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About That TIAA-CREF Deal.

Why buy Nuveen?

Dazed and Confused

Monday morning a Morningstar analyst informed me that TIAA-CREF had purchased Nuveen Investments. My response: "Huh? Maybe this will make sense to me at a later date." It's currently Wednesday morning and, as of yet, no such luck.

I don't know why an investment-management firm would wish to buy Nuveen. There was a time when Nuveen had a compact, comprehensible business. It was a municipal-bond underwriter and investment manager, based in Chicago, and a market leader and innovator in two niche business, unit investment trusts and closed-end funds. (Nuveen pioneered the leveraged closed-end muni fund.) Buying Nuveen meant instantly becoming a leader with municipal bonds, UITs, and closed-end funds.

Doing a deal with that version of Nuveen would have been similar to Franklin's purchase of Templeton in 1992. Franklin was a bond manager that joined forces with an international-stock firm, which made integration a snap. Franklin had one large bond management group, another large international-stock management group located elsewhere, and the two units continued to do their own things. Franklin finished its three-legged stool four years later when it added U.S. equities manager Mutual Series.Things are not so simple with Nuveen. Over the past 15 years, Nuveen has conducted several of its own, smaller acquisitions. As a result, it no longer is solely a muni-bond specialist. Nor does it continue to run all of its assets from its Chicago office. Rather, its investment-management operations are spread across the country, in what Nuveen calls a "multiboutique" system.

This leads to the question of how TIAA-CREF–or any other asset-management company for that matter–can benefit from Nuveen. Nuveen's operations are pleasantly profitable, as are those of every other mutual fund company of a certain size. However, Nuveen would also be pleasantly profitable if it were owned by Microsoft, or (as was recently the case) by a private equity firm. What makes Nuveen more useful for TIAA-CREF than for other owners? Where is the strategic value?

No doubt that TIAA-CREF believes that it has the answers. The trouble is, I've heard such stories before and they rarely seem to pan out. Although mutual fund firms have collectively spent hundreds of billions of dollars on acquisitions, most of the industry's leaders grew organically. By my calculation, nine of the 15 largest U.S. fund companies (counting exchange-traded funds, but excluding money market funds and funds of funds) built essentially their entire businesses without acquisitions. Among those 15 are the three largest fund companies, Vanguard, Fidelity, and American Funds, which have more assets than the remaining 12 combined.

(At $800 billion in total fund assets, the new TIAA-CREF/Nuveen combination would seem to belong high on this chart. However, the new company does not have many of its assets in mutual funds and ETFs, as TIAA-CREF's biggest business is annuities to educational and hospital 403(b) plans. For its part, Nuveen runs money in a wide variety of ways, including separate accounts in addition to the aforementioned closed-end funds and UITs.)

Table 1: 10 Largest Fund Families — Mutual Funds and ETFs (No Money Market Funds, No Funds of Funds, U.S.-Based Assets Only)

	Assets ($ Billion)	Structure
Vanguard	2343	Home grown
Fidelity	1181	Home grown
American Funds	1119	Home grown
BlackRock	868	Acquisition
PIMCO	524	Home grown
Franklin Templeton	442	Acquisition
T. Rowe Price	431	Home grown
State Street	380	Home grown
JP Morgan	236	Acquisition
Invesco	233	Acquisition
DFA	228	Home grown
OppenheimerFunds	199	Acquisition
Columbia	165	Acquisition
MFS	159	Home grown
Dodge & Cox	158	Home grown

Source: Morningstar.

Of the six companies on the list that have grown partially though acquisitions, and thus are labeled as Acquisition, the biggest two, BlackRock and Franklin Templeton, would appear to be somewhat different from the TIAA-CREF/Nuveen deal. Franklin Templeton, as previously mentioned, is a tripartite construction, whereas Nuveen alone has seven investment-management divisions. BlackRock, too, is made up of three major parts: the iShares operations in San Francisco, its New York-based bond management, and the former Merrill Lynch investment-management group in Princeton, NJ.

As shown by J.P. Morgan, Invesco, OppenheimerFunds, and Columbia, it is possible to become a large mutual fund/ETF organization through acquisitions. Each of those cases is a bit different–Columbia and especially J.P. Morgan coming from bank mergers, OppenheimerFunds doing most of its deals 15 years ago and now growing organically, and Invesco biting off a single big chunk with its purchase of AIM. However, they do offer some general support for TIAA-CREF's thesis.

This discussion, of course, is from the perspective of the shareholder of the mutual fund company, as opposed to the fund owner. What about the latter? Should fund investors be pleased if their fund companies make acquisitions? Are acquired? Do neither?

I asked Vanguard founder Jack Bogle a variation of those questions. His response: "Whatever happened to, 'Don't do something, just stand there?'" He also wondered whether companies with a mutual ownership structure should "use their capital to buy other firms," and mentioned the "ego-building need of successor CEOs to outdo their predecessors."

So you know where he stands: against. Next column, I'll weigh in as to what this means for TIAA-CREF and Nuveen fund owners.

John Rekenthaler has been researching the fund industry since 1988. He is now a columnist for Morningstar.com and a member of Morningstar's investment research department. John is quick to point out that while Morningstar typically agrees with the views of the Rekenthaler Report, his views are his own.

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