The Business Case for Diversity on Corporate Boards

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Sources

Catalyst, Women CEOs of the Fortune 1000 (January 15, 2014) and additional Catalyst research and analysis.

FORTUNE 250 Companies in 2013

Board Composition:

• 84.4% white
• 81.5% male
• 68% older than 60

• The most recent appointees are more diverse: 22.4% female and 16.8% nonwhite

Russell Reynolds Associates 2014
Boards with least one Director who is...

![Bar chart showing proportions of boards with directors based on gender and minority status.](chart.png)

Russell Reynolds Associates 2014
Minority representation on Boards is mirrored in the C-suite

Russell Reynolds Associates 2014
So why does this matter?

Historically, arguments have focused on social justice.

However, “boosting the number of women lags behind other priorities when viewed as a social good, as opposed to an economic necessity”

Kate Taylor, *Forbes* 6/26/2012
So why does this matter?

The glib answer is that we ignore talent if we only recruit from the pool of white males.

Deeper answers derive from the fundamental fact that each of us brings a unique perspective to the table.
Why is diversity important?

Scott E. Page

Page illustrates his theorem that *diversity trumps ability*:

Groups that include people with lesser abilities but different points of view will out-perform groups with smarter individuals who think alike.
Scott Page insight

Value

variables
Three individuals with similar viewpoints

Value

variables
Three individuals with different viewpoints

Value

variables
Crowdsourcing

1906 country fair in Plymouth: what is the weight of an ox?
Crowdsourcing

787 people took guesses, which varied by more then 20%

Average guess: 1197 pounds

Surowiecki, 2004. *The Wisdom of the Crowd*
Crowdsourcing

787 people took guesses, which varied by more than 20%

Average guess: 1197 pounds
Real weight: 1198 pounds

Surowiecki, 2004. The Wisdom of the Crowd
Who wants to be a millionaire?

Lifelines:
- call a friend
- ask the audience
Who wants to be a millionaire?

Lifelines:
- call a friend: 2/3 correct
- ask the audience: 90% correct
Scott Page again

“The squared error of the collective prediction equals the average squared error minus the predictive diversity”

Translation: when the diversity of the group is high, the collective prediction is closer to the actual value
Collective intelligence

- Individuals were measured for their intelligence via a battery of tests.
- A subgroup was asked to solve a problem on their own. Individual success was strongly correlated with individual intelligence.

Woolley et al, 2010 Science 330: 686
Collective intelligence

• Individuals were measured for their intelligence via a battery of tests
• A subgroup was asked to solve a problem on their own. Individual success was strongly correlated with individual intelligence
• Small groups were asked to solve the same problem collectively
• Group success was completely unrelated to average intelligence of members or highest intelligence within the group

Woolley et al, 2010 Science 330: 686
Collective intelligence

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Researchers were surprised that it was *not* related to

• Group cohesion
• Group motivation
• Group satisfaction

Woolley et al, 2010 Science 330: 686
Collective intelligence

Factor $c$, collective intelligence, was a function of
• Social sensitivity among group members
•Extent to which all group members spoke in the exercise
• Proportion of females in the group

Woolley et al, 2010 Science 330: 686
So what does any of this have to do with business?
McKinsey Organizational Health Index
McKinsey Organizational Health Index

Probability of achieving above-median financial performance (based on EBITDA/sales) Percent

- Top 25%: 68
- Middle 50%: 48
- Bottom 25%: 31

Level based on OHI score

More than twice as likely to outperform peers
Companies with 3 or more women in top positions scored higher than peers

Companies in the top quartile of women representation on executive committees relative to those with no women at the top

• reap a 47% higher return on equity
• earn 55% more before interest and tax
More data from Catalyst:

Companies in the top quartile of women’s representations on the board experienced a 26% higher return on invested capital than those with no women.
Let’s unpack this a bit

Credit Suisse 2012
2360 companies across the world
The good news

Across all work sectors and geographic regions, women’s participation on corporate boards has increased from 2005 – 2011

Even so, IT lags other sectors and Europe leads other regions
What about profits?

• Credit Suisse studied global companies across regions and sectors, dividing them into small cap and large cap

• Compared share price performance from Dec 2005 to Dec 2011 (*spanning the recession*)
Share price performance

• From Dec 2005 to July 2007, the relative share price for both large and small cap companies was slightly higher in companies with no women on the board.

• From Aug 2007 through December 2011, companies with women on the board did much better.
Relative performance of companies with women on the Board

*Relative share price performance of all companies (with market cap > USD 10 bn)*

Source: Thomson Reuters, Credit Suisse

*Performance of stocks with some female board representation divided by the performance of stocks with no women on the board, where all stocks have market capitalization greater than USD 10 bn.

