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NOVEMBER 2023

California State Teachers' Retirement System (CalSTRS)

Shelly Heier

Institutional Investing Diversity Cooperative

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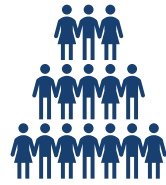
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California State Teachers' Retirement System
November 2023

Institutional Investing Diversity Cooperative

Consulting industry collaborating to improve diversity data collection



- 28 institutional consulting firms
- > \$44 Trillion in assets under advisement



- Aligned around the importance of DEI data transparency
- Shared belief that diversity enhances investment decision-making



- *How can you measure progress if you don't have the data?*

Defining a diverse manager

Ownership

- History, tied to MBE/WBE classifications
- **Specific and easily quantified; more readily available**
- Not directly tied to investment decision making or investment results
- Ownership may not lead to further economic distribution

Contribution to Investment Decisions

- Harder to classify and quantify
- **More directly tied to investment results**
- Multiple facets of diversity – cognitive, perspectives, education, background
- W2 income (or carry) can build to broader ownership & economic distribution

Case for investment team diversity

“Broadening Diversity Considerations” by Ian Toner and Marianne Feely

- “Regarding cognitive diversity, academic research has documented **advantages of diverse groups for process and performance over short time periods** and noted the potential advantages are greater for longer-term groups (Watson, Kumar and Michaelson, 1993)”
- “We believe one of the chief benefits of diverse fund management organizations is the greater diversity of cognitive thought brought to bear in the investment process. This view is bolstered by numerous financial industry publications. In one example , James Ware and Michael Falk identify **diversity of thinking styles as important to 86% of a group of top teams** they identified to participate in their study. Ware and Falk make another observation related to soft skills, noting that **86% of these teams agree capacity for good debate is important.**”
- “A more generalized framework constructs a model studying individuals who differ in how they represent problems internally (perspective) and the algorithms they use to generate solutions (heuristics), (Hong and Page, 2000) . The paper posits **that collections of agents outperform individuals partially because people see and think about the problems differently.**”

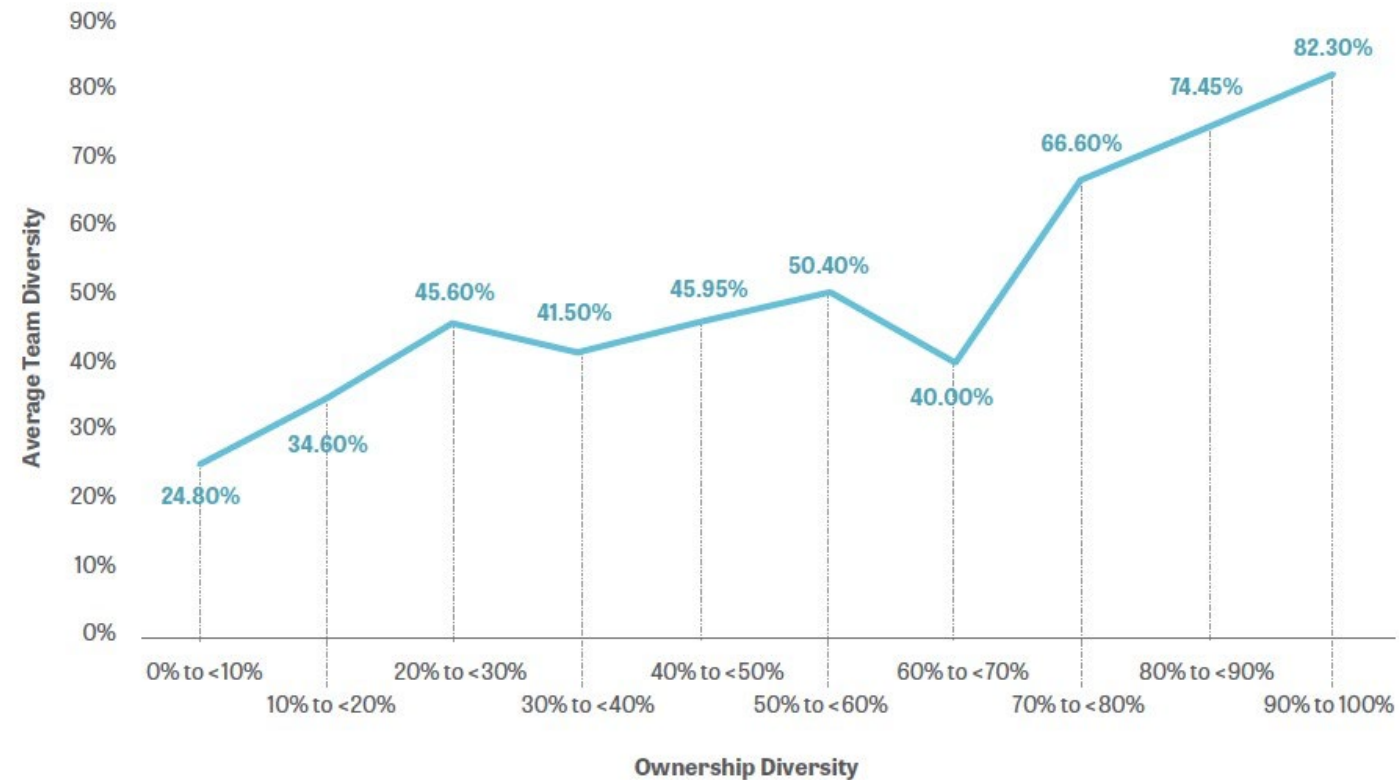
“Broadening Diversity Consideration” July 2020 Ian Toner, Marianne Feely. <https://www.verusinvestments.com/broadening-diversity-consideration/>

3 Watson, Warren E., Kamalesh Kumar, and Larry K. Michaelson. “Cultural Diversity’s Impact on Interaction Process and Performance: Comparing Homogeneous and Diverse Task Groups.” *The Academy of Management Journal* 36, no. 3 (1993): 590-602. Accessed March 2, 2020. www.jstor.org/stable/256593. 4 Ware, James and Falk, Michael, 2016. “Top Performing Equity Teams: The Common Factors They Share”, Focus Consulting Group white paper. 5 Hong, Lu & Page, Scott E., 2001. “Problem Solving by Heterogeneous Agents”, *Journal of Economic Theory*, Elsevier, vol. 97(1), pages 123-163, March.

Knight Foundation – 2022

Concluded the relationship between ownership (equity %) and team (headcount%) is positively correlated

Figure 1. Average Team Diversity by Ownership Diversity



Analysis considered 204 active, non-public based US firms, which managed 1,450 public products representing \$3 trillion in assets

Knight Diversity of Asset Managers: Ownership & Teams. April 5, 2022.
knightfoundation.org/reports/kdam-metrics/



Removing unintended hurdles in the pursuit of alpha

Hurdle-based approach

- Find reasons to exclude groups of managers to achieve a small candidate list
- Common hurdles:
 - Track record length
 - Assets under management

Positive-characteristics approach

- Identify possible candidates from total universe
- Seek positive evidence of capability across metrics **believed to drive performance**