

Breaking up the value chain

An extract from European IMRE News March 2009

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Recent market events, as well as competitive pressure, are making institutional investors more likely to outsource non-core activities across the value chain.



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With the proliferation of investment products, tremendously shrinking asset bases and increasing regulatory requirements, institutional asset managers currently face major challenges in fulfilling their given duties. In the context of today's difficult markets and tough competitive environment, this is forcing many to reconsider what their core competencies are.

Typically, these asset managers perform three main functions in the fiduciary management of investor assets. Viewed collectively, these comprise the investment management 'value chain'. The first and foremost function is the duty of governance, which is key to the asset manager's core value proposition and cannot be outsourced. More suitable for outsourcing 'make or buy' decisions are, secondly, the investment function and, thirdly, the underlying operations. For these functions, market trends differ depending on how critical the activities are, and the appetite for alternative sourcing options in certain countries. Consequently, outsourcing models range from the traditional, encompassing middle- and back-office functions only, to comprehensive outsourcing of both these functions and front-office portfolio management (e.g. full fiduciary management outsourcing).

Traditional outsourcing

The traditional outsourcing model covers all non-core and non-critical activities. This comprises mainly typical operations functions, but should be evaluated (and challenged) for comprehensiveness in virtually every instance. Surprisingly, this questioning and structured break-up of the value chain (as well as fair judgment on core and non-core functions) has rarely been observed in the past. Currently, the Swiss market – which trails the more mature European (e.g. UK or Luxemburg) and US markets – is taking some initial and very careful steps. However, recent market and competitive trends have put pressure on Swiss institutional asset managers to focus not only on value-generating tasks surrounding the investment process but also on ensuring cost-efficient and flexible operations. Given these circumstances and the large number of specialist providers in this field, Swiss asset managers have begun to challenge parts of their operational value chains and are, increasingly, considering alternative sourcing options.



Fiduciary management outsourcing

More progressively, there is increasing pressure to outsource the investment function – again, a form of outsourcing that is already seen in more mature markets. For example, in the past insurers have been judged on their broad ability to manage liability-driven investment strategies effectively. Yet, more recently they have been asked to tackle heightened competition and decreasing margins by seeking greater investment returns. Consequently, they are now seeking to incorporate sector specialists firms' best ideas into their investment portfolios. This is driving them to review whether their investment management function is a core competency. If not, it could also become a candidate for outsourcing, with sector specialist managers performing the money management while the insurance company focuses on the functions it naturally performs best, such as marketing, sales, customer service and liability forecasting. In this more progressive model, both investment management and platform processing can be provided as an integrated solution – full fiduciary outsourcing.

Given the strength of these trends and the continued focus on core competencies, it is fair to ask if there are any natural limitations as to the scope and granularity of the de-construction of value chains. Right now, the answer appears to be that the trend is increasingly spanning the front, middle and back-offices, as well as becoming increasingly granular in its treatment of the front-office investment process.

Summary

In conclusion, investment management is rapidly becoming a mature industry. As evidence, specialist service providers have emerged across the full value chain, from front to back office, and including areas previously thought “off limits” for outsourcing, such as the investment process itself. Service providers are offering their specific competencies at cost and quality levels that benefit both the investment management firms themselves and their clients – and the market is growing to accept this.

Investment Management and Real Estate contacts

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