



2022 investment management outlook

Positioning for a greater impact

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KEY MESSAGES

- Progress toward quantifiable and transparent business metrics can help firms achieve a higher bottom line, financially and socially, based on our survey conducted in the summer of 2021. Respondents that made a lot of progress quantifying the impact of DEI initiatives were more likely to indicate that employee engagement and productivity have become much stronger since the start of 2021, than those who did not make a lot of progress quantifying the impact of DEI.
 - The workplace talent model is likely to continue to shift in 2022 as employees and firms adapt to the ever-changing requirements of operating in today's environment. Internal communication plans are often baked into bold talent actions to maximize benefits. Implementing good business decisions absent communication plans that are cognizant of cultural impact can lead to suboptimal results. However, when firms pull additional levers with an eye on increasing overall employee well-being and communicate those plans effectively, they can create opportunities for a stronger culture over the long term.
 - An overwhelming majority (85%) of our respondents that use AI-based solutions in the preinvestment phase either strongly agreed or agreed that AI helped them generate alpha. Using natural language processing and generation (NLP/G), a type of AI technology, analysts can save time spent on data collection and instead focus on analyzing data with a higher potential for insights.
 - Since investment management is a highly relationship-oriented business, firms that can better engage with clients and deliver on their expectations will likely be more successful. Our survey shows that 38% of respondents from digitally advanced firms expect significantly better revenue prospects in 2022 compared to just 13% for other, less digitally advanced firms, supporting the notion that digital interaction is part of the relationship.
 - There appears to be a significant regional difference in the implementation of digital transformation and modernization of governance mechanisms. European firms lead on the responsible implementation front with 27% of the respondents indicating that their firms are accelerating digital transformation as well as updating governance, followed by Asia Pacific (20%) and North America (11%). Left unchecked, inadequate governance and reporting that trails digital transformation could lead to significant financial, legal, and reputational repercussions.
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The year ahead

FINDINGS OF THE 2022 global outlook survey point toward varied results and expectations for investment management firms. This outlook will explore the connections between actions taken, the self-perceived cultural health of investment management firms, and growth expectations for 2022. The survey findings are interesting, and there's plenty to pay attention to—for example, responses from investment management industry leaders indicate a correlation between strengthening firm culture and revenue growth expectations. Talent matters and culture matters. The crucible of the pandemic

continues to test leadership to present a vision for the future and credible tactical steps to achieve it.

To begin with, this outlook will focus on asset growth and performance within the investment management landscape. We will then look at other success enablers such as talent models, technology and change, and vision. The varied results we expect in 2022 may be driven by the ability of some firms to create a virtuous cycle of vision, operational achievement, alignment with stakeholder expectations, staff resilience, and strengthening culture.

ABOUT THE DELOITTE CENTER FOR FINANCIAL SERVICES 2022 GLOBAL OUTLOOK SURVEY

The Deloitte Center for Financial Services conducted a global survey among 400 senior investment management executives in finance, operations, talent, and technology.

Survey respondents were asked to share their opinions on how their organizations have adapted to the varied impacts of the pandemic on their workforce, operations, technology, and culture. We also asked about their investment priorities and anticipated structural changes in the year ahead, as they pivot from recovery to the future.

Respondents were equally distributed among three regions—North America (the United States and Canada), Europe (the United Kingdom, France, Germany, and Switzerland), and Asia Pacific (Australia, China, and Japan).

The survey included investment management companies with revenues of at least US\$500 million and was fielded in July and August 2021.

The investment management landscape: Opportunities abound

In 2021, the investment management industry fared well despite the pandemic-driven market volatility. In the United States, while most active equity managers trailed the broader US equity composite, more managers (43%) achieved one-year alpha on an absolute returns basis in 2020 compared to the longer 10-year period over which 83% underperformed.¹ On average, the equally weighted performance of US active equity funds outperformed the broad benchmark by 0.6%, outperforming for the first time since 2013.² When considering the all-funds comparison, US active equity managers may be well-positioned to start a trend for a second consecutive year, as these funds outperformed by almost 5% for the one-year period that ended on June 30, 2021.³ However, when different style segments and risk-adjusted returns are taken into consideration, the path to resurgence for active managers becomes more complicated.⁴

Active managers' success varies significantly between global regions. Equity active managers in Euro area, the United Kingdom, and Japan enjoyed outperformance relative to their regional benchmarks over the one-year period ended 2020 (4.2%, 8.0% and 2.9%, respectively).⁵ Portfolio managers in Australia, however, have some catching up to do as the average equity fund trailed the broad Australian market index by 0.2%.⁶ Perhaps the volatility and uncertainty around the direction of global financial markets is helping to turn the performance tide in favor of active managers. Time will tell.

In the global alternative investment management space, private capital (private equity, private credit, infrastructure, and real estate) continued its relative outperformance to hedge funds, returning 15.5% in 2020 compared to 11.1% for hedge funds,

even as both saw AUM rise around 20% during the year.⁷ AUM growth in private capital and hedge funds is likely to continue through 2022 as investors indicated high levels of satisfaction in the performance of private capital and hedge funds in the first half of 2021.⁸ For hedge funds, the US\$57.8 billion in new capital flows through the first five months of 2021 speaks to the overall positive sentiment from investors.⁹ Private equity funds may also see inflows increase as the number of investors planning to increase their allocations to private equity in the second half of 2021 rose to 43% from 34% in the first half of 2021.¹⁰ Overall, investor sentiment remains positive and alternative investments may be well-positioned for growth across asset types.

