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Special Report

INVESTMENT OUTSOURCING

OCIO rides market rebound to big growth

Managers also see clients shift from internal management post-pandemic

By CHRISTINE WILLIAMSON

The year ended March 31 was a strong one for OCIO managers, many of which had double-digit growth in assets under management thanks to a wave of new clients and strong performance.

The combination of buoyant market returns in the last three quarters of 2020 through the first quarter of 2021 and higher investment in OCIO strategies brought the industry to a new record total of $2.46 trillion in assets managed worldwide with full or partial discretion for institutional investors as of March 31, data from *Pensions & Investments'* latest industry survey showed.

Market returns were a significant driver of OCIO manager growth in the year ended March 31. The S&P 500 Total Return index was up 56.4% in the year ended March 31; AlphaNasdaq OCIO Broad Market index, up 30.7%; and Bloomberg Barclays U.S. Aggregate Bond index, up 0.7%.

In sharp contrast, the S&P 500 was down 6.9% the prior year, the AlphaNasdaq OCIO index was down 3.4% and the Bloomberg Barclays U.S. Aggregate Bond index was up 8.9%.

Daniel Burke

STRONG: Christopher B. Philips said Vanguard had a good 2020, once it got past June.

Timothy J. Braude, managing director and global head of OCIO at New York-based Goldman Sachs Group Inc., said in an interview that in 2020 "our OCIO clients experienced a very fast drawdown and a very fast recovery. Equities were up 50% to 60%, and we and our clients had a very big year. 2020 was like a supercharged version of what we saw after the global financial crisis in 2008."

"The really rapid recovery gave investors a chance to step back and decide what they wanted to do about moving away from in-house portfolio management and into an OCIO arrangement," said Mr. Braude, adding that Goldman Sachs had "a very strong year" of organic OCIO growth in the year ended March 31.

22.7% growth

Total OCIO assets managed for worldwide institutions with full/partial discretion grew 22.7% over the year, compared with a rise of 8.4% in the year

The largest managers of outsourced assets by type

U.S. institutional outsourced assets under management, in millions, as of March 31.

Foundation assets

Rank	Manager	Assets
1	Vanguard Group	$23,730
2	PNC Financial	$16,677
3	Northern Trust	$6,291
4	Global Endowment Mgmt.	$6,110
5	Agility	$5,209
6	Fund Evaluation Group*	$4,997
7	Fidelity Institutional	$4,226
8	Commonfund	$3,867
9	Russell Investments	$3,790
10	Aetos Alternatives	$3,756

*As of Dec. 31

Endowment assets

Rank	Manager	Assets
1	Vanguard Group	$10,791
2	Mercer	$9,930
3	Commonfund	$8,427
4	Agility	$6,590
5	State Street Global	$6,533
6	Strategic Invest. Group	$6,500
7	Hirtle, Callaghan	$6,200
8	TIFF Advisory Services	$5,215
9	BlackRock	$3,849
10	NEPC	$3,313

ended March 31, 2020, to the previous peak of $2.01 trillion.

Over the five-year period ended March 31, growth of worldwide OCIO AUM was up 90.5% compared with 54.6% for the five years ended March 31, 2020.

For periods ended March 31, worldwide OCIO assets managed with full discretion for institutional investors totaled $1.95 trillion, up 23.8% for the year and up 124.5% for the five-year period, *P&I* data showed.

After the outbreak of COVID-19 last year when work, home and social life became difficult, "there was recognition among asset owners that things had gotten too complicated for an internal investment committee to handle. On the corporate side, employees saddled with dealing with liabilities and other issues decided they weren't being paid to manage a defined benefit plan and started looking at OCIO options," said Steven F. Charlton, partner and director of consulting services at NEPC LLC, Boston, in an interview.

"Markets helped, but our growth was mostly organic," Mr. Charlton said.

NEPC had the second-highest growth rate among OCIO managers surveyed, up 90.9% to $53.7 billion in the year ended March 31, moving the firm to the 12th spot in *P&I*'s ranking from 18th.

Industry sources, including specialist OCIO search consultants, said they've seen a spike in interest from new OCIO investors or existing OCIO investors interested in manager upgrades.

"There's been a huge pick up in OCIO search activity. OCIO is gathering momentum," said Bradley H. Alford, founder and CEO of OCIO search firm Alpha Capital Management LLC, Atlanta, in an interview.

