Pensions&Investments

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CRAIN COMMUNICATIONS

ESG

BlackRock's proxy votes reveal a nuanced stance

Jeenah Moon/Bloomberg

Under fire over ESG, firm's investments and voting tell different story

By **ARLEEN JACOBIUS** and **CHRISTINE WILLIAMSON**

RELATED CONTENT

- DOL finalizes rule allowing ESG factors in retirement plans. **Page 2**
- Terrence Keeley urges investors to focus on direct investing. **Page 18**

BlackRock Inc. is being publicly eviscerated by some pension funds, other investors and politicians for its stance on environmental, social and governance factors. But a closer inspection of the world's largest manager's ESG investments, votes and internal practices show that they are not all that revolutionary.

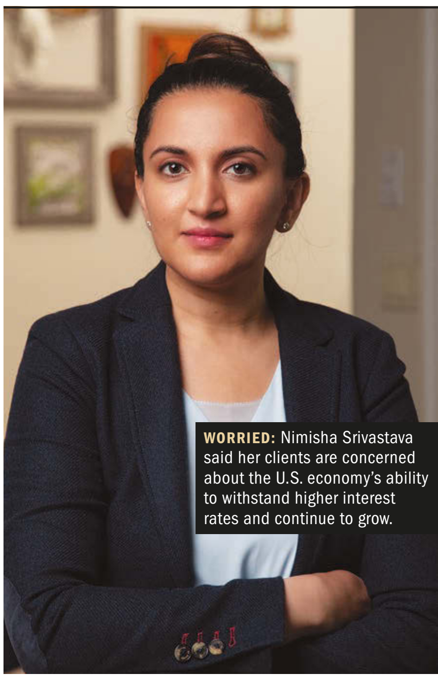
The firm in May 2021 committed to the Net Zero Asset Managers initiative, under which 77% of its assets under management would be aligned with net-zero by 2050 or sooner, up from 25% currently.

But the latest data show BlackRock voted in favor of climate change shareholder proposals fewer times than many of its rivals in the July 1, 2021, through June 30, 2022 proxy season.

And some of its ESG strategies, including its private capital energy transition funds, can still invest in fossil fuel companies.

"We expect to remain long-term investors in carbon-intensive com-

SEE **BLACKROCK** ON PAGE 26


Rick Hovis

WORRIED: Nimisha Srivastava said her clients are concerned about the U.S. economy's ability to withstand higher interest rates and continue to grow.

SPECIAL REPORT INVESTMENT CONSULTANTS

Consultants facing pressure as clients press for guidance

Volatile markets hurt some firms' AUA as they work to help clients navigate storm

By **PALASH GHOSH**

MORE ON INVESTMENT CONSULTANTS

- Greater scrutiny of ESG prompts caution. **Page 13**
- Economy not as bad as previous financial crises, experts say. **Page 15**
- Asset owners want more data about managers' diversity efforts. **Page 16**

Investment consultants have their work cut out for them as they advise and guide asset owner clients through an increasingly difficult investment climate — which in some cases also has dragged down their assets under advisement.

According to *P&I's* latest survey results, total institutional assets under advisement for investment consultants slipped 0.6% to $46.85 trillion as of June 30, compared to $47.14 trillion the previous year. Over the same period, U.S. institutional tax-exempt AUA rose slightly — 2.7% to $27.1 trillion.

Nimisha Srivastava, the Charlotte, N.C.-based North America head of investments at Willis Towers Watson PLC, said her clients are generally concerned about the U.S. economy's ability to withstand higher interest rates and continue to grow. They also are worried about the likelihood of a slowdown, or recession, which would have longer-term implications for economic growth and has the potential to impact both asset prices and volatility negatively. These factors, in turn, could result in asset owners not reaching their return or strategic objectives, she noted.

SEE **ASSETS** ON PAGE 16

Investing

FTX collapse not deterring pension funds about crypto

By **JOHN KIMELMAN**

RELATED CONTENT

- FTX crash draws more calls for crypto regulation. **Page 6**

The sudden collapse of global cryptocurrency exchange FTX has accelerated the yearlong downturn in bitcoin and other digital assets while igniting fresh concerns over the loosely regulated nature of the crypto industry.

But several public pension fund managers with modest crypto-related investments said they see no reason to give up on the sector.

"The washing out of weak players or inappropriate actors, while causing volatility and while admittedly stressful, is ultimately a healthy thing," said Andrew J. Spellar, chief investment officer of the $4.5 billion Fairfax County Employees' Retirement System, in an email.

And Ajit Singh, CIO of the $5.3 billion Houston Firefighters' Relief & Retirement Fund, points out that the crypto investment world has survived and even thrived in the wake of similar collapses arising from scandal and mismanagement.

"The current FTX fiasco is deja vu because in 2014 the largest crypto exchange,

SEE **CRYPTO** ON PAGE 28

Pension Funds

CalPERS boosts staff's investment authority, checks crypto

By **ARLEEN JACOBIUS**

The largest U.S. pension fund was busy at its November meeting, giving investment staff more leeway to invest in private assets.

Other items of note during its three days of meetings: CalPERS CEO Marcie Frost decried the politicization of ESG investing and also said the pension fund is examining its exposure to cryptocurrencies in its private equity portfolio.

CalPERS' investment committee on Nov. 14 changed its investment policy regarding staff investing in private assets, including an increase in the amount certain staff members can invest without board approval.

Nicole Musicco, chief investment officer for the $443.2 billion California Public Employees' Retirement System, Sacramento, said staff needed the changes so the investment team could be "set up to be agile" and responsive to market conditions. Staff wanted to "really make sure we have the appropriate tools in place to execute on the strategic asset allocation that we endeavored starting in July," she said.

