

2020 investment management outlook

Crossing boundaries for profitable growth

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Contents

2020: Crossing boundaries	3
Finding growth with markets and products	5
Creating operational efficiencies	11
Customer experience and engagement	17
2020: Thriving in new territory	21
Endnotes	22

KEY MESSAGES

- The pace of mergers and acquisitions (M&A) may pick up over the coming year as investment managers look beyond their core capabilities to achieve top-line growth and extend client service offerings.
 - To expand into emerging customer segments, leading firms will likely try to resonate culturally with their new customers, deliver through current or newly developed technology, and meet the changing investment expectations, such as ESG (environmental, social, and governance) principles, of these new segments.
 - Private equity (PE) firms have started adopting alternative data for sourcing deals and conducting due diligence, following hedge fund and long-only managers.
 - Adopting and using insights from alternative data sets for managing and transforming portfolio companies can be a game changer for PE firms.
 - In 2020, Deloitte expects leading investment management firms to cross the boundary from traditional cost-efficiency projects into a save-to-transform approach, increasing competitive advantage in the process.
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2020: Crossing boundaries

THE CHANGES FACING many investment management firms are significant. Internally, long-standing operating models may need transformation to keep up with the competition, and digital-enabled customization is becoming a client expectation. Externally, firms may discover finding investors in new demographic segments or geographies is the most effective path to asset growth. Investors are adjusting their portfolio allocations in search of total return. In the retail market, this adjustment includes an expanding eye toward alternative investments. Consequently, many boards of directors of public firms with investment management capabilities are looking for new leadership they believe are better suited to deliver results in an increasingly dynamic and complex industry landscape. CEO turnover has been rising recently, with at least 37 US and European investment managers changing CEOs from 2017 to August 2019.¹

Externally, firms may discover finding investors in new demographic segments or geographies is the most effective path to asset growth.

In 2020, many investment management firms are highly motivated to cross boundaries in search of profitable growth. Crossing boundaries often means leaving the comfort zone and performing new activities or doing standard activities in dramatically new ways. Success can be found crossing boundaries with purpose: by modernizing business operations and by upgrading technology infrastructure to reimagine growth, operational efficiencies, and client experiences. All these changes are intended to delight investors with revitalized capabilities.

A quick glance at the asset growth in the investment management industry over the past nine years shows steady growth—a sign of health and stability. However, the details seem to tell a more complicated story. The mix of investments has changed dramatically over the past 10 years (figure 1). Passive funds are now the largest portion of the total US fund assets, as asset growth has followed performance. Passive funds have outperformed active funds on average, with the exception of PE, which has outperformed and grown assets steadily over the past nine years (figure 1), even with regular PE fund liquidations. These shifts coincide with an interesting global economic backdrop. While the US economy continues its record expansion, major countries in Europe may already be in recession, and China's growth slowdown is likely to continue.² A Brexit deal adds to the confusion, with investment managers executing their contingency plans.

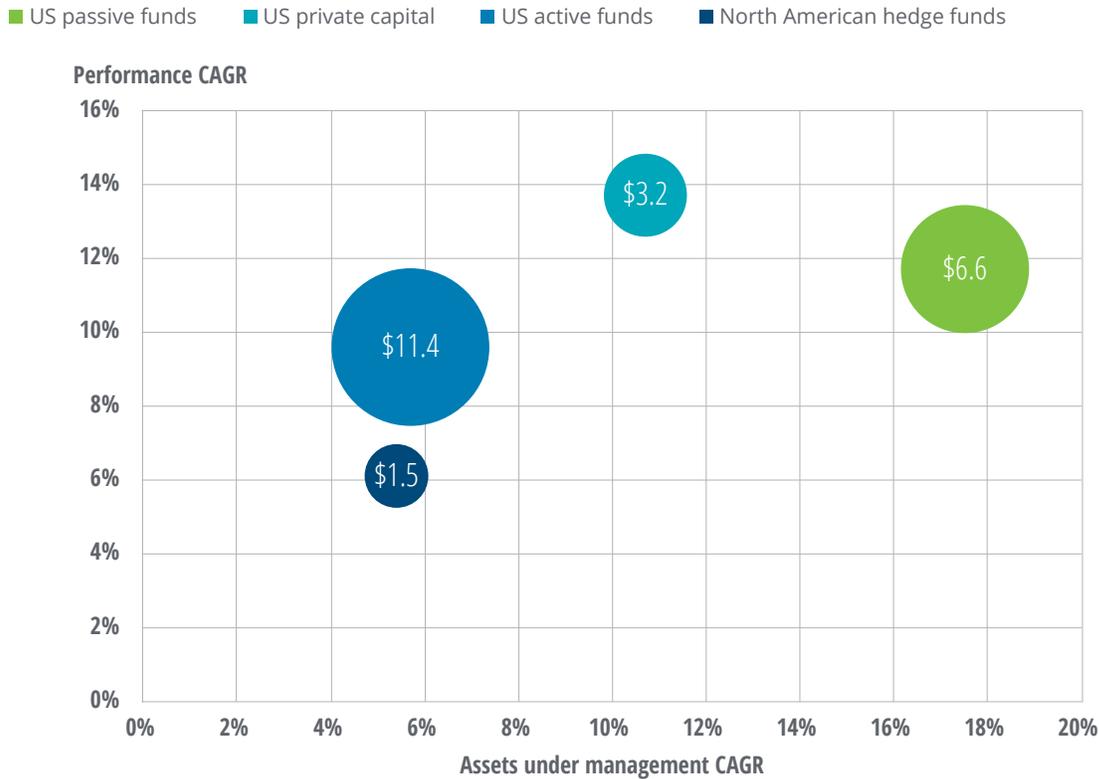
European regulators and investment hubs in Luxembourg, Dublin, Frankfurt, and Paris also continue to work on a smooth Brexit transition for investment managers.³

In spite of the overall steady industry growth, the pressures faced by long-only investment managers, PE managers, and hedge funds have remained constant for the past several years. The cumulative effect of fee pressure, a shift to passive investments, and concentration of success in gathering assets is driving many firms to continue to take bolder actions to find growth, operate efficiently, and engage customers. In 2020, many alternative and long-only investment managers alike could cross boundaries and leave their comfort zones.

