

# Performance

**2019 Investment  
Management Outlook:  
Mid-Year Review**

Page 6

**The future of the asset  
management industry**

Page 30

**Amundi-Pioneer  
The recipe for a successful  
integration process**

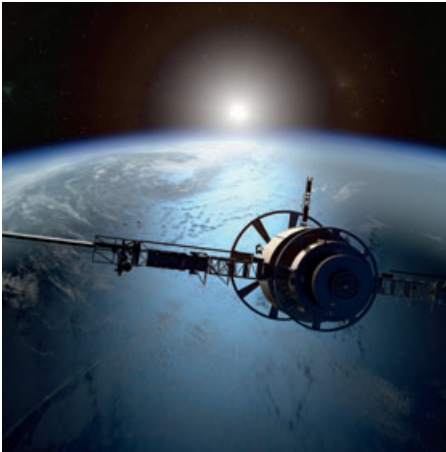
Page 44

**Distribution 2.0  
How technology will redefine  
relationships with asset  
management clients**

Page 56



# In this issue



Page 6



Page 12



Page 36

---

06

**2019 Investment  
Management Outlook:  
Mid-Year Review**

---

44

**Amundi - Pioneer**

The recipe for a successful  
integration process



Page 44



Page 56



Page 68

---

12

**Managing M&A Integrations**

A guide for investment and wealth managers

---

20

**Engaging the whole firm**

Improving client experience in institutional and wholesale investment management

---

30

**The future of the asset management industry**

---

36

**Artificial intelligence**

The next frontier for investment management firms

---

50

**India Budget 2019 brings some gain, some pain for foreign investors**

---

56

**Distribution 2.0**

How technology will redefine relationships with asset management clients

---

68

**A financial frontier:**

Opportunity from the East

# Foreword



Ridley Scott once said that he was amazed at how much he could squeeze into a thirty-second commercial. The same could be said about this particular magazine, which with this edition, marks its 30<sup>th</sup> publication. When we first came up with the concept, none of us truly dared to believe how much content we could and would cover in 30 packed editions. However, we cannot take all the credit. It is thanks to you our readers, for your enthusiasm to delve in between its covers three times a year coupled with your willingness to contribute and share your knowledge, expertise, and insights with your peers, which makes this a must-read amongst the myriad of asset management publications that exist today.

As befits the last edition before the start of a new and exciting decade for our industry, we have taken the opportunity to go retrospective and discover how accurate we were with our Investment Management outlook published just under a year ago. Interestingly, we discovered that our predictions and trends were more often on track than not. One of those trends relates to Merger & Acquisitions activities, a topic which continues to feature in this issue. Firstly, we examine the theoretical critical success factors to manage integration post-merger, followed by insights from Christine Gentil on the recipe for success in relation to the Amundi-Pioneer merger, which involved integration of seven different locations and over 2,000 new employees.

To a certain extent we can argue that integration is perhaps the single most critical driver affecting our entire industry,

firmly entrenching and impacting our strategic decisions, our cultural diversity, our social responsibilities, and our technological development to name but a few. Improving the client experience is another area where integration is key both from a human and technological aspect. Sometimes casting a critical eye on basic functions within our value chain can radically, yet positively, revitalize your business and client interactions. Read on to see how artificial intelligence and other technological advances will refine our future relationships with clients.

Keeping on the theme of the future, Noel Fessey of the European Fund Administration gives us his interpretation of topics that will shape both asset management and asset servicing including his three steps to heaven, shop 'til the competition drops, and extinction rebellion... Food for thought for future articles, perhaps?

No edition of Performance is complete without our customary journey around the globe. Today, we focus on the East with India being our first port of call. We provide an analysis on the 2019 Indian budget including details of proposed regulatory reforms for Foreign Portfolio Investors, key tax changes, and the rationalization of KYC norms. Travelling further east, we explore the financial frontiers of Asia, shedding light on exciting opportunities.

To conclude simply, please enjoy the pearls of wisdom in this 30<sup>th</sup> anniversary edition and we'll be back early next year, at the start of a brand new decade.

A handwritten signature in black ink, appearing to read 'Vincent Gouverneur', with a stylized flourish at the end.

**Vincent Gouverneur**  
EMEA Investment  
Management Co-Leader

# Editorial

## Challenging times for the investment management industry

The investment management industry is in a period of rapid change, driven by shifting investor preferences, margin compression, continued regulatory developments, and advancing technologies.

Investor preferences continue to adapt. In 2018, 16 of the top 20 net flow funds were passive mutual funds while Exchange-traded Funds (ETF) continued to gain ground. The advent of zero cost ETFs may accelerate this growth further. According to State Street Global Advisors' estimates and Investment Company Institute's data, global ETF assets could touch the \$25 trillion mark by the end of 2025, up from \$4.8 trillion in 2018. In addition, active funds have underperformed benchmarks. Studies have shown that 86.7 percent of US active funds have underperformed their benchmark, on a net-of-fees basis, over the ten-year period ending in 2017. European funds have similar results: 85.4 percent of actively managed European equity funds underperformed over the same period.

Retail customer preferences are also diverging. Most Millennials and Gen Z have made a quantum change in their investment practices from those of their parents. These cohorts will eventually hold a significant share of global investable assets as the multi-trillion dollar inter-generational wealth transfer progresses in the US and Europe. They tend to prefer engaging with online and mobile channels, a low minimum initial investment amount, and 24/7 access to investment advice on smart devices.

Regulatory fragmentation continues as securities regulations across the US, Europe, and Asia are changing according to diverse priorities. Additionally, the onset of new rulings globally will likely complicate regulatory compliance management in 2019.



**Tony Gaughan**

Global Asset Management Sector Leader

In contrast, tech-savvy firms are putting pressure on the traditional value chain. These tech-savvy disruptors could shake up online fund distribution, digital advice, or micro investing with their expertise in digital experience delivery or large customer bases. These potential new entrants are likely to provide low-cost services, coupled with digital age capabilities, aiming to build relationships with Millennial and Gen Z cohorts before they are targeted by incumbent firms. Many traditional investment management firms are planning for potential disruption caused by new technology-based entrants.

Successful firms in 2019 will likely be the ones that can continue to manage these challenges with plans designed to withstand changing market conditions. In doing so, investment management business leaders should consider the following three questions. Firstly, how to grow the business? Secondly, what are the possibilities to run operations more efficiently, and thirdly, how to deliver the next level of customer experience?

The bottom line for investment managers is that increasingly execution drives success. Many firms have spent a lot of time developing plans and strategies. 2019/20 may be the year that some firms innovate and emerge through the execution of bold actions. Some investment managers will likely push their boundaries as they seek to grow their business, run operations resourcefully, and deliver improved customer experience. In contrast, firms that do not invest in such criteria becoming the inorganic growth fuel for firms with more efficient and effective platforms that yield higher profitability.



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# 2019 Investment Management Outlook: Mid-Year Review



**Douglas J. Dannemiller**

Senior Manager  
Deloitte

Last November, the Deloitte Center for Financial Services published a 2019 Investment Management Outlook. We focused on how firms were picking the right growth options, creating operational efficiencies, and delivering next level customer experience. In each of these areas, we noted market trends and made a few predictions. Let's see how some of these trends and predictions are actually playing out in 2019 [▶](#)









### Picking the right growth options

First, let's explore the trends we identified that have continued to be topical today: Mergers and Acquisitions (M&A), development of alternative data capabilities, and the accelerating use of Artificial Intelligence (AI) across the organization.

#### M&A

Many investment management firms have used M&A as a tool for growth, capability enhancement, and cost optimization through scale. The levels of M&A have been consistently high throughout the first half of 2019<sup>1</sup>. Global regulatory requirements and competitive pressures are expected to continue to drive higher than average M&A activity in investment management.

#### Alternative data processing

Many firms are developing alternative data processing capabilities to improve alpha generation. The alternative data providers' marketplace is growing on a daily basis, with over 400 firms selling alternative data as of July 2019<sup>2</sup>. Another trend this year involves notable long-only managers, such as CPPIB, developing capabilities to augment their investment processes<sup>3</sup>. Alternative data inclusion in the investment decision process is becoming a mainstream capability.

#### AI

In investment management firms, AI traction is accelerating in back, middle, and front office processes. In addition, AI implementation varies dramatically across businesses. For example, tech-savvy hedge funds are applying AI to enhance trading capabilities, while more brand name and traditional firms are using AI to

gain efficiencies in the back and middle office. Evidence indicates firms are using AI in conjunction with, rather than as a replacement for, personnel. The use of AI in this context is an efficiency or effectiveness play, not a replacement strategy<sup>4</sup>.

#### Predictions

Our 2019 predictions included bleak growth opportunities with "to be determined" at best and "not likely to pan out" at worst. A prediction that we would see success among investment managers, specifically those who have an operating model focused on distribution agility, local partnerships, and product transparency targeting the Chinese market, is still too early to comment.

While another prediction, that fulcrum fees would emerge as a growing trend in 2019, appears to have plainly missed the mark. Key investment product distributors are slow to embrace variable fees. Perhaps businesses doubt that an investment firm should be paid more for doing what is expected of them in the first place.

In our "bottom line on growth" we recommended that firms consider investment in data storage and analytics and be aggressive when acquiring new capabilities. Both of these recommendations stood the test of time through the first half of 2019. For example, in their largest deal since the financial crisis, Morgan Stanley recently acquired the SaaS equity administration provider Solium Capital at a 43 percent premium in order to enhance their wealth solutions for the workplace and provide their advisors with another channel for clients.<sup>5</sup>

- 1 Martin Järvengren and Dr. Roger Kiem, "Financial Institutions M&A: Sector trends - June 2019: Asset/Wealth management," White & Case LLP, July 8, 2019, <https://www.jdsupra.com/legalnews/financial-institutions-m-a-sector-38176/>
- 2 Website: "Industry Stats", Alternativedata.org, accessed 8 August 2019, <https://alternativedata.org/stats/>
- 3 Geoff Zochodne, "How CPPIB is tapping 'alternative data' to refine its investment processes", Financial Post, 18 March 2019, <https://business.financialpost.com/news/fp-street/how-cppib-is-tapping-alternative-data-to-refine-its-investment-processes>
- 4 Matt Egan, "How elite investors use artificial intelligence and machine learning to gain an edge," CNN Business, February 17, 2019, <https://edition.cnn.com/2019/02/17/investing/artificial-intelligence-investors-machine-learning/index.html>
- 5 Liz Hoffman, "Morgan Stanley, in Its Biggest Deal Since Crisis, Courts Future Millionaires," The Wall Street Journal, February 11, 2019, <https://www.wsj.com/articles/morgan-stanley-in-its-biggest-deal-since-crisis-courts-future-millionaires-11549885394?shareToken=ste095a4ad968946119842bd59e64ae065>

### Creating operational efficiencies

In our Outlook, we noted a trend that investment managers are quick to embrace cloud and advanced analytics for differentiating processes in the front office and for non-differentiating processes in the middle office.

Are firms continuing to follow the advanced analytics trend called out in our Outlook? It appears so. Even in the front office, where firms are concerned about the balance between talent and technology. While many firms are reluctant to discuss strategy, Franklin Templeton revealed its plans to develop advanced analytics in the front office to improve efficiency and alpha generating capabilities.<sup>6</sup> Admittedly, this evidence is anecdotal, but until a comprehensive dataset covering the industry emerges, there isn't anything else to go on. Let's say the trend is likely to continue.

Also in our Outlook, we made further predictions on operational efficiencies: one focusing on the use of proprietary indices in Exchange Traded Funds (ETFs) accelerating, and another predicting that Private Equity (PE) firms along with long-only managers would join hedge funds with utilization of alternative data in their investment decision processes.

Utilization of proprietary indices has continued, but it has not accelerated. As of July, roughly 22 percent of the index funds brought to market during 2019 used proprietary indexes compared to 30.3 percent in 2018 and 27.4 percent of ETFs launched in 2017.<sup>7</sup> One of the important reasons for the slight downturn may be the

increased regulatory scrutiny of proprietary indices, focused on disclosures.

As for alternative data adoption in the investment management process by PE firms and long-only managers, there is evidence to support our initial prediction<sup>8</sup>. Long-only firms are developing alternative data capabilities, and PE firms are as well, albeit with slightly customized buying approaches to mesh with the buy and hold strategies in PE funds<sup>9</sup>.

### Delivering the next level of customer experience

In our Outlook, we emphasized the ability to develop and deploy applications to capture the next generation of investors. We noted that digital maturity was lagging in investment management compared to other industries. We also stressed the importance of Digital Voice Assistants (DVA), because this emerging technology interface incorporates AI and represents an opportunity for fintech firms to come between investment managers and their customers. Trends this year confirmed our Outlook's prediction. Several of the largest investment managers are reported to be deep into DVA development<sup>10</sup>.

Our forecasts for customer experience are less piercing compared to some of our other Outlook predictions due to the topic being much more subjective. We said that "customer engagement and building meaningful relationships will be more in focus than ever as investment managers compete for Assets Under Management (AUM) in 2019," and that "many investment managers will strive to offer newly designed customer portals, most likely

by acquisition or partnership with tech-savvy firms." Unfortunately, we can't say customer engagement is more in focus than ever; however there is evidence to show that new customer portals are being developed.<sup>11,12</sup>

This exercise reveals that trend identification is valuable and important, and that predictions are inherently uncertain. What is your experience? Are trends playing out as you expected? Are your strategic plans unfolding as expected in 2019? 2020 will soon be upon us. As we take a look back to how we thought 2019 would unfold, we also begin planning for the next year. Don't hesitate to call on us to share our insights and perspectives to inform your planning process. Look for our next Investment Management Outlook to come out before the start of 2020.



6 Randy Bean, "Franklin Templeton Embarks On Ambitious Data And Analytics Transformation", Forbes, 13 Mar 2019. <https://www.forbes.com/sites/ciocentral/2019/03/13/franklin-templeton-embarks-on-ambitious-data-and-analytics-transformation/#75efca4da706>

7 Jill Gregorie, "SEC Examiners Flagging Flaws in Custom-Built Indexes," Ignites, July 15, 2019, [https://www.ignites.com/c/2438173/289523/examiners\\_flagging\\_flaws\\_custom\\_built\\_indexes](https://www.ignites.com/c/2438173/289523/examiners_flagging_flaws_custom_built_indexes)

8 Nick Wells, "Alternative data comes of age and investors are noticing", CNBC, April 23, 2019. <https://www.cnbc.com/2019/04/23/alternative-data-comes-of-age.html>

9 Press release, "Eagle Alpha Announces New Solutions for Private Equity Firms", BusinessWire, 11 April, 2019. <https://www.businesswire.com/news/home/20190411005868/en/Eagle-Alpha-Announces-New-Solutions-Private-Equity>

10 Meghan Morris, "Alexa, what ETF should I buy?", Business Insider, June 13, 2019. <https://www.businessinsider.in/Alexa-what-ETF-should-I-buy-Asset-managers-like-BlackRock-and-Invesco-are-testing-out-voice-assistants-but-its-too-early-to-tell-if-customers-will-actually-use-them/articleshow/69773482.cms>

11 Dieter Holger, "Startups Target Millennials With Social-Investing Apps", Wall Street Journal, June 10, 2019. <https://www.wsj.com/articles/startups-target-millennials-with-social-investing-apps-11560219180>

12 Lananh Nguyen, "JPMorgan app draws Millennial investors with lure of free trades", Bloomberg, May 15, 2019. <https://www.bloomberg.com/news/articles/2019-05-15/jpmorgan-app-draws-millennial-investors-with-lure-of-free-trades>



**To the point:**

- Even in the tenth year of an equity bull market, most investment management firms find their quest to improve profitability challenging
- Many firms are executing growth strategies in new geographic or assets class territories in search of profitable growth
- Advancements in analytical capability and data availability are at the forefront of competition throughout investment management

“History tells us that in challenging times the odds favor the bold over the timid, now is one of those times in investment management.”

**Tony Gaughan**  
**Global Asset Management Sector Leader**  
**Deloitte**



# Managing M&A Integrations

A guide for investment  
and wealth managers

**Baber Din**

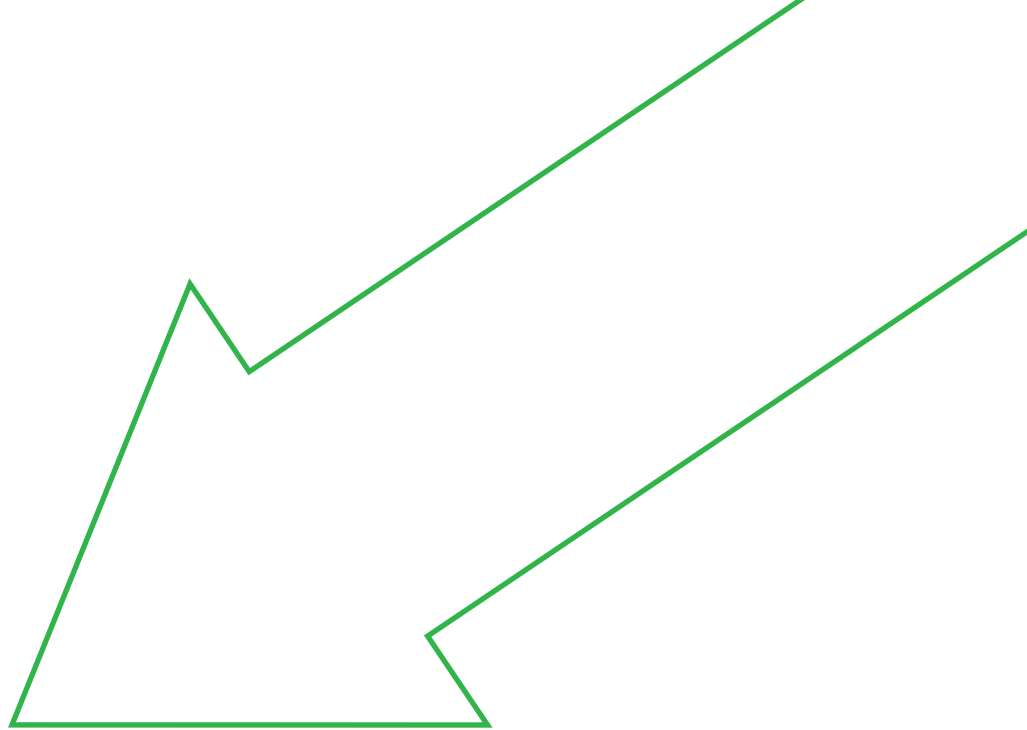
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## The quick read

The integration journey to deliver targeted value creation is exciting yet difficult if underestimated—as many investment and wealth managers keep learning, to their, and their shareholders', cost.

Here are the critical success factors for managing your next M&A integration:

### Strategy shapes approach.

Transaction value drivers should determine both the overall approach and which elements of the businesses should be integrated. For example, the industrial logic of a domestic investment management deal between propositionally similar firms, focused on creating cost synergies in operations and de-duplicating front-office capabilities, will drive different integration priorities to, say, a cross-border transaction between geographically or propositionally diverse firms, where revenue synergies through distribution are of greater delivery importance.

### Managing cultures is the hardest challenge to resolve.

Cross-border, private/listed, and big/small company combinations present areas of great risk, often exacerbated by differing investment ethos or culture. The integration should seek to create a post-merged culture that fosters common behaviors and ways of doing business.

### Talent retention is a key risk area.

Where other businesses may be able to rely on proprietary technologies, market dominance, or brand power, investment and wealth managers rely on people—and people can leave. Key personnel should be retained by engaging them early, having a clear communication strategy and minimizing the period of business and cultural disruption.

### Integrations need to be managed extensively.

As business-as-usual is vulnerable to merger stress, a robust governance structure and a resource capacity review of the work-streams within it, are critical. Furthermore, an appropriately resourced Integration Management Office (IMO) is always recommended.

### Technology integration is key to deal success.







Running multiple systems is costly, and at the same time, system migrations increase execution risk significantly. In addition,

investment and wealth managers are used to steady state running and incremental change: therefore, the challenge in addition to integrating systems is often one of delivering an integrated user experience that replicates the look and feel of what the business users are accustomed to. Agreement on operational platforms should be established pre-signing where possible. Furthermore, single rather than multiple outsource providers, at least regionally, should be used where possible to cut costs and complexity.

### Synergy targets are frequently too vague.

A detailed synergy plan with specific, quantified synergy targets and a tracking process is essential. For example, it was very clear in our conversations with both firm executives and outsource service providers that they have a huge and critical role to play in informing the integration cost impacts, which need to be understood and tracked closely. ➔

The investment and wealth management sector is going through substantial changes. There are six key themes that currently face all firms, creating both challenges and opportunities:

-  1. The secular shift of assets from defined benefit to defined contribution savings and the rise of wealth in Asian markets
-  2. New regulatory pressures across all aspects of the business
-  3. Achieving differentiated saving and investment outcomes in uncertain markets, exacerbated by structurally lower risk free real rates of return across the developed world
-  4. Downward pressure on fees in certain asset classes and parts of the value chain, through increased competition and transparency
-  5. The imperative to harness new technologies to protect against disruption and improve cost efficiency
-  6. Evolving business models and increased vertical integration product development to distribution.

These themes combine to make it increasingly difficult for firms to deliver sustained organic earnings growth to their owners. This has driven a market appetite for achieving better scale and improved capability through inorganic routes, increasing M&A activity.

The opportunity to create something new and better through M&A, and to do so quickly and effectively, need not descend into unanticipated crises, unplanned costs and huge management distraction—but often does.

Why? Firms in this sector are often mid-sized businesses, without dedicated M&A or change resource. Their front office businesses are highly dependent on

talented individuals—who are independent, well remunerated, and very mobile. They also utilize IT systems that can be notoriously difficult to integrate, and have clients who are susceptible to any disturbance of business-as-usual. These attributes can conspire against acquirers without a clear and actionable vision, developed early.

