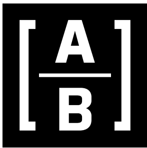
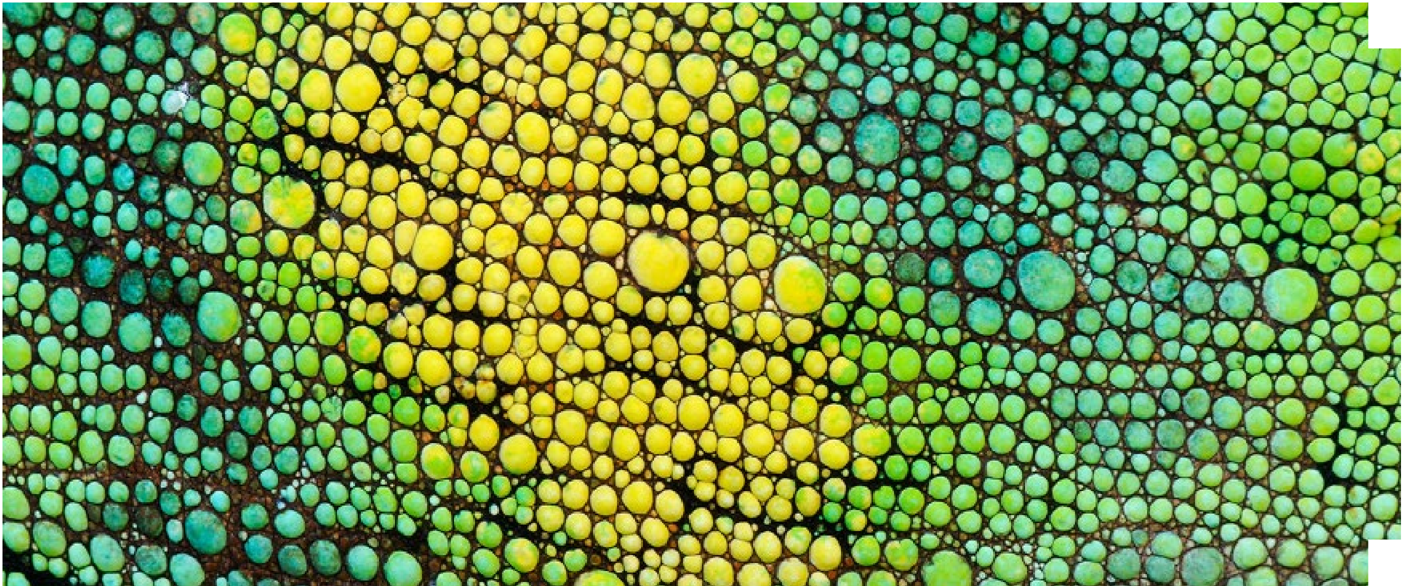


ALLIANCEBERNSTEIN

AB IQ

INSTITUTIONAL INSIGHTS

Q3 2021



INIGO FRASER JENKINS
Co-Head—Institutional Solutions

Metamorphosis

An Investment Industry in Transformation

Innovation is overtaking a broad swath of the investment industry, from portfolio design to the definition of alpha and from investment methodology to organizations themselves. Much of this evolution is driven by changes within the industry (such as lower fees on passive and quasi-passive products as well as the growth of alternatives) and exogenous factors in the broader policy and market outlook.

Rotation from Traditional Active to Passive/Alts Barbell

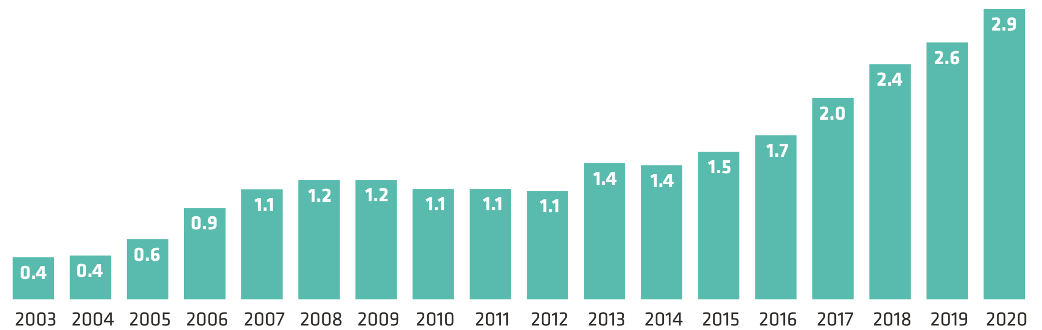
One area seeing transformation is the realm of asset allocation. We think the rotation from traditional active funds into a passive/alternatives barbell will continue, motivated by the view that traditional equity and fixed-income allocations will be unable to generate high returns and that alternatives may offer better diversification. Some investors also specifically seek inflation protection.

The macro outlook of high asset valuations, lower real returns and less diversification all point toward a continuing push into alternatives. At a more fundamental level, this migration is also supported by relatively fewer initial public offerings (excluding special purpose acquisition companies, at least) and companies choosing to wait longer before they list, depriving public markets of some early-stage growth opportunities.

