BofA SECURITIES

Everybody Counts: A Diversity & Inclusion Discussion

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Candace: Hello everyone and thank you for joining today. I'm Candace Browning, Head of BofA Global Research and I'm joined here today by Haim Israel, who's the Head of our Global Thematic Research effort and Savita Subramanian who's Head of Quantitative Research, Equity Strategy as well as ESG Research at BofA.

So today, we're going to talk about a primer that Haim and Savita have written about diversity and inclusion, and the title of the primer, which I think is great, is "Everybody Counts." So we're going to have a conversation about why everybody counts and what the benefits are that can be derived, not only for society, but also for markets and investors, from investing in diversity and inclusion.

In your primer, you talked about the fact that while diversity is important, inclusion is really key. So can you talk a little bit about what you meant by inclusion?

Haim: Sure thing, Candace. And you're completely right. One cannot go without the other and that's the key here in our primer. First of all, we said in our primer that diversity is having a seat at the table but inclusion is having a voice. Most companies in the S&P 500 have a policy around diversity, but not everybody have around inclusion. So we need to have a more diversified workforce, societies, communities and so on. But how do we do that? There's an economic price tag on that. Just in the United States, in S&P companies, there's roughly around $450 billion to $550 billion of economic costs, which are related to unsatisfied diversity and inclusion policies around that. That said, everybody always have a diversity policy. But when you do not have an inclusion policy which is satisfying enough of the workforce, we see lower satisfaction. And today, the culture satisfaction at work is the most important topic when you are choosing work. A workplace is actually two times more important than your actual pay. So if you do not do that right, you are actually missing a lot.

Candace: Savita, investors frequently think that they're going to have to give up some of those, you know, very high returns if they invest in companies that are highly diverse. So but you pointed out, in fact that that is absolutely not the case in the primer.

Savita: The cynics out there think that focusing on diversity and some of these sort of so-called softer aspects of the company are concessionary. You have to concede returns in order to do the right thing. And again, our research finds the absolute opposite. So what we've found is that companies that have diversity of thought leadership, be it gender, persons of color, school, you know, background…these are very, very important attributes in terms of avoiding serious governance missteps. And I think that that's the real critical linkage here is that what gender diversity does is it brings a different level of thought leadership and checks and balances to the top of the house. And what we found is that that's actually a great risk mitigator.

What's also interesting is that we found that gender diversity, and persons of color or racial, and ethnic diversity are more important or seem to have a stronger linkage between future ROE in sectors that are business to consumer. And I think that really what that's bringing out is the fact that when you have a leadership team that is completely disconnected with the end consumers at a corporation, you're not necessarily going to have the best, you know, strategy around supporting customers and driving the business. So what we're seeing is that there is a very strong linkage, just increasingly so, between diversity and return, between diversity and alpha. And I think this is all telling us that this is not just a nice to have component of your investment decision, but it's actually a very necessary component of how we think about stocks.

Candace: How much capital have we sacrificed by not including everyone in our potential workforce? I think you've done some estimates around that.

Haim: It's in the trillions of dollars. And there's a lot of different estimates. If we will completely harness diversity and inclusion into the U.S. economy, the U.S. GDP would grow since the '90s by $70 trillion. $70 trillion is give or take the global GDP today. That's how much that we are missing. And there are a lot of very different numbers out there, which actually break down this $70 trillion. But now I'll give you a couple of examples. Today, the U.S. Latino community, if we just take them, they're the eighth largest economy on the planet. So if we completely integrate them into the society, we are talking about between $15 trillion to $20 trillion. If we take LGBTQ, that is the fourth-largest economy in the world with a total GDP of close to $3.9 trillion each and every year.

Candace: Those numbers are just huge, Haim. It reminds me also that the numbers, I think, going into ESG funds and funds that look at these kinds of metrics, is also huge. So Savita, could you talk a little bit about the amount of money flowing in and what the impact of that might be over a long period of time?