This article builds on the CaseyQuirk publication *“More Perfect Unions: Integrating to Add Value in Asset Management M&A”* released earlier this year<sup>1</sup>, providing real life, practical experience of how sector participants have confronted integration challenges and what they have learned as a result.

1. <https://www2.deloitte.com/content/dam/Deloitte/us/Documents/financial-services/us-integrating-to-add-value-in-industry-m-and-a.pdf>

### Starting points: Strategy shapes approach

#### Knowing what you want from a deal is the foundation of all successful mergers and acquisitions.

The strategic rationale and investment thesis for a transaction (including the expected return and financial effects), cannot be assessed separately from a clear vision of how the target will be combined with the acquirer. If it is, then you've only done half the work.

It is only when investment and wealth managers know exactly what they want to get out of an inorganic growth strategy that they can set effective integration strategies and structures.

A desire to expand strategic footprint—by acquiring new manufacturing capability (e.g. in real assets) or access a new distribution channel (e.g. D2C)—or a belief that a larger combined business can drive significant scale cost synergies, as well as opportunistic purchases, are the most common motivations for M&A. To successfully achieve those ends, firms need to address several key questions, including which elements of the individual business operating models need to be integrated, and the cost of integrating or upgrading technology and processes. Similar considerations should determine the integration strategy.

For example, the industrial logic of a domestic investment management deal between propositionally similar firms, focused on creating cost synergies in operations and de-duplicating front-office capabilities, will drive different integration priorities to, say, a cross-border transaction between geographically or propositionally diverse firms, where revenue synergies through distribution are of greater delivery importance.

Similarly, in a wealth management context, valuation multiples expand for bigger and more diverse businesses with more stable, recurring earnings. That multiple expansion, created through both scale and extension of economic participation across the value chain, will often be a key value driver of M&A; to maximize this, demonstrating you have consolidated the

“advice process” to a controlled platform and/or investment solution is vital.

Lastly, any integration plan needs to be alert to existing issues in either the acquirer business or issues at the target identified through diligence; simply combining two challenged businesses will not, of itself, solve problems, however effective the programme management.

Hence the integration plan and priorities absolutely need to be driven by the strategic rationale for a transaction, the desired end state, and any known issues. Each will differ. However, all the firms who have contributed to this report agree: when it comes to M&A and the integration challenges that follow, plan always beats no plan—and early plan beats late plan.

The Integration Director at a global investment management firm says that all the assumptions that govern the purpose and execution of the deal should be stated clearly, agreed very early on, and embedded in the governance structure. “Normally, something like 10 to 15 key assumptions should be stated and agreed at the very start of the integration process,” he says. “This is crucial to set the scene.” The Director of Corporate Development at a UK wealth management firm adds; “a key mitigation of deal risk is making sure that all the major integration issues are outed as early as possible; you have to make the threshold for issues a low one. And that means you need to lock down questions like how the balance of cultures will be managed between integrating firms, how long managers will stay at the newly integrated firm, what the front office view is on strategies and approach for the future, plus any due diligence issues.”

Moreover, timing is frequently the making—or the unmaking—of M&A deals. That is not just about being lucky on market timing (although history shows that the perception of transaction's success can certainly be aided by buoyant markets in the year or two after closing). However, from an integration perspective, our clients tell us that dealmakers need to be selective in deciding what needs to be in place early, and what needs time to mature, and what doesn't need to be done at all.

Forcing integration can be culturally counter-productive where the aim of the M&A activity is increased revenue scale or capability, rather than cost synergy, says the Head of Acquisitions at a UK wealth management firm. “We are not very aggressive on integration timescales, as cost synergies have not been a key driver of our deals. Our acquisitions usually retain responsibility for running their own businesses.”

“Where issues are kicked down the road with a view to sorting them out later, that typically does not go well.”

#### UK Asset Manager.

Timing does not mean that integration is always best done fast. The Chief Operations Officer at a UK wealth management firm says that speed can be the enemy of success in some post-merger integrations. “We performed a post-deal client migration that was done to a deadline with great time pressure. There was not enough time to syndicate thinking, it landed poorly with client managers and they did not feel as if they owned the process. And as a result the whole exercise has had to be repeated, more carefully.” ➤

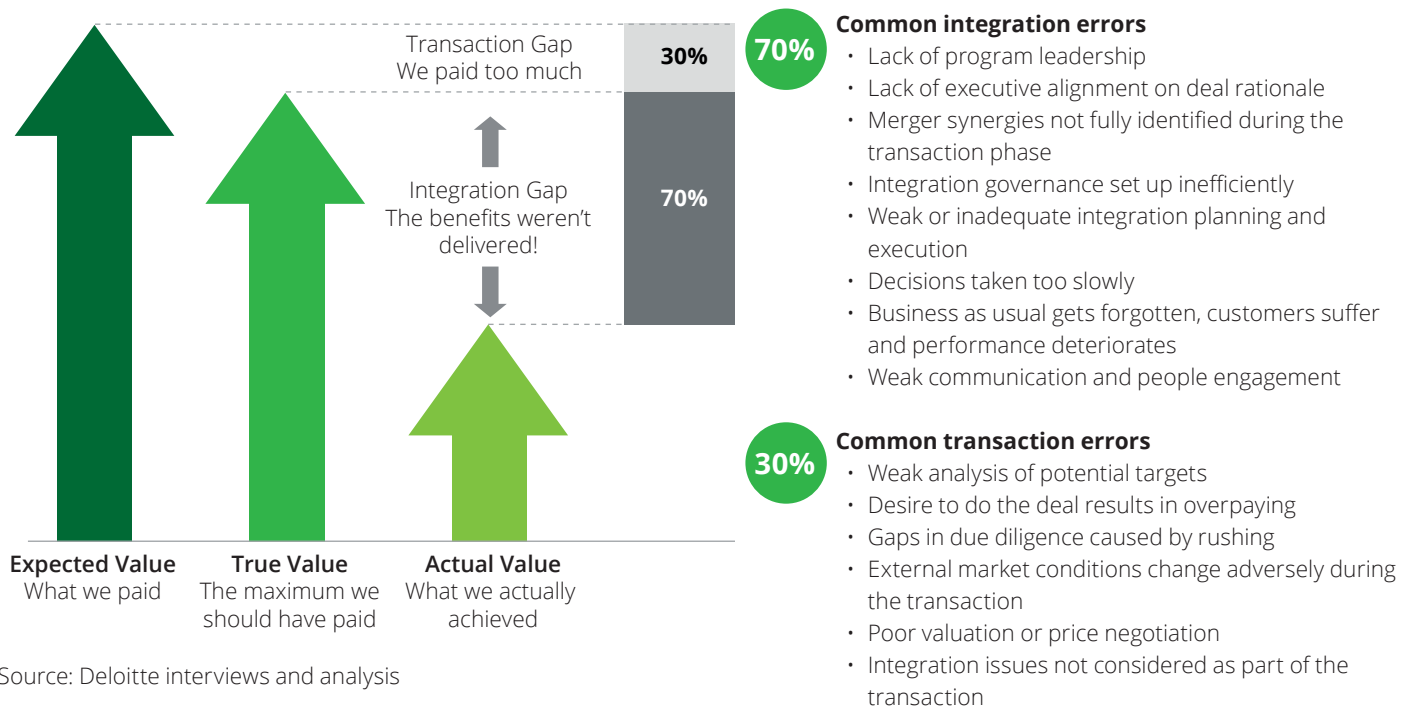
**How to manage integrations**

**Merger failure is seldom caused by buying the wrong business—it’s more about how it is integrated.**

As many large corporates have learned to their cost, managing the integration phase of an acquisition is very challenging. The risk is that the value of the deal becomes eroded during the integration phase, and can even be lost entirely as costs

rise and key talent leaves the business. Planning and a clear structure are vital from day one. “Managing integrations well requires both management expertise and management capacity. We have recently seen integrations that have gone wrong because of the difficulty of keeping the day-to-day business running at the same time as managing the integration,” says Andy McNeil, Partner Deloitte.

Figure 2: the integration gap



“The governance structure is critical. Typically the Chief Operating Officer and the Chief Technology Officer team are involved in governance—but one thing is sure, if you lack a governance structure then it is bound to cause issues.”

**UK Asset Manager**



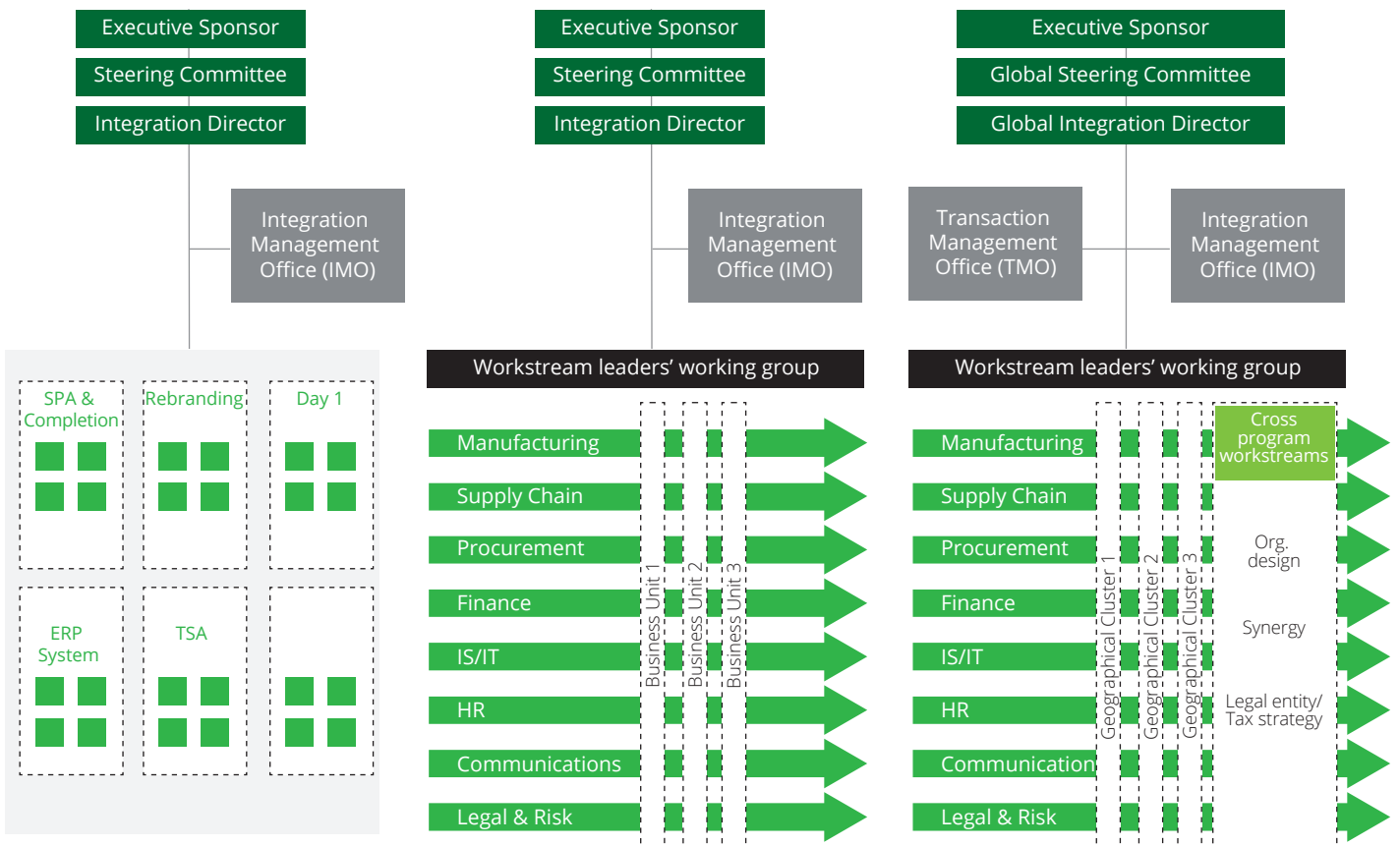
According to experienced integration managers investment and wealth management businesses, the most effective responses to these challenges involve structuring the integration process with a sufficient level of work-streams and resources, and ensuring an adequate flow of quality management information including risks, issues, and dependencies management through planning to execution stages. Furthermore, program structure and roles and responsibilities should be customized based on integration requirements. ➔

“Where integration issues are left unaddressed they can come back and bite you a lot quicker than expected, because of the way that everything gets put through the integrated system shortly after completion.”

UK Asset Manager

Figure 3: example governance structures

Source: Deloitte interviews & analysis



For example, a wealth manager with extensive integration experience cited 10 or 11 work-streams—and in the case of a large global investment management integration, the acquiring business set up 26 work-streams globally. “Particular investment was made in traveling and bringing people together,” says the Integration Director. “More time than may be usual was spent together, quite a lot of people moved location temporarily, and the two firms became more embedded as a result, with the firm moving to a single model in nearly every function over time.

“Good management information throughout the process is key. This requires honest status reporting from all work-streams—management needs to be forewarned of problems, and you shouldn’t end up with a sudden switch from green status to red. Neither should the CEO just assume these things will be okay—they need to be managing and running the process, and making sure the IMO is able to manage across cultures.” In our experience, the reporting needs to cover not only financial, but also operational and cultural metrics.

## Managing Integrations

We asked senior executives at a range of investment and wealth managers to describe typical issues with managing integrations, and how they addressed those challenges.

**Invest in a well-resourced Integration Management Office (IMO)** suggests the Integration Director of a global investment management firm. “Investment managers are typically smaller than banks and that means that heads of department are often managing people across multiple locations. This is unique to investment management, it causes challenges, and integration needs to take this into account. This is where we found that an IMO makes a big difference, especially when it comes to collection of accurate information.”

### **Don’t let integration challenges interfere with business-as-usual**

counsels the Chief Operating Officer at a large wealth management firm. “We have had integration managers who are external and that has worked well,” he says, adding; “ideally we would prefer the head of integration to be an internal resource. But, that said, you do need someone to manage the integration who does not have a senior business-as-usual role, and that probably also means the role has to be specifically incentivized.”

### **Cross-border mergers bring special integration challenges**

“The regulatory issues are unique,” says a senior executive at a global investment management firm. “The US SEC is a rules-based system, whereas almost every other regulator is principles-based. This makes it challenging to interpret and correctly apply the regulations, and therefore challenging to integrate.”

### Conclusion

Every integration is different—not least because the operating model and culture of every investment and wealth manager is different, so each combination is unique. Yet the conclusion we draw from our research in the sector is that there are consistent and practical lessons that can be drawn from recent experiences.

We find the six common areas of concern that should be top of mind in all investment and wealth manager M&A projects are setting **strategic direction**, working towards **cultural fit**, systematizing **integration management**, and securing the **talent base**, as well as planning for **technology integration** and setting realistic **synergy targets**.

The individual M&A stories may be different, yet the success factors are often the same. In our research across the sector, three M&A success-or-failure themes emerge repeatedly:

#### First, and most obviously, plan beats no plan

The number of firms that assume that superficially similar businesses will be easy to merge is surprising. Our interviews stress that in fact no merger is easy. The merger and integration plan has to be clear on what should be integrated, and what not. It should be informed by the costs of merging even slightly incompatible systems (balanced by the cost of running dual systems). It should include executive functions, sufficient work-streams, staffing, and a properly resourced IMO. It should also recognize that synergy is not the only driver of M&A, yet if synergy is the target then early synergy wins are more likely to deliver than deferred synergy benefits. All of this means that a clear integration plan, pre-signing, is crucial to firstly assessing the merits of a transaction, and then actually executing it in line with expectations.

#### Secondly, speed is critical

However, the right speed of integration does not necessarily mean fast. While all issues should be 'outed early', time taken to complete integrations is often the key to avoid attrition of talent and clients in people oriented businesses. Investment and wealth management businesses are easy to disrupt, and disruptive integrations that are run too fast for comfort, can risk the entire business. Set a responsible speed and stick to it.

#### Thirdly, culture is remains a key challenge as an M&A issue

Mergers throw up multiple issues of cultural difference, especially when the merging entities come from different worlds. Managers say cultural issues take the longest to finalize in integrations, and can be the hardest to flush out earlier in transactions, due to information and access restrictions. However, they have the biggest impact on outcomes, and seemingly, small issues often have outsized effects.

These are the leading challenges. Our survey also suggests that there are solutions: identify issues and solicit key player buy-in early, plan integrations intensively to minimize disruption, expect technology costs and devise cost mitigations, and aim for consistency in the merged business.

#### To the point:

- Merging cultures is the hardest challenge to resolve
- Talent retention is a key risk area
- Integrations need to be managed extensively
- Technology integration is key to deal success
- Synergy targets are frequently too vague

# Engaging the whole firm

## Improving client experience in institutional and wholesale investment management

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In the investment management industry, it is often said that investment performance is the predominant factor by which clients judge investment managers. While there is certainly some truth in this statement, in reality, clients take an approach to judging investment managers that is both broader and more nuanced. Investment performance will remain key but, with competition intensifying in the market, investors tell us that client experience is increasingly important. In a recent paper by Deloitte-Casey Quirk, *Distribution 2.0*, we reported that 76 percent of buyers client experience is a contributing factor to manager terminations.<sup>1</sup>

But, what exactly does client experience mean and what is it that really matters? Despite the market's increasing focus on this area, there is a lack of publicly available research, and feedback from clients to managers can be patchy and anecdotal.

To address this gap and tell the story of what shapes the experience from the client's perspective, Deloitte interviewed fifteen investment management clients from institutional and wholesale channels, including wealth management, insurance, and pensions in the UK and the Netherlands. Our interviews were semi-structured and clients commented on past experiences.

Our aim was to move the debate forward from 'there are moments that matter' to developing a deeper understanding of the most important drivers of client experience.

In our recent report, *Engaging the whole firm*, we addressed this issue in three ways. First, we examined the perspective of clients, as captured by our interviews, to understand their experience of dealing with investment managers, their concerns, and what is important to them. Second,

we analyzed the client feedback that we received and presented a framework for thinking about client experience (CX). Lastly, we considered the implications of our research findings for investment managers.

This article provides an overview of the key points raised by our research. The full report can be found: <https://www2.deloitte.com/uk/en/pages/financial-services/articles/engaging-the-firm.html>

### Investment management CX: the client perspective

Our interviews with clients of investment managers identified a wide range of issues that they consider important in their dealings with investment managers. We have grouped these into seven 'drivers' of CX (Figure 1).

<sup>1</sup> Distribution 2.0, Casey Quirk by Deloitte, March 2019, <https://www2.deloitte.com/us/en/pages/financial-services/articles/technology-asset-management-distribution-whitepaper.html>



**Figure 1: Seven drivers of investment management client experience**

**Partnership approach**

- Offering solutions and bespoke relationships
- Strategic (broad) partnership
- Manager-client knowledge transfer

**Doing the basics well**

- Timeliness, accuracy and quality of reporting
- Accessibility of information and data
- Co-ordination across client touchpoints

**Operational friction**

- Speed of operations
- Accuracy of operations

**Attentiveness**

- Responding to data/information requests quickly
  - Proactively sharing data/information
  - Resolving issues quickly

**Clarity of purpose and communication**

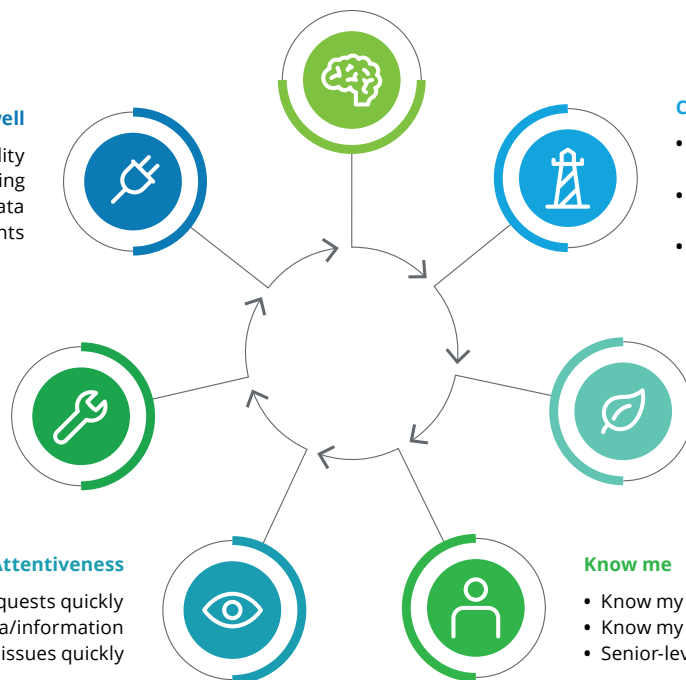
- Explanation of portfolios, products and processes
- Articulation of edge or point of differentiation
- Transparency of fee structure

**Long termism**

- Sales approach
- Longevity of client-manager relationships
- Transparency of relationship

**Know me**

- Know my end investors (and show me)
- Know my business (and show me)
- Senior-level client-manager relationships





### Doing the basics well

Clients and investment consultants commented on the timeliness, accuracy, and quality of the reporting they receive from investment managers. Our interviewees noted that reports can be late and/or contain errors, and this erodes the credibility of reports, makes it harder for the recipient to get an up-to-date view on performance and, in the case of investment consultants, can increase the workload in the run up to client meetings.

“Reporting is a big factor. Reporting's quality is determined by its regularity and clarity. Sometimes we encounter errors in the reports.”

### Group Pension Manager Pension Scheme

“It's all about getting access to the right people and information. In the future we'll see more automated ways of providing ongoing information.”