Staff members are implementing its new asset allocation amid what she expects to be "continued rocky roads through the next 12 to 18 months," Ms. Musicco said.

SEE **CalPERS** ON PAGE 30

SOUND BITE

THRIFT BOARD'S **ELIZABETH PERRY** on engaging participants: 'We're all bombarded with information all the time, and part of the way that we figure out what to give our attention to is **what feels relevant to us**.' **Page 2**

Ultrashort bonds do well in difficult year

Ultrashort bonds rose to the top in rough year, while energy and natural resources equity outperformed. **PIonline.com/top-managers**

INVESTMENT CONSULTANTS

Greater ESG scrutiny prompts caution

Recent political skirmishes have many asset owners seeking more data to evaluate risks

By BAILEY McCANN

ESG continues to be top of mind for asset owners, but investment consultants say recent high-profile political skirmishes have many asset owners seeking more data to evaluate risks vs. potential rewards.

A growing number of states are putting environmental, social and governance investment practices under the microscope, with some states putting limits on how state pension plans can invest in ESG funds.

For example, the $8.2 billion Missouri State Employees' Retirement System in October pulled $500 million from funds managed by BlackRock Inc. over its approach to ESG investing. The concern, the retirement system said, was over BlackRock's public statements and record of prioritizing ESG initiatives over shareholder return.

But other state pension funds continue to move toward greater ESG information gathering and integration.

According to meeting minutes from Nov. 14, the $124.7 billion Minnesota State Board of Investment in fiscal year 2022 had its consultants and data providers conduct "portfolio-wide surveys to gather ESG information from managers with a particular focus on climate change risk management and diversity." The goal of these surveys, the board said, was to "establish a baseline so that the SBI can better monitor changes to its long-term risk exposures."

If it seems like the response to ESG is all over the board, it's because it is. Viewpoints about the utility of ESG strategies in investment portfolios fall across a wide continuum for both regulators and allocators, investment consultants said. BlackRock has emerged as something of an example of this continuum. Even as conservative states divest, New York City Comptroller Brad Lander, fiduciary for the $242.4 billion New York City Retirement Systems, recently wrote to BlackRock CEO Larry Fink pushing him to do more on ESG issues and said pension dollars could be at stake.

As a result, consultants that are tasked with tracking ESG investment strategies, frameworks and investment rules are facing heightened demands from investors for ESG education and information. They are also conducting their own surveys to track allocator sentiment and interest in ESG.

"ESG has become much more political," said Greg DeForrest, San Francisco-based senior vice president and manager of Callan's West Coast consulting team. "The politics are masking investment metrics and merits behind considering ESG factors when you look at investing in any category of investments or securities specifically."

Over the summer, Callan, which advised on $4.18 trillion in total U.S. institutional, tax-exempt assets as of June 30, according to *Pensions & Investments* data, conducted an ESG survey of 109 institutional investors including public and corporate retirement plans as well as foundations and endowments.

The survey pool was a mix of Callan clients and non-clients and their responses highlight the broad variance in how investors are thinking about ESG.

In a November webinar on the survey results, Thomas H. Shingler, a senior vice president and Callan's ESG practice leader, pointed to a decline in the number of institutional investors considering ESG.

Some 35% of respondents said they were considering ESG factors in their investment decisions, down from 49% in 2021. That decline likely reflects the additional scrutiny ESG strategies are under from regulators as well as pushback against the use of such strategies in pension fund portfolios, industry sources said.

The reasons given by respondents underline a growing divide among investors. For pension funds and other investors that do use ESG in investment decisions already, half of the respondents said they thought it aligned with fiduciary responsibility. For those that do not incorporate ESG, 47% said they thought that the benefits of ESG were unproven and unclear.

Rob Villanueva

DISTORTION: Callan's Greg DeForrest said ESG becoming more political is 'masking investment metrics and merits behind considering ESG factors' in any category.

Striking a balance

Matt Scott, Bristol, England-based senior strategic research consultant at Mercer Investments LLC, which advised on $4.94 trillion in total U.S. institutional, tax-exempt assets as of June 30, said that even if the rhetoric is making investors more cautious, they should be wary of focusing on it to the exclusion of effectively analyzing potential investments.

"People try to bring an element of the culture war to this discussion and many of them want to get caught up on terminology," he said. "But ESG factors have long been considered in some form because there is an investment opportunity and a business improvement opportunity. Solving the world's problems can be pretty profitable, but you have to strike the right balance."

Mercer recently published an investment outlook looking at how ESG might influence investment opportunities. Mr. Scott has been speaking with investors about issues like the global energy transition and highlighting where investment is still needed. He noted that there are areas of underinvestment like metals and mining companies that supply the components needed to run renewable energies such as solar and wind. "What we're talking

SEE ESG ON PAGE 16

Investment consultant statistics at a glance

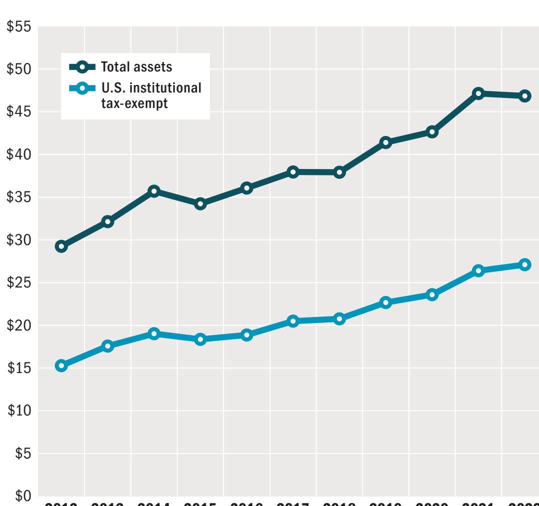
Assets are in millions as of June 30.