For traditional investment managers, there are various regional opportunities for asset growth. Pension funds in China are in the process of outsourcing assets to external investment managers. The outsourced portion of pension assets may grow to as much as RMB 6 trillion (~US\$1 trillion) over the next several years.¹¹ Given this, we expect more investment management firms to explore opportunities in China.

In 2021, the investment management industry fared well despite the pandemic-driven market volatility.

Cryptocurrency is another potential area for growth for investment management firms. Cryptocurrencies number in the thousands, each introduced with a different purpose and different valuation drivers. Investment management firms have the opportunity to create novel products by bundling these currencies into funds with different risk and return characteristics. Some investment management firms have already launched products related to these digital assets. Europe is leading the space hosting eight of the top 10 best performing

exchange-traded products (ETP) that track cryptocurrencies.¹² More passive and managed digital asset products could be launched globally in 2022 as both client demand increases and regulatory clarity are expected.

For the firms that are not achieving alpha, digital transformation is one path that can help create a credible story about their brand promise to generate alpha, which may be a prerequisite to AUM growth. However, digital transformation can be difficult to achieve. More and more firms are choosing the mergers and acquisition (M&A) path

to align their investment strategies with advanced digital operations. As a result, continued increases in M&A activity are expected within the investment management space in 2022.

As firms are positioning differently to achieve alpha, the outlook for 2022 is likely to be driven by the quest to have the investment strategies supported by highly advanced digital capabilities. Firms can take many approaches to achieve these capabilities, but typically first and foremost is developing and maintaining a talent pool that can execute strategies to achieve their vision.

The need to bring agility into talent management

TODAY, MUCH OF the discussion of what the future of the workplace may look like is centered around some sort of a “hybrid” workforce model in which some employees are on-site, some work remotely, while others may work from anywhere depending on their needs and schedule.¹³ While the return to the workplace strategy remains under development, it is accompanied by several other important talent-centric success initiatives to meet strategic goals while enhancing corporate culture. These include redefining the communication strategy for talent, quantifiably addressing the firm’s vision and purpose, upskilling existing talent to meet changing requirements, staff resilience, and the utilization of mergers, acquisitions, and outsourcing. Let’s explore each one of them in detail.

Return to the workplace

Every investment management firm faces the return to the workplace transition. Most firms currently have hybrid approaches in place. However, only a few firms have declared and implemented long-term strategies at either end of the spectrum of opportunities—majority back as soon as possible and highly flexible on return to the workplace. There are interesting cultural dynamics at play in these approaches that firms may consider as they formulate their long-term strategy. Almost three-fourths of the survey respondents indicated their firm is likely to adopt either a majority back as soon as possible or a highly flexible on return to the workplace strategy.

When asked to report on their firm’s culture since the onset of the pandemic, 38% of these respondents reported that their firm’s culture has become much stronger compared to only 25% who indicated that their firms are likely to adopt a more complicated hybrid model for the long-term. The declared long-term intentions of the firms at the ends of the spectrum are likely contributing to respondents indicating that their firms are emerging much more culturally stronger. A group of investment management firms, including Goldman Sachs Asset Management, have well-articulated positions that investment management is best carried out over the long-term with an apprenticeship model that requires employees to be present in the office.¹⁴

Almost three-fourths of the survey respondents indicated their firm is likely to adopt either a majority back as soon as possible or a highly flexible on return to the workplace strategy.

The firms in the middle may be suffering from a specter of uncertainty haunting employees. Only 25% of respondents at these firms with wait-and-see or hybrid workforce model approaches indicated that their firm is emerging with a much stronger culture since the start of the pandemic. The communication level needed to help

employees understand a complex and still changing end-state is likely much harder to achieve.

Developing and communicating these vital return-to-the-workplace plans optimally is tricky and impactful—especially for the firms that choose a hybrid end-state.

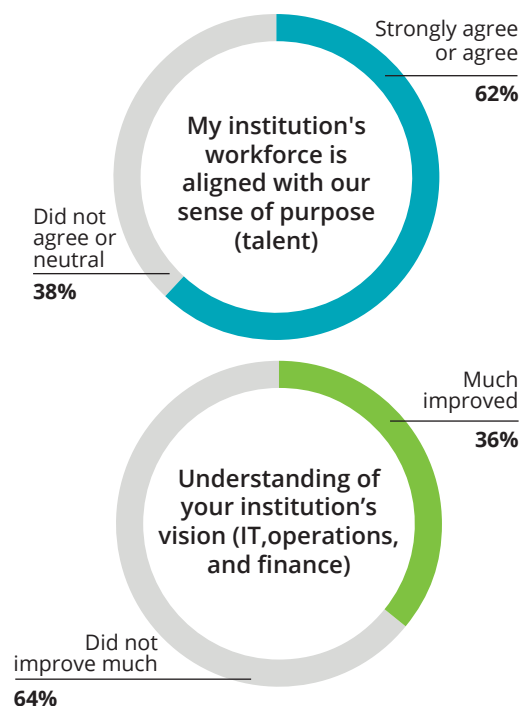
Communication strategy

From the uncertainty related to the return to the workplace to the increased demand for social justice, leaders at many investment management firms have had ample reasons to reexamine their firm's vision and purpose. As they reconsider their firm's mission statements, there's also an opportunity to rethink how they will communicate this renewed sense of purpose with their employees to ensure they feel empowered and aligned with it. However, many investment management firms may find this challenging due to the existing gap in alignment between functional organizations within the firm about purpose. According to our survey, 62% of talent professionals strongly agree or agree that their firm's workforce is aligned with their institution's sense of purpose. This number is not improving dramatically. Only 36% of respondents outside of talent (IT, operations, and finance) believe that their understanding of their institution's vision has improved since the start of 2021, as shown in figure 1.

