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Organization

Delivering through diversity

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Our latest research reinforces the link between diversity and company financial performance—and suggests how organizations can craft better inclusion strategies for a competitive edge.

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Full Report (PDF-7MB)

Awareness of the business case for inclusion and diversity is on the rise. While social justice typically is the initial impetus behind these efforts, companies have increasingly begun to regard inclusion and diversity as a source of competitive advantage, and specifically as a key enabler of growth. Yet progress on diversification initiatives has been slow. And companies are still uncertain about how they can most effectively use diversity and inclusion to support their growth and value-creation goals.

Our latest study of diversity in the workplace, *Delivering through diversity*, reaffirms the global relevance of the link between diversity—defined as a greater proportion of women and a more mixed ethnic and cultural composition in the leadership of large companies—and company financial outperformance. The new analysis expands on our 2015 report, *Why diversity matters*, by drawing on an enlarged data set of more than 1,000 companies covering 12 countries, measuring not only profitability (in terms of earnings before interest and taxes, or EBIT) but also longer-term value creation (or economic profit), exploring diversity at different levels of the organization, considering a broader understanding of diversity (beyond gender and ethnicity), and providing insight into best practices.

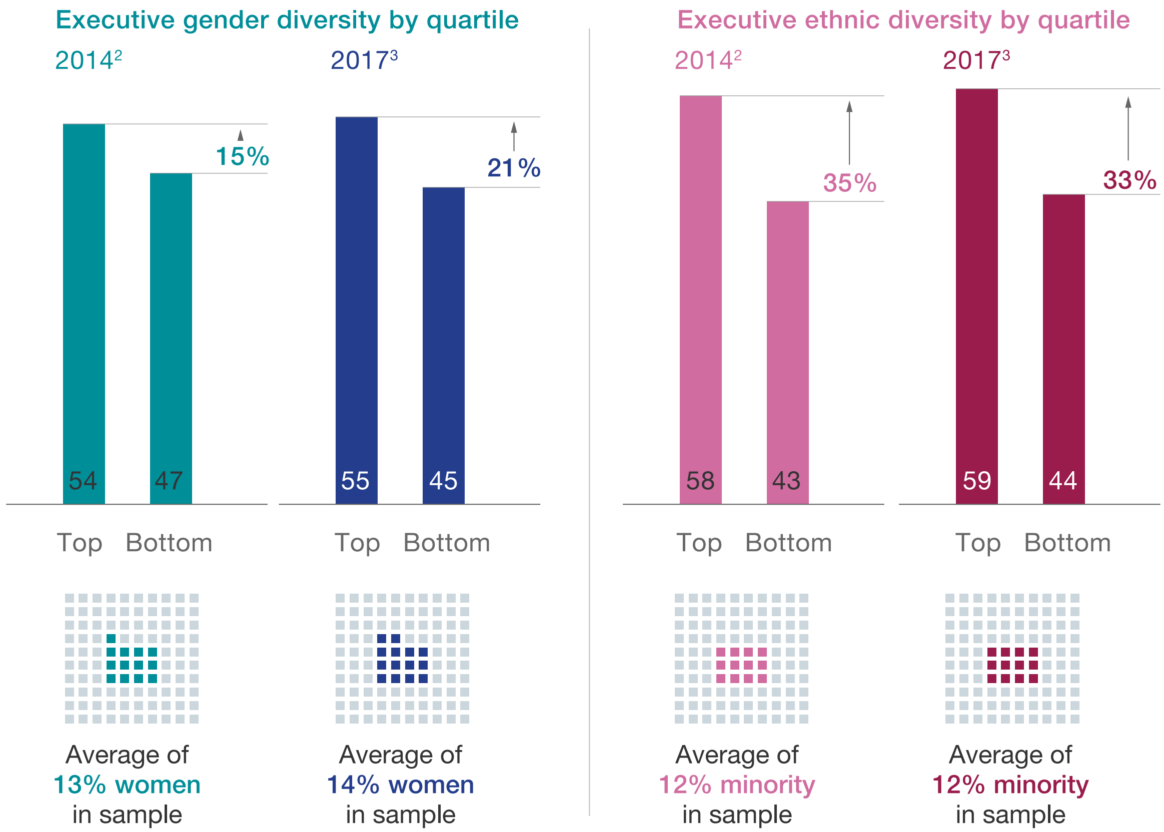
Diversity and financial performance in 2017

In the original research, using 2014 diversity data, we found that companies in the top quartile for gender diversity on their executive teams were 15 percent more likely to experience above-average profitability than companies in the fourth quartile. In our expanded 2017 data set this number rose to 21 percent and continued to be statistically significant. For ethnic and cultural diversity, the 2014 finding was a 35 percent likelihood of outperformance, comparable to the 2017 finding of a 33 percent likelihood of outperformance on EBIT margin; both were also statistically significant (Exhibit 1).

