

Exploring the financial materiality of social factors

Author: Michael Lewis



IN A NUTSHELL

- Covid-19 has led many types of inequalities to widen over the past year with implications for economic growth, investment returns, government policies and meeting the Sustainable Development Goals (SDGs)
- Asset managers have a range of options to address the financial materiality of social issues. Norms-based screens can help avoid the financial risk of laggard companies or seek to profit from companies with strong practices
- Engagement can encourage investee companies and governments to help improve equality and avoid social harm. This can be particularly effective if done through coalitions such as the "Just Transition". Private debt and equity impact investments can enhance equality by creating agricultural jobs in Africa or improving financial inclusion
- If companies fail to respect the principles and guidelines of social norm conventions and protocols such as paying a decent wage or dealing fairly with suppliers, then ultimately they risk losing their social license to operate

1 / Summary

In this paper, we examine the social factors that pertain to companies and why this is attracting increasing attention among institutional investors. Indeed, in a report¹ by CREATE-Research and DWS published last month it found that 59% of investors polled cited Covid-19 as a key driver of their heightened interest in the Social pillar because of its growing materiality. As well, 66% of investors polled regard employees as financially the most material component of the "S" pillar. The fact that social bond issuance increased tenfold last year compared to 2019 provides further evidence of the rising importance of social factors from a financial perspective².

These latest observations reinforce the findings of a number of DWS white papers we have published over the past few years which have examined the materiality of social issues on corporate financial performance (CFP), how corporate reputation has one of the strongest correlations to CFP, why shareholder primacy is being rejected in favour of stakeholder-centric capitalism and how integrating social factors into investment portfolios can deliver secondary market exposures³.

¹ CREATE-Research, DWS (May 2021). Passive Investing 2021: Rise of the social pillar of ESG

² Climate Bonds Initiative (April 2021). Global State of the Market Report

³ DWS Research Institute (December 2015). ESG and corporate financial performance; DWS Research Institute (September 2018). ESG and CFP: Digging deeper; DWS Research Institute (September 2020). Stockholder versus stakeholder; DWS Investment Insights (November 2020). Spotlight on 'S' - Integrating the social factor into investment portfolios

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Yet when it comes to globalisation, digitalisation and the associated productivity gains, these have been increasingly accruing to the owners of capital rather than labour. Left unchecked, a focus on shareholder value to the exclusion of all else holds risks since the pandemic has triggered an even greater examination of the support mechanisms companies are providing to their employees, contractors and customers and how this affects company performance.

This paper is organised in three sections. The first provides an overview of the financial materiality of social factors and the guiding principles companies need to consider. The second section focuses on the double materiality of how widening social disparities, aggravated by the pandemic, affect economic growth and the SDGs, while the final section assesses how asset managers need to respond when it comes to their investment approach and what role other actors, such as regulators and standard setters, need to play to advance this growing area of ESG investing.

Section I: Guiding principles and the financial materiality of social factors

A global survey released at Davos in January 2020, found that 56% of people believe that capitalism, as it exists today, does more harm than good in the world⁴. The survey also found that trust in companies can be strengthened if these entities contribute to communities, deal fairly with suppliers, pay a decent wage and partner with external organizations and governments on key issues. If they don't, companies risk losing their social license to operate. This is particularly relevant given the ongoing Covid-19 crisis since it has increased inequalities between and within countries and according to income, gender, race and age with implications for growth as well as social and political stability.

While the classification of environmental taxonomies are based on science, many of the guidelines and responsibilities on states and businesses in the area of social issues are more qualitative, based on agreed upon norms and rights and are typically encompassed in the following principles and protocols:

1. **International Bill of Human Rights**⁵ (1976) which has at its core promoting fundamental freedoms for all without distinction as to race, sex, language or religion
2. **OECD Guidelines for Multinational Enterprises** (1976) provide voluntary principles and standards for responsible business conduct in areas such as environmental protection, marketing such that consumer interests are respected, abiding by the letter and spirit of tax laws, combatting bribery, promoting supply chain responsibility and the disclosure of all material matters
3. **ILO Declaration on Fundamental Principles and Rights at Work** (1988) commits member states to respect and promote in four areas: freedom of association and the effective recognition of the right to collective bargaining; the elimination of forced or compulsory labour; the abolition of child labour and the elimination of discrimination in respect of employment and occupation
4. **UN Global Compact** (2000) which calls on companies to align strategies and operations with universal principles on human rights, labour, environmental and anti-corruption, and take actions that advance societal goals
5. **UN Guiding Principles on Business and Human Rights** (2011) which includes business enterprises preventing or mitigating adverse human rights impacts that are directly linked to their operations, products or services including their business relationships, such as supply chains, even if they have not contributed to those impacts

From a company perspective, a distinction could be made between “social CSR” and human capital management. The former can be considered as the way in which a company interacts with the outside world in the area of environmental management, responsible sourcing and community relief funds and the latter how a company invests in its employees through human capital management, often an important part of a company's intangible assets.

