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Episode 2: Applying Innovation in Asset Management – is the buy-side finally catching up?

Transcript:

0:05 - Joyce Pogge:

Hi, everyone, we are live from our virtual finlabs. I'm your host, Joyce Pogge of the New York marketing team at Synechron, and welcome to finsights from our finlabs. Your go-to podcast for the latest in innovation and transformation from our finlabs experts.

In our new series, Investech we'll be focusing on the latest trends within the world of asset management, as well as innovation across the financial services industry more generally, and what lies ahead. Today, I'm joined by Sandeep Kumar, Managing Director at Synechron, and Head of the Investech accelerator programme. Sandeep, thank you so much for joining us.

0:48 - Sandeep Kumar:

Joyce, thank you for having me on finsights, very happy to be here.

0:52 - Joyce Pogge:

Wonderful. Before we really dive in, can you give a quick introduction about yourself and background in the industry for our listeners?

1:04 - Sandeep Kumar:

Sure, I've been in this industry for almost 25 years. I've had the chance to work on both sides; sell-side and buy-side, as well as with the intermediaries. About five years ago, when we launched our blockchain programme, we took up some relevant use cases and it saw some great success with our clients. Since then, we have launched a number of such programmes, making use of data science API's targeted towards specific business areas, such as wealthtech/regtech. I'm very happy to be leading this new edition of our accelerator programme focused on the buy-side firms. We're calling it Investech, and we hope to tell you more about it.

1:45 - Joyce Pogge:

Thank you so much, Sandeep. So for today's show, we're looking at how asset management firms are accelerating and applying innovation, how the buy side can gear up to catch up to the sell side, and how they're looking to take advantage of various emerging technologies to really accelerate transformation. While ultimately, we'll really put more of a microscope on the buy side, before that, I'd love to get your opinion on some of the success stories within the financial services industry. Are there any that you can share that are top of mind?

2:18 - Sandeep Kumar:

Yes sure, if I look at banks in general, sell side commercial banking, the biggest innovation that comes to our mind in the last five to 10 years is around API's (Application Programming Interfaces). I think using that simple concept, many banks have done wonderful interfacing with their customers, counterparties, and their partners. I would rate API's as having the biggest impact in terms of innovation, in terms of developing that ecosystem of transactions around these firms. In fact, if you ask me, the 'I' API should stand for innovation, in my view, it is that powerful. And I'll give you some examples. If you look at the launch of global transaction banking from Goldman Sachs, firms like JP

Morgan, and many others have taken great advantage of API's. There are firms like Bank of New York Mellon, DBS, and Singapore. These all have launched great API programmes among many others,

and brought their partners, their counterparties, their clients seamless into a single integrated type of transaction. And we should also note that this kind of progress has been made possible because of several technical components and despite these banks being heavily regulated, you know, despite many of these constraints around data, privacy, and so on, this is remarkable progress. And if I combine API's, I also want to mention about open source movement. We are seeing great, great progress with open source components coming from many banks, many banks contributing to a common industry code base. And that is also having a great impact on the banks in general.

4:09 - Joyce Pogge:

So, I noticed you said that you think that the 'I' should stand for innovation. And it's clear that continuous innovation is very critical for the success of businesses, especially within financial services. So, my question is twofold, what do you think makes that so important? And why should asset managers be ramping up their digital programmes? Do you think that the current global situation where there's a particular focus and say, the climate crisis has put pressure on asset managers specifically?

4:39 - Sandeep Kumar:

Yes, I think you bring some relevant points. If I talk about asset managers, a very key component of their equation is how they deal with asset owners. And both asset owners and asset managers are going through unprecedented crisis and multiple of them at the same time. We have gone through a pandemic, we are in the middle of it, we are going through a financial, economic crisis. This is leading to great changes in the way we work, the way we spend money and the way we look at investments. So, if I combine all of these crises happening all at once, the asset managers are trying to deal with it in many different ways. Their clients are demanding greater access to data or greater access to reports, and more frequent, more granular data is needed from them. If I take the example of ESG, (Environmental, Social and Governance) that kind of investment team has become mainstream now, this is no longer a buzzword or secondary activity. Each type of investor, whether it's a pension fund, a retirement fund, or an asset manager on the institutional side, or on the wealth management side, they are rightly worried about the longevity of the returns, the stability of their returns, and so on. So, what we see is many of these new pressures on the investment side is leading to more demands on more granular systems, more real time data, more analytical views. And all that will put a lot of pressure on the digitization that is just about starting in on the buy side; the journey to cloud, the ability to use alternative data, and API's interconnectivity becomes far more relevant, far more important now.

