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The path to operational excellence: revolution or evolution?



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Achieving greater operational efficiencies has never been more critical. Managers that keep a cool head when approaching digital transformation and can identify the strengths and weaknesses in their operations and then invest in new solutions where needed, will be the ones who bring true operational excellence to their businesses.

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The path to operational excellence: revolution or evolution?

As asset managers seek out greater operational efficiencies across their businesses, Ed Gouldstone of Linedata sets out why evolution, rather than a complete systems overhaul, is often the best path for success

With the onslaught of regulation that followed the financial crisis, asset managers have had little bandwidth to focus on upgrading their IT infrastructure. Now that the dust has settled, digital transformation is firmly back on the agenda. Increasingly, fund houses see achieving greater operational efficiencies as a vital way to deliver value for their clients in a period of mounting uncertainty.

However, recognising the need for digital transformation is seldom the problem. Most of the asset managers we consult with, see the drastic efficiency-saving benefits that digitalisation can bring but are unsure of the right approach to take.

The hype surrounding the disruptive technologies that have emerged in recent years—from artificial intelligence (AI) to cloud and distributed ledger technologies (DLT)—may make it seem like firms are confronted with a black and white choice. That is, either they take a revolutionary stance by doing away with their old systems entirely. This means they risk losing aspects which are already working and they continue to patch their existing architecture without experiencing the desired efficiency gains.

In reality, the choice is far less binary. And while disruptive technologies may deliver value over the long-term, they are not the silver bullet they are sometimes purported to be. Industry leaders are therefore prudent not to make sudden wholesale changes without due consideration.

The key to successful digital transformation is not just fixing old systems and achieving base-level operational

efficiencies. The goal should be true operational excellence—optimising processes across the entire organisation to deliver sustainable efficiencies and cost control while supporting business growth and revenue-generating improvements.

Standing still is not an option

Achieving greater operational efficiencies has never been more critical for the success of the asset management industry. Fund houses are being squeezed at both ends, facing rising costs and pressure to reduce fees. Recent research by McKinsey found that profits for European and US asset managers fell by 2.4 and 3.3 percent, respectively, last year. Furthermore, the costs of running investment businesses increased by 8 percent in 2017, and Western European asset managers have experienced a 72 percent rise in total costs since the end of 2007.

In this context, automating and streamlining workflow processes is imperative to drive down costs and boost shrinking margins. However, back-end operations are at breaking point. Built-up over many years, and exacerbated by mergers and acquisitions, most firms are trying to soldier on with a patchwork of 'Frankenstein systems' that are rife with issues. Reporting requirements, order management, compliance checks, due diligence and internal accounting are often all run on different platforms. This creates a complex, and not always synthesised, web of IT infrastructure which often faces compatibility problems.

Such fragmentation means that a lot of manual resources must be allocated to keep these disparate

systems up and running. Teams of people are doing highly repetitive tasks when automation is key to efficiency.

Furthermore, disconnected IT architecture decreases the ability to extract and aggregate the necessary data to streamline operations, generate reporting, address regulatory compliance and make smarter business decisions. For example, different systems in different regions make it difficult to get an aggregate view of holdings exposure and risk at a global level, increasing data management overheads.

These problems can seem so insurmountable that many firms have resorted to 'workarounds' in order to get the job done, but inevitably these tactical solutions become 'strategic' solutions as other priorities arise. This approach is clearly unsustainable. In addition to creating massive costs, such measures prevent asset managers from achieving the efficiency gains they require to safeguard the future prosperity of their businesses.

Taking an evolutionary approach

To ensure that a digital transformation programme successfully resolves a firm's operational inefficiencies, those driving change must take a strategic approach rooted in achieving the desired short- and long-term results. Critically, this involves developing a plan and roadmap that focuses on simplifying systems architecture and leads to more effective management and use of data.

