Institution: London School of Economics and Political Science

Unit of Assessment: 19: Business and Management Studies

Title of case study: Gender diversity on boards: are quotas the answer?

1. Summary of the impact (indicative maximum 100 words)

Research by Ferreira and colleagues at LSE shows that a gradual approach to gender-balanced boards based on matching of skills to needs is more effective than the imposition of quotas. The impact of this research has been achieved by engaging with practitioners and regulators in formal evidence-based governance debates and consultations. LSE research has informed the debate on how to best achieve gender diversity and played a central part in the UK Government's decision not to impose gender quotas but instead to endorse a self-regulation regime, a position which is gathering support in the EU as well.

2. Underpinning research (indicative maximum 500 words)

Research Insights and Outputs: Corporate governance is the system by which corporations are organised and controlled, and the rules that govern the relationships amongst different stakeholders. Improving corporate governance can lead to a better allocation of resources, both capital and human resources in the economy, which affects economic growth and has consequences for the distribution of its rewards. The Corporate Governance Research Programme at LSE's Financial Markets Group (FMG) has a longstanding record of research and research dissemination in this area including practitioner workshops on these issues. Understanding the costs and benefits of different governance regimes and mechanisms is central to FMG's research agenda.

Gender diversity of corporate boards and the links to corporate performance is an important policy issue. LSE research on the prevalence of gender diversity at board level and its effects is based on a general analytical model that identifies key features of the corporate governance problem and how this interacts with performance. This theoretical framework provides the foundation for a rigorous empirical examination of the issues relating to board composition that, in turn, forms the basis for an evaluation of the policy debate on gender diversity at board level and, specifically, the effectiveness of quotas to achieve it, which has been proposed as one regulatory way in which to achieve greater diversity.

The key theoretical model underlying LSE's research on corporate boards is set out in the influential paper by Ferreira [1] (co-authored with Adams, an FMG Research Associate). Regardless of gender diversity, and thus generally, many governance reform proposals are based on the view that boards have been too friendly to executives, for example, by awarding them excessive pay. Although boards are often on friendly terms with executives, it is less clear, however, that they have systematically failed to function in the interests of shareholders. To address this tension, the research develops a model that considers the board's dual role as *advisor* as well as *monitor* of management. Given this dual role, the CEO faces a trade-off in disclosing information to the board: if the CEO reveals more information, s/he receives better advice; however, an informed board can also monitor the CEO more intensively Using this model that trades off this key tension between advising and monitoring, Ferreira and colleagues have conducted a number of studies that examine key aspects of different board structures, and have developed a framework for policy evaluation of these structures, including the empirical analysis of gender diversity in the boardroom (Adams and Ferreira [2], [3]; Adams and Funk [4]).

Article [2] is the key impact paper on gender diversity in the boardroom. It draws on [1] to identify the relevant trade-offs between the nature of governance and performance. It shows in a cross-section of US firms that female directors have a significant impact on board inputs and firm performance. Specifically, it finds that female directors have better attendance records than male directors and that they are more active monitors, such as by being the chair or a member of important monitoring committees of the Board of Directors. These results suggest that gender-diverse boards allocate more effort to monitoring; that is, these are boards of firms where the CEO enjoys relative less managerial power and where the interests of shareholders have greater primacy. Accordingly, the research finds that pay is more equity-based and CEO turnover is more sensitive to share price performance (that is, low performance is more strongly associated with lower pay and CEO dismissal) in firms with more gender-diverse boards.

But is stronger monitoring better for all firms? Or as the equilibrium analysis in [1] would suggest, do all firms benefit equally from increased monitoring? The research suggests that it depends on the presence of other board monitoring mechanisms over the CEO. For example, the research suggests that companies with fewer takeover defences, which indicate better governance, benefit less from extra monitoring. Actually, the research shows that such firms can suffer from "over-monitoring". Mandating gender quotas for directors does not, by design, take the differential presence and strength of monitoring across firms into account, and neither, by consequence, its differing effects on firm value. This suggests that a self-regulating approach to board gender diversity may be preferable.

Key Researchers: Ferreira has been at LSE since 2006 and has been Professor of Finance since 2011; he was Director of the FMG's Corporate Finance and Governance programme from 2008-2012. Adams has been an FMG Research Associate since 2008.

3. References to the research (indicative maximum of six references)

[1] Renée Adams and Daniel Ferreira, "A Theory of Friendly Boards", *Journal of Finance*, 2007. DOI: 10.1111/j.1540-6261.2007.01206.x

[2] Renée Adams and Daniel Ferreira, "Women in the Boardroom and Their Impact on Governance and Performance", *Journal of Financial Economics*, 2009. DOI: 10.1016/j.jfineco.2008.10.007

[3] Renée Adams and Daniel Ferreira, "Strong Managers, Weak Boards?" *CESifo Economic Studies*, 2009 (Symposium on Executive Pay). DOI: 10.1093/cesifo/ifp023

[4] Renée Adams and Patricia Funk, "Beyond the Glass Ceiling: Does Gender Matter?", *Management Science*, 2012. DOI: 10.1287/mnsc.1110.1452

Evidence of quality: The foundational article [1] is widely cited and influential by itself. It has won the Emerald Citations of Excellence Award in 2011 for papers with proven impact since publication; the 2006 Egon Zehnder International Prize for the best paper in the ECGI Working Paper Series on company boards and their role in corporate governance; and is the second most cited paper out of all articles published in the *Journal of Finance* since 2007. It has more than 780 Google Scholar citations. The key study in this impact case study [2] is widely cited with over 460 Google Scholar citations.

