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**The Business Case for Equality and Diversity: a survey of the
academic literature**

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Department
for Business
Innovation & Skills

BIS OCCASIONAL PAPER NO. 4

**THE BUSINESS CASE FOR EQUALITY
AND DIVERSITY**

A survey of the academic literature

JANUARY 2013



Government
Equalities Office

Putting equality at the heart of government

ECONOMICS

The Views expressed within BIS Economics Papers are those of the authors and should not be treated as Government policy

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Foreword

In difficult and challenging economic times, using the talents of the whole workforce is more important than ever. Considering the diversity of your workforce and fostering an inclusive working environment can bring business benefits and provide a market advantage in economically straightened times. This tough climate has led us to take a fresh look at the evidence helps us understand how diversity usefully feeds into evidence based policy-making and has positive impacts for businesses.

A real strength of the UK is our labour market flexibility and making the most of everyone's skills, working patterns and potential is vital for success. The UK is considered to be one of the most diverse nations in the world. Respecting that diversity and being inclusive gives firms the widest possible pool of talent and competitive advantages.

This research is ambitious as it has taken a comprehensive review of the key economic evidence that underpins the business benefits of equality, diversity and inclusion.

The academic evidence only tells a part of the story. This is why we are developing in-depth case-studies which could demonstrate where businesses have reaped real benefits and why. This kind of evidence will make it more real to a wide range of businesses – large and small, domestic and international and in a variety of sectors. We need to move away from diversity being a “human resources” issue to realising that companies can prosper by making the most of the diversity and flexibility of their workforce and customers.



JO SWINSON

Minister for Employment Relations and Consumer Affairs and Minister for Women and Equalities

Executive Summary

Understanding the business impacts of equality and diversity: what does the evidence tell us?

This report considers the evidence for the business case for equality and diversity in private sector organisations. The aim is not to make the business case, but to assess the current evidence from academic journals and some key practitioner sources.

Key findings

- Studies appear to have found evidence that firms have reaped business benefits from equality & diversity, but not all firms in all contexts at all times.
- The firm's economic and organisational **context** is crucial in determining how equality and diversity brings about business benefits. The business case is likely to depend on the markets a firm operates in, its labour market, organisational and other strategies and the actions of managers and leaders.
- How diversity is managed is also crucial: if appropriately, it can bring benefits to business, if poorly, it can increase costs. Different approaches are likely to be needed, depending on the nature of diversity, the internal workplace context and external environment.
- There is **no single approach** that all businesses can adopt to ensure equality and diversity are beneficial. To be effective, equality and diversity need to be embedded in the business strategy, not treated as an ad-hoc addition.

Key policy implications

- There is no “one-size-fits all solution”. Businesses know best their own market and sector, and should approach equality and diversity with that in mind. Government needs to take this into account in its engagement with business on this issue.
- This is not saying that businesses can ignore equality and diversity if it is not in their business interests (they still have to comply with the law), but rather that they may be overlooking important business benefits.
- Gestures cost money: to achieve benefits and avoid costs, businesses need to see diversity as a strategic resource.
- Being strategic about equality and diversity means more than merely complying with legislation, although this too can result in business benefits.

Approach

This research was commissioned by the Department for Business Innovation & Skills (BIS) and the Government Equalities Office (GEO).

This report sets out the findings from a systematic review of the (primarily academic) literature on the evidence for the business case for equality and diversity. The business case is distinct from the legal and moral case in that it involves factors which can improve the economic performance and competitiveness of the firm. The focus is on evidence that is relevant for businesses seeking market advantage in a competitive environment.

The report aims to:

- improve understanding of theoretical positions and issues related to the business case for diversity and equality
- develop a consistent framework for assessing evidence on the business case
- within this framework, present a review of the evidence
- create a robust compendium of the evidence.

These are needed to assess a fragmented literature where different conceptual frameworks, methods, and measures have been used, and where there are substantial methodological challenges. These different approaches to understanding and assessing the business benefits from equality and diversity explain some of the variability in findings.

A key distinction in the assessment is the difference between *External* and *Internal* Business Benefits, both of which can improve measures of business performance such as profitability.

External Business Benefits arise when firms better represent the world (and legislative environment) around them. For instance, having staff with roots in other countries and cultures can help a business address its products appropriately and sensitively to new markets. Consumers are becoming more diverse and firms may need to reflect this or risk losing out in important markets.

Internal Business Benefits arise from improving operations internal to the firm. For example, a diverse workforce which includes a range of perspectives can improve creativity and problem-solving, resulting in better decisions. Also a diverse workforce can offer greater flexibility.

Future research

The academic research analysed in this paper tends to involve the comparison of data on activities and performance across a number of companies, with little consideration of the role of internal processes and policies. This kind of evidence cannot explain *how* business benefits were realised, which would be of more use to

businesses facing specific challenges. Evidence on what has actually worked and why would require detailed company case studies.

There are already quite a few case studies of the business benefits from equality & diversity, but they tend not to focus on business performance impacts, or to look at firms' context and strategic response, what worked and why. The insight from this report suggests that the business case for equality & diversity might have more resonance with businesses if there was credible evidence of this more practical kind.

More generally, there is a need to take forward existing work analysing diversity in teams, and workplace equality and diversity management.

Next Steps

A second project stage is planned from January 2013 to consult the private sector and explore options such as the development of case studies which clearly demonstrate the business benefits of good equality and diversity practice, and the success factors which have proved critical in specific cases.

Illustrative evidence from case studies examined in this research

The analysis of academic research was supported by evidence from a survey of organisations carried out on behalf of the GEO which considered their approaches to equality and equality legislation. The survey revealed widespread engagement with equalities and equality legislation.

There were a number of reasons provided as to why organisations positively embrace equality. Most respondents felt the approach derived from a sense of moral obligation on the part of the owners or managers, as well as a concern to be in compliance with workplace equality legislation. An additional driver was the concern that the organisation should be viewed favourably by communities, customers and suppliers.

The case studies below provide high level snapshot examples of current practice and impacts on business performance.

Enterprise Rent-A-Car: Work life balance and opportunities for progression

Enterprise Rent-A-Car has always seen gender diversity as a top business priority and fundamental to creating a culture of success. They view it as something that propels business growth and creates a tremendous opportunity for employees.

Issue

Enterprise Rent-A-Car wanted to ensure that they developed female talent so that women form a representative proportion of the workforce at all levels of the organisation, ensuring future sustainability.

Action

Enterprise Rent-A-Car has taken the following actions:

- Launched a new scheme for keeping new parents in touch with business developments whilst on maternity leave. Involving senior leaders across the business rather than just HR. 'Mums and Tots' update meetings were rolled out across the business.
- Providing top quality mentoring and sponsorship opportunities for promising female talent.
- Launching a Leadership Development Pilot Group designed to help women achieve promotion to more senior roles.
- Launched a maternity coaching project with Talking Talent.

Result

Enterprise Rent-A-Car achievements in 2011 included:

- A 3% increase in the number of women in the UK workforce to 37%.
- 89% of women returning from maternity leave.
- Over 50 female employees being mentored by senior directors, with a 9% promotion rate to senior roles.

Eversheds LLP: Increasing Overall Female Representation

International law firm Eversheds LLP has a strategic commitment to being a great place to work.

Issue

Eversheds has a significant number of women at entry level, but fewer female partners. They have an aspiration for 25% of the partners in the organisation to be female by 2015.

Action

Eversheds introduced a flexible working scheme called FlexAble. This allowed staff to agree flexible working hours on a short term basis with their managers rather than formal contractual changes.

Result

- The number of people working flexibly has nearly doubled from 48% to 91%.
- Productivity improved by 5% compared to the same period the previous year.
- Partnership is now 22% female following the 1 May 2012 promotions process.

Introduction

Scope and aim of research

This report sets out the findings from a systematic review¹ of the literature on the business case for equality and diversity, commissioned by the Department for Business Innovation & Skills (BIS) and the Government Equalities Office (GEO).

The report aims to:

- improve understanding of theoretical positions and issues related to the business case for equality and diversity;
- develop a consistent framework for assessing evidence on the business case;
- within this framework, review the evidence;
- create a compendium of the evidence.

The research does not aim to establish a new business case for equality and diversity, but to assess the most robust evidence, draw implications from the findings and present a dispassionate picture of the evidence identifying gaps and conflicting messages. The report focuses on diversity in terms of 'protected characteristics'².

Methodology

The literature contains conflicting findings and a variety of methodological approaches. This paper focuses on evidence from peer-reviewed academic journals, and also considers some key practitioner sources. The focus is on evidence that has relevance for institutions facing competition within market settings³. We consider research from countries other than the UK (a lot of evidence comes from the US) if it has relevance to firms located within the UK and potentially operating across international borders. In fact, although the legal framework across EU countries is similar, the approaches to protected characteristics can be very different.⁴

The systematic review considered evidence from a range of social science disciplines - detailed in Appendix 1.

¹ An approach to the review of published evidence that is systematic, transparent, and therefore, replicable.

² Protected Characteristics are defined in the Equality Act 2010. These include: age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation.

³ We do not ignore findings from research in the public sector, other non-market settings and at a national level, but focus on findings that are of relevance to firms operating in competitive markets.

⁴ For instance, in France it is illegal to collect information on ethnicity and debates in Germany tend to focus more on the issue of citizenship and country of birth, than self-reported ethnic group.

The first stage of the systematic review involved academics and practitioners in identifying review questions, key words and search strings relating to the 'business case for equality and diversity'.⁵ A matrix of search terms across different disciplines then defined the parameters for a search of evidence appearing in peer-reviewed journals.

Following a review by the project team, 64 academic articles were considered to be of acceptable quality and of some relevance. These form the basis for the evidence reported in Section 3 of the Report. The different methodological approaches adopted by researchers studying equality and diversity proved challenging, but ultimately the review had to focus on a search for evidence that captured cause and effect, between aspects of equality, diversity and business outcomes. Whilst this implies a focus on studies that attempt to quantify impacts, we also considered studies taking a more qualitative approach.

The aim is not to impose an initial set of interpretations, but to assess the literature so as to (i) arrive at definitions and clarifications of terminology (highlighted as numbered PROPOSITIONS) and (ii) construct a framework to consider the evidence.

We first develop a robust conceptual framework (Chapter 2), which is then used to consider and assess the evidence (Chapter 3). We finally present the practitioner and strategic literature, and outline the implications for firms and policy makers (Chapter 4).

The business case and the moral case

In this section we briefly describe some of the most relevant theoretical positions and issues related to the business case for equality and diversity. In particular, we outline how it relates to the so-called 'moral case'. We finally clarify terms such as 'diversity', 'equality' and 'inclusion', 'unconscious bias' and 'micro inequities' [from part of 3.4].

For the purposes of this research it is helpful to distinguish between equality and diversity approaches that have 'improve[d] organisational performance' as their main driver, and contrast these to policies and practices driven by considerations of equity. These drivers are often presented as the *business case* and *moral case* respectively. This reflects two broad areas of investigation in the literature: one includes studies of the instrumental ways that diversity contributes to organisational performance; the other considers ethical and responsible ways that diversity at work can be managed. The Moral case has often been expressed in terms of Equal Opportunities, which has found manifestation in various pieces of legislation; the business case, instead, is often referred to in terms of **managing diversity**. However, it is hard to fully separate managing diversity in the workplace from the provision of equal employment opportunities, as legislation shapes the way in which diversity is managed (Monks, 2007).

⁵ We thank those who contributed to three practitioner-focused events on 2 November 2011; 15 December 2011 and 10 January 2012.

