THE AGE OF OPTIMIZATION IN CORPORATE ACTIONS AUTOMATION

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Agenda

• Introduction
• Trade Lifecycle Optimization (TLO) framework
• Corporate actions and TLO
• Technological challenges and use of third party solutions
• Conclusion
The market environment has become more complex and uncertain

The financial markets continue to face a number of key challenges going forward:

– declining return on equity for broker-dealers
– de-risking and deleveraging for banks
– regulatory and compliance burdens for wealth management firms
– under-investment in key operational and IT areas for some buy side firms
– weakened trust from clients across many sectors
– a crowded list of regulatory initiatives continues to drive market infrastructure changes across the front, middle, and back offices
Section 2  Trade Lifecycle Optimization
Definition of Trade Lifecycle Optimization

• A transformational initiative that addresses some of the issues discussed in the previous slides is Trade Lifecycle Optimization (TLO)

• TLO is a conceptual framework for addressing challenges and opportunities across the front, middle, and back office of securities trading, operations and IT

• TLO offers multiple levels of efficiency, including trading efficiency, collateral efficiency and clearing, and settlement efficiency

• It is expected to gain traction in the coming months and years
TLO is a conceptual framework for addressing challenges and opportunities across the front, middle, and back office of trading, operations and IT.

Full trade lifecycle optimization covers multiple steps including pre-trade, at-trade and post-trade optimization.

**Trade lifecycle optimization**

**Pre-Trade**
- Pre-deal capital, risk and collateral analysis
- Scenario analysis
- Liquidity sourcing
- Pre-trade certainty
- Venue choice

**At-Trade**
- Transaction cost analytics (TCA)
- Algorithmic switching

**Post-Trade**
- Collateral optimization
- Cross product netting
- Portfolio margining
- Clearing and settlement optimization
- Integrated balance sheet and financial resource management

TLO offers more informed decisions, which lead to multiple levels of efficiency (trading, post-trade)

Source: Celent
Market participants are just beginning to address the various issues discussed and these are early days for TLO

• To date, most firms have addressed optimization in a narrow and fragmented way

• For example, firms have sought highly efficient trading systems to navigate an array of financial markets and intermediaries, have adopted sophisticated risk analytics and collateral management systems, and have embraced trade verification utilities

• Others have taken an even more holistic view to implement post-trade workflow automation tools such as reconciliation and exception management systems to complement front office automation with back and middle office automation

• However, only a few have combined these systems into a transformational package
But Celent predicts that trade lifecycle optimization (TLO) will gain traction

- An acceleration toward the Age of TLO will occur when executives in the industry, who see the potential to reshape securities trading due to cost and capital constraints, start seeking an integrated approach for efficiency and performance in IT and operations.

- We believe early adopters of TLO may be able to gain competitive advantage in terms of operational efficiency and/or trading performance.

- The way to achieve this is to look at pre-trade, trade, and post-trade automation tools in a holistic way and to create a strategy to implement these tools.

- While vendors or service providers will have the complete package, financial firms can nonetheless seek a set of tools that can be integrated.
TLO drives widespread benefits for organizations

- Declining margins, regulatory pressures, and market infrastructure changes are forcing firms to consider *driving efficiency across the entire enterprise*
  - operational efficiency
  - long-term transformation initiatives
- Celent predicts the concept of trade lifecycle optimization (TLO) will gain traction in this environment
- While TLO is a framework being brought forward by Celent, it is also being advocated by leading institutions and vendors

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TLO is a very forward looking framework

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Section 3  Corporate Actions and TLO
Corporate actions processing is a complex process

• It involves many parties, regional differences and market specifics

• Today, data and software automation have matured as financial services organizations have become more cost conscious

• It is the intelligent management of these exceptions along the corporate actions processing lifecycle that leads to substantial benefits

• In addition to automation of corporate actions, the alignment of business processes across the enterprise must take place to truly benefit from corporate actions systems and tools

• Corporate actions automation needs to be seen as a front-to-back office initiative, not only a back-office operation
Corporate actions automation tools fit squarely into the TLO framework because they allow firms to optimize post-trade operations

