REWARD VALUE

Reward Value Background Note

Managerial and Capital Market Short Termism

Short-termism is an issue, maybe as a result of investor nearsightedness, but definitely as a result of poorly designed executive compensation. Additionally, whilst stakeholderism cannot necessarily be equated with long-termism, there may be a mismatch between societal and shareholder time preferences and/or sub-optimal long-term societal value creation due to market failures. The issues of corporate financial short-termism and societal long-term value creation (e.g. the need for climate action) thus may intersect. Corrective policy action is warranted to achieve societal first-best outcomes, but should avoid constraining investor behavior. Instead, policies targeted at facilitating and leveraging share- and stakeholder monitoring and voice, combined with executive remuneration reform seem more appropriate.

Introduction

There exists widespread concern about short-termism in firm decision making and capital markets. Short-termism is often taken to be the idea that investors and firm executives unduly sacrifice future value and growth by investing insufficiently in the "long term", but instead reap (high) current period profits at the expense of (in net present value terms) higher future profits. Concerns over such practices have sparked significant public debate as well as (increasing) calls for public intervention.

The European Commission's consultations on Sustainable Corporate Governance explicitly references short-termism as a challenge.[1] Alongside the European Commission, the concerns about short-termism are felt by several other institutes and organizations. For example, from a regulator perspective, all three financial regulators in Europe,

[1] See European Commission (2020). Public consultation sustainable corporate governance.

EBA[2], EIOPA[3] and ESMA[4], have already highlighted their concerns in their contributions to the consultation on the Renewed Sustainable Finance Strategy of the European Commission. Concerns about short-termism also inspired BlackRock, CPPIB, the Dow Chemical Company, McKinsey and Tata Sons to co-found FCLT Global – a not-for-profit organization working across the investment value chain in support of a growing long-term orientation.[5] UNPRI has also voiced concerns about short-termism in the investment value chain, as expressed in their mission statement.[6]

Many of such calls for action often assume, note and/or as a backdrop see an interdependency between corporate (often: financial) short-termism, and the challenges in achieving societal outcomes with long-term value – most notably, the need for climate action. Care is required when linking questions of *horizon* (short-term vs. long-term) to questions of *objective* (shareholder value vs. stakeholder/societal value). Investors and firms striving for shareholder value maximization may be short-termist by not investing in assets with long-term value, or long-termist by doing exactly so. Likewise, stakeholders may be short-termist by making demands that are detrimental to the firm's long-term financial health , or long-termist by promoting a dynamic business environment. In the context of societal value creation, the issue of (for lack of a better word) "short-termism" then is to what extent *future total value* (both shareholders *and* stakeholders) is *unduly low* as a result of *nearsighted actions* by *either* shareholder *or* stakeholders. This frames the issues more broadly than the definition noted above that reflected on the trade-off between current and future (firm) profits, but that is not to say that fundamentally stakeholder value can always be equated with long-termism (or shareholderism with short-termism). At the same time, it remains the case that there exist widespread concerns over both stakeholder interests in corporate value creation as well as short-termism in shareholder- and managerial time horizons. Whilst it is useful in setting (regulatory) policies, to consider whether (and if, to what extent) time horizons and stakeholder objectives interact (e.g. long-term effects of climate change disproportionately affecting stakeholders vis-à-vis shareholders?), optimal policy design is typically nevertheless directly targeted at short-termism or stakeholder value creation specifically.

Reviewing short termism

The academic literature on short-termism often deals separately with short-termism by investors and short-termism by managers at the firm level ('managerial myopia'). The distinction is important, yet often ignored in public or policy debates, and its implied nuances can help suggest a way forward.

