OMS

Organizational Maturity Services LLP

Human Governance Briefing
Special Issue: Responsible investing?

What is ESG without the *V and the H*?

This Special Issue of HG Briefing asks the straight question - are 'responsible' investors being entirely responsible? ESG (Environmental, Social, Governance) has become shorthand for responsibility but are these three factors achieving any significant impact on **V for value** and has anyone managed to factor in **H, for the human factor,** to corporate governance, strategic business planning and operational management? Whatever the answer to these questions, and they are bound to be complex, the Maturity Institute (MI) and OMS LLP are focused on bringing V and H to the fore in leadership and management development in order to raise the maturity level of corporations across the globe for the benefit of all societal stakeholders.

The two short pieces below illustrate this journey by re-visiting how the corporate and investment communities have so far responded to the very serious issues of governance that currently undermine global capitalism. In the first, we consider how investors have been approaching Sports Direct, an easy target for ESG aficionados and activists. The results of poor governance and management are obvious but the root causes less so. Do asset owners and managers have the necessary capability to help resolve the underlying human governance issue? In the second, we take a brief look at how the UK pension industry is being guided on similar issues and ask whether such guidance is leading to the right solutions?

SPORTS DIRECT.COM

Sports Direct: Investor Ire Misses Value Goal

Asset owners and managers were busy at the AGM of Mike Ashley's Sports Direct last week; voicing serious concerns about oppressive working practices and poor corporate governance. Through the Investor Forum, many are calling for the company to conduct an independent review of both. Yet these are *symptoms* of deeper organizational issues, not the root causes, so any subsequent investigation is unlikely to produce the best resolutions. Also, do lawyers (who tend to carry out such reviews) have the necessary expertise and skills?

Ashley, successful entrepreneur, majority shareholder and primary decision maker, has always shown disdain for outside intervention; be it from investors, unions or even the UK Government. Why? Because he would need convincing that any changes required will improve the value of his empire. The three issues of governance, working practices and market value are indeed connected but, in the absence of a capability in *human governance* in the boardroom, no one will be able to convince Ashley how they are connected and whether significant value improvement can be gained.

If Ashley's perception is that 'interference' does not positively affect his firm's value then it's a view shared by the market. Efforts by Sports Direct to address these issues might have been seen as a step in the right direction but the share price finished little different than before the AGM (see chart). Further work to address the specific issues raised thus far is, in our view, unlikely to significantly affect market value in the future.

A better diagnosis?

Human governance diagnostics (using the OM30 PLUS questionnaire) ask a number of fundamental questions about corporate value while adopting a whole system perspective: This is founded on MI's Ten Pillar framework for long-term, maximised value creation. The simplest yet most searching question is one of principle - 'does the company manage people as a source of value or as just the cost of doing business?' It is blatantly obvious that managers who use zero hour contracts subscribe to the 'cost only' principle. Yet it is now equally obvious that the value and business risk implications of doing so are material and can be quantified. As Mark Mandevelde averred in his FT piece "Many of the people employed there are not doing profitable work."

Even from a cursory glance at the media output during the last week, the valueless outcomes of Ashley's management approach are apparent and Ashley himself had to admit *"John Lewis is something to be looked up to" he says. "They seem to galvanise everybody together."*

Mike Ashley pulls out a wad of £50 notes during Sports Direct security check

Ashley's intuitive take is right but that does not mean he or his board have any capability to do so. In this respect Sports Direct management is no different to the vast majority of companies who still fail to ***galvanise*** their human capital into a coherent system for creating value.

The existence of extensive, yet inefficient, security checks is one clear indicator that that trust is thin on the ground. Staff are required to do a specific job rather than aspire to contribute more widely to value: such as to improve the operations on a day-to-day basis. OMS's evidence, gathered from OMINDEX ratings of a wide array of firms, clearly reveals that the financial loss is enormous.

Managing people primarily as a cost makes them invisible as human beings and leads to unacceptable working practices. Regardless of their level, or the apparently repetitive nature of their work, each employee has more to offer than labour alone. Mature leadership and human governance in the boardroom, and high value human capital management practices, are now imperative at Sports Direct but this is a much wider issue; one that afflicts the FTSE250, S&P500 and any other index you might wish to consider. Whatever the Investor Forum is doing to help the situation they need to reach this level of maturity themselves in order to become effective.

PENSIONS AND LIFETIME SAVINGS ASSOCIATION

Where is the PLSA in corporate reporting?

In June 2015 the UK's NAPF (now PLSA) raised many of the above issues. This came in the form of a report entitled "Where is the workforce in corporate reporting?" (June 2015). The answer came in one line from PLSA CEO, Joanne Segars, stating that it was a "chicken and egg situation (that) has resulted in an unsatisfactory impasse." In short, if companies are not asked for *V&H* information they cannot provide it: but if investors don't know what questions need asking then everyone ends up in a vicious circle.

Segars' admirable response was to "kick-start this agenda", which resulted in a guide for its members - "Understanding the worth of the workforce. A Stewardship Toolkit for pension Funds." (July 2016). However, the 'Stewardship Toolkit' proved to be a simplistic, tick box, collection of disconnected metrics purporting to serve as proxies for management quality: rather than the coherent, whole system overview that is now required. This approach is the antithesis of an effective response to the inherent complexity of stewardship and governance. As the Sports Direct situation has again highlighted; complex, whole system issues cause material damage and pension funds (and their beneficiaries) need better guidance on how these issues should be examined and diagnosed (i.e. with the sophistication they demand) for appropriate solutions to be found.

Postscript:

If you have a responsibility for stewardship and corporate governance, the type where ***V and H*** are firmly integrated and embedded, and realize that this will not be resolved with standard check lists, please contact us. For companies who wish to understand where V and H sit in their own organization, there is more information here.