CERULLI ASSOCIATES

10 × 10

10 of the world's leading institutional investors

10 of the world's leading asset managers

Part One

Diversity and Inclusion

Commissioned by:

Russell Investments

October 2021

In 3Q 2021, Russell Investments held its annual Partner Innovation Lab, a roundtable event where large asset owners from various geographies brainstorm their greatest concerns and areas of interest. Russell asked Cerulli Associates to interview participating organizations, as well as some of Russell's asset management partners, to extract individual perspectives on topics discussed at the event. In aggregating insights, Cerulli sought to compare asset owner and manager views on key topics, as well as leverage data and insights from its existing suite of research on the institutional asset management space. Interviews were conducted from mid-July to mid-August and spanned a series of topics:

1. **Diversity & Inclusion**

   The first installation of this series covers research dedicated to exploring asset owner and manager perspectives on promoting diversity & inclusion.

2. **Climate Change Investing**

3. **Seeking Future Returns**

Participating Firms

10 Asset Owners

Organization
The Boeing Company
Fujitsu Global
Mazda Motor Corporation
Microsoft
Mitsubishi Electric
Nestlé
Roche
Unilever
The New York Presbyterian Hospital
Robert Wood Johnson Foundation
Thomas Jefferson University

×

10 Asset Managers

Organization
Brevan Howard
Hamilton Lane
Oaktree Capital Management
RBC Global Asset Management /BlueBay Asset Management
Western Asset Management Company
BlackRock
J.P. Morgan Asset Management
Morgan Stanley
Putnam Investments
Wellington Management

Summary

Speaking to some of the world's largest and most successful institutional investors and asset managers, Cerulli was able to gather insights from some of the industry's thought leaders. For efforts surrounding diversity and inclusion, where many industry participants are in the early stages of building out policies, Russell Investments and Cerulli believed these firms could provide a template for approaches. Rather than presenting participants with a series of survey questions, interviews had an open format. The goal of the open format was to uncover topics that would not necessarily surface in a traditional survey with multiple-choice questions. Participants were given free rein to describe approaches from angles that they saw fit. Cerulli found that institutional asset owners and managers have revamped their focus on diversity and inclusion, dedicating resources towards refining their approaches, setting goals, and implementing policies. While asset owners and managers have sought to promote a diverse and inclusive environment internally, many have also sought to promote diversity externally, encouraging their asset management partners and vendors to adopt measures. Asset owners and managers cite the need to grow the pool of diverse talent in the asset management space.

KEY POINTS

- Asset owners and managers must define diversity before they can promote it, and they must also define what constitutes success. Most 10X10 participants define diversity in terms of gender, race, and ethnicity, and they generally set goals for diversity (or set aspirational benchmarks) based on diversity metrics of the country in which the hiring office is located.

- In addition to promoting diversity, participants cite the need to maintain an open and inclusive environment. This generally derives from the understanding that diversity only adds values to the extent that organizations are inclusive. Alternative meeting formats are an example of one of the tools used to promote inclusivity.

- In implementing diversity measures for their hiring and recruiting initiatives, asset owner and managers cite the need to search for untapped pools of talent. Some of these measures include broadening the group of universities from which they draw talent or specifically targeting certain Historically Black Colleges and Universities (HBCUs).

- Several participants cited challenges in retaining diverse talent in the middle of their hierarchical structures (i.e., mid-level career employees). Measures meant to address this problem include the provision of career development and mentorship programs. Employee engagement surveys are a tool that firms can use to assess their diversity and areas of flight risk, as well as assess their level of inclusivity.

- In addition to promoting diversity at their own organizations, asset owners and managers taking a comprehensive approach often look to promote diversity beyond their organizations' walls. For asset owners, efforts to promote diversity externally generally targeted asset managers. By including diversity inquiries in their RFPs, asset owners encourage managers to consider diversity at their own organizations and adopt measures to improve. Managers take a similar approach to promoting diversity externally, but their targets tend to be the vendors they employ.

- While asset owners and managers generally define diversity externally the same way they define diversity for their own internal purposes, they must define parameters for diversity when they shift their focus to other firms. Many asset owners spoke of efforts to select woman- and minority-owned firms as asset management partners. Others say that looking at diversity at the ownership level is an incomplete approach, as it does not consider the diversity of the employee base. A consequence of assessing diversity more broadly is that the required data and information becomes more costly to obtain.

- Asset managers tend to be larger than asset owner investment offices, which has several implications for their D&I approach. Namely, they are able to evaluate diversity more granularly and can gain exposure to more demographics. While implementing measures to promote diversity externally are a relatively large and costly resource constraint for small investment offices, larger asset managers can absorb the corresponding costs more easily.

Diversity & Inclusion

Cerulli Associates asked asset owners and managers to describe their current approaches to promoting diversity & inclusion (D&I), including how they define and measure diversity and how they develop and implement measures. Cerulli also asked participants to explain the catalysts behind their decisions to incorporate D&I policies and the evolution of their views. A key finding in this study is that D&I initiatives mostly pre-date organizations' push toward responsible investing, with nearly every firm sharing that it is an organizational initiative dating back at least 10 or 20 years. Institutions and managers have been considering diversity before the "D&I" label really took hold. The recent uptick of D&I focus represents more of a broadening out and re-thinking of the initiative, rather than an abrupt adoption. Importantly, participants in this study used different acronyms when addressing this topic, including diversity & inclusion (D&I) and diversity, equity, and inclusion (DEI). While terms are often used interchangeably, there are some important nuanced differences highlighted in the exhibit below.

