Expert view

The True Cost of Doing Nothing in Asset Management

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First published by Henry Stewart Publications

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Abstract

The asset management industry as previously known has changed forever.

While it can already be seen that a number of asset managers have taken the leap towards innovation, is what can be seen on the surface really preparing them for the future?

Do digital investor portals, environmental, social and governance (ESG) investments and a growing interest in crypto-currencies mean they are digital to the core? And if not, why not?

This paper looks at the key strategies asset managers need to adopt to make sure their investment operations can support the needs of investors, now and in the future.

It covers adopting a long-term IT strategy versus worrying about short-term profit and embracing new technologies like cloud and artificial intelligence (AI) to enhance operational efficiency and transparency across the organisation.

Introduction

For the past two years, the industry has faced a time of unprecedented demands that will ultimately produce new winners and losers.

The pandemic taught people many things and changed the lives of every individual on the planet. While all industries were impacted in different ways, looking at the asset management industry, unarguably one of the key themes was the need for **accelerated innovation.**

The asset management industry has changed forever — while many firms were lagging behind the fast-paced innovation taking place in the banking world, it can now be seen that a number of asset managers have taken this leap towards innovation. But is what can be seen on the surface preparing them for the future? Do digital investor portals, environmental, social and governance (ESG) asset classes and a growing interest in cryptocurrencies mean they are digital to the core? And what about those firms that are still 'waiting to see what happens'?

In 2022, the Boston Consulting Group (BCG) released the annual global asset management report[1], discussing the turbulent shift that the global asset management industry will make towards an inflationary economy, rising interest rates, and global trade disruptions. While turbulent times may be on the cards, this still presents multiple opportunities for the industry, and optimising investments in technology as a core part of their growth strategy, is a key element to the success of asset managers in the future.

As BCG points out[2]:

> The firms likely to be the winners of the future are those that develop strategies to adapt to the changes that lie ahead. Technological leaps played key roles in the evolution of the asset management industry and emerging technologies point to rapid future disruption.

It is not an exaggeration to say that the next big task for every industry player will be to create their growth strategies as they rethink every aspect of their business, from client engagement to investment products. Strategies will be likely to include developing new innovative products for retail investors, gaining an edge in advanced data and analytics and moving to the forefront of ESG strategies for private market portfolios.

But what does this all boil down to?

01 Taking advantage of troubled times

As the medium-term outlook continues to improve, all asset managers must be ready to change, and change now. The pandemic has given everyone a special insight into their own long-term strategies. It is becoming increasingly clear that taking a short-term view of progress based on the increasing quarterly profit sheet is outdated. Instead long-term investments in software and technical infrastructure is becoming vital to remain competitive.

The need to constantly post incremental profits, supplement budgets and cost-cut to keep shareholders happy is a given of modern commerce. However, the impact of these exercises, if being used as an excuse to delay upgrading IT systems, can be that the execution of the long-term IT strategy is constantly being postponed to the detriment of the company's performance.

> **But companies can no longer put their medium and long-term profitability at risk for short-term cost savings.**

The trigger for change is too often after a significant event has occurred, especially when customers or

brands (regulatory) have already been affected. It is now important for the industry to change and quickly embrace the new world.

Cloud adoption in particular gained significant new ground and acceptance during the pandemic largely due to the switch to remote working, with most financial services firms reaping the benefits of cloud data hosting. Some recent lessons were learnt on the dangers of on-premises data centres when, due to COVID-19 restrictions, one German bank was prevented from accessing their data centre to switch code when a server malfunction occurred.

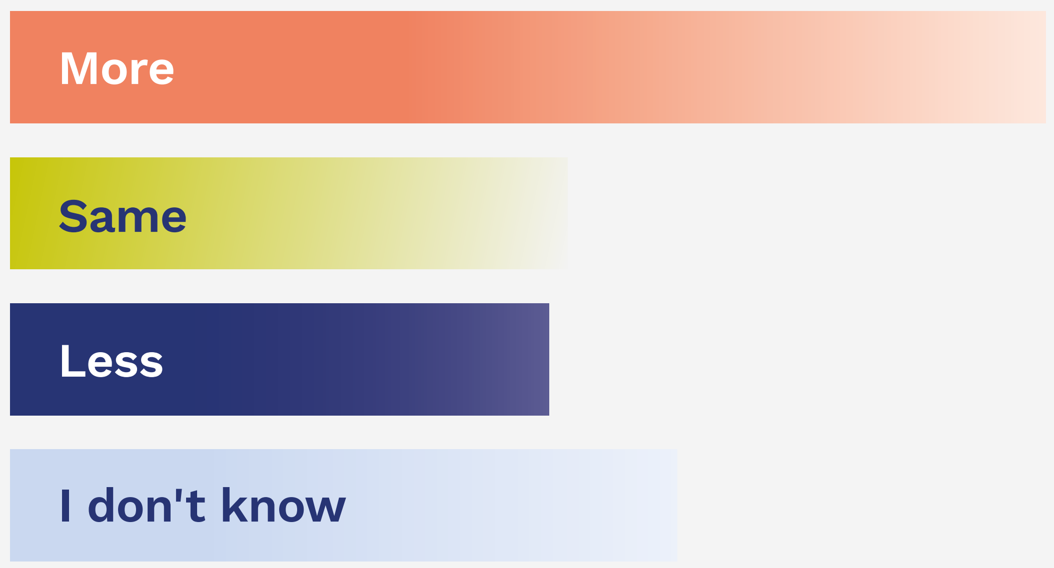
> Asset managers must be ready for the cloud and carefully monitoring all new technologies, including AI, blockchain and others.

