ESG: Women: the X-factor

Part I: ESG: Why Are Women the "X-factor"?

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Bank of America Merrill Lynch

Candace Browning

Head of Global Research
BofA Merrill Lynch Global Research

Savita Subramanian

Head of U.S. Equity & Quantitative Strategy
BofA Merrill Lynch Global Research

Candace: Women have more economic power than ever before, but society has a long way to go before women's economic potential is fully realized. If we could erase the gender pay gap tomorrow, the global economy could grow by as much as $28 trillion in less than a decade.

I'm Candace Browning, Head of Global Research at Bank of America Merrill Lynch and I'm here today with Savita Subramanian, Head of U.S. Equity and Quantitative Strategy at Bank of America Merrill Lynch. Savita and her team recently looked at how the lack of equal representation of women at all levels of management can affect everything from a company's performance to its return on investment. Savita's report called "Women: the X-factor," shows the huge impact women are having on the economy, the workplace, and financial markets. Welcome, Savita.

Savita: Thank you, Candace.

Candace: So Savita, could you start maybe by giving us a simple definition of what is the X-factor?

Savita: We were kind of riffing on the X chromosome, which was one of the reasons that we use that title, but it's really this sort of unknown factor or this extra factor that's driving changes. Women are actually driving a lot of change, and companies that show a greater focus on gender diversity are actually outperforming relative to their peers.

Candace: Now, Savita, you're a quantitative analyst, and as such you're focused on the monetary returns of stocks. But here you've actually used gender equality to help you understand and analyze returns. That doesn't seem like an obvious place to start from. What actually inspired you to do this research and to ask these questions?

Savita: Candace, this is really a departure from kind of traditional quantitative analysis where we look at financial data and try to figure out whether it's predictive of returns and results. But, you know, part of the impetus for this study was that we've looked at all the financial data in a lot of different ways. The financial data's become a little more commoditized.

So we've been increasingly focused on issues that aren't necessarily captured by the standard financial metrics. And it seemed to us like companies that embrace and encourage different perspectives would fare better than those that didn't. So we effectively tested this theory in various ways. One way was by looking at gender diversity, and that's really what spawned the X-factor report.

Candace: What did you discover about how women are driving change in education, in the labor force, in the home and in the world?

Savita: There's lots of big changes that we are seeing, just from the advent of women really entering the workforce in a much more profound way than we've seen in prior decades. Since the mid '90s, there are now more women with a bachelor's degree or higher than there are men. So this is the first time in the history of the data that women are arguably, you know, more formally educated than men in the workforce.

Savita: The number of women in the global workforce grew by 20% over the last decade. This is a huge growth rate. Women are also the sole or primary breadwinner in a record 40% of all U.S. families, and this is driving a lot of change in behavior from a consumption level to an investment level. Our economists' work suggests that women are spending more time working, less time on household chores. And what that suggests is that there's a lot more outsourcing of these tasks. But it also reflects the fact that women are doing a lot more online and very efficiently.

Candace: The data says that women have a very strong desire to invest in ways that promote social well-being. Is the same true for men?

Savita: Investing in ways that promote social well-being is important for both women and men. But I think what we noticed in our research in kind of a broader scale is women, millennials, high-net worth individuals, institutional investors (like pension and endowment funds) are increasingly concerned about allocating their capital towards responsible investments. And this isn't just from an altruistic perspective, but it's also from a risk reduction perspective. There is a huge potential impact on the market and on the economy. 44% of U.S. women make decisions about financial assets in their households...74% of women, globally, which is interesting.

Candace: So let's delve into just a little bit more, Savita...some of the, you know, the work that you did in the X-factor report itself.

Savita: Gender parity is becoming a much bigger focus of U.S. corporations and of global corporations. But we're still at a point where women earn only 83% of what men earn in the U.S. And this is basically across full-time and part-time positions. World Bank estimates that it would take 170 years to reach equal pay if we improved that....if we close that gender gap at the same rate that we've been going.

So we think that it's gonna happen a lot quicker going forward. I think the other area where we really should and could see a lot of change is at the C-suite level of corporations. Women now make up less than 4% of CEO jobs globally, 10% of CFO jobs globally, and we've got female CEOs in just 5% of S&P companies. So this is up from 2% in 2010. This is getting better. But, it's still a lot of work to be done here. And it's pretty surprising, but a good 1/5 of companies in the U.S. market have an all-male executive committee.

Candace: So, Savita, on that note, do you actually see indications that companies are changing how they operate? Are they actually beginning to think more about creating programs that promote diversity or improving their, you know, environmental statistics?

Savita: It's a pretty big reaction that we're seeing amongst corporations and it's taking different shapes and forms. CEOs should care about these aspects because, basically, their shareholders care about these aspects of corporations. One great example of this is with the retailers. So our analyst, Lorraine Hutchinson, has highlighted the lack of board diversity in specialty retail stocks, which she covers. And this is an industry that targets mostly young women. So boards are surprisingly old and male. And in her view, board diversity might have saved this industry from some of its challenges, be it, you know, shifting to online....changing behavior of consumers...you know...more price-sensitive shopping.

In our work, we found if you just took a broad swathe of stocks and you looked at which stocks had gender diversity and which didn't, we found that gender diversity amongst executives, board members, and managers consistently suggested higher returns on equity. Also, consistently suggested lowered price volatility and lower earnings risk. These are factors that investors care about.

Savita We also found that companies that place a bigger emphasis on future diversity and in hiring trends enjoy consistently lower price and earnings volatility. And interestingly this trend was very strong within tech companies. So technology is an industry that thrives on innovation. It thrives on human capital retention. And it thrives on really thinking differently.

Candace: Well, that certainly proves, Savita, that if you're a CEO or a portfolio manager or just a shareholder in one of these companies, you really should care about this data.

Savita: Absolutely. Everything that we worked on for these reports suggested that we're in the very early innings of these themes really percolating and kind of cross-pollinating the investment landscape.

Candace: Which would make me think that you are optimistic that these trends have real staying power. If that's true, you know, what can companies, and we as individuals, do to, you know, keep this momentum going into the future and to expand it?

Savita: I'm very optimistic, Candace. I think that that these metrics make a ton of sense from a very basic, fundamental level. And that's the idea...that a company with less risk deserves a higher premium. And one way to mitigate risk, and we've seen this empirical linkage in our work, one way to reduce your risk is by having checks and balances, not just at the top of an organization, but throughout the culture of an organization. So it's really in everyone's best interest, be it CEOs, boards, employees, investors, shareholders, you know, all of us should be promoting these characteristics.

So these are all contributing to this sea change in the investment landscape, which is really driving allocations of funds into responsibly-run companies. Assets in U.S. funds and ETFs that are focused on gender diversity or equality have grown at a staggering 80% annualized rate over the last three years.

So money is moving based on these attributes, which makes me think that these indicators are valid and drive results in a very meaningful way. It's not just an investment fad, but this is something that has actually proven to deliver results and should continue to do so in the future. And we also noticed in some of our work that, you know, corporations are starting to adopt these policies. But by shareholders encouraging these changes, this creates a much more virtual cycle for corporations to actually start to disclose the information that investors care about.

Candace: Savita, thank you for sharing your insights. It seems clear that women are an economic X-factor that can no longer be ignored, and their enormous potential is just beginning to be recognized. And the benefits aren't just for women. They're for the world. So thank you again, Savita, for the conversation and for your work.

Savita: Thanks, Candace.

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