BOARD BRIEF:
Why Gender Diversity Matters

Diversity in leadership and openness to new perspectives is crucial for charting the course in business. Without more than symbolic representation, we risk going backward instead of forward.[1]

Dina Dublon
Member of the boards of Microsoft, Accenture and PepsiCo.

This guide presents current research outlining how companies are stronger, better-positioned to tackle external and internal challenges and more focused on the bottom line when their boards embrace gender diversity.

A. The diverse group almost always outperforms a homogenous (and potentially more capable group) by a substantial margin.

B. There is a strong business case for diversity – gender diverse leadership gives businesses a distinct competitive advantage that translates directly to the bottom line.

C. Organizations that focus on diversity experience improved talent retention and corporate image.

A number of propositions exist for the business case for diversity on boards:[2]

- ❐ Diverse boards tend to be more independent and, with fewer ties to management, can have a greater ability to **monitor** managers objectively.
- ❐ Diversity improves board **decision making** as a result of unique perspectives, increased creativity, and non-traditional innovative approaches.
- ❐ Diversity improves **information** provided by the board to managers due to special skill sets, experience and complementary knowledge held by diverse directors.
- ❐ Diverse directors provide **access** to important constituencies and resources in the external environment.
- ❐ Board diversity sends important **positive signals** to the labor, product and financial markets.
- ❐ Board diversity provides **legitimacy** to the corporation to both external and internal constituencies.

A. The diverse group almost always outperforms a homogenous (and potentially more capable group) by a substantial margin.

- In a recent report by Ernst and Young, researchers demonstrated that groups with greater diversity tend to perform better than homogeneous ones, even if the members of the homogeneous groups are more capable. In fact, the diversity of the group's members matters as much as their ability and brainpower, if not more. Their conclusion: "The diverse group almost always **outperforms** the group of the best by a substantial margin."[3]
- Further, research on group behavior demonstrates that diverse groups, when properly managed, make more **innovative business decisions** than non-diverse groups.[4]
- A recent study conducted by researchers at Carnegie Mellon to measure the "**collective intelligence**" of a small group of people found that, all else being equal, teams with more women scored higher than teams with fewer women. What distinguishes high-IQ teams from lower-IQ teams includes factors such as the proportion of women, an individual's social perception abilities, the group's ability to take turns contributing rather than be dominated by a single member and the IQ of individual team members.[5]

B. There is a strong business case for diversity – having women at the top give businesses a distinct competitive advantage that translates directly to the bottom line.

> The business case suggests that women directors will increase profitability and shareholder returns. Women deserve a fair chance to serve on boards.
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> Professor Betty Simkins
> Williams Companies Professor of Business & Professor of Finance
> Oklahoma State University

- McKinsey & Company research on the relationship between organization and financial performance and on the number of women managers at companies suggests that companies with higher numbers of women at senior levels are also companies with **better organizational and financial performance**.[6] Specifically, this research showed that companies around the world with the highest scores on nine important dimensions of organization—from leadership and direction to accountability and motivation—are likely to have **higher operating margins** and **market capitalization** than their lower-ranked counterparts.[7,8] Secondly, among the companies for which information on the gender of senior managers was available,[9] those with three or more women on their senior management teams scored higher on all nine organizational criteria than did companies with no senior level women.[10] It is also notable that performance increases significantly once a **critical mass** is attained; namely, at least three women on management committees for an average membership of 10 people. Below this threshold, no significant difference in company performance is observed.
- Another study conducted jointly between McKinsey & Company and the Amazone Euro Fund analyzed the financial performance, relative to the average for their sector, of 89 European listed companies (with a stock market capitalization of over €150 million) with the highest level of gender diversity in top management posts.[11] There is no doubt that, on average, the companies in the study **outperformed** their sector in terms of **return on equity** (11.4% vs. an average of 10.3%), **operating result** (EBIT of 11.1% vs. 5.8%), and **stock price growth** (64% vs. 47% over the period 2005-2007). This study and others show that companies with a higher proportion of women on their management committees are also the companies that have the **best performance**.

- Research by professors at the business schools of Columbia University and the University of Maryland also supports these findings. Using data on 1,500 U.S. companies from 1992 to 2006, results of another study demonstrate "strong positive association between Tobin's Q,[12] **return on assets** and **return on equity** on the one hand and the [female top management] participation rate on the other."[13] The authors add that they found "at least indicative evidence that greater female representation in senior management positions leads to—and is not merely a result of—**better firm quality and performance**.

