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REPORT

The People Factor

HOW INVESTING IN EMPLOYEES PAYS OFF

MARCH 2023

CPP Investments
InsightsINSTITUTE

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FCLTGlobal's mission is to focus capital on the long term to support a sustainable and prosperous economy. We are a non-profit organization whose members are leading companies and investors worldwide that develops actionable research and tools to drive long-term value creation for savers and communities.

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ESG Initiative

The mission of the Environmental, Social and Governance (ESG) Initiative is, consistent with the vision of Joseph Wharton, to harness the power of business to "solve the social problems incident to our civilization." The ESG Initiative conducts research that investigates the intersection of ESG factors and business and further advances Wharton's best-in-class education of current and future practitioners, enabling them to serve a world undergoing tremendous change.

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Preface

Key takeaways

- Over a three-year period, committed employers — companies that back up talk about investing in employees with action — are associated with a 4.0% higher return on invested capital (ROIC) on an absolute basis than counterparts that did neither.
  - Similarly, over the short term (within one year), committed employers are associated with better outcomes than companies that neither communicate nor demonstrate committed investment in employees. Results include:
    - **1.2% higher contemporaneous annual ROIC on an absolute basis**
    - **0.5% higher contemporaneous annual sales growth on an absolute basis**
    - **2.8% lower annual employee turnover on an absolute basis.**
- Investing in employees is about the sum of the parts: no individual sub-component (e.g., increasing wages; improving diversity, equity & inclusion (DEI); addressing benefits; and monitoring employee health & safety) contributed directly to value creation. But, taken as a whole, these sub-components are correlated with long-term value.
- A suite of measures that creates a high-performing, inclusive workplace where employees feel valued and inspired to do great work is associated with higher sales and lower costs and, by extension, superior returns.
- Geographic and pre-/post-COVID-19 analysis suggests a sharp uptick in the prevalence of employee-friendly talk in the U.S. pre-pandemic was not matched by similar levels of action, while levels of talk and action in Europe remained steady.

The People Factor: How Investing in Employees Pays Off explores the role of labour practices in corporate value creation. The report analyzes how articulating employee-related commitments and following through with investments in employees impacts the ability of companies to deliver strong business outcomes. This new analysis should be of interest to a range of stakeholders, including corporate Boards of Directors, management teams and investors focused on long-term value creation.

This report is a result of research conducted by FCLTGlobal in collaboration with the CPP Investments Insights Institute and the ESG Initiative at the Wharton School of the University of Pennsylvania. A working group comprised of FCLTGlobal members provided additional perspectives. The research builds on *Walking the Talk: Valuing a Multi-Stakeholder Strategy,* a first-of-its-kind report published in 2022 that set forth the rationale for pursuing a multi-stakeholder approach to business by highlighting the value of delivering tangible outcomes to stakeholders (i.e., the walk) and presenting the firm as committed to stakeholder harmony (i.e., talk). Stakeholders examined in that foundational report included communities, customers, employees, the environment, government, shareholders and suppliers.

The intent of this report is to make the case that following through on employee-centric commitments as stated in annual reports is associated with long-term value creation. Our goal is not to imply causation. While we conclude that companies walking the talk in their employee orientation create value, the causation debate remains open for further research. We also recognize that there are a number of non-financial factors that could contribute to lower annual employee turnover and, therefore, higher sales growth and ROIC. These factors, which are often hard to measure and were not part of this study, include corporate mission/purpose, high-quality training, as well as meaningful interactions with — and developmental feedback from — managers and opportunities for professional growth.

Executive Summary

From the COVID-19 pandemic to the subsequent spike in inflation, widespread adoption of remote or hybrid work and the Great Resignation, the past few years have been marked by monumental global events and workplace shifts that have changed our daily lives and affected economic activity in numerous ways.

