Centralizing and Standardizing the Alternative Investment Industry for Greater Growth

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Prepared for: DTCC
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EXECUTIVE SUMMARY

Over the last decade, alternative investments (AI) have gone from being niche products reserved for large institutional and ultra-wealthy clients to being more widely accepted and mainstream. As both institutional and retail investors become more sophisticated, seeking alpha and sustainable investment returns, the alternative space has continued to gain in popularity through a variety of different investment products and structures. The value growth of hedge fund and private equity assets has outperformed the value growth of the S&P 500 index since 2010, providing an indication of this trend.

This paper, Centralizing and Standardizing the Alternative Investment Industry for Greater Growth, commissioned by The Depository Trust & Clearing Corporation (DTCC) and produced by Aite Group, explores the current state of AI operations across financial intermediaries, AI managers, and fund administrators. Based on personal interviews with executives with deep knowledge of both the industry and their firms’ alternative investment operations and technologies, this research highlights the following findings:

- As the AI market continues to grow and attract greater interest from investors, approximately two-thirds of those interviewed share concern about their firm’s ability to scale their operations based on current paper-based processes.

- Operational processes have not kept pace with those used to support traditional asset classes, such as equities and mutual funds, and as a result, AI processing continues to be labor-intensive and error-prone. When asked to provide the most significant operational challenges, more than 71% of respondents cite a lack of standardization in processes, and 65% cite manual processes/lack of automation.

- Seventy-six percent of respondents characterize their level of concern regarding their operational risk profile as low. On the other hand, most respondents also indicate that their operations are hampered by a reliance on manual processes, which tend to heighten operational risk. There appears to be a large disconnect between how firms operate and how they perceive their operational risk profile. Firms have become so accustomed to the current state of inefficient processes that they do not recognize the level of risk to which they are exposed.

- There is overwhelming support for the adoption of an industry-wide solution. However, participants say the challenge is coming to an agreement on structure and standards. All industry stakeholders, including AI managers, financial intermediaries, fund administrators, software vendors, and institutional investors need to collaborate and compromise to help grow business and move the industry forward.
METHODOLOGY

To better understand the practices and infrastructure approach in the AI space, DTCC commissioned Aite Group to undertake a study looking at the state of affairs in AI operations among key industry participants. The study consisted of personal interviews with securities industry executives deeply familiar with alternative investment operations that focused on the following topics:

- Trends impacting the industry
- Operational concerns and challenges
- Current levels of automation and straight-through processing
- Opinions about the use of an industry tool to improve and facilitate alternatives processing

Throughout Q2 and Q3 2016, Aite Group conducted interviews with representative securities industry executives who typically have over 10 years of experience in AI operations to capture more color and qualitative insights. The executives were drawn from three different types of firms: AI managers, fund administrators, and financial intermediaries.

- **AI managers**—a mix of single-fund, fund-of-funds, and real-estate-focused managers representing over US$100 billion in assets under management (AUM)
- **Fund administrators**—large fund administrators overseeing more than US$2.3 trillion in AI, representing over 50% of market share among single-manager fund administrators
- **Financial intermediaries**—self-clearing broker-dealers and clearing/custody providers with close to US$9 trillion in AUM, representing over 50% of U.S. retail client assets

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1. In Q2 and Q3 2016, Aite Group conducted personal interviews with 17 securities industry executives from prominent firms concerning the state of automation in AI processing, operational challenges, and opinions on market drivers impacting the AI sector.

2. Financial intermediaries can take the form of RIAs, private banks/bank trusts, and broker-dealers, and they connect end investors and/or institutional investors with investment products managed by others through their financial advisors/relationship managers.
MARKET TRENDS

As the AI market has matured in the past 10 years, it has seen an increasing potential for innovation and expansion. Today, many AI products are becoming more retail-like, with account minimums decreasing and transparency and reporting requirements increasing to attract more mainstream retail investors. This, in turn, requires more complex distribution efforts.

The ongoing volatility and uncertainty in global financial markets have both institutional and retail investors turning to the AI market in hopes of capturing higher investment returns. After a slowdown during the financial crisis in 2008 and 2009, the hedge fund market has regained its growth momentum, reaching over US$3 trillion in AUM by the end of 2016. Like the hedge fund market, the global private equity market continues to see strong growth in recent years, consistently raising over US$500 billion in total global capital since 2013 (Figure 1).

