EVALUATE YOUR OCIO PROVIDER

Evaluate your OCIO provider with these five key factors

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With interest rates rising and inflation remaining at stubbornly high levels, businesses head into the waning months of 2022 facing a double whammy of higher operating expenses and potentially challenging investment returns. With the stakes so high, and resources increasingly limited, many companies are turning to an Outsourced Chief Investment Officer (OCIO) provider to ensure they can effectively manage their investment program. It's more imperative than ever that your OCIO provider step up to the plate—or it may be time to make a switch. And, it goes without saying that if you haven't worked with an OCIO provider yet, we believe there's never been a more critical time to consider outsourcing your organization's investment needs.

But how can you ensure that your current strategic investment partner—or the one you are considering choosing—will be up to the task at hand? After all, not all OCIO providers are created equally. Capabilities, skill set, depth of knowledge, resources and investment philosophy can vary sharply from one provider to the next.

To help provide you with answers to this all-important question, we've developed a questionnaire to guide you through an evaluation process of your current or potential OCIO provider. Think of it as conducting an annual checkup—or risk assessment—on your outsourced investment partner. Below, we share the five key factors we believe all OCIO providers should be assessed by. With decades of experience managing the investments of organizations as a fiduciary, we have unique insight into what it takes for companies to achieve their investment goals.

1. Does your OCIO partner provide ongoing strategic advice and direction that will impact your results?

We all know the deal: During the OCIO bidding process, potential providers promise round-the-clock communication, collaboration and attention to your organization's needs.

But once the contract is signed, these types of promises can go unfulfilled. Think back to how engaged your provider has been with you since the ink dried. Have they truly given your organization the personalized attention it's needed as the days, months and years have ticked by? And, if you're thinking about OCIO for the first time, check and see if the provider even has the capabilities and resources to deliver on this promise in the first place.

This is very important in today's highly uncertain market environment. With fewer opportunities to carve out excess returns, every stone needs to be overturned to identify potential opportunities and potential risk. Doing this requires hands-on, daily portfolio oversight. Picking good managers and portfolio rebalancing on a quarterly cycle is no longer sufficient, and, quite frankly, no longer acceptable—especially in today's volatile markets. A strategic OCIO provider will have grabbed the reins on day one and continuously be taking active, real-time ownership of your organization's portfolio.

Beyond demonstrating a commitment to day-to-day portfolio management, it's also instrumental that your OCIO provider be giving clear, direct advice on improving the portfolio's structure in order to meet return expectations. If it's your first time searching for an OCIO provider, ask upfront how they will go about doing this during the selection process. A skilled provider should be able to offer solid advice on both portfolio structure and allocation—and thoroughly demonstrate how they will optimize returns for your organization.

> *If you're dipping your toes into the OCIO waters for the first time, how can you determine if the OCIO provider bidding for your services will actually deliver on their promises?*

2. Does your provider have strong risk management capabilities and ongoing fiduciary oversight?

It's also critical for your OCIO provider to have strong risk management capabilities. If you're just starting down the OCIO path, make sure that the provider demonstrates this during the selection process. Remember that as fiduciaries, providers have a duty to manage all risk, including unintended risks that the organization may be unaware of. A true fiduciary should be proactively identifying all unintended risks and developing a plan to mitigate each one.

The importance of this cannot be overstated. Many times, unintended risk can prove detrimental to a portfolio's short-term return objectives. By the time the risk has been mitigated, the damage is often already done. It goes without saying that fiduciaries must monitor all risks with a sense of vigilance and ensure that the risks are managed out ahead of time.

Of course, it's one thing to say this, and another to actually do it. If you're dipping your toes into the OCIO waters for the first time, how can you determine if the OCIO provider bidding for your services will actually deliver on their promises? How will they identify some of the unintended risks that can occur in your portfolio when hiring multiple managers? Do they have insight into your total portfolio holdings—not just each manager individually? Ask them what the 1-in-20 risk event is that could detrimentally impact your portfolio. Then, ask how they would address this risk ahead of time. What capabilities have they built and what specific steps would they take to manage out the risks in real time?

Responses to questions like these are where the contrasts between different providers become more readily apparent. Successful portfolio management requires much more than just picking good managers. A true fiduciary partner will already know what risks have been taken, what exposures exist and exactly how each of these risks may impact performance. They'll stress their commitment to dynamic portfolio management and to making adjustments in real time.

