility, are usually initiated by large investors during the year, rather than at the AGM.

Barbara Heller, Managing Partner at SWIPRA Services: "Companies can implement their strategies in different ways. When assessing business models, market participants must be able to understand risks and opportunities of various business models, the related socially responsible actions and the relevance of corporate culture. This requires an intensified dialogue and an increasingly forward-looking, integrated reporting, but does not mean to just provide more information but other, new ways of disclosure. Expectations on members of the boards of directors in this regard are increasingly high and we see a substantial need for action."

Corporate governance and corporate social responsibility – Required integration

According to the surveyed companies, recent engagements focused primarily on the governance topics of "compensation" (26%), "strategy" (25%) and "board of directors" (23%). Only 6% stated that CSR, overall, remained an individual key topic in the investor dialogue. Consistent with SWIPRA's



holistic approach to corporate governance (see [SWIPRA Outlook AGM 2019 Season](#)), this indicates that non-Swiss shareholders, which largely shape these engagements do not consider CSR in isolation, but rather as integrated in the corporate governance framework, in particular in their assessment of the "corporate strategy", linked to the "composition of the board" and the "remuneration structures".

As a consequence, the integration of CSR into strategic objectives, remuneration structures and ultimately into the composition of the board of directors as well as the associated communication is becoming increasingly important. 54% of institutional investors consider the speed and quality of addressing CSR issues (such as compliance failures, environmental damage, incidents involving employees, etc.) suitable measures to evaluate board performance. The existence of a CSR framework and its integration into corporate strategy is also important to better assess the opportunities and risks of CSR as well as their potential influence on the development of corporate value. A majority (60%) of non-Swiss investors say that they use this for assessing the board. As a result, the performance of a board will, going forward, be increasingly evaluated based on how effectively corporate social responsibility is integrated with corporate objectives. Accordingly, shareholders will demand more transparency in this regard. This is consistent as it can be observed that companies that found themselves in such problematic situations tend to perform below-average over the longer term.

Investors are now even prepared to deviate from their long-time demanded focus on clearly defined, quantitative performance indicators in remuneration systems. Instead, they now increasingly call for the inclusion of qualitative CSR indicators. 79% of investors consider strategically relevant CSR goals important in the short-term bonus to foster a long-term sustainable business, although around 44% view this as giving the board greater discretion in determining variable remuneration. For the first time, the majority of investors (69%) expect qualitative targets, especially related to CSR, to not only have a negative impact on the short-term bonus (in the event of non-achievement or failures, but to also have a positive impact, analogous to financial KPIs, in the event of target (over)achievement. Investors are, therefore, looking to create incentives for CSR behavior as a basis to achieve long-term corporate goals.

Professor Alexander Wagner, Department of Banking and Finance, University of Zurich: "Research shows the increasing importance of CSR for investors, but most of these findings relate to the US market. The SWIPRA survey now provides us with a deeper insight into the Swiss market. CSR is no longer a niche or special topic in Switzerland but is seen as a central component of good corporate governance.."

Board of directors – Focus on responsibility and independence

As a consequence, investors become increasingly critical of the composition of boards of directors (see [SWIPRA outlook for the 2019 AGM season](#)). Only 19% of the investors believe that the boards of directors in Switzerland are acting diligently enough in the area of corporate social responsibility. And only 36% of institutional investors are satisfied with the disclosure of the composition and succession planning of the board of directors (2018: 37%).

Also, only 25% of asset managers consider the structures of Swiss boards to be appropriate to ensure independent decision-making. Two-thirds of investors are taking the view that chairpersons of board committees should, in principle, be independent from management and also from the Chairperson of the board to ensure objective decision-making. Further, a majority of investors believes that large information gaps between the Chairperson and the other members of the board of directors may impair the individual members' contribution.

Compensation – Pay for what?

The relationship between performance and bonus amount, "pay for performance", remains a critical issue in the disclosure of compensation. Only 13% of institutional shareholders are really satisfied with



the reporting on "pay for performance". Since current systems with a focus on financial performance indicators already seem very unclear from the investors' point of view, increased inclusion of qualitative, non-financial targets is likely to further increase complexity. CSR targets will hence increase the challenges and need improvements in the way disclosure and traceability of "pay for performance" is done.

AGM ballots – Diligent despite costs

There are still large differences in opinion on voting rights between Swiss and non-Swiss institutional shareholders. Just 38% of Swiss asset managers and only 11% of pension funds believe that benefits from exercising voting rights exceed the costs. Remarkably, 66% of non-Swiss asset managers take the opposite view. The majority of companies (65%) believe that their institutional shareholders exercise their voting rights with sufficient duty of care. This may be the result of the fact that shareholders having a regular dialogue with the companies are also those exercising their voting rights.

Anchor shareholder companies – Need for explanation

According to prior SWIPRA AGM analyses, minority shareholders tend to behave more critically than shareholders of companies with a broadly diversified shareholder base. The current survey provides possible reasons for this: 60% of investors believe that companies with an anchor shareholder have a lower quality governance disclosure. Access to the boards of directors in these companies also seems more difficult: only 21% of investors stated that they had sufficient access. In comparison, 42% of investors indicated that they had sufficient access to SLI[®] companies. The difference between Swiss and non-Swiss investors is striking: the former state to have better access to the Board of Directors than non-Swiss investors in smaller companies (outside the SLI[®]) and companies with an anchor shareholder.

The SWIPRA Corporate Governance Survey

In collaboration with a research team from the Department for Banking and Finance at the University of Zurich, headed by Dr. Christoph Wenk Bernasconi, all companies of the Swiss Performance Index SPI[®] as well as institutional investors from Switzerland and abroad were invited to participate in the seventh SWIPRA survey on corporate governance in Switzerland. During the survey period (August/September 2019), 78 Swiss companies listed on the Swiss Stock Exchange, representing around 78% of the SPI[®] market capitalization, and 77 institutional asset managers and asset owners from Switzerland and abroad took part. The participating investors, around 30% of whom are domiciled abroad, represent almost 30% of the equity investments managed worldwide and hold substantial stakes in Swiss companies. In addition, some institutions participated anonymously, whose size and relevance cannot be estimated.

A summary of the study's results can be downloaded using the following link: <http://swipra.ch/en/survey/>
Figures and data are available at presse@swipra.ch.

About SWIPRA Services

SWIPRA Services provides corporate governance services for listed companies and their boards of directors as well as for institutional investors. We work with our clients with the aim of increasing the value of the company in the long term, based on principles of value-based management and empirically relevant criteria. SWIPRA Services is exclusive partner of Morrow Sodali in Switzerland. www.swipra.ch

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