Competition to attract and retain employees has also become fiercer. In turn, companies have rapidly evolved their workforce strategies and adopted new tools for prioritizing employees. Whereas some companies and investors may see these actions as opportunity to create a talent advantage to remain competitive over the long term, some others may view higher spending on employees as a cost burden.

To bring more empirical research to the forefront in this ongoing conversation, we developed a novel approach to analyzing the business outcomes associated with the employee-related commitments and investments made by companies. Building on the walk/talk multi-stakeholder orientation methodology set out in the 2022 *Walking the Talk: Valuing a Multi-Stakeholder Strategy* report, we examined whether employee-related walk/talk performance was associated with better value-creation outcomes, as measured by financial- and non-financial factors. Such factors include return on invested capital (ROIC), sales growth and annual employee turnover.

The research found there is a positive relationship between walk/talk scores and ROIC over longer time horizons. Analyzing value-creation outcomes over three years from the onset of respective walk/talk outcomes, we found that:

Companies with high walk/high talk scores (for the purposes of this paper, we refer to such companies as committed employers) are associated with 4.0% higher three-year ROIC on an absolute basis compared to companies with low walk/low talk scores.

There are also positive short-term outcomes for committed employers. All else equal, in the short term (within one year), companies that walked the talk are associated with better outcomes than companies that neither communicate nor actually take actions to invest in employees:

- **1.2% higher contemporaneous annual ROIC on an absolute basis,**
- **0.5% higher contemporaneous annual sales growth on an absolute basis,**
- **and 2.8% lower annual employee turnover on an absolute basis.**

We conclude that companies which focus on the employee experience outperform peers on key financial metrics. A strong employee stakeholder focus is defined by improvements to overall corporate culture. Individual, one-off investments in workers do not appear to have a lasting impact. Companies will deliver the strongest value-creation outcomes by walking the talk through demonstrable action and nesting employee engagement efforts within a more comprehensive, multi-stakeholder strategy.

While further data and research is required to fully assess the relationship between investments in employees and corporate value creation, we believe this report is an important first step.

Introduction

Three years since the onset of COVID-19, there is little debate that the pandemic has impacted how businesses operate. This is exemplified by companies having shifted to remote and hybrid work, and/or having adopted new standards and procedures to make their workplaces cleaner and safer.

But beyond the obvious effects on where people work, COVID-19 has also impacted how people think about work. Existing frustrations about wages and working conditions in some sectors were exacerbated by the pandemic. Across industries and job functions, employees reevaluated their priorities and expectations of their employers, resulting in historically high rates of workers choosing to voluntarily leave their jobs.[1]

While this paper does not make a forecast with respect to the permanence of these recent phenomena in resignations and work arrangements, it is clear that increased competition for talent forced employers to seek new ways to attract workers. Companies announced wage increases and enhanced benefits, as well as commitments to workplace-culture improvements and diversity, equity & inclusion (DEI). This trend marked one of the most significant reorientations toward worker preferences in modern times.

The corporate community's response to the Great Resignation, however, is not without its skeptics. Many workers, for instance, pointed out that companies who talk of improving employee livelihoods did not always match their actions. The International Monetary Fund found that nominal wage growth in 2021 "did not fully keep up with price inflation" in advanced and developing economies, meaning that real wage growth was fairly flat.[2]

Furthermore, while many companies have embraced that additional investments in employees are needed, investor reactions have varied.

Share prices of some major companies have dropped following announcements of wage hikes, while other stocks have risen in the wake of job cuts.[3] At the same time, however, a growing number of institutional investors have prioritized employee issues in their stewardship and engagement, and interest in human capital disclosure appears to be on the rise.

Mixed reactions from workers and investors underscore the imperative of a thoughtful approach to investing in employees — one that is effectively communicated, includes different elements (refer to Tools for Investing in Employees section on the next page for more details) and that balances value creation with the interests of multiple stakeholders.