Earlier D&I initiatives predominantly focused on gender. Several studies show that corporations' commitment to hiring more women started as early as the 1980s and became mainstream in the 2000s. While this has translated to more women in the workforce, data reveals that growth has not been uniformly distributed across roles. Most participants in this study painted a similar picture, stating that despite recent progress, there are still large disparities across hierarchical structures. One asset manager pointed out that the financial services space is more advanced in this respect than other industries, namely tech and media, and provides a template for success.

> Finance, broadly, is more advanced than tech and media. Finance has showed that if you make a genuine commitment to gender diversity, you can be successful in that. There was a commitment to build networks for women and you're seeing some of that success now."
>
> *– asset manager*

Diversity & Inclusion Acronym Definitions and Explanations, 2021

D — Diversity: Anything that sets one individual apart from another, including the full spectrum of human demographic differences as well as the different ideas, backgrounds, and opinions people bring.

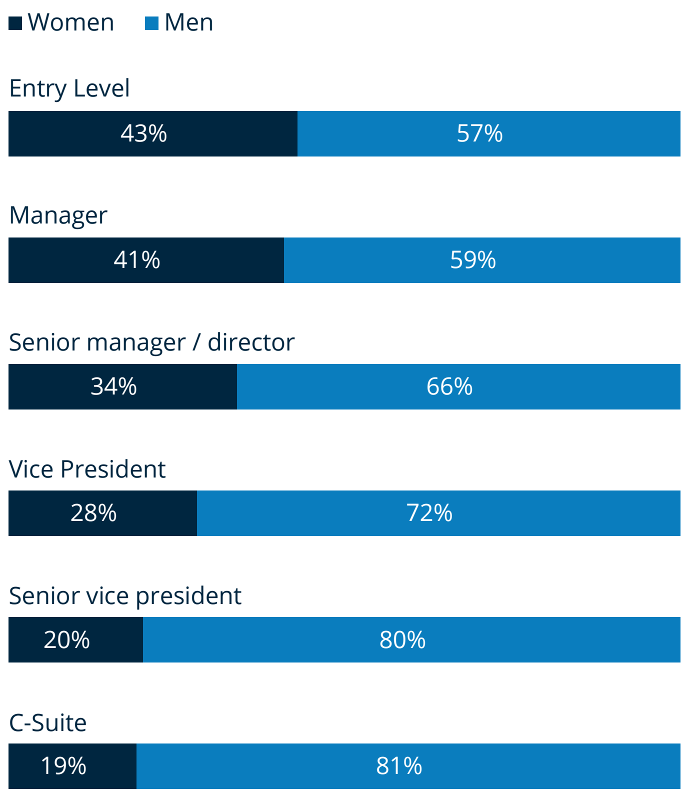
I — Inclusion: Cultural and environmental feeling of belonging and sense of uniqueness; extent to which employees feel valued, respected, encouraged to fully participate, and are able to be their authentic selves.

B — Belonging: Experience of being treated and feeling like a full member of a larger community.

E — Equity: Fair treatment for all, while striving to identify and eliminate inequities and barriers.

Source: Harvard Business School Publishing
Analyst Note: Common acronyms include D&I, DEI, and DIB.

Asset Management and Wholesale Banking Employees by Gender, 2020



Source: McKinsey & Company and LeanIn.Org 2020 Women in the Workplace Study

Given the consensus that diversity metrics were considered earlier, Cerulli asked organizations why this issue has become more pressing in recent years. Participants generally pointed to the political climate and, particularly, the events surrounding the murder of George Floyd as drivers to re-evaluating the issue. While most organizations have been monitoring diversity metrics in some form, recent efforts encompass organizations incorporating comprehensive approaches, with a strong focus on promoting racial and ethnic diversity. Organizations are formalizing their approaches, mainly by building processes and forming positions or committees.

> In the last two years, the conversation has been more at the forefront than any time in the past."
>
> – *asset manager*

> There was something in the air last year that caused people to increase their focus on it. I guess it was the George Floyd video. In that setting, we had the coronavirus, which meant there was an increased focus on it. Of course it became elevated."
>
> – *asset manager*

> Particularly over the last six to twelve months there has been a heightened focus."
>
> – *asset owner*

> The era of good intentions is coming to an end. There needs to be a genuine commitment and those results are going to take some time. It takes at least a generation for those things to develop."
>
> – *asset manager*

Channel Drivers of D&I

In looking at catalysts of implementation, it's important to assess the channels driving this push. These drivers include both internal and external demand. Internal demand refers to demand from within the organization – either top-down or grassroots bottom up. For institutional investors, external demand comes from end-beneficiaries and, in the case of corporates, clients that their sponsoring organizations serve. For managers, external demand generally comes from institutional clients but can also come from broader client bases. Notably, these external channels can exert pressure directly, via their own demand, or indirectly, via things like regulatory pressure or legislative efforts. These indirect channels can magnify the impact of smaller groups backing the initiatives.