### Investment Consultant

### Providing access to information

**and data** outside the reporting cycle also affects the client experience. It is frustrating for clients to expend more effort than expected on retrieving information and/or data, particularly as this compares badly with the quick and easy access to information that they enjoy as self-service retail customers in other industries.

A good experience is dealing with an investment manager that is **co-ordinated across multiple interactions**. Clients said that it is important for an investment manager's people to talk with each other (and with the investment consultant where applicable) to agree a united front. A lack of co-ordination can reduce the quality of service. For instance, a lack of information sharing among client-facing staff at the investment manager makes it harder for the manager to really understand the client's needs in depth.



### Operational friction

Our interviewees stated that operational friction has an important effect on their overall experience with, and perception of, an investment manager. In particular, they cited two criteria by which they judge managers: the speed and the accuracy of operations. One wealth management client commented that transfers from one platform to another should be faster.

“On the ops side, it's about: Don't surprise us; I just want this to work.”

### Head of Funds Global Bank-embedded Wealth Manager





### Attentiveness

For our interviewees, the **speed with which investment managers respond to requests for information and data** is a driver of the overall experience. Quick responses to requests for information, data and opinions help the client to be well-informed on markets and portfolios, and this builds transparency in the client-manager relationship. In addition, some interviewees held the view that response speeds are determined by the empowerment of client-facing staff, implying that a responsive manager is also a well-organized manager.

Furthermore, quick responses allow clients to serve their internal stakeholders better. A pension client said that when managers respond quickly to his questions on capital market developments, this in turn helps him provide more informed and faster answers to queries from trustees.

“There are times when I may need data and ask for it at the last minute, and in these cases, some can turn it around and that helps me pitch to my firm. I'd say turnaround times play a big role in client experience. In addition, there's a big dispersion in the speeds with which asset managers can respond.”

**Head of Fund Research  
Wealth Manager**

We were told that an important component of good client experience is working with an investment manager that **shares material information and data proactively**.

Proactive sharing of material information increases transparency around the factors that are relevant to investment performance, and this in turn helps the client to make better-informed decisions. In addition, when a manager shares ideas proactively, the client sees the manager-client relationship as a joint endeavor.

On the other hand, withholding material information from the client is a poor experience. One wealth management client recalled a time when he was not told about two analysts leaving a fund: this was a poor experience because it was a material item of information and he felt uninformed when this news eventually did break. Allied to this, clients said that it is important for managers to use a communication channel appropriate to the gravity of the message. For the most important information, there is no substitute for a timely telephone call.

A key concern is the **speed and efficacy of an investment manager's responses to issues and challenges**. Our interviewees see this as an indication of both how well-organized the manager is, and how well they know the client.

“Responsiveness matters. How the investment manager responds when something goes wrong is important. This gives you a good insight into how well organized the manager is, and how well the manager knows you. We had an issue and the manager effectively put a SWOT team on it, talking to us and reassuring us that the issue was being put right.”

**Group Pension Manager  
Pension Scheme**



### Know me

Several interviewees said that it is a good experience when an investment manager **demonstrates an understanding of the client's business**. This engenders confidence in the manager's ability to recommend and/or build the best products for the client's needs. The opposite is also true. When an investment manager shows a lack of understanding of the client's business, this undermines credibility and worsens the experience. One wealth management client illustrated this point by recalling how certain investment managers had recommended a type of fund that his firm manufactures in-house.

In addition, understanding the client's business means that time-wasting is less likely. One investment consultant cited cold-calling and unnecessary emails as examples of poor experience stemming from not knowing the client's business well enough.

"[Manager X] has been very in tune with what we're trying to achieve. This is positive for client experience."

**Investment Proposition Manager  
Defined Contribution Pension Provider**

Allied to this point, clients with end investors said that they appreciate dealing with investment managers that demonstrate an **understanding of their end investors**. This is a feature of good experience because it gives clients confidence in the manager's ability to recommend and build successful products. An interviewee from a Defined Contribution (DC) pension provider said that his experience of managers had been partly shaped by their understanding of the costs and operational constraints in the DC market. He recalled how, in the wake of pension freedoms (ending the compulsory purchase of annuities in the UK), investment managers and banks developed annuity-like products that were innovative yet too expensive for DC savers. Being recommended these products was a poor experience because it revealed a lack of understanding of what would work for end savers in the DC market.

Clients like having **senior-level relationships with their managers**. This demonstrates commitment on the part of managers.

"A good experience, for example, has been dealing with [investment manager X]. They've provided us with access to their top people."

**Investment Proposition Manager  
Defined Contribution Pension Provider**





### Long-termism

Interviewees commented that a **long-term approach to sales**, as opposed to a more short-term and sales-led approach, is a positive factor. Most obviously, a long-term approach to sales builds trust in the manager, which in turn helps to demonstrate the value the manager is delivering.

In addition, a long-term approach builds credibility in the manager because it demonstrates an understanding of the strengths, weaknesses and suitability of different funds. In contrast, according to one interviewee, a sales-led approach in which all funds are pushed equally hard can signal a degree of naivety in the salesperson.

"Sales behavior for the long-term is key, and providing the ability for investment manager and client to have a multi-year relationship matters."

### Head of Funds Global Bank-embedded Wealth Manager

Closely linked to this point, the people we spoke with commented that a transparent relationship with investment managers is a good experience because it builds trust. This issue can arise when clients judge how well relationship and portfolio managers respond to questions; receiving open and direct responses to questions is a good experience.

"Once appointed, the client experience comes down to the strength of the relationship. Openness is very important."

### Head of Division Investment Development, Wealth manager

Clients said that maintaining **long-standing relationships between their people and their opposite numbers** at investment managers is a good experience because it fosters confidence. Clients recognize that it takes time for salespeople to develop a deep understanding of his or her firm's products, and the firm more broadly. However, once this understanding has been achieved, clients become more confident that the manager's salespeople will select and recommend the best products for their needs.





### Clarity of purpose and communication

Clients and investment consultants agreed unanimously that another aspect of good experience is receiving a **description and explanation of portfolios, products and processes** that is clear and easy to follow. This helps to build the client's understanding of the investment manager's value proposition and to set the right level of expectations. In turn, this has a large impact on the experience once the manager has been appointed. With expectations calibrated at the right level, the client is less likely to be disappointed by performance. In addition, being unable to follow an investment manager's explanations of key points can be frustrating for clients.

"Managers can struggle to define their edge—in other words their point of differentiation—and this dents the client experience. All managers say that they're long term investors. Manager X is brilliant at this, they can clearly demonstrate that they are different."

### Head of Fund Research, Wealth Manager

Finally, two interviewees raised the specific issue of **transparency of fees**. They stated a preference for market-standard (i.e. flat) fees on assets under management, rather than more complex and harder-to-understand performance-based fees.



### Partnership approach

Some of our interviewees indicated that they are looking for a partner that is willing and able to **transfer knowledge and insight**, in addition to managing investments. One client said that a large part of the value proposition of an investment manager is knowledge, adding that this matters more in insurance investment management than in other client segments.

"Finding a partner is key—someone who is willing to work with us. We like an investment manager with credible experts who can speak on topics of interest—things like public policy. Manager X is great on this. They have a warm body in the firm who can speak on just about anything, from smart-beta to factor investing to tax to insurance regulation—and this kind of expertise is helpful."

### Vice President, External managers, Insurer

Interviewees said that clients are interested in forming **strategic partnerships** where the manager services the client across a range of needs (e.g. multiple investment classes). This is a good experience because the client can benefit from economies of scale from multiple investments with a single provider. In addition, there is a better alignment of interests between manager and client than with a narrower relationship.

Some clients want an investment manager to work with them to build **customized solutions** and see close partnerships as the best kind of relationship for achieving this. In such cases, close partnership is a good experience because it builds trust and credibility in the investment manager's efforts to build a client-specific solution. Conversely, dealing with a disengaged manager is a negative experience.

"Dealing with Manager X has felt like a dual partnership. Conversely, we had one manager offer us something off the shelf then come back with something more tailored to our requirements only when he found out other investment managers were in the hunt."

### Investment Proposition Manager, Defined Contribution Pension Provider

Interviewees gave us extensive and detailed feedback on their experiences with investment managers. This feedback demonstrates that CX is a broad topic, covering a diverse range of areas from operations to sales approach to strategic partnerships. However, across all seven drivers of CX that we discussed with clients, we observe that at its most fundamental CX is influenced not just by what managers do, but also what they don't do, the behavior of their people, and the timing of interactions between managers and clients.



## Investment management CX: a framework

So far, we have presented client feedback as seven drivers that clients believe have a material impact on their experience of dealing with investment managers. Clearly, this feedback should be of interest to investment managers. So what should they think about this feedback, and how should they make sense of it?

To answer these questions, we provide a framework for investment managers to think about client experience. Within this framework, some of the seven drivers have an immediate and direct impact on interaction with the client. Others are more long-term and strategic, impacting relationship-building and alignment between managers and clients. Given these differing time horizons, we suggest that there is a sequence in which to address the drivers of CX.

To provide clarity on this point, we group the seven drivers into three levels,

which we refer to as ‘Do’, ‘Deliver’ and ‘Differentiate’. Put simply, client feedback shows that it will be hard for managers to build a high quality client experience that is differentiated, unless they can execute the day-to-day aspects of the client-manager relationship well, even if this goes unnoticed until something goes wrong.

### Do

The first level concerns doing the basics well and avoiding operational friction. Its significance is that clients consider these aspects of their interactions with managers to be fundamental but unremarkable. If a manager executes poorly at this level, the experience slips into negative territory. However because good execution is something that is expected, when it is achieved the client experience is likely to be neutral.

### Deliver

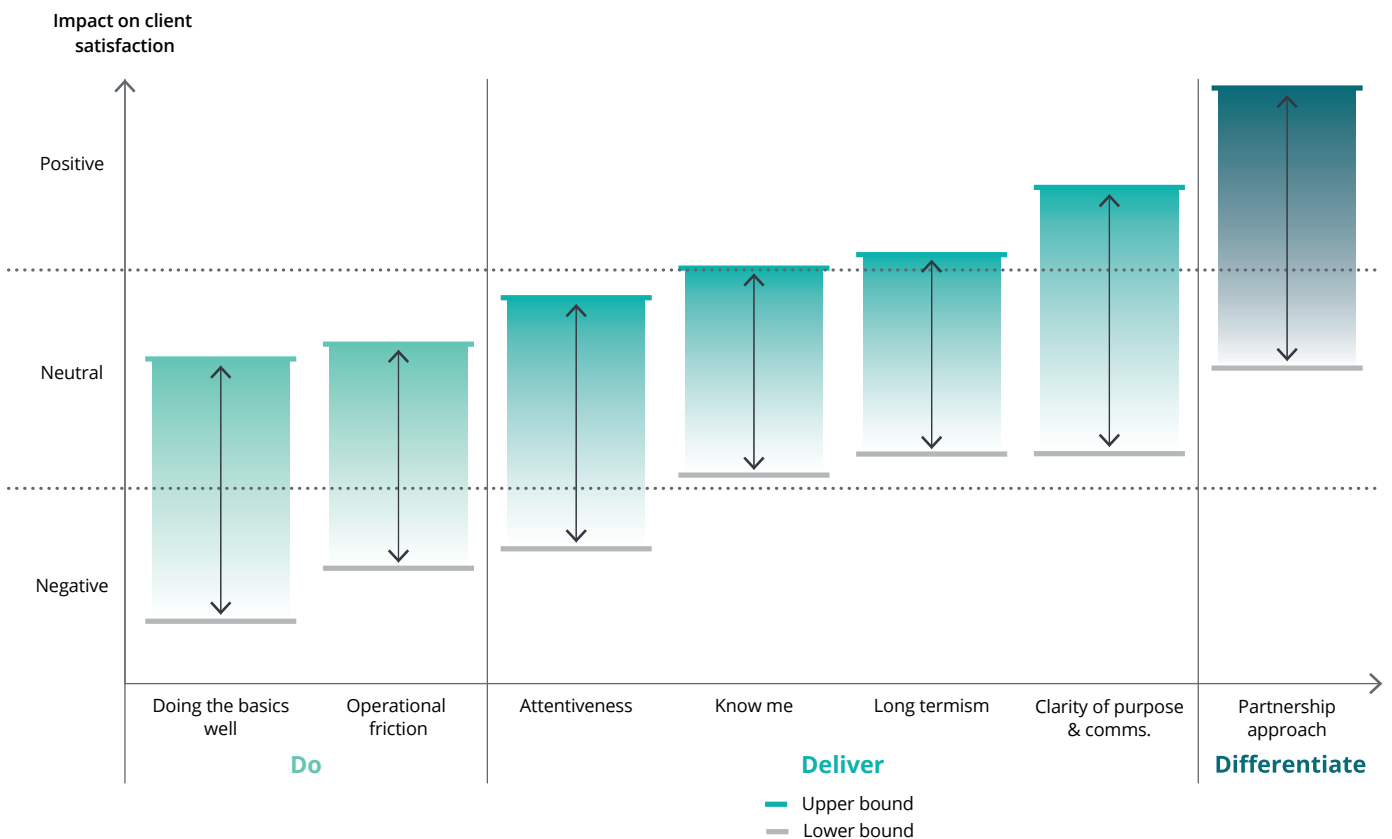
The second level is broad and covers four main drivers of client experience. These are being attentive, knowing the client,

adopting a long-term approach, and being clear about purpose and communications. These are core aspects of the experience with the manager that clients expect to run smoothly. If they are executed poorly, the experience could turn negative. In contrast, if they are executed well consistently, there is scope for enhancing the client experience.

### Differentiate

The third level has the greatest potential for improving the client experience, but is the hardest to execute well. Virtually all the clients we interviewed became animated when discussing how managers could operate more effectively by adopting a partnership approach. They would like, but do not expect, to forge partnerships with select investment managers that are characterized by a deeper level of co-operation than is generally found in client-manager relationships. If a partnership approach is executed well, this is a strong positive for client satisfaction (Figure 2).

Figure 2. Investment management client experience hierarchy



### The CX hierarchy

As a final observation, we suggest that these levels are not discrete and are in fact cumulative. Clients think that it is hard to develop a partnership with their investment managers when the relationship is at a lower level, characterized by operational difficulty and other frictional interactions, a lack of attentiveness, or when managers display an extremely short-term outlook. Therefore, investment managers need to **Do** the basics well and **Deliver** on the core of their relationship, if they wish to develop a **Differentiated** long-term partnership with their clients.

## Implications for investment managers

The investment management industry is increasingly competitive, and although margins are still healthy relative to other industries, they are starting to reduce. In addition, managers are developing new capabilities such as solutions and real assets. Against this background, **what are the implications of our CX research findings for investment managers?**

First, investment managers should recognize that it is essential to do the basics well but that this **requires investment**. Areas of potential friction with clients get in the way of building a positive relationship and, during periods of performance challenge, these frictional items create additional 'noise'. In addition, the ability to be operationally sound and reliable is a fundamental platform on which to build a strategic relationship. At a time when margins may be under pressure, and there are front office demands on investment, **managers should not neglect the investment needed to deliver a good client experience.**

Second, clients have given feedback about the seven drivers, which relate to skills and capabilities across the entire investment firm. Functionally areas such as operations, client service and sales are impacted, but other less visible areas such as the technology underpinning the client relationship are also affected. This re-confirms our view that to excel in client experience at the highest level, **a whole-firm approach is required.**

Lastly, in addition to having implications for investment and building capability, client experience is, as much as anything, a cultural issue. Firms should make it part of their DNA to deliver a positive client experience and ensure that it is not just the responsibility of sales and client service or client operations staff. **Building a culture for a positive client experience should be a continuing priority at the highest levels of the firm**, permeating everything that the firm does. Only then will it have a lasting influence on both operational and strategic choices of the firm. ●



#### To the point:

- Client Experience (CX) is a broad topic, covering a diverse range of areas from operations to sales approach to strategic partnerships, however this research has identified seven key drivers of CX
- At its most fundamental, CX is influenced not just by what managers do, but also what they don't do, the behavior of their people, and the timing of interactions between managers and clients
- We provide a framework for investment managers to think about client experience. This framework shows that some of the seven drivers have an immediate and direct impact on interaction with the client; others are more long-term and strategic, impacting relationship-building and alignment between managers and clients
- Given these differing time lines, we suggest that there is a sequence in which to address the drivers of CX

# The future of the asset management industry

Noel Fessey, CEO European Fund Administration S.A. looks at what is shaping asset management and servicing.

**The views expressed in this article are the personal views of the author and not those of Deloitte**



### Passive aggressive: here to stay

Passive investing is more popular than ever for a simple reason: on average, active managers under-perform markets after fees and costs, and those who out-perform do so more by luck than skill. Index funds and passive ETFs, if well implemented, reliably deliver the index less a small cost. Since most investors do not have the skill to choose good active managers, they are better off going passive.

Influenced by marketing campaigns, low cost, stories of active manager closet tracking, and reforms of practices such as trailer fees, investors have embraced passive investing. In the US from 1995 to 2017, cumulative net flows into passive funds were US\$4.2 trillion compared to US\$2.4 trillion into active funds<sup>1</sup>. In June 2019, Vanguard reported<sup>2</sup> that ~40 percent of all US mutual funds were index funds, only ~15 percent of all US equity investible securities were owned by equity index funds, and less than 5 percent of US exchange trading volume was driven by index strategies. Passive investing has further to go—but it is here to stay.

### Beta have a smart answer

Smart beta is the active industry's tacit confession that most portfolio managers can't produce alpha, and can be replaced by low cost reliable beta spiced up with bets on volatility, liquidity, quality, value, size, momentum, whatever (hence the term factor investing). Alpha purists and active manager veterans dislike smart beta. They fret about their incumbent interest and reputation; what does it say about their active franchise? Pragmatists consider it an essential and legitimate response to the passive industry's encroachment into their markets: when facing substitution risk, have your own substitute product ready (which is partly why index purists also dislike it). Cannibal child of the active industry though it is, smart beta is also here to stay.

### Pure alpha: the new unobtainium

Alpha nevertheless remains the quintessence of active investment management. Which is a problem, because it is horribly difficult to obtain. In 1975, 15 percent of active managers were skillful (producing alpha after fees and costs).

In 2006, only 1 percent were<sup>3</sup>. Why? Uniform fair disclosure laws and technology have made financial information a commodity with little alpha potential, even for assiduous readers of small print. Alpha-generating information advantage is therefore harder to find. It decays as more people find and use it, and they have learned to use it very quickly indeed. Clever investment process also counts less: post-crisis public markets are structurally different; alpha is a zero-sum game the quickest win, and most active managers are not quick enough. ➤



1. Working paper RPA 18-04, Federal Reserve Bank of Boston, 27 August 2018.

2. Don't stop believing in the benefits of indexing, Vanguard website, 17 June 2019.

3. The future of investment management, Ronald Kahn, CFA Institute Research Foundation, 26 May 2018.

### It's not rocket science. Is it?

What can active managers do? In the past 15 years, socio-economic and non-financial data have grown exponentially—and will keep growing. They are available in countless dimensions and formats. Vast data lakes contain potentially valuable investing signals. Active managers trawl them with cloud-based big data technology and data science, seeking information advantage, to detect and win alpha before the advantage decays. Speed is of the essence, decay inevitable, restless innovation vital. Data scientists research alpha as if it were a sub-atomic particle or an astrophysical puzzle. But caution: too often "big data" and "easy" are heard in the same sentence. It isn't easy, and it's especially hard to infer a signal's cause and use it to produce alpha. Perhaps there's still room for the old ways. Value investing, anyone?

### Squeeze them until the bps squeak

There may still be room for value investors, but not on yesterday's terms. Between 2012 and 2017, passive managers reduced fees by 25.7 percent and active managers by 8.6 percent. Fees may drop another 20.7 percent and 19.3 percent respectively by 2025<sup>4</sup>. The loss of market share to passive

adds to the pressure on active managers. They nevertheless increased margins by more than 10 percent between 2012 and 2017 thanks to 53.7 percent growth in assets under management (AuM) and by reducing cost ratios faster than fees, despite spending more each year on technology and operations. At some point, the AuM growth elevator will slow, maybe even fall, yet the squeeze on fees will go on.

### Three steps to heaven

Active managers are responding in three ways: positioning, operational redesign, and corporate mergers. First, they are more clearly articulating value for money—such as pure alpha or the benefits of non-financial returns—and diversifying onto a broader stage and better terms, where passive managers can't easily follow. Private assets (equity, real estate, debt) fit the bill nicely. Bank retrenchment in the past 10 years has enabled asset managers to draw institutional investors into private assets, where price pressure is lower and client longevity greater. Positional shifts also include other alternative assets, outcome-based solutions for institutional investors, and wealth services for mass affluent and high net worth individuals.

Second, they are redesigning their operations. This is not big data, nor fiddling with robotic process automation. It is a fundamental rethink of what to keep in-house. Everything but the core investment process will be a candidate for outsourcing. Investment book of record, order management, trade processing, collateral management, portfolio administration, risk measurement, compliance monitoring; all and more will go to firms who specialize in cloud-based front-to-back-office services. This will profoundly change asset managers and service firms.

Third, they are merging to reduce cost and gain scale. Well, that's the theory, and it's as old as the industry. Yes, M&A hit an 11-year high of 253 deals globally in 2018<sup>5</sup>, but alpha and scale do not sit well together, nor do alpha males thrust together by merger. Integrating asset managers is notoriously difficult and, for as long as margins remain viable and customers slow to switch (common behavior in this and other industries), owners will hesitate to sell. This is partly why, after years of difficult conditions, there are still 4,200 asset management firms in Europe<sup>6</sup>.

In the past 15 years, socio-economic and non-financial data have grown exponentially—and will keep growing.



4. Asset and Wealth Management Revolution, Pressure on profitability, PwC, October 2018. (All numbers in this paragraph.)