For many, investment in new technology has begun with the low hanging fruit, typically robotic process automation (RPA), with one of the biggest impacts being the decreasing reliance on offshoring. Historically, investment operations were very labour-intensive but with new levels of automation increasing straight through processing (STP), and evolving AI models, there is huge potential to move away from offshoring and only retain staff who are process experts or accounting experts. Why those roles?

> Because real experts are needed to face auditors, regulators and clients, who do not want to speak to a call centre or a Bot. They want real people with a deep understanding of the business process.

In a recent survey of investment professionals it became clear that AI models are either well established or increasingly important for a growing number of asset managers, with 47 per cent indicating they will maintain their current investment levels or increase investment over the next 12 months (Figure 1).

Figure 1: What level of investment does your business plan to make towards AI in 2022?



Even shortly before the pandemic, Forrester Research said in a report[3]:

> As customers embrace online banking and new digital disruptors, banks must ramp up their digital transformation efforts or face irrelevance. However, for too many, digital transformation is seen as a series of one-off projects that are delivered late and over budget, creating a spiraling technical debt that limits updates and cripples longterm value. To break this vicious cycle and empower digital transformation at scale, banks must invest in banking development platforms that enable the development of fast and flexible services.

A banking development platform must be quick and easy to update, simple to maintain, secure by design and easy to extend. An essential, key to success is how these platforms are designed and architected.

Forrester maintains that while conventional thinking dictates that internally- developed platforms deliver greater flexibility at lower costs, actual results from transformation efforts show otherwise.[4]

> **Technology decision- makers must abandon the traditional 'buy versus build' mentality, and instead adopt a 'buy, build, extend, and assemble' approach**

to creating a banking development platform that takes full advantage of the benefits of commercial components where possible.

The same goes for asset managers.

02
A confident investment landscape

Economic recovery is not straightforward — it is often a messy and intricate process, full of highs and frightening lows. Take the global financial crisis. As an example, according to a recent Alt-Fi Wealth Report,[5] although the UK's recession post-crisis lasted just five quarters (the UK COVID-19-related recession lasted for six) and the stock market bounced back to prefinancial crisis levels within six years, the lasting economic impact was still felt almost a decade later. For people in the UK, their average weekly regular earnings only surpassed their pre-crisis peak (adjusted for inflation) during the final quarter of 2019 — 12 years later.

COVID-19's lasting impact on the economy and personal finances is set to be a similarly messy long-drawn-out affair, with many questions still unanswered. How long will the behavioural changes of the past 24 months last? Will the legacy of COVID-19 on people's investing habits be one of caution, or confidence? When will people's finances return to their pre-COVID-19 norms, or will they ever? If not, what is the right direction for the digital asset management industry?

A significant minority, according to the Alt-Fi report[6] (8 per cent, versus 3 per cent in 2020) now class their personal finances as having 'improved a lot' in the period following the worst of the pandemic. A declining number of people with deteriorating finances is also seen. Fewer than a third (27 per cent) now say their finances have 'worsened', down from 35 per cent in 2020. This has continued to drive saving and investing. Overall, people have been putting more money into their savings accounts and pensions during the last year — additionally there has been a rise in account openings.