The new growth spurt in OCIO search and hiring activity in 2021 is in sharp contrast to March, April and May 2020 in the aftermath of the COVID-19 outbreak when many asset owners shelved their OCIO search plans to deal with other more pressing work issues, Mr. Alford said.

Later in 2020, the level of search activity became so frenetic that Mr. Alford had to stop accepting new OCIO searches and created a waiting list, noting that "the crush is easing a bit so we can take on more searches now."

Mr. Alford said the majority of Alpha Capital's OCIO searches in 2020 and so far in 2021 were for endowments and foundations.

Mercer still at top

Mercer LLC, New York, retained its position as the largest manager of worldwide OCIO AUM with full/partial discretion for institutions, up 40.9% to $367 billion in the year ended March 31. Goldman Sachs Group rose to second place from seventh with assets of $207.7 billion, an increase of 31.6% in the year ended March 31.

In 2022, the top spot in *P&I*'s ranking of OCIO managers might be filled by a new manager if the merger between Aon PLC and Willis Towers Watson PLC comes to fruition.

Aon managed $202.8 billion and Willis Towers Watson managed $167.7 billion in worldwide OCIO assets managed with full/partial discretion for a total of $370.5 billion as of March 31, topping Mercer's total. Aon dropped to the third spot this year despite 17.8% growth in AUM. Willis Towers Watson ranked sixth, dropping two spots.

The London-based firms announced their plan to unite in March 2020 in an all-stock $30 billion deal with a combined equity value of $80 billion. The U.S. Justice Department sued to block the deal earlier this month due to concerns about stifling competition.

The Vanguard Group Inc., Malvern, Pa., had its best year ever for OCIO strategies in calendar year 2020, despite a challenging, slow search-and-hire environment between March and June, said Christopher B. Philips, principal and head of Vanguard Institutional Advisory Services, in an interview.

"It was barren. No one did anything during that period, but since the end of

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The largest managers of fully discretionary assets

Worldwide institutional outsourced assets under management, in millions, as of March 31.

Rank	Manager	Assets managed with full discretion	% of assets with full discretion	% of assets with partial discretion
1	**Mercer**	$352,307	96%	4%
2	**Goldman Sachs Group**	$207,701	100%	
3	**Aon**	$152,107	75%	25%
4	**BlackRock**	$138,037	87%	13%
5	**State Street Global**	$110,506	61%	39%
6	**Willis Towers Watson Invest.**	$100,644	60%	40%
7	**Northern Trust**	$100,464	100%	
8	**Russell Investments**	$95,581	52%	48%
9	**Vanguard Group**	$52,008	84%	16%
10	**Alan Biller and Associates**	$49,003	80%	20%
11	**SEI Investments**	$43,583	41%	59%
12	**CAPTRUST Financial**	$42,920	100%	
13	**NEPC**	$41,332	77%	23%
14	**Bank of America**	$35,019	99%	1%
15	**River & Mercantile Solutions**	$34,400	80%	20%
16	**Aegon Asset Mgmt.**	$34,088	86%	14%
17	**J.P. Morgan Asset Mgmt.**	$33,882	100%	
18	**Strategic Investment Group**	$29,426	100%	
19	**PNC Financial**	$28,868	96%	4%
20	**Meketa Investment Group**	$20,600	100%	
21	**Wilshire Advisors**	$20,409	100%	
22	**PFM Asset Mgmt.**	$17,207	100%	
23	**Sterling Capital**	$15,485	100%	
24	**BNY Mellon**	$14,474	87%	13%
25	**Agility**	$12,033	100%	

*As of Dec. 31

June last year, the momentum for OCIO strategies has been strong," Mr. Philips said, adding "we've been onboarding a lot of new clients, some of which are coming to Vanguard from other OCIOs managers." He said growth was pretty even across defined benefit plans, endowments and foundations.

Vanguard's OCIO AUM managed for worldwide institutions with full/partial discretion totaled $61.9 billion in the year ended March 31, up 40.6% over the previous year.

Among OCIO manager winners in *P&I's* ranking of 59 firms was Discretionary Management Services LLC, Merriam, Kan., which had the highest growth of 409.1% to $1.5 billion in worldwide assets managed with full/partial discretion in the year ended Dec. 31

The high growth rate was from the firm's addition of a new, large client for liability-driven portfolio management. Adam J. Strumpf, senior consultant, declined to name the client in an email.

Hirtle Callaghan & Co., West Conshohocken, Pa., experienced the largest decline — 20.9% to $10.6 billion — in worldwide institutional AUM.

