SHEIN

A Corporate Governance Report

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1 Introduction: *Contextualizing SHEIN's Situation*

SHEIN is an Asian fast-fashion e-retailer. Since founded in 2008 in China by Yangtian Xu and 3 co-founders, the company has grown to becoming the 2nd largest shopping app in the US in 2022 (Statista: SHEIN, 2023), while having customers in more than 150 countries. The company is a private company, and it is characterized by a lack of transparency, with ownership, financial & company information being held as secret as possible for the public. However, in an internal "management report" seen by Financial Times, SHEIN reported revenue of $22.7bn in 2022 (Appendix 1). The company aspires to go public in the US this year, but it has met persistence due to allegations of using forced labor (McLymore, 2023). Despite being founded in China, SHEIN has decided to establish the Singapore-registered Roadget Business Pte. Ltd., referred to as 'Roadget', as the legal entity with rights to operate SHEIN's global website (Lin, 2022), making SHEIN a Singapore-registered firm. This action was taken, as new tougher rules for Chinese firms going public offshore complicated SHEIN's desired IPO in the US (Lin, 2022). The purpose of this paper is to analyze the overarching corporate governance issues that SHEIN are facing, to recommend solutions enabling SHEIN to realize the IPO.

2 Ownership Structure: *Founders & Investors*

The ultimate owner of Roadget, meaning SHEIN, is "Beauty of Fashion Investment Co. Ltd." holding a minimum of 50.01% stake, while the remaining owners are General Atlantic (growth equity firm), Tiger Global (investment firm), Sequoia Capital (venture capitalists) and Mubadala (sovereign wealth fund, UAE) (Appendix 2). Bloomberg has estimated that CEO & founder Yangtian Xu owns 34%, and that other shares are split with the 3 co-founders, Xiaoqing Gu, Miao Miao & Xiaoqing Ren, who each estimated holds a 7.6% stake, so combined the 4 founders owns 56.8% of the shares, assumingly owned through Beauty of Fashion Investment (Appendix 2).

The remaining 43.2% are owned dispersed by the other investors (Appendix 2), and the owner identities can be categorized as passive institutional investors. Firstly, because diversified portfolios make it difficult for the investors to monitor all portfolio companies, but also due to their fiduciary duty to maximize the value for their beneficiaries, hence avoiding monitoring costs (Thomsen & Conyon, 2019). General Atlantic, Tiger Global and Sequoia Capital could be active in their monitoring, due to the identity of the firms being growth equity, investment firm, and VC, but as the board structure section will reveal, they do not have board seats. Moreover, there's been no public indication that they monitor SHEIN through shareholder activism. Sovereign wealth funds as Mubadala are typically passive. We assume that this 43.2% group of owners all have the goal of profit-maximizing, securing returns to their beneficiaries, hence they have an owner-oriented view.

SHEIN has concentrated ownership (La Porta et. al, 1999) with CEO & Founder Yangtian Xu being the majority shareholder. Hence, his higher equity stake removes the free-rider and collective action problem, as his stake is expected to incentivize him to monitor, reducing type I agency problem (Jensen & Meckling, 1976). This concentrated ownership however also increases the risk of private benefits (Gilson & Gordon, 2003).

As Xu has founded the company, one could assume he would have a firm-oriented view, focusing on the survival of the firm. Hence, as there's concentrated ownership, type II agency problems can occur, if interest are misaligned between majority and minority shareholders (Jensen & Meckling, 1976). However, that does not seem to be the case with SHEIN, as it appears that all shareholders have been quite focused on growth and financial maximization, despite founders perhaps also caring about firm survival.

