Jay Tikam,
Managing Director,
Vedanvi Ltd.

Amit Vij,
Head of Business Development,
Capital Markets,
WNS Global Services

Neelesh Pal,
Lead Consultant,
WNS Global Services

Three Trends Shaping the Asset Management Industry, and How to Capitalise on Them

vedanvi
Risk & Regulatory Consulting

WNS
Extending Your Enterprise


FINANCIAL REPORT
3.45
2.58
6.58
12.3
7.42
8.52
6.47
5.42
0.58
6.02
3.56
7.43

Three Trends Shaping the Asset Management Industry, and How to Capitalise on Them

Jay Tikam,
Managing Director,
Vedanvi Ltd.

Amit Vij,
Head of Business Development,
Capital Markets, WNS Global Services

Neelesh Pal,
Lead Consultant,
WNS Global Services

After analysing the disruptive trends that can potentially transform the asset management industry, WNS recommends suitable response strategies to counter these trends and enable the industry to stay profitable

Introduction

The economic meltdown of 2008-09 caused major upheavals in the financial services industry, not seen since the 1930s. As banks were seen to be the major catalysts of the crisis, they were first in the firing line, and subjected to higher levels of regulatory scrutiny.

It appeared that asset management companies emerged relatively unscathed through the crisis. That was until now. After introducing stricter regulations to straighten out the anomalies in the banking sector, regulators have now trained their guns on the asset management sector to pre-empt any systemic risks impacting the global financial services market. That's because, asset managers have begun to step in to spaces where banks are de-leveraging, post the crisis. This is evident from the fact that the UK's alternative finance sector has grown from GBP 267 Million in 2012 to GBP 1.74 Billion in 2014. Investments of asset management companies in alternative finance are growing at a CAGR 10.7 percent per annum compared to 6 percent for traditional investments. Understandably, regulators are concerned about the emergence of 'shadow banking', which can possibly lay waste the efforts of regulators to bring the financial system back on the rails.

However, if asset managers are under the impression that regulations are the only challenge they need to mitigate, there's news. Technological advancements and changing customer behaviour are influencing the asset management industry, in ways that were never seen before.

We explore three major disruptive trends, and suggest the best responsive strategies to not only counter, but also to capitalise on these trends.

New players (big or small) bring a faster, more efficient and cost effective product, service, or an innovative delivery model. That's because these players are better than the incumbent ones at identifying and meeting changing customer needs

Trend 1 - Digital Disruption Bringing Structural Changes in Business Models

Technology-led disruptive innovation creates new market demands and disrupts incumbent players, who can't respond as quickly as the newer and more nimble, tech-savvy entrants. There are plenty of examples around us. Uber disrupted the taxi business, Air BnB disrupted the holiday accommodation market, and iTunes, disrupted the music world.

Nutmeg.com is a classic success story of a company stepping in to fill the needs of a technology-savvy customer base. This London-based online investment management company started its operations in 2011, and is set to acquire 100,000 customers. The online wealth management portal has brought cheaper pricing, simplicity and transparency to the world of investment management. In contrast to traditional players, they have a simple fee structure, ranging from 0.3 percent to 1 percent of assets under management. For this fee, its customers get a fully-managed investment portfolio.

Asset managers are equally vulnerable to new disruptive entrants who are altering the industry landscape and grabbing customers and market share. Customers, especially the Millennials in the age group of 18-34, want change. A 2015 Salesforce study has thrown up interesting insights:

- Millennials prefer to take things in their own hands when it comes to their investments. They rely more on online reviews and peer recommendations than the advice of financial advisers. Their Baby Boomer counterparts (age 55 and above), on the other hand, depend on a mix of online reviews and financial advice for making their investment decisions
- Millennials have very little tolerance to standardised and traditional fee structures and outdated financial models

On the lending side, peer-to-peer lending and crowd-funding have revolutionised the way personal and small businesses are financed in the UK, and across the globe. In the UK, peer-to-peer lending has seen nearly 200 percent growth rates year-on-year.

Initially, banks dismissed such financing activities as a passing fad. But banks are now finding the new market entrants snapping at their heels. The fact that in 2015, Goldman Sachs and Hargreaves Lansdowne announced plans to launch some form of online lending platforms gives us a glimpse of how even banks are entering the world of alternative finance.

