

CASE STUDY  
**HON HAI**



Engagement objective: **Social**  
Human capital management



Engagement objective: **Governance**  
Succession planning

Hon Hai has demonstrated concrete improvements in its corporate governance, as well as its approach to labour relations and wider investor disclosure, since Hermes EOS began engagement in 2010.

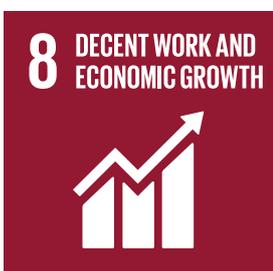
### Background

Our engagement with Hon Hai Precision Industry (Hon Hai) started in 2010 when employee incidents at its factories in China raised concerns over the company's human capital management. Workers complained about long working hours, low pay and pressure from supervisors to keep a high pace of work. In addition, we have had longstanding concerns about corporate governance, due to the dominating influence of the founder and chair / CEO Terry Guo.

### Company overview

Established in 1974, Hon Hai is one of the largest electronics manufacturing service providers in the world. Also known as Foxconn, it is a Taiwan-based company involved in the manufacturing and sales of computer, communication and consumer electronics products. The company operates manufacturing sites across Asia, Europe, Mexico and South America, though its largest production facilities are located in Mainland China.

### Sustainable Development Goal



### Our engagement

Following a difficult engagement dialogue with limited progress, we recommended voting against the election of board directors to signal the need for action in 2010. By 2012 the company had taken positive steps to identify problematic labour issues such as wages and overtime and acknowledged the need for further improvements.

An in-depth discussion with the head of the social and environmental committee later that year secured us a visit to the factory in Shenzhen to inspect the working conditions and review the implementation of the Fair Labor Association's (FLA) recommendations. We left the site encouraged by the company's actions but pointed out that sustainable change would necessitate a change in company culture and tone from the top management. Following our visit, we shared best practice examples of sustainability disclosure and were encouraged that implementation of FLA recommendations was progressing ahead of schedule.

Following another difficult engagement dialogue, we spoke at the annual shareholder meeting in June 2014. Eight major international institutional investors, in addition to our clients, requested to be formally represented by us in this effort. The intervention was covered by the Financial Times as an example of how corporate engagement is gaining momentum in Asia. The company announced in March 2015 that it was launching a strategy and vision website to provide more clarity.

In 2015, the adviser to the chair / CEO presented at our client event. His presentation of the company's human capital management and corporate governance provided further insight into the company's thinking. The adviser credited the feedback from Hermes EOS as contributing to the improvements at Hon Hai.

In 2016, we were the first institutional investor to visit the company's Chengdu factory to gain first-hand insights into labour practices through dialogue with workers. However, we were subsequently disappointed by student overtime practices at a different site, which violates the company's stated employment policies and disclosed weaknesses in policy implementation.

## Eight major international institutional investors, in addition to our clients, requested to be formally represented by us

We had an unprecedented direct dialogue with the chair / CEO at the 2018 shareholder meeting. We requested separation of the CEO and chair roles and clear succession plans for key positions at the business segment level. The low attendance levels of the board chair and chair of the audit committee at board meetings was also highlighted. In his response, the chair / CEO sought to reassure us that succession planning was being considered.

### Engagement timeline

- 2010** Employee incidents prompted start of engagement.
- 2012** Engaged head of social and environmental committee. Visited Shenzhen factory. Met with senior executive at headquarters in Taipei.
- 2013** Met with a senior executive to discuss strategy and disclosure. Repeatedly sought meeting with chair / CEO for evidence of cultural change to sustain improvements in labour practices.
- 2014** Lack of positive response to request for a private meeting with the chair / CEO led to joint investor engagement at company's AGM.
- 2015** Engaged company at AGM on issues including labour practices and strategy disclosure. Adviser to chair / CEO spoke at Hermes EOS client event.
- 2016** Visited Chengdu factory, including dialogue with workers, to better understand labour practices in action.
- 2017** Met with adviser to the chair / CEO and an independent board director on corporate governance and strategy. Raised concerns about students having been found working overtime.
- 2018** Engaged chair / CEO directly during AGM for a 40 min dialogue around succession planning and labour practices.
- 2019** Chair / CEO steps down and company institutes a steering committee as executive decision-making body.



## Changes at the company

After our speech at the annual shareholder meeting in 2018, company representatives, including an independent board director, gave further reassurance that succession planning was being worked on. We took part in an investor call before the 2019 meeting (AGM) to discuss succession and corporate governance, the first time the company has ever facilitated such investor dialogue. During the call, the proposed directors presented their roles and strategies for their business units and the overall future governance structure.



In June 2019 the chair / CEO announced plans to step down as chair of the board at the AGM later the same month. We were pleased that the company put in place a committee-style governance structure. Decision-making should now be a more inclusive process involving all heads of key business units which we hope will lead to a constructive balance of influence. The operations committee will take charge of daily operations and will be made up of four members from the board of directors. The audit committee was also partly refreshed, with the chair stepping down.

## The adviser credited the feedback from Hermes EOS as contributing to the improvements at Hon Hai.

We believe that this rebalancing of power is a significant milestone in the company's history. The company has taken on board our feedback on the need for improved transparency and communications, as well as a governance structure that removes reliance on one founding chair / CEO. Although the company's work to ensure this structure works well for its stakeholders has just begun, we believe it has met our most pressing objectives relating to succession planning and is now in a stronger position to prepare for the future.

### Next steps

While we are encouraged by the company's corporate governance development, we will seek to meet with an independent non-executive director to continue to engage on the effectiveness of the new board and its decision-making process. We would like to see more clarity and transparency about strategic planning to adapt to new challenges and opportunities from digitalisation and artificial intelligence, as well as greater insights into the company's management of climate change risks and opportunities via the Climate Action 100+ collaborative engagement.

## HERMES INVESTMENT MANAGEMENT

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Our goal is to help people invest better, retire better and create a better society for all.

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#### High active share equities

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#### Credit

Absolute return, global high yield, multi strategy, unconstrained, real estate debt and direct lending

#### Stewardship

Active engagement, advocacy, intelligent voting and sustainable development

### Offices

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