



HOW INSTITUTIONS AND OCIO'S ARE EVOLVING FROM THE PANDEMIC

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INTRODUCTION

In many ways, our lives and world will be fundamentally changed by the pandemic. We are living through a real-life business continuity and risk management / stress test environment. As we adjust to the future, now is a good time to consider the impacts of the current environment and look forward and consider what we should be doing with respect to our investment portfolios.

PlanPILOT surveys clients and OCIO firms to gain valuable insights to what institutional investors are thinking about and doing. Within this informational document, we are going to explore a few fundamental aspects of lessons learned that every institutional investor should consider now.

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LESSONS LEARNED TO MOVING FORWARD

REVISIT YOUR LONG-TERM OBJECTIVES

It is OK to be concerned. Pandemic is an unusual event with many unpredictable aspects. Risk = uncertainty of being able to achieve one's goals. Institutions are recognizing now is a great time to review and re-assess their long-term view. Ask yourself some important strategic questions: Has your mission changed due to this pandemic? Have your investment objectives changed? Has your risk/return profile changed? Has your liquidity profile changed?

Most investors appear to be answering these questions no and staying the course. That is wonderful, but there are still likely considerations like those that follow that need to be analyzed more deeply to keep you on path.

Some investors though have more serious concerns. The pandemic will have significant impact to their operations and capital needs. This results in liquidity issues in the short-term, and perhaps sustainability and viability worries for the long-term. These institutions need to engage various internal and external partners to address many of these matters with urgency. **A good OCIO provider can lead your institution through this analysis and help maintain a balanced, forward-looking point-of-view.**

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LESSONS LEARNED TO MOVING FORWARD

REVIEW YOUR ASSET ALLOCATION POLICY & ITS IMPLEMENTATION

In this environment, return and risk assumptions are shifting, return expectations down and risk measurements up, so institutions are reviewing their asset allocation to remain aligned with their spending needs. An OCIO is an invaluable partner in this exercise in providing realistic expectations.

The rebalancing methodologies being employed are varied. The institution needs to be aware of and comfortable with the OCIO's rebalancing plan and timing. Some OCIO's are rebalancing intra-quarter, while others are waiting for the regular quarter end rebalancing cycle. Some are moving slowly and buying on market dips, while others are more regularly moving back to strategic targets. Some are rebalancing broadly, while some are buying very selectively, likely high-quality equities and bonds. Some OCIO's are using option strategies to get market exposure, or ability to move in / out markets quickly, instead of being invested more directly to hedge market risks. Each institution needs to understand and support the plan being utilized by its OCIO.

OCIO's are split between strategic and tactical positioning. Some keep within tight ranges of long-term position targets, while others are making short-term bets on market movements. While most investors probably experienced most of the downturn, some OCIO's were more prescient of the market downturn and de-risked in advance. On the other hand, not being in the markets when they turn upward can be even more costly. Again, each institution needs to be aware of and support the OCIO's strategic versus tactical playbook.

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LESSONS LEARNED TO MOVING FORWARD

The active versus passive debate is also being accentuated. Active managers provide greater value, at least in theory, in limiting downside risks and managing volatility. It is a great time for your OCIO to assess if your active managers are delivering on this promise. If not, manager changes are appropriate, as well as further consideration of the use of passive strategies.

Events like the pandemic certainly provide an impetus to review the use of private and illiquid vehicles. An organization facing operational liquidity issues needs to be especially careful in assessing their liquidity profile.

If you have a pension, it is also a great time to re-visit whether your duration and credit exposures match between your assets and liabilities. If not, significant changes to your funded status are likely to continue to occur. Pensions need to be reviewed to avoid unwanted changes to funding and need for contributions, especially during a time of economic crises. **As can be seen, your institution and OCIO need to be closely aligned on the execution of your investment program to increase the likelihood of obtaining needed outcomes.**

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LESSONS LEARNED TO MOVING FORWARD

REVISIT YOUR SPENDING POLICY

In a crisis like the pandemic, there is often conflict between reducing spending due to lower portfolio values and not wanting to deplete principal too much, versus the need to increase spending due to greater operational and working capital needs. Although we are long-term oriented institutional investors, we also have to accommodate the short-term needs.