The channel drivers of D&I slightly differ from that of responsible investing. While some participants said that their move toward responsible investing or environmental, social, governance (ESG) investing incorporation was entirely self-driven, the general consensus was that external demand played a larger role compared to D&I. Several participants told Cerulli that demand from certain geographic areas, namely Europe, prompted them to incorporate ESG investing, and this has since spilled over into internal processes. External demand for the adoption of D&I metrics will likely play more of a standardizing role. Via RFPs filed by institutional investors, managers will gravitate toward similar methods of tracking D&I metrics. In terms of preliminary drivers, however, managers primarily cite internal demand as the catalyst for adoption. Participants across the board believed that diverse teams lead to better outcomes.

> A team of 11 quarterbacks won't win a Superbowl. You need people with different skills and different experiences to solve a problem."
>
> – *asset manager*

> Bias can lead people to build teams of people more like themselves. [It] can lead to inferior objectives."
>
> – *asset owner*

> "It's internal values more than external. External talks a good game. But we also have a very young workforce, and diversity and inclusion is a very high value for them that they want to represent. For us, it's a reflection of that and trying to be what we say we are."
>
> – *asset manager*

Comparing Perspectives on D&I: Asset Owners v. Asset Managers, 2021

		Asset Owners	Asset Managers
Internal diversity efforts	**Size Characteristics**		
		For small organizations, challenging to gain exposure to every demographic	Large organizations can evaluate and promote diversity more granularly
		Small level of turnover has large impact on investment office diversity	Small level of turnover has minor impact on firm diversity
External diversity efforts		Evaluating diversity at third parties relatively large resource constraint for small investment offices	Evaluating diversity at third parties relatively minor resource constraint for large firms
	External Party Perspective		
		Consider diversity at asset management partners and investment holdings	Consider diversity at vendors and investment holdings
	Industry Perspective		
		May promote diversity in financial industry, but are often focused on corporate sponsor's industry instead	Promote diversity in their own industry

Source: Cerulli Associates
Analyst Note: Exhibit reflects Cerulli's view of the main perspectives and characteristics that differentiate asset owner and manager approaches to diversity & inclusion.

Almost all participants with whom Cerulli spoke described the incorporation of D&I metrics as a grassroots initiative. One manager with whom Cerulli spoke described a formalized grassroots system in which "employee resource groups are created and structured by employees." These employee resource groups (ERGs) each represent a unique demographic (e.g., Black, Latinos, LGBTQ+) and are tasked with creating more concrete suggestions to improve diversity on teams. Each ERG nominates an executive sponsor who reports to a more-centralized diversity & inclusion committee. What makes this structure truly a grassroots initiative is the way these ERGs are formed. While this firm has more of a formalized grassroots initiative process, most organizations say the need for additional diversity has generally arisen through company and team meetings. Several said that their younger employees are particularly focused on diversity efforts. This grassroots push for diversity distinguishes the movement from that of ESG, particularly for managers. When managers speak about the main drivers behind ESG implementation, most cite client demand as the primary driver rather than demand from employees from within the organization.

While most asset owners and managers have some sort of grass-roots initiative, many also cite organizations' leadership driving a top-down approach. This often takes the form of the CEO, board of directors, or an executive committee making diversity a firm-wide objective. Besides communicating to the firm that diversity is an important initiative, the top of the organization may incentivize diversity via executive compensation.

Specifically, organizations will factor team diversity as a component of executive bonuses. One manager with whom Cerulli spoke explained that 5% of executives' bonuses were tied to improvements in their teams' diversity metrics. Another manager said that rather than tying specific employee bonuses to team diversity, the firm's overall bonus pool was partially determined based on improvements in diversity. Similar to other efforts surrounding D&I, organizations generally aim to tie these bonuses to incremental improvements in diversity, rather than absolute measures. Another top-down measure that regularly surfaced in interviews was firms requiring diversity training for hiring managers or their employee bases more broadly. The broad objective of this initiative is to make sure employees are aware of their own biases.

> We now have a dashboard for [employee] managers so you can see where you are and how you are improving on diversity. That improvement will become a share of compensation."
>
> *– asset manager*

> We've launched speaker series and corporate messaging. Now embedded in sessions we are required to talk about unconscious bias and specific hiring trainings."
>
> *– asset owner*

> From a senior-level view, our board of directors oversee the global compensation committee that sets our bonus pool goals. One of those goals is to have 30% women in senior leadership roles."
>
> *– asset manager*

> I would say there would not be as much of a focus on DEI if we hadn't had that top-down review and the push from the firm to include DEI."
>
> *– asset owner*

> Our CEO has made it one of his top-three priorities. With that, we have objectives we need to meet. Starting last year, our head of diversity is now on the operating committee of highest-level leaders."
>
> *– asset manager*

> In the last year, we held an online forum on racial justice. Different employees who represent different backgrounds and they broadcast their different experiences and their road to [our firm]."
>
> *– asset manager*

> Where [our CEO] speaks about diversity - it's important that we focus on gender, race, ethnicity, and also diversity of thought and background. You don't get that if you are focusing on people who have had similar experiences in their formulative years, and then through college."
>
> *– asset manager*

> We've stopped short of setting fixed quotas. We've subscribed to initiatives to help identify junior talent that we can build up."
>
> *– asset manager*

Defining Diversity

Before an organization can create goals for diversity, it must first define it. Most organizations have established committees tasked with determining metrics through which they will promote diversity. Another key challenge both asset owners and managers face is defining parameters for success, an undertaking that is also placed with these D&I committees. Cerulli finds that organizations generally look at diversity through the lens of gender, race and ethnicity. Across calls, participants also mentioned diversity of backgrounds, circumstances, age, and sexuality. No participants mentioned religious diversity as a measure they evaluate. Notably, for factors such as sexuality and religion, most jurisdictions prohibit inquiries of such nature. When participants mentioned the promotion of sexual diversity, this was geared more toward inclusion measures than diversity. One participant described the ultimate goal of these diversity measures was to promote diversity of thought.