Investor short-termism

With respect to investor short-termism, the picture is often mixed. It is difficult to fully reject the canonical finance argument that the decision to buy or sell a share in a firm is a reflection of (discounted) expected future cash flows. Anecdotally, Tesla's valuation is high despite low current earnings because investors expect that the company will be (highly) profitable in the future. Empirically, expectations of future earnings matter for the level of the stock market.[7] On

[2] EBA (2019). Report on undue short-term pressure from the financial sector on corporations.
[3] EIOPA (2019). Potential undue short-term pressure from financial markets on corporates: Investigation on European insurance and occupational pension sectors.
[4] ESMA (2019). Undue short-term pressure on corporations.
[5] See fcltglobal.org/about/.
[6] UN PRI (2020). PRI strategic plan 2021-24 consultation paper
[7] Greenwood, R. & A. Shleifer (2014). Expectations of Returns and Expected Returns. *Review of Financial Studies* 27(3), 714-746. Note that this is not to say that investors may not err in their expectations or that expectations always conform to rational expectations.

the other hand, firms that (marginally) adopt a long-term outlook create more value, not just for shareholders, but also for other stakeholders.[8] If this is the case, then the open question is why shareholders do not force firms to always be long-termist.

Whilst part of the answer may be that this is the result of investors nearsightedness, the academic literature on investor short-termism is mixed. Public firms invest less than private firms, especially in industries where asset valuations are sensitive to earnings news (a fact consistent with short-termist distortions of investment decisions)[9], but preliminary evidence suggests that this gap disappears when controlling for firm quality.[10] Money managers may however also depress corporate innovation by inducing short-termist pressures on firms.[11] Conversely and contrary to the view that large investors drive corporate short-termism, institutional ownership spurs R&D and especially R&D productivity.[12] Quarterly corporate reporting dampens corporate investments[13], but contrarian evidence also exists[14].

Additionally, investor behavior that is often perceived as short-termist does not necessarily have to come at the expense of the long run or does not necessarily have to be the result of a short-termist outlook. In fact, the opposite may be true. Intervention by activist investors and hedge funds can improve long term firm outcomes.[15] Short selling (or the threat thereof) can also discipline managers[16] (to create long term value), which is important given the fact that unchecked managers destroy (long-term) value.[17]

In short, although there is evidence that investor behavior contributes to capital market short-termism (esp. reporting frequency), and notwithstanding that such behavior should be addressed, the evidence is mixed and an overzealous focus on possible investor short-termism may also risk throwing out the baby with the bath water. Nuance is important for the right policy diagnosis and prescription.

Managerial myopia

With respect to managerial myopia, a similar picture appears. Few executives will boldly declare that they do not care one bit about the long run, yet the oft quoted figure is that 78% of executives say that they would scrap long term projects for short term gains.[18] Executives may hold off on discretionary expenditures to beat analyst forecasts, which

[8] Flammer, C. & P. Bansal (2017). Does a long-term orientation create value? Evidence from a regression discontinuity. *Strategic Management Journal* 38(9), 1827-1847.
[9] Asker, J., J. Farre-Mensa & A. Ljungqvist (2014). Corporate Investment and Stock Market Listing: A Puzzle? *Review of Financial Studies* 28(2), 342-390.
[10] Maksimovic, V., G. Phillips & L. Yang (2019). Do Public Firms Respond to Industry Opportunities More Than Private Firms? The Impact of Initial Firm Quality. *NBER Working Paper 25634.*
[11] Agarwal, V., R. Vashishtha & M. Venkatachalam (2017). Mutual Fund Transparency and Corporate Myopia. *Review of Financial Studies* 31(5), 1966-2003.
[12] Aghion, P., J. Van Reenen & L. Zingales (2013). Innovation and Institutional Ownership. *American Economic Review* 103(1), 277-304.
[13] See amongst others, Kraft, A., Vashishtha, R. & M. Venkatachalam (2018). Frequent Financial Reporting and Managerial Myopia. *Accounting Review* 93(2), 249-275.
[14] Kajuter, P., F. Klassmann & M. Nienhaus (2019). The Effect of Mandatory Quarterly Reporting on Firm Value. *Accounting Review* 94(3), 251-277.
[15] Brav, A., W. Jiang, S. Ma & X. Tian (2018). How does hedge fund activism reshape corporate innovation? *Journal of Financial Economics* 130(2), 237-264.
[16] Fang, V., A. Huang & J. Karpoff (2015). Short Selling and Earnings Management: A Controlled Experiment. *Journal of Finance* 71(3), 1251-1294. Massa, M., B. Zhang & H. Zhang (2015). The Invisible Hand of Short Selling: Does Short Selling Discipline Earnings Management? *Review of Financial Studies* 28(6), 1701-1736.
[17] See e.g. Harford, J., M. Humphery-Jenner & R. Powell (2012). The sources of value destruction in acquisitions by entrenched managers. *Journal of Financial Economics* 106(2), 247-261.
[18] Graham, J., C. Harvey & S. Rajgopal (2005). The economic implications of corporate financial reporting. *Journal of Accounting and Economics* 40(1-3), 3-73.

