Investment Institute Sustainability

AGM season 2023:

New challenges highlight the achievements of responsible investors

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Key points

- There has been a revolution in corporate annual shareholder meetings over recent years. Companies have been encouraged towards higher standards of reporting and behaviour by responsible investors

- The most recent AGM season has seen intriguing themes emerge around the appropriateness of pay deals, a divergence in ESG resolutions and concerns around the role of voting

- The scenario for annual meetings is now more complex, with competing interests at play, but we see this as a reflection of the strides made to put sustainability and good governance at the heart of corporate decision making

The landscape for corporate governance has seen a revolution over the past few decades. It used to be the case that annual general meetings (AGMs) were sleepy affairs where company resolutions were generally rubber-stamped by shareholders with little appetite to rock the boat. However, a series of governance crises at the beginning of this century and a concurrent evolution in regulation have encouraged asset managers and other institutions to deepen their expertise in the governance field – and driven corporates to improve their accountability to shareholders.

In many ways, it has been a triumph of responsible investment. Active, engaged investors have managed to spotlight the potential risks and opportunities linked to environmental, social and governance (ESG) themes and make them part of the mainstream debate around corporate performance. Now, rather than sleepy AGMs, we see active, complex and material consideration of investor concerns which we think serves to benefit all stakeholders over the short and long term.

Traditional governance topics continue to develop, including the steady evolution of 'say-on-pay' votes across various geographies. Most notable, though, has been the integration of shareholder expectations around ESG, reflected either through the multiplication of ESG-related proposals submitted by shareholders, or through the early development of 'say-on-climate' resolutions submitted by companies, often after pressure from their investors.

AGMs are now an unmissable opportunity for dialogue between shareholders, corporate leadership and, increasingly, civil society. In this paper, we discuss three major trends from the 2023 meeting season that highlight how ESG topics are increasingly entwined in the meeting process and how shareholder voting has become a concrete avenue to enact meaningful stewardship of assets.

Executive pay and notion of 'social acceptability': Can investors drive change?

Globally, executive pay attracted renewed attention during the 2023 AGM season. After two financial years impacted by the COVID-19 crisis, we have seen some significant spikes in pay packages, mainly driven by an increase in quantum and windfall gains in some cases. Many responsible investors, including AXA IM, advocate for fairer compensation structures, especially in a time of economic crisis, which has prompted a cautious approach towards this issue in our analysis and engagements.

Let's take the example of the UK, which faced its worst cost-of-living crisis in half a century with persistently high inflation that reached the double digits in the final quarter of 2022 and first quarter of 2023.[1] Investors expect companies to acknowledge and address this in their compensation policy.

Our view is that the cost-of-living crisis presents a risk to investment performance due to its potential impact on worker productivity, which in turn could negatively impact economic performance and overall market returns for investors.

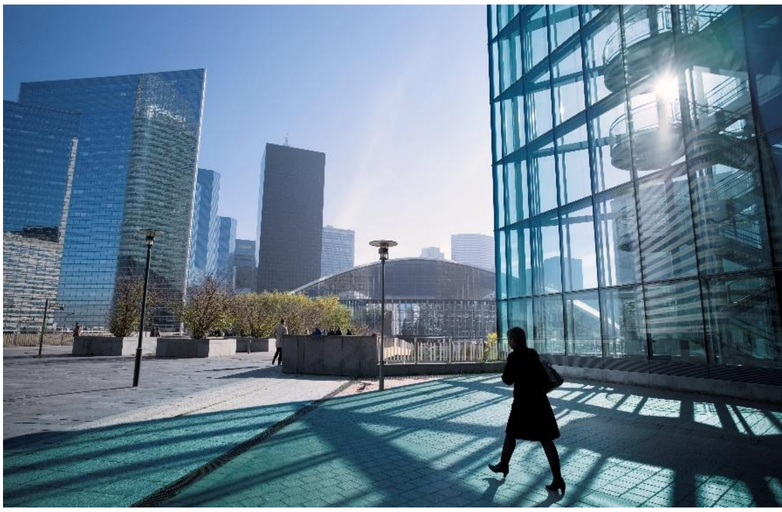
In turbulent times, protecting the most vulnerable employees and insisting on retention could be key to navigate through the crisis as an employer. This AGM season offered investors an important opportunity to encourage companies to convert the short-term pay changes into long-term structural changes.

