The Business Case for Diversity: Is Diversity Cost Effective?

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Abstract

The business case for diversity is that diversity initiatives create a competitive edge for an organization. This paper identifies nine possible ways such a competitive edge might occur: better customer service, better problem solving, better critical analysis, tolerance of different ideas, better understanding of organizational communication patterns, more flexible, valuing fairness and respect for individual contributions, more innovative, and sharing best practices. A review of the business literature shows that diversity effects upon business indicators, such as return on equity, sales, and market share, depends upon driving factors, such as company strategy. Recommendations for military use follow.

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One can make the case for diversity several ways (Cox, 1993). It is the legal thing to do. It is the moral thing to do. And it is the right business practice to follow. In other words, diversity management makes good business sense. This latter statement is known as the business case for diversity – diversity management increases profits by providing a competitive edge to the firm (Karsten, 2006). Here we will look at the various aspects of diversity that might contribute a competitive edge to an organization practicing diversity management. Then we will examine the evidence. Does the business case work?

Reasons that Diversity Can Create a Competitive Edge

There are several possible reasons that diversity can produce a competitive edge for an organization.

1. Better customer service

   The argument here is that most organizations have different kinds of customers; i.e., a diverse customer base. A diverse employee base can better understand and communicate with different types of customers and thus better serve their diverse needs (Cox, 1993, 2001; Karsten, 2006; Kochan, Bezrukova, Ely, Jackson, Joshi, Jehn, Leonard, Levine & Thomas, 2003; Konrad, 2003). In short, "your workplace should reflect your customer base" (Minyard quoted in Robinson & Dechant, 1997, p. 26).

   A good example of this concept is Coors Brewing Company (MillerCoors, 2008). Coors began as a company with a homogeneous white workforce brewing one brand for mostly white male college students. Currently Coors brews over 20 brands for many different customers. Its workforce composition now mirrors its diverse customer base.

2. Better problem solving

   A team composed of diverse members has the advantage of more information, richer perspectives, and a greater number of approaches to solving problems than a team composed of the same type of people. In short, diversity can be a knowledge resource for problem solving (Karsten, 2006; Richard, McMillan, Chadwick, & Dwyer, 2003; Thomas, 2005). Moreover, diverse groups can apply divergent thinking (looking at differences) rather than convergent thinking (looking at the same thing) to solve problems (Cox, 1993, 2001; Thompson, 2003).

   To illustrate, Ford Motor Company (2008) uses its employee resource groups to suggest better ways to serve minority customers. Ford finds that heterogeneous teams with women and minority members produce better solutions to complex problems than traditional white male teams.

3. Better critical analysis

   A diverse team has a wider expanse of experience and knowledge than a homogeneous team. The diverse team can thus better evaluate organizational ideas from different perspectives (Cox, 1993; Konrad, 2003). Moreover, counterarguments based upon these ideas can improve critical analysis through introducing differing view points and evaluating different scenarios (Thomas, 2005).

4. More tolerance of different ideas

    A diverse employee base would contain a broad expanse of ideas reflecting different views and values. To best use these various perspectives, the organization must adopt a tolerant attitude toward employees holding different ideas (Cox, 1993; Konrad, 2003).

5. Better understanding of organizational communication patterns

    Diverse groups of employees may communicate with each other face to face, by cell phone, or email. Further, they may use different phraseology and even different languages in communication. Networking may occur through different media. Becoming aware of these diverse communication techniques allows a better understanding of patterns of knowledge flow around the organization (Jackson, Joshi, & Erhardt, 2003).

    For example, Chevron (2008) uses its networking communication patterns to improve mentoring. They pair mentors with employees from different networks to broaden employee knowledge and skills. Surveys show that employees believe that this networking extension adds business value to Chevron.