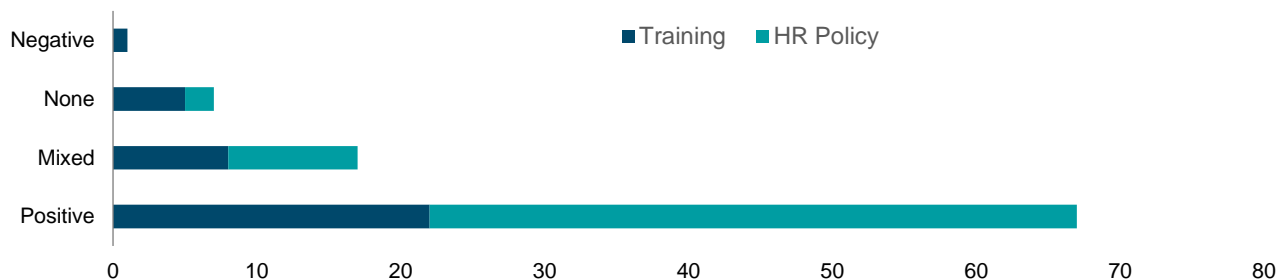
Human capital research has been undertaken in a multitude of disciplines for example in the fields of economics, labour studies, human resource management, psychology and sociology, but investment outcomes have been a focus only in a

⁴ The 2020 Edelman Trust Barometer (January 2020)

⁵ The Universal Declaration of Human Rights was adopted in 1948. Together with the two Covenants on Civil and Political Rights and on Economic, Social and Cultural Rights, these form the International Bill of Human Rights. The two Covenants came into force 1976

minority of them. For example, a 2015 research paper⁶ titled “The Materiality of Human Capital to Corporate Financial Performance” identified 92 studies that assess one or more of the traditional investment outcomes, 36 specifically on training and 56 on HR systems more generally. The financial metrics included total shareholder return, return on assets, return on earnings, return on investment, return on capital employed, profitability and Tobin’s Q. This research addressed a common misunderstanding that the materiality of ESG factors in general, and human capital in particular, is not yet backed up by research pertinent to mainstream investors. Although there is sparse evidence of such materiality for numerous social factors, the research offered compelling evidence of the correlation to financial outcomes for training and HR policies more generally, Figure 1.

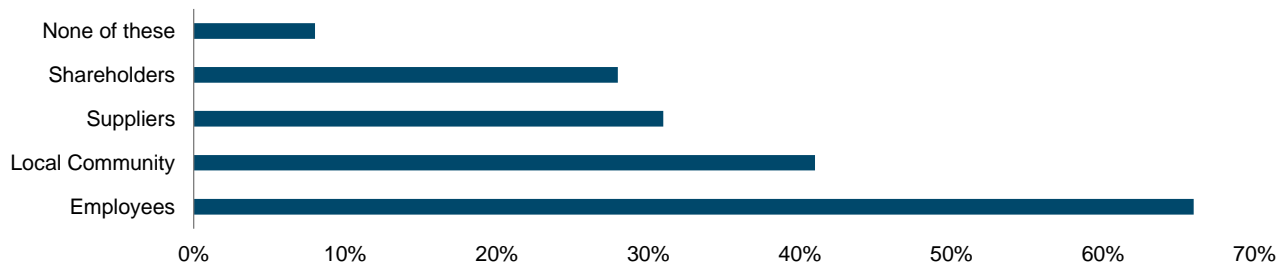
FIGURE 1: A LARGE NUMBER OF REPORTS ON HUMAN CAPITAL SHOWS A POSITIVE LINK TO FINANCIAL PERFORMANCE



Source: DWS Research Institute, Investor Responsibility Research Center Institute (April 2015) –92 studies assessed in all

Clearly, the key story behind Figure 1 is not lost on investors, as illustrated in the *CREATE-Research survey*, where 66% of those polled regarded employees as financially the most material component of the “S” pillar. Perhaps surprising to some was that shareholders ranked behind employees, local community and suppliers but, in our view, it simply reinforces the notion that shareholder primacy has been rejected in favour of stakeholder-centric capitalism.

FIGURE 2: INVESTOR SURVEY SHOWS THAT WELL-BEING OF EMPLOYEES IS SEEN AS THE MOST FINANCIALLY MATERIAL SOCIAL FACTOR*



* The survey reflects responses from 142 pension plans in 17 jurisdictions with collective Assets under Management of EUR 2.1 trillion to the question “Which of the four key clusters covered by the social factor do you regard as financially material to investment returns?”
 Source: CREATE-Research Survey 2021, DWS Investment GmbH (May 2021)

Despite research pointing to the materiality of human capital policies to investment performance, information about such policies has not become a staple of corporate reporting. This leads one to ask: “Why do we not see more reporting of human capital information in public annual reports?” Thankfully, the regulators are paying attention to the aspect for human capital management being reported separately in annual reports. For example, the SEC⁷ recently mandated publicly listed U.S. companies to include human capital resources disclosure for Form 10-Q quarterly and Form 10-K annual reports and registration statements. The SEC’s action reflected a move to a “principles-based” approach tailored to each individual company, rather than a mandated set of disclosures. The final rules added a new requirement that a company disclose,

