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DELIVERING POST-TRADE ALPHA

POST-TRADE FORUM DISCUSSION PAPER

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The recovery from the initial phases of the pandemic dominated management agendas in 2021, as the industry adjusted to what has been widely described as the ‘new-normal’. The adoption of remote and hybrid working practices created momentum around digitalisation agendas, which whilst focussing on new ways of working (rather than transforming underlying processes) made organisations more open to embracing innovation. And the experience also highlighted the value of resilience to the C-suite, increasingly recognising the value that managed services can bring in times of market stress.

Externally, the market landscape also evolved as regulators heightened scrutiny around areas such as transaction reporting, KYC, and control environments. Events such as the Archegos default also increased focus, with the UK regulators expressing frustration that lessons learned from the 2008 crisis had not been acted upon. Alongside this, there was also renewed focus on market infrastructure change, with the push towards T+1 in the US and the increasing rise in focus around digital assets and the transformation in post trade they could potentially unlock.

Looking ahead to 2022, these themes will continue to be high on the agenda of post trade leaders across the capital markets spectrum, as the need to transform legacy systems and processes remains. Regulatory focus around areas such as operational resilience and thematic reviews will continue, whilst ongoing revisions (‘re-fits’) to existing regimes by the CFTC and ESMA will drive a need for enhancements to existing systems and processes that have been in place for over a decade.

But though this agenda may seem quite similar to every other year, the reality is that the market dynamics now create an opportunity for innovation. One which if approached correctly, can enable a transformational shift in operating model design, delivering a leaner, more automated and modernised set of systems and processes across middle and back office. One which creates post-trade ‘alpha.’



HERE IS WHY, AND HOW

WHY?

The inertia that characterised large swathes of capital markets (slow cloud adoption, lack of collaboration, introspective views of transformation opportunities) has been cut through by the disruption the pandemic created. And this shift in mindset has enabled the industry to glimpse what can be possible, in terms of pace of change and the role that modern technology can play. Alongside this, the focus on operational resilience that regulators globally are mandating, is forcing organisations to think differently around how they measure and manage their critical business processes. This is challenging the C-suite across the industry to demonstrate understanding of key pinch points (many of which the pandemic shone a light on) and proactive management of any vulnerabilities.

What this creates is an emerging dynamic around post trade thinking, one which moves away from a 'hold and maintain' approach to processing and is forcing boards and risk committees to address vulnerabilities. Many of these are legacies of the past, where lack of return on investment or the availability of cheap, offshored labour pools made them easier to address by throwing people at the problem. But the pandemic (and increasingly regulators) has increased pressure on remediation, which creates an opportunity for post trade leaders to be heard.

HOW?

We see five key themes enabling the future of post trade, enabling capital markets organisations to take a transformational shift in processing capabilities and creating post-trade 'alpha.' These are:

Data Centricity

BCBS 239 laid out well intentioned principles, but the industry has not achieved the benefits that full adoption could have delivered. Furthermore, the challenges within most organisations around data continue to be a blocker to innovation – preventing adoption of external tools and services that can be transformational to post trade operating models.

The post trade environment across capital markets, where many of the process challenges are problems that cannot be ignored and must be fixed, does not offer a “blank canvas” or “greenfield site” from which to start transformation. But adopting data centricity – loosely, an architecture where data is permanent and the primary asset, whilst applications come and go over time – can be the catalyst for organisations to bring in greenfield thinking to their legacy architecture. Not only does this provide a platform for innovation but is increasingly going to become a critical part of senior managers agenda going forward, as they respond to regulatory demands.

Post trade leaders should be focussing on the data that creates the challenges that they face – rather than the systems and processes that compensate for it – to create a catalyst for transformational change.

Mandate Collaboration

The fundamental challenge for post trade processing is that there are always two-parties – at least – to every transaction and lifecycle event. Not matter how efficient one of these may be, this benefit is pretty much negated if the other party involved does not operate in the same way. The uniqueness of most capital markets players in the way that their systems, data, and processes are configured makes unilateral efforts worthless, given that the other party will also need to mirror these efforts. To do this bilaterally is impractical, given the spread of counterparties that each organisation will typically work with. The symptom of this issue is the rash of email exchange containing two (generally unstructured) versions of transactional or other data. This is a major driver of manual work, which makes the need for industry wide collaboration key to resolving some of the inherent inefficiencies in post trade processing.

But one by-product of the pandemic has been the rise of collaborative tooling and a realisation of the value adoption can bring. This maturing of the landscape and shift in mindset (internally and externally) makes these toolsets an integral part of a post trade leaders’ armoury. One which must form a central part of their future state domain.

Embrace Standardisation

The industry has no shortage of standards; SWIFT has been operating since the late 1970s and the FIX protocol that has been around since the 1990's. More recently, the CDM that has been designed through ISDA is starting to help de-clutter OTC derivative processing. All of which can be powerful innovation enablers when adopted by organisations.

