FUNDfire
A Financial Times Service

OCIOs Under Pressure to Increase Fee Transparency

Search firms and regulatory organizations have tried to make it easier for asset owners to compare the costs of different OCIO providers.

By Sabiq Shahidullah | October 24, 2024

Outsourced chief investment officers, or OCIOs, face growing pressure from industry groups to make their fee schedules clearer to prospective clients.

It's difficult to make a fair comparison of OCIO providers since they bundle client fees in different ways, said **Chris McGoldrick**, managing director of OCIO and retirement solutions at **PNC**.

And clients' total costs include not just the OCIO's services fee, but also asset manager fees and custody fees.

While some OCIOs will bundle all fees, others will only bundle certain items, like the provider and custody fees. Manager fees are often charged separately and vary depending on asset allocation and whether strategies are active or passive, McGoldrick said. Large banks and asset managers with OCIO arms sometimes construct client portfolios using their own products, adding another layer of complexity to comparing fee structures.

"When you think of some of the largest asset managers in the world that have OCIO businesses, it's not always clear if they're going to charge a direct investment management fee [if] you use their own products, or if they're going to keep that separate," McGoldrick said. "I don't think there's consistency."

McGoldrick added that he encourages clients to "go under the hood" of OCIO costs to ensure they are getting the appropriate value for what they're paying.

The OCIO market has nearly doubled in size over the past eight years and is projected to hit $4.7 trillion by 2029, up from $3.1 trillion in 2024, according to **Chestnut Advisory Group**.

But even as the market grows, a lack of publicly available OCIO fee and performance data makes comparison harder, said **Ravi Venkataraman**, a managing partner at Chestnut Advisory. "There isn't transparency," he said. An OCIO knows its own fees, but lacks insight into the fees of the firms it's competing against, he added.

The OCIO industry is "unlike mutual funds, where there are standard reporting processes and heavy regulation by the [Securities and Exchange Commission]," said **Tom Donahoe**, an endowment and foundation specialist at **OCIO Monitor**, which evaluates the performance of OCIOs.

The lack of standardized performance reporting has also made it difficult for investors to compare the value OCIOs are adding.

The **CFA Institute** has proposed applying a version of its Global Investment Performance Standards, known as GIPS, to standardize OCIO performance benchmarks. Industry reactions have been mixed, with some critics arguing the standards are too restrictive to fit the OCIO model, while others claims the standards leave room for manipulation.

"The standardization of reporting performance has not been settled, so it's difficult for the average endowment or foundation to compare apples to apples," Donahoe said.

Some companies have sought to make it easier for asset owners to compare OCIO providers by aggregating data and providing evaluation services.

In August, OCIO Monitor launched a peer fee and performance review service for asset owners to help them ensure their OCIO fees are in line with market value.

OCIO search firm **Alpha Capital Management** recently introduced a peer universe tool populated with performance and asset allocation data from 1,200 institutions and 51 OCIOs.

Using the tool, a $250 million foundation could input its performance data to see how it compares with similar organizations, said **Brad Alford**, founder of Alpha Capital Management.

"It increases transparency," Alford said. "It gives asset owners the ability to look at performance, as well as asset allocation, versus their peers."

Alpha Capital Management also partnered with **Nasdaq** in 2019 to create a set of indices to help asset owners evaluate their OCIO's performance. The indices cover different investor types such as pensions or endowments, as well as risk levels, like an aggressive or conservative asset allocation.

"Transparency is scary to some firms, but we're pushing it, and asset owners want it," Alford said.

While greater fee transparency would make it easier for asset owners to compare OCIOs, it could also lead to greater industry consolidation, Venkataraman said. Large OCIOs can generally charge lower fees since they already have established technology and research infrastructure.

"If they've got a 50-person research group, adding 10 or 20 clients does not mean that they're going to hire an additional research person, they're just going to allocate larger amounts to those investment opportunities," Donahoe said. "Their marginal cost of adding new clients is de minimis."

Consolidation, such as **Mercer**'s acquisition of **Vanguard**'s OCIO business last year, is already putting downward pressure on fees., Donahoe added.

Smaller OCIO firms may struggle to compete with the behemoths, at least on fees.

OCIOs on the smaller end of the asset spectrum could specialize and focus on providing highly customized portfolios for their clients, Venkataraman said.

"The pension funds love the big firms," Alford said. "But the endowments and foundations like the smaller firms where they'll get a lot of attention and access to niche managers."

What will happen to the middle segment of the OCIO market – firms that are neither specialists or massive companies – is unknown, Venkataraman said. "The guys in the middle will have to decide, what is their competitive advantage, what's their value-add?" he added.