Response Strategies to Trend 1

1. Raise Awareness

Disruption is not yet widespread in the asset management industry. So executives, who often have more pressing and immediate priorities to deal with, may not think of the impending disruption as an urgent necessity. Proactive planning is impossible without the right level of organisational awareness, especially at the executive level.

Asset management companies should establish frameworks to spot potential disruptions and create innovative strategies to counter them. An impact assessment strategy should form a key part of stress testing and scenario

2. Segment Clients and Serve their Needs

Client satisfaction is always a key business imperative. To better understand clients' needs, asset managers can segment their client base into those who require personal attention vis-à-vis those who prefer a self-service model. According to the Salesforce study, Generation Xers (age 35 to 54) and Millennials (age 18 to 34) prefer greater independence in making their investment management decisions. Even if they do decide to work with financial advisors, they prefer a collaborative and participative approach. Baby Boomers (age 55+) prefer the advised route, with some delegating all their investment decisions to advisors and fund managers.

Those clients with a preference for self-service models tend to opt for cheaper tracker funds. They are savvy researchers who find and evaluate investments on their own, and are also more willing to venture into alternative types of assets to reap higher returns. Instead of favouring one asset manager, such clients spread their investments across multiple platforms, bringing greater diversity and security to their

It is considered a best practice to conduct focused discussions with external experts to understand the evolution of the market within the context of the business model

assets. To respond to these types of clients, assets managers can:

- Re-focus strategy and operations for a more intimate and direct engagement instead of heavily relying on the advised route
- Lower investment barriers and allow smaller clients to try out cheaper index-based or algorithm-based "robofunds"
- Allow such clients to consolidate and analyse their portfolio, and provide investment tools to easily create and execute their investment strategies
- Facilitate interaction among fellow investor clients by creating communities and forums. 'Social trading' empowers individual investors to build and share investment strategies and portfolios with other investors

High-touch, high net worth clients can receive a more personalised service at higher fees. Technology can also be leveraged, but not necessarily substitute personalised service. For example, a financial adviser can offer a self-service client the option to make investments, or provide advice, via a mobile phone application. Bespoke research, tailored specifically for each individual client, can also be a differentiator to enhance high net worth client loyalty. The research can also capture key investment trends based on insights from Twitter feeds of analysts and investors.

3. Re-align Business Models and Business Relationships

Many asset managers may not feel threatened by the new disruptive players starting to invade their sector. After all, asset managers are expected to manage risks. However, the rapid growth of the alternative finance sector has taken asset managers and bankers by surprise. While the volumes of alternative finance are still low, a growth rate of 200 percent per annum is alarming. No wonder, the European Central Bank (ECB) has decided to classify all investment funds as 'shadow banks', signalling the need for regulatory focus. On the other hand, banks are feeling threatened because they are now competing for the same client base.

Even regulators are now becoming concerned about the changes that alternative lenders can potentially introduce into the financial system.

Asset managers have to radically re-think their business models to anticipate and proactively respond to the impending disruptive changes brought about by alternative lenders and the resultant regulatory changes. Some of these strategies can be:

- **Widening the base of the customer pyramid:** Asset managers can focus more on the mass affluent market without diluting the quality of service delivered to the high net worth client base
- **Blending human intelligence with technology:** Customers trust technology more than human advice. So logically, asset managers should focus on what they are good at – creating investment management products and distributing them through technology providers such as Google, Amazon, Facebook, and LinkedIn
- **Partnering with new players:** New players, such as Nutmeg.com, attract a new breed of wealth management clients, who are averse to making investments through traditional players and their methods. Even if they do, they may only invest a smaller proportion of their funds. To tap into this market, asset managers can partner with newer players by white-labelling their products and delivering them on a technology platform. The newer players are likely to agree to such tie-ups as they may not have the scale and experience to create such diverse products

Trend 2 – Complex and Frequent Regulatory Changes

Regulatory compliance is a key business imperative in the financial services industry. Some asset management companies operate across different countries, which impose different regulatory mandates. According to Thomson Reuters' research, on an average day in 2014, 155 regulatory updates were issued by regulators globally. That amounts to a staggering 40,603 updates per annum. The updates take on many forms, including rule book updates, regulatory announcements, policy papers, speeches and enforcement notices.

Every regulatory update can have an impact on the business. Asset managers and compliance teams need to be cognizant of each update, understand and interpret its impact, and embed the update in the compliance process of the business. It's a tough task, and one that can easily pass under the radar, simply because of the volumes involved.

