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Gender Equality as an Investment Concept

by Joseph F. Keefe, President & CEO, Pax World Management LLC

"The best clue to a nation's growth and development potential is the status and role of women." — David S. Landes, *The Wealth and Poverty of Nations*

The above quote, from a learned historian, speaks to a *nation's* growth and development potential—and today there is a strong consensus among international development experts that investing in women and girls is probably the most important strategy for alleviating poverty and promoting sustainable development around the globe. CARE, one of the world's largest international humanitarian organizations, puts it succinctly on its web site (www.care.org): "We place special emphasis on investing in women and girls because our six decades of experience show that their empowerment benefits whole communities."

There is also an emerging consensus that the status and role of women may be an excellent clue to a company's growth potential—that the best companies, and therefore the best investments, are those that take advantage of the talents, ideas and contributions of half of the world's population. In fact, numerous studies—some of which are highlighted below—have shown that companies that empower and advance women are likely to reap the benefits in terms of improved performance and profitability.[1] Among the many contributions that women can make to a company, it turns out that share price may be the most significant of all.

It is becoming increasingly evident, in other words, that gender equality and women's empowerment can be understood as investment concepts. Integrating a gender lens into investment strategies may be a strategy for obtaining better long-term investment performance.

Moreover, this elemental lesson—that the role of women can be critical for business success, and therefore investor success—comes at an opportune time: In the wake of a financial crisis and recession that have destroyed trillions of dollars in value, battering the retirement nest eggs of many Americans, there is an urgent need for economic and investment strategies that are focused on long-term value creation rather than short-term profits derived

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[1] I want to thank Julie Fox Gorte and Heather Smith of Pax World for the insights contained in their study, "Gender Empowerment and Financial Markets: A Literature Review for an Emerging Investment Discipline," 2010, which surveys the state of the literature, including academic studies and other sources, linking gender empowerment and financial performance.

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from financial engineering. Investors are hungry for strategies whose trajectories point not toward more financial bubbles, and the crises that inevitably follow, but toward long-term growth that is sustainable in the true sense of the term—the creation of durable, enduring value.

In my view, investing in women—or investing in companies that are committed to gender equality and women's empowerment—is just such a strategy. Moreover, there is a growing body of evidence to suggest that it is a smart investment strategy:

- A 2007 Catalyst study, for example, divided Fortune 500 companies into quartiles based on the percentage of women on their boards, and then compared "top-quartile" ompanies to "bottom quartile" companies on the basis of return on equity, return on sales and return on invested capital. The study found that top-quartile companies outperformed bottom-quartile companies on all three financial indicators by 42% to 66%. This pattern of outperformance held across five of the seven industries studied.[2]

- In an earlier, 2004 study, Catalyst found a similar correlation between overall senior management gender diversity and financial performance. In the 2004 study, Catalyst identified a universe of 353 of the Fortune 500 companies for which financial data was available from 1996 to 2000, and again divided the companies into four quartiles based upon the percentage of women on their management teams. Catalyst found that "top-quartile companies" had total shareholder return that was 34% higher and a return on equity that was 35.1% higher than "bottom quartile" companies, which results were consistent across industry.[3]

- A study of the profitability of Fortune 500 firms between 1980 and 1998, determined that the 25 firms with the strongest record of promoting women to the executive suite were more profitable than the median firms in their industries.[4]

- A 2008 study by McKinsey found that companies with greater numbers of women in senior management scored higher than lower-ranked counterparts on nine dimensions of organization, such as leadership, accountability and organization, and that higher-scoring companies are more likely to have above average earnings and financial valuations.[5]

- A recent study of French companies found that those with more women in their management withstood the 2008 market downturn better than those with fewer women, and attributed this success to gender diversity contributing to managerial efficiency and the fact that women tend to be more risk-averse than men.[6]

- A study of the relationships between gender and trust concluded that gender diversity of corporate boards is one indicator of trustworthy corporations. Trustworthiness, in turn, is an important element of reputation and brand value. "If there is a locus of trust in the corporation, it is the board…Based on existing research in the social sciences, [a] promising focus for enhancing trust in the corporation is gender

Past performance does not guarantee future results.

