

What Do Investors Want? Solutions, Not Products

In this article we begin the third part of our [Back to Basics](#) series, aimed at helping asset managers and OCIOs successfully navigate this difficult market environment. The series is organized around our [Golden Circle](#) framework, [described in detail on our website](#). After examining WHY investors should hire you, and HOW can your firm deliver, we now turn to the crucial question: **WHAT do your target investors want?**

Effectively addressing what clients want is the most visible, powerful and yet vulnerable part of the investor-manager relationship. This is also the most rapidly evolving aspect of the investment industry.

Increasingly, what investors want are holistic solutions to help them achieve their investment goals. As a result, the solutions industry is currently experiencing explosive growth. There are many types of investment solutions being offered today, ranging from derivatives-based risk management strategies, value-add advice, multi-asset products and services all the way to fully-discretionary portfolio construction and investment management, commonly referred to as OCIO. In this article, we will focus on OCIO solutions.

The OCIO Business: Heading to \$4 Trillion

OCIO services are the single most rapidly growing investment management segment today. Global OCIO AUA surpassed \$2.4 trillion in 2021, and Chestnut forecasts global OCIO AUA will exceed \$4 trillion by 2026.



Investors Seeking Solutions Turn to OCIOs

As we discuss in our report, [The Widespread Impact of OCIO Growth](#) every asset manager and investment consultant is facing new opportunities and challenges created by the growth of OCIO. In this article we briefly discuss the investor needs driving the desire for more comprehensive solutions like OCIO, this segment's pressing need for standards and improved transparency, and recommended best practices for asset managers and OCIO providers to optimally benefit from the continued growth of this investment market segment.

Increased Investment Complexity Is Driving OCIO Growth

Each time the capital markets experience elevated volatility or another new investment

product, more institutional investors realize they may not be properly equipped to effectively navigate the complex, fast-moving investment marketplace of today.

As we discussed in our recent [Client Experience](#) article, It's more important than ever to be able to customize your product offerings (e.g. guidelines, exclusions, risk exposures) to meet clients' unique needs, rather than offering a one-size-fits-all solution. A fully-delegated OCIO mandate is the ultimate full-service customized investment solution.

Our research clearly illustrates how higher investment complexity is driving investors to seek OCIO services. Investors named governance advisory as the most important factor (tied only with fees) driving their OCIO hiring decision.



OCIO Governance Advisory Addresses a Wide Range of Investor Needs

Institutional boards and investment committees are increasingly seeking expert advice on an ongoing basis regarding how to address a wide range of issues and constituent concerns. Many of these issues come down to establishing investment policies and then setting and managing constituent expectations based on those policies. The most frequently-sought types of governance advisory today include:

- **Portfolio risk/return goals** - OCIOs provide a holistic approach to helping each client articulate a fully customized set of risk/return goals that can be consistently implemented
- **Risk Management** - The range of risks that institutional board members are responsible for today encompass everything from liquidity to DEI standards to Board size and tenure rules
- **Ongoing Capital Markets and Investment Education** - As new asset classes and vehicles continue to multiply, institutional Board members seek and value customized education to supplement their investment knowledge and understanding
- **ESG and DEI Implementation and Measurement** - Investors seek advice on creating and implementing ESG and DEI investment policies reflecting the institution's values and constituent needs

OCIO Is the Wild West of the Investment Industry Today

Although the OCIO and solutions industry is currently experiencing explosive growth, it is currently poorly defined, its capabilities are often misunderstood, and it has little in the way of standards and norms enjoyed by other mature investment industry segments.

Ten years ago, new OCIO searches were mostly conducted on an ad hoc basis, with participants largely selected via personal Board member relationships. Today we estimate approximately half of all OCIO searches are led by third-party search consultants, most of whom are former investment consultants.

All the OCIO search consultants use processes and analytic tools mirroring those used by traditional investment consultants for manager selection. While OCIO fee transparency has improved as a result, the attempt to use performance analytics developed to evaluate single, clearly-defined investment products (e.g. U.S. small cap growth equities) to evaluate whole portfolio outcomes has been an awkward fit for the OCIO industry.

The desire for a custom solution - not a pressing need to obtain outstanding investment performance - is the primary reason investors are hiring OCIOs at a rapid pace, as our research above demonstrates. There is currently no effort to create any commonly-accepted and objective evaluation of OCIO providers' ability to effectively deliver custom solutions that meet clients' needs, however.

There are currently several efforts to standardize OCIO investment performance

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reporting. The CFA has a working group aiming to bring GIPS to the OCIO industry. The new Alpha Nasdaq suite of OCIO indices aim to give investors the ability to objectively measure OCIO performance against peers. The nine different Alpha Nasdaq indices make a herculean effort to reflect the different types of investor plan types (e.g. Healthcare operating reserves) and risk profiles (e.g. aggressive) among OCIO clients. Nonetheless, every single OCIO client is seeking - and paying for - a customized solution.

While performance standards are important, we believe that the OCIO industry has an even greater pressing need for a holistic measurement of client outcomes and provider value. We expect to see much more innovation, activity and investor education on this issue as the industry continues to grow and evolve.

How to Benefit from the Growth of OCIO

The growth of OCIO has created new opportunities and challenges that every asset manager, investment consultant and

OCIO provider must address in order to remain competitive.

We recommend all OCIO providers put themselves in the **Golden Circle**, answering the same three critical questions we work with each of Chestnut's clients to address (and that we have been attempting to answer in this entire content series):

- **What do your target investors want?**
- **How can your firm deliver?**
- **Why you?**

OCIOs should seek to create a strong 'why you' embedded across each element of their growth strategies - product, distribution and investor education/brand. OCIOs have now penetrated every investor segment, from DB to DC, non-profit to wealth management, and everything in between. The needs of each investor segment are quite distinct. Only this client-centric approach enables these OCIOs to develop the trust necessary to raise and retain capital from their target investors.

For asset managers, we recommend they approach the OCIO marketplace as a separate client channel with unique needs, summarized below.

Unique OCIO Needs for Asset Managers to Address

- Trust and understanding are the foundation of any successful asset manager/OCIO relationship
- Understand each OCIO's client base and market positioning
- A strong product rating is just the starting point
- Be prepared to sell and negotiate at a firm-wide level
- The ability to customize products is critical

It is not a coincidence that these OCIO go-to-market best practices highlight many of the same issues we have discussed throughout this [Back to Basics](#) series, such as how investor [Trust is Crucial](#). At most large OCIO providers, portfolio allocation decisions are almost always led by people outside the manager research team, sometimes centralized and at times client-specific. These decision-makers want to engage with asset managers who understand and can help them address the client investing needs they are aiming to meet. Any dialogue with an OCIO decision-maker should consider the impact of a product or sleeve on the broader asset class or portfolio, address how the manager's product(s) and philosophy fit with the OCIO's current portfolio positioning and portfolio construction approach.

In summary, the rapid growth of the OCIO industry will continue as investors seek

holistic solutions to help them effectively navigate the increasingly complex investment marketplace. While the rapid growth of the industry has validated a real client need, it largely remains the 'wild west' of the investment industry, with a pressing need for transparency and a holistic measurement of client outcomes and provider value. OCIO providers and their asset manager partners can most effectively benefit from this industry growth by implementing the best practices outlined above.

Please feel free to contact [Chestnut Advisory Group](#) for more detailed insights on how your firm can benefit from the rapidly-growing OCIO marketplace.

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