In addition to the updates, numerous new regulations emerge in the asset management industry. Each new regulation necessitates implementation of a complex, large-scale, multi-year change program.

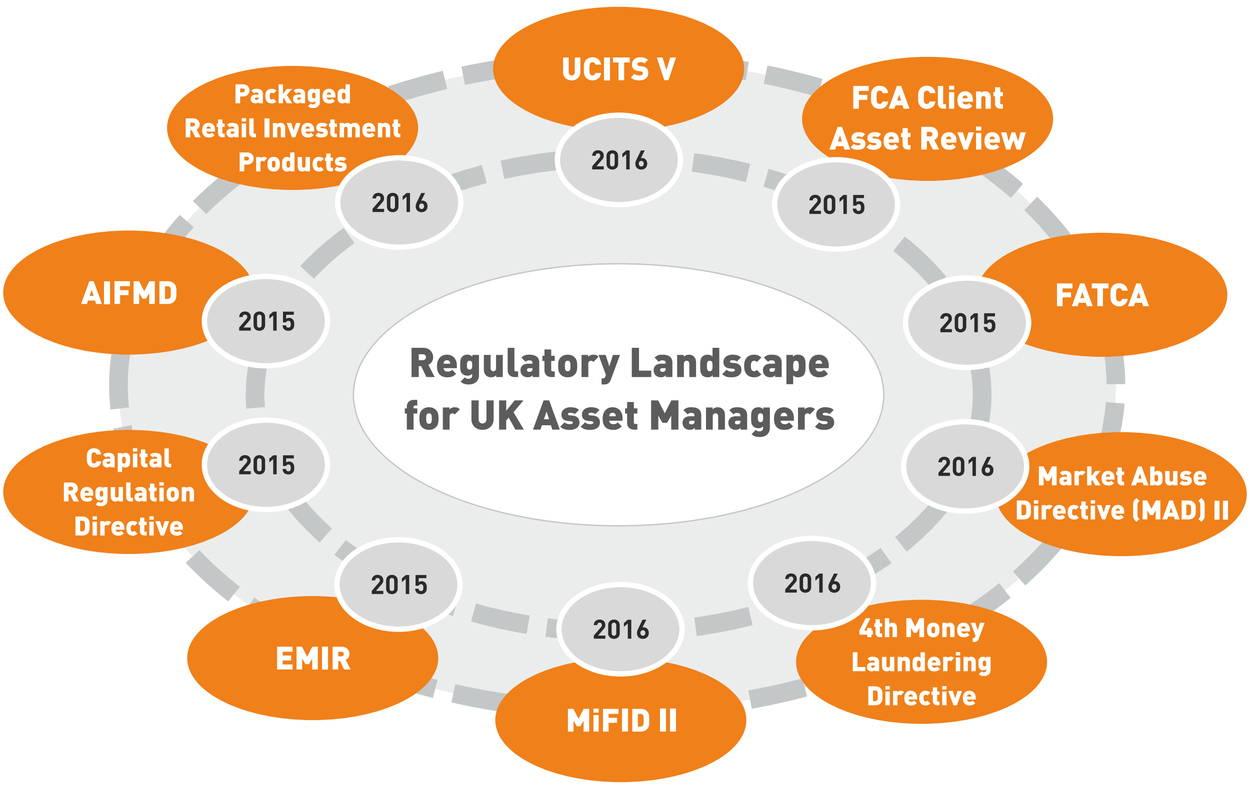


Fig 1: Current and upcoming regulatory mandates in the UK

Companies are likely to incur increased costs due to the time spent by compliance teams to compile information on monitoring and regulatory reporting

There is a growing shortage of skills to monitor and manage compliance as the demand increases amidst a shrinking supply of talent

Impact of Regulatory Change

- The extent of regulatory change is one of the most significant challenges. Asset managers need to address the impact in a way that not only ensures compliance, but also enhances operational efficiency, competitive advantage, and facilitates geographic expansion. But what exactly are the implications of extensive and frequent regulatory changes in this sector?
- More strain on existing resources to manage changes arising from the regulatory burden – revenues may be dented, or the organisation may be exposed to operational risks
- Difficulty in remaining competitive in certain geographies, necessitating a re-alignment of the business structure
- Discontinuing certain product types as they become uneconomical to the business
- Revamping client on-boarding and current management processes

Most importantly, new regulations compel large scale changes in information technology systems, methods of working, and in the organisational culture.

