

# **MSCI ESG Ratings Methodology: Labor Management Key Issue**

MSCI ESG Research LLC

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## Introduction

This document provides essential information on the components of the Labor Management Key Issue to enable users of ESG Ratings to understand how our outputs are determined. Labor Management is a Key Issue in the Social Pillar of the MSCI ESG Ratings model. Companies are evaluated on the complexity of their workforce (size, labor intensity and regions of operation), the relationship between management and labor, the strength of worker protections, and their employee engagement efforts.

For additional details on the MSCI ESG Ratings Model, refer to Section 2, Data, ratings and scores, of “ESG Ratings Methodology.”

### Exhibit 1: MSCI ESG Key Issue hierarchy

3 Pillars	10 Themes	33 ESG Key Issues
Environmental	Climate Change	Carbon Emissions
		Climate Change Vulnerability
		Financing Environmental Impact
		Product Carbon Footprint
	Natural Capital	Biodiversity & Land Use
		Raw Material Sourcing
		Water Stress
	Pollution & Waste	Electronic Waste
		Packaging Material & Waste
		Toxic Emissions & Waste
	Environmental Opportunities	Opportunities in Clean Tech
		Opportunities in Green Building
		Opportunities in Renewable Energy
Social	Human Capital	Health & Safety
		Human Capital Development
		<b>Labor Management</b>
	Product Liability	Supply Chain Labor Standards
		Chemical Safety
		Consumer Financial Protection
		Privacy & Data Security
		Product Safety & Quality
	Stakeholder Opposition	Responsible Investment
		Community Relations
	Social Opportunities	Controversial Sourcing
		Access to Finance
		Access to Health Care
		Opportunities in Nutrition & Health
Governance	Corporate Governance	Board

3 Pillars	10 Themes	33 ESG Key Issues
		Pay
		Ownership & Control
		Accounting
		Business Ethics
	Corporate Behavior	Tax Transparency

## Risks associated with this Key Issue

- Production delays due to labor unrest.
- Reduced productivity and product quality.
- Loss of growth opportunities, market share or pricing power due to damage to brand value.

## Labor Management Key Issue Score

The Labor Management Key Issue Score evaluates the company's level of exposure to, and management of, risks on this Key Issue. The Key Issue Score is based on the Exposure Score and the Management Score using the formula below. The Exposure Score and the Management Score are combined such that a higher level of exposure requires a higher level of demonstrated management capability in order to achieve the same overall Key Issue Score.

$$KI_i = 7 - (\max(EXP_i, 2) - MGMT_i)$$

Where:

- $KI_i$  is the Key Issue Score for company  $i$ .
- $EXP_i$  is the Exposure Score for company  $i$ .
- $MGMT_i$  is the Management Score for company  $i$ .

## Labor Management Management Score

The Labor Management Management Score evaluates the company's ability to manage its exposure to risks on this Key Issue. It is based on an average of the scores associated with each of the Management Score categories listed below.

These scores are derived from data points that are scored on a 0-10 scale, with 10 corresponding to best practice and 0 corresponding to lack of management. Refer to Section 3.3, Analyzing risk management, of “ESG Ratings Methodology” for additional details. Sources are company disclosures except where otherwise indicated. The following formula is used to calculate the Labor Management Score:

$$MGMT_{LBM,i} = \frac{STRAT_{LBM,i} + PROI_{LBM,i} + PERF_{LBM,i}}{3}$$

Where:

- $MGMT_{LBM,i}$  is the Labor Management Management Score for company  $i$ .
- $STRAT_{LBM,i}$  is the Strategy Score for company  $i$ .
- $PROI_{LBM,i}$  is the Programs & Initiatives Score for company  $i$ .
- $PERF_{LBM,i}$  is the Performance Score for company  $i$ .

The following data points, without constituting an exhaustive list, are representative of the inputs to the Management Score and are used in the Management Score calculation:

### Management Score category: Strategy Score

- **Employee equity programs.**

**Definition:** The scope of the company’s workforce eligible for an employee stock ownership plan or employee stock purchase plan.

- **Workforce eligible for non-pay benefits.**

**Definition:** The scope of the company’s workforce eligible for material non-compensation benefits. Best practice is to cover all employees. The indicative list of major non-compensation benefits includes: pension (defined benefit pension plan, substantial matching on defined contribution plan e.g., 401k), retirement plans (Simplified Employee Pension Individual Retirement Account (SEP IRA), etc.), housing (employer-provided or employer-paid), group insurance (health, dental, life etc.), disability income protection, tuition/certification reimbursement.

- **Scope of workforce eligibility for variable performance-based component to pay.**

**Definition:** Indicates whether non-officer staff are eligible for variable performance-based pay, such as bonuses, and considers the scope of employees eligible for performance-based pay.