increases firm value in the short run, but decreases firm value in the long run.[19]

Such behavior may be driven by executives' compensation packages. The literature on this topic is somewhat more unequivocal in signaling potential short termism, especially with respect to potential short-termist manipulation. Whilst managerial compensation historically has increasingly aligned managerial and shareholder interests[20], and CEO pay is related to CEO talent, firm size, as well as performance[21], executives cut discretionary expenditure surrounding vesting dates and are more likely to just meet analyst's expectations.[22] Executives strategically release (discretionary positive) news equity vesting months.[23] Preliminary evidence suggests that in vesting months, firms have a higher probability of share repurchase or M&A activity, but that those decisions hurt long-term value.[24] Short pay durations may increase the incentive for manipulating short term performance, although it should be noted that firms may self-select into short or long term pay durations.[25] Investment is cut when executives' incentives become short term.[26] There is a risk that such manipulation is more prevalent for executives nearing the end of their terms.[27]

Stakeholders and market failures

In the context of societal value creation, the Introduction suggested that the issue of (for lack of a better word) "short-termism" is sometimes reframed as a question of to what extent *future total value* (both shareholders *and* stakeholders) is *unduly low* as a result of *nearsighted actions* by *either* shareholder *or* stakeholders. Note that the distinction between share- and stakeholders is unhelpfully artificial if their value objectives and time horizons overlap. The question then is to what extent this is the case. Again, the issue is nuanced.

On the one hand, it is not the case that investor and stakeholder interests never align. In fact, they may often at least partially do so, as share prices at least to some extent reflect issues such as employee satisfaction, material stakeholder issues, and environmental considerations.[28] Indeed, the adoption of long-term equity pay plans (by shareholders) appears to drive both shareholder *and* stakeholder value creation[29].

On the other hand, conflicts between share- and stakeholder horizons do exist. Preliminary