Diversity Management

Diversity management has been defined as a “*management philosophy of recognising and valuing heterogeneity in organisations with a view to improve organisational performance*” (Ozbilgin and Tatli, 2011). Ozbilgin and Tatli suggest that this approach has been offered as an alternative to equal opportunities and reflects significant moves towards liberalisation and deregulation in the US and UK. Diversity management has moved away from the emotive and legal case for equality, towards individualised and performance-driven business case arguments. Subeliani and Tsogas (2005) state that diversity management “*positively values difference and thus provides a radically new approach to the question of difference at work* *Managing diversity seems to be a proactive strategy [with] the aim of maximizing the utilization of employees’ potential*” (p.832). In line with this, Ozbilgin and Tatli (2011) found that diversity management is more common in the private sector due to the emphasis on profit and sales, while public sector organisations tend to focus on social responsibility. They also observe that the increased emphasis on value for money in the public sector heralds a move towards diversity management in this sector.

Whilst equality or positive action focuses on protected minority groups that are demographically different, Diversity Management tends to encompass a broader definition of difference to include a greater variety of characteristics (both visible and invisible). Diversity approaches tend to relate to the characteristics of groups and individuals (workers, consumers or otherwise) whilst ‘equality’ can relate to opportunity or autonomy, process and/or outcome.⁶

Equal Opportunities, Inclusion, Unconscious bias and Micro inequities

Demographic trends since the 1950s have increased the diversity of the UK population. The first pieces of legislation focused on equal opportunities for women and ethnic minorities⁷, as immigration increased the ethnic diversity of the UK and the role of women grew in all parts of the economy and society. Social and economic trends, such as an ageing population, the lowering of international barriers to trade, increased movement of capital and labour across borders together with technological innovation, have all contributed to increased diversity in the workplace across a range of characteristics, which legislation has subsequently ‘protected’ (for instance age, religion or belief⁸). This has been accompanied by an increased willingness amongst politicians to legislate to ensure equal treatment on other characteristics such as disability, sexual orientation and transgender.⁹

Some of the most important original theories of discrimination were primarily focused on behaviours arising from “conscious” decisions of individuals to discriminate

⁶ See for instance, Government Equalities Office (2010), *The case for equality – draft report for Phases 1 & 2*, April.

⁷ Sex Discrimination Act (1975) and Race Relations Act (1976).

⁸ Religion and Belief (2003) and Age (Oct 2006).

⁹ Disability (1995); Sexual Orientation (2003 and 2007).

between groups (for instance, Gary Becker's PhD (1957), *The Economics of Discrimination*). These approaches (particularly in economics) assumed that individuals from certain groups had a "taste for discrimination", in that they purposefully and openly disliked individuals from other groups and would act to avoid them in social and workplace settings. One can see the array of equal opportunities legislation as an attempt to stop such practices.

However, in the UK during the 1980s and 1990s, a series of high-profile cases changed the nature of the debate, by alerting the public to the potential for institutions to have systems and processes in place that perpetuate discriminatory practices — even in situations where individuals may not necessarily have a conscious "taste for discrimination". The murder of Stephen Lawrence in 1993 following a racist attack, and the subsequent public inquiry headed by Sir William Macpherson into the handling of the case by the police and the Crown Prosecution Service, raised awareness of the potential for such unconscious biases.

There is a strong moral case for the eradication of discrimination, but the issue is highly emotive. The recognition and valuing of difference in society is an essential part of the process of its eradication and the overcoming of ignorance. Within firms, the building of an inclusive culture requires a long-term strategic effort. The challenge of making everybody feel valued and respected can be more acute in more diverse workplaces (because of the greater potential for micro-inequities and unconscious bias), and this is perhaps why policies of inclusion and engagement are often seen as important in diverse settings.

Whether discrimination and bias is conscious or unconscious, it is likely to impact negatively on the working lives of those who experience it and ultimately lead to negative impacts on performance and commitment at work. The work on micro-inequities¹⁰ can be similarly seen within this context, as it provides insight into the potential for unconscious behaviours among a group to impact negatively on the working lives of others.

The arguments that the overcoming of such biases (conscious or unconscious) leads to more productive and harmonious societies are compelling. Within the economics literature, the original argument put forward by Becker and others was that market systems would work to bring about such changes, as there would be opportunities for non-discriminatory firms to enter markets and make higher profits than the less efficient discriminatory firms.¹¹ This is not to suggest that such theories do not see a role for legislation, but that they see the market mechanism and the legislative framework being aligned, and ultimately leading to similar outcomes.

¹⁰ Rowe, M. (2008), "Micro-Affirmations and Micro-inequities", *Journal of the International Ombudsman Association*, Vol. 1, No. 1, March.

¹¹ Becker's theory originally relies on workers having a taste for discrimination which manifests in wage negotiations and it is not clear how models such as this translate into the study of unconscious bias. That is, in Becker's original model discriminating individuals act as if they were willing to pay something, either directly or in the form of a reduced income, to be associated with some persons instead of others.

Conclusions

Some research (Armstrong *et al*, 2010) suggests that equality and diversity are at opposite ends of the same continuum, and merely indicate a progression in developing equality in organisations (McDougall, 1998). Others suggest that it is not useful to distinguish between the two (Malvin and Girling, 2000), or highlight potential conflict: accommodating diversity could have a detrimental effect on the ability of an organisation to also adopt equality (see for instance, Kirton and Greene 2010).

A Framework for the Evidence

This chapter sets out a framework that helps assess this fragmented and complex literature, providing a simplified overview of concepts, theoretical issues and debates.

Types of Diversity

Scholars have struggled to define diversity clearly. This may be because the term has been used to describe a large number of differences between people (Mannix & Neale, 2005). We might simply describe surface-level diversity as demographic difference, and deep-level diversity as differences in attitudes and beliefs (Harrison et al, 2002). Table 1 gives an example of how this approach could be developed into one that is more complex, including several categories of diversity characteristics.

Table 1: Categories and types of diversity

| Category | Type of diversity |
|--|--|
| Social category differences | Race |
| | Ethnicity |
| | Gender |
| | Age |
| | Religion |
| | Sexual orientation |
| | Physical abilities |
| Differences in knowledge and skills | Education |
| | Functional knowledge |
| | Information or expertise |
| | Training |
| | Experience |
| Differences in values or beliefs | Abilities |
| | Cultural background |
| | Ideological beliefs |
| Personality differences | Cognitive style |
| | Affective disposition |
| | Motivational factors |
| Organisational/ community status differences | Tenure or length of service |
| | Title (work function, seniority, discipline etc) |
| Differences in social and network ties | Work-related ties |
| | Friendship ties |
| | Community ties |
| | In-group memberships |

Source: Mannix and Neale, 2005

However, the characteristics in Table 1 can be viewed in a number of alternative ways. For example, the *Four Layers of Diversity Model* (Gardenswartz & Rowe, 1994) categorises them into organisational, external, internal and personality.

Reported Business Benefits of Equality and Diversity

Studies that consider the business case for equality and diversity, tend to focus on the potential for costs and benefits associated with a business having (or lacking) equality practices; or the potential for benefits from having a diverse workforce.

For example, a recent interview study found anecdotal evidence that the lack of an equality management policy could lead to high labour turnover, loss of talented employees, employment tribunals and the associated bad publicity (Ozbilgin & Tatli, 2011). Another study examined the costs of discrimination using a survey of 139 Hispanic employees from multiple organisations. Their results supported the idea that perceived discrimination can contribute to negative employee outcomes such as lower organisational commitment, lower job satisfaction and higher work tension (Sanchez & Brock, 1996). Likewise, a report by the Commission for Racial Equality (1995) suggests that discrimination increases absenteeism.

One particular case-study suggested that a construction company considered that a positive action policy had given it a competitive advantage with customers who valued fair employment practices (Welsh et al 1994). A wider empirical study using the 1998 UK Workplace Employee Relations Survey (WERS) found evidence suggesting that equal opportunities policies (EOPs) improve productivity. This effect became more evident as the share of female and ethnic minority employees in the workplace increased, with short-term negative effects in segregated workplaces. This suggests that the benefits of Equal Opportunities Policies were enhanced by greater diversity, but were ineffective until the underlying balance of employee characteristics was improved (Perotin and Robinson, 2000).

Based on a review of the literature, Cox & Blake (1991) proposed six main business benefits of a diverse workforce:

1. Cost argument: the cost of doing a poor job in integrating workers is increasing, so those who manage diversity will gain a cost advantage.
2. Resource-acquisition argument: adopting a diversity–management approach will develop reputations of favourability for the organisation as prospective employers for women and ethnic minorities, so these organisations will get the best personnel.
3. Marketing argument: multi-national corporations (MNCs) will obtain insight and cultural sensitivity from having members with roots in other countries, and this will improve marketing.
4. Creativity argument: the presence of diversity of perspectives and less emphasis on conformity to past norms should improve creativity.
5. Problem-solving argument: heterogeneity in groups potentially produces better decisions and problem solving through a wider range of perspectives.

6. System flexibility argument: the system becomes less standardised, and therefore more fluid, which creates more flexibility to react to environmental changes.

This range of potential business advantages for diversity has been supported by several authors (e.g. Subeliani & Tsogas, 2005) who suggest that increased diversity can lead to a better understanding of local markets and customers, increased ability to attract and retain the best people, greater creativity, better problem solving and greater flexibility for organisations. This was supported by anecdotal evidence collected through surveys or interviews with managers and diversity personnel. For example, interviewees in one study suggested that diversity led to them recruiting and retaining the best talent, improved organisational performance and efficiency, increased productivity and creativity, enhanced trust relationships, satisfaction and commitment within the workforce, improved customer relations and service delivery, and helped to create a positive corporate image and reputation (Ozbilgin & Tatli, 2011). An earlier study by the same authors, using a survey of 285 diversity and equality officers, suggested that the top ranking business benefits for diversity were perceived to be: ability to recruit and retain the best talent (63.9%); because it makes business sense (60%); to improve business performance (48.1%); to address recruitment problems (47.3%); a desire to improve customer relations (43.2%) and to improve products and services (42.6%) (Tatli & Ozbilgin, 2007).

These studies provide a useful understanding of the common beliefs about the business case for diversity and equality. There are additional studies (e.g. Litvin, 1997; White et. al., 2004; Swann, et. al., 2004; Subeliani and Tsogas, 2005; Urwin et. al., 2006) and these postulate variations around the themes described above.

PROPOSITION 1: Equity rather than the profit motive appears to be the primary driver of equality approaches. In contrast, diversity approaches appear to be more often driven by considerations of productivity and profit. In any case, whether driven by equity or profit, there is the potential for business benefits to accrue.

Can we Separate Equality from Diversity Business Benefits?

Some of the literature implies that the business benefits of equality are different to those arising from diversity. Other studies suggest an overlap between the two and some a conflict between them.

Here we distinguish between business benefits that arise mostly as a response to the external environment, and those that are driven by internal needs and pressures¹².

The first type of business benefits include those which may accrue to firms when they implement policies and practices that aim to increase diversity in line with a changing external environment. Therefore, we call these **External Business Benefits**. These benefits can arise as a result of either diversity or equality approaches¹³, but the

¹²Zanoni et al. (2010) point out that, notwithstanding the growing amount of critical diversity research, this area is still in need of theoretical and conceptual improvement.

¹³They are business benefits that may arise from policies and practices driven by considerations of either profit and/or equity.

distinguishing factor is that the potential benefits are closely linked to firms achieving a more representative workforce.

