Effective human capital management is critical for long-term performance. (UBS)

Three reasons why investing in people matters

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Investing in human capital benefits both employees and companies through increased productivity and lower turnover rates, crucial for long-term performance. Climate change, AI, and an experience-driven economy are key factors for effective workforce management. ESG leaders excelling in human capital management may better handle near-term challenges and extract long-term value from improved labor productivity. Investing in themes like "Diversity and Equality" can also be a way to identify companies focused on employee retention and productivity.

In 2022, about a third of IKEA's US workforce quit, and half of its new hires in the UK and Ireland left within a year, according to Bloomberg and company reports. Each departure cost IKEA at least USD 5,000 to replace. To tackle this, the company raised wages, made shift schedules flexible, and adopted new technologies. These changes led to a 44% drop in voluntary turnover in Ireland and a 25% drop in the US within only eight months.

This example shows that investing in employees can lead to operational success and meaningful financial impact. With labor strikes and shortages on the rise, effective human capital management—including diversity, inclusion, and employee health and safety—is crucial for long-term value creation. It has the potential for both companies and investors to unlock additional long-term value from improved labor productivity.

Here are three reasons why effective human capital management is increasingly important:

1. Climate Change Impacts Productivity: Extreme heat affects sectors requiring outdoor physical labor, like agriculture, mining, and construction. The Federal Reserve Bank of San Francisco notes that decreased productivity can slow capital accumulation and consumption. Heat exposure has caused up to 2,000 worker fatalities and 170,000 workplace injuries in the US, based on a report from Public Citizen. Companies must consider climate risks for employees exposed to heat stress.

2. Emerging Technologies and AI: AI and other technologies can boost efficiency and productivity if employees are properly trained. An MIT study found AI too expensive to replace humans in most jobs, but it will impact nearly every job according to the Harvard Business Review. As emerging technologies and AI manifest their potential, sufficient ethics and data security policies are necessary, and the shift toward a new era of digital transformation will be one that reduces learning friction toward building a more equitable and inclusive workforce.

3. Employee Engagement Drives Customer Engagement: Engaged employees provide better customer service—a key competitive advantage. In an experience-driven economy, quality customer service is more important than ever. A Forbes survey found 48% of consumers are willing to pay more for quality service, leading to customer loyalty and better pricing strategies.

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For more, see **Sustainable investing perspectives: Semiconductors, three reasons to invest in people, and transition risk for real estate**, 9 July 2024.