OUTCOMES BEYOND PERFORMANCE

THE (NEW) WORKING WORLD

Part III: promoting workplace well-being

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HERMES INVESTMENT MANAGEMENT

8 DECENT WORK AND ECONOMIC GROWTH

PART III: PROMOTING WORKPLACE WELL-BEING

This is the third part of a four-part paper on SDG 8 – decent work and economic growth. In our first two instalments, we demonstrated how we are engaging with companies on their hiring practices and efforts in the shift towards fairer pay outcomes. In this paper, we progress to the issue of employee benefits.

Key points:

- **Investing in employee well-being leads to higher productivity and boosts the business bottom line.**
- **Companies will seemingly get the best employee satisfaction result by focusing on three core offerings: health insurance, paid holiday allowance and pension plans.**
- **Many companies are pre-empting the threat posed by poor employee health by introducing so-called 'wellness programmes' where any upfront cost is more than compensated by higher productivity, lower staff turnover and reduced healthcare expenses.**

Our investment focus on SDG 8 intersects with a number of the other Global Goals (see 'Part I: getting to work on SDG 8'). We engage with companies on four questions:

1. **Who are companies employing** – are there opportunities to provide mutually beneficial employment opportunities to individuals from deprived communities or from higher unemployment constituencies?
2. **How much do they pay** – are companies paying a fair and 'living' wage to direct and indirect workers to enable them to live dignified lives?
3. **What additional financial and non-financial benefits are provided** – are employees coming to work healthy, motivated and thus productive?
4. **Development and training** – with human capital a rented asset, are companies sufficiently developing their people by investing in opportunities for employees to advance their skills and careers?

Already, we have tackled the question of who companies are employing: in the first instalment of this paper, we showed that among others, two portfolio companies – **SSP** and **Cineworld** – have potential to embrace an 'Opportunity Employment' mindset, expanding their frontline recruitment efforts to reach under-tapped talent pools, such as youth (the disproportionate population of young people who are out of school and out of work), persons with disabilities or ex-offenders.

More recently, we addressed the issue of fair pay. As evidenced by our engagement with portfolio company **AMN Healthcare Services**, a healthcare staffing company, gender pay inequality is an issue across professions, seniority and regions. Research by AMN subsidiary Merritt Hawkins found a near 40% gender pay gap among physicians. The company's public commitment to take action (as documented in its latest corporate social responsibility report) is further evidence of its intention to address the issue of gender pay inequality in healthcare.

Replacing an employee who quits costs, on average, 21% of their annual pay.

In this instalment, we progress to engagement on employee benefits and broader well-being. With aging workforces across most (if not all) developed markets, occupational injury and illness is often a growing cost – both to governments as well as to businesses in the form of underperformance and, in the US in particular, incurred healthcare costs. Evidence shows that investing in employee well-being leads to higher productivity and boosts the business bottom line[1]. Workplace benefits play a key role in helping to retain and engage employees. Furthermore, the rise of non-communicable, "lifestyle" diseases within affluent economies cannot be tackled by governments alone. Forward-looking companies have always recognised that since so many working practices, not least long hours, sedentary work and stressful conditions, are themselves known causes of ill-health, then they have a responsibility as well as a practical and commercial imperative to mitigate these effects. Three of the key human capital challenges confronting many businesses, namely those of talent shortages, ageing demographics and non-communicable diseases are intricately connected and workplace wellness is a key element in the solution. In our view, wellness (physical and mental) is likely to become ever more important to companies as we collectively spend more years of our lives at work than ever before.

Job perks: the value of employee benefits

Employee turnover is not only disruptive, it is also expensive. Replacing an employee who quits costs, on average, 21% of their annual pay through hiring and training expenses as well as productivity losses[2]. Even the loss of workers at the bottom end of the pay scale (which in the US equates to those earning under $30,000 each year – about half the workforce there falls into this band) costs businesses 16% of an employee's annual wage[3].

Keeping valuable staff happy, healthy and motivated is clearly an imperative for companies, if not for their own sake then at least for profitability reasons. Measures of employee job satisfaction, such as those appearing on Glassdoor (a website where employees and former employees anonymously review companies and their management), offer investors important clues about the health – and potential future performance – of many businesses.

