How are current global events impacting executive pay globally?

By Chris Blair

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Since the Covid pandemic, the world has been affected by many events that are now the new normal and businesses will now have to make strategic changes to the way they operate. These events are geo-political - the invasion of Ukraine; logistical - supply-chain bottlenecks; economic - high energy prices, demand supply issues - global commodities pressures and chip shortages, rising inflation and possible recession.

Image source: Kirill Ryzhov – 123RF.com

2020, understandably, saw low pay-outs for executives, and in the light of uncertainty regarding Covid-19, targets for 2021 were set conservatively. As a result, there was a considerable upward trend in variable pay for executives in 2021, as remuneration levels caught up to previous levels, and corporate performance improved.

However, in 2021 the labour market came under multiple new pay pressures as it saw resignation levels reach record highs (dubbed “The Great Resignation”), especially amongst Gen-Z employees. This gave employees the opportunity to negotiate higher salaries, as employers become legitimately concerned about staff shortages and the retention of current employees. In addition, employees have demanded more flexible working conditions and many companies have adopted hybrid models of work that allow employees to work the majority of time where they choose.

Markets have faced innumerable challenges since the beginning of 2022, including those that have arisen as a result of geopolitical tensions. Economists are predicting that we could see a recession in the next few months, despite the fact that employment levels remain high in many developed countries – South Africa bucks the trend here. Energy prices, supply chains, global shortages are some of the issues that are having a major impact on markets and on companies. Inflation has risen, stock markets have been affected negatively, and many companies are readjusting their internal earnings forecasts. Some companies have announced layoffs because of these pressures.

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Focus on ESG

A major trend from 2021 that has gathered momentum - and will continue to do so - is that of sustainability. Since the beginning of 2021, legislation around ESG and climate has continued unabated. Much of the legislation focuses on disclosure so that the market can judge the performance of companies in these areas. There is continued legislative activity in the areas of performance management and human capital management and related topics. Some of the legislative activity we've seen is directly related to pay. There is a drive to toughen clawbacks that allow companies to reclaim past variable pay that was not justly earned because of economic windfalls or tail winds emanating from the Covid pandemic. Many of the more substantive laws on conduct risk, protection of investors and customers, and protection of the environment have also been further strengthened during this period.

Once again, an increase in the use of Environment, Society and Governance (ESG) non-financial metrics in remuneration plans has been recorded, with strong support from some institutional investors like Blackrock. However, many companies are attempting to set hard targets that are measurable and specific - rather than softer 'progress' targets. More than two thirds of publicly listed companies across six continents are now using ESG metrics in their short-term incentive plans.

Since 2021, the use of equity-based instruments has become more widespread, and we have seen a greater use of performance shares (PSU). Countries that commonly use PSUs are adopting a restricted-shares approach on a greater scale. The market continues to pressurise companies to make use of post-vesting requirements that can extend the duration of LTI plans by up to two years. In the UK, the majority of large listed now have post-vesting requirements. This has come about as companies align themselves with the recommendations of the Investment Association.

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In the last few months, we have seen a growing trend of company shareholders disapproving say-on-pay, or in some countries, being willing to vote against the re-election of board members. Investors and proxy advisors are now demanding that boards disclose how they aim to increase their diversity – and represent the under-represented - at board level, and are setting policies on gender, race and other diversity issues. An example would be to vote against a Chair who oversees a board where less than 30% of the members are women.

All these factors will need to be taken into consideration by remuneration committees as they make remuneration and performance decisions at the end of the financial year. The major trends we have seen can thus be summarised as such:

- The strengthening of the link between ESG and pay
- The increased use of equity-based tools
- Increased legislation around ESG
- The demand for diversity within boards

This article is based on research conducted by the Global Governance and Executive Compensation Group (GECN), one of the largest independent compensation groups in the world. 21st Century is the GECN consultancy for Africa.

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