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OCIOs Are Hungry for Nonprofit Business as their Pension Client Base Matures

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The OCIO industry has been growing a staggering 16.5% annually since 2015, crossing $1.9 trillion in U.S. assets at the end of last year, according to Cerulli Associates. Much of that growth has come from corporate pension plans handing the largest providers the keys to manage their funds. But industry professionals are increasingly betting on nonprofits to bring new assets through the door.

"No one's forming new pension plans," says **Rob Cittadini**, managing director of institutional sales at Russell Investments. "But we're seeing the rise of new nonprofits."

Nonprofit endowments controlled about $1.7 trillion in assets in the U.S. in 2017, according to an analysis by *Philanthropy Daily*. These endowments are often designed to exist in perpetuity, supporting either the foundations or the universities that they are attached to for generations to come. Advisors and industry observers expect a range of new organizations to pop up over the next several years, as Baby Boomers – who control more than half of the entire country's wealth – age and either donate to existing charitable groups or set up their own private foundations.

"We see more people retiring and leaving assets to charity foundations … it's an opportunity to continue broadening and growing our client base," says **Joe Halwax**, managing director for institutional investments at OCIO boutique **Wespath**, the nonprofit investment arm of the **United Methodist Church**.

Large firms are on the hunt for new nonprofit clients as well.

"What we see is a maturing defined benefit outsourcing universe, where pension clients are less and less frequently coming to us wanting to know more about outsourcing," says Russell's Cittadini. Corporate pension clients have historically made up a large chunk of the firm's OCIO unit, which in total controlled $86.8 billion in fully discretionary assets as of June, according to the firm. But today, Cittadini says, nonprofits are a "high growth space, and it's high growth in terms of OCIO adoption and just new organizations."

Wilshire Associates has also traditionally served mostly pension clients. The firm is still picking up new corporate defined benefit clients, but has also observed "a shift more toward endowments and foundations," says managing director **Ryan Lennie**. Wilshire has $18 billion in OCIO assets, according to the firm.

Russell and Wilshire are not the largest players in the OCIO space – that title goes to Mercer and the soon-to-be-completed Aon and Willis Towers Watson combination. Post-merger, both Aon, under whose brand the combined company will operate, and Mercer will control roughly $300 billion in OCIO assets, a big chunk of which belongs to pension clients. But search consultants say it can be difficult for such mega-firms to tap into the nonprofit space.

"The pension funds are going away. Every CFO's happiest day is when they finally sell their DB plan," says **Brad Alford**, founder and principal of search firm Alpha Capital Management. "We get asked all the time – how do we get in with endowments and foundations," he notes. But nonprofits often aren't interested in the 10 largest firms. "They just feel like they're a small fish in a big pond," Alford adds.

Search consultants play an important role in mediating nonprofit OCIO mandates. All of the search firms surveyed by Cerulli Associates last year have helped at least one foundation client find a match before, and 88% said they have mediated a mandate for an endowment.

Another challenge OCIO providers face when trying to tap into the nonprofit space is that while there are many endowments and foundations, they tend to be much smaller than pension funds, so one new client can only bring so much in assets under management through the door. The country's largest university endowment, for instance, is Harvard University, with $42 billion in assets. The largest foundation is the **Gates Foundation**, with roughly $50 billion in assets, an absolute anomaly in the nonprofit landscape. Both are relatively small compared to some of the country's largest pension funds.

And the nonprofits OCIOs are trying to target are even smaller in scale.

Across the endowment and foundation space, OCIOs surveyed earlier this year by Cerulli said they anticipate by far the highest growth to come from institutions with between $101 million and $250 million in assets. Around one-fourth of respondents said they expect endowments and foundations with between $251 million and $500 million to provide the highest growth opportunities.

Beyond that, the range of OCIO providers available for such clients is also much larger. A double-digit billion pension plan can only go so many places for a full-service OCIO – but a $150 million endowment can be serviced, hypothetically, by almost every OCIO boutique out there.

"It's a very fragmented market," says **Chris Philips**, head of institutional advisory services at Vanguard. "That's one of the challenges facing the OCIO providers in the space. There's a lot of choice," he adds. "That's where the value of a search consultant comes in."

About two-thirds of Vanguard's OCIO client base is nonprofits, Philips says, with pensions making up the remaining third. The index giant's OCIO solution – one of the cheapest in the business – controlled $56 billion in assets in September, up significantly in recent years.

For pension-focused OCIOs, the shift to nonprofits means that they must put in some additional effort.

“As we’ve talked to endowments and foundations, it’s just having them recognize that, while Wilshire might be known a bit more publicly for pension clients, … endowments and foundations have always been an important part of our business,” Lennie notes. He adds that such clients make up about a third of the firm’s OCIO client base today.

Search consultants, still, are convinced that such large providers have an uphill battle ahead of them.

“Endowments and foundations don’t want to be with a $5 [trillion or] $10 trillion dollar firm that has all these conflicts,” says Alford. “Small boutiques – that’s where we’re seeing the most demand.”

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