## Management Score category: Programs & Initiatives Score

- **Employee satisfaction survey frequency.**

**Definition:** The frequency (if any) with which the company surveys its employees.

- **Restructuring policies and programs.**

**Definition:** Indicates whether the company has established clear policies for employees following a restructuring or layoff, such as offering severance pay or assistance with outplacement, reemployment or retraining.

- **Scope of skills and knowledge development training.**

**Definition:** The scope of the company's workforce covered by training (if any) that would provide an opportunity for an employee to move up or into a new role.

- **Support for degree programs or certifications for employees.**

**Definition:** The scope of the company's workforce eligible for support in pursuing degree programs or new certifications through tuition or fees reimbursement, sabbaticals, etc.

## Management Score category: Performance Score

Assesses the company's performance on industry-specific and region-specific labor management metrics (including turnover, employee productivity, strikes and external recognition) relative to its peers.

### Representative performance metrics:

- Employee turnover.
- Employee productivity.
- Strikes.
- External recognition.

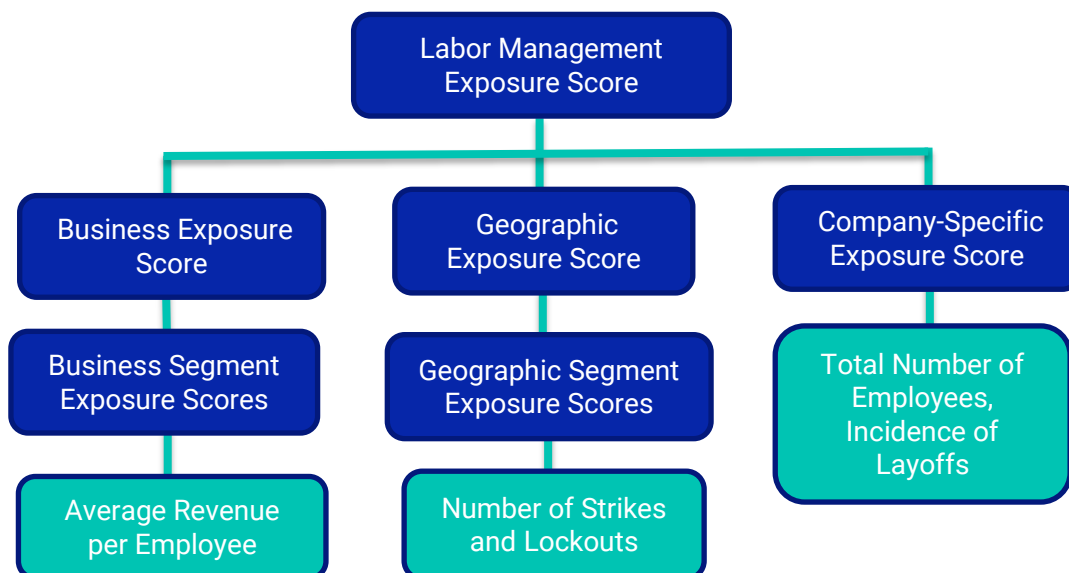
## Labor Management Exposure Score

The Labor Management Exposure Score evaluates the company's exposure to risks on this Key Issue. It is based on the average of the Business and Company-Specific Exposure Scores, combined with the Geographic Exposure Score. The Geographic Exposure Score functions as a multiplier on the Business Exposure Score, with an impact ranging from -50% to +50%. The Business, Geographic and Company-Specific Exposure Scores are scored on a 0-10 scale, with 10 corresponding to the highest risk and 0 corresponding to the lowest risk. Refer to Section 3.2, Analyzing risk exposure, of "ESG Ratings Methodology" for additional details. The following formula is used in the Exposure Score calculation :

$$EXP_{LBM,i} = \frac{BUS_{LBM,i} + COM_{LBM,i}}{2} (1 + 0.1(GEO_{LBM,i} - 5))$$

Where:

- $EXP_{LBM,i}$  is the Labor Management Exposure Score of company  $i$ .
- $BUS_{LBM,i}$  is the Business Exposure Score of company  $i$ .
- $GEO_{LBM,i}$  is the Geographic Exposure Score of company  $i$ .
- $COM_{LBM,i}$  is the Company-Specific Exposure Score of company  $i$ .

**Exhibit 2: Exposure Score components**


## Business Exposure Score

The Business Exposure Score is a weighted average of the Business Segment Exposure Scores of a company's business segments. Scores are weighted by the proportion of a company's total assets in each business segment,<sup>1</sup> using the following formula to calculate the Business Exposure Score:

$$BUS_{LBM,i} = \sum_{j=1}^{n_i} w_{Asset,i,j} BSE_{LBM,j}$$

Where:

- $BSE_{LBM,j}$  is the Business Segment Exposure Score for business segment  $j$ .
- $w_{Asset,i,j}$  is the weight of business segment  $j$  for company  $i$  based on the contribution to total company assets.
- $n_i$  is the number of business segments of company  $i$ .