To avoid widening the gap between average worker pay and the total remuneration available to executives, many investors specifically asked whether companies had taken steps to support their lowest paid employees and pushed for increases in executive base salary to be proportionally lower than the overall workforce.

In terms of escalation, if the approach retained by the company was not aligned with expectations, then many investors withdrew their support from resolutions to approve the remuneration report or, in rare cases, to reappoint the chair of remuneration committee.

While a large majority of UK employers took appropriate action to address the cost-of-living crisis for their workforce, some were widely considered to be lagging and this did translate into a notable increase in dissent at AGMs around remuneration-related items.[2]

There was another side to this debate, however, especially in the UK. Some companies blamed large investors for encouraging a 'skills drain' by exerting engagement and voting pressure on executive pay policies. This raised the spectre of companies being put at a competitive disadvantage relative to US competitors by creating a substantial gap between UK and US pay levels. This has been consistent concern over the years whenever investors identify what they see as excessive pay deals; it was raised by London Stock Exchange chief executive officer (CEO) Julia Hoggett, who called on firms to pay bosses more.[3] Her comments were largely rejected by investors, but still, this need to rethink the always-difficult balance between fairness and competitivity is one of the key takeaways from the 2023 AGM season.



Fragmentation around ESG

We witnessed an important and challenging moment in how the world addresses ESG during the 2023 AGM season.

On one hand, 2023 saw an increase (+12% from 2022) in the overall volume of ESG-related shareholder proposals, including in markets where ESG resolutions have not been common practice. For example, France has seen its first ever advisory-only climate-related proposal submitted by shareholders, while Japan saw in recent years a surge in the number of climate-related proposals.

On the other hand, in the US, although the overall volume of ESG-related shareholder proposals continues to increase, so did the number of what we might call 'anti-ESG' proposals (from 21 in 2021 to 88 in 2023 so far, according to think tank The Conference Board).[4]

A divergence in ESG-related voting results from around the world helps illustrate a growing nuance in how ESG issues are addressed. Taking the example of Japan, climate proposals submitted at Toyota Motor or Mizuho Financial received support from 15% and 19% of votes, respectively, reaching levels of support which we believe the company will need to take seriously. In the US, however, average support on environmental or social shareholder resolutions, after reaching a record high in 2021, has declined in a trend likely to reflect the increased prescriptiveness of the resolutions.

A large number of climate-related proposals in US have made explicit reference to seeking to limit global temperature increases to +1.5°C from pre-industrial times, as set out as an 'ideal' scenario in the 2015 Paris Agreement. However, current evidence suggests the world is already missing this target.[5]

The debate in the US has also been coloured by political support for the oil and gas sector in certain states which has become a major media story and is likely to have made domestic investors more cautious, and potentially more reluctant to support ESG resolutions.

We can see an example of this regional divergence in the voting records. For several years, the non-governmental organisation, Follow This, has been submitting a similar climate resolution at all oil and gas companies. This year the proposal submitted at France-based TotalEnergies recorded 30% approval[6], while at US company Chevron support fell to some 10% of investors from 33% a year earlier[7].

This growing transatlantic divide over ESG has even led CEOs of some European energy companies to debate the potential valuation implications.[8]

It may be that this AGM season is also witnessing the emergence of a new 'greenhushing' trend, whereby some companies and investors become reluctant to publicly communicate on ESG. One prominent asset manager executive has said they fear the acronym itself has become "entirely weaponised" through its politicisation. We expect this fragmentation around ESG will likely encourage ESG-focused investors to reiterate the evidence of links between ESG factors and long-term financial performance.

Growing societal focus in voting

In June 2023, the European Parliament approved its draft of the Corporate Sustainability Due Diligence Directive (CSDDD),[9] requiring companies to consider the potential negative impact of their activities on human rights and the environment. One provision directly targets the responsibilities of asset managers and investors on these aspects, requiring them to engage with investee companies and exercise voting rights with the aim of inducing companies to minimise or end any adverse environmental or social impact.

