FEMINA INDEX: BETTING ON GENDER DIVERSITY IS A PROFITABLE SRI STRATEGY

Gender diversity is one of the main issues faced by corporations with regard to social responsibility.

MICHEL FERRARY

Socially responsible investment (SRI) attempts to consider both financial return and social good in order to support socially responsible corporate practices in a profitable way. SRI has become a major trend in asset management. The U.S. SIF Foundation estimates that in 2012 in the United States, $3.744 trillion was dedicated to sustainable and responsible investments. The Euro SIF evaluates that SRI represents €2.3 trillion in Europe.

SRI intends to promote corporate social responsibility (CSR) among large private companies by investing in firms that are developing socially responsible practices. CSR is evaluated through three dimensions: environment, social justice, and corporate governance (ESG). However, SRI faces two important issues, as outlined below.

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How to articulate SRI and profitability

Several academic researches highlight the difficulty of reconciling profitability and SRI. For a long time, the choice was presented as doing well (business growth and profitability) or doing good (socially responsible corporate behavior). Several fund managers require their investors to renounce a higher profitability in order to support socially responsible practices. The common belief was that doing both simultaneously was only possible at the expense of one of them. However, an alternative trend argues that doing well by doing good is a possible path. Socially responsible corporate practices might positively contribute to the growth and profitability of the firm and support its stock price. The methodological issue to invest in a socially responsible way is to find criteria to identify firms doing well and good.

How to operationalize the three criteria in order to justify an investment decision

One approach is to develop a complex index combining the three dimensions. The MSCI KLD 400 and the Euronext Vigeo World 120 illustrate this choice. However, the complexity of the rating can be confusing and lead to inconsistent recommendations. For example, in the past, Vigeo gave a very positive rating to the oil company Total, while the company was simultaneously being accused of supporting the dictatorship regime in Burma. Another approach is to screen out some industries due to their socially irresponsible activities (such as tobacco, gambling, weapons, or adult entertainment). The last method is to favor one dimension (environment, social justice, or governance) over the other two in order to invest in a socially responsible way.

From the latter perspective, some investors focus on the social dimension of corporate practices and scrutinize labor relations, human rights, and equal employment opportunity. Our research fits into this perspective. We have decided to focus on the social justice dimension by way of exploring the gender diversity–performance relationship in order to answer the following question: Do gender-diversified firms perform better or worse than the market?

Gender diversity is one of the main issues faced by corporations in regard to social responsibility. All industries are concerned, and this question is pertinent to half of the human population. Finding any evidence that gender diversity might contribute to a firm's performance and stock price would be a strong lever in the endeavor to promote equal employment opportunity and to support SRI.

Several financial analysts and scholars have already explored the gender diversity-performance relationship. Existing researches mainly analyze the relationship between the firm's performance (growth, profitability, and stock price) and the proportion of women on the board of directors or on the executive committee. The focus on diversity at the top level is justified by arguing that strategic decisions determining the firm's performance are taken at this level.

However, existing research did not report any clear evidence in regards to the gender diversity-performance relationship. Conclusions are generally cautious. They mainly imply that no negative or positive relationship exists between gender diversity at the top level of firms and performance. They also emphasize that nothing can be robustly stated from a statistical point of view.

These narrow conclusions are related to two methodological limitations. First, there are very few women in top managerial positions of large companies. In 2012, according to the Catalyst database, women held 16.6 percent of board seats at Fortune 500 companies. Only 89 of these companies had three or more women on their boards of directors (17.8 percent). That means that 82.2 percent of Fortune 500 companies had two or fewer women on their boards of directors (10 percent have no women) in 2012. That same year, women held 14.3 percent of executive officer positions at Fortune 500 companies. Only 64 of the Fortune 500 companies had three or more women on their executive committees (12.8 percent), and 139 of them (27.8 percent) did not have even one.

These very low proportions of women on boards of directors and executive committees weaken the opportunity for women to really influence the decision-making process of these groups. Simply including women in a group is of no real consequence. What matters the most is the proportion of women in the group. Professor Rosabeth Kanter of Harvard Business School emphasizes in her seminal article on gender studies that a minority group has to reach a 35 percent threshold in order to actually change the functioning of a group and make a difference.[1] Only a critical mass can really make a difference by modifying the social dynamics in a group and influencing its organizational culture. Otherwise, any minority presence squares more with tokenism for communication purposes, as opposed to aiming to really change the organization dynamics. Kanter points out that when making up less than 15 per-

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cent (skewed group), a minority group is just a "token" and cannot influence the "dominant" group that represents 85 percent or more of the population. Only in "tilted groups" with less extreme distributions (35-65 percent) might a minority free itself from the pressure of the dominant population and influence the culture and the functioning of the group.

