Choosing an OCIO provider

5 key factors for organizations to consider

The overall economic picture remains muddled. Ongoing trade tensions and slumping global growth have cast a cloud of uncertainty over the globe, and forward-looking return expectations continue to look less than impressive.[1] In such an environment, organizations' need for a strategic investment partner is no longer a nice-to-have. In our opinion, it's mission-critical to their long-term success.

We believe this can best be accomplished by teaming with an outsourced CIO (OCIO) provider, in order to enhance the organization's investment program and free up additional resources to focus on core business matters. Yet it's important to realize that 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.

With over 39 years of experience managing organizations' investments as a fiduciary, we have unique insight into what it takes for those in the industry to achieve their investment goals. We've identified five key factors in particular that we believe organizations should look for when searching for an OCIO provider.

1. Can the 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, have the OCIO providers built the capabilities and resources to really deliver on their promises? Will they truly give your organization the personalized attention it needs as the days, months and years tick by?

This is a very important point to ponder in an increasingly volatile, low-return 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.** A strategic OCIO provider should grab the reins on day one and take active, real-time ownership of your organization's portfolio.

Doing this requires hands-on, daily portfolio oversight.

Beyond demonstrating a commitment to day-to-day portfolio management, it’s also instrumental for the OCIO provider to give clear, direct advice on improving the portfolio’s structure, in order to meet return expectations. **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. Simply put, the provider must show they will **own** your investment program.

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

It’s also crucial, in our opinion, for the provider to thoroughly demonstrate their risk management capabilities 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 will proactively identify all unintended risks and develop 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. 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.

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3. Fee transparency and the notion of value over cost

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 during the selection process.

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Honesty and transparency over fees are crucial at this stage of the game. Think of the provider's willingness—or lack thereof—to provide full fee disclosure as a glimpse into what your partnership may be like. If they're hiding fees from you at the negotiating table, what else might they keep you in the dark on once contracts have been signed?

A good OCIO provider will be entirely honest and upfront on their free structure. They'll be more than willing to dive into the nitty gritty, thoroughly explaining each fee. **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, when you evaluate fees, 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 the 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, since 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.

4. Can the provider act as an extension of your staff, helping ease internal workloads?

What good is any OCIO provider if they're not taking work off your plate? After all, one of the reasons organizations outsource in the first place is to free up more time and resources to address issues core to their business.

We often hear that organizations want an OCIO partner that won't create any additional work for them. **This isn't enough of an ask.** Your OCIO partner needs to go one step further and take full ownership, to the point where your organization has ***less work*** to do on the investment front.

Don't be content with a provider who promises to create zero additional work. Ask them how a potential partnership would result in less work and make your life easier overall. How will they take 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 can they help ease your overall burden?

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

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

Last but not least, an OCIO provider needs to thoroughly understand the ins and outs of your particular industry. Remember, the financial health of your organization is at stake—and when it comes to managing your benefit plans, people's retirement is at stake. There's no time for learning on the job. **This cannot be 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.

During the interview process, press the provider on their experience in your industry. See if they understand the specific challenges unique to your line of work. Do they understand the impact of mergers and acquisitions activity on an organization's balance sheet? If you have a pension plan, do they understand the impact of its funded status and contribution requirements on the company's financial health? Do they understand how each asset pool at a company can impact the overall financials of the organization? Above all else, do they understand how organizations in your industry think?

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Tease this out during the selection process. A strategic OCIO provider will go beyond demonstrating their understanding of the pressures in your industry and what keeps you up at night. They'll also tell 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'll be well-versed in the day-to-day challenges of organizations like yours, and they'll strive to take preemptive actions. They'll not only speak your language, they'll routinely converse in it.

Bottom line

There's no shortage of OCIO providers to choose from these days. But when it comes to risk management prowess, strategic vision, fee transparency, resources and industry expertise, not all are on the same page. It's well worth the dig to see who is.

[1] As of December 2020.

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First used: December 2019 AI-27936-12-22