1 "It's official: happy employees mean healthy firms," published by the LSE Business Review in July 2019.
2 "Why do employees stay? A clear career path and good pay, for starters," published by the Harvard Business Review in March 2017.
3 "There are significant business costs to replacing employees," published by the Center for American Progress in November 2012.

For instance, research demonstrates a link between Glassdoor company star ratings and profitability: a one-star higher rating predicts about a 1% higher annual return on assets while the highest-rated firms outperform the stock market[4].

The above intuitive relationship should come as no surprise to any of us given our own lived experiences. It is however a truism that is growing in importance given the growth in the service economy, wherein employees are the face of the business as well as sources of innovation and organisational knowledge. While the products and services many companies offer can appear quite similar on the surface, exceptional service can be a competitive advantage. Competing through service is only possible when the organisation treats its employees as a valuable resource.

While staff satisfaction to a large degree hinges on pay levels – or relative pay equity. Existing staff members, and potential employees, are increasingly looking for companies to provide a range of benefits beyond simply fair pay.

Keeping valuable staff happy, healthy and motivated is clearly an imperative for companies.

Some firms view non-financial benefits as an important weapon in the ongoing global war for talent. Forward-thinking companies are designing staff recruitment and retention packages that play to employee welfare needs such as health insurance or pension plans, prompting others to offer similar benefits for competitive reasons rather than a philosophical commitment to employee welfare.

The type and generosity of employee benefits varies considerably across country, industry and company: in particular, the benefits will be pitched to the type and age of workers each firm is trying to attract.

For example, companies looking to recruit graduates may provide innovative student loan repayment options as part of the remuneration package while pension and healthcare benefits would likely be more prevalent for those hiring mid-career individuals or wanting to retain an older workforce.

Despite the increasing number of exotic staff benefits on offer (such as massage services) – influenced largely by the high-tech sector – companies will seemingly get the best employee satisfaction result by focusing on just three core offerings, as below:

1. health insurance (by a distance the most valued benefit)
2. paid holiday allowance
3. pension plans

However, there is plenty of scope for businesses to tailor bespoke employee benefit plans around a number of further areas that both could increase labour market participation and help meet other health-focused SDGs. For example, for almost all companies offering greater support to parents is increasingly understood to be essential to increase the levels of diversity within companies – aspiring for greater representation is undeliverable without affording greater flexibility around parental duties.

While some governments mandate employee benefits others, such as the US, leave the decision up to individual companies. In fact, the US likely has the least-generous government-decreed employee benefit system of any developed country, which hands more responsibility for employee welfare to each company – but it also provides an opportunity for leading firms to use staff benefits for competitive leverage and to lift productivity.

With US unemployment at historic lows, wage pressure on the rise and skills shortages present in some areas, benefits can make the difference between retaining or losing talented staff.

The US offers some of the least generous employee benefits

1. There is no requirement to provide paid leave in the US, as a result only 76% of workers have access to paid leave and the median number of days provided is seven (versus a 20-day minimum in Europe)[5].
2. Maternity leave is similarly strict, with 12 weeks unpaid leave the norm (13% of employers offer paid leave)[6]. The US is the only OECD country to not mandate paid leave for new mothers[7].
3. The US is the only industrialised country without a national paid family leave policy (although larger companies are beginning to offer paid paternity leave). It has been proven that paternity leave helps reduce the wage gap between men and women. The World Economic Forum found that the countries that offer paternity leave are the most successful in closing the wage gap between men and women[8].

Improving mental well-being at work (SDG 3.4)

Health is more than just physical. Across the world the issue of mental well-being is coming to the fore as the incidence of employee depression and stress continues to rise, leading to lower productivity in addition to individual human suffering. According to the OECD, mental ill-health knocks 4% of GDP in the UK through lost working days, lower productivity and increased healthcare spending[9]. According to one study, workers' mental health affects their intellectual, emotional, and social growth, as well as work ability, productivity, and ultimately organisational productivity and competitiveness on the market[10].

Some countries have introduced legislation aimed at alleviating work-related mental illness: France, for instance, passed a law allowing employees to ignore work emails outside of working hours[11].

