

Vanguard Investment Stewardship Insights

Diversity in the workplace



December 2020

Vanguard publishes *Investment Stewardship Insights* to promote good corporate governance practices and to provide public companies with our perspectives on important governance topics and issues that come up for shareholder votes.

This annual review of our policies and expectations of portfolio companies takes place amid increased awareness of the acute problems and long-term risks of systemic inequality. We have seen greater attention paid to issues of diversity, equity, and inclusion, and we believe they will remain a topic of intensified focus in the 2020–2021 proxy year. We anticipate that many shareholder proposals, too, will focus on this theme.



Vanguard's views on diversity extend beyond the boardroom to leadership teams and workforces. As firms compete for employees with the right skills and experience, they face greater pressure on how they attract, develop, and retain their workforces.

This Insights piece outlines our expectations of boards on a range of workforce diversity, equity, and inclusion matters, including how our views on this topic will affect our engagements and voting.

Our workforce diversity expectations of public companies

Strengthen oversight of diversity-related strategy and risks. We look for companies to publish policies on employee recruitment, retention, and inclusion. We expect them to outline the steps the board is taking to ensure that employees feel they can succeed.

Disclose diversity measures beyond the boardroom. We seek disclosure of workforce diversity measures (gender, race, and ethnicity) at the executive, nonexecutive, and overall workforce levels. Globally, companies should reflect these and other categories appropriate to their local jurisdictions, industries, and company-specific needs.

The case for getting it right and the risk of getting it wrong

For many companies, their most valuable asset isn't a patent or a product. It's their people. Boards oversee strategy and risk, but it's the workforce that executes that vision. Companies and their boards should demonstrate how workforce diversity is integrated into their broader talent strategy. Human capital management matters are critical to a company's long-term success, and boards should provide appropriate oversight of them.

Getting this right has its upside. Studies have shown that diverse groups make better decisions, which can set in motion a virtuous circle that enables a company to innovate, seek out new customers, or enter new markets.¹ Studies have also found that companies that make diversity and inclusion central to their corporate culture can be more productive (as measured by revenue and market value) than firms that don't, because employees feel welcomed and set up for success.²

And getting this wrong comes at a steep cost. The competition for employees is fierce. The top talent of tomorrow will find employers who consider employees' needs and get diversity and inclusion right. Furthermore, talent pools are—and will become—more diverse than ever before. Companies that fail to include a wider array of individuals will miss out on large portions of the talent pool and put their long term success in jeopardy.

Reputations and operations are also at stake. When a company makes significant missteps on people and diversity-related matters, it can result in product boycotts, employee turnover, reputational damage, lawsuits, and regulatory investigations. Its brand may incur lasting damage, both as a business and as an employer.

¹ Hewlett, Sylvia Ann, Melinda Marshall, and Laura Sherbin, December 2013. How Diversity Can Drive Innovation. *Harvard Business Review*.

² Turban, Stephen, Dan Wu, and Letian Zhang, February 2019. When Gender Diversity Makes Firms More Productive. *Harvard Business Review*.

Considerations for boards' workforce diversity strategies

Vanguard recognizes that companies will differ in their specific goals, programs, and challenges when it comes to workforce diversity and inclusion. We seek to understand how a company's approach aligns to its strategy and how current and future risks are assessed. No matter a company's approach, it is important that its board establishes clear oversight processes and provides sufficient disclosure. Boards should also be aware that, over the last few years, we have seen an increase in shareholder proposals that request disclosures on workforce diversity measures and other equity and inclusion-related matters such as gender pay gaps. We expect this trend to continue.

We encourage companies to consider and make progress on at least the following elements of diversity, equity, and inclusion:

- **Strengthened oversight of diversity-related risks and strategies.** Boards should ensure that their management teams provide an appropriate line of sight into diversity risks and strategies. Boards should expect management teams and senior leaders to have long-term views and strategies on diversity and to be accountable for progress. A strong workforce diversity strategy goes beyond measuring and disclosing workforce demographics. Boards should expect management teams to assess other factors, including how long employees are staying in their roles, pay inequity among diverse groups, whether high-potential employees are being appropriately identified and developed, and whether company culture allows all employees to succeed.
- **Disclosure of workforce diversity.** Specific, comparable disclosure on management and workforce diversity allows for insight into progress over time and clarity on a company's current state. In the U.S., this should include breakdowns by gender, race, and ethnicity, at least at the board, executive, nonexecutive management, and workforce levels. Globally, companies should reflect these and other categories appropriate to their local jurisdictions, industries, and company-specific needs. Widely used frameworks provide helpful starting points, including those from the Sustainability Accounting Standards Board and the Employer Information Report (the EEO-1) that's required for most of the Vanguard funds' U.S. company holdings through the U.S. Department of Labor.

Questions for boards to consider

Vanguard intends to engage with company boards and leaders more frequently on workplace diversity. Through such meetings, we are able to share our perspectives and learn how boards oversee the risks and opportunities related to human capital management. These conversations—and the public disclosures that companies issue—may also inform the way the funds vote on shareholder proposals.

Below are some typical questions we might ask directors during an engagement. We share them here in the spirit of disclosure, and in the hope that boards and leadership teams may find them useful, even if they are not engaging with our team.

- What role does the board play in shaping the company's culture and workforce?
- What reporting does your company provide on workforce diversity? What improvements or additional workforce disclosure is the company considering?
- Does your company have functions or specific executives responsible for implementing and supporting diversity, equity, and inclusion programs?
- Where in the "life cycle" of an employee do you see your company having the greatest risks or advantages in attracting, developing, and retaining talent?
- Does the board monitor diversity-related risks outside of its immediate workforce, such as in the company's supply chain?

From our discussions with boards, we gain an understanding of how they have prioritized workforce diversity. That feedback enables us to understand a board's grasp of its diversity risks and opportunities and where the company is on its journey toward a more diverse workforce.