WHAT CHANGED? HOW EMPLOYEE EXPECTATIONS HAVE SHIFTED SINCE COVID-19:

A BlackRock analysis suggested that the pandemic triggered a "structural shift" in employees' expectations for the workplace. Workers reassessed life, family and health. They embraced more flexible work arrangements and increasingly prioritized "human factors" such as wellbeing and work-life balance.[4] Likewise, the 2021 edition of JUST Capital's annual survey on the most important business issues saw the American public put five work-related responses in the top 10, including providing "benefits and work-life balance" and paying a "fair, living wage."[5]

Tools for Investing in Employees

Companies can invest in their employees in a variety of ways. Our research focuses on a few specific actions, including increasing wages, enhancing non-wage benefits, offering stock and improving DEI in the workplace. While not an exhaustive list, these options cover the spectrum of worker pay, overall wellbeing and corporate culture and generally position employees as a key stakeholder to company success. Each action also presents its own unique advantages and disadvantages, as seen in Figure 1.

It is crucial that companies consider these potential tradeoffs and understand how they affect value creation. Plus, no matter the specific action taken to invest in employees, companies must be able to articulate how these investments align with their long-term strategy and investors' return expectations.

In other words, companies must make the case that the types of investments described above are just that — investments that will deliver long-term value creation. Our research helps provide the insights companies need to make this case by analyzing the connection between these investments and several key value creation-related outcomes.

FIGURE 1: ADVANTAGES AND DISADVANTAGES OF OPTIONS FOR INVESTING IN EMPLOYEES

INCREASING WAGES	
✓	Directly addresses many employees' short-term demands; particularly important in an inflationary environment
✗	No guarantee of improved productivity; increase may not be enough to retain talent
ENHANCING BENEFITS	
✓	Addresses an increasingly relevant concern of employees in a post-pandemic world
✗	An uneven offering — given the demand for benefits is highly varied among employees
OFFERING STOCK	
✓	Provides employees with value without hurting short-term bottom line
✗	Impacts may be valued differently based on financial experience, stock volatility and need for short-term liquidity
IMPROVING DEI IN THE WORKPLACE	
✓	Additive to a company's workplace and culture — leading to better outcomes, decision-making and long-term value creation
✗	Hard to quantify; opportunity and culture may take years to change

Results

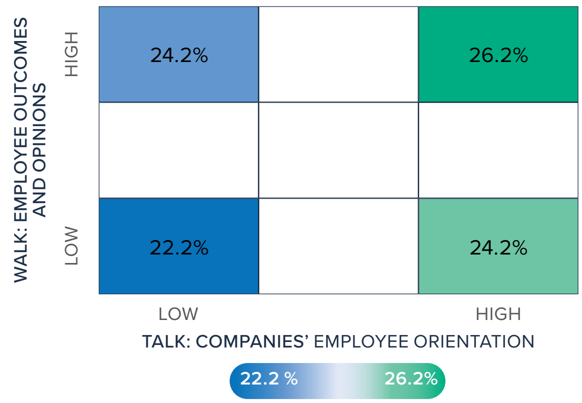
Long-term observations

There is a positive relationship between walk/talk scores and ROIC over longer time horizons, as evidenced in Figure 2. To generate long-term measures, we analyzed value-creation outcomes over three years from the onset of respective walk/talk outcomes.

Committed employers — as evidenced by strong employee-oriented language (high talk, or further right in Figure 2) and strong performance on material employee-related ESG scores (high walk, or further up in Figure 2) — are associated with 4.0% higher three-year ROIC in absolute percentage points.