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[2]*Catalyst, "The Bottom Line: Corporate Performance and Women's Representation on Boards," 2007.*

[3]*Catalyst, "The Bottom Line: Connecting Corporate Performance and Gender Diversity," 2004.*

[4]*Roy D. Adler, "Women in the Executive Suite Correlate to High Profits," European Project on Equal Pay.*

[5]*Desvaux, Devillard-Hoellinger and Meany, "A Business Case for Women," The McKinsey Quarterly, September 2008.*

[6]*Professor Michel Ferrary, "When Gender Diversity Protects Stock Prices From the Crash," Ceram Business School, 2009.*

[7]*Joan MacLeod Heminway, "Sex, Trust, and Corporate Boards," Hastings Women's Law Journal, April 15, 2007.*

[8]*Jessica Bennett & Jesse Ellison, "Women Will Rule the World," Newsweek, July 6, 2010.*

diversification of boards of directors."[7]

- A July 6, 2010 *Newsweek* article reported on a McKinsey survey that found, of companies that had made efforts to empower women in emerging markets, 34 percent reported increased profits, and another 38 percent said they expected to see profit as a direct result of those efforts.[8]

I could go on, but you get the picture: there is mounting evidence that gender diversity has positive financial consequences.

When women are at the table, the discussion is richer, the decision-making process is better, management is more innovative and collaborative, and the organization is stronger. This is particularly the case with a critical mass of women in leadership roles. They bring new perspectives, consider different issues when making decisions, and tend to use a more collaborative leadership style, increasing win-win problem solving. At the same time, women are also more likely than men to ask tough questions and ask for more detail and substantiation. For these reasons, "a critical mass of three or more women on corporate boards can cause a fundamental change in the boardroom and enhance corporate governance."[9]

"It could be that women boost corporate performance, or it could be that better-performing firms have the luxury of recruiting and keeping high-potential women," wrote Hanna Rosin in her article, "The End of Men," in the July/August 2010 issue of *The Atlantic*. "But the association is clear: innovative, successful firms are the ones that promote women."[10]

Investing in companies that advance women, in other words, is simply a smart investment strategy.

In the financial sector, one can make the argument that this is particularly the case. We all know that the financial crisis and recession resulted from excessive risk taking and leverage by major banks and other financial institutions, most of it related to the packaging of subprime mortgages into opaque derivatives like collateralized debt obligations (CDOs), and insurance bets on their eventual default (credit default swaps), in a casinolike atmosphere that took down, first, the major financial institutions on Wall Street, and second, the entire global economy. Nice job, guys.

And in fact, it was guys who were mostly responsible. Women today hold only 3 percent of the CEO positions and 15 percent of the board positions among Fortune 500 companies.[11] Whereas women comprise nearly half of the country's workforce, they accounted for only 21 percent of middle managers and just 15 percent of all senior executive, corporate officer and board positions, according to a 2001 Catalyst study.[12] In the financial services industry, it may be even worse. According to recent research, women represent a mere 10 percent of all traditional mutual fund managers, a figure that has barely budged over the past decade despite increasing numbers of women financial advisers and women with degrees in finance. The disparity is even more apparent in the world of hedge funds, where women managed a mere 3 percent of the approximately $1.9 trillion invested as of early 2008.[13]

There is some evidence, moreover, that the financial crisis might not have been as severe had more women been in positions of authority. For example, there is some support for the proposition

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[9]V.W. Kramer, A.M. Konrad, and S. Erkut, "Critical mass on corporate boards: Why three or more women enhance governance," Wellesley Centers for Women, Paper No.WCW 11, 2006.

[10]Hanna Rosin, "The End of Men," The Atlantic, July/August 2010.

[11]Catalyst, "US Women in Business," June 2010.

[12]Catalyst, "Women in Financial Services: The Word on the Street," 2001, cited in "A Road Map for Achieving Critical Mass – and Why it Matters," The National Council on Research for Women, p. 17.

[13]"Women in Fund Management," The National Council for Research on Women, © 2009, p. 7.

that women in senior executive positions, including women fund managers, may be more risk averse—or at least take a different approach to risk—than do their male counterparts:

- One study found that overconfidence among single men investing in common stocks resulted in widespread over-trading (as much as 67 percent higher when compared with single women), leading to reduced gains and increased portfolio instability. In general, women tended to hold their investments longer and invest in holdings where there was less expected variance in investment results.[14]

- Another study looked at managers of U.S. equity mutual funds from 1994 through 2003 and documented similar differences between male and female fund managers: Women managers tended to take less risk and to follow less extreme investment styles which are more stable over time), while male managers had a more active style, with higher turnover ratios than female managers.[15]

Following the financial crisis, New York Times columnist Nicholas Kristof wrote about a meeting of the World Economic Forum in Davos, Switzerland, where "…some of the most interesting discussions revolved around whether we would be in the same mess today if Lehman Brothers had been Lehman Sisters. The consensus is that the optimal bank would have been Lehman Brothers and Sisters."[16]

In other words, in the wake of a financial implosion and severe global recession, when investors are seeking greater transparency, better risk-management and more stable long-term growth, one can make the case that promoting gender diversity in the executive suites of corporate America has never been more important. Quite simply, the business case for advancing women is increasingly clear. Closing what we might call "the gender diversity gap" looks to be a very profitable proposition.

