STATE STREET ALPHA

The Future Is Open

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Our clients are constantly grappling with market uncertainty, shrinking margins, changing regulatory requirements and a fast-changing technology landscape. As a result, their investment needs are ever evolving, creating a need for flexible and collaborative solutions that enable innovation at scale.

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When it comes to technology, change is the only constant. At first there was the mainframe, then workstations, personal computers, the internet, cloud, smartphones and chatbots. Each subsequent technology increased the ease of use and choice.

Today, investment managers are thinking more than ever about technology's ease of use and choice as the rapid growth of passive investment strategies has overtaken traditional and fundamental active management. Margin pressure has caused them to rethink the scale, agility and cost of their technology infrastructure.

The COVID-19 crisis accelerated this process, highlighting any lurking deficiencies in operational or technology resilience.

Many of them have infrastructure that was built 20 years ago as all-encompassing monolithic platforms, when money management businesses were smaller, exchange traded funds did not exist and quantitative strategies were less sophisticated. Today, as managers are consolidating or adding new strategies to outperform beta-aligned indices, these monolithic systems have grown into overlapping clusters of platforms that are expensive to operate and even more difficult to extend, especially as fee structures and technology budgets compress. For organizations that have experienced a merger or acquisition, the challenges of blending data across different systems are even more acute.

For many investment institutions, it is an opportune moment to re-envision their processing footprint.

So What Needs to be Done?

Asset managers generally have two choices to tame their technology sprawl: leave things alone (and absorb the cost) or rip out their current infrastructures for "integrated" platforms that service a wider array of strategies, asset classes and geographies.

The problem is that both of these choices are flawed. Few, if any, asset managers can continue to absorb the cost of their existing technology sprawl as revenues decline, and the idea of a monolithic system that can meet both current and future needs is a fiction for most medium-size and large asset managers. There are few, if any, systems that fully support all investment strategies, asset classes and geographies.

Instead of looking for a single vendor to provide a comprehensive product, look toward a provider with an open architecture that enables third parties to easily develop and provision apps and services into the platform.

The migration from flip phones to smartphones is an apt analogy for the change taking place in the investment industry. The flip phone, provided and supported by a single carrier, created a walled garden of services that were strictly governed by the carrier.

The smartphone, however, with its open standards and access crushed the flip phones' closed strategy by supporting millions of third-party application developers. Converting the device into a platform gave the user access to a virtually unlimited array of functionality, from search, banking and games to anything in between. Turning the device into a platform also kept the technology relevant by continually onboarding new products and services that were seamlessly integrated with everything else. We do not buy a new phone when we want to consume a new app; we simply download a new game, content stream or service from the app store that operates in concert with everything else on the platform.

There is, however, a new idea percolating in the industry: asset management infrastructure as a platform.

The Rise of Asset Management Platforms

The shift from flip phones to smartphones describes the current state of investment technology. Investment professionals consume information and data from various sources and analyze markets through the lenses of different technologies, which are increasingly developed by disparate providers of risk and portfolio analytics, charting tools, alternative data and trading algorithms. Migrating to an open platform architecture takes the old single-provider, tightly controlled order management system and opens it up to smaller but focused third-party application developers that, without order management access, have virtually no way to get their innovative services, analytics and applications onto an asset manager's desk.

We believe change is coming in the following ways.

- Traders, portfolio managers and quants increasingly want more than what a single provider's walled garden can offer. Even moderately sized asset managers use one or more data vendors, externally sourced risk models, third-party algorithm wheels stocked with algorithms from various brokers and transaction cost analysis from other providers.

- More innovative applications and analytics are open source, making them cheaper and easier to license. Coupled with the new class of desktop interoperability tools that streamline integration and deployment of these applications, firms can tailor their investment operations with minimal reliance on the platform vendor.

- Market fragmentation, especially in global fixed income markets, forces investment firms to source liquidity from multiple trading venues. Platforms can streamline the process of establishing and certifying Financial Information eXchange connectivity with new venues, enabling asset managers to access the venues that are best aligned with their asset and product mix across the geographies they trade in.

- Regulations, most notably Markets in Financial Instruments Directive II, have created significant regulatory reporting requirements. Establishing connectivity with multiple Approved Reporting Mechanisms and Approved Publication Arrangements is yet another task best suited for technology platforms.

Against a backdrop of relentless fee compression driven by changing investor preferences for low-cost index funds, asset managers are increasingly voicing their frustration with monolithic single-provider solutions. In our Growth Readiness Study 2020, we interviewed 523 institutional investment industry executives globally to understand their challenges with data and technology integration.

Half of all respondents agreed that their investments in advanced technologies are often delayed due to challenges in integrating these applications with existing systems. More than a third of those surveyed agreed that they struggle to take advantage of third-party data and analytics because of difficulties with onboarding new technology.

This paints a picture of widespread frustration and fear of lost opportunity. It also underscores how critical the human element is, as new tools are only as effective as the people who use them. Organizations must have the right talent in place to reap all the gains that technology can offer.