FIGURE 2: MEDIAN ROIC — CUMULATIVE THREE-YEAR ESTIMATE

Employee outcomes and opinions vs. companies' employee orientations[6]



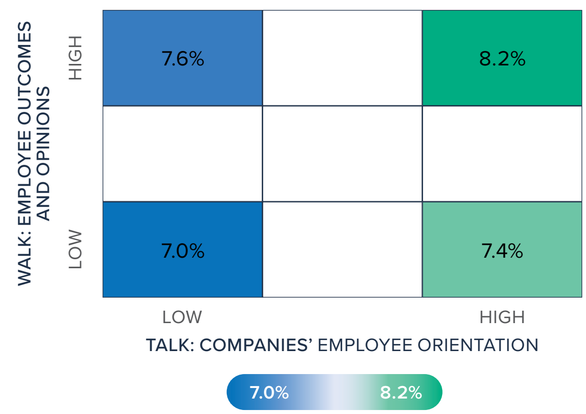
Short-term observations

Controlling for sector-specific effects, our results indicate that companies that are committed to investing in their employees (committed employers — i.e., those with high walk/high talk scores) are associated with lower short-term (up to one year) employee turnover and financial outperformance, as evidenced in Figure 3. Specific results include:

- **1.2% higher contemporaneous annual ROIC on an absolute basis**
- **0.5% higher contemporaneous annual sales growth on an absolute basis**
- **2.8% lower annual employee turnover on an absolute basis**

FIGURE 3: MEDIAN ROIC — CONTEMPORANEOUS

Employee outcomes and opinions vs. companies' employee orientations[7]



THE TALK SCORE: To create talk scores, our natural language processing (NLP) model analyzed annual reports issued by companies in the MSCI All Country World Index from 2010–2021. We assigned target words and corresponding phrases to seven distinct categories: human capital demographics; attraction, development and retention; labour relations; DEI; evaluation & policy; health & safety; and labour costs. We also looked for colocations with words conveying association, positive versus negative sentiment and risk or reward.

Co-occurrences of these words and phrases were counted to create an aggregated employee orientation score and weight-measured by volume to determine how much of the annual report's text content was given to employee-oriented language. The talk score was considered with respect to a firm's country-year, country-sector-year and country-industry-year (based on the 77 SASB industry codes and 11 SASB sectors).

THE WALK SCORE: This score represents the average of the environmental, social and governance (ESG) scores from TruValue and MSCI data which pertain to the employee stakeholder group. We generated percentiles of each measure by industry-year.

For additional details on methodology, refer to Appendix 1.

Other observations

In an effort to unpack employee-oriented strategies, we examined specific actions characterized as non-compensation investments such as employee engagement, DEI commitments and programs, labour policies and employee health & safety. While we concluded that no individual sub-component alone sufficiently explained the walk-talk outperformance, taken together these actions are collectively correlated with long-term value creation.

Generally, specific, individual sub-component factors are not strongly associated with improved value-creation outcomes. For example, compensation-related investments work best in tandem with non-compensation-related investments:

- **A strategy that relies solely on increasing wages is not necessarily sufficient to deliver greater value creation, as high walk/high talk results on wage-related sub-components are not associated with better short- or long-term ROIC or turnover.[8]**
- **Likewise, high walk/high talk scores on non-wage-related benefits sub-components are not associated with better ROIC, sales growth or turnover.[9]**
- **However, we do observe firms that commit to and implement both wage and non-wage benefits are associated with stronger short- and long-term ROIC.**

GEOGRAPHIC DIFFERENCES — OBSERVATIONS OF U.S. AND EUROPEAN COUNTRIES:

Our research revealed interesting differences across regions, particularly between U.S. and European firms.[10] Examples include:

- **Walk and talk frequency** — Since 2018, there has been an increase in talk frequencies at U.S. companies. Talk has also increased at European firms in that time, but at a considerably lower rate. Median talk scores for U.S. companies increased 13.9% between 2018 and 2021, while walk scores only increased 7.6% over the same time period. Comparatively, during this period, European walk and talk scores increased only 0.1% and 0.2% respectively.[11]
- **Strength of correlations** — The correlation between high walk/high talk scores and explicit financial outcomes — ROIC and sales growth — is stronger at European firms. There is evidence of a similar relationship for U.S. companies, but the correlation appears weaker.