Response Strategies for Trend 2

1. Initiate Smarter Regulatory Tracking

In 2015, approximately 30 legislative changes were introduced, which had an impact on Europe's asset management sector. Similarly, there would have been numerous changes or new regulations introduced in other geographies. Staying abreast of these changes, understanding their impact on the business, and implementing the change organisation-wide is no trivial task.

Researchers across the organisation track every regulatory announcement on a daily basis. A centralised approach and the use of technology can help asset management firms to track regulatory developments and plan the requisite change programs. A central team can monitor and store the updates in a central regulatory database, and also leverage the local knowledge of their counterparts from around the globe.

Big data analytics and taxonomy mapping will help compliance teams understand the links between different regulatory requirements, and the region, country, business unit, function, and process. If the processes are mapped against the regulation, an automatic workflow could be set up to ensure the right level of compliance. If the central database is linked to this regulatory taxonomy map and business processes, the organisation can collate evidentiary documentation for overseeing firm-wide regulatory scrutiny.

2. Implement Centralised Regulatory Coordination

A multinational asset management firm has many regulators to deal with. Let's take an example of a UK-based firm, whose lead regulator is the FCA, and it operates across France, Germany, and the US. The French business may have operations in France and the US, and would therefore deal with the French, the US and UK's home regulator. Similarly, the UK head office will also be engaging with regulators in the other geographies. An inefficient process indeed!

A re-alignment of the firm-wide regulatory liaison function can not only bring efficiencies, but also save costs and help implement compliance quickly. The regulatory liaison function could be structured in such a way that it optimises regulatory touch-points. For example, the central function that operates at the group level, can act as the nodal point to coordinate with all regulatory engagements. The central team could engage local businesses in regulatory discussions and leverage conversations it already had with other regulators on the same topic. This team can also proactively communicate important strategic changes to all the offices across different geographies. The local business entities can also coordinate with the central regulatory team while engaging with their regional regulators.

The central team can be supported by an in-house captive or a specialised service provider such as WNS, which could conduct research and manage interactions across the global offices. This service provider can also take over the responsibility of keeping all the offices updated about regulatory developments