This gap in employees' alignment with their organizational purpose may exist due to uncertainty among employees outside of the talent function regarding their personal contribution to the firm's vision. To remove this uncertainty, firms may rethink their vision and allow all their employees to become cocreators of the firm's

FIGURE 1

There is a gap in alignment of purpose and vision between respondents from talent and other functions



Source: The Deloitte Center for Financial Services Global Outlook Survey 2021.

purpose.¹⁵ By giving their employees a voice, a collaborative relationship with workers that is sustainable and possibly even a differentiator may take hold.¹⁶ This approach should be considered regardless of the long-term workplace strategy, as only 37% of all respondents indicated their understanding of their firm's vision was much stronger since the beginning of 2021. It's important to note that successfully engaging with employees in cocreating the firm's purpose goes beyond taking employees' input; it includes giving them influence into how best to achieve that purpose.¹⁷

Transparent quantifiable metrics

Investment management firms today have the opportunity to reimagine the role they play in society taking into consideration a broader range of stakeholders such as employees, customers, regulators, and shareholders. Key focus areas in this regard are trust and confidence. As a first step to boost trust and confidence, the investment management industry can look to confront greenwashing. Greenwashing is one of the biggest challenges in making sustainability decisions as some sustainability initiatives are plagued with a lack of transparency.¹⁸ A similar issue that many investment management firms face as they work to address a lack of diversity in senior levels is diversity-washing. Disclosing progress using quantifiable metrics may help prevent accusations of both greenwashing and diversity-washing.¹⁹ Through these types of disclosures, investment management firms may contribute to the rebuilding of the public's trust in institutions as the future of financial services moves toward a higher bottom line for the benefit of all of society's stakeholders.²⁰

When a firm delivers a message around social issues, being genuine may be more crucial to gain its workforce's support as opposed to trying to make the boldest statement.²¹ Being able to demonstrate the firm's progress toward achieving a goal is a key component of avoiding potential diversity-washing claims from stakeholders. For example, our survey indicates that many investment management firms have made some strides in their diversity, equity, and inclusion (DEI) efforts. The percentage of respondents who strongly agree or agree that their firm is focusing on increasing the level of diversity in hiring, development, and leadership increased to 60% from 43% in the prior year. One possible explanation for such a meaningful increase may be that these firms reported their progress on DEI initiatives.

Avoiding potential negative implications of diversity-washing is one part of the solution. To make sure they make meaningful progress on achieving their goals, firms should first quantify the impact that their efforts are making. Our recent survey results show that DEI reporting is related to employee engagement and productivity.

Respondents who made a lot of progress quantifying the impact of DEI initiatives in their financial statements were more likely to indicate that employee engagement and productivity have become much stronger (39%) since the start of 2021, than those who did not (19%) make a lot of progress quantifying the impact of DEI. Productivity appears linked to achieving aspects of the firm's vision. Respondents also indicated that collaboration and teamwork became much stronger for firms that made a lot of progress quantifying DEI initiatives than firms that didn't (38% vs. 28%). Progress toward quantifiable and transparent business metrics can help firms achieve a higher bottom line, financially and socially.

In addition to increasing the focus on DEI, many firms are implementing broader ESG initiatives. However, few firms are reporting the impact of these initiatives in a robust way. In most cases firms are increasing their focus on ESG initiatives but are failing to realize the full benefit of differentiation. This gap between implementation and communication demonstrates the importance of reporting quantifiable metrics to all stakeholders. Firms that do not adequately report the impact of ESG initiatives may be perceived by customers and regulators as performing greenwashing.²² Greenwashing has led to increased risk of losing clients, regulatory scrutiny, and deteriorating access to financing.²³

Intelligent employee upskilling

In 2022, investment management firms have an opportunity to use training and development to

help their talent stay abreast of developments in products, asset classes, processes, and technologies. Investing in employees' relevant training needs can help reap benefits in multiple ways. Doing it well by tailoring opportunities for upskilling to each employee's personal goals can improve collaboration and employee well-being and create a stronger culture. While 65% of respondents working in senior talent roles strongly agree or agree that their firm is educating and training talent on relevant skill sets, only 35% of respondents from other functions believe their firm's emphasis on learning has been much stronger since the pandemic. A possible solution for narrowing this gap is to use a personalized upskilling approach aligned with each employee's goals. Rather than allocating the trainings available to employees, firms can flip the script by setting up an opportunity marketplace allowing employees to take control of their career path.²⁴ This change may in turn improve employee retention.²⁵ As employees begin to feel their firm's training opportunities align with their own, the firm may experience positive impacts elsewhere. For example, the respondents who reported a much stronger emphasis on learning at their firms were:

Respondents indicated that collaboration and teamwork became much stronger for firms that made a lot of progress quantifying DEI initiatives than firms that didn't.

- 28% more likely to say collaboration has gotten much stronger across teams
- 34% more likely to report much stronger employee well-being

- 52% more likely to indicate that their firm has developed a much stronger culture at their organization since the onset of the pandemic.

Training programs at investment management firms will likely see increased emphasis in 2022, and the most successful programs are likely to enable employees to drive their training curricula.