6. More flexibility

    In order to respond to diverse customer needs, the organization must be able to change quickly to meet rapidly changing customer desires, competitor actions, and economic fluctuations. In short, dealing with varied and changing environmental factors forces the organization to be flexible (Cox, 2001). Such organizations can reorganize or retool quickly to take advantage of environmental changes. Flexible organizations thus have a distinct advantage in highly complex and volatile environments.

7. Valuing fairness and respect for individual contributions

    In order to capitalize on the advantages of increased information and wider, richer perspectives, the organization must allow individuals to feel that they operate in a fair environment that values their inputs (Cox, 1993; Mor Barak, 2005). Organizational values of fairness and respect for the individual then are not only morally correct stances, but deliver better organizational results.

    Diversity climate instruments can measure the degree of perceived fairness in the organization. Diversity climate consists of perceptions of the presence and enforcement of relevant policies, such as affirmative action, perceptions of the fairness of organizational procedures, such as performance evaluation and the reward structure, the diversity reputation of the organization, the diversity commitment of top management, and the overall tendency of the organization toward inclusion of all employees (Avery & McKay, 2006; McKay, Avery, & Morris, 2008). In addition, Holvino, Ferman, and Merrill-Sands (2004) suggest other items that a diversity climate survey should cover: fair appraisal, reward, and promotion; access to job-related information; influence in decision making; opportunities to acquire new skills; opportunities to mentor and network; and chance to serve diverse customers.

8. More innovative

    In order to serve the diverse needs of both customers and employees, diverse organizations must not be locked into certain modes of operations. Rather, to survive they must be innovative and look to new and different ways to serve their customers and their own members (Cox, 2001; Hays-Thomas, 2004; Thomas, 2005).

A good example of diversity innovation is Bank of America, which has an increasingly large Latino customer base. To better serve their Hispanic customers, Bank of America partners with the La Raza Hope Fund to invest in low and moderate income Hispanic communities to create more business opportunities (Bank of America, 2008).

9. Share best practices

Organizations practicing successful diversity initiatives can benchmark – share these best practices with other organizations (Layne, P., 2002; Wheeler, 2001). Organizations thus can save valuable time and effort in adapting the best practices of other organizations that can work for them, rather than testing new initiatives in a trial and error mode. For example, Bank of America maintains both internal and external benchmarking for best practices (DiversityInc, 2008).

Moreover, government organizations, such as the Equal Employment Opportunity Commission (EEOC) and professional organizations, such as the Society of Human Resource Management (SHRM), maintain lists of best practices online that diversity managers can easily access (Kalev, Dobbin, & Kelly, 2005).

Evidence for the Business Case for Diversity

There are a number of studies published in top rated management research journals that provide support for the business case for diversity.

Financial Performance.

Simons, Pelled, and Smith (1999) found that job-related diversity (diversity in jobs held, education, and time with the company) among executives produced better financial performance than non-job-related diversity (age). Further, Keller (2001) found that functional diversity (job and technical expertise) improved technical quality and budget performance in research and development organizations. On the other hand, Kochan et al (2003) found that racial diversity was positively associated with growth in a financial services company's business portfolios. Moreover, Richard, et al (2003) showed that racial diversity enhanced the return on equity (ROE) of banks with an innovative strategy, while racial diversity decreased ROE of banks with a low innovation strategy.

Market Performance.

Frink, Robinson, Reithel, Arthur, Ammeter, Ferris, Kaplan, & Morrisette (2003) found that optimal market performance occurred when the gender distribution of a company was 50% female and male. In addition, Kochan et al (2003) found that gender diversity was positively related to speed of response to customers in an information processing firm. McKay, Avery, & Morris (2008) showed that strength of diversity climate (fair treatment, respect for different views, and visible commitment to diversity) moderated sales performance. Blacks and Hispanics sold more in a strong pro-diversity climate. In fact, strong diversity climates produced a yearly increase of $20,800 gain in sales per black employee and a $27,040 gain in sales per Hispanic employee.

Problem Solving.