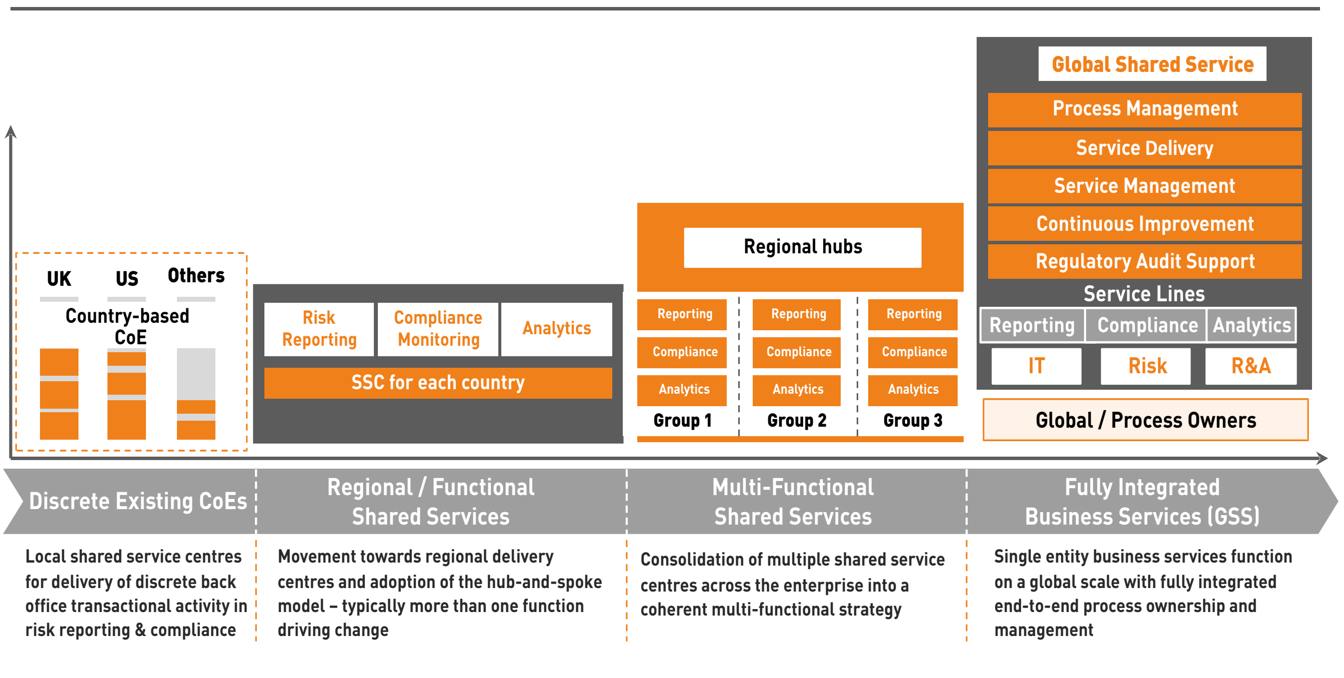


Fig 2: Sourcing options for setting up a Regulatory Compliance CoE

3. Consider Outsourcing as a Business Strategy

Financial services firms are gradually warming up to the idea of outsourcing activities of a regulatory nature to a third party. Outsourcing can bring about significant positive business impact such as:

- Compliance costs are contained as firms need not fight for scarce in-house resources
- Businesses or departments have additional skill-sets at its disposal, and need not compete for the same resources within the firm or poach from each other
- The firm has increased bandwidth to take on additional compliance responsibilities. The business-as-usual staff need not be overburdened, so profitability and operational efficiency are improved

Considering the pace and amount of regulatory changes being introduced, asset management companies will have to work with innovative structures to cope up. They should be open to different sourcing models, such as shared services, co-sourcing and outsourcing.

The ideal structure can be one in which a specialist compliance partner provides technical expertise on a consultancy basis. This partner has client-facing account managers who bring in experts from third-party organisations, such as WNS, from cost-effective offshore locations for routine compliance, analytics, and reporting tasks

The client has to deal with only the local compliance partner, while the account manager will manage all their compliance needs.

Larger asset management firms can develop captive shared services functions and co-source skilled process experts on a need basis.

The below diagram depicts WNS and Vedanvi's point of view on managing compliance through offshore centers to gain efficiency, effectiveness, and cost optimization.

Regulation	Relevant Requirements	Potential function for offshore set-up
Basel III / Capital Requirements Regulation / CRD 4	• Capital Computation • Stress Testing • Regulatory Reporting	▪ Data Management ▪ Reporting Services ▪ Risk Analytics
MIFID II	• Regulatory Reporting • Governance & Data Maintenance • Trade Reporting	▪ Reference Data Management & Reporting ▪ Trade Compliance Monitoring ▪ Client Screening & KYC Services
AIFMD, RDR, PRIIPs	• Regulatory Reporting • Customer Disclosure	▪ Pre-Trade & Post-Trade Confirmation ▪ Compliance Screening ▪ Data Management & Reporting
KYC / AML	• Transaction Screening • Customer Screening	▪ KYC – CDD, EDD, PEPs & NN Screening ▪ AML – Transaction Monitoring & Reporting
European Market Infrastructure Regulation (EMIR)	• Derivative Transaction Monitoring • Regulatory Reporting	▪ Reference Data Management ▪ Compliance Services
FATCA & MAD II	• Customer Screening • Suspicious Transaction Reporting	▪ KYC – CDD & EDD ▪ Transaction Screening & Reporting

Fig 3: Managing compliance through offshore centers

Trend 3 – Increasing Pressure on Margins

Asset management firms incur heavy costs related to compliance. As per a recent report, complying with European Union regulations cost asset managers in the UK GBP 2 Billion per annum. According to the Financial Times, in 2015, the asset management sector's cost base has increased by 44 percent since 2007. The spike in cost has outpaced revenue growth in North America, Western Europe and emerging markets, resulting in declining margins. In all fairness, even if we do not attribute all the increased costs to compliance alone, it does put significant pressure on margins.