Asset managers are facing a world where they need to grow their business and differentiate their investment capabilities, all while operating within a constrained budget as they rethink their technology footprint. Fortunately, the industry is moving toward open Application Programming Interface-driven platforms that easily integrate services, analytics and applications from a host of providers. Ease of integration is highly dependent on an open and extensible data platform.

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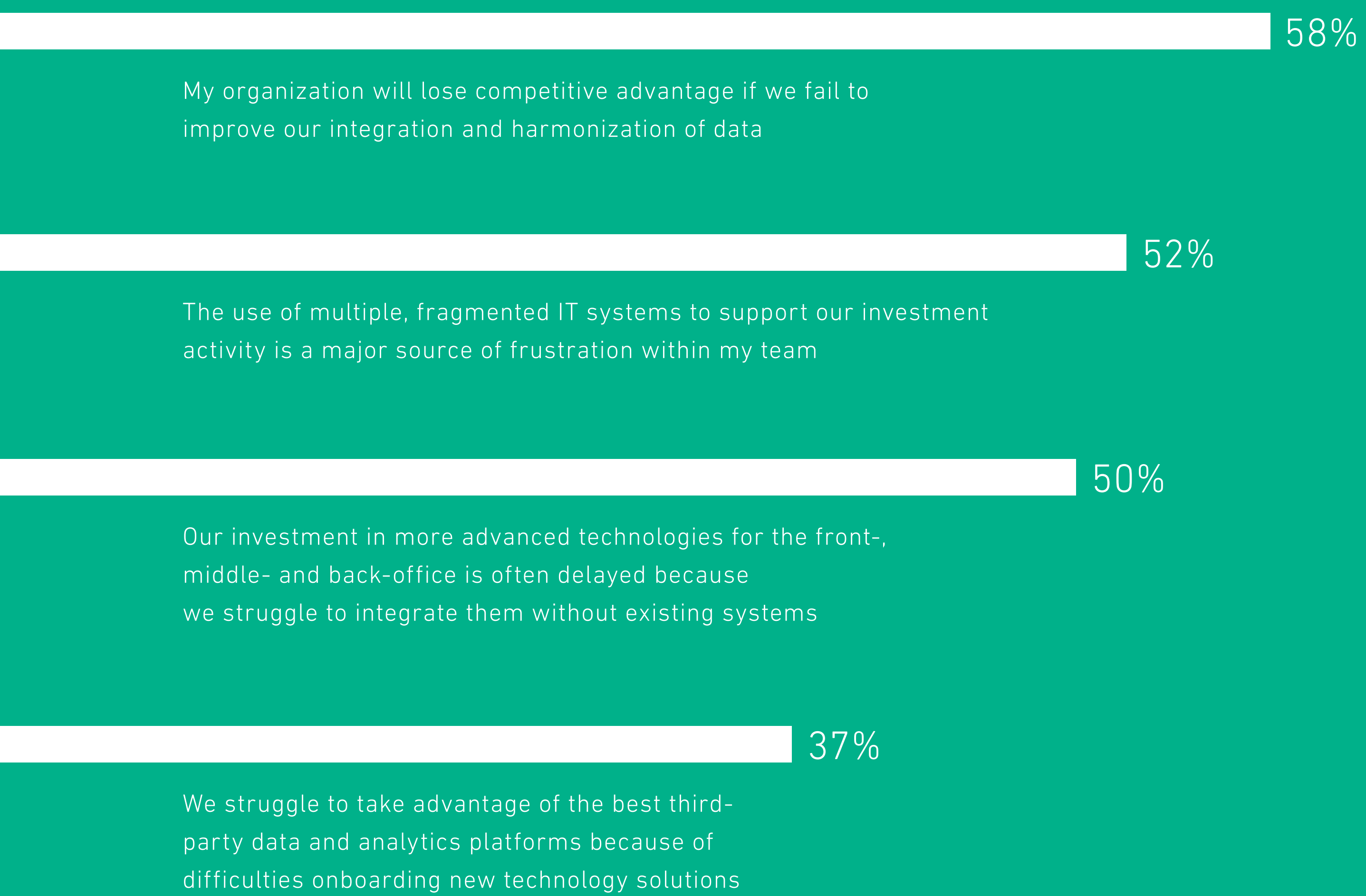
This type of technology architecture leverages an asset manager's core technology and seamlessly interoperates with the tools and services a firm needs to scale and grow its business without the disruption of massive technology change.

Thinking about the asset management technology footprint as a platform instead of an application attracts users not by forcing them into a limited single vendor paradigm, but by offering the choice of preferred third-party intellectual property delivered by a growing community of providers.

Looking to the future, we believe that investment institutions that use open platforms with robust data management foundations will have a significant advantage. They will have the right capabilities to implement their strategies, scalability to grow and resiliency to stay prepared in any environment.

Industry Views of Data and Technology Challenges (% in Agreement)



Source: State Street: Growth Readiness Study 2020

For more information visit our
Volatility to Value page or **Contact Us**.

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