FIGURE 1

Over the last decade, assets have moved into passive funds while private equity continues to outperform

US funds asset growth and performance, 2009–18



Methodology for performance and AUM chart:

1. US passive funds: Passive domestic funds comprise AUMs for 1940 Act Index ETFs (domestic and global equity, bonds, and commodity) and index mutual funds (domestic and global equity, and hybrid and bond) sourced from ICI Factbook 2019. S&P 500 Index has been used as the proxy for passive fund performance. S&P 500 Index returns have been sourced from one-year performance for S&P 500 provided in SPIVA Year-End US Scorecard reports for the years 2009–2018.
2. US active funds: Active domestic AUM comprises actively managed mutual funds (domestic and global equity, and hybrid and bond) and 1940 Act Actively Managed ETFs sourced from ICI Factbook 2019. US Domestic Active Funds (Equal-Weighted) returns have been sourced from one-year performance for all domestic funds provided in SPIVA Year-End US Scorecard reports for the years 2009–2018.
3. US private capital: US private capital AUM and performance data has been sourced from Preqin. AUM is the sum of unrealized value and dry powder. Performance looks at one-year rolling returns.
4. North American hedge funds: North American hedge funds AUM and performance data has been sourced from Eurekahedge North American Funds Key Trends March 2019 report. Hedge fund performance represents Eurekahedge North American Hedge Fund Index return, which is an equally weighted index of 536 constituent funds.

Note: The size of the bubble indicates 2018 AUM of the asset class in US\$ trillions.

Sources: ICI Factbook 2019, Eurekahedge, Preqin, S&P Global Market Intelligence.

Finding growth with markets and products

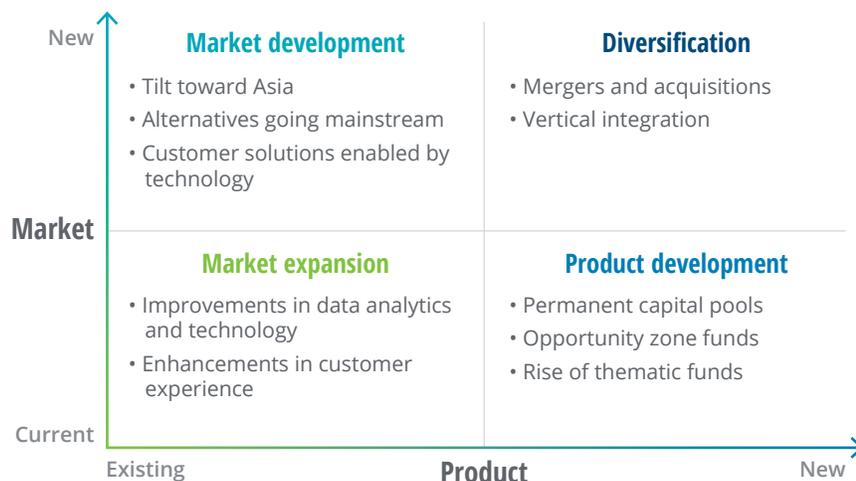
LAST YEAR, OUR 2019 outlook highlighted that some firms were likely to push their boundaries with bold actions such as being aggressive in acquiring new capabilities and embracing emerging technologies in search of growth. In many ways they did. Investment management firms continue to use M&A activity to bolt on new capabilities, while developing emerging technologies such as artificial intelligence (AI) and alternative data continue to be at the forefront of strategic plans.⁴ In 2020 the aggressiveness is expected to progress, and significant boundaries could be crossed, such as: PE firms fueling growth through permanent capital pools and investment management firms opening new market segments through technology.

Let’s analyze growth through the lens of a two-by-two growth matrix. The four categories are based on the degree to which new markets or products are developed. Using this framework, the four quadrants are: market development, diversification, market expansion, and product development (figure 2). Investment management firms find different paths to success, and many will follow one or more that lead to growth in new areas or through enhanced capabilities. Each quadrant of the matrix presents different challenges to overcome. This section digs deeper to better understand the paths investment managers are expected to take to find growth in 2020.

FIGURE 2

Making the right growth choices: Investment managers make their growth choices for both the short- and long-term horizons

Market and product development growth alternatives



Source: Deloitte Center for Financial Services analysis.

Diversification: Offering new products in new markets

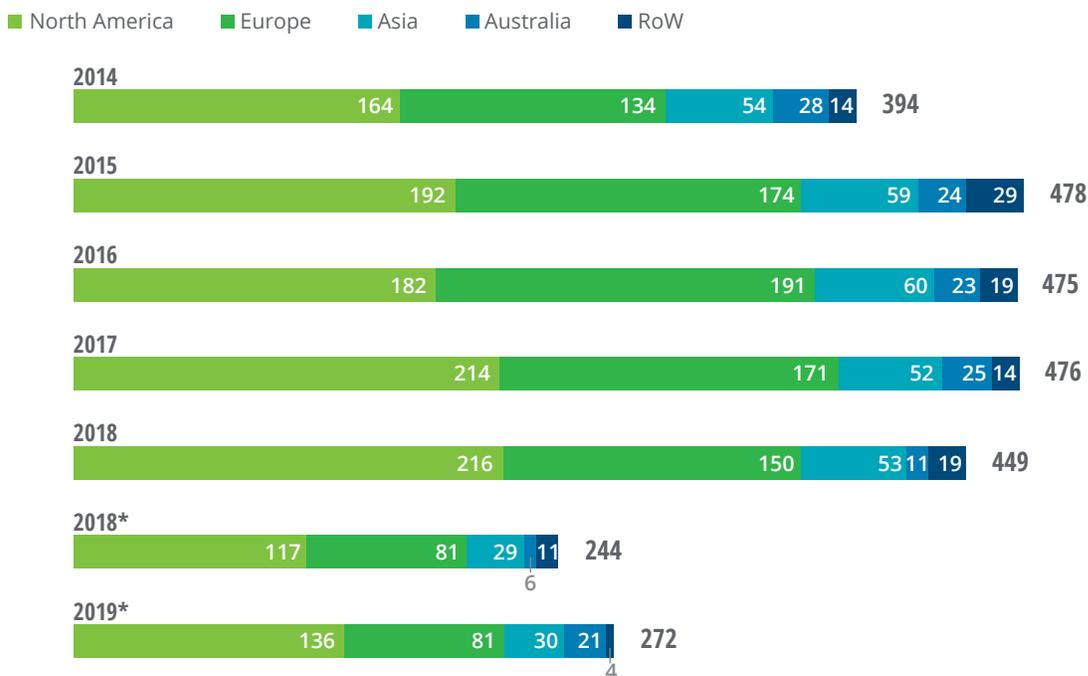
Investment managers continue to rely on mergers and acquisitions (M&A) to diversify product offerings and geographic presence. Over the last five years, achieving scale and adding new capabilities were the key objectives for most investment manager M&A. In fact, M&A transactions between investment managers touched a high in 2018.⁵ Deal activity continues to remain strong from a bolt-on capabilities perspective, while merger-of-equals transactions are slower to transpire. Even when M&A are the right strategic choice for both firms, desired results are often not achieved due to suboptimal postmerger integration.⁶ From a geographic diversification perspective, most European firms

