Preface

Hearty greetings from the Infosys Banking & Capital Markets team. On behalf of Infosys, I am delighted to present the first issue of our journal “FINsights”, a compendium of articles, which bring you insights into the technology powering the financial services business. The aim of the journal is to bring you the latest in technology, applied to your business scenarios, which will enable you to win in today’s flattening business world.

The first issue of FINsights focuses on the wealth management industry; an industry which is grappling with multiple challenges. An increasingly demanding and informed customer base, a challenging compliance environment and the jostling for a customer centric “trust” based role amongst trust banks, brokerages, insurance companies and family offices make for a very challenging business environment. This journal has a set of articles which look at these and other unique characteristics of the wealth management industry and I hope that they will not only make for enjoyable reading, but also help you in addressing some of your vexing business challenges.

I would like to thank all the contributors from Infosys Banking & Capital Markets group and also Alois Pirker from Aite group and Matthew Bienfang from TowerGroup for their insightful articles. I hope you will enjoy reading these articles as much as we have enjoyed putting them together. Please do not hesitate to get in touch with me in case you have any queries or comments. I look forward to your feedback and suggestions in making FINsights a relevant and topical journal.

Happy Reading!

Ashok Venuri
Senior Vice President and Head - Banking & Capital Markets Group
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From The Editors Desk

The wealth management industry is changing rapidly to meet the evolving needs of its participants. This is one area where true financial services convergence seems to be happening as trust & private banks, brokerages and retirement planning focused companies are all trying to get a bigger slice of the action.

Opportunities in new geographies and asset classes are driving a lot of the change in the industry today. These will lead to increased investments in the core processing platforms, as well as the need to tie the various platforms together. The need to bring systems together is very important to financial services firms from a financial planning & advice, customer data, client service and a Business Intelligence (BI) & reporting perspective. Open architecture is another very important consideration that is driving changes to the way the banks service clients. Further, the need to offer clients a wide bouquet of products is driving consolidation of information across the different products and asset classes. Changes in banker and advisor team structures as well as client segmentation for servicing will lead to better cost structures.

All of the above have technology implications for banks. Technology will need to be aligned with business to meet the needs of an agile organization that can respond rapidly to changing business circumstances. Technology itself is evolving rapidly and can sometimes drive changes in the organization through the ability to deliver more than what was hitherto considered possible. Information Technology (IT) organizations that are able to plan and react early, and then execute well on these changes are the ones that will succeed in meeting the needs of their business.

We are happy that this book addresses some of the biggest business challenges and technology implications addressing wealth management firms today. The debate on some of these topics is very timely. We hope that the journal will inform you and enable you to formulate a response to the many challenges facing our industry. We look forward to your feedback.

Happy Reading!

Balaji Yellavalli & Manish Jha
Editors
Driven by ever-more demanding clients, enabled by the combined thrust of technology and marketing, the concept of open architecture which validates the decoupling of asset manufacturing from advisory services seems to be the future of the wealth management industry model. Today, high-net-worth individuals are demanding access to a wide range of wealth managers through open architecture platforms that help firms strive to strike the perfect balance between top-notch investments and personalized advice. The industry though has a long way to go before open architecture becomes the norm and can be efficiently supported by the infrastructure available for unified planning and connectivity.

Emmanuel Chesnais
Principal
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The Role of Open Architecture
At 33 trillion dollars in worldwide assets, the wealth management industry has been growing at 8% per annum and attracts more and more global firms. Expecting retirement of 77 million baby boomers, a number of firms in the wealth management industry are trying to improve their market share through acquisitions, new product launches and geographic expansion. The latest research by Bear Stearns has estimated total fees for wealth managers to exceed 200 billion dollars by 2010. Most experts also agree that wealth management is a very stable revenue producer compared to other sectors in financial services and firms consider it as one of the best ways to diversify their overall business holdings.

Wealth managers have traditionally been offering their clientele the combination of a broad range of investment products, proprietary or not, and advisory services. This decoupling of asset manufacturing from client advisory services resulting in the outsourcing (partial or not) of the former to third parties lies at the core of “open architecture”.

The two biggest challenges for an advisor today are managing the client relationship and ensuring that strategies are built in the client’s best interest, not the advisors’. Open architecture should help advisors to overcome the second challenge and ensure advisor independence. Metaphorically, open architecture creates a “Costco” for high-net-worth individuals with financial advisors as the knowledgeable floor representatives who sell membership and potentially assist clients in finding, choosing and potentially customizing the best product for a fixed fee.

**Benefits of Open Architecture**

Overall, open architecture will offer great benefits to both wealth managers and clients. One of the greatest benefits for the industry will be tremendous cost reduction and improved productivity. After years of customizing middle and back offices for every new strategy, with the transition to open architecture, wealth management firms can finally concentrate their resources on marketing and new clients. Also gone will be the perceived conflict of interest inherent in pushing only proprietary products as advisor’s independence is reinstated. Another major advantage will be an ability to build more direct relationships with the client, thus increasing retention and competitiveness. Currently, an advisor handles all relationship networks and it is common industry practice for an advisor to take the majority of his clients with him to his new firm. A successful implementation of open architecture can provide industry leaders with an additional boost to keep the client even after the departure of an advisor through the competitive advantage of the firm architecture. Also, open architecture can help managers and advisors to stabilize revenue per client through fixed fee and open new opportunities for newcomers in the industry.