[19] Bhojraj, S., P. Hribar, M. Picconi & J. McInnis (2009). Making Sense of Cents: An Examination of Firms That Marginally Miss or Beat Analyst Forecasts. *Journal of Finance* 64(5), 2361-2388.
[20] Frydman, C. & R. Saks (2010). Executive Compensation: A New View from a Long-Term Perspective, 1936–2005. *Review of Financial Studies* 23(5), 2099-2138.
[21] Gabaix, X. & A. Landier (2008). Why has CEO Pay Increased So Much? *Quarterly Journal of Economics* 123(1), 49-100.
[22] Edmans, A., V. Fang & K. Lewellen (2017). Equity Vesting and Investment. *Review of Financial Studies* 30(7), 2229-2271.
[23] Edmans, A., L. Goncalves-Pinto, M. Groen-Xu & Y. Wang (2018). Strategic News Releases in Equity Vesting Months. *Review of Financial Studies* 31(11), 4099-4141.
[24] Edmans, A., V. Fang, & A. Huang (2020). The Long-Term Consequences of Short-Term Incentives. *ECGI Working Paper* 527/2017.
[25] Gopalan, R., T. Milbourn, F. Song & A. Thakor (2013). Duration of Executive Compensation. *Journal of Finance* 69(6), 2777-2817.
[26] Ladika, T. & Z. Sautner (2020). Managerial Short-Termism and Investment: Evidence from Accelerated Option Vesting. *Review of Finance* 24(2), 305-344.
[27] Edmans, A., X. Gabaix, T. Sadzik & Y. Sannikov (2012). Dynamic CEO Compensation. *Journal of Finance* 67(5), 1603-1647. Marinovic, I. & F. Varas (2019). CEO Horizon, Optimal Pay Duration, and the Escalation of Short-Termism. *Journal of Finance* 74(4), 2011-2053.
[28] See Edmans, A. (2011). Does the stock market fully value intangibles? Employee satisfaction and equity prices. *Journal of Financial Economics* 101(3), 621-640. Eccles, R., I. Ioannou & G. Serafeim (2014). The Impact of Corporate Sustainability on Organizational Processes and Performance. *Management Science* 60(11), 2835-2857. Khan, M., G. Serafeim & A. Yoon (2016). Corporate Sustainability: First Evidence on Materiality. *Accounting Review* 91(6), 1697-1724.
[29] Flammer, C. & P. Bansal (2017). Does a long-term orientation create value? Evidence from a regression discontinuity. *Strategic Management Journal* 38(9), 1827-1847.

theoretical analysis suggests that some short termism may be optimal for shareholders, though this may come at the expense of bond holders.[30] Even in optimal contracts, agency conflicts can induce both non-first-best short-term and long-term investment levels.[31] The issue with respect to multiple stakeholders then largely is the extent to which share- and stakeholder time horizons and outcomes overlap so that societal welfare is optimized. Here there may be some cause for concern. Although share prices do reflect intangibles, the link is not perfect.[32] Social discount rates are typically lower than discount rates implied by the equity risk premium, implying that shareholders may discount the future at a faster rate than societal stakeholders would.[33] As noted above, corporate equity prices reflect sustainability considerations, yet it is unclear to what extent this is sufficient to address demonstrable market failures with respect to climate change for instance.

Policy considerations

In our view, the literature highlights that short-termism is an issue that needs to be addressed. The evidence on the extent to which short-termist behavior is driven by investors is mixed, but that need not be a reason to not worry about short-termism. Even if investors are actually long-termist, poorly designed incentives for executives can cause adverse short-termist behavior. Even if investors are actually long-termist, it may still be the case that investor time horizons are different from societal time horizons and that market failures generate non-first-best societal outcomes. This take on the issue has several implications for public policy.

- Helpful policies target market failures as directly as possible as to further increase the alignment between (long term) share- and stakeholder outcomes. This is part of the reason why *carbon taxes* are often seen as the most effective policy tool available in dealing with climate change. To the extent to which such policies prove to be infeasible to implement, alternative policies that try to mimic an actual price mechanism may be supportive. Assessing and quantifying the impact companies have on societal stakeholders and the environment is one approach.[34] The development of such impact assessments may be supported by harmonization of reporting, disclosure and accounting frameworks and requirements. We stress that this is a pragmatic choice and, in many cases, sub-par to more direct interventions such as actual and/or adequate carbon pricing.
- Disclosure and assurance on corporate impacts are useful *tools* to facilitate governance mechanisms such as voice and engagement. Voice and exit are complementary governance mechanism, but voice precedes exit and long-term investors