have been looking to expand into Asia, while many US-based investment managers have focused on increasing their presence in both Europe and Asia. Firms in North America and Europe account for 80 percent of M&A activity within the investment management industry and are driving continued high levels of activity (figure 3). This trend highlights the importance of inorganic growth in these mature markets to boost scale and broaden product lines into new asset classes.⁷ Brookfield Asset Management’s recent acquisition of a majority stake in Oaktree Capital Management to create an alternative giant is a good example. The combined business is expected to have US\$475 billion in AUM, offering a diversified suite of private investments including debt, equity, infrastructure, and real estate funds.⁸

FIGURE 3

The need for scale is clearly visible in North America, which accounts for half of the entire or majority stake acquisition deals for investment managers in 2019

Investment management industry M&A activity by geography, number of M&A deals



* Indicates deals through July of each year.

Note: RoW (rest of world) includes South America and Africa.

Source: Deloitte Center for Financial Services analysis of M&A data sourced from S&P Global Market Intelligence.

M&A activity in the industry permeates the entire investment management ecosystem. Firms are striving to integrate vertically and to offer clients solutions across the investment value chain, from financial data to advisory services and alternative investments. These “value chain” mergers may unlock growth for investment managers through the development of a vertically integrated portfolio of services. Principal Financial obtained institutional trust and custody service offerings for the nonretirement market through its acquisition of Wells Fargo’s Institutional Retirement and Trust business. Principal Financial also used the transaction to attain scale by doubling the size of its US retirement business and to bring on key industry talent.⁹ Value chain M&A will likely increase over the coming year as firms expand client service offerings and geographical footprint.

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WINNING THROUGH DIVERSIFICATION

M&A can be a strong path to immediately achieving scale and serving new clients, but they are not a panacea.¹⁰ Often when investment management M&A fail to achieve the expected value, it can be attributed to integration issues.¹¹ When front, middle, and back offices are spread across geographies, managing integration across culture, talent, and technology is difficult. Some firms will likely implement an integration management office (IMO) to develop a clear integration plan and control the information flow between workstreams and senior management.¹² Thoughtful planning for M&A integration that begins in the transaction phase will emerge as a leading practice in 2020. Selecting the right strategic partners to fulfill growth requirements

and executing with excellence on the postmerger integration plan will likely differentiate the exceptional firms taking this approach.

Market development: Bringing existing products and services to new investors

Finding new markets and investors for existing products is an important component of profitable growth for investment management firms. Investment managers can find new market opportunities by exploring new geographies, scanning (or driving) regulatory changes, and by deploying new technologies.

Asia is one such target for investment managers.

Major demographic shifts are taking place in the region, which accounts for 62 percent of the world’s millennials as well as 63 percent of the world’s aging workforce (aged between 50 and 60 years as of 2019).¹³ Investment managers, including PE firms, are aiming to provide investment solutions for these two varied

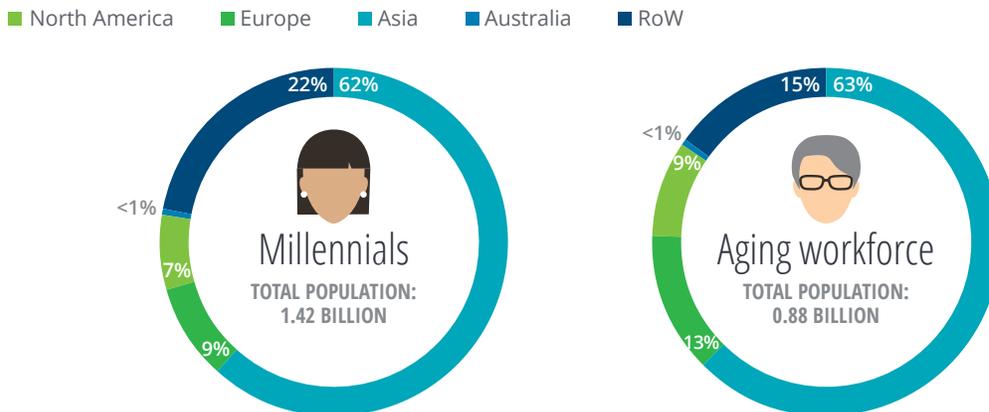
investor segments. The estimated opportunity for public funds in China will surpass US\$2.6 trillion AUM in 2020.¹⁴ The regulatory climate for investment management firms to enter China improved several times over 2019.¹⁵ However, the region’s diversity tends to pose unique challenges for foreign investment management firms, including cultural, economic, geopolitical, and regulatory risk. This emerging customer segment in Asia paints a picture of the challenges that come with enormous growth potential.

On the regulatory front, supporting capital formation, innovation, and levelling the playing field between large and small investment advisers is a focus. In addition, allowing retail investors to gain access to alternative investments is a market

FIGURE 4

Asian millennials and aging workforce present a market development opportunity for investment managers

Global population by geographic region, 2019



Note: RoW includes South America and Africa. Aging workforce population: between 50 to 60 years old. Percentages may not total 100 percent due to rounding.

