



KNIGHT
FOUNDATION

DIVERSIFYING INVESTMENTS

A STUDY OF OWNERSHIP DIVERSITY IN THE ASSET MANAGEMENT INDUSTRY

Executive Report
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I. INTRODUCTION AND BACKGROUND

Introduction

Research across a multitude of fields and industries has identified the potential economic and social benefits of diversity. Yet, the asset management industry continues to face challenges with a lack of diversity. Research studies and articles have consistently documented the low level of representation by women and racial/ethnic minorities among asset managers. Analyzing and exploring diversity in the asset management industry is vital given its sheer enormity and the wealth it generates (\$71.4 trillion in assets under management and \$100 billion in profits in 2015).

This report captures insights from a new study about the state of diversity in the U.S. asset management industry. Professor Josh Lerner (Harvard Business School) and Bella Research Group led the research. Whereas numerous studies have documented the lack of diversity among asset managers and asset management firm employees, this study contributes a new perspective by analyzing the diversity of ownership of asset management firms.

The research was commissioned by the John S. and James L. Knight Foundation, a private grantmaking foundation. Beginning in 2010, Knight Foundation embarked on an effort to diversify its endowment holdings and now invests \$472 million with diverse-owned firms (representing 22.5 percent of endowment holdings). Knight supported this study to inform the larger discussion unfolding about diversity in the asset management industry.

Research

The research addressed the following key questions:

- What is the number of women-owned and minority-owned firms and funds as well as the amount of assets under management (AUM)?
- How have diverse-owned firms and funds performed compared with all firms?
- How has diverse ownership trended?
- How have different types of investors engaged with diverse-owned firms?

While prior research has examined diversity in each of these asset classes at the level of fund managers, this research takes a different look at diversity at the level of firm ownership. Women- and minority-owned firms were



identified among the universe of asset management firms, though the definition for diverse ownership varies slightly across the data sources. Firms are commonly considered women-owned or minority-owned if at least 25 percent of firm ownership is held by female or minority individuals. While the report uses this definition, it also distinguishes between substantial diverse ownership (25 to 49 percent) and majority diverse ownership (50 percent and higher) where the data permits.

This research encompasses four asset classes: (1) mutual funds, (2) hedge funds, (3) private equity and (4) real estate. Addressing the questions required developing a suitable methodology for gathering and analyzing data. This report utilized several robust databases capturing information about asset management firms, and then ran a series of “stress tests” on the data to assess the impact of various gaps. Yet, there are clear limitations to the data that should be noted. Firstly, there is no single database across asset classes with authoritative or complete data on diverse ownership. Compounding this, the databases use different criteria for “ownership.” Thus, several firms will have invariably been left out of this analysis or their degree of diverse ownership may be imperfectly defined in the analysis.

Readers are encouraged to learn more about the methodology, data sources and limitations in the Appendix.

Key Findings

1. **COMPOSITION:** Firms with female or minority ownership make up a low percentage of all firms in the asset management industry. These diverse-owned firms represent an even smaller fraction of the total number of funds and total AUM across all asset classes.
2. **PERFORMANCE:** Diverse-owned funds perform at a level comparable to that of their non-diverse peers. Within conventional statistical confidence levels, funds managed by diverse-owned firms typically perform as well as non-diverse funds after controlling for relevant characteristics (such as firm size, fund size, geography and investment focus).
3. **TRENDS:** Representation of diverse-owned firms has increased modestly in recent years among hedge funds, private equity and real estate. However, AUM with diverse-owned firms has fluctuated significantly year-to-year.
4. **DATA:** The biggest barrier to research on diverse ownership or management is the lack of data, as most data providers for the asset management industry do not track diversity in a systematic way. The report relies on the most comprehensive data sources available, but to encourage further research on this topic, improved data on the composition of firm ownership and management is required.

For the full report and set of findings, click [here](#).