Although regulatory expenditure can be anticipated and budgeted for, asset managers can be caught unawares because of:

- The scale of regulatory change emerging from a variety of new legislations. For large asset management companies, being classified as a Global Systemic Important Financial Institution

The company could also explore availing the services of consultants with industry expertise to conduct the as-is assessment

(G-SIFI) creates a more significant compliance burden. G-SIFIs are institutions whose distress or systemic failure could cause significant disruption in the financial system and economy, because of their size, complexity and linkage with other businesses. Such institutions have to follow additional compliance mandates, which impacts margins

- The ability of a company to absorb cost spikes becomes weaker when the top-line is also under pressure. Market volatility affects revenue as the latter is directly related to the performance of the client's portfolio. Also, disruptive players and alternative lenders begin to grab market share by offering higher returns at significantly reduced costs
- Like in the case of banking, regulation erodes certain high-profit businesses because of added compliance costs. A good example is algorithmic trading, which has been hugely profitable, and has attracted very little regulatory scrutiny until now

Response Strategies for Trend 3

1. Conduct As-is Assessment

The most effective method to manage the impact on cost margins would be to conduct an as-is assessment of the nature of regulatory changes and their impact. The assessment would facilitate the formulation of a suitable combat strategy.

In case of an impact arising out of a regulatory change, the typical response strategy could be breaking down the regulation into logical parts and assess the impact of each part on the asset management company's business lines. For instance, with the issuance of the Fourth Money Laundering Directive, the proposed changes would impact both the funding and investment businesses, apart from overall client on-boarding and remittance operations.

Similarly, when competitors introduce new offerings, the typical response would be to review the product basis the firm's own portfolio and investment strategy and align it suitably.

2. Implement Automation

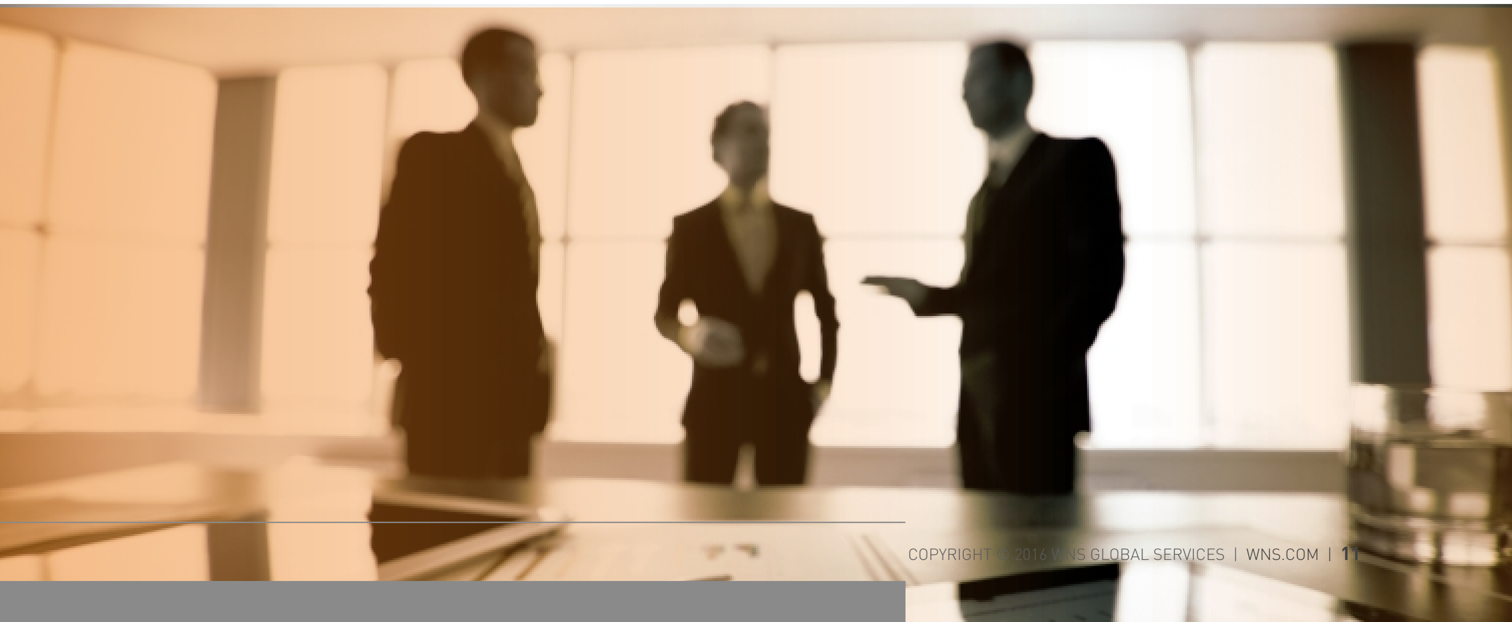
Automating manual processes increases efficiency, reduces resource costs, and improves margins. So which functions in an asset management company can be automated?

