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Stakeholders Take Center Stage: Director Views on Priorities and Society

STANFORD BUSINESS GRADUATE SCHOOL OF

ROCK CENTER FOR CORPORATE GOVERNANCE STANFORD

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We are Diligent Institute

Diligent Institute provides publicly available, industry-leading research on global board governance. Today's increasingly dynamic world presents a dizzying array of economic opportunities and challenges. As companies navigate that environment, high-quality governance is more important than ever to ensure effective oversight, protect and create jobs, and positively impact the economy. The Institute equips board directors and corporate leadership teams at organisations around the globe with the information to make forward-looking decisions that leave a meaningful mark on the world.

Diligent Institute was founded in 2018 to offer a global perspective on the complex and disruptive board governance topics that directors and leadership teams are tackling today. The Institute serves as the global governance research arm of Diligent Corporation, the pioneer in modern governance. Diligent® empowers leaders to turn governance into a competitive advantage through unparalleled insight and highly secure, integrated Sofware-as-a-Service (SaaS) applications, helping organisations thrive and endure in today's complex, global landscape.

The Diligent Institute is solely funded by the Diligent Corporation and functions as a think tank and research arm.

Executive Summary

New research from the Diligent Institute and the Rock Center for Corporate Governance at Stanford University finds that corporate directors are not as shareholder-centric as commonly believed and that companies do not put the needs of shareholders significantly above the needs of their employees or society at large. Instead, directors pay considerable attention to important stakeholders - particularly their workforce - and take the interests of these groups into account as part of their long-term business planning.

While directors are largely satisfied with their environmental, sustainability and governance (ESG) related efforts, they do not believe the outside world understands or appreciates the work they do.

Directors recognise that tensions exist between shareholder and stakeholder interests. That said, most believe their companies successfully balance this tension.

In general, directors reject the view that their companies have a short-term investment horizon for running their businesses.

Recently, more than 180 CEOs in the Business Roundtable amended the association's *Statement on the Purpose of a Corporation* and for the first time embraced a commitment to address the interests of all stakeholders - not just shareholders.[1]

In the winter of 2019, the Diligent Institute and the Rock Center for Corporate Governance at Stanford University surveyed nearly 200 directors of public and private corporations globally to better understand how they balance shareholder and stakeholder needs.[2]

[1] See Business Roundtable press release, "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy that Serves All Americans,'" (August 19, 2019).

[2] This study is a companion survey to one conducted of 200 CEOs and CFOs by Stanford Graduate School of Business and the Rock Center for Corporate Governance at Stanford University in the spring of 2019, available at: https://www.gsb.stanford.edu/faculty-research/publications/2019-survey-shareholder-versus-stakeholder-interests.

Key Findings

HIGHLIGHTS FROM THE RESEARCH INCLUDE:

- **Stakeholder interests are vitally important and directors believe they are being met.** Corporate directors overwhelmingly (89%) believe it is important or very important for their company to consider the interests of non-shareholder stakeholders (such as employees, local communities and the general public) as they pursue their business objectives. Almost all directors (92%) are satisfied with the job their company does to meet the interests of these stakeholders.

- **Shareholder primacy is not the rule.** Most directors (77%) do not believe that shareholder interests are significantly more important than stakeholder interests; only a quarter (23%) believe shareholder interests are significantly more important. By contrast, a third (32%) believe shareholder interests are only slightly more important, another third (36%) believe shareholder and stakeholder interests are equally important, and a small minority (10%) believe stakeholder interests are more important than shareholders.

- **The general public is missing the story - or the story isn't being told well by companies.** Corporate directors do not believe they receive the recognition they deserve for their efforts. Only a slight majority (57 %) believe their most important stakeholders accurately understand the job their company does to meet their interests. This lack of public recognition extends to other constituents as well. Just over half (56%) of directors believe their largest institutional investors understand what their company does to meet shareholder interests; 27 per cent do not. Furthermore, only 18 per cent of directors think the media accurately understands what their company does to meet stakeholder needs, while 58 per cent do not.

- **Pressure to act is greater outside the U.S.** Companies domiciled outside the U.S. face greater pressure from external constituents to do more for stakeholders than U.S. companies. Over half (57%) of directors of APAC companies receive high or moderate pressure from advocacy groups. By comparison, only 30 per cent of U.S. directors say they receive high or moderate pressure from advocacy groups. The same holds true for pressure from investors. Sixty-four per cent of directors of APAC companies say they face pressure from their largest institutional investors to do more for stakeholders, while only 27 per cent of U.S. directors say this.

Key Findings - CONTINUED

- **Larry Fink has a more receptive audience abroad than in the U.S.** In recent years BlackRock CEO, Larry Fink, has sent letters to the CEOs of BlackRock's portfolio companies encouraging them to consider broad social interests as they pursue their business objectives. Directors of companies within and outside of the U.S. both report receiving this letter. Outside the U.S., directors are significantly more likely to agree with Larry Fink's ideas than inside the U.S. For example, almost all (94%) of APAC directors agree with Mr. Fink that "Society is increasingly looking to companies, both public and private, to address pressing social and economic issues," and 65 per cent say they are motivated by this statement to implement new initiatives address these issues. By contrast, only 81 per cent of U.S. directors agree with Mr. Fink's statement, and only 48 per cent are motivated by it to start new initiatives. Similarly, more APAC directors (79%) than U.S. directors (67%) agree with Mr. Fink that companies face pressure to "maximize short-term returns at the expense of long-term growth".

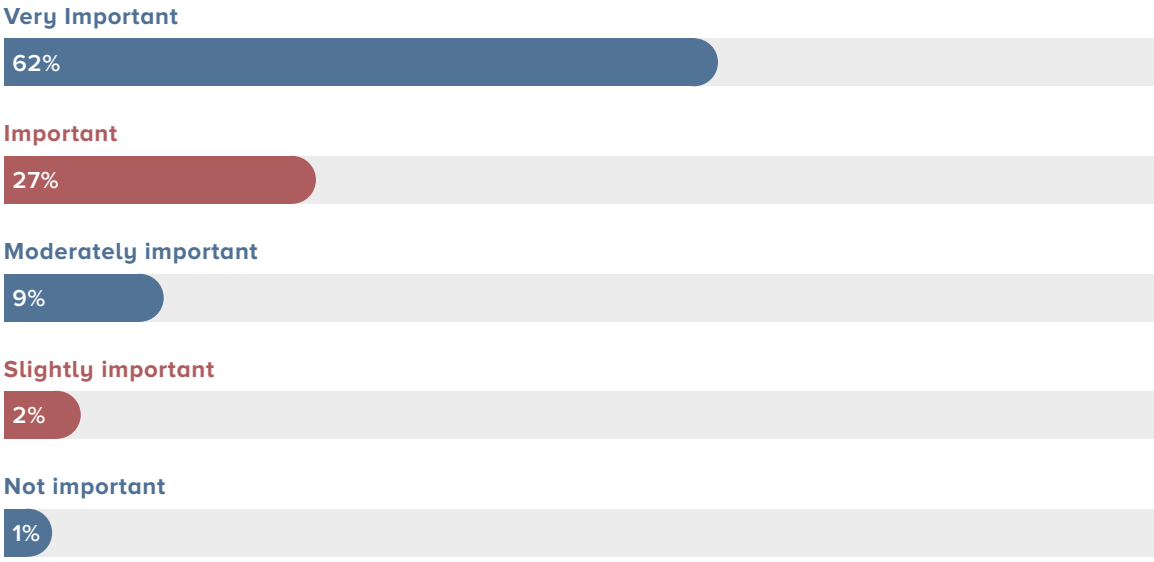
- **Directors reject the idea that their companies are short-term oriented.** Seventy-two per cent of respondents say their company predominantly considers an investment horizon of 3 or more years in managing the business. Twenty-five per cent of respondents adopt an investment horizon of 1 to 2 years. Practically none (4%) use an investment horizon of less than a year. Responses are similar for both U.S. and APAC directors.

- **The environment is directors' largest long-term worry.** Forty-one per cent of directors say that environmental issues including climate change, pollution, waste, or recycling are the single most important ESG-related issue that has the power to negatively impact their business over the long term. Other issues that are a top concern for directors are increased taxes and regulations (19%), macroeconomic factors that influence trade and the economy (18%), and workforce-related issues including the availability of employees, unionisation, and regulation (14%). Responses are largely similar between U.S. and APAC directors.