5. M&A activity in fund sector breaks 11-year record, Chris Flood, Financial Times, 16 February 2019.

6. Asset Management in Europe, EFAMA, September 2018.





### Shop till the competition drops

M&A activity in the asset service sector is also up. Price also drives change here: the top five global custodians, pressed by asset managers suffering fee compression, reduced charges by 18 percent per unit of AuC/A in the five years to 2017<sup>7</sup>. Struggling with innumerable post-crisis regulations and the debilitating effect of unorthodox monetary policy, they can ill afford this, but competition for clients is brutal. Smaller administrators are compelled to follow. A shakeout is underway, in which three themes stand out: scale, sector convergence, and technology bets.

First, it is axiomatic that survival demands scale and operational gearing. Scale needs growth, which is a problem when large mandates move infrequently. Firms are therefore turning to M&A for inorganic growth. Bulge bracket firms have been active—Crédit Agricole and Santander's April 2019 decision to merge their custody and asset service units to create a €5.1 trillion AuC/A business is one recent example—but mid-market firms have been most active. One has grown its AuA from US\$35 billion to US\$622 billion through 10 acquisitions in the last three years. Inorganic growth (often funded by private equity; you need money to make money) promises scale, geographic coverage and sectoral expertise. Leading consolidators are made of this, the thinking goes, and there are plenty of targets. Well, yes, but

the targets have small clients who are inimical to scale and who do not grow, and some activities do not scale. Success depends on integration, which is expensive, and sometimes a problem shared is just a bigger problem. The mid-market private equity exits will be interesting.

Advocates of niche-as-strategy may be nodding at this point. They should pause. Price and service competition is ubiquitous. Niche-as-strategy may be wishful thinking, which competition will relentlessly expose. To survive in a niche, a firm must be highly specialized and be as well equipped with technology as its larger and better-resourced competitors, who will put great energy into drawing away its best clients. Very few niche firms will do this well, and most will subsist on small clients, unable to grow, starved of investment capital, with growing conduct-of-business challenges. The brighter future and better clients belong to the consolidators.

Second, boundaries between service sectors are dissolving. Organically and through M&A, firms are diversifying in search of growth. Take the private assets sector: asset managers, seeking product and market diversification, have built private asset divisions, which need a mix of fund and corporate services. Corporate service firms, increasingly exposed to asset managers and the alternative side of the fund industry, are challenging incumbent

Bank retrenchment in the past 10 years has enabled asset managers to draw institutional investors into private assets, where price pressure is lower and client longevity greater.

firms for a share of work on primary funds, funds of funds, securitization vehicles, etc. Having built global networks, corporate service firms are also competing with the accounting and tax practices of large audit firms.

Third, firms are making big bets on technology. In 2018, State Street's acquisition of Charles River Development (US\$2.6 billion) and SS&C's acquisition of DST Systems (US\$5.4 billion) and Eze Software (US\$1.45 billion) surprised competitors and clients. Did they drink too much FinTech Kool-Aid? Not likely. They are positioning themselves for when asset managers let partner firms move the service boundary up to and including the investment book of record, and perhaps even to portfolio construction. They are setting themselves up as vertical integrators seeking more of the value chain, and as innovators seeking a technological edge. There is a hint of defense here: BlackRock's Aladdin enjoys parental advantage in the race to be the dominant asset management platform. (BlackRock also pitches Aladdin at pension funds, insurers, institutional investors, and corporate treasurers.) As this plays out, it will focus the minds of mid-market asset servicers and software firms. There will be room for them, but the competition will be hellish, as it always has been, and it might even attract tech giants. ➤

7. Growing pains: how asset servicers are keeping up with rapid growth, PwC AWM Conference Dublin, October 2018.

## Most FinTech firms will survive only in the fossil record, extinguished by intense competition and lack of funding.

### Giants, dinosaurs, and fossils

An online bookstore founded in 1994 is the world's largest e-commerce retailer and second-largest streaming media company. It provides marketplace, finance, and payment services to merchants and is a global leader in cloud-based computer services. It offers remittance services and credit cards to retail customers and will soon offer checking accounts in the US.

A social networking app founded in a university dormitory in 2003 is the Western world's largest, where 2.3 billion people meet friends to share news, pictures and messages. It has become a major news channel, disrupting mainstream media, the advertising industry, and social and political discourse. In June 2019, it announced the launch of a digital currency—Libra—which its customers will be able to use

even if they do not have a regular bank account. (Non-banking customers are a major target: there are an estimated 1.7 billion people in the world without a bank account, but many of them have a smartphone and internet service.)

These are Amazon and Facebook — tech giants who, with Apple, Google and Netflix, dominate our digital lives. Their rise begs a question in asset managers' minds: when will they come for us? Are we dinosaurs facing extinction?

Relax. For years, grocery chains have offered checking accounts, scrip currency (loyalty points), credit cards and insurance, white-labelling financial institutions' products. Amazon works the same way and Facebook's Libra co-opts several financial giants, including MasterCard, Visa and PayPal.

Tech giants dislike anything that prevents them from deploying one global business model. They prefer to avoid regulated industries, where rules, supervision and enforcement fracture markets and inhibit tech disruption. (Libra will be interesting: politicians and central bankers responded immediately with talk of shadow banking, systemic risk and regulation; "an open mind" ... "but not an open door<sup>8</sup>," said the governor of the Bank of England). Tech giants particularly dislike uncertain customer outcomes. They do not yearn to declare that their customers' money



is at risk, that they may not get back the amount they originally invested. Tech giants have better uses for their capital and management time.

Don't relax for too long. Alibaba's famous demonstration of how to build the world's largest money market fund is a warning. Yes, it's special to China and not easily transportable into the West, but it will come. Vanguard and Invesco have joint ventures with Alibaba to sell funds in China. They and others will find ways to fit funds into our Western digital lives, perhaps becoming the merchant of record behind a tech giant's distribution power. The prize could be great: in the Eurozone, 40 percent of household assets are in cash; only 8 percent are invested in funds by 11 percent of households<sup>9</sup>. Retail is also not everything: how would your asset management CIO and CTO like to go head-to-head with Google in alpha search?

8. Will Facebook's Libra currency shake up financial services?, Noonan and Megaw, Financial Times, 18 June 2019.

9. Beyond 10% - the case for enlarging the pool of retail investors in Europe's investment funds, Mackay Williams, 2013 (The author estimates that these numbers remain true in 2019).



What about FinTech? Will this 21<sup>st</sup> century Cambrian explosion, this remarkable expansion, experimentation and diversification reshape the industry? Yes, with caveats. Most FinTech firms will survive only in the fossil record, extinguished by intense competition and lack of funding. The rest will integrate with older firms, generally in the financial technology or asset service sector. (Let's be frank: exit is part of the business plan.) Some will thrive in niches.

Very few, if any, will disrupt asset management for three reasons. The first is distribution: they face an insuperable challenge to sell enough to gain the heft needed to disrupt large firms who wield incumbent advantage. Put simply, small FinTech cogs don't easily turn big industry wheels. The second reason is most FinTechs lack real intellectual advantage over asset managers. All asset managers of consequence are necessarily technology specialists. Try implementing modern portfolio theory (1952) or any later

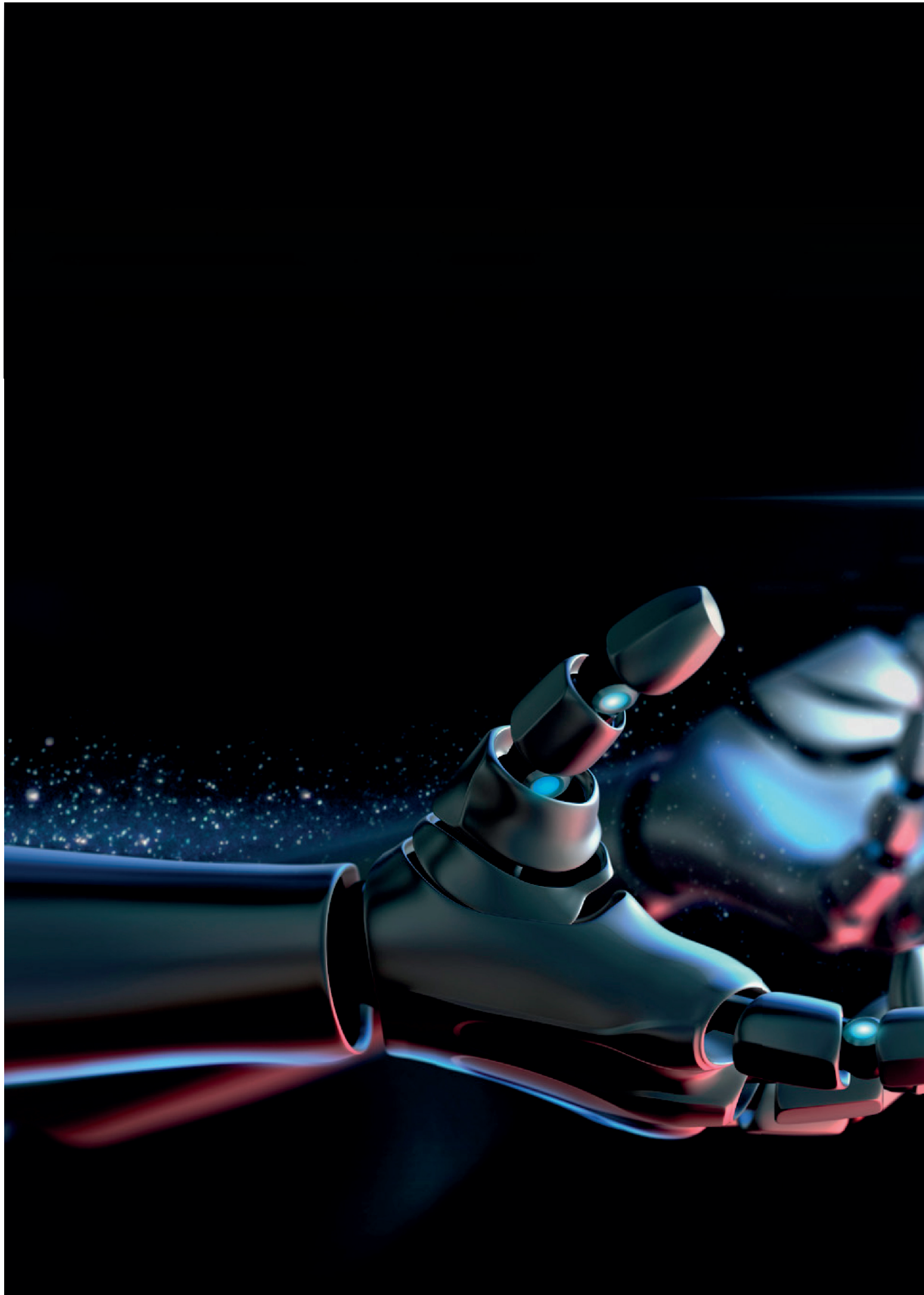
investment or product innovation without it and you will see. The third reason is most FinTechs are not trying to compete with asset managers, they're trying to sell them technology.

#### **Extinction rebellion**

So, is asset management's future passive? Mostly yes, but active management will flourish because it is antithetical to passive in three ways. First, smart beta enables investors to take views on factors that might affect their investment outcomes. Second, information advantage has not been entirely extinguished, and a skilled pure alpha investor may still be able to profit from it. Third, financial return is not the only investment goal: for many years, investors have applied non-financial goals to mandates. These, known by the acronyms ESG, CSR and SRI or as sustainable investing, increasingly define mandates. How will they shape the industry? That's a question for another article. ●

#### **To the point:**

- “Must prove value”: active managers are facing challenges from passive competitors and are responding by clearer positioning on value for money, operational redesign and M&A
- Asset service M&A is up, as firms seek scale, sector convergence, and advantage through technology
- Tech giants will not kill asset management dinosaurs (yet), and most FinTechs will become industry fossils
- TLDR: asset management's future is mostly passive, but there are three reasons why active management is not facing an extinction event



# Artificial intelligence

The next frontier  
for investment  
management firms

**Luke Halpin**

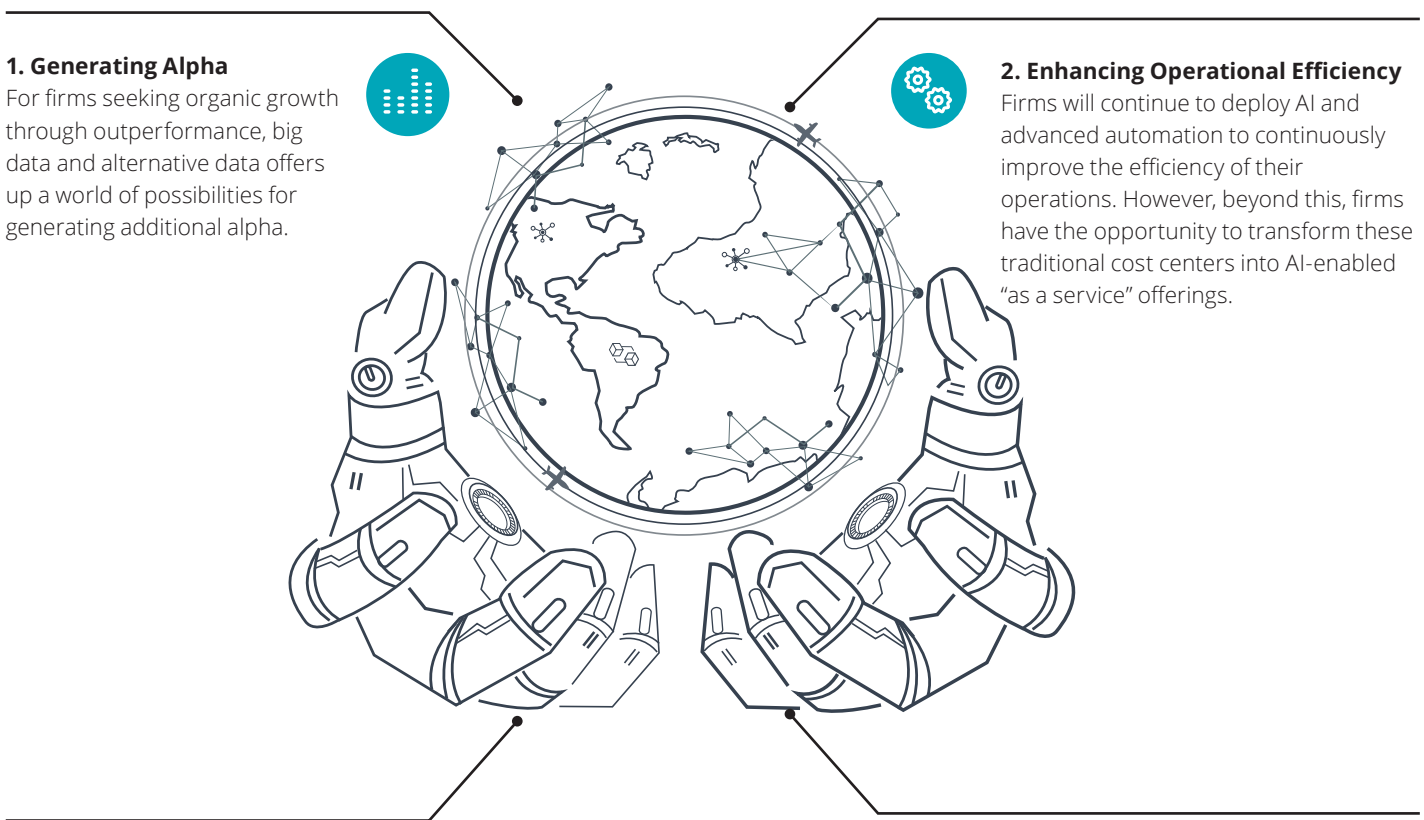
Manager  
Deloitte

### Four pillars for transformation

The evolving status quo in the investment management industry thrusts into the spotlight the growing importance for firms to make bold decisions to allocate capital to capabilities and initiatives which offer potential for transformation and value creation. We have identified the following four pillars for transformation.

When these four pillars are augmented with AI, investment management firms can rapidly transform business models, operations, and internal capabilities. The successful development and implementation of AI will however be heavily influenced by the choices that stakeholders make today with regards to a firm's technology strategy, standard

operating model, core infrastructure, and talent agenda. Firms that move early will likely stand in good stead to capitalize on these four pillars.



- Automate data analysis
- Reduce administrative activities
- Refocus employees' time to higher value-add activities

**PILLAR #1: GENERATING ALPHA**

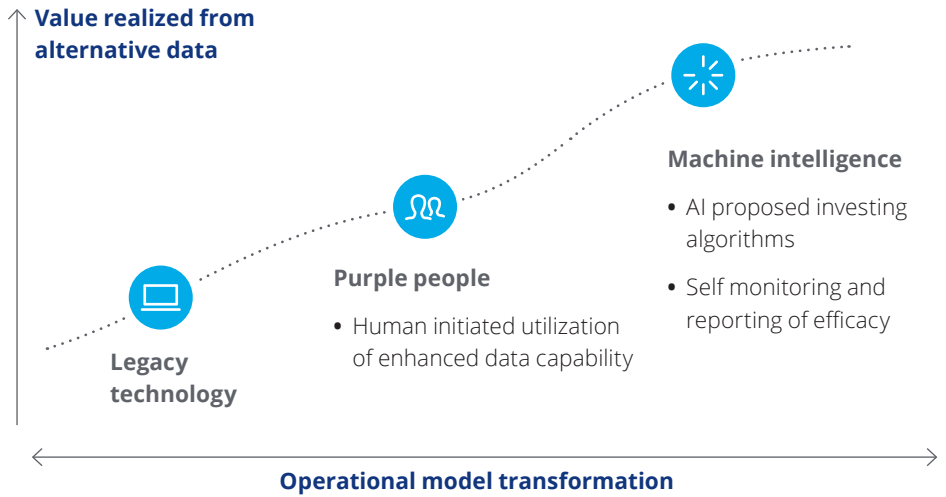
At the core of every active investment manager is the goal to generate alpha for their clients. As technology and data evolve, firms that keep pace, or lead, in the application of new approaches open up the opportunity to outperform. The rate of data creation is growing exponentially, and firms that transform data into fuel for investment insights will improve their opportunity for alpha.

**How to get started with alternative data—the operating model<sup>1</sup>**

**Alternative data adoption requires operating model changes**

An ongoing talent and technology race is on for alternative data implementation as investment management firms see the rewards of implementation. ➔

**Alternative data requires a diverse talent pool**



Investment managers could unlock the transformative benefits of alternative data adoption by implementing incremental changes in their operating model

**Points to consider while adopting alternative data**

**Adopting alternative data**

<b>Identifying the right alternative data type</b>	<ul style="list-style-type: none"> <li>Identifying the right data type and having quick access is important for integrating within the investment decision-making process</li> <li>Regular efficacy testing of the dataset signals could also be required to test for alpha decay</li> </ul>
<b>Having an integrated data analytics platform</b>	<ul style="list-style-type: none"> <li>An integrated analytics platform for undertaking different analytics promotes idea sharing and generates greater efficiency</li> <li>Combining this with traditional financial data can lead to differentiated market insights</li> </ul>
<b>Establishing a fluid data architecture</b>	<ul style="list-style-type: none"> <li>Required to manage vastly different technology, storage, and computing requirements for varied alternative data types</li> <li>System should handle multiple data feeds via API along with scalable processing power</li> </ul>
<b>Building a collaborative insights team</b>	<ul style="list-style-type: none"> <li>Insights team composed of data scientists, engineers, and analysts better positioned to derive new insights from alternative data</li> <li>Cross-functional trainings could also prepare the insights team for handling new datasets quickly</li> </ul>

1. "Alternative data for investment decisions: Today's innovation could be tomorrow's requirement", Deloitte, 2017.

### How intelligent machines can help Idea throughput

With advanced analytics of structured and unstructured data, firms can vastly improve the quantity of information used to support investment ideas. Machines can process events at roughly 2,000 times the speed of humans and they work around the clock.<sup>2</sup> Imagine a typical analyst, constrained by time, being transformed from reading a few analyst reports and listening to the earnings call for a name that they follow, into having a dashboard that summarizes all of the available reports and compares the earnings call across time and competitors. Machine-assisted analysts will likely be better.

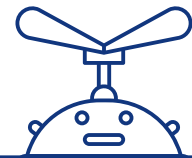
### Idea quality

Some insights may come only from digesting vast quantities of data. When faced with extremely large datasets, humans are overwhelmed without computer assistance. Computers don't get frustrated sifting through the data, searching for the magic correlations. When computers can identify these ideas and pass them along in a digestible format to their human bosses, decision quality can improve. Hypothetically, imagine a computer analyzing Boston Marathon data. What if it discovered that the frequency of a running shoe brand being worn sometimes changed from year to year. And that when

it changed by more than 2 percent it was highly predictive to the revenues for the shoe brand over the next quarter.

### If firms can do more and do it better, odds are their results will improve

Adopting alternative data can focus on augmenting existing investment processes, rather than transforming them. This approach may help ease tension between portfolio managers and data analysts. Assessing investment strategies for strategic fit for alternative data is an important early step to take. It starts with a basic question: In a perfect world, what information would you like to know as you analyze a firm? Followed by: What information do you currently use as a proxy for that information? After those two questions are answered, then a search for alternative datasets that also relate to the desired information can commence. Once found, datasets that show initial promise can be fully tested as part of the investment model. Datasets that pass rigorous testing for alpha generation can be evaluated for risk characteristics and desired controls. After the risks are understood then decision models can be adjusted to incorporate the new input from alternative data. At this point, ongoing monitoring of the drivers and results of the investment decisions can track the efficacy of changes.