- Corporate actions tools allow firms to optimize repeatable and predictable processes
- Corporate actions tools are part of larger workflow and technology ecosystems; sit alongside reconciliation, security master
- Systems are increasingly multi-faceted and must accommodate multiple data sources/custodians/etc
- Corporate actions automation has not and will not be considered a profit center per se, but rather a way to decrease potential losses
- Some of the main benefits of corporate actions automation can be summarized as follows:
  - Reduction of operational risks/processing errors
  - Enhancement of staff productivity
  - Reduction of costs
  - Improvement in customer service

The main benefit thus far of corporate actions automation has been operational efficiency
Section 4 | Technological challenges and use of third party solutions
The technology environment for corporate actions processing is challenging

- Spending on corporate actions is expected to stay level over the next year.

- Celent has found that spending for corporate actions typically sits with the operations team’s budget, and front and middle offices are not at present spending money themselves.

- Firms are currently justifying spending on corporate actions primarily through the business case of operational efficiency, as opposed to front office benefits and risk mitigation.

- A primary barrier to adoption of corporate actions automation systems is the belief that the initial buy-in for such systems is high.
Financial firms and vendors must respond strategically to these challenges and issues

- Vendors are responding to the challenge through:
  - Pricing flexibility (security level pricing, modules)
  - Implementation methods (SaaS)
  - By increasingly positioning their solutions as part of front-to-back initiatives and moving beyond the operations budget

- For financial firms, corporate actions should *no longer be thought of as a discrete process affecting only the back office*
  - Budgets for corporate actions should move beyond the operations staff
  - Will be part of trade lifecycle optimization
  - Corporate actions tools can be considered parts of larger vital long-term transformation projects (data management/data repository, other initiatives)

Vendors must position their tools as part of long-term transformational initiatives to break out of the back office
Summarizing Build Vs. Buy Decisions

• Generally speaking, the larger firms typically deploy a mix of build and buy best in class tools

• Medium-size firms are more open to a SaaS environment due to lower costs

• Smaller firms are more oriented to obtain corporate action functionality from back office solutions, rather than buying expensive corporate action specific suites

• Through our research, we have identified the following factors that are useful when making the build vs. buy decision:
  – Current structure and staff
  – Complexity of corporate actions
  – Current corporate action processing system
  – Other existing solutions
  – ROI potential
Section 5 Conclusion
Moving to the age of optimization: We see two distinct phases

The evolution of the age of optimization


- Buy and sell side firms use available data sets and calculators to make more informed choices
- Work underway to better complete the TLO circuitry
- Initial engagement with third-party vendors begins and some internal builds proceed

Phase 2: (2015-2017): The Lets See the Benefits Phase

- Buy and sell side firms consider other data sources and analytics to create more-real-time TLO to drive advantage across front/middle back offices functions
- Third-party integration work is completed and internal and consultant technology builds slow down
- Firms begin to see the tangible benefits of TLO

Conclusions

- We believe the actual movement to the age of TLO could take several years and will likely follow fits and starts
- Given that, for example, collateral optimization is driven by regulatory requirements among other factors, the ebb and flow of regulatory pressure will be a significant accelerator of change (or brake if regulators decide to ease up on the pressure)
- Moreover, adopting new analytics, data streams and software is an often painful process and needs buy-in across organizations, which can take several years
Recommendations for TLO: Working with multiple technology enablers

Alignment of the dive to TLO with technology enablers

• In order for firms to attain full trade life cycle optimization, they will have to align their strategic business goals with core technology enablers
  – This will prove difficult for firms using only one technology platform
  – Firms will have to utilize and retain a number of different technology platforms in their portfolio to reach full trade lifecycle optimization

• Celent believes that certain vendors exceed others in different verticals of the trade lifecycle (i.e. one vendor may be superior in enterprise collateral management but fall short of delivering full trade portfolio optimization; other solutions may be point reconciliations or corporate actions solutions)

• Financial institutions must still retain multiple platforms to seize opportunities for full trade lifecycle rewards
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