But the challenge for adoption is less around the availability of data standards, it is much more around how organisations can apply them to drive standardised processing. Many organisations maintain expensive point to point connections between themselves and third-party service providers, where extensive manipulation or mapping of data is required to bring information into and out of their infrastructure. This is not only expensive to maintain, but also limits connectivity to solution providers.

Leveraging the data centricity outlined earlier, organisations must focus on enabling the opportunities these standards provide. Post trade leaders must challenge blockers to adoption internally, making the case for the value that this brings by adopting industry tool sets. Biting the bullet will ultimately unlock cost and inefficiency, through enabling access to innovative tools and services that are increasingly being adopted by others.

The Role of Technology

Most post trade leaders and owners have recognised the increasingly important role that technology will play in the future of their business models. The need for democratisation of technology – bringing process owners closer to technology decision making – is key to ensure that operating models are optimised. And with the Fintech industry offering commoditised solutions that solve common problems (such as the use of email as a workflow tool), it is critical that a 'tech-first' approach to middle and back-office processing is mandated.

Process owners however must be active in this discussion, understanding the role that technology can play in enabling their future state. The functional boundaries between IT and Ops will become increasingly blurred over time as the industry recognises that the post trade domain desperately needs the level of electronification that transformed the front office over the last decade. This must be led by process owners however, who cannot remain passive in discussions regarding future state architecture and must drive the value proposition for change.

Plan for Digitalised Assets

Whether this is merely thinking about how to connect to platforms that can bring post trade efficiency – such as the creation of digital representations of assets – or connectivity into managed services that can enable settlement of digitalised assets, the reality of taking a ‘wait and see’ approach is rapidly become unviable. The momentum around how DLT as a technology catalyst is disrupting the post trade landscape, the progress of both CDBC currencies and also tokenised securities, as well as the increasing emergence of crypto as an asset in its own right poses fundamental challenges to current state post systems and processes. In some sense, this shift will be so stark that it will ultimately force institutions to dual-track their infrastructure – as historic complexity makes consolidation of digitalised assets alongside traditional processing impossible. This will be the worst of both worlds, whereby the benefits of the new world become eroded through lack of synergy with the old.

The momentum around adoption provides a platform for transformation across the post trade landscape but is something that leaders should be considering now. And making the case for how the old and new are integrated into a future state operating model, rather than reacting to this trend when it is too late.

For organisations that can leverage the transformational opportunities that this industry dynamic creates, they will find themselves at a significant competitive advantage to those who don’t. They will find themselves making a leap-forward in capabilities, leveraging data centricity to access third party services that support innovative collaboration and enhanced customer outcomes. And not only will this deliver resilient processing, but it will also deliver efficiency – reducing TCO and ultimately improving the bottom line – thus ultimately creating post trade ‘alpha.’

About ISITC Europe

ISITC Europe CIC is a non-profit industry body and a catalyst for collaborative innovation within the capital markets. We bring together a diverse community from across the capital markets ecosystem for a joined-up approach, so that we are all better equipped to navigate the rapidly changing financial markets.

The Post Trade Forum

The goal of the post trade forum is to make a positive impact on the industry. This will be accomplished by engaging practitioners across the Capital Markets post trade ecosystem to generate ideas that will provide tangible improvements. The support of the ISITC post-trade forum members will give credibility and energy to these ideas and allow ISITC to promote their adoption across the various bodies that can influence the outcome. To do this, the Post Trade Forum will provide a dedicated platform for post-trade leaders from across the financial markets spectrum to engage and collaborate in order to share best practice and drive operational efficiency. A focus area will be innovation as an enabler of efficiency, bringing thought leadership and practical experiences together to support the industry in increasing automation. To find out more or to request to join the forum please visit: <https://isitc-europe.com/innovation-forums/post-trade-forum/>

About the Authors: Co-chairs of the ISITC Europe Post Trade Forum

James Maxfield is co-founder of Ascendant Strategy, a boutique post trade consultancy that specialises in strategy and technology-enabled transformation within capital markets. Prior to launching the business in 2017, James worked for 20 years within large, global sell-side institutions such as UBS, Lehman Brothers and Nomura, holding a variety of senior global leadership roles across Operations, Middle Office, IT and Change Management. James is a published author, speaker, and respected thought leader within the post trade space, where his experiences, provides a unique perspective on delivering transformational outcomes.

Alastair Rutherford has nearly 30 years' experience leading the design and delivery of post-trade solutions in investment banks, many of these at MD level. He has worked at Morgan Stanley, Credit Suisse, ABN Amro, Lehman Brothers and Nomura. He is co-founder of Ascendant Strategy, a post-trade consultancy that brings together IT and Operations alongside other stakeholders to create and deliver solutions that are process-lead and enabled by robust and innovative technology.