⁶ The research was funded by the Investor Responsibility Research Center Institute (IRRCi) and co-authored by Larry Beeferman and Aaron Bernstein with the Labor and Worklife Program at Harvard Law School (April 2015)

⁷ SEC (August 2020). Modernization of Regulation S-K Items 101, 103, and 105

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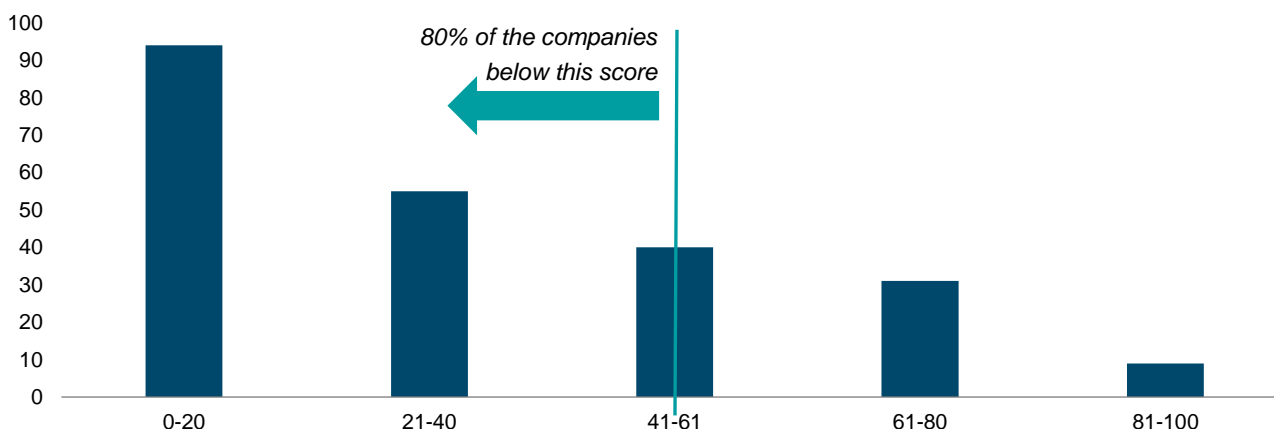
when material to an understanding of the business, a description of its 1) human capital resources, and 2) any human capital measures or objectives that are a focus of managing the business. Approximately 26% of companies in the MSCI USA Investment Market Index (IMI) reported racial and ethnic data as of February 2021, but, MSCI estimates that there were at least 70 variations of workforce demographic categories⁸.

A rather more targeted stance appears to be undertaken in Germany, where the Supply Chain Act was passed by the German Bundestag in June 2021, and which will come into force in January 2023. To ensure compliance with minimum social standards, companies will have to have a risk profile for each supplier and report annually on potential risks in their supply chain as well as the countermeasures they have put in place. Non-compliance could result in large fines⁹. At an EU level, work has been underway in the development of a social taxonomy to complement the bloc’s environmental classification system. This taxonomy will examine the relevant social metrics around employee, consumer and community rights and protection. More details of this approach will be published by the European Commission during the third quarter of 2021.

As we wait for improved human capital resources disclosure, the work of the World Benchmarking Alliance (WBA) sheds light on how leading companies are performing on various attributes related to human rights, decent work and ethical conduct. The WBA mission is to measure and incentivize businesses towards a sustainable future that works for everyone. In a sense, it is a private sector roadmap in delivering the UN Sustainable Development Goals. Of the three pillars mentioned above, the WBA’s 2020 Corporate Human Rights Benchmark assesses the human rights disclosures of 229 global companies across five sectors identified as presenting a high risk of negative human rights impacts. These are in the agricultural products, apparel, automotive manufacturing, extractives and Information and Communication Technology (ICT) manufacturing sectors.

The worrying parts of the WBA’s study are that a minority of companies demonstrate the willingness and commitment to take human rights seriously and secondly the disconnect between commitments and processes on the one hand and actual performance and results on the other¹⁰. The study points out that in March last year, 176 international investors representing US\$ 4.5 trillion in assets under management sent a letter to the 95 companies that failed to score any points on the human rights due diligence indicators, calling for urgent improvement. Since then only 16 companies have improved their due diligence when it comes to human rights.

