

# Our approach to engagement on human capital management

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Investment Stewardship

**BlackRock Investment Stewardship (BIS) advocates for sound corporate governance and business practices that support the long-term value creation that our clients depend on to achieve their financial goals. As part of our fiduciary duty, we assess a range of factors that can affect the financial performance of the companies in which we invest on behalf of our clients.**

Our [Global Principles](#) underscore our belief that in order to deliver value for shareholders, companies should also consider their other key stakeholders. In our experience, companies that build strong relationships with their stakeholders are more likely to meet their own strategic objectives, while poor relationships may create adverse impacts that could expose companies to legal, regulatory, operational, and reputational risks and jeopardize their social license to operate. **This is why we ask companies to report on how they consider the interests of their workforce in business decision-making.**

In this context, we seek to understand a company's approach to human capital management. The following describes how we evaluate and engage with companies on this topic.

## Human Capital Management as an Investment Issue

Human capital can be defined as “the knowledge, skills, and health that people invest in and accumulate throughout their lives, enabling them to realize their potential as productive members of society.”<sup>1</sup> From a corporate perspective, human capital management (HCM) is the approach that companies take to harness these contributions.<sup>2</sup> This approach may vary across sectors and over time, but is a factor in business continuity, innovation, and success for all companies.

Technological disruption, demographic shifts, and rising economic and social inequalities<sup>3</sup> are altering the social contract between companies and their workforce and transforming the labor market, with many companies and investors considering robust HCM to be a means through which to achieve a competitive advantage. Companies need to be able to attract, retain, and develop workers with the skills and expertise necessary to execute their long-term strategy and to deliver value creation. It is therefore important that companies explain as part of their corporate strategy how they establish themselves as an employer of choice for the workers on whom they depend, and support a diverse and engaged workforce aligned with and contributing to its purpose and corporate culture.<sup>4</sup>

Furthermore, companies have a role to play in advancing human capital development and fostering a more prosperous and inclusive society. This can create a virtuous cycle that reinforces a company's social license to operate. For example, investing in efforts to build a strong local workforce in the community in which it operates may bolster economic growth, which in turn may have a positive effect on consumers.

Research has consistently shown the importance of human capital to company performance. Companies included in Fortune Magazine's “100 Best Companies to Work For” list earned, over the long-term, excess risk-adjusted returns of 3.5%.<sup>5</sup> Another report surveyed a multitude of studies on human capital and found that there is a positive correlation between human resource initiatives and investment outcomes such as total shareholder return, return on assets, return on earnings, return on investment, and return on capital employed.<sup>6</sup>



## UN SDGs alignment

*We believe that there is significant intersection between many of the topics that we discuss with companies and aspects of these eight [Sustainable Development Goals](#) (SDGs).*

The COVID-19 pandemic has deepened our conviction that human capital is one of a company's most valuable assets. Companies with sustainable business practices, particularly those that focused on supporting the needs of their workforce, demonstrated greater resilience during the crisis.<sup>7</sup> Moving forward, as companies adapt their business models and HCM practices to the shifting nature of work, we are committed to contributing to efforts that improve corporate reporting, strengthen industry standards, and shape market views on this topic.<sup>8</sup>

## Our Expectations of Boards and Management Teams

**BIS asks that companies demonstrate a robust approach to HCM and provide shareholders with the necessary information to understand how it aligns with the company's stated strategy and business model.** These disclosures may address how a company identifies its key human capital priorities, the policies in place to address these priorities, and how the board oversees management to ensure accountability. We also ask that companies provide details of any relevant goals and targets so shareholders can measure progress.

We believe that clear and consistent reporting on HCM matters is critical for investors to make an informed assessment of a company's HCM practices. We consider the Sustainability Accounting Standards Board's (SASB) materiality framework<sup>9</sup> to be a helpful tool for companies considering enhancing their disclosures on industry-specific human capital metrics.

We recognize that demographic characteristics may vary by country, so we ask that companies report this information in accordance with regional frameworks. For example, US companies could report and disclose in line with the Equal Employment Opportunity Commission's EEO-1 Survey.<sup>10</sup> We also recognize that workforce composition has changed significantly in recent years, with contract, freelance, and gig workers<sup>11</sup> (alternative workforce) being important contributors to many companies' success. While a company's obligations to its employees may differ from that of its alternative workforce, we believe it may face business risks if its HCM strategy does not extend beyond its core employees. We expect companies that extensively rely on these workers to address how their HCM approach for employees compares with their alternative workforce and provide the rationale for any differences.

## How We Engage on Human Capital Management

In evaluating HCM practices, we are focused on understanding the effectiveness of a company's board and management in supporting the needs and meeting the expectations of its workforce. In our dialogue with companies, we advocate for business practices that foster a diverse, equitable, and inclusive workforce culture; enhance job quality and engagement; facilitate positive labor relations, safe working conditions, and attractive wages; and prioritize human rights.<sup>12</sup>

Through our analysis of company disclosures and engagement with management, we aim to understand the following:



**Board oversight of human capital risks and opportunities.** This includes a company's designation of a specific board committee with oversight responsibility, the type and frequency of information reviewed by the board and this committee, and how performance on human capital metrics may be linked to executive compensation to encourage accountability



**Commitment to advancing diversity, equity and inclusion.** This includes a company's efforts to recruit, retain, and develop diverse talent; create an inclusive workplace for all workers; support executive training for underrepresented groups; and address any compensation gaps across different workforce demographics



**Workforce engagement.** This includes the processes a company uses to understand and address workforce expectations, and how senior leadership assesses the efficacy of its efforts (e.g. opinion surveys). These processes should promote constructive dialogue with respect to terms of employment and working conditions, and incorporate the interests of workforce representatives into the company's overall HCM strategy, where applicable



