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OCIOs Expect Pandemic-Fueled Client Boost, See First Spike in Activity

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Outsourced CIO (OCIO) providers are getting ready for a new wave of clients as they believe the coronavirus-induced economic crisis will trigger asset owners to reconsider how and by whom their investment portfolios are managed.

Half of the consulting and OCIO firms surveyed by Chestnut Advisory Group between April and May said they have increased their growth expectations for the next two years since the beginning of the pandemic, with 36% leaving their projections unchanged, and another 14% lowering them. Responding firms collectively oversee $18.3 trillion in assets.

"After the great financial crisis in 2008 and 2009, OCIO growth really took off," **Simon Segall**, senior advisor at Chestnut, said during a webcast presenting the results last Thursday. "We asked ... if OCIOs expected another surge after the pandemic, and the answer was a pretty resounding 'yes.'"

OCIO leaders at Russell Investments, SEI and BlackRock, which already oversee $162 billion, $167 billion and $205 billion in outsourced assets, respectively, echoed that sentiment in interviews with *FundFire.* All three firms believe they will grow their OCIO assets more quickly than anticipated pre-pandemic, with the skill and speed necessary to navigate today's volatile markets serving as a key driver to push previously non-OCIO institutions toward the offering.

Some said they are already seeing an uptick in request-for-proposal (RFP) activity that started after the first pandemic shock was over.

"It's been like a swimmer plunging into a body of cold water – initially, there's a gasp and pause and time to reflect [and say], 'What just happened, what's going on," says **Rob Cittadini**, managing director for institutional sales at Russell. "Now that that initial shock has worn off,… the asset owners we speak with on a regular basis are coming out with more questions, not just on partnering on the investment program, but on outsourcing the investment program."

Several public institutional investors have already launched searches for their first OCIO provider in recent weeks. The $2.9 billion **Police and Fire Retirement System of the City of Detroit** initiated an OCIO search during its committee meeting in May, as reported by sister publication *MandateWire.* The $1.5 billion **District of Columbia Other Post-Employment Benefit Fund** also issued a request for proposal for OCIO services in May, as reported by *MandateWire.*

Mercer and Aon, which control some of the largest non-discretionary and discretionary client asset pools in the industry, said in statements that they believe the pandemic will accelerate OCIO adoption as well.

The optimism isn't just coming from the providers themselves, however. Some OCIO search firms, which have risen to a more prominent intermediary role in recent years, say that after a slow-down period in March and April, searches have picked back up.

"Normal searches ticked down with the onset of [COVID-19], and it delayed those searches in process," **Tom Donahoe**, managing director for OCIO search and governance at Manager Analysis Services, said earlier this month. In the last few weeks, however, "we [have] seen an uptick in searches, both normal searches as well as those due to performance-related catalysts."

"We're as busy as we've ever been," adds **Brad Alford**, founder and principal of search firm Alpha Capital Management.

It is unclear what exactly the mix of replacement searches and first-time outsourcers will look like. More than half of all respondents to the Chestnut survey said they expect between 21% and 30% of all investors to review their existing investment consultant or OCIO relationship.

OCIO performance results in the first quarter – the worst quarter since 1987 for the stock market – likely served as the "last straw" for some investors, search consultants say.

An anonymized sample of 645 client portfolios included in the **AlphaNasdaq** suite of performance indices for OCIOs showed an average return of -11.71%, net of fees, for the first quarter, barely outperforming a traditional 60/40 portfolio that lost 12.01%, as reported.

But there was a "pretty big spread between the top and bottom quartiles," Alford notes.

In Q1, the bottom quartile of all portfolios included in the index returned -15.07%, and the top quartile returned -9.83%. And the gap wasn't just a crisis phenomenon: Although much smaller, there was still a 1.6 percentage point difference between the 75th and the 25th percentile among five-year annualized returns and 10-year annualized returns as well.

"You can pick really bad OCIOs and really good OCIOs, and there's a meaningful difference between top and bottom," says Alford. For institutions, he adds, "at a billion dollars, every 1%… is $10 million, and that can pay for a lot of things."

Industry professionals still expect a significant amount of OCIO growth in the coming years from new converts, not just replacement searches launched by disgruntled clients.

"Based on everyone I'm talking to, the higher-[growth expectation] is… because there's new people looking to outsource that weren't before, or they were thinking about it, but the pandemic and the market crisis woke them up," says **Amanda Tepper**, founder and CEO of Chestnut.

Some OCIO providers, while noting they expect new clients from all sectors of the institutional landscape, say they believe a good chunk of that growth is going to come from larger asset owners that have only slowly warmed up to outsourcing their investment programs.

“That’s been a trend that has been in place for a couple of years, but the crisis seems to have been accelerating certain things,” says **Ryan Marshall**, BlackRock’s global head of client portfolio solutions. “It’s not just more than $500 million, but larger than $1 billion” plans that are looking to outsource, he notes, adding that many of those searches are coming from the corporate defined benefit landscape.

Others say college endowments, hit hard by the crisis, might flock to them.

“The one area that is definitely going to see an uptick and that has the most, a lot of stress, is the college and university marketplace,” says **Paul Klauder**, executive v.p. and head of SEI’s institutional group.

While providers emphasize that the switch to online and the traditionally slow decision-making process at many institutions means it will take some time before the first pandemic deals close, some believe they might see the first pandemic-induced assets sweep through the door soon.

“There’s a couple [of contracts] in the final decision-making process,” says Klauder. “We hope it’s close.”

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