FIGURE 3: VERY FEW COMPANIES HAVE STRONG SCORES ON THE HUMANS RIGHTS BENCHMARK



Companies are scored from 0 (lowest) to 100 (highest) according to six measurement themes. These cover companies’ human rights related policy commitments and governance, their systems and processes for implementing those policy commitments, their performance in relation to specific practices and responses to allegations of impacts, and their overall transparency.
 Source: DWS Research Institute, World Benchmarking Alliance’s Corporate Human Rights Benchmark (2020) Findings – covers 229 companies

⁸ Cited in HSBC (June 2021). Racial Diversity

⁹ Linklaters (June 2021). German Parliament passes Supply Due Diligence Act

¹⁰ World Benchmarking Alliance (November 2020). Corporate Human Rights Benchmark across sector

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From an individual sector perspective, the average score for automotive companies was 12%, which was consequently the worst performing sector, Figure 4. Two thirds of the companies scored 0 across all human rights due diligence indicators. These poor results suggest implementation of the United Nations Guiding Principles on Business and Human Rights is weak across the sector. While a granular examination of the WBA's study is beyond the scope of this paper, their findings underline the need for urgent attention required with regard to the social pillar of sustainability, especially in the backdrop of the COVID-19 crisis. For example, decisions made to chase low-cost labour have led to long and highly complex supply chains where the producers of goods are often located nowhere near the end users. Across different industries, supply chains have become multi-tiered and contractors have increasingly outsourced to subcontractors, which have made traceability problematic. And audits have failed to stem social and environmental abuses such as the incidence of forced labour, excessive working hours or health and safety¹¹. This is naturally an important area for investors from a company engagement perspective, which we examine in Section III of this report.

FIGURE 4: AMONGST FIVE KEY SECTORS, THE AUTOMOTIVE SECTOR HAS THE WORST AVERAGE HUMAN RIGHTS ASSESSMENT



Source: DWS Research Institute, World Benchmarking Alliance's Corporate Human Rights Benchmark (2020) Findings – covers 229 companies

¹¹ Harvard Business Review (May 2021). Overselling Sustainability Reporting

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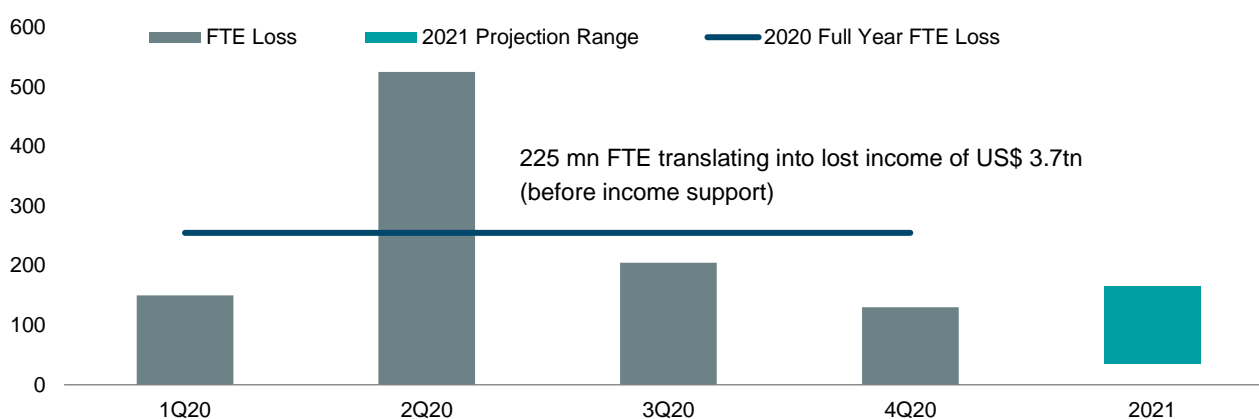
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Section II: Societal materiality of inequalities and Covid-19

In this section we explore the societal impact of inequalities that have been exacerbated by the Covid-19 pandemic on social issues. We assess how, like in previous crises, inequalities have widened based on age, gender, race and ethnicity, disability and class and making those already vulnerable even more so. We show how the pandemic has had a disproportionate impact on women in particular and we consider the implications from a government and corporate perspective. .

According to the ILO¹², the pandemic has led to lost income of US\$ 3.7 trillion for the global workforce, or roughly 4.4% of global GDP, and the equivalent of 255 million full-time jobs lost in working hours, which is four times greater than the jobs lost during the 2009 global financial crisis. However, these income and employments losses have not fallen evenly with certain regions, sectors and communities being disproportionately affected.

FIGURE 5: ESTIMATES OF EMPLOYMENT LOSSES IN 2020 AND 2021E IN MILLIONS



Source: DWS Research Institute, ILO Monitor (January 2021). FTE - Full-time equivalent jobs (assuming a 48-hour working week)

The pandemic has also exposed inequalities within countries and between particular segments of society particularly exposed such as the low skilled and low-paid as well as women and young adults. For example, job losses during the pandemic have been most extreme in the low-skilled sector (10.8%) while job losses among high skilled workers has been relatively small in comparison (2.2%). With sectors such as hotel and catering services, retail and construction hardest hit while the information and communication and financial services sectors have enjoyed positive jobs growth. Covid-19 has also revealed that many of the essential services we rely on are undertaken by individuals with weak forms of worker protection.