	2022 data	One-year change	Five-year change
Total assets under advisement	$50,086,264	-0.7%	30.7%
Institutional	$46,853,906	-0.6%	23.5%
U.S. institutional tax-exempt	$27,102,624	2.7%	32.2%
Assets under management	$1,040,350	-7.5%	31.5%
Number of minority- & women-owned consultants	3	50.0%	N/A
Number of consultants with a diverse-manager search policy	25	13.6%	N/A
Number of consultants providing advice on cryptocurrency	19	26.7%	N/A
Number of consultants offering cryptocurrency manager searches	13	-7.1%	N/A

Historical data may include retroactive updates.

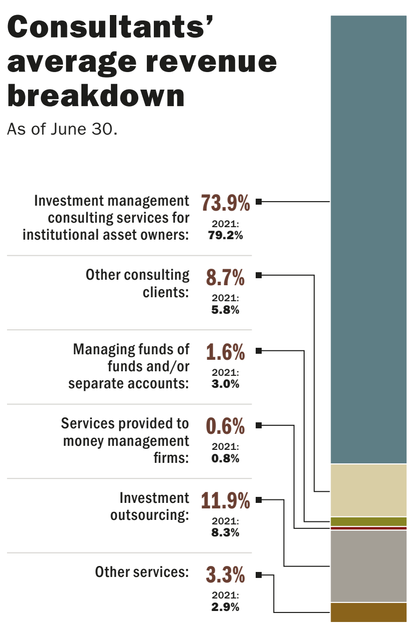
Growth of institutional advisory assets

Assets are in trillions as of June 30.



Consultants' average revenue breakdown

As of June 30.



The largest investment consultants

Ranked by worldwide institutional assets under advisement, in millions, as of June 30.

Rank	Consultant	Assets
1	Mercer	$16,452,259
2	Callan	$4,786,234
3	WTW Investment Services	$4,700,000
4	Aon	$3,798,070
5	RVK	$2,972,009
6	Meketa Investment Group	$2,801,821
7	NEPC	$1,523,957
8	Wilshire Advisors	$1,049,066
9	Russell Investments	$1,001,006
10	PPCmetrics	$785,000
11	CAPTRUST Financial	$718,215
12	Verus	$676,756
13	Rocaton Investment Advisors	$620,000
14	Morgan Stanley/Inst'l Cons.	$567,703
15	Bank of America	$462,904
16	NFRC	$460,194
17	StepStone Group	$451,509
18	Segal Marco Advisors	$381,847
19	Marquette Associates	$338,277
20	Cardinal Investment Advisors	$269,691
21	Fiducient Advisors*	$242,000
22	UBS Institutional Consulting	$165,973
23	SageView Advisory	$150,992
24	Asset Consulting Group	$141,000
25	Alan Biller and Associates	$133,663
26	Cliffwater	$110,369
27	LCG Associates	$102,208
28	AndCo Consulting	$89,695
29	Fund Evaluation Group	$69,880
30	Bellwether Consulting	$64,834
31	Gallagher Fiduciary	$62,988
32	CBIZ Investment Advisory	$62,130
33	Investment Performance	$59,707
34	Prime Buchholz	$58,673
35	Milliman	$51,048
36	IIC	$51,000
37	Portfolio Advisors	$38,290
38	Angeles Investment Advisors	$37,009
39	Concord Advisory Group	$31,290
40	George & Bell Consulting	$31,000
41	Innovest Portfolio Solutions	$30,927
42	Multnomah Group	$26,559
43	Capital Market Risk Advisors	$20,000
44	DeMarche	$19,410
45	Strategic Capital Investment	$18,530
46	Compass Financial	$17,189
47	Highland Consulting	$16,300
48	Dahab Associates	$15,400
49	Benefit Financial Services	$13,575
50	Newport Capital Group	$13,510
51	Asset Advisors	$12,000
52	Quan-Vest Consultants	$11,345
53	Francis Investment Counsel	$10,585
54	Canterbury Consulting	$9,989
55	PlanPilot	$8,117
56	Sellwood Consulting	$7,488
57	BilkeyKatz	$7,055
58	Conrad Siegel	$6,487
59	Bolton Partners	$6,186
60	Hamilton	$3,578
61	Vergence	$3,000
62	Pacific Portfolio	$2,698
63	Comperio Retirement	$1,700
64	Guidance Point Retirement	$1,550
65	Equitas Capital Advisors	$382
66	Benefit & Invest. Consulting	$79

*Data are as of Dec. 31

The largest consultants by total worldwide advisory assets

Assets are in millions as of June 30.

Rank	Consultant	Assets
1	Mercer	$16,452,259
2	Callan	$4,786,234
3	WTW Investment Services	$4,700,000
4	Aon	$3,798,070
5	Bank of America	$3,111,606
6	RVK	$2,972,009
7	Meketa Investment Group	$2,801,821
8	NEPC	$1,536,899
9	Wilshire Advisors	$1,295,405
10	Russell Investments	$1,001,006
11	PPCmetrics	$785,000
12	CAPTRUST Financial	$756,564
13	Verus	$676,756
14	Rocaton Investment Advisors	$620,000
15	Segal Marco Advisors	$569,549
16	Morgan Stanley/Inst'l Cons.	$567,703
17	NFRC	$460,194
18	StepStone Group	$451,880
19	Marquette Associates	$349,421
20	Cardinal Investment Advisors	$269,691

The largest consultants by U.S. institutional, tax-exempt advisory assets

Assets are in millions as of June 30.