Survey Results

Shareholder vs. Stakeholder Interests in Business

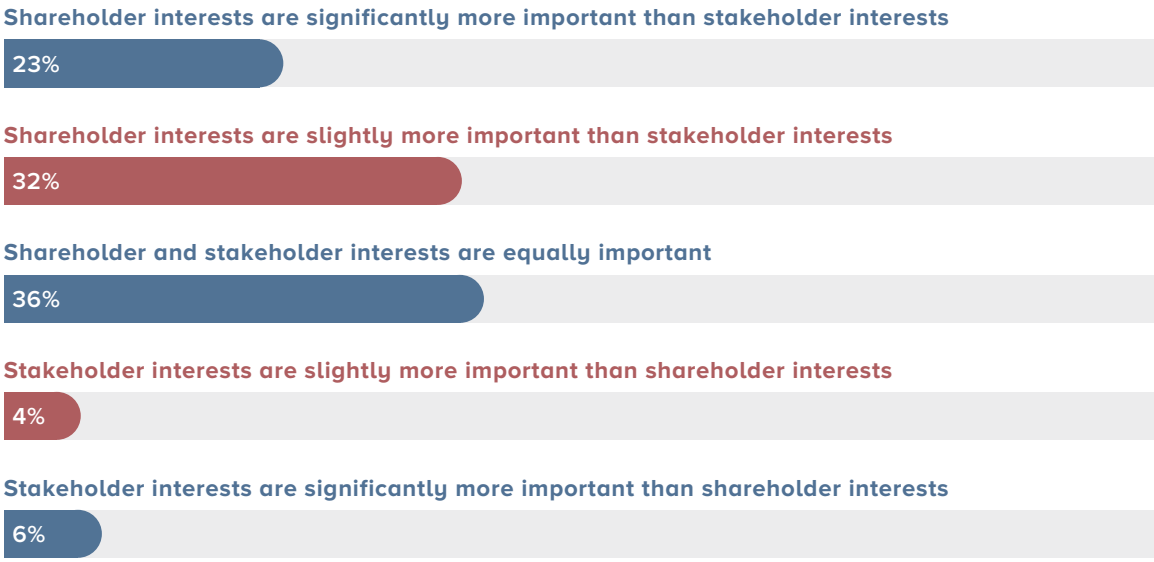
Generally speaking, how important is it that your company consider the interests of non-shareholder stakeholders (such as employees, local communities, the general public, etc.) as you pursue your business objectives?



> "Broadly, my role as an independent board member [involves] strategic oversight and management accountability. In each of those cases, we have to take into account many impacted parties [not just shareholders]."

Stakeholder Influence on Long-Range Plans

In general, how important are stakeholder interests relative to shareholder interests in the long-term management of your company?



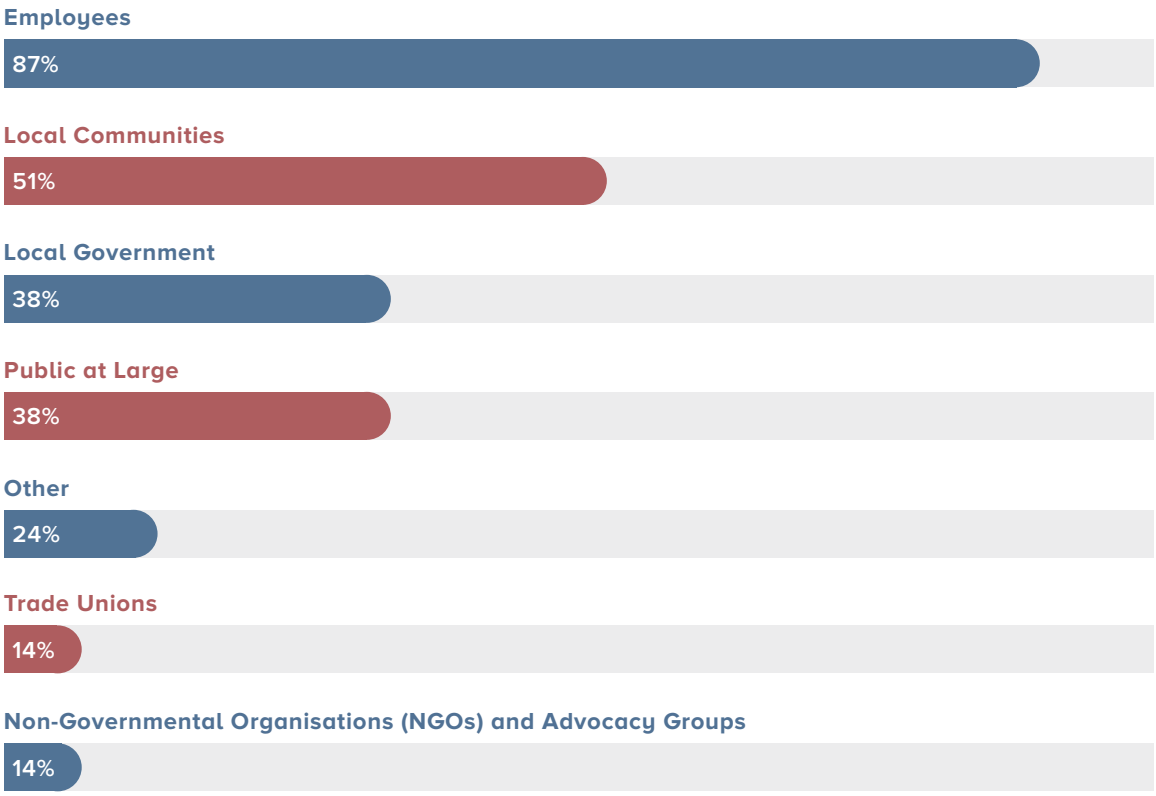
> "Our job as a board is to listen to the forces that are out there, but we have to stay true to the mission and vision of the company, the values of the company, and the strategy. If you keep your eye on those elements, then you can more mindfully balance the input from stakeholders."

> "You're constantly juggling both shareholders and stakeholders. Sometimes [their interests are] competing, sometimes [they are] complementary."

> "I want to hear what [stakeholder] concerns are. I want to hear with equal weight, but I may not act with equal weight. Our job is to decide, take input from all kinds of sources, and make sense of it."

Stakeholder Influence on Daily Operations

Which stakeholders play a key role in or are impacted by your company's daily operations and long-term strategy?



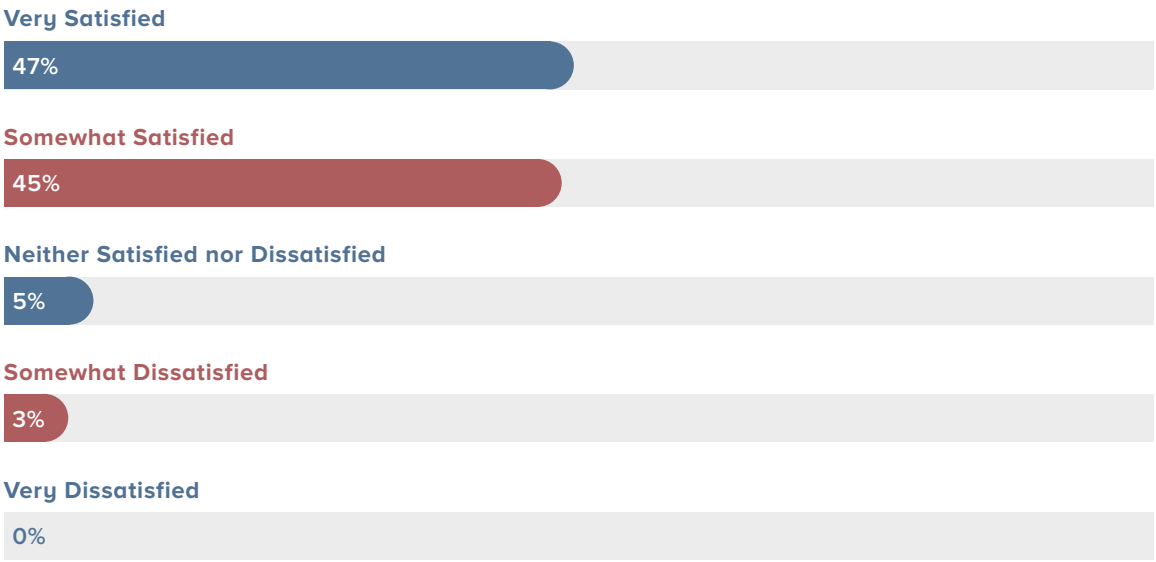
> "If you're not responding to the needs, wants, and interests of employees, I guarantee customers will suffer. They'll respond in way that are negative to the business, and your investors will suffer. This is an ecosystem that is interrelated."

> "If you treat your employees terribly, have a lousy culture, and are not competitive in compensation, how are you ever going to achieve shareholder returns?"

> The environment cannot speak itself, but there are NGOs and people who [speak on its behalf]. ... We treat the environment as effectively represented by those people... and monitor the environment as a stakeholder in the same way.

Meeting Stakeholder Interests

How satisfied are you with the job your company does to meet the interests of these stakeholders?

