Engaging with shareholders helps mitigate the impact of a crisis

When an environmental or social controversy reaches the media, active dialogue with major investors can soothe the market.

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An alleged human rights violation scandal, a conflict with local communities or an environmental accident can shake a company and alarm investors. But knowing that some

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shareholders are working with the company to address the problem can send a signal of confidence to the market.

Research by IESE professor Fabrizio Ferraro, together with Irene Beccarini, Diego P. Guisande and Andreas G.F. Hoepner, indicates that dialogue with shareholders moderates the negative impact of such crises on companies' valuations.

At a time when the anti-ESG movement is gaining momentum — questioning whether companies should engage with shareholders on environmental and social issues — the study suggests that this very engagement can help protect market value following a reputational crisis.

Shareholder engagement can drive changes in a company's policies or practices, as well as influence how other investors perceive risk. And when a company is already under media scrutiny, that perception can affect its valuation.

Institutional investors do not make decisions in isolation. They observe one another and place greater trust in those they consider more credible and better informed. Although dialogue between shareholders and companies is private, some of the information filters through. As a result, dialogue can send different signals depending on the context:

- **When there is no controversy,** knowing that a shareholder is in discussions with a company about an environmental or social issue may alert other investors to risks they were previously unaware of.
- **When the problem has already come to light,** the interpretation changes. The media have already made the risk visible, and what is new for the market is something else: Some shareholders remain engaged with the company and are in dialogue with it because they believe the problem can be addressed. The authors describe these dialogues as "soothing whispers" to the investment community. The crisis remains unresolved, but investors with firsthand information continue to back the company.

Stakeholders apply pressure, shareholders respond

Environmental or social controversies are associated with lower company valuations the following year. However, the data indicate that this decline is smaller when there is active

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shareholder engagement. In other words, dialogue moderates the financial impact of controversies generated by other stakeholders.

This does not mean that conversations with investors automatically create value. The study finds no evidence that dialogue on its own improves financial performance; its beneficial effect emerges when a company is facing a reputational crisis.

The identity of the interlocutor also matters. The authors argue that this effect occurs only when the dialogue involves investors with sufficient prestige and influence within the investment community to shape others' perceptions, and when the discussions focus on ESG issues.

The problem does not have to be resolved

According to the authors, the effect of shareholder dialogue does not depend on the problem being resolved. It is enough for the company to have acknowledged the issue for dialogue to send a positive signal to the market, even before a solution has been proposed or implemented.

The authors point out that companies' efforts to secure shareholder support during a reputational crisis can help preserve their long-term financial performance. It may, therefore, be worthwhile for investor relations departments and executives to take the initiative in inviting or seeking dialogue with shareholders concerned about environmental and social issues, particularly following a controversy.

Ultimately, dialogue with institutional shareholders after a crisis provides an opportunity to discuss risks, mitigate their consequences, and strengthen investor and market confidence. When other investors perceive that informed shareholders remain committed to the company, perceptions of risk may decline — and with them, the financial impact of the crisis.

About the study

The research analyzed 771 S&P 500 companies between 2007 and 2019, combining financial information with data from RepRisk and Federated Hermes EOS. RepRisk, a database that uses artificial intelligence to track negative news about ESG issues, made it possible to identify and classify environmental and social controversies reported in the media. Federated Hermes EOS, which engages with companies on behalf of major institutional investors, provided data on 182 shareholder dialogues on environmental and social issues.

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5 steps for stakeholder dialogues

In separate work on stakeholder dialogues, IESE Prof. Antonino Vaccaro and researchers from the University of Turin identified five steps to bring stakeholder voice into your organization's accounting.

1. Map your stakeholders

Use surveys and focus groups to understand expectations. This will help determine how much weight each group should carry in your decisions. Ensure less visible groups, such as temporary workers and smaller suppliers, are not overlooked.

2. Set the rules of engagement

Determine methods for dialogue, such as consultations or workshops, with clear ground rules. Take minutes so that dialogues are documented, including any points of disagreement. Do not force consensus; at this stage, the goal is to agree on how conflicts will be addressed.

3. Set objectives and priorities

Work with stakeholders to define objectives (what), strategies (how) and responsibilities (who). Seek an accounting framework that incorporates social and environmental criteria alongside financial ones.

4. Put it into practice

Update accounting and accountability procedures. Appoint teams responsible for implementation. Train employees. Distribute oversight among multiple stakeholders to prevent power from becoming concentrated.

5. Communicate, listen and adapt

Make your commitments and results known through various communication channels. Gather feedback to identify areas for improvement. Keep the dialogue going. This step strengthens trust and transparency.

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