Savita: It's kind of staggering to look at just the investor interest in ESG, impact investing, you know, sustainable themes in the marketplace. Just to wrap some numbers around it if you look at just this year, $4 of every $10 that moves into global equity funds was diverted to ESG funds. So basically, almost half of money moving into the market is being invested in funds that pay attention to diversity and inclusion, to environmental risks, to governance risk. ESG funds have seen the strongest asset growth out of any of the categories we look at: growth, value, income.

Well, last year, we had a bear market. And we had the opportunity to see how investors behaved during that stress period. And what we found was…we saw outflows from almost every other risk asset class you can think of: equities, credit. Folks were just moving money out of the market and moving into cash, with the sole exception of ESG funds, which continued to see inflows during that super quick bear market that we experienced in 2020. So I think what a lot of this points to is that this is a sticky investor base, that investors are realizing that ESG is not a bull market phenomenon, but it's actually a bear market necessity.

Candace: I'd like to talk a little bit about the economy. We're already starting to see some shortages in some areas. What might that mean in terms of D&I? Will it be helpful to D&I?

Savita: Some of these aspects that haven't necessarily been thought of as critical to talent retention are going to become even more compelling. Think about the U.S. economy. More and more jobs are within technology and healthcare, which are high-skilled labor forces, and talent retention is paramount within those areas of the market. So if you think about the biggest risk for an innovator, for a company that innovates, is to lose their super smart talent to a competitor.

I think what's also interesting is that when we're looking at the data that we can scrape from various sources, what we're finding is that culture, as an organization, is most correlated with overall job satisfaction by employees. And when you think about culture, which is this ineffable, kind of undefinable characteristic, a huge part of it is what the workforce looks like, how openly you feel like you can converse with your fellow employees and a lot of that has to do with diversity of thought. You can't just tick the box and create a great culture for your organization. It's a much more complicated endeavor and I think that that's what companies should be focused on today.

Candace: Let's switch gears just a little bit and talk about consumers. And in particular Haim, I'm interested in Gen Z consumers and what they think about diversity and inclusion and I think you've done some work on that?

Haim: Oh yeah, we did a lot of work around Gen Z because we see them as a very disruptive generation that is coming, and I believe that they're going to be the crusaders when it comes to D&I. First and foremost because they are big, big believers in ESG. More than 90% of them say that ESG or the fundamentals of ESG, is going to be the criteria that's going to lead their investment decision, that's compared to roughly 48% of the boomers, so it's almost double.

Today, they have seven trillion dollars at their disposal as a net income. That is not a lot of money. That's 10% of global GDP, worldwide, but by the end of this decade, we believe that this is going to go up five times to $33 trillion, passing millennials. And if you also take into account the money that they're going to inherit from the boomers—the great transfer of wealth—that could be above $50 trillion dollars at their disposal by the end of this decade, meaning more than boomers, more than any other generation and they will put this money to work.

Candace: Haim, you decided to write this primer. We've been talking about diversity and inclusion for a very, very long time. What's happening that's different and are you optimistic that we're going to see some real change here?

Haim: I am very optimistic. Let me give you the analogy around climate change. We knew about climate problems since the 70s, for the last 50 years. But I was asking myself what happened that in the last 12 months we achieved more progress on climate change than we did in 50 years. And the answer is the capital markets. Capital markets have got involved and got involved big time. The amount of money that Savita outlined ($4 out of $10), expectations of $20 trillion of ESG assets by 2025 and the corporates which are moving that way…this is what seems to be in the equation. We have Gen Z which is now starting to get into the economy and will put to work $50 trillion. And we have the investors which are scrambling for yields. Once the capital market got involved, and I'm a big believer that Wall Street is there to get involved, things are going to move very, very fast. That's why I'm so optimistic.

Candace: Well that's great and I hope you're right and so do a lot of other people, because as you said in the title of your primer, everybody counts.