Rank	Consultant	Assets
1	Mercer	$4,940,352
2	Callan	$4,182,436
3	Aon	$3,254,524
4	Meketa Investment Group	$2,798,491
5	RVK	$2,776,428
6	NEPC	$1,520,005
7	Wilshire Advisors	$1,044,323
8	Russell Investments	$775,603
9	WTW Investment Services	$741,253
10	Verus	$676,756
11	Rocaton Investment Advisors	$614,700
12	Morgan Stanley/Inst'l Cons.	$544,969
13	Segal Marco Advisors	$381,847
14	Marquette Associates	$338,038
15	CAPTRUST Financial	$302,177
16	Morgan Stanley/Inst'l Cons.	$567,703
17	NFRC	$460,194
18	StepStone Group	$451,880
19	Marquette Associates	$349,421
20	Cardinal Investment Advisors	$269,691

The largest consultants by managed assets

Assets in funds of funds or other discretionary money management products, in millions, as of June 30.

Rank	Consultant	Assets
1	Mercer	$345,746
2	Russell Investments	$299,200
3	StepStone Group	$136,537
4	Wilshire Advisors	$84,203
5	Morgan Stanley/Inst'l Cons.	$47,178
6	WTW Investment Services	$38,000
7	Aon	$32,600
8	Portfolio Advisors	$21,180
9	UBS Institutional Consulting	$8,810
10	Segal Marco Advisors	$8,478
11	Callan	$5,527
12	NEPC	$3,542
13	Angeles Investment Advisors	$3,410
14	CAPTRUST Financial	$2,736
15	Fund Evaluation Group	$1,037
16	Morgan Stanley/Inst'l Cons.	$567,703
17	NFRC	$460,194
18	StepStone Group	$451,880
19	Marquette Associates	$349,421
20	Cardinal Investment Advisors	$269,691

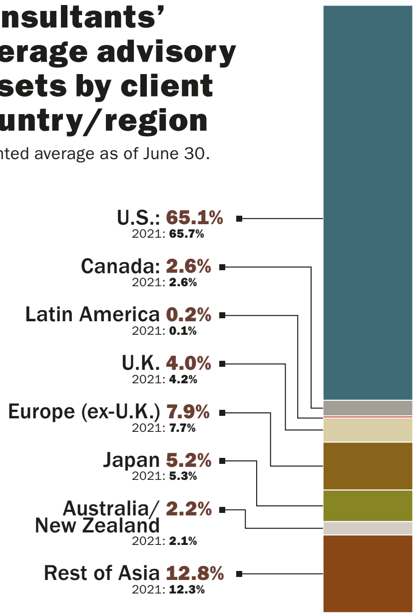
Consultants offering outsourced CIO services

As of June 30.

- Alan Biller and Associates
- AndCo Consulting
- Angeles Investment Advisors
- Aon
- Asset Advisors
- Asset Consulting Group
- Bank of America
- Callan
- Canterbury Consulting
- CAPTRUST Financial
- CBIZ Investment Advisory
- Cliffwater
- Compass Financial
- Conrad Siegel
- DeMarche
- Equitas Capital Advisors
- Fiducient Advisors
- Fund Evaluation Group
- Gallagher Fiduciary
- Investment Performance
- LCG Associates
- Marquette Associates
- Meketa Investment Group
- Mercer
- Milliman
- Morgan Stanley/Inst'l Cons.
- Multnomah Group
- NEPC
- Newport Capital Group
- NFRC
- PlanPilot
- Prime Buchholz
- Rocaton Investment Advisors
- Russell Investments
- Segal Marco Advisors
- Sellwood Consulting
- Strategic Capital Investment
- Verus
- Wilshire Advisors
- WTW Investment Services

Consultants' average advisory assets by client country/region

Weighted average as of June 30.



Consultants providing services to/collecting fees from money management firms

As of June 30.

- Callan
- DeMarche
- Mercer
- NEPC
- UBS Institutional Consulting
- Wilshire Advisors

Minority- & women-owned investment consultants

As of June 30.

- Benefit & Invest. Consulting
- Capital Market Risk Advisors
- RVK

Independent investment consultants

Consultants not providing services to/collecting fees from money management firms, as of June 30.

- Alan Biller and Associates
- AndCo Consulting
- Angeles Investment Advisors
- Aon
- Asset Advisors
- Asset Consulting Group
- Bank of America
- Bellwether Consulting
- Benefit & Invest. Consulting
- Benefit Financial Services
- BilkeyKatz
- Bolton Partners
- Canterbury Consulting
- Capital Market Risk Advisors
- CAPTRUST Financial
- Cardinal Investment Advisors
- CBIZ Investment Advisory
- Compass Financial
- Comperio Retirement
- Concord Advisory Group
- Conrad Siegel
- Dahab Associates
- Equitas Capital Advisors
- Fiducient Advisors
- Francis Investment Counsel
- Fund Evaluation Group
- Gallagher Fiduciary
- Guidance Point Retirement
- Hamilton
- Highland Consulting
- IIC
- Innovest Portfolio Solutions
- Investment Performance
- LCG Associates
- Marquette Associates
- Meketa Investment Group
- Milliman
- Morgan Stanley/Inst'l Cons.
- Multnomah Group
- Newport Capital Group
- NFRC
- Pacific Portfolio
- PlanPilot
- Portfolio Advisors
- PPCmetrics
- Prime Buchholz
- Quan-Vest Consultants
- Rocaton Investment Advisors
- Russell Investments
- RVK
- SageView Advisory
- Segal Marco Advisors
- Sellwood Consulting
- StepStone Group
- Strategic Capital Investment
- Vergence
- Verus

Diversity of investment consultants' U.S.-based employees

Average percentage of female and minority employees as of June 30.

