

The power of people

by Drew Campbell

*How diversity, equity and inclusion can
unlock value in the investment world*



For most of its time as a leading initiative in the investment and business worlds, environmental, social and governance (ESG) has focused on the E, but the S is now taking more prominence with diversity, equity and inclusion (DEI) initiatives becoming a larger part of the conversation. Much like the challenges and obstacles environmental and climate-related initiatives faced when those standards were first being presented to investment managers and investors, social and DEI principles and standards are also facing hurdles. Understanding what DEI is and how it can be used in investment processes and within companies is the first challenge most people in the investment world will face.

“We view DEI as a component of the ‘S’ pillar of ESG, and DEI-related metrics are included in our quarterly monitoring and annual reporting on ESG-related performance,” says Sarah Borg-Olivier, chief operating officer with Instar Asset Management. “Social elements of ESG have historically been viewed as less tangible than environmental and governance factors and are perhaps even uncomfortable for people to discuss and explore.”

DEI is a complex subject, Borg-Olivier explains. “You need to think differently about how you have the conversation and how you measure and communicate performance and outcomes.”

To have open dialogues and make real progress, Borg-Olivier says people need to get comfortable being uncomfortable. “That’s a leadership capability we often don’t think about, but it’s important to embrace that engagement if you want to invite openness and encourage belonging in an organization,” she says.

Including a diverse range of backgrounds and perspectives to investment decision-making can lead to better outcomes, say DEI practitioners. In March, the Investor Leadership Network, composed of 13 global investors, and consultancy Diversio, engaged with asset managers and owners, industry associations, and government bodies to develop a set of inclusion metrics for company managers to give investment teams resources.

“As of 2021, at least 50 percent of our members collected some form of employee engagement or human capital management data,” the *Inclusive Finance Playbook* report notes. “The industry is clearly moving in this direction, and our members alongside other investors have expressed a clear need for

consistent metrics to guide this evolution and allow sector benchmarking, tracking, and best practice sharing.”

Shami Nissan, head of sustainability with investment manager Actis, says there is ample evidence now of a link between diverse teams and higher quality decision making across multiple industries. “The smartest companies will look for ‘culture add’ not ‘culture fit’ in the understanding that it is our differences which drive value — the ‘diversity bonus,’” she says.

Actis has an active inclusion and diversity working group made up of people from across geographies, functions, nationalities and practice areas. A DEI specialist and senior adviser with expertise in organizational change supports the group.

“If you want to get the best out of people — if you want them to give that extra discretionary effort and to reach their full potential — an inclusive and diverse environment is critical,” says Nissan. “We believe diverse groups make better decisions. Whether you are looking at a deployment opportunity, a value creation strategy or a point of risk mitigation, you need that diversity of thought to be an effective investor.”

Nissan says having multiple perspectives around the table ensures that every angle is covered in a discussion. The COVID-19 pandemic is a good example.

“Throughout the pandemic, it became apparent that inequality has grown, hitting certain groups disproportionately, including least-developed countries, the poor, women, the disenfranchised and marginalized,” says Nissan. “We have seen gender equality become a focus across the world, with higher demand for gender lens investing. It was becoming increasingly clear that taking a gender lens could amplify and multiply the effect of investment — women tend to spend their wealth on supporting family and the community, increasing economic growth.”

Actis invests globally and has thousands of employees in locations around the world working in diverse communities. The company drives initiatives through its portfolio companies, such as empowering local communities with land titles in Brazil; focusing on fairness for farmers in India; partnering with Masai landowners in Kenya; and bridging a skills gap in the Kenyan construction industry.

“Sometimes it is a question of us supporting and sometimes challenging our

portfolio companies in these matters, but equally our portfolio companies teach us,” says Nissan. “Some of our companies are already highly gender-diverse and have some creative ideas on fostering inclusion.”

Hamilton Lane, a private markets investment firm that allocates capital through primary funds, fund-of-funds, secondary transactions and direct investments, has incorporated “Social Justice Chats” and is working with the Out Investors network, a network of investors that supports LGBT+ people to help employees better understand the diversity and cultural experiences both within its own workforce and with the clients and larger world it works with.

“Once a month, we pick a topic focused on an underrepresented community or organization,” says Katie Moore, managing director in Hamilton Lane’s fund investment team and a leader of the firm’s emerging and diverse investment programs. “That includes topics such as women’s rights and the Black Lives Matter movement was a few years ago. All of this is important culturally and helps us to partner with the right organizations and feature the right speakers.”

Hamilton Lane engages with younger employees through an emerging talent program and works with underrepresented college students to train them on the asset class, and through the process learns what is important to them.

“Drawing from them, acknowledging their insights and hearing their thoughts and ideas is valuable,” says Moore. “Younger people think

about the world so differently than the way some others of us do.”

Moore says Hamilton Lane truly believes there is a link between this kind of diversity of thought, and this is borne out through the firm’s extensive due diligence process.

“We have the data to show that is true,” she says. “Every investment manager is put through the same process; the same rigor; the same decision making. We have seen that diverse managers in combination with strong portfolio construction — you still have to pick good managers — can lead to significant outperformance over the public markets, and in some cases even over the traditional established managers.”

