

Utilities: Creating a
role in the fabric of
the industry

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Top Ten Challenges for
Investment Banks 2015

Utilities: Creating a role in
the fabric of the industry



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Utilities: Creating a role in the fabric of the industry

Increased regulation, tighter margins and ever-changing market conditions are exerting growing pressure on investment banks to focus on returns, rather than just revenues. It is essential that investment banks seek to cut costs whilst addressing increased data management burdens and tackling the challenges and restrictions imposed by new regulations.

Many firms have reached a limit on the benefits of offshoring and outsourcing for cost efficiency and require a new model for reducing costs. There is also an increasing realisation that standards (for example, a Legal Entity Identifier) will play an important role in the emerging ecosystem, as they will allow for greater "interoperability" across firms. Finally, there is an increasing realisation that, for many firms, achieving cost reduction through internal scale cannot be fully achieved with in-house shared services.

Therefore, Accenture believes the market is now ready to embrace utilities to meet these goals by adopting industry-wide collaborative approaches. The industry has periodically created utilities in the past (e.g. depositories) and it appears we are entering

the next wave of innovation in the form of a new breed of utilities (see Fig. 1).

The emergence of utilities

The concept of shared utilities is not new and has been applied in industries outside of investment banking with great success. A utility in this context is an entity created by a variety of industry participants to create efficiencies by collectively performing a set of non-differentiating functions that are similar across the member companies. Over the years, investment banks have created utilities or shared platforms in selected domains but, up until now, core securities processing capabilities have been excluded from these approaches. The post-financial crisis cost pressures have served to highlight the opportunities for utilities to reduce costs,

