The AMBACHTSHEER Letter

Sustainable Pension Design • Effective Pension Management

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DOES BETTER GOVERNANCE PRODUCE BETTER OUTCOMES?

NEW EVIDENCE FROM THE CORPORATE SECTOR

"In this study, we explore the organizational and performance implications for organizations that integrate [sustainability into their] corporate policies. Our overarching thesis is that such organizations represent an alternative and distinct way of competing for the modern corporation, characterized by a governance structure that in addition to financial performance, accounts for the environmental and social impact of the company, a long-term approach to maximizing inter-temporal profits, an active stakeholder management process, and more developed measurement and reporting systems…..".

From a new study published in **Management Science**
by Robert Eccles, Ioannis Ioannou, and George Serafeim

How One Thing Leads to Another

All recipients of this *Letter* recently received a copy of our survey-based study on pension governance quality and long-term investing effectiveness.[i] Its key messages were that many of the 81 pension organizations in the survey have some way to go in devising effective organizational governance and long-term investing processes. A hopeful finding was a positive correlation between perceived governance quality and long-term investing effectiveness. While these findings are material, they beg an important question: does better governance really lead to better organizational outcomes over the long-term? The stronger the evidence that this is actually the case, the stronger the case that pension organizations and their stakeholders should actively work to raise the effectiveness of their governance processes. They would have a clear fiduciary duty to do so.

While there is some evidence that better governance does indeed produce better organizational outcomes over the long-term, it has not been statistically strong for the simple reason that unambiguous, comparable metrics of governance quality and organizational performance over long periods of time have not existed.[ii] A helpful reader of our recent pension governance quality and long-term investing paper pointed out that this is no longer the case.[iii] As evidence, she attached the paper from which we quote above: "The Impact of Corporate Sustainability on Organizational Processes and Performance" by Robert Eccles (Harvard Business School), Ioannis Ioannou (London Business School), and George Serafeim (Harvard Business School). We call the authors EIS below. The paper provides strong evidence that, at least in the corporate sector, better governance does indeed lead to better organizational outcomes. This *Letter* summarizes EIS's findings and sets out their implications for the governance and investment strategies of pension organizations.

The Design of the EIS Sustainability Study

The essence of study design was to create a long-term database on the key characteristics of what EIS called *high-sustainability (HS)* and *low sustainability (LS)* corporations. Through a series of statistical routines they created a 'matched' sample of 90 *HS* and 90 *LS* corporations, with detailed data sets for each over the 1993-2010