Asset Management: Reinventing Reporting For the New Era of Transparency and Compliance

Executive Summary
As assets under management (AUM) inch back to pre-crisis levels, it may appear as if the asset management industry has weathered the financial storm. However, the transformative forces in today’s world are compelling asset managers to rethink their operating models for effectively addressing demands from clients and regulators.

One such decision is to reassess reporting, data management and decision support capabilities within the firm, specifically those related to post-trade areas, such as operational reporting, business intelligence, firm-level executive dashboards and client reporting. The emergence of cloud computing-based models offers asset managers the ability to source reporting as a service from a provider via a variable, usage-based payment model. Asset managers can leverage such emerging service models to modernize their reporting in order to meet the information demands of clients, regulators and decision-makers, while obviating the need for ongoing capital investments in their platforms.

Transformative Forces
Even as AUM returns to pre-crisis levels (see Figure 1, next page), the asset management industry is adjusting to the five transformative forces (see Figure 2, page 3) that are causing them to rethink their operating models. To stay competitive, asset managers must continue to focus on their core business of creating innovative investment strategies and offering the highest level of client service while coping with the onslaught of financial regulation.

Restoring Client Confidence
While buoyant investor confidence marked the heyday preceding the U.S. credit crisis, a series of economic shocks and scandals have significantly dented investor confidence. To restore client confidence, asset managers need to scale new heights in client servicing and transparency.

Focus on client servicing: Client service has emerged as a key focus area for asset managers. Studies indicate that asset managers who have mastered the art of servicing their clients are able to retain assets even during difficult times. An Investment Metrics survey conducted by Chatham Partners during November 2010 reveals that institutional investor satisfaction with investment managers is greatly influenced by client service, regardless of the economic climate or investment performance (see Figure 3, page 4).
The study indicates that 60% of overall satisfaction can be attributed to investment performance, but this can often be cyclical and unpredictable. The rest, 40%, is attributable to client service that can be delivered consistently. More important, of the top-five factors in order of importance attributable to client service, two are related to client reporting (see Figure 4, page 5).

Both institutional and retail investors alike are demanding greater value addition from their asset managers, such as research and analytics, in addition to the expected offerings of better client servicing, fund performance against the benchmark and absolute returns. Investors are also emphasizing customized solutions that are focused on specific outcomes or timeframes. Demand is also growing for information, research and tools that enable slicing and dicing of data to understand portfolio performance and risks, whether periodically, on-demand and in real time. Platforms that meet these new expectations can better engage customers and help generate more business. Beyond meeting the need for greater transparency, asset managers who find innovative ways of providing differentiated services will be ideally positioned to win market share.

Focus on transparency: The AUM recovery in 2010-2011 was accompanied by a heightened demand for transparency. Institutional investors such as insurance funds, pension funds, corporate and other entities have increased their scrutiny, and they now demand complete, accurate and timely information of their portfolio holdings and performance. Heightened transparency by asset managers is increasingly viewed as critical to boosting institutional investors’ transparency efforts.

Dawn of a Compliance-Driven Future
An unprecedented wave of financial regulation on both sides of the Atlantic is subjecting asset managers to a greater level of regulatory scrutiny. Several regulations, such as the Dodd-Frank Act, MiFID II and Solvency II (which are focused on improving investor protection, transparency and liquidity, as well as systemic and firm-level risk management), have resulted in new reporting requirements for asset managers. This underscores the need for aggregating, integrating and managing data across firm operations for reporting purposes, a daunting task for most asset managers. A firm’s data management and reporting platforms need to be adaptable to adequately cope with such regulations.

Global Assets and Operations
While allocation of assets across the globe is not a new phenomenon, the trend is likely to intensify. According to a survey of institutional investors in 2011 by McKinsey & Co., allocations to emerging markets have increased by a factor of three during the past five years. The share of emerging markets in global AUM is expected to increase from 11% in 2009 to 15% in 2015, and the share of profits is projected to rise from 27% to 35% during the same period (see Figure 5, page 5).

