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The 2023 AGM season: What will dominate discussions?

As companies gear up for their annual general meetings, **Jonathan Harker** and **Andrew Stevenson** consider some of the current hot topics and offer advice on what investors are looking for.

'Macroeconomic volatility'; 'turbulent economic times'; 'choppy waters'; 'the rise of the activist and the retail voice' – these are just some of the well-laboured themes that form the backdrop against which AGMs and shareholder voting will play out in 2023. Ideally, companies want to see voting outcomes well managed, likely issues flagged well ahead of time, and potential dissent mitigated or curbed before the vote reports force a corporate governance A&E to manage in the last 48 hours before the deadline. Investor policies and retail sentiment are driving heightened scrutiny around the complex, ESG-driven voting agenda more than ever. Knowing your voter is therefore more critical than ever, as is engaging with them and their influencers to mitigate shock. Here we look at some of the thematic expectations for 2023 and a reasoned approach to managing them.

Jonathan Harker is senior director and head of account management – EMEA at Morrow Sodali.
j.harker@morrowsodali.com

Andrew Stevenson is senior director and head of international engagement at Morrow Sodali.
a.stevenson@morrowsodali.com

> **"Stakeholders want restraint in executive pay and pensions, aligning the experience of the wider workforce"**

Executive remuneration

Always controversial, and hot again in 2023. In the UK, 2022 was the third year-on-year increase in contested remuneration reports. With high levels of inflation and crises in living and energy costs, stakeholders want restraint in executive pay and pensions, aligning the experience of the wider workforce. Remuneration looks to have returned to pre-pandemic levels or even subject to increases, and the rationale that it is a post-COVID correction is hard to swallow.

Some sectors may get more scrutiny than others, such as those with large, low-paid workforces that have endured tough times, for example retail, hospitality and transport. As will companies whose profits are resultant from difficult geo-political circumstances, including energy companies that have arguably profited from war, and banks because they service the mortgage-stricken.

We have seen an increase in ESG-related KPIs regarding director remuneration, particularly relating to climate targets, and there is a recognised necessity for ESG KPIs in the context of long-term rather than short-term strategy.

Ultimately, restraint is expected and egregious amounts will not be tolerated.

Director votes and board accountability

Year upon year we see increases in the targeting of director elections as an escalation of topical dissent, with more variety in the motivation. We foresee greater dissent on diversity – ethnic, not just gender – with more votes against the chairs of nomination committees or other responsible members. There are more demands on the board today. The complexities are deeper and broader. If a board cannot demonstrate adequate oversight of these specific themes, we will see more dissent from the investor.

If companies are struggling with accountability or having issues with the skill sets of directors, this may present a good opportunity for an activist, whether it is a traditional hedge fund activist or a concerned shareholder. Companies need to understand what needs to be communicated, have comprehensive disclosure about credible plans, and the board needs to be trained so that it can engage on every topic.

Board skills, diversity and overboarding

With increasing complexity in the opportunities, challenges and the sheer number of topics a board must address, it is important that directors represent stakeholders and demonstrate that they carry the right combination of skills and are not over-committed. Investors need assurance that directors can contribute to all the meetings they attend and give all mandates the attention they deserve.

Over the last two years, we have observed a shift from gender diversity to diversity in its broader sense. We believe ethnic diversity will be firmly on the agenda for 2023. It comes back to the overall policy, the steps the company is taking, the journey they are on, and where they are now. Diversity can be very political and needs a credible plan. A board assessment or regular evaluation exercise is the bedrock to engagement with investors around succession and why a company might not be able to satisfy a target.

If a company has concerns about 'overboarding', it needs to look at the size, location and scope of the companies where directors have mandates. There are several ways to test whether a director can fulfil their fiduciary duties. Proxy advisors have solid red flags that are not adjustable with engagement but, once a potential issue is identified, it is imperative to engage on this with shareholders who are more open to context.

Shareholder resolutions, voting and say on climate

In 2022 we saw softer than expected support for the ambitious proposals on climate that were put forward by both companies and investors. Shareholders have been sceptical about simplistic environmental proposals. Companies must be more definitive about the targets they adopt and justify why they are meaningful. Investors are looking for substance and SMART (specific, measurable, achievable, relevant, and time-bound) targets, so we expect more dissent in the absence of detail and science-based targets. Investors are committed to ESG principles, and year-on-year we see more shareholder resolutions being filed.

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Materiality now in all things ESG is critical. Businesses with a relatively small workforce and small carbon footprint will likely face more 'social' issues, and how they manage people will trump the environmental factors. Say on climate resolutions may not be a priority for all, and it is important to be in tune with investor focus, especially with heightened market volatility.

Avoiding surprises at the AGM

The key is knowing your shareholders and conducting effective, measured stakeholder engagement. To prevent surprises, we need to know whom we are dealing with and what their perceptions are of governance, performance and strategy. IR teams are much closer to board members these days and they need to inform the board of changing sentiment and rising concerns.

It is critical that companies have a year-round strategy for engaging with stakeholders. That process starts as soon as the last AGM has finished in a self-enriching cycle. Boards tend to engage with the top shareholders, but they need to engage with a number of investors of all sizes. Larger investors, whilst powerful in a vote, may not be indicative of all the views down the register, which could harbour activists or the negative sentiment of collective retail investors.

In recent years there has been a shift in IR teams toward working more closely with the company secretary, who is the de facto chief governance officer of a company. As well as maintaining dialogue with the portfolio managers, they should target the governance/stewardship teams who have more control over the vote.

Investors and proxy advisors expect responsiveness. To be prepared, companies must look at negative votes from the prior AGM and engage with dissenters. A long cycle is essential to avoid the heat of the season when everyone is trying to resolve critical issues quickly. Proxy advisors issue updated guidelines annually, so it is good to review these and engage on any foreseeable issues. The main proxy advisors should be treated like an investor and a medium of communication. They can be contacted via their platforms, and company secretaries are likely to know these channels already.

Boards themselves should be open to engagement all year round and give investors as long as possible to consult on policies. Investors expect the board to be able to enunciate strategy, and any one member of the board should, effectively, be able to engage with any investor. It is important to make sure it is not completely enshrined at the chair/executive level. That being said, when meeting investors, it is advisable that companies offer up independent directors. This will help investors to get a feel for the inner workings of the board, giving them an opportunity to ask questions around topics such as board composition, independence and effectiveness, to name but a few.

Conclusion

If a company expects difficulties on a forthcoming vote, it must get to grips with the shareholder base. How do they behave? How will they vote? Will they vote? To anticipate market reactions to strategic initiatives or governance changes, homework has to be done; mechanisms are needed to track sentiment. Similarly, if a company wants to increase turnout, it is vital to understand the shape of shareholder behaviour, and how to mobilise the different constituencies. Being prepared is vital to a successful AGM. ■