Referring back to the categories used above (Cox & Blake, 1991), these can be represented as:

- There is a rising cost of integrating workers poorly, as demographic diversity increases.
- Firms can only ensure that they attract the best personnel by selecting from the widest pool. Adopting a diversity management approach will attract more talented women, ethnic minorities and other groups than otherwise.
- There is the potential for marketing gains from improved insight and cultural sensitivity, from having members with roots in other countries. Consumers are becoming more diverse and the firm needs to reflect this, or it will lose out on important markets.
- There are savings from a reduction in employment tribunals and other workplace costs when firms and workers comply with equality legislation.

PROPOSITION 2: *External Business Benefits* may arise when firms better represent the world (and legislative environment) around them.

These suggested business benefits invariably relate to levels of demographic diversity (in terms of protected characteristics).

The second type of business benefits, which we call **Internal Business Benefits**, can be represented as:

- Diversity can increase creativity and problem-solving by providing a wider range of perspectives
- Diversity can create more flexibility to react to environmental changes.

This rests on the assumption that bringing together a greater variety of tacit dispersed knowledge may improve business outcomes. This category of business benefit can apply across all types of diversity, not just demographic.

PROPOSITION 3: *Internal Business Benefits* suggest that diversity is, of itself and independent of external drivers, a desirable workforce characteristic that can enhance productivity and other business outcomes.

The box below shows how some key economic theories and the legal context clarify the proposed distinction and underline its importance for policy.

Internal and External Business Benefits

One of the enduring economic frameworks for consideration of discrimination suggests that discriminating employers perceive the cost of hiring a worker of a different (minority) group as being higher than the actual cost (Becker, 1957)¹⁴. But within this same framework, we can suggest that if there are business benefits from diversity, then the perceived benefit of hiring the minority group worker should actually be greater than those of hiring the majority group worker¹⁵. If employers expected such business benefits, then they would be inclined towards profit-driven affirmative action, in contrast to the discrimination model.

Those who argue for affirmative action on ethical grounds suggest that firms (and society) should place a greater value on the promotion of individuals from groups that suffer disadvantage. In our simple economic framework, the two approaches may at first seem to be the same. But this is where we come to an important distinction between Internal and External Business Benefits.

Consider a firm which perceives a diversity benefit associated with minority workers:

External business benefits: As the levels of diversity in the firm increases, our definition implies that the benefits fall for each additional minority employee hired, until it reaches zero when the firm achieves a workforce which is representative of the population. In a world where business benefits accrue to firms which best reflect the society they serve, there are no additional benefits of hiring minority over majority group workers for firms that have achieved a representative workforce.

Internal business benefits: The suggestion is that increased diversity improves problem solving and other outcomes, independent of the levels of diversity in wider society. This is detached from the concept of representation. If increased diversity, of itself, is desirable then there can continue to be benefits even after a firm has achieved a representative workforce.

We are not distinguishing between diversity and equality policies; rather the two types of benefits that may flow from one or more of these approaches. The representation of External Business Benefits in our model is similar to a positive action approach.

The question still remains of how these categories of hypothesised benefits relate to the *Moral* and *Profit-driven* distinction suggested in Proposition 1. The following section presents a framework that brings the two together.

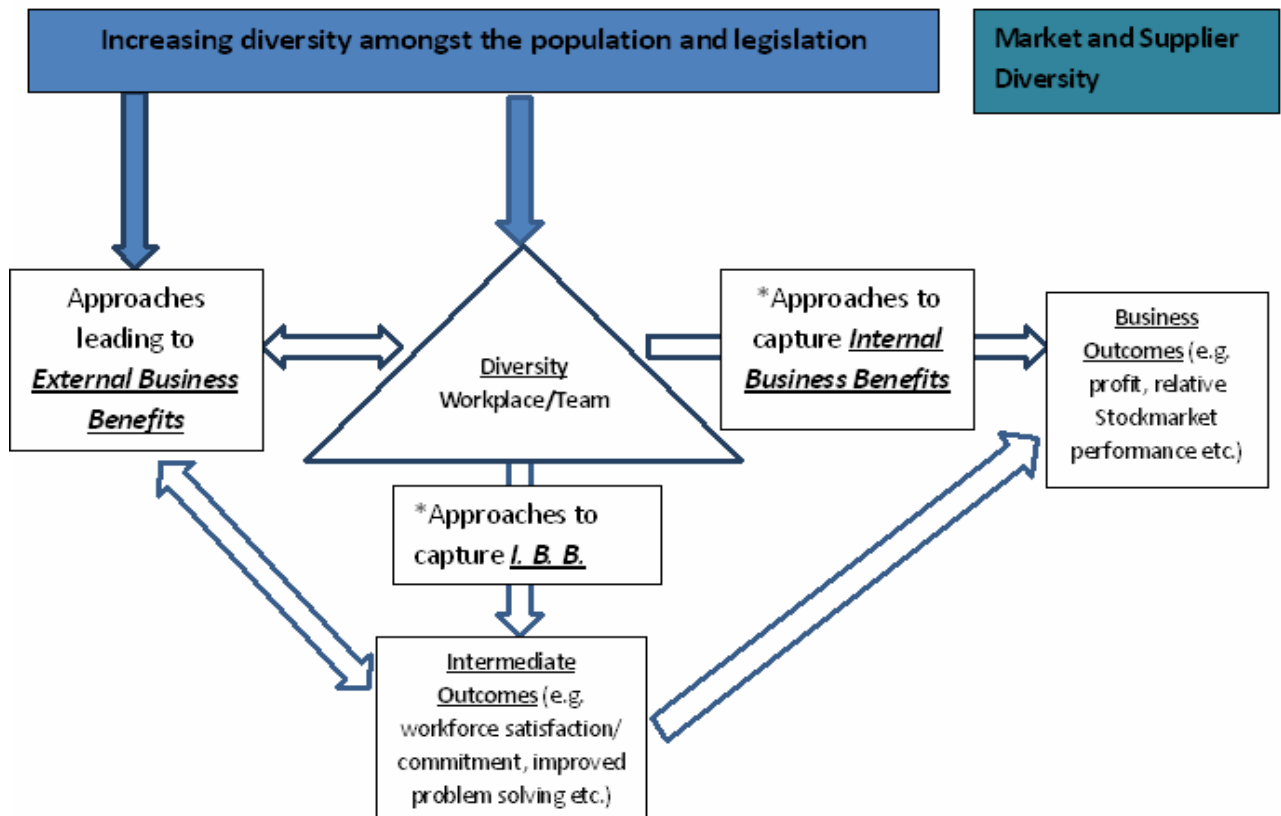
¹⁴ A discriminating employer perceives that the wage paid to a minority worker is the $Wage + d$, where 'd' is the discrimination coefficient and reflects how prejudiced the employer is (higher 'd', greater prejudice and higher perceived cost of employing a minority worker).

¹⁵ One could call this a diversity coefficient (D). In an environment where there are seen to be gains from increased diversity, we can think of an employer perceiving a minority employee's wage as $Wage - D$ (where 'D' is the additional business benefit arising from a subsequent increase in diversity).

Building the Framework

Figure 1 provides a simplified overview of many of the debates within the literature¹⁶. In some respects, this is a hybrid of models from the Human Resource Management (HRM)-Performance literature (e.g. Paauwe, 2004), of which the High Performance Work Systems (HPWS) and the High Performance Work Organisation (HPWO) models are a subset.

Figure 1: A Framework for External and Internal Diversity Business Benefits



Culture/leadership can be thought of as an envelope around this diagram

*Approaches to capture Internal Business Benefits

¹⁶ A version of this framework was first developed in the initial scoping phase of our study, and further refined to take on comments, following presentation to audiences of practitioners and academics.

The transparent boxes, arrows [\leftrightarrow , \leftarrow , \rightarrow] and triangle [Δ] of the diagram represent relationships between aspects of interest within the firm. The **blue rectangles** blue rectangles represent diversity external to the firm, in the population, the Market and amongst *Suppliers*. This allows us to consider the evidence of a business case for equality and diversity, within the context of our categories of hypothesised **External** and **Internal** Business benefits and the distinction made in Proposition 1.

For instance, the box containing **Approaches leading to External Business Benefits** represents those policies, practices and strategies that firms have in place to achieve a representative workforce. We can position these in Figure 1 as a response [\leftarrow] to **Increasing diversity amongst the population and legislation**¹⁷; they also impact upon, and are influenced by [\leftrightarrow], both the levels of [Δ - Diversity within the firm] and also **Intermediate Outcomes** such as satisfaction and commitment. The approaches (policies, practices and strategies) that may lead to **External Business Benefits** have the level of diversity in the external environment and equalities legislation as their main focus.

In contrast, the boxes containing **Approaches to capture Internal Business Benefits** represent those policies, practices and strategies that firms have in place to use diversity for Business Benefit. We can position them in Figure 1 as facilitating the link [\rightarrow] between levels of [Δ - Diversity within the firm] and improved **Intermediate Outcomes** and/or **Business Outcomes**. These approaches are focused primarily on levels of diversity within the firm and the potential for this to lead to business benefits.

We can now clarify the link between these two types of hypothesised business benefits, and the distinction between policies/practices suggested in Proposition 1.

Within the category of **Approaches leading to External Business Benefits** we include all policies and practices that are driven by considerations of equity and therefore all 'equality approaches' fall within this category. The assumption is that policies and practices that facilitate equality of access (to professions, levels of seniority and employment itself) based on ability, should eventually lead to workplaces that are representative of wider society¹⁸. The implication from some of the literature in section 2.1 is that, even in instances where policy is driven by considerations other than the profit motive (such as equity or the *moral case*), business benefits could accrue.

¹⁷ Together with Market and Supplier diversity.

¹⁸ In practice, a firm's equality approaches may not lead to a representative workplace in the short term because of the potential for pre-labour market discrimination. For instance, we observe differing educational outcomes across gender and ethnic groups (see Urwin et. al. 2010), and this may result in workplaces that look different to the population as a whole. Such situations often motivate calls for affirmative action, in contrast to equality approaches, but ultimately the aim of representative workplaces is the same in both cases.

PROPOSITION 4: All equality approaches, and diversity approaches driven by considerations of equity, have the potential to lead to business benefits that fall within our category of *External Business Benefits*.

The category of Approaches leading to *External Business Benefits* includes diversity approaches that aim to improve firm performance by better representing the demographic and legislative environments. These diversity approaches are primarily driven by business arguments of, “the world is changing and businesses need to change if they are not to suffer negative consequences,” and invariably relate to protected characteristics.

PROPOSITION 5: Diversity approaches, driven by business arguments of “the world is changing and businesses need to change if they are not to suffer negative consequences”, fall within our category of *External Business Benefits*. These diversity approaches, driven by motives of profit arising from workplaces better representing society, have the potential to drive forward the equality agenda.

In contrast, the policies and practices included within our Approaches to capture *Internal Business Benefits* do not include equality approaches, and are driven by the profit motive.

PROPOSITION 6: Diversity approaches, driven by business arguments which are not based on the concept of demographically representative workplaces, fall within our category of *Internal Business Benefits*. These diversity approaches, driven by the belief that greater diversity of itself can lead to improved business performance, have the potential to drive forward the equality agenda, but this is not necessarily always the case.

We now have some clarity on the nature of the possible business benefits arising from different approaches to equality and diversity. We also have an indication of how these various approaches relate to the equality agenda. The challenge now is to ask, in which areas of our framework is there clear evidence of approaches to equality and diversity leading to enhanced business outcomes?

Before moving on to consider the evidence of such business benefits, we clarify some remaining aspects of the framework.

- We focus on workplace diversity, as opposed to concepts such as **supplier diversity** and **market diversity**, in line with the focus of academic literature.
- Diversity of the workforce is represented as an ‘Access Pyramid’ [Δ] to reflect the fact that we invariably find greater diversity at more junior levels of a profession/company. For instance, within the Law profession we systematically observe higher levels of gender and ethnic diversity at the level of paralegal (most junior), and much less diversity at the level of partner (most senior) (see 2012 Diversity League Tables).