4. Details of the impact (indicative maximum 750 words)

Impacts: LSE research on gender diversity in the boardroom has contributed significantly to public debate and policy-making in the UK and beyond.

a. *Public Debate*: There is an on-going public debate about the potential costs and benefits of introducing gender quotas on company boards in the UK and in the EU more generally. Laws mandating such quotas are already in effect in Norway, and recently have been approved in France and Spain. There is currently a push by some country members for an EU-wide mandatory quota. The committee of the European Commission is explicit in its support for quota-based initiatives. The UK has been an opponent of such mandatory quotas, and has supported instead a voluntary approach based on self-regulation.

Research by Adams and Ferreira has significantly influenced the public debate on gender diversity in the boardroom, and has also influenced the UK position. Ferreira was invited to give oral evidence to the Treasury Select Committee inquiry on Women in the City in the House of Commons. His input has influenced the Committee's conclusion not to support a "*legal requirement for boards to contain a particular proportion of women*" (see [5], p. 33).

Adams and Ferreira have been at the centre of the public debate on the issue of gender diversity. For example, Ferreira has written an opinion piece discussing mandatory quotas [6]; gave numerous interviews to the press; and has been invited to discuss this issue with practitioners and regulators at important events, such as the International Corporate Governance Network Conference in Toronto (2010). Adams has presented her follow-up paper based on the work with Ferreira – "Beyond the glass ceiling: does gender matter?" [4] – at our LSE Governance Research Debates, with Lucy Kellaway (*FT*) as a discussant. This paper has also been cited in the *FT* and discussed in *The Wall Street Journal* blog. Many policy articles written by leading academics also cite the evidence in the paper (an example can be found in [7]). Paper [2] has also directly influenced the views of some major companies on the issue of gender diversity on boards. An example is the recent report by Credit Suisse on gender diversity and performance [8], which refers to many of the findings of the paper.

b. *Policy-making*: Paper [2] has had an immediate impact on the British public debate on the issue of women on boards. It was published at the end of 2009, soon after the now famous comment by Harriet Harman that female under-representation on bank boards was partly to blame for the financial crisis (The "Lehman Sisters" episode). The publication of paper [2] received extensive coverage in the British press (*FT*, *Guardian*, *The Times*, *The Economist*, etc – for evidence see [9] and [10]), as well as in the international press. The Report of the Treasury Committee [5] explicitly refers to the evidence in the paper, as well as the oral evidence given by Ferreira (for evidence see pages 10, 11 and 14 of [5]). In particular, when referring to the desirability of quotas, the report notes that "*Dr Ferreira noted that while quotas can achieve gains in the long run, they are associated with costs in the short run*" ([5], p. 14). This argument is based on the theoretical foundations laid down in paper [1], which emphasise both the benefits and costs of increased monitoring by boards. The European Commission has also used the findings in [2] in its recent assessment of the effectiveness of imposing quotas for gender diversity in the boardroom (see [11]). And there is evidence that LSE governance research has had impact beyond the boardroom. For example, Paper [2] is cited twice in responses to a consultation on "Women in the Workplace" by the House of Commons (see [12]). The paper is also cited in an OECD report on entrepreneurship [13].

Wider Implications Effective corporate governance is vital to long-term firm performance. LSE research has established that the imposition of gender quotas in the boardroom is not necessarily the most effective way to match skills to needs. By informing the UK government's approach to this matter, LSE research has contributed to a more nuanced and context-dependent policy approach to governance and economic performance in the UK. The reach of future impacts is likely to be beyond the UK.

5. Sources to corroborate the impact (indicative maximum of 10 references)

All Sources listed below can also be seen at: https://apps.lse.ac.uk/impact/case-study/view/25

[5] House of Commons Treasury Committee, "Women in the City," Tenth Report of Session 2009-10. https://apps.lse.ac.uk/impact/download/file/1430

[6] Daniel Ferreira "If women ruled boards," The Sunday Telegraph, August 9, 2009, (Business, page 4). https://apps.lse.ac.uk/impact/download/file/1432

[7] Johanne Grosvold, Stephen Pavelin, Ian Tonks, "Gender Diversity on Company Boards," VOX - Research-based policy analysis and commentary from leading economists. https://apps.lse.ac.uk/impact/download/file/1433

[8] Credit Suisse, "Gender Diversity and Corporate Performance," August 2012.

https://apps.lse.ac.uk/impact/download/file/1434

[9] *The Economist*, “Skirting the issue: Imposing quotas for women in boardrooms tackles a symptom of discrimination, not the cause,” (Schumpeter column, March 11, 2010). https://apps.lse.ac.uk/impact/download/file/1435

[10] *Financial Times* (August 7, 2009): “Doubt cast on women in boardroom,” (page 2) and “Keep this research away from the diversity dinosaurs,” (page 16, Lombard column). October 26, 2009: “Jury’s out over taking women on boards,” (page 25). Also quoted on 15-Oct-2009, page 4, “Maternity leave hurts women, says banker.” (Also discussed at FT’s management blog). https://apps.lse.ac.uk/impact/download/file/1436

[11] European Commission, 2012, “IMPACT ASSESSMENT ON COSTS AND BENEFITS OF IMPROVING THE GENDER BALANCE IN THE BOARDS OF COMPANIES LISTED ON STOCK EXCHANGES. https://apps.lse.ac.uk/impact/download/file/1437

[12] House of Commons, Business, Innovation and Skills Committee, “Women in the Workplace.” https://apps.lse.ac.uk/impact/download/file/1438

[13] OECD (2012), “Women on company boards”, in *Entrepreneurship at a Glance 2012*, OECD Publishing. https://apps.lse.ac.uk/impact/download/file/1439