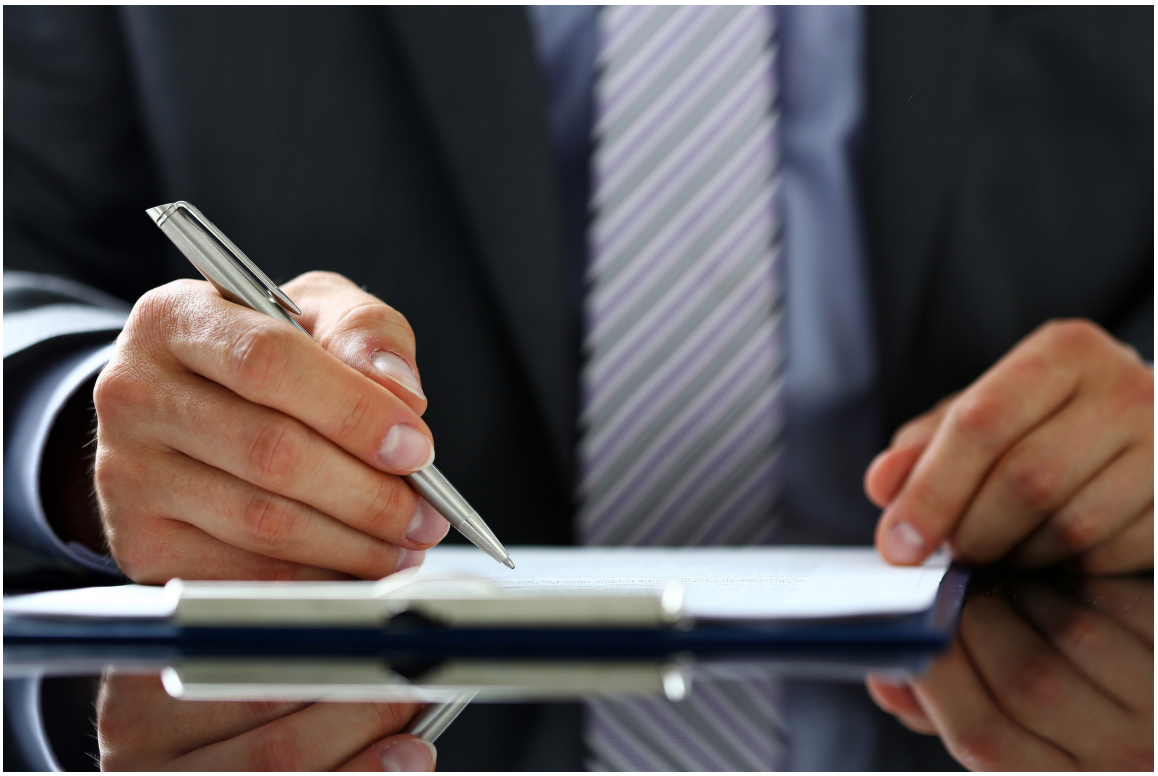


> "The idea of being a good corporate citizen has been in place [in our company] for a long time."

Financial Impact of Stakeholder Interests

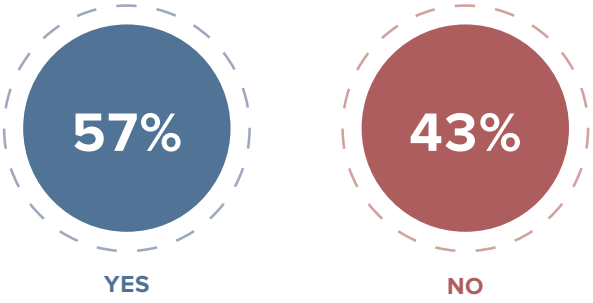
What is the financial impact to your company of meeting the interests of these stakeholders? (Respondents requested to select one answer for the short-term impact and one answer for the long-term impact.)

	LONG -TERM IMPACT		
SHORT-TERM IMPACT	HIGH OR MODERATE COST	LITTLE OR NO COST OR BENEFIT	HIGH OR MODERATE BENEFIT
High or moderate cost	37%	4%	12%
Little or no cost or benefit	5%	10%	5%
High or moderate benefit	0%	0%	28%



Understanding Stakeholder Interests

Do you believe these stakeholders accurately understand the job your company does to meet their interests?



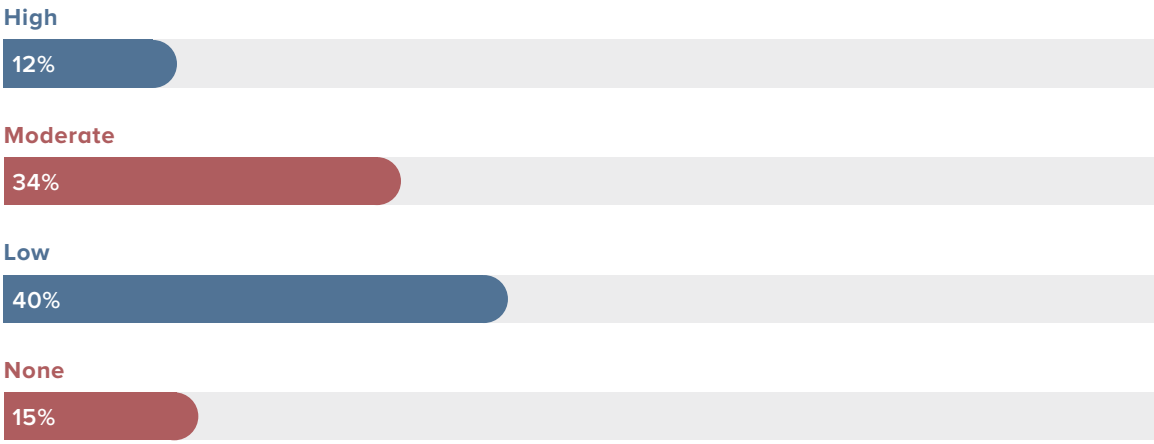
Do you believe the media accurately understands the job your company does to meet the interests of these stakeholders?

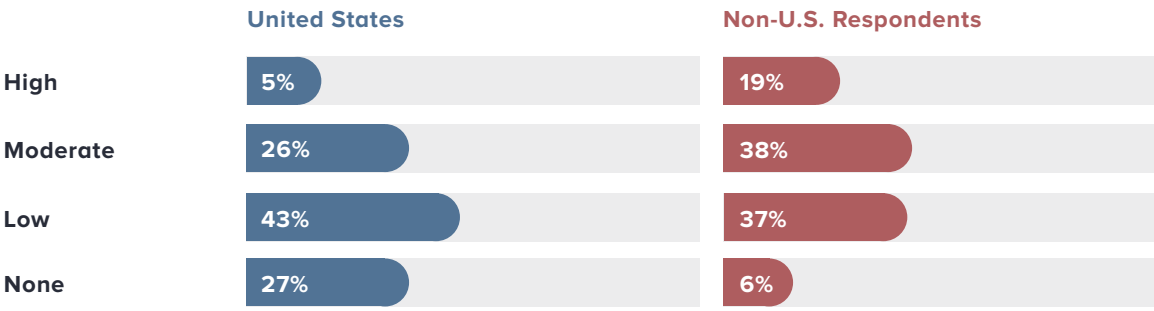
> "I think the media has overplayed this obsession with shareholders."

> "If we do our job communicating with our stakeholders... a more well-rounded perspective will emerge."

Pressure from Advocacy Groups

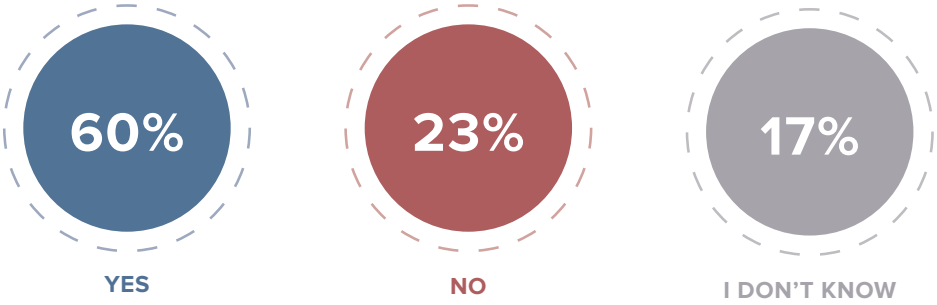
How much pressure does your company receive from advocacy groups to do more to meet the interests of these stakeholders?



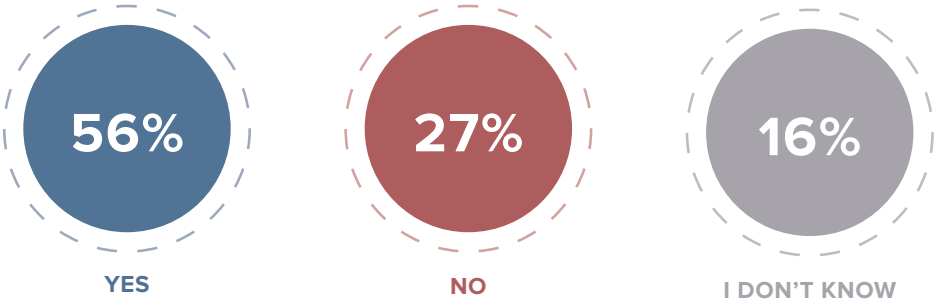


Pressure from Advocacy Groups

Do you believe that your largest institutional shareholders really care about the interests of these stakeholders?

