

CASE STUDY

September 2019

HYUNDAI MOTOR



Engagement objective: **Governance**
Board composition and effectiveness



Engagement objective: **Environment**
Carbon emissions and sustainable vehicle technology

Hyundai Motor has improved its board composition and skill sets, making progress from its historically dominant founding family, and acknowledging minority shareholder interests. Hermes EOS has engaged with the company since 2008 on various issues and continues to press for gender diversity on the board and tackle sustainability challenges.

Background

The company is part of a large conglomerate with a number of affiliated companies, where the founder family continues to hold a significant stake through circular shareholdings. This was illustrated by a controversial land purchase in 2014, which raised questions about a lack of transparency in the process and misalignment of interests between controlling and non-controlling shareholders.

Hermes EOS has engaged on governance issues since 2008, including our support of an investor coalition through a joint letter and AGM attendance, to seek wide-ranging corporate governance reforms – a highly unusual practice in South Korea.

This case study highlights our engagement following this, and the importance of a board consisting of directors with the right diversity of skills and experience to protect minority interests.

The company's non-executive directors have traditionally come from an academic, legal or accounting background and lacked ample business or management experience.

In addition to the corporate governance challenges, the company was ranked as a relatively poor corporate sustainability performer, particularly from the perspective of the emissions of its vehicles in a 2015 report by CDP¹.

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Company overview

Hyundai Motor is a South Korean manufacturer of automotive vehicles, which is also engaged in financial and other businesses. Including its approximately one-third share in KIA Motors, it is one of the world's largest vehicle manufacturers, selling over seven million vehicles in 2018, over 50% of which were sold overseas.

¹ <https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/cms/reports/documents/000/000/618/original/auto-report-exec-summary-2015.pdf?1470224892>

Our engagement

In our meeting with the newly appointed lead independent director in 2015, who headed the company's corporate governance committee, we raised concerns as to whether the independent directors displayed the requisite balance of skills and experience required for a major international company.

We followed this up with a series of meetings in Seoul, including one with the same director at his university office in early 2016 where we pressed the company to embark on an externally facilitated board evaluation, with the expectation that this would lead to significant refreshment of the board. We also suggested that it allow shareholders to propose candidates to the nomination committee and referenced examples of companies that had successfully done this.

Initially, Hyundai Motor was reluctant to adopt the recommendations, although it did acknowledge that the board would benefit from greater diversity and that it was considering our suggestion of recruiting a board member with an international background. We continued to press for an external board evaluation and proposed an initial development of a self-assessed board director skills matrix as a means of triggering improved diversity.



Engagement timeline

- 2008** began engagement with Hyundai
- 2015** raised new governance concerns with lead independent director
- 2016** pressed for an external board evaluation
- 2017** continued efforts and raised environmental concerns
- 2018** met with independent chair

We also raised our concerns about the apparent weakness in the company's sustainability performance, particularly the carbon intensity of its vehicles, as revealed in a report published by CDP. We introduced it to CDP to better understand the results and following this, the company acknowledged its performance could be improved. It then shared its improvement plans, including catching up with Japanese peers who had invested earlier and more decisively in green technologies, and enhancing communications around this.

With little initial improvement, we continued to question vehicle sustainability performance over the next three years, including meeting with the independent chair in 2018.

Changes at the company

In 2018, the company announced it would seek shareholder nominations for an independent director and conduct an internal board evaluation.

In early 2019 a team of five external governance specialists reviewed a range of candidates suggested by shareholders for the role of independent director responsible for shareholder rights protection. They highlighted the skills gaps in the current board including international expertise, an understanding of shareholder interests and governance knowledge. The subsequent election at the AGM of one of these candidates and others nominated by the company, replacing directors with academic backgrounds, has materially improved relevant skills and the experience. They included a non-Korean national as executive director, who had previously worked for another global automotive manufacturer.

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In our recent meeting with the new shareholder-nominated independent director, we were comforted by his clear understanding of shareholder concerns about the need to strengthen minority protection and the proposals he had made to improve board effectiveness, drawing on his past experience at a global financial institution.

In addition, Hyundai Motor has made good progress on improving the sustainability of its vehicles, launching a number of lower emissions models including IONIQ, which is offered in hybrid, plug-in hybrid and fully electric variants, and KONA Electric, the first fully electric compact sport utility vehicle. The company is also accelerating the development and promotion of hydrogen fuel cell vehicles and is planning to substantially increase its sustainable vehicle models from approximately 3.8% to 20% of total sales by 2025. Moreover, the company has set up an ESG taskforce consisting of investor relations, sustainability and procurement teams, and is considering setting up a science-based target on carbon emissions.

Next steps

Despite the improvements in board independence and skills, we will continue to assess the effectiveness of the board, especially in protecting the interest of minority shareholders. Given a lack of gender diversity with no women on the board, we continue to press for the appointment of the first female director and to argue for an external board evaluation. We will also monitor improvements in overall fleet emissions to ensure that the company makes progress against peers.



Sachi Suzuki
Engagement, Hermes EOS

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