Having said that, we also see a greater case for making distinctions within alternatives. For private equity in particular, the outlook may become less favorable. The amount of committed but uninvested capital (so-called dry powder) has nearly tripled over the past decade (*Display*), bidding up the entry price and forcing down future returns. Indeed, the average multiple for private equity deals has risen over this time frame as a consequence.

RECORD DRY POWDER EXPECTED TO DEPRESS FUTURE RETURNS

Global Private Uncalled Capital, USD Trillion



Past performance does not guarantee future results.
As of September 8, 2021
Source: Preqin and AllianceBernstein (AB)

Also, the strong recent track record of private equity returns has benefited from an incredibly favorable period for businesses that rely on leverage, with both credit spreads and risk-free rates declining. That backdrop can't be relied on to continue.

A further consideration for private equity is the question of the nature of diversification it offers—one should not conflate diversification with stale prices. Private equity also faces considerable risk from fund selection, given its much wider spread of outcomes between top and bottom quintile funds compared with active public equity.

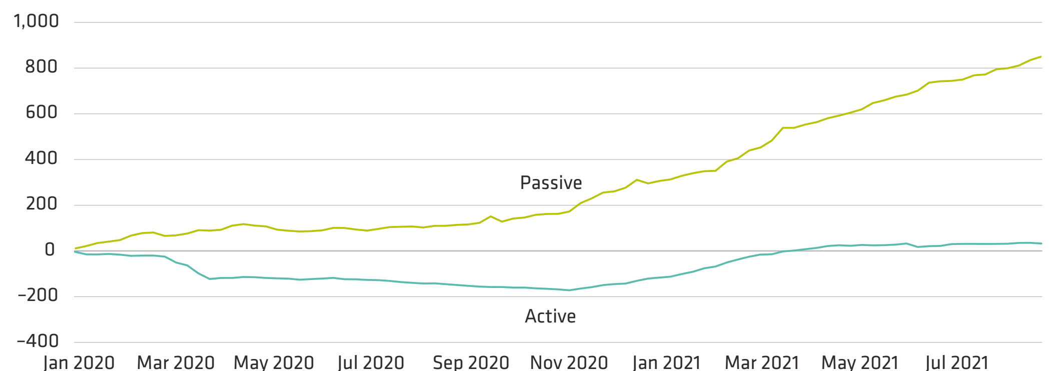
If part of the rationale for private equity is that it can deliver higher returns than public equity, and if going public is the ultimate exit, the implication is that over multiple cycles the returns from private equity can't escape the same constraints as public equity. That is, other than by using leverage, which investors can access separately. The bottom line: allocations to alternatives will likely expand, given a supportive macro environment, but the average private equity investment might disappoint.

A Blurring Line Between Passive and Active

During the pandemic, we have witnessed a net rotation into passive and away from active. The passive share of assets under management (AUM) actually fell slightly in the early stages of the pandemic, but this decline stemmed from cuts in passive allocations as a quick way to reduce equity exposure. In the (belated) rotation back into equities that started a year ago, the rate of rotation from active to passive increased further (*Display*).

NET ROTATION INTO PASSIVE DURING COVID-19 PANDEMIC

All Equity Cumulative Active and Passive Flows (USD Billion)



Past performance does not guarantee future results.
As of August 25, 2021
Source: Emerging Portfolio Fund Research Global and AllianceBernstein (AB)

We expect the passive share of US equity AUM to increase further; passing the 50% threshold was not in any way a limit, merely a marker along the route. The realistic near-term limit to passive allocation comes not from the market but from asset owners who realize that passive allocations in a 60/40-like framework pose the risk of delivering negative real returns.

As the active/passive equity migration continues, the line between what counts as active and what counts as passive is not a fixed line marked in stone but a dynamic frontier.

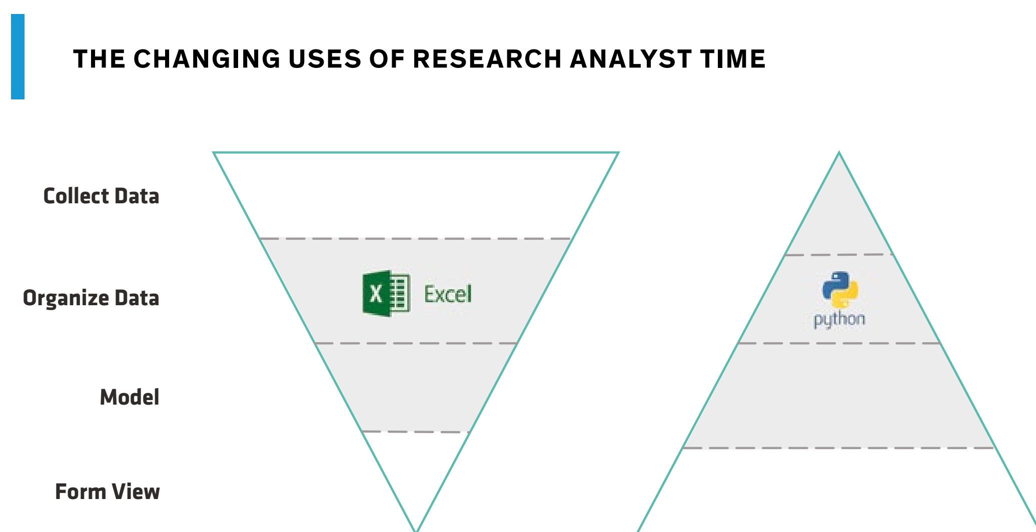
This is most evident in the declining fee for equity factors from over 20 basis points to 4 basis points in the past decade. So, the cheap benchmark that funds are compared with is no longer simply the broad market index but the broad index and a set of cheap factor exposures that are almost free. In this way, the benchmark for active management is revealed to be multivariate—not univariate.

