# THE GLASS CEILING IN THE GLASS CEILING

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# THE GLASS CEILING INSIDE THE GLASS CEILING

Seven years ago, one of the co-founders of Free Float, Damion Rallis, was asked in a meeting with a portfolio manager: “Prove to me having more women on my board will improve my returns. That’s how we make our decisions.”

There are now countless studies[1] set to answer that question, both academic and investor driven. The silver bullet of “generating alpha” is capitalism’s only way of integrating a social quandary: there are huge cohorts of humans left out of power for social bias reasons. There are countless other studies showing that, when social bias can be limited, there are significant changes to the way we view excellence.[2]

At the time, though, market focus on diversity was not just myopic, it was casually indifferent to the potential of diversity. It had never been done that way. Why change now?

Damion was succinct in making the point: “Prove to me having more men on your boards improved your returns.”[3]

While portfolio managers writ large may not have turned into boardroom diversity evangelists, no matter what the anti-woke movement says, the market has moved a long way since the paltry diversity on boards in 2015. So much so that in 2022, for the first time in history, **women occupied more than 30% of publicly-traded corporate board seats on average globally.** Corporate boards now routinely and openly discuss the need for diversity inside the boardroom. While we can argue the finer points—it hasn’t happened fast enough, the progress has been astounding but insufficient, people of color are still a small fraction of that, and so on—the headlines[4] are[5] celebrating the progress[6] made so far.

But are they really worth celebrating? According to the data, there may be more women, but the data also says something altogether disheartening.

**Representation does not equal power.**

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[1] https://www.dlsu.edu.ph/wp-content/uploads/2022/09/12Altaf-082622.pdf
[2] https://journals.sagepub.com/doi/abs/10.1177/237946152000600108
[3] The answer to which was, “we can’t, but…”
[4] https://www.msci.com/research-and-insights/women-on-boards-progress-report-2022
[5] https://www.reuters.com/business/sustainable-business/women-make-up-40-boards-top-uk-companies-first-time-2023-02-28/
[6] https://www.pionline.com/governance/mscis-women-boards-report-shows-slow-steady-progress

# 1 MEASURING POWER

The blunt instrument of "body count"—and the emphasis on disclosing and collecting body count data—is just that: a blunt instrument. Whether it's the "magic number" of at least three women on the board or a magic percentage of 30%, more people in the room might increase the *odds* a diverse cohort absorbs boardroom power, but it doesn't *guarantee it*. And the data, in fact, contradicts it.

Power is derived from sources beyond representation. A seminal paper by Triana, Miller, and Trzebiatowski, *The Double-edged Nature of Board Gender Diversity: Diversity, Firm Performance, and the Power of Women Directors as Predictors of Strategic Change*,[7] outlines the problem succinctly:

> When boards are demographically diverse (i.e., heterogeneous), they should be able to provide diverse information and knowledge to direct the firm (Geletkanycz and Hambrick, 1997; Goodstein et al., 1994). However, there may be critical political factors that can affect a diverse board's ability to impact strategic change.
>
> One potentially critical moderator that has received little attention with respect to board diversity is the role of director power. Based on what we know about power, or the ability of individuals to exert their will (Finkelstein, 1992; French and Raven, 1959), not all directors have the same level of influence on the firm's strategy.

Finkelstein established the four sources of power in *Power in Top Management Teams: Dimensions, Measurement, and Validation*[8] in 1992: structural power, ownership power, expert power, and prestige power. The major limitations of measuring power since Finkelstein's paper in 1992 has been data availability and a scalable methodology. There was no natural language processing to extract potential expert indicators, and there was no effective way of putting a number to "prestige" across people and markets.

Free Float Analytics solves this problem by pulling from a wide range of academic research, from Finkelstein to Trzebiatowski to primatology[9] (how alphas are identified by ape populations), and combining it with sports analytics[10] to create a way to measure how influential each individual director is on a given board in a given year.