Figure 1: Growth in Hedge Fund and Private Equity Assets

![Graph showing growth in hedge fund and private equity assets from 2010 to 2016.]


Despite this growth, the industry continues to be mired in inefficient processes, including paperwork, spreadsheets, traditional mail, and faxes. In addition, new products (both registered and unregistered) and product structures continue to emerge, raising the bar for firms in terms of operational variance. The disparity between front-office/client demands and back-office processing capabilities must be reconciled for firms to achieve scale and operational efficiency, and to reduce operational risk.

These pressures on AI operations, varying by client segment and their differing needs, make it difficult to scale service and keep up with growing business opportunities while meeting a host of regulatory demands. In a marketplace already functioning under heavily manual-intensive processes, continued growth will highlight existing technology’s limitations and make it even tougher to scale.
OPERATIONAL CHALLENGES IN THE AI MARKETS

The lack of a single technology platform to support key aspects of counterparty communication and processing in use across the industry raises operational challenges. Respondents say this results in numerous manual steps; therefore, any mistake along the way can have a negative impact on performance calculations, lead to incorrect client balances, expose confidential client data, open opportunities for fraudulent activity, and ultimately undermine the fund’s reputation.

The majority of respondents mention five principal operational burdens plaguing alternative market participants (Figure 2).

**Figure 2: Top Operational Challenges**

<table>
<thead>
<tr>
<th>Biggest Operational Pain Points (N=17)</th>
</tr>
</thead>
<tbody>
<tr>
<td>71% Lack of standardization</td>
</tr>
<tr>
<td>65% Manual processing and lack of automation</td>
</tr>
<tr>
<td>12% Regulations</td>
</tr>
<tr>
<td>12% Difficulty scaling</td>
</tr>
<tr>
<td>12% Security/privacy</td>
</tr>
</tbody>
</table>

*Source: Aite Group interviews with 17 alternative investment industry executives, Q2 to Q3 2016*

1. LACK OF STANDARDIZATION

The major cause of most AI operational ills, according to survey respondents, is the lack of standardization. While AIs are neatly categorized into a single asset class by many industry observers, the reality is that there is a plethora of different products with varying structures and registrations that fall under the AI banner.

Only 24% of study participants describe the level of data standardization as high. The lack of standardized processes, data formats, and communication has necessitated significant numbers
of proprietary feeds—substantially increasing overall workload, ongoing processing costs, and potential for processing errors. On top of that, each stakeholder configures its own workflow somewhat independently of its external partners, which results in a tremendous amount of work to onboard connections.

This bespoke nature of dealing with counterparties leads to a situation in which operational knowledge is not institutionalized; rather, it sits with individual employees. Should these employees leave the organization, institutional knowledge can be lost, contributing to greater operational inefficiencies and risk.

Standardized formats are also rare within the same manager, requiring different internal reports to be reconciled, often manually, because there is no golden copy of data. To complicate matters further, some subscription documents can be 50 to 100 pages each, with critical information potentially buried throughout the document.

While fund administrators and larger financial intermediaries have implemented plans for standardizing and automating many of the processes and much of the communication internally, much more needs to be done.

Agreed standards adhered to across the industry would vastly streamline data transfer and reporting processes, reduce the burdens of maintaining multiple data streams, and lower overall cost and operational risk. The DTCC Alternative Investment Product (AIP) Service provides an existing solution by compelling standardized formats across the industry and automating transactions through its centralized processing hub.

2. MANUAL PROCESSING AND LACK OF AUTOMATION

Today, market participants tend to exchange data using customized spreadsheets via email, in addition to communicating by phone, traditional mail, and faxes. This ultimately leads to manual rekeying of information to prepare consolidated statements and regulatory data reports. Again, the lack of standardization across the industry exacerbates this challenge, as outdated processes lead to higher operational costs and a greater potential for errors.

A few interviewees mention the inclusion of a “four-eyed check” system for reviewing reports before sharing them externally. Two full-time employees must manually review each report before it can be shared.

Figure 3 outlines a typical subscription workflow cycle. The process can vary greatly between firms, and even within firms, but the current approaches to the subscription process require significant manual intervention.

