

# Selection & Survival

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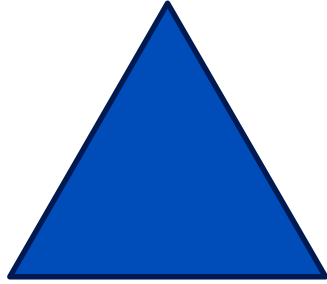


trusted heritage  
advanced thinking



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# Selection & survival – predictable trends?



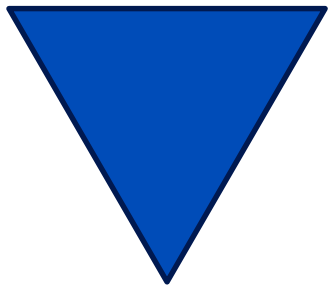
Operational risks  
Investments in talent  
Risk modelling/analysis  
Regulation & legislation

Acceptance of liabilities  
Investments in technology  
Strength of balance sheet  
Proprietary sub-custody network



Market volatility  
Efficiency & scale  
Demanding clients

Product mix & complexity  
Convergence traditional / alternative  
Regulation & legislation



Revenues / profitability  
Product innovation & speed  
Client longevity

Financial remuneration  
Entry of new providers  
Sustainable business efficiencies

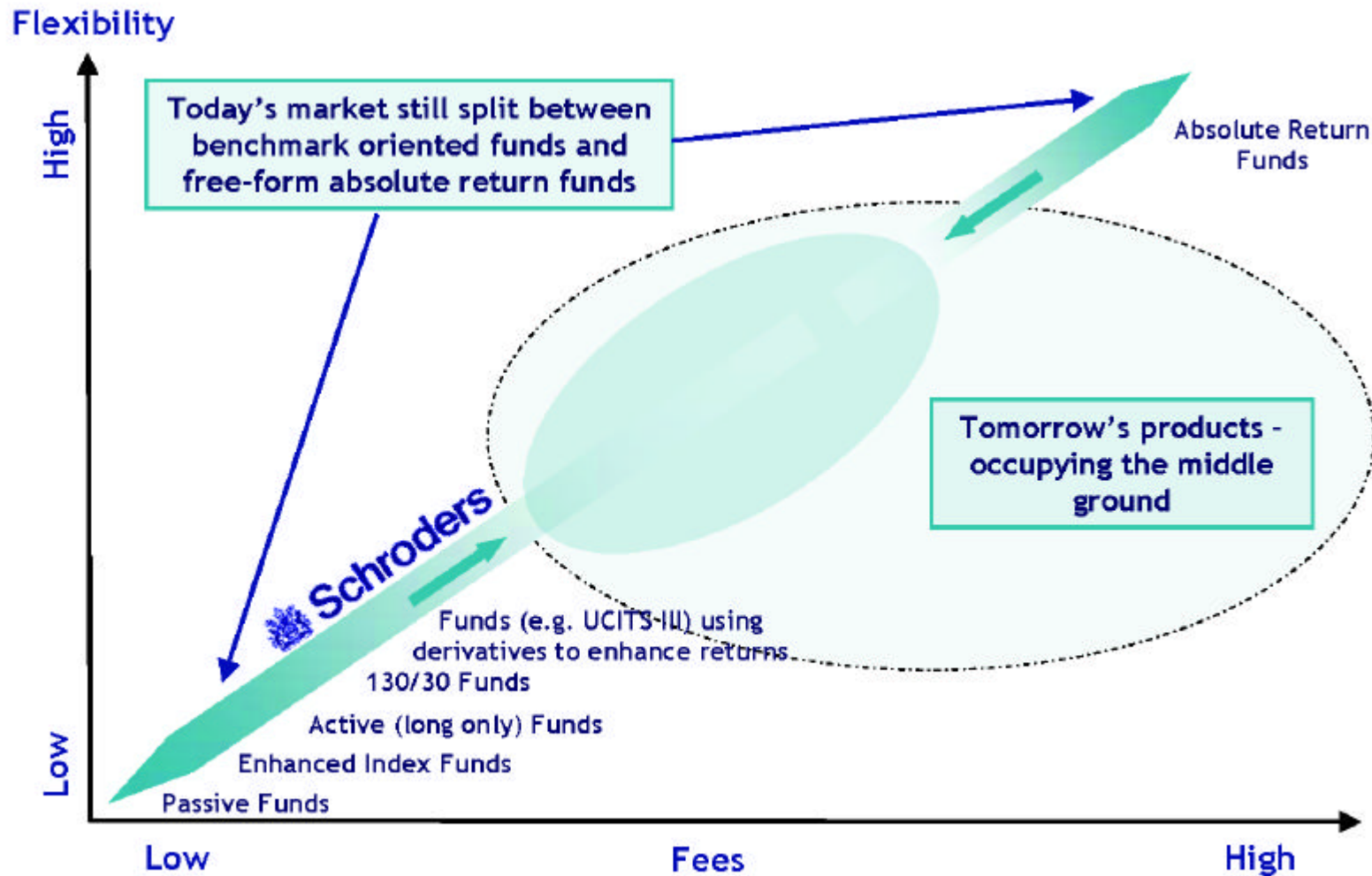


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# “Business as unusual” – the role of the investment manager