Given lowering return expectations and rising risk levels, the ability of portfolios to support spending needs is being revisited. Changes in spending can be painful, if not critical to the future of the institution.

Liquidity needs are being met in different ways. Some institutions, with the aid of their OCIO, maintain short-term reserves for these stormy scenarios. Many base spending on rolling market value averages, which serves to smooth out the peaks and valleys. Many institutions maintain lines of credit in order to be able to continue to support their operating needs. Banks, and OCIO's affiliated with banks, can be a source of needed financing.

In the worst case, an OCIO may need to make asset sales. Certainly, the OCIO will look to liquidate better performing assets, but during serious market downturns these are harder to find. Forced liquidations can be painful and problematic, and can be difficult to accomplish with too high levels of private and illiquid investments than an institution needs to meet its goals. **As illustrated, your institution and OCIO need to work closely to increase the likelihood of meeting your spending needs.**

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LESSONS LEARNED TO MOVING FORWARD

ENGAGE IN EXHAUSTIVE RISK MANAGEMENT

We are living through a real-life risk management and stress test environment. Many OCIO's are already providing risk management services. If yours is, great; be sure to continue. Now is a good time to assess how your portfolio matched-up to these forecast scenarios, and consider whether any strategic changes are needed for future.

If you are not utilizing deep risk management tools, now is certainly the time to engage in exhaustive risk management. Risk modeling means more than volatility measures, like standard deviation. Various other scenarios should be considered for future events, like stress tests, Monte Carlo scenarios, value-at-risk, downside risks, maximum drawdown, etc., in the event of a possible re-emergence of the pandemic or other market shock scenarios down the road. Your OCIO should perform or revisit stress tests, crisis scenarios and potential impact to your liquidity needs. It is critical to understand the possible stresses moving forward from where we exist today.

It is a good time to review performance in more critical ways, too. Performance can be measured in various ways. Absolute performance is likely to be negative during the crisis, but how did it compare to the expected downside forecasts? The management skill of the OCIO can be compared to investment policy benchmarks, as well as industry standard comparisons.

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LESSONS LEARNED TO MOVING FORWARD

The active management skill of the money managers can be compared to stated benchmarks, and to peer groups, to determine each manager's ability to protect on the downside. These measures will affirm whether your portfolio is performing as anticipated, or whether changes may be necessary. This process also affirms if value is being received for the fees being paid.

Performance also needs to be evaluated on risk-adjusted measures, like Sharpe and Information Ratios. These provide assessment of manager skill in employing appropriate levels of risk, but also provide for easier comparison to peers and industry measures.

Your institution with the help of your OCIO needs to assess and re-evaluate the risks, the downside protection provided, and look forward to how future scenarios can be anticipated and planned for more efficiently.

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LESSONS LEARNED TO MOVING FORWARD

DOCUMENT LESSONS LEARNED AND DECISIONS MADE

We are living in an environment that is in many ways unprecedented. This experience will be the subject of finance texts, case studies and history books for future generations. It has been said that those who do not learn from history are doomed to repeat it. Documenting the lessons learned and decisions made is essential to move forward now and to assist future decision-makers.

The primary document for an institutional investment portfolio is the investment policy statement. Investment policy statements should normally be reviewed periodically, usually annually. In this environment, that is especially true. Institutional goals, spending objectives, liquidity needs, asset allocation, return and risk assumptions and expectations, manager oversight criteria, risk measures and downside scenarios and plans, and service expectations should all be carefully analyzed and documented.

The most effective institutional investors and OCIO providers commit significant time and effort on their investment policy statement. This in turn governs future analysis and decision-making. It benefits new trustees, investment committee members and senior management who take on oversight of the investment portfolios.