AUM, Revenues and Profitability
Operating profits improved in 2010, but gains were less impressive in 2011 due to market declines and cost growth.

Index: The year 2007=100
* McKinsey forecasts, based on 3Q 2011 reported results
Source: 2011 McKinsey/U.S. Institute Asset Management Survey; Merrill Lynch

Figure 1
<table>
<thead>
<tr>
<th>Transformative Forces</th>
<th>Events/Drivers</th>
<th>Imperatives</th>
<th>Technology Implications</th>
</tr>
</thead>
</table>
| Need to restore investor confidence | • U.S. financial crisis  
• Madoff scandal  
• Eurozone debt contagion | • Better understanding of the portfolio’s risk exposure.  
• Adaptable allocation strategies that allow taking advantage of global investment opportunities.  
• Self-help analysis tools for analyzing impact of unfolding economic events on the portfolio.  
• Increased transparency and granularity in reporting.  
• Focus on client servicing. | • Demand for aggregated client-level views with transparent reporting on individual holdings and transactions.  
• Advanced analytics and data cubes that support real-time, ad hoc analysis.  
• Multiple channels for consuming data, anytime, anywhere. |
| Regulations | • Dodd-Frank Act  
• MiFID II  
• Basel III  
• Solvency II | • Adaptable business model in light of the revised regulatory regime.  
• Agility in meeting regulatory requirements.  
• Higher cost of compliance. | • Increased need for data management and governance to produce accurate firm-level data.  
• Reporting tools capable of producing aggregated dashboards and data analytics. |
| Global assets and operations | • Increasing importance of emerging markets as an asset class.  
• Significant shift in wealth to East, resulting in increased focus on emerging markets for raising new asset sources.  
• Slowdown in developed economies. | • Client need for asset allocation in global asset classes.  
• Global operations to tap into investable assets within emerging markets.  
• Increased regional regulations.  
• Increased infrastructure requirements. | • Demand for holistic views that integrate data from global operations.  
• Insightful performance and risk analytics that provide decision support for complex investment strategies.  
• Increased data management and robust data strategy. |
| Margin squeeze: Pressure on top-line and bottom-line | • Volatile financial markets.  
• Shift in client preference to ETF and index-based passive investments.  
• Challenges in raising new assets from clients. | • Increased pressure on fees.  
• Lower fees from ETF and passive investments.  
• Higher operating and technology costs. | • Robust, adaptable architecture that can cater to changing requirements without proportionally increasing total cost of ownership. |
| New technologies | • Increasing use of mobile phones, tablets and social media.  
• Cloud computing.  
• Next-generation user experience. | • Increased real-time communication with clients.  
• Adoption of variable cost services and technology platforms.  
• Intuitive, easy-to-use interface. | • Scalable cloud-based platforms.  
• Newer channels for information delivery, such as mobile channels.  
• Emergence of social media as a competitive differentiator. |

Source: Cognizant Research Center

Figure 2
Investors in the U.S. and Europe are increasingly looking to global investment exposure for higher returns and risk diversification. Emerging markets such as Asia will be explored for new clients and investment opportunities.

As a result, asset managers aim to realize more than half of their growth from emerging markets during the next five to 10 years by adopting a mix of strategies such as partnerships, joint ventures, organic growth and inorganic acquisition strategies. This widening geographic presence presents challenges in terms of regulatory compliance and managing multiple operational systems that increase complexity when aggregating data on a consolidated level, among other organizational obstacles. This, together with the demand for global assets and the increasing proportion of emerging markets in the global AUM business, will demand larger scale, which in turn will require additional infrastructure investments that are resulting in increased cost pressure.

Mounting Pressure on Margins
Changing client behavior is motivated by growing risk aversion, preference for passive funds, demand for a heightened level of service and greater momentum toward performance-based fees. New, more conservative clients want value for their money, less focus on alpha, robust risk management systems and absolute clarity on reporting. Changing client preferences are bound to put upward pressure on costs and downward pressure on revenue, leading to squeezed margins.

