



Generational Wealth. Generational Solutions. Corporate Services

A photograph of a modern conference room with a long white table, white chairs, and a large window with blinds. A white box with blue and black text is overlaid on the image.

# GOVERNANCE AND COMPLIANCE DIGEST

## BOARD DIVERSITY AND INCLUSION

---

It is often said that two heads are better than one; even better is when those two heads bring different perspectives. This has given credence to the concept of diversity within boards of directors which has become an increasingly important topic in recent years. A diverse board can bring a wealth of experience, skills, different perspectives, and other qualities into a single pool which would enhance quality decision making and invariably, the company's performance.

### **Exploring the Concept of Board Diversity and Inclusion**

The concept of diversity within boards refers to the composition of a board with regards to expertise, managerial backgrounds, age, gender, language, education, ethnicity, culture. The purpose of achieving diversity is to bring a range of perspectives and experiences to the decision-making process. Hambrick and Mason (1984)<sup>1</sup>, discovered that top management heterogeneity has a greater tendency to increase firms' performance. The key pillars of diversity within boards are inclusion, equity, and a sense of belonging. By creating an inclusive environment where everyone feels valued and heard, boards can foster equity and belonging, leading to improved decision-making outcomes.

## **CATEGORIES OF BOARD DIVERSITY**

### **Age Diversity**

The first key pillar of diversity within boards of directors is age diversity. An organization's board should represent a range of ages and generations to ensure diverse perspectives and experiences. Older directors can bring wisdom and experience, while younger directors can bring fresh ideas and innovative thinking. Having a mix of ages can also help to bridge the gap between different generations within the organization and ensure that the board is better equipped to navigate the changing business landscape. Age diversity specifically brings benefits such as a broader range of experiences and perspectives, increased creativity and innovation, and a better understanding of emerging trends and technologies. Having a diverse age range within the board can bring different perspectives and ideas, which can ultimately benefit the organization.

### **Gender Diversity**

Gender diversity is another key pillar of diversity within boards of directors. It refers to the representation of both women and men on the board. Women are often underrepresented on boards, despite the fact that they make up half of the population and the workforce. Ryan and Haslam (2005)<sup>2</sup> argue that women are more likely to be placed in positions of leadership in circumstances of the downturn. The implication is that the presence of women on the board could be perceived by shareholders that significant change is on the way, thereby making

<sup>1</sup> Hambrick, D. C. & Mason, P. A. (1984). Upper Echelon: The organisation as a reflection of its top managers. *The Academy of Management Review*, 9(2), 193-206.

<sup>2</sup> Ryan, M. K., & Haslam, A. (2005). The glass cliff: Evidence that women are over represented in precarious leadership positions. Retrieved from: <http://www.uts.edu.au/oth/wexdev/pdfs/ryanhaslam.pdf>

them more confident in the company's success, which results in an increase in share price.

## **Ethnic and National Diversity**

Ethnic diversity on the board refers to a mix of customs, heritage, origins, races and religions. While it can pose challenges related to cross-cultural communication and interpersonal conflicts (Cox, Jr., 1991)<sup>3</sup>, the presence of foreign nationals on the team is expected to confer competitive advantage on the firm in the form of international networks, commitment to shareholder rights, and managerial entrenchment avoidance (Oxelheim & Randøy, 2003)<sup>4</sup>. Directors from different ethnic backgrounds bring a wealth of experience and different perspectives to the boardroom, enabling better responses to issues related to diversity and inclusion thereby creating a more inclusive workplace.

## **BENEFITS OF BOARD DIVERSITY**

### **Catalyst for Change**

Enhancing board diversity increases the likelihood of proactive responses to a company's challenges. When diversity increases and a board becomes more engaged and professional in its practices, it becomes less likely that important concerns will be ignored by directors or receive scant attention. A director, interviewed by the Harvard Law School Forum gave a simple example to illustrate the foregoing:

*After the CEO of an underperforming company gave the board an update on the company's performance that indicated that one of its businesses would again be performing more poorly than projected, the incumbent directors remained silent, being accustomed to receiving such news. A newer, cognitively diverse member of the board broke the silence and asked "OK, so what do we have to do to improve revenues? What are your plans to address this?"*

*"It was an obvious question," the director told the Harvard Law School Forum, "but one that members of the board likely would not have asked in the past."*

Adding new, cognitively diverse directors to a board increases the likelihood that it will take a fresh look at salient issues, and now with the input of individuals with no emotional attachment to past decisions or ties to the people who made them. Cognitively diverse directors can also serve as a catalyst for a board to implement changes and make difficult decisions that are long overdue. Many of the directors interviewed by the Harvard Law School Forum described how new directors "helped push *the board past status quo thinkers*" and take steps that many on the board knew were necessary, such as replacing an underperforming CEO or selling

<sup>3</sup> Cox, Jr., T. (1991). The multicultural organisation. *Academy of Management Executive*, 5(2), 34-47.

<sup>4</sup> Oxelheim, L., & Randøy, T. (2003). The impact of foreign board membership on firm value. *Journal of Banking and Finance*, 27(12), 2369-2392.

a noncore business<sup>5</sup>.

### **Positive Reputation for the Firm**

The moral and societal value of diversity cannot be overlooked in today's socio-political environment. A diverse board signals to the firm's internal and external stakeholders that it is in sync with their values, preferences, interests, and aspirations. This increases the stature and reputation of the firm, which, some studies tie to better performance.

### **Enhanced Innovation and Decision Making**

Diverse perspectives in the boardroom foster a culture of creativity and innovation, leading to a broader range of insights and informed decision-making. Different backgrounds and experiences can challenge conventional thinking and help identify innovative solutions to complex problems. Diverse boards are also more likely to identify market opportunities, anticipate emerging trends, and adapt to changing customer demands.

### **CONCLUSION AND RECOMMENDATIONS**

It makes intuitive sense that improving diversity can enhance board performance. Studies have shown that diverse personal experiences, such as living, studying or working abroad are associated with greater creativity, that diverse cities are more productive and prosperous, and that diverse teams are more innovative and process facts more thoroughly and accurately than homogeneous ones.

We therefore strongly encourage companies to improve gender, racial, and ethnic diversity on their corporate boards. We recommend, however, that companies do so in a way that maximizes the diversity new directors bring to the boardroom. We encourage boards to select demographically diverse candidates that also improve cognitive differences in the boardroom, by identifying candidates who have unique views and perspectives as well as professional backgrounds, skills, and experiences that aligns with the company's strategic and operating needs.

<sup>5</sup> Harvard Law School Forum on Corporate Governance: <https://corpgov.law.harvard.edu/2020/07/14/maximizing-the-benefits-of-board-diversity-lessons-learned-from-activist-investing/>

Copyright © 2023 First Fiduciary, All rights reserved.

Our mailing address is:

First Fiduciary

3A, Kayode Otitoju Street, Off Admiralty Road,  
Lekki Phase 1, Lagos.