Regardless of the limited government actions to date, the main responsibility for worker well-being – both mental and physical – will continue to fall on employers, not least given the degree to which

4 "Employee satisfaction and corporate performance in the UK," by Efthymia Symitsi, Panagiotis Stamolampros, George Daskalakis, and Nikolaos Korfiatis published in SSRN in March 2018.
5 "Employee Benefits Survey," published by the Bureau of Labor Statistics in 2019.
6 "How to ask for maternity or paternity leave when your company has no policy," published by the New York Times in May 2019.
7 "OECD Family Database – Parental leave systems," published by the OECD in August 2019.
8 "Which countries offer the most paternity leave?" published by the World Economic Forum in August 2015.
9 "Mental illness costs UK £94bn a year, OECD report says," published by The Guardian in November 2018.
10 "Healthy Occupational culture for a worker-friendly workplace," by Igor Grabovac and Jadranka Mustajbegovic published by the Archives of Industrial Hygiene and Toxicology in March 2015.
11 "French workers win legal right to avoid checking work email out-of-hours," published by The Guardian in December 2016.

causes are under their control, such as repetitive work, a lack of control, pressure to meet strict targets and relationships between colleagues and supervisors.

Workplace wellness programmes (SDG 3.4)

Healthy workers cost employers less – a fact coming into sharp focus for those countries and industries with aging workforces.

Interestingly, while the price of employee illness is most often counted in days off work, there is another less obvious, but possibly more significant, cost in the form of 'presenteeism' – where workers turn up for work but underperform due to sickness or stress. For example, US company Dow Chemical conducted a study from 2002 of the annual health costs for its employees: it attributed $661 to absenteeism, $2,278 to direct health care and a whopping $6,721 to 'presenteeism'[12].

Many companies are pre-empting the threat posed by poor employee health by introducing so-called 'wellness programmes' where any upfront cost is more than compensated by higher productivity, lower staff turnover and reduced healthcare expenses (which is especially important in the US where employers directly pay health insurance premiums). Indeed, on the back of writing to our investee companies around this agenda in early 2019, our conversations with multiple Human Resource (HR) directors have reinforced this premise with it being consistently noted that there is a direct relationship between employee engagement with wellness initiatives and company incurred health costs. One company suggested that, for example, those employees not involved in their wellness programmes are 59% more likely to have an avoidable visit to A&E.

Employers can boost the career prospects of women by supporting more generous early-years childcare services.

Three common workplace well-being and health interventions are:

1. Mental health promotion and support for mental illness
2. Physical health promotion through activity and nutrition programmes and programmes aimed at reducing smoking prevalence
3. Programmes concerned with improving occupational health and safety in the workplace and tackling specific occupational health issues such as musculoskeletal disorders

As many countries struggle with non-communicable diseases like obesity (which imposes an estimated total cost in the US of nearly $80bn a year) wellness interventions are proving their worth.

A World Economic Forum paper from 2011 gathered the evidence and reported that cardiovascular disease, chronic respiratory disease, cancer, diabetes and mental health would result in a cumulative output loss of $47tn over the two decades to 2030[13]. It is no surprise that in this context, many companies are responding in a proactive and paternalistic fashion.

Companies, however, face ethical and privacy challenges when collecting the employee data necessary for successful health programmes. Anonymous health risk assessments – which combine a lifestyle survey with biometric tests such as blood pressure, cholesterol, glucose, and body mass index – offer one way for managers to identify and track the progress of groups facing the greatest needs.

Technology, too, is aiding companies that seek to improve employee health with innovations such as wearable fitness trackers (which can provide a wide range of biometric data) and 'telemedicine', which is on the rise in the US and the UK. Telemedicine can deliver a number of personalised healthcare services either through video or telephone, which in turn reduces time away from work. At the same time, employees would be more likely to seek treatment or further medical advice following a virtual diagnosis.

Childcare: meeting the needs of working parents (SDG 4.2, 5.5 and 10.1)

Childcare services are a much-valued employee benefit, reducing many family-related employee stresses while also contributing to the long-term health of the wider population. Good childcare has been linked with positive adult life outcomes, with the effect enhanced for those who come from less-privileged backgrounds.