- The arrows [\leftrightarrow , \leftarrow , \rightarrow] represent possible links between workplace practice, diversity and business outcomes. It is not assumed that these are always positive. Our systematic review does not exclude evidence of negative impacts.
- Figure 1 is not able to capture dynamics. However, we do consider separately the potential for some effects to emerge in the short-term and some aspects of the business case to take longer to filter through to tangible business outcomes.
- There is a distinct lack of clarity in the use of *Metrics of Diversity and Business Outcomes* in the literature. Even the larger cross-firm studies of diversity and those carried out under laboratory conditions often fail to clearly define their measures and metrics of interest. Similarly, studies attempt to relate a wide range of potential business outcomes to differing levels of diversity.¹⁹

¹⁹ This critique of the literature would require an entire study in itself – cf Appendix 1 for a brief discussion.

Evidence on the business case

This section presents evidence on the impacts of equality and diversity on business performance. It focuses on work appearing in peer-reviewed academic journals. There is some reference to the evidence from practitioner research, but this will feature mostly in Chapter 4 of this report.

The research identified three types of evidence. First, we consider the evidence on workplace diversity; secondly, we summarise the findings from the literature on equality approaches and practices; finally, we describe the evidence on diversity in teams. Where relevant, we outline the main methodological issues for each type of evidence.

Evidence on Workplace Diversity

Sections 3.1.1 to 3.1.4 summarise the findings from evidence on the link between workplace diversity and indicators of firm performance. We do this separately for each strand of demographic diversity, starting with gender diversity. The evidence on workplace diversity impacts is predominantly qualitative.

Gender diversity in the workplace

Recently, there has been a high-profile debate across Europe around the issue of gender representation at executive level in large (usually publicly quoted) firms. This debate is illustrative of the challenges faced when considering evidence on Internal and External business benefits.

The 2012 *Female FTSE Board Report* suggests that only 15 per cent of FTSE 100 board members are female (Sealy and Vinnicombe, 2012). According to the *GMI Ratings' 2012 Women on Boards Survey*²⁰, the percentage of women on US boards in 2009-2011 was 12.6%. The same survey suggests that this US proportion was somewhere below the figure for France (16.6%) and very close to the 12.9% of female directors on supervisory boards in Germany; whilst Norway comes top with 36.3%²¹.

The evidence on gender diversity in the workplace falls within both our categories of business benefits. The evidence that suggests business benefits accrue to firms when they access more talent (Terjesen *et al.*, 2009; Grosvold, Pavelin and Tonks, 2012²²) and better represent stakeholder groups (Brammer *et al.*, 2009), falls within the category of External Business Benefits. The evidence that suggests more diverse boards are more effective, independent of the benefits that one may expect from better representation of stakeholder groups (Higgs 2003; Tyson 2003), reflects the

²⁰ Gladman, K. and Lamb, M. (2012), *GMI Ratings' 2012 Women on Boards Survey*, March.

²¹ Both France (2010) and Norway (2006) have introduced legislation that mandates an increase in female representation on company boards.

²² Grosvold, J., Pavelin, S. and Tonks, I. (2012), *Gender diversity on company boards*, Voxeu.

category of Internal Business Benefits. Similarly, some researchers suggest substantial differences in gender approaches to management (Marshall, 1984; Gherardi, 1995; Wajcman, 1998) and that diversity of such approaches is beneficial.

Widely quoted research from McKinsey²³ suggests that European listed companies with greater gender diversity in top positions outperform sector averages. The return on equity of such diverse firms was calculated as 11.4 per cent compared to 10.3 per cent on average, whilst these firms also achieved stock price growth of 64 per cent relative to a sector average of 47 per cent [between 2005 and 2007]. Virtcom Consulting²⁴ suggest that greater race and gender diversity on corporate boards were associated with a 16.2 per cent return over five years compared to lower economy-wide averages.

These findings suggest that higher levels of gender diversity are correlated with a firm's performance. However following the guidance in HM Treasury's *Green Book*²⁵ we would ideally wish to have strong evidence of a causal relationship. This would require controlling for other differences between firms to compare like with like. For instance, we tend to find that younger companies (on average) grow at faster rates than older companies (Haltiwanger, Jarmin and Miranda, 2010; Neumark *et al.*, 2008), and smaller companies have higher proportions of women than larger companies (Urwin, 2011; 2012). We could be observing a situation where younger (predominantly smaller) companies that have greater gender diversity are also more likely to grow. In this example, we would observe a correlation between gender diversity and firm performance, but these two variables would not be directly related. They would only be correlated with each other because both are correlated with 'firm age'. We are unable to distinguish between this case of correlation and a case where diversity has a direct causal impact on performance.

One of the few papers testing for a direct link between gender diversity on boards and firm performance is Ahern and Dittmar (2011)²⁶, who use the Norwegian 2003–2008 policy change as a 'natural experiment'. The introduction of quotas in this period, which forced firms to have 40 per cent women on their boards, left some pre-quota firms with a longer road to travel than others. In more technical language, the authors use the pre-quota variation in female board membership as an instrument.

The authors found that firms reporting the greatest increase in female board membership reported falling stock-market valuations and deterioration in operating performance. They also identify an increase in younger and less experienced boards. However, this evidence is more a comment on the short-term impacts of a quota policy, than it is on the impacts of increasing gender diversity. Whilst the introduction

²³ Desvaux, G., Devillard-Hoellinger, S., and Baumgarten, P. (2007), *Women Matter: Gender Diversity, a Corporate Performance Driver*, New York: McKinsey and Company

²⁴ As cited in, Government Equalities Office (2010), *The case for equality – draft report for Phases 1 & 2*, April 2010.

²⁵ HM Treasury (2003; 2011: p. 53), *The Green Book: Appraisal and Evaluation in Central Government*, London TSO.

²⁶ Ahern, K. and Dittmar, A. (2011), "The Changing of the Boards: the impact on firm valuation of mandated female board representation", Stephen M. Ross School of Business, *Working Paper Series*.

of quotas presents us with a natural experiment, it also changes the very nature of our question to one of, “what are the impacts of mandated (involuntary), rapid increases in gender diversity?”. Any lack of sufficiently experienced women to fill the top jobs would explain these findings.

A recent Deutsche Bundesbank Discussion Paper²⁷ adopts methods that are better able to identify causal impacts of board composition on corporate risk-taking, without completely changing the nature of the question being asked²⁸. The authors find that board changes that increase the representation of women are more closely linked to increased levels of risk-taking. These findings may be explained by those of researchers such as Booth and Nolen (2009, 2009a) who suggest that differential attitudes towards risk-taking are moderated, with, “girls found to be as competitive and risk-taking as boys when surrounded by only girls”.

These results underline the complicated and potentially contingent nature of any findings in highly complicated workplace and economic environments. For example, in the present environment, risky behaviours in banking are frowned upon, but before 2008 risk-taking behaviours may have led to greater returns.

Age diversity in the workplace

Here we consider evidence of the link between age diversity in the workplace and business performance. This evidence falls predominantly within our category of *External business benefits*. Whilst the Deutsche Bundesbank Discussion Paper above suggests that risk-taking is greater when boards are made up of younger members, the overall body of research tends to focus on the case for attracting and retaining older workers, rather than on that for age diversity *per se*.

For example, a recent report for the Chartered Institute of Personnel and Development (CIPD) (2012) claims that UK employers will need to fill an estimated 13.5 million job vacancies in the next ten years, but there are only seven million young people leaving school and college over this period. This is supported by a report from the Institute of Directors (2009) that concluded that the skills and experience of older workers were essential for maintaining quality and an ongoing skilled workforce in manufacturing. The other side of this argument is that employing older workers will “block” the recruitment and career progression opportunities for younger workers (Parry and Harris, 2011). Indeed, a recent survey, also from the CIPD, suggests that 23 per cent of employers expect to recruit fewer individuals as a result of the removal of the default retirement age (2011). However, none of these claims has been tested empirically.

The same CIPD report also focuses on the fact that older people are an “*untapped source of labour*” (p.4), that people are living and keeping fit for longer, and that the dependency ratio (the ratio between those in work and those over pensionable age) is deteriorating. More specifically, the report claims that older workers have

²⁷ Berger, A., Kick, T. and Schaeck, K. (2012), “Executive board composition and bank risk taking”, Discussion Paper No 03/2012.

²⁸ They employ a difference-in-difference estimator to identify the relation between changing board composition and corporate performance, with the focus on mandatory executive retirements.

advantages in terms of experience, flexibility, loyalty and customer service, although again these claims are not supported by empirical evidence.

An academic study in Australia (Brooke, 2003), based on archival survey data, found that there were net human resource costs from employing older, compared to younger, workers; once the benefits to recruitment and training were offset against increased absenteeism and workplace injury. Another academic paper in the US (McNaught and Barth, 1992), using a case study of the *Days Inn* hotel chain, found that older workers cost slightly more than younger workers but that this was offset by other advantages of employing older workers.

Ethnic diversity in the workplace

The evidence supporting a link between ethnic diversity and positive business impacts falls within both of our categories of business benefits.

In a review, Scott (2011)²⁹ identifies a variety of evidence (Richard, 2000; Erhardt, et. al. 2003; Herring, 2009) from the US that finds positive correlations between board-level and workforce ethnic diversity and firm profitability, similar to the evidence on gender diversity from Virtcom Consulting cited above.

In the UK, studies of FTSE 100 firms have suggested an 'association' between the total value of a company's stock and appointment of directors from Minority Ethnic backgrounds (Singh, 2007). A case study of Rabobank Nederland (Subeliani and Tsogas, 2005) found that a firm had increased its market share among the ethnic population of the country as a result of increasing ethnic diversity in the workforce.

Studies often identify positive impacts of ethnic diversity in certain business settings. Richard et. al. (2003) suggest a favourable relationship between increasing ethnic diversity and rising returns on equity for banks that are pursuing an innovation strategy. Richard (2000) identifies a positive correlation between workforce ethnic diversity and productivity in firms pursuing growth strategies. McKay *et al.* (2008) finds that average ethnic differences in sales performance are moderated by diversity climate.

Unlike the evidence on workplace gender diversity, no studies were identified that attempt to capture the causal impact of ethnic diversity on business outcomes.

Disability, religion and sexual orientation

There are very few workplace studies that attempt to quantify the impacts of diversity on business outcomes, when considering disability, religion and sexual orientation. In many instances this is a result of data limitations. Very few private sector firms collect systematic and useable data on religion and sexual orientation (see for instance, 2012 Diversity League Tables). Even if they do, response rates can be very low and data on disability are often hard to analyse as they are often self-reported and can cover a wide range of conditions.

²⁹ Scott, D. (2011), *Equality and Diversity – a Good Business Proposition?*, mimeo.

The same is true of publicly available datasets. There are studies of sexual orientation in the field of economics³⁰, but these do not investigate the business benefits of such diversity. Studies of religion are relatively new, as questions on religion have been included in regular surveys such as the Labour Force Survey only since Spring 2004.

However, some studies adopt a wide definition of workplace diversity, not restricting it to specific social categories such as gender, ethnicity. One may consider that findings from this kind of research might apply to any form of diversity, including disability, sexual orientation and religion. For instance, Joshi (2006) proposes that a team's demographic composition interacts with the organisation's demography to determine the nature and extent of its external networks; this then impacts positively on sales performance.

In addition, some of the practitioner and case studies literature (Section 4) illustrate how religion, disability and sexual orientation diversity may impact on business performance.