The subscription/redemption process typically involves reams of paper and manual processes. Electronic signature has only taken hold across some firms and products and is not the standard. Expensive overnight shipment of documents that are hundreds of pages long is still the norm.
Figure 3: Typical AI Subscription Process

Only 18% of firms interviewed characterize their level of internal systems automation as high in the subscription/redemption process, though respondents indicate automation levels have increased over the last three years.

There is room for improvement, as 65% of firms interviewed indicate that the level of data standardization when communicating with counterparties is low (Figure 4). Only a few respondents describe communication with external partners as highly automated with high levels of data standardization. Those firms that are AIP members report high levels of automation and standardization for products that sit on the AIP platform, but firms that are not members have medium or low automation.

Automation brings lower costs and risks, along with greater efficiencies, providing the ability to direct resources to more strategic concerns related to growing the business. In addition, standardized and automated processes can help ease compliance pressures, providing ready access to the data required by key regulations. The current industry utility, AIP, provides the standardized formats and automated processes to help achieve these outcomes.
Figure 4: Level of Automation and Data Standardization in Communicating With External Partners

<table>
<thead>
<tr>
<th>Q. In terms of automation, how would you characterize levels of automation for systems involved in communicating with external partners? (N=17)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
</tr>
<tr>
<td>41%</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Q. How would you characterize the levels of data standardization in communicating with external partners? (N=17)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
</tr>
<tr>
<td>65%</td>
</tr>
</tbody>
</table>

Source: Aite Group interviews with 17 AI industry executives, Q2 to Q3 2016

3. REGULATORY CHALLENGES AND PRESSURES

The heightened regulatory scrutiny of recent years has increased compliance burdens, which tend to mandate that firms compile and report massive amounts of data. Some respondents also express a concern that some rules appear to be drafted without sufficient industry expertise, leading to unintended operational challenges for market participants. This can require additional resources and unnecessary duplicative reporting—especially when processing and tracking of transactions is manual and unstandardized.

While some regulations in the U.S. are under review and are being reconsidered, investors have indicated their high expectations for a level of transparency and protection. Notable regulatory examples include the following:

- **Dodd-Frank Act’s hedge fund registration requirements**: Hedge funds above certain AUM thresholds are required to register with the U.S. Securities and Exchange Commission (SEC), particularly if they have any separately managed accounts or maintain only investment funds as clients. There are also requirements, in some cases, for hedge funds with lower AUMs to register with a home state.

- **Dodd-Frank’s Form PF**: Form PF (private fund) is a SEC rule that requires private fund advisers to report regulatory AUM to the Financial Stability Oversight Council (FSOC), which monitors risks within the financial sector.

• **Financial Industry Regulatory Authority’s (FINRA’s) new pricing rule change:** This requires nontraded real estate investment trusts (REITs) and direct participation programs to be fairly valued on a monthly basis.

• **Department of Labor fiduciary rule:** This significantly increases investment advice standards for retirement accounts and imposes requirements for disclosure of all commissions, fees, and expenses.

Other, more long-standing regulatory requirements also impact the AI sector. For example, in 1972, the SEC’s Rule 15c3-3 stipulated that broker-dealers must maintain physical possession or control of securities they hold on behalf of their customers at an approved “control location.” However, since many AI funds are uncertificated and cannot be held physically by a broker-dealer, this has presented a great challenge.

In 2012, the SEC gave AIP broker-dealer members the ability to designate AIP manufacturers (e.g., funds) as “good control locations” to satisfy this SEC rule, thereby enabling broker-dealers to more actively provide AI options to their clients.

Easing compliance burdens is one main reason many firms have turned to the centralized AIP service, which helps to facilitate the transparency needed to meet regulatory demands.

4. **DIFFICULTY IN SCALING BUSINESS**

Advisors representing individual investors make a great number of requests for customized investment offerings, which are difficult for AI providers to deliver, especially in the midst of a drive toward standardization. While some firms view their bespoke offerings as a competitive advantage, by accommodating so many exceptions, the AI sector has been very tough to scale for greater business growth.

5. **SECURITY/PRIVACY**

Concerns over security (including cybersecurity) and data privacy have increased exponentially in recent years. For example, due to the manual nature of most current operational processes, the risks are high for some firms to accidentally disclose investor information or send tax forms to the wrong investors.