Historically, it has been extremely difficult for new players in the industry to build a sufficient clientele, especially in Europe. Successful implementation of open architecture can be one of the most important marketing assets for a firm to build new relationships in a market where investors are known for embracing opportunities in new investment vehicles such as hedge funds, funds of hedge funds, private equity and untapped emerging markets. Overall, we believe open architecture can take the wealth manager one step closer to achieve the status of “trusted advisor”.

Open architecture also ushers in tremendous opportunities for clients. For starters, after many years of being at a disadvantage private investors finally get the same access to investments as institutional investors. Banks, like UBS and Credit Suisse have already admitted to plans for cross-serving products from the corporate investment bank to private clients. The recent growth in proprietary products among large investment banks can eventually lead to exposure in new strategies for private investors as well. On the other hand, smaller firms can use open architecture by offering better customized products across multiple asset classes and blend in better stability in their performance.

Managed accounts programs are the true pioneers of open architecture. The biggest advantages are lower expenses, tax efficiency, and an ability to customize the portfolio while keeping all benefits of the regular mutual fund. SMA (“separately managed accounts”) or wrap accounts also provide better diversification and truly ensure the independence of the advice. For example, Charles Schwab Open Select program currently consists of 60 strategies through 41 managers. The industry recently introduced the new level of open architecture called UMA or unified managed accounts. It allows investors to keep SMAs, ETFs and mutual funds integrated in a single environment. Overall, clients are the biggest beneficiaries of open architecture as they get better services, and better performance without necessarily adding extra fees.

**A Technology Perspective**

Wealth management platforms designed with an open architecture are integrating front-office with middle and back-office components, including third-party ones thus adding a broad range of features and functionalities, to form an end-to-end solution. A first series of challenges revolves around integrating the open architecture platform with the current client sales, service and investment processes.
To be competitive, wealth managers need the capability to efficiently document client objectives and develop recommendations that integrate proprietary and third-party offerings. To that end, technology should enable an aggregated view of the customer’s entire assets and liabilities,comings and outgoings. It should also utilize overlay management technologies to effectively customize an investment program for each client. Indeed, varied risk tolerance, different cost basis for each security,gains and losses from outside assets,unmanaged securities and other factors make each client unique. Equally important to overlay management is the maximization of after-tax performance while maintaining compliance with the investment policy statement defined for the client.

Finally, the complexity of the interfaces to multiple internal and external managers has to be harnessed to produce holistic consolidated reporting for an entire client relationship. Customized client reporting and portfolio diagnostic tools using color asset allocation visuals and featuring the wealth manager’s own branding have become de facto standard options.

A second series of challenges are focused on the integration of the open architecture platform with the current operations infrastructure. Wealth management institutions have a significant investment in proven capabilities that meet their fiduciary and operational requirements. New products and service capabilities cannot be implemented until they are integrated within current operational systems. Linking expanded open architecture investments to existing accounting and custody infrastructure requires building direct connectivity tools. By the same token, operational capabilities have to be updated to access and incorporate new products and enhanced services and new products have to be integrated with current offerings and operations. Again, leveraging pre-built components can provide a faster way to direct connectivity and going forward, allowing for smoother growth as the business scales.

Beyond these technical challenges, building a unified platform with expanded capabilities such as multi currency, derivatives or alternative investments will require not only tremendous knowledge of these products and vehicles but also intensive capital investments. And firms may not be able to pass these costs to the customers through revamped fee structure so there is a potential threat to overall industry profitability.

We believe that one solution to this issue will be for cooperation within the industry to share into the costs and benefits of the development. In fact, sharing a product within many firms has been very successful for separately managed accounts. Most of the firms within the sector have adopted either CheckFree or Vestmark as trading processing platforms. As it stands, SMA is an extremely important business and one of the key contributors in growing revenue for most of the firms. Surely, there is heavy competition between industry leaders to deliver more customized products to their clients yet they would realize the benefits of sharing the common platform. Building a strategic platform for open architecture can become another example of beneficial cooperation. Other potential benefits of joint development will be an ability to reduce maintenance expenses in the future and save on training for new employees once the platform becomes commonly used within the industry.

Looking ahead

Over the past few years, the wealth management industry has made considerable foray towards implementing open architecture thanks in large part to the combined thrust of technology and marketing. Player-wise, private banks are clearly leading the pack due to the very nature of their business whereas universal banks are moving more slowly.

Trying to find the right business model within this open architecture world brings challenges of its own. One problem is having too many products on offer. The more products, the greater the expertise required and associated costs hence pressure upon advisors to sell them. Shifting the focus away from sales and on personalizing the interaction with clients appears to help strike a balance.

In the US, most large firms currently offer a combination of in-house and third-party products through their wealth management platforms, but pride themselves in combining product excellence with sound, personalized advice.

Clearly open architecture is extremely popular with the new generation of ultra wealthy primarily because they have a greater comfort level with alternative investments and socially are a lot more open to paying a fee for the service provided. Channels such as the Internet or mobile phones are also seeing a significant development of fee-based memberships and subscriptions thus pointing to evolving perceptions vis-à-vis technology on the part of the clientele.

In an industry where more than anywhere else the client is king, investors are the perennial guiding light of the wealth management business. To that effect, the plethora of benefits that open architecture brings to all participants will go a long way towards turning wealth managers into successful trusted advisors.
Emmanuel is a Principal with Infosys’ Banking & Capital Markets practice. He has over 12 years of professional experience in the Financial Services industry both as a consultant and a practitioner. His work experience and domain knowledge relate to the areas of risk management, regulatory compliance, capital and derivatives markets and hedge funds.