Female

Total: 41.4% (2021: 39.3%)

Senior management: 25.4% (2021: 21.8%)

Investment: 24.0% (2021: 20.4%)

Minority

Total: 18.5% (2021: 17.7%)

Senior management: 9.3% (2021: 7.1%)

Investment: 13.6% (2021: 11.8%)

Investment consultants with a diverse-manager search policy

As of June 30. Data may include consultants with an informal policy.

- AndCo Consulting
- Angeles Investment Advisors
- Asset Consulting Group
- Bank of America
- Callan
- Canterbury Consulting
- CAPTRUST Financial
- Cardinal Investment Advisors
- Francis Investment Counsel
- Fund Evaluation Group
- Innovest Portfolio Solutions
- Marquette Associates
- Mercer
- Morgan Stanley/Inst'l Cons.
- NEPC
- PlanPilot
- Portfolio Advisors
- Prime Buchholz
- Rocaton Investment Advisors
- RVK
- Segal Marco Advisors
- StepStone Group
- Verus
- Wilshire Advisors
- WTW Investment Services

DIFFERENCES: Sue Crotty said inflation was far worse in the early 1980s, and this crisis doesn't have the systemic failure that 2008-2009 had.

Economy not as bad as previous financial crises, experts say

By PALASH GHOSH

Is the current economic climate worse than the market turmoil witnessed during the global financial crisis of 2008-2009 or the period of runaway inflation in the early 1980s?

While the landscape now looks dark for many asset owners and investors, Sue Crotty, New York-based senior vice president and chief investment officer at Segal Marco Advisors — who has been in the industry for 40 years — said she does not think conditions are the worst she has ever witnessed and is trying to impart that wisdom to her clients.

"We are definitely in a bear market now, and many investors and asset owners have never before experienced things like high interest rates and high inflation," Ms. Crotty said. "But I remember how bad inflation was in the (early) 1980s, worse than now."

Indeed, in January 1980, the annualized inflation rate was 13.9%, reached a peak of 14.8% in March of that year and remained well above 12% for the remainder of the year.

By comparison, inflation stood at 7.7% in October, down from 9.1% in June.

Ms. Crotty also tells her clients that the current crisis has a "different feel" from the global financial crisis of 2008-2009. "Back then, we witnessed dislocation and systemic failure in markets and the economy," she said. "That crisis was more comprehensive than what we are seeing today."

In that prior economic conflagration, the meltdown in the subprime mortgage market resulted in financial institutions getting stuck with trillions of dollars of almost worthless investments in subprime mortgages. Investment banking giants Lehman Brothers and Bear Stearns collapsed in the maelstrom.

Nimisha Srivastava, the Charlotte, N.C.-based North America head of investments at Willis Towers Watson PLC, concurred with Ms. Crotty that the global financial crisis was certainly worse than the current climate.

"While this year has been disappointing from a returns perspective, the sell-offs and poor returns from mainstream markets have been fairly orderly, notwithstanding some smaller segments of the market which have experienced heightened liquidity issues," Ms. Srivastava added.

However, Ms. Crotty warned that the current bear market won't be resolved anytime soon.

"This year has been a long slog, but we are advising clients to remain cautious and not panic," she said.

Ted Benedict, San Diego-based managing principal and consultant at Meketa Investment Group, concurred.

"While markets have been very volatile, the economic climate actually doesn't seem that bad," he said. "Demand is strong, the labor market is tight, and personal savings rates were solid coming out of the pandemic."

The uncertainty of the present climate is coming from "uncertain future inflation expectations and the future economic climate in a higher interest rate environment," he noted.

"The economic climate was worse in 2008, when you saw market liquidity evaporate, a weakened banking system, and a wave of bankruptcies," he added.

Assets

CONTINUED FROM PAGE 1

Clients have focused more recently on "where they will get their required returns from … what levers they can pull in this environment of tightening global financial conditions and negative skew of downside risks," she said.

Ms. Srivastava said the firm is a "strong proponent" of diversification.

"We continue to believe asset owners need to be evaluating additional types of strategies they can add to their portfolios to make them more resilient in times of uncertainty," she said. "We have seen particular focus on real assets and hedge fund strategies this year. Given market developments, we (also) are currently strongly advocating that asset owners add or increase their alternative credit allocations."

Alternative credit, with its high carry and low-duration characteristics, is a "strong play" in the fixed-income space, she said. "We believe it has the potential to deliver strong risk-adjusted returns from here," she added.

Ms. Srivastava also said: "Real assets exposure has benefited client portfolios by not only adding a diversified revenue stream but also inflationary protection as well. Private credit offers this as well, particularity given the floating rate nature of certain lending strategies."

Willis Towers Watson had worldwide institutional AUA of $4.7 trillion as of June 30, up 30.6% from June 30, 2021, making it the third-largest consultant in *P&I's* database. Ms. Srivastava attributed the increase in AUA to "a combination of growth and new client expansion" as well as client portfolio diversification.

Top macro issues

Rising inflation and climbing interest rates also are the top macro issues for Segal Marco Advisors' asset owner clients, said Sue Crotty, New York-based senior vice president and chief investment officer.

"These factors impact the entire portfolios of our clients," she said. "With the exception of certain real asset classes like real estate and infrastructure, almost all other assets are down double digits (this year)."

Year-to-date through Nov. 14, the Russell 3000 index was down 16.7%, while the Bloomberg U.S. Aggregate Bond index slumped 14.3%.

While stocks and bonds used to be negatively correlated in prior years, that relationship has evaporated this year in a scenario Ms. Crotty described as "unusual" and a "double whammy."

However, Ms. Crotty said she is advising her clients to stay cautious and conservative and try to ride it out.

"Remember two years ago when some investors were enamored with cryptocurrencies like bitcoin as the next wave of investing as a non-correlated asset class?" she pointed out. "And you see what's happened with crypto since."

