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Global Transfer Agency rethinking the business model in the current market conditions

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The Transfer Agency business and the coexistence of various business models

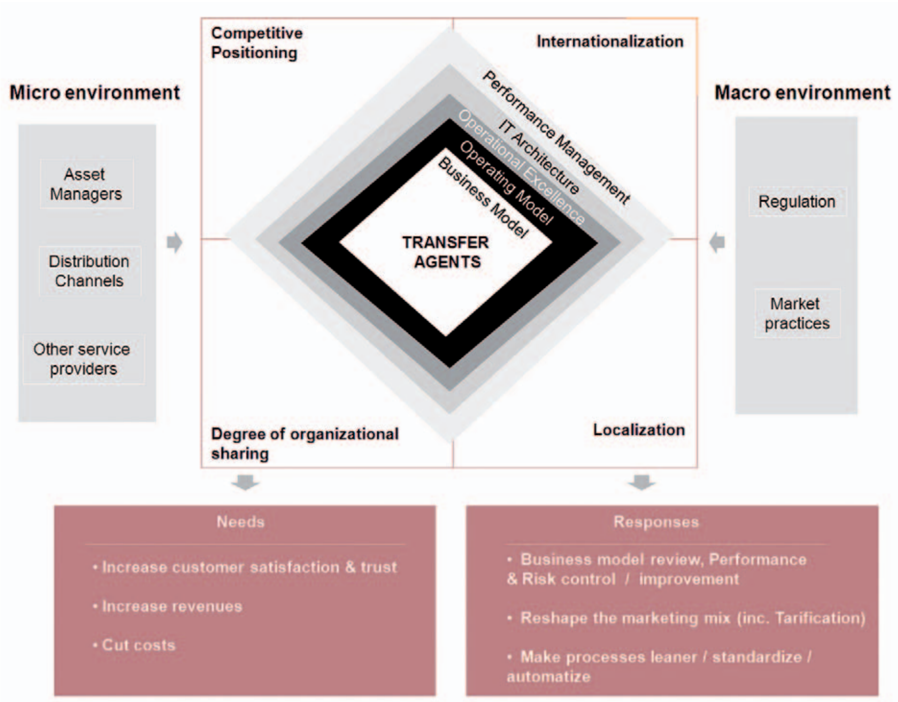
Luxembourg is the market of cross-border distribution, and therefore is based on the development of the transfer agency activity. The CDS model, which is an alternative model to the transfer agency, is mostly developed in countries where domestic markets are more relevant.

Due to the expansion of funds distributed cross-border (whether pure cross-border or round-trip funds) in a variety of markets including Asia and Eastern Europe, the business of transfer agents in Luxembourg needs to constantly adapt to the changing environment. In addition, the current crisis has posed additional pressure on fund service providers, including transfer agents.

Some of the drivers of change are structural; others are contingent to the current market conditions. In any case, the interaction of both categories implies a change in the way the business model is carried over (see table below).