Sources: Deloitte Center for Financial Services analysis of population data from United Nations, Department of Economic and Social Affairs, Population Division (2019). World Population Prospects 2019, Online Edition. Rev. 1, made available under the Creative Commons license <https://creativecommons.org/licenses/by/3.0/igo/> (accessed on October 1, 2019).

development opportunity. In December 2018, investment management firms and industry representatives met with the US Securities and Exchange Commission (SEC) to explore this option, and a few months later,¹⁶ the SEC requested public comment on the proposal.¹⁷ These changes involve creation or revisions to definitions of accredited investors, financial thresholds for investing in private funds, and restrictions on business development companies. For example, Vanguard has expanded access to retail investors in its Alternative Strategies Fund by lowering the minimum investment amount from US\$250,000 to US\$50,000.¹⁸ Ultimately, this move may drive change in asset allocation on a huge scale and could have implications on the liquidity, risk, and return objectives for millions of retail investors. However, before alternative assets are readily available in 401(k) accounts or have greater penetration into retail investor segments, regulators will likely ask for controls to mitigate risk and for reliable liquidity solutions through secondary markets or other liquidity methods.

Technology can be used to develop solutions that address the liquidity and control concerns of embedding alternative investments in portfolios across varied client segments. A US-based invest-tech firm has built a technology platform that provides high-net-worth clients with access to alternative investments.¹⁹ The modular platform supports the subscription, administration, and reporting processes for private equity, private credit, hedge funds, and other alternative investments.²⁰ Platforms, coupled with investment advice and risk controls, may be important ingredients in a coming change that opens access to alternative investments.

WINNING THROUGH MARKET DEVELOPMENT

Creative marketing approaches to build appeal of existing products for new investor segments, either geographically, demographically, or both, typically depend on first developing a deep understanding of the needs and motivations of the new target markets. Only then can existing products and services be positioned ideally within the segments.

The cultural differences between many of these emerging investor segments are stark compared to the traditional customers. Leading firms will likely resonate culturally, deliver through current or newly developed technology, and meet the changing investment expectations, such as ESG principles, of these new segments. What is needed to win here goes well beyond new packaging and a catchy marketing slogan. Also, the long view may be a required approach, as some firms are already targeting investor segments—well before they have profitable levels of investable assets—with the knowledge that wealth flows both geographically and generationally over time.

Product development: Creating new products for existing markets

Many investment managers are crossing traditional industry boundaries to develop new products and reimagine others. Change is being seen across different product categories, from mutual funds and ETFs to alternatives. In the mutual fund and ETF category, products focusing on sustainability, market volatility, and megatrends are being launched. These new funds are a significant departure from funds defined by investment market capitalization, growth or value orientation, and geographic region. The new approach seems to resonate with most investor goals and emotions. In Europe, 168 new sustainable funds were launched in the first half of 2019, on track to exceed 305 sustainable offerings introduced last year.²¹ Rising investor demand drove net flows into sustainable funds, pushing assets in Europe to a record 595 billion euros (more than US\$656 billion).²² Regulatory developments in the European Union (EU) such as the creation of a standard ESG taxonomy and ESG-specific benchmarks may drive the growth of sustainable funds further. Fund houses are also launching thematic funds to provide investors with exposure to short- and long-term themes. In light of the recent market

turbulence and the length of the bull market, some firms are launching ETFs that provide investors downside protection, although the funds limit the potential upside.²³ Additionally, new megatrend funds focused on global challenges including urbanization, health care, and technology disruption have also recently been launched.²⁴ These thematic approaches may draw a stronger connection with investors in 2020 than some previous classification systems, such as large cap value, which are devoid of emotional connection.

Shifting to alternatives, many PE firms are looking at increasing their permanent capital assets, creating products similar to closed-end mutual funds.²⁵ The recent resurgence in business development companies (BDCs) embodies this shift to permanent capital structures and debt markets. Due to proposed regulatory changes in fee reporting, the popularity of BDCs is likely to continue to grow.²⁶ Additionally, a new investment category, opportunity zone funds, targets more than US\$2 trillion in assets through tax relief on unrealized gains.²⁷ These funds may enable investors to write off capital gains taxes, provided the holding period of an investment in a designated opportunity zone exceeds 10 years.²⁸ Some investment managers and PE firms have already begun investing or raising funds to invest in these opportunity zone funds.²⁹ The search for growth by PE firms is finding value in new structures and is unrestrained by asset class.

WINNING THROUGH PRODUCT DEVELOPMENT

The needs of existing customers can change as their financial circumstances and opportunities in the market change. Offering new products to these existing, but evolving, customers is typically an important growth strategy. Leading firms that take this approach will likely have exceptional insights into their customers' evolving needs and personal circumstances. They may also have the ability to develop new products that are tailored to realize the benefits from both regulatory-driven change

and from market opportunities. Firms that excel will likely embrace cannibalization of existing products to optimize the growth potential of new launches, rather than cede the new developments to faster-moving competition. This approach will likely reward not just a ramped-up product management operation, but a change-oriented one.

Offering new products to existing, but evolving, customers is typically an important growth strategy.

Market expansion: Finding new growth with existing products and markets

Many existing active portfolios have fallen short in their effort to provide alpha. On average, active portfolio performance has trailed passive counterparts for the past nine years, and the gap appears to be widening.³⁰ For these products, and active management as a whole, to turn the tide, they need credible revitalization of their investment processes. While there are many paths to revitalization, let's look at one popular approach many firms are considering: the combination of AI algorithms and access to alternative data sets.

AI and alternative data have been used by many investment managers to augment investment decision processes. Even PE firms, which typically have long-term strategies, have started adopting alternative data for sourcing deals and conducting due diligence, following hedge fund and long-only managers. Adopting and using insights from alternative data sets for managing and transforming portfolio companies can be a game changer for many PE firms. Alternative data vendors have already come out with PE-focused solutions.³¹ Using alternative data strategies calls for a matching technology infrastructure, coupled

with strong data governance and quality programs, to manage the large data sets. Typically, firms deploying alternative data use cloud solutions that can provide both processing power on demand and large data storage capacity. Talent and culture are also important elements of alternative data success, as investment management firms bridge the gap between data science expertise and investment savvy to realize results.

WINNING THROUGH MARKET EXPANSION

As a whole, active managers, other than those in PE, have been on the losing side of the market expansion strategy for the past decade. Index performance coupled with low fees have surpassed the promise of alpha with a premium brand in the eyes of many investors. In order to win the market expansion battle, active managers should credibly make the case that their expertise is worth the cost. Any active manager looking to win in their existing markets with their existing products has this mandate, and will be asked to demonstrate it. That's much easier said than done, but firms with visionary leaders have the opportunity to regain the upper hand in this strategic territory. These firms may also refresh their offerings by providing compelling investment strategies with the desired portfolio wrappers (e.g., mutual funds, separate accounts, collective investment trusts, ETFs, models). Many long-only managers could offer active equity management in an ETF wrapper in 2020.