6:38 - Joyce Pogge:

So, I'm really glad that you mentioned ESG, because we're hearing a lot about it both in the industry in general, and with some of our own clients as well. So, in 2019, in their annual shareholder report, HSBC pledged their commitment to ESG and lowering their carbon footprint. Similarly, a survey carried out by responsible investor in conjunction with UBS, also in 2019, found that 78% of asset owners globally, are already integrating ESG into their investment processes. So, you mentioned this before a little bit, but in the coming months, do you think that we'll really see ESG become a critical part of long-term investment strategies?

7:19 - Sandeep Kumar:

Yeah, you're right. ESG has become a mainstream investment team now. And many firms many more firms are taking notice adjusting to it and we should also remember that this is not a very new concept in the industry, many firms like Nuveen Investments have been doing responsible investing for a number of years, and they are one of the biggest owners of farmlands in the world. And they rightly care about the environmental, social and governance factors because they deal with clients who worry

about the retirement funds, etc. So, but what has happened this time is because of multiple crisis, this is taken central stage. And if I compare ESG with another type of rating in the industry, let's say we are

very used to seeing the credit rating of companies, and it's quite mathematical, it's based on financial formulas. And over the period of time, at least there is a consistency in ratings from whether you will look up the ratings from SNP or DNB, Moody's and so on. They may have a different nomenclature, but you can relate what does it triple A rating from agency one mean, on a numerical basis, etc. But measuring ESG is quite hard. When you go and measure the factors of E, S and G, it is quite hard because these are not financial numbers.

You're trying to

assess a company's environmental quotient, how they deal with social issues, how diverse is their board, these are very hard to measure factors. And on top of this, there's there's lack of standardisation in the industry, there is no accounting or there is no auditing that happens today in a global way. So, all this makes it very difficult. So, on one hand, we have such a great rush for all types of companies, all types of asset managers/investors trying to measure their ESG quotient of their portfolios or their investments. And on the other hand, there is such a lack of standardisation/uniformity in the industry. This makes it a very difficult problem to solve. So, what is needed again, is that brings me to the topic of data. We need lot more data, a lot more alternative data from many different sources and you need tools to make sense of this data. And finally, you need very smart workbenches and toolkits to be able to come to a standard so that an asset manager is able to say your score on an ESG portfolio is about 70 out of 100. And they can convince their clients or their asset owners saying yes, indeed, they both match in terms of measuring the ESG impact. And industry is far from that standardisation as of now.

10:19 - Joyce Pogge:

But you do think that one day there will be a standard way to measure these components.

10:24 - Sandeep Kumar:

I think, yes, it takes time but since it is such an important metric, and I think all parties are keen to make standards around it. It will never become like the standards that we have with credit rating as an example, because this is linked to financial numbers. This will never become that mathematical, but I think there will be a lot of standards coming up. The European Union has come up with their own taxonomy. So many of these things will help. United Nations has published a set of standards called 'PRI', and principles of responsible investing. So all of these things are helping the companies but it will take some time and if I look at the landscape within the buy side firms, there is a need to be able to upgrade their data platforms to be able to ingest all types of data to make sense of these calculations and be in sync with their customers. It will take some time but certainly it's possible.

11:30 - Joyce Pogge:

So, given some of the trends and themes we've discussed so far, it's clear that there are a number of ways for organisations to innovate. How do you think that investment management firms can really take advantage of this applied innovation and ramp up their existing strategies?

11:46 - Sandeep Kumar:

If I look at innovation within the asset management industry, there are two key components that I think of; one is cloud and the second is data. If the funds can take care of these two things; cloud and data, I think they would have solved half of their innovation journey. And they would have enabled their firms, their portfolio managers, traders, their investors, to be able to take advantage of the innovation that they can offer. So, if I talk about cloud, I think, in general buy-side is slightly lagging behind other sectors of banking in terms of cloud adoption. And banking, being a heavily regulated industry, itself is lagging behind in terms of cloud adoption, compared with let's say, retail or other sectors. So that is the first thing that these firms need to look at, what percentage of their systems and transactions happen through cloud and I bring up API's, as an example, they should check saying, what percentage of transactions with their counterparty is happening still through FTP versus API's as

an example. When you try to connect many participants, what happens is in the buy-side industry, it's using third party systems in a very, very big way. There's a lot of dependency on the major third-party systems, from BlackRock Aladdin, to SimCorp Dimension to Charles River, and so on.

And many of these systems need to coexist, they need to coexist with each other, they need need to coexist with asset managers own internal systems. And bringing them all to the cloud adds another layer of complexity, they need to coexist. And they need to coexist in a multi cloud environment. So, all this is going to take some effort and time. But that will be one of the baseline factors in making progress with innovation. And the second being data. Data is at the core of what the industry does. The data needs to be clean, the data needs to handle many types of sources, including structured data, unstructured data, and the data needs to be

shared in a secure way with their counterparties. So, all this is again, is going to take a lot of effort. And this will lead to more innovation once they solve data running on cloud.