The drop was the result of the firm's recategorization of some assets as non-institutional and the loss of a major client that returned to in-house portfolio management, said a spokeswoman who declined to name the client.

As in prior years, the U.S. OCIO market remains the most important for managers, with 66.1% of worldwide institutional AUM managed with full/partial discretion coming from U.S. clients as of March 31, a slight decline from 67.5% as of the same date a year earlier.

Assets managed with full/partial discretion for U.S. institutional clients rose 20.1% to $1.63 trillion for the year ended March 31 and 87.2% over the five-year period.

Equity returns help

Sources agreed that OCIO growth was strongly buoyed by very favorable performance, especially in equities.

Goldman Sachs' Mr. Braude and other OCIO managers said defined contribution plans had very strong asset growth in the year ended March 31, given the fact that many DC plan participants tend to be heavily invested in equity, and they greatly benefited from market returns in the year ended March 31.

Mr. Braude said Goldman Sachs saw strong client growth from defined benefit and defined contribution plans, endowments, foundations and health-care companies.

The U.S. defined contribution plan segment had the largest AUM growth in the year ended March 31, up 54.8% to $246.4 billion, according to *P&I* survey data. In contrast, OCIO growth for DC plans was only 1.8% over the prior year.

"Individuals in 401(k) plans did see

their assets fall 20% to 30% if they were invested in a lot of equity in the early part of 2020 but gained it back later in the year and into 2021," Goldman Sachs' Mr. Braude said.

The growth in defined contribution plan OCIO adoption is still is in its early stages, but sources said the client segment is poised to boom. For DC plans an OCIO manager is a fiduciary manager.

One driver behind heightened interest in offering OCIO strategies for defined contribution plans is the shrinking pool of defined benefit plans, said Amanda Walters, principal, Casey Quirk, a practice of Deloitte Consulting LLP, New York.

"OCIO managers are looking for new revenue streams as defined benefit plans continue to decline," Ms. Walters said.

U.S. defined benefit plan OCIO assets were up 6.9% to $561.5 billion as of March 31, similar to growth of 7.5% the prior year.

Goldman Sachs' Mr. Braude said "in almost every circumstance when we're talking with a plan sponsor about closing their defined benefit plan, they also are asking about OCIO for their defined contribution plan."

Fiduciary responsibilities

In addition to the benefits of handing off the day-to-day management of defined contribution plans to an OCIO manager, plan sponsors also pass on their fiduciary responsibility for the plan to the manager, said Clinton S. Cary, Chicago-based managing director and head of U.S. delegated investment solutions at Willis Towers Watson, in an interview.

Given that 2020 was "a record year for defined contribution plan litigation, the threat is pushing DC sponsors to consider hiring a prudent expert like an OCIO manager that will assume the role of fiduciary of the plan," Mr. Cary said.

Mr. Cary said his firm and others also are eyeing the enticing opportunity to offer defined contribution plan OCIO services to pooled employer plans created by the 2019 SECURE Act once the Department of Labor provides further regulatory guidance for PEPs.

"PEPs will potentially be a big source of growth for the OCIO industry," Mr. Cary predicted.

Regarding another growing OCIO client segment, endowment and foundation OCIO investors "did better (in terms of performance) than pension funds because of their higher exposure to equity and alternatives," said C. Kane Brenan, CEO of endowment specialist TIFF Advisory Services Inc., Radnor, Pa., in an interview.

TIFF's endowment and foundation OCIO clients' performance was up 25% in the year ended March 31, he said.

TIFF's OCIO assets managed worldwide with full/partial discretion for institutions totaled $7.4 billion, up 12.5% over the year ended March 31.

Total AUM managed for U.S. foundations rose 35.3% to $105.9 billion in the year ended March 31, compared with growth of 32.2% a year earlier. Endowment assets were up 26.3% to $96.2 billion as of March 31, down from 54.9% growth the previous year.

As for the prospects for OCIO managers, "the industry is maturing, and with that comes the usual symptoms, including fee pressure, the beginning of possible consolidation among smaller players and firms closing or getting out of the OCIO business," said Andrew H. McCollum, head of investment management at Coalition Greenwich, Stamford, Conn., a division of data and analytics company CRISIL Ltd.

Mr. McCollum said in an interview he expects continued growth for OCIO firms at 7% to 8% annual levels, adding that OCIO is "one of the few areas of growth in the asset management industry."

But he cautioned "we likely will see shuffling of the deck chairs as investors consider manager changes and it's likely the industry will shrink. In a maturing industry, the number of players always goes down." ■