Given the metrics through which organizations assess diversity, Cerulli asked participants how they set diversity goals. Several said that their committees develop aspirational benchmarks, often tied to diversity in the country of the office in which they are hiring. Notably, there are considerable discrepancies in diversity from country to country, with the U.S. being one of the more diverse countries in which asset owners and managers operate. There are also further nuanced aspects, including the question of whether or not to localize further or consider laborforce participation in efforts to develop a diversity benchmark. Some asset managers described efforts to benchmark themselves against industry peers. Regulatory differences from country to country also complicate the practicality of implementing some of these measures.

Some asset owners and managers told Cerulli that they do not have specific diversity benchmarks or targets. These organizations are more directional, taking the approach, "We just need more." While they are not necessarily behind in considering diversity measures, these organizations tend to be further behind in achieving results. One asset manager with whom Cerulli spoke explained how the private equity space struggles with this due to its historical makeup.

> There's a number of dimensions to this. I think about diversity, mainly in terms of diversity of thought which comes from different circumstances, backgrounds, age, and other things."
>
> *– asset owner*

> There's been an inflection point and people want to actually see results. That's tough to do. DEI can mean different things to different people. [It is] difficult to define what success is going to be."
>
> *– asset manager*

> It gets more complex in EMEA. We have to be sensitive to the regulations in that part of the world. Every industry can't and won't reflect the diversity of the U.S. population."
>
> *– asset manager*

> We generally view the metrics as the composition of the U.S. If you try to break it down into the labor force, there's different labor force participation metrics."
>
> *– asset manager*

> We track our diversity statistics monthly. And we have targets in terms of what we hope to look like in a three-to-five-year time frame."
>
> *– asset manager*

> As part of the monthly committee meeting, we go through the diversity data and we look at the percentages by team and region, that are Black, female, Asian, Latino, and we set targets where we would like to see the ball progressing. Those targets are set with the head of diversity & inclusion. Sometimes we are ahead and sometimes we are behind. In a couple of instances, they've been poached by someone else."
>
> *– asset manager*

> We do [monitor diversity metrics], but probably not that overtly…I'm more interested in diversity of thought than just filling buckets of types of people."
>
> *– asset owner*

> I did not want to set goals, I just wanted to do it. Now, I think my colleagues, they want to set goals…I gave my opinion on doing this as a continual process, but they just wanted to be more aggressive in terms of timeline."
>
> *– asset owner*

While organizations struggle immensely with defining parameters of their responsible investing strategies, several said that measuring diversity is a bit more straightforward. For one, there are not as many conflicting sources. Asset managers with whom Cerulli spoke generally have some sort of self-assessment survey they administer year-to-year. The manager will leverage a third party to survey its employees, asking them questions surrounding diversity and inclusion.

Another important aspect of implementing diversity targets is establishing a time frame. Organizations varied in their view on this – some participants said that they were planning to implement their current policies indefinitely, while others believed they would implement measures until they reached their diversity targets, then continue to monitor diversity going forward. The latter group tended to believe that once they reached their targets, diversity would at least partially be a self-feeding process. One manager explained this as an attempt to develop a "critical mass" in those diverse populations.

> A lot of it is critical mass. If we reach a critical mass of one group, then it will keep improving the situation. Getting the initial representation is the difficult part… It's a self-feeding process."
>
> *– asset manager*

> It's always been too easy for those involved in recruitment to hire people like themselves."
>
> *– asset manager*

> Right now, left to its own devices, it would be a much more white-male firm…that would be the path of least resistance. In private equity, the hiring pool is dominated by a particular race. You hire who you know."
>
> *– asset manager*

> We have number targets, and they indicate the direction. It's a slow-moving process. It's a recognition that it could take ten years to get there."
>
> *– asset manager*

A few participants took the approach of implementing short-to-intermediate-term targets and plan to reassess at regular intervals (e.g., every three to five years).

Implementation

When attempting to improve diversity within an organization, it's important for asset owners and managers to assess diversity across their structures, including throughout their employment hierarchies. One manager with whom Cerulli spoke broke this down into four buckets: hiring, developing, promoting, and retaining.

Both institutional investors and managers implement diversity measures via hiring and recruiting practices. Almost all participants spoke of the need to search for untapped pools of talent, often recruiting from non-traditional channels. For entry-level roles, asset managers have traditionally targeted certain universities, falling in line with "you hire who you know" thinking. Some have addressed this by expanding the group of universities from which they draw talent. Others have implemented "blind" hiring processes, where they don't target any specific universities. Some participants (both asset owners and managers) said that their companies have begun to broaden their focus on academic majors as well. For experienced candidates (non-entry-level roles), organizations are broadening their focus to roles outside the asset management space. Notably, for some positions that require asset management experience, this is more challenging and highlights the reason why industry participants are putting efforts into growing the pool.

