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Prospects for OCIOs Grew in 2023 but Scrutiny Remains

OCIOs gained clients from new segments and large mandates in 2023, while the CFA institute sought to standardize in the space with proposed guidelines.

By Sam Heller

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The outsourced chief investment officer, or OCIO, space continued its rapid growth over the past year, with bigger and more complex clients looking to outsource investment management.

However, the sector continued to face questions about conflicts of interest, and draft guidelines to streamline the industry emerged.

A study done by search consultant Charles Skorina estimated that 101 OCIOs oversaw roughly $3.4 trillion in assets at the beginning of 2023, outpacing Cerulli Associates 2021 projection that the industry would manage $2.9 trillion in assets by 2025.

OCIOs have won mandates from large pension funds that had not previously considered outsourcing their investment offices. This trend started in 2020 but has been accelerating over the past year, said Thomas Kennelly, senior investment strategist at State Street Global Advisors, in an interview earlier this year.

This year, BlackRock landed the $10 billion London-based Royal Mail Pension Plan, and Goldman Sachs Asset Management took on the $29 billion BAE Systems defined benefit plan.

"Some of these very large pools can be very complex on the investment side and the operational side," said Jeff Saef, BlackRock's head of the Americas solutions, multi-asset strategies and solutions, in a July interview. "[A]t some point, that complexity sort of tips over to a point where... it's so difficult to manage internally, [and] that led to more of these larger OCIO searches."

The largest OCIOs in the field have won most of the big pension mandates, but new small and mid-sized prospects have sprouted.

The growing trend of philanthropists making massive donations led traditionally smaller endowments to seek out OCIOs – the donations, dubbed transformational gifts, can be $250,000 and upward.

National chapters of fraternities and sororities also started to consider OCIOs to help manage their portfolios, which can range from under a million to $300 million.

Bank of America worked with nearly 50 Greek organizations as of July, said Bill Jarvis, managing director and philanthropic executive at Bank of America.

“Fraternities and sororities are among the most complex, tax-exempt organizations with which we work,” said Dianne Chipps Bailey, national philanthropic strategy executive at Bank of America in a July interview. “The OCIO model makes great sense for them because they want to entrust the stewardship of their long-term assets to a partner that can understand [their] fiduciary [obligations] and discretion.”

With more complex clients entering the space, OCIOs started expanding the services and blurring the lines between their offerings and the role of investment consultants. For some clients, OCIOs will offer research, educational materials and help updating investment policies, as reported in May.

OCIO FEG Investment Advisors also began working with the University of Dayton’s student-run investment fund to help them manage a portion of The Dayton Foundation’s portfolio. This has strengthened their connection with both clients, and the firm has started replicating the process with other community foundations and schools, said Quincy Brown, senior vice president at FEG, in October.

Growth in the sector was accompanied by additional scrutiny.

With no standard rules on performance reporting or OCIO-client relationships, the space has been the “wild west,” and clients cannot understand the differences between who they are hiring, said Amanda Tepper, founder and co-owner of the Chestnut Solutions Institute in November.

“It’s super confusing right now for anyone looking to hire [an OCIO],” she said. “People are using different languages, different terms to describe the same thing — there is no common understanding.”

In September, the CFA Institute sought to fix these problems by drafting guidelines to bring OCIOs in line with global investment performance standards, or GIPS. The new guidelines were created with the help of a working group consisting of 15 industry members.

The GIPS guidelines aim to standardize the process of grouping similar portfolios, based on objectives and asset classes, and create standardized benchmarks and fees.

When the final draft of the guidelines is published, they are expected to hold significant weight the industry, Tepper said.

The guidelines are not mandatory for OCIOs, but some search consultants have already said they will not consider any OCIO in their search that does not comply. These search consultants conduct anywhere from a quarter to half of all searches for OCIO providers, Tepper said.

But some industry players take issue with aspects of the guidelines.

The public comment period for the exposure draft closed at the end of November, and some smaller OCIOs worry that in their current state, some managers will find ways to game the system.

“Any level of ambiguity around this will also leave the recipients of this information skeptical of the process and feeling misguided,” Canterbury Consulting said in their comment.

The proposed guidelines allow OCIOs to come up with their own definitions of risk-mitigating or liability-focused assets, which determines which groups they fall into. If firms are coming up with their own definitions, it would render comparisons between OCIOs essentially “meaningless,” OCIO LCG Associates wrote.

The CFA Institute intends to refine the draft in 2024, but there are other gray areas that aren't covered by the proposed guidelines that puzzle search consultants. Firms with both OCIO and asset management divisions have faced questions regarding conflicts of interest from search consultants throughout the year.

Consultants contend that some managers are able to collect double fees if they place proprietary investment strategies into OCIO portfolios – and investors may not realize when these products have been added to their portfolio.

"The OCIO model is the most conflicted model I've ever seen before – giving the investment advisor the ability to hire and fire themselves," said Brad Alford, founder of search consultant Alpha Capital Management, in an interview. "It's a huge problem in the industry, as it is very hard to fire someone you work down the hall from."