Workplace Diversity

Much of the evidence on workplace diversity and business performance is qualitative and/or of a case-study nature (Monks, 2007; Shen et al, 2009). Evidence from case studies finds conflicting evidence of systematic business impacts of diversity from workplace studies (Kochan et al., 2003) and impacts seem to be moderated by organisational context and management processes.

Evidence on Workplace equality approaches

This section considers evidence on the potential business impacts of equality approaches.

Over the last two decades an extensive literature has developed around the possible links between Employee Relations or Human Resource Management [HRM] practices and workplace performance (Arthur, 1994; Barney, 1995; Ichniowski, et. al., 1997; Becker and Gerhart, 1996; Ramsay et. al., 2000; Hope et. al., 2005). These evaluations of HR practice often focus on the potential for promotion of flexibility, equal opportunities and other 'enlightened' practices to impact on business performance (Huselid, 1995; Purcell, 1999; Appelbaum at al., 2000; Sung and Ashton, 2005). The standard approach in these studies is to 'bundle' together a variety of indicators of workplace practice to create measures that are then correlated with firm performance.

For instance, data from the Workplace Employment Relations Survey (WERS) suggest that in 2004, 20–25 per cent of all workplaces monitored recruitment to

³⁰ Frank, J. (2006), "Gay Glass Ceilings", *Economica*, Vol. 73, No. 291; pp. 485-508.

ensure gender, ethnic, age and disability equal opportunities. On work–life balance, the majority of workplaces offered the possibility of reducing (70%) or increasing working time (57%), and in nearly half of workplaces it was possible to change working patterns (Kersey *et al.*, 2005). A variety of empirical papers use the WERS and other datasets to investigate the link between these indicators of employee relations practice and improved workplace performance (Forth and Rincon-Aznar, 2008).

All of this literature implicitly captures some impact of equality policies and practices, and one branch focuses on this explicitly. For instance, analysis by O’Connell and Russell (2005) of Irish survey data, regarding the relationship between equal opportunities policies in the workplace and measures of employee job satisfaction and commitment, found that this was unambiguously strong and positive. However, controlling for other factors, little evidence was found to suggest that equal opportunities in the workplace have a significant impact on either job satisfaction or commitment.

An econometric investigation of the link between policies and practices promoting equal opportunities and business performance, carried out by Riley, Metcalf and Forth for the Department for Work and Pensions (2008), concluded that this was not only complex, but that it was difficult to prove large or widespread benefits. However, the analysis did not find any evidence that policies and practices resulted in a net cost to businesses, and found that where there were benefits, these tended to occur in larger organisations. The study recognised that the nature of business benefits explored was narrow, and further work was needed.

Some of this literature deals more specifically with issues that are traditionally associated with gender diversity and the concept of work–life balance (WLB). De Menezes and Kelliher (2011) carried out a systematic review of evidence on the business case for flexible working, and concluded that, “*Taken together, the evidence fails to demonstrate a business case for the use of flexible working arrangements*”. In contrast, Dex and Scheibl (2001) looked at the business case for flexible and family-friendly working arrangements across ten small and medium-sized enterprises and four large organisations. They conclude that SMEs can reap business benefits from adopting flexible working arrangements. Interestingly, a greater degree of genuine flexibility is possible in the small-scale context where relationships are understood and working conditions are clear and visible.

Armstrong *et al.* (2010) used a survey to examine the relationship between high-performance work systems and diversity management practices with productivity outcomes. They found that increased use of high-performance work systems led to higher performance and that diversity management in addition to high-performance work systems led to even more gains. Firms that used diversity management demonstrated high levels of labour productivity, increased workforce innovation and decreased voluntary turnover. When firms used high-performance work systems and diversity management in tandem the combination explained 13.2 per cent of the correlation with labour productivity, 8.8 per cent of workforce innovation and eight per cent of voluntary turnover.

In a slightly different study, Wright *et al.* (1995) looked at the impact of announcements of awards for exemplary affirmative action programmes (as a proxy for effective diversity management) and of damages for discrimination on stock price

valuation (using event study methodology). They found that announcements of awards may be associated with increased competitive advantage (increased stock price) and announcements of discrimination may be related to inability to achieve such advantages.

Sung and Ashton (2005) found positive effects on overall organisational performance, commitment and effectiveness from High-Performance Work Practices (HPWP). On the other hand, a 2004 DTI and CIPD survey suggested a weaker relationship between HPWP, workplace diversity and work-life balance. Reviews of the literature (see for instance, Boselie and Paauwe, 2005) suggest it is still unclear what can be concluded from these studies.

Armstrong *et al.* (2010) was also critical of this evidence base: “Concrete evidence that demonstrates the bottom-line effects of diversity and equality management ... is much less evident and, when tentative evidence has been found, it has tended to be context specific ... Relatively little hard data supports the claim that diversity and equality initiatives influence firm performance “ (p.978).

This underlines how data and methodological issues can make it difficult to test the main proposition. Firstly, evidence relating to the impact of a policy often sheds little light on impacts from the diversity we associate with it. Furthermore, studies attempting to capture the impact of stated policies and practices could suffer from an *Empty Shell* approach (Noon and Hoque, 2004) adopted by many firms. If firms adopt an approach where diversity practice rests purely on paper alone, survey indicators of the type used in these studies will be unlikely to capture relationships between diversity practice and business outcomes.

Secondly, the methodological approaches used in some studies in order to capture the true [causal] impact of diversity on business outcomes can rarely deal with the complicated nature of workplace environments and may omit relevant variables, leading to biased estimates. There are in fact a range of complicated inter-relationships between policy, practice, levels of diversity, intermediate outcomes and business outcomes.³¹

Workplace Equality

Moving towards more diverse workplaces can impose costs on firms. There is some evidence that these can be avoided if appropriate equality and diversity policies are put in place. These equality and diversity approaches can facilitate the transformation of workplaces into diverse environments that are more representative. There is then a potential for the securing of business benefits for the firm.

³¹ More technically, our intermediate outcomes, levels of diversity and policy itself are all potentially endogenous. Standard methods of estimation would result in bias estimates and whilst relatively simple two-stage methods exist for dealing with endogeneity where either the dependent variable or independent variable is of continuous nature, such procedures are generally not consistent with categorical endogenous variables. To capture the relationships considered here, we would need to estimate some form of multivariate probit model, accounting for the potential for errors to be correlated across our various structural equations.

Evidence on Diversity in team and group settings

This section considers evidence on business outcomes from 'team' or 'group-level' diversity. This literature falls within our category of Internal business benefits. Almost without exception, the studies we consider test the proposition that increased diversity leads to improved business outcomes (with a particular focus on problem-solving), in situations where there is more control over environmental factors (through experimental or quasi-experimental studies), therefore overcoming some of the methodological problems described above.

For example, McLeod and Lobel (1992) used an experiment with 137 students to compare the performance of ethnically diverse and ethnically homogenous groups in a brainstorming task and found that heterogeneous groups produced better quality ideas. There was, however, no impact of ethnic heterogeneity on the number of ideas produced. The authors noted that simply increasing diversity without other interventions might not have a positive impact, and that creativity might not be improved if group member ability is not well matched and the group members do not know each other well.

Riordan and Shore (1997) proposed that the degree of similarity of an individual to their group would affect their work-related attitude and behaviour. Using a survey of 1,554 employees from a major insurance company, they found that only similarity in race-ethnicity affected work group productivity, work group commitment and advancement opportunities, but that these results were more complex than expected. White participants were more positive when in mostly White groups than when in mostly minority groups but this was not true of African-American or Hispanic participants. No gender effects were reported.

O'Reilly, Williams and Barsade (1997) used survey data from 32 project teams in a large clothing manufacturer and found support for:

- a) a negative effect of diversity on group process;
- b) a negative effect of conflict on the implementation ability of the group; but
- c) a positive effect of diversity on group performance once the negative effects of conflict on performance were controlled for.

Millhous (1999) used qualitative interviews to examine the experiences of Russians and Americans working in collaborative groups and concluded that cultural differences can impede collaboration, but that there were also benefits from heterogeneous groups. Differences in culture did not generally predict failure, conflict or other negative outcomes and most groups were positively evaluated and productive.

Stahl *et al.* (2009) attempted to combine the findings from earlier studies using a meta-analysis³² of 108 empirical studies. They found that cultural diversity led to process losses through task conflict and decreased social integration, but to process gains through increased creativity and satisfaction. The effects of cultural diversity

³² Meta-analysis is a form of investigation that combines the findings from a number of existing empirical studies and uses statistical methods to combine them into one analysis.

varied depending on the context. They theorised that increased diversity led to both an increase in divergent processes, which bring different values and ideas to a group, and a decrease in convergent processes, which align the team around common objectives, commitment or conclusions. They also commented that most research on team-level outcomes of cultural diversity emphasises the negative effects on teams, but that looking at the positive effects of cultural diversity on team outcomes could also be useful.

They concluded that multi-cultural teams, characterised by differences in experiences, mental models, modes of perception, information-processing, use a wider variety of approaches to evaluating problems and have a broader reference base of potential action–outcome linkages to draw upon to inform action. All this then leads to more creativity. In addition, in a culturally diverse team, members may continue to challenge ideas and provide input long after a mono-cultural team has reached saturation level and experienced group-think. Although most research says that interactions are more satisfying when between culturally homogeneous people, they surprisingly found a positive relationship between cultural diversity and team member satisfaction and suggested that this might be because diversity satisfies individuals' needs for variety, development or adventure.

A number of researchers have found that effects of diversity in teams change over time. For instance, Watson *et al.* (1993) used an experiment including 173 upper-level undergraduates enrolled in a management course at a large university, divided into 36 work groups. Less diverse work groups were more effective than heterogeneous groups during the early tasks, while heterogeneous groups reported problems agreeing and working together etc. This meant lower task performance in heterogeneous groups during the first nine weeks. At nine weeks, the groups performed about the same on the range of problems and solutions generated, but homogenous groups remained superior in overall task performance. Group performance improved for both types of groups with overall performance being equivalent at week 13. By the end of the study (week 17), the diverse groups had become more effective at identifying problems and generating solutions, but overall performance remained the same for the two groups.

Chatman and Flynn (2001) used a similar methodology for an experiment with 119 students and 161 officers from a large US financial services firm. They found that greater demographic heterogeneity reduced group cooperation, but that this effect diminished over time. Individuals who were more demographically different from their work group changed more, becoming more cooperative as a result of contact with the other team members. Cooperation was more stable in less diverse groups. Cooperative norms mediated the relationship between group composition and work outcomes. For instance, if the cultural norm of the group was less cooperation, then diversity would have less positive outcomes.

A number of papers have discussed the different levels of diversity within teams, and concluded that different types of diversity can have different outcomes for group performance. Harrison and Klein (2007) suggested that diverse groups in organisations often fail to realise the performance benefits that result from diversity in knowledge, information or ideas. However, a diverse group is also diverse in values, beliefs and attitudes. This can lead to “separation” when group members are polarised into two extreme and opposing factions. In addition, one group member may outrank all the others in seniority, wealth, power etc. (“disparity”). Separation

and disparity can have detrimental effects on group cohesion, coordination and morale. Stahl *et al.* (2009) found that culturally diverse teams argued more if the task was complex, if they were co-located and if they had longer tenure, and communicated less effectively if larger in size. They also found that satisfaction was lower in large culturally diverse teams, and social integration was less in teams that were co-located.

Similarly, Homan *et al.* (2007) suggested that informational diversity, defined as “*differences in knowledge bases and perspectives that members bring to the group*”, enhanced group performance by stimulating the elaboration of task-relevant information and perspectives. However, this effect can be reduced or reversed when this converges with other aspects of diversity such as gender, personality differences, or attitudes and values. This can create a “diversity faultline” which is when an “us- and them” distinction emerges. Homan *et al.*'s empirical study found that informationally diverse groups performed better when they were persuaded of the advantages of heterogeneity rather than homogeneity, therefore avoiding the problem of diversity faultlines.

