



# 20 / 20

## OCIO Performance Standards

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FINANCIAL DUE  
DILIGENCE

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EMPLOYEE  
ENGAGEMENT

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GOVERNANCE /  
RISK MITIGATION

# SUMMARY

The evolution of the Outsourced Chief Investment Officer (OCIO) has entered a new stage – a focus on results.

The evolution of the Outsourced Chief Investment Officer (OCIO) has entered a new stage – a focus on results. The initial stages (producing savings on total direct costs, relieving administrative burdens, and assuming fiduciary responsibility) remain important to an OCIO's value proposition. However, an OCIO's performance results will be an increasingly important aspect of its long-term success.



*Uma Kolluri*

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Investment Consultant  
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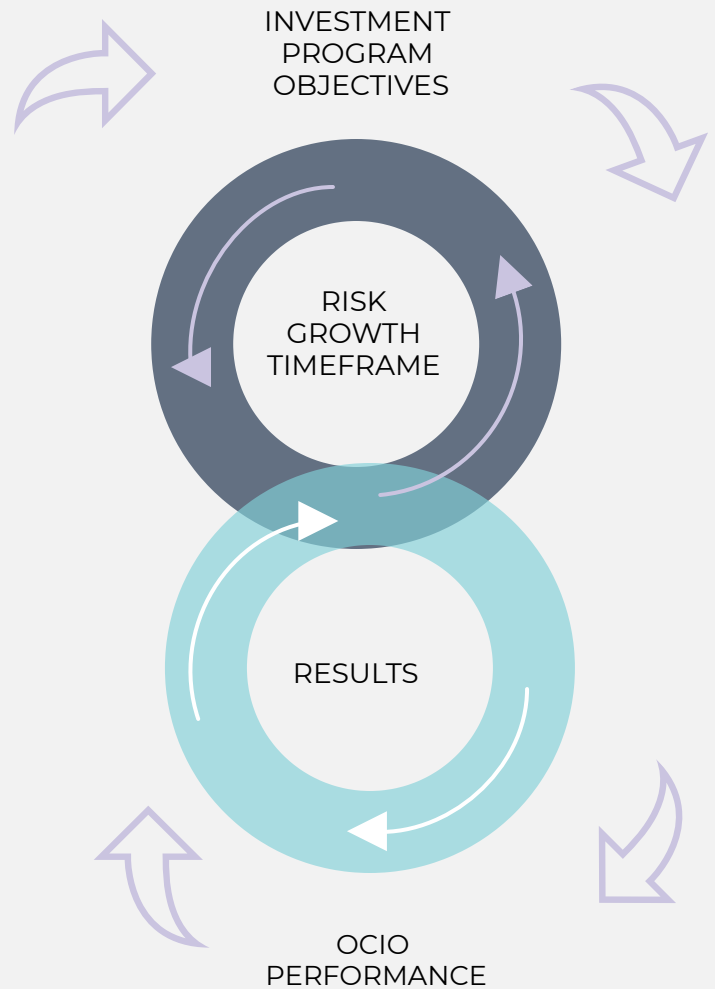
No single investment metric can ever adequately serve to evaluate the wide range of investment program goals OCIOs support.

## The Challenge

# Benchmarking Complexity

Each asset pool has its own set of unique characteristics that require independent evaluation.

Investment committee members and trustees are increasingly interested in an OCIO's ability to help meet spending targets, close a pension funding gap, or assist participants in reaching a financially secure retirement. As a result, confidence in an OCIO will increasingly rest on an ability to review relevant performance results.



An investment program's objective and circumstances are critical to understand before evaluating an OCIO's performance.

PHIL EDWARDS - Curcio Webb



## Heterogeneous Goals

Even within an investment program, objectives vary widely, making it difficult to make comparisons of OCIO performance results.

Endowments and foundations focus on spending objectives, while pension plans may concentrate on minimizing contributions or improving funded status. Total portfolio goals are not relevant to a defined contribution plan. Within each of these segments, there is further variation. Endowment or foundation objectives range from creating income on an annual basis to building capital over the longer term. A pension plan sponsor's definition of risk can take several forms – improving the funded status, controlling funded status volatility, or achieving an estimated return on assets target. Defined contribution plan sponsors are focused on expenses and peer group returns.