Staff resilience

Employee productivity, well-being, improved risk appetite, empowered decision-making, and team collaboration are elements of culture that together represent staff resilience. Staff resilience risk is mitigated when firm cultures are strengthened. Respondents who reported that their firms' overall culture became much stronger since the beginning of 2021 were:

- 61% more likely to indicate that they have gotten much stronger in terms of empowered decision-making
- 58% more likely to say their risk appetite has become much stronger
- 37% more likely to report much stronger employee engagement and productivity
- 27% more likely to state collaboration has gotten much stronger across teams
- 25% more likely to report much stronger employee well-being

In fact, only 20% of respondents in firms that have emerged much stronger culturally ranked staff resilience risk among the top two operational risks, compared to 40% at firms with lesser cultural strength ranks.

Firms are taking specific strategic actions aimed at building a strong company culture and mitigating

staff resilience risk. The Carlyle Group has taken such a step by linking its chief executive officer's compensation to developing an inclusive culture at the firm.²⁶ Moreover, the company has also set aside US\$2 million to recognize employees that have gone above and beyond to meet DEI goals.²⁷ DEI initiatives can help to build better culture and improve profitability and productivity.²⁸ While many firms have programs addressing DEI, Legal & General Investment Management (LGIM) represents one success story. LGIM attributes their ability to achieve gender parity in senior leadership to being flexible, adaptable, and constantly receptive to employees' views.²⁹ These culture strengthening actions can impact employee resilience at an important time, when good talent is hard to replace, and openings can strain productivity.

The workplace talent model is likely to continue to shift in 2022 as employees and firms adapt to the ever-changing requirements of operating in today's environment. Internal communication plans are often baked into bold talent actions to maximize the benefits. Implementing good business decisions absent communication plans that are cognizant of cultural impact can lead to suboptimal results. However, when firms pull additional levers with an eye on increasing overall employee well-being and communicate those plans effectively, it can create opportunities for a stronger culture over the long-term.

Mergers, acquisitions, and outsourcing

As firms manage their cost, capability, and scale equations, mergers, acquisitions, and outsourcing continue to be in the solution set. Survey findings indicate that global M&A activity is expected to

increase broadly with concentration in investment management firms with between US\$5 billion and US\$10 billion in annual revenue over the course of 2022. This finding aligns with expectations for continued consolidation among smaller and mid-sized investment management firms to gain more capabilities to better serve clients.³⁰

Interestingly, our survey shows that adding new technology capabilities is the top driver for respondents' M&A transactions, followed by increasing scale and distribution channel expansion. These firms are looking to fuel growth through enhanced products and customer experience delivered to an expanded client (and prospect) base. M&As are expected to accelerate in 2022 as many firms can still potentially benefit from them.

Rather than allocating the trainings available to employees, firms can flip the script by setting up an opportunity marketplace allowing employees to take control of their career path.

The number of deals in the investment management space has increased from 516 in 2016 to 628 in 2020.³¹ Furthermore, the number of deals announced through Q3 for 2021, 2020, and 2019 are 548, 457, and 484, respectively, showing a spike in 2021.³² The deal value has increased to US\$31.6 billion for the first three quarters of 2021 compared to US\$26.3 billion and US\$22.2 billion during the same period in 2020 and 2019, respectively.³³

Outsourcing has recently garnered attention from FINRA for its impact on extended enterprise risk.³⁴ In addition to the regulatory and risk considerations, investment management firms may benefit from conducting a more holistic review of the potential effects that outsourcing may have on its workforce. When a strategic decision is made to outsource a function, the firm may also want to take steps to ensure that cross-functional processes remain unaffected. Respondents in talent roles who indicated that increased outsourcing could most effectively improve their institution less

frequently suggested hiring more risk and compliance management talent. Investment management firms that neglect to include the need for enhanced governance and control as costs in their outsourcing decision-making process may overstate the benefits to the firm and its stakeholders. To effectively minimize disruption to the firm's culture, employee engagement, and employee well-being, firms can communicate the strategic nature of the transaction and the benefits to both the affected employees and to the firm.

When making a strategic decision to outsource a function, firms should take steps to ensure that cross-functional processes remain unaffected.

Reinvesting to change the business

INVESTMENT MANAGERS ARE increasingly investing in transforming their operations. Firms are using cost savings driven by pandemic-related pressures and a positive economic environment to invest in cloud and outsourced services more frequently than replacing proprietary and on-premise technology. Though most firms are digitally transforming their businesses, they have made progress to varying degrees. One factor that sets apart firms in their digitization journey is their agility in execution. Only about half (49%) of our survey respondents reported that their institution's agility in execution has emerged much stronger since the beginning of 2021. Demonstrating the importance of agility to digital transformation, a vast majority (85%) of these "much stronger" respondents ranked their organization 8 or higher on a 10-point scale when asked to indicate how close their firm is to the ideal digital organization, compared to just over half (51%) of all other respondents. That said, firms of all stripes are expected to continue their digitization efforts in the next year. Survey responses indicate that the most important drivers for digitization include improving operational efficiency (45%) and creating opportunities that did not exist or were not viable previously (42%). Let us dive deeper into each of the drivers.