Although the final version of the directive is still under discussion between European institutions, this already sends a clear signal on how governments see the responsibility of investors towards society, as well as what is perceived as the significant influence of their voting powers.

This development, along with the expansion of ESG-related offerings from asset managers, is likely to further emphasise scrutiny on asset managers' stewardship approaches, often most clearly reflected in voting decisions. Asset owners are increasingly scrutinising how their managers cast votes on their behalf on specific resolutions, helping to address any potential misalignment between the wishes of pension savers and asset manager voting patterns.

The UK Asset Owner Roundtable, for example, has commissioned an academic review on how asset managers have "interpreted their clients' long-term interests in the exercise of their stewardship duties"[10], focusing on votes at key European AGMs. The UK's Financial Conduct Authority, meanwhile, has an ongoing consultation on vote reporting and transparency which aims to "better equip asset owners to hold asset managers to account on their voting activity".[11]

We expect that evolutions in market guidance, stewardship codes, and sustainability-linked regulation will further focus on voting as a powerful lever for asset managers to maximise the success of their stewardship policies and secure sustainable outcomes.

In that context, we think recent regulatory moves in the UK and Europe – that would give firms more power to implement unequal voting rights structures – risk diluting the leverage of asset manager and institutional investor votes and in turn risk damaging the effectiveness of collective stewardship efforts.[12]

Resistance and acceptance

The level of sophistication from the asset management industry – and from asset owners – on corporate governance and voting has drastically evolved and improved over the years, to the point that an increasing range of environmental, social and governance issues are habitually addressed by investors during engagement with companies. Those firms have in turn become increasingly more accountable and responsive to their shareholders.

The demands fall on every player. Asset managers themselves are now under greater scrutiny from regulators, asset owners, and society to better report on voting decisions and stewardship outcomes, while companies that remain unresponsive to shareholder concerns are more likely than ever to come under fire. We have seen this in significant opposition levels on individual Board reappointments and through the development of climate-related litigation against companies (and Boards) that fail to align their strategies with the necessary climate transition.

Of course, all of this has made things more complex – messy even. Progress has reached the point where there may be resistance to some ideas, alongside the perhaps less-newsworthy widespread acceptance of others. In short, there are no more sleepy AGMs.

We can't speculate on the damaging crises or scandals that may have been averted through this intensified scrutiny, but we do believe that engaged, active and responsible investors have helped foster a more benign, and perhaps rewarding, investment environment.

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[1] Monetary Policy Report - May 2023, Bank of England, May 2023
[2] AXA IM took the decision to oppose remuneration resolutions at 15 different UK AGMs in 2023. Our full voting record can be viewed here.
[3] London Stock Exchange chief calls for UK firms to pay bosses more | Executive pay and bonuses | The Guardian
[4] 2023 Proxy Season: More Proposals, Lower Support, The Conference Board Inc, June 2023
[5] Global temperatures set to reach new records in next five years, World Meteorological Organization, May 2023
[6] Record support for Follow This climate resolution at TotalEnergies thanks to coalition of 17 investors | Follow This (follow-this.org) / Combined shareholders' meeting of TotalEnergies SE on May 26, 2023: Results of Resolutions
[7] Investors miss opportunity to urge ExxonMobil and Chevron to drive down emissions by 2030 as votes for Follow This climate resolution fall | Follow This (follow-this.org) (Combined shareholders' meeting of TotalEnergies SE on May 26, 2023: Results of Resolutions / Chevron Corporation Form 8-K: Results of resolutions)
[8] Total's chief tells investors European listing to blame for oil group's trading discount, Financial Times, April 2023
[9] Corporate sustainability due diligence, European Commission, February 2023
[10] UK Asset Owner Roundtable convenes asset managers over proxy voting concerns (professionalpensions.com)
[11] Vote Reporting: A consultation and discussion paper from the Vote Reporting Group (fca.org.uk)
[12] FCA proposes to simplify rules to help encourage companies to list in the UK, FCA, May 2023. EU Legislation in Progress: Listing Act, European Parliament, 2023

Image source: Getty Images UK.