Jayne and Dipboye (2004) provided a more detailed analysis of the differences between the ideas of the business case for diversity and research findings and concluded that increased demographic diversity does not necessarily improve the talent pool, as it does not guarantee an increase in task-related knowledge, skills, abilities, experiences and other characteristics. Moreover, they suggest that increased diversity does not necessarily build commitment, improve motivation or reduce conflict. In fact it can result in negative outcomes such as lower commitment, lower satisfaction, more perceived discrimination and other negative behavioural and attitudinal outcomes. In addition, group-level diversity does not necessarily lead to improved group or organisational performance; in fact research has produced mixed results.

Williams and O'Reilly (1998) concluded from a large literature review that the idea that diversity management brings benefits to organisations and its employees in terms of increased productivity or creativity of work groups may be overstated, as most research has been conducted in classroom or laboratory environments. Similarly, Watson *et al.* (1993) and Kochan *et al.* (2003) comment that there is very little resemblance between the conditions that exist in many diversity studies and those in organisational settings; there are few studies in real organisations and fewer still that use objective performance measures³³.

This strand of the literature suffers from a lack of clarity on metrics across studies and research is often carried out under less-than-experimental conditions. This makes comparison of very specific findings problematic and can lead to questions over the validity of any identification strategies.

³³ These studies have relatively high internal validity, but there are questions over their external validity. Results from studies that are considered externally valid are those that remain relevant in more complex social and business environments. Internally valid studies have more robust experimental designs, that are better able to identify the sort of causal impacts that we have discussed in other parts of this study. Unfortunately it is often the case that as internal validity is increased through more robust experimental design, external validity is reduced.

Team/Group Diversity

These research studies have found a variety of positive, negative and mixed outcomes. There is some evidence that demographic diversity can bring together a greater variety of tacit dispersed knowledge (in the mould of Knight, 1921; and Stahl *et al.*, 2009) and facilitate problem-solving. There is also evidence that the accompanying heterogeneity of values, beliefs and other characteristics can hold back improved outcomes.

Remaining branches of the literature and important terminology

The matrix of terms and subject disciplines covered by this systematic review is presented in the Appendix. Much of the evidence that we have identified comes from the general management, HRM and employment studies literature and to a lesser extent from marketing and psychology. However, we were able to find very little else that is relevant.

Within the field of sociology, Herring (2009) provides some statistical evidence of a positive correlation between diversity and organisational outcomes. He distinguishes between:

1. The “value in diversity” perspective, which argues that a diverse workforce is beneficial for business.
2. The “diversity as process loss” perspective, which argues that diversity is counterproductive because of the problems it causes with group processes.
3. A view that says both 1 and 2 are true, with net impacts on business performance dependent on the magnitudes of the effects.

These three perspectives on diversity have some similarities to the findings that are suggested by the diversity-in-teams literature. Herring used data from the 1996 and 1997 *National Organizations Survey* and found that diversity was significantly correlated with increased sales revenue, increased customer numbers, increased market share and increased relative profits. This study of correlations would suggest that the positives outweigh the negatives.

There is some literature in Economics, Sociology and fields such as Human geography, on the impact of diversity at the level of region, city and country. However, whilst these have implications for firms and the diversity of the workplace, they do not investigate the link between workplace diversity and firm performance.

For instance, Sturgis *et al.* (2011) [sociology] use survey data to investigate the links between ethnic diversity and regional trust relations³⁴. The researchers used a

³⁴ Considering the responses of individuals from regions with varying levels of diversity, to survey questions asking about the level of trust and other indicators of neighborliness within communities.

Herfindahl-Hirschman Index (HHI) to measure diversity.³⁵ The focus of this study is to test whether Putnam's 'Hunkering-down' hypothesis fits the data. Putnam's theory suggests that greater diversity should lead to less social cohesion and so the authors' finding of little significant link between diversity and regional indicators of trust relations is considered positively.

In the field of economics, much of the work carried out in this area is included in our section on workplace equality approaches, as it tends to appear in industrial relations journals. Work that considers diversity, particularly at an organisational or workplace level, is sparse when compared to the literature that has developed around discrimination and equal opportunities. Dex (1986), reviewing the economic research on discrimination, found that in most circumstances, discrimination increased employers' costs by restricting labour supply. Econometric work that considers issues such as gender (Harkness, 1996; Manning and Swaffield, 2008) and ethnic (Blackaby, et. al. 1998) pay gaps is separate and distinct.

Market and supplier diversity

One aspect of Figure 1 that we have not yet considered, are the concepts of Supplier and Market Diversity.

Supplier diversity gives all businesses equal opportunities to compete. In the UK this is not seen as positive discrimination, but about 'levelling the playing field' to give under-represented businesses the same opportunity to supply goods and services to both public and private sector organisations as other qualified suppliers. For instance, *Transport for London* defines "Diverse Suppliers" as: Small and Medium Enterprises (SMEs); Black, Asian and Minority Ethnic (BAME) businesses; suppliers from other under-represented or protected groups; and suppliers with a diverse workforce.

The benefits of supplier diversity are seen as:

- improved customer satisfaction;
- government compliance;
- enhanced supply chain processes/performance;
- increased flexibility;
- enhanced innovation/creativity;
- improved local economies;
- increased market share;

³⁵ A measure usually used in studies of market concentration. It is calculated by squaring the market share of each firm in a market and summing the result. The HHI can range from zero to 10,000 and, when applied to the issue of diversity, provides an indication of increasing diversity (with each 'firm' replaced by an ethnic group in the calculations)

- increased supplier competition and sourcing; and
- better quality problem-solving.

Market diversity involves studying the impact of socio-demographic identities and influences in Business to Consumer (B2C), Business to Business (B2B), Consumer to Consumer (C2C), and Supply Chain Management (SCM). Some practitioner studies (for instance, Urwin *et al.* 2011) suggest that marketplace diversity initiatives can give significant returns on investment. The proposed benefits arise from the potential for firms to respond to global competition, instant communication, customised and locally responsive market requirements for products and services by tapping into differing cultural and ethnically diverse environments (Senge and Sterman, 1991; Golembiewski, 1995). This ability of firms to ‘read’ diversities in the environment and respond in an agile way is embodied in the concept of absorptive capacity (Cohen and Levinthal, 1990; Zahra and George, 2002) and corporate agility (Sambamurthy *et al.*, 2003; Mathiyalakan *et al.*, 2005) (concepts that we return to in Section 4).

However, although useful, the specific concepts of supplier and marketplace diversity are considered predominantly within the practitioner literature. There may be some value in these approaches and generally they are of interest, but there is simply too little written on them in the academic literature and robust evidence of any impact on business outcomes is limited.

Bringing together the findings: the importance of context

Evidence from team-based diversity studies and research on workplace equality approaches suggests that:

PROPOSITION 7: Diversity, if well managed, has the potential to lead to both *Internal and External* business benefits; but if it is poorly managed (in either workplace or team settings) there is the potential for increased business costs.

This proposition points out the importance of context: the business case for diversity is dependent on labour market context, organisational competitive strategies and (in team or group settings) the actions of team leaders or other facilitators.

This is in line with Ozbilgin and Tatli (2011) and Kochan *et al.* (2003) who conclude that diversity does not have a positive impact on performance consistently under all conditions, and that context is potentially crucial in determining diversity’s impact on performance. These authors suggest that negative impacts of racial diversity can be mitigated by training and development-focused initiatives. Chatman *et al.* (1998) simulated an organisation with MBA students. They found that the benefits of demographic diversity are more likely to emerge in organisations that make membership salient and discourage people to emphasise individualism and distinctiveness amongst members.

Chatman and Flynn (2001) focused on the level of contact between team members. They found that, following contact with diverse team members, people were more likely to re-categorise colleagues in terms of work-group membership, rather than their previous demographically based identities.

Polzer *et al.* (2002) conducted a longitudinal study of 83 work groups of MBA students and found that interpersonal congruence³⁶ moderated the impact of diversity on group processes and performance. In groups that achieved high interpersonal congruence, demographic diversity enhanced performance in creative tasks and in groups with low interpersonal congruence, demographic diversity impaired performance.

Increasing diversity increases 'difference', and this has the potential for both positive and negative outcomes. This suggests that some aspects of increased diversity can hold back enhanced business outcomes, which would potentially flow from other aspects of change. This underlines a central need for policies and practices that capture the positive aspects of increased diversity, and ensure that they are leveraged for business benefit.

PROPOSITION 8: The business benefits of increased diversity may only be secured when accompanied by appropriate policies and practices, including appropriate training for those who lead teams.

The implication is that, studies which attempt to identify quantifiable business benefits of equality and diversity must effectively,

- clarify the specific type of *Diversity* (gender, ethnicity, age, disability etc.) being considered and measure it consistently across studies,
- capture, and control for, the very different *Internal* and *External Diversity Contexts*; including the nature of the external competitive environment, the extent of any internal diversity-management approaches and/or strategic initiatives to leverage diversity for business benefits,
- link the interactions between these indicators of *Internal* and *External, Diversity* and *Diversity Contexts*, with measurable business outcomes (again with consistency across studies).

Figure 1 hinted at these challenges. Our review of the evidence suggests that even when we have experimental (team-based) studies, results can be conflicting because there is so much that is not captured in each individual study.

³⁶ The degree to which group members see others in the group, as others see themselves. For example, if a member of the team sees themselves as a good communicator, and the rest of the team agree that this is the case, then there is a high degree of interpersonal congruence within the team.

PROPOSITION 9: In attempting to capture quantifiable business benefits of equality and diversity, we face substantial methodological challenges. Many studies manage to overcome some of these challenges, but this still leads to variability in findings.

In each situation where we observe increased diversity, the nature of that diversity, the internal workplace context and external environment are likely to require different approaches to ensure business benefits. There is a need for more research in this area, which takes forward existing work analysing diversity in teams, workplace equality and diversity management. However businesses can gain insight from the Strategy literature, and the findings from Case Studies, as these approaches to investigation allow insight into particular contexts where diversity may lead to business benefits.

Strategic Approaches

If the likelihood of equality and diversity leading to enhanced business outcomes depends on the wider business context, firms may need to adopt a strategic approach, with diversity considered as only one aspect in a wider audit of the firm's strategic capability.

This section introduces some of the literature that considers diversity in this strategic context, describes relevant approaches and illustrates them with case studies.

Strategic approaches to equality and diversity

The strategy of a firm is necessarily contingent and takes into account factors such as the external environment, industry success and survival factors, as well as workplace context.

Key concepts in the Strategy literature relevant to diversity

Diversity Density: the extent to which individuals from diverse groups are represented at all levels of the organisation.

Diversity Mindset: the extent to which an organisation's senior executives view diversity as a business strategy rather than a management (or HRM department) issue.

Absorptive Capacity: an organisation's ability to recognise the value of, gather and apply, new external knowledge from the environment and make strategic choices that contribute towards competitive advantage.

Customer Agility: the ability of firms to leverage the voice of the customer to gain market information and detect competitive opportunities.

Cognitive Diversity: the extent to which we observe differing cognitive approaches amongst the individuals of a group or team.

As Hopkins *et al* (2008) suggest, the higher the *diversity density* that exists within an organisation, the easier it is for it to assimilate knowledge of *external diversity* and apply it through strategic actions. This proposition, derived from the work of Cox and Blake (1991), underlines the importance of diversity at all management levels and within a variety of job categories. Here we see the firm's *internal diversity* as an essential prerequisite for the creation of a *diversity mindset*.