3 Board Structure: *Non-Independent Board*

The board of SHEIN consists of 4 directors, the 4 co-founders of SHEIN, with the CEO being chairman (Appendix 3), so it's a one-tier board with CEO-duality. This board structure reduces information asymmetries between agents and principals (Palepu, 2000), which therefore decreases the need of monitoring, hence decreases agency costs and agency problem I (Jensen & Meckling, 1976). Moreover, 2 of the founders are women (SHEIN, 2022), meaning that 50% of the board members are female. This is also positive, as women are proved to be tougher monitors than men (Adams & Ferreira, 2009), as well as a diverse board improves firm performance (Cucinelli, 2013). However, there's also multiple disadvantages with SHEIN's board structure. Due to the CEO-duality and the fact that all directors are founders, all directors are not independent. This is not optimal, as independent directors are more objective monitors (Gordon, 2007). Moreover, groupthink is more likely to occur with dependent directors, as they are likely to prefer group consensus more than presenting alternatives or critique, and this can result in poor decisions (Janis, 1972). Also, the minority shareholders' interests might be neglected, as every single board member is also a significant shareholder & founder. Therefore, despite low levels of information asymmetry and high degree of gender diversity, the board structure is not optimal, with power concentration on few individuals and only non-independent, non-objective directors, possibly resulting in wrong decision-making.

4 Stakeholder Issues: *Working Conditions, Pollution & Chemicals*

The wrong decision-making might have affected SHEIN. Despite the great financial success of SHEIN, the company has faced criticism in the media, due to the company's negative effects on its stakeholders (de Ferrer, 2022).

Firstly, tests conducted for Bloomberg ties SHEIN's clothing to the Chinese Xinjiang area (Bloomberg, 2022), an area where the UN has confirmed that forced labor has taken place (Pollard, 2022). Moreover, investigations have shown that workers of suppliers for SHEIN work under questionable conditions, with only one day off per month, working 75-hours per week, violating the local labour laws of China (Jones, 2021). Multiple SHEIN customers have received products with concerning "Help me"-signs from the production (Appendix 4). Hence, it appears that the high growth and great returns to shareholders of SHEIN has come with a cost for stakeholders, the workers in the company's supply chain. So, there's a type III agency problem, as stakeholders, the workers, suffer due to the profit-maximization (Jensen & Meckling, 1976). President Biden signed an act in 2021 (Uyghur Forced Labor Prevention Act, 2022), banning goods produced in the discussed area from entering the US. Moreover, U.S. lawmakers are trying to convince SEC to block SHEIN's IPO, until SHEIN has proven that is does not produce in the area (McLymore, 2023). Therefore, this is critical for SHEIN, as the US is one of its biggest markets, and the company aspires to IPO in the US. However, moving production facilities would create a new type III agency problem, as it would possibly mean that the workers of the suppliers might get fired, which could be worse than having a job with bad conditions. SHEIN is therefore in a dilemma, but it must move its production to be able to sell its goods in the US, stop the negative political/media attention, and realize the US IPO.

In addition, other stakeholders have suffered while SHEIN has profited: the environment & human health. SHEIN's own ESG report outline that the company's fossil fuel combustion grew with 3864% from 2021 to 2022 alone, polluting 991 tonnes of CO_2 (SHEIN, 2022). Moreover, tests show that SHEIN's clothing include chemicals of concerning levels breaking

EU regulatory limits (Greenpeace International, 2022), putting SHEIN's customers' health in danger. So, while SHEIN has seen tremendous growth, it has polluted and negatively affected the environment, as well as the customers health has been put in danger, so there's a type III agency problem (Jensen & Meckling, 1976). This has resulted in a lot of negative media attention, and people protesting against SHEIN (Appendix 4). Because of that, SHEIN hired a Head of ESG in 2021, Adam Whinston, to improve its ESG efforts (SHEIN, 2023). Winston has presented new sustainability initiatives, and a goal for SHEIN of reducing its emission by 25% in 2030 (SHEIN, 2022) So, the firm is trying to improve on its ESG efforts.

The above-mentioned type III problems can have consequences for SHEIN if the firm is not reacting appropriately, as the negative media attention can evolve into a negative brand image and a corporate scandal, which has proved to correlate with worse shareholder value (Zhang, et al., 2019). Therefore, even though it might be costly in the short run and will work against the interest of owner-oriented shareholders, the most profitable in the long run is to take responsibility for the problems: pollute less, secure safe working conditions and fewer chemicals in products, to avoid the scandal, hence avoid loss of profits. The valuation of SHEIN has taken a major hit recently (Cao, 2023), and the stakeholder issues could be one of the reasons, confirming the need of action. Hence, media and reputation are in this case informal control enhancing mechanisms that effects the governance of SHEIN into improving its ESG for the sake of shareholders, as the only social responsibility of the firm is to maximize profits (Friedman, 1970), but it also benefits other stakeholders (Thomsen & Conyon, 2019).