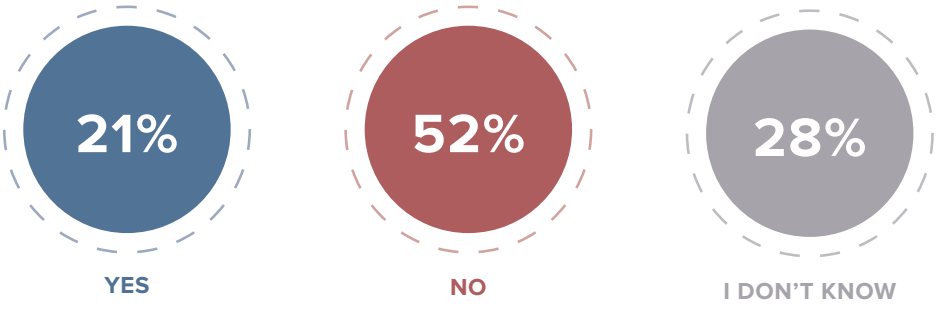


Do you believe that your largest institutional shareholders accurately understand the job your company does to meet the interests of these stakeholders?



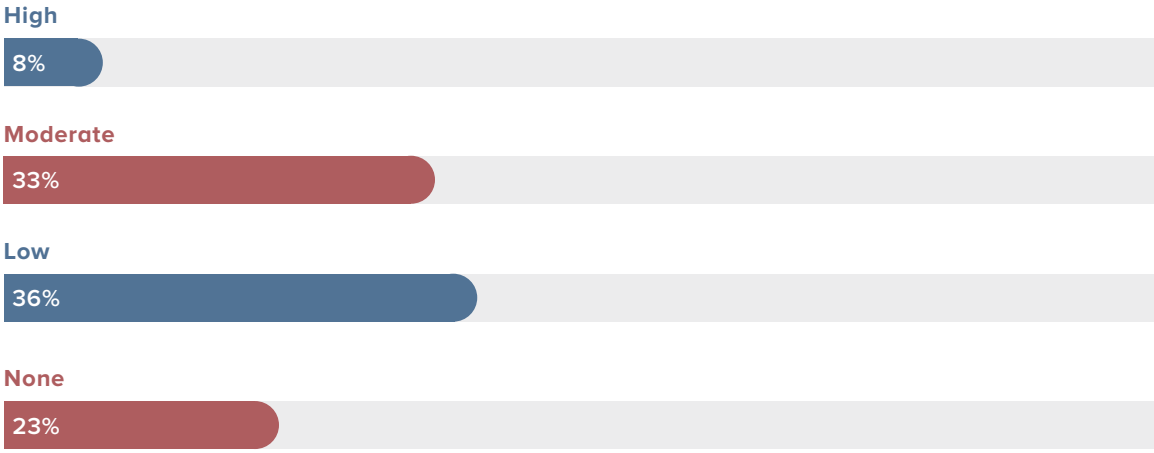
Alignment of Shareholder and Stakeholder Interests

Do your largest institutional shareholders believe that a conflict exists between their own interests and the interests of these stakeholders (i.e., do they believe that meeting the needs of these stakeholders comes at the cost of lower shareholder value)?



Pressure to Focus on Stakeholder Interests

How much pressure does your company receive from your largest institutional shareholders to meet the interests of stakeholders as you develop your long-term strategy?

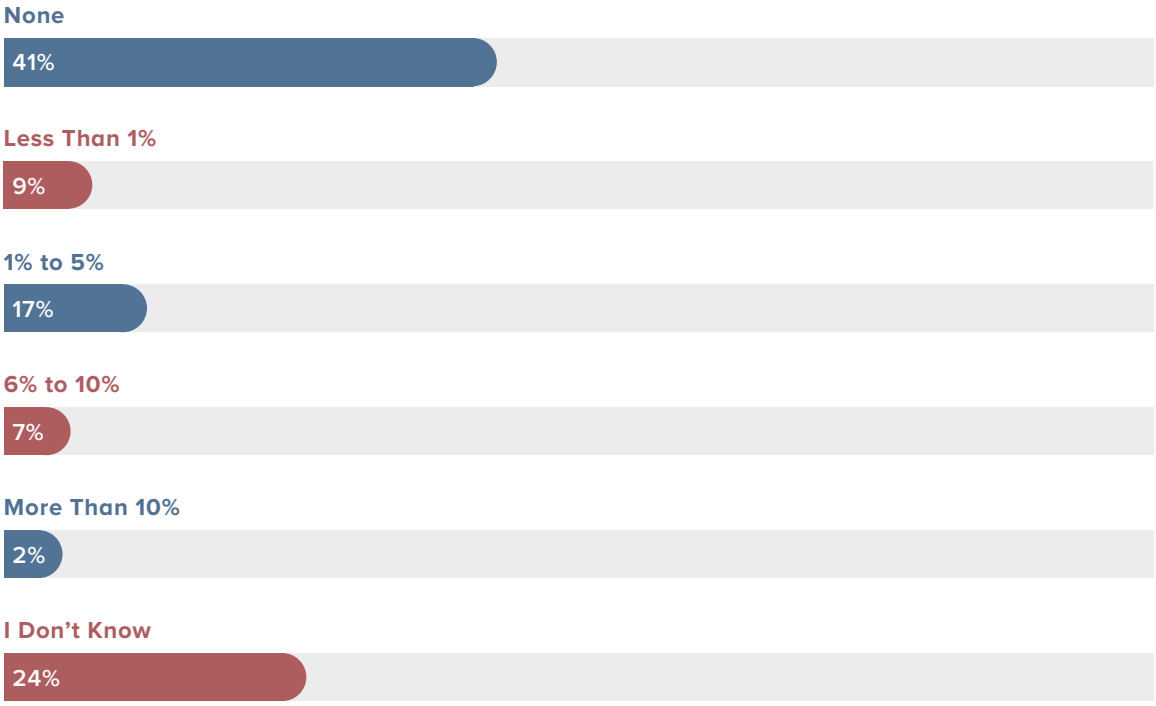


> "Pressure from institutional shareholders is valid. They represent a big piece of ownership. ... Still, they are not as close to the business as the management team and the board. So while their perspective is important, they shouldn't drive a decision that otherwise wouldn't be reached by management and the board."

> "The board is not under obligation to do what [shareholders] ask, but they are under obligation to listen, and they have the obligation to communicate. This is more of a two-way street than ever before."

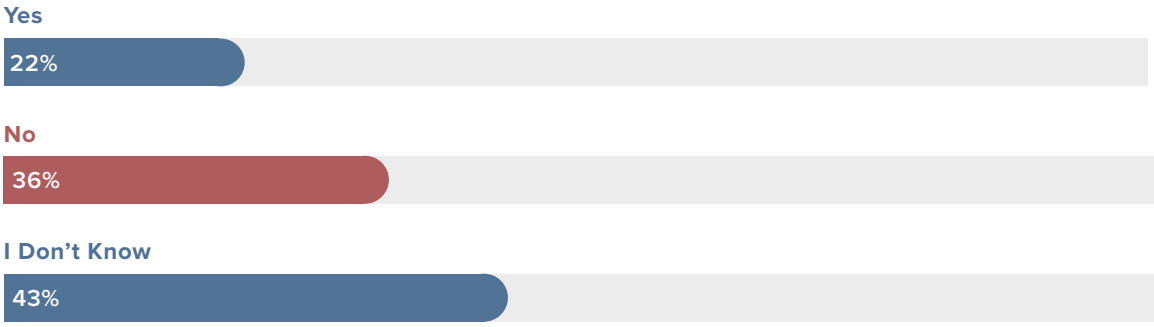
BlackRock's Impact

Approximately what percent of your company's publicly traded shares are owned by BlackRock?

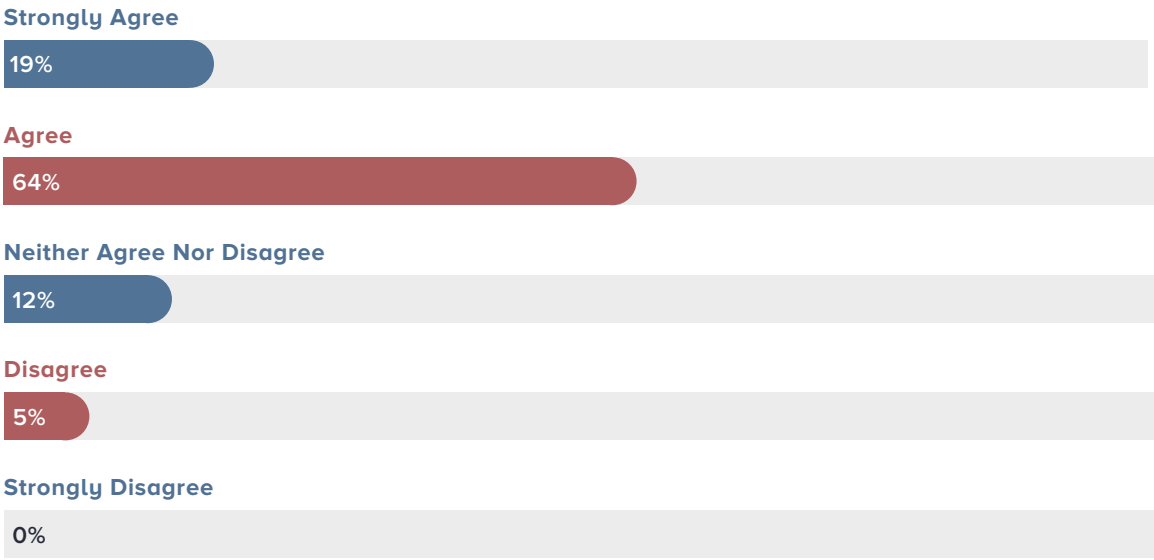


Larry Fink's Impact

In January 2019, BlackRock CEO, Larry Fink, sent a letter to all companies that BlackRock invests in, encouraging them to consider broad societal interests as they pursue their business objectives. Did your company receive this letter?

