Women on boards: No quotas...yet

EU to vote on controversial issue next month; INSEAD corporate governance leaders weigh in.

The European Union (EU) has postponed to November 14 voting on a proposal that could compel European companies to reserve 40 percent of board seats for women by 2020. The European Commission’s lawyers claim that EU regulators do not have the authority to mandate such targets. EU Justice Commissioner Viviane Reding - who proposed the quota mandate - said, “It took centuries to get gender equality on the map. Therefore, boardrooms can wait for three more weeks. I will not give up.”

Some commissioners said had the vote been held as-scheduled, Reding’s proposal would have been defeated. “The postponement is one more embarrassment for women, and is not timely given the current state of the EU,” commented Ludo Van der Heyden, The Mubadala Chaired Professor in Corporate Governance and Strategy at INSEAD. “I hope we will now see a softer, more inviting and symbolic proposal that raises the issue in a highly meaningful way – so that we can see strong EU
Commission support for the proposal that will come in November."

"The current drive to increase the number of women on corporate boards in Europe, even by the means of a quota, is based on two arguments: firstly mixed boards take better decisions, which will lead to better results and, secondly, women on boards will eventually lead to more women in senior management," says Annet Aris, Adjunct Professor of Strategy at INSEAD. "For the first argument more and more research is being published which is at least showing a positive correlation between the number of female directors and company results. On the second point, whether women on boards have a positive effect on female management, there is so far very little academic proof."

INSEAD Enjoins Public Comments

Last spring, Commissioner Reding called for public comment on the issue of “Gender Imbalance in Corporate Boards in the EU”. Among the respondents was INSEAD’s Mubadala Chaired Professor of Corporate Governance and Strategy, Ludo Van der Heyden. The INSEAD report was based on a survey sent to members of the school’s Corporate Governance Initiative Network (ICGI), consisting of INSEAD board members, participants in the International Directors Programme, VIP contacts of the ICGI, ICGI faculty members and HR experts.

The INSEAD report included the following key findings:

1. Gender imbalance at senior executive and board levels is global, well-documented and unacceptable from a societal view;
2. Women have the required competences for effectiveness and excellence at senior business and board levels; recognise that they can also have different career paths and face different hurdles from those faced by men; and admit that we are not talking about high numbers since there are many fewer board members than managers and executives;
3. Corporate responsibility is ultimately exercised at the board level – women’s presence at that level is the right battle and must be part of the societal agenda of business;
4. Women queried on the issue of gender diversity are very engaged on the issue - and this ought to be visibly recognised. Women see self-regulation at corporate level as having been largely ineffective, and many have regretfully come to the conclusion that regulation is now called for in view of little previous change. Men are on very soft ground when saying that the change ought and will come naturally;
5. To paraphrase the U.S. President, saying "Yes, we can" is insufficient; the time has come for the EU to take the lead by stating "Yes, we will!"

What should the EU do now?

1. Commit visibly – and with no hesitation - to the break-through goal of gender diversity at board level in the wider context of reducing gender imbalance in business and at senior executive levels.
2. Define a highly visible goal in terms of gender diversity to be reached gradually – so that business can anticipate and make gradual progress on the issue - keep monitoring the progress and express the sincere hope that you will not have to introduce quota and sanctions in the near future – yet keep the right to do so.

To read INSEAD’s full report submission that is part of the INSEAD Corporate Governance Initiative, click here.

COMMENTARY

Gender quotas for boards: how to destroy European Competitiveness

The following is a reply to the INSEAD Knowledge News Alert “Women on Boards: No Quotas…Yet” from INSEAD Finance Professor Theo Vermaelen, who is expressing his personal viewpoint.

In the middle of the economic crisis one would expect that Eurocrats would find something more constructive to do with their time than imposing absurd laws such as requiring women to make up at least 40 % of listed European companies’ boards. This law is the brainchild of Ms. Viviane Reding, the Commissioner for justice, fundamental rights and citizenship.

