

How has asset servicing changed?

QUINTESSENCE ASKED FIVE REPRESENTATIVES FROM LEADING INTERNATIONAL CONSULTING FIRMS FOR THEIR PERSPECTIVE ON THE CHANGING FACE OF ASSET MANAGEMENT AND SERVICING IN THE WAKE OF THE GLOBAL FINANCIAL CRISIS. HERE'S WHAT THEY SAID

► **QUESTION 1:** Are you seeing a flight to security in the asset ownership/asset management industry and, if so, what are the implications for asset servicing?

NAVIGANT CONSULTING
Mark Lester, director:

There is a flight to security, notably in the areas of collateral and cash deposits. As a result, a greater degree of flexibility and transparency in the servicing model is needed, consistent with a greater demand for the understanding and measurement of risk.

CITISOFT
Howard Mannion, EMEA:

I see this more in terms of a 'flight to quality' - investors are now more aware of risk and some have lost trust in their advisers, which is why the 'safe havens' and boutique managers are doing so well. Financial product providers need to respond by offering new products with high levels of capital protection and the opportunity to generate capital growth and/or income. In this way, they may be able to encourage investors to start investing in the capital markets again.

KPMG LLP
Richard Pettifer, director, investment management industry segment manager:

One of the problems is defining and monitoring 'security'. Brand and reputation don't count for much anymore, and obtaining financial information to monitor the health of an organisation can be difficult. Identification of risk and mitigation through diversification and other means is key.

FUSIONEXPERIENCE
Alasdair Kinloch, principal consultant, alternative investments:

We saw a flight to security last year across all client types. This started with clients moving away from securitised mortgage and loan products, then reducing derivative and alternatives exposure, and finally moving large parts of their portfolio into cash. Some private clients were even requesting 100 per cent gilt portfolios to avoid exposure to banks. However, 'safe haven' assets no longer represent particularly good value, so this position will not last forever.

MERCER
Sonja Spinner, senior associate:

We are seeing a clear flight to security. Clients are asking us to evaluate sub-custodian network monitoring processes, cash exposures to custodian balance sheets, and the security of cash held in pooled fund vehicles. In order to win business, asset servicing firms will have to give strong assurance of the quality of their internal controls and financial strength.

► **QUESTION 2:** What other trends are you seeing in terms of asset servicing and asset servicing consultancy?

Lester:

Asset servicers are attempting to reduce costs and increase efficiency by improvements to the operating model and greater automation. In addition, more costs are being charged directly to funds, thereby reducing the manager's expenses.

Mannion:

Citisoft is seeing an increase in the focus on operational efficiency: this might be by integrating systems, shared services, improved straight-through processing (STP) or other strategic initiatives.

Pettifer:

Asset servicers need to take stock of the increasing levels of risk and responsibility they are carrying. This is a result of much wider use of complex instruments in the investment management industry, together with the increasing geographic dispersal of services around the globe. Asset servicers need to ensure their risk management processes are strong and robust.

Kinloch:

The next few years should see higher-quality servicing and more robust competition. The growth area lies in developing enriched customer experiences.

Spinner:

Investors are keen to generate additional portfolio returns without too much incremental risk. They are actively ensuring that their fee schedules for services reflect current market levels, that FX transactions are being executed within market day ranges and that income is being collected on a timely basis.

“Asset servicers need to ensure their risk management processes are strong and robust”

► **QUESTION 3:** What is the crucial piece of advice you would give your clients?

Lester:

We would advise all clients to keep evidence of why actions have been taken - this is essential in the area of treating customers fairly. Accountability for outsourcing arrangements and the emphasis on personal responsibility by the FSA may lead to greater demand for information such as KPIs. Get there first and lead the process, so you're not producing different packs and figures for each client.

Mannion:

Take this opportunity to reduce your operational costs - revenues, particularly for cash products, will continue to be squeezed for the foreseeable future. However, make sure that your project is properly planned and managed. In times of intense cost pressures, it is all too easy to make knee-jerk changes that result in a deterioration in client service - which has become a major differentiator for firms in these challenging times.

Pettifer:

Ensure the right skills and resources are in place to understand and manage the risks being taken. Be clear on what the client proposition is and make sure that it is being properly delivered.

Kinloch:

Use this opportunity to position yourself for growth. During the last recession, those who increased their customer experience investments achieved an average return on capital of 4.3 per cent, compared with a loss of 0.8 per cent for those who cut. Re-engineer any processes that are not fit for purpose and make sure your systems and platform are scalable across all product lines and able to cope with a return to volume and complexity.

Spinner:

The advice we would give to investors would be to ensure they are happy with the fund manager's in-house or outsourced administration processes by undertaking operational due diligence reviews. Ultimately, investors' assets are at risk if there are inadequate controls to prevent fraud, operational or counterparty risk.

4.3%
Return on capital earned by firms that increased their customer experience investment



Left to right: Mark Lester, Howard Mannion, Richard Pettifer, Alasdair Kinloch and Sonja Spinner