Exhibit 1

Gender and ethnic diversity are clearly correlated with profitability, but women and minorities remain underrepresented.

Likelihood of financial performance[1] above national industry median, %



[1]Average earnings-before-interest-and-taxes (EBIT) margin, 2010–13 in Diversity Matters I and 2011–15 in Diversity Matters II.
[2]Results are statistically significant at p-value <0.10.
[3]Results are statistically significant at p-value <0.05.

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Several other findings on gender diversity, ethnic diversity, and diversity around the world are also interesting.

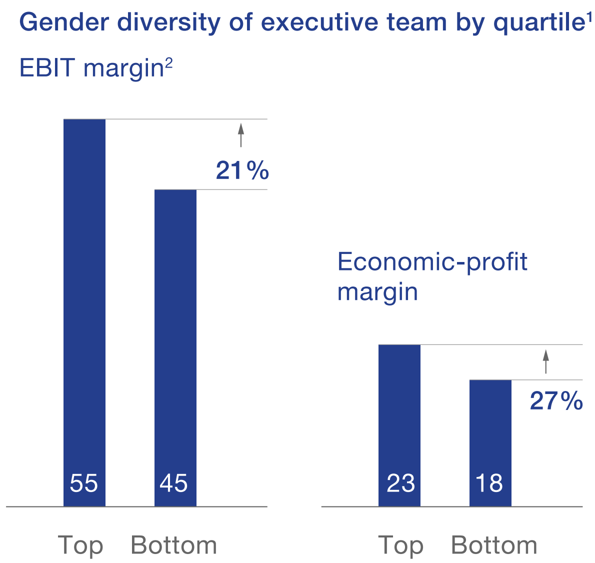
Gender diversity

Gender diversity is correlated with both profitability and value creation. In our 2017 data set, we found a positive correlation between gender diversity on executive teams and both our measures of financial performance: top-quartile companies on executive-level gender diversity worldwide had a 21 percent likelihood of outperforming their fourth-quartile industry peers on EBIT margin, and they also had a 27 percent likelihood of outperforming fourth-quartile peers on longer-term value creation, as measured using an economic-profit (EP) margin (Exhibit 2).

Exhibit 2

Gender diversity on executive teams is strongly correlated with profitability and value creation.

Likelihood of financial performance above national industry median, %



[1]Results are statistically significant at p-value <0.05.
[2]Average earnings-before-interest-and-taxes (EBIT) margin.

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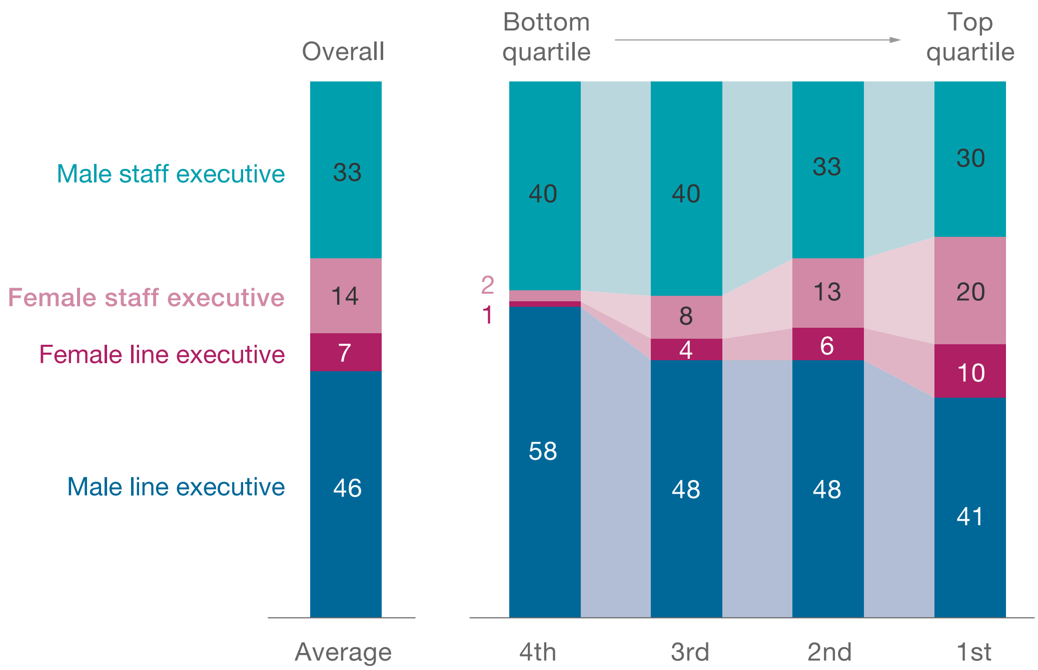
For gender, the executive team shows the strongest correlation. We found that having gender diversity on executive teams, specifically, to be consistently positively correlated with higher profitability across geographies in our data set, underpinning the role that executive teams—where the bulk of strategic and operational decisions are made—play in the financial performance of a company.