On one hand, this massively raises the bar for active management, but on the other hand it bolsters active management by revealing which kinds of funds genuinely add value through return streams that can't be easily replicated. We think that this evolution shifts the key definition of alpha in the industry away from simple excess return and toward idiosyncratic alpha measurement versus a passive factor set.

From Excel to Python…and Then Machine Learning?

A very different kind of innovation in the industry is transforming the methodology of financial analysis. We would argue that the switch from paper spreadsheets to Excel 30 years ago did not materially change the nature of financial models—it merely made them more complicated and easier to update. But a switch from Excel to Python is likely to fuel a more profound change, with analysts spending their time very differently (*Display*).

THE CHANGING USES OF RESEARCH ANALYST TIME



For illustrative purposes only.
As of August 31, 2021
Source: AllianceBernstein (AB)

Already, some data collection—such as web-scraping prices—is executed with Python. Python also seems likely to increasingly handle organizing that data. In time, this could extend to the actual modeling process. There's always resistance to this type of change, but there are push and pull factors.

The pull factor: as "passive" strategies develop, the dividing line between passive and active will shift, requiring active approaches to tap a broader set of data in order to achieve idiosyncratic returns and stay ahead of the competition. The push factor is cost: it's likely more efficient in time and personnel to manipulate data in Python, and inexorably declining fees and pressure on margins will force the transition.

This process has advanced the most in quantitative modeling. Modeling for truly systematic investment wasn't taking place in Excel in the first place, but here the methodology is changing by adopting machine learning—and in some cases the claim of artificial intelligence. The push and pull factors are similar, but the jury remains out on how far the process will play out. Adoption of machine learning for manipulating and extracting data seems set to grow dramatically, but it's unclear to what extent it can be applied to making actual investment decisions.

There are also open questions on how much complexity is acceptable in financial models, especially when they fail; preferences may develop for different kinds of machine learning models. So-called ensemble models like random forests can be constrained structurally so that they can be mapped onto the "real world," while neural nets and support-vector machines lack that option.

Factors Could Become the New Asset Classes

The past four decades have been an extraordinary time, with prices on financial assets rising and diversification among them plentiful. Now, investors face a strategic valuation problem. This isn't necessarily bearish, but it does imply low expected real returns on major asset classes. And if inflation rises, bond diversification may not be as effective, which could increase portfolio risk.

Set against this backdrop, valuation spreads within asset classes are very extreme. At the same time, we can demonstrate that the diversification benefits of factors tend to be more stable than those of asset classes. Perhaps at least part of the answer to the current risk/return dilemma is to consider asset classes and factors as interchangeable. After all, securities markets are ultimately merely composed of assets issued by companies and governments—who's to say that a more "primal" way of dividing them up is by their legal structure (asset class) rather than financial characteristics (factors)?

One pushback on this notion is that it requires investors to deploy assets in a way that, for the past decade, would have been very suboptimal.

For 10 years, the cheap and accepted option of simply buying passive stocks and bonds has been a great trade. Meanwhile, the average return of factors has been below their longer-run average rate of return, with the case of apparent "failure" of the value factor prominent in that. However, we think that cyclical factors explain at least some of this. A factor approach would certainly not be a panacea, but we think it might be essential to achieving a given level of risk/return and will likely appeal more to investors who believe that the post-pandemic world will be fundamentally different.

Organizational Implications: Falling Silos?

What are some of the organizational ramifications of the innovations we've discussed? In an environment in which it's harder to generate a given level of real return, it's more likely that the industry will need to consider its output as a "return stream" rather than a certain kind of fund "product."

This could lead to realigning organizations based on the nature or characteristics of return streams (alpha, factors, security-specific, macro) rather than asset class. Moreover, the switch from Excel to Python for financial models seems poised to blur the distinction between quantitative and "fundamental" models—and hence the historic partition between these modes of investing.

At the same time, to the extent that this modeling change enables the use of (expensive) new data sets, it implies that the new models that are needed, and the teams that develop them, become functions spread across organizations rather than limited to a specific asset class. That shift could make new modeling capabilities more cost-efficient. It might be necessary to break up long-established investment industry silos before these changes can be fully realized.

The views expressed herein do not constitute research, investment advice or trade recommendations and do not necessarily represent the views of all AB portfolio-management teams.

CHRISTOPHER W. MARX
Senior Investment Strategist—Equities

ERIN BIGLEY, CFA
Senior Investment Strategist—Fixed Income

Investing Reinvented

Capturing Disruption in Companies and Portfolios

In a world of pervasive innovation, investors need a new mindset to identify transformational companies and portfolio strategies with true return potential. But reaping the benefits of innovation also requires some old-fashioned fundamental sense.

Do flashy products or services that claim to change the world stand up to traditional business scrutiny? Are innovative funding structures capable of incentivizing good corporate behavior and producing solid returns over time? Will new trading technology create meaningful advantages for investors on the right side of change?