> **Our approach [is challenged] by talking to other asset owners.** We also have to think about recruitment, are we recruiting people who have a diversity of experience."
>
> *– asset owner*

> Traditionally you canvas the top programs. That candidate pool is fairly homogeneous at times. We are looking at different ways to create a candidate pool. Looking at arts and sciences programs rather than just MBA programs."
>
> *– asset manager*

> I wanted to make sure that [my firm] had a blind hiring process; that my alma mater had an equal shot at opportunities here."
>
> *– asset manager*

In addition to acquiring talent, asset owners and managers with whom Cerulli spoke described the necessity of measures meant to retain talent. Managers' self-evaluation surveys are an example of a tool used to help with this – to "identify flight risk," as one asset manager put it. Although promotions are a tool that organizations could use to retain diverse talent, no participants mentioned diversity being a key input into promotion decisions. Rather, organizations seem to focus more on developing diverse talent so that they are later promoted on their own merits. Tools used for developing talent include mentorship programs, where entry-level employees are matched with an executive mentor. One asset manager explained that its mentorship initiative also included a program for tenured employees. Specifically, this firm has a leadership program in which a group of select women and minority employees are paired with personnel on the firm's operating committee, signally to them that they are valued and on track to be a future leader at the company.

Many organizations cite difficulty in retaining diverse talent in the middle of their hierarchical structures. One of the reasons for this is that firms are competing for the same limited pool of candidates for roles requiring experience in the asset management industry. This especially applies to roles requiring investment management experience. While the asset management industry is somewhat ahead of other industries in terms of gender diversity, one participant noted that there are varying levels of progress across employee functions. This is partially rooted from candidate pools from which employers draw talent. For example, human resources and marketing functions require many skills that can be acquired from outside the space (i.e., inter-industry skills). Because firms can acquire diversity from the broader labor force, these groups tend to be more diverse. For roles that strictly require investment management experience, organizations are subject to the pool that the industry feeds them - a pool that tends to exhibit limited diversity. In attempts to increase diversity at their own firms, managers find themselves recruiting talent from their peers (or "poaching diverse talent," as one managers puts it), rather than building up diversity across the industry. Hence, several organizations have put efforts into growing the overall pool of candidates in the asset management space (covered in the following section).

> We are conscious that we don't want to just be poaching diverse talent from our peers."
>
> *– asset manager*

> I don't think that we've added to the industry-wide pool of diversity because we are taking elite, diverse, talent from elsewhere."
>
> *– asset manager*

> Some organizations do well at the bottom and top, but struggle hiring diverse candidates in the middle. You lose people in their mid-careers, due to lifestyle changes or career changes. There's a donut hole in the middle there."
>
> *– asset manager*

> Changing the makeup of your employee base is not something that you can do quickly. You want it to happen naturally over time. That departure of early career hires is something we've tried to fix through development and mentorship programs. The jury is still out on trying different things. Large firms have the resources to do those things. Do smaller firms have the ability to do that? I don't know."
>
> *– asset owner*

> When you look at our history, the junior levels are very diverse. As you get more senior, it's less diverse...You have to recruit across the U.S., not just the Northeast and West Coast. From the top down, we've been pretty good at bringing in senior people."
>
> *– asset manager*

Efforts to promote diversity are met with certain challenges, depending on the traits of the concerned organization. Maintaining a diverse group of employees can be especially difficult

for small investment offices. One asset owner with whom Cerulli spoke cited this as a challenge for its investment team, simply because headcount was limited to five people. Instead, at this asset owner, diversity is considered at a broader, enterprise level. In addition to company or office size, a firm's location can invite potential barriers to implementation. As previously mentioned, regulations differ by jurisdiction and some jurisdictions prohibit organizations from considering gender or racial identities in their hiring initiatives.

While most comments regarding D&I tilted toward the diversity component, some participants had a very attuned focus on the inclusion aspect. One manager explained that organizations can recruit a diverse workforce, but if it isn't inclusive, that organization will not reap the benefits of diversity. In other words, diversity only adds value to the extent that the environment is inclusive. An asset owner explained that in order to foster creativity, an organization must uphold an inclusive and open environment: "Getting people to think in a creative way is better for solutions. I think it's partly the people you recruit but also how you run your business." Self-evaluation surveys are used to measure an organization's level of inclusivity. Other tools used are alternative meeting formats, where employees are given the opportunity to speak their mind both before and after meetings.

> We've done a lot of thinking about how we run our meetings and making sure we are curating opinions. Part of that is communicating to people on the team that everyone has good ideas...We get written inputs pre-meetings, and sometimes we do voting. I'll get people's opinions before the meeting. Then we'll have the discussion and see if they've changed their opinions."
>
> *– asset owner*

> [For] the engagement survey, I pay attention to the question, "Do I feel I can bring my true self to work?" That's really important from an inclusion perspective. Do people feel like they have the psychological safety to bring their best ideas to work."
>
> *– asset manager*

There is broad alignment across organizations with whom Cerulli spoke – in order to take on D&I, an organization must devote resources to address it. As mentioned earlier, most organizations have a D&I committee or council. This generally includes managers from across the organization and personnel from the demographics they are looking to target (women and minority personnel). Increasingly, Cerulli has observed companies hiring heads of diversity & inclusion. This role is primarily charged with formalizing the firm's approach, as well as tracking diversity statistics and monitoring certain initiatives. While some participants mentioned that they had a head of ESG who would evaluate external partners on ESG metrics, participants with a head of D&I did not say that this person evaluated third parties with whom the organization partners.