Improving operational efficiency

Operational efficiency is increasingly important for traditional investment managers as the rise of low-cost passive investing increases competitive pressures. For private equity firms, efficient deal

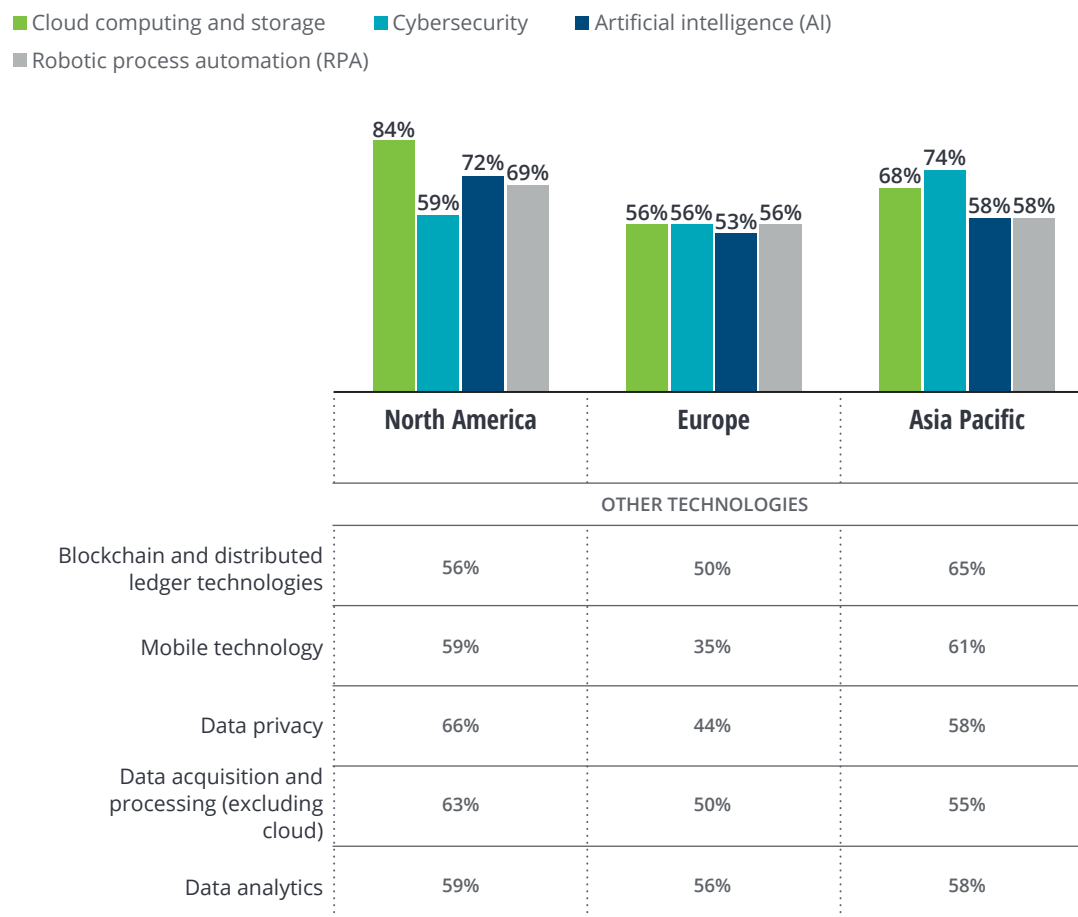


sourcing and improving portfolio company operations is a focus area as deal valuations rise.³⁵ Firms are increasingly turning to digitalization for operational improvements. As seen in figure 2, respondents from all geographies are expecting a bigger increase in net spending across emerging technologies compared to last year. This trend is likely supported by higher revenues and expanded margins that firms have enjoyed through the first

FIGURE 2

Firms surveyed across the globe plan to increase spending on emerging technologies

Expected net spending increase on emerging technologies over the next 12–18 months



Note: Net spending increase = Percentage of respondents indicating increase in spending – percentage of respondents indicating decrease in spending.

Source: The Deloitte Center for Financial Services Global Outlook Survey 2021.

half of 2021. Cloud computing and storage is a top priority, possibly aimed at supporting flexible work and enhancing operational agility and efficiency. Cybersecurity solutions that help firms securely adopt new working models continues to be one of the top priorities in 2022 as it was last year.

However, there are subtle differences at a geographic level. Spending in Europe appears to be

evenly distributed across technologies for respondents, with cloud, cybersecurity, robotic process automation (RPA), and data analytics expecting to see a net increase among firms (56%). Respondents in North America indicated net increases in spending on cloud (84%) and artificial intelligence (AI) (72%), whereas those in Asia Pacific were focused more on cybersecurity than on cloud with net increases of 74% and 68%,

respectively. Even though increases on cloud spending is a priority across geographies, it may have different drivers. Firms in Europe and North America may be focusing on creating new opportunities using data analytics and AI, while those in Asia Pacific may be targeting operational efficiency improvements.

Realizing the cost- and time-saving potential of technologies such as AI and RPA, most survey respondents said their firms are expecting a net increase in spending on these two technologies. This change represents a dramatic shift from reported spending cuts last year on these technologies. Firms may now be moving their focus from operating remotely to operating efficiently. To make the most of these technologies, firms may need to get the right data infrastructure in place. As data is the building block of AI models, firms may need to implement a data warehouse system that aggregates and stores clean data. Similarly, effective RPA implementation may require robust data exception handling to ensure the systems work as expected. Intelligent automation—which employs AI and RPA either in isolation or combination—may enable firms to reduce costs, grow revenues through better customer-targeting, and operate processes two to three times faster than humans can perform without these advanced technologies.³⁶ Invesco, using intelligent automation, has saved 3 million minutes per year across 35 business functions spanning the front- and back-office.³⁷ Implementation of these technologies led to annual cost savings of around US\$2.1 million.³⁸

However, the path to adoption may not be easy. Most respondents' institutions faced challenges in implementing AI (67%), cybersecurity (58%), and cloud computing (54%). Complexity of technology implementation is the top barrier for implementing AI (29%) and cloud (31%), while cybersecurity implementation is stifled by reliance on legacy

systems (16%). A clear institutional vision and well-defined use cases may help firms overcome some of these hurdles by enabling coordinated actions to hire required talent and modernize systems. Emerging technology adoption enables more than just cost savings. It can help generate alpha and serve clients better.