Dazzling investment fads aren't always supported by strategic rationale. Still, innovation can be harnessed to capture powerful return sources and to create solutions to evolving investing problems. As always in investing, the secret to success is to ask the right questions and to take a sober look behind the hype to gain a comprehensive understanding of the latest developments.

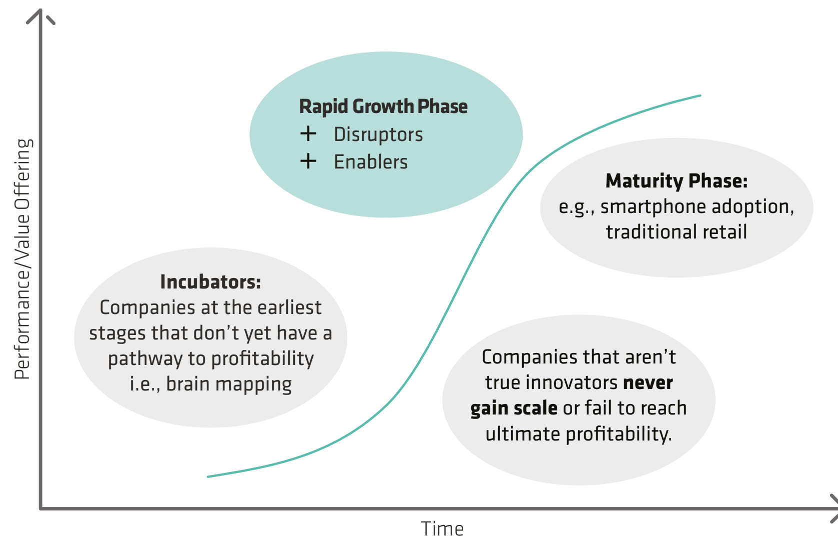
How to Identify Investible Innovation

It's perfectly natural for investors to get excited about the next big thing. Early investors who backed companies like Apple or Amazon.com and stuck with them enjoyed outstanding returns. Yet identifying successful innovators in hindsight is easy. It's harder to find the most investible companies today, when countless firms say they are poised to disrupt a wide range of industries. Setting guidelines can help facilitate a successful search for innovation with return potential.

What features point to **truly disruptive** companies? Lasting innovators introduce features or attributes unquestionably different in a product, service or process. Many innovations offer evolutionary improvements on current products or processes. Breakthrough innovation refers to revolutionary developments like synthetic biology, electric vehicles (EVs), or true artificial intelligence and autonomous driving.

To be a successful investment though, a disruptive company needs a market with robust demand. Highly differentiated product sets add resilience to profitability and create high barriers to entry from new competitors. Companies that benefit from network effects—the tendency to exponentially expand customer reach, which drives future monetization opportunities—are particularly attractive. The sweet spots for successful investments often lie in the steeper portion of the innovation "S-curve," or the rapid growth phase (*Display*).

FINDING ATTRACTIVE INVESTMENTS ON THE INNOVATION S-CURVE



Source: AllianceBernstein (AB)

For innovators, commercial success also requires exceptional management teams. When creating a new market, management must have vision and focus, always with an eye on competitive threats and a willingness to "self-disrupt" their own processes to stay ahead.

Enablers: Leaders Behind the Scenes

Don't just be seduced by headline-grabbing products. Instead, look further afield as technology enablers are often a better source of investible innovation in public equity markets. Enablers might not have the sexiest products or services. However, these companies provide the underlying technology to power blockbuster products and burgeoning trends. As a result, they tend to benefit from powerful demand drivers. And because they don't dominate the headlines or investors' attention, they often offer much better valuations and long-term return opportunity.

For example, suppliers of car safety systems aren't household names, but they are almost certain to benefit from steady growth as automatic braking systems and blind-spot detection systems become mainstream in vehicles. Sophisticated sensors are becoming commonplace in a wide range of products, from computers to trains to spacecraft. Companies that make components for the Internet of Things are well positioned to benefit from an increasingly interconnected world.

Platform companies that benefit from network effects are another wellspring of innovative potential. Network effects are the disproportional benefits generated by the addition of new users. Think about companies like PayPal and Salesforce.com; they function as matchmakers, reducing business friction as the number of participant connections grows. That helps grow a company's total accessible market—and effectively lower transaction costs, which can stabilize revenues.

What's the secret to success for high-density platforms? Leaders enjoy a protective supply and demand model that often assures consistently high return on invested capital and stable sales growth. Would-be disruptors struggle to cross an ever-widening network-effect moat. For example, in the US, Zillow's online real estate database controls most of the country's house listing supply and most of the viewer demand—a high barrier that new entrants can't seem to clear. And great platform businesses **tend to yield strong-performing stocks**—not just among the few concentrated at the top but across a broad swath of global companies.

Emerging-Market Innovation: Not Just China

Innovation is no longer just a developed-market story. **In emerging markets (EM), too**, investors can discover abundant innovation. That's why technology and internet-centric companies make up about 40% of the MSCI Emerging Markets equity benchmark—up from only 11% in December 2007.

