VIEWPOINTS

A Charles River Conversation

APAC Asset Owners: An Industry in Transition

NAVIGATING STRUCTURAL AND REGULATORY CHANGE

Charles River

A State Street Company

APAC ASSET OWNERS INCLUDING PENSION, SUPERANNUATION AND SOVEREIGN WEALTH FUNDS

face a number of operational challenges from cost pressures, increased regulation and a search for greater returns in today's low yield environment. Charles River convened a panel discussion to explore these challenges and the role technology vendors play in helping funds formulate effective solutions.

DENNIS BAILLON

Director of Sales, Asia Pacific
Charles River Development

With more than 23 years of experience in the financial and technology industries, Dennis has a breadth of industry knowledge and expertise gained from a variety of roles, both in Europe and more recently the Asia Pacific. Dennis joined Charles River in 2003 and has held a number of positions within the firm including Implementation Manager, Product Specialist and Sales Manager. Dennis now heads up Charles River's regional APAC Sales team focusing on extending the footprint of the Charles River Investment Management Solution and growing the organisation's client base across the Asia Pacific. Prior to joining Charles River Dennis held positions at leading asset management firms including Aberdeen Asset Management, Equitilink and UBS Global Asset Management.

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PETER SHERRIFF

Principal Architect, Asia Pacific
Charles River Development

Having worked in the financial and technology industries for more than 23 years, Peter joined Charles River in 2002 based in the London office where he was responsible for establishing the support function for non-US clients. In 2004, Peter moved to Australia to establish the Asia Pacific operations and has been in his current role since 2008. As Principal Architect, Peter uses his extensive business, product and client knowledge to work closely with the pre-sales and sales team to identify and define the end to end solution to deliver maximum business benefit from the use of Charles River IMS for prospect and client organisations. Prior to joining Charles River, Peter held a number of development and client services positions at Misys Asset Management Systems.

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REGULATORY CHANGE

Evolving regulatory requirements and their interpretation for governance impact asset owners, increasing compliance costs and compelling funds to seek expertise interpreting and implementing these regulations.

CHALLENGING INVESTMENT ENVIRONMENT

The persistent low interest rate environment, increased volatility and aging populations are driving asset owners to diversify their investment strategies in order to retain assets and mitigate the impact of these trends.

INCREASED ADOPTION OF ESG AND ALTERNATIVES

APAC asset owners are increasingly shifting their portfolios to gain exposure to international and non-public markets, real assets and Environmental, Social and Governance (ESG)-driven investments. To support this shift, funds are actively seeking specialised expertise in managing these products and asset classes, and the ability to hedge associated FX exposures.

LEVERAGING GROWING DATA VOLUMES

The growing volume and diversity of data captured by asset owners can provide valuable investment insights for organisations with the expertise to extract that information.

"RIGHT SOURCING": STRIKING A BALANCE

While significant aspects of operations may be outsourced, accountability for meeting regulatory obligations remains with the asset owner. Consequently, a fundamental re-think of fund operating models is occurring, with funds determining the optimal mix of outsourcing versus insourcing to suit their organisation.

FUND CONSOLIDATION

Several factors impact the viability of running pension and sovereign wealth funds. These include increased competition, the current investment environment, member interest and regulatory and staffing costs. This is forcing smaller funds to consolidate and merge with peers in order to gain economies of scale.

APAC asset owners face growing regulatory hurdles. How are they responding?

PS It varies and depends on the market and segment. Using Australia as an example, there has been significant regulatory change in recent years, resulting in additional reporting burdens on asset owners. This has changed the dynamic between asset owners and their outsourcing providers, requiring them to adjust their operating model to provide solutions for additional oversight and reporting.

Trustees of these funds realise that while they can outsource certain functions, accountability for meeting their regulatory obligations remains in-house. This contributes to the shift we are seeing, with some Australian asset owners moving to manage those obligations internally, rather than continuing to outsource.

DB Asset owners are also seeking assistance on how they can best comply with these changes. The knowledge and expertise needed to interpret and manage these changing obligations are not necessarily existent in-house, particularly around risk management and enhanced transparency.

In response, asset owners are reaching out to consultants, technology providers and asset managers looking for advice, best practices and innovative ways to approach these changes. By understanding what some of the larger asset managers are doing, how they're doing it, and what platforms they're using to do it, they can see what's possible. From there, they start talking to technology vendors for guidance on how to implement potential solutions.