*26% outperformance over 6 years*

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*Relative share price performance of all companies (with market cap < USD 10 bn)*

Source: Thomson Reuters, Credit Suisse

*Performance of stocks with some female board representation divided by the performance of stocks with no women on the board, where all stocks have market capitalization less than USD 10 bn.

*17% outperformance over 6 years*
The bottom line

**ROE: 0 vs. 1 or more women on the board**

*Source: Credit Suisse*

![Graph showing percentage of ROE with 0 vs. 1 or more women on the board from 2005 to 2011. The graph shows a fluctuation in percentages with a notable increase from 16% to 12% from 2010 to 2011.]
How might you explain this effect?
What is driving this difference?

• Better companies are more inclusive companies
• A more diverse group arrives at better outcomes
• Including women brings different leadership skills
• They tap deeper pools of talent
What is driving this difference?

• Including women brings companies closer to their consumer base
• Corporate governance is better
• Risk-taking behavior is reduced
Quotas for women on boards

- Norway
- Spain
- France
- Italy
- Iceland
- Belgium
- The Netherlands
- Malaysia
- Germany (2 months ago): target of 30% by 2016
Supervisory-board directors

Big publicly listed companies’, % female

- **Norway**: 2009: ~0%, 2012: ~20%, Target: 40%
- **Sweden**: 2009: ~10%, 2012: ~20%, Target: 40%
- **France**: 2009: ~10%, 2012: ~15%, Target: 40%
- **Britain**: 2009: ~10%, 2012: ~15%, Target: 40%
- **Netherlands**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Denmark**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Switzerland**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Belgium**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Poland**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Spain**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Germany**: 2009: ~5%, 2012: ~10%, Target: 40%
- **Italy**: 2009: ~5%, 2012: ~10%, Target: 40%

Source: Russell Reynolds Associates

*40% quota since 2008*
What happened in Norway?

- Few large corporations and only 414 publicly traded companies
- Government involvement in corporate structure
- Board members are elected by employees
- Egalitarian society: father parental leave is now 12 weeks, and maternal leave up to 47 weeks
• In Norway, all government boards and committees must have at least 40% women and 40% men

• In 2002, Minister of Trade and Industry Ansgat Gabrielsen decided *unilaterally* to mandate 40% women on corporate boards
  – Deadline of 1 January 2008
  – Noncompliance would result in either closure or delisting from the Oslo Stock Exchange
Business leaders, media, investors and many women described the new regulation:

“Women will be second-class board members”

“We cannot find qualified women”

“Women are not interested in board work”
But
1) the government supported its Minister
2) “Golden Skirts”, a parallel to WELD, was quickly set up by women in business
3) By the January 1, 2008 deadline all companies were in compliance
In 2010 company executives said

Achieving gender parity was actually not difficult
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Achieving gender parity was actually not difficult and it

Increased pre-meeting preparation of members
Added to quality of discussions
Created a less competitive atmosphere
Led to more informed decision-making
And women sit on multiple boards

![Bar chart showing the number of individuals by gender and the number of board seats occupied. Men and women are compared for 2, 3, 4, and 5 or more board seats.](chart.png)
But there is still work to be done

• Only 3% of women board members are board chairs, while 32% of the men are chairs

• Employee representatives are 2x more often male than female

• The women board members are younger: they have replaced the young men, not the old boys
A different approach: the UK

• rejects quotas altogether
• Instituted an annual review of FTSE 100 boards
• The Davies report, first offered in 2011, gives data every year on makeup of corporate boards
• In 2011, they set a target of 25% by 2015
The Davies report 2014
In 2011, 21% of the FTSE Board were all male
In 2011, 21% of the FTSE Board were all male
The FTSE 250

• Progress has been made, but the data are not as encouraging
  – Currently 15.8% women
  – 19% have all-male boards and 22% have only one woman

• The Davies report names names and makes recommendations for future progress
What about here?

Lots of verbiage about the issue

• The SEC in 2009 requires corporations to report on how they consider diversity in their nominating committees — but allows companies to define diversity

• Committee for Economic Development report (2012) makes recommendations but sets no goals
Some efforts

• Thirty Percent Coalition Goal: 30% by 2015
• 2020 Women on Boards Goal: 20% by 2020
Some efforts

• Thirty Percent Coalition **Goal: 30% by 2015**
• 2020 Women on Boards **Goal: 20% by 2020**
• The Alliance for Board Diversity tracks progress by gender and ethnicity. Four organizations, including Catalyst, Executive Leadership Council, Hispanic Association on Corporate Responsibility, and Leadership Education for Asian Pacifics
Thanks for your interest!
Any questions?