Our approach to engagement on human capital management

Investment Stewardship

BlackRock

BlackRock Investment Stewardship (BIS) encourages companies to have sound corporate governance and business practices that support the durable, long-term financial value creation that our clients depend on to achieve their investment goals. As part of our fiduciary responsibilities as an asset manager to act in our clients' financial interests, we assess a range of risks and opportunities that can affect the long-term performance of the companies in which we invest on their behalf. We engage companies to understand their approach to the material drivers of risk and financial value in their business models, provide feedback, and raise any concerns. We may signal continuing concerns through our voting, where clients have authorized us to vote on their behalf. In all cases, our voting is intended to advance the long-term financial interests of our clients as shareholders.[1]

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."[2] From a corporate perspective, human capital management (HCM) is the approach that companies take to harness these contributions in their workforce.[3] This approach may vary across sectors and geographies, as well as over time, but is an important factor in business continuity, innovation, and success for all companies.

In our experience, companies that invest in the relationships that are critical to their ability to meet their strategic objectives are more likely to deliver durable, long-term financial performance. By contrast, poor relationships may create adverse impacts that could expose companies to legal, regulatory, operational, and reputational risks. This is particularly the case with regard to a company's workforce, as a significant number of companies acknowledge the importance of their workers in creating long-term financial value.[4]

In many markets, companies face a number of challenges in relation to their workforce, including aging demographics such that key workers are retiring; technological shifts that require workers to have very different skills from those they originally trained in; workforce shortages in some segments of the market; and worker turnover particularly stemming from the prevalence of contract, freelance, and gig work. Poor human capital practices may lead to worker protests, stakeholder activism, or a breach in international and/or national standards,[5] potentially resulting in declines in production, regulatory action, and/or damage to a company's reputation.

As a result, many companies and investors consider 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, meet the needs of their customers and others in their value chain, and deliver financial returns for shareholders.

Companies can also play an important role in advancing human capital development, which in turn can reinforce a company's reputation in the communities within which it operates. For example, a company investing in efforts to build a strong local workforce may bolster local economic growth, which may have a positive effect on consumer spending.

How we engage on human capital management

In our engagements, BIS focuses on understanding the effectiveness of boards and management in ensuring a company has the workforce necessary for delivering long-term financial performance. Our discussions cover material workforce-related risks and opportunities, which may include how a company's business practices foster a diverse and inclusive workforce culture; enhance job quality and employee engagement; enable career development; promote positive labor relations, safe working conditions, and fair wages; and consider human rights.[6]

BIS looks to companies to demonstrate a robust approach to HCM and provide shareholders with the necessary information to understand how the approach taken aligns with the company's stated strategy and business model. BIS does not seek to direct a company's policies or practices, which are the responsibility of management and the board. We find it helpful when companies provide clear and consistent reporting on HCM matters to help investors to understand a company's approach to a potentially material business risk. We recognize that there are different reporting standards and frameworks on HCM, which may be voluntary or required by regulation. In such cases, we appreciate when companies provide context on their reporting and highlight the metrics reported that are industry- or company-specific.

Through our analysis of company disclosures and engagement with corporate leadership, we aim to understand the following, as appropriate and relevant to the particular company:

- **Board oversight of human capital risks and opportunities.** This includes the board's approach to overseeing HCM (e.g., whether a specific committee has oversight responsibility), and the type and frequency of information reviewed by the board and this committee, including measures of progress in management's human capital strategy.

- **Workforce engagement.** This includes the processes a company uses to understand workers' views and feedback on areas for improvement, and how senior leadership assesses the efficacy of its efforts (e.g., employee opinion surveys). These processes should promote constructive dialogue with respect to terms of employment and working conditions, and result in the perspectives of workers being reflected in the company's overall HCM strategy, where appropriate.

- **Workforce compensation.** This includes how management establishes a compensation philosophy that is aligned with the company's purpose and corporate culture, and whether the company's pay practices (e.g., salary, benefits, and stock ownership) are effective in attracting and retaining talent and deliver equal pay for equal work.

- **Training and development.** This includes the programs companies offer to enable 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. In industries or markets where workers may be displaced due to structural shifts materially impacting the company's business model, such as the low-carbon transition or the integration of emerging technologies into production processes, this may include re-training and re-deployment opportunities for affected workers. It may also include companies collaborating with universities and other training organizations to develop new talent pools.

- **Efforts to advance diversity and inclusion.** This includes a company's efforts to recruit, retain, and develop workers drawn from the diverse talent pool available to companies, create a workplace where all workers have an equal opportunity to succeed, and support executive training and development opportunities to foster an inclusive workplace.

- **Worker rights and protection.** This includes a company's procedures to prevent involuntary and child labor; enable worker organization and collective bargaining; and prevent workplace harassment, discrimination, and misuse of employer power, in line with applicable laws and regulations related to all of these topics.[7] These procedures may encompass codes of conduct, equal opportunity employment policies, whistleblowing systems, and grievance mechanisms. It also includes how a company's HCM strategy and compensation programs align to create a healthy culture and prevent unwanted risk taking or behaviors.

- **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 (for example, paid parental and sick leave, personal counselling sessions, and compliance with occupational health and safety policies).

Endnotes

1. This commentary should be read in conjunction with BIS' Global Principles and regional voting guidelines. Other materials on the BIS website might also provide useful context.
2. As defined by the World Bank's "Human Capital Project." Source: The World Bank, "The Human Capital Project: Frequently Asked Questions", October 3, 2022.
3. Bernstein, A., and Beeferman, L, "Corporate Disclosure of Human Capital Metrics", Pensions and Capital Stewardship Project Labor and Worklife Program, Harvard Law School, October 19, 2017.
4. This perspective is also backed by research, for example: Fedyk, A and Hodson, J, "Trading on Talent: Human Capital and Firm Performance", Review of Finance, forthcoming. October 15, 2022.
5. Specifically, breaches in international standards such as the UN Guiding Principles on Business and Human Rights (UNGPs) (2011) and the Organization for Economic Cooperation and Development's (OECD) global standards for promoting responsible business conduct (updated in 2023).
6. For additional insights, see BIS' commentary on our "Approach to engagement with companies on their human rights impacts."
7. Where local human rights laws or regulations differ from international labor standards such as those outlined in the International Labor Organization (ILO) Declaration on Fundamental Principles and Rights at Work, we encourage companies to explain how they navigate any ambiguities or contradictions. of the ILO Declaration was last amended in 2022.

Want to know more?

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