Asset management firms should start by understanding what is working well, what is not, and should start fixing those parts that are not. The solution, therefore, is two-fold: understanding, either through internal or external auditing, which systems are not adequately supporting operational efficiency and enabling future business growth, and secondly, replacing these with new, modular and flexible solutions that are compatible with the rest of the system.

That was the thinking behind Linedata Optima, an advanced workflow management tool designed specifically to optimise fund administration. It runs

off existing core systems—which have been used by fund managers for many years and continue to serve their purpose—and delivers operational excellence by digitising processes and business controls, surfacing data through an application programming interface (APIs), providing unrivalled transparency and interaction and allowing firms to streamline and automate repetitive processes.

This approach stands in contrast to the 'rip and replace' model that is sometimes driven by the narrative surrounding disruptive technologies. The most obvious example of this is the push in some quarters of the industry to onboard DLT systems. These can be very expensive—running into the tens or even hundreds of millions in some cases—for a technology that is untested in asset management applications and may take a decade or more to deliver a return on investment.

Ultimately, before undertaking large-scale technology projects, firms should clearly define their goals and expected benefits and choose a path that lets them test assumptions incrementally. Will this technology work for my business? Will it improve my client and regulatory reporting? Can we reduce turnaround on our net asset value production?

In some cases, a fundamental restructuring of system architecture is necessary to achieve the desired results. Yet even then, organisations should structure their transformation journey in stages to achieve meaningful near-term benefits, measure performance against expectations and adjust course as necessary to achieve their ultimate objectives. Clear, honest internal communication is critical, so members of staff understand why changes are being made and how these will benefit the organisation in the long-term.

Leveraging data for advanced analytics

Data is the lifeblood of every asset management organisation. Regardless of the chosen system architecture path, a sound data strategy lays the foundation to leverage machine learning and data analytics for even more advanced efficiency gains.

It is well known that AI and machine learning's capacity to analyse vast sums of market data can aid better-informed front-office decision-making, but these technologies can also have widespread applications on the operational side.

Indeed, our recent research into industry adoption of AI revealed that a quarter of asset managers identify back-office functions as the area of their business that stands to benefit the most from its application.

A wide array of routine processes, including trade validation, reconciliation and exception management, currently require significant human intervention. However, a large proportion of these activities do not involve complex decision-making and can readily be automated.

An additional application, which we have incorporated into Linedata Analytics Service, is the capacity for machine learning to reduce operational risk and support compliance. This service takes operational data about market transactions and other events that have previously resulted in losses and compliance issues and combines it with broader market data. Using this enhanced dataset, we build a machine learning model that identifies and tests for patterns that indicate when errors are more likely to occur. Delivering these insights to the client's operations team enables them to take preventative action and avoid potentially costly and damaging incidents.

Future-proofing systems

An important consideration is how to future-proof systems architecture, enabling ongoing advancements while readying a firm for the next wave of innovation.

By taking the modular approach discussed, and using technologies that are fully API-integrated, organisations can add and retire applications with relative ease.

On top of this, having a single user interface to bring it together makes a business more flexible. Getting the user interface and user experience right gives managers a more holistic understanding of their business and allows them to maximise operational efficiencies while

changing things seamlessly under the hood, therefore minimising business disruption.

Beyond the technology itself, managers should carefully choose the right vendor to support their business as it scales.

Working with a global provider can help firms roll out solutions worldwide as well as bringing a level of local and institutional knowledge to the table concerning evolving regulation, asset classes and cultural practices—a key advantage when firms are pushing into new markets.

Managers want to equip themselves with the right IT systems that allow them to achieve their goals, keeping pace with technological innovation while helping them improve productivity across their businesses. Indeed, with increased emphasis on fees, mounting economic pressures, and continued geopolitical uncertainty, the incentive to boost margins remains strong.

With this in mind, managers that keep a cool head when approaching digital transformation, and can identify the strengths and weaknesses in their operations and then invest in new solutions where needed, will be the ones who bring true operational excellence to their businesses. By achieving that, operational technology no longer forms a barrier to business evolution and growth but becomes the foundation of its success.

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