And if it is profitable, *ergo*, we should be investing in it. So, how can investors do that? How can we fashion investment strategies that capitalize on what women have to offer? How can gender equality truly become an investment concept?

My company has asked itself these questions, and I think we've found some answers:

Apply a Gender Lens

First, if gender diversity on boards and in senior management is material to a company's business prospects, as the above evidence suggests, then it clearly makes sense to integrate these factors into fundamental analysis and investment portfolio construction. Yet very few money managers do this. Based on the above evidence, I would suggest that by ignoring gender diversity they are leaving money on the table.

At Pax World, we have long integrated diversity analysis and other gender criteria into the company research we conduct for our mutual funds. Our funds favor investments in companies with diverse boards and management teams while seeking to avoid companies that fail to provide a safe work environment for women by encouraging or tolerating harassment, or that have a history or pattern of discrimination or mistreatment of

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[14]B.M. Barber, and T. Odean, "Boys Will be Boys: Gender, Overconfidence, and Common Stock Investment," The Quarterly Journal of Economics. pp. 261-292, 2001.

[15]A. Niessen and S. Ruenzi, "Sex Matters: Gender and Mutual Funds," University of Cologne: Department of Corporate Finance & Centre for Financial Research. 2005, cited in Women in Fund Management, The National Council for Research on Women, © 2009, n 13.

[16]Nicholas D. Kristof, "Mistresses of the Universe," New York Times, February 7, 2009.

women, are involved in the exploitation or trafficking of women, or whose products demean women or use negative stereotypes in their advertising, promotion or marketing.

We also offer a specific fund, the Pax World Global Women's Equality Fund (PXWEX), which is the only mutual fund in America whose focus is on investing in companies that are global leaders in advancing gender equality and women's empowerment. Specifically, the Fund seeks to invest in companies that promote gender equality through internal policies and programs, transparency regarding the effectiveness of those policies and programs and accountability among employees to assure implementation and observance of those policies and programs. In particular, we favor companies that embrace or aspire to embrace the best practices embodied in the Women's Empowerment Principles, a joint initiative of the United Nations Development Fund for Women (UNIFEM) (www.unifem.org) and the United Nations Global Compact (www.ungc.org).

Promote Board Diversity

Second, investors actually have more power than they realize. They can say "no" to all-male corporate boards, and in fact, have an opportunity to do so each year when companies send out their annual proxy to shareholders. If investors don't vote their proxies directly, they just need to make sure that whoever does vote their proxies—be it their financial adviser, mutual fund or retirement fund votes in a manner that advances rather than thwarts gender diversity on corporate boards.

How is this accomplished? It's actually relatively easy:

At Pax World, we simply adopted a proxy voting guideline providing that, when we receive a company's annual proxy with its slate of directors submitted for shareholder election, we will not support any slate of directors that does not include women. When we withhold support, we register our concerns with the company by sending a follow-up letter explaining the reason for our opposition, urging them to embrace gender diversity on their board and providing them with model charter language for their nominating committee establishing a board diversity program.

This is a very simple step that any mutual fund, pension fund or other money manager can take if they want to promote gender diversity on corporate boards. And yet the overwhelming majority of them don't. Instead, they essentially rubber stamp most if not all management supported proxy proposals, including a company's hand-picked slate of all-male directors. What a shame—and what a lost opportunity.

If you believe that women should be better represented in the board rooms of corporate America, but you are invested through financial intermediaries that rubber stamp all-male corporate boards, then you are unwittingly part of the problem rather than part of the solution – or at least your investments are. You might think about switching to a firm that better understands your values and priorities.

Be an Engaged Shareholder

There are other ways for investors to promote board diversity as well. Not only can they do so by voting their proxies, but they can go beyond that and actually engage with companies to promote greater diversity on corporate boards.

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Again, there are limited opportunities to do this directly, but your mutual fund or pension fund can, and my company frequently does so on behalf of our shareholders.

For example, Pax World is currently co-leading an investor initiative, in collaboration with the United Nations Principles for Responsible Investment (UNPRI), which involves sending letters to companies in several countries urging them to formalize and expand their commitment to gender equality. Companies are targeted based on an absence of board and management diversity, inadequate disclosure and other policies related to diversity, and a lack of programs to encourage diversity and women-owned vendors in their supply chains.

