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Investment Operations Outsourcing:

The Secret of Successful Outsourcing May Be ‘Right Sourcing’ and ‘Robust Issue-Tracking’

NEW YORK — Of all the challenges in outsourcing any investment operation, the biggest one that draws bated breaths centers around making the changeover and actually handing functions to the outsourcer, while keeping the operations running without a hitch.

“To go from the current state to the future state, there are three main components,” says Michael Taylor, Director of Outsourcing at **RBC Dexia Investor Services**. “I’d liken it to a heart transplant where you need to disconnect the heart, keep it going while it’s disconnected and then reconnect within the new environment. That’s simplistic, but those are the main steps we see in a system or process outsourcing transition. You need to disconnect the core process or technology, continue to do daily activities through the transition, then reconnect the new process or technology.”

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The danger of not reconnecting the new system properly is that a client can be affected, or brokers, or ultimately the investment firm’s reputation. “The vendor should have a proven track record,” says Taylor. “The vendor needs to know the investment manager’s business and their specific requirements.”

The operations cultures of the outsourcer and provider must match. “The more the client gets to know the vendor, some of those issues are worked out,” says Taylor. “In some cases, they don’t fit. The vendor and client have different cultures and it doesn’t feel right and they have to move on.”

For all the planning for an outsourcing transition that is done beforehand, when the plan is put into action is when “the rubber meets the road,” says Pawan Verma, Director of Outsourcing at **PricewaterhouseCoopers**. “The transition is all about the change and risk management,” he says. “The outsourcers need to be ready for that change. Often the outsourcer will have delegated a lot of responsibility to the service provider as the transition manager.”

In consulting on outsourcing methods, PricewaterhouseCoopers advises that a sound outsourcing model includes teams from both the outsourcing firm and the service providers. This emphasizes being careful not to lose — or alienate — key people who manage operations, according to Verma. "Knowledge transfer is a big thing as part of the transition process," he says. "Often the outsourcers don't have a good idea of all the gory details of the processes and the platforms that enable the processes. It's all in their heads because they've been working on them for long time. They know how to do it and it's not codified."

The changeover cannot be done in "big bang" fashion, cautions Verma. "Before moving to the next activities in the transition plan, make sure the preceding activity is done completely," he says. "Then you can move to next set of steps detailed in your plan. The outsourcer and service provider have to drill down with a comprehensive transition plan that cuts across everything."

To serve clients who outsource functions to their firm, RBC Dexia seeks to guide the management of the transition and give clients tools to understand how the transition will work, explains Taylor. "The third-party provider should have the tools and personnel to support the investment manager so they understand how the relationship is going, identifying any issues and resolutions required," he says. "The provider also has to give the client a chance to tell if things need to be improved or if they have new [investment fund] products coming out — what those products are and how they benefit the customers."

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In choosing RBC Dexia, **Manulife Financial** sought a partner that could support its growth. "Manulife has a large product suite so they needed someone with the size to support a lot of diverse funds," says Taylor. "We brought a lot of that scale and flexibility to the table. Because we invest heavily in our systems and people, Manulife was pleased with our commitment to functions they were previously doing themselves. The last thing an investment management shop wants is outsourcing to a provider who ultimately doesn't invest in maintaining technology and the service starts going down. We demonstrated that we would continue to improve our services over time."

In addition, making a change to a different outsourcing provider can be a tricky business, says Cliff Warner, Chief Operating Officer, **London & Capital**, which serves as adviser for about $2 billion in investment assets for high net worth individuals and institutions worldwide. "What tends to happen is you give notice to one to sign with the new one, but you haven't finished all the negotiations to sign with the new one because you want to get up and live," he says. "You don't want to be forced to hit a deadline or time scale that you can't meet. As a regulated company, we don't want our funds to be left on the shelf. You need great project management to be sure you know all the things on the list are being done. More importantly, you need communication that's consistent between the three parties. If it breaks down between the two other parties, you have to pick it up quickly."

In contrast to other firms, London & Capital outsources more than just back-office functions. "We are a hybrid of a company that manufactures [investment fund] products and provides solutions for clients," says Warner. "We manufacture certain products but not all the products. We buy into others' products to incorporate into out strategies for portfolio management. We sell individual funds directly and strategies that have a hybrid of our products and products from third parties. What we can't outsource is the relationship."

London & Capital outsources its distribution but retains a sales desk, adds Warner. The firm is examining outsourcing parts of its operations, as well as fund administration and custody. "The idea is to stay lean with what adds value and outsource things that are commoditized and don't add value," says Warner. "The result is a portfolio manager who tells clients about new products and strategies, and keeps the client relationship going by providing service."

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Unlike the aforementioned firms who have outsourced, **Schroders plc**, the global asset management firm with $226.1 billion in assets under management, moved away from outsourcing in London, ending its use of **JPMorgan** for certain operations. For one of those, portfolio accounting, Schroders turned to SimCorp's Dimension software. "In line with UK market practice, we no longer provide custodial services, allowing us to build a modern infrastructure that supports investment management, client servicing and enterprise data management," says Markus Ruetimann, Group Head of Operations and IT at Schroder Investment Management Ltd., a unit of Schroders. "We control and directly manage the core data underlying our investment management process and client portfolios. However, Schroders continues to have many outsourcing arrangements with custody and fund accounting services providers across the globe."

To determine whether to outsource a particular function, Schroders first identifies which data flows and processes it needs to control directly, explains Ruetimann. The firm typically will not outsource to a provider who is only offering a beta version of a program. For its IT infrastructure in London, Schroders extended a contract with **CSC**. In Philadelphia, Schroders outsourced custody and fund accounting to **The Bank of New York**. Schroders is also examining outside providers to administer its UK investment trusts.

Another issue in transitions is clashes of operational cultures. "Often when firms are moving work, it's to a low-cost country," adds PWC's Verma.

"Teams on the outsourcer's side are in the US or Europe and know how to work with each other. If that work goes to India, there is a very different set of cultural values or attributes. Not many understand bridging and morphing of the two, and working in a global cultural scenario. That's another layer of complexity to resolve and needs care and feeding for all to work together."

Another issue in transitions is clashes of operational cultures. Not too many people understand the bridging and morphing of the two.

Service provider **Lab49 Inc.** opened a new office in Bangalore in October, but cautions that offshoring should be done with care. "A mistake that outsourcers fall into is thinking it's a quick fix — just open an offshore center, get thousands of engineers from India and get it done very quickly," says Vivake Gupta, Director and co-founder of Lab49. "But it's never a quick fix. It takes enormous planning and even after that, the advantages aren't the same." Ruetimann echoes this advice not to see outsourcing as a way of removing problems. "Do not outsource," he cautions. "'Right-source.' Outsourcing gives the potential impression that the problem or challenge has gone away."

Being ready for the unexpected is another principle for achieving successful outsourcing transitions, explains Verma. "You will always have issues when doing a transition," he says. "You will not have talked through every little detail. Good outsourcers recognize that will be the case and build a process to handle those issues. They have robust issue-tracking mechanisms and a robust escalation resolution mechanism." ❑