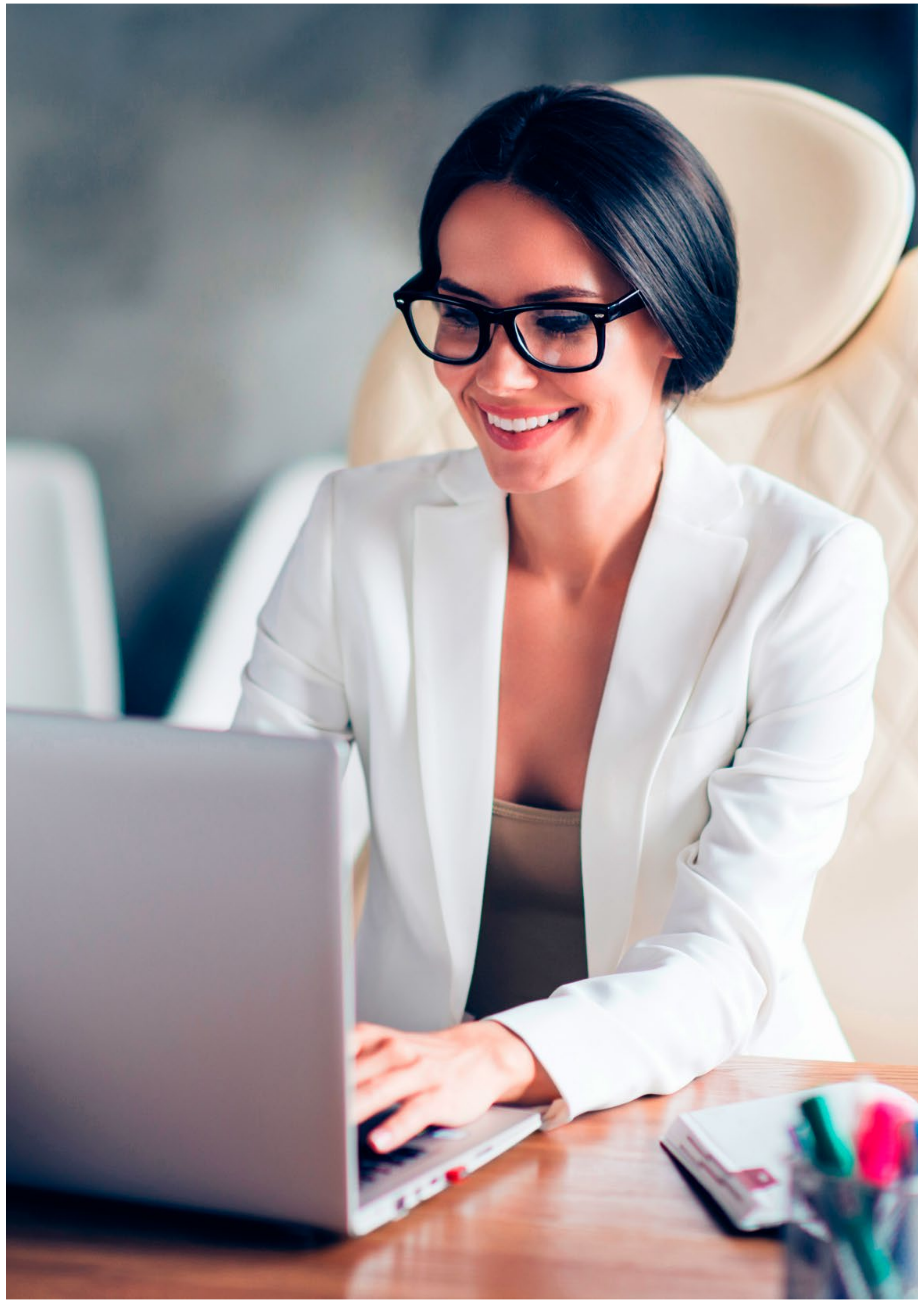
Alt-Fi's key takeaway from this was that people seem more confident, especially in riskier investment decisions, in comparison to the takeaway the year before when people were taking the time to reorganise, refocus and reassess their finances.

The new-found confidence for many investors led to 14 per cent of people investing in heavily volatile cryptocurrencies and two-thirds of respondents looking for ethical investment options.

This growing interest in new asset classes, new geographies, cryptocurrencies, ESG and more meant many asset managers adapted their portfolios and investment strategies. But while the front office may be getting excited about new products, the back office is often not ready. Many back office operations teams are still methodically replacing the pieces of the puzzle, one after the other.

Instead, the industry needs to invest in putting a framework in place so that all of the disparate elements of front, middle and back office can talk to each other.

That in itself requires sophisticated API frameworks and carefully thinking about the broader ecosystem they need to build to meet their evolving client offering.



03 The technology decision

Which technologies will be relied upon? Should everything be in the cloud? What are the cloud requirements? Should everything be in the same cloud or will there be a multi-cloud or hybrid approach? Has AI already been invested in? Is blockchain on the roadmap?

Back-office operations and in particular areas like fund accounting are not the areas that attract innovation often. This is usually focused on the front office (market-facing, end-client engagement, distribution channels and investment decision making).

> **But the lack of innovation in the core means the whole industry is running on legacy infrastructure built in the 1990s.**

Perceived as the 'boring stuff', fund accounting, tax accounting and some other things means there are no start-ups entering the market to force the pace of change in the same way that has been seen in the front office, with Robo-advisory for example. But it is essential. Clients, auditors and regulators all rely on the data.