Moreover, asset managers’ margins are expected to come under even greater pressure due to several factors:
• Increasing client preference for passive investments.
• Performance fees under the scanner.
• Increasing compliance costs.

Increasing client preference for passive investments: An analysis of actively managed funds conducted during 2011 by KPMG indicates that over the past 10 years, 85% of “long-only” active managed funds failed to deliver above benchmark returns. This led to a marked shift of risk aversion, as evidenced by a significant rise in demand for passive and exchange traded funds (ETF) investments.

The global market for exchange traded products (ETP) increased from $108.7 billion in 2001 to $1524.4 billion in 2011, at a CAGR of 30.2% (see Figure 6, page 6). Passive investment products are outpacing traditional active products and are set to garner a substantial share of global AUM in the coming years.

The significant growth in lower margin passive products and the growing competition

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**Client Servicing Achieves Top Honors**

What are the drivers for investor satisfaction?

Survey base: 1,726 investors surveyed between 2007-2009

Source: Investment Metrics, Chatham Partners

Figure 3
Client Servicing: Emerging Priorities

Market/Investment knowledge of portfolio team
Clarity of investment reports
Problem resolution skills of client service representative
Timeliness of investment reports
Frequency of contact of client service representative
Ease of navigation of Web site
Level of preparation for investment review meeting
Client service representative understands my unique needs
Responsiveness of client service representative
Reporting capabilities of Web site

Survey base: 1,726 investors
Source: Chatham Partners
Figure 4

for funds may further restrict fees applied to these passive products. There are two potential future scenarios on the passive front. First is the view that this could be a secular long-term trend that is unfolding gradually. The other likely scenario is that the trend may reverse when the markets start trending up, cyclically, and traditional funds are perceived as increasingly attractive.

In the short- to medium-term, however, asset managers cannot afford to miss the opportunity of tapping into passives’ growth momentum. As low-margin products, passives could potentially dilute the profitability of asset managers and compel them to further squeeze their overall costs.

Further, the ETF industry has lower levels of standardization and automation of processes compared with other traditional funds in the market. This forces asset managers to seek a cost-effective operating model.13

Performance fees under the scanner: Investors are also carefully examining fee levels in relation to the performance14 of their asset manager. The rising demand of a fee-for-

Emerging Markets: New Growth Frontier

The U.S. asset management industry’s share of global AUM and profits will continue to decrease as emerging markets grow.

![Share of global AUM and profits](chart)

Source: McKinsey Global Banking Profit Pool
Figure 5
performance model is likely to exert downward pressure on revenues.

**Increasing compliance costs:** The cost of doing business is increasing due to rising compliance requirements and the expense of managing increasingly global operations. For instance, regulations around OTC derivatives are likely to increase trading costs of these securities.

The reporting requirements by clients and tighter regulations across the U.S. and Europe are bound to raise the cost of operations. With the decline in revenues and increase in costs, the operating margin of some firms is likely to be impacted. Asset managers will eventually be forced to assess models that enable them to maintain flexibility in managing operating costs during both market upturns and downturns.\(^5\)

**Emergence of New Technologies**

The emergence of new technologies such as mobility and social media allows clients to access real-time information and improve communication among stakeholders.

The use of cloud computing is also gaining momentum. This computing approach allows asset management firms to move toward a variable cost model and quickly adapt to changing business conditions with increased agility, scalability, flexibility and efficiency.

**Growing Prominence of Reporting**

To succeed in the emerging era of transparency and compliance, asset managers need to substantially improve their reporting functions to satisfy clients and regulators. In the post sub-prime era, ad hoc requests for reports by investors in areas such as portfolio performance have increased exponentially. This sudden spurt in demand for reports is placing enormous pressure on asset managers whose systems were not designed to meet this deluge. To reassure clients, asset managers need to offer traditional reporting packages, as well as customized reports, with additional requested analysis and information.