Investors should look beyond the usual suspects for EM innovation. It's not just about exports and it's not just in China. The new wave of EM innovation is focused on developing new technologies for domestic use. Local internet companies are growing fast and establishing strong market positions in countries as diverse as India, South Korea or Russia. Poland's Allegro, for example, is an internet shopping destination with a 33% market share of Polish e-commerce, well ahead of US competitors such as Amazon.

In fintech, India is one of the world's fastest-growing markets. In 2020, India processed US$25.5 billion in real-time payments, according to ACI Worldwide. Banks in India are leveraging technology and big data to grow their business. For example, HDFC Bank has developed technology to approve personal loans for customers in as little as 10 seconds; its personal loan business grew over 12% year over year in April 2021.

Green Revolution Drives Change

Innovation is not only driven by technological change. Sometimes social change, like increased environmental attention, can drive change. In both emerging and developed markets, growing global efforts to combat climate change are creating fertile ground for innovators. For example, although EVs are still a niche product today, with only 7 million vehicles in the global fleet of 1.6 billion, technological breakthroughs are widely expected to promote a huge increase in adoption. By 2030, we expect 200 million EVs on the road around the world. The beneficiaries of this shift will be not only EV manufacturers, but also auto-parts suppliers, battery-makers and certain semiconductor companies that are enabling the transition.

In the rapidly evolving world of climate solutions, many companies are pioneering completely new industries with rapidly growing demand drivers. Investors can take innovative approaches to find them, for example, by searching for companies with formidable **carbon handprints**. In contrast to carbon footprints, which measure the negative impact of companies on the environment, companies with carbon handprints are creating positive solutions to global climate challenges. Companies with formidable carbon handprints will be at the forefront of efforts to reduce the world's carbon intensity. Many offer products and services that will facilitate the transition to a low-carbon economy or help communities become more resilient against the physical effects of climate change. Examples include companies providing decarbonization solutions for clean energy, resource efficiency, transportation and sustainable agriculture, as well as resiliency solutions for water and infrastructure.

Novel Funding Models and Portfolios

Alongside the vibrant innovation driven by companies, the financial sector is rapidly offering new ways for companies to raise money and for investors to back them.

In equity markets, special purpose acquisition companies, known as SPACs, have become wildly popular on Wall Street over the last year as an alternative to initial public offerings (IPOs). In this model, investors fund a "blank check" company with the intention of purchasing a yet-unnamed privately held company and taking it to market. SPACs have helped hundreds of companies find a speedier path to market than traditional IPOs, but they also have a complicated financial structure and present risks to the initial financial backers—who don't know what the target company will be. Although SPACs have existed for some time, their recent popularity surge demonstrates the market's growing appetite for innovative funding structures that break through established Wall Street norms. While the SPAC boom is opening up exciting new funding opportunities for innovative companies, investors must approach these deals with caution and be aware of the risks, as they are typically signing a blank check for a target company to be determined later.

Fixed-income investors are also seeing big changes in issuance structures, particularly when it comes to environmental, social and governance (ESG) bonds. While green bonds to finance a specific environmentally focused project or projects have been around since 2007, the concept has been expanded and enhanced in recent years. Today, investors can also buy bonds that are dedicated to social projects—such as new buildings for communal benefit, educational programs for underprivileged demographics and more hospital beds for low-income areas. **Green and social bonds** offer the ability to marry an investing strategy to a project aligned with a responsible investing agenda (*Display*).

ESG STRUCTURES: THE LANDSCAPE

	Project-Based Structures			Target-Based Structures
	Green Bonds	Social Bonds	Sustainability Bonds	KPI-Linked Bonds
Short Description	+ Funds dedicated to green projects + Follow the ICMA GBPs framework	+ Funds dedicated to social projects + Follow the ICMA SBPs framework	+ Funds dedicated to both green and social projects + Follow the ICMA SBPs and GBPs frameworks	+ No requirements for the use-of-proceeds + The issuer is committed to meet green target(s), otherwise coupon/ return will increase + ICMA recently issued guidelines for this structure
Subject to a Framework?	✓	✓	✓	✓
Project Based?	✓	✓	✓	✗
Funds Committed?	✓	✓	✓	✗
Issuer Retains Flexibility?	✓	✓	✓	✓
Direct Impact if KPI Not Met	✗	✗	✗	✓
Included in Green Indices?	✓	✗	✗	✗
Impact Report	✓	✓	✓	✗

Analysis is for illustrative purposes only and is subject to revision.
As of May 17, 2021
KPI denotes key performance indicators; ICMA denotes International Capital Market Association; GBP denotes Green Bond Principles; and SBP denotes Social Bond Principles
Source: AllianceBernstein (AB)

Bonds with key performance indicators (KPIs) were introduced in recent years, which penalize companies for not meeting explicit sustainability goals. These are different from the project-specific green bond format by linking a company's sustainability goals to its bottom line. For example, in 2020, Italian utility Enel issued a bond that pins the company's renewable energy goals to its bottom line. If Enel falls short of having 55% of its electricity generation capacity in clean energy by the end of 2021—up from 46%—the bond's coupon rises by 0.25%.

Innovations in this area could get a boost if companies begin to set ambitious KPIs and convert the majority of their capital structures to such bonds. A components manufacturer recently committed to a sustainability performance target featuring a greater-than-20% reduction in greenhouse gas emissions within 10 years—an ambitious target in the context of its industry peers. Further, the company has committed to future bond issues in the same format as part of its long-term strategic plan.

