alongside rigorous debate. This rigour is only achieved through a diverse board whose members offer truly fresh insights from a variety of perspectives.

- **Seize the day** - Diversity is not simply about protecting the business from risks, it is equally about identifying and capturing opportunities. A diverse board also has a greater potential to attract high quality employees from a far wider range of fields and backgrounds. This 'virtuous circle' serves to further strengthen and sustain the business.
- **Lead by example** - Part of the potential to attract new employees directly links to the reputation of the company and how it promotes diversity both internally and externally. Diversity in the boardroom may signal to more junior employees that the company encourages change, is open and fair. These attributes may help retain highly skilled staff and attract high quality employees from a far broader selection of candidates.

DIVERSITY FINALLY ON THE AGENDA…

As one of the UK's largest investors, LGIM is highly active in challenging the composition of boards and bringing diversity into the broader discussion on board nominations and succession planning. For the 2011 calendar year to the date of this publication, LGIM has engaged with over 200 companies regarding corporate governance and the role of board diversity has been raised at a majority of these meetings. Most promisingly, in all cases the discussions have been welcomed by the companies, who recognise that further progress in this respect will only strengthen their business over time.

Encouraging developments include the fact that even the traditional UK bookmaking company, William Hill, has recently taken strides to expand the diversity of the board through appointing two women on the basis of their strength in media and retail experience.

…YET STILL EARLY DAYS

While these developments are encouraging, greater pressure needs to be put on boards to improve diversity on many levels. In particular, boards should consider:

- **Greater networking** - Companies need to leverage on the relationships they have with other businesses in their industry to help identify candidates with suitable skills and industry knowledge.
- **Widen the recruitment net** - Individuals who may not yet be CEOs but who hold high leadership positions should also be considered in the pool of candidates.
- **Ground roots** - Companies need to interact with head hunters to extend the diverse pool of candidates for the recruitment of key people. Key investors have a role to play here in interacting with head hunters and investment advisors. LGIM has been involved in this area playing an educational role from the start. We have seen companies increasingly looking for our input in recruitment and we are becoming more and more involved in finding the right people.
- **Pipeline and succession planning** - The board nomination committee needs to change the way it seeks new candidates – the future requirements of the company should be analysed and a truly diverse selection of qualified candidates should be put forward ahead of board vacancies.
- **Organic growth** – The talent of a company should be nurtured - internal recruitment is far cheaper, and often a better cultural fit.

THE BOTTOM LINE

Quotas and checklists are not the answer to achieving board diversity. While non-executive directors educated on the merits of diversity can help challenge the executives on board composition and help improve matters, there is a crucial role for large, long-term shareholders to monitor and drive change through time.

Sound corporate governance is a business practice that should never be viewed as an afterthought, or a series of external checks and balances that have to be done rather than should be done. To have the greatest positive long-term impact on a business it must be encouraged and fostered from within the very core of a company.

UK forecast:
Walking a fine line

UK economy	Price inflation (HCP)		GDP (growth)		10 year Gilt yields		Base rates		$/£		£/€	
Market participants forecasts	2011 %	2012 %	2011 %	2012 %	2011 %	2012 %	2011 %	2012 %	2011	2012	2011	2012
High	4.80	3.30	1.10	2.00	3.10	2.81	0.50	0.50	1.63	1.81	0.92	0.95
Low	4.00	1.70	0.60	0.40	2.00	3.20	0.50	0.50	1.40	1.43	0.85	0.80
Median	4.50	2.80	0.90	1.30	2.30	2.75	0.50	0.50	1.56	1.63	0.87	0.85
Last month median	4.40	2.55	1.10	1.70	2.60	3.47	0.50	0.50	1.56	1.65	0.86	0.85
Legal & General Investment Management	**4.50**	**2.80**	**1.00**	**0.50**	**2.30**	**2.75**	**0.50**	**0.50**	**n/a**	**n/a**	**n/a**	**n/a**

Source: Bloomberg L.P. and LGIM estimates

The forecasts above are taken from Bloomberg and represent the views of between 20–40 different market participants (depending on the economic variable). The 'high' and 'low' figures shown above represent the highest/lowest single forecast from the sample. The median number takes the middle estimate from the entire sample.

According to the preliminary estimate from the Office for National Statistics (ONS), the UK economy grew by 0.5% during the third quarter of 2011. While this was higher than many market participants anticipated, the ONS suggested this was mostly due to the bounce back following the loss of a working day in the second quarter which the UK enjoyed thanks to the Royal Wedding. With survey data deteriorating, however, the UK economic recovery remains very fragile and continues to be at risk of dipping back into recession. Private sector activity remains very weak and unemployment continues to rise while we are still to see the full impact of government austerity measures.

While Chancellor Osborne has come under increasing pressure to slow or reverse the government's austerity programme in order to boost the economy, fear of a Greek-style crisis has kept the government focused on reducing their deficit. We believe that government debt will continue to rise and while the recent announcement of further quantitative easing (QE) provides some support to the economy, the effectiveness of further QE coupled with harsh government austerity measures remains highly uncertain.

Inflation remains at more than twice the Bank of England's 2% target and we believe this will remain sticky at elevated levels for the rest of the year due to the lagged effects of higher energy and other import prices experienced earlier in the year. We believe inflation will subside in 2012, however, once the impact of higher VAT falls out of the headline calculation and amidst a weak growth environment. The UK's significant surplus of skilled labour is also likely to keep labour costs low. As a result, both our reading and the median market participant's forecast show inflation easing to 2.8% in 2012.

For further information on Fundamentals, or for additional copies, please contact william.lea@lgim.com

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