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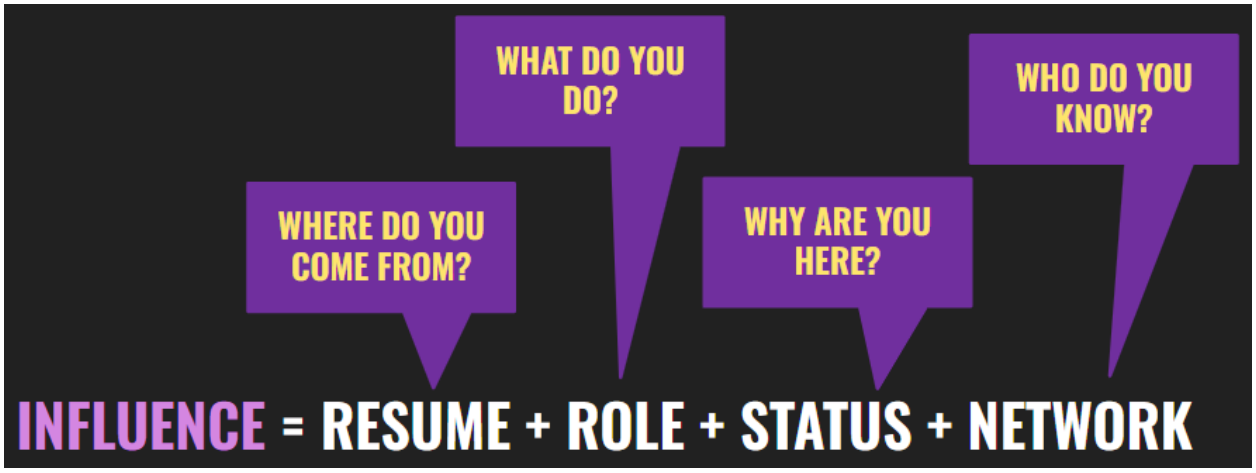
[7] https://www.jstor.org/stable/43663431
[8] https://pubmed.ncbi.nlm.nih.gov/10120413/
[9] Like Andrew J.King, Caitlin M.S. Douglas, Elise Huchard, Nick J.B. Isaac, Guy Cowlishaw; Dominance and Affiliation Mediate Despotism in a Social Primate. 2008. https://www.sciencedirect.com/science/article/pii/S0960982208014176
[10] Like those created by Bill James, https://sabr.org/sabermetrics




Bill James pioneered baseball analytics, called sabermetrics, in the 1970s and 80s, by developing a range of statistical concepts to identify each individual player's contributions to team performance. Free Float Analytics uses elements of power similar to Finkelstein: resume, status (as, say, a large shareholder or an insider), role, and social network, plus a version of Bill James' "win shares"—a measure of an individual player on a team's contribution to a win—to create a system to estimate power dynamics in the boardroom. Essentially, Free Float Analytics does the "cachet accounting" across the lifecycle of a director: how they got there, their expertise, their lineage with the company, and the titles they hold. After assigning "wins" to more than 200,000 directors at 9,000 publicly traded companies across 30 different data points, we can begin to answer: *Who (most likely) commands the boardroom?*