The costs of these operational challenges must be weighed against today’s budgets, but respondents report that it is difficult to adequately prioritize addressing these limitations and concerns. The adoption of an industry-wide utility could help address operational process and risk concerns; however, it is imperative for firms to balance concerns about initial costs with the long-term benefits they—and their investors—would gain.
TOP ROADBLOCKS TO AUTOMATION AND DATA STANDARDIZATION IN THE AI MARKETS

To enable firms operating in the AI marketplace to improve operational efficiency, reduce costs, improve their operational risk profile, and fulfill the potential for greater business growth, the industry must establish data standardization in conjunction with intercompany automation. This section explores the top five factors impeding progress: perception of low operational risk, low budget availability, product variation, timing, and the number of exceptions.

1. PERCEPTION OF LOW OPERATIONAL RISK

Despite the response of most participants that their firms’ processes incorporate a number of manual steps, their concern about operational risk is low (Figure 5). The common viewpoint is that the current state is simply the cost of doing business.

Figure 5: Concern With Operational Risk

Q. Please rate your concern with the state of operational risk with regard to processing subscriptions/redemptions and reporting investor balances and activity within your alternative investments area. (N=17)

Source: Aite Group interviews with 17 AI industry executives, Q2 to Q3 2016

That cost of doing business could be high, with manual processes making firms more susceptible to human error, inaccurate record keeping, and data manipulation. Objectively, manual processes are more difficult to track than processes completed through an automated, auditable workflow, thus increasing the chances of not only fraud but also compliance violations. If market participants continue to be content with this high level of operational risk, a transition toward more AI automation and standardization will be stymied.

One respondent shares, “Even though we are beholden to stacks of paper and manual processes, we have extremely tight control over operational risk.”
2. SCARCITY OF TECHNOLOGY BUDGET

While most respondents acknowledge that their firm would benefit from better automation and industry standards, many also share that it is tough to secure a technology budget for improvements due to other organizational priorities and the perception that AI operations handle lower volume compared to other operations. However, the reality is that the vast majority of AI business is transacted on behalf of institutional and high-net-worth customers for extremely high-dollar values, so it is of equal importance to process these transactions efficiently and correctly.

One respondent opines, “We would like to invest in better technology that would help automate manual processes but have been unable to get approval from another department head that controls our budget.”

While the initial cost of onboarding to an industry utility solution and adjusting processes to align to standards may be difficult to prioritize in a firm’s budget, the long-term savings and benefits are well-documented in other sectors, such as mutual funds and equities.

3. PRODUCT BREADTH AND VARIATION

The universe of AIs is large and quite varied. The sheer number of products with different structures exponentially raises the bar on operations. It can seem like a daunting task to automate processes in this landscape—especially when the tools at hand are manual. That said, well-established industry utilities such as AIP are designed and built to provide standardized formats that suit diverse needs and set the stage for streamlined, automated transaction processing and reporting.

4. TIMING

Unlike equities, exchange-traded funds, fixed income, and mutual funds, AI products are typically offered by subscription, with cutoff dates for subscribing to and redeeming positions in some cases. To add to the complexity, private equity products involve future capital calls. The inherent complexity of dealing with thousands of alternative products, each with its own timing restrictions for subscriptions/redemptions, presents challenges in developing a standardized approach to processing. While this may seem like a roadblock, a centralized offering with a strong infrastructure would be able to accommodate deviations in timing—and with automated processes, avoid manual overloads in attempting to meet deadlines.

One respondent raises concerns about a scenario in which the firm could be overwhelmed with redemption requests shortly before cutoff time and would not be able to physically process all of the paperwork before the deadline.
5. ACCOMMODATIONS/EXCEPTIONS

White-glove service is rampant in the AI industry, whether between investors and their financial advisors, financial advisors and their firms, or AI managers and their fund administrators. Anyone who has worked in the middle and back office knows that the front office is not particularly concerned with the difficulty or ease of processing exceptional requests; it simply needs to get them done.

Conversations with respondents reveal that they perceive the most operational risk in accommodating requests that require them to diverge from their set processes. No one wants to turn away business, but the number of exceptions to standard processes leads to an environment in which it is difficult to scale service and technology in tandem.
TOP FACTORS INHIBITING AI BUSINESS GROWTH: A SEGMENT VIEW

Alternative managers, fund administrators, and financial intermediaries hold somewhat similar views on the main issues that are hindering AI business growth, along with some divergences, as seen in Figure 6.