Asymmetric regional impact on the sustainable development goals

When assessing poverty and human development two of the most widely referenced indicators are the numbers living on less than US\$1.90 a day (extreme poverty) and the United Nations Development (UNDP) index, which measures a country's progress as it relates to education, health and living standards. Over the past four decades there has been a steady reduction in extreme poverty globally, helped in large part by rising living standards in China. However, according to the World Bank¹³ the Covid-19 pandemic has likely pushed between 88 million and 115 million people into extreme poverty last year, that is those living under US\$1.90 per day, and potentially rising further during 2021, Figure 6. Meanwhile, the UNDP declined in 2020 for the first time since the index was launched in 1990 as the pandemic has hit income, health and education¹⁴.

¹² ILO Monitor (January 2021). Covid-19 and the world of work

¹³ World Bank (January 2021). Poverty and shared prosperity 2020. Reversals of fortune

¹⁴ UNCTAD (March 2021). Impact of the COVID-19 pandemic on trade and development

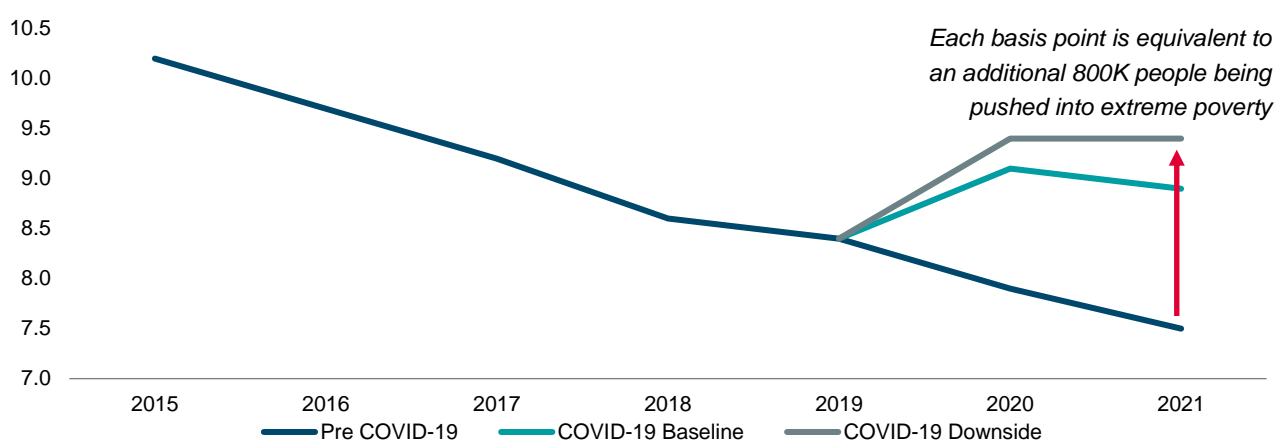
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These impacts have hit countries unevenly. For example, many of the support mechanisms to handle the pandemic on the labour market, such as furlough schemes, have not been available for many countries due to fiscal constraints, whereby in other places these have been essential to cushion employment losses, for example in Europe.

The pandemic has also revealed significant weaknesses in healthcare provision. The WHO calculates that over a third of the world’s population, mostly in emerging markets, currently lacks basic handwashing facilities at home¹⁵, the most effective method for COVID-19 prevention. While the tendency over the past 40 years in the developed world has been the growth in single occupancy homes, in emerging markets multi-generational dwellings are still the norm with the associated health risks. While the large share of service-based economies have facilitated the ability of employees to work from home in developed markets, along with internet access, this has not been open to the same degree in emerging markets which are more agricultural and manufacturing based and where internet access at home is significantly less widely available.

FIGURE 6: GLOBAL POVERTY RATE (%) AT THE US\$1.90-A-DAY POVERTY LINE, 2015–21E



Source: DWS Research Institute, Updated estimates based on Lakner et al. (2020), PovcalNet (online analysis tool), World Bank, Washington, DC, <http://iresearch.worldbank.org/PovcalNet/>, and Global Economic Prospects. Note: Three growth scenarios are considered: (1) pre-COVID-19 uses the January 2020 Global Economic Prospects growth rate projections, predating the COVID-19 crisis; (2) COVID-19-downside and (3) COVID19-baseline use the June 2020 Global Economic Prospects growth rates projecting a contraction in global growth for 2020 of 8 percent and 5 percent, respectively

Widening gender inequality

Women have been among the hardest hit when it comes to the effects of the pandemic and this has been true in both developed and emerging market countries. This can be seen in terms of employment loss, reduced working hours and leaving the labour market altogether. In some sectors, women have also been on the frontline of the pandemic in terms of the provision of essentials services, for example making-up an estimated 70% of health care workers. Where employment losses have occurred, namely in the tourism, retail and informal sectors, these typically have higher female participation rates¹⁶. In terms of reduced hours or leaving the workforce entirely, working mothers have been the ones that have predominantly provided home school supervision, unpaid care and domestic work. In one U.S. survey, one in four women cited lack of child care facilities as responsible for leaving the workplace. The European Institute for Gender Equality data show that about a quarter of women employees across the EU are in an irregular or precarious job compared to approximately 15% for men.

