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Video Transcript: TSR – The Alignment Tool We Can't Ignore

Dave Swinford: There are a couple of big misconceptions about TSR. One is that it's a performance measure. It isn't. It's an alignment measure. What I mean by that is that because of the way TSR works, when TSR for a particular company is poor, managers pay does go down. When TSR is very good, managers pay goes up, because they perform worse or better relative to the comparison group. Pay is moving in the right direction with shareholder returns, but it's an alignment tool.

Studies back in the '80s and '90s show that TSR is about 80 percent determined by general market factors and industry factors other than the company. The second misconception is that investors want people to use it. If you talk to investors, they view TSR as acceptable when you don't know something better to do. Those people are much more focused on, what is your strategy? What specifically are you going to do to generate value ahead of your industry over the next few years? How do you drive that through the management team to make it work?

I think that one of the things that we try to do as an organization, as Pearl Meyer, is when there is a minority practice, let's say 39 percent of companies do something, I don't want to dismiss that and simply say, "Sixty-one percent of the companies do this. You should do it." I want to understand why the 39 percent do that, because we can learn from those minority practices as well as from the majority practices. It's a tool we can't ignore from an incentive plan design perspective because of the alignment advantage. But it's also not an answer to having the right goals to drive long-term value creation.