Creating new opportunities

ALPHA GENERATION

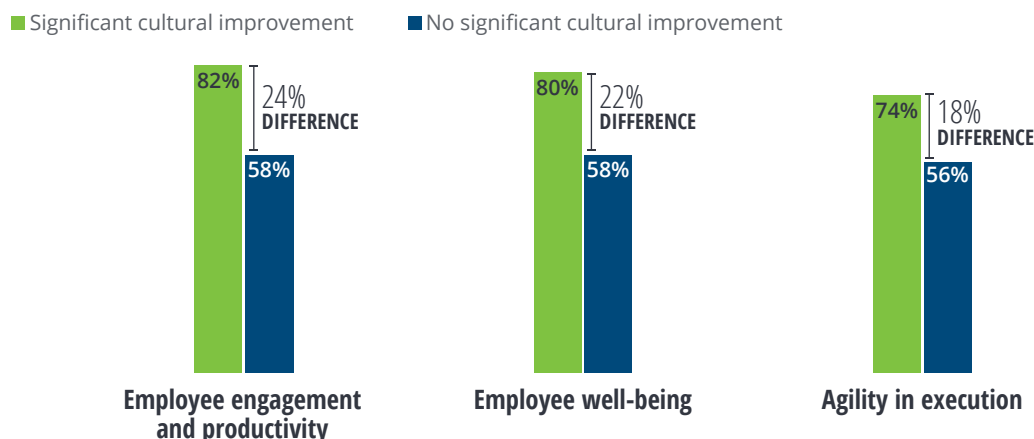
Firms can use natural language processing and generation (NLP/G), a type of AI technology, to summarize structured and unstructured data from diverse sources. Using NLP, analysts can save time spent on data collection and instead focus on analyzing data with a higher potential for insights.³⁹ An overwhelming majority (85%) of respondents that use AI-based solutions in the preinvestment phase either strongly agreed or agreed that AI helped them generate alpha.

Nearly three-fourths of our survey respondents said that they would increase their budget for alpha-generating technologies such as AI, including NLP/G, (71%) and alternative data (74%) over the next 12–18 months. However, just increasing funding may not guarantee success. Our survey found that alpha generators—respondents who strongly agreed or agreed that AI helped their firm generate alpha—stood out from their peers on certain cultural aspects. There was a strong correlation between the ability to generate alpha and better employee engagement and productivity, employee well-being, and agility in execution (figure 3). A combination of these factors also likely translated into better revenue prospects for alpha generators in 2022. Nearly a third of alpha generators (32%) were more likely to report that they expect significantly better revenue prospects as compared to about one-fifth of all others (21%).

FIGURE 3

Firms that were able to achieve alpha using AI were also more likely to focus on—and improve—cultural factors, such as employee engagement, suggesting a strong correlation

The ability to generate alpha with AI is linked to cultural improvements



Source: The Deloitte Center for Financial Services Global Outlook Survey 2021.

Leadership vision is the most important factor to kickstart the AI adoption process.⁴⁰ Firm leadership will likely play an important role in bringing together the finance and operations teams and identify use cases where AI can bring in efficiency or financial results. Once such promising use cases are identified, leading practices call for firms to develop them in a sandbox followed by scaling the most promising use cases.⁴¹ UOB Asset Management Ltd. (UOB) followed such a sandbox approach while implementing its Multi-Signal Predictive Analytics Project.⁴² The sandbox allows users to develop analytical prototypes and analyze data stored in its data lake and enterprise data warehouse systems.⁴³ Moreover, UOB's AI adoption workflow process is designed to identify, scale, and fine-tune the most productive use cases while decommissioning the ones that do not meet business needs.⁴⁴

To more effectively implement AI, firms may consider establishing T-shaped teams, wherein an innovation team acts as the conduit between the investment and technology teams.⁴⁵ The innovation team's responsibility is to effectively bridge the communication gap so that the data scientists on the technology team can bring the best solutions to address the most critical investment problems. Since AI models may require iterations and time before they work as expected, firm leadership can create an open culture using this structure that allows for experimentation and discovery prior to success. Some firms including Vanguard Group and Nuveen are coaching employees to overcome fear of failure and promote innovation.⁴⁶ Since the innovation team is not a part of any traditional function, it may need leadership support to work effectively. Moreover, firms may need external expertise to set up the T-shaped teams.