### AI and alternative data in action

Man Group has been a pioneer in using AI and alternative data to support alpha generation with funds incorporating AI now collectively managing in excess of US\$12 billion. The assets under management of the UK-based hedge fund manager's AHL Dimension Fund has quintupled since 2014.<sup>3</sup> Notably, in collaboration with Oxford University, Man's AHL unit has established the Oxford-Man Institute to accelerate research into machine learning which underpins AHL's investment process.<sup>4</sup>

As alternative data use for alpha generation matures, more firms and investment strategies can be supported. At first alternative data supported event driven or other short-term trading strategies, most often used by hedge fund managers. Now, more sophisticated technologies are creating datasets that support managers with a long-term approach. Alternative data is no longer just for hedge funds.

2. "Man vs. Machine: Speed and Scale in Threat Intelligence", Chris Pace, 15 November, 2017. Retrieved from <https://www.recordedfuture.com/machine-learning-results/>.

3. "The New Physics of Financial Services. Understanding how artificial intelligence is transforming the financial ecosystem", World Economic Forum, August 2018, [http://www3.weforum.org/docs/WEF\\_New\\_Physics\\_of\\_Financial\\_Services.pdf](http://www3.weforum.org/docs/WEF_New_Physics_of_Financial_Services.pdf).

4. "The Oxford-Man Institute, Man AHL and the direction of machine learning". Retrieved from <https://www.man.com/oxford-man-institute-man-ahl-and-the-direction-of-machine-learning>.





## PILLAR #2: ENHANCING OPERATIONAL EFFICIENCY

### Back office “as a service” model—from cost center to profit center<sup>5</sup>

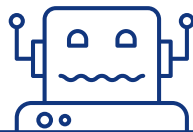
Investment management firms must be more cost sensitive in the current operating environment. Managing the cost of operations remains critical to survival in order to offset the waves of new regulations, fee pressures and the shift to lower-cost passive products. In response, many firms are undertaking large transformation programs with a focus on outsourcing and process automation.

The advancement of AI is also serving as a catalyst for firms to turn traditional operational centers of excellence into services which can be offered as a service to competitors. Non-core activities can in turn be externalized to specialist providers. Early AI adopters will have the advantage of converting these “as a service” capabilities into profit-centers and creating a competitive advantage. AI-enabled services that achieve operational excellence can continuously improve at such a rapid pace that it becomes impossible for competitors to catch up. At that point, the service becomes both a defensible advantage and a sustained revenue source for firms.

AI is also impacting middle and back office functions that firms must retain in-house

due to regulatory obligations such as oversight functions. With the power to augment monitoring and decision-making AI is a game-changer for compliance and risk management.

In operations, AI-enabled processes are increasingly being built on modular and cloud-based architecture to enable more agile operating models. Cloud-based architecture makes it easier for firms to “plug and play” with third-party services, as well as to externalize “as a service” offerings. Where service offerings are AI-enabled, they can ingest and process more data to, in turn, facilitate continuous learning and improvement. ➔



#### IM in action—externalization of best-in-class processes

Aladdin, by BlackRock, is a great example of a leading investment management firm that developed respected internal services, then made them commercially available. BlackRock’s CEO Larry Fink has stated that he wants Aladdin to make up 30 percent of BlackRock’s revenues.<sup>6</sup>



#### Efficiency is no longer a differentiator

Increasing standardization and uniformity of processes results in the commoditization of similar capabilities, prompting firms to seek out new value propositions.



#### Data solutions as the “epicenter”

The cost of operations and the ever-growing scale and complexity of data are critical speed bumps. Continuous investment in AI-enabled data solutions can help firms innovate, improve services, and reduce costs.

5. “The New Physics of Financial Services. Understanding how artificial intelligence is transforming the financial ecosystem”, World Economic Forum, August 2018, [http://www3.weforum.org/docs/WEF\\_New\\_Physics\\_of\\_Financial\\_Services.pdf](http://www3.weforum.org/docs/WEF_New_Physics_of_Financial_Services.pdf).
6. “BlackRock bets on Aladdin as genie of growth”, Attracta Mooney, 18 May 2017. Retrieved from <https://www.ft.com/content/eda44658-3592-11e7-99bd-13beb0903fa3>.

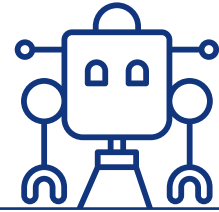
**PILLAR #3: IMPROVING PRODUCT AND CONTENT DISTRIBUTION**

AI in investment management is reshaping distribution and enabling firms to extend their distribution models into new markets and customer segments which have been traditionally underserved. AI is also facilitating scaled distribution of customized products and tailored client interactions. As sales team productivity continues to decline, driving growth in a challenging operating environment will require industry incumbents to adopt a new approach to distribution and client servicing models. AI can help firms fundamentally enhance their existing models and time-to-market. Let's take a practical example—Customer Relationship Management (CRM) tools can provide the workflow and interaction with the sales team. AI-enabled analytics can provide differentiated insights and actions. Together, these tools can equip sales teams with easier and quicker access to relevant content.

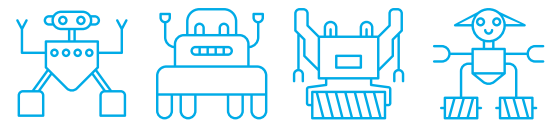
Advisor and customer segmentation, and customer experience have emerged as new battlegrounds in investment management.

AI is changing how financial institutions attract and retain customers, and through this, offers the opportunity for firms to innovate and enhance the investor journey, from segmentation and outreach through to content distribution and reporting. What is certain now is that investment management firms can no longer rely solely on price and outperformance to attract investors. Firms that adapt their products and integrate AI, data, and analytics into their service delivery models will be better placed to optimize and execute their product and content distribution strategies.

Enhanced digital engagement can also enable improved sales efficiency by using AI-enabled robo-advisors and chatbots to impact the sales and servicing cycle. Firms have recognized a new opportunity to gain direct distribution to investors, benefit from enhanced efficiencies in servicing small accounts, and offer value-added services for advisors. This has translated into a wave of investment activity, with asset managers and intermediaries acquiring or investing in robo-advice technology.



**IM in action—B2B platforms**  
 In 2018 UBS Asset Management announced that it is launching a white-label platform, UBS Partner, which will allow advisors to assess client portfolios against individual goals and risk appetites, as well as make buy or sell recommendations, based on proprietary algorithms.<sup>7</sup>



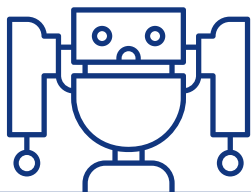
How intelligent machines can help	Example
<p><b>Seamless client experience</b>                      Leverage digital technologies to deliver a personalized, consistent and efficient client experience, customized by tier and segment</p>	<p><b>Robo advice: Hybrid solutions to enable</b>                      AI-based automated advice which supports customers when and where they make decisions</p>
<p><b>Marketing and sales optimization</b>                      Empower business development and relationship management sales teams with the insights and tools they need to more efficiently engage their clients to win and/or retain flows</p>	<p><b>AI-enabled intelligent dashboards</b> which adapt to every interaction that advisors have with their customers to make critical information accessible on-demand</p>
<p><b>Content effectiveness</b>                      Produce and distribute relevant, high-quality and timely content on demand to internal and external consumers</p>	<p><b>Predictive modeling</b> can provide unexpected insights, enable better insight-driven decision making, and provide a competitive advantage</p>

7. "UBS launches 'Aladdin for advisers'", Robert Van Egghen, 13 March 2018. Retrieved <http://igniteseurope.com/emailcontent/1909544/223684>.

**PILLAR #4: MANAGING RISK**

AI can bolster compliance and risk management functions as risk issues typically include ambiguous and/or improbable events.<sup>8</sup> Traditional methods of risk analysis can no longer handle the ever increasing volume of data. AI-enabled risk management can identify and manage both known and unknown risks in these vast pools of data. In terms of practical examples, AI can help investment management firms to:

- **Automate** consumption and analysis of data
- **Reduce** administrative activities
- **Focus** employees' time on exception-based handling and resolution of identified errors, inconsistencies in expected outcomes, and compliance violations



**IM in action—Liquidity risk management**

In 2017, BlackRock announced that it would incorporate internal trade data into its existing market liquidity model, and apply machine learning techniques to more accurately calculate the cost of redemptions and gauge liquidity risk.<sup>9</sup>

**How intelligent machines can help**



**Investment compliance management**

Identify investment guidelines from source documents (IMAs, exemptive orders, prospectus, regulations, house rules, investment policy statements) and create or update rule libraries



**Liquidity risk management**

Identify liquidity events, and based on defined triggers, automate response protocols



**Operational risk management**

Create exception-based dashboards to identify processing errors and gap SLAs (KPIs and KRIs)



**Conduct risk**

Use bad behavior models to identify employees exhibiting similar patterns to stop behavior before it grows in duration



**Regulatory reporting**

Extract information from regulations to identify new or updated requirements



**Reputational risk management**

Scan horizon to sense potential threats, seize opportunities, and shape perceptions within a 72 hour window



RPA



Natural language processing



Cognitive

**To the point:**

Where should investment management firms start?

- Clearly define your AI strategy
- Determine your go-forward path
- Continue to focus on short-term value and quick wins
- Embrace strategic collaborations and partnerships to solve for issues collectively and benefit from collective ideation, shared capabilities, and investment. Co-development will enable firms to sustainably develop unique and differentiated products and services
- Work with industry stakeholders

8. "Why artificial intelligence is a game changer for risk management", Deloitte, 2016.

9. "BlackRock to use machine learning to gauge liquidity risk", Faye Kilburn, 24 July 2017. Retrieved from <https://www.risk.net/asset-management/5307586/blackrock-to-use-machine-learning-to-gauge-liquidity>.





# AMUNDI-PIONEER

## The recipe for a successful integration process

### The main guidelines adopted by Amundi

**Christine Gentil**

Global Head of Business Support and Operations  
AMUNDI

The objective of a merger is to create value for clients and shareholders by bringing two entities together. While the work carried out during the due diligence phase enables the companies to assess the merits and expected benefits of the operation, the true test remains the integration phase.

I truly believe that the success of this phase largely depends on the migration of operational systems, since this phase adds value and allows businesses to be integrated onto a shared platform. Amundi has extensive experience in this field, having worked on the integration of Crédit Lyonnais Asset Management (2006), Société Générale Asset Management (2010), CPR

(2011), and BFT (2012) and also integrated Amundi Services' clients onto our A.L.T.O.<sup>1</sup> platform. The Pioneer team brought a wealth of experience of operational change and system migration processes. Drawing on these experiences, we have developed strong principles that were rigorously applied during the AMUNDI/PIONEER integration. ➤

1. Amundi Leading Technology and Operations

### Go fast

When it comes to merging international companies, it often takes several years for all entities to start working on the same platform. Over time, people become doubtful, fearful, and demotivated, so you have to move quickly. Here are a few simple principles to put this into practice: Be ready to start on day one.

Above all, it's vital to take advantage of the time that elapses between the date on which the merger agreement is signed and the date on which the merger takes effect (with the consent of the regulatory and competition authorities in the countries concerned). Amundi's senior management team used this period to define the target organizational structure, senior managers, and governance of the new entity on which all migration efforts were subsequently based.

The information system that would underpin all business lines also needed to be identified during this period. This was where simplicity and clarity were key. We chose one IT platform and developed new functionalities where needed. Choosing and combining tools from two different platforms is a nightmare: the selection process leads to endless discussions, territorial disputes, and unnecessary infrastructural complexity and support requirements.

I believe that a simple and clear choice was the key to ensuring swift progress and a successful outcome for the project. Once made, everybody was focused on achieving the same aim and there was no need for any more discussion. That's when the real work began for us: identifying the functional gaps that needed to be filled as quickly as possible. A number of these gaps shaped the structure of the migration roadmap; this was the case with certain US financial instrument categories for which we subsequently developed a full process chain.



Choosing the first entity to migrate is a key decision because it determines the pace of the migration. We tend to focus on an entity that is significant but not too large, that doesn't have too many gaps to cover, and that has a dynamic management team. Then—crucially—we set ourselves an ambitious deadline and stick to it! Other entities to be migrated are processed in order of complexity (the most complex is kept for the end in order to allow time for IT and the business line to analyze and implement solutions for gaps). We chose Pioneer Germany for the first migration batch and the process of onboarding it onto our A.L.T.O. platform was completed within four months. When you know that the timelines are tight, there's no time to waste! All in all, the migration projects took place over 18 months (across seven locations).

The organization of projects plays an important role because new entrants to the platform must trust the project leadership: this is the best way to onboard and integrate them, and to create mutually supportive relationships between the various teams.

Above all, it's vital to take advantage of the time that elapses between the date on which the merger agreement is signed and the date on which the merger takes effect.

### A strong partnership between Operations and IT

I strongly believe that this point is the secret to success!

Success relies on having an internal IT system over which we have complete control and a team of talented professionals focused on achieving the same goal.

As Operations (data management and the middle office) covers a large proportion of the value chain, it is generally the first business line to be affected. To prepare for this, we have to agree with the IT team what is possible in terms of implementation and what is not.

Migration projects are characterized by trade-offs and unforeseen events; they are a constant balancing act between what must be done in the required timeframe and reduced technical solutions or workaround processes. The partnership between the IT and Operations teams is key.

The most efficient way to stick to the roadmap is to manage the project with clear milestone and deadline targeting. Only a strong partnership between IT and Operations allows us to meet these challenges. Both teams must demonstrate pragmatism and authority throughout all projects to avoid deviations: they must accept and impose temporary workaround procedures and reduced functionalities in order to triage requests for IT development and avoid delays.

The teams must be in daily contact; decisions must be quick and synchronized—like the steps in a tango!

### Set up a war machine

Our teams, working in partnership, have a clear mandate from senior management. This mandate is vital to the successful management of the projects. A streamlined, smooth governance process (steering committee meetings at senior management level occur every two weeks) allows decisions to be taken very quickly and no subject to be left pending. As part

of the Pioneer merger, we appointed a clearly identified leader for each country, identified KPIs (progress expressed as a percentage), set up monitoring by the steering committee, and established a strict change management process. There is no “maybe” and no “I’ll explain my concerns in an email”: all issues are discussed each week and escalated to the steering committee if necessary. When there is a strong governance structure in place, everyone is on the same page and there is no frustration.

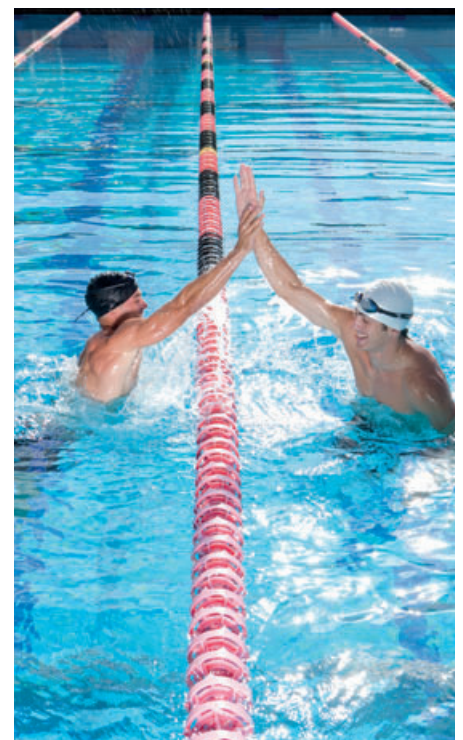
### Safeguard data quality and invest in migration tools

Large-scale migration requires impeccable data quality. This will require various parties agreeing on the data to be migrated and setting up comparison tables. This is no easy task because, despite quality controls, data quality is not always perfect. The architecture and ownership of the data to be migrated is generally not organized in the same way (centralized or locally managed). It can be difficult to collect additional data when the data is not centralized and is distributed over several business lines. This preparatory work on the data and the data-cleansing phase must start as soon as the merger agreement is signed in order to have a plan of attack ready for day one. Another strong advantage Amundi enjoys is our unique, global data management unit and tool, which disseminate data (portfolios, benchmarks, securities, prices, etc.) throughout the rest of the IT platform. In order to gradually onboard the middle office, risk, and investment teams onto the database platform, we have developed a “parallel run” mode that allows portfolio positions to be migrated to the new platform. This parallel run mode was set up thanks to IT investing in position-loading functions. Clearly, this has proven to be a wise investment. These migration tools and methodologies have been reused for each batch of the project. They must be designed and developed early so that they are available from the first migration batch onward.

### Integrate people

The human dimension is very important in this type of project and this represents a significant change for employees of the two groups to be merged. It is necessary to identify key people as quickly as possible (i.e., those with the skills to lead the integration project). Great care must be taken to retain and motivate these people who will play a key role during and after migration. They are an asset to the company and as such they must be protected.

It is then necessary to quickly put the teams to work on migration projects, even if it means using backfill reinforcement to manage the day-to-day business. Training sessions, site visits, and any other contact between the teams will only strengthen the links between the two groups—cooperation and trust will be real assets during the project. There is only one team! Company mergers generate culture shocks. It is a phenomenon that must be taken into account: we may do the same job, but we do not always speak the same language. We must overcome misunderstandings, listen to each other, and treat each other with kindness during this period. ➤



**Promote a cross-business-line approach**

The problems encountered during migration projects are very often complex and rooted in the fact that processing chains often operate across multiple business lines and are difficult to tackle. I believe that only a holistic structure can overcome these issues.

Throughout the migration process, it is vital to draw upon a network of experts involved in the project and encourage them to discuss issues among themselves and with IT to find solutions. Experts will have to be appointed in each stream so that everyone can see the existing system from every angle. It will also be their responsibility to identify solutions that minimize the impact on clients.

The biggest challenge in this kind of project is staying unified: everyone must quickly become one team working towards a shared goal! It is important to keep in mind that a successful project should make you forget that you belong to the old entities; it will create a strong sense of pride among the teams and especially the absorbed entities that will have been on the front line of the project. I am convinced that it is essential to establish strong bonds of trust between the two companies' workforces, as these prove crucial both during and after the project.

The migration project is not the only factor for success: the continuity of commercial dynamism and the realization of expected synergies complete the picture of a successful merger.

The success of our merger will be judged in terms of people and processes. I am convinced that the ability to execute such an operation depends, above all, on the quality of management, and the enthusiasm and expertise of the teams involved. ●





Amundi/Pioneer migration project—key figures:



Duration of the integration process:

**18 months**



**1,200 portfolios**

(€200 billion in AUM)



**7** <sup>main investment</sup> locations <sup>to migrate</sup>



**2,000 new employees** <sup>to be onboarded</sup>

**To the point:**

- Go Fast
- Define the target organization very early and set up a project governance capable of making quick decisions
- Choose the best existing IT platform that will be upgraded: set up a migration and change management plan which will be applied to each entity
- Set an ambitious timetable and stick to it
- Put merged entities at the forefront to facilitate training and integration

# India Budget 2019 brings some gain, some pain for foreign investors

**Rajesh Gandhi**

Partner  
Tax  
Deloitte

**Karamjeet Singh**

Director  
Tax  
Deloitte

The Indian Finance Minister presented her maiden budget for the current financial year 2019-20 earlier this year. Following the overwhelming victory of the central government in the elections, there was widespread expectations that the government would announce bold reforms and could take radical measures to accelerate the country's economic growth.

In an earlier statement, the Prime Minister of India laid down an objective of scaling the size of Indian economy to US\$5 trillion by 2024-25 and achieving this objective will require India to sustain real GDP growth of 8 percent per year from 2019-20 onwards.

In the fiscal year 2018-19, India's growth rate moderated to 6.8 percent from 7.2 percent. Nonetheless, India continues to be the fastest growing major economy in the world. The country has maintained its macroeconomic stability by containing inflation within 4 percent and by maintaining a manageable current account deficit to GDP ratio.

Against this backdrop, Budget 2019-20 sets out a road map for the government's investment policy, with a focus on further improving the social infrastructure of the country. Some such measures include further liberalization of foreign investment norms, heavy investment in infrastructure projects, strategic disinvestment of PSUs<sup>1</sup>, extension of reduced corporate tax rate to more companies, impetuous to NBFCs<sup>2</sup> as well as regulatory and tax incentives for start-ups.

The budget proposed a few regulatory reforms for Foreign Portfolio Investors (FPIs). ➔

1. Public sector undertakings

2. Non-banking finance companies







### Increase in statutory FPI limit

Under the current FPI regulations, equity investment by all FPIs taken together in an Indian company is restricted to 24 percent share capital of the company. However, the company is permitted to increase this cap (by passing a special resolution) from 24 percent to the extent of sectoral cap i.e. the outer limit up to which foreign investment (in all forms including FPI, FDI<sup>3</sup>, FVCI<sup>4</sup> etc.) is allowed in a company. Given the availability of this discretion, various Indian companies have set different caps for FPI investments, which makes tracking and monitoring of such caps cumbersome and confusing. In this year's budget, the government has proposed to remove the 24 percent limit restriction for FPIs and set the default FPI limit up to the sectoral cap. If an Indian company wishes to restrict FPI investment lower than the sectoral cap, it can choose to do so by passing a special resolution. This proposal would bring clarity to FPIs, enable ease of limit monitoring and would open up FPI investment limits in many Indian companies.

### Merger of FPI and NRI routes

Under the current regulatory framework, non-resident Indian citizens (NRIs) have a special route (NRI-PIS route) to make portfolio investments in India wherein they need to open special bank accounts with Indian banks. Since NRIs have a separate route, there are currently restrictions placed for them to invest through the FPI route. This year's budget has proposed to merge the NRI route with the FPI route whereby there will be a single window available to foreign investors (whether Indian citizens or otherwise) to make portfolio investments into India.

### Rationalization of KYC norms

The budget also proposed to rationalize the existing know your customer (KYC) norms applicable to FPIs. The government will provide more clarity on this in the coming weeks and it is expected that the relaxations will make the KYC requirement materially easier for FPIs.