We also recently launched a separate shareholder engagement campaign that involved sending letters to all of the companies held in our Pax World Global Women's Equality Fund urging them to endorse and ultimately embrace the best practices embodied in the *Women's Empowerment Principles*. Again, by engaging with the companies we own, we believe that we can advance gender equality and women's empowerment over time, and that this in turn will be good for Pax World investors.

Invest in Micro-Finance

Finally, another option is to invest a portion of your assets in micro-finance initiatives that support women entrepreneurs around the globe. We do this at Pax World, both directly and through the Calvert Foundation, supporting such organizations as Accion International, Blue Orchard Loans for Development, FINCA Microfinance Fund, Kenya Women Finance Trust, BRAC Africa Loan Fund, Pro Mujer and others.

You don't even have to wait for your mutual fund or pension fund to invest in women's microenterprise. You can do so directly by loaning money to individuals through a web site called Kiva (www.kiva.org). If you go to the Kiva website, you can meet people from all over the world—particularly women—who want to borrow money to finance small businesses. According to the Kiva website, the loan recipients are carefully vetted by on-the-ground microfinance organizations, the re-payment rate is over 98% and, of the $100 million plus in loans to some 378,000 entrepreneurs around the globe, over 82 percent of them have been women.

So, investors really can make a difference. They can invest in funds that in turn invest in companies that promote gender equality and women's empowerment; they can vote or insist that their representatives vote their proxies in favor of greater gender diversity on corporate boards; they can participate as active shareholders and engage companies to advance women; they can invest in women's micro-finance. There is a range of strategies that investors can pursue to promote gender equality.

And I might mention one last, very important reason why integrating gender factors into your investments makes eminent sense: there is a large, and growing, market.

Women today start new businesses at twice the rate of men and comprise some 43 percent of Americans with gross assets of $1.5 million or more, according to the latest government figures. They are the breadwinners or co-breadwinners in two-thirds of American households. In the United States, women outnumber men in the attainment of college degrees (by 20 percent), as well as graduate and law diplomas; 72 percent of highschool valedictorians were women last year. Women are already responsible for 83 percent of all consumer purchases; they hold 89 percent of U.S. bank accounts, 51 percent of all personal wealth, and are worth more than $5 trillion in consumer spending power—larger than the entire Japanese economy. As Newsweek reported in its July 6, 2010 issue, "women are the biggest emerging market in the history of the planet."[17]

What we are ultimately talking about is fashioning investment strategies that are responsive to and take advantage of this mega trend. The best managed companies in the world are those that are ready to take advantage of the myriad contributions women can offer. Conversely, holding back half of the world's population through unequal educational and job opportunities, unequal wages, let alone violence and oppression, is not only morally reprehensible, it's dumb economics. Businesses that ignore what women can bring to the table are handicapping themselves and will eventually fall behind in the emerging global economy. Those that invest in and empower women will be advantaged. This is becoming more and more evident.

What we are seeing is a convergence of the macroeconomic data on global development with more micro financial data on how firms and investment portfolios behave. As Robert B. Zoellick, president of the World Bank, has stated: "One motivation for women's empowerment is basic fairness and decency. Young girls should have the exact same opportunities that boys do to lead full and productive lives. But second, the empowerment of women is smart economics.... In fact studies show that investments in women yield large social and economic returns."[18]

Eliminating gender inequality and empowering women are finally being recognized, on a global basis, for what they are—urgent moral and economic imperatives. This is as true for businesses and investors as it is for broader economies. Gender equality is fast becoming an investment concept.

The next decision is ours. Are we going to take advantage of this opportunity or not? Are we going to invest in gender equality and women's empowerment or are we going to make the mistake of ignoring these vital trends?

We have a choice in the way we invest. We can take advantage of opportunities or we can ignore them. We can be part of the solution, or part of the problem. When it comes to advancing gender equality and women's empowerment, it's time for investors to become part of the solution.

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[17] *Jessica Bennett & Jesse Ellison, "Women Will Rule the World," Newsweek, July 6, 2010.*

[18] *"Ministers, Bank President, Tout Women's Empowerment as Key Development Goal," The World Bank News Release, April 12, 2009.*

Pax World Investments

You should consider a fund's investment objectives, risks, and charges and expenses carefully before investing. For this and other important information, please obtain a fund prospectus by calling 800.767.1729 or visiting www.paxworld.com. Please read it carefully before investing.

An investment in the Pax World Funds involves risk, including loss of principal.

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