By contrast, a provider lacking in these capabilities will go light on the specifics. They'll talk of portfolio rebalancing or adjusting manager weightings at quarterly meetings instead, skipping over the fact that this effectively amounts to a *set it and forget it* approach, whereby portfolio adjustments are only made four times a year, regardless of daily market volatility.

3. How transparent are your OCIO provider's fees and what is their value/cost ratio?

It's no secret that many an OCIO provider often has a complex fee structure. The exact breakdown of this structure, however, should be anything but secret.

Simply put, honesty and transparency over fees is crucial. A provider's willingness to provide full fee disclosure upon request speaks volumes about their commitment to transparency. If they keep hiding fees from you, what else are they keeping you in the dark on?

A good OCIO provider will be entirely honest and upfront on their free structure and will inform you well ahead of time of any changes in cost. They'll be more than willing to dive into the nitty gritty, thoroughly explaining each fee you have questions about. You should demand no less. Ask what each fee is for, and the value it provides. Press the provider for additional details on charges that confuse you and ask about costs you don't see listed.

In addition, for those giving OCIO a go for the first time, during the fee evaluation period, it's important to look at the total estimated fees based on the same assumed asset allocation—active and passive—for all providers. Too often an organization will only compare the OCIO fees, assuming that the additional investment management fees will be the same across all providers. This is rarely the case. Providers that have a more substantial footprint in OCIO will likely be able to leverage their scale to significantly reduce the fees for the underlying investment managers selected, which will make their total estimated fees less.

Ask the provider if they can provide a total estimated fee based on managers they have actually implemented for other clients. Ask what other fees might impact the performance of their portfolio that aren't clearly transparent. Ask what percentage of passive investments they have assumed in their investment manager fee estimate to ensure they haven't gamed pricing.

A quality OCIO partner will not shy away from these questions. Instead, they'll be able to clearly demonstrate the value behind each fee, and why the fee is worth paying for. Remember Warren Buffet's old adage: Price is what you pay, value is what you get. Premium services are worth a premium, but the value must be justifiable.

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4. How well does the provider act as an extension of your staff, helping to ease internal workloads?

What good is any OCIO provider if they're not taking work off your plate? After all, one of the reasons many organizations outsource in the first place is to free up more time and resources to address issues core to their business. It goes without saying that this offering has become even more paramount in the two-plus years since the COVID-19 pandemic hit.

Don't be content with your current provider if they merely create zero additional work. The right partnership needs to be resulting in *less* overall work on your end. Has your provider taken the lion's share of the workload off your back? Do they have the right systems and the right infrastructure to support what you're already doing internally? How else are they helping ease your overall burden?

The right provider's staff will be acting as an extension of your staff and doing all of the heavy lifting. They should be overseeing and providing all of the operational, administrative and audit support needed to ease your internal workload. They should be available 24/7. Their support should make you feel like you're being given the white-glove treatment—which is exactly how your organization should be treated.

> *How experienced is your provider in your industry?*

5. Does your provider have dedicated knowledgeable resources that pertain to your industry?

Last but not least, your OCIO provider should thoroughly understand the ins and outs of your industry. Remember, the financial health of your organization is at stake—the current economic environment has resulted in challenging operating margins for many businesses, which is why a strong investment program is needed to ensure the overall resiliency of your organization's financial plan. There's no time for learning on the job. If you're in the OCIO selection process, make sure this is not the provider's first rodeo. Your partnership needs to be a sharing experience, not a learning experience. Tricks of the trade and lessons learned from previous engagements should be shared by the provider to make sure your organization is on the right path.

How experienced is your provider in your company's industry? Ask yourself if they've demonstrated an understanding of the specific challenges unique to your industry throughout your partnership. Do they have a thorough understanding of how organizations like yours think?

Remember, a strategic OCIO provider will go beyond demonstrating their understanding of the pressures in the industry and what keeps you up at night. They should also be telling *you* the things you should be thinking about—the myriad of investment options at your disposal, and how each option may impact your return objectives. They should be well-versed in the day-to-day challenges of organizations like yours and should strive to take preemptive actions. How often has your provider done this over the course of your partnership?

The bottom line

How well did your OCIO provider score? When it comes to risk management prowess, strategic vision, fee transparency, resources and industry expertise, not all are on the same page. If your current provider isn't exceeding your expectations in each of these categories, it may be worth exploring a new partnership. And if you're just beginning your outsourcing journey, it's well worth the dig to find a provider that positively checks all of these boxes.

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