UNDERSTANDING THE NUMBERS

One of the challenges ESG has faced in acceptance and adoption is a belief that investment returns would suffer. Collecting and analyzing data to understand how incorporating these principles into company operations and investment decision-making affects performance is an important step toward wider use of ESG.

Hamilton Lane is working with Novata, a company it has invested in, to help develop an ESG-reporting platform for the private markets. The design phase of creating the platform included input from limited partners and general partners alike.

“When you think about the ever-changing market standards and expectations, Novata is what we think will be a pivotal tool to help get that data consistency and meet companies where they are — whatever data analytics and metrics are important for them to track and understand. There is no one size fits all solution,” says Moore.

That kind of flexibility in data tracking and analysis is needed for the myriad of sectors, applications, geographies and other variables that are present where companies do business.

There are a number of standards from which to choose to measure ESG and DEI performance, and that can be both beneficial but also add confusion to the process. Deciding which standards and benchmarks to use is critical because it will drive the process.

Abigail Rayner, principal with HarbourVest Partners, an investment adviser that allocates capital through fund-of-funds, secondaries and direct transactions, emphasizes the importance of consistency in data collection and analysis when considering the use of ESG principles.

Diversity, equity and inclusion definitions

- **Diversity** is making a concerted effort to have people of diverse backgrounds visibly present and represented in the workplace. Race, gender, socioeconomic background, sexuality, religion, and other socially ascribed attributes intersect to create an individual’s identity.
- **Equity** is the guarantee that there is a level playing field where everyone is assumed to have access to the same life opportunities. In the absence of this, equity refers to our commitment to level the playing field to create a more fair experience in a pluralistic, multicultural society. It acknowledges that marginalized groups of people face more obstacles compared with their more privileged counterparts, resulting in different life changes that we often assume are merit-based.
- **Inclusion** is the active response to diversity awareness. The workplace must create a culture of safety and belonging for diverse groups of people for them to thrive.

Source: *Diversio* Diversity & inclusion best practices report

EXAMPLES OF ENGAGEMENT TACTICS

MINORITY OR PASSIVE INVESTORS

DATA COLLECTION & REPORTING

Screening for inclusion at the pre-investment stage using publicly available data

Tracking regularly and divesting when a minimum threshold is not met (e.g., an inclusion-related scandal surfaces)

COMPANY ENGAGEMENT

Signaling intention to use an inclusion screen publicly

Working with other investors through pledges and industry commitments (e.g., 30 percent club)

MAJORITY OR ACTIVE INVESTORS

DATA COLLECTION & REPORTING

Updating reporting expectations to include Inclusion Metrics

Benchmarking performance and incorporating into risk assessment or due-diligence frameworks

COMPANY ENGAGEMENT

Engaging with executive teams and boards of directors

Communicating the importance of inclusion at annual general meetings

Source: *Diversio* Diversity & inclusion best practices report

Note: *Diversio's Public Market* tool provides benchmarking solutions for publicly available data to support pre-investment activities

“We have participated in ILPA’s Diversity in Action working group, which, in addition to showing an overall commitment to advancing DEI initiatives and sharing best practices, aims to define a diversity team metrics template,” says Rayner. “We believe it is vitally important that data collection efforts are streamlined across the board so that investors have a consistent approach when requesting diversity data or information.”

ILPA, the Institutional Limited Partners Association, is helping investors and investment managers understand ESG from the perspective of the finance world and has partnered with the National Association of Investment Companies to support diverse investment managers. The two organizations hosted a North American Roadshow for diverse managers in July and will host a European Roadshow on Dec. 9 for the same purpose.

ILPA has an ongoing Diversity in Action Initiative, which includes a DEI and Inclusion Roadmap, an ESG Assessment Framework and a Diversity Metrics Template, all of which have tools to help people and companies implement ESG principles and objectives into their processes.

HabourVest has developed an ESG Manager Scorecard to assess general partners on nearly 30 different environmental, social, and governance-focused indicators. The scorecard includes a diversity and inclusion component that is aligned with ILPA’s standard DEI due-diligence questions.

“We implement and assess DE&I internally at a firm level and externally through industry partnerships, while we use ESG metrics to measure the impact our partners have on the environment and society,” says Rayner. “While developing our scorecard and the embedded DEI component, we aligned with the standards set forth by both ILPA and the Principles for Responsible Investment, so the approach is harmonized.”

Borg-Olivier concludes by making the point of why people are so important to companies and organizations — they are the ones who run them and they are at the heart of their success.

“Our teams should reflect the broader world — it helps us to relate more meaningfully to our investors, customers, partners, communities and other stakeholders,” says Borg-Olivier. We recognize that DEI is a strategic leadership imperative, not merely an HR exercise. It’s also a pressing moral and social issue. How do we communicate the importance of DEI in our words and actions? How do we foster a corporate culture that leans towards new ideas and change? How do we remove diversity-related barriers to recruitment and career progression? Getting DEI right is integral to how our companies serve our stakeholders and create economic and social value.” ❖

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