14:24 - Joyce Pogge:

So, while cloud seems to be a huge contributor as you mentioned to the strategies, data has really been a key touch point during our discussion today. Can you elaborate a little bit more on why it's such a crucial area for asset managers to consider and understand when they're looking at their digital strategies?

14:43 - Sandeep Kumar:

So when I look at data, data is the lifeline of any investment management firm and the way a firm is able to handle data, internal data and the data coming from their partners and external sources can really set them apart. Some of the firms have taken charge of this, they have very advanced data pipelines. By advanced I mean they can do a very efficient data ingestion, whether it's a structured data or semi structured data or unstructured data. They can run it through their cleaning scrubbing engine very efficiently. They have an advanced data lake, or a data fabric, on which they can run their data science models. They use technologies such as graph, which will help you make sense of multi-dimensional data and help you find missing correlations. So, all of this makes it a very powerful ingredient to run your models, to run your scenario analysis, and to run complex things such as performance attribution and many topics. So, getting good control on audio data pipeline is a very, very key aspect of it. And since the industry relies on many data sources, there is an amount of data privacy that these firms need to be aware of, which is a very important ingredient. It's not like they can take any data from anywhere and just start using it. There's a lot of privacy concerns that need to be satisfied and that brings additional complexity in the way these data engines can function.

16:22 - Joyce Pogge:

I'm really glad you brought that up because we've we've touched on why and how investment and asset management firms can and should implement their innovation strategies. But when recommending organisations to embrace innovation, it's often easier said than done. Before ideating, let alone delivering any new technology or programme, there's a set of constraints that companies have that they have to face. So, in your opinion, what are the constraints that investment managers will face or are currently facing in their journey towards digital.

16:57 - Sandeep Kumar:

In terms of constraints, I would say, the data privacy constraints are the biggest. Just imagine there's a hedge fund manager; they are trying to look at all types of data but there is a data privacy angle involved, in how much of this data is private, cannot be shared, whether it's healthcare, shopping, and so on and so forth. Similarly, when we look at large asset managers, they deal with multiple lines of business, data from one line of business cannot be shared with another line of business. So, all of this presents many, many data privacy challenges. And this has been a global challenge, this kind of challenge exist in the banking world, investment banking and many other regulatory industries. So, in

my view, I think this is one of the biggest cost constraints and there is a concept of differential data privacy, or noiseless, data privacy, and some of the emerging start-ups are working in this area. There is very good amount of research coming from firms like MIT in this topic and we are doing a proof of concept with a company called Leap Year and this is one of the most advanced companies in the space

and this aims at solving that challenge of data privacy in a way that is acceptable to regulators, it's acceptable to all the participants, and that will really remove this biggest constraint in terms of innovation and data privacy challenges can be solved. All other aspects, which I mentioned earlier, which is cloud, which is data ingestion, running data science models, etc. are being solved, have been solved in other industries, other segments but data privacy is one one aspect that many industries, many segments are struggling with. So, this is the biggest constraint in my view.

18:57 - Joyce Pogge:

Going back to the very beginning of our conversation today, we talked a little bit around ESG, and how the world is a little bit unpredictable right now, we have multiple global crises going on. So, we know that the

future is

unpredictable. But how do you think asset managers can ensure their readiness for the future, even if it's a small step as part of a larger strategy or journey?

19:22 - Sandeep Kumar:

So, there are two key things to be kept in mind when asset management firms are undertaking their innovation journey. Number one is to adopt cloud and API's that's very, very essential in terms of improving infrastructure to be ready to handle different types of transactions. Number two, take charge of your data pipeline. If you have an advanced way of injecting, processing, and managing your data sets, that gives you a great advantage in terms of doing innovative work in the industry. So, these are the two things that I would recommend in terms of applying innovation in investment management.

20:03 - Joyce Pogge:

Well, thank you, Sandeep. We're just about at the end of time today. But thank you so much for joining us. It was really great to hear what the by side can do in terms of innovation, whether it's a heavy focus on data and the build out of data lakes, as you mentioned, migrating to cloud, which is a crucial part, or looking at how investment management firms can take advantage of innovation. Are there any final comments that you'd like to leave our listeners with?

20:29 - Sandeep Kumar:

Yes, in my experience, whenever we have tried to run innovation projects, there are two things that matter; one is keep the end customer in mind and keep it simple. These are the two things we try to adhere and that's my advice to anyone trying to innovate.

20:49 - Joyce Pogge:

Thank you so much for your time, Sandeep and thank you for our listeners for tuning in. If you're interested in finding out more about Synechron and what we do, please visit www.synechron.com and if you liked what you heard, don't forget to like and subscribe.

Catch you next time.