Client needs apart, an improvement in reporting capability is also an important internal requirement for asset managers. Senior managers require insightful reporting on processes and risk exposures to ensure they are not caught off-guard.

While demand for accurate and timely information from all three users of the reporting platform — clients, regulators and both portfolio managers and firm executives — is steadily increasing, many firms’ existing platforms are struggling to keep pace with these ever-growing requirements due to multiple challenges:

- In many cases, reporting continues to be performed through homegrown legacy systems, most of which have significantly outgrown their initial functional scope and

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**Global Exchange Traded Products Posting Stellar Growth**

![Global ETP market size (in $ billions)](chart)

*Source: BCG Global Asset Management Market Sizing Database, 2011*

Figure 6
outlived their architectural and technological life expectancy.

- In some other cases, reporting is achieved through data generated from disparate point solutions that get stitched together manually using office automation software such as Microsoft Excel. As a result, it’s extremely difficult to both achieve a holistic view and drill down into details through a single report.

- The trend of outsourcing middle-office functions to asset servicers further complicates the equation, since managers are now dependent on the capabilities of the servicer’s platform. This issue is significantly aggravated when outsourcing is handled by multiple service providers for risk mitigation purposes or limited to a specific entity or specific region. Managers may be forced to aggregate data across providers or across in-house systems and the provider to obtain a firm-level view.

- M&A activity spread over multiple geographies often results in data that is scattered across multiple systems. For example, an asset manager may use one portfolio accounting system for traditional assets and another, more specialized system for alternative assets. Some of the core systems used by managers are legacy and do not lend themselves to easy integration. Lack of a consistent data strategy, or a budget to implement one, can result in major data quality issues.

- Finally, most reporting platforms are traditional in that they comprise “reports” that are specifically designed and developed per user group. In such cases, each little tweak to an existing report results in a development cycle.

The Case for Cloud-Based Reporting Platforms

Given the increasing demand for reporting from the imposing duo of investors and regulators and the prospect of declining margins and the fixed cost structure, we believe there are two imperatives for asset managers. First, they must reinvent their post-trade reporting platforms to comply with the changing industry order. Second, they must seek tier-one providers to deliver reporting as a service. By using a cloud-based reporting platform in which services are paid for as they are consumed, asset managers can obviate high up-front investments for the post-trade infrastructure and variabilize their costs.

Reinventing Post-Trade Reporting Platforms

A robust, insightful and self-help-based post-trade reporting platform is a key component of the operating model of a global asset

Anatomy of a Post-Trade Reporting System

Source: Cognizant Business Consulting

Figure 7
management firm. In the changing industry order, such a reporting platform can satisfy the exacting demands of clients and regulators alike, as well as the organization’s internal need for improved risk management and portfolio decision support.

We believe that three key aspects of the new post-trade reporting systems – operational reporting, client reporting, business intelligence and data visualization – should be structured to serve the increased demands for transparency, client service, regulatory reporting and risk management (see Figure 7, previous page).

Positive developments are allowing asset managers to leverage these platforms to address emerging requirements and challenges.