Considering this 35 percent threshold, out of the Fortune 500 companies, only eight of them (1.6 percent) have more than 35 percent women on their boards of directors and only 10 of them (2 percent) have more than 35 percent of women on their executive committees. These very low percentages support the idea that large companies mainly engage in "window dressing" by recruiting a small number of women for top management positions in order to please stakeholders. From a methodological perspective, this small sample limits the possibility of robustly exploring, from a statistical viewpoint, the relationship between gender diversity at the top managerial level and firm performance.

THE FEMINA INDEX IS A DIVERSIFIED PORTFOLIO THAT INCLUDES SIX DIFFERENT INDUSTRIES.

Exploring the gender diversity–performance relationship at the top managerial level suffers from another limitation. It favors the analysis of the decision-making process at the strategic level in order to explain a firm's performance while ignoring another key factor of a firm's performance: execution. Research in management points out that success of a firm depends on the quality of strategic decisions taken by top managers, but this research also emphasizes the importance of execution to the successful implementation of the strategic intentions of top executives. The quality of execution depends more on middle managers and professionals who are in charge of implementing strategic decisions than on top managers who make these decisions. Middle managers are people who make up the organization and run the day-to-day business through multiple micro-decisions. For this reason, it makes sense to analyze the impact that gender diversity at the middle-management level has on firms' performances. Moreover, due to the size of this population in organizations, gender diversity at the middle-management level more greatly influences the firm's culture than do one or two women in the executive committee.

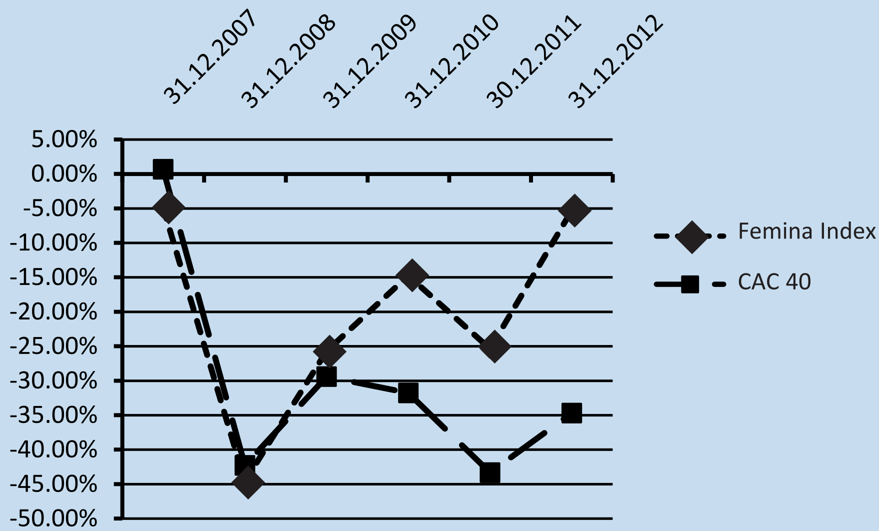
Based on the previous comments, this study analyzes and simulates a portfolio of French stocks selected with regard to the proportion of women at the middle-managerial and professional positions in each company. This portfolio is labeled the Femina Index. This research is based on an original set of data made possible by a French law that defines precisely the status of managers and professionals and obliges firms to disclose this information.

Our sample is made up of the 40 firms composing the CAC 40 index (the main benchmark French stock-market index). The gender diversity in the managerial population differs greatly among the firms belonging to the CAC 40. For example, in 2007, women represented 57 percent of LVMH's managers and only 8 percent of the managers at Total (the oil company).

