Managing change

Ben Pumfrett, Head of Product and Profitability, Middle Office - RBC Investor & Treasury Services.

When talking to asset managers, what do you think is top of the list in terms of the challenges they're facing when dealing with their firm's middle and back offices?

The first thing they mention is increasing complexity, both from an operational and a regulatory perspective. Challenges we often discuss include supporting market changes linked to market expansions or new asset classes, achieving scale while balancing costs and managing operating models underpinned by legacy technology.

In addition, in-house operational teams are seeing great demands from the front office, particularly when it comes to the data needed to feed front office decision-making. As such, requirements for greater integration are pushing the middle and back-office teams to perform value-add tasks to support traders and their management team. This additional level of complexity against the backdrop of legacy technology and internal resource bandwidth are challenging the best of teams.

Naturally, individuals are focused on business as usual functions, therefore expecting this additional level of acute expertise in support of a project to help meet these change obligations can be difficult. We often see this as the biggest blocker for projects internally as it can prevent asset managers from moving forward at the speed of change being targeted.

The final point I would mention is the increasingly global aspect of business. Many asset managers we partner with are regionally focused, and therefore being able to deploy a global operating model can be a challenge. However, this pivot is essential to support their expanded investment markets and asset classes, particularly against the backdrop of regulatory reporting and shortening settlement cycles.

All these factors play into how much asset managers can focus on their core capabilities, investment strategies and distribution networks, while also delivering strategic change.

Few organisations, let alone financial organisations such as RBC, operate in an isolated national environment. As you mentioned, managers who expand outside of their home market find they're operating with different rules, regulations and market environments. How does that work in practice?

Market expansion, navigating new regulatory demands and adapting to unique market nuances can be challenging and managers need to have flexibility and deep knowledge of their systems to navigate ongoing changing situations.

We are also witnessing shorter settlement cycles in many markets, which can create more of a challenge when it is time imperative to solve issues. Add to that the penalty regime under CSDR that now crystallises a commercial impact if issues aren't dealt with in a timely manner. There's a compression effect on both sides to ensure transactions settle on time and this time window is only going to reduce further with the plans for other markets to push to T+1.

Some of our North American clients trading in European and Asian markets lose most of their

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working day before they can resolve queries with local brokers. By having an outsourced middle office trade management service and leveraging a global footprint and operating model, asset managers are better equipped to deal with shortened windows or market changes such as the CSDR penalty regime. Having a small window to operate and make changes can be a challenge, more so when there is just a regional operating model in place.

Another area of focus for asset managers is the increased performance and efficiency of their operating model, in particular dealing with brokers and custodians in their time zone and not dealing with matters the next day. A dynamic outsourcing solution can help reduce the impact of queries on teams and increase the client experience by providing greater certainty on the data being used by the front office.

Asset managers are facing some fee compression and ongoing low interest rates at the same time. How do you think they're coping with these wider market-related stresses?

The fee compression we are seeing definitely has knock-on effects on suppliers. As mentioned previously, managers are looking at costs as well as new ways of gaining alpha through new strategies, expansion into a specific region or new asset classes such as fixed income, private capital or derivatives. This focus on getting into other asset classes puts pressure on managers' middle and back-office teams, technology and their ability to support these expansion plans.

As part of this they are also working on how to reduce in-house costs and focusing on the firm's core competencies. This is where outsourcing comes into play which is moving further up the chain in terms of middle office activity and even into execution.

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Being able to move from a fixed to a variable cost base can be attractive and this is helping drive the outsourcing market further. Managers are also relying on legacy technology and know a significant capital investment may be needed to update their technology in support of their ongoing operating model and front office demands. In some cases, they find themselves at a crossroads which forces them to question what they want to achieve and what that next step looks like. For example, do they want to invest in an expensive capital outlay to update systems or can they get access to systems needed at a cost they can manage.

The pandemic has brought this decision point forward on many fronts, because working from home has put a lot of focus on asset managers' operating models in terms of how they work and importantly, their resilience. This has really come to the fore in the past 18 months, with managers not only reviewing how they can meet existing regulatory and front office demands, but also how they can ensure they have a robust operating model going forward.

Everything we have talked about comes back to data: its availability (including timeliness), volumes, data flows etc. As such, it's fair to say a challenge is always data. How do you think managers are coping with those growing amounts of data that they're having to effectively manage?

