BUSINESS ROUNDTABLE PROMOTES EVOLVING CORPORATE PURPOSE: WILL COMPANIES BROADEN PERFORMANCE METRICS?

US corporations should promote the interests of diverse stakeholders beyond investors, according to a recent statement by the Business Roundtable (BRT), an association of CEOs of approximately 200 leading US companies. The Aug. 19 “Statement on the Purpose of a Corporation” says that US corporations should commit to deliver value to all stakeholders — including employees, customers, suppliers and communities.

Is this a groundbreaking strategic change for corporate America, or does the statement simply formalize the way many companies already operate?

Investors and the media are debating this question. Some view the BRT statement as a repudiation of Milton Friedman’s guidance in “The Social Responsibility of Business Is to Increase Its Profits,” which asserts that free-market capitalism itself increases social welfare. However, the BRT’s opening paragraph notes that “the free-market system is the best means of generating good jobs, a strong and sustainable economy, innovation, a healthy environment and economic opportunity for all.”

That opener hardly signals a sudden shift in corporate values. Instead, the statement accurately reflects evolving corporate governance practices that respond to pressure from investors, employees and customers. Many companies promote corporate sustainability by considering a company’s environmental, social, and governance (ESG) impact.

INCREASING FOCUS ON ESG

Over the past few years, the ESG trend has taken off on numerous fronts:

- Influential institutional investors like BlackRock and State Street Global Advisors have adopted responsible investment policies.
- Ratings organizations now prepare ESG performance rankings (more formally in Europe than in the US), and specific investment funds focus on issuers that are “best in the class” on ESG matters.
- The Sustainability Accounting Standards Board (SASB) has issued detailed, quantifiable industry-specific metrics addressing most, if not all, of the objectives in the BRT statement.
- Proxy advisers like Institutional Shareholder Services rate issuers on ESG matters.

HUMAN CAPITAL AS AN ESG FACTOR

Companies are also under pressure from employees and boards of directors to consider their ESG impact. Mercer’s Global Talent Trends research shows that younger generations are drawn to and more engaged in working for an organization with a purpose they can embrace. Substantial evidence shows a strong positive relationship between human capital management (HCM) and business performance, including shareholder value.

The SASB standards bolster the view that human capital is an asset whose value and associated risks should be disclosed in a company's financial reports and other communications. In addition, proposed SEC rules would require companies to disclose human capital measures or objectives — such as attraction, development and retention of employees — considered in managing the business.

As a result, HCM — and its link to corporate sustainability and risk management — is gaining attention in corporate boardrooms across the country. For example, companies are measuring their gender pay equity, employee diversity, productivity and turnover, taking action to address gaps and reporting to increasingly interested stakeholders on progress.

STRIVING FOR LONG-TERM SUSTAINABILITY

The BRT statement indicates that a cross-section of corporate America's leaders are formally embracing these views on the importance ESG and HCM. So, why now? Consistent with best practices on performance management and executive pay, this may represent a shift in executives' focus from the "what" to the "how." While investor returns (the "what") will always be a primary driver, performance must also take into account how an organization treats its employees, customers, business partners and the communities in which it operates.

In response to these trends, many companies are already pursuing ESG and HCM objectives. A recent Mercer survey found that 51% of companies either currently use ESG metrics in their incentive plans or are considering doing so. But even when incentive plans incorporate ESG metrics, they carry little weight.

If the axiom "what gets measured gets done" holds true, companies should reframe not only what gets measured but also what gets rewarded in the C-suite, the boardroom and beyond. The BRT statement can serve as a catalyst for corporations to evaluate their ESG strategies and actions.

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