A number of studies have explored the concept of a global or 'executive' mindset, generally defined as the ability of an organisation's senior executives to demonstrate openness to, and awareness of, diversity across cultures and markets (Gupta & Govindarajan, 2002; Laczniak & Lusch, 1997; Paul, 2008). The studies suggest that a global mindset guides senior executives' collection and interpretation of new information about these markets.

However, it is unlikely that such aspects of diversity translate seamlessly into business benefits without additional facilitative structures in place. For instance, if employees do not feel engaged or included in the workplace, they are unlikely to offer up insights that improve *absorptive capacity* (Cohen and Leventhal, 1990; Hopkins *et al*, 2008; David, 2010). Hopkins, *et al.* (2008) further expand 'diversity mindset' to include a component whereby executives recognise the need to create a 'safe' environment that facilitates knowledge sharing among the firm's diverse workforce. We have already considered arguments that more diverse marketing teams may allow different cultures to be better understood (*Customer Agility*). Such teams need to be supported by appropriate infrastructure, such as information systems that allow up-to-date, accurate, information on market segmentation.

The 'mini case' below illustrates a diversity-based solution applied by a high street café chain faced with external challenges. In situations where we expect business benefits to arise, the link between diversity and enhanced business outcomes is dependent on wider facilitative structures.

Mini-Case Example 1

A leading high street cafe chain wanted to attract and retain diverse employees to match its customer profile by building an attractive employer brand.

It developed benefits that would appeal to a multicultural, predominantly young, workforce and built an employer brand reputation of being an exciting, sociable place to work. Innovative and themed social events were designed to embrace different cultures. For instance, employees dressed to represent their country or their country's football team colours; celebrating the Olympic Games by adapting their uniforms and decorating its outlets with flags and posters, charting the achievements of different countries. Managers were informed about important dates, dress codes, special considerations and key facts for all major religions.

It has developed such an attractive employer brand that most applicants hear about it by 'word of mouth'. Diverse employees now reflect the customer base and are better able to be locally responsive to customer needs. For example, having multi-national staff in its Central London outlets has enabled it to communicate better with non-English speaking tourists. This has contributed to it notching up some record sales weeks during the economic downturn.

The case study provides insight into the approach of a particular firm, but also underlines the challenge for more empirical studies. Written up as a case study, there would seem to be a compelling business case for diversity. However, it would be challenging to directly relate the improvements to diversity.

The above discussion sits most clearly within our category of *External Business Benefits*. In fact, the benefits of diversity are derived from the firm's ability to absorb information on *external diversity* and adapt accordingly, despite the clear need for the firm to develop [internal] *diversity density* and *diversity mindset*.

In contrast, the strategy literature that considers *cognitive diversity* tends more towards our category of *Internal Business Benefits*. Consider for instance, a longitudinal case study illustrating the potential for *cognitive diversity* to enhance

organisational learning and absorptive capacity (David, Cox and Haberberg, 1999). The study exposed senior executives in several software companies to facilitated scenario planning interventions, and then measured shifts in cognition using causal mapping techniques developed by Eden (1992) in pre/post intervention interviews. The conclusions suggested that actively involving senior executives in scenario planning workshops generated more diverse thinking and provided richer 'mental models'. This, in turn, improved 'absorptive capacity' and the ability to identify, understand and exploit opportunities in the external environment (whether related to demographic diversity or otherwise). The study suggests that diversity of thinking is desirable of itself. The case study below provides some illustration of this approach in practice.

Mini-Case Example 2

A Hi-Tech global Corporation had to transform its business model to respond to dramatic changes in the employment market and its customer base. Its business needed to transform from selling hardware to selling service solutions to new types of customers, e.g. IT Directors, Finance Directors and CEOs.

Its Employee Surveys had demonstrated a direct correlation between employee engagement, customer satisfaction and business results. It decided to communicate a clear diversity vision across the organisation, focused on enhancing the delivery of its business imperatives. A UK Diversity Task Force was established comprising twelve people from across the organisation and from different levels.

Action plans generated by the Task Force were integrated into the overall business agenda of addressing future profit generation needs. An action outcome was that senior and middle managers should attend workshops to develop their capability in building high performance teams through valuing difference and how to harness the cognitive diversity offered by these differences to enhance team performance, problem solving and creativity.

Even in the economic downturn the Company has continued to grow and attributes this to the active role its employees have played in helping it succeed in driving the transformation of its business.

The interaction of *diversity density*, *diversity mindset* and other characteristics of the firm contribute towards the development of 'distinctive' capabilities that in turn allow the accumulation of strategic resources. Interventions to encourage and foster diversity in organisations require a diversity friendly infrastructure at the organisational level (David, 2010). Interventions that focus in a general sense on 'valuing diversity' are not sufficient to bring about the sustainable benefits that translate into organisational performance (Golembiewski, 1995). Similarly, even if many individuals develop diversity-friendly relationships in a large system, it is not at all clear that systemic behaviours and attitudes will change sufficiently to make a difference.

PROPOSITION 10: Single threaded diversity solutions, such as reliance on recruitment or requiring every employee to take diversity training, are not sufficient to create lasting change or sustainable advantage.

The suggestion is that to achieve sustainable diversity friendly systems, systemic and structural organisational components need to change in tandem with the introduction of diversity policies. The 'mini case example' below indicates how such a multi-dimensional approach can work³⁷.

Mini-Case Example 3

A professional services firm, which had a well-developed diversity and inclusion strategy for several years [and therefore a diversity mindset], recognised the importance of bringing together staff with common interests and considered that networks were key in achieving this. A particular business benefit sought by the firm was the encouragement of staff engagement, which it considered to be directly linked to increased talent retention.

The firm had been actively providing support for its population of working parents with a variety of initiatives including regular parenting seminars, emergency childcare and comprehensive maternity coaching. It decided to launch a parents' network using online social networking technology to bring together working parents globally and provide a source of useful information. Much of the information came from parents themselves [e.g. websites for children's clothing and suggestions for activities during school holidays].

The initial content of the site was developed by a group of interested working parents who began posting information. External providers were brought into the project to provide expert guidance and advice. When online, a participant's hierarchical position within the firm was not known. This provided a level of anonymity, which encouraged dialogue across grades. Reported outcomes included an increase in staff engagement, improved staff retention among single mothers, and a positive impact on the firm's external reputation.

By using its diversity mindset to see both outside the firm (improve its interaction with external stakeholders) and align some elements of its structure and architecture in response (operational agility) this firm's initiative has contributed significantly to increasing engagement, the retention of talented women and its reputation as an Employer of Choice.

³⁷ Other successful examples include the Metropolitan Atlanta Rapid Transit Authority (Golembiewski, Robert and Kiepper, 1988) and Avon Products (Thomas, 1991), which show how effective results are only produced where there is close attention to systemic procedures as well as to the organisation's structural dimensions.

Viewing Diversity as Strategic Capability

In considering the wider strategic context, we can see diversity as one of the drivers of the firm's internal capabilities and as something that is accumulated as a strategic resource. As David (2010) points out, strategic resources are things an organisation has access to such as retail branches or a loyal customer-base. The strategy literature emphasises the continuous development of embedded capabilities, as these enable an organisation to effectively utilise its strategic resources for competitive advantage.

The implication is that firms begin by identifying the key success requirements for the business, in terms of industry success and survival factors (*ISSFs*) and then consider the ways that diversity can help to secure such requirements. The emphasis is on starting from a broad perspective, which takes into account the overall business goals and the external environment/context of the industry.

Practice-oriented research in this area³⁸ shows how this process can expose blind-spots, where diversity initiatives have not yet been implemented, but may have the potential for a significant return on investment. The development of a Diversity Scorecard³⁹ is often central to such approaches (as it forces a comprehensive review of existing and potential equality, diversity and inclusion initiatives).

However it is important to note that the capability to manage diversity strategically in this way is not one that can be acquired instantaneously: first, there are critical steps in the process by which diversity is achieved. A useful model is provided by Wheeler (1998), and elaborated by David (2010). This model identifies typical 'steps' or phases relevant to organisations as they go through the process of creating and developing diversity, through to fully leveraging diversity for competitive advantage.

PROPOSITION 11: A strategic approach to diversity begins with consideration of a firm's key requirements for success, and then considers where diversity can help achieve such success.

The implication is that success in securing the business benefits of diversity is driven by a pragmatic strategic approach, where diversity is leveraged to tackle a specific business challenge.

³⁸ See for instance, Urwin, P., Karuk, V., David, A., Dodds, I. and Moss, G. (2011), *The Strategic Economic Impact of Diversity on Business Performance*, Commissioned by Diversity Works for London.

³⁹ Hubbard. E. (2004), *The Diversity Scorecard*, Elsevier-Butterworth-Heinemann.

Implications

In this final section, we draw out the implications of the research findings for firms and policymakers.

Firms

Revisiting our extension of Becker's model, the findings from a review of the literature suggest an adjustment. There is some evidence to support *Internal* and *External Business Benefits*, and this implies a diversity coefficient that incentivises recruitment of minority employees. However, we also have evidence of costs associated with diversity and these have to be overcome to realise any business benefits (whether *Internal* or *External*). This implies an important distinction between firms that already have equality and diversity structures in place and those that do not:

- Firms that do not already have a history of equality and diversity approaches (for whatever reason), may perceive the costs of increased diversity outweigh the potential business benefits. They have a diversity coefficient that is lower than firms who have already incurred the costs of policies and practices that manage diversity.
- Firms that already have the relevant equality and diversity structures in place are more likely to consider that the business benefits of increased diversity outweigh the potential costs.

However, this may be less of an issue when considering *Internal Business Benefits*, as we may expect this kind of benefit to accrue more immediately and firms may be able to create 'pilot' diversity initiatives focused on particular pockets of their business activity, even when extensive equality and diversity infrastructures do not exist in the wider environment. The suggestion from studies of diversity in teams, that positive impacts arise in the presence of well-trained facilitators, presents these firms with a business argument for focused diversity initiatives (which could then prove their worth and be rolled out across the business).

In contrast, firms that do not already have extensive equality and diversity structures in place, may perceive the costs of achieving *External Business Benefits* as potentially greater than the benefits, in the short-run. This is a rather myopic approach, but one can perhaps see that in a recessionary context (when immediate survival is perhaps more of an imperative), the potential for longer-term gains associated with *External Business Benefits* may be less effective as a driver of the equality and diversity agenda⁴⁰.

⁴⁰ There is a suggestion in the research that the interaction between increasing diversity and associated costs may not be linear – from a very low base, costs increase until they begin to fall; and benefits only kick in when a critical mass of diversity is reached. This implies that our diversity coefficient would provide even less incentive for firms at the beginning of the diversity journey. This is an amount of detail that we are not able to comment on, given the research as it stands, but our general implications would not change.

Following this reasoning and implications from the strategy literature, firms that already have extensive equality and diversity structures in place are (other things remaining equal) likely to have already achieved a more representative workforce. Therefore, they are also less likely to perceive a continued significant pull from external business benefits. Our discussion of strategic approaches to diversity gives some indication of how firms at this stage of the diversity journey are working to create structures that ensure effective leverage of diversity for either external or internal business benefit.

We cannot ignore the fact that much of the work in this area, and therefore our theoretical framework, is less appropriate for smaller businesses. From the perspective of these firms, that do not already have extensive equality and diversity approaches in place, continued expansion of the legislative framework adds to perceived costs.

The conclusion for firms must be that there are no hard and fast rules. Firms that have spent time and effort developing robust equality and diversity initiatives in better economic times now possess diversity as *resource and capability*. In these straightened economic times, they are now able to build a more strategic approach to diversity.