Segal Marco Advisors reported worldwide institutional assets of $381.8 billion as of June 30, down 5.5% from the previous year. Ms. Crotty attributed the decline primarily to falling markets.

Liz Linder

NEW FACTORS: Meketa's Stephen P. McCourt cited rising inflation and interest rates as something new that is affecting forward-looking return expectations.

While Meketa Investment Group Inc. regularly reviews asset allocation policy with clients, "what is new this year is the impact of rising inflation and interest rates on forward-looking return expectations," said Stephen P. McCourt, San Diego-based managing principal and co-CEO at Meketa.

Mr. McCourt said in an email that he advises clients to adopt well-balanced, strategic asset allocation policies "intended to weather the market volatility and dynamics we have seen in 2022."

Meketa's institutional assets under advisement totaled $2.8 trillion as of June 30, up 4% from a year ago.

Re-examining fixed income

Thomas Toth, a Broomfield, Colo.-based managing director of Wilshire Advisors LLC, said while he had been advising clients to "shy away" from core fixed-income investments given low yields and asymmetric risks, he is now recommending that they re-evaluate that position in light of the rising interest-rate environment and higher expected returns for fixed income.

"We are more constructive on fixed income now," he said. "Fixed income has generally provided ballast and liquidity in a portfolio, and now we are having discussions with some of our clients, particularly institutional plan sponsors, about re-examining their fixed-income exposure."

Wilshire reported worldwide institutional assets under advisement of $1.05 trillion as of June 30, down 3.2% from a year prior.

Along with Mr. Toth, Segal Marco's Ms. Crotty is bullish on fixed income.

"Real returns from bonds are now very attractive," she said. "Fixed-income yields are now higher than they have been in decades."

Indeed, as of Nov. 14, investment-grade bonds were yielding about 4.78% to maturity, while high-yield bonds were yielding about 8.84%.

Once inflation falls, locking in these yields might be a good investment, especially for savers and retirees, she added.

Jay Love, Atlanta-based partner and U.S. investment leader at Mercer Investments LLC, agreed. "With these higher yields we are seeing, it makes some sense to move more into bonds, particularly those with longer liability durations," he said.

Mercer, the largest consultant in *P&I's* database, saw its worldwide institutional assets under advisement fall 5.2% to $16.45 trillion as of June 30, which Mr. Love largely attributed to market drops.

Higher interest rates have made forward-looking returns for bonds much better than they were only a year ago, acknowledged Greg Allen, San Francisco-based CEO and chief research officer at Callan LLC. "While our clients are just starting to absorb this into their long-term planning process, the initial reaction has been a recognition that they can now potentially meet their long-term return targets while taking less risk," he said.

But he said, "It's too early to tell whether this will result in a trend towards increasing fixed-income

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ESG

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about here is investing in technology improvements," he explained. "Metals and mining companies can help us capture and store these types of energy. That's important in an energy transition which is already happening. That's just a fact. It doesn't have to be some type of moral crusade."

Waiting and watching

Looking beyond the headline rhetoric, some of the decline in investment interest may be a result of allocators taking a wait-and-educate approach, consultants said.

Over recent administrations, views of ESG have varied widely with the Department of Labor under President Joe Biden pushing back on the Trump administration's approach to ESG before governors got in the mix.

Just this month, the DOL finalized a rule to explicitly permit retirement plan fiduciaries to consider climate change and other ESG factors when selecting investments and exercising shareholder rights. The rule was first proposed in October 2021 and is a reversal of two rules promulgated under the Trump administration.

Prior to the final rule's release Nov. 22, Mr. DeForrest said ERISA fiduciaries were eagerly awaiting the DOL's guidance on ESG and had been in a bit of a holding pattern until that guidance was available.

In the meantime, institutional investors have been continuing to educate themselves on the range of ESG strategies, ratings and frameworks that were available.

Steve Voss, Chicago-based senior partner and director of investments, North America at Aon PLC, said they are having more conversations with allocators about defining and refining ESG investment beliefs and approaches. The consultant advises on $3.25 trillion in U.S. institutional assets, according to the *P&I* survey.

"ESG is a complex issue regardless of whether you're running a defined benefit plan, defined contribution plan or are a not-for-profit foundation or endowment," Mr. Voss said. "ESG means a lot of different things. We spend time helping our clients understand the landscape as it relates to their particular interests."

In October, Aon brought on Daniel Ingram as a partner and head of responsible investing to continue to advance Aon's ESG offerings. Mr. Voss said that Mr. Ingram will be helping with improvements to the firm's dual-pronged ESG approach. Aon already considers ESG as part of its investment manager research efforts, looking at how ESG impacts investment strategy for a given manager. The other prong involves looking at how ESG is incorporated or can be incorporated into investor portfolios.

Ahead of the final rule's release, Mr. Voss said the firm would be discussing the new guidance with its clients and would be "using those updates to inform how ESG might be incorporated in ERISA portfolios."

He also predicted that the DOL's guidance was unlikely to mean a significant shift in allocation strategies right out of the gate.

"We think it's going to be a months and years, not a weeks and months approach to ESG investing across all investor types," Mr. Voss said. "The specific guidance while important isn't the only consideration, fiduciaries have to consider what is best for plan participants overall and as a result those plans tend to take a very measured approach to making changes."

Mr. Voss added that the months-and-years approach is likely also true for large state plans. "Public funds, just like ERISA funds, have to take into consideration the best interest of their participants absent what legislative action does or doesn't ultimately do. So we are seeing a lot of states take a wait-and-see approach," he said. ■

Brian Croce contributed to this story.

Asset owners requesting more information about managers' various diversity efforts

As asset owners grapple with ESG considerations, they're also weighing diversity among their managers and how that affects performance, an institutional consultant said.