Figure 6: Top Factors Inhibiting Growth

1. REGULATORY PRESSURES

According to most respondents, regulatory scrutiny, including a perception of overreach, is a top factor negatively impacting AI growth. Across the three segment types, there is a concern that regulations could make the management of certain products cost-prohibitive, especially if the products require tedious operational processing and reporting.

For example, for fund administrators, any regulatory demands that may force firms to come up with a more real-time valuation on hard-to-value investment vehicles will levy substantial burdens, with reporting efforts taking valuable time and resources away from generating growth.

The work involved to ensure ongoing compliance and avoid future penalties can also be expensive for all market participants. According to respondents, regulations could potentially have a negative impact on whether financial intermediaries will commit to distributing and maintaining certain AI products for their customers as well as how retail customers view AIs.

2. LACK OF STANDARDIZATION

Both fund administrators and financial intermediaries ranked lack of standardization as another top concern in regard to growing the AI market. Challenges related to the use of unstandardized formats impede fund administrators’ ability to add more funds in the long run, due to the inability to scale operations to support larger numbers of transactions—and for fear of increasing operational risk. Lack of standardization has also caused some financial intermediaries
to view the alternative sector as an unattractive market to be in, with labor-intensive approaches leading to very little profit for the firms.

3. FUND PERFORMANCE

For AI managers and financial intermediaries, maintaining high fund performance is a potential top constraint on AI growth. A main cause of this anxiety is the attention spent on remaining relevant in customer portfolios; low fund performance makes it difficult for intermediaries to support AIs for their retail customers and also discourages the introduction of new fund managers onto intermediaries’ platforms. In addition, high management fees are a constant worry, as costs could scare off certain advisors and investors, especially those acting in a fiduciary capacity.

For AI managers, calibrating client expectations is also important, especially as adoption of alternatives expands to the less-experienced retail segment from solely institutional investors, with needs for education on the risks and rewards associated with investing in AIs.

4. DATA MANAGEMENT

Alternative managers are struggling to establish optimal data management processes to efficiently communicate internally as well as with clients, regulators, financial intermediaries, and third-party service providers, such as fund administrators. More resources are needed to optimize data aggregation, normalization, scrubbing, and reporting to ensure that client expectations are met. In today’s competitive marketplace, the ability to compile and report data is a base expectation for conducting, maintaining, and growing business.

5. SCALABILITY

Driven by lack of standardization and automation, the only way to scale the business for many firms has been to increase head count. For fund administrators, this is a very expensive and inefficient way to grow a business and is not sustainable in the long run, in terms of both risk management and cost control. Industry utilities are renowned for their ability to take on firms’ processes that are not value-added so that resources and head count can be pointed toward efficiently growing the business instead of managing operations.
DRIVING CHANGE IN THE AI INDUSTRY

Greater alignment is needed if the AI industry is to advance as a whole. Change is happening slowly, and it will be driven by the following factors.

REVENUE AND COST PRESSURES

The financial services industry is under continuous pressure to grow revenue while keeping costs low. Operations is a cost center, and firms are continuously seeking to cut costs and be nimble. Growing a business based on manual processes necessitates increasing head count, which is in direct conflict with cost containment.

NEED TO BUILD SCALE

Once reserved only for institutional investors and high-net-worth clients, AIs are becoming more mainstream. Current manual, paper-based processes cannot be scaled well to meet imminent market growth and business opportunity. Firms can find themselves strapped for resources and needing to hire more staff, which cuts into profitability. Additionally, the probability of errors will increase based on higher volume in the current nonstandardized, manual environment, leading to client dissatisfaction, increased reputational risk, and data security issues.

CLIENT EXPERIENCE

There is a certain cachet associated with investing in AI products, especially hedge funds and private equity funds. This distinction revolves around investors’ feelings of prestige in investing in alternative products originally targeted at the ultra-wealthy—and likely helps make the lack of transparency into these funds’ operations acceptable by investors and financial advisors.

However, times are changing. With the average client increasingly glued to his or her smartphone, there is an expectation for immediate status updates and access to information regarding investments, causing investors to seek out providers that put a greater emphasis on the client experience as a differentiator.