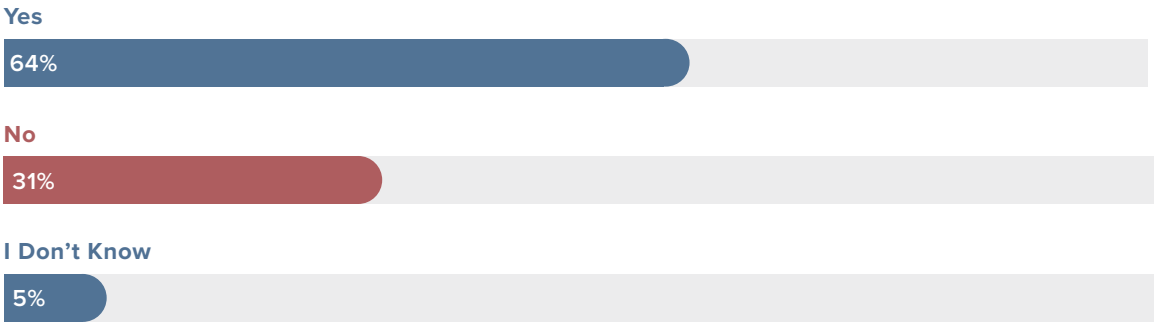


[If yes] Do you agree with these ideas expressed by Mr. Fink?

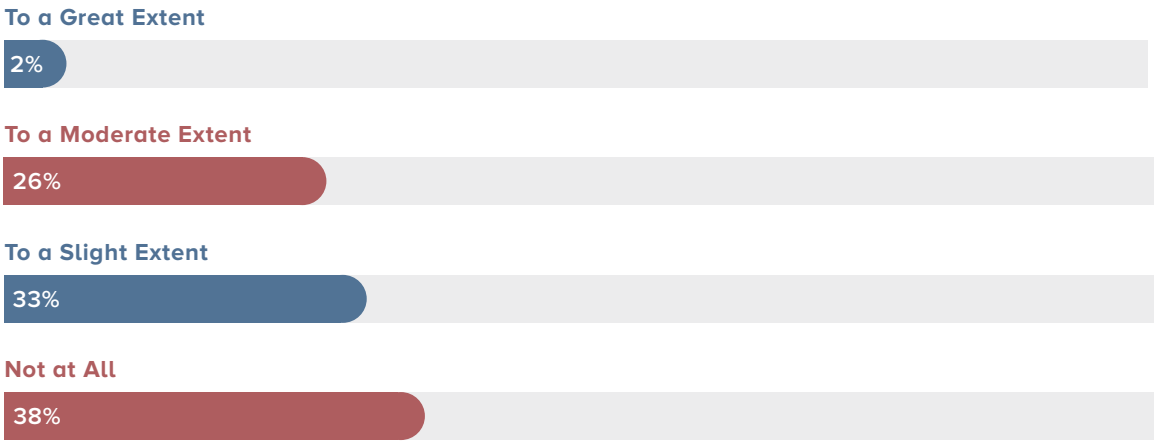


Larry Fink's Impact - CONTINUED

[If yes] Did the board discuss the ideas in this letter?

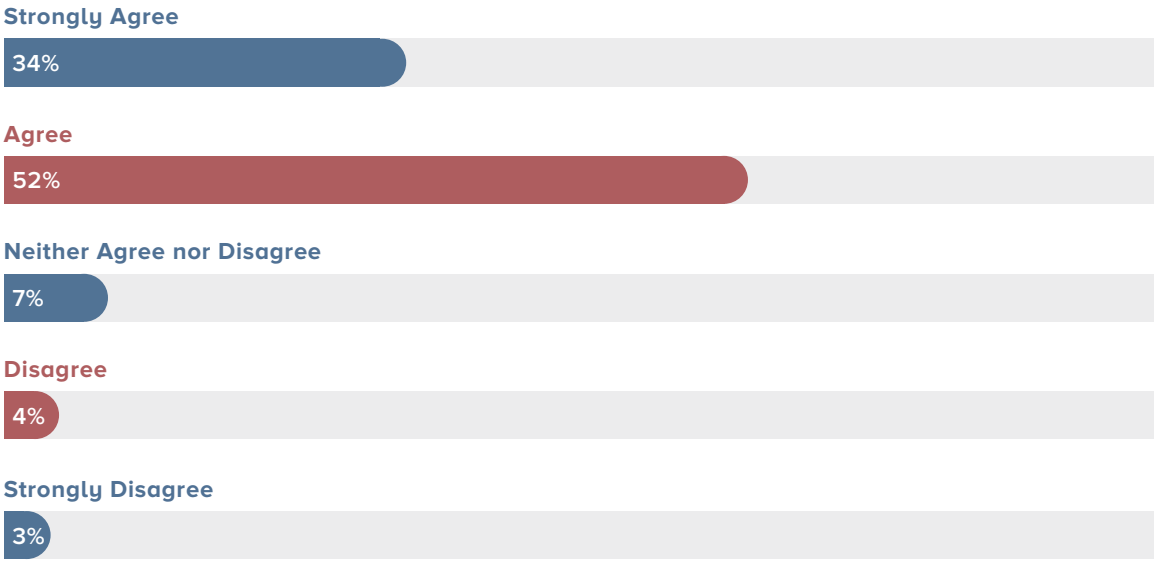


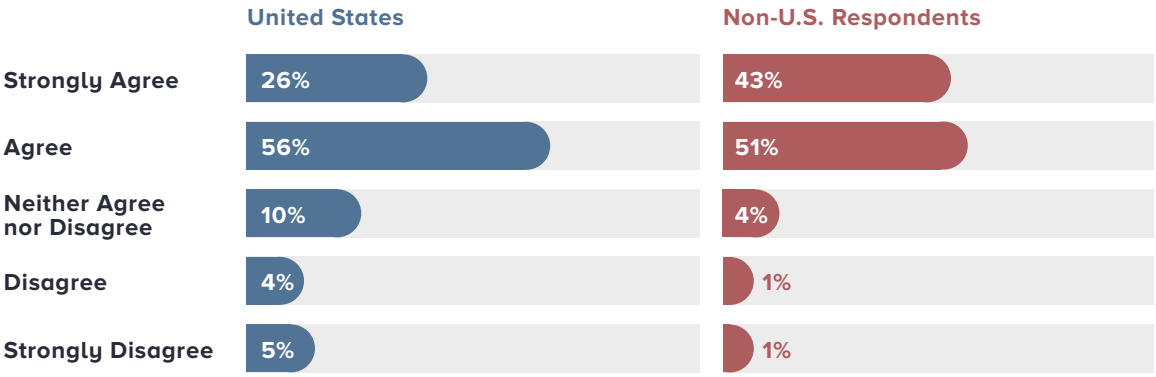
[If yes] To what extent did this letter motivate your company to evaluate or implement new initiatives to address one or more societal interests or more societal interests?