Out of the 40 largest public French companies making up the CAC 40 index (building on Kanter's argument that a minority group should represent at least 35 percent of the population in order to influence the functioning of an organization), we composed the Femina Index portfolio with stocks of the firms with more than 35 percent of female managers in their 2007 workforces. The Femina Index is a diversified portfolio that includes six different industries. This portfolio is made up of ten companies: L'Oréal, LVMH, and PPR (luxury industry); AXA, BNPParibas, and Société Générale (financial services industry); Sanofi (pharmaceutical industry); Publicis (advertising industry); Accor (hospitality industry); and Danone (food industry).

The portfolio has been simulated over two periods surrounding the 2007 financial crisis, and it is benchmarked with the CAC 40 index. The first simulation is from 2007 to 2012 (pre-crisis portfolio), and the second ranges from 2009 to 2012 (post-crisis portfolio). The risk exposure has been controlled for by computing the beta coefficient of the portfolio over the two periods.

EXHIBIT 1 Cumulative Performance from January 2007 to December 2012



Investment 01/2007	31.12.2007	31.12.2008	31.12.2009	31.12.2010	30.12.2011	31.12.2012
Femina Index	–4.86%	–44.61%	–25.69%	–14.76%	–25.36%	–5.28%
CAC 40	0.69%	–42.29%	–29.40%	–31.76%	–43.33%	–34.70%

Pre-crisis investment — Portfolio performances from January 2007 to December 2012 (six-year period)

The Femina Index was back-tested over six years from January 2007 to December 2012 (Exhibit 1). This period was chosen in order to simulate a mid-term strategy initiated before the 2007 financial crisis. The CAC 40 index reached its highest opening level, 6117.52, on June 18 of 2007. The performances of the Femina Index and the CAC 40 were computed and compared at the end of each year over the period.

The simulation shows that over a period of six years, the Femina Index outperforms the CAC 40 by losing only 5.28 percent of its value, while the CAC 40 dropped by 34.7 percent. Concretely, a fund manager who would have invested €10 million in the Femina Index in January 2007 would have €9.47 million in December 2012 (–5.28 percent), as opposed to having €6.53 million if he or she had invested in the CAC 40 (–34.70 percent).

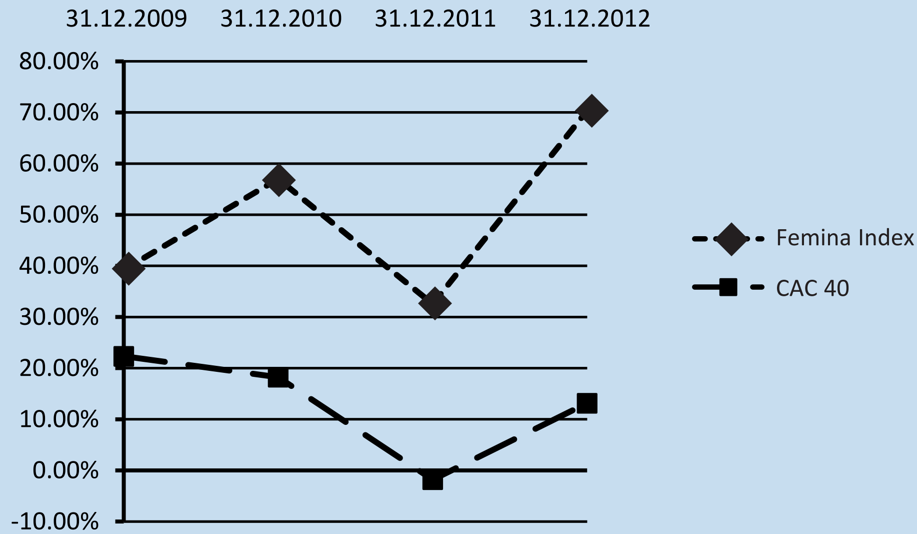
Moreover, except in 2008, the Femina Index outperforms the CAC 40 every year over the six-year period. This means that from 2007 to 2012, an investor could have disinvested from the Femina Index at the end of each year (except 2008) and beaten its reference index.

This performance does not result from a higher risk exposure. The beta coefficient of the Femina Index over six years is 1.04, meaning that it is an almost risk neutral investment strategy in comparison with the CAC 40.

Post-crisis investment — Portfolio performances from January 2009 to December 2012 (four year period)

The Femina Index was back-tested over four years from January 2009 to December 2012 (Exhibit 2). This date was chosen in order to simulate a short-term strategy initiated close to the lowest level of CAC 40 index after the 2009 financial market crisis. The CAC 40 index reached its lowest opening level, 2552.99, on March 9 of 2009. The performances of the Femina Index and the CAC 40 were computed and compared at the end of each year over the period.