[30] Hackbarth, D., A. Rivera & T. Wong (2018). Optimal short-termism. *ECGI Working Paper* 546/2018.
[31] Gryglewicz, S., S. Mayer & E. Morellec (2020). Agency conflicts and short- versus long-termism in corporate policies. *Journal of Financial Economics* 136(3), 718-742.
[32] See Edmans, A. (2011). Does the stock market fully value intangibles? Employee satisfaction and equity prices. *Journal of Financial Economics* 101(3), 621-640.
[33] Compare Heal (2017). The Economics of the Climate. *Journal of Economic Literature* 55(3), 1046-1063, who references that a social discount rate of 2.5-3% would be considered high, to Jorda, O., K. Knoll, D. Kuvshinov, M. Schularick & A. Taylor (2019). The Rate of Return on Everything, 1870-2015. *Quarterly Journal of Economics* 134(3), 1225-1298, who report historical returns on risky assets of ±7% and ±2% on safe assets. Similarly, Wibbens, P. & Siggelkow, N. (2020) Introducing LIVA to measure long-term firm performance. *Strategic Management Journal* 41(5), 867-890 employs a constant cost of capital of market performance to discount financial returns, whereas Freiberg, D., D. Park, G. Serafeim & T. Zochowski (2020). Corporate Environmental Impact: Measurement, Data and Information. *HBS Working Paper 20-098* employs social discount rates of 0-3%.
[34] See e.g. Freiberg, D., D. Park, G. Serafeim & T. Zochowski (2020). Corporate Environmental Impact: Measurement, Data and Information. *HBS Working Paper 20-098*.

intervene more intensively.[35] Facilitating voice, then, strengthens corporate governance, especially by active engagement of (long-termist) investors.

- Relatedly, whilst disclosure and assurance on corporate impacts enables monitoring and/or lowers the cost of monitoring, the benefit of monitoring (long-term value) and engagement is greatest for shareholders with large stakes ('blockholders').[36] Although identification of causal effects is challenging[37], there is evidence suggesting that blockholders can significantly influence corporate policies[38], increase payouts to shareholders[39], drive long-term (financial) performance[40], as well as ESG outcomes[41], irrespective of whether blockholders are traditional activists or passive investors.[42] Enabling monitoring, voice and the threat of potential exit by blockholders may then be a supporting factor for long-term (societal) value creation.
- An open question is to which extent (blockholder) voice provides an adequate safeguard for societal value creation if the principals with voice are (predominantly) shareholders. If engagement may direct firms towards better societal outcomes and if there are unresolved residual market failures unaddressed by public policy, there may be a case for organizing increased stakeholder voice to the effect of generating better societal outcomes. We stress that this is an open question – as of yet it is unclear what the advantages and disadvantages of more shared governance would be, and/or (beyond if) how it should be organized.[43]
- Voice, compensation and firm performance are related. Blockholder engagement affects executive compensation[44], privately owned firms with 'strong principals' (private equity sponsors) have different compensation policies than public firms with dispersed owners[45], and say-on-pay legislation has affected executive remuneration and strengthened the link between pay and performance.[46] This link between pay and performance can be employed to spearhead long term value creation (or at least to prevent incentives actively pulling or pushing executives in the 'wrong' direction). Long-term pay plans drive long-term value creation