Companies that fail to achieve the KPI within the specified timeline are penalized with a coupon step-up on the bond. Accordingly, investors must research the company's overall sustainability strategy and determine whether the KPI aligns with that goal.

For all ESG-related bonds, investors must be vigilant about greenwashing. That means making sure that the issuer's projects are genuinely environmentally beneficial and not misrepresented. Metrics established for a project's impact report should be specific, material and credible. This is especially important in KPI-linked structures, where companies have much more flexibility around the use of proceeds. Innovative bond structures cannot deliver returns or ESG results automatically, but rather, require comprehensive due diligence and engagement with management on the part of investors.

Even without a KPI structure, bond investors are finding new ways to align their financial goals with social and environmental initiatives. In the US, some municipal bonds issued by state and local entities are designed with specific impact goals in mind, such as ensuring safe drinking water or helping underserved kids. For example, in 2019, the Essex County Improvement Authority issued $70 million in municipal bonds to mandate the replacement of 18,000 lead water service pipes that risk the health of thousands of Newark residents. So far, nearly 21,000 lines have been swapped out. Last year, the Arizona Autism Charter School in Phoenix issued $9 million in muni bonds to renovate and add facilities.

Keeping Up with Innovation

With so much innovation unfolding across companies, portfolios and asset classes, investors may struggle to keep up with the pace of change. Innovation is indeed everywhere, affecting everything from the company held in your portfolio on the other side of the world to the trading systems that turn over securities every day and the growing range of strategies on offer.

Advanced technology can help bond managers scan the entirety of the bond market in real time, suggest potential trades, build out trades in seconds and invest new portfolios more quickly. Three years ago, it took an average of 35 days to get a new credit or emerging-market debt portfolio 90% invested. Today, that can be accomplished in half the time—if bond managers have mastered the tech revolution. And every extra day those assets are invested amounts to more interest earned. Lastly, cutting-edge tech allows traders to cut through the noise of thousands of bonds trading at any given time to find opportunities and source liquidity. In contrast, bond **managers who don't have the right tech will fall rapidly behind in the post-pandemic world**.

Innovation in trading, investing or portfolio structures, however, is only as good as its ability to help meet investment goals. By keeping that principle front and center, we believe investors will be able to distinguish between changes that will end up as footnotes to market history and those that will deliver lasting improvements to long-term performance and the consistent achievement of strategic objectives.

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The Pandemic Effect on Organizational Wellness:

Expert Roundtable

The challenges of the COVID-19 pandemic have reinforced the importance of organizational wellness and made it more challenging to maintain. But the stakes are high, with wellness a major driver of organizational performance, talent retention and recruitment.

We asked experts in the medical and investment management industries to provide a deeper perspective on organizational wellness, how to maintain and assess it, and the moving parts as leadership teams lay out a pathway for returns to offices.

Every organization is made up of individuals, and the pandemic has had profound effects on so many people. Can you share with us some of the lingering issues that firms should expect employees to still be coping with even as they return to offices in some form?

Dr. Lindsey McKernan, PhD, MPH, Associate Professor, Psychiatry and Behavioral Sciences, Vanderbilt University Medical Center: The pandemic created a unique mix of challenges. Many people have suffered elevated levels of anxiety and depression, trauma, physical strain (such as chronic fatigue), grief and burnout. Protecting themselves and loved ones from the pandemic while logging many work hours was an intense and protracted source of stress.

We all cope differently when met with stress. While one person may retreat, another could dive into work for distraction or to feel more in control. Some workers endured periods of withdrawal and may have seen work performance suffer—being late on deadlines they normally would have met, missing or being late for meetings. Other staff may have coped by being extreme overproducers who sacrificed much more than normal—late-night emails, green lights always on, severely blurred lines between professional and personal.

We need to be mindful of grief and loss when reconnecting with our employees. Grief was a common factor among many. Some may have lost loved ones and friends, and many of us have lost out on parts of our lives and our children's lives that we never expected to miss. A number of studies have shown that connections to people who have died from COVID-19 are surprisingly widespread. In one US survey, one in three respondents knew someone who passed away from the virus. Grief is complex and lasting.

All of these aftereffects will be present to some extent in returning colleagues. It's also important to know that grief can be intensely private for some, and you may not know the extent of loss a person has suffered through the pandemic.

Remote work necessarily balances safety and collaboration. What considerations (safety, logistics, productivity, personal interactions, flexibility) are in the mix as you enter the "return to office" era, whether it's hybrid or fully in office? What's top of mind?

Lee Georgs, Chief Operating Officer and Executive Board Member, Redington: Our Health Committee, which was set up during the first few weeks of the March 2020 lockdown, is driving our return-to-office policies. But we're also listening to team leaders, business leaders and individual employees. We hope to phase back into the office gradually once the government lifts restrictions.

It's a bit complex logistically: we've hired extensively during the pandemic, but our office footprint hasn't grown so we need to implement both a hybrid working model and hot-desking system at the same time. We want to stay connected in the phased return, so we'll experiment until we get it right. Our headquarters in London is a traditional open floor plan arrangement, which means we're looking at ways to keep people focused and efficient in a naturally louder, more energetic environment. Headphones are a start, but there's more to be done.