The OECD has also found that a woman's labour mobility – those job-to-job transitions that boost career and salary progression – is stymied, compared to men, by child-rearing duties.

Employers can, therefore, both help those workers from less-wealthy backgrounds and boost the career prospects of women by supporting more generous early-years childcare services, along with providing for more flexible parental leave. Greater gender representation within workforces, specifically within more senior positions, can only really be achieved if there is a greater sharing of parental responsibilities enabled by employers.

Improved childcare options should create a better-skilled, more employable and productive population over the long term, significantly reducing wasted human potential with obvious spin-off benefits for corporate profitability.

Pension and savings plans (SDG 1.2)

The generational shift from defined benefit (DB) employer-provided pensions to defined contribution (DC) retirement savings schemes is a global phenomenon. Under the DC model, employees bear the risk and responsibility for managing their retirement savings that was previously shouldered by employers.

Nonetheless, help with pension plans is one of the top three employee benefits people value in prospective employers, Glassdoor research shows. While the current cohort of retirees may be comforted by their DB pensions, concerns about retirement savings will undoubtedly grow for the generations still working.

The evidence suggests that the DC generation are facing a looming savings crisis. According to a 2018 study by the US National Institute on Retirement Security, two-thirds of 'millennials' – loosely defined as those born from the early 1980s through to the early years of this century – have no retirement savings.

12 "What's the hard return on employee wellness programs," published by the Harvard Business Review in December 2010.
13 "The global economic burden of non-communicable diseases," published by Harvard School of Public Health and the World Economic Forum in September 2011.

Meanwhile, data from the US Economic Policy Institute shows the median retirement savings balance for working age families is just $5,000 while households approaching retirement have saved only $21,000 – a sum that, after taxes, is enough to sustain a couple for a little more than a year of life at the official poverty line.

But the looming pension crisis is certainly not a US issue alone. The latest Melbourne Mercer Global Pension Index suggests that tens of millions of workers face impoverishment in old age, noting that pension systems in Japan, Austria, Italy and France are unsustainable. Indeed, research by the International Longevity Centre (ILC) notes that 28 of 30 developed countries face an intergenerational savings gap.

"… today's twentysomethings are projected to do worse than current retirees," the ILC report concludes.

Insufficient savings for retirement, however, is a distant issue for many in low-paid work, not least given difficulties with managing day-to-day needs. In these circumstances companies can help their employees avoid exorbitant interest rates and build more positive financial and credit profiles.

To that end, a few companies allow employees to take loans against future paycheques through arrangements with local credit unions. Alternatively, platforms have formed which allow companies to offer a "financial wellness" benefit – essentially allowing employees to access their wages (their earned pay) as needed[14]. Adopters of such approaches have reported improvements in productivity, motivation and retention.

How are we engaging on workplace benefits?

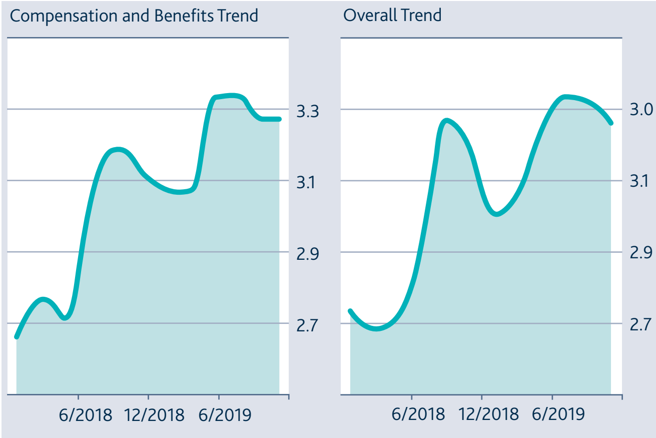
Since the inception of the Hermes SDG Engagement Equity Fund, we have been encouraging companies to play a more active role in addressing the issue of workplace benefits – both financial and non-financial.

In our engagement with boat and engines maker **Brunswick Corp** around the issue of decent pay and working conditions, we were impressed by the consistent firm-wide healthcare policy and associated low employee turnover level within its principal manufacturing facility. Indeed, 86% of Mercury Marine's employees participate in biometric screenings and health-risk assessment to understand focus areas for personal wellness (up from 40% in 2014).