	Driver	Challenges			Business model	Operating model	Processes	IT
		Revenues	Costs	Risk containment				
Structural factors	Increase in the pool of investors / markets covered / funds available		v	v	Diffusion of Global TA models, and emergence of additional services related to the global reach (including global reporting and web access, distribution support, and fiscal advice/calculation)	Use of hub/spoke approach to substantivate Global TA, and Centralization of distribution support despite difficulty of standardizing operating models across markets: lack of organizational economies of scale.	Order processing (large number of orders are manual - STP rates at 47% (ITAS 2009)), and confirmation due to large volumes of trades; harmonization of processes across different funds / promoters	Diffusion of Global TA and Investors' platforms (issues: connectivity, communication standards, missing information), diffusion of Service Oriented Architecture
	Cost pressure on distribution channels (control on inducements and trailer fees), along with the diffusion of guided and open architecture	v	v		Transparency in costs pushes the emergence of offering on trailer fee calculation.	Need for qualified resources mixing functional and IT skills	Lack of homogeneity of calculation approaches, periodicity, rules	Specific investments for tools supporting trailer fees calculations, when transfer agency packages do not support trailer fees calculations or volumes are too high
	Evolution and variety in the distribution channel types and standards		v	v	Emergence of order centralizers as to consolidate volumes and reduce variety of standards to be implemented.	Need for increasing standardization efforts	Need for process harmonization across different funds / promoters	B2B platforms cohexist along with non-standard messaging approaches / tools
	Increase of product and fiscal complexity stemming from master/feeder structures and cross-border mergers		v	v	Emergence of advisory roles within fund service providers, and corresponding offering (fiscal, product structuring, distribution support)			
	Diffusion of the European Management Company passport		v		Constraints of localization of certain commoditized services (register, compliance AML/KYC) and impact on costs of keeping these services in Luxembourg	Possibility of organizing non-sensitive activities on an European or Worl-wide basis (trailer fees, taxes, investors' communications...)	Evaluation of impacts stemming from existing duplications, and implementation hub and spoke with near shoring solutions	Evaluation of impacts stemming from shared infrastructure on a cross-border basis (depending on the chosen model: diffused competencies vs. centralized competencies)
Contingent factors	Financial market conditions (decrease of fund savings until the beginning of 2009 world-wide; increase of fund mergers/closures/launches)	v	v		Impact on tarification (re-negotiation) structure, level and periodicity; and emergence of services like distribution support	Greater constraints to conduct change management	Attention to cost rationalization for highly manual activities	Attention to cost rationalization
	Challenges in balancing current and financial needs: replacement initiatives in IT, for TA packages are suspended		v	v	-	-	-	Expansion of functionalities of TA packages is limited to quick wins. No major implementation, rather emergence of the ASP/Service bureau approach

In presence of a variety of business models, we can argue whether one of these will emerge as prevailing in the coming future as the best way to achieve the strategic objectives of revenues, cost containment, and operational risk control (see next figure).



Different business models are available to carry out Transfer Agency activities. Some of them are more tilted on the functional side (1 & 2), others more to the IT side (3 & 4)[1]:

1. Specialized division in an integrated banking model, where the bank is specialized in investor services
2. Specialized operators within asset management or (universal) banking groups
3. Joint ventures between service providers and IT companies
4. ASP / Service-bureau from IT vendors (and, more rarely, transfer agents)

The competitive positioning, the degree of internationalization, the localization choices and the degree of organizational[2] sharing differ in each of these options. They imply a different way of carrying out strategic objectives and structuring the underlying operating models accordingly.

For instance, groups, where fund servicing is a complementary and intra-group specialty, will tend to concentrate their operations within one location, or, if required by large volumes and local specificities, implement local operational sites. The degree of organizational sharing will be quite low in this case as each site will behave mostly in an independent manner.

Roots for reshaping the current business model of Transfer Agency service providers

Since October 2008, the fund industry has been characterized by negative net sales, the launch and closure of a number of funds, and fund mergers. Despite the crisis, the activity of transfer agents (and distribution support) has been intense. The liquidity drain that affected the fund industry has an impact on the P&L of service providers, as renegotiations of third-party services take place, as a result of expiring Service Levels Agreements, or consolidations of funds. In this environment, the transfer agency services, which are already considered to be heavily commoditized, are likely to be priced down further. In this context, the ability and possibility of supporting Global Transfer Agency activities and services (including distribution support, and web reporting) seem to be the way ahead. But is it really the unique way ahead?

[1] To be noted that some providers mix different business models as they are moving from one to the other.

[2] We define competitive positioning as the set of all the elements related to the service and product offering definition, the degree of specialization in transfer agency activities, risk management, and fees structuring. The degree of internationalization refers to the geographical width of the transfer agency activity that could be offered in one country, regionally, or globally. The localization dimension refers to the degree of complexity stemming from the different standards in place with different distributors and distribution networks, and the supports needed to this extent. Organizational sharing relates to the ability of an organization to concentrate global activities within fewer world-wide centres, and share the output of these activities in an efficient manner, across the various entities performing the transfer agency business globally.