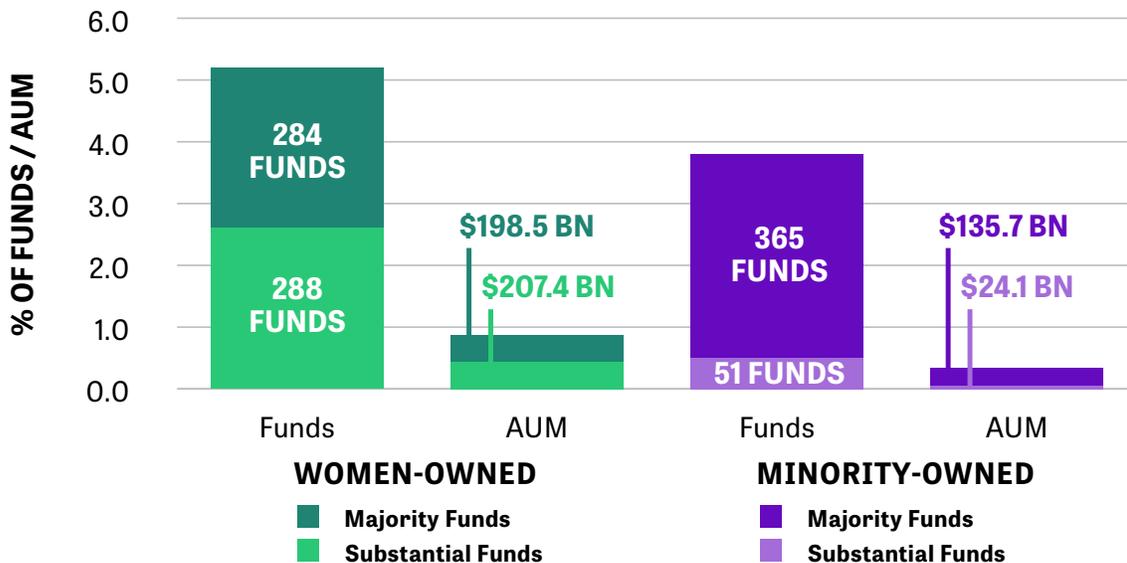
II. CURRENT STATE OF DIVERSE OWNERSHIP

In the asset management industry, firms owned by women or minorities represent a small fraction of the total number of firms, total number of funds, and total AUM. Aggregating across the four asset classes studied, diverse-owned firms represent just 1.1 percent of AUM. Findings for each asset class and summarized below.

Mutual Funds

The research identified 127 women-owned and 107 minority-owned firms as of Q2 2016, managing 572 and 416 mutual funds, respectively. Women- and minority-owned mutual funds represent just 5.2 percent and 3.8 percent of all mutual funds, respectively.

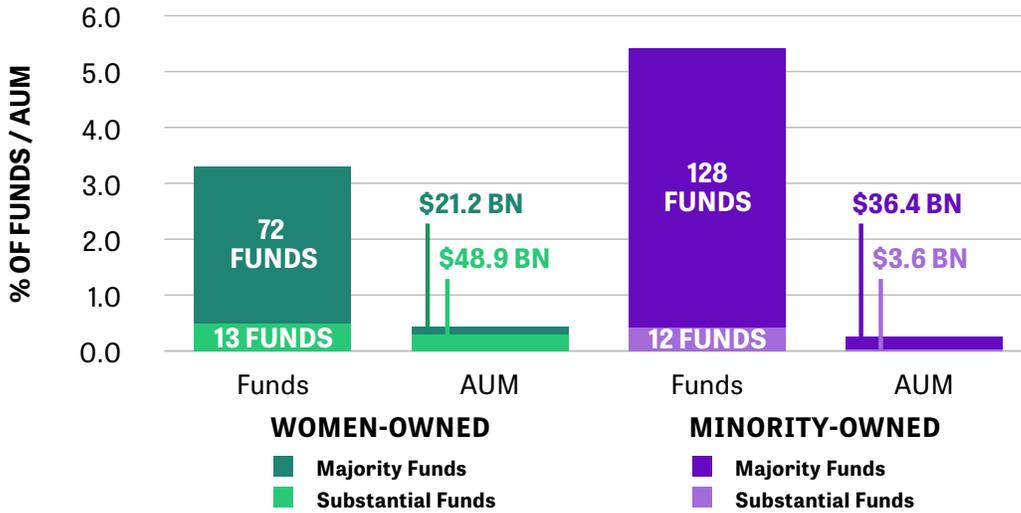
The women-owned mutual funds comprise 288 funds with substantial female ownership (25 to 49 percent) and 284 funds with majority female ownership (50 percent and higher). Together, these women-owned funds manage \$405.9 billion in AUM, accounting for less than 1 percent of the total industry AUM. Similarly, minority mutual funds comprise 51 funds with substantial minority ownership and 365 funds with majority-minority ownership (that is, 50-plus percent minority ownership); all together, minority-owned mutual funds manage less than 0.5 percent of the industry AUM.