The most effective oversight teams and OCIO's acknowledge that this stage is the most important by far, and the portfolio management and results assessment simply flow from this.

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LESSONS LEARNED TO MOVING FORWARD

COMMUNICATE WITH DONORS

No doubt your donors are experiencing concern not only about their own professional and personal situations, but also about the livelihood, plans and goals of your institution. True, some donors will not be able to support in whole or in part at the level they may have in the past, while others will be able to provide as much or more support.

Some institutions may be dependent on additional contributions to meet their liquidity needs that may not be met by their investment portfolios at this time. If so, one cannot be shy in asking for assistance.

No doubt we have all been approached or solicited by institutions for support, especially in the current environment. Pro-active and forward-looking institutions are reaching out to their donors to maintain and hopefully expand their relationships. There are still plenty of people and institutions that have the means and the desire to support their favorite causes, institutions, and charities, but you will never know if you do not at least ask.

Most OCIO's provide some level of donor support. Most will be able to educate on market conditions and forecasts. Some will provide support with donor marketing and events. **If needed, your OCIO can be a great resource to assist with donor outreach.**

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LESSONS LEARNED TO MOVING FORWARD

REVIEW YOUR OCIO RELATIONSHIP AND USE OF INTERNAL RESOURCES

It is often said that adversity and real-life experience builds character. Times like these hopefully serve to deepen relationships. If you have an existing OCIO relationship, this is a great time to re-evaluate it. Have you had proactive and regular communications with your OCIO provider? Most OCIO's are publishing market analyses and outlooks in writing and through calls and webinars. Is your OCIO keeping you informed?

Are your mission and objectives still aligned with your OCIO provider's approach? Do you fully understand and accept your OCIO's asset allocation implementation, ability to meet your spending objectives and liquidity needs, and risk management approach? If not, now may be the time to consider a change. Expert search consultants maintain databases of information and deep relationships with highly qualified OCIO's. Getting to know your needs and objectives, and worries and concerns, more fully will allow a consultant to match-up your institution with well-aligned OCIO's.

If you are not outsourcing presently, we expect your internal resources are even more stretched now than ever. Institutions are more pressed than ever to make the best use of their increasingly limited and strained resources. Is now the time to consider outsourcing? An OCIO will provide expertise in asset allocation setting and implementation, assessing and aligning your portfolios with your spending and liquidity needs, intensive risk management, and other resources, like donor education and support. Going it alone is probably not the wisest course of action with the specialized expertise and resources available to you.

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LESSONS LEARNED TO MOVING FORWARD

A skilled search consultant can lead the process to consider a short list of highly qualified and mission aligned OCIO's, and steer your decision making on selection, pricing, implementation, and oversight of the OCIO. Yes, there is a modest cost to outsourcing, but the potential opportunity cost and downside risks of not employing the needed expertise is likely even greater and costlier in the long run.

CONCLUSION

We are living through a real-life business continuity and risk management / stress test environment. The complexity of portfolio oversight is increasing. The risks of neglect and making mistakes is painful at best, and is often critical to an institution's survival.

Now is a great time to consider the impacts of the current environment, and to look forward and consider what we should be doing with respect to our investment portfolios. Partnering with highly qualified experts to lead the process is essential to successful outcomes.

As demonstrated here, PlanPILOT has valuable insights to what institutional investors are thinking about and doing with the assistance of their OCIO's for their investment portfolios. We are pleased to have provided this overview for your consideration. Please let us know how we can be of further assistance to your institution and valuable investment portfolios.

PlanPILOT is actively engaged in providing an objective, independent approach to conducting searches for OCIO service providers for clients with endowments/foundations or other asset pools. PlanPILOT does not provide OCIO management services, we only lead the due diligence efforts over an external provider. Whether selecting an OCIO initially or reviewing an existing OCIO relationship, we lead clients in a RFI or RFP process to best match the OCIO to their institutional objectives, free-up internal resources and satisfy their fiduciary oversight responsibilities for good stewardship.

[Learn More!](#)

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