5 Recommendations: *Improvements to Prepare for the IPO*

Having addressed the firm structure, and type III agency problems, improvements to prepare for the IPO will be suggested.

Firstly, the firm would benefit from a more objective board, so investors can feel confident that their interest are considered. Therefore, SHEIN should expand its board, and the new members should be independent directors. Independent directors will also positively affect market liquidity and price efficiency of the potential stock (Aspris & Frino, 2014), which is attractive for shareholders of the stock when going public. Moreover, SHEIN could create board committees as that can add value to boards (Thomsen & Conyon, 2019), and perhaps someone else than the CEO should be the chairman, to secure objective, effective monitoring.

Secondly, SHEIN must continue to improve its ESG efforts and focus on the triple bottom line. Initially, to cope with the type III agency problems, and to avoid reputational damage and political resistance of the IPO. Moreover, a study by NYU Stern's center for Sustainable Business finds a positive relation between ESG efforts and stock performance (Whelan et al., 2020), hence improving on ESG will be beneficial for shareholders of SHEIN. Moreover, investor activism, not investing in non-ESG is a growing phenomenon (Berg et al., 2021).

Lastly, SHEIN should become more transparent with company information, as that will be required once the firm goes public. As an example, the U.S. Securities and Exchange Commission (SEC) requires both annual and quarterly reports for listed firms (SEC.gov). Hence, SHEIN might as well start working on its transparency now to prepare for the IPO, also to build investor confidence for future shareholders.

6 References

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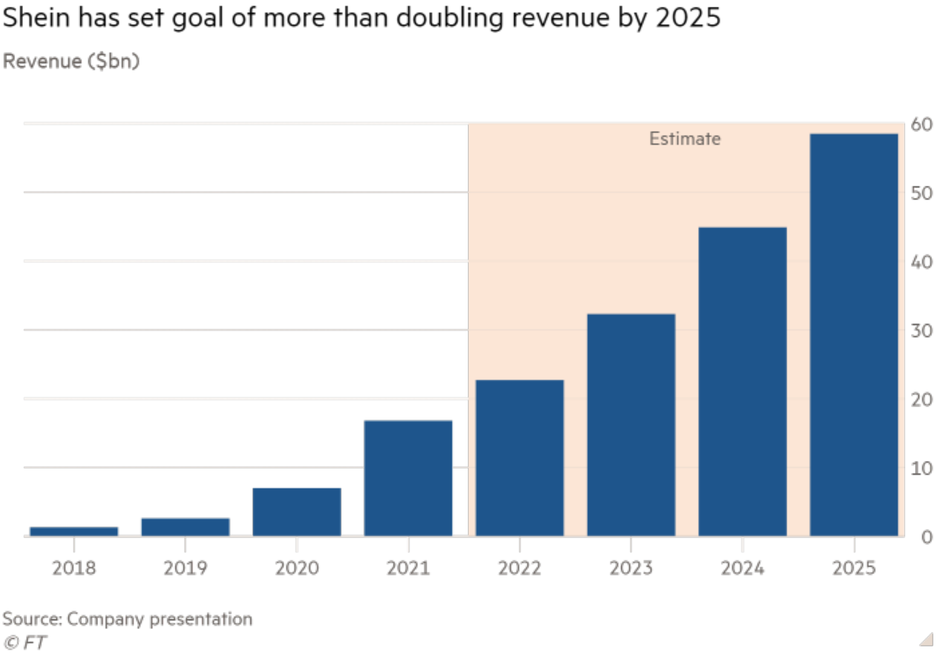
7 Appendices