- Investment solutions must evolve to meet the needs of the long-term “buy & hold” investor
  - Delivery of a simple, one stop default option
  - Protection against long-term uncertainty
  - Reduced investment risk without materially lower returns
- Two approaches are likely to prevail
  - Asset class diversification (global diversification, multi-asset, multi-manager)
  - Switching strategies (low cost global equity exposure, dynamic asset allocation)
- Administrative strategies for pensions and long-term savings are changing too
  - Focusing on a specific retirement date (lifestyle strategies/target date funds)
  - Tomorrow’s retirement (next generation funds offering certainty of income, combined with flexibility and capital growth potential)

# “Business as unusual” – middle ground in product management



Source: Banc of America Securities-Merrill Lynch research



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# “Business as unusual” – operational challenges

## – Talent

- In-house skills required to manage multi-manager, multi-asset, multi-jurisdictional and multi-dimensional and multi-provider operating environments
- Skills and operational flexibility required by external providers (e.g. global securities services providers, software vendors)
- Financial re-engineering in the “back- and middle offices” (e.g. exotic OTC derivatives, investment risk analysis, operational risk modelling, complex performance attribution)

## – Technology

- Convergence of traditional and alternative processes and technologies
- Shorting techniques (physical and synthetic) require enhancements to order & transaction management-, portfolio accounting-, risk management- and performance systems
- Management of different lifecycle events (e.g. corporate actions)

## – Time-to-market

- Ensuring operational readiness both internally and of outsource providers



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# Asset Management Industry (synopsis) – investing for the future

- Investors look for liquid, transparent and more advanced investment styles
- Diversification, risk control and alpha / beta separation key focus
- Segmentation and client service tailoring critical for longevity
- Expansion of onshore, advanced UCITS III products
- Expansion of indexed products
- Consolidation of hedge fund industry continues
- Continued convergence between traditional and alternative asset management styles/products
- War for talent continues in wake of decreasing revenues and associated remunerations
- Globalisation and specialisation accentuated
- Operational alpha and superior investment performance as well as “duty of care” essential for future success

# Renaissance of the custodian – a new era or more of the same?

- Renewed focus on safeguarding client assets
- Segregation of client money
- Provision of long and short position support (expertise, technology, workflows)
- Fiduciary overlay and declining profitability forcing the change of fees and pricing models?
  - standard services
  - operational risks
  - implied and/or explicit obligations / liabilities
  - operational complexity
  - time-to-market
- Is big really beautiful?

# Sourcing strategies considerations – quality, costs and risks

- Sourcing strategy driven by requirement to ensure operational integrity and agility
- External sourcing aimed at primarily capturing operational and technological expertise with a secondary focus on transforming fixed into variable operating costs
- Internal skill pools used to support client and fund management functions and complex activities such as derivatives operations, performance attribution and risk management
- Operational scale, client segment and geographic reach another key component in the decision whether to in- or outsource, off- or near-shore
- Operational complexity (e.g. new fund, new investment instrument) managed in-house until processes mature and/or can be standardised
- Management of operational dependencies necessitates an appropriate balance between in-house and external expertise



# Understanding risks – where does the buck stop?

- Liability for direct loss
- Liability for consequential loss
- Pricing of risks and liabilities
- Education of clients/investors

# Mitigation of operating risk – a shared responsibility!

- **Clarity** about the real investment and market risks
- **Precision** in wording client documentation
- **Honesty** about what can and cannot be done
- **Access** to shared skills and expertise
- **Transparency** about operational weaknesses

# Regulation – opportunity or threat?

- Regulatory evolution or revolution?
- False sense of security for our investors?
- Who bears the costs of increased regulation?
- An opportunity for those who have scale?
- A barrier to entry for smaller companies?

# Regaining investors' trust – a joint opportunity!

- We must endeavour to **explain** investment, trading and operational risks to investors
- We must improve our **understanding** and **respect** clients' risk & reward profile
- We must encourage **ethical investment** – “it may be legal, but is it decent?”
- We must **simplify** investment documentation/fund prospectus
- We must **collaborate** more effectively when launching new investment products
- We must **interact** with regulators to ensure fair and appropriate regulation

# Selection & survival – a new approach to “duty of care”



# Conclusions – selection & survival

- Structural and fundamental issues to be addressed collectively by industry, governments and regulators
- Regaining investors' trust and expanding client longevity vital to future business growth
- Transparent, liquid, un-leveraged products to dominate for some time
- Increased emphasis on risk control, alpha/beta separation, reappraisal of asset allocation
- Organic growth will prevail led by increasing wealth in emerging economies, private wealth/DC in the Western world and slowly recovering key economies (USA, Europe, Japan and China)
- Industry consolidation to continue as sellers dispose of non-core AM businesses and buyers seek scale to offset market falls
- Operational integrity and agility paramount for a high performing business
- Extensive use of technology to ensure sustained efficiencies as profitability declines
- War for talent to continue (particularly in wealth management and IT)
- Globalise, specialise or get out.....



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