These differences in results underscore the varying societal and regulatory environments faced by U.S. and European businesses. Employee-oriented governance and co-determination policies have been prevalent in Europe for decades. Meanwhile, post-2018 increases in talk frequency in the U.S. fit a more recent timeline of increased interest in the subject.[12]

Methodology

This project builds on the methodology first utilized in *Walking the Talk: Valuing a Multi-Stakeholder Strategy.* We analyzed the talk — what companies say or commit to regarding investing in employees — and the walk — how companies acted on their commitments.

We adapted an NLP technique to examine over 40,000 annual reports for employee-centric language (the talk) and incorporated employee-related ESG scores from leading data sources (the walk). The walk and talk topics we assessed are associated with the specific options for investing in employees (increasing wages, enhancing non-wage benefits, offering stock and improving DEI).

Finally, we developed correlations of walk/talk results with outputs associated with value creation, including ROIC, sales growth and turnover. Changes in walk/talk scores and value-creation outcomes over time were also compared with country and sector information.

A NOTE ON LIMITATIONS OF THE DATA:

Due to data constraints, the research results provide information on overall trends rather than precise data points.

Similarly, correlation does not imply causation. The data sample was limited to firms that produced talk (annual reports) and walk (ESG scores) information, so the total number of data points diminishes when testing over longer periods of time. ESG data and aggregate scores are not standardized across providers and inherently rely on the interpretations of their respective providers. Certain other outputs, such as productivity, were studied but did not show statistically significant results and were not included in results.

For additional details on approach, data limitations and areas for further research, refer to Appendix 2.

Takeaways

Our research provides companies and investors with important insights that should help them evaluate employee and other stakeholder-oriented action.

As mentioned, we do see positive effects associated with high employee walk/talk performance on value-creation outcomes. These results are the strongest when companies are “all in” on increasing employee outcomes through multiple levers rather than through one sub-component alone.

Nevertheless, we also observed certain areas with material data limitations and results with less statistical significance. In fact, our results are not as significant as those observed when looking across multiple stakeholder groups, as described in *Walking the Talk: Valuing a Multi-Stakeholder Strategy.*

This leads to two key takeaways. First, when a company develops strategies to invest in its employee base, an approach that incorporates different levers (including, but not limited to, wage and non-wage benefits, DEI initiatives, health & safety measures, labour policies, as well as culture and lifestyle benefits) is most effective. The best approaches will result in systemic improvements to company and employee culture. This is more difficult to measure than the specific relationships described above, meaning companies should also seek to communicate the intent of their strategies.[13] By doing so, companies can integrate and proactively respond to investor priorities.

Second, our research indicates that companies must ensure their worker-focused strategy is integrated in a more comprehensive, multi-stakeholder strategy.[14]

So, What? Actions Companies and Investors Can Take Now

Below are examples of how companies can integrate the findings from this research and focus on employees within a comprehensive, multi-stakeholder strategy for long-term corporate value creation, and how investors can consider these factors when evaluating investee companies.

COMPANIES

- **Execute a long-term employee investment plan while addressing short-term realities. Consider:**
  - Recognizing and evaluating any tradeoffs between the competitive pressures of short-term demands, such as wage increases and hybrid work environments, and long-term resilience
  - Analyzing the impact of a range of levers, including, but not limited to, wage and non-wage benefits, employee stock ownership, DEI initiatives, health & safety measures, labour policies and lifestyle benefits throughout the organization over various periods of time
  - Establishing a strong purpose-driven corporate culture that employees can contribute to and benefit from
  - Providing employees with high-quality training, meaningful interactions with and professional development feedback from managers and growth opportunities
  - Inventorying, anticipating and communicating corporate strategies for long-term investments in employees as part of a bigger company strategy
  - Tracking and publishing pay equity and employee ownership metrics to show progress over time and importance to the company
  - Allocating funds for a multi-year program of making significant investments in training and professional development, and measuring the return on that investment through tracking the promotion of internal managers
- **Highlight the employee voice alongside key financial and operational metrics by:**
  - Tracking employee satisfaction in all parts of the business
  - Incorporating employee satisfaction, key DEI statistics, pay equity and employee ownership metrics into regular board and senior management reports
  - Sharing corporate employee investment objectives with the broad workforce, soliciting suggestions for improvement and rewarding bonuses based on them