There is therefore a growing need to call on governments around the world to prioritise gender equality as they seek to recover from the economic impact of COVID-19 since barriers to women’s education and labor force participation reduce human capital and so weigh on growth potential. Besides higher rates of female unemployment relative to men globally and

¹⁵ WHO (June 2019). 1 in 3 people globally do not have access to safe drinking water

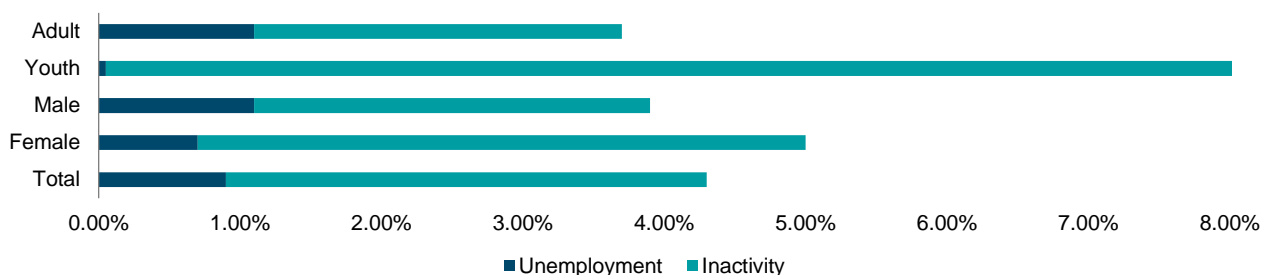
¹⁶ ILO Monitor (January 2021). Covid-19 and the world of work

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the pandemic's negative effect on employment in sectors with high female participation rates, the gender-pay gap is also at risk of widening further. This is important since excessive pay gaps between men and women, between management and workers and between companies and the wider population have potentially important investment implications. Research¹⁷ has shown more diverse companies tend to outperform.

FIGURE 7: DECOMPOSITION OF EMPLOYMENT LOSSES INTO CHANGES IN UNEMPLOYMENT AND INACTIVITY

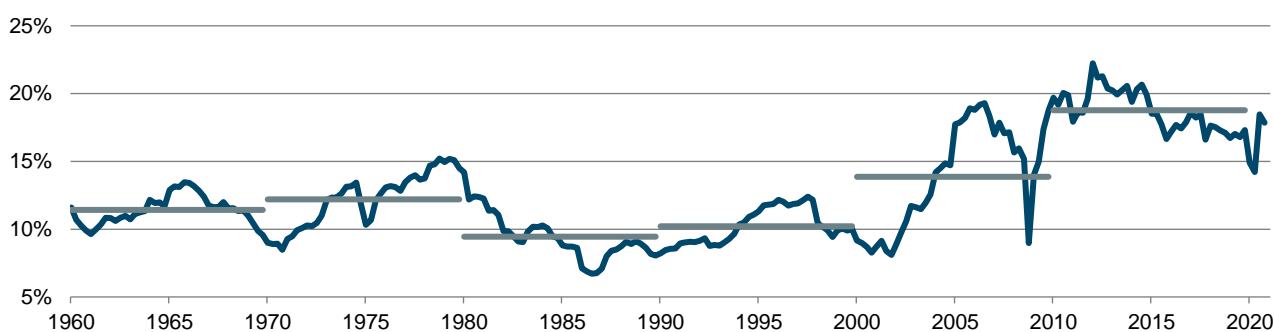


Source: DWS Research Institute, ILO estimates (January 2021). The two bars in each row show the difference in, respectively, unemployment and inactivity (withdrawal from the labour force) in 2020 as a percentage of employment in the "no pandemic" scenario. Youth = aged 15–24 years; Adult = aged 25+ years.

Fiscal stress and business conduct

The past 25 years has also witnessed the benefits of globalization, digitalization and the associated productivity gains accruing to the owners of capital rather than labour. Figure 8 shows U.S. corporate profits after tax when compared to employee compensation which have been trending upward since the end of the 1980s. With public sector debt levels already high and welfare and health systems now stretched, this is placing increasing scrutiny on the role of corporates when it comes to responsible business conduct and specifically in the area of abiding by the letter and spirit of tax laws. As highlighted in a recent DWS note¹⁸, it is no wonder governments are looking to take measures to address tax avoidance and shore up the erosion of their tax bases given some benefits accruing to a company are delivered by the state such as public infrastructure services. Steps to redress the balance are illustrated by G7 plans to introduce a global minimum corporate tax rate of 15% and ensuring that at least some of the profits in countries where multinationals operate are taxed.

FIGURE 8: U.S. CORPORATE BUSINESS PROFITS AFTER TAX DIVIDED BY EMPLOYEE COMPENSATION



Source: Board of Governors of the Federal Reserve System: Z.1 Financial Accounts of the United States, DWS Investment GmbH as of March 2021.