We have also had multiple interactions with **Clean Harbors**, a leading hazardous waste management company in the US, on the topic of employee benefits and welfare. Given its reliance on logistics, the company has struggled, like others, with the US trucking industry's persistent driver shortages owing to the aging workforce, turnover rates, reduced capacity and lifestyle priorities.

During a difficult period in 2015, Clean Harbors made cuts to its 401k (an employer-sponsored retirement savings plan) and other employee benefits. Perhaps unsurprisingly, morale suffered, and employee turnover increased, exacerbating recruitment and retention challenges. In 2018, the company announced plans to reinvest in its workforce including reinstating and improving the 401k and enhancing its healthcare benefits. More broadly, in acknowledgement of the challenges it was facing, it has been reviewing its entire employee value proposition which should stand it in good stead in future. Its actions to date have been well received as evidenced by the boost in sentiment towards the company on Glassdoor in the past two years (see figure 1).

Figure 1. Sentiment towards Clean Harbors has improved in recent years



Source: Glassdoor as at November 2019.

Future engagements

We will continue to engage on SDG 8. Specifically, we will ask company management teams and boards:

1. Does the company's pension savings plan afford a dignified retirement? We are ever less sympathetic to the disparity in pension arrangements offered to executives as contrasted with the wider workforce.
2. Does the company offer family leave policies that support equitable parental duties and women returning to the workforce? In turn, are return-to-work rates monitored?
3. Given that employees typically consume one or several meals plus snacks during work hours, can the company actively provide healthy and nutritious (and affordable) meals?
4. Does the company understand the health of its workforce? Does it understand what interventions it can make to improve employees' physical and mental well-being while simultaneously improving productivity and customer service?

In so doing, more companies will see the merits in promoting the well-being of their workforces – and they will reap the benefits of healthier and happier employees.

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14 See Hastee and Wagestream as two examples of such providers in the UK.

CASE STUDY

ENGAGEMENT PROGRESS: CLEAN HARBORS

Clean Harbors is the largest hazardous waste management company in the US and the largest collector, recycler and re-refiner of used motor oil.

Engagement context

- Clean Harbors has a sizable workforce (>14,000), a significant proportion of whom work in logistics. They, like others, have struggled with the US trucking industry's persistent driver shortages. The company's drivers are typically more skilled than other truckers making them an attractive asset and a scarce resource. During a difficult period in 2015, Clean Harbors made cuts to its 401k (an employer-sponsored retirement savings plan) and other employee benefits. As a result, employee turnover increased, exacerbating recruitment and retention challenges.
- The company has an extensive footprint across the US with a network of sites comprising 11 hazardous and non-hazardous landfills and nine of the 13 hazardous-waste incinerators in North America. Therefore, management of health and safety is an important issue both for its employees and the local environment.
- The company's Safety-Kleen business applies a genuinely circular closed-loop business model to motor oil, collecting approximately 250m gallons of used motor oil annually and re-refining that oil into a usable product that is delivered back to the same customers. Scaling this business should be a win-win for the company and industrial resource-efficiency.

Engagement timeline: January 2018 to December 2019

Milestones | **1** Raise SDG issue at the appropriate level | **2** Company recognises that the issue is valid

Employee benefits and welfare

1 — **April 2018:** In a call with the company, we discussed the truck driver labour shortage, the company's efforts to train and develop staff as well as the need to improve its 401k scheme.

2 — **April 2018:** The company confirmed that it is committed to providing competitive pay and benefits. It also informed us that it had reinstated its matching 401k plan.

Climate change – scope 1 emissions

1 — **October 2019:** During a call with the CFO, we explained that the company should set an emissions reduction target for its fleet and disclose progress against it.

2 — **October 2019:** During a call with the company, it agreed that it first needs to establish an emissions baseline for reporting and set a target for its fleet.

Enhance sustainability reporting

1 — **April 2018:** Having initially written to the company chair to initiate a dialogue, and given the company's strong sustainability story, we conveyed the potential benefits to the company of enhancing its existing limited sustainability reporting, in particular with respect to human capital management and GHG emissions.