- Michel Ferrary (CERAM Business School, France) has also found a **direct correlation** between the proportion of women in top management at a corporation and its **stock price** during a time of general economic downturn.[14] He found that, "[t]he more women there were in a company's management, the less the share price fell in 2008." Ferrary suggests that women managers tend to **balance** the risk-taking style of their male colleagues, a trait especially important in **protecting profits** in bad times.[15]

> Feminization of management seems to be a protection against financial crisis. Currently, financial markets value firms that take less risk and are doing more stable business.
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> Michel Ferrary
> Professor of Management
> SKEMA Business School (France)

- Two separate Catalyst studies have explored the link between gender diversity at the top (on both boards and in senior management) and company financial performance in Fortune 500 companies with some of the following findings:[16]
  - In one study, a group of companies were divided into quartiles based on the percentage of women on their boards and their **performance** compared on the basis of return on equity, return on sales and return on invested capital. Across five of the seven industries studied, the analysis revealed that "top-quartile" companies **outperformed** "bottom-quartile" companies on all three **financial indicators** by 42% to 66%.
  - In the other study, the group of companies with the highest representation of women on their top management teams experienced **better financial performance** than the group of companies with the lowest women's representation. This finding holds for both financial measures analyzed: **Return on Equity**, which was 35.1% higher and **Total Return to Shareholders**, which was 34% higher. Financial performance was also consistent across five industries analyzed[17] in that the group of companies with the highest women's representation on their top management teams experienced a higher ROE than companies with the lowest women's representation.

C. Organizations that focus on diversity experience improved talent retention and corporate image.

- **Attract and retain talent.** The business case for diversity asserts that companies that recruit, retain and advance women will benefit for a number of reasons. Ultimately, companies that have diversity and manage it properly make better decisions, produce superior products and retain several key business advantages over more homogenous companies.[18] Further, as one study has shown, there is a direct and positive correlation between the percentage of women board directors in the past and the percentage of women corporate officers (as well as other line positions) in a company in the future. Put simply, companies with more women on their boards

> So, let's for the moment forget all the talk about the "China Century" or the "India Century" or the "BRIC Century." The real story is that the 21st century is going to be the "Women's Century." As the world desperately looks for ways to restart and reset the global economy, the solution lies right in front of us. In the words of World Bank President Robert Zoellick, gender equality is simply "smart economics".
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> Muhtar Kent
> Chairman of the Board and Chief Executive Officer
> The Coca-Cola Company

five years later also had more women in senior leadership, especially in P&L roles.[19] And besides helping companies to fill shortfalls of talent, gender diversity can allow them to attract and retain it and meet other business goals. One European Commission study showed that 58% of companies with diversity programs reported higher productivity as a result of improved employee motivation and efficiency, and 62% said that the programs helped attract and retain highly talented people.

- **An asset for corporate image.** Gender diversity is an asset for corporate image and helps bring a company, its employees, shareholders and customers closer together.[20] The aforementioned European Commission study found that diversity programmes not only had a positive impact on employee motivation but also noted an increase in customer satisfaction (57%) and an improvement in brand image (69%).[21] Another study has found gender diversity of boards to be one indicator of corporate trust, which in turn, is an essential element of reputation and brand value.[22] It is also clear that capital markets and investors are paying greater attention to gender diversity as a driver of corporate performance. Investment funds such as Calpers and Amazone (Europe) now include this indicator among their investment criteria, while rating agencies (Core Rating, Innovest, Vigeo) and private initiatives (The Gender Equality Project) are developing tools to measure gender diversity.