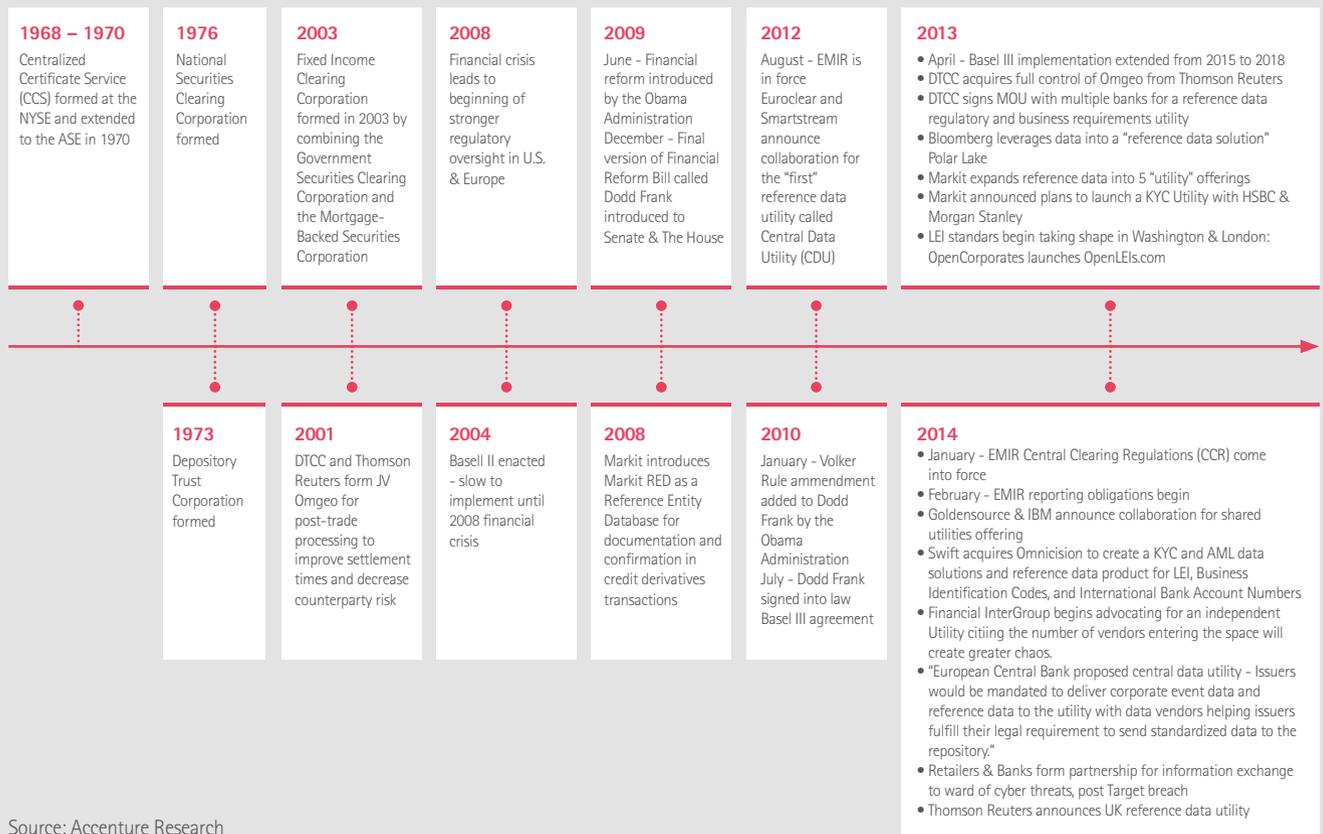
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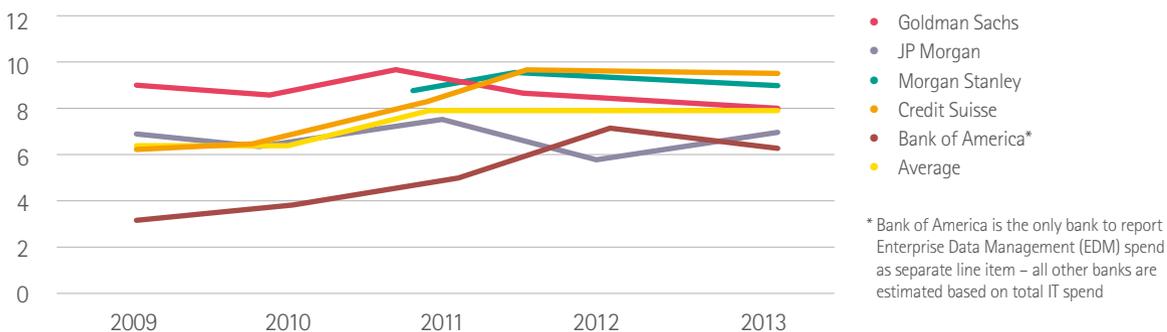
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Figure 1: Evolution of the utility concept in capital markets



Source: Accenture Research

Figure 2: Estimated Data IT spend across selected investment banks, as % of revenue



Source: Banks, Accenture Research

achieve standardisation of processes, mutualise risk and increase service quality in these core processing domains.

Currently, some of the key challenges that banks face are related to data management: poor data quality, inconsistencies, poor standards across source systems and consumers, and a lack of transparency around costs. Accenture estimates that data-related IT expenditure represents approximately 8% of revenue on average across the larger investment banks (see Fig. 2), with Burton-Taylor predicting reference data spend alone reaching upwards of \$1.8 billion in 2014. With data burdens growing organically and now accelerating due to changing regulations, the market has responded.

Costs and benefits of utility adoption

The potential benefits of utility creation are without question. By embracing utility usage, banks will be able to ensure that duplication of effort is minimised, in turn allowing a shift of resource to areas of greater value. In addition, bringing together the operations of a number of organisations can further enhance cost

savings by ensuring economies of scale, and the establishing of best practices and industry standards.

According to our estimates, the use of utilities can achieve cost savings of \$40-50m annually per firm among the top 20 global investment banks for reference data alone. Eventually, greater cost efficiencies can be achieved once market participants realise that certain core functions, such as reconciliations, could also be performed by utilities without degrading competitive positions.

As transaction volume has improved, transaction profitability has been under pressure – driving the need for scalability and the deployment of infrastructure whose costs can adjust to market volumes. Accenture Post-Trade Processing is an innovative solution which will help banks reduce post-trade processing costs, including minimising future change spend, adapt to new regulations and increase speed to market, leveraging proven, market relevant technology.