"Our research into diversity has shown that investment teams with greater diversity have outperformed those that are less diverse over time," said Nimisha Srivastava, the Charlotte, N.C.-based North America head of investments at Willis Towers Watson PLC, which advises on $4.7 trillion in worldwide institutional assets, according to *P&I* data.

"We work with clients to measure the diversity in their manager portfolios, then helping them manage this over time. This could be measuring progress, achieving target objectives, identifying new additions or engaging with existing managers to evolve."

With respect to diversity, Stephen P. McCourt, San Diego-based managing principal and co-CEO at Meketa Investment Group, said that many of his clients are "interested in the diversity of their vendor's staff, and the DEI policies and practices their vendors implement."

Meketa, he added, "surveys the asset manager marketplace annually to collect information on diversity and related practices and provide our clients with this information." Meketa advised on $2.8 trillion in worldwide institutional assets as of June 30.

In fact, Wilshire Advisors just released a report showing that the total number of mandates awarded to diverse-owned firms doubled to 21% in 2021 from 10% in 2018, while the inclusion rate of diverse-owned firms in manager searches increased in 2021 to 56% of all searches after remaining stable at just under one-half of all searches from 2018-2020.

"We believe that diversity in all its forms leads to better business outcomes, and we're committed to diversity, equity and inclusion both in our workplace and in the asset manager searches we conduct for our clients," said Jason Schwarz, president of Wilshire, in a Nov. 2 news release.

Wilshire's report also showed that from 2018-2021, the percentage of Wilshire clients investing with diverse-owned firms grew to 39% from 20%.

Added Joanna Bewick, senior vice president and portfolio manager at Wilshire: "Broadening the investment manager opportunity set is not only beneficial in principle, but diversity also maximizes the talent pool and increases the likelihood of capitalizing on investment opportunities in an increasingly global and diverse world. The investment consulting industry has a duty to improve equity and inclusion for diverse managers."

Wilshire advised on $1.05 trillion in worldwide institutional assets as of June 30.

— PALASH GHOSH

ESG

Ex-BlackRock exec: Jettison ESG for direct investing

Terrence Keeley urges investors to adopt impact strategies that truly earn a profit and do good

By ERIN ARVEDLUND

Why should institutional investors at pension funds, endowments and foundations read Terrence Keeley's new book?

To hear out Mr. Keeley's revolutionary idea: If asset owners reallocate just 1.6%, or about $3.5 trillion, of $220 trillion in capital annually, the United Nations Sustainable Development Goals could be achieved easily. That is the total amount of investible assets, whether private or public, equities or fixed income, held by institutions and ultra-high-net-worth investors.

By scrapping traditional ESG index funds, pensions and other institutional funds could invest in impact strategies that truly earn a profit and do good. The former BlackRock Inc. executive said in an interview that he has officially "moved on from the ESG industrial complex." Instead, he advocates investing directly in waste reduction, helping the underserved, skills training, health care, affordable housing, renewable energy and education.

"Even thoughtful investors are questioning what impact current ESG offerings are actually having. It's leading to cynicism," he said.

He points to another way: the 1.6% solution (more on that below).

Mr. Keeley's views carry weight after years of working with BlackRock's institutional investors as a managing director until 2021; he worked closely with founder Larry Fink, who penned the foreword to "Sustainable: Moving Beyond ESG to Impact Investing."

ESG-integrated investments already encompass more than $120 trillion in financial assets, based on United Nations Principles for Responsible Investment figures. But those assets "aren't doing well or doing good," Mr. Keeley said.

Essentially, ESG is fatally flawed, he said. For one thing, he opposes divesting from or excluding oil and gas and other emitters from portfolios. "Investments have consequences. And to the extent you want to have a positive impact on the environment, that means investing, not divesting," Mr. Keeley said. "The divestment argument needs to go away. Let's examine ESG more deeply."

Second, he said, ESG in its current form "is not living up to its promise. The understanding people have when they buy an ESG product is that it will perform at or in excess of the market, while simultaneously doing some kind of good."

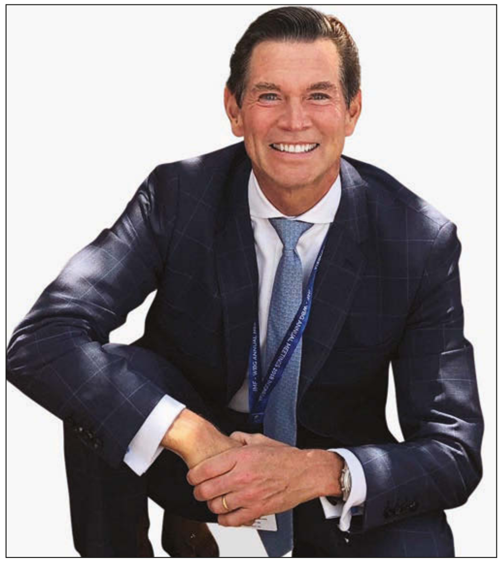
Instead, MSCI Inc., S&P and Bloomberg ESG indexes "have underperformed the broader indexes," over the past five years, he said. And "we need more rigorous ways of measuring impact and risk-adjusted returns."

Moreover, "your temperature-aligned funds (in institutional plans) aren't helping to lower the earth's temperature. Those invest only in companies in accordance with the Paris 2050 objective, like Amazon or Google. There's no causality in buying those funds and the world becoming temperature aligned."

Moreover, "I don't recommend buying dirty companies. But divesting from oil and gas isn't going to cut it. We don't have an oil and gas crisis, we have a net emissions crisis."

He points to Occidental Petroleum Corp. as a leader in the oil and gas industry, which has built one of the largest carbon capture facilities currently operating under CEO Vicki Holub.

"We have to start over. We need more inclusive, sustainable growth strategies," like those of Jim Sorensen of the Sorenson Impact Foundation in Salt Lake City, he said.



