Investing for Inclusion
A Home Court Advantage

A 288% increase is significant by most standards. In this case, that metric represents viewership of the NCAA women's championship basketball game in 2024 compared to the viewership in 2022. Nearly 19 million people watched the final game, the most-watched basketball game of professional or college level since 2019. The star of NCAA women's basketball was Caitlin Clark, whose rise has continued as the overall first draft pick for the WNBA. Selected by the Indiana Fever, Clark's initial four-year contract secures her over $380,000, around $76,000 for her first year. Conversely, the 2023 NBA first draft pick, Victor Wembanyama, secured a four-year contract for over $55 million.

Sports, it turns out, imitates life. There are many factors – team budgets, league revenues, etc. – that contribute to the different salaries between these two star athletes, but gender pay gaps and other disparities are common both on and off the court. Just as viewership interest has spiked for women's sports (hopefully driving an increase in female players' salaries), investor interest in financial and investment opportunities to address gender and racial inequity has also grown. As of January 2024, there were $2.4 BN in assets managed (AUM) globally by funds with a gender- or diversity-related focus; this AUM has more than doubled from $1.1 BN in January 2019.

And, just as sports leagues have recently promised to address gender and racial inequities, public companies have also made commitments to address diversity, equity, and inclusion, both within their own workplaces and more broadly in society. Regulatory changes have also spurred companies to evaluate and address certain aspects of inclusion and representation within their walls, for example, the Nasdaq Board Diversity Rule, the European Union's underrepresented gender quota, and Canadian Business Corporations Act. Public companies that ignore the various requirements for gender and diversity disclosure face risks: delisting, fines, or other operational and financial penalties. Growing research supports that companies who avoid penalties and capture the opportunity to improve their gender and racial equity reap financial benefits and outperform peers, two aspects attractive to investors.

New Data from Key Industry Players

Blackrock recently published one of the largest studies ever performed on this topic.[1] The study focused on the relationship between female representation in the workforce and financial performance, and went a step further, examining how the findings can aid in the investment decision-making process. Ultimately, Blackrock researchers found a positive relationship between several diversity-oriented characteristics and financial success. These findings are consistent with a growing volume of research on diversity, equity, and inclusion aspects of financial performance; we will dive into a few throughout this article.

Gender-Balanced Workforces Over Male or Female Dominated

The outperformance of companies with gender-balanced workforces relative to those skewed in either extreme suggests that benefits stem not from the dominance of men over women or vice versa but from the diverse talents, experiences, and perspectives that can enhance a business' decision-making abilities. Blackrock found that companies with more balanced representation outperformed the highest and lowest women's representation quintiles in terms of average return on assets (ROA) over the past decade. Additionally, Morgan Stanley found that from 2011-2022, companies with greater diversity throughout all levels of the organization outperformed their less-diverse peers in terms of stock performance by 1.2% annually. However, achieving gender parity across the overall workforce is not enough; Blackrock's research specifies that companies closest to parity across key roles were more likely to outperform relative to companies where representation tilts one way or the other.

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Higher Female Representation in Senior Positions

Shifting focus up the corporate ladder, Blackrock's study indicated near gender-parity in entry-level positions but noted a marked decline in female representation as position seniority rises. Specifically, female representation declines from 49% in entry-level positions to 33% in middle management, 29% in senior management, and 18% in executive roles. The data show that companies improving gender balance throughout the chain of command are being rewarded: companies with executive teams in the top quartile for gender diversity were 25% more likely to achieve above-average profitability compared to those in the lowest quartile. Further, companies with female representation in middle management mirroring that of the overall workforce generated 36 basis points of excess monthly return compared to less diverse peers. Importantly, the companies actively working to close the representation gap at higher organizational levels have also demonstrated positive relative stock performance.[2]

Women-Friendly Policies

Using the average length of maternity leave as a proxy for "women-friendly" policies, Blackrock researchers found that incorporating this data into investment decisions may provide a boost to portfolio returns. Specifically, by overweighting companies with longer maternity leaves and underweighting those with shorter leaves, their hypothetical portfolio produced a 1.07% annualized excess return from 2019-2023.[3] Blackrock also found the length of maternity leave to be positively correlated with employee sentiment and a negatively correlated with employee turnover rates. Of course, all companies should strive to have happy employees, and a large body of research suggests there is also a strong economic case for doing so. A 2023 McKinsey study clearly underscores this economic rationale, where it found lower employee sentiment linked with lower productivity, higher attrition, and higher costs.

What Does That Mean?

So, why is it that companies displaying these characteristics tend to outperform? One simple answer may be culture. That is, companies with gender-balanced workforces, more equitable hiring practices and promotion approaches, and women-friendly policies may also be the companies with positive workplace cultures. Regardless of whether these characteristics lead to better culture, or a better culture brings about these characteristics, the results are clear: a more balanced gender representation from top to bottom unlocks an organization's access to a broader talent pool, enhances employee sentiment and comfort level, and fosters better alignment between leadership and the rest of the organization.

Corporate culture is the shared values, beliefs, and practices that guide the way employees work and make decisions. Put differently, culture is the unique way a company embodies its mission and meets the needs of its customers. Any way you define it, culture is a crucial differentiator, not only when it comes to attracting and retaining customers, but talented employees as well. A positive relationship between company culture and financial performance has strong academic backing. This same logic may explain in part why companies with greater racial and gender equity may have robust workplace cultures and thus experience financial success.

"What gets measured gets done" can be a mantra to help companies measure, track, and improve in areas of diversity, equity, and inclusion that fall short of best practice. As regulatory and reputational risks continue to grow, top performing companies with respect to diversity and inclusion may accrue even more advantages. Maintaining and upgrading their own 'home court' better situates a company to win again and again, as a desirable employer, a product or service provider, and an investment opportunity.

It's clear: diversity and inclusion help create a high-performing team led by strong coaches, who return consistent wins to the fans.

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LEARN MORE

The 1919 Inclusive Investing Strategy aims to identify companies who meet our criteria in reflecting a commitment to upholding diversity, inclusion, and equality, both internally and with their community of stakeholders. Learn more here.

For more than 50 years, the 1919 Responsible Investing team has partnered with clients to ensure that their investment portfolios express their values and support their desire to have a positive impact on the world. Learn more here.

1919 Women & Wealth is committed to engaging and supporting women as they create and manage wealth. We provide investment and planning resources derived from decades of experience. A dedicated team partners with you to identify your values, priorities, and short- and long-term objectives. Learn more here.

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ABOUT 1919 INVESTMENT COUNSEL

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Notes

[1] Blackrock performed a global study of roughly 1,250 large companies.

[2] Blackrock created a hypothetical long-short portfolio, longing companies that are promoting more women to senior roles and shorting those that are not. The hypothetical portfolio generated 0.72% excess return per year relative to the MSCI World Index from January 2019 to January 2023.

[3] Blackrock's hypothetical portfolio was measured against the Russell 1000 Index using performance figures from January 2019 to January 2023.

- Blackrock is a leading publicly traded investment managemnet firm providing a broad range of investment management and technology services to institutional and retail clients worldwide. The company manages over $10 TR in assets.
  Source: BlackRock Inc. 2024 March quarterly filing.

- Morgan Stanley is a global financial services firm maintaining significant market positions in each of its business segment: Institutional Securities, Wealth Management and Investment Management. The company manages over $1.4 TR in assets.
  Source: Morgan Stanley 2024 March quarterly filing.

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