GECN™ GROUP | GLOBAL GOVERNANCE AND EXECUTIVE COMPENSATION GROUP

North America • Continental Europe • United Kingdom • Asia • Australia • Africa

GECN GLOBAL INSIGHTS JULY 2022

Will 2021 Pay Trends Continue in 2022?

I. In 2021, multiple factors created pay pressures

In 2021, we had observed a considerable uptick in variable compensation for executives. This was related to low payouts in 2020, better corporate performance in 2021, and targets that had been conservatively set for the year.

In early 2022 there was no reason to think that the trend would not continue. Many felt that a compensation ‘catch-up’ remained needed at the executive level and below. After all, the labor market remained tight, offering employees leverage to negotiate higher salaries. Moreover, with resignation levels having reached record levels in 2021 in many markets (particularly among GenZ), employers worried less about higher labor costs and more about talent loss and staff shortages.

More recently, however, inflation has kicked up and stock markets have been rattled, in part due to the factors discussed on the right. Many companies are readjusting their internal earnings forecasts, and some have even announced layoffs. Despite continued strong employment levels in many countries, some economists no longer exclude the potential of a recession in the months ahead.

This may explain also why the past few months have seen more cases of company shareholders expressing higher disapproval on say on pay, and more willingness in some countries to vote against the re-election of Board members.

Thus, it remains to be seen whether the 2021 pay pressures will dissipate by year end, or only remain in certain countries or sectors or for certain types of positions.

This short read provides collective insights from the GECN Group companies across the globe on how current developments may impact executive and other pay in 2022. While it notes that some pay trends from 2021 may be affected, it concludes that the ESG and related trends will not let up.

For more on GECN and its Group companies, visit us at http://gecn.com/

To receive a copy of the forthcoming 5th Annual GECN Global Study on ESG and Pay, click here: http://gecn.com/contact/

II. In 2022, new impacts complicate the picture

Supply-chain bottlenecks, high energy prices, global commodities pressures, chip shortages, and geopolitical tensions are affecting markets and companies so far in 2022.

Collectively, these dynamics will challenge Board compensation committees when they evaluate their companies’ performance at year end and make pay decisions. For what looked to be clear economically in 2021 is now looking cloudier. At the same time, Boards would be well advised - as we argue below - not to let up in their oversight of companies on ESG, including exploring the connection to compensation.

III. ESG link to pay not waning

One 2021 trend that we do not see relenting in 2022 relates to sustainability.

Our 4th Annual GECN Group Global Trends study recorded again an increase in the use of ESG metrics in executive compensation plans. For example, over two-thirds of publicly listed companies now have some ESG metric in their short-term incentives.

While institutional investors, like BlackRock, have taken strong stands supporting the use of non-financialmetricsincompensation, the ESG movement is now at a point where it has its own momentum. For example, we are now seeing more effortstoset specific,quanti fiableperformancetargetsaroundESGmeasures, rather than softer
'progress' aspirations.

Boards thus will wish to have this point front and center as they review and form views on their companies' short-term as well as long-term incentive plans.

At the same time, the risk side of ESG has become more apparent. As companies recognize in ESG an opportunity to promote themselves to shareholders and their products to clients, they need to ensure their claims in disclosures and advertising do not exceed their actual demonstrable ESG progress. Beyond 'greenwashing', there are many important ethical and legal reasons why Boards should concern themselves with the governance of ESG at their company.

IV. Regulation is rising

As in 2021, there continues to be regulatory activity around the world on climate and other ESG topics.

Many of these regulations focus on disclosure so that the market can judge how companies are performing in these critical areas. Others go further in strengthening substantive laws on the environment, customer and investor protection, and conduct risk.

Some of the above are directly pay related, such as the efforts to toughen claw-backs to make it easier to recoup past variable pay that was not justly earned. Others touch on human capital management and thus indirectly also on performance management and related topics.

V. Board diversity is in focus

The push for diversity in companies is also now reaching the Board itself.

Some investors and proxy advisors are setting policies on gender, racial, and other diversity. They are also demanding more disclosure on how boards aim to increase their diversity. For example, some proxy advisors advise that they will vote against the re-election of the Nomination Committee Chair of Boards having less than 30% women.

VI. Further spread in use of equity-based instruments

As in 2021, we continue to see gains in the use of performance shares (PSU).

In countries where PSUs are already common, we are seeing high adoption of a 'Restricted Shares' approach.

Furthermore, we do not see any reduction in market pressure to prolong LTI plan duration, in particular post-vesting holding requirements which can be as much as two years. As an example, in line with updated recommendations from the Investment Association, a majority of large, listed companies in the UK now have post-vesting requirements.