We're planning to start with a three/two model, with most people in the office three days and home two. Initially, we'll bring full teams in together, rather than splitting them. We'll need to balance intra and inter-team touch points and collaboration but, with many new people, we feel strongly about the need to solidify teams. Of course, we'll learn and adapt as we go.

Nicole Hartigan, Head of People and Culture, Frontier Advisors: Top of mind is retaining the benefits of collaboration and the synergies from many minds working toward solutions for our clients. You can collaborate remotely, but there's a lot of value from interactions that happen in person and within groups—often from those who may otherwise be on the periphery of an issue. Good solutions are often an amalgam of ideas or observations that might not otherwise connect without the extra dimension that in-person interactions provide.

We're encouraging our team to aim to be together two days each week (Tuesday and Thursday). On those days, we can more easily hold team meetings, including firmwide meetings. Having as many of our people together as possible is also invaluable in keeping that sense of camaraderie and connection that is so important in maintaining our strong culture. And being a part of a strong team culture is critical to the personal satisfaction and fulfillment we each gain from our jobs.

Dr. Lindsey McKernan: Even for workers initially coming in on a limited number of days, it's their first time in an office in over a year—and a massive environment change. Any transition is fertile ground for a stress response, and could resurface pre-existing or dormant mental health challenges.

> **"Organizations must put a high priority on compassion and empathy, supporting colleagues as they seek a new sense of stability."**
>
> – Dr. Lindsey McKernan, PhD, MPH, Associate Professor, Psychiatry and Behavioral Sciences, Vanderbilt University Medical Center

Organizations must put a high priority on compassion and empathy, supporting colleagues as they seek a new sense of stability. Communication has to be consistent, open and transparent at all levels to keep people anchored. Respect new boundaries between work and home: they've been blurred, and they need to become less blurred.

For those returning, organizations should encourage them to take stock of how they feel about it. It's important to acknowledge these feelings and to normalize the sense of discomfort a person feels, emphasizing that you can move through it together. Also, encourage employees to consider the benefits of coming back: What aspects of work—and teamwork—could improve by connecting in person? How could the boundaries between the office and home work in your favor?

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How has the mix of benefits, including wellness, evolved as a result of the COVID-19 pandemic? What elements have you introduced or expanded to keep the work/life balance as healthy as possible—and how did the delivery of those benefits adapt to a remote environment?

Lee Georgs: The combination of physical and mental effects of the pandemic are different for everyone; some employees or loved ones have become ill, compounding the mental strain. People with long COVID-19 symptoms have needed extra sick days, medical help and support. We've adjusted schedules to allow people to return in a way that works for them and doesn't overburden them as they recover.

For some, childcare and homeschooling are big issues. For others, household members are frontline workers—doctors and nurses—and have needed flexible schedules. In one instance, we arranged medical care and therapy for an employee whose home office setup created physical issues—so we assessed the specific needs of the individual and then upgraded their equipment. Some people have needed extra mental health support (which we've facilitated) as well as more time away from the office to get well.

"It's important to be open about the challenges we face, so we've had senior leaders share their own struggles."

– Lee Georgs,
Chief Operating Officer and Executive Board Member, Redington

It's important to be open about the challenges we face, so we've had senior leaders share their own struggles. Knowing—and seeing—that someone else is experiencing the same issues as you creates a stronger sense of community and a feeling that you can speak up and ask for help. This is especially important when remote work prevents "casual collision opportunities": stumbling across a colleague during the course of the day, which is only possible in a physical setting.

Nicole Hartigan: To promote wellness, our team has taken on personal exercise challenges and group challenges coordinated remotely. Beside the personal benefits, they provide fun and healthy competition between teams. An area of our intranet is set aside for staff to post pictures of what they're up to and to set a challenge for others to match. Often this involves family, a nice way for us all to learn a little more about out colleagues' lives if they wish to share.

In the office, we've been providing staff with healthy snacks. Because of limitations around the communal use of our kitchen and food preparation areas, it's been important to enable colleagues to come together again in the breakout area for conversations away from their desks. Providing pre-made healthy sustenance has been a way of encouraging that.

While working remotely, we've staged many social events virtually, ranging from trivia quizzes to birthday and farewell presentations as well as regular end-of-week drinks and catch-ups. It's hard to replicate social events remotely, but it's also vital to celebrate milestones and come together. With some imagination and creativity, virtual celebrations can be great fun.

Tell us how you're working to retain top talent whose priorities may have changed as a result of the pandemic? What benefits, including work/life balance, are prospective employees looking for in an organization post-COVID-19? What's the best way to remain competitive in attracting top talent?

Lee Georgs: We have a history of embracing flexible working and trying out different working arrangements to accommodate family needs or personal circumstances. I think that's going to become more and more the norm going forward. Psychologically, people have been through a war, and this will reverberate for years to come.

We need to create work environments that suit people's home, family and outside commitments: to find a way for people to continue contributing in a way that works for both them and the company. Experienced people are a little more practiced at flexing that muscle, but it's harder to do that early on in your career.

I don't know if the ultimate answer is a hybrid working environment, but we also don't want to move into an environment where those in the early stages of their careers are all in the office and those that are more senior and established are working from home. We have to find a way to help everyone thrive.