Social Issues and Corporate Strategy

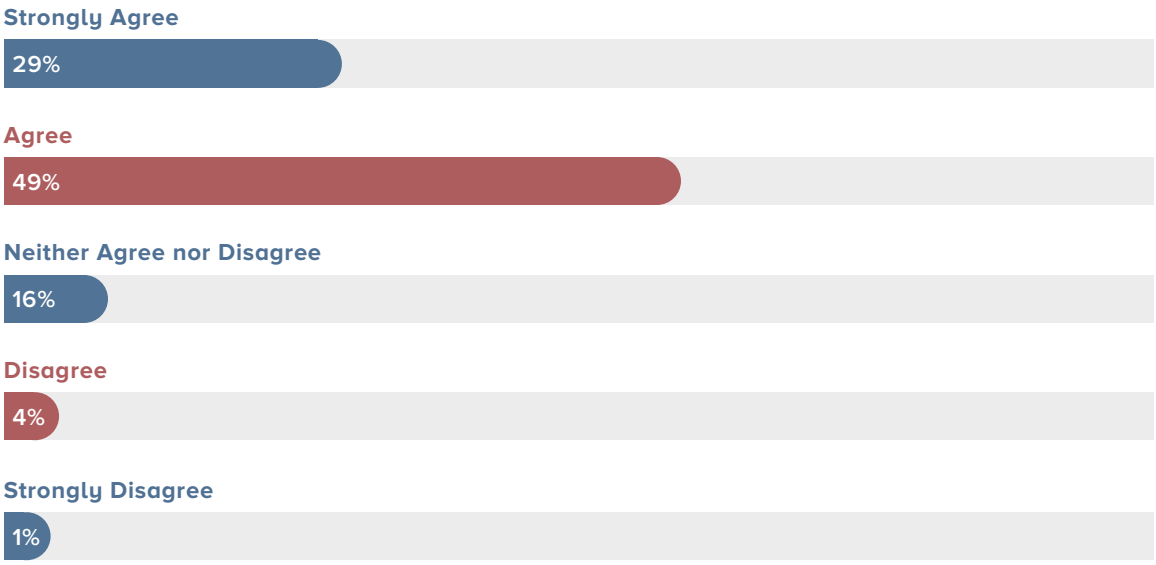
In the letter, Larry Fink writes that: "Society is increasingly looking to companies, both public and private, to address pressing social and economic issues. These issues range from protecting the environment to retirement to gender and racial inequality, among others." Do you agree with this statement?





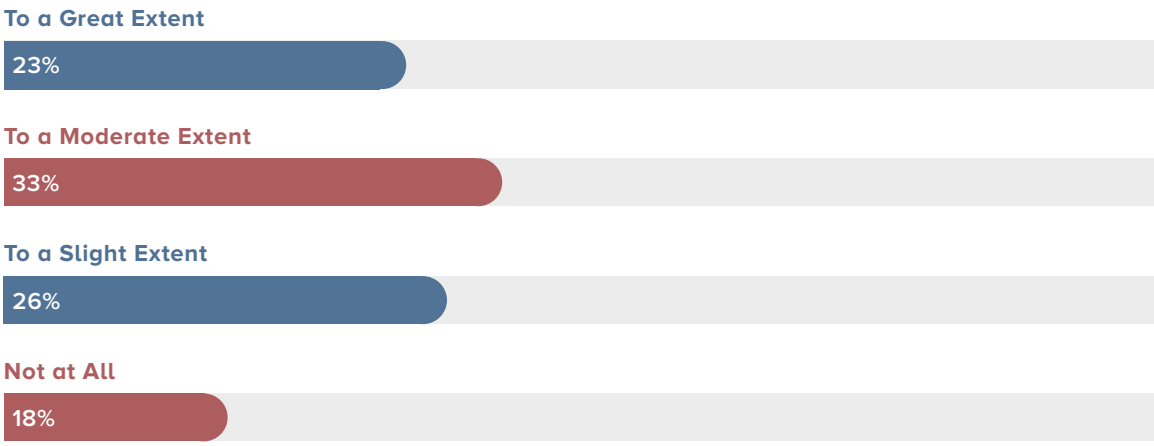
Corporate Obligations

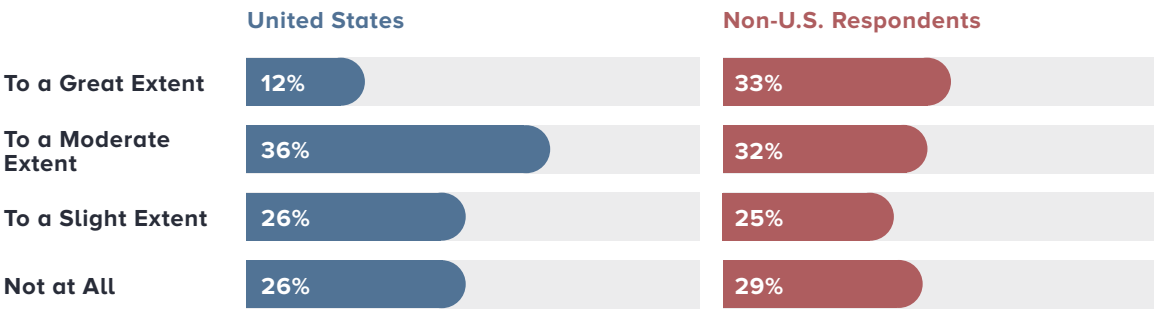
Do you agree that your company has an obligation to address these issues?



Corporate Obligations

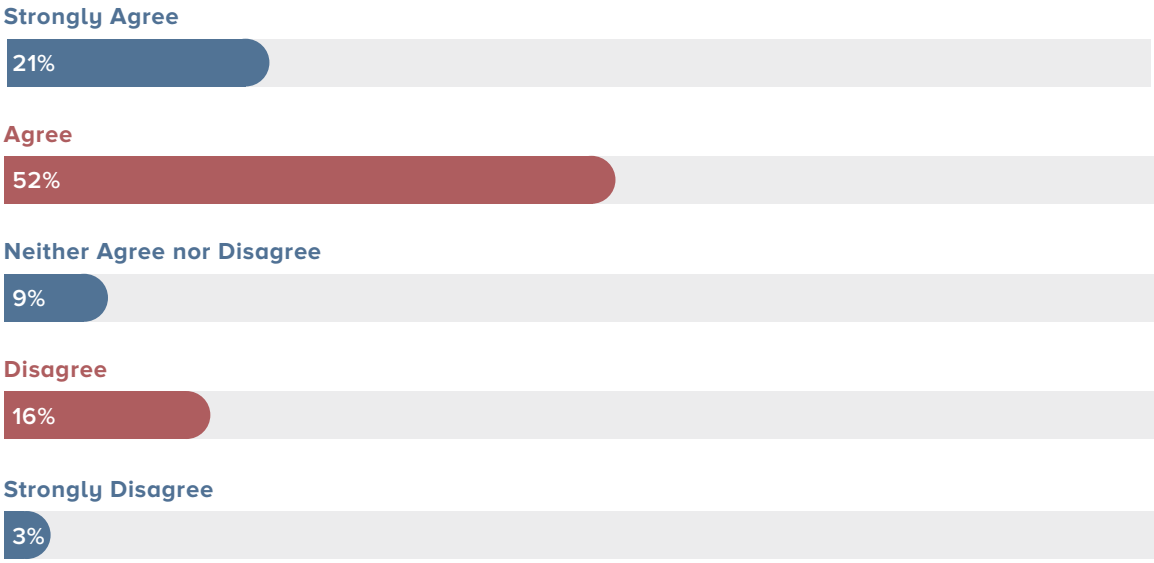
To what extent does this statement motivate you to evaluate or implement new initiatives to address a specific social or economic issue?

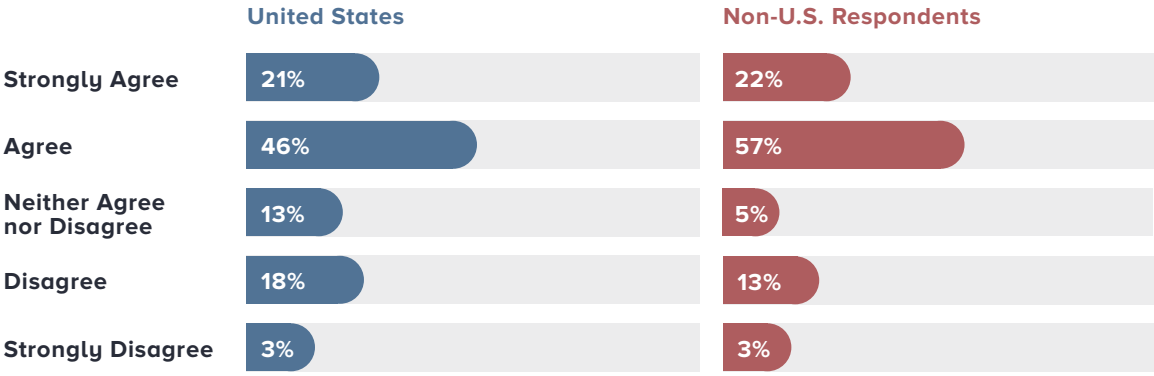




What Incentives Drive Strategy?