INVESTORS

- Determine whether investee companies are walking the talk on investments in their employees
- Reflect on investment in employees as part of the due diligence process
- Consider the potential return of strong employee investment programs or the potential risks of weak employee programs
- Particularly during times of stress, carefully consider the long-term implications of potential cuts to investments in employees similarly to how one might assess potential cuts to R&D, brand building or capital expenditure

Appendix 1
Methodology

UNIVERSE

Annual year-end data for companies in the MSCI All Country World Index, or "ACWI" (approximately 2,900 active constituents across 23 developed and 27 emerging markets). The ACWI covers approximately 85% of the market cap in each market.

SOURCES

Bloomberg and Wharton Research Data Services (annual reports), Compustat, FactSet, JUST Capital, MSCI, RavenPack, Revel.io, TruValue Labs via FCLTGlobal and the ESG Initiative at the Wharton School, University of Pennsylvania.

YEARS COVERED

2010-2021

Y VARIABLES

- Return on invested capital (ROIC) normalized by Sustainability Accounting Standards Board (SASB) sector-year.
  - FORMULA FOR RETURN ON INVESTED CAPITAL:

$$\frac{\text{Net income}}{(\text{shareholders' equity} + \text{long-term debt})}$$

- Sales growth
  - Annual percentage change in year-end sales (US$)
- Productivity
  - FORMULA FOR PRODUCTIVITY:

$$\frac{\text{sales}}{\text{employees}}$$

- Employee turnover
  - Annual percentage change in logged number of employees

KEY X VARIABLES

- **Employee walk percentile.** This measure captures the average of the environmental, social and governance (ESG) scores from TruValue and MSCI data which pertain to the employee stakeholder group.
  - We generated percentiles of each measure by industry-year.
- **Generating employee scores within data sources**
  - **TruValue data** contains 26 materiality categories, four of which pertain to the employee stakeholder group. We mapped these 26 ESG issues, whose materiality differs by industry. We then calculated an aggregate employee stakeholder score by taking the mean of the employee-specific materiality categories, weighted by the number of articles in each materiality category. The employee stakeholder score was derived from: employee engagement, DEI, employee health & safety, labour practices and systemic risk factors.
  - **MSCI data** was coded into stakeholder groups. For the employee measure, we used the average of four scores: labour management, health & safety, human capital and access to healthcare.

Appendix 1 (cont'd)

Methodology

KEY X VARIABLES (CONT'D)

- **Employee talk score**
  - This measure captures how much a firm's annual report language is spent on employee-oriented language.
  - To calculate our talk score, we first measured the number of significant words (related to the concepts of risk, reward, positive, negative or affiliation) in proximity to employee words divided by the volume of the firm's annual report.
  - We then regressed this measure of employee talk on a vector of indicator variables capturing a firm's industry, sector, country and year.
  - Our final measure is the firm's residual — that is, its actual employee talk measure — minus its predicted employee talk measure from the regression. We standardized this measure.
  - Our list of employee words was generated using an original list available in Appendix 2 of Zhang (2021). Linguistic construct lists (e.g., positive words) were collected from the Loughran-McDonald master dictionary and the Linguistic Inquiry and Word Count software program.[15]

MODEL SPECIFICATION

- Our main models regressed sales growth, ROIC, employee turnover and productivity on employee walk, employee talk and a set of control variables.
  - Employee walk and talk scores were considered with respect to a firm's country-year, country-sector-year and country-industry-year (based on the 77 SASB industry codes and 11 sectors).
- We ran separate models for contemporaneous independent variables, as well as independent variables lagged by one and three years. Our control variables were always lagged by one year.
- We ran separate models which considered various combinations of analysis, including:
  - Employee stakeholder sub-components, derived from TruValue Labs: employee engagement, DEI, employee health & safety, labour practices and systemic risk factors
  - Sub-components grouped into wage-based vs. non-wage-based incentives
  - Complete analysis on U.S. sub-sample of firms
  - Complete analysis on European subsample of firms: Austria, Belgium, Cyprus, Czech Republic, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Malta, Netherlands, Norway, Poland, Portugal, Spain, Sweden and Switzerland.