<sup>1</sup> The percentage of assets is typically calculated as the company-reported asset value of the segment divided by the total asset value. In certain cases, industry-specific metrics are used to calculate the percentage of assets, such as power generation, production volume or reserve value. In cases where neither segment assets nor a relevant industry-specific proxy is available, the percentage is calculated based on segment revenue.



## Business Segment Exposure Scores

The Business Segment Exposure Score of a business segment is based on a mapping of the business segment as disclosed by the company to a corresponding business activity. MSCI ESG Research uses the Standard Industrial Classification (SIC) system along with industry-specific adjustments to define business activities. The score associated with a business activity is used to calculate a Business Segment Exposure Score. Each business activity score is determined by the Employee Revenue Score of the segment.

$$BSE_{LBM,j} = ER_j$$

Where:

- $ER_j$  is the Employee Revenue Score for business activity  $j$ .

The Employee Revenue Score of a business activity is calculated by using the five-year trailing average revenue per employee attributed to a given business segment, such that a lower revenue per employee gets a higher score. Business activities with lower revenue per employee tend to be more labor-intensive, resulting in a higher Business Segment Exposure Score.

## Geographic Exposure Score

The Geographic Exposure Score is a weighted average of the Geographic Segment Exposure Scores of the countries and regions in which a company operates. Scores are weighted by the proportion of a company's total assets in each geographic segment through the following equation:

$$GEO_{LBM,i} = \sum_{r=1}^{n_i} w_{Asset,i,r} GSE_{LBM,r}$$

Where:

- $GSE_{LBM,r}$  is the Geographic Segment Exposure Score of region  $r$ .
- $w_{Asset,i,r}$  is the weight of total assets in region  $r$  for company  $i$ .
- $n_i$  is the number of geographic segments for company  $i$ .

For geographic segments reported as regions (example: Asia Pacific), a nominal GDP-weighted country aggregation is used to calculate region-level scores, using the following equation:

$$GSE_{LBM,r} = \sum_{c=1}^{n_r} w_{GDP,r,c} GSE_{LBM,c}$$

Where:

- $GSE_{LBM,c}$  is the Geographic Segment Exposure Score of country  $c$ .
- $w_{GDP,r,c}$  is the specific weight of country  $c$  within region  $r$ .

## Geographic Segment Exposure Scores

The Geographic Segment Exposure Score is determined by the Strikes and Lockouts Score for a country.

$$GSE_{LBM,c} = SL_c$$

Where:

- $SL_c$  is the Strikes and Lockouts Score in country  $c$ .

The Strikes and Lockouts Score for a country is calculated using the trailing 10-year average number of strikes and lockouts for a given country. The higher the number of strikes and lockouts, the higher the score, with the score varying from 0 to 10.

## Company-Specific Exposure Score

The Company-Specific Exposure Score is determined by a simple average of the Total Employees Score and the Layoffs Incidence Score.

$$COM_{LBM,i} = \frac{TE_{LBM,i} + LI_{LBM,i}}{2}$$

Where:

- $COM_{LBM,i}$  is the Company-Specific Exposure Score of company  $i$ .
- $TE_{LBM,i}$  is the Total Employees Score of company  $i$ .
- $LI_{LBM,i}$  is the Layoffs Incidence Score of company  $i$ .

The Total Employees Score is derived from the total number of employees of a company.

The Layoffs Incidence Score for a given company is calculated from the number of layoffs in the last three years. A score of 10 is assessed if layoffs affect more than 10% of the company's workforce or more than 1,000 employees.

## Data Sources

The following sources are used to determine the Labor Management Exposure Score:

International Labour Organization, Refinitiv, MSCI ESG Research, company disclosures.

## Contact us

[msci.com/contact-us](https://www.msci.com/contact-us)

### AMERICAS

United States	+ 1 888 588 4567 *
Canada	+ 1 416 687 6270
Brazil	+ 55 11 4040 7830
Mexico	+ 52 81 1253 4020

### EUROPE, MIDDLE EAST & AFRICA

South Africa	+ 27 21 673 0103
Germany	+ 49 69 133 859 00
Switzerland	+ 41 22 817 9777
United Kingdom	+ 44 20 7618 2222
Italy	+ 39 02 5849 0415
France	+ 33 17 6769 810

### ASIA PACIFIC

China	+ 86 21 61326611
Hong Kong	+ 852 2844 9333
India	+ 91 22 6784 9160
Malaysia	1800818185 *
South Korea	+ 82 70 4769 4231
Singapore	+ 65 67011177
Australia	+ 612 9033 9333
Taiwan	008 0112 7513 *
Thailand	0018 0015 6207 7181 *
Japan	+ 81 3 4579 0333

\* toll-free

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