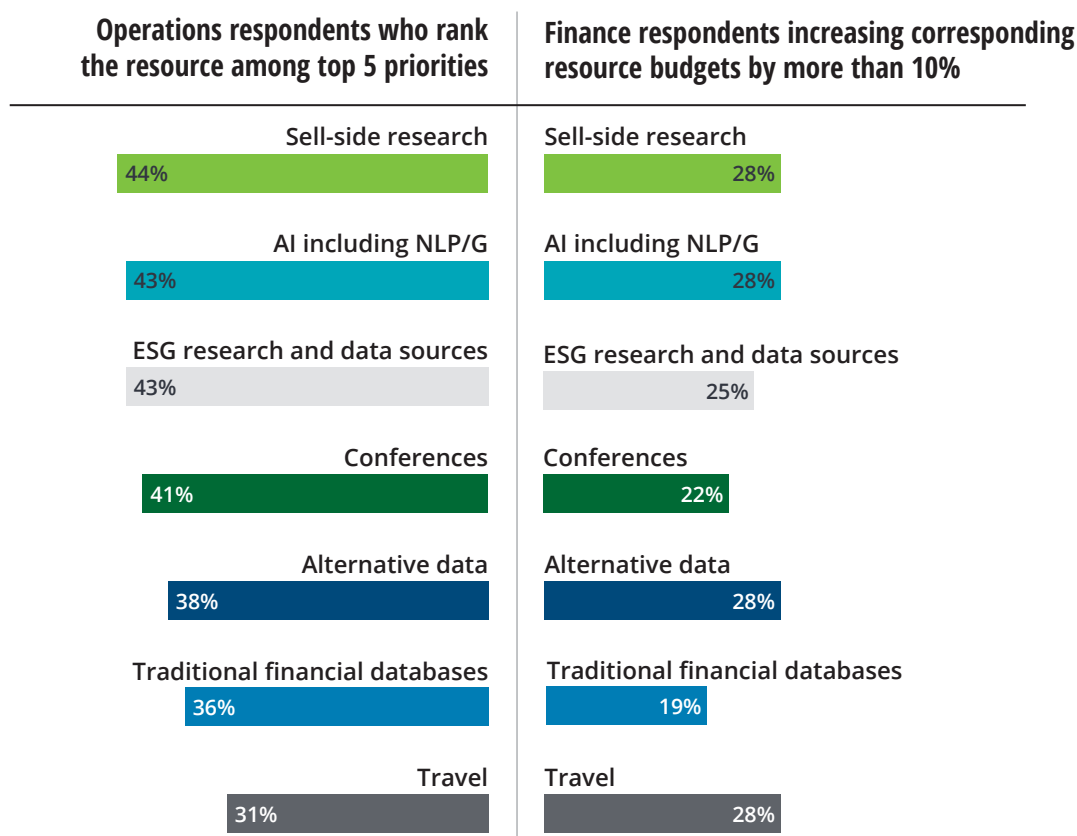
Alignment of capital allocation priorities between finance and operations is important to enhance the investment decision-making process. Survey results indicate that the finance and operations teams are aligned on some topics but not on others, signaling that leadership has some work to do (figure 4). At a global level, firms appear to be most misaligned on the importance of conferences, ESG research, and traditional financial databases. Respondents in Asia Pacific were most misaligned

on the importance of traditional databases (a 33 percentage point difference), whereas those in Europe and North America were most misaligned on conferences (25 and 30 percentage point differences, respectively). The leadership of firms with misaligned functional priorities may have to clearly communicate their strategy across functions and ensure that adequate funding and resources are available to address the organization's priorities.

FIGURE 4

Finance and operations teams surveyed are most misaligned on the importance of conferences, ESG research, and traditional financial databases

Priorities in spending, operations vs. finance



Source: The Deloitte Center for Financial Services Global Outlook Survey 2021.

CLIENT SERVICE

Investment managers are engaging with clients in some ways not possible earlier. Firms are utilizing technology to interact with clients through digital channels, handle client queries through intelligent chatbots, leverage virtual meetings in their sales and relationship building processes, and provide customized reporting. Firms can also produce personalized client interactions using data analytics by identifying clients' interests, preferred content format, and frequency of interaction.⁴⁷ Personalized communications help clients get the insights they seek. This capability in turn may enable advisers to close deals faster.⁴⁸ Since investment management is a highly relationship-oriented business, firms that can better engage with clients and deliver on their expectations could be more successful. Our survey shows that 38% of respondents from digitally advanced firms expect significantly better revenue prospects in 2022, compared to just 13% for other, less digitally advanced firms.

As firms focus on “reinvesting” to change the business, their core technology infrastructure will likely determine the direction of their spending to

generate the most benefit. A firm's core technology infrastructure generally has a significant bearing on its digitization strategy. Firms with modernized core infrastructures can increase their in-house technology spending on advanced technologies to enhance their investment decision-making process and client service. Those with legacy infrastructure may have to adopt a different approach to efficiently leverage advanced technologies and data analytics. Less digitized firms can turn to third-party cloud-based asset servicing platforms to get a unified view of client data across the extended organization. Such an approach allows firms to rapidly derive insights from data and develop products faster while mitigating some of the risks associated with substantial technology development projects.

Reinvesting to change the business is a monumental task. Alignment of all parts of the organization to the strategy and vision are key components to success. Managing talent through training and communication is another key component. When these are performed in coordination, firms may be better positioned for long-term differentiation.

Modernizing operations responsibly

Governance trailing transformation

Under the pressure of necessary change, many firms have still not been able to implement adequate governance and reporting mechanisms. According to our survey results, while 54% of the respondents indicated that their firms are accelerating digital transformation of business services, only 19% said that they have also updated governance and reporting mechanisms. There is a significant regional difference in the implementation of digital transformation and modernization of governance mechanisms.

European firms lead on the responsible implementation front with 27% of the respondents indicating that their firms are accelerating digital transformation as well as updating governance, followed by Asia Pacific (20%) and North America (11%). Left unchecked, inadequate governance and reporting that trails digital transformation could lead to significant financial, legal, and reputational repercussions. Firms are expected to work toward closing this gap throughout 2022.

Operations are transforming on multiple fronts. To stay lean and improve efficiency, some firms are partnering with external service providers to advance their digital transformation journey.⁴⁹ At the same time, firms are also embracing the virtual work environment. These new arrangements have increased the risk associated with extended enterprise and misconduct, respectively.⁵⁰

Our survey findings reveal that 95% of firms are making some structural change across front-office, middle-office, and back-office operations (figure 5).

