Valuing Diversity

By **Deborah Gilshan,** Founder, **The 100% Club**

"The reality is that there is a power in the status quo that motivates the desire for "proof" of the business case for diversity - we all see homogeneity as the norm, which perhaps gives it more power than it deserves."

Professor Katherine Phillips

There has been significant focus on finding evidence that diversity is beneficial. But why is such proof necessary? Does it change why we value diversity? Is the search for it hindering progress? Does it risk reinforcing the status quo? Does it strengthen the idea that some people belong and others have to prove that they do?

I am not the first to raise these issues but they are at the core of the debate about diversity and inclusion. How can we reframe the value proposition of diversity to accelerate systemic change?

Diversity and Investor Stewardship

Having been involved in diversity advocacy since 2011, the pace of change in the past two years, and the evolving expectations on companies, investors and society, has been unparalleled. The urgency for this change has been fuelled by the Covid-19 pandemic and racial injustices that have amplified existing systemic inequalities which were already being exposed through movements such as #MeToo.

This coincides with significant shifts in finance, including a recognition that companies are accountable to a wider set of stakeholders. All types of stakeholders are making their voices heard on social justice.

There are also heightened expectations for more assertive stewardship exercised by investors and other providers of capital, using their full range of ownership rights. This is being demanded by savers and pension funds as well as regulators, NGOs and many other actors across the investment chain.

The expectations for progress in all of these areas in 2022 and beyond are high. The diversity agenda continues to increase, and at pace. The role of investors remains critical to progress and has the power to be transformational. But it needs to deliver its full potential.

Diversity as a systemic opportunity

Inequalities as systemic risks positions diversity as part of the systemic solution. System level change is needed to realise the opportunity of diversity in creating a fairer and more equitable society. Part of that system level change is fully utilising investor capital, including more forceful stewardship interventions from investors in order to address systemic inequalities.

Reframing the value proposition of diversity

Generating system level change will not be easy. A good place to start is reframing the value proposition of diversity. Research from Citi Global Perspectives and Solutions in September 2020 estimated that not closing the racial inequalities gaps between black and white people has cost the US economy $16 trillion in the previous 20 years. On gender, the World Economic Forum 2021 Global Gender Gap report estimates that it will take 268 years to achieve economic gender parity. Rather than focusing on the reasons why social injustices should be addressed and diversity should be achieved, we should consider the social, economic, reputational and opportunity costs if they are not.

The investment case for social factors

Highlighting the investment case around social factors is also key. The social licence to operate of companies is now more critical than ever. Social factors are being recognised as sources of investment risk and return. Human capital management, diversity, equality and inclusion continue to heighten in investor focus.

Earlier this year, the UK's Department for Work and Pensions held a call for evidence on how UK occupational pension schemes manage social factor risks and opportunities in their investment portfolio. ICGN **responded** to the consultation, noting that: "diversity, and other ways to optimise human capital management, can be seen as an opportunity set within social factor integration into investment portfolios."

Diversity controversies, and related litigation and regulatory issues, are increasing. According to a March 2021 report from Kepler Cheuvreux, ethnicity and racial diversity are where least progress has been made but where sources of the most material investment risks are emerging. Kepler Cheuvreux also found that, from analysis of news flow from RepRisk, gender diversity controversies have increased sixfold in the period 2017-2021 compared to 2013-2016.

The connections between board diversity and governance should drive the integration of diversity into portfolio analysis. A holistic approach, incorporating all diversity considerations into both investment processes and stewardship activities, will be necessary in order to seize the opportunity that diversity represents.

Escalating stewardship on diversity

The increasing focus on the outcomes of stewardship should deliver more forceful interventions in managing social factors, including through escalation. Evidence of such escalation can be found in the 2021 annual meeting seasons in many markets, where diversity, racial equity and social injustices have featured prominently, alongside other long-term systemic issues such as climate change.

On racial equity, proposals at US companies have included requests for racial equity audits and racial pay gap disclosures amidst a heightened focus on board level accountability and diverse representation. Racial justice scorecards for companies are being created. Shareholder derivative lawsuits have been filed targeting the lack of racial board representation.

Shareholders are increasingly supporting resolutions related to diversity. A May 2021 report from As You Sow indicated that support for workforce diversity disclosure resolutions was at over 60% in 2021, a marked increase from prior years. It is significant that a higher number of diversity resolutions are being proposed and that there are increasing levels of support for these resolutions, demonstrating shifts in investor sentiment.

The systemic opportunity of diversity also necessitates a more collective approach by investors. Investor collaborations in the area of human capital and diversity include the Human Capital Management Coalition in the US, the 30% Club Investor Groups in the UK, France, Japan, Australia, Brazil and Canada, the 40:40 Vision initiative led by HESTA in Australia and the Workforce Disclosure Initiative in the UK. ICGN investors are often integral to these collective investor initiatives and many ICGN members have attested that diversity and inclusion are high priorities for their stewardship activities.

In addition, the role that investors play in holding companies to account on corporate spending in support of organisations which work against the rights of minorities will be critical.

How are companies responding?

Many companies have publicised their commitments to diversity. However, there is increasing pressure for companies to be authentic in their diversity commitments. They must move beyond platitudes, especially as market regulators and stock exchanges are now incorporating diversity expectations into listing standards.

Some companies are linking debt issuances to progress social justice. Diversity targets are increasingly being incorporated into pay structures. Chief Diversity Officers are being appointed at board level. Companies are linking diversity to strategic deliverables.

More diversity data is being requested at board level, in the C-suite and across the workforce. However, whilst data and transparency are key drivers of progress within companies, outcomes are now being measured in terms of impact, improving board structure and representation, and corporate culture. This is because the board is the outward face of the organisation and its collective skill set is under heightened scrutiny. How does a board ensure it oversees issues related to human, indigenous and civil rights?

2022 and beyond

Public scrutiny will only increase and the voices of stakeholders will get louder. Investor stewardship strategies on diversity, and how companies respond, will continue to be heavily scrutinised. All parties must deliver on their stated commitments to create truly inclusive cultures.

In accelerating more sustainable systemic change, we should not only applaud companies that have appointed diverse directors, but also challenge more strongly those who have not. Equally, instead of only championing shareholders who are using stewardship to advocate for change, we should shine the spotlight more brightly on those who are not doing so. Because the time to start acting has passed.

Deborah Gilshan is the Founder of The 100% Club, a networking alliance and advisory business on investment stewardship, ESG and diversity. She has 21 years of industry experience and has worked for two asset owners and an asset manager. Deborah is an Ambassador of the 30% Club and serves on the Advisory Panel of the UK's Financial Reporting Council. She is a member of ICGN's Nomination Committee and previously chaired ICGN's Ethics & Systemic Risk Committee. Deborah is the lead author of "The Ethics of Diversity" from the UK's Institute of Business Ethics. Some of the issues raised in this article are explored further in the report, which is available ***here.***