¹⁷ McKinsey & Co (May 2020). Diversity wins – How inclusion matters
¹⁸ DWS Investment GmbH (June 2021). CIO Chart of the Week: Tax and mend

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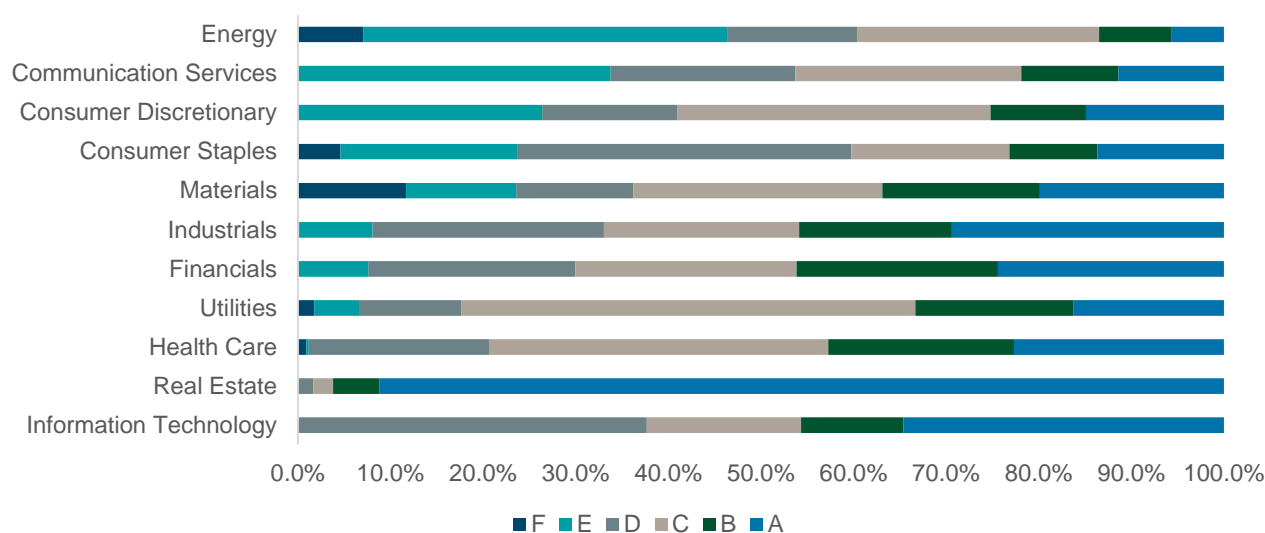
Section III: Social issues and asset manager activity

There are many routes available to investors and specifically asset managers in addressing social issues from an investment and corporate perspective. For example, these can range from the investment and engagement approach to the company's disclosures and public advocacy activities. In this section we examine these in greater detail.

1. Risk management and integrating social factors into the investment process

The Covid-19 crisis has increased the focus of integrating social aspects into the investment process, an area that has often been overshadowed by the responsibilities of integrating the multiple dimensions of climate risk. Our own work in terms of social screening analysis has been informative since we have discovered that violations are not limited to the traditional red flags raised when screening according to climate risk. The type of norm violations often differ according to sector.

FIGURE 9: ENERGY, CONSUMER STAPLES AND MATERIALS ARE MOST PRONE TO NORM VIOLATIONS



Note: A-D refers to no, low or manageable risk, E to severe violations, F to most controversial violations in MSCI AC World Index sectors
 Source: DWS Investment GmbH (April 2021)

The DWS total norm rating incorporates separate norm for Human Rights and Labour Rights across sectors and provides useful insights. For example, human rights issues are most pronounced in the oil, gas and consumable fuels, metals and mining and tobacco sub-industries while the banks and pharmaceuticals sub-industries are more affected by incidents relating to business ethics. On the flip side, we have identified equity real-estate investment trusts, water utilities, software, healthcare technology and biotechnology, thrifts and mortgage finance with the lowest degree of norm risk currently.

This risk management approach will require better data capture in terms of scope and depth as it relates to social issues. It is therefore hoped that the EU taxonomy relating to social issues will help to address these gaps. To be published in the third quarter of this year it will mean the environmental taxonomy will be supplemented in areas such as human rights, decent employment, equality, access to healthcare and non-discrimination.

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2. Thematic investments covering a specific or range of social factors

Just as the climate crisis has triggered a range of investment products to support the Sustainable Development Goals (SDGs) as they relate to climate action, the pandemic has increased the focus on investment products that address the five SDGs focused on basic needs, namely ending poverty and hunger, promoting good health, quality education and gender equality. Unanimously agreed and signed by all UN members in 2015, the SDGs have become an important investment framework for sustainability-focused investors.

The tenfold increase in social bond issuance last year to US\$249 billion is one example of how health and broader social issues have grown in interest¹⁹. Besides the increase in social bond issuance, we also expect to see an increase in social-specific thematic indices on the equities side that specifically target the social aspect. While currently two in 10 ESG indices focus on the S-pillar, investors polled for the CREATE study expect to double their allocations within the next three years based on more thematic indices becoming available. Once a benchmark is established, then there is an additional access route via Passive²⁰.