Policymakers

Whilst the UK legal framework is predominantly influenced by concepts of equal treatment, it also contains distinctive, unequal treatment-inspired legal rules in respect of certain protected identities (for instance, in respect of age, disability and pregnancy and maternity) and some general legal rules have moved decisively away from the 'equal treatment' conception of equality⁴¹. There have also been some key points along this journey from equality law's equal treatment origins, with the creation in 2000 of the public sector equality duties and enactment of a single equality duty in the Equality Act 2010. However, perhaps most importantly for the discussion here, there is now a considerably extended scope for lawful voluntary positive action created by the Equality Act 2010 (see for instance, Barmes, 2009).

However, whilst these developments suggest a greater freedom for organizations to take positive action, there remain questions of how EU law will affect interpretation of the new UK positive action provisions. This extended scope for voluntary positive action can either be seen as going further than European Union equality legislation or as contravening it. Firms are unable to tell *a-priori* which of these views will be taken by the European Court of Justice. As Barmes (2010; page 1) suggests,

“A significant effect of this state of affairs is that in areas of uncertainty and contestation, of which positive action is a paradigm example, organizations are ill advised to take domestic law at face value. Rather they need to look behind the facade to see if EU law has an impact.”

⁴¹ See for instance, Barmes, L. (2010), “Navigating multi-layered uncertainty: EU, Member State and Organizational Perspectives on Positive Action”, in Healy, G .Kirton, G. and Noon, M. (eds) *Equality, Inequalities and Diversity - From Global to Local*

Whilst there is potential for the legislative framework to be aligned with diversity approaches, the uncertainty facing firms represents a significant barrier if they wish to take a strategic approach, which potentially promotes the interests of one specific protected group through differential treatment. From our discussion of the legislative framework, policymakers and firms need to work together to ensure that strategic approaches to diversity do not fall foul of EU-wide rules.

These are important and complicated trade-offs that require extensive and detailed debate between policymakers, practitioners and academics. Unfortunately the existing evidence-base needs to be expanded further, so that such discussions can be better informed going forward.

Conclusions

This research considered the evidence for the business case for equality and diversity in private sector organisations.

The research concludes that the business case for diversity is dependent on labour market context, organisational competitive strategies and the actions of team leaders or other facilitators. Therefore, the business benefits of increased diversity may only be secured when accompanied by appropriate policies and practices, including for instance appropriate training for those who lead teams.

The variability in the findings from the review is also due to the methodological challenges of capturing quantifiable business benefits of equality and diversity.

In each situation where we observe increased diversity, the nature of that diversity, the internal workplace context and external environment are likely to require different approaches to ensure business benefits. However businesses can gain insight from the Strategy literature, and the findings from Case Studies, as these approaches to investigation allow insight into particular contexts where diversity may lead to business benefits.

Therefore, the four key conclusions from the research are that:

- Diversity, if appropriately managed, can result in business benefits. However, if poorly managed, it can also increase business cost.
- The firm's economic and organisational context is crucial in determining the way in which equality and diversity brings about business benefits.
- There is no single approach that businesses can adopt to ensure equality and diversity are beneficial.
- Strategic approaches are likely to be more successful: equality and diversity need to be embedded in the business organisational strategy, not ad-hoc additions to the business.

There is a need for more research in this area, which takes forward the existing work in terms of diversity in teams, workplace equality and diversity management, and sheds light on the ways strategic approaches work in practice, possibly through a thorough assessment of case studies.

Appendix

This Appendix contains a brief description of the Method for this systematic review and a note on metrics used across studies of the business case for diversity.

Method

Systematic reviews aim to systematize the process of reviewing an evidence base and ensure that it is transparent, and therefore, replicable. Organisations such as the Cochrane Collaboration (2001) were set up to specifically promote the production of such reviews within medicine and, in a parallel development, the Campbell Collaboration has attempted to do the same in the social sciences.

Following the standard approach, the first stage of the systematic review undertaken here involved the identification of review questions, key words and search strings relating to the 'business case for equality and diversity'. The development of review questions and search terms was carried out through a process of engagement with academics and practitioners across a range of relevant disciplines; in workshop events, face-to-face meetings and by correspondence.

An outcome of this first stage was the creation of a matrix of search terms across different disciplines, which defined the parameters for a search of evidence appearing in the academic literature (i.e. published in peer-reviewed journals); and a list of key practitioner sources.

The criteria for a first filter of this literature was one of 'relevance', with direction given to those carrying out the initial search to err on the side of selection rather than rejection of a paper for consideration. In the next stage, the project team reviewed these papers to consider both the quality and relevance of each piece of literature – those studies selected at this stage then formed the main body of our review.

Review questions

The Department for Business Innovation & Skills (BIS) and the Government Equalities Office (GEO) commissioned this research to comprehensively assess the evidence (principally the academic peer-reviewed literature) on the business case for equality and diversity. The research was tasked to consider the case for organisations to adopt equality and diversity policies and measures in order to realise business impacts.

The study aimed to (i) develop a rigorous conceptual framework within which to structure the research, (ii) identify and de-fragment the evidence base (drawing on econometric and qualitative research as well as case studies), (iii) assess the strength of the evidence base and (iv) identify and assess relevant factors that influence the realisation of any business impacts.

The aim was not to make the business case. Rather the study aimed to synthesise the existing evidence, consider that which is robust and then provide a dispassionate picture of this evidence within a generic framework for analysis; identifying gaps, conflicting messages and considering important questions, such as,

- if the diversity business case is so compelling, why aren't all firms doing it?,
- can we identify diversity-related business behaviours principally driven by the profit motive, which also move forward the equality agenda; or are there potential conflicts between equality and diversity approaches?

Scope of review and key search terms

Three practitioner-focused events (on 2nd November 2011; 15th December 2011 and 10th January 2012) and correspondence with experts from the fields of HRM, economics, law, sociology, and business (including strategy, management, marketing and psychology among others) defined the parameters for the systematic review.

More specifically, the initial correspondence resulted in initial outline matrices of search terms and strings, which then formed the focus of discussions in the practitioner events.

Table 1 contains the final parameters for the systematic review arising from these events. The following list of terms were also considered as being potentially relevant, but did not form part of the review unless, at completion of the review, they were not identified anywhere in the literature collated. The list acts as a safety net to ensure that we have at least something on all of the terms considered as relevant in the three events.

- Gender; inequalities; age; disability; sexual orientation; religion; ethnicity; intersectionality; work-life balance (WLB); employment gaps; younger workers; industrial segmentation/segregation; unconscious bias; supplier diversity; procurement; social class; sticky floors; leaky pipeline; positive action; positive discrimination; race equality; social model of disability; social norms; representation; Boards; health and safety; micro-inequities; hyper-formalisation; talent management; face fitting/image management; public procurement; recession; migration; CSR; X-cultural competency; generation Y; invisible inequalities; mutual gains; holistic regional development; regulation/social regulation; fair trade.

Table 2 details the key journals that formed the focus for a more 'inductive' aspect of the study, with the last four years of each of the listed journals being trawled to see if any issues/aspects had been missed.

Table 3 details the practitioner sources specifically pursued. The aim is not to be exhaustive, as there is simply too large a volume of practitioner literature.

We considered findings from all relevant branches of the literature, even where this included a predominance of (more qualitative) methodological approaches that do not attempt to identify causal impacts.

Search methodology

A search for *practitioner evidence* was made, from websites of the networks, organisations and publications listed in Table 2. Results of this initial search were then brought back to meetings, discussed and additional action suggested.

Academic sources: Using the matrix of search terms in Table 1, various search engines were used, including JSTOR, Google Scholar and Business Source Complete. As one would expect, searching on the keywords generally returned large amounts of irrelevant material and only a few highly relevant articles. However, using the references of these articles proved highly effective in finding more relevant articles. Thus, methods of cross-referencing were employed to complement the more general searches.

For instance, starting with the term “multicultural”, a search was carried out in JSTOR that returned 7,038 English language articles. Restricting the disciplines to business, economics, finance, law, management and organisational behaviour, marketing and advertising and sociology reduced this figure to 959, only one of which was sufficiently relevant to the topic (“Globalisation and the Market for Team Mates”). Most were immediately excluded as irrelevant because they were not about business. Articles about business were only considered relevant if they specifically addressed the effects of multiculturalism on the company in a way that impacted on the bottom line. Searching the references of this article led to further relevant hits.

Outcomes in Brief

The key criterion in this review was to find articles that were not simply about equality and diversity, but specifically relevant for assessing impacts on company profitability. Articles addressing the effect on a determinant of profitability (e.g. low turnover) were also considered relevant.

Practitioner sources: 48 articles

Generally the sources under review can be categorized as follows:

1. Government and Supra Government bodies (EU)
2. Corporate/Business organizations
3. Non-profit business organizations

Category 1: more regulatory in nature and efficiency-based, however it is difficult to find a common KPI to measure efficiency. The empirical evidence of “benefit” is contingent upon the definition of efficiency, which varies from one organisation to another.

Category 2: more relevant, succinct and empirical in nature. However more confined to either multi-national organisations or regions/entities with a diverse demographic profile.

Category C: tend to consider social aspects rather than business.

Academic journals: 64 articles

The criteria for assessment of the quality of the article were its relevance, the robustness of the methodology, and how applicable it is to more general cases. Empirical studies using controls were given more weight, but we also recognise the limited external validity of some studies.

Metrics of Diversity and Business Outcomes

There is the potential for variety in measures of diversity. For instance, the majority of the literature which considers gender diversity will simply measure the proportion of women (for instance on the boards of FTSE 100 companies) and firms with a higher proportion of women will be considered more diverse. In these contexts the assumption is that the ideal level of diversity is 50/50⁴². When we begin to consider the literature which deals with, for instance, ethnic diversity and age diversity the same approach is adopted, but it is less clear what an 'ideal' level of diversity would be. In many cases it is a level of representativeness of the population as a whole, but then we are drawn into debates over the extent to which any external benchmarks for this representation should be regional (especially in the case of ethnic diversity, which varies substantially across UK regions).

Within this context, there is also a question of how we define 'more' and 'less' diversity. For instance, Sturgis et. al. (2011) use a *Herfindahl-Hirschman Index* (HHI) which is a measure usually utilised in studies of market concentration - calculated by squaring the market share of each firm in a market, and then summing the result. The HHI can range from zero to 10,000 and when applied to the issue of diversity, it provides a good indication of increasing diversity (with each 'firm' replaced by an ethnic group in the calculations).

However, this type of clarity is simply not apparent within the wider diversity literature and even large meta-studies often fail to clearly define their measures and metrics of interest (for instance, Stahl et. al. 2010). Thus, when moving on to consider the diversity literature which considers diversity of values, beliefs, knowledge, skills etc. it becomes even harder to clearly define what measures are being used to capture diversity.

Similarly, there is immense variety in the range of potential business outcomes that studies attempt to relate to differing levels of diversity. Studies of gender representation at board level use indicators such as stock price performance relative to industry averages; the team-level studies are more concerned with various indicators of problem solving (variously defined) and when we come to consider the literature on HR Performance, there are a range of intermediate outcomes such as workforce satisfaction and commitment. Case-study evidence often focuses on diversity initiatives to reduce staff turnover and/or improve staff engagement.

In the present study we are focused on identifying evidence of impact, rather than limiting ourselves to a specific type of business impact or specific types of diversity.

⁴² See for instance, Government Equalities Office (2010), *The case for equality – draft report for Phases 1 & 2*, April

In the text it is made clear what particular impacts we are considering and, where possible, which measures of diversity are being used. However, the majority of the studies do not consider the issue of diversity metrics.

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