### Key tax changes

On the tax front, the budget did not bring much cheer for taxpayers, especially foreign investors. There was an expectation that the government would provide tax relief on equity investment by either reducing the long-term capital gains tax (introduced last year) or by removing the securities transaction tax levied on stock market transactions. However, no such measures were announced in the budget. Instead, the government increased tax rates for non-corporate tax payers and introduced a buyback tax for listed companies.

### Increase in tax rates for non-corporate taxpayers

The government has increased the surcharge (applied on the base tax rate) for taxpayers other than companies and partnership firms. The surcharge has been increased from the current highest rate of 15 percent to 37 percent where the taxpayer's annual income exceeds INR50 million. The increase in surcharge would also impact FPIs which are not set-up as corporations or partnership firms. The effective tax rates for FPIs (whose annual income exceed INR50 million) post the budget changes would be as follows:

There was an expectation that the government would provide tax relief on equity investment.

3. Foreign direct investment

4. Foreign venture capital investment

Type of Income		Corporates (no change)	Partnership firms (no change)	Others (e.g. trusts)	
				Existing	Proposed
Capital gains on transfer of listed equity shares/units of equity mutual fund/units of business trust (STT is paid)	Long-term	10.92%	11.648	11.96%	14.248%
	Short-term	16.38%	17.472%	17.94%	21.372%
Capital gains on transfer of debt securities (including debt MFs)	Long-term	10.92%	11.648%	11.96%	14.248%
	Short-term	32.76%	34.944%	35.88%	42.744%
Capital gains on listed derivatives	Short-term	32.76%	34.944%	35.88%	42.744%
Interest on qualifying bonds		5.46%	5.824%	5.98%	7.124%
Dividend		Exempt	Exempt	Exempt	Exempt

Source: Indian Finance Act, 2019



The amendment places a non-corporate fund (for e.g. a unit trust set up in UK) at a tax disadvantage vis-à-vis a corporate fund (e.g. a SICAV in Luxembourg). Interestingly, in certain countries such as the US and UK, regulated investment funds, though legally set-up as trusts, are considered to be companies for home country tax purposes. Such funds would also be adversely impacted by the change.

#### Buyback tax

Under the tax law, an Indian company distributing dividends to its shareholders is required to pay 20 percent dividend distribution tax. To avoid such distribution tax, a company could distribute income to the shareholders through a share buyback instead of dividend payout. Upon receipt of buyback proceeds, the shareholder would be required to pay capital gains tax, which would typically be significantly less than the 20 percent distribution tax the company would have had to pay if the income was distributed as dividend. To address this anomaly, the government introduced a 20 percent buyback tax on “unlisted” companies in the year 2013.

In the current year’s budget, the government has extended the 20 percent buyback tax to listed companies as well. Once the company discharges distribution tax, the buyback proceeds received by the shareholder would be exempt from capital gains tax.

#### Angel tax relief

In recent times, there has been a significant tax litigation in India on start-ups, wherein tax authorities have sought to tax the share subscription money received by Indian companies in excess of fair valuation in

the judgement of tax officers. Since such start-up companies are often funded by angel investors, the issue is widely known in India as the “angel tax” issue. The government has proposed to resolve this issue by notifying a specific class of Indian companies (likely to be start-up companies) who would not be taxed for receipt of share subscription money at a valuation exceeding the company’s current fair market value. A similar proposal has been introduced to not apply fair valuation method in taxing capital gains arising from transfer of shares of unlisted companies in certain situations.

#### Tax incentives to promote International Financial Services Center

India has set up its first International Financial Services Centre (IFSC) in the newly established Gujarat International Finance Tec-City (GIFT), in Gujarat. The Indian IFSC offers business opportunities in banking, capital markets, insurance, asset management, and ancillary services and it seeks to compete with major financial hubs such as Singapore, Hong Kong, and Dubai. There are two international exchanges already operational in the GIFT IFSC where non-resident investors can trade in various derivative products on Indian as well as international securities. The government has provided significant tax sops to promote Indian IFSCs such as no capital gains tax, tax holiday on business income, exemption from GST<sup>5</sup> etc.

In the current year’s budget, the government has provided additional tax incentives to units set up in IFSC. The key incentives introduced in this budget include increasing the tax holiday period for taxation of business income, tax exemption

for interest received on monies lent to units set up in IFSC, exemption from capital gains on income arising to certain AIFs (Alternative Investment Funds) set up in IFSC and exemption from distribution tax for income distributed by such AIFs.

#### Tax audits

Tax audits (scrutiny assessments) currently involve significant interaction between the taxpayer or the taxpayer’s representative and tax officers. It is proposed to establish an e-assessment framework allowing the scrutiny to be completed on the basis of documents and other information provided by the taxpayer via the online income tax portal without the need for face-to-face interaction with the tax authorities.

#### Comments

The 2019-20 budget contains no significant changes to Indian tax legislation, in part because the government was only recently re-elected. In addition, a committee established to redraft the Income-tax Act 1961, is expected to submit its report shortly.

Various stakeholder demands such as reducing the ordinary corporate tax rate to 25 percent for all companies irrespective of turnover, extending the sunset clause relating to tax benefits available to units in a special economic zone to new units established after 31 March 2020, and the reduction or abolition of the alternative minimum tax were not considered.

More progressive changes to the tax laws are expected to be announced during the year and in the FY 2020-21 budget that will take place in the first week of February 2020.



In the current year's budget, the government has provided additional tax incentives to units set up in IFSC.

#### To the point:

- India continues to be the world's fastest growing major economy with the current GDP rate close to 7 percent. The country is also continuing on its path to fiscal discipline and has maintained its macroeconomic stability by containing inflation within 4 percent
- Policy reforms remain high on government's agenda and there are definite steps being taken for further improving ease of doing business such as rationalization of FPI KYC norms, liberalization of foreign investment limits, merger of FPI-NRI routes etc
- Government intends to increase tax on super-rich to fund the large amount of capital needed to support development projects. The higher tax rate also affects offshore and domestic funds set up as trusts and Association of Persons. The maximum effective tax rate for long-term/short-term capital gains will increase from 11.96 percent/17.94 percent, to 14.25 percent/21.37 percent respectively
- Buyback of shares by listed companies will now trigger a distribution tax of 20 percent and the income will correspondingly be exempt for the shareholders
- Government is drafting a new Direct Tax Code that will replace the existing tax law



# Distribution 2.0

How technology will redefine relationships with asset management clients





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The rapid innovation and progress of technology, particularly in the last decade, has transformed the distribution of goods and services fundamentally. In many industries, data, analytics, and digital applications have removed intermediaries, compressed value chains, and reduced costs.

Unlike previous industrial revolutions, however, this wave of technological change has also permitted more personalized interaction with individual consumers, as well as emphasized the experience, not just the outcome, of a purchase—transforming transactions into relationships.

Asset management has been slower than other financial services industries to embrace new technologies. Winning asset managers of tomorrow, however, will embrace distribution technology—partly to deliver efficiency, but mostly to deliver a better client experience at scale, helping them acquire and retain more clients. Four conclusions can be distinguished as:

- Buyers in asset management have changed dramatically
- Most asset management firms have failed to keep up, making only incremental changes to address new buyer needs
- Asset management firms that place technology at the center of distribution strategy can enjoy dramatic improvements in distribution efficiency
- But deploying the necessary technology only works in conjunction with enterprise-wide initiatives designed to transform the entire distribution organization.

Asset managers cannot provide customization and service-oriented capabilities using only salespeople; delivering them effectively requires leveraging technology.

### New buyer needs

Both retail and institutional buyers of asset management products and services worldwide have evolved dramatically since the 2008-2009 global financial crisis. Clients of asset management firms are now:

- **More complex.** Retail and institutional buyers have become more focused on outcomes than benchmarks, rewarding managers more for the cash flows they can create rather than less certain asset appreciation.
- **More powerful.** The number of decision-makers reviewing and selecting asset managers for portfolios is consolidating in both the institutional world and among individual investors.
- **More demanding.** As the overall standard for digital delivery of products and services rises across all industries—exemplified by real-time information, rapid delivery, seamless interactions, and customized fulfillment—asset management has fallen behind.
- **More time-constrained.** Asset owners and large intermediaries need to handle more internal functions with fewer staff, and they have less bandwidth available for selecting asset managers and onboarding and monitoring investment firms they have already chosen.
- Finally, **more diverse.** While the industry continues to view clients as relatively faceless retail and institutional “channels,” most buyers require a personalized approach. Increasingly, similarities among buyers stem more from their specific needs and objectives as investors—implying that the industry relies on a client segmentation framework that may not reflect true client preferences.

All of these changes in buyer needs have reshaped the engagement model that clients seek from their asset managers. The industry’s traditional engagement model has been transactional and linear in nature while interviews with clients reveal that buyers want something different from asset managers. They view their interactions with asset managers as more of a journey: a continuous, accretive, and often two-way relationship. Clients describe their optimal engagement with asset managers in many ways, but their feedback tends to focus on four areas, which can be categorized as “four E’s”:

- **Entice**, where asset managers foster interest among clients by engaging them with tailored content, messaging, advertisements, events and similar outreach. Prospective clients receive, through multiple media, personalized content that reflects their top-of-mind portfolio objectives and concerns.
- **Enter**, a phase where buyers expect detailed discussions about their specific needs, and high levels of engagement from the asset manager’s specialists to collaborate on potential, more customized, solutions to meet longer-term portfolio objectives.
- **Engage**, a phase that begins with onboarding, where clients seek a streamlined and increasingly automated process. Buyers expect ongoing service to remain personalized, usually through two key functions: customized reporting that answers client-specific questions; and enterprise value-added tools.
- Finally, **extend**, where technically proficient distribution professionals bring content and specialists to review the client’s needs and suggest specific investment capabilities or services that could further help clients meet their declared objectives. Absent from the depiction is the fifth “E”, exit, which focuses on gathering information about client departures.

### Deteriorating distribution economics

Most leaders of distribution organizations are aware of the growing expectations gap, but so far many have addressed it by hiring more salespeople. The industry's estimated sales and marketing-related headcount, as measured by full-time equivalents, ballooned 50 percent between 2012 and 2017. Yet on average, dedicated sales professionals generated slightly more than half as much revenue—and less than half as much profit—per employee between 2012 and 2017.

Figure 1: Systemic Sources of Distribution Inefficiency, 2018



**No single view of client** across enterprise, poor data quality

Only **13%** of asset managers reach their "target state" CRM



**Limited ability** to turn data into insights

Only **17%** of asset managers successfully enhance distribution through use of data and analytics



**Poor user experience** and low adoption

Only **7%** of asset managers report adding value to their clients through distribution transformation



**Disconnected tools** across sales, service and marketing, resulting in disjointed efforts

Only **18%** of asset managers report having technology functions adequately servicing distribution



**Challenged execution:** missed timelines and budgets; misaligned management teams

About **76%** of distribution leaders label "sales productivity" a "top of mind issue"



Asset managers cannot provide customization and service-oriented capabilities using only salespeople; delivering them effectively requires leveraging technology. Many asset managers argue they have “digitized” distribution. But their improvements in most cases have been incremental, and failed to address several symptoms of distribution inefficiency:

- **No single view of a client** exists, in many cases, because of fragmented client data—collected at varying levels of detail, under differing hygiene conditions, and housed in several places across an enterprise.
- **Inability to turn data into insights**, as they lack definition around desired analytics, the necessary data scientists, and quality or complete data sets.
- **Disconnected tools** across sales, service and marketing, as different, silo-ed groups within organizations add applications without considering how to coordinate such tools together across the length of the client journey.
- **Poor customer experience**, with: inefficient onboarding with disjointed hand-offs among multiple participants, a lack of customized approach, outdated client reporting, or a lack of service quality. **Execution challenges** compound these problems.

These suboptimal outcomes likely all stem from a single root cause. Most asset managers have viewed technology only as an extension of their existing distribution strategy. Consequently, distribution technology has received limited management attention, talent and budget. To be successful, asset managers need to place distribution technology at the very heart of their strategy. This will lead most asset managers to rethink their distribution function altogether—with enough change to label the new structure Distribution 2.0.

#### **Distribution 2.0 technology**

Asset managers still need functions around client and product, an organizational model that brings together people and processes, and an engagement model that serves as a base framework for communicating with prospects and clients. But as buyers demand more personalized service and more consistent communication with asset managers—a sum of interactions that often gets described as client experience—legacy functions are insufficient. Distribution technology links existing sales and service capabilities with client needs, using automation and processing capabilities that allow firms to deliver client experience at scale across retail and institutional clients. (Figure 2)

Asset managers that have invested heavily in distribution-related technology already are seeing clear benefits. During the three years ending 2017, those asset managers who ranked in the top third of peers for spending on distribution technology grew twice as fast as the industry overall in terms of net new flow, and eclipsed rivals in the bottom third, most of whom shrank. An asset manager’s size and distribution technology budget are only loosely correlated, with some smaller firms ranking among the more aggressive spenders.

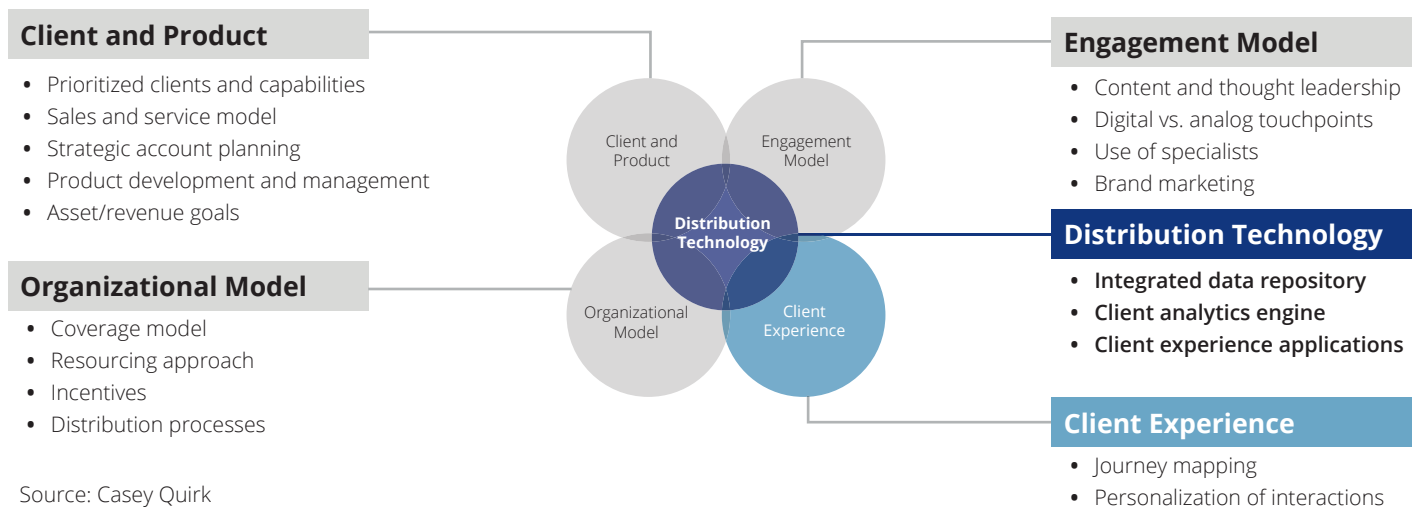
Additionally, asset managers that report leveraging data and analytics as a primary input to their distribution efforts benefit from significantly longer institutional client tenure than those that do not.

Most distribution leaders realize they need to invest further in technology to support a wider number of more customized and complicated relationships with buyers and intermediaries. Nearly two-thirds of distribution leaders labeled technology or new talent—usually referring to professionals more comfortable with using technology in distribution—as a number-one management priority for the next three to five years.

Distribution technology can mean many things, but effectively deployed, it usually consists of three critical layers (Figure 3).

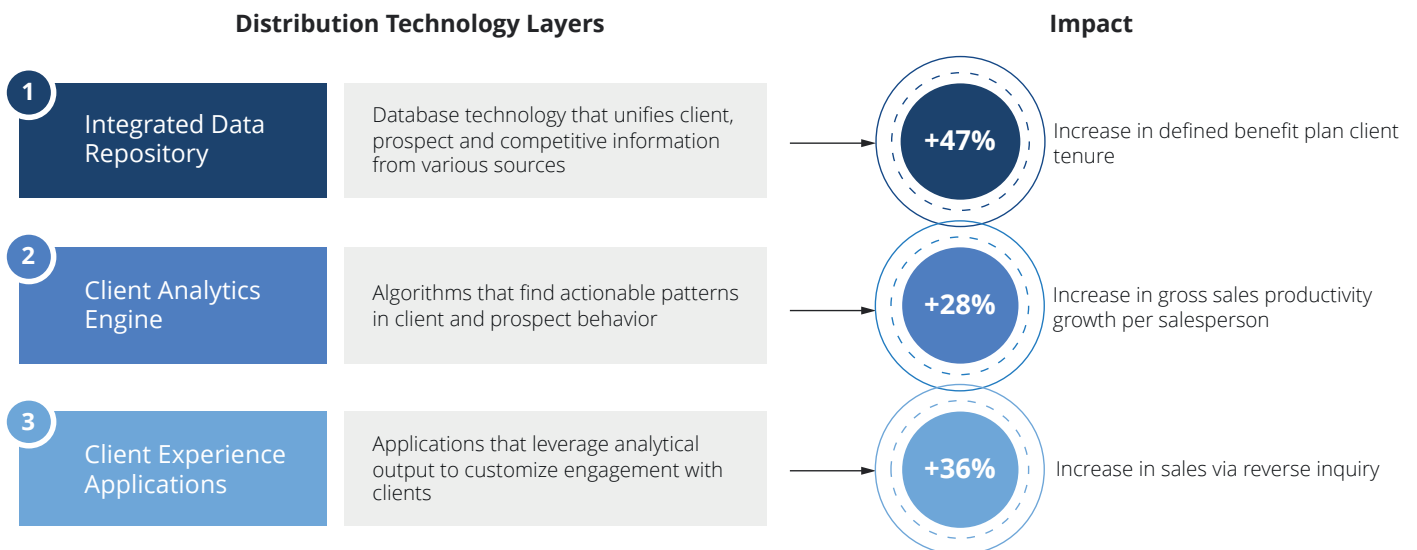


**Figure 2: Distribution 2.0 Strategy Requirements**



Source: Casey Quirk

**Figure 3: The Three Layers of Distribution 2.0 Technology**



Sources: Casey Quirk Distribution Benchmarking, Casey Quirk/McLagan Performance Intelligence, Casey Quirk analysis

Few firms have built any of the three layers completely, let alone finished all three seamlessly, and while specific applications and technologies vary from firm to firm, each layer of distribution technology has characteristics common to most asset managers building them.

### 1. Integrated data repository

An integrated data repository is the data architecture that centralizes data about clients, competitors, and the operating environment to create a single source of information for the entire enterprise. Most asset managers suffer from fragmented data about buyers, resulting in inefficient prospecting and poor-quality interactions with current clients. This fragmented view means asset managers rarely see how unorganized they look to a buyer; conversely, the disorganization is all the client sees.

Asset managers usually need to work with multiple sets of distribution data, all of which they struggle to organize and reconcile:

- **Data from the client**, including account information, transaction history, performance and risk tolerance
- **Sales and marketing history data**, including calling activity, past RFPs, marketing and conference data, and feedback from past and present clients
- **Third-party data**, such as data packs from intermediaries and data feeds from custodians
- **Industry business intelligence databases** containing data from not only asset owners and intermediaries but also other asset managers, usually focused on descriptive client information, performance, assets and flows

The integrated data repository often is a series of highly interlinked database management systems, not spreadsheets. Well-built repositories share some characteristics:

- They are **extensive**, including flow, asset, performance, touchpoint, and demographic data, connected by consistent and robust reference data and metadata
- They are **flexible**, built on scalable server infrastructure with flexible connectivity to multiple applications and user groups
- They are **well-governed**, with clear data stewardship and data strategy ownership.

### 2. Client analytics engine

While an integrated data repository provides a single source of truth, a client analytics engine links the applications and technology that allow distribution organizations to harness the centralized data effectively. The client analytics engine requires data scientists to develop algorithms and data mining applications that comb data for patterns and markers that match marketing, sales and relationship management objectives. Output from analytics engines support a variety of analyses, roughly grouped into at least four categories:

- **Descriptive**: profiling clients and activity within client segments based on business intelligence, internal reporting, and statistics
- **Predictive**: identifying client attributes that represent high-probability prospecting targets, and then isolating the best next potential buyers to pursue – and capabilities to offer
- **Cognitive**: leveraging machine learning to transform extensive, unstructured data into meaningful, human-like insights upon which a distribution professional can act
- **Prescriptive**: suggesting a course of action to increase the likelihood of a given outcome.

### 3. Client experience applications

The final layer of distribution technology consists of applications that leverage analytics to support more customized interactions with buyers, using real-time information to better coordinate marketing, sales, and service personnel. These applications vary the most from firm to firm: while they may share similar third-party base applications, their deployment, data visualization and use cases should reflect an asset manager's specific comparative advantages.