**Spoiler alert: It's not women.**

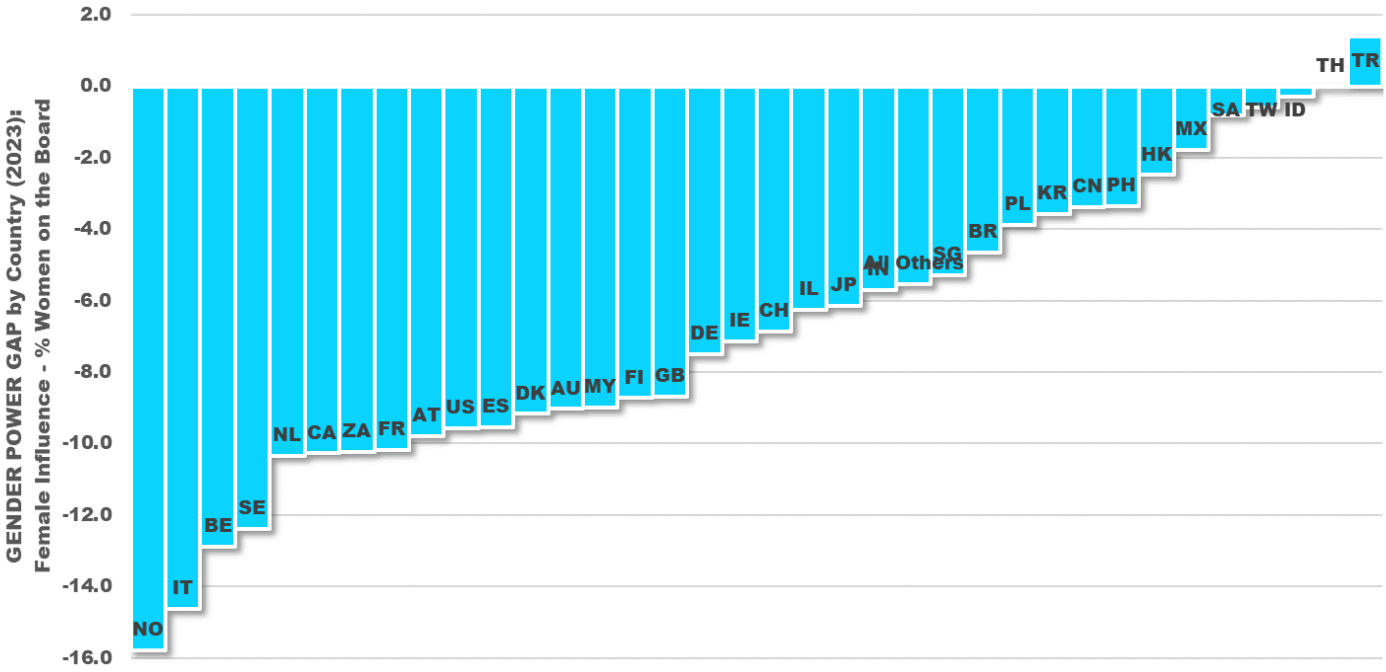
## 2 THE IMPLICATIONS

Globally, the average publicly traded, large cap company board is 10 people large. In a perfectly egalitarian board, each director might have 10% of the board's influence. In reality, that actually never happens. Directors have seniority. They are assigned hierarchical roles—some have equity stakes, while others do not. There are hundreds of combinations and factors that accrue to a board member's individual influence, but even in all these combinations, one thing remains true: **at 71% of publicly traded companies, women have less power than representation**.

Worse (part 1): the size of the power gap is not just consistent, but correlates to gender quotas at the country level. For instance, Norway was the first country to introduce a gender quota on boards at 40%.[11] While compliance with body count has largely not been an issue (proving there are, in fact, women to put on boards), power most definitely **is** an issue. Norway has the highest power gap of any country at nearly -16%, meaning that if the average board of a Norwegian company has 40% women, those women control, on average, just 24% of the influence. In an