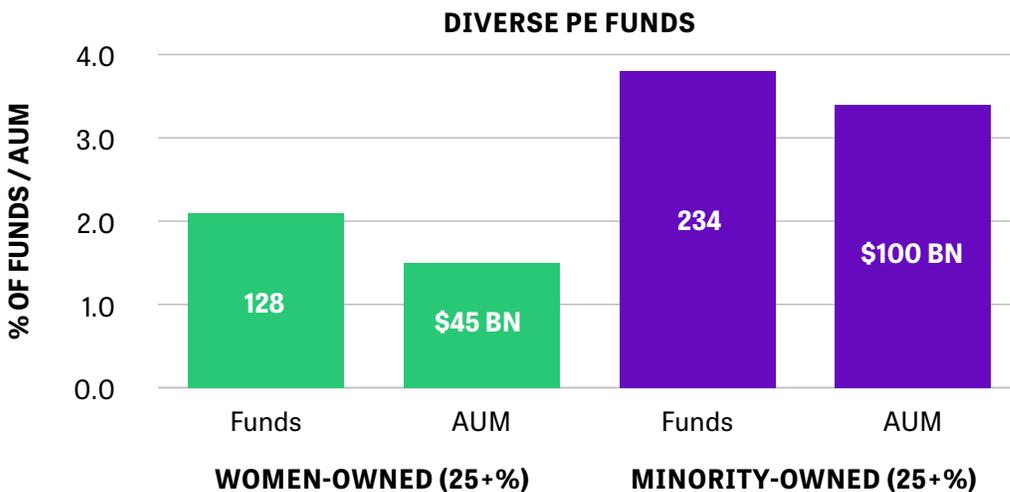
Hedge Funds

As of mid-2016, hedge funds managed by women- and minority-owned firms represent about 3.3 percent and 5.5 percent of all hedge funds, respectively. Most of the identified diverse hedge funds are managed by firms with 51 percent or more female or minority ownership. Together, women- and minority-owned hedge funds control less than 1 percent of the total industry AUM.



Private Equity

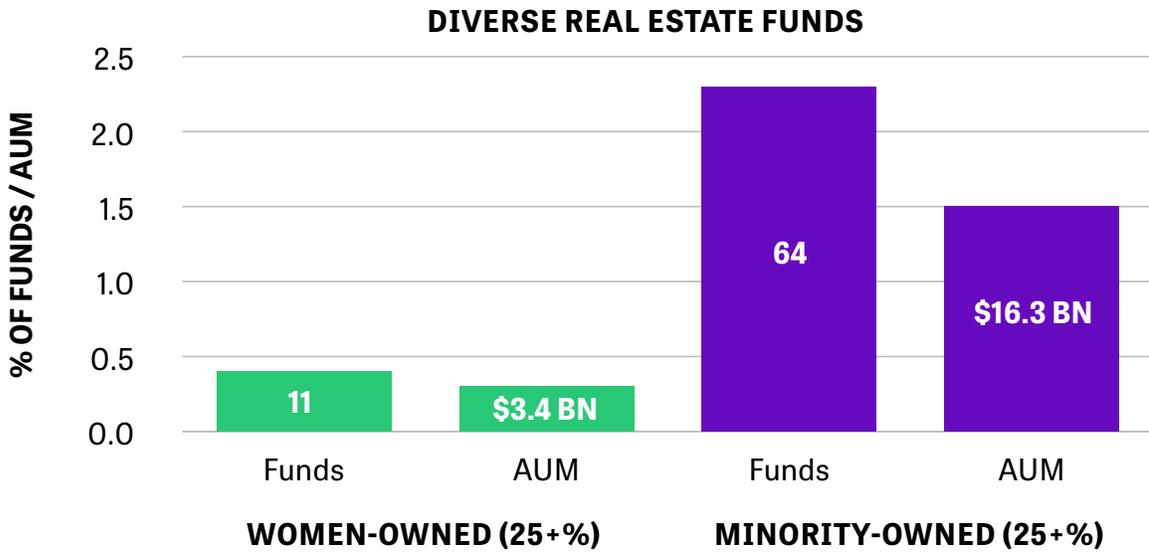
Among active private equity funds (established since the beginning of 2004), the research identified 128 funds managed by women-owned firms and 234 funds managed by minority-owned firms, making no distinction between substantial ownership (25 to 49 percent) and majority ownership (50-plus percent) because of data constraints. These firms represent less than 6 percent of the total fund count and control less than 5 percent of AUM in the private equity industry.