STATISTICAL SIGNIFICANCE

Determined by multivariable regression with the key independent variables lagged by one, two and three years. Weakly significant = 0.1, significant = 0.05, and strongly significant = 0.01.

OUTLIERS

Normalized percentile scores used in analysis. Extreme values for variables were winsorized at the 1st and 99th percentiles.

Appendix 1 (cont'd)

Methodology

INDICATOR VARIABLES (DEPENDENT ON SPECIFICATION)

- Years: 2010–2021
- SASB sectors: Financials, Infrastructure, Services, Transportation, Technology & Communications, Extractives & Minerals Processing, Resource Transformation, Health Care, Consumer Goods, Food & Beverage, Renewable Resources & Alternative Energy
- SASB industries: Aerospace & Defense, Agricultural Inputs, Air Freight & Logistics, Airline, Aluminum, Apparel & Footwear, Auto & Truck Manufacturers, Auto Components, Banking, Beverages: Alcoholic, Beverages: Non-Alcoholic, Biotechnology, Business Services, Cable & Satellite, Cement, Chemicals, Coal, Commercial Printing, Construction & Engineering, Construction Materials, Consumer Electronics, Copper, Diversified Financials, Diversified Metals & Mining, Electric Utilities, Electronic Equipment, Instruments & Components, Environmental & Facility Services, Farm & Construction Machinery, Fertilizers & Agricultural Chemicals, Fishing, Hunting & Agriculture, Food Retail, Food, Beverage & Tobacco Products, Forest & Paper Products, Gas Utilities, Gold, Government Services, Health Care Equipment & Supplies, Health Care Providers & Services, Health Care Technology, Homebuilding, Hospitals, Hotels, Resorts & Cruise Lines, Household Durables, Industrial Conglomerates, Industrial Gases, Industrial Machinery, Information Technology Services, Insurance: Life, Health & Medical, Insurance: Property & Casualty, Insurance: Reinsurance, Internet Services & Infrastructure, Investment Banking & Brokerage, Iron & Steel, Leisure Products, Life Sciences Tools & Services, Lumber & Wood Production, Medical Devices, Medical Equipment & Supplies, Metals & Mining, Natural Gas Distribution, Oil & Gas Exploration & Production, Oil & Gas Refining & Marketing, Other Consumer Services, Other Diversified Financials, Other Industrial Metals & Mining, Other Pharmaceuticals & Biotechnology, Other Specialty Retail, Packaged Foods & Meats, Paper & Paper Products, Personal Products, Pharmaceuticals, Pipelines, Plumbing, Heating & Air-Conditioning, Pollution Control Equipment & Services, Real Estate Management & Development, Renewable Electricity, Semiconductors & Semiconductor Equipment
- Country
- Firms

CONTROL VARIABLES

Log(sales), log(total assets), Debt/total assets

CONSTRUCTION OF THE WALK-TALK MATRIX

- Taking our final employee walk and talk scores, we proceeded to split the sample into nine subgroups, forming a three-by-three grid. Firms in the lowest tercile of walk and talk scores were grouped into the "1-1" (bottom left) bucket, while firms in the highest tercile of walk and talk scores were grouped into the "3-3" (top right) bucket.
- Firms can move between buckets as they become more or less employee oriented. However, firms are often slow to move, and large jumps of more than a single bucket or tercile are rare.