[11] https://link.springer.com/chapter/10.1007/978-3-319-56142-4_2

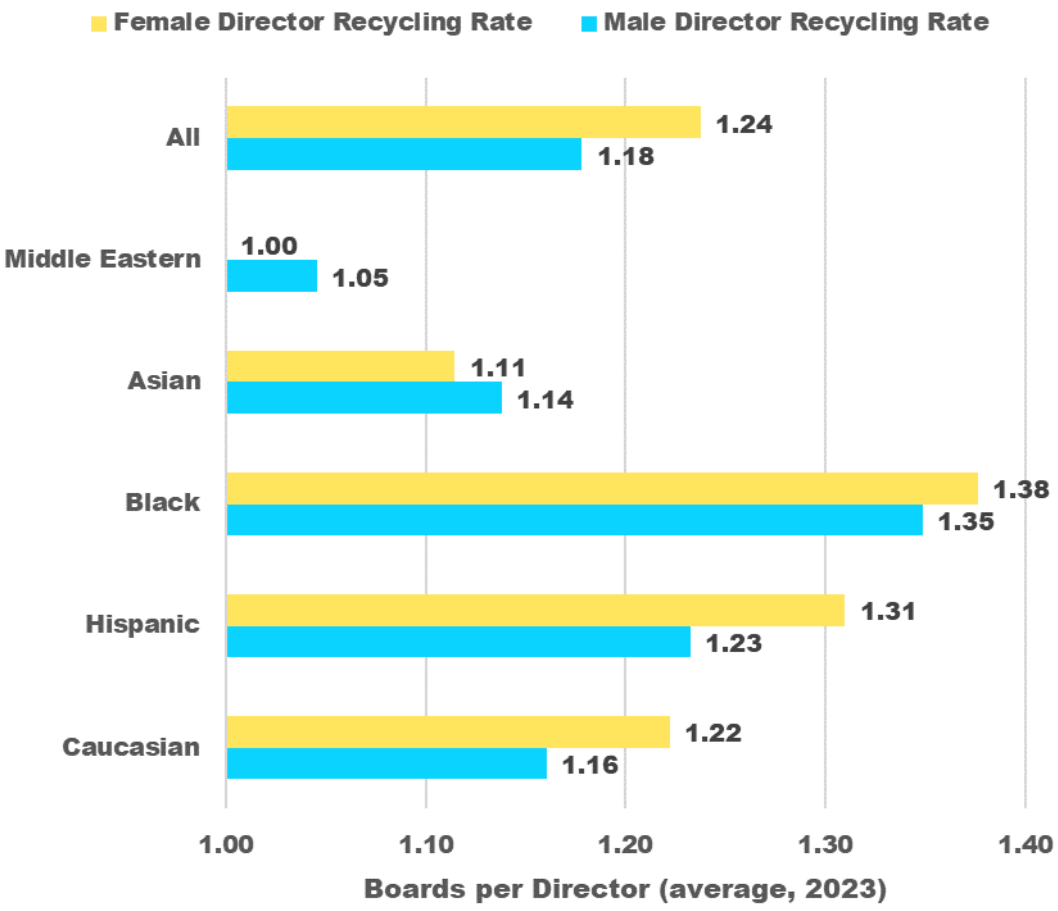
odd (yet intuitive) way, countries that largely (and historically) eschew having women on the board at all tend to perform better on power gaps. For example, Thailand and Turkey, not known as places for women to go for equality on corporate boards, tend to have fewer women, but treat them equally where they exist.




Worser (part 2): opportunities are not what they seem. MSCI recently noted that the new push is for 40% women on board[12] given the progress that's been made to date, and while this is likely to necessitate some growth of the talent pipeline, it doesn't guarantee it. In fact, if history is our guide, the talent pool will have much slower growth as long as companies recycle directors.

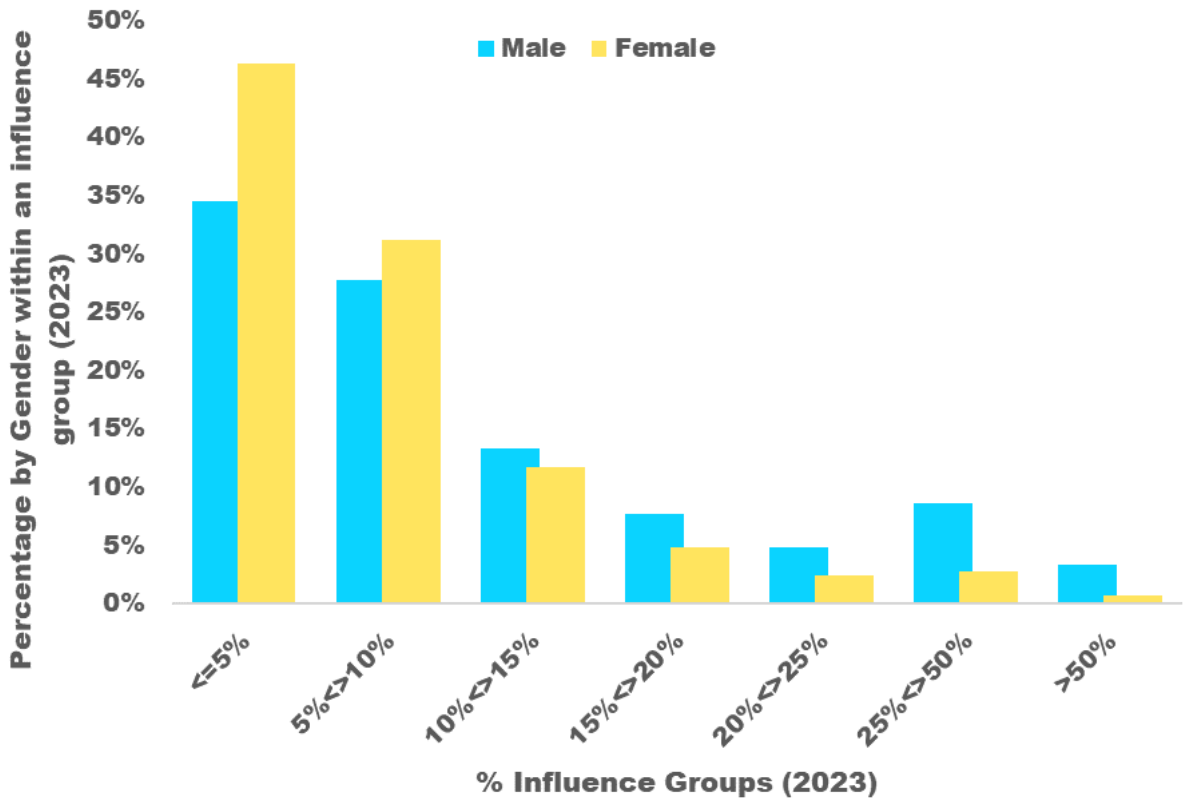
If you focus on the S&P 500 where diversity data is arguably the strongest, women are recycled at a higher rate than men across virtually every diversity demographic. It seems unintuitive to think that women occupying more boards per person is *bad*, but what it suggests is rather than tapping the enormous potential pools of female talent, boards have been content to go with "known quantities." Women have 5% higher recycling rates than men, and being a Black women on a board means you are actually 20% more likely to get more board seats than your white male counterparts.