**Worker rights and protection.** This includes a company's procedures to protect its workforce and prevent workplace harassment and/or discrimination (e.g. whistleblowing, codes of conduct, and equal employment policies, etc.). It also includes how a company's HCM strategy and compensation programs align to create a healthy culture and prevent unwanted behaviors



**Workforce compensation.** This includes how a company's compensation philosophy is aligned with its purpose and culture, and whether its pay practices (e.g. salary, benefits, and stock ownership, etc.) are designed to attract and retain talent



**Health and safety.** This includes safety management plans, as well as the workplace wellness programs a company offers to support workers' physical and mental health and safety (e.g. paid parental and sick leave, personal counselling sessions, and compliance with occupational health and safety policies, etc.)



**Training and development.** This includes the programs companies offer to allow their workers to develop their skills and expertise to contribute to a company's goals, have opportunities for advancement, and adapt to the workplace of the future

BIS identifies companies for engagement based on our [Engagement Priorities](#), our prior history of voting and engagement with the company, and our assessment of a company's financial and governance performance relative to its peers. As an issue that manifests across sectors, we discuss HCM with most companies in which we are invested on behalf of our clients but consider industry- and market-specific context.

We also engage companies on HCM where there is evidence<sup>13</sup> that an event could have an adverse effect on shareholder value. For example, poor human capital practices may trigger worker protests, stakeholder activism, or a breach in international standards, resulting in regulatory action or damage to a company's reputation. In advance of engagement, we analyze information in the public domain on the company's exposure to and management of human capital risks. Where available, we also refer to third party research on the company's business practices. If we identify that a company is not effectively addressing material human capital risks, or its disclosures setting out its approach are inadequate, we will engage with company leadership to explore the topics outlined above, amongst others, to further understand the company's approach and address our concerns.

Where a company's practices or disclosures fall short such that we are unable to assess the board and management's effectiveness in addressing these issues, we may vote against the re-election of directors responsible for these decisions. We may also express our concern through voting for shareholder proposals that address business-relevant human capital risks. Similarly, when a company's business operations or practices have resulted in adverse impacts or outcomes that may materially impair a company's license to operate, we may take appropriate action in the context of our voting decisions.

## Conclusion

Failure to manage human capital risks and opportunities can affect critical relationships with a company's workforce and potentially impact shareholder value. As a long-term investor, we will continue to advocate for robust human capital practices and improved disclosures.

## Endnotes

1. As defined by the World Bank's "Human Capital Project. More information about the Project is available at: <https://www.worldbank.org/en/publication/human-capital/brief/about-hcp#:~:text=Human%20capital%20consists%20of%20the,societies%20by%20developing%20human%20capital>
2. Bernstein, Aaron and Beeferman, Larry. "Corporate Disclosure of Human Capital Metrics". Pensions and Capital Stewardship Project (2017). Labor and Worklife Program, Harvard Law School. Available at: <https://lwp.law.harvard.edu/publications/corporate-disclosure-human-capital-metrics>.
3. For BlackRock's views on the investment themes driving markets in 2021, consult our 2021 Global Outlook. Available at: <https://www.blackrock.com/corporate/literature/whitepaper/bii-2021-global-outlook.pdf>.
4. For additional insights, see "BlackRock Investment Stewardship's Approach to Engagement on Long-Term Strategy, Purpose and Culture". Available at: <https://www.blackrock.com/corporate/literature/publication/blk-commentary-engaging-on-strategy-purpose-culture.pdf>.
5. Edmans, Alex. "Does the Stock Market Fully Value Intangibles," *Journal of Financial Economics* 101 (2011): 621-640. Available at: <http://faculty.london.edu/aedmans/Rowe.pdf>.
6. The survey, conducted by Harvard Law School's Labor and Worklife Program, concluded that companies that had a workforce that was not engaged had an average one-year operating margin below 10%; however, those that consistently promoted workers' well-being had an average one-year operating margin of 27%. More information is available at: [https://lwp.law.harvard.edu/files/lwp/files/final\\_human\\_capital\\_materiality\\_april\\_23\\_2015.pdf](https://lwp.law.harvard.edu/files/lwp/files/final_human_capital_materiality_april_23_2015.pdf).
7. For more information, refer to BlackRock's "Sustainable Investing: Resilience Amid Uncertainty". Available at: <https://www.blackrock.com/corporate/literature/investor-education/sustainable-investing-resilience.pdf>.
8. As members of SASB's Investor Advisory Group (IAG), we are currently participating in SASB's consultation to strengthen its human capital reporting standards and better incorporate evolving market trends. More information about the consultation is available at: <https://www.sasb.org/standard-setting-process/current-projects/human-capital/>.
9. For additional insights into our view of the SASB framework, see "BlackRock Investment Stewardship's Approach to Engagement on TCFD and SASB Aligned Reporting". Available at: <https://www.blackrock.com/corporate/literature/publication/blk-commentary-tcf-sasb-aligned-reporting.pdf>.
10. More information is available at: <https://www.eeoc.gov/employers/eeo-1-survey>.
11. In a "gig economy", people work part-time or in temporary positions, often providing services to clients or customers through online platforms. Examples include ridesharing, food delivery, and caregiving.
12. For additional insights, see "BlackRock Investment Stewardship's Approach to Engaging Companies on their Human Rights Impacts". Available at: <https://www.blackrock.com/corporate/literature/publication/blk-commentary-engagement-on-human-rights.pdf>.
13. This includes information made public by workers, regulators, non-governmental organizations, or other third parties.

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