Nicole Hartigan: The fundamentals of retaining talent remain. Challenging and interesting work, a sense of purpose, recognition for effort, the ability to balance work and life and a positive team culture are all key for most people. Remaining more than competitive in what we can offer our team across these areas is as much of a priority as it was pre-COVID-19.

We already offered a lot of flexibility in working remotely, but the pandemic has accelerated that. Employees and clients are now alert to the opportunities of different ways of working. We need to not just respond to that but to proactively encourage and support our people in finding a balance that works for them and their teams. Ultimately, that balance will provide the best results for our staff, our firm and—most importantly—our clients.

People want to work for organizations that will support them in achieving great outcomes and be part of something that they can feel proud of. The pandemic has likely increased the importance of purpose in all areas of our lives. Good people will always want to work in organizations with strong values and a clear purpose.

In what ways has culture had to evolve and adapt during the pandemic? What role does leadership play in maintaining a diverse, inclusive culture that addresses all employees' needs while ensuring cohesiveness and overall wellness? How can you determine the mental and physical wellness of an organization—as opposed to that of an individual?

Lee Georgs: Culture is a living, breathing, amorphous thing that firms need to look after as the number one priority. It's going to change and evolve—it has to evolve. What you must fiercely defend are the parts of a culture that are non-negotiable.

We conduct a quarterly pulse survey to find out how we're doing on engagement, alignment and culture. We drill down by team, business line, gender, ethnicity and seniority. It's not a perfect measure, but it's our temperature check. It's especially important when we're not in the office—it includes gauging the opinions of those individuals hired during the lockdown who have never been to our office or met one another.

I have no doubt the virtual environment has impacted our culture, as will the eventual return to in-person contact. We need to hold onto cultural pillars: call out behaviour that doesn't align with our values and ask for and give feedback regularly across the company. We've always tried to instil these habits; we've worked harder at it during remote work and will continue to work at it in a hybrid environment.

Nicole Hartigan: We all have a role to play in building a strong culture that thrives in any situation. But, it's clear that leadership lays the foundations and is responsible for gauging the health of an organization's culture—and for providing any nudges required to stay on track.

Leaders regularly checking in on individuals and genuinely seeking their ideas and impressions is critical in gauging organizational health. Communicating business strategy and financial health is important, but listening to the way each team member sees the strategy and hearing their ideas is the only way to really understand an organization's mood. Looking for different perspectives and experiences within the team will reveal the level of cohesiveness that exists, and will also unearth challenges and opportunities.

"Communicating business strategy and financial health is important, but listening to the way each team member sees the strategy and hearing their ideas is the only way to really understand an organization's mood."

– Nicole Hartigan, Head of People and Culture, Frontier Advisors

Harnessing the benefits of diversity is more than just recruiting a team with diverse backgrounds. The benefits come from ensuring that everyone has the chance to contribute and share their unique insights and experience. Being able to blend a broader set of experiences and perspectives, rather than expecting diverse thought to adapt to existing practices, provides the most complete and original solutions and keeps an organization fit

How much of a priority is investing with asset managers that emphasize wellness? How can you determine if a firm is aligned with your view of wellness? Are there attributes you look for or questions you ask? Is there specific data (e.g., employee retention data, engagement surveys, etc.) to quantify the wellness of the asset manager? What's the biggest challenge in assessing organizational wellness?

Lee Georgs: Wellness is critical because it influences so much of how organisations do business. As part of our ongoing due diligence process, we require detailed questionnaires from our asset managers and vendor partners. They cover many aspects, including ESG and I&D [inclusion and diversity], both of which are vital to wellness. These, and many other wellness aspects, flow into an asset managers' decision-making processes, which is critical.

Decision-making groups experience all kinds of phenomena; not all of them good. If the highest paid person in the room speaks and everyone agrees, why even have a group? You must elicit different perspectives so that issues are surfaced, heard, discussed and evaluated in order to establish a better decision-making process. It's crucial that the organisational make-up is diverse if you want to be able to draw out different perspectives and ultimately reach complex, difficult decisions.

As investment consultants, we work very hard to ensure that every member of the pension trustee boards and investment committees we work with understand the decision-making levers at play. It's important that every person in the room has a voice and contributes to the ultimate decision. That's no different to a portfolio management team at an asset manager that we're assessing. It's only by ensuring everyone at the table has a voice that is considered that we can ensure we are making the best possible decisions in order to progress against our agreed objectives.

Nicole Hartigan: We've always assessed the cultures of managers we evaluate, but we've increased scrutiny of this area and the need to measure elements that contribute to culture. We are also in the process of building out a more rigorous, repeatable framework for assessing and monitoring culture within our asset-manager research program.

The program revolves around eight principles that underpin a defined, repeatable process. They include areas such as inclusiveness and diversity, an embedded fairness and equality within businesses, and the desire and courage to disclose shortcomings and improve. With recent innovations, we're collecting a lot more data from managers on retention and diversity, which will enable us to track this through time and across managers.

In addition to desktop research of material provided by managers, our assessment involves multiple discussions with a range of staff over a long time. We then triangulate the evidence contained in available data with our observations in order to test consistency and authenticity. Most asset managers have a convincing corporate story, but it's only when we develop an understanding of the intricacies of culture that we can truly assess an organization's wellness.

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