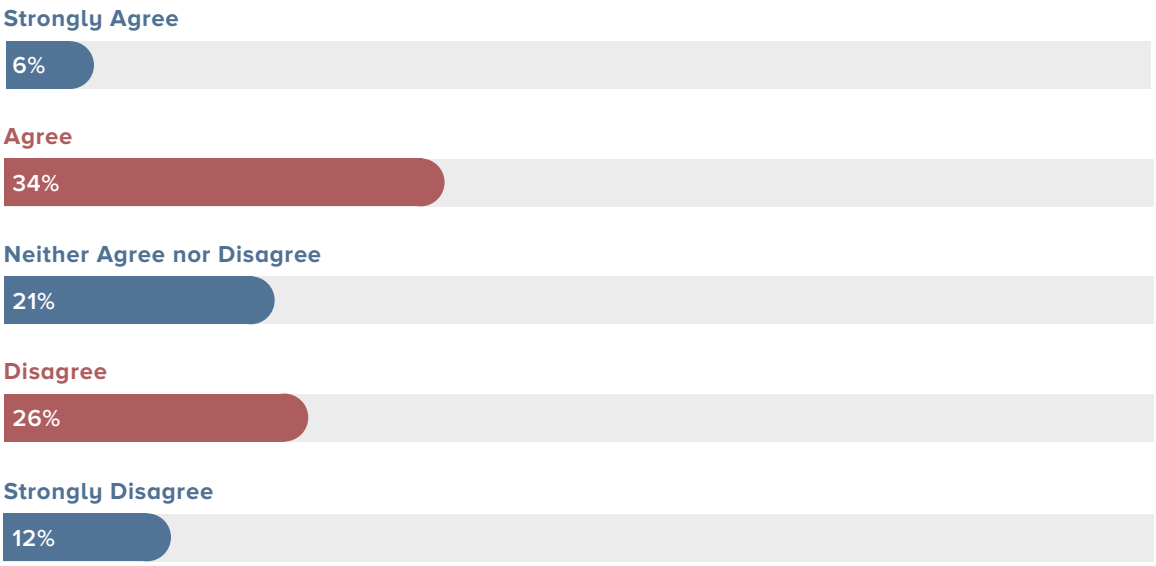
In his letter, Larry Fink also writes that: "Companies must navigate the complexities of a late-cycle financial environment including increased volatility which can create incentives to maximize short-term returns at the expense of long-term growth." Do you agree with this statement?





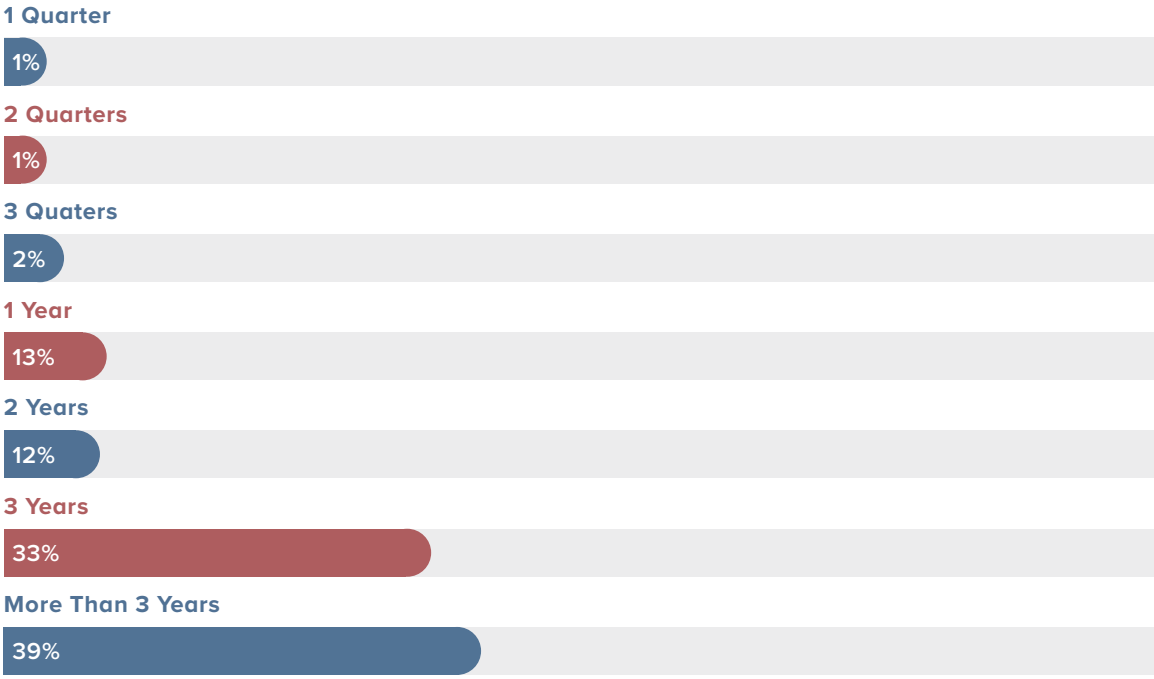
Incentives for Short-term vs. Long-term Growth

Do you agree that your company faces incentives to maximize short-term returns at the expense of long-term returns?



Investment Horizon

In your best estimation, what investment horizon does your senior management team predominantly consider in managing the company?



> "Investment horizon varies a lot by company, depending on where they are on the maturity curve, market influences, what the competitive landscape looks like. There may be times that a company rightfully should focused on the short term, but in general, they should be more focused on the long term."

> "Investing in business takes a few years to pay off. Anything strategic ... [requires] a three to four-year horizon."

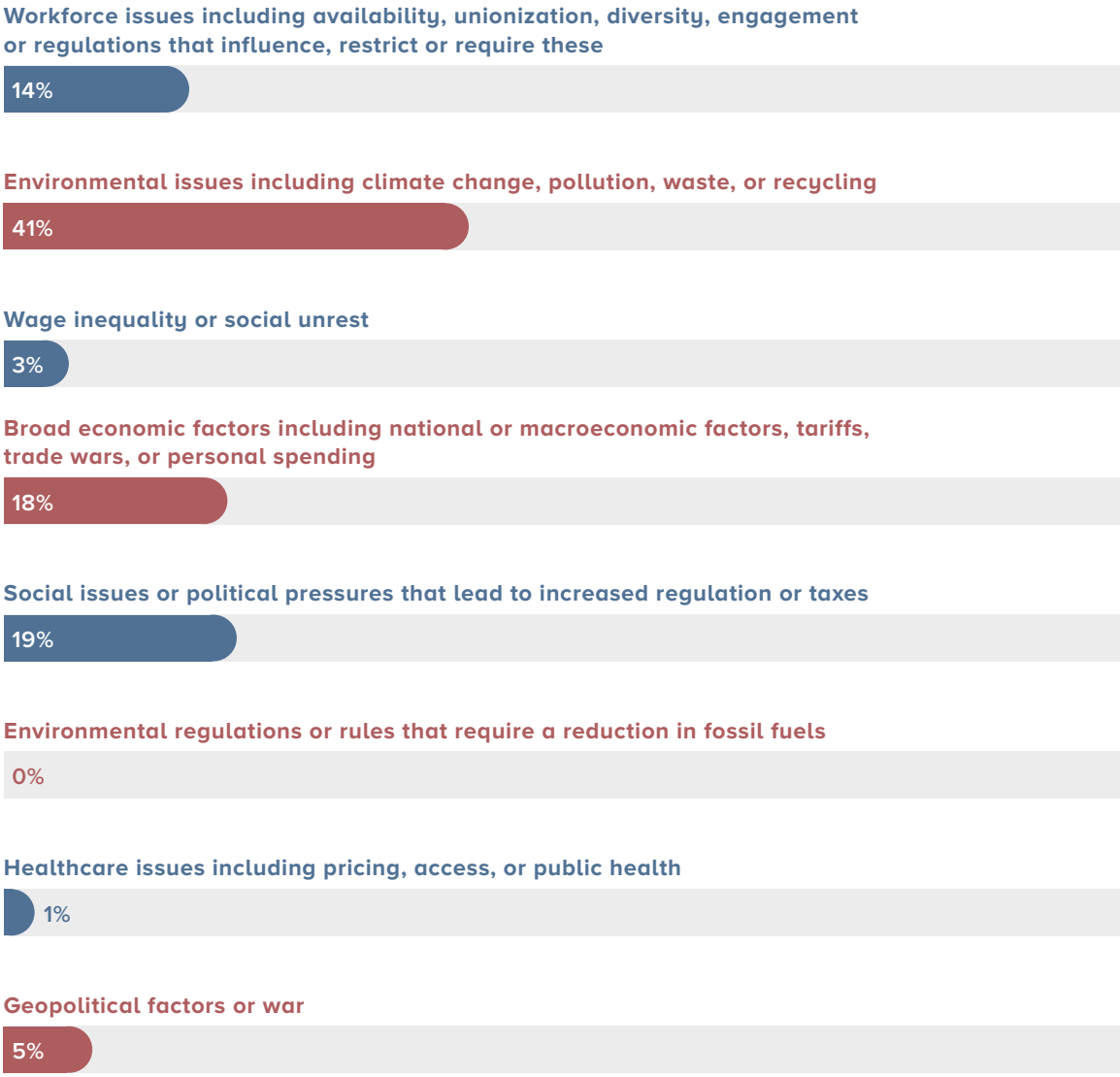
> "We are a company where quarters are important, but ... we are focused on how we drive long-term results while maintaining short-term success."

> "Shareholder return is not meaningfully measured quarter by quarter by quarter."

