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ISS: Smarter through processing: the world of STP according to SmartStream

Darryl Twiggs, executive vice president for global product management, tells ISS about a shift towards a more horizontal approach for processing rather than the traditional silo mentality that has dominated in the past.

ISS: SmartStream is focused on STP for the fund industry, but the industry is very diverse. Some players have a high degree of automation, others have relatively little STP. How would you characterize the state of play in Europe now?

Darryl: In our experience, the larger the organisation, the greater degree of STP process, or certainly intent to have an STP process. We’re seeing the large organisations completing the automation across all instrument types through their post-trade processes. They are also looking to participate in new initiatives that require them to be automated. These initiatives could include, for example, Target 2 Securities, but they also have to put in place interfacing to things like the confirmation side, to external matching agencies and Omgeo CTM. So I think on the Tier One/Tier Two scale, we’re seeing a consolidation of automation and integration with externalized services as part of an STP step. We’re also seeing, as part of that model, consolidation within the organisation in a move to what we describe as an internal utility model.

Traditionally, within an organisation, each line of business repeats each of the process steps necessary through the lifecycle of the trade. What we’re seeing now is that the banks are realizing they can re-use economies of scale on their solutions to provide an internal service. For example, in the reconciliations space, they are setting-up a reconciliations team, which is reconciling all instrument types and then providing the results or the exceptions back to the lines of business to resolve. The organizations tend to be moving from a siloed to a horizontal structure in an effort to promote STP, looking to engage the lines of business more. That’s definitely happening.

In the smaller organizations, what we are seeing is that the banks, or those organizations looking to find sources of STP, are looking at manually intensive operations. The term that’s often used to describe this is that they ‘out-service’ those operations. They’re looking to supplement their processes through external parties that can provide the automated processing. Once complete, the small organization only has to deal with the results of that process.

ISS: Do you feel that the intensity and scale of the regulatory reform has made firms less focused on the advantages of pursuing an STP-orientated strategy or the converse, where regulatory changes have encouraged players to look at their systems from top to bottom?

Darryl: I’ve seen both from our customer base and from talking to other financial institutions. There has been a partial step towards further STP automation however, I’ve also seen the converse, where a tactical activity has taken place and an organisation has simply recruited more people to do more manual activity, particularly in the reporting process. It’s a mixed bag. I think that arises because ultimately there is a resistance to any type of investment, in terms of cost, but also because there is a degree of uncertainty regarding what the regulator requires of the institution. This in particular is a challenge for the multi-national institutions, where they see local regulators applying different degrees of reporting. The lack of clarity and the right level of detail can be a barrier for

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ISS: Various reporting requirements deal with different parts of an institution and often different datasets. In terms of integrating these requirements, is that a big
There is a huge challenge in normalizing the data, sourcing the data, getting the data to be of the right quality.

ISS: Are there any important technological trends, either in the wider world or at in-house level, that are impacting your own business and the business of clients?

Darryl: Over the last two years we've seen increased interest from our customers in the use of software as a service and to make use of the internet to connect to hosted environments -- the use of cloud computing to gain power, being agnostic as to where that actual data is being processed. That brings in some new structures within the organization whereby, if you're outsourcing effectively the processing of certain data, you want to make sure that the data is being correctly processed. Consequently a new control team must be put in place to monitor the results of that externalised processing and to facilitate regular reporting. Once accomplished the bank then has the opportunity to introduce KPIs, SLA agreements and so forth. It changes the dynamic of that process. That can only be realized because we have now enhanced the technology platform to offer those services which are only available through the use of cloud computing.

ISS: Do you expect the pace of change we've seen to speed up, slow down, or maybe remain the same for the next couple of years? It's been an extremely busy period for the industry in terms of making adjustments in the post-crisis world.

Darryl: I think what we'll see are some of the tactical decisions that have been made and put in place for monitoring and reporting will now have to be absorbed into strategic tools and processes. I would expect the vendors supporting the post-trade operations space to provide a great deal of support for new regulations reporting by adopting more tools that can be used for stress-testing and analysis. I don't believe any of this will actually slow down the pace of change but will instead enable all the change to be more readily consumed.

ISS: You spoke about cost being a key concern. If you were to pick one issue, either elaborating on that or a different issue you think the back and middle office really needs to grapple with, what would you say it is and why?

Darryl: When I look at the cost and fees associated with post-trade process, we've seen execution trade revenues reduced substantially. Over the last 18 months we've seen settlement revenues drop 70% and that has exposed the true cost of post-trade processing. I think there is, and will continue to be, a huge focus on the reduction of post-trade costs if for no other reason than to simply balance the books. That's where there must be a larger focus and that is one of the primary concerns that our client base has, above and beyond the introduction of new regulations.

ISS: How would that then play out?

Darryl: It goes back to what I said right at the very beginning. We need a new operations paradigm. Financial institutions have to move away from vertical lines of business with post-trade processing supporting them and instead have to look at more horizontal structures in order to rationalise the number of systems they are currently supporting. Vendors have historically been very successful in selling their solutions for particular instrument types. What the banks are really looking for are solutions that are abstracted or support all instrument types, so they can deploy a single solution across the entire back office space thus reducing the number of systems they have to support. The concept of using a utility internally and the greater use of externalised utilities will drive successful cost-cutting operations.