Real Estate

The research identified 11 women-owned funds and 64 minority-owned funds among the universe of real estate funds in Preqin (established since the beginning of 2004). Together, this represents less than 3 percent of all real estate funds. Representation by AUM is even lower, with women and minorities representing about 0.3 percent and 1.5 percent of the industry totals, respectively.





III. PERFORMANCE OF DIVERSE-OWNED FIRMS

Within conventional statistical confidence levels, funds managed by diverse-owned firms typically perform as well as non-diverse funds, after controlling for relevant firm- and fund-level characteristics (firm size, fund size, geography, investment focus, etc.).

The research used several regression models to test performance, and the vast majority of regression coefficients for female and minority ownership are insignificant (that is, there is no discernible difference between the performance of diverse and non-diverse funds). In a few select cases, diverse-owned firms either outperformed or underperformed non-diverse firms.

The research also analyzed the distribution of performance and the extent to which diverse-owned firms comprise the top performance quartile across asset classes (i.e., what percentage of women- and minority-owned funds performed in the top 25 percent?). Among mutual funds and hedge funds, about a quarter or slightly more of minority-owned funds are represented in the top quartile of performance.

In private equity, women-owned firms are overrepresented among top quartile performers while minority-owned firms are underrepresented among top performers.

TOP QUARTILE PERFORMERS

ASSET CLASS	Women-Owned	Minority-Owned
Mutual Funds	25.2 %	28.4 %
Hedge Funds	24.4 %	27.8 %
Private Equity	33.3 %	19.8 %

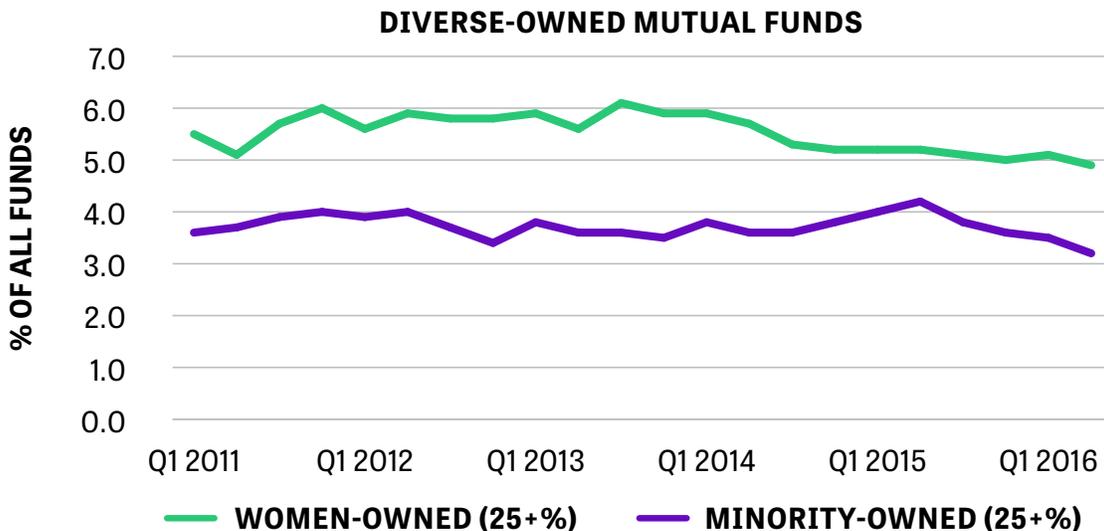


IV. TRENDS IN DIVERSE OWNERSHIP

In recent years, representation of diverse ownership has generally increased in terms of the number of diverse firms and funds as well as the amount of AUM. Yet diverse firms still represent a small fraction of the total asset management industry. Trends over time are described for each asset class, using the number of funds as the measure of diverse ownership. Additional details and figures that chart the timeline trends for firms and AUM are available in the full report.