Finding growth in 2020

These four quadrants of strategic choices for growth are not mutually exclusive. Many firms will pursue approaches in multiple areas, with the objective of combining asset growth and profit expansion. Successful investment managers will evaluate opportunities across product categories and markets to deliver the optimized product, return, and service expectations for investors.

Creating operational efficiencies

SHRINKING MARGINS CONTINUE to bring daunting challenges to many firms, forcing new actions such as outsourcing front-office functions and increasing technology expenditures to stay competitive. As firms transform their operations, risk management grows in importance. The further the departure from the old way of doing things, often the greater the need for new policies, procedures, and controls to manage both external risks (such as cybersecurity) and internal risks (such as having the right talent). In 2020, most firms are expected to cross the boundary from traditional cost efficiency projects into a save-to-transform approach, increasing competitive advantage in the process, and never losing sight of customer expectations.

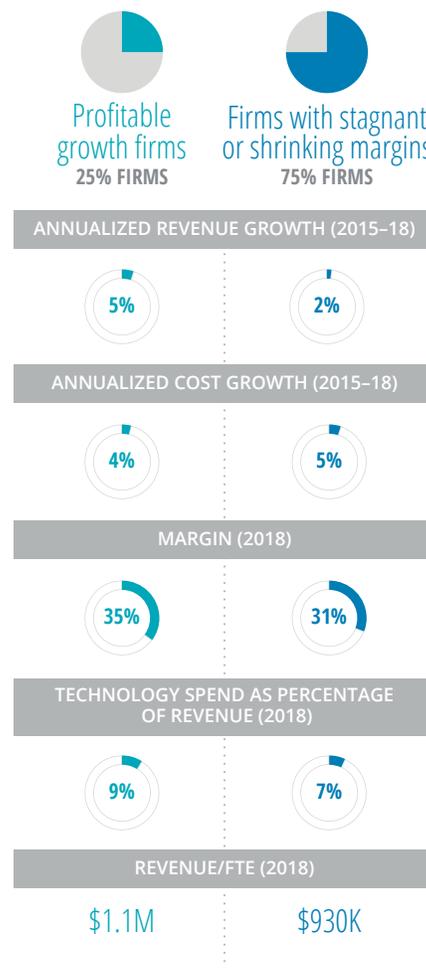
Operational transformation: Path to greater efficiency

Successful operational transformation may appear elusive, but even so it should be attempted to achieve profitable growth.³² Firms that achieve their goals most often transform people, processes, and technology in coordination.³³ Casey Quirk, a Deloitte business, conducted a study of more than 95 investment managers headquartered in North America, Europe, and Asia Pacific, that shows that just 25 percent of investment management firms surveyed are able to grow profits and margins simultaneously.³⁴ These successful firms employ an elevated level of technology spend as a percentage of revenue compared to counterparts with shrinking margins (figure 5). The best positioned firms also have higher revenue per full time

equivalent (FTE) than the others. These results imply that some firms are more adept at rightsizing

FIGURE 5

Successful investment managers achieve operational efficiency through greater technology expenditures



Source: "Investing for Growth, Performance Intelligence 2018," Casey Quirk, a Deloitte business, and McLagan.

their operations using technology and outsourcing noncore functions than their competitors.

Successful firms in 2020 and beyond will likely design their investment analysis and decision-making process, the core investment operating engine, to incorporate the most recent data. These dynamic data-driven insights can provide portfolio managers and analysts with investment decision support. Finally, delivering customized portfolio information to investors at scale rounds out the common tenets of the successful firms. As firms execute on these strategies, both investment management firms and their service providers alike recognize that many of the traditional boundaries between front, middle, and back office are being crossed. The recent uptick in the adoption of a “golden copy” comprehensive, real-time investment book of record (IBOR) illustrates the point. The golden copy provides a real-time security position and cash view to front-, middle-, and back-office personnel alike. This comprehensive approach mitigates compliance risks arising from different views of portfolio positions and enables the firm to have a unified

view while executing transactions in real time. The breakdown of these boundaries may lead investment management firms to become less compartmentalized and more nimble.

“Modern and robust risk management capabilities are growing in importance for investment management firms because of the roles they can play enabling strategic growth.”

— *Krissy Davis, partner, Risk & Financial Advisory, Deloitte & Touche LLP*

With the growing adoption of digital technologies, many firms are shifting to a “save-to-transform” mindset that marries cost-cutting with strategic enablement.³⁵ The save-to-transform approach includes technology as a key priority in addition to cost, growth, and talent. For example, firms following this approach with regard to distribution tend to invest in technologies that help reduce distribution costs while providing innovative delivery models that meet the growing demand for personalized investment experiences.³⁶ Similarly, firms are focusing on implementing cognitive technologies such as AI and machine learning and robotic process automation to facilitate digital enablement, a key element of save-to-transform.³⁷ The adoption of the save-to-transform mindset by investment management firms is expected to increase dramatically in 2020 because of the benefits beyond traditional cost reduction strategies.



Managing risks: Winning by not losing and crossing boundaries confidently

Investment managers appear up to the challenge of augmenting their risk management practices to support operational transformation. Deloitte’s global cost survey of executives directly involved in

cost management decision-making shows that the number of investment management firms taking steps to control risk trails the number transforming their operations by only a few percentage points. The percentage of firms surveyed that are implementing operational transformations range from 37 to 51 percent by project type, and between 34 and 40 percent for risk management–related actions (figure 6).

Leading operational transformation practices could combine growth enablement and operational efficiency. In today’s environment, with many firms working overtime to achieve operational efficiencies, how well risks are managed and mitigated can mean the difference between success and failure.