EXHIBIT 2 Cumulative Performance from January 2009 to December 2012



Investment 01/2009	31.12.2009	31.12.2010	30.12.2011	31.12.2012
Femina Index	39.25%	56.99%	32.53%	70.34%
CAC 40	22.32%	18.24%	–1.81%	13.15%

The simulation points out that over a period of four years the Femina Index outperforms the CAC 40. Its value increases by 70.34 percent, while the CAC 40 goes up only by 13.15 percent. Concretely, a fund manager who would have invested €10 million in the Femina Index in January 2009 would have €17.03 million in December 2012 (+70.34 percent), as opposed to €11.31 million if she or he had invested in the CAC 40 (+13.15 percent).

Moreover, the Femina Index outperforms the CAC 40 every year over the four-year period. That means that from 2009 to 2012, an investor could have disinvested from the Femina Index at the end of each year and beaten the reference index.

This performance does not result from a higher risk exposure. The beta coefficient of the Femina Index over four years is 1.08, meaning that it is an almost risk neutral investment strategy in comparison with the CAC 40.

Conclusion

The performances of the Femina Index investment strategy support the idea that SRI strategy based on the social justice dimension of CSR might generate a decent profitability and even outperform the market. Picking stocks on the criteria of gender equality at the middle-management level is an investment strategy that maximizes financial return and social good. There is a business case supporting CSR practices that promote equal employment opportunity for women. This is consistent with previous academic researches pointing out that SRI strategies based on social criteria outperform SRI strategies based on environmental or governance criteria. By contributing to the firm's growth and profitability, gender diversity is implicitly related to the stock-price performance. Under the efficient-market hypothesis, the latter reflects the former.

Several reasons might explain the contribution of gender diversity to firms' business performance. First, by recruiting women, a firm enlarges its pool of talent, thereby increasing its probability of recruiting more efficient people. Second, women represent a major segment of customers. Having women on board provides some market insight and might help the sale process with female customers. Third, according to academic research, gender diversity contributes to creativity and improves the decision-making process in the organization. Fourth, promoting women sends a positive signal that motivates the entire pool of female employees. Fifth, an increasing number of stakeholders (customers, administrations, investors, and media) are sensitive to corporate commitment to supporting gender diversity. Promoting equal employment opportunity contributes to a company's positive image.

Gender diversity at the middle-management level provides a sustainable competitive advantage that surpasses the advantage of gender diversity at the board level or at the executive committee level. Indeed, it is relatively easy to change the proportion of women at the top levels. For example, a 10-member board of directors that includes only one woman might easily replace two men with two women and move the proportion of women from 10 percent to 30 percent. The same change at the middle-management level would require a large company to fire thousands of male managers and professionals in order to recruit thousands of female managers and professionals. This change cannot be done on a short-term basis. There is a human capital inertia that gives a sustainable competitive advantage to gender-diversified firms over those firms that are less diversified and would like to increase diversity.

Finally, the positive gender-diversity–stock-price performance relationship highlights the moral dimension of financial markets and the market efficiency when it comes to the eradication of certain kinds of discrimination. In the 1960s, Gary Becker, Nobel Prize winner in economic sciences, argued that discrimination (defined as the valuation in the market place of personal characteristics of the worker that are unrelated to worker productivity) is an irrational economic behavior for a firm.[2] A firm that discriminates among workers by recruiting employees based on personal characteristics (such as gender, race, religion, class, caste, sexual preference, or national origin) will have, on average, a less productive workforce that will lead to lower firm performance. Conversely, a firm recruiting only on the criteria of worker productivity — without any other discrimination — will put together a more productive workforce and will achieve better business performance. At midterm, due to their lower performances, discriminatory firms should be eliminated by the market, and only firms that support equal employment opportunity should survive. The superior business performance of gender-diversified firms supports Becker's theoretical argument that states that markets punish discrimination. ■

NOTES

[1] Kanter, R. M., Some effects of proportions on group life: Skewed sex ratios and responses to token women, *The American Journal of Sociology* 82 (1977) 965–990.

[2] Becker, G. S., *The Economics of Discrimination*. (Chicago: University of Chicago Press, 1957).