Mutual Funds

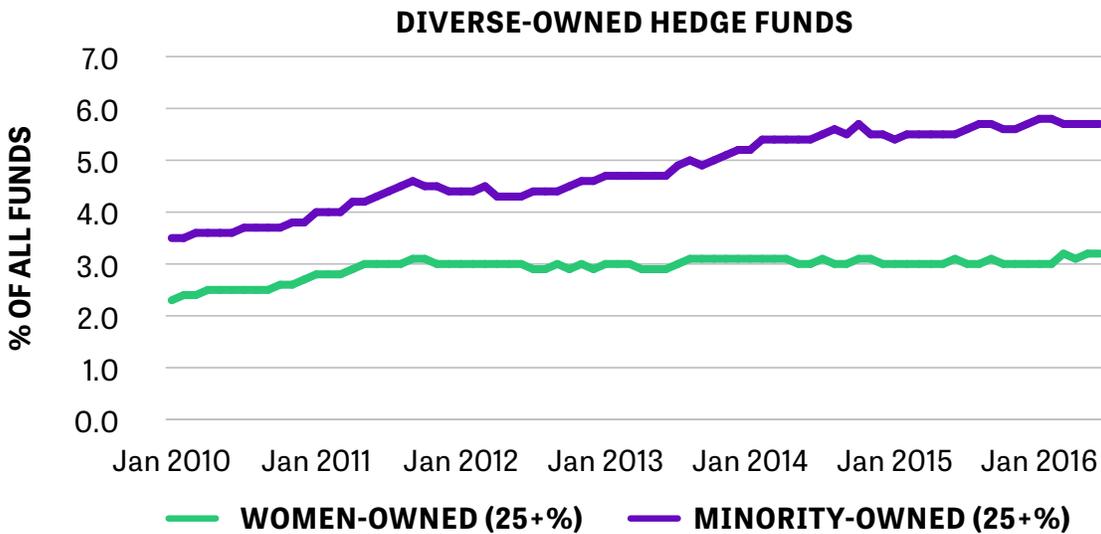
We do not observe any distinct upward or downward trends in the representation of diverse mutual funds since 2011. However, the net change between Q1 2011 and Q2 2016 shows a slight decrease in diverse ownership (5.5 percent to 4.9 percent for women-owned funds; 3.6 percent to 3.2 percent for minority-owned funds).





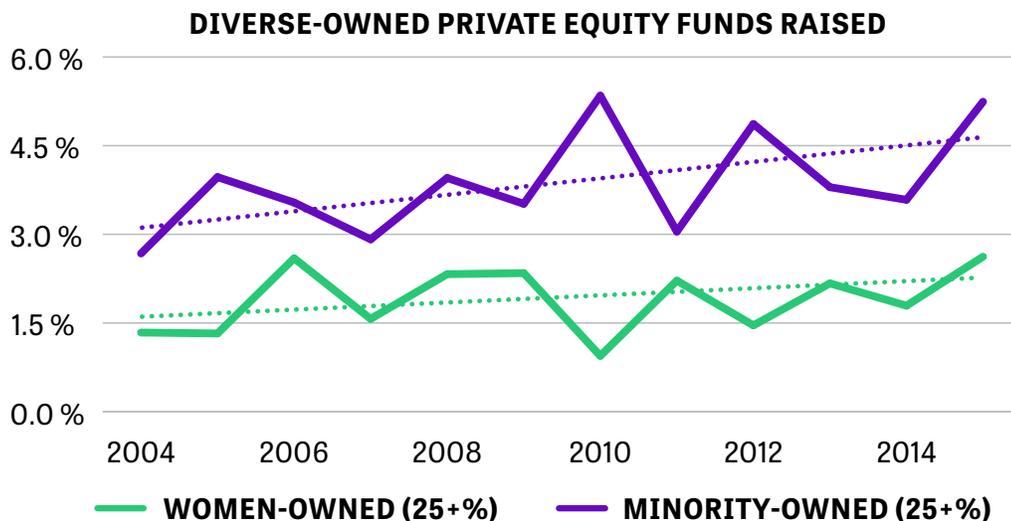
Hedge Funds

Since 2010, women- and minority-owned hedge funds have gained representation, but these hedge funds represent a tiny fraction of the industry.