[35] McCahery, J., Z. Sautner & L. Starks (2016). Behind the Scenes: The Corporate Governance Preferences of Institutional Investors. *Journal of Finance* 71(6), 2905-2932.
[36] Edmans, A. (2009). Blockholder Trading, Market Efficiency, and Managerial Myopia. *Journal of Finance* 64(6), 2481-2513.
[37] See Edmans, A. & C. Holderness (2017). Blockholders: A Survey of Theory and Evidence. *Handbook of the Economics of Corporate Governance Volume I,* 541-636.
[38] Cronqvist, H. & R. Fahlenbrach (2008). Large Shareholders and Corporate Policies. *Review of Financial Studies* 22(10), 3941-3976.
[39] Crane, A., S. Michenaud & J. Weston (2016). The Effect of Institutional Ownership on Payout Policy: Evidence from Index Thresholds. *Review of Financial Studies* 29(6), 1377-1408.
[40] See above e.g. Aghion, P., J. Van Reenen & L. Zingales (2013). Innovation and Institutional Ownership. *American Economic Review* 103(1), 277-304, and Brav, A., W. Jiang, S. Ma & X. Tian (2018). How does hedge fund activism reshape corporate innovation? *Journal of Financial Economics* 130(2), 237-264.
[41] Dimson, E., O. Karakas & X. Li (2015). Active Ownership. *Review of Financial Studies* 28(12), 3225-3268.
[42] Appel, I., T. Gormley & D. Keim (2016). Passive investors, not passive owners. *Journal of Financial Economics* 121(1), 111-141.
[43] Preliminary evidence from Germany and Finland suggests that mandated board representation of workers has no effect on wages, but possibly on capital formation – see Jager, S., B. Schoefer & J. Heining (2019). Labor in the Boardroom. *NBER Working Paper 26519*.
[44] Cronqvist, H. & R. Fahlenbrach (2008). Large Shareholders and Corporate Policies. *Review of Financial Studies* 22(10), 3941-3976.
[45] Cronqvist, H. & R. Fahlenbrach (2013). CEO contract design: How do strong principals do it? *Journal of Financial Economics* 108(3), 659-674.
[46] See Ferri, F. & D. Maber (2012). Say on Pay Votes and CEO Compensation: Evidence from the UK. *Review of Finance* 17(2), 527-563. Correa, R. & U. Lel (2016). Say on pay laws, executive compensation, pay slice, and firm valuation around the world. *Journal of Financial Economics* 122(3), 500-520.

for both share- and stakeholders.[47] Contracting CSR outcomes correlates with better financial and non-financial outcomes.[48]

- Relatedly, note that say-on-pay is (increasingly) employed as a de facto say-on-performance.[49] In the context of shareholder engagement and voice, the need to address unresolved market failures to generate optimal societal outcomes, as well as the necessity of pay reform, it may be warranted to codify and extend the 'say-on-pay as say-on-performance'-practice into broader legislation that facilitates a share- and/or stakeholder say on purpose, performance and pay.
- Given the positive value of share- and stakeholder engagement, policy makers should be careful when considering policies that may be summarized by the quip "the advantage of [a policy] is that it protects entrepreneurial management from the demands of ordinary shareholders; the disadvantage of [a policy] is that it protects entrepreneurial management from the demands of ordinary shareholders."[50] Policies that limit the room, decrease the benefit, and/or increase the costs for share- and stakeholder demands, engagement and/or ultimately exit may have adverse side effects that limit their effectiveness.
- Lastly, more and better share- and stakeholder engagement and executive pay reform may not be the end-all-be-alls of achieving better long-term societal outcomes. Corporate governance reform may be a useful second-best solution as long as first-best public policies are not implemented, a useful supporting measure for first-best public policies when or if first-best policies are implemented, but not necessarily a silver bullet. At the same time, this is not to debase the merits of governance and compensation reform. Better compensation policies and corporate governance may serve as catalysts for change; or conversely, not improving board room practices may prevent directed firm action towards better societal outcomes.

Conclusion and policy suggestions

In short, short-termism is an issue that warrants remedy. Although in many cases public policy is the first-best response, board room reform is a useful contributing factor without change will be more difficult ('catalyst for change'), a (temporary) second-best solution as long as optimal public policies prove infeasible to implement, or both.

Given the preceding policy considerations, we offer the following suggestions for policy makers and regulators:

- Harmonize and mandate the use of audited non-financial disclosures that reflect the (long-term) impact that firms have on stakeholders. Convergence of work-in-progress private sector initiatives (see e.g.

[47] Flammer & Bansal (2017). Does a long-term orientation create value? Evidence from a regression discontinuity. *Strategic Management Journal* 38(9), 1827-1847.
[48] Flammer, C., B. Hong & D. Minor (2019). Corporate governance and the rise of integrating corporate social responsibility criteria in executive compensation: Effectiveness and implications for firm outcomes. *Strategic Management Journal* 40(7), 1097-1122.
[49] The effect of say-on-pay on the level of executive compensation is often conditional on poor performance, see Ferri, F. & D. Maber (2012). Say on Pay Votes and CEO Compensation: Evidence from the UK. *Review of Finance* 17(2), 527-563.
[50] The quote originally is about dual class shares, and reportedly due to Financial Times columnist Andrew Hill.