[12] https://www.msci.com/www/blog-posts/40-women-on-boards-the-new/03679268344




The implication to that gap can be seen in the actual influence data, as well. Despite having women with more experience (given their recycling rate), those women are kept in positions of low influence.

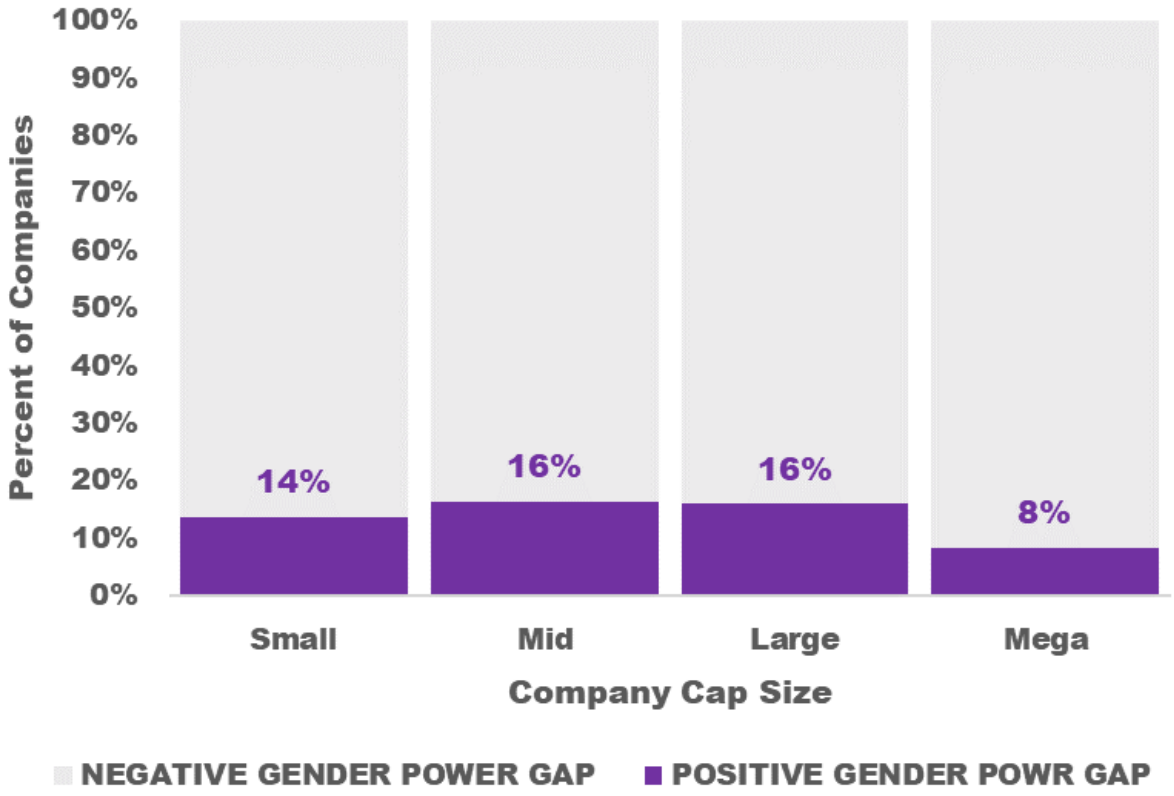
Which brings us to worstest (part 3): power concentrations on boards are uniquely correlated with gender identity. Across every cohort of diversity (for our data on S&P 500 companies), and globally across every company, the **only correlation that holds is that women have less power than men**. For instance, 46% of women have 5% of board influence or less, compared to 34% of men. The same is true between 5-10% influence: 31% of women sit in this low influence zone while 28% of men do. Overall, a whopping 77% of female directorships have 10% or less influence over their boards compared to 64% of male directorships.