- **Investment advisory –** Introducing robo-advisory for Millennial clients, who constitute the bulk of the clientele, would greatly reduce the need to hire investment advisors to cater to this segment. Human advisory could be positioned as a premium service subjected to minimum investment thresholds. According to Financial Times, Barclays, Royal Bank of Scotland, Lloyds and Santander UK are developing rob-advisory capabilities
- **Transaction processing –** Many asset managers deal with diverse applications for front-, mid- and back-office, for which human intervention is needed to build the interface. Human effort reduces efficiencies and impacts margins. A comprehensive technology suite, or a robust interface solution, would ensure minimal human intervention, and improve margins. Additionally, cloud computing can significantly reduce fixed technology costs, although security concerns remain

3. Develop Innovative Product Strategy

Considering the dynamic market trends, coupled with regulatory compliance challenges, it is imperative for asset managers to explore alternative product strategies. These could include:

- **Peer-to-peer lending –** It is a practice, which is fast gaining momentum considering the potential returns involved. However, it goes without saying that the associated risks need to be thoroughly assessed
- **Exchange Traded Funds (ETF) –** ETFs have been identified as an area of significant demand from investors with many boutique managers using ETFs as a low cost method of investing in an asset class and bolstering performance through stock picking and direct investment
- **Social channels –** Social channels can be highly effective in sharing investment insights to attract investors. Using big data analytics, asset managers can gather valuable insights about target customer segments, assess trends, evaluate pain-points, competitor strategies and so on, which would be critical for designing sales and business strategy



Outsourcing non-core operations to experienced Business Process Management (BPM) players, such as WNS, can significantly improve margins. To make this happen, it is critical to de-couple non-core processes and evaluate the potential for outsourcing data consolidation and analytical tasks

4. Outsource Non-core Operations

The figure 2 in the previous section provides a glimpse of the regulatory functions, which can be considered for outsourcing. Similarly back-office trade functions that can be easily outsourced include settlement, reconciliation, performance monitoring, data management, and so on. Outsourcing, as a strategy, can benefit businesses by returning annualized gains of up to 40 percent.

Conclusion

In this paper, we have dwelt on the importance of why asset management companies should proactively track the three trends shaping the asset management sector and appropriately respond to them.

Smart planning, and a proactive response strategy to regulatory change can bring significant business benefits. Regulatory change can be seen as an opportunity to 'spring clean' the organisation, improve product performance, create stronger customer engagements, and bring operational efficiencies in the business.

Evolving customer demands can be a blessing in disguise necessitating a revamp of legacy systems, thereby creating more nimble and customer-centric service models that delight customers and bring down costs.

Technological innovation and the emergence of a more tech-savvy consumer are likely to usher in new market opportunities to provide higher yielding products, and drive operational efficiency.

About WNS

WNS (Holdings) Limited (NYSE: WNS) is a leading global Business Process Management (BPM) company. WNS offers business value to 200+ global clients by combining operational excellence with deep domain expertise in key industry verticals, including banking and financial services, consulting and professional services, healthcare, insurance, manufacturing, media and entertainment, retail & consumer packaged goods, telecom and diversified businesses, shipping and logistics, travel and leisure, and utilities. WNS delivers an entire spectrum of business process management services such as customer care, finance and accounting, human resource solutions, research and analytics, technology solutions, and industry-specific back-office and front-office processes. WNS has delivery centers world-wide, including China, Costa Rica, India, the Philippines, Poland, Romania, South Africa, Sri Lanka, UK and US.

About Vedanvi

Vedanvi is a boutique consultancy that provides advisory services, training, capacity building and managed services in the areas of risk management and regulatory change. Vedanvi's core consulting services include risk and capital consulting, governance, strategy and board support, regulatory intervention and change projects, and outsourcing (risk and actuarial).Today, Vedanvi's associates offer business value to top 100 multinational financial services firms, global consultancies and regulatory bodies.

How WNS and Vedanvi can Help

WNS and Vedanvi join hands to provide a comprehensive suite of offerings to the asset management industry. Through this partnership, we aim to work closely with client organizations in addressing challenges in regulations, compliance and risk management by applying global best practices, and ensuring cost-effective execution support, backed by proven technology and analytical tools.

To know more, write to us at
marketing@wns.com or visit us at www.wns.com

vedanvi
Risk & Regulatory Consulting

WNS
Extending Your Enterprise