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[1] Quoted from The White House Project, "The White House Project: Benchmarking Women's Leadership" (2009).
[2] Adapted from David A. Carter, Frank P. D'Souza, Betty J. Simkins and Gary W. Simpson, "The Diversity of Corporate Board Committees and Financial Performance" (March 1, 2008). Available at: http://www.fma.org/Prague/Papers/TheDiversityofCorporateBoardCommittees1-28-2008_UNC_.pdf.
[3] Ernst and Young, "Groundbreakers Study, Diversity an Equation for Success" (2009), http://www.ey.com/GL/en/Issues/Driving-growth/Groundbreakers---Diversity--an-equation-for-success.
[4] Catalyst, "The Bottom Line: Connecting Corporate Performance and Gender Diversity" (New York: Catalyst, 2004) citing Karen A. Bantel and Susan E. Jackson, "Top Management and Innovation in Banking: Does the Composition of the Top Make a Difference?", *Strategic Management Journal*, Vol. 10 (1989): 107-124; and Anne S. Tsui and Barbara A. Gutek, *Demographic Differences in Organizations: Current Research and Future Directions* (Lanham, MD: Lexington Books, 1999).
[5] Anita Williams Woolley, Christopher F. Chabris, Alex Pentland, Nada Hashmi and Thomas W. Malone, "Evidence for a Collective Intelligence Factor in the Performance of Human Groups", *Science* Express (30 September 2010), http://www.sciencemag.org/cgi/content/abstract/science.1193147.
[6] McKinsey & Company, "Women Matter: Gender Diversity, A Corporate Performance Driver" (2007). Note that although the analysis did not show a causal link, this research clearly argues for greater gender diversity among corporate leaders.
[7] Georges Desvaux, Sandra Devillard-Hoellinger and Mary C. Meaney (McKinsey & Company), "A Business Case for Women", *The McKinsey Quarterly* (September 2008). The analysis derived from a survey of 115,000 employees at 231 private and public companies around the world. The nine dimensions of organizations are leadership, direction, accountability, coordination and control, innovation, external orientation, capability, motivation, work environment and values.
[8] McKinsey & Company, "Women Matter: Gender Diversity, A Corporate Performance Driver" (2007).
[9] Information was available for 101 of the companies, which allowed McKinsey & Company to analyze 58,240 employee evaluations.
[10] In addition to undertaking these analyses, McKinsey & Company joined with the Amazone Euro Fund to conduct a study on the financial performance of the 89 European public companies with the greatest gender diversity in top posts. They found that, on average, these companies outperform their sectors in returns on equity, operating results and stock price growth. The full study, *Women Matter*, can be found on www.mckinsey.com/locations/paris/home/womenmatter.asp.
[11] McKinsey & Company, "Women Matter: Gender Diversity, A Corporate Performance Driver" (2007). Companies were selected on the basis of the following criteria: the number and proportion of women on the executive committee, their function (a CEO or CFO having greater weight in corporate decisions than a Communications Manager) and, to a lesser extent, the presence of more than two women on the board, statistics on gender diversity in the annual report.
[12] A standard measure of corporate value: the market value of a company divided by the replacement value of its assets.
[13] Cristian L. Deszō and David Gaddis Ross, "'Girl Power': Female Participation in Top Management and Firm Performance", Working Paper (December 2007).
[14] Michel Ferrary, "Global Financial Crisis: Are Women the Antidote?", CERAM Research (October 2008).
[15] Michel Ferrary, "Why Women Managers Thrive in a Down Turn." Financial Times (March 2009), http://www.ft.com/cms/s/0/27836d74-04e4-11de-8166-000077b07658,dwp_uuid=1d22aad4-0732-11de-9294-000077b07658.html; Michel Ferrary, "When Gender Diversity Protects Stock Prices From the Crash," Ceram Business School (2009).
[16] Catalyst, "The Bottom Line: Corporate Performance and Women's Representation on Boards" (New York: Catalyst, 2007), http://www.catalyst.org/publication/200/the-bottom-line-corporate-performance-and-womens-representation-on-boards ; Catalyst, "The Bottom Line: Connecting Corporate Performance and Gender Diversity" (New York: Catalyst, 2004), http://catalyst.org/files/full/financialperformancereport.pdf.
[17] The five industries analyzed in the study were Consumer Discretionary, Consumer Staples, Financials, Industrials and Informational Technology/Telecommunication Services.
[18] Catalyst, "The Bottom Line: Connecting Corporate Performance and Gender Diversity" (New York: Catalyst, 2004), http://catalyst.org/files/full/financialperformancereport.pdf.
[19] Lois Joy (Catalyst), "Advancing Women Leaders: The Connection Between Women Board Directors and Women Corporate Officers" (New York: Catalyst, 2008), http://www.catalyst.org/publication/273/advancing-women-leaders-the-connection-between-women-board-directors-and-women-corporate-officers.
[20] McKinsey & Company, "Women Matter: Gender Diversity, A Corporate Performance Driver" (2007).
[21] *Ibid.*, citing "Cost and Effectiveness of Diversity", European Commission, 2003.
[22] Joan MacLeod Heminway, "Sex, Trust, and Corporate Boards," Hastings Women's Law Journal (April 15, 2007).