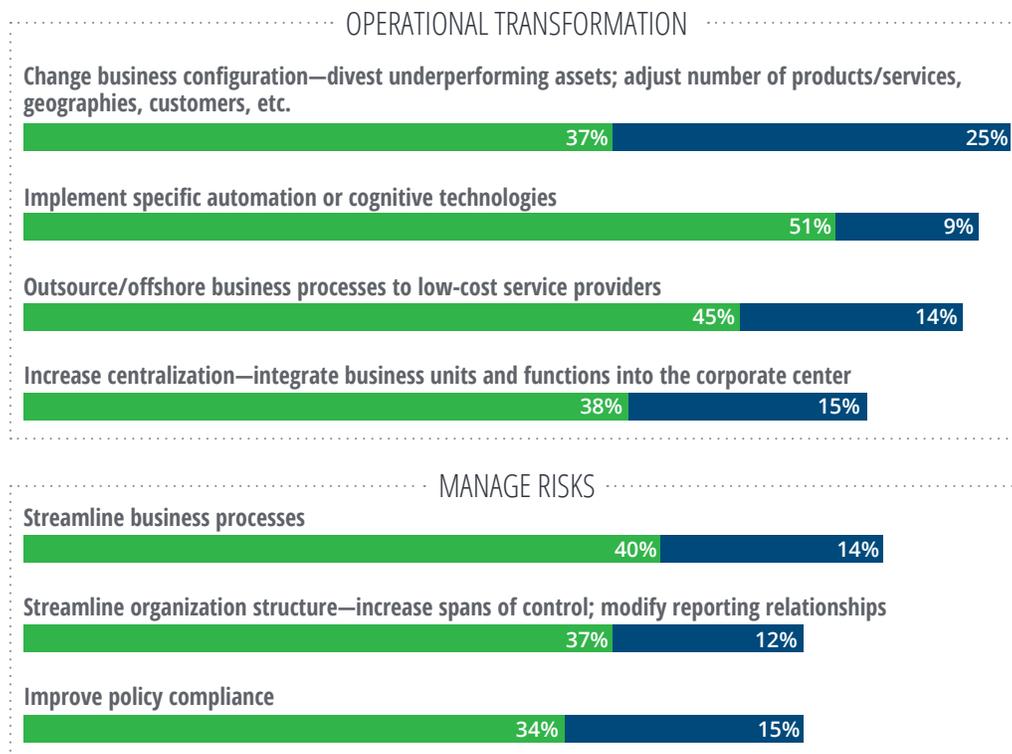
Investment management firms are in a tight squeeze. A single operational mistake can jeopardize a firm’s profit and reputation, while at the same time failure to implement true change may generate strategic risk. This situation calls for firms to assess and modernize the three lines of defense (LOD) as operations are transformed. Using Deloitte’s strategic choices framework (figure 7), firms can enhance the three LOD on a prioritized basis to match their overall growth strategy and their current level of capability to manage risk.

Many firms today focus on the defensive half of the risk strategy framework. The defensive half of the risk management spectrum, operator and steward, enables winning by not losing. In their role as

FIGURE 6

Investment management firms are combining operational transformation and risk management to improve competitive advantage

■ In process of implementation ■ Not implemented but planned



Source: Deloitte's 2019 Global Cost Survey.

FIGURE 7

Strategic choices framework



Source: Deloitte Risk & Financial Advisory, 2019.

stewards, chief risk officers can protect the risk functions that cover the existing business model on a day-to-day basis. Defense also covers the reaction to external change. Some of these changes are driven by industry events, such as competitor pricing changes or mergers, and others are less rational, such as terrorism and natural disasters. Risk management can create plans and contingencies for all of these risks, which help firms react effectively and mitigate losses.

In 2020, successful firms are expected to execute on the additive or offensive risk management playbook, represented by the top half. The catalyst and strategist roles of risk management enable firms to more confidently plan for the future and execute operating model changes. These roles

enable proactive change. For example, the catalyst activities in risk management may identify that both retail and institutional investors are using a higher percentage of low-cost index investments in their portfolios. The strategist function in risk management has a seat at the table in formulating the response for the firm.

Modernization of risk management is expected to go hand in hand with operational transformation for firms crossing boundaries to find profitable growth throughout 2020. Robust and modern risk management practices can act as strategic enablers for entering new markets, launching new products, and revamping enterprise critical processes. The results of Deloitte’s global risk management survey indicate that risk management modernization may

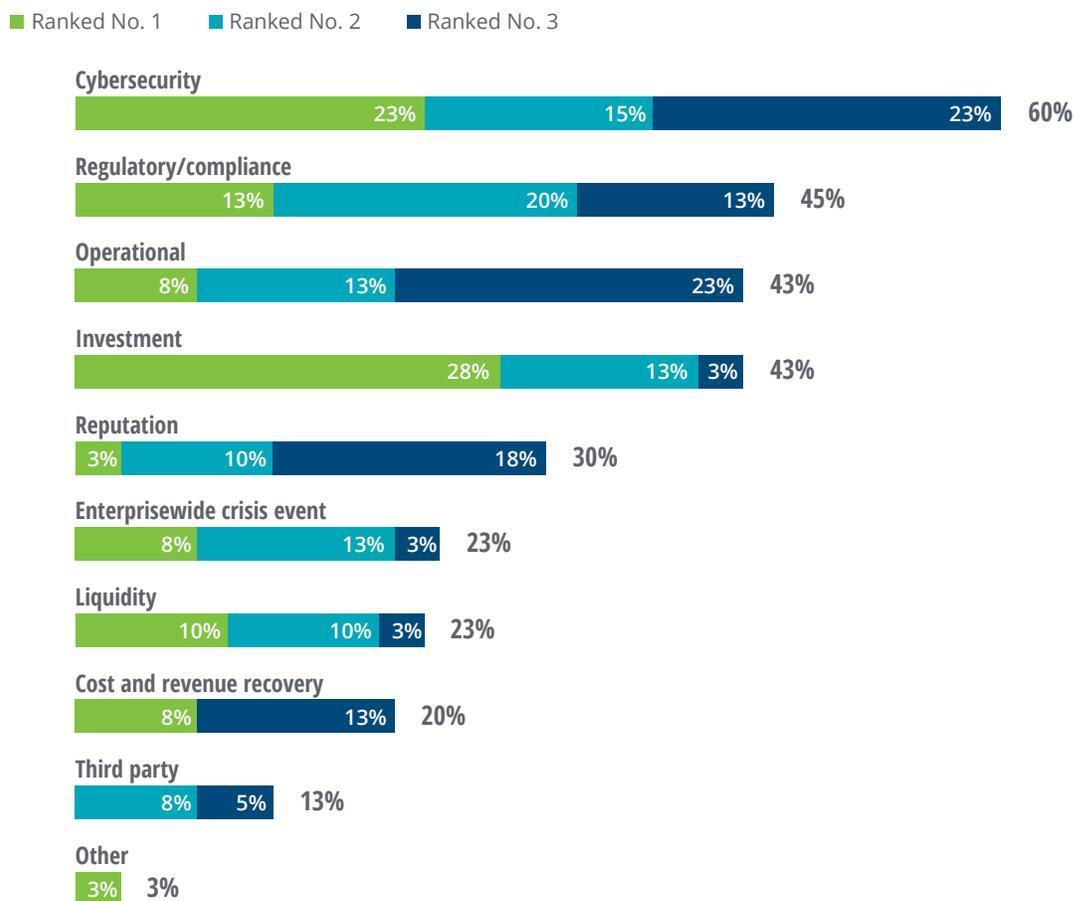
be needed at many investment management firms (figure 8). The majority of investment management firms (60 percent) participating in the survey indicated that cybersecurity was among the top three challenges from a risk management perspective, likely as a result of heightened regulatory attention. Cybersecurity has been among the SEC's top enforcement priorities for the last four years.³⁸ European financial regulators are also focusing on cybersecurity and published joint advice in 2019 recommending legislative improvements to specify cybersecurity requirements for financial