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What are you seeing outside of Australia?

PS Looking more broadly across Asia, many national pension schemes still have a significant number of both large and small defined benefits plans in operation. They're likely to see increasing solvency requirements being applied to them in the coming years, as we've seen in other geographies. Any changes to risk management frameworks and additional stress testing scenarios, or a need for the defined benefit funds to hold significant capital reserves will drive further adoption of technology platforms. Organisations increasingly realise the role of technology in helping them manage and model risk across their investments.

DB We are also starting to see that some of the changes to accounting and financial reporting have an effect on regional asset owners. Even if they haven't had to adopt the latest standards yet, they're having to plan and factor it into their project schedules and budgets and determine how to manage the impact on their investments. For example, the additional recognition of fair value changes within IFRS 9 are likely to see an increase in the impact of market volatility on affected asset owners.

The global investment environment has been challenging for some time. How does that affect the strategies asset owners are implementing?

PS Regulatory changes mentioned previously are also impacting the investment environment, whether it's changes to the classifications of assets or capital reserve requirements. Asset owners are having to find new investments that offer consistent yields with lower volatility over a longer time horizon, such as shifting their equity investments from growth stocks to dividend stocks.

Additionally, the persistent low-yield environment brings its own challenges. Whilst this is a global problem not unique to Asia Pacific, the volume of defined benefit plans and ageing populations in Asia is significantly widening the liability gap. The third challenge impacting funds is the rising cost associated with meeting their ever-changing regulatory obligations. Increasingly, asset owners are looking to technology vendors for services and solutions that help them meet these challenges.

Leveraging massively growing volumes of data has become increasingly important for asset managers looking to generate alpha and gain a more granular view of exposures. How does that apply to asset owners?

DB Funds want real time access to their data in order to implement asset allocation changes and use either internal or external resources to implement overlays and track their combined position.

That's leading a lot of the Australian asset owners, largely the pension funds, to enhance their internal data management, data scrubbing, and reporting tools. This will enable them to gain better insight into what's impacting their investments, and also position them to better meet newly introduced reporting regulations.

PS There's a whole set of data related challenges because many funds throughout the region have historically outsourced nearly everything, from asset management to using custodians for reporting and compliance services.

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Increasingly, they are realising that they have very little insight into their investments, and no real-time visibility. In order to derive insights from that data, they need to have it in-house and find a way to consolidate and validate the information available to them.

Many of the conversations we're having in Australia are focused on acquiring data from custodians, benchmark providers, and their external managers, then bringing all of this disparate data together and distributing it to other systems.

The majority of Australian superannuation and sovereign wealth funds acknowledge they need a tool to in-source data acquisition and management. They've never had this data in-house, so they haven't been able to explore the breadth and depth of information embedded in the data to derive actionable insights.

What additional initiatives are you seeing around data?

DB The next step for the more advanced firms jumping on the big data bandwagon is to derive additional investment insight and make strategic decisions from these insights on the direction of the fund. Additionally, they are looking to integrate business intelligence and reporting tools that deliver data to stakeholders in real time.

This is a big step for firms that have historically been constrained by disparate data siloes. Asset owners need to get the data in-house first, and then look at leveraging insights after that. Technology is the enabler to make this all possible.

What shifts are you seeing in asset allocations?

PS Looking across Asia, we are seeing funds that were historically domestically-invested start to increase their overseas exposure. Korea is an example where markets have been very solid, but as they expect growth to slow, firms are looking offshore for additional diversification and enhanced returns.

We're also seeing increased asset owner interest in alternatives, whether that's private equity, unlisted real estate, direct loans or infrastructure.

One theme coming out of the consulting and asset management groups suggests that Asian asset owners are starting to look at outsourcing more of their asset management functions.

That may be related to the shifting focus from domestic to overseas assets and alternatives, where they don't have the same level of exposure and their teams have less experience. It makes sense to outsource the fund management component as asset allocations become more international.

DB Given the long-term investment horizon of these funds, alternative asset classes such as real estate and infrastructure are certainly good investment vehicles for them. With regulators increasingly allowing funds to diversify asset classes and market exposure, we believe this trend will become even more prevalent.

> Increasing demands for corporate transparency are driving the dissemination of timely and accurate ESG data, enabling investors to make socially aware investment decisions.