We estimate that the utility has the potential to realise a reduction in costs per trade of up to 30-50% (see Fig. 3).

By transferring the fixed cost model currently employed by banks to a variable cost model, clients will see a decline in the marginal costs per trade for every additional bank that joins the service, benefiting both new entrants and incumbents.

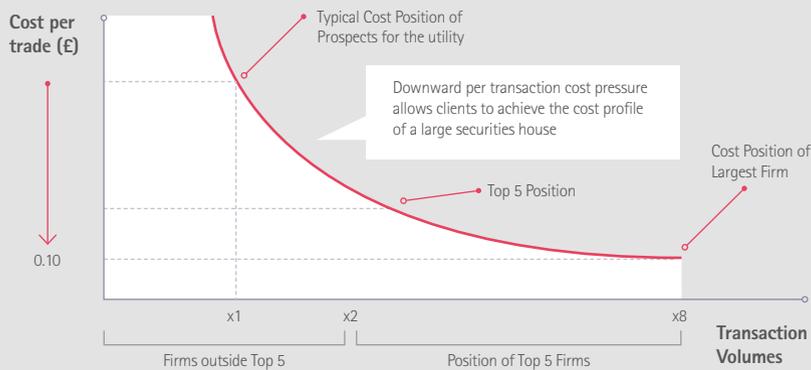
Challenges & opportunities

The use of a utility does not remove any of the regulatory responsibilities borne by banks. However, utility adoption improves data quality through increased volume of participant inputs, which in turn improves reporting to regulators. A further potential benefit is to create industry best practices as a means of driving standards, which is being seen with various industry entities such as SIFMA, DTCC etc., as opposed to responding to sometimes misguided regulatory mandates. Finally, from a regulatory perspective, moving day-to-day processing functions to the utility model allows banks to focus on the control and governance functions

The opportunity exists for a number of market participants to collaborate, establish a leading utility provider, and then profit from other organisations who wish to use the service.



Figure 3: Industry Cost Curve example – Equities



Source: Accenture Research

required to meet the regulatory requirements of the firm's activity.

The next challenge, which is actually an opportunity, is the creation of the first true market utility for financial services, as a neutral party that is not viewed as a disruptive force in the industry. To date there have been several examples of private vendors attempting to build a market utility, only to fail due to the markets' lack of trust. Accenture believes market participants have the

opportunity to create consortia for utility functions which will be viewed as neutral, third parties benefiting all in terms of data quality, lower costs, and improved regulatory reporting.

Conclusion

Utilities are potentially the next meaningful opportunity for banks to cut costs significantly while improving data quality, and to create data standards around which the industry and regulators can coordinate, in contrast to the

regulation/reaction cycle of today's world. Regulatory burdens are continually on the rise, data volumes and management costs are continuously increasing, and banks need to find a mechanism that enables them to achieve cost reductions and efficiencies at a time when targets are set around returns rather than revenue.

Utility services provide banks with a great opportunity to improve data quality and coordinate each organisation's best practices to set an industry standard. The opportunity exists for a number of banks to collaborate, establish a leading utility provider, and then profit from other organisations who wish to use the service. The challenge remains in finding those organisations that are willing and able to make the first move. From Accenture's perspective the choice is simple: choose to lead the transformation and have the first mover advantage, or get left behind.

About Accenture

Accenture is a global management consulting, technology services and outsourcing company, with more than 305,000 people serving clients in more than 120 countries. Combining unparalleled experience, comprehensive capabilities across all industries and business functions, and extensive research on the world's most successful companies, Accenture collaborates with clients to help them become high-performance businesses and governments. The company generated net revenues of US\$30.0 billion for the fiscal year ended Aug. 31, 2014. Its home page is www.accenture.com.

Accenture Experts

To discuss any of the ideas presented in this paper please contact:

Bob Gach

Managing Director
Accenture Strategy
robert.p.gach@accenture.com
+1 917 452 5952

Chris Brodersen

Capital Markets Research
New York
c.brodersen@accenture.com
+1 917 452 1093

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