### FUND OBJECTIVES VARY BY INVESTMENT PROGRAM

Achieve spending objectives

▼ 50%



Build capital

▼ 33%



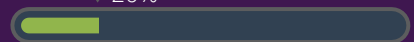
Beat the market

▼ 73%



Minimize expenses

▼ 20%



Manage market volatility

▼ 77%



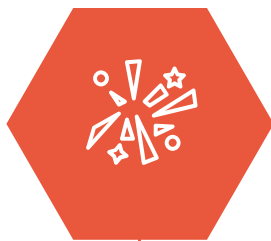


## Challenge #2

# Differing Time Horizons

Market conditions change.  
Fund timelines vary.

Given the volatile market environment in the first quarter of 2020, performance results for the period ending March 31, 2020 can be materially different than the period ending December 31, 2019. The same is true when evaluating annualized (e.g., three-year, five-year and ten-year) as well as annual track records. Each time period can tell a different story. Additionally, investment program time horizons can materially differ. Defined contribution plan sponsors may have less patience for underperformance than a pension plan sponsor or endowment.



### Market Volatility

What were the market conditions during the investment period?



### Investment Time Horizon

What's the length of the investment period? 5-10 years?



### Liquidity Requirements

How soon does the fund need the money?

## Differences in Investment Philosophy

The OCIO's investment approach must be considered.

The OCIO's investment philosophy along with the market environment must be integrated into the evaluation. For example, firms that are willing to position assets opportunistically or hedge market risks will have achieved different track records in the first quarter of 2020 than those who follow a long-term strategic investment approach. (Importantly, we are not trying to judge whether one investment approach is better than another, but whether the selected approach demonstrates an opportunity to contribute to an investment program's objectives.)

## USEFUL BENCHMARKING

Trust and investment committees capture their objectives in an investment strategy which is translated into a benchmark. As a result, Curcio Webb's primary objective is seemingly straightforward - determine whether an OCIO can, more often than not, beat the committee's benchmark (net of underlying investment managers' fees plus the proposed OCIO fees) without taking on excessive risk. But this is easier said than done, primarily because trust and investment committee benchmarks can significantly differ.

For example, the benchmark for a pension plan that is close to 100% funded will be very different than the benchmark for a pension plan that is 80% funded. The same is true for a \$2 billion endowment or foundation as opposed to one that has \$250 million in assets. This requires an ability to understand the investment program's objectives, ask for relevant performance information, evaluate the results, and translate this into meaningful information upon which the investment committee members and trustees can make confident decisions.

## Solution



# COMPOSITE TRACK RECORDS

Curcio Webb encourages firms to adopt (including verification) the 2020 Global Investment Performance Standards (GIPS®), as these provide a combination of discipline and flexibility.

Flexibility is important, as it allows different firms to showcase their performance track records in a light that best reflects their firm's OCIO business. A firm with less than 50 accounts should not be expected to offer the same composites as a firm with more than 500 accounts.

The discipline is useful to understand how the composites are constructed, such as the definition of accounts included and excluded, the number of accounts and the dispersion of returns.

## CREATING CONSISTENT COMPARISONS



### BUSINESS ENTITY

A definition of a distinct business entity determines the size of the OCIO business and composites that can be created.



### DISCRETION

A definition of discretion determines which portfolios should be included or excluded.



### RECORDS

Requirement to consistently maintain information related to the portfolios and performance track records.



### COMPOSITE

All fee paying discretionary segregated accounts must be included in one composite and fee paying pooled funds in another.



### CALCULATIONS

Standards for performance calculations, whether time-weighted or money-weighted.

# COMPARING COMPOSITES

## Flexibility is key to providing consistency

One OCIO firm can have multiple composites that need to be considered individually. For example, an OCIO firm may have asset class composites and an investment program composite. The asset class composites shows outperformance, but with generally higher risk than the benchmark. The investment program composite shows outperformance with less risk. This demonstrates the OCIO's ability to combine managers in a way that optimizes returns and risk. At times, composites may not be sufficient. Interviews with OCIO's to better understand the composites and their components may be necessary to gain a full understanding. For example, a firm's hedging program may have produced weaker results in a year such as 2019, but was entirely consistent with its investment philosophy.

To truly understand an OCIO's performance, composite results must be viewed through a lens aligned with the investment program objectives. Only with this approach can trustees and investment committee members truly have confidence in an OCIO's ability to deliver expected results.

A black and white photograph of a train station platform. A train is blurred in motion, moving from right to left. Several people are standing on the platform, also blurred. The scene is captured with a long exposure, creating a sense of movement and activity.

CURCIO + WEBB

Get started with OCIO

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