Appendix 1 - Revenue Data

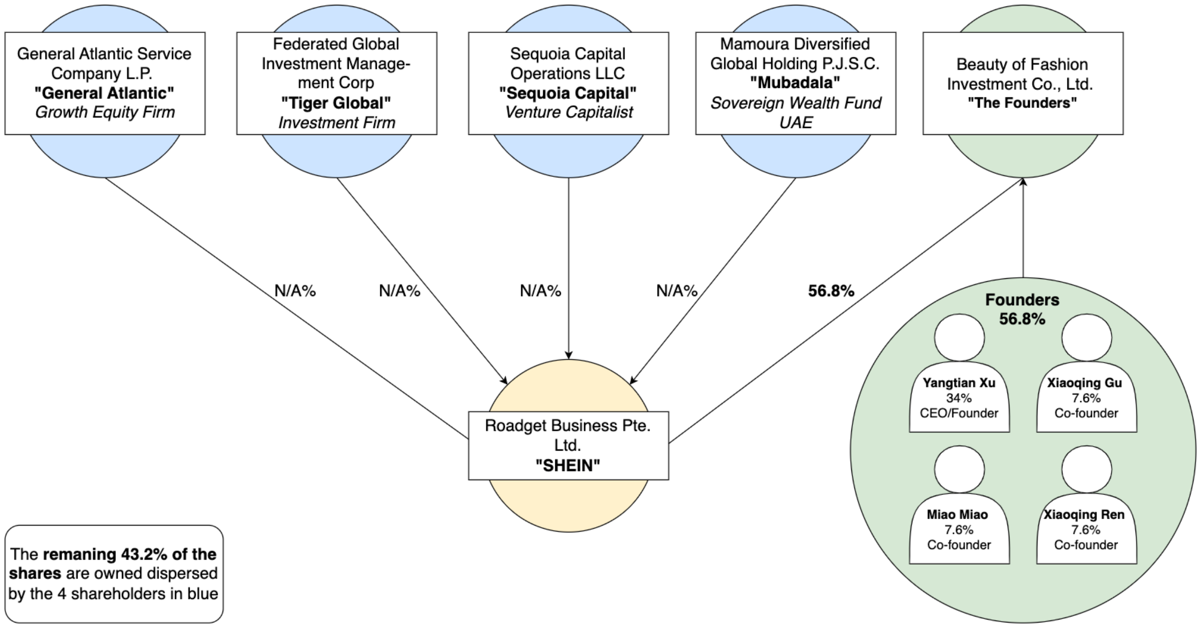


SHEIN had revenue of $22.7bn in 2022, and the growth is expected to continue, with the revenue almost reaching $60bn in 2030.

Source:

Financial Times. (2023, February 17). Shein gives investors lofty revenue projections as it prepares for IPO. *Financial Times*. https://www.ft.com/content/9709f1b8-a8b8-4210-bdd8-784a3025758d

Appendix 2 - Ownership Structure



Above appears a visualization of the ownership structure, created by the author to visualize and give an overview.

It is based on the following sources:

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Appendix 3 - Board Structure

The board of directors, the 4 founders:

XIAOQING GU
Director (since 22/11/2019)

MS MIAO, MIAO
Director (since 22/11/2019)

MR XIAOQING REN
Director (since 22/11/2019)

MR YANGTIAN XU
Director (since 22/11/2019)

Source:

ROADGET BUSINESS PTE. LTD. (n.d.). Orbis | Bureau van Dijk. Retrieved June 12, 2023, from https://orbis-r1-bvdinfo-com.esc-web.lib.cbs.dk/version-20230324-3-3/Orbis/1/Companies/Report

Chairman of the board is CEO & founder Yangtian "Sky" Xu:

Disclosure	Notes
GRI 1: Foundation	
Statement of use	SHEIN has reported with reference to GRI Standards from the period January 1 2022 to December 31 2022
GRI 1 used	GRI 1: Foundation 2021

Disclosure	Pages in ESG report 2022	External assurance	Notes and clarifications
GRI 2: General Disclosure			
2-1: Organizational details	p. 8 & 9	No	SHEIN is headquartered in Singapore.
2-3: Reporting period, frequency and contact points	p. 82	No	SHEIN publishes annual ESG reports.
2-11: Chair of the highest governing body	p. 67	No	Sky Xu, SHEIN's CEO is the chair of the highest governing body

Source:

Shein GRI Index Report 2022. (2022). In *https://sheingroup.com/esg-reports/.* SHEIN.

Appendix 4 - "Help me"-signs in SHEIN products + Protestors Against SHEIN