firms.³⁹ In the long term, the regulators have proposed to establish a voluntary EU-wide cyber resilience testing framework.⁴⁰ Increased regulatory scrutiny of the industry to protect investors' interests has led to regulatory and compliance issues being ranked as the second biggest challenge (45 percent). The European Securities and Markets Authority's recommendation for quarterly liquidity stress tests (LSTs) is one such example. European alternative funds and undertakings for the collective investment in transferable securities are expected to periodically run LSTs starting on September 30,

FIGURE 8

Top risks from investment managers' perspective

Over the next two years, which are the three risk types that you believe will present the greatest challenges in your organization's investment management business?



Note: Some percentages do not total due to rounding.
 Source: Global Risk Management Survey, 11th edition, Deloitte, 2019.

2020.⁴¹ Another regulatory priority, operational risk, is a significant challenge for 43 percent of firms surveyed. There is a widespread opinion that the use of alternative data in investment and operational processes is attracting regulatory attention.⁴² Firms with a modern risk management framework are likely to adapt their processes and controls to manage the new risks that using alternative data carries. This example highlights how risk management can be a strategic enabler, and a partner for growth, when the risk management approach is modern and robust.

The firms that are expected to be most efficient in 2030 are planting the seeds today that will help them to be successful. These firms will likely have

modular operations linked through a common framework of processing power and data. As new markets, products, and processes are developed, automated operational transformation technology can connect the various people, process, and technology layers to model the operation. At the same time, they can implement algorithms to monitor risks and record operational results. In this future world, risk management should be baked into operations with the same level of depth as human resources or finance. Further, risk management should be used to drive new developments to the same extent it is used to protect existing operations. Firms will likely realize that failure to change is as risky and detrimental as making ill-considered changes.

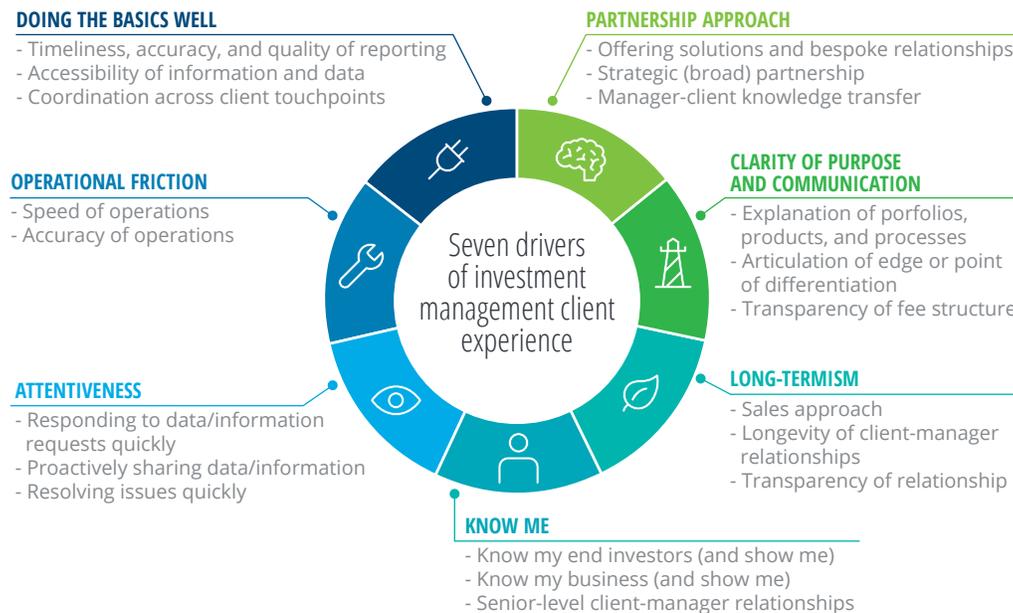
Customer experience and engagement

CONSUMERS ACROSS THE globe are more mobile, read more product reviews, and buy more online than ever before. Tech-savvy firms provide seamless digital user experience and anticipate their needs to offer exactly what they want. Consumers also expect similar seamless and personalized experiences from investment managers.⁴³ As a result, customer experience (CX) has become an important factor in the evaluation of investment managers by their customers. According to a survey of retail and institutional investors conducted by Casey Quirk, a Deloitte business, 76 percent of participants stated CX was

a contributing factor to manager terminations.⁴⁴ In a world where performance is not the only contributor to differentiation, creating a delightful CX at every touchpoint can help firms retain customer assets—and it is within every organization’s capability. In order to do so, however, CX needs to be a strategic priority for firms to cross the boundary from siloed approaches to a truly holistic customer-centric enterprisewide solution. As investment managers work to improve CX, they can focus on seven common drivers of investment management CX (figure 9). These drivers are based on the perspectives gained

FIGURE 9

Client experience incorporates attitude and capability



Source: *Engaging the whole firm: Improving client experience in institutional and wholesale investment management*, Deloitte LLP, 2019.

through more than a dozen in-depth interviews with clients of investment management firms in the United Kingdom (including wealth managers, insurers, and pension funds).⁴⁵

Let's take a closer look at two important elements of the customer life cycle, client onboarding and reporting, and highlight the drivers impacting the onboarding and reporting experience in the coming year.