A few respondents shared that once subscription documents are mailed by the financial intermediary, the status of the application goes into a virtual black hole in which no one really knows the current status until the fund manager or fund administrator sends a confirmation file to the financial intermediary. This uncertain status can persist for over a month.
NEW TECHNOLOGIES BRINGING NEW COMPETITIVE PRESSURE

Competitive pressures come from all angles, but it’s the less obvious scenarios that catch incumbents off guard. Technology has changed the fabric of global society and has reshaped traditional business models. While it may seem inconceivable now, it is realistic to envision some investment managers distributing their AI products entirely through digital channels. This will require financial intermediaries, fund administrators, and AI managers to further automate and standardize their processes to remain competitive.

Streamlined processes will be an entry point to this change—the bare minimum needed to grow, compete, and succeed.

REGULATION

Compliance with current and yet-to-be-determined regulations always looms large. Whether firms like it or not, this is the reality. The addition of more regulations requiring real-time data will not abate any time in the near future, especially in light of some of the harmful public impacts and negative publicity surrounding scandals in past years (e.g., Madoff and Lehman Brothers, both in 2008).

Firms can take a proactive approach to future regulation, which most often involves collecting data, running reports, and sharing information. By better utilizing automation and standardized data for communication with external partners, firms will be better prepared to comply with future regulations. An added benefit is to build confidence in public perception by embracing transparency. Technology dollars are scarce, but firms that view investments in automation and data standardization as unnecessary risk handicapping themselves in the long run.
CONCLUSION

As AI products continue to proliferate and gain more mainstream acceptance, a roadblock to future growth is the great variance in how firms approach AI operations, highlighted by the continuance of antiquated manual processes that lead to heightened costs and operational risk.

To counter this situation, investing in standardization and automation will produce benefits that include reduced operational cost/overhead, ability to scale operations for imminent business growth, better operational risk and audit controls, improved client experience, better responsiveness to competitive pressures, and better ability to comply with future regulations while promoting industry transparency. These gains can be achieved via widespread adoption of an industry utility.

An industry utility serves as a hub through which counterparties communicate with each other—receiving, holding, verifying, and sending data, funds, reports, and messages via standardized file formats, thus relieving firms of operational burdens associated with data management across multiple product structures. It offers a unified approach to automating data exchange and transaction processing among counterparties, which enables participants to streamline their operations and avoid non-value-added tasks, such as building and maintaining proprietary technology applications.

All respondents we spoke with for this research that are part of a financial intermediary or fund administrator share a positive sentiment toward a single centralized industry service tool for AI processing and communications. AI managers’ sentiment was neither negative nor positive. The challenge they face is how to achieve industry-wide participation.

Key findings of our research follow:

- At least 65% of interviewees indicate that the most significant challenges their firms encounter revolve around a lack of standardization and the manual nature of operations. Regulatory changes, scalability issues, and data privacy are also identified as major concerns.

- Communication with external partners continues to be based on manual and/or inefficient methods, such as faxes, spreadsheets, and emails; only 18% of interviewees indicate that their firm has a high level of automation and data standards.

- A big roadblock to better automation and data standardization includes a false sense of operational risk control. Most participants indicate that their concern regarding their operational risk profile is low, yet the vast majority also acknowledge that they rely heavily on manual processes, which are rife with operational risk.

- Key factors that will ultimately drive stakeholders to better standardize data, processes, and communications include competitive pressures, revenue/cost pressures, the need to scale their businesses, the need to improve the client experience, and regulatory change.
• Support for the idea of an industry solution for standardizing processing and communication is overwhelmingly positive; the difficult part is gaining widespread adoption.

Further to that last finding, achieving widespread adoption of a centralized industry platform has been done successfully in the mutual funds and payments industries, among others, which could serve as a model.

Below are considerations, based on our discussions, for each segment of participants for the adoption of an industry utility that would accommodate increased demand from an operational perspective.

Financial intermediaries:

• Establish requirements and use your influence. Require managers wanting to place products on their platform to use the industry utility. AI managers may view this practice as restrictive but would see benefits through decreased operational costs and increased distribution capabilities. Financial intermediaries would benefit from more streamlined processes that reduce operational cost and risk, would be better able to scale their AI business by supporting more AI managers, and would provide more timely and efficient client service.

