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For OCIO Providers, the Fee Pressure Is On

By Aziza Kasumov

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OCIO assets are still growing, but the ascent of third-party search firms and the rise of lower-cost providers has intensified the pressure to slash fees.

“Every provider has evaluated fees closely,” says **Rob Cittadini**, managing director of institutional sales at Russell Investments. “I talk to my peers in the industry, and we’re all feeling it.”

At least one OCIO firm has recently reduced its published fee schedule: **Spider Capital Management,** which oversaw $4.3 billion in assets as of June, including the **University of Richmond**’s endowment and the funds of several unaffiliated endowments and foundations. Beyond published fees, search consultants say quoted fees are coming down at firms across the industry, a trend they believe is far from over.

“OCIO fees are continuing to come down,” says **Brad Alford**, founder of search firm Alpha Capital Management. “There’s tremendous fee pressure across the industry.”

“Any time you do a search, even if you retain the incumbent, you’re probably going to knock five or 10 basis points off the fee,” adds **Frank Szymanek**, a senior consultant in **Planpilot**’s search practice.

OCIO providers have felt the pressure to lower their fees for several years already, a trend in line with the asset management industry at large, where fees have come down significantly over the years.

Yet for OCIOs, the increasing importance that search firms play in intermediating client mandates has forced fees to go down even further. Search firms usually help with negotiating fees and, unlike an institutional investor going blindly into an OCIO search, they know what others are offering. Some search firms, for instance, do not even include OCIOs in a search if their fee schedule is too high.

“I’ve seen firms still bidding 30 basis points, 40 basis points, and I’m saying, I can’t really even include you because you’re so far off the ballpark,” says Szymanek, referring to the OCIO fee only, before considering fees for underlying managers. OCIO fee schedules that include underlying manager fees – called bundled fees – have increasingly become obsolete in the industry over the years, as reported.

Another trend fueling fee pressure is the boom of cheaper alternatives in the OCIO marketplace – the so-called “Vanguard” effect.

The index giant's OCIO offering, for instance, costs five basis points for its largest accounts, not including underlying manager fees. In most OCIO searches, that would be the cheapest option, which could pressure other OCIOs in the search to lower their fees to stay competitive.

For Vanguard, the bet appears to be paying off. The company's institutional arm has seen steep growth in its OCIO unit over the years: Between 2012 and 2016 alone, assets grew from $12 billion to $35 billion, as reported. Since then, Vanguard's OCIO assets have climbed to $56 billion as of September 2020, up $8 billion this year alone.

The index giant's brand has become synonymous with forcing subsections of the investment world to reckon with fees. In the advisory space, for example, Vanguard's low-fee model portfolio offering, based on exchange-traded funds (ETFs), has contributed to the firm's overall growth, all while exerting pressure on competitors to lower their fees.

"A lot of organizations, from the smallest to the largest, are really looking themselves in the mirror and are asking tough questions of their providers for justifying the fees and the performance," says **Chris Philips**, head of institutional advisory services at Vanguard, of the firm's success in the OCIO space. "That's been an industry trend that we've benefitted from," he notes.

Vanguard's efforts mean other providers must stand ready to defend their fee levels.

"We dedicate resources to [intermediaries and OCIO search firms] because of how critical that is in this new world of OCIOs," says Cittadini. "That allows us to tell the Russell story, including why the fees are what they are," he adds.

Russell managed $86.8 billion in fully discretional OCIO accounts at the end of June. That's down more than $10 billion from the end of last year, but still up more than $11 billion from its asset count at the end of 2018 when the firm managed $75 billion in fully discretional OCIO accounts.

Despite their constant landscaping of the industry, search consultants say that navigating providers' fee schedules can be challenging.

The vast majority, 91%, of search firms surveyed by Cerulli Associates earlier this year said that a lack of transparency surrounding fees is at least a moderate challenge when working with providers. Close to one fifth of respondents said the challenge was significant.

"The two major challenges that search consultants tell me about is that some providers have a lack of transparency into performance track records and fee schedules," says **Laura Levesque**, associate director in Cerulli's institutional practice.

The other strong hurdle revealed in the Cerulli survey is inadequate communication around performance, at the heart of which lies a lack of industry standards and consensus around how performance should be measured and compared among OCIO firms. In the end, industry professionals say, the performance puzzle goes hand in hand with the pressure to justify fees.

"In order to actually assess Vanguard, versus pick-your-firm, you really need to have an apples-to-apples approach," Philips says.

Contact the reporter on this story at akasumov@fundfire.com or (212) 542-1209.