2 — **April 2018:** Pleasingly, the company, signalling that it takes shareholder feedback seriously and appreciated our view on sustainable development, indicated that it would take a look at expanding its reporting on its sustainability efforts including through group-level KPIs.

Theory of change

- There have been persistent driver shortages in the US trucking industry in recent years owing to the aging workforce, turnover rates, reduced capacity and lifestyle priorities. The Bureau of Labor Statistics estimates that the average age of a commercial truck driver is 55 and 94% are male. By actively reaching out to targeted constituencies, providing decent pay and benefits and investing in training and development, the company is able to directly influence the living standards of its workers, improving well-being, reducing unemployment and improving its productivity levels.
- Clean Harbors' fleet of more than 17,000 transportation vehicles represent a significant emissions reduction opportunity. Applying more sustainable practices and articulating more quantifiably its strategy for transitioning to cleaner energy vehicles such as, CNG, electric and hydrogen should drive a reduction in total emissions generated.
- The company's closed-loop oil refining business offers a real impact opportunity – recycling used motor oil is good for the environment, reduces energy consumption and promotes the domestic re-refining industry.

Engagement themes

- **Employee benefits and welfare**
- **Climate change**
- **Sustainability reporting**

SDG alignment

7 AFFORDABLE AND CLEAN ENERGY
8 DECENT WORK AND ECONOMIC GROWTH
12 RESPONSIBLE CONSUMPTION AND PRODUCTION

Investment context

The company's network of over 100 waste management facilities across the US provides it with a significant moat, not least given the difficulties in securing new permits for hazardous-waste incinerators and landfills. It is expected to benefit from renewed investment in the domestic petrochemical industry, with new capacity driving higher-value waste streams into the Clean Harbors network. Tightening of regulations, such as the International Maritime Organisation's 2020 global sulphur cap, should prove to be tailwinds to the closed loop oil business.

3 Develop and commit to a credible plan for change

4 The plan succeeds and relevant impact metrics are disclosed

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April 2019: Further to writing to the CEO on the topic, the company explained that it is changing its wellness programme provider this year to improve its offering. It is also investing further in pay and benefits, undertaking its first engagement survey in several years and has set an internal target to reduce voluntary turnover in 2019 with a clear line of sight to performance on a site-by-site basis.

October 2019: The company has included voluntary turnover as a metric for site manager compensation. As a result, turnover numbers are trending down. It has undertaken its engagement survey and plans to publish its results. Encouragingly, the company's Glassdoor ratings have steadily improved during this period.

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November 2018: We met with the Head of Investor Relations at the company's headquarters to discuss sustainability reporting. The company indicated a willingness to do more, particularly on CO_2 emissions.

April 2019: The company published an improved sustainability report, which included a number of quantifiable KPIs marking a significant step forward although absolutely with scope for further improvements still.

Engagement commentary

Since 2018, we have engaged with the company on multiple occasions and it has proven to be very receptive to our dialogue. In recognition of the particularly tight labour market conditions, Clean Harbors has made a significant effort to widen the pool from which it recruits. By the end of 2018, veterans accounted for 6% of the company's workforce (compared to 1% of the general population).

During a difficult period in 2015, Clean Harbors made cuts to its 401k and other employee benefits. In 2018, the company appointed a new HR Director and announced plans to reverse these cuts – reinstating and subsequently improving its 401k offering as well as enhancing its healthcare benefits. Further progress was made in 2019. The company undertook its first engagement survey for many years, began to review its employee value proposition and importantly established clear internal targets to reduce voluntary turnover.

While difficult to quantify the impact of any of the singular changes made in the past two years the company acknowledges that the cost of unnecessary turnover is significant and, for that reason, it now has a very clear focus on addressing the problem in a holistic fashion with meaningful targets and accountability.

While the company has various pilots underway to improve the efficiency of its fleet the size of the task is not straightforward. In the first instance they are working to establish baseline measurements for their trucks. This, alongside the policy environment and their ability to scale up their closed-loop motor oil business, will be topics we will be prioritising during 2020 given the very positive steps already now made on the decent work agenda.

HERMES INVESTMENT MANAGEMENT

OUTCOMES BEYOND PERFORMANCE

Hermes Investment Management

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