Private Equity

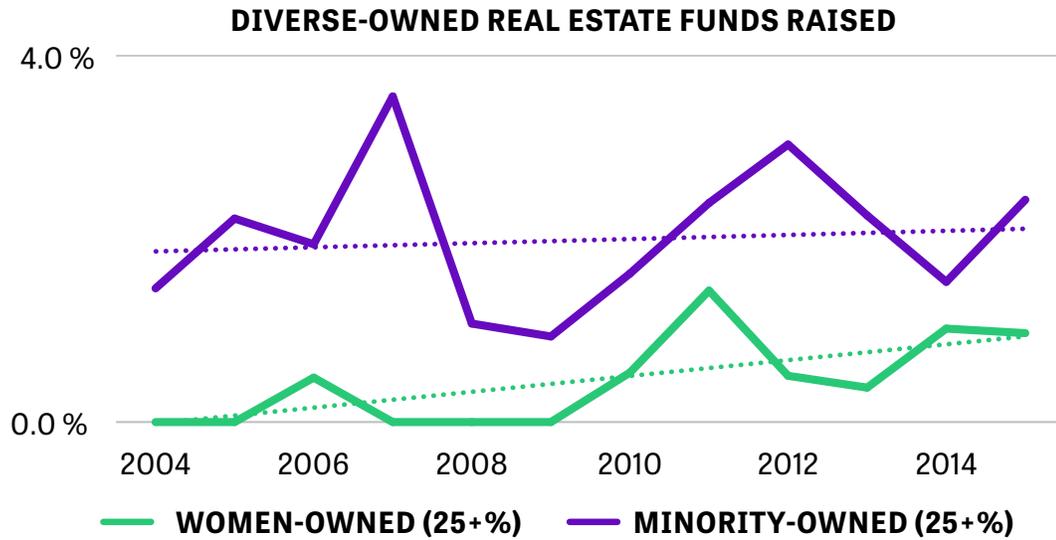
There is some evidence of an increase in the representation of women- and minority-owned private equity funds since 2004, in terms of the number of funds raised and the amount of fundraising dollars. However, since these figures represent the number of new funds every year and not the number of active funds each year, the data have fluctuated considerably year-to-year.





Real Estate

Despite significant fluctuations in the data, there is evidence of an increase in the representation of diverse-owned real estate funds. As with private equity, the data represent the number of new real estate funds each year, not the total number of active funds each year. Therefore, there is substantial fluctuation year-to-year in the representation of funds with diverse ownership.





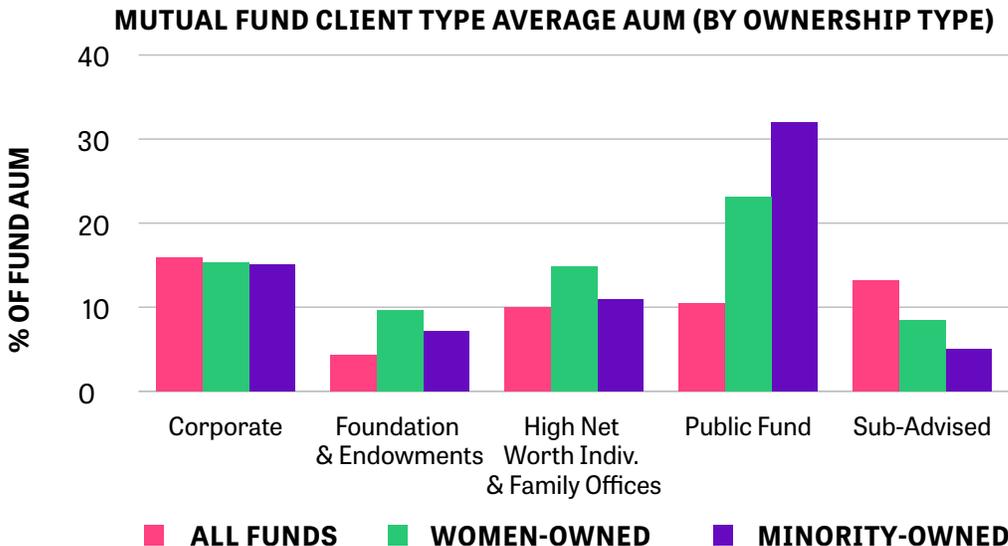
V. INSTITUTIONAL INVESTOR TYPES FOR DIVERSE-OWNED FIRMS

Finally, the research analyzed the mix of institutional investor types that invest with diverse mutual funds and private equity firms. The mutual fund analysis utilized data on the AUM invested by different institutional investor types; the private equity analysis utilized data on the number of limited partners by type. The available hedge fund data do not have information on investors, and the sample of diverse real estate investment funds is too small for a meaningful treatment of this topic.

Overall, public funds appear to be better represented among diverse funds compared with non-diverse funds, for both the mutual fund and private equity industries. In addition, foundations and endowments are well-represented in diverse mutual funds but are underrepresented in diverse private equity funds.

Mutual Funds

The research examined the mix of institutional investor types and the AUM they invest with diverse and non-diverse mutual funds based on the most recent data from Q2 2016. The average women- or minority-owned fund has proportionally more AUM invested by public funds, foundations, endowments, high net worth individuals and family offices (compared with non-diverse funds). Investments from corporate clients and sub-advised funds make up a larger proportion of the AUM with non-diverse funds.