> The approach for [our firm] coalesced around the DEI committee, which is made up of leaders across asset classes and geographies."
>
> *– asset manager*

> Diversity and moving the needle forward – it can't just sit within HR. That necessitates people across the business own it. That's what the committee is for. We need to have the same global framework across different geographies and different businesses. We need to involve people across those lines."
>
> *– asset manager*

> I would say that this is distinct from ESG. This has its own structure, budget, and policies that we've put in place."
>
> *– asset manager*

Diversity Downstream

Beyond efforts to promote diversity for their immediate needs, several participants described efforts to promote diversity in the industry at large. Asset managers, in particular, have created programs that seek to guide minorities toward the asset management space. Managers employing these programs look to grow the potential candidate pool downstream. The $90 million AltFinance program funded by Apollo Global Management, Ares Management Corporation, and Oaktree Capital Management, for example, includes a mentored fellowship program as one of its three pillars. Specifically, this program partners with historically Black colleges and universities (HBCUs) to provide students with a clearer pathway to careers in the alternative investment industry. Similarly, Morgan Stanley funded its $40 million HBCU Scholars Program, with a goal of providing scholarships to HBCU students and eventually recruiting them.

An example of an initiative to grow the pool even further downstream, Ariel Investments launched a program to promote financial literacy among elementary school kids. Specifically, the Ariel Investment Program grants incoming first grade classes $20,000 to learn to invest and eventually contribute a portion of profits toward 529 college savings programs.

> We aren't getting what we need from the schools. Some research will take you all the way back to third grade. So by underserving broader populations in education, you are making it so you can't achieve your goals later on."
>
> – *asset manager*

> We have a duty to help make sure that investment management is accessible…We are talking about how we can design, recruit, and build a framework that gets people in that's good for us, and good for the industry."
>
> – *asset manager*

In addition to forming their own peer-to-peer partnerships, asset owners and managers look to partner with third-party organizations specifically formed to address diversity. Examples of these third parties include non-profits such as Girls Who Invest, The Robert Toigo Foundation, and Invest in Girls.

Sample List of Non-Profits with D&I-Related Missions, 2021

TOIGO
Bringing Diversity to Life

Robert Toigo Foundation

Works to provide resources for minorities entering or already in the financial services industry.

Founded in 1989

POSSE

The Posse Foundation

Identifies, recruits and trains individuals with extraordinary leadership potential. Posse Scholars receive full-tuition leadership scholarships from Posse's partner colleges and universities.

Founded in 1989

Invest in Girls
A PROGRAM OF THE COUNCIL FOR ECONOMIC EDUCATION

Invest in Girls

Works with schools, community organizations, corporations and foundations to provide financial literacy programming to young girls.

Founded in 2010

GAIN
Girls Are INvestors

Girls Are INvestors (GAIN)

Community of investors, with charitable status, set to change the staggering lack of gender diversity in investment management, from the ground up.

Founded in 2010

girls who invest

Girls Who Invest

Dedicated to increasing the number of women in portfolio management and executive leadership in the asset management industry.

Founded in 2015

Source: Non-profits' websites.
Analyst Note: Sample is limited to organizations mentioned by participants throughout research calls.

Evaluating Diversity of External Parties

Another avenue through which asset owners and managers promote diversity externally is by encouraging their business partners and vendors to adopt measures. Asset owners, for example, have sought to track diversity at their asset management partners and prospects. In their assessment of diversity of third-party partners, asset owners generally try to apply the same metrics that they apply to their own organizations, primarily focusing on gender, race, and ethnicity. Some asset owners look at diversity through the lens of ownership structure, targeting woman-owned and minority-owned businesses. The theory with this approach is that certain biases percolate from the top down, and by investing their assets with a minority-owned business, they are essentially diversifying biases. A drawback to this approach is that it does not consider diversity throughout the organization – a firm could have a diverse ownership structure but an otherwise homogenous employee base. One participant explained another drawback to this approach – that it does not work for public companies, a large portion of the asset management universe.

> Historically, the percentage ownership has been important for us...We see the value of that, but we don't want to exclude a large portion of the asset manager community where that metric doesn't apply. In that regard we are developing metrics to look into other factors where DEI is implemented into the process. What's the makeup of the individuals managing our account?"
>
> *– asset owner*

> We are looking at evaluating those firms from a practice standpoint. What is the makeup of their employee base? Is there diversity in decision-making roles within the organization (senior, mid, and junior levels)? [Is there a] pipeline of succession for women and minority candidates?"
>
> *– asset owner*

Certain investors look to assess diversity further down the personnel hierarchy, looking at diversity at the manager level. Others assess diversity throughout the organization, although this often presents a challenge from a data gathering/maintenance perspective.