• Communicate with advisors. Influence them to conform to standardized formats of a centralized solution, which would help advisors and the industry at large realize greater efficiencies and faster processes.

Fund administrators:

• Embrace a collaborative approach to a centralized industry utility platform. While fund administrators have made substantial investments in proprietary technology, if they can become unified in their support for an industry platform, it would help spur standards that would benefit all segments of the industry at large.

• Become more competitive. Adoption of a single industry platform would allow fund administrators to concentrate resources on value-added services, such as performance reporting and risk management, as well as provide better overall client service. Adoption of a platform would also allow fund administrators to reduce internal technology development costs and operating costs/head count. Ultimately, fund administrators will be able to use their own resources to better differentiate their value-added services instead of spending a significant amount of their operating budget providing commoditized services.

AI managers:

• Enhance capital raising and distribution. Many small and midtier AI managers outsource the capital-raising function and have limited resources to allocate toward marketing. If they connect to a centralized industry hub, distribution—and therefore capital raising—can be enhanced through greater presence on financial intermediary platforms that require managers to operate in conjunction with industry standards.
• **Look beyond the current environment.** Competitive pressures can come from less obvious sources, and firms can better prepare to compete with the efficiencies of automation and standardization afforded by a centralized industry platform.

• **Improve transparency.** The AI industry has had a few negative events that have contributed to poor public perception. While the cachet around these investments is appealing, investor confidence in the industry would grow with the improved transparency and standardization of processes brought by a centralized tool, regardless of whether a regulation is dictating this.

DTCC’s AIP solution encompasses the core elements of a centralized industry platform today and is poised to serve as a foundation for post-trade communication, settlement, reconciliation, reporting, and compliance. Current members have reaped benefits from a centralized approach to AI operations; further adoption and collaboration among key industry participants will only help increase product coverage and flexibility, driving down costs and improving operational risk control across all members.
ABOUT AITE GROUP

Aite Group is a global research and advisory firm delivering comprehensive, actionable advice on business, technology, and regulatory issues and their impact on the financial services industry. With expertise in banking, payments, insurance, wealth management, and the capital markets, we guide financial institutions, technology providers, and consulting firms worldwide. We partner with our clients, revealing their blind spots and delivering insights to make their businesses smarter and stronger. Visit us on the web and connect with us on Twitter and LinkedIn.

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ABOUT DTCC

With over 40 years of experience, DTCC is the premier post-trade market infrastructure for the global financial services industry. Operating facilities, data centers, and offices in 16 countries, DTCC, through its subsidiaries, automates, centralizes, and standardizes the post-trade processing of financial transactions, mitigating risk, increasing transparency, and driving efficiency for thousands of broker-dealers, custodian banks, and asset managers worldwide. User-owned and industry-governed, the firm simplifies the complexities of clearing, settlement, asset servicing, data management, and information services across asset classes, bringing increased security and soundness to the financial markets. In 2015, DTCC’s subsidiaries processed securities transactions valued at more than US$1.5 quadrillion. Its depository provides custody and asset servicing for securities issues from over 130 countries and territories valued at US$45.4 trillion. DTCC’s global trade repository maintains approximately 40 million open OTC positions and processes roughly 280 million messages a week. To learn more, visit us at www.dtcc.com or follow us on LinkedIn, Twitter, Facebook, and YouTube.

Alternative Investment Product (AIP) Services is a platform that links global market participants—including broker-dealers, fund managers, fund administrators, and custodians—to fully automate AI such as hedge funds, funds of funds, private equity, non-traded REITs, managed futures, and limited partnerships. AIP effectively addresses the manual and often risky operational issues outlined in this research, thereby improving the AI community’s ability to scale to meet rising demand, increase efficiency, and drive down cost and risk while growing business.

AIP supports:

- Security master fund profiles, including offering and redemption periods, liquidity terms, holdbacks, payment instructions, and more
- Initial and subsequent subscriptions processing and settlement
- Redemptions/tender offers processing and settlement
- Exchanges/Switches
- Statement of account or position reporting and performance
- Valuation reporting
- Activity and distribution reporting and settlement
- Account maintenance
- Payments, including commissions and distributions

For more information about AIP, please contact MarketingCommunications@dtcc.com. For press inquiries, please contact dtcc@fullyvested.com.