In addition, social thematic strategies can also include gender-lens investing and financial inclusion strategies. The findings of the Liechtenstein Institute's financial sector commission on modern slavery and human trafficking report²¹, published in September 2019, was useful to shine a light on the fact that not only was migration a sign of the failure of labour markets to provide decent employment opportunities, but, that the exclusion of an estimated 1.7 billion adults from banking services was pushing people and households into risky borrowing, labour and migration practices²².

Their analysis also found that almost one of every four victims of forced labour were exploited outside their country of residence which points to the high degree of risk associated with migration. Microfinance investment can therefore not only provide yield and diversification benefits, but, also help millions of entrepreneurs, many of whom are women, across the developing world improve their lives and boost regional growth and keep them away from dangerous lending practices. Indeed without the work of microfinance financial institutions, lending rates could be in excess of 300% compared to MFI lending rates of 25-30%. Other interesting investment opportunities, which might appear more climate-related that addressing basic needs includes renewable energy in emerging markets. This can deliver clean energy to households and small businesses which avoids the use of firewood for cooking and/or kerosene for lighting which will have a transformative effect on the health and livelihoods of women and their families.

3. Engagement with investee companies

At the heart of the SDGs is the concept of promoting an agenda that leaves no one behind. This means not just incentivising companies to meet high standards in the areas of human rights, decent work and ethical conduct but also to support a Just Transition when it comes to climate change.

When it comes to our activities, human rights and human capital management are an integral part of DWS's engagements with investee companies. According to the composition of our own engagement topics by individual pillar, 13% of all topics discussed were S-related. Labour rights as well as health & safety are particularly important components. One case study illustrated in the latest DWS Engagement Report²³ examined labour controversies with an online retailer which related to unfair termination of employees for protesting, alleged poor working conditions and inadequate safety measures.

The statement of investor commitment to support a Just Transition on climate change, launched in February 2018 and endorsed by 161 investors representing US\$10.2 trillion in assets, including DWS, aims to address the fact that the social

¹⁹ Climate Bonds Initiative (April 2021). Global State of the Market Report

²⁰ CREATE-Research, DWS (May 2021). Passive Investing 2021: Rise of the social pillar of ESG

²¹ A Blueprint for Mobilizing Finance Against Slavery and Trafficking (September 2019) - Liechtenstein Initiative for a Financial Sector Commission on Modern Slavery and Human Trafficking

²² World Bank Global Findex Database (April 2018). Financial inclusion on the rise, but gaps remain

²³ DWS (March 2021). Active Ownership <https://www.dws.com/en-gb/solutions/esg/corporate-governance/active-ownership-report-2020/>

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dimension of the transition to a resilient and low-carbon economy has been given insufficient attention, particularly in terms of the implications on the workplace, supply chain management and wider community issues²⁴.

The UNFCC has identified 1.47 billion jobs in sectors critical to climate stability with almost two-thirds in the agricultural sector, as well as in other sectors such as manufacturing, buildings, transport and energy²⁵. Investors therefore have a role to play in ensuring that companies have systems in place which prevents social harm. This can be challenging since violations can occur some distance away from the corporate and so not under its direct control. Typical examples of remoteness to a corporate's operations include forced labour, child labour, discrimination as well as general labour standards in their supply chain.

As part of its work in this area, the PRI and the Grantham Institute have provided guidance for investors including in the area of corporate engagement topics²⁶. Asset managers can also push investee companies to participate in initiatives that provide more information on their workforces. These include the Workforce Disclosure Initiative (WDI) established in 2016 and the Social & Human Capital Coalition. Areas of focus typically centre around the living wage, pay ratios, lost time through injury, workforce diversity and investment in training and development, among others.

4. Reporting and disclosure

Just as is the case for climate-related disclosures, investors lack clear, standardised, comparable and consistent data when it comes to assessing how companies approach human capital management. This has meant investors relying on voluntary information which does not facilitate an easy comparison of company policies and practices between countries and both across and within sectors. However, integrated reporting is focusing on human capital disclosures with IIRC and ICGN the main standard setters. DWS has been active in a number of sustainability reporting consultations over the past year

The work of the Workforce Disclosure Initiative is also helpful. In 2020, 141 companies covering 12 million employees across 19 countries and in all 11 economic sectors reported to the WDI on metrics such as wage levels, staff turnover, diversity and workers' rights. While reporting companies are skewed to the UK, representing 40% of the total, nevertheless the 2020 survey reveals the participation of companies by sector varies significantly. For example, financials and consumer discretionary combined capture a third of responses while healthcare and communication services combined account for 14% of responses. This is important since the pandemic has shown that those sectors which have been hit hardest, or where worker rights are least protected for example in the gig economy, disclosure among these sectors are falling short of what investors require.

Contributor

Jay Joshi

Research House

²⁴ The Investing in a Just Transition initiative (February 2018) is led by the Grantham Research Institute on Climate Change and the Environment at the London School of Economics and Political Science (LSE) and the Initiative for Responsible Investment at the Harvard Kennedy School

²⁵ UNFCC (2016). Just transition of the workforce, and the creation of decent work and quality jobs

²⁶ PRI, Grantham Institute (2019). Climate change and the just transition. A guide for investor action

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