What's the state of ESG investing in the region?

PS We see asset owners increasingly embracing ESG, looking for more sustainable investments that align with their 20 to 30 year investment horizon. The pace of ESG adoption in APAC has been remarkably fast, driven by some of the region's largest asset owners with hundreds of billions of dollars in assets.

Increasing demands for corporate transparency are driving the dissemination of timely and accurate ESG data, enabling investors to make socially aware investment decisions. Responsible investing as a part of a long-term strategy works to minimise risk - return ratios and is growing in adoption under the premise that sustainability is linked with good financial results.

Given the shift from domestic to global investments, how are asset owners hedging their FX exposures?

DB APAC funds often use overlay managers to assist with this activity and is an example of a service where we commonly see a mix of firms utilising insourced versus outsourced managers.

Regardless of the model a firm adopts to manage FX hedging, the visibility and transparency of the real currency exposure to ensure an accurate understanding of the data, and ability to influence that lies with the asset owner.

PS APAC asset owners tend to be invested in a broader cross-section of markets than their European and North American counterparts, resulting in exposure to dozens of currencies.

They recognise it's not practical to take currency positions in 50 different currencies to manage that exposure, so they optimise a basket of currencies that may be eight or 10 of those 50 and that can effectively proxy for a region.

For example, the Euro is the predominant currency in Europe, but you've also got Scandinavian currencies and Pound/Sterling.

The idea is to create a basket of currencies that broadly proxies across the whole set of investments in a region and then optimise the mix of these over time.

What's required to support this from a technology standpoint?

DB This complexity from changing asset allocations and managing greater FX exposures means firms are demanding more from their financial management technology — the process needs accurate and timely data and a platform that allows this information to be interrogated in different ways to derive actionable insights.

Consolidation among smaller funds appears to be increasing. What's driving that?

DB The previously mentioned factors including prolonged low yields, rising costs, and aging populations are all impacting the long term viability of smaller superannuation and pension funds across the region. The cost of managing these funds is too high, and they are being encouraged by regulators to either merge or cease operations. Funds need to become more cost efficient in the way they manage assets in order to remain viable. All of this combined with pressure from stakeholders to deliver on targets means that consolidation is a way to remain competitive.

FUNDS NEED TO BECOME MORE COST EFFICIENT IN THE WAY THEY MANAGE ASSETS IN ORDER TO REMAIN VIABLE. COMBINED WITH PRESSURE FROM STAKEHOLDERS TO DELIVER ON TARGETS MEANS THAT CONSOLIDATION IS A WAY TO REMAIN COMPETITIVE.

PS There are a few very sizeable sovereign wealth funds in Asia Pacific that generally operate differently from institutional asset owners and have different investment objectives and investment behaviour. Governments tend to retain control over what they can invest in, resulting in less flexibility in investment strategies and markets although they have the same obligation to provide returns to their shareholders.

One of the greatest demands on financial technology providers will be to offer solutions that deliver actionable insights and transparency throughout the investment lifecycle.

Where do you see the greatest demands on technology providers from APAC asset owners moving forward?

PS The volume of data asset owners collect will continue to grow. As a result, one of the greatest demands on financial technology providers will be to offer solutions that deliver actionable insights and transparency throughout the investment lifecycle. Along with enabling greater use of data, asset owners are also looking to technology providers to offer tools and thought leadership on how to make the best use of this data. From straightforward aspects such as trend analysis and business intelligence, through to more complex processes that provide intelligence around how the data is interpreted via machine learning or AI tools, this will drive better, more insightful decision making across all areas of the business.

NEXT STEPS:

Read more about our solutions for Asset Owners. Contact us to schedule a demo or visit crd.com.

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CHARLES RIVER DEVELOPMENT, A STATE STREET COMPANY

Charles River enables sound and efficient investing across all asset classes. Investment firms in more than 40 countries use Charles River IMS to manage more than US$25 Trillion in assets as of April 2019 in the institutional investment, wealth management and hedge fund industries. Our Software as a Service-based solution (SaaS) is designed to automate and simplify investment management on a single platform – from portfolio management and risk analytics through trading and post-trade settlement, with integrated compliance and managed data throughout. Headquartered in Burlington, Massachusetts, we support clients globally with more than 750 employees in 11 regional offices.

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