The purpose of stewardship

“Stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.”

This definition, adopted by the FRC in its recent revamp of the UK Stewardship Code, is perhaps broader and more far reaching than what many would consider to be stewardship. Yet it reflects two important goals: long-term value creation and a recognition that companies and assets exist within broader social and environmental systems. For long-term investors, the proper and sustainable functioning of these systems are as integral to the ability to derive return as the companies that operate within them.

Asset owners predominantly view stewardship through the lens of voting and engagement activity which, in many cases, is undertaken by asset managers acting as their proxy. Yet this lens is not particularly well focused, with some placing an emphasis on levels of activity, rather than outcomes, as measures of success. Consequently, there is a risk that asset owners do not properly engage with or understand the actions of their managers making it harder for them to be held to account.

One commonly considered measure is the extent to which asset managers vote against management recommendations. But is a manager who votes against management on 20% of occasions better or worse than a manager who votes against management on 30% of occasions? Without the context provided by an understanding of voting policies and the knowledge of individual resolutions, we cannot say.

We can, however, begin to explore trends in the data, for example, by considering whether managers are more or less likely to vote against management on particular issues. This provides greater insight and allows asset owners to develop their understanding of the stewardship activity that managers undertake on their behalf.

Voting against management at AGMs may be in line with policy, the recommendation of a voting adviser or the outcome of a failed engagement but this requires the manager to elucidate the reasoning for their vote.

Where managers engage with companies for the purposes of creating change, they are not just focused on routine governance issues such as executive remuneration, but increasingly on environmental and social themes such as climate change and human rights. In engaging on such issues, there is an implicit acknowledgement that companies have obligations to a range of stakeholders beyond investors. This responsibility to customers, employees, suppliers and communities as well as shareholders was recently recognised[1] by over 180 leading US companies who signed a 'Statement on the Purpose of a Corporation', outlining a new standard for corporate responsibility.

Commitments such as these chime with the definition of stewardship set out by the FRC yet the challenges presented by the current pandemic have served to highlight differing standards of corporate behaviour.

1 https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans

Such promises depend on those who invest to hold companies to account which in turn requires asset owners, and their investment managers, to consider which practices are acceptable and which are not.

Pension fund trustees over the next 18 months will need to prepare Implementation Statements that reflect the execution of their voting and engagement policies. Rather than focusing wholly on quantitative assessments, the current situation offers a chance for trustees to reflect on the purpose of stewardship and the outcomes that they want to observe. By doing this, they can then hold asset managers more effectively to account.

Simon Jones
Head of Responsible Investment
simon.jones@hymans.co.uk
0131 656 5141

Caoimhe Bain
Responsible Investment Consultant
caoimhe.bain@hymans.co.uk
0207 082 6028

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London | Birmingham | Glasgow | Edinburgh T 020 7082 6000 | www.hymans.co.uk | www.clubvita.co.uk

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