To hammer home the point, the other end of the spectrum—high influence players—is almost exclusively male. Nearly 1 in 5 men (17%) have 25% or more influence; effectively, 17% of men account for more than a quarter of their boards' decision-making power. Meanwhile, just 6% of women have the same level of influence.

## 3 THE UPSHOT

While the numbers are not pretty, there are always outliers to the rule, and in some cases, they're not that outlying. According to our data, globally 14% of small cap companies actually have positive gender power gaps, meaning women command more influence than percentage body count. (This includes only companies where women are, in fact, on the board; fully 15% of small caps globally have no women at all on their boards.) That number is 16% for both mid- and large-cap companies globally, as well. In fact, the biggest outlier is mega-cap companies. It's more than a little ironic that the largest companies that are often the biggest champions of diversity have a scarcity of gender power. Only 8% of mega-cap companies, half the number of large cap companies, have achieved positive power gaps.

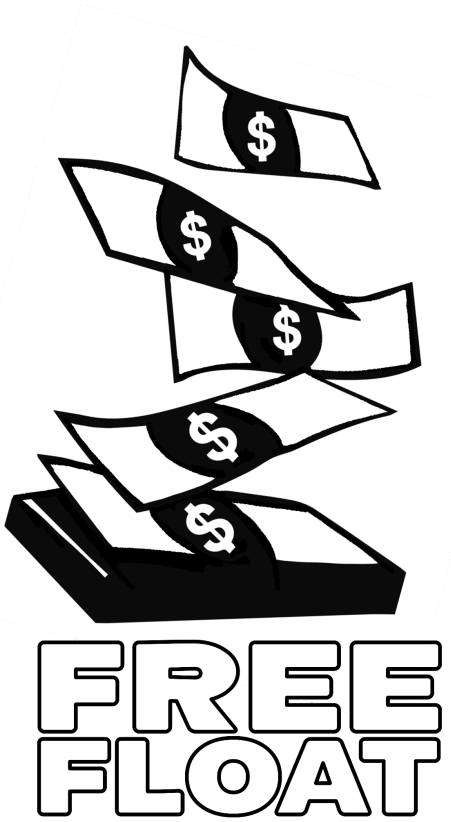



This leaves investors who have targeted diversity—primarily gender diversity—in a quandary: do you continue to focus on a percentage of people in the room, or do you pivot toward a focus on the roles those people take?

In the S&P 500, there are only 67 companies where the gender power gap actually skews *towards* women. Even the largest companies in the world who have done an excellent job of adding women to their boards have yet to add diverse power. The "ask" here of companies and boards is much trickier, and arguably more aggressive, a tact the large stewardship groups are generally loath to take. However, the paper by Miller et al. suggests that power does have a relationship with performance, particularly when times are good and boards aren't defensive to strategic change:

> "During times of low firm performance, having powerful women directors results in the most negative relationship between board gender diversity and amount of strategic change. However, when firm performance is high, having powerful women directors results in the most positive relationship between board gender diversity and amount of strategic change."

**In the end, it's a question of what investors want. For those seeking change, body count is just the starting point. But influence might be the goal.**

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