Executive teams of outperforming companies have more women in line roles versus staff roles. We tested the hypothesis that having more women executives in line roles (typically revenue generating) is more closely correlated with financial outperformance. We know from research, such as our *Women in the Workplace 2017* report, that women are underrepresented in line roles. In our data set, this holds true even for top-quartile gender-diverse companies experiencing above-average financial performance. Yet these top-quartile companies also have a greater proportion of women in line roles than do their fourth-quartile peers: 10 percent versus 1 percent of total executives, respectively (Exhibit 3).

Exhibit 3

Even among top-quartile companies, women executives are more likely to occupy staff roles than line roles.

Executive roles[1] split by gender-diversity quartile,
companies with above-median financial performance, %



[1]Executive roles by responsibility and gender at UK and US companies with above-median financial performance, split by gender-diversity quartile. Above-median financial performance calculated using average earnings-before-interest-and-taxes (EBIT) margin.
Note: Figures may not sum to 100%, because of rounding.

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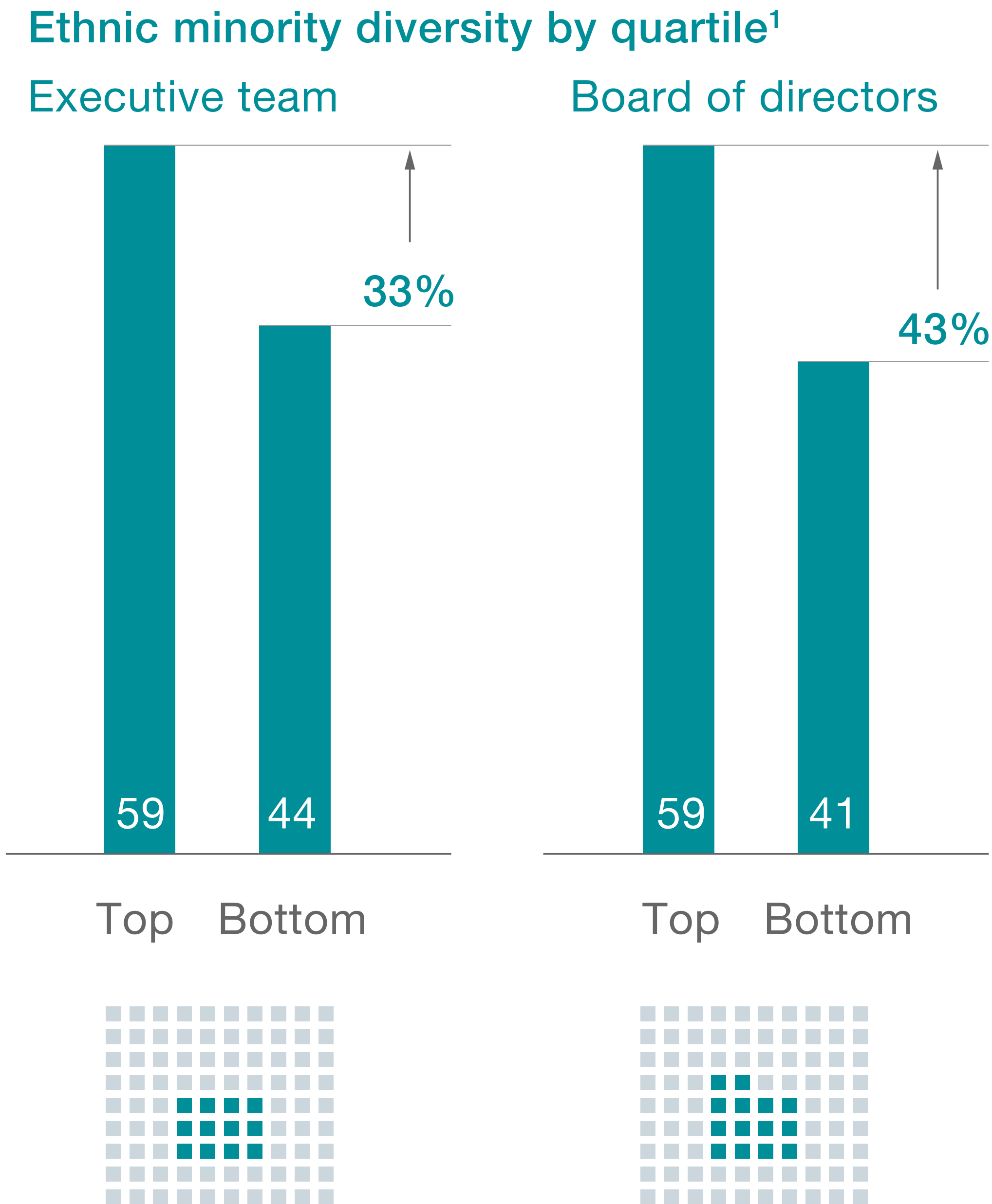
Ethnic and cultural diversity