Watson, Kumar, and Michaelson (1993) evaluated homogeneous and heterogeneous (gender, race, and ethnicity) problem solving groups in an organization. They found that the homogeneous groups produced better solutions at first, perhaps because their members with similar backgrounds allowed cohesion and other group dynamics to coalesce more quickly. After 17 weeks, however, they found that the heterogeneous groups were producing more innovative solutions. They conclude that over time diverse groups overcome their surface differences and can thus focus upon deep attributes, such as knowledge, values, and experience, that can improve innovative problem solving.

Strategy.

Richard and colleagues (Richard, 2000; Richard et al, 2003; Richard, Barnett, Dwyer, & Chadwick, 2004) found that racial diversity produced better results in firms that had an innovative growth strategy. Specifically, diversity improved productivity, sales, return on equity, and market share. In short, diversity enhanced innovation, which paid off in superior firm performance. On the other hand, diversity did not affect performance in organizations with a downsizing strategy. Moreover, Richard et al (2004) examined gender and racial diversity and found that diverse organizations that had an entrepreneurial strategy performed better than non-diversified entrepreneurial firms. In other words, diversity provided enhanced information and wider perspectives that an entrepreneurial climate required.

Does the Business Case for Diversity Work?

From these solid research studies, we find that diversity can be a factor in organizational success. Most importantly, we cannot conclude that diversity works in all situations (Kochan et al, 2003). Rather, the organizational context is crucial (Kochan et al, 2003; Richard et al, 2003; Jackson, et al, 2003). In those organizations where diversity enhances organizational processes (Svyantek & Bott, 2004) and diversity can improve job performance by supplying task-relevant knowledge (Kearney, Gebert, & Voelpel, in press), diversity can improve the organization. To illustrate, if innovativeness is valued in the organizational climate, the strategic plan, and job performance (Richard, 2000; Richard et al, 2003; Richard et al, 2004) diversity can enhance innovation by producing more informational and knowledge resources, wider perspectives, and richer experiences to draw from.

On the other hand, if the organizational climate is dominated by established inflexible procedures, the organizational environment is focused on the status quo (Sonnenschein, 1997), problem solving can occur quickly (Jackson et al, 2003), the organization is stable and unchanging (Cannella, Park, & Lee, in press), group members do not have to actively communicate with one another (Konrad, 2003), and the job tasks are simple and routine (Bowers, Pharmer, & Salas, 2000), diversity will probably not produce a competitive advantage. In short, context factors such as type of strategy, complexity of the environment, task requirements, time frame, and relations with customers, determine whether diversity produces a competitive edge.

Recommendations for the Military

1. Cost out diversity initiatives to determine the dollar value of diversity techniques.

   Calculate the cost of such initiatives as Equal Opportunity Advisors (EOAs), diversity training, and partnering with local community groups (e.g., sponsoring diversity events).
2. Identify diversity effective units.

Identify units who score high on diversity climate indicators on instruments, such as the DEOMI Equal Opportunity Climate Survey (DEOCS). Indicators may be job satisfaction, workgroup cohesion, organizational commitment, and turnover (Cox, 1993).

3. Calculate the “return on diversity”.

   The return on diversity would be the cost of diversity initiatives compared to the indicators of the effectiveness of diversity.

4. Use this return on diversity as a diversity effectiveness measure.

   Use return on diversity in calculating budgeting for diversity initiatives. Publish return on diversity in recruiting advertising focused upon universities (e.g., the cost of ROTC as a diverse organization compared to the benefits to the university) and businesses (e.g., the possible returns from military diversity initiatives that company employees receive from their Guard and Reserve duty that may carry over to the company).

Conclusion

The business case for diversity advocates that diversity can improve the performance of the organization, specifically the bottom line. Research in the business sector shows that diversity can improve a number of financial, customer, and market measures, if the situation requires the knowledge resources that diversity can provide.

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