Your People Deliver Your Firm

In our previous Back to Basics articles, we've talked about the importance of projecting warmth in addition to competence to gain the trust of clients and potential investors. In this article we explore those warmth projectors themselves: your people.

Managers best establish their warmth by demonstrating their understanding of investor needs and concerns. In this article we focus on two areas currently topping investors' trust-building concerns, diversity, equity and inclusion (DEI) and firm culture.

Your people bring the other three 'Ps' to life. Every allocator analyzing asset managers and OCIOs for potential engagements considers the famous 'Four Ps': Philosophy, Process, Performance, and People. In our research article Trust for the Win, we explain how investor trust is built via a matrix with two axes: warmth and competence. Investors assume most managers are highly competent, and are able conduct most of their analysis of any managers' first three 'Ps' via databases.

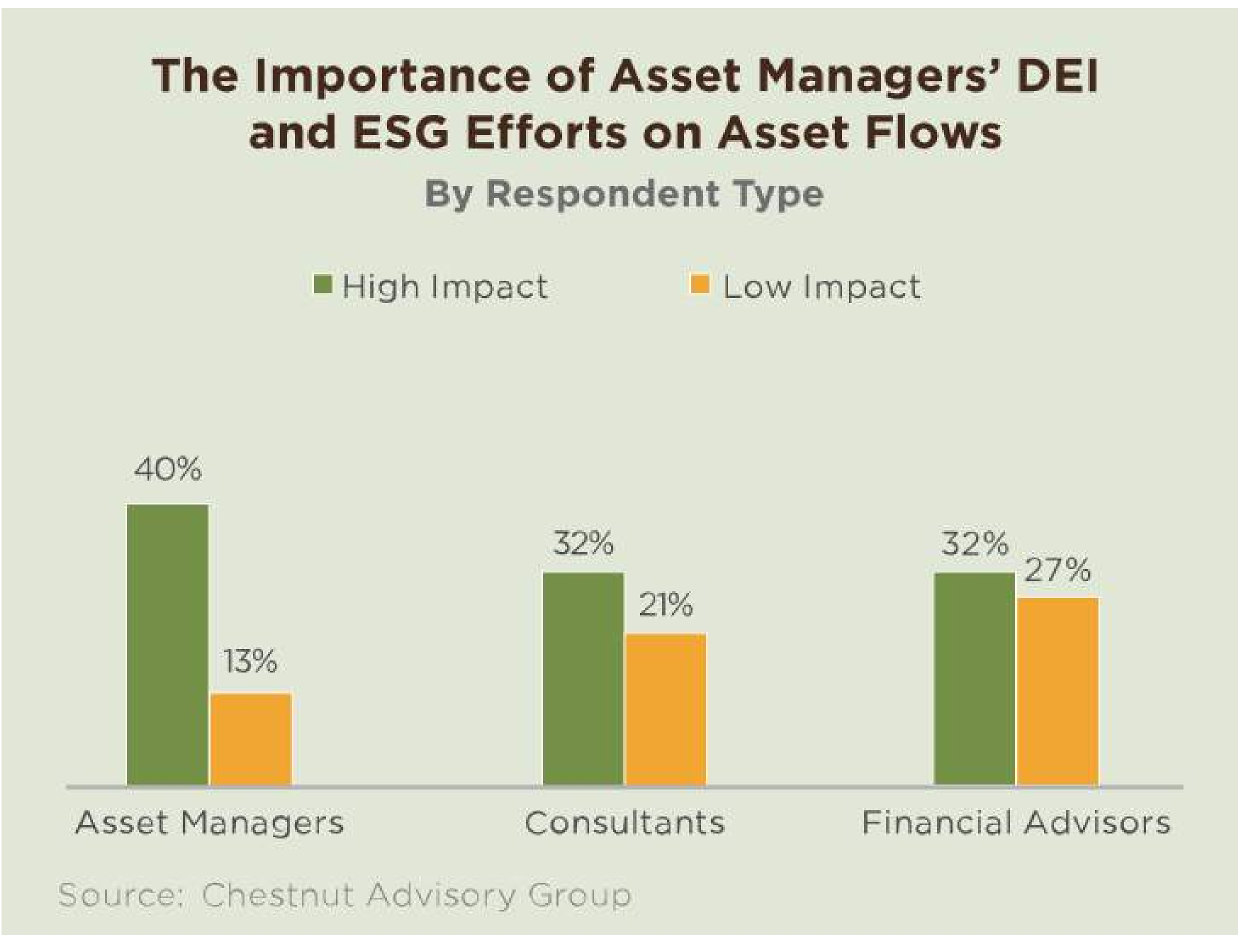
Measuring a manager's warmth, however, always comes down to a judgment around whether the manager can be trusted to always service the investor's best interests, or not. While databases attempt to objectively measure a firm's people (around topics such as employee turnover and DEI), these responses by themselves are not enough for most allocators to make a hire decision.