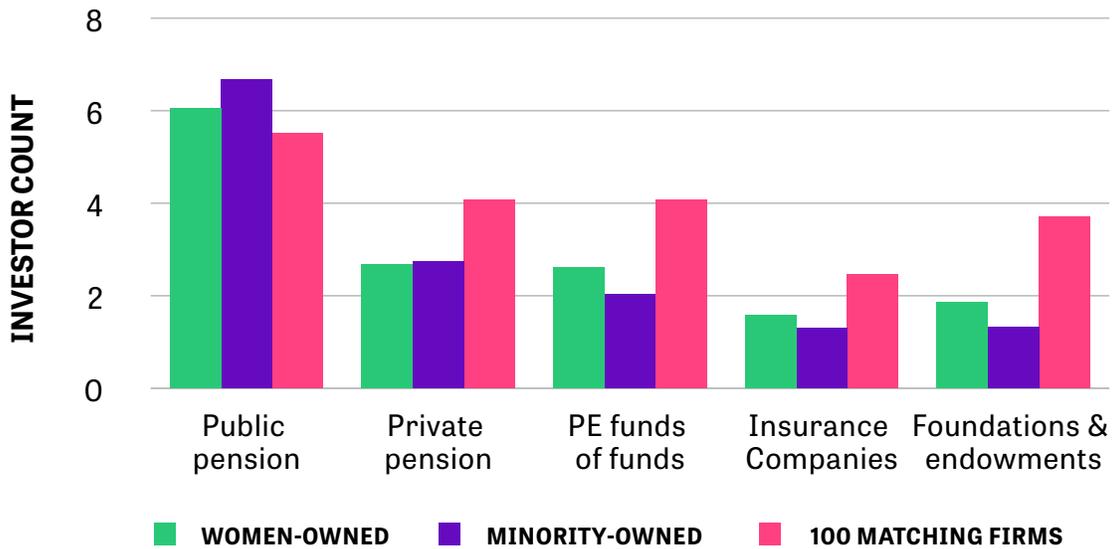




Private Equity

The research examined the representation of LP types that invest in diverse-owned private equity firms compared with their representation in a random sample of private equity firms from Preqin.¹ These data show the representation in terms of the number of LPs, not in terms of AUM, because such data are not available. Among the most substantial differences, foundations and endowments represent a smaller proportion of the investors in women- and minority-owned firms, and public pensions make up a larger fraction of the investors in minority-owned firms, on average.

PRIVATE EQUITY INSTITUTIONAL INVESTOR COUNT (BY FUND TYPE)



¹ We randomly sampled 100 firms that have at least one fund meeting the criteria for inclusion: (1) based in U.S., (2) not a private equity fund-of-funds and (3) vintage year 2004 or later.



VI. CONCLUSION

The study sheds light into just how little diversity there is in ownership of asset management firms. Aggregating across all four asset classes examined in this report, diverse-owned firms represent just 1.1 percent of industry AUM. While diverse-owned firms have grown in representation in recent years, the growth has been moderate and has not uniformly occurred across all asset classes.

An important finding of the research is that there is no statistical difference in performance between diverse-owned firms and their peers. A common refrain has stated that poor performance among diverse-owned firms has precluded their receipt of greater investment; the findings of this study cast doubt on this assertion.

Quantifying the performance of diverse funds and the current level of diverse ownership is an initial step to understanding and encouraging diversity in asset management. We hope to increase awareness and knowledge of this important topic and encourage enhanced data reporting in the future.

The report is intended to serve as a foundation for future inquiry and more robust data collection about diversity in the asset management industry. Creating a public, nonproprietary database with this information should be a top priority for the institutional investment community.

Gathering, analyzing and discussing better information about diversity in the asset management industry is critical to advancing progress.

The study was commissioned by the John S. and James L. Knight Foundation and led by Josh Lerner, Chair of the Entrepreneurial Management Unit and the Jacob H. Schiff Professor at Harvard Business School, and the Bella Research Group.



APPENDIX: RESEARCH METHODOLOGY

This note provides a summary of the methodology developed by Bella Research Group for the analysis of asset management firm ownership diversity. The full report contains a more detailed description of the methodology.