> "We are very much a long-term sustainable company. [We have] a brand that's been going well for [many] years. Our duty is to make sure it continues to go well."

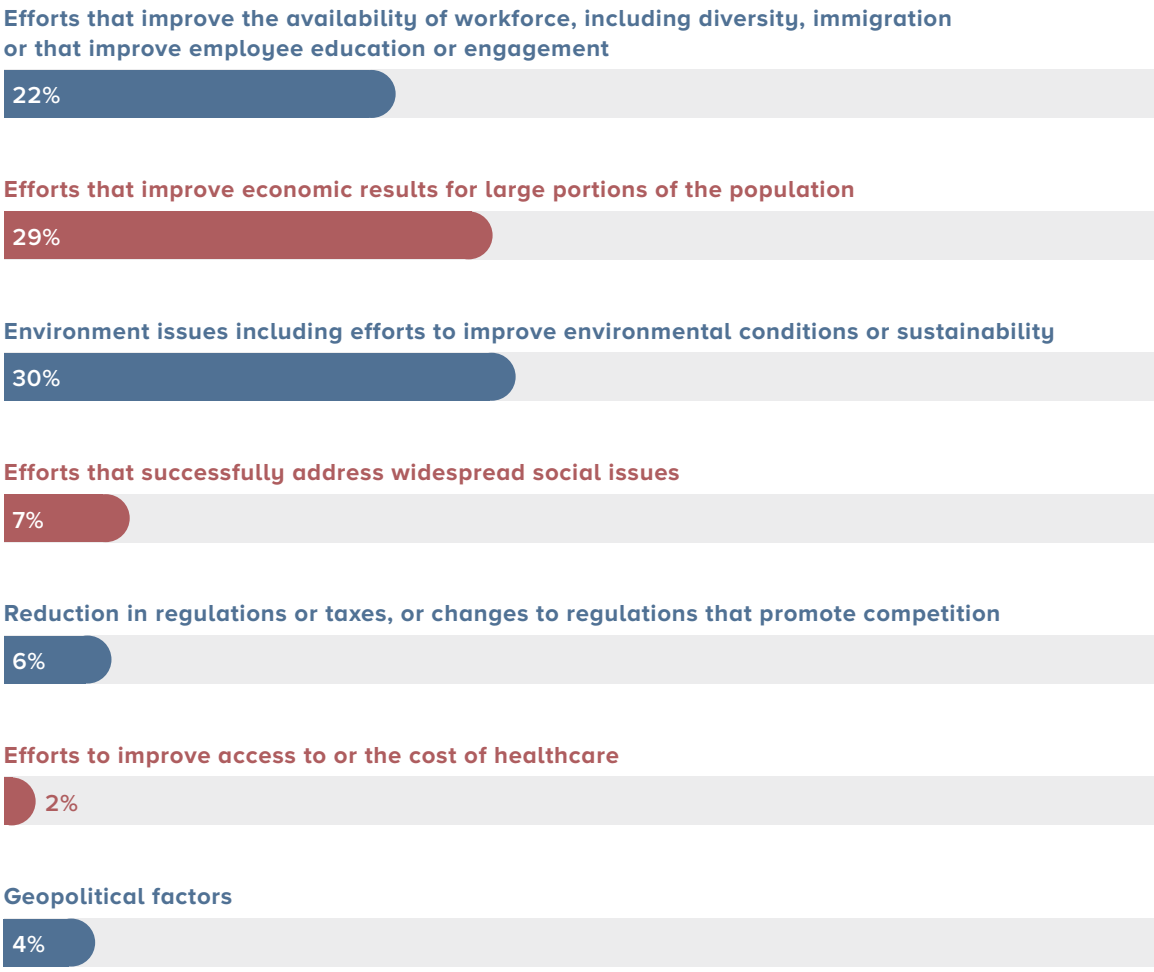
Most Pressing Issues

What is the single most important environmental or societal issue that has the power to negatively impact the performance of your company over the long-term? [unprompted]



Critical Issues Driving Performance

What is the single most important environmental or societal issue that has the power to positively impact the performance of your company over the long-term? [unprompted]



Respondent Information

WHAT IS YOUR TITLE? (SELECT ALL THAT APPLY)

Chairman of the board	11%
Chairman and CEO	2%
Lead independent director	10%
Outside board member	47%
Inside board member	9%
General counsel	6%
Management, not a board member	11%
Other	4%

WHAT IS THE PUBLIC LISTING STATUS OF YOUR COMPANY?

United States exchange listing	31%
Non-U.S. exchange listing	32%
Both U.S. and non-U.S. exchange listings	7%
Private, not publicly traded	29%

IF NON US WHERE IS YOUR COMPANY PRIMARILY LISTED?

Africa	13%
North America (outside the U.S.)	19%
South and Central America	0%
Asia Pacific	13%
Australia or New Zealand	34%
Europe	13%
Middle East	0%
Other, please specify:	9%

HOW CONCENTRATED IS THE OWNERSHIP OF YOUR COMPANY?

Ownership is widely dispersed (no single party has effective voting control)	55%
An investment group has a significant minority or majority voting interest	19%
A family or individual has a significant minority or majority voting interest	15%
Other, please specify:	11%

WHAT IS YOUR GENDER?

Male	73%
Female	27%

WHAT IS YOUR AGE?

Average	59

WHAT IS YOUR COMPANY'S REVENUE?

< $1 billion	53%
$1 billion to $10 billion	34%
$10 billion to $25 billion	8%
> $25 billion	5%

WHERE IS YOUR COMPANY DOMICILED?

United States	45%
Africa	8%
North America (outside the U.S.)	13%
South and Central America	1%
Asia Pacific	5%
Australia or New Zealand	15%
Europe	7%
Middle East	1%
Other, please specify:	5%

HOW MANY EMPLOYEES DOES YOUR ORGANISATION HAVE?

Up to 499	29%
500 - 999	16%
1,000 - 4,999	26%
5,000 - 19,999	18%
20,000 or more	11%

Respondent Information - CONTINUED

WHAT INDUSTRY IS YOUR COMPANY IN?

Business services	3%
Chemicals	6%
Commercial banking	4%
Commodities	2%
Communications	18%
Computer services	3%
Electronics	15%
Energy	3%
Financial services	5%
Food and tobacco	5%
Healthcare	3%
Industrial and transportation equipment	3%
Insurance	1%
Other manufacturing	2%
Other services	3%
Retail trade	1%
Technology	3%
Transportation	0%
Utilities	1%
Wholesale trade	4%
Other	16%

About the Authors

DAVID F. LARCKER

David F. Larcker is the James Irvin Miller Professor of Accounting at Stanford Graduate School of Business, director of the Corporate Governance Research Initiative, and senior faculty of the Arthur and Toni Rembe Rock Center for Corporate Governance. His research focuses on executive compensation and corporate governance. Professor Larcker presently serves on the Board of Trustees for Wells Fargo Advantage Funds. He is coauthor of the books A Real Look at Real World Corporate Governance and Corporate Governance Matters.

Email: dlarcker@stanford.edu
Twitter: @stanfordcorpgov
Full Bio: http://www.gsb.stanford.edu/faculty-research/faculty/david-f-larcker

DOTTIE SCHINDLINGER

Dottie Schindlinger is Vice President of Thought Leadership for Diligent, leading provider of board software used by over 650,000 directors and executives globally. A frequent presenter, her work has been featured in *Forbes, The Wall Street Journal, Corporate Board Member*, and *Corporate Secretary*. She co-authored the book, *Governance in the Digital Age: A Guide for the Modern Corporate Board Director*, and co-hosts *The Corporate Director Podcast*, an interview show featuring leading corporate directors. Dottie serves on the Advisory Board of the Diligent Institute and is Vice Chair of the Board of Alice Paul Institute. She is a graduate of University of Pennsylvania

Email: dschindlinger@diligent.com
Twitter: @govtechgeek

BRIAN TAYAN

Brian Tayan is a member of the Corporate Governance Research Initiative at Stanford Graduate School of Business. He has written broadly on the subject of corporate governance, including boards of directors, succession planning, compensation, financial accounting, and shareholder relations. He is coauthor with David Larcker of the books A Real Look at Real World Corporate Governance and Corporate Governance Matters.

Email: btayan@stanford.edu
Full Bio: http://www.gsb.stanford.edu/contact/brian-tayan

ANNIE KORS

Annie Kors is the Lead Researcher for Diligent Institute, the global think tank and research arm for Diligent Corporation. The Institute provides publicly available, industry-leading research on global board governance. She authored *Winds of Change: Environmental Sustainability Rises to the Board Level* and *Governing Through the Fog: Corporate Director Perspectives on Political Uncertainty*. Given Diligent's reach, the Institute's research is derived from real experience across sectors and geographies, utilizing quantitative surveys, case studies, and interviews with leading professionals.

Email: akors@diligent.com

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CONTACT

Diligent Institute
111 W 33rd St
16th Floor,
New York, NY
10001

Email: Diligentinstitute@diligent.com
URL: www.diligentinstitute.com