At the end of the day, the selection of an asset manager or OCIO comes down to the allocator's perception of the people at each manager in the running for the engagement. In order to arrive at this perception, allocators conduct extensive personal interviews as part of their operating due diligence and continue to insist on finals presentations delivered by the team of people that would be working with them if they are hired.

Effectively addressing investors' growing interest in the diversity of their managers' teams has become an important opportunity for managers to demonstrate their warmth, but this only works if the firm's people actually walk the talk.

80% of investors view DEI as important. According to a recent study by NEPC, a whopping eighty percent of institutional investors believe DEI is important to incorporate into their investment programs. A DEI review is part of every new manager hiring decision today.

In our Making the Most of the DEI Growth Opportunity article, we shared our research showing that manager DEI efforts are increasingly driving asset flows.



How are investors assessing manager DEI efforts? While manager DEI data are beginning to be reported, the current data are spotty at best. To determine which managers have a credible DEI approach, therefore, investors turn right back to those same Ps: Philosophy, Process and People.

Asset managers and OCIOs must have a clear and truthful statement of their current DEI approach. Just as with a firm's purpose, everyone at the firm must understand and embody the firm's DEI approach so that it comes across as genuine to investors. When done right, a firm's DEI discussion with investors is a great warmth-building exercise.

Here is a summary of the manager DEI best practices we discuss in our report:

Best DEI Practices for Asset Manager Growth

- Thoroughly understand your target investors' DEI interests
- Don't 'diversity wash', authenticity is critical
- As the industry has not thus far set any agreed-upon DEI standards and practices, most managers don't yet have a detailed DEI philosophy or policy; managers should own that fact rather than try to hide it
- Fully complete all DEI database and DDQ questions, even if you don't like how your data looks
- To be credible, invest in your DEI efforts

Your people will convey your DEI efforts, whatever they are, whether they try to or not. Even if the diversity of the group of people a prospective investor meets with do not reflect your firm's DEI efforts, as long as your people consistently demonstrate their understanding of the importance of this issue to the client and their firm's current approach to this issue, you build client trust. After all, DEI is just one aspect of any firm's culture, about which investors deeply care.

Culture stems from purpose. The heart of every successful asset manager, in our view, is a successful firm culture. Further, we believe that a strong purpose is the foundation for any successful asset manager's culture, as we discussed in our last article. It is crucial for the investment and distribution sides of the house to come together to develop a unifying purpose that is equal parts client-centric (distribution value add) and authentic (investment value add). Once articulated, the purpose must permeate the entire organization, from compliance, operations, and trading to client service and beyond. Each person needs to relate to the firm's purpose and understand how they contribute to it.

A common purpose binds together disparate departments and creates, at the most successful managers, a great culture where everyone feels heard, valued, and believes that they belong to the same team bound by a common set of goals, values, and norms. As the firm's people embody that belief, the firm's culture becomes quite obvious in client interactions at all levels. The more consistent the investor experience is with a wide range of the firm's people, the more additive client interactions become to building investor trust.

Culture clashes can inhibit growth. One measurement of the importance allocators place on manager culture is how they treat managers involved in M&A transactions. Our research shows that investment consultants immediately put such managers on a watch list, where they remain for 12-18 months on average to determine whether key people remain and the firm's culture can be reassessed.

Culture issues are a primary hurdle to talent retention post-transaction, and senior talent departures are generally an automatic trigger for eventual client redemptions. It is common for managers to estimate post merger AUM projections due to "investment" factors but much less common to fully factor in potential culture clash impact, employee and asset retention.

Cases where asset manager firm culture impedes post-M&A cost-cutting are widespread. In one scale-seeking merger we were involved in, each predecessor firm had such a strong and successful culture that merging the two into one became a herculean task. While there were many other challenges to this deal, we believe culture was the primary reason that a full decade after the deal closed, external clients and vendors, as well as internal employees, would refer to working with either the pre-merger Firm A or Firm B side. Needless to say, at that point the new firm's net flows were strongly negative.

In conclusion, we believe the 4th "P" of People is all about DEI and culture. Firms that are committed to this will project warmth and will be differentiated in the future.

Stay tuned as we continue to unpack the layers of the Golden Circle in our ongoing Back to Basics series of thought leadership and research. Please feel free to contact Chestnut Advisory Group for more detailed insights on delivering a superior client experience.