Definitions

The research uses the term “diverse-owned” to refer more broadly to the group of firms owned by women and/or minorities. The definition of “minority” includes racial/ethnic minorities (such as Hispanic, black, Asian and Native American) but does not include other groups such as veterans or disabled persons. Firms may be classified as both women-owned and minority-owned if they have substantial levels of ownership held by women and minorities (for example, firms with both women and minority owners or firms owned by women who also belong to racial/ethnic minority groups). Typically, firms are considered women- or minority-owned if at least 25 percent of firm ownership is held by female or minority individuals, respectively. It is important to note that the classification of diverse owned firms varies slightly across the data sources used in this study.

Data sources

No single database contains all the information needed for the analysis, so several data sources were used, each specializing in a different asset class. To assemble a “universe” of the U.S. asset management industry, the research relied on publicly available data and the following commercial databases:

- eVestment Traditional Database
- Hedge Fund Research (HFR)
- Preqin Private Equity
- Preqin Real Estate

This report includes all active U.S.-based funds from the above databases, excluding funds of funds. For private equity and real estate, we define “active” funds as those with vintage years 2004 or later.



Data analysis and limitations

To quantify the extent of diverse ownership in each asset class, the subsets of women- and minority-owned firms from each database were compared with the “universe” of all U.S.-based firms listed in each database. The results are further broken down by other firm- and fund-level characteristics such as investment focus, firm location and geographic target. These data are also used to analyze timeline trends, performance and the mix of institutional investor types.

The databases used have relatively strong, but not perfect, coverage of each asset class. There may be biases in the types of firms that report to commercial databases and the data that they make available. The approach to analyzing the data for each asset class and any limitations are further described below.

MUTUAL FUNDS: Data on institutional mutual funds were obtained from the eVestment Traditional Database which includes mutual funds, separately managed accounts, commingled funds, and a limited number of exchange-traded funds. These data were used to investigate the current state of diversity for this class of assets, construct a timeline of diverse managers, analyze the performance of these diverse firms, and describe the types of institutional investors engaged with these firms. Firms with at least 25 percent ownership held by women or by racial/ethnic minorities were identified, and some analyses further break down the groups of women- and minority-owned firms into two categories: substantially diverse (25 to 49 percent ownership) or majority diverse (50-plus percent ownership). It is important to note that fund managers often benefit from economies of scale, with many of the largest fund managers structured as publicly traded companies. Therefore, a robustness check was conducted for the mutual fund performance analysis which used mutual fund size as a proxy for public ownership and dropped the largest 5 percent of mutual funds. The core set of regressions (described in the report) were estimated with this restricted data set and compared with the results for the full data set. The estimated parameters were similar for both sets of regressions, suggesting that performance is similar for diverse and non-diverse mutual funds. Therefore, the robustness check supports the findings using the full data set, and it suggests that the effect of including public companies is minimal. While the study found that some minority- and women-owned mutual funds performed among the top funds, it is important to note that academic evidence suggests that actively managed mutual funds generally underperformed public markets during the study period, regardless of ownership status.

HEDGE FUNDS: Hedge Fund Research (HFR) data were used to analyze the current state of diversity in the hedge fund space, construct a timeline of diverse managers and analyze the performance of these diverse managers. As with mutual funds, ownership groups were separated into substantially (25 to 49 percent) and majority (50-plus percent) diverse. HFR covers roughly half of the hedge fund industry and was selected among several hedge fund databases because of its detailed demographic information on



firm ownership, which is crucial to this report. While there is no reason to believe that the characteristics of the hedge funds covered in HFR differ in any meaningful way from the total universe of hedge funds, any conclusions drawn from these data should be interpreted cautiously. HFR does not include information about the investors in each hedge fund, which precluded analyzing the investor types with diverse and non-diverse hedge funds.

PRIVATE EQUITY AND REAL ESTATE: These asset classes rely on Preqin, a leading data source in the alternatives industry. Because Preqin does not provide data on ownership, however, diverse firms in these asset classes were identified from a variety of publicly available and proprietary sources. The ownership information was merged with data on firm- and fund-level characteristics from Preqin. In using this approach, the analysis will have inevitably missed some diverse-owned firms, particularly in the real estate space. This may introduce some biases, such as a bias toward larger, better known diverse firms. The sources used for this report provide greater coverage of diverse-owned private equity firms than that of diverse-owned real estate firms. For private equity, the research analyzed the current state of diversity, timeline of diverse ownership, performance, and institutional investor types of diverse- and non-diverse-owned funds. However, given the small sample size of diverse-owned real estate firms and the potential biases in the data collection, the report includes findings pertaining to the current state of diversity and trends in diverse ownership but was unable to meaningfully analyze performance or institutional investor types.



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