Asset managers benefit in two ways from client experience applications:

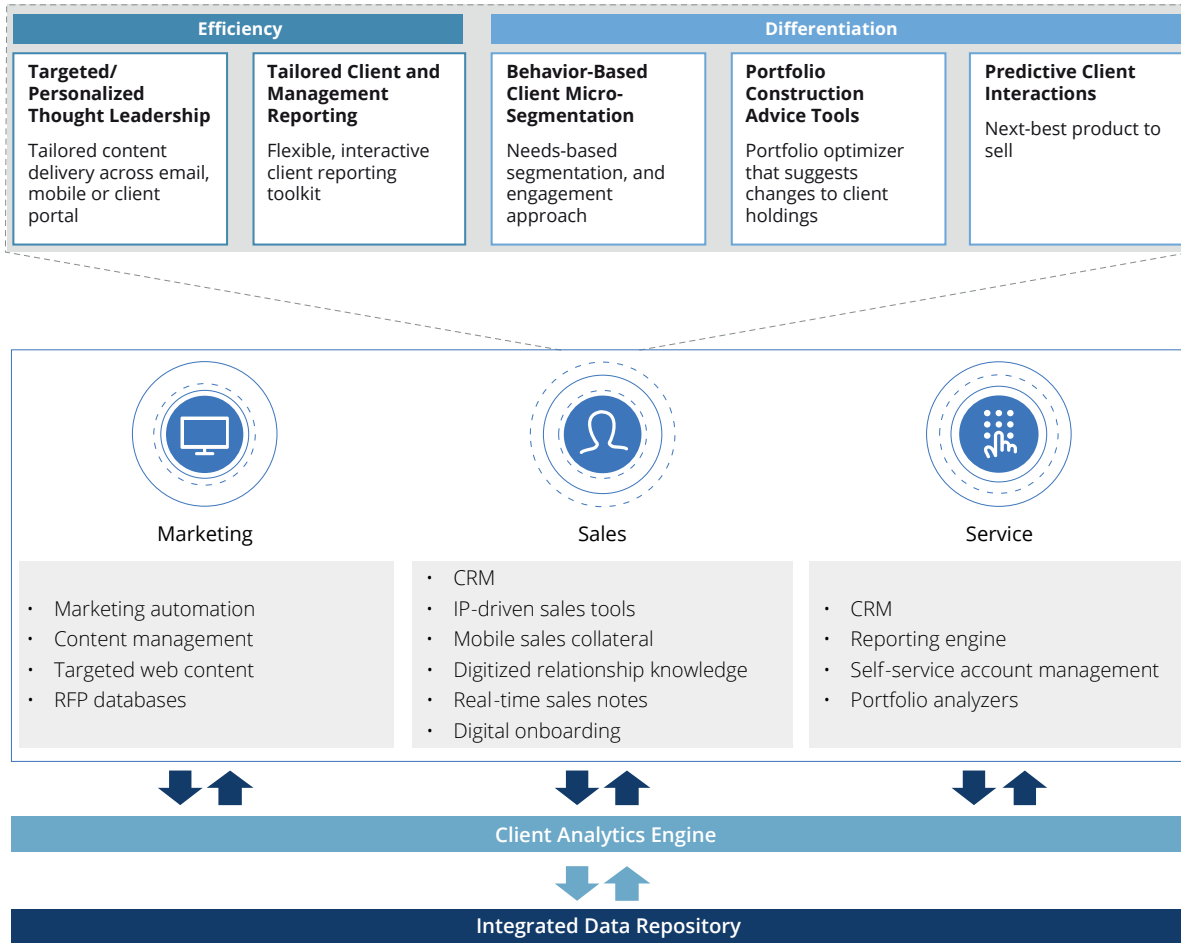
- Efficiency
- Competitive differentiation

Client experience applications span multiple distribution functions:

- Marketing
- Sales
- Service

Importantly, a customer relationship management (CRM) platform can provide the necessary relationship management tools to track, manage, and support interactions across marketing, sales and service. This requires firms to view CRM as more than a contact tracking system. Instead, well-designed CRM systems can pull together analytics and applications, proactively creating a common view of prospects and clients, as well as supporting an integrated set of client interactions across the enterprise.

Figure 4: Distribution 2.0 Technology Layer 3: Client Experience Applications



Source: Casey Quirk

Asset managers usually need to work with multiple sets of distribution data, all of which they struggle to organize and reconcile

### Deploying Distribution 2.0

Distribution technology, therefore, is best viewed not as a singular proprietary system, but rather as a combination of component technologies, third-party and in-house, brought together within a clear blueprint and ideally connected into the three technology layers described earlier.

Newer distribution technology likely will erode the asset management industry's current lines between intermediary clients and institutional buyers. Distribution 2.0 technology blends the high-touch content effective in institutional relationship management with the mass customization delivery mechanisms of the intermediary world, permitting asset managers to deliver more customized and service-oriented client experience at scale to buyers regardless of their size.

There is no technology to organize distribution technology: that requires support from human capital across the enterprise. In fact, the technology will not work without capable distribution talent, which the various applications and systems leverage, not replace. Implementing a technology-centric distribution model effectively depends on three enterprise-wide initiatives, involving officers across multiple functions:

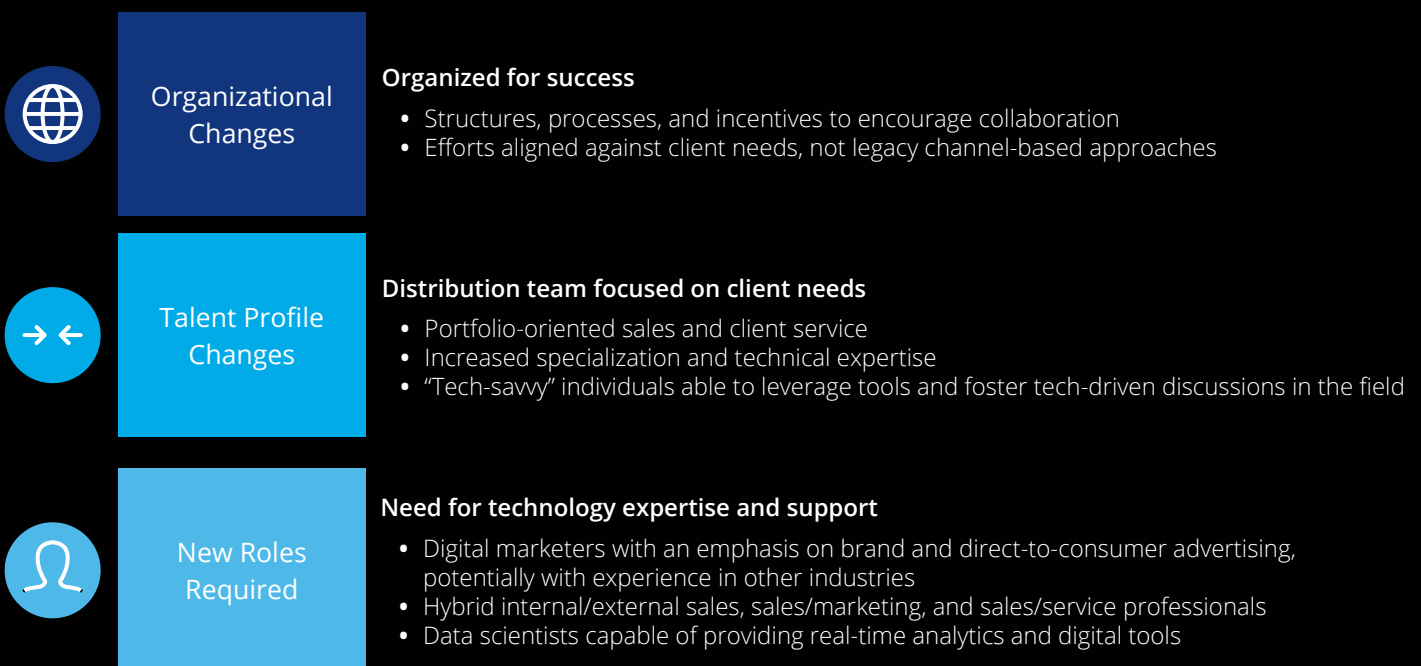
- A **new talent model** for the distribution organization
- An **action-oriented approach** to execution that focuses on rapid prototyping and more iterative processes that test, learn and refine
- A **change management** program with a dedicated leader, designed around sequential implementation and quick wins.

### 1. New talent model

Legacy distribution organizations within asset managers share many characteristics that no longer resonate with buyer demands: they lack the data to segment clients at anything more detailed than the blunt level of channels, they silo sales and service functions in many cases, and they "outsource" technology discussions to the CTO or contractors, deeming them less strategic for success.

Supporting technology-led distribution, however, involves organizing around buyers, not channels, in a way that better supports specific client journeys. Consequently, asset managers can reorient their talent acquisition and retention strategies as follows:

Figure 5: New Talent Model for Distribution 2.0



Source: Casey Quirk



**2. Action-oriented execution**

Asset management’s manufacturing-oriented model is ill-suited for rapid change, as it views innovation as only a product-level function; changes to the delivery model are viewed as wholesale shifts that are expensive, unwieldy and high-risk. Consequently, most distribution leaders have been reluctant to install the three layers of technology required in a new client environment, perhaps fearing that such projects are too big to succeed—at least on their watch.

Some distribution organizations that have started to transform themselves have done so by taking cues from the playbooks of other industries. They embrace the complexity of distribution transformation, but also appreciate the necessity of such changes. Consequently, to break down what is an often overwhelming transition, iterative execution processes—which embrace rapid prototyping and market testing in real time with pilot clients, rather than attempting to solve all issues perfectly at once—will be a necessary method that asset managers use to get their organizations and clients comfortable with new technology in a sequential, more affordable, way.

Creating Minimal Viable Products (MVPs)—smaller changes, in terms of applications or processes—allows asset managers to gather “quick wins” that have several advantages: they can test and refine them in real time, they can fit into smaller budgets, and they can convince more skeptical distribution professionals that technology can be a highly useful tool in a day-to-day situation.

**3. Change management program**

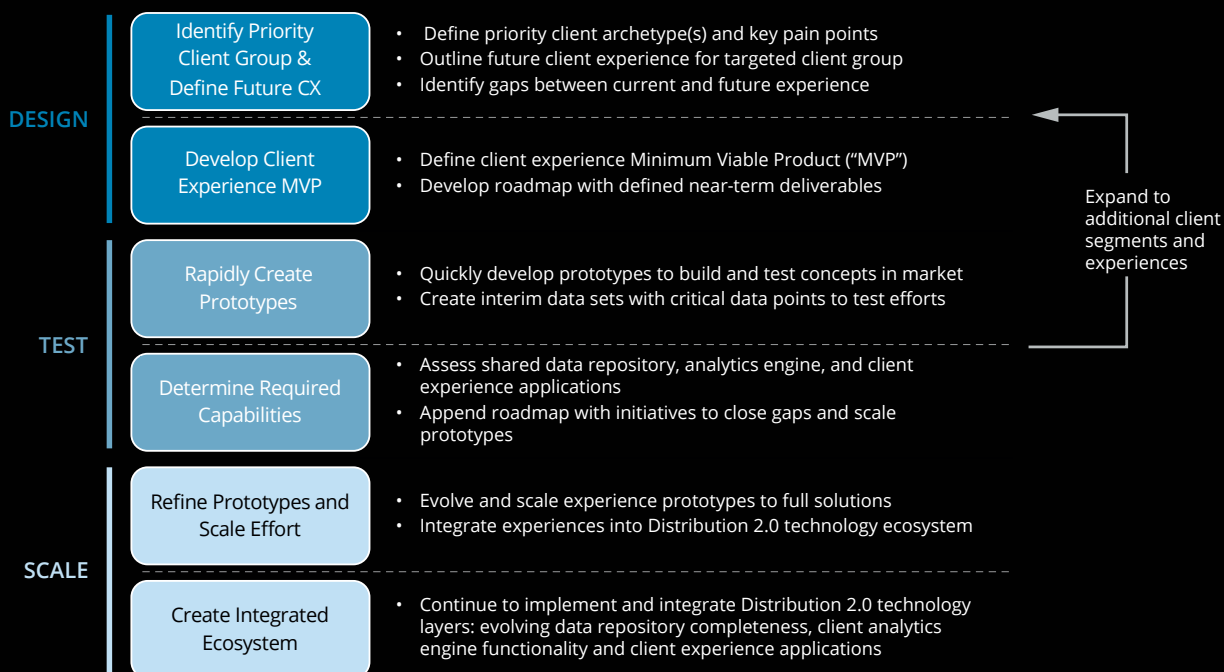
The iterative process may encourage innovation, but it cannot function in a purely decentralized way. Most asset managers have failed to implement broad changes regarding distribution technology, perhaps because executives view such restructuring as a side project of an existing manager, rather than the responsibility of a dedicated leader. Asset managers seeking to transform their distribution organizations must assign the task to an enterprise-level executive, familiar with not only distribution and technology, but also with the products and services that may adjust as a result. Additionally, experienced project managers, potentially residing within a transformation office, will be necessary.

The distribution transformation leader should have several key priorities:

- Setting the vision for distribution strategy across all elements, including technology and human capital
- Driving the integrated approach, including development of MVPs, as well as other initiatives
- Acting as champion for distribution transformation across internal constituencies
- Defining and measuring key success metrics, and tracking progress • Ensuring implementation consistency across functional areas and geographies.

Some of this leader’s first decisions will focus on deciding where to start. Implementing a Distribution 2.0 transformation all at once likely involves more budget and bandwidth than many asset management firms can afford. Transformation programs designed around “quick wins” tend to have the best chance of success. To date, asset managers successfully implementing new distribution technologies do so by focusing initial efforts on a core client set: usually one with specialized needs and representing a sizable portion of economics to the enterprise.

**Figure 6: Distribution 2.0 Strategy and Implementation Approach**



Source: Casey Quirk

This client-specific approach has several advantages. Narrowing the scope reduces execution risk and shortens implementation time. Building around MVPs permits real-world testing across a smaller, more loyal client base, safety-testing new ideas. Most importantly, successful smaller changes build confidence across the enterprise that new ideas in Distribution 2.0 can improve client acquisition and retention, raising appetite for broader transformation across the enterprise.

**To the point:**

- Buyers in asset management have changed dramatically
- Most asset management firms have failed to keep up, making only incremental changes to address new buyer needs
- Asset management firms that place technology at the center of distribution strategy can enjoy dramatic improvements in distribution efficiency
- But deploying the necessary technology only works in conjunction with enterprise-wide initiatives designed to transform the entire distribution organization





- /Promotion
- /Research
- /Business
- /Development
- /Engineering
- /Manufacturing
- /Planning



# A financial frontier: Opportunity from the East

Deloitte Luxembourg's 2019 Cross-Border Fund Distribution Conference shed light on exciting opportunities in the relatively untouched investment hub of Asia. ▶

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### Setting the scene

Asian growth is inescapable; the key question is whether international asset managers are brave enough to embrace the resulting opportunities. Much of the evidence suggests that Asia will offer some of the best future opportunities for the asset management industry with its incomparable GDP growth, extensive financial infrastructure development, significant regulatory advancement, regional integration and major social change. Despite this, the Asian asset management industry remains relatively untapped, with major pools of capital eagerly awaiting the right investment opportunities. We will endeavor to shed

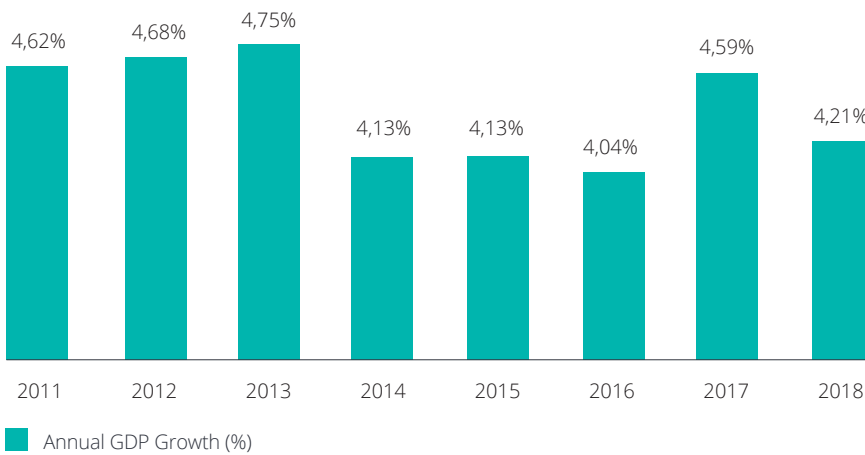
some light on the region, explain how to undertake cross-border distribution and share our expertise to help you harness this relatively untouched prospective investment hub.

The APAC region has developed at an astronomical rate over the last 20 years with GDP growing at around twice the speed of the European Union and the United States. Consequently, a flourishing middle class has evolved, looking for alternative investment options for its ever-increasing capital. This trend is noticeable not only in more developed countries such as Japan and Australia, but also in developing countries such as Thailand. In parallel, Asian investors are seeking returns

beyond their borders in international markets. The ageing Asian population is increasing the pressure on its local pension regimes to meet the needs of their beneficiaries. Hence, major institutional investors are turning to international markets to achieve the high yields they desire, while diversifying their investments in a bid to hedge their risks.

This trend is particularly evident in regional financial hubs including Singapore, where the professional investor market dwarfs the emerging retail opportunities. Such factors have created a perfect storm for the future of the Asian asset management industry.

### East Asia & Pacific annual GDP growth, 2011-2018



Source: Worldbank database

Asian growth is inescapable; the key question is whether international asset managers are brave enough to embrace the resulting opportunities.



Following a panel discussion at Deloitte Luxembourg's Cross-Border Fund Distribution Conference, it became evident that the success of the Asian asset management industry effectively lies with its financial regulators. Historically they have (often unfairly), been considered less mature in comparison to some of their European counterparts. However, this perception is changing as over the past decade Asian financial regulators have been at the forefront of developing robust comprehensive regulatory regimes for both local and foreign fund distribution. Most importantly, there has been a clear policy shift towards opening up foreign fund distribution channels while reducing regulatory complexity. For example, regulators in Singapore, Taiwan, Thailand, South Korea, New Zealand, Hong Kong and Japan, have all updated their foreign fund distribution regulation in the last year alone. A further example of Asian regulatory maturity is the introduction of local fund passporting regimes, which act as catalysts for further regional integration in an attempt to create a UCITS-equivalent brand in Asia. Fundamentally, unlike the EU, the Asian fund distribution market is far from harmonized. Consequently, we often liken the region to a "galaxy of stars" rather than an integrated region. Therefore, while

opportunities for foreign fund distribution are almost immeasurable, accessing this region will require an in-depth understanding of its specificities coupled with the development of a clear, strategic roadmap.

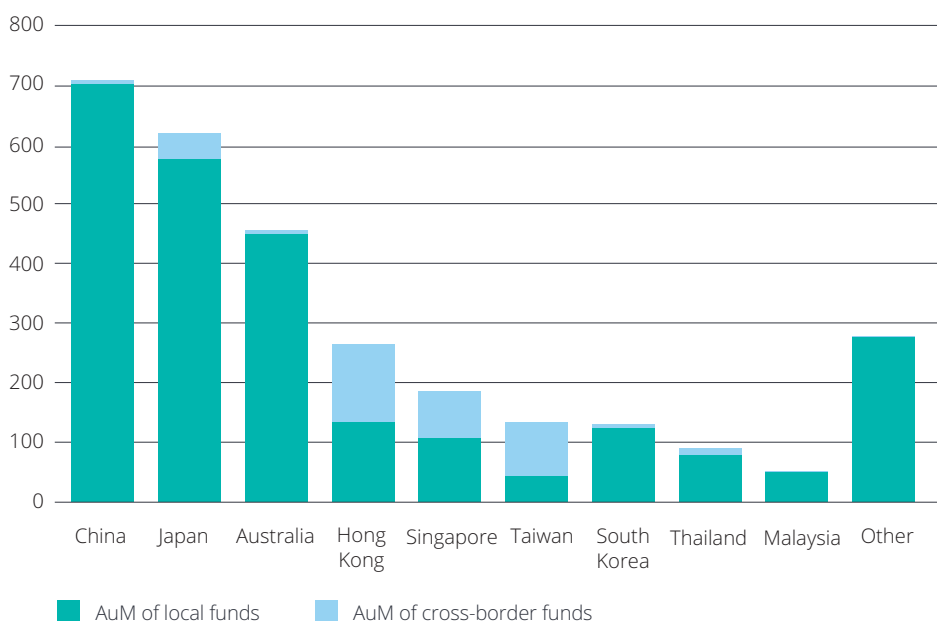
**Cross-border distribution**

Cross-border fund distribution options in Asia are extensive, with many European domiciled asset managers already creating their Asian footprint. However, these options are often unique to each country and the type of investors targeted. Such diversity reflects the historical, economic, cultural and political differences that the region is renowned for. Notably, there exist stark differences between Asian countries when comparing assets held by foreign funds versus locally domiciled funds. As one would expect, distribution to retail investors is most prevalent in the internationally renowned financially open jurisdictions of Hong Kong and Singapore due, in part, to the maturity of these country's regulators. However, one would be mistaken for thinking that foreign fund retail distribution was limited to these countries. For example, strong foreign fund retail distribution markets also exist in Taiwan, Macau, and South Korea.

Despite this market trend similarity, there are noteworthy differences between countries, especially their retail distribution regulatory regimes. Conversely, a few dissimilarities between these regulatory regimes include the necessary language of legal documentation, fund maintenance and annual reporting requirements, local tax rules, country specific documentation, and the need for local representatives. The most common distribution channel utilized also varies between countries, with the banking and insurance sectors competing with independent financial advisors to be the main channel for cross-border fund distribution in the region. It is worth noting that new technology has contributed to the emergence of alternative distribution channels, with many investors now gaining access to foreign funds online. This is an important consideration, as these technologies will eventually disrupt the currently entrenched distribution channels. Furthermore, technological advancements will allow new market players to leapfrog existing incumbents through the avoidance of legacy systems. Therefore, we predict significant, yet positive, disruptions to the Asian fund distribution landscape in the future.