- In light of the dramatic advances in user experience technologies, it is now possible to create an intuitive and easy-to-use interface that can empower business users to define their own workspace and reports with minimal dependency on technology staff. This can dramatically reduce the technology development pipeline for “new” or “custom” reports and the associated cost of maintaining such reports.
- Client reporting and client servicing can be dramatically changed by exposing an easy-to-use analysis toolkit to sophisticated investors, akin to the decision-support tools used by the firm’s portfolio managers. Savvy investors could utilize the toolkit to quench their thirst for transparency and for custom reporting on their portfolio. Going a step further, the next generation of features could allow investors to create their own custom, aggregated views by merging data on mandates held elsewhere with those held at the manager. This would empower the investor to analyze the entire investment book, not just those investments managed by the firm. Such features will not only eliminate ad hoc reporting requests but will also prove to be a significant differentiator and a strategy for attracting new money.
- In the case of internal users and decision-makers, the reporting paradigm can be shifted significantly. New technologies make it possible to create intelligent, context- and time-sensitive interfaces that can “understand” the need of information consumers and their actions and display the most relevant data at any point in time. For example: The default start-of-the-day interface for a portfolio manager managing an active strategy could be a visual dashboard of the performance of his/her portfolios, while that for a portfolio manager managing a passive strategy could focus primarily on cash inflows and outflows. Toward the end of the day, the default dashboard could change to those focusing on status of executed trades. The dashboard produced for the firm’s chief investment officer would be an aggregate of all portfolios and associated risk measures, allowing the executive to focus on the most critical data points.

Road Ahead: Sourcing Reporting as a Service

On the one hand, having an innovative reporting platform can help asset managers address most reporting requirements and potentially attract new money; on the other hand, many firms are unable to fund multi-year programs to modernize or rebuild their current platforms.

Sourcing new post-trade reporting platforms from a trusted tier-one partner can help asset managers variabilize fixed costs and enable them to focus on their core functions (see sidebar, below) of generating investment performance.

Migrating to a cloud-based reporting platform delivered in the form of business process as a

Advantages of Reporting as a Service Model
- Increased business agility/flexibility.
- Improved quality of service.
- Avoidance of capital expenditure.
- Transfer of ownership responsibility to the provider for infrastructure, technology and resources.
- Usage-based fee, which enables conversion of Cap-Ex to Op-Ex.
- On-demand reporting, anytime, anywhere.
service (BPaaS) can improve agility in reporting while variabilizing fixed costs by enabling asset managers to embrace a pay-per-use model. This model aligns very well with the current business environment. Asset managers, for example, can:

- Provide online access to their clients with data tailored to their specifications.
- Generate reports on-demand.
- Provide query tools that offer data mining and analytics capabilities. This lends interactivity to the process, which is vital to customer satisfaction.

With the advent of sophisticated applications for mobile and Web-based environments, significant changes are in the offing for asset management information delivery systems. It is imperative for asset management firms to use the latest advances in technology, such as cloud computing models, and utilize their benefits to strengthen or advance competitive advantage.

In a survey conducted by Linedata Exchange in 2011, 36% of investment management firms queried said they were already using the cloud platform. Moreover, 18% said they hope to be using cloud delivery models in the next two to three years (see Figure 8, above).

Among the concerns associated with flexible sourcing models such as reporting as a service, data security and confidentiality figure prominently. This calls for providers to embed effective data security and governance mechanisms to ensure safety of the data being handled.

Sourcing post-trade reporting as a service offers a compelling way for asset managers to stay agile, while focusing on their business core. This is essential today, given the macro-economic pressures – transparency, regulatory, competitive – and the never-ending quest to contain costs, as well as the need for operational scalability (upward and downward, in sync with business cycles).
Footnotes


8 Alpha is a risk-adjusted measure of the so-called “active return” on an investment. It is the return in excess of the compensation for the risk borne and, as a result, is commonly used to assess active managers’ performance. Often, the return of a benchmark is subtracted in order to consider relative performance, which yields Jensen’s alpha.


11 “Global Asset Management 2011: Building on Success,” BCG.

12 “The Agile Asset Manager,” KPMG.


14 “The Agile Asset Manager,” KPMG.

15 “Formula for Success,” KPMG.
About Cognizant

Cognizant (NASDAQ: CTSH) is a leading provider of information technology, consulting, and business process outsourcing services, dedicated to helping the world's leading companies build stronger businesses. Headquartered in Teaneck, New Jersey (U.S.), Cognizant combines a passion for client satisfaction, technology innovation, deep industry and business process expertise, and a global, collaborative workforce that embodies the future of work.

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