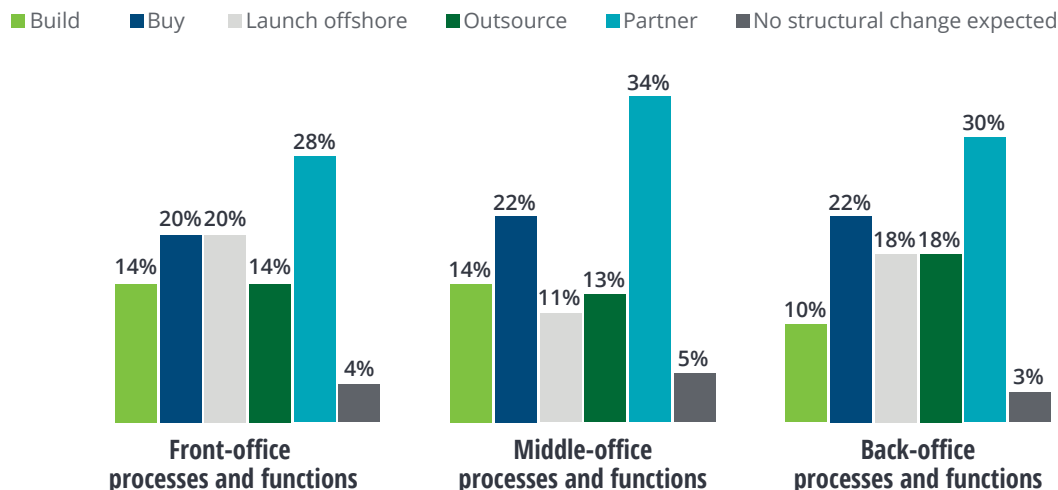
Most of these structural changes increase the firms' dependency on a greater number of external entities. Organizations with more external entities are more complex, which in turn can make these firms more susceptible to third-party risk. However, even in the face of these increased risks, 40%–50% of the firms that are planning to implement structural changes have not fully recalibrated risk management practices. If not managed properly, this gap between implementation and risk mitigation can lead to various third-party incidents related to cybersecurity, business continuity, data privacy, and ultimately reputational risk.⁵¹

Remote work models open the possibilities for conduct risk for investment management firms. Firms are increasingly investing in programs to promote ethical decision-making and reduce conduct risk. The percentage of survey respondents who agree or strongly agree that their firm is investing in training for ethical decision-making to reduce conduct risk has increased from 33% in 2020 to 57% in 2021, indicating progress on the talent front. However, technology enhancements trail training solutions with just 33% of respondents surveyed implementing surveillance and control solutions. The disconnect is even higher among European and North American firms with just 23% and 28% of respondents, respectively, indicating their firms are implementing surveillance and control solutions, compared to 46% of respondents in Asia Pacific. Firms will most likely be exposed to conduct risk until improvements are made in surveillance and control systems to match the complexities of the hybrid work environment.

FIGURE 5

Most firms are planning structural changes across their front-office, middle-office, or back-office operations

Structural changes respondents expected to transform operations over the next 12–18 months



Source: The Deloitte Center for Financial Services Global Outlook Survey 2021.

In addition to bringing new technologies into the scope of existing controls, technological solutions that can help mitigate the heightened level of conduct risk include recalibration of insider deal alert generation models, enhancement of personal accounts monitoring, prioritization of higher risk events, data analytics on alert metadata, and restriction on use of high-risk communications systems.⁵² Furthermore, establishing appropriate intelligent third-party risk management and real-time monitoring systems, and verification of third party responsible operation claims can help mitigate the third-party risk amplified by the higher pace of digital transformation.⁵³

Another consideration to mitigate the cybersecurity and data privacy aspect of third party and conduct risk is the Zero Trust framework, which assumes that all network traffic may be malicious.⁵⁴ This

methodology helps manage network access for all users and devices. It continuously verifies identities and hides applications not specifically permissioned to each user. This control posture for corporate applications and data can help deter misconduct and third-party incidences.⁵⁵

Furthermore, regulators such as the European Securities and Markets Authority and US Securities and Exchange Commission are seeking input from market participants on the use of digital engagement practices and increased reliance on third parties to examine the potential risks and concerns.⁵⁶ Firms that are putting governance and controls mechanisms in place simultaneously alongside their transformation journey, are likely to have an upper hand when such measures become mandatory compliance requirements.

Looking ahead

ALTHOUGH THE PAST two years have tested the mettle of investment management firms, their people and leadership have made a difference. Many firms' cultures have strengthened over the course of the pandemic, and there is a connection between strengthening cultures, revenue outlook, and the ability to implement important new technologies to meet evolving investor preferences. Survey results indicate that there is a virtuous cycle connecting corporate vision, strategy execution, customer service, and employee resilience. This cycle can lead to financial improvements and operational achievements. Determining where this virtuous cycle begins or ends is likely an impossible task. However, the elements that fuel the cycle are likely leadership and employee drive to exceed customer expectations.

Leadership establishes and communicates the vision for the organization. When executed well, there is alignment across functional areas for strategic priorities including capital allocations, staffing, development, and implementation. In 2022, firms with strong leadership are expected to achieve differentiated results to a greater degree than in years past, because of the magnitude and the pace of change expected throughout 2022.

The biggest development in stakeholder expectations for investment management firms is related to ESG and data processing. Investment management firms are processing new data sets with AI to meet customer ESG priorities and investment return expectations. It is likely that these efforts and the accompanying sense of achievement can also fuel the virtuous cycle. It appears that customer demand is changing investment operations and products offerings for the better, and this change will likely continue or perhaps accelerate throughout 2022.

Survey results indicate that there is a virtuous cycle connecting corporate vision, strategy execution, customer service, and employee resilience.

Investment management firms with high levels of success are likely to be simultaneously strengthening their cultures and achieving a higher bottom line.

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