> We tend to favor metrics that are broader than just ownership structure. We want to look at the whole employee base because that's more representative of diversity than just one or two owners."
>
> *– asset owner*

> Ownership is still a superficial view of DEI. We need to look at the GPs themselves - is there a culture of DEI at those firms? ... The ultimate strategy is to nudge folks to be more aware of where they stand in this area. On the public side, I think there is a greater focus already, so we don't have to be as proactive there."
>
> *– asset owner*

> The challenging part right now, from a resource perspective, that's a lot of data to maintain. We are evaluating outside parties that can provide support in that area."
>
> *– asset owner*

Asset owners' methods of evaluating diversity at third parties are continuously evolving and expanding. One asset owner with whom Cerulli spoke said that it began evaluating diversity in select strategies before broadening. "[For equity mandates,] we began a program focused on hiring managers with a diverse background in ownership." In the following years, this asset owner expanded efforts to a broader range of asset classes. Another asset owner started looking at managers' ownership structure before broadening their focus to managers' entire organizations. Another assessed D&I of managers in its public investment portfolio, then expanded to private investments. Notably, multiple asset owners mentioned that measuring diversity in the alternatives space is more difficult than it is for traditional managers due to the lack of reporting requirements. Finally, a select few asset owners have gone so far as to evaluate diversity at holdings/portfolio companies of funds.

> We started moving away from ownership, to who are the decision-makers, the partners, the managing directors. If all of the low-ranking employees are women or minorities [while ownership is male / white], that doesn't say great things about the culture of diversity. On the private side, who is sharing the economics? Who is getting the carry? Privates tend to have the worst metrics, but you are making incremental changes over time."
>
> *– asset owner*

Most organizations do not have formal policies for diversity – it is simply a consideration in the overall process. Similar to the pattern of managers factoring incremental improvements in diversity to compensation rather than absolute levels, some asset owners look for managers that are making progress on diversity initiatives rather than judging them on their level of diversity at a given point in time.

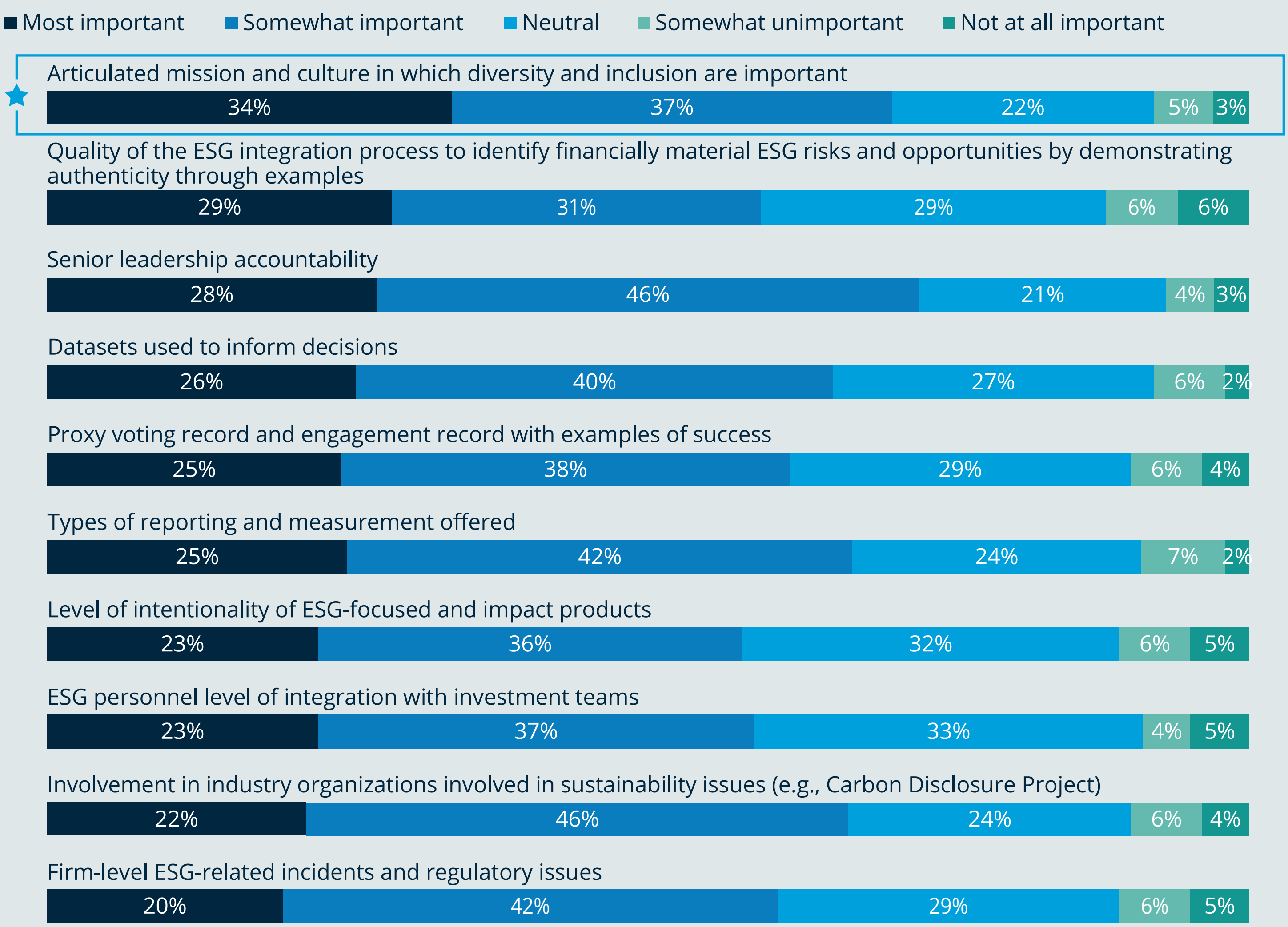
> We don't have any hard guidelines on this. It's part of the wider decision-making process."
>
> *– asset owner*