The fact that there are fewer women than men on boards is not necessarily proof of injustice or male chauvinism as Ms. Reding seems to imply. Typically, board members are CEOs of other companies and it is a fact that most CEOs are men. Unless Ms. Reding wants also to put a gender quota on CEOs, the board gender quota will put more people on...
boards without leadership experience in business.

Given today’s massive unemployment in Europe and fight for survival, any regulation should pass a cost-benefit test: what are the consequences of the regulation for European competitiveness and growth? After all, a board is not a social club. Board members are chosen by shareholders who expect them to maximise shareholder value.

**Consequences?**

The proponents of the law could argue that there are no negative consequences, quite the contrary: male chauvinist boards systematically discriminate against highly qualified women, so replacing men by women will increase shareholder value. If this was the case, one would expect activist hedge funds to take stakes in all-men boards, change the gender composition and make money in the process. In other words, if male chauvinism was inefficient, it would create arbitrage opportunities and there would be no need for regulation. However, I am not aware of any activist hedge fund that is involved in such a strategy.

The idea for gender quotas comes from Norway that imposed them in 2004. Evidence scheduled for forthcoming publication in The Quarterly Journal of Economics shows that mandatory gender quotas in Norway destroyed shareholder value in the short- and long-run. It is the work of two university finance professors, Kenneth Ahern, currently of UCLA’s Marshall School of Business and Business Economics, and Amy Dittmar of the University of Michigan’s Ross School of Business - one of the leading female finance scholars in the world.* The Norwegian case provided an ideal experimental setting as the announcement of the law was unexpected. On the day of the announcement stocks of companies without women on the board fell by 3.5 percent while stocks companies with women on the board did not fall. Examining subsequent performance the authors conclude that a forced 10 percent increase in women representation led to a 12.4 percent decline in Tobins’ Q. On average, the size of the boards did not increase which means that men were fired to make room for women. They find that the law brought in less experienced and younger board members, as expected. Another explanation could be that women typically care more about stakeholder value than shareholder value.** Regardless, the authors conclude (page 5) that:

“the results suggest that the constraints imposed by the law had a large negative effect on firm value”.

The findings can be explained by the fact that in Norway, a very socialist country, shareholders don’t matter so these costs are irrelevant. But then this should be made clear to European investors up front: we are going to put people on the board who don’t care about your interests or don’t know how to create shareholder value. These investors can then decide whether they want to hold stocks in companies with such a new governance model. I expect that Europe will then follow the Norwegian example: before the law was enacted, there were 600 publicly traded companies in Norway. Three years later the number was reduced to 300, reflecting the fact that companies responded to the law by going private, a fact also documented by Ahern and Dittmar (2012). So an honest argument of the proponents should be: we know that this is economically inefficient, it will destroy our capital markets, but we don’t care as this is all about fairness and equality.

**The EU evidence**

The European commission document of 14 November 2012 “Impact assessment on costs and benefits of improving the gender balance in the boards of companies listed on stock exchanges” ignores the evidence on Norway, but cites a number of studies (using data of companies that don’t have gender quotas) that show that there is a positive relation between financial performance and the percentage of women on the board. For example a McKinsey study finds that companies with women on the board have a 41% higher return on equity. If this was true, then there is no reason for gender quotas: all board members in the world should be sent a copy of the McKinsey report and any Chairman concerned about shareholder value should immediately replace men by women. The reason why this may not be happening is that correlation does not mean causality. It could simply be that women are more represented in high growth companies. Moreover as the samples are based on companies who voluntary choose women on the board the research is irrelevant for the question at hand: what happens if women are forced on the board (at the expense of men) because of EU imposed quotas. The Ahren and Dittmar (2012) paper is the only one who answers this question.

The European Union was originally motivated as a union to promote free enterprise and trade. Today it’s obvious that we moved far away from this objective. Regulating all aspects of people’s lives and using corporations to promote political pet projects, regardless of costs, seems to be the new mantra.


** Shareholders and stakeholders: how do directors
decide?” David Matsa and Amalia Miller, Strategic Management Journal (forthcoming).

Theo Vermaelen is Professor of Finance and The Schroders Chaired Professor of International Finance and Asset Management at INSEAD. Leave a comment below or reply directly to this commentary by clicking here.

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