First, the four business models outlined above do have distinctive characteristics and challenges to face, and respond to specific and distinguishing needs in the fund industry. Secondly, focusing on global distributors or (institutional) investors certainly enables achieving a large part of the market, but can cause failing in markets where distribution is fragmented, and retail represent a consistent share of fund investing. Therefore, the new choices in terms of competitive positioning (product, market, channels and pricing) must be in line with the business model in place, or the target model (see table below).

Thirdly, we observe that among the two groups of providers (one group stressing the functional part of the transfer agency services, the other stressing the IT side of the service), the IT-tilted group seeks to achieve larger volumes and standardized flows, while the former stresses on the ability to manage complexity for smaller volume/size funds. For this reason, when considering changing the reach and the breadth of geographical servicing, the first group should consider further automating, consolidating and standardizing the IT platforms. Eventually, a mix of global/local approaches should be integrated.

Among all these groups, will the ASP/service bureau be the ultimate type of business model? In our view not necessarily, as the competitive positioning and the willingness to retain certain competences internally will push or retain from such a choice.

	Business Model characteristics						Strategic Objectives		
	Business model	Description	Competitive positioning (service offering, tarification, product coverage, investor coverage)	Internationalization (geographic coverage)	Localization (complexity of distribution network)	Organizational Sharing (degree of sharing of operational teams across countries)	Revenues	Costs	Risks
Functional	Integrated	Originally in-house based, more focus on third-party offering. Transfer Agency services are integrated in a banking model focused on investor servicing, and are often offered in bundled agreements. Tailor made services, and functional expertise are core offering.	Importance of offering and other items of the marketing mix.	Regional moving to Global	High	Mid to High	Increase span of offered services; review tarification	Increase operational standardization; increase activity sharing across sites; manage costs from local specificities	Manage complexity from both IT and business activities
	Specialized	Mostly in-house based, part of asset management or universal banking groups. Operational efficiency primes, while service offering is leaner.	In-house products coverage, across markets: transfer pricing is not necessarily calculated, relevance of the cost items	Local to Regional, with different sites	Medium	Low to mid	Ensure appropriate coverage of local specificities, define transfer pricing	Control and reduce costs as activity is non-core to main business	Manage financial risks
	Joint venture	Mainly third-party servicing. Transfer Agency services are integrated in banking model focused on investor services, but IT support is externalized through partnerships with IT companies.	Service offering is based on global reach and processing times (including standardization, and automatization)	Global	High	Mid to High (unique IT platform, shared activities though sites world-wide)	Renforce services associate with timely delivery and web-reach.	Focus on reducing costs of non standardization	Manage volume peaks and timely delivery
IT	ASP/Service bureau	Shared IT infrastructure among different service providers, externalization to IT vendor. The objective is to minimize IT costs related to licence, and maintenance. Functional aspects of the transfer agency activity needs to be performed under one of the other paradigms.	Providers offering this service stress on the possibility of reaching economies of scale for customers (service providers). Costs is the main driver of such offering, no direct benefit can be defined for funds promoters / distributors / investors.	Regional to Global	High	High (infrastructure), Low to Mid (processing: functional activities can be organized centrally or locally or can be shared)	Assess tarification vs. other models	Increase volumes to achieve economies of scale	Manage operational risk coming from lack of control of service providers (legal, IT, delays)

Transfer Agency – the way forward

Generally speaking, transfer agency providers focus on costs and risk management rather than revenues, as until today the pricing of such services has been either bundled in third-party general offering or not formally priced in deals intra-group.

Not being able to manage revenues as an independent source, providers have focused until now on costs, and ways to reduce them (automation, and standardization of IT and processes, search for economies of scale: see table below), and operational risks (which are therefore not factored in pricing).

However, the diversity of markets, and their specificities make somehow difficult to reach for true economies of scale and full standardization, on the cost side. Certainly, efforts in this direction should be continued, despite the fact that rethinking the revenue side of the equation should now become a priority.

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Contacts

NGR Consulting Luxembourg
38, rue Pafebruch
L-8308 Capellen

Tél.: +352 26 65 20 52

Site Web : www.ngrconsulting.com