The demand for decision-making data is clear and ever increasing as is the sheer amount of data that is now available. The challenge is not only access to the data, but timeliness and accuracy of it. Asset managers can become overwhelmed with the level of data and their ability to absorb it. They need to ensure they have the right data and have confidence in its accuracy before it's flowed through the business.

We are seeing much higher demand from the front office for intraday data, especially around cash management. Any asset manager we speak to always brings up cash management as one of the top challenges, particularly where they have multiple providers or custodians, and when they want a consolidated and consistent view of their cash positions. Having a clear view on cash not only assists on being able to more fully invest cash to improve performance but also avoidance of costs or regulatory/mandate breaches from overdrafts.

It's not just about dealing with multiple parties or different formats – it's about trying to manage how they work together, which can be a challenge. When it comes to intraday data specifically, it's about getting the data in order before absorbing it and providing transparency to any exceptions.

This leads to the other key element which is the integrity of the data. Demand for more intraday data is one thing but managers still want certainty over that data, or at least be able to identify exceptions. The ability to have that exception-based view – by this, I mean highlighting data attributes that may be above a certain tolerance level or transparency to the checks performed, so that there's confidence in the data that's going back into the front office – has also been highlighted as a focus area.

We have seen a fair amount of consolidation on the asset manager side recently. How are managers dealing with this as they seek to grow their businesses through M&A?

We have certainly seen plenty of M&A activity. In practice, this means merging the cultures of the two firms, their operations teams, but also possibly different operating models, technology systems, including respective front office systems and risk monitoring. This can also introduce multiple service providers where asset managers all want to get a consistent view of data, be able to check their risks and manage their business correctly on a holistic level. Ultimately, it still comes down to data consolidation and aggregation. In the longer term, it's about integrating technology and operating models to achieve the efficiencies and cost savings targeted via the combination.

There is a balance between being able to maintain control of your business and receiving the benefits from that M&A activity, which means looking towards single platform/single operating models where possible. However, this is time-consuming.

Asset managers will move certain activities first to get some benefits and certainty from a data perspective. They can carry out that data consolidation work with an external provider or in-house. By doing that, they can have a holistic view of their position and then work on the backend plumbing to finalise details. There may be reasons that they aren't able to move out of some technologies, and that can take time to process, so having a data solution that provides that consolidated view allows progression while the back-end consolidation progresses more slowly.

Having data that allows asset managers to have complete oversight provides direct control over their business. However, the challenge as earlier mentioned is that this can be quite time consuming for the asset manager in terms of resources, especially when it comes to back-end consolidation. It's about being able to free the people that have that knowledge away from the BAU. They must find a way to do that if they really are to benefit from the M&A activity and reap the benefits.

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We have discussed the macroeconomic market environment challenges, data and the competitive landscape. In your view, what are some of the options for asset managers to deal with those specific challenges?

Managers can invest in growing their internal infrastructure. There are some considerations in terms of pure capital outlay to update some of the platforms or systems they use. The technology is available but can be quite expensive to access and the process, resource commitment and timeliness to implement these systems in practice is challenging.

The other option is to outsource to a third party. This provides you with access to technology that may be out of your initial capital range and have the ability to move into a more standardised operating model. Historically, during the first generation of middle office outsourcing deals, firms believed their operating model to be a competitive advantage and wanted to leverage providers to run it for them more cheaply. We see that evolving as asset managers now want to use a standard model that runs globally and at scale. There is no competitive advantage in matching a trade or processing a corporate action. Utilising those service provider frameworks, standards and best practice workflows allows managers to focus on their strategic plans and benefit from the experience of external service providers.

However, they must consider third party oversight and how to make the process efficient. When outsourcing, managers don't want to be in a position where they are replicating activity to check that things have been done correctly. There's a real focus on that exception-based oversight, to ensure that they are not spending time identifying issues but resolving them.

By providing clients with the tools and access to be able to identify the important differences, they can focus on resolution and monitoring rather than on identifying or replicating activities to check the work of the provider.

From an outsourcing perspective, we've had some clients who used basic in-house solutions that could only handle cash for collateral management for example. They've looked to us for help, notably in supporting efforts to use securities as collateral. This has freed up a lot of cash balance for them to use elsewhere, and helped them place that cashflow, which was effectively doing nothing, into the fund and into their investment strategy to increase performance. ■

Contact:

Ben Pumfrett,
T.+44 0207 653 4364
M.+44 0754 551 3847
RBC Investor & Treasury Services
rbcits.com