A DIFFERENT APPROACH: Terrence Keeley said investors questioning the impact of current ESG offerings has led to cynicism.

The 1.6% solution

Mr. Keeley's recommendation is for investors to reallocate assets into the direct impact investing world, and step away from the mishmash of E, S and G.

"These are all genuine concerns, but the way we're going about it, combining those and building alpha-based products is senseless."

Mr. Keeley recommends reallocating capital toward an emerging class of strategies with more verifiable social and environmental benefits.

Insurance companies, sovereign wealth funds, central banks, pension funds and ultra-high-net-worth investors can also step up buying green bonds and other real assets such as energy-efficient properties, he said.

For example, Ford Motor Co.'s plant producing the electric F-150 trucks was financed using green bonds, he noted. ExxonMobil also has issued green bonds, Mr. Keeley said.

He personally owns BlackRock's Pext/Next funds — one is a pure fixed-income fund and the second is a multiasset fund. Those funds are the BGF ESG Fixed Income Global Opportunities Fund and the BGF Sustainable Global Allocation Fund.

These types of funds that overweight in securities classified as having positive externalities (Pext) and avoid those with negative externalities (Next).

In his foreword for Mr. Keeley's book, Mr. Fink wrote: "Our job at BlackRock is to offer our clients (who are the actual owners of the assets we manage) a range of choices they can select from to achieve their unique financial objectives. Some choose sustainable investing options, others don't. The choice is theirs. In recent years, the number of clients looking to incorporate sustainability into their portfolios has continued to grow, but, at the same time, so have the critics of sustainable investing. It has sparked a lively debate. It's a debate I welcome."

In the foreword, however, Mr. Fink demurred on whether BlackRock would embrace Mr. Keeley's 1.6% solution.

"In his conclusion, he offers a provocative solution … for assets owners to consider as they construct their portfolios. I don't agree with all of the opinions or conclusions in Terry's book, but I welcome his contribution, and that of many others, to this critical dialogue." ■

Assets

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allocations in long-term strategic targets."

Callan, the second-largest consulting firm in *P&I's* ranking, saw its assets under advisement jump to $4.79 trillion as of June 30, up 48.76% from a year ago, which Mr. Allen attributed in an email to "gaining a small number of very large plans as clients."

He cautioned, however, that "investment consultants who work with very large plans on both a retainer basis as well as a project basis tend to have these year-over-year AUA fluctuations."

The firm declined to identify its new clients. However, *P&I* reported last October that the Federal Retirement Thrift Investment Board, Washington, which administers the $743 billion Thrift Savings Plan, hired Callan, along with four other firms, to assist the board in several areas, including investment policy evaluation and design, portfolio governance and portfolio manager evaluation, investment option review and evaluation, investment manager search, and more.

Return to 60/40?

Segal Marco's Ms. Crotty thinks the traditional 60/40 asset allocation could even come back.

"The 60/40 portfolio has not really existed in years given how much money has been flowing into alternative assets," she said. "But now I see an increasingly challenging environment for asset flows into alternatives in the coming years given that clients are already overweight to targets. As such, we might see a rotation back to traditional equities and fixed-income securities."

Wilshire's Mr. Toth said that as many of his clients, including both public and private pension funds, have increased their allocations to non-traditional asset classes like private markets, he worries that these positions might now represent an overweight in some portfolios.

"Although we think private assets are a valuable part of an investment portfolio, we are cognizant of the risk of being overallocated relative to private asset targets given the 'denominator effect,' and are helping clients manage around the risk," he said.

That risk can be managed, Mr. Toth explained, by "updating commitment pacing schedules for private equity, credit and real asset portfolios to align with lower total fund market values." However, he added, "We are not recommending dramatic reductions in commitments to avoid a 'stop-start' approach to making commitments and want to take advantage of opportunities offered by the market volatility."

With the Fed expected to cease its program of rate hikes sometime next year (as long as inflation numbers come down meaningfully), Mr. Toth also said that there may be a light at the end of the tunnel out of the current crisis.

"Historically, markets begin to rally when the underlying economic conditions are still relatively poor and this is something we want our clients to be aware of," he said. "On this basis, we suggest that they continue to actively rebalance portfolios and look for opportunities to judiciously add risk in preparation for market upturns."

Mr. Toth noted that this could be done by tilting more toward global equity, for example, or by moving into small-cap equity or making additional allocations to below investment-grade credit.

OCIO trends

Demand for OCIO services has increased due in part to market weakness and volatility as well as the ever-increasing complexity of investible securities, according to Mercer's Mr. Love, noting, however, that he wouldn't classify the rise in demand as "huge."

"While we haven't seen a huge spike in demand, we've had more discussions with clients over how to maneuver in this climate," he said.

In *P&I's* consulting survey, Mercer reported $345.75 billion in managed assets as of June 30, down 12% from the previous year.

Callan's Mr. Allen said demand for OCIO services has been "pretty steady" for the last few years. "The most notable change would be an increase in the number of replacement opportunities, where a client made the decision five to seven years ago to adopt this model and are now going back out to the market to consider changing their provider," he said. "Another change we've noticed is that there seems to be more opportunities this year where the process is being run by a third-party search firm rather than directly by the client. This reflects the complexity involved in making these decisions."

Mr. Allen also observed that "many times we are being asked to bid on the relationship on both a discretionary and non-discretionary basis. It seems that in these cases clients are using the RFP process to evaluate the relative merits of the two governance models."

Callan reported $5.53 billion in managed assets as of June 30, up 2% from the year-earlier period. ■

Corrected index managers graphic:

Growth of index assets

Assets managed internally, including passive and enhanced strategies, in trillions, as of June 30.