IFRS[51], WEF[52], the 5 standard-setters: SASB, CDP, CDSB, GRI and IIRC[53]) is promising. At the same time, ensuring consistency with policy and mandated disclosures (e.g. NFRD) is essential. An open question is what disclosures should be mandated. Not all disclosures are relevant for all firms and some disclosures may reflect intangibles too imperfectly to add value. Note that the need for mandated non-financial disclosures can be sidestepped if policies are implemented that directly affect firm's bottom lines – e.g. a carbon tax.

- The integration of reporting with shareholder rights may be helpful. Consider mandating a separate vote on 'non-financial statements' in addition to the required vote on financial statements. If companies report on or move to reporting on an integrated basis, the suggested bipartite vote should be upheld and reflect a vote on financial value and a vote on non-financial value.
- Develop corporate governance and reporting guidance to help bridge the gap between legal requirements and stakeholder expectations. Firms (are required to) discuss corporate strategies in annual reports, but detail with respect to how policies and major corporate decisions are consistent with long-term value creation for both share- and stakeholders is often insufficient. Guidance may be a remedy. Special attention may be given to major capital decisions, e.g. buy backs/dividends, mergers, or investments. With respect to buy back for instance, firms should be expected to explain in sufficient detail e.g. the extent to which current shareholder capital distribution comes at the expense of future profitability and the extent to which firm shock resistance is reduced.
- Relatedly, consider extending say-on-pay legislation to incorporate purpose, performance and pay. Say-on-pay is turning into a de facto say-on-performance ('is pay appropriate given how the company performed?'). Codifying this practice creates transparency and increasing the scope to purpose creates room for discussion ('is performance appropriate given purpose and does pay adequately reflect both?').
- Investigate whether blockholder formation can be facilitated by harmonizing capital market practices. Governance regimes and capital market regulations differ across Europe and this creates transaction costs. Notification requirements for major holdings for instance differ across jurisdictions and may imply hurdles for block formation (or increasing block size). Investigate the optimal notification threshold.
- Investigate whether more stakeholder-oriented governance models can be a contributing factor to safeguarding long-term stakeholder interests in corporate policies, and if so, how such models should be organized (seat at the table vs. actual hard power; organized at management, board or AGM level; etc.).
- Investigate whether quarterly reporting/guidance should be discouraged. Although quarterly reporting may facilitate monitoring of firm behavior by share- and stakeholders and supports positive

[51] *Consultation Paper on Sustainability Reporting*. IFRS, September 2020.
[52] *Toward Common Metrics and Consistent Reporting of Sustainable Value Creation*. WEF, Deloitte, EY, KPMG, PWC, 22 January 2020.
[53] *A powerful interim step towards a single, coherent global set of reporting standards*. Shared vision from GRI, CDP, CDSB, IIRC & SASB, 11 September 2020.

engagement, it may also overly direct attention to the short term in the sense that i) private firms exempt from quarterly reporting display different investment behavior, and ii) executives at public firms sometimes change policies just for the sake of making quarterly expectations. This implies a trade-off and it is unclear whether this trade-off currently is optimized.

- Drive pay reform. Currently, executive pay is skewed towards annual financial targets and payouts, even for ostensibly long-term pay components in the sense that LTIPs often feature rolling annual vesting. This induces short-termist behavior that needs to be addressed. In addition to pay reform at public entities, consider the 'value chain effects' in pay reform. Altering pay practices at public firms may alleviate short-term pressures, but if asset manager compensation remains short-term focused, short-termist pressures in engagement could persist. For a sketch of the outlines of a future-proof remuneration model, see our Green Paper[54].

[54] *Reward Value Green Paper*. Reward Value, December 2020. See rewardvalue.org.