Appendix 2

Additional Results and Notes (includes non-statistically significant results, limitations and areas for additional research)

DEPENDENT OUTPUT VARIABLES

- **Sales growth**
  - U.S. firms in particular exhibit positive, statistically significant sales growth in the short-term, but the effect does not persist over long-term (three-year) period
  - It is difficult to isolate what is driving this association
    - Wage- and non-wage-related benefits exhibit positive effects, though mainly driven by non-wage actions (employee engagement, DEI and employee health & safety)
- **Annual turnover**
  - Effect does not persist over long-term (three-year) period
  - Results are more complex at U.S. firms
    - Wage-related benefits exhibit lower rates of turnover in the long-term when controlled for by country-sector
    - This may reflect an environment of economic volatility in which employee risk tolerance is lower, making wage-related benefits an important and motivating signal of job security

SUBCOMPONENTS OF EMPLOYEE-RELATED VARIABLES

- Many subcomponents of employee-related variables were not positively or negatively correlated with output variables as standalones (e.g., just labour policies on ROIC)
  - Wage-related benefits, including employee wages and bonuses
  - Non-wage related benefits, including employee engagement; DEI; employee health & safety; labour practices; and systematic risk

OTHER LIMITATIONS

- **Productivity and turnover measures are not without flaws**
  - Productivity is hard to measure as it does not account for outsourced work (i.e., a firm has much higher sales/employee when more of its work is outsourced). In an ideal world, we would compare the productivity of existing work on similar tasks, but this is not possible. High productivity could also signal worse work-life balance and over-stretched resources.
  - The effects of the Great Resignation might mean that turnover is more relevant in post-COVID-19 time periods (e.g., the need COVID-19 created for companies to downsize their labour force). Turnover data may also be skewed based on companies' COVID-19 layoffs.
  - In addition, measures of turnover and productivity may be inherently linked, given that both rely on the number of employees, since productivity = sales/employees.
- **Pre-COVID-19 walk and talk predict post-COVID-19 walk and talk**
  - The uniqueness of the COVID-19 context is important to consider when examining the outcomes of companies' investments in their employees.
  - Empirical results support the materiality of COVID-19 to companies' employee-centered walk and talk scores. More specifically, empirical estimates find that for every percentile in walk and talk above the average a firm is positioned in 2019, there is a predicted statistically significant decline in a company's 2020-2021 walk (-0.29) and talk (-0.34) scores. Relatively higher walk and talk scores before the pandemic, coupled with slight declines at the onset of the pandemic, suggest there may be a structural shift in employee orientation when the effects of the pandemic settle.
  - For example, given referent walk score of approximately 50 in 2019, a firm with a walk score in the 60th percentile in 2019, would on average drop to the 57th percentile ((60-50)*-0.29) in the COVID-19 period, 2020-2021.

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Endnotes

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6 Calculated as cumulative three-year ROIC estimates of firm-year observations from each bucket. Of note, firms can move between buckets as they become more or less employee oriented, but are often slow to move, and large jumps of more than a single box are rare. For further detail, see Appendix 1.

7 For full analysis graphics and results, contact research@fcltglobal.org.

8 Increasing wages alone, for example, may elicit a mercenary response that shifts the focus toward financial reward.

9 These benefits may not matter, for example, if employees don't have enough base compensation to offset their cost-of-living.

Endnotes (cont'd)

10 European firms include Austria, Belgium, Cyprus, Czechia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Malta, Netherlands, Norway, Poland, Portugal, Spain, Sweden and Switzerland. Of note: U.K. is excluded in this comparison.

11 U.S. companies started from a slightly lower raw talk frequency in 2018, but had eclipsed their European counterparts in talk by 2021.

12 "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans.'" Business Roundtable. 2019. https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans.

13 While there are limitations to our analysis, the conclusions suggest that improving the employee experience is a fundamental driver of value creation. It is oftentimes easy to default to wage and non-wage benefits, but non-financial factors that enhance workplace safety and DEI can yield large value-creation outcomes for employers.

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