Client onboarding: From drag to delight

The client onboarding process at many investment management firms is cumbersome and can rob firms of the opportunity to create a positive first impression. Typically, the onboarding process is inefficient, time-consuming, and requires filling out forms manually as a result of operational friction from legacy systems.⁴⁶

Additionally, the manner in which client data is collected and stored within the organization can further deteriorate the onboarding experience. Potential clients may be requested to provide the same information multiple times due to lack of coordination across client touchpoints, and some clients may abandon the process. Centralized data storage can prevent clients from becoming frustrated and improve application conversion rates.

Today's customers expect a faster and smoother onboarding experience delivered through digital channels. In 2020, many leading investment managers will likely leverage advanced technologies to respond to rising customer expectations and to reduce the potential for operational friction (figure 9). These expectations are being shaped by other financial services sectors that have deployed digital platforms for a more

seamless onboarding experience.⁴⁷ In many applications, these platforms have reduced the onboarding time from weeks to days and often support image- or video-based biometric

Centralized data storage can prevent clients from becoming frustrated and improve application conversion rates.

authentication and e-signatures.⁴⁸

Delighting clients by streamlining the onboarding process may not only drive competitive advantage, but can also lay the foundation of a long-term relationship. Danish online trading firm Saxo Bank and Allianz Global Investors are each making headway to improve the onboarding process. Saxo Bank built a digital client onboarding tool that utilizes robotic process automation (RPA) to enable clients to fund their account within one hour of application. RPA enhances the integration of data from multiple sources to speed up the client identification process. By reducing operational friction, the innovative process led to a record 18,000 clients onboarded in April, twelve times the typical monthly average.⁴⁹ Allianz Global Investors has also taken steps to enhance the client experience from the very beginning of the relationship by employing a "know me" approach (figure 9). The firm eliminated the distinction between its direct sales and client service teams and formed one relationship management group. This model enables deeper relationships because it can provide the client continuity with a single point of contact from the start.⁵⁰

On the institutional front, where client relationships can be more complex, client onboarding is typically just as important. Client portfolio customization requirements recorded through the proposal stage may need to be operationalized. Seamlessness is important to meet client expectations. Internally, a

fully streamlined onboarding process can also help accurately price services. Particular customer requirements may be predictably expensive to follow. In these cases, integrated onboarding processes can enhance the customer experience while at the same time protect the operating margin by modeling client profitability beginning in the proposal stage. Improvements in client experience can be achieved through development of technology, processes, and people, depending on the existing strengths of the firm.

Prioritizing these drivers can have a material positive impact on the overall onboarding experience. The technologies deployed to improve these processes are mature, and the technology-leader cost penalties are correspondingly diminishing.

Meeting evolving client reporting and communication expectations

Once onboarding is complete, ongoing communication is a central component of the customer relationship. Client reporting, in its multiple forms and channels, plays a very important role in building the manager-client relationship, and expectations continue to evolve. Clients often demand more complex and frequent information about their investments and markets. They want personalized information delivered through digital channels with the tools to perform customized data analyses at their fingertips. The traditional approach of standard portfolio reporting using emails of static documents or hard copies may have an adverse impact on the overall CX.

The disconnect between client expectations for custom reporting and what is actually delivered presents investment managers with an opportunity to set themselves apart. According to a survey of 100 Europe- and North America-based buy-side

firms, only 12 percent use customization more than half of the time for client reports.⁵¹ One way to offer a user-oriented CX is to provide clients with digital tools to generate custom reports about portfolio performance and capital markets.

More innovation in digitized client reports may be just around the corner. After three years in development, Schroders is close to achieving its vision of the next-generation reporting: a mobile-enabled, interactive, customizable digital factsheet.⁵² Other firms are also taking this path, and client communication is expected to be customizable at scale—becoming important components of CX differentiation.

More innovation in digitalized client reports may be just around the corner.

Firms making the transition from static hard copy and PDF reporting to digital interactive reporting face challenges more pressing than the previous reporting developments. The first challenge is with end-to-end security and a second challenge is data integrity. The data being accessed is highly sensitive to both the client and the investment management firm. The firm's intellectual property is on display in the context of the client's financial holdings. Additionally, the reputational risk of a breach of this information may prove devastating. As a result, firms are prioritizing end-to-end security.

Responding promptly to clients' requests for data and information can go a long way in strengthening the manager-client relationship. Therefore, a single "golden source" of information may be a prerequisite for client-directed custom reports. For custom reporting, some data is calculated rather than stored. In these instances, the calculation methods are context-dependent; for

example, performance reporting may differ from regulatory reporting. The transformation to interactive digital reporting gives clients access to data at their fingertips, which increases the importance of data structure, labeling, and accuracy. Building in quality controls is an essential practice when the client is driving the process. Without these strong controls, the firm may expose itself to reputational risk.

By 2030, two important aspects of CX are expected to definitely change. The technology available to serve customers should advance dramatically, since the rate of technological advancement is

accelerating. The customers being served represent the second change. In 2030, millennials will likely be well on their way to becoming the age segment with the largest investable wealth, and they will be working in decision-making roles in client firms. Millennials are expected to soon be setting the expectations for both retail and institutional client service. With these changes on their way, the standard for excellence in customer experience today could be outdated in 2030. Firms that fail to make progress on all seven drivers of customer experience could lose ground to both competitors and customer expectations.

2020: Thriving in new territory

LAST YEAR, MOUNTING pressures on profitability caused investment management firms to push boundaries in search of innovative growth solutions. In 2020, the battle for profitable growth is more likely to intensify than dissipate. Investment management firms that develop and execute upon strategies that not only push the boundaries but cross them will likely lead the pack. Even strategies to grow in current markets with current products require

revitalization. Firms that have command of data and processing and keep client relationships at the forefront as they seek to expand their business, run operations with a “save-to-transform” mindset, and delight customers may attract a greater share of asset inflows. Even though risks abound in current market conditions, opportunities for growth exist for those who embrace a holistic approach.

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