**Market share of foreign funds in key APAC countries**  
July 2018 AuM (Billion US\$)



Distribution of foreign funds to professional investors in Asia is much more extensive than to retail investors, mainly because marketing to professional investors often comes with fewer regulatory requirements. This results in significantly quicker market access; hence, foreign fund managers often use it as a stepping-stone to Asia. There is a growing trend of Asian financial regulators simplifying the professional investor regimes to encourage foreign fund distribution. For example, in recent years the Thai Securities and Exchange Commission introduced laws opening up new channels for foreign fund distribution to professional investors. Moreover, in 2018, the Monetary Authority of Singapore (MAS) extended its definition of institutional investors, following a similar move taken by the Korean Financial Supervisory Service in 2017. Another noticeable trend is increasing international cooperation between Asian and European regulators through the development of mutual recognition schemes and signature of Memoranda of Understanding (MoU). For example, the Hong Kong Securities and Futures Commission (SFC) has developed numerous mutual recognition regimes, most notably with Luxembourg, France, Switzerland, and the UK. Moreover, Australia, Hong Kong, Japan, Korea, Malaysia, New Zealand, Singapore, Thailand and Vietnam have all signed MoUs with many EU regulators in relation to Alternative Investment Funds (AIFs) to allow AIFs domiciled and managed in Asia, the possibility to distribute in the EU through the various national private placement regimes.

The most ambitious intercontinental integration project is still ongoing—the extension of the AIFMD passport to Asia. The European Securities and Markets Authority (ESMA) assessed the possibility of extending the AIFMD passport to third countries and, in its most recent opinion in 2016, gave extremely encouraging feedback on AIF integration between Asia and Europe. Predictably, due to the maturity of their markets and regulators, Hong Kong and Singapore appeared as the two most likely locations to benefit from such a passport extension. According

to ESMA, these two financial centers offered no significant obstacles regarding investor protection, competition, market disruption or the monitoring of systemic risk. Unfortunately, due to extenuating circumstances, this AIFMD passport has yet to be fully extended to any third country. One potential future blocking point to take into account is that neither Hong Kong nor Singapore consider all EU member states' regulatory regimes as equivalent to their own, particularly in regards to UCITS. Understandably, ESMA has suggested that if there were little equivalence in the UCITS world, European regulators would equally struggle to reconcile such unequal treatment in the alternative sphere. While obstacles exist, the rapid growth of cross-border distribution in Asia, particularly to and from Europe, sees no sign of slowing down. Nonetheless, the need for a bespoke approach to cross-border distribution in the region continues to be of paramount importance.

“Asian growth is inescapable; the key question is whether international asset managers are brave enough to embrace the resulting opportunities.”





**Regional Distribution**

One significant point mentioned during the Cross-Border Distribution Conference was the strength of the UCITS brand, particularly in Asia. Consequently, one of the most recent significant shifts in the Asian asset management industry is the deepening levels of regional integration in pursuit of a UCITS-like regime or, at the very least, in pursuit of some of its benefits. We have witnessed such integration occurring on three levels: informal market practice, bilateral regulator-to-regulator, and regional, all of which have experienced varying levels of success. At the market practice level, we are aware of instances where regulators have looked to their regional peers for guidance on regulatory regimes and registration of foreign funds.

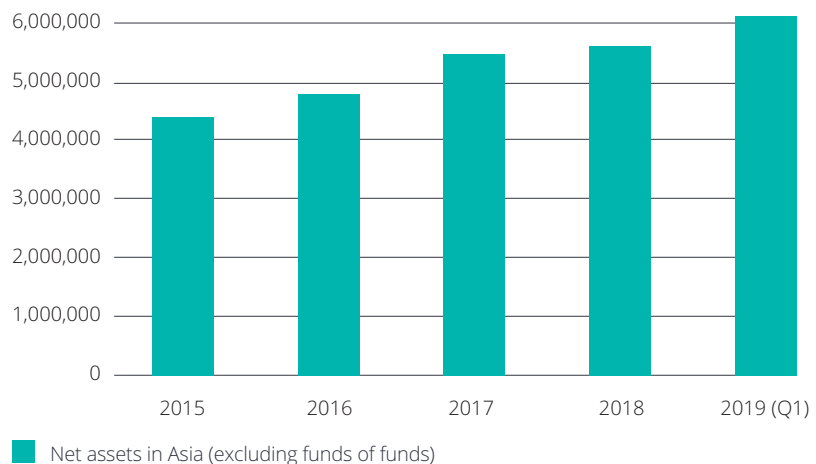
A second level of integration relates to bilateral agreements. Following on from Hong Kong’s pursuit of mutually beneficial relationships with European regulators, the SFC has also been at the forefront of Asian bilateral integration. Hong Kong has signed mutual recognition agreements with Australia and China, while also developing an Exchange Traded Fund (ETF) regime allowing international and Chinese mainland investors to trade in ETFs listed on the Hong Kong, Shanghai and Shenzhen stock exchanges. However, our perception is that some of these bilateral agreements have not been as successful as had been hoped, for example, despite Australia and Hong Kong’s mutual recognition agreement there have been no material asset flows in either direction in over ten years.

The most exciting element of fund distribution integration in Asia is the introduction of regional fund passporting regimes. 2014 saw the introduction of the ASEAN Collective Investment Schemes (ASEAN CIS) regime which is open to all 10 ASEAN nations; in 2018 the ASEAN CIS only had three members –Singapore, Malaysia and Thailand. In February 2019, the Asia Region Fund Passport (ARFP) was launched with Japan, Australia and Thailand all allowing the distribution of funds domiciled in these jurisdictions to professional and retail investors in their local markets. New Zealand followed suit by

implementing their local ARFP regulations in June 2019. Leaving only South Korea that has agreed to take part in ARFP but has yet to implement the regulations into national law. To date, only these five countries out of the 21 Asia-Pacific Economic Cooperation (APEC) members have agreed to take part in the ARFP. It is worth noting however, that the ARFP has specific qualification criteria including legal structure, assets, restrictions on portfolio allocation, valuation and pricing, reporting and capital requirements, which may prove cumbersome to overcome. In addition, each jurisdiction has also introduced specific local requirements, such as specific documentation and additional mandatory reporting.

The ARFP is seen by many as the future Asian version of the globally recognized UCITS brand and is therefore not to be underestimated, especially when coupled with its significant investment opportunities. This will of course take time especially when considering that the UCITS brand, although only 30-years-old, also required time to reap the benefits of both local and global success. Tax harmonization has been the issue of note contributing to the ARFP’s perceived slow uptake. However, Singapore, as one of the region’s fund powerhouses, has made its intentions clear to join the ARFP once these tax issues are resolved. Many see this as the pivotal contributor to the ARFP’s future success.

**AuM evolution in Asia per year**



Source: EFAMA Statistics 2013-2017

**Opportunities**

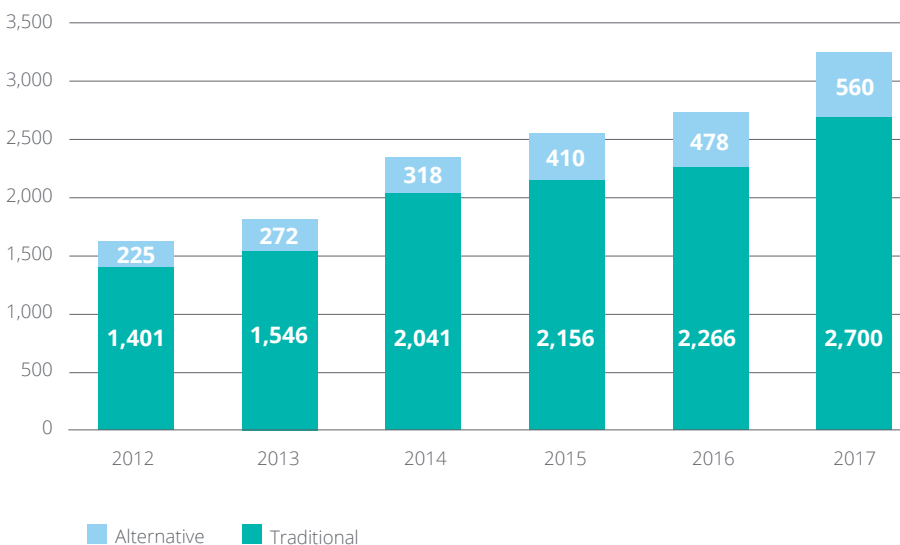
Evidently, any successful global distribution strategy must include Asia. The real question, therefore, is how best to take advantage of the significant amount of untapped capital given the lack of harmonization in the region. Hong Kong and Singapore naturally draw interest with their status as major financial hubs with mature and responsive regulators, comprehensive laws, and numerous cross-border distribution possibilities. However, we see Singapore as having the edge. Although Hong Kong offers huge potential, the intense control of the highly concentrated banking sector as a key fund distribution channel makes the penetration of new products into the market an unreasonably hard task. Singapore, on the other hand, offers a burgeoning institutional investor market seeking foreign investment with a much more open-architecture distribution model.

Nonetheless, Singapore is far from the only option. There are other jurisdictions in the region that are worthy of consideration, which may potentially offer more profitable opportunities. Japan and Australia are such examples. Both jurisdictions offer significant potential through their “perfect” mix of substantial asset pools, a growing trend towards foreign investment, and mature responsive regulators with a policy objective of increasing foreign fund distribution.

Pension schemes in Japan are experiencing pressure to meet the ever-growing drain on their assets caused by the country’s ageing population. Additionally, the Japanese government has introduced various initiatives to shift the trend from household savings, to higher yielding investment products. Combining this trend with the shift of wealth towards a younger, less risk averse generation and a market trend

towards a reduction in domestic equity and bond exposure, a positive image develops that shows the significant potential for foreign funds to distribute in Japan.

**AuM of asset management industry in Singapore (Billion US\$)**



Source: MAS Asset Management Survey 2017

**HNWI wealth, 2018 (US\$ billion)**



**18,460**  
United States



**7,523**  
Japan



**5,034**  
Germany

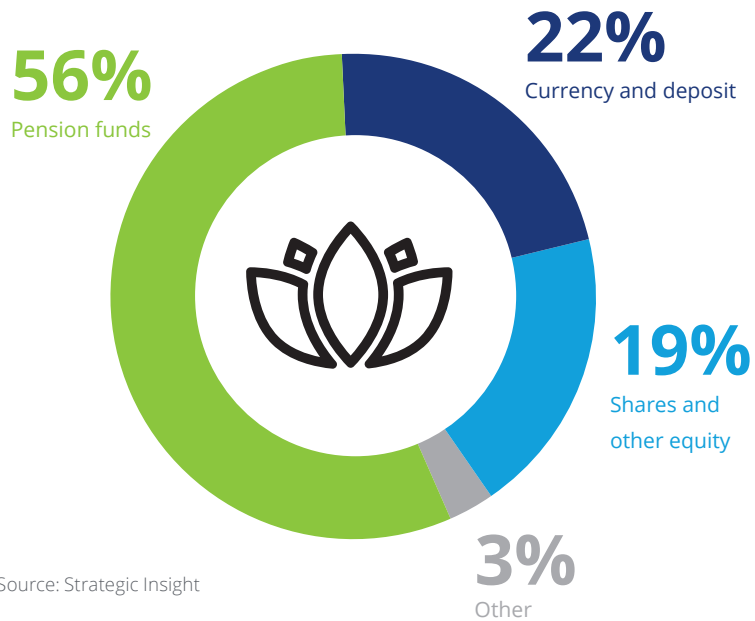
Source: Bank of Japan

Australia is equally exciting. The mandatory pension scheme contributions into the superannuation funds are set to increase further over the coming years, thereby significantly increasing the pension fund asset pool. Additionally, a significant reduction in compelling domestic investment opportunities leads to the ever-increasing need for these superannuation funds to diversify their holdings. Despite the different regulatory regimes present in Australia, if foreign funds were more inclined to enter the market and specifically target these Australian pension funds, they would certainly discover motivated investors with significant pools of investable capital.

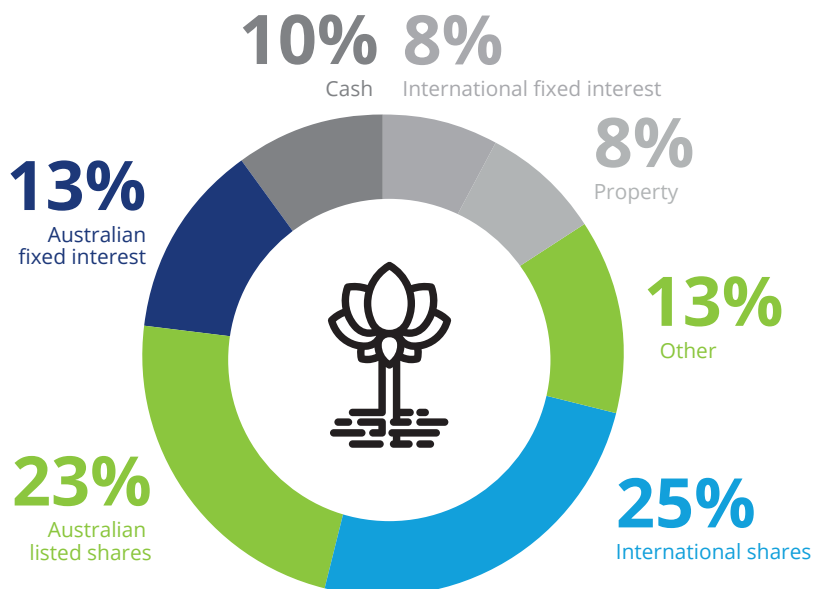
**What next?**

While the lack of homogeneity in the region, both in terms of varying levels of market maturity and the diversity of opportunities, paints a somewhat daunting picture, the prospects should not be underestimated. From bilateral MoUs, to direct retail distribution channels, from region-wide fund passports to feeder fund capabilities, there are innumerable ways to access the Asian fund distribution market. What is evident is the need to develop a dedicated and strategic roadmap to navigate this complex region, with clear objectives in terms of investor types, distribution channels and regulatory regimes. Should you wish to learn more about this exciting new frontier for the asset management industry, our publications on Asia offer an excellent next step for your foray into this region.

**Australian household financial assets' allocation, 2018**



**Australian superannuation funds' asset allocation, 2018**

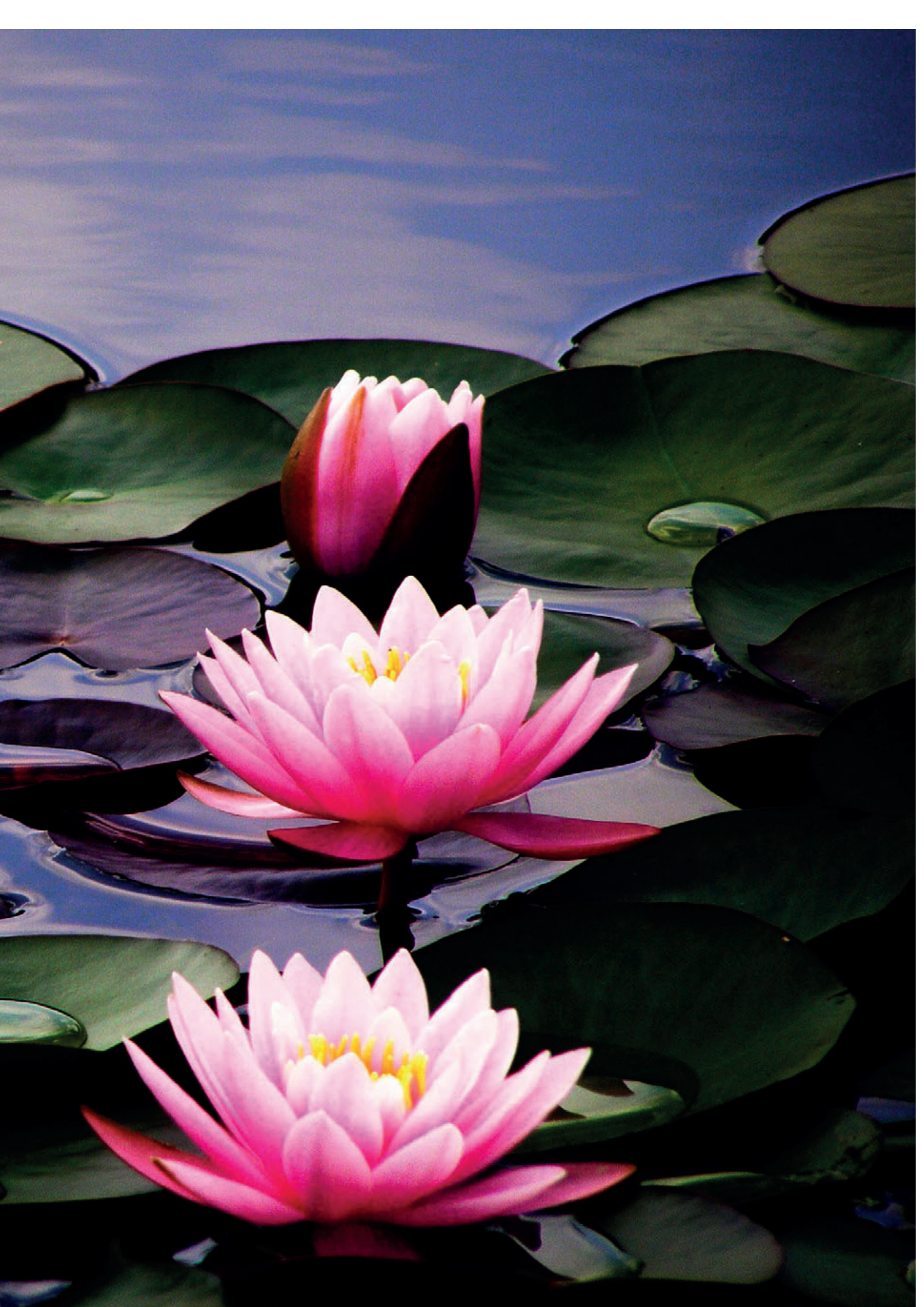


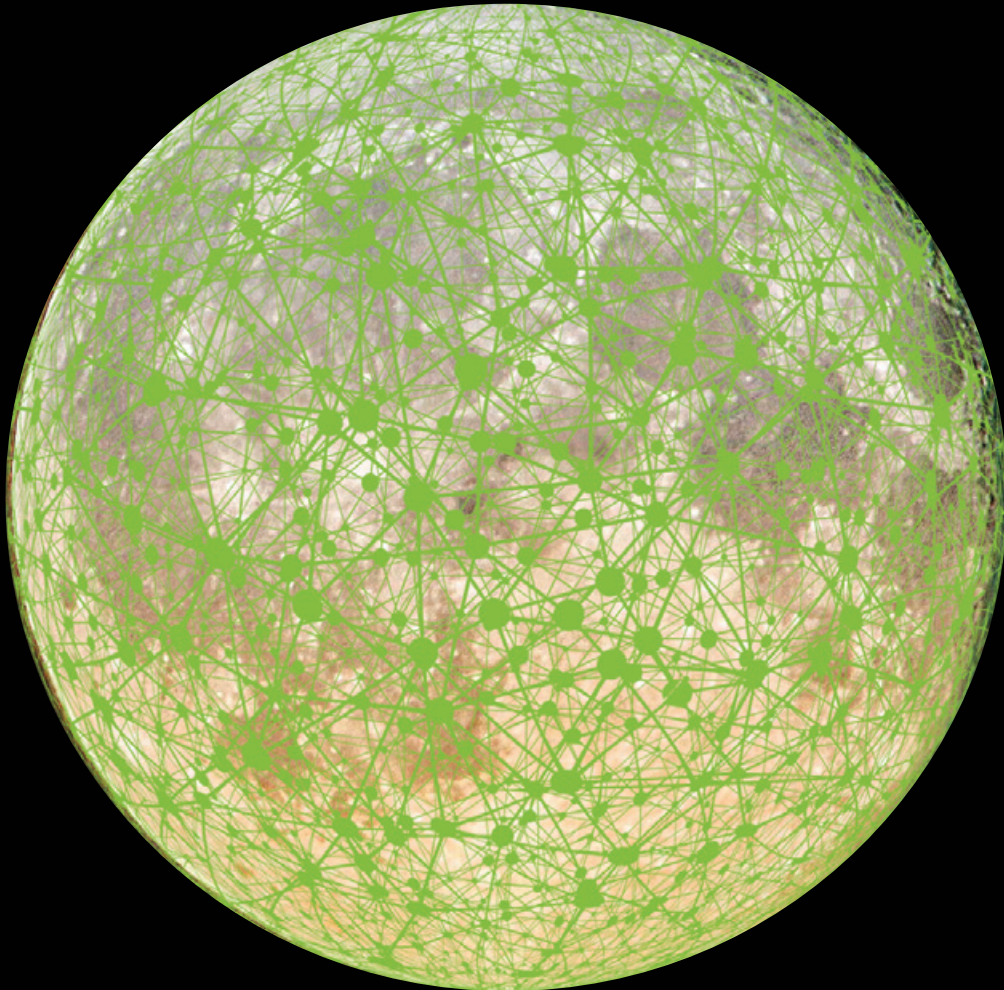


**To the point:**

- Much of the evidence suggests that Asia will offer some of the best future opportunities for the asset management industry with its incomparable GDP growth, extensive financial infrastructure development, significant regulatory advancement, regional integration, and major social change
- Over the past decade, Asian financial regulators have been at the forefront of developing robust comprehensive regulatory regimes for both local and foreign fund distribution
- Cross-border fund distribution options in Asia are extensive, with many European domiciled asset managers already creating their Asian footprint
- The real question, therefore, is how best to take advantage of the significant amount of untapped capital given the lack of harmonization in the region
- Although Asia is often considered as being off the beaten track, the windows of investment opportunities are beginning to open

“Singapore... offers a burgeoning institutional investor market seeking foreign investment with a much more open-architecture distribution model.”





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**26 September**
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- Delegation, Oversight & Due Diligence  
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