> **And with new regulation always on the horizon, such as the FRS in the UK, it cannot be assumed that just because people have accounted for their investments in the same way for 20 years that they will continue to do so for 20 more.**

It is essential that asset managers plan for the future and interpret these guidelines in line with their Target Operating Model and their transformation programmes.

Can asset managers clearly show from their strategies where they are going?

04 The challenge for many asset managers

All too often, when a longer- term plan is placed before management, there is a temptation to postpone it for budgetary reasons. The second issue is that if the board comes back for more cost-cutting, is that because they had not fully bought in to the plan? And if more budget is required to execute the plan, what challenges will be faced without that leadership buy-in?

> **The contradiction between a long-term strategy and the short-term will have to be resolved. There is no point continuing to defer the investment, thinking that some savings will be executed in the short term.**

At this point it must be asked whether the board truly understands or simply does not buy into the strategy. And actually, it is true, savings are being made for the quarter. But the situation is also being made worse for the years to come. In addition, if the systems are not updated now, then stress is placed on the medium-term profitability for immediate savings.

Figure 2: What is the biggest risk of delaying change?

In the same survey referenced previously, investment professionals were asked what the biggest risk of delaying change was (Figure 2). Becoming uncompetitive was the biggest risk, with quality deterioration and increasing risk of errors following closely behind. Is that a risk asset managers are really willing to take?

Despite the fact that asset managers have been forced to plan major changes, because they are facing huge operational risk and potential catastrophic IT security breaches in their current systems, they find that their plans often come to a halt just at the point of no return.

Suddenly they are asked to leave major IT investment for one more year — 'work with what you have. You can add a few more Excel spreadsheets to accommodate for the new requirements, and we can make it work. Let's wait another year'.

The problems then start multiplying when the entire solution is working on a stretched database that is not properly supported. Imagine, for instance, that an IT security breach is discovered in the code or in the infrastructure that is running it and the risk to the business is unknown. This is a big catalyst for change. Suddenly the problems become critical, must be fixed and the upgrade cycle is pushed into place so quickly that requests for information (RFI) and requests for proposal (RFP) are issued to a selection of service providers. Somehow the deal is closed in just a few months, when usually there would be time to make choices based on the long-term strategy, rather than another short-term fix.

Asset managers need to push their boards to realise that they need to invest with wisdom and speed. It is understood that return on investment needs to be quicker. Nobody thinking of investing in something that has 10 or even five years' return on investment does so without trepidation. But three to four years from now many asset managers will have been left behind in the march to digitisation.

They need to replace the pieces of the IT infrastructure puzzle but with new pieces that are radically different to the old ones.

> **What is the best way to do this? The answer is to strategically plan a roadmap where each stepping stone represents changing one application at a time, but with the introduction of a series of unique APIs so the receiver can communicate with the new puzzle pieces, but also those replaced in the future.**

05
Innovate the essentials

While a lot more innovation and new solutions in the front office space continue to be seen when it comes to technology and investment strategies, the essential systems enabling asset managers to value, support and deliver day-to-day, need essential investment, and need it now. While processes like fund accounting might not get many as excited as new distribution apps or Robo-advisory, what it will do is prepare for the future, reduce the total cost of ownership (TCO), reskill employees and ultimately, most importantly, enable the provision of new products and services to clients, to always stay ahead of the competition. The true cost of nothing is losing clients, reputation and business.

> Do not wait until it is too late to change.

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Learn more about Temenos Multifonds and how you can transform your investment operations

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About Temenos
Temenos (SIX: TEMN) is the world's leading open platform for composable banking, creating opportunities for over 1.2 billion people around the world every day. We serve two-thirds of the world's top 1,000 banks and 70+ challenger banks in 150+ countries by helping them build new banking services and state-of-the art customer experiences. The Temenos open platform helps our top-performing clients achieve return on equity three times the industry average and cost-to-income ratios half the industry average.

About Multifonds
Specialists in asset servicing and fund accounting software for over 25 years, Temenos Multifonds is a single global platform used to manage over 30,000 funds across 35 jurisdictions – encompassing all asset classes and fund types, from traditional mutual and UCITS, insurance and pension funds, as well as alternatives including ETFs, hedge funds, and private equity. Our extensive experience within the industry has led to our recognition as a trusted partner by leading institutions around the world to administer, service and value assets for their global client base. Our solutions include an integrated Investment Book of Records (IBOR) and Accounting Book of Records (ABOR), along with highly sophisticated workflow and XAI-enabled exception-driven processing, which improves the efficiency of fund operations across both middle- and back-office functions across the board – including more focused asset managers who may require just a single NAV per day, to complex, multi-jurisdictional asset managers who require multiple IBORs and NAVs across different time zones and stakeholders.

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