Good corporate governance requires diversity

A hallmark of our era of disruption, populism and apparent de-globalisation is the erosion of **trust** in organisations and institutional systems. Trust is gained through better governance, which in turn is built on transparency, accountability and openness to diversity.

It is no coincidence that both Singapore and the UK issued new codes of corporate governance this year. Reinforcing systems of good governance attracts investment and represents sound risk management. Conversely, failure of corporations to include long-term multi-stakeholder considerations can rapidly erode trust in the system.

At its core, corporate governance rests on two pillars: risk governance and change governance

Today, the nature of risk faced by businesses makes it difficult to extrapolate from past performance. Nokia and Blackberry had more than half the share of their respective markets as recently as ten years ago. The fact that Amazon is now worth more than Walmart suggests that a start-up today could be larger than Citibank in fifteen years' time. The geo-politics of trade war and tech-driven disruption has turned risk into uncertainty.

Risk preparedness requires systems and processes that can cater to a wider range of possible scenarios. In the face of a larger set of material unknown unknowns, it also requires a more complete interrogation of possible blind spots in a company's strategic plan. A balance must be struck between avoiding wasting resources and retaining strategic optionality.

A professional culture of diversity must underpin risk- and change governance

Diversity needs to be explicitly valued and proactively designed.

In their recent book titled "Meltdown: Why Our Systems Fail and What We Can Do About It", Chris Clearfield and Andras Tilcsik remind us about the failed blood-testing company Theranos and the composition of its board. (*Read Clearfield and Tilcskik's blog post about the book here.*). Valued at over $8 billion as recently as 2015, the company collapsed when it transpired that the underlying medical technology did not even remotely perform as advertised. Some of the board members were former Secretaries of State Henry Kissinger and George Shultz, former Secretary of Defence Bill Perry, retired General James Mattis and retired Admiral Gary Roughhead among others – all highly accomplished individuals.

There are several observations to be made about this board. Firstly, with the exception of the chief executive, this was an all-male board. There was no gender or racial diversity. Secondly, the average age was 76 years. Unfortunately, lack of age diversity is quite common in boards, which can be inconsistent with the new-age disruption that they face. Thirdly, Theranos' board showed an apparent lack of diversity in expertise. Most were military officers, senators and former cabinet ministers: none with any obvious medical or technology experience.

It is important to highlight that the optimum amount of domain expertise is *not* one hundred per cent. Clearfield and Tilcsik point out a study of US community banks that shows that the banks that failed had *more* bankers on their board of directors! Banks whose directors came from a wider range of backgrounds such as doctors and military officers were apparently saved by their diversity in expertise.

This underscores the dual role of diversity

Firstly, diverse backgrounds and cognitive styles can help unearth issues that might be lost in homogenous group-think. Secondly, the presence of non-experts has the effect of slowing things down and bringing up challenges to consensus amongst insiders. While this might at times feel unnatural, uncomfortable or unnecessary, deliberately designed diversity is invaluable from the perspective of risk governance.

Malcom Gladwell, in his book "Outliers", points out the importance of allowing constructive conflict in the cockpit to reduce the risk of plane crashes. Risk committees in banks can also experiment with designing approval processes in a manner that sweeps across all perspectives. For example, a version of Edward de Bono's Six Thinking Hats (where each hat separately represents the perspectives of overview, facts, optimism, pessimism, creativity, and emotions) can be more effective in surfacing risk issues than more standard ways of conducting meetings.

Diversity is an explicit requirement of governance codes around the world. Singapore's MAS requires that banks have an explicit policy around diversity and periodic reporting on how they are performing against that policy. In the UK, the "30 per cent club" was launched a few years ago. It is a voluntary statement of intent to have women make up at least 30 per cent of the top listed companies.

As of June 2018, FTSE 100 companies already have 29 per cent female directors against 12.5 per cent in 2011. The proportion is lower in Singapore, although it has been rising in recent years. According to the Diversity Action Committee, among the largest 100 listed companies in Singapore, women accounted for 14.7 per cent of the directorships in June 2018 against 12.2 per cent a year earlier.

Gender inclusion is a necessary condition for diversity. With real intent and deliberate action (for example, by simply avoiding all-male panels in professional conferences), we can collectively move the needle. This is not just the right thing to do. It is a stepping stone towards better governance.

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Notes:

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Date originally posted: 2018-11-12

Permalink: http://blogs.lse.ac.uk/businessreview/2018/11/12/good-corporate-governance-requires-diversity/

Blog homepage: http://blogs.lse.ac.uk/businessreview/