> It was at an annual meeting; three principals walk in and I was about to ask about the lack of diversity and they brought it up before we could even get there. They had just lost a diverse group of associates and they had a plan to do better. And a year later they did everything they said they would do. So you have to be in the maintenance mode with every manager."
>
> *– asset owner*

Particularly for U.S. corporate plan sponsors, rules surrounding pecuniary factors represent a legal barrier. One corporate pension plan sponsor with whom Cerulli spoke said that the flurry of ERISA plan lawsuits, the administration change, and the DOL not providing specific guidance prevented it firm from taking on the initiative via its pension portfolio. Another plan sponsor said, "You have to prove that a pecuniary factor exists," and further explained that this prevented it from effectively incorporating D&I measures in its investment process.

> Companies have a fiduciary duty, and the regulators were clear that everything you do has to be for a pecuniary purpose. You have to prove that the pecuniary purpose exists...it prevents you from turning the dials and start tracking it [diversity metrics] right away."
>
> *– asset owner*

Asset Owners: Key Criteria Used to Evaluate Asset Managers on ESG Considerations, 2020



Source: Cerulli Associates | **Analyst Note:** n = 200 (all respondents).

Across its research of the institutional space, Cerulli often hears from managers that they are receiving more inquiries on D&I metrics. Every asset manager with whom Cerulli spoke for this project confirmed this trend. Although managers are receiving more questions, many say that it ultimately does not impact their asset owner prospects' investment decisions. One asset manager with whom Cerulli spoke in this study seemed to agree with that notion, remarking "Institutions [asset owners] talk a big game about diversity but they don't make a selection based on diversity."

> [D&I inquiries are] coming from RFPs, asking firm-wide and bank-wide diversity statistics, but also in the particular product or asset class…Two or three years ago, it was every so often, now it's a surprise if a potential client doesn't ask for it."
>
> – *asset manager*

Similar to asset owners, some managers report on efforts to promote diversity at their vendors. One manager said that it made certain to have women- and minority-owned firms in its pool of vendors. Another described measures similar to those used by asset owners (described above) but instead targeted towards trading firms, operational support providers, and companies used for ancillary activities (e.g., travel). In addition to evaluating D&I metrics at their vendors, managers are increasingly making D&I a focus of product development efforts, considering metrics across their stock holdings and developing products geared towards addressing these challenges.

> With larger businesses, we look at the data that they publish, like composition of board, diversity data available across the organization…In the U.K., we access gender pay data."
>
> – *asset manager*

> We are developing diverse supplier academies… It's not just about giving money, but helping them build capacity."
>
> – *asset manager*

Asset Managers: Top Social Themes Addressed for Product Development, 2020

Source: Cerulli Associates

Leveraging Partners

Asset owners that didn't have approaches to assessing D&I externally mentioned that they intended to start this initiative by talking to their investment consultants or OCIOs. Some of these asset owners are in the brainstorming stage, trying to discover ways to assess and implement diversity measures. They rely on these types of partners to educate them on initiatives of other clients. By using intermediaries, these investors can discover best practices.

> "We aren't doing anything with D&I right now. Once we get ESG to a place we are comfortable with, then we will shift our focus to D&I. We would turn to our investment manager to take on this project and see what their capabilities [are] and see what the best practices are. If you have a small team, this is just not something that you will be able to take on."
>
> *– asset owner*

> "When we do a search for an investment manager, we go to [our consultant] and have them give us their highly ranked manager list in this area. So we are relying on them in that regard, to include the full breadth of manager candidates out there. It would be our expectation that they are including women or minority-owned firms in their population set. [That's] one of the beauties of working with an investment consultant. There's only five people on our team; we can't keep track of every manager in every area, so we rely on those managers [personnel at investment consultant] to do that for us."
>
> *– asset owner*

A broad takeaway from this research is that promoting diversity requires proactive behavior. To take on a comprehensive approach, an organization must define diversity, set goals or objectives, implement measures to carry out those objectives, and employ systems to track progress. An organization must also maintain an inclusive environment for it to tap into diverse perspectives. Another takeaway is that diversity is not free – an organization must devote resources to acquire and maintain it or, alternatively, absorb a substantial opportunity cost.

Cerulli Research and Consulting

For nearly 30 years, Cerulli has provided global asset and wealth management firms with unmatched, actionable insights.

Headquartered in Boston with offices in London and Singapore, Cerulli Associates is a global research and consulting firm that provides financial institutions with guidance in strategic positioning and new business development. Our analysts blend industry knowledge, original research, and data analysis to bring perspective to current market conditions and forecasts for future developments.

info@cerulli.com www.cerulli.com @cerulli_assoc /cerulli-associates