Top-team ethnic and cultural diversity is correlated with profitability. In our 2017 data set, we looked at racial and cultural diversity in six countries where the definition of ethnic diversity was consistent and our data were reliable.[1] As in 2014, we found that companies with the most ethnically diverse executive teams—not only with respect to absolute representation but also of variety or mix of ethnicities[2] —are 33 percent more likely to outperform their peers on profitability. That's comparable to the 35 percent outperformance reported in 2014, with both figures being statistically significant (Exhibit 4).

Exhibit 4

Ethnic diversity in the executive team and board correlates with stronger profitability.

Likelihood of financial performance above national industry median, %



Average of 12% minority in sample

Average of 14% minority in sample

[1]Average earnings-before-interest-and-taxes (EBIT) margin 2011–15. Results are statistically significant at p-value <0.05.

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The penalty for not being diverse on both measures persists. Now, as previously, companies in the fourth quartile on both gender and ethnic diversity are more likely to underperform their industry peers on profitability: 29 percent in our 2017 data set.

Ethnic and cultural diversity on executive teams is low. We focused on our US and UK data sets to examine ethnically and culturally diverse representation among US and UK companies, considering the pipeline starting with university graduates. Black Americans comprise 10 percent of US graduates but hold only 4 percent of senior-executive positions, Hispanics and Latinos comprise 8 percent of graduates versus 4 percent of executives, and for Asian Americans, the numbers are 7 percent of graduates versus 5 percent of executives. In the United Kingdom, the disparity is even greater: 22 percent of university students identify as black and minority ethnic, yet only 8 percent of UK executives in our sample do.

Black women executives are underrepresented in line roles and may face a harder path to CEO. As discussed, within our US and UK data sets, overall representation of women on executive teams shows an apparent bias toward staff roles. Among our US sample, not only do women hold a disproportionately small share of line roles on executive teams but also women of color (including Asian, black, and Latina women) hold an even smaller share.

Line roles versus staff roles on executive teams tend to differ in their ability to propel individuals to the CEO position, with line roles the more likely incubators of future CEOs. In our US sample, black female executives, specifically, are more than twice as likely to be in staff roles than in line roles, and our sample denotes an absence of black female CEOs. Other studies have found that black women suffer a double burden of bias that keeps them from the uppermost levels of corporate leadership. Underrepresentation on executive teams in general, and in line roles in particular, could be an important piece of this story.

Diversity around the world

The correlation between gender and ethnic diversity and financial performance generally hold true across geographies, though with some variations in certain regions. Our data yielded some noteworthy findings concerning the country-level differences in executive-team diversity:

Australian companies lead the way when it comes to the women's share of executive roles (21 percent). The share in the United States is 19 percent and in the United Kingdom is 15 percent. The same holds true for board positions, with Australian companies at 30 percent, US companies at 26 percent, and UK companies at 22 percent—and for women at the whole company level. The disparity among these countries is interesting, given that women's participation in the workforce is similar in all three and given that they dominate among top performers, representing 47 percent of the data set but more than 70 percent of the top-quartile companies.

The picture on ethnic and cultural diversity on executive teams is nuanced. Among our sample, South Africa has the highest levels of diverse representation on executive teams, with 16 percent of executive positions held by blacks. However, this must be understood in the context of local demographics: South Africa's population is 79 percent black, but among large corporations, the impact of South Africa's complicated social history means that the large majority of global and national corporate entities are led by white executives (69 percent in our sample). As our work considers the local context with respect to ethnicity, we therefore evaluated South Africa's diversity from this perspective, defining black South Africans as the minority. Singapore, the United Kingdom, and the United States follow South Africa with 11 to 12 percent of ethnically diverse executives.

When considering ethnic-minority representation in the broader population, British executive teams seem closer to achieving a "fair share." This, however, masks huge variations within the UK data set, in which a large proportion of companies have no ethnic minorities on their executive teams (or boards) and a handful of companies have particularly international executive teams. Ethnically diverse representation on UK and US executive teams increased by an average of six and five percentage points, respectively, since 2014. However, this was offset by declines in other geographies, leading to an overall lower increase of one percentage point across regions (Exhibit 5).

Exhibit 5

Delivering impact through diversity

Our research confirms that gender, ethnic, and cultural diversity, particularly within executive teams, continue to be correlated to financial performance across multiple countries worldwide. In our 2015 report, our hypotheses about what drives this correlation were that more diverse companies are better able to attract top talent; to improve their customer orientation, employee satisfaction, and decision making; and to secure their license to operate—all of which we believe continue to be relevant.

Companies report that materially improving the representation of diverse talent within their ranks, as well as effectively utilizing inclusion and diversity as an enabler of business impact, are particularly challenging goals. Despite this, multiple companies worldwide have succeeded in making sizable improvements to inclusion and diversity across their organizations, and they have been reaping tangible benefits for their efforts.

We found that these companies all developed inclusion and diversity (I&D) strategies that reflected their business ethos and priorities, ones that they were strongly committed to. Four imperatives emerged as being crucial:

Articulate and cascade CEO commitment to galvanize the organization. Companies increasingly recognize that commitment to inclusion and diversity starts at the top, with many companies publicly committing to an I&D agenda. Leading companies go further, cascading this commitment throughout their organizations, particularly to middle management. They promote ownership by their core businesses, encourage role modeling, hold their executives and managers to account, and ensure efforts are sufficiently resourced and supported centrally.

Define inclusion and diversity priorities that are based on the drivers of the business-growth strategy. Top-performing companies invest in internal research to understand which specific strategies best support their business-growth priorities. Such strategies include attracting and retaining the right talent and strengthening decision-making capabilities. Leading companies also identify the mix of inherent traits (such as ethnicity) and acquired traits (such as educational background and experience) that are most relevant for their organization, using advanced business and people analytics.

Craft a targeted portfolio of inclusion and diversity initiatives to transform the organization. Leading companies use targeted thinking to prioritize the I&D initiatives in which they invest, and they ensure there is alignment with the overall growth strategy.

They recognize the necessity of building an inclusive organizational culture, and they use a combination of “hard” and “soft” wiring to create a coherent narrative and program that resonates with employees and stakeholders, helping to drive sustainable change.

Tailor the strategy to maximize local impact. Top and rapidly improving companies recognize the need to adapt their approach—to different parts of the business, to various geographies, and to sociocultural contexts.

Paying rigorous attention to all four imperatives (Exhibit 6) helps to ensure that inclusion and diversity will support a company’s growth agenda. In our experience, companies tend to fall short on leadership accountability for meeting goals, on building the business case, and on the coherence and prioritization of the resulting action plan.

Exhibit 6

Diversity leaders bring fresh perspectives on how to build an effective strategy by drawing on the stories of leading global companies.

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It is worth noting that while progress on representation can be brought about relatively rapidly with the right set of initiatives, embedding inclusion within the organization can take many years and often requires action outside the organization. Companies that do this well can create a strong corporate ethos that resonates across employee, customer, supplier, investor, and broader stakeholder groups.

This work sheds light on how companies can use inclusion and diversity as an enabler of business impact. It is important to note, however, that correlation does not demonstrate causality, which would be challenging to demonstrate. While not causal, we observe a real relationship between diversity and performance that has persisted over time and scale, and across geographies. There are clear and compelling hypotheses for why this relationship persists including improved access to talent, enhanced decision making and depth of consumer insight and strengthened employee engagement and license to operate. We encourage businesses to examine the case for inclusion and diversity at a more granular level to craft an approach that is tailored to their business, learning from leading diverse companies around the world as to ways to do this with high impact.

The business case for diversity continues to be compelling and to have global relevance. There's an opportunity for promoting diversity in senior decision-making roles, and specifically in line roles on executive teams. Although levels of diverse representation in top teams are still highly variable globally—with progress being slow overall—there are practical lessons from successful companies that have made inclusion and diversity work. Creating an effective inclusion and diversity strategy is no small effort and requires strong, sustained, and inclusive leadership. But we, and many of the companies we studied, believe the potential benefits of stronger business performance are well worth it.

Download Delivering through diversity, *the full report on which this article is based* (PDF—7 MB).

1.Brazil